

WHAT DROVE OUTPERFORMANCE IN GEM IN 2016?

2016 was an outstanding year for value investing in global emerging market(GEM) equities.

In 2015, there were many stock specific opportunities created by heightened volatility and fear. Then, in 2016, driven by signs of a revival in economic and corporate growth, and realisation that quality and growth stocks had become too expensive; value investing roared back – outperforming the market across virtually every major geography and companies of all sizes.

As confidence returned to GEM equities through 2016, we took the opportunity to sell some of our GEM stocks that had outperformed at much higher prices.

In 2017, we still see many attractive stock specific opportunities driven by participants' behavioural biases, such as a tendency to over-react to new information or run with the herd mentality. Some stocks will become oversold relative to their long-term earnings potential; others will become crowded trades – highly correlated and expensive.

Our job is to recognise and take advantage of these disparities, taking positions where most investors lack confidence, and then moving out as the crowd moves in.

As we move through 2017 and beyond, plenty of opportunity lies ahead, with the long-term structural case for GEM remaining in place. GEM equities remain cheap, with stock prices remain attractive both in absolute terms and relative to developed markets – and the size of the gap between value and quality stocks remains anomalously large.

At the same time, corporates in emerging markets are looking strong, with earnings and free cash flow coming through. Finally, we expect volatility to continue across GEM equity markets, and we will be once more positioned to take advantage of the resulting value stock-picking opportunities.



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