

UBS Emerging Markets Equity Fund

May 2024

Fund description

The Fund is an actively managed fund investing in a high conviction portfolio of 25–40 emerging markets equities.

Target market

The Target Market Determination (TMD) for the Fund sets out the class of consumers for whom the product, including its key attributes, would likely be consistent with their likely objectives, financial situation and needs. To access to the TMD and other Fund documentation visit our website.

Investment strategy

The Fund has a high conviction focused strategy and invests in emerging markets equity securities, taking meaningful positions at the company level seeking to identify the best opportunities to add value.

Investment objective

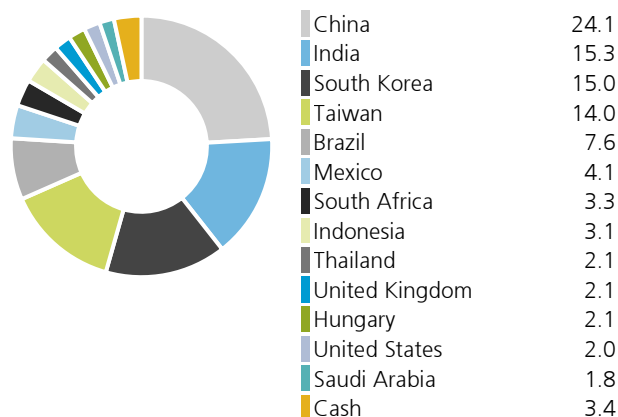
The Fund aims to provide a total return consisting of capital growth and income that outperforms (after management costs) the MSCI Emerging Markets Net Total Return Index over a rolling full market cycle (normally 3–5 years).

Fund information

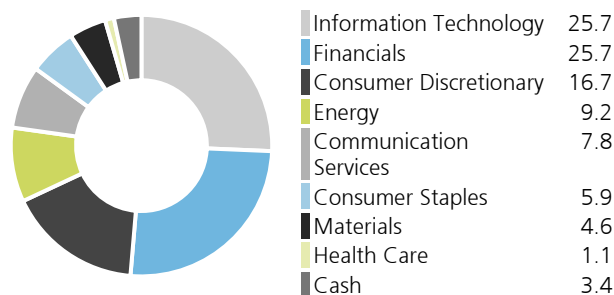
Inception date	27 July 2018
Fund size	\$ 48.8m
Management fee	1.20% pa
Performance fee*	Yes
Minimum initial investment	\$50,000
Typical number of holdings	25 to 40
Distributions	Annually
Buy/sell spread	+/- 0.40%
Currency management	Unhedged
APIR code	UBS8018AU

* The performance fee is calculated as 20% of the amount by which the Fund outperforms the MSCI Emerging Markets Net Total Return Index

Country/regional allocation (%)



Sector allocation (%)



Active security positions

Overweight	Underweight
Kweichow Moutai Co Ltd A	Alibaba Group Holding Ltd
Grupo Financiero Banorte O	Icici Bank Ltd
Pinduoduo Inc Adr	Meituan-Class B
Reliance Industries Ltd Inr10	China Constr Bank 'H' Shs Cny1
Samsung Electronics Krw5000	Hon Hai Precision Industry

Active industry positions

Overweight	Underweight
Banks	Capital Goods
Semiconductors & Semiconductor Equipment	Utilities
Energy	Financial Services
Food, Beverage & Tobacco	Materials
Consumer Durables & Apparel	Consumer Services

Investment performance

Fund	1 month %	3 months %	1 year %	2 years % pa	3 years % pa	5 years % pa	Since inception* % pa
Total return	(1.59)	2.43	8.50	3.25	(5.78)	1.76	1.47
Benchmark**	(1.81)	1.35	9.36	5.32	(1.36)	4.40	3.61
Added Value	0.22	1.08	(0.86)	(2.07)	(4.42)	(2.64)	(2.14)

* 27 July 2018.

** MSCI Emerging Markets Net Total Return Index.

Performance figures are net of ongoing fees and expenses. The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns. Differences may arise as Russian securities were partially suspended from trading since 25th of February 2022.

Performance/attribution comments

The portfolio slightly underperformed the benchmark in May. Consumer Staples was the key detractor, while Consumer Discretionary contributed the most, all due to our stock selection. Market-wise, Brazil was the key detractor, while United States (Mercadolibre is listed in the US) contributed the most, respectively due to our stock selection and allocation effect. On the stock level, our holdings in PDD Holdings, Mediatek and Mercadolibre were the key contributors. PDD outperformed as Q1 earnings showed a strong beat in profit and revenue. PDD continued to win market share in both domestic and overseas markets despite fierce competition. Additionally, Temu gained users in markets like Europe, Japan and South Korea rapidly, despite significant reduction in expenses which narrowed its operating loss. Mediatek outperformed with the semiconductor sector. Investors expect the industry to be at the start of another multi-year upturn and positive sentiments were reaffirmed by Nvidia's recent quarter results which reflected strong demand for Artificial Intelligence (AI). Mediatek has been able to capture the market opportunities in each product cycle successfully and we believe networking, high performance computing and ASIC could be among key drivers for the company beyond 2024. Mercadolibre outperformed on the back of better than expected 1Q24 results which were reported in May. MELI's net income in the quarter grew 76% y/y, 13% above consensus as Brazil and Mexico momentum outweighed Argentina headwinds. On the other hand, our holdings in Suzano, China Mengniu Dairy and Samsung Electronics detracted. Suzano underperformed on news that the company may embark in a large and complex M&A, raising concerns about its capital allocation decisions, and high potential leverage. We decided to divest post news flow. Mengniu underperformed as the stock trended lower over the period amid concerns about continued consumption weakness and low visibility of revenue growth acceleration. In addition, the unexpected change in CEO also caused concerns on the company's strategy. Going forward, we believe that consumption recovery will be more gradual than expected, though margin expansion thesis remains intact with valuations remaining attractive. Samsung Electronics underperformed as investors remained cautious about its slow progress in the high bandwidth memory business used in AI applications. We continue to hold it as we believe the stock will catch up somewhat with its high-flying peers. Following inventory adjustments and a turnaround in memory demand from PC and mobile, the company is also seeing signs of an order recovery from enterprise and cloud servers. With

memory order momentum building, recovery should gain more traction in the coming year.

Market review

EM equities posted flattish returns in May. EM market rallied at the start of the month on the back of tech rally and supportive China policy measures but corrected towards the month-end as optimism on Fed easing receded. Sector-wise, Information Technology and Utilities are the key outperformers, while Health Care was the key underperformer. Within Asia, Taiwan was the key outperformer, riding on the tech rally. Within Latin America, Argentina was the key outperformer as inflation slowed down and benchmark interest was further reduced to 40%.

Outlook

Short-term sentiments towards Chinese equities appear to be improving, with the HSCEI (Hang Seng China Enterprises Index) being the best performer among major global indices YTD to end May, in USD terms. A combination of factors are likely providing some support, including more significant measures to support the property market, reduce property inventory and towards longer-term capital market development. In addition, China offers good value against other markets that are looking increasingly expensive. We have maintained the view that current Chinese equity valuations bake in significant market pessimism, and there is alpha to be reaped in some of the high quality companies we are holding. On the macro level, we believe that growth momentum will remain soft in the near term and expect that improvement in consumer and business confidence is required before the economy turns around. We are also expecting geopolitical issues to continue dominating headlines with the US elections looming nearer. The recently proposed US bills, such as one targeted at "certain biotechnology providers" and another to "prohibit index funds from investing in Chinese companies" are part of the political noise, with more such bills likely to be proposed, before the November elections, that could upset markets.

Outside of China, we expect a mild growth recovery, with Asia ex-China growth in 2024 slightly outpacing 2023 in aggregate. In our view, there is an improving export outlook for countries that are more plugged into the tech supply chain. Our analyst was in Taiwan in March and witnessed that the cyclical upturn is intact though

momentum is sluggish outside of AI-related investments. We may need to be more patient for the tech-led manufacturing rebound to benefit industries beyond semiconductors and high-growth areas such as artificial intelligence (AI), that are mainly in Korea and Taiwan.

In Korea, the “corporate value-up programme” continues to elicit investor interest. We followed Japan’s development over several years as the authorities worked to close the valuation gap, and believe Korea is sowing the same seeds, which will not happen overnight but over a period. Meanwhile we are monitoring the progress. The Financial Services Commission (FSC) recently announced they would set up a disclosure website, launch the Korea Value-Up Index and ETFs tracking the index this year. Meanwhile tax reforms continue to be debated in the government. Since last year, our boots-on-the-ground research has made us aware of improving governance ranging from payouts to investors, rising corporate activism, to softer issues such as employee retention, gradually rising female participation, and better work life balance. Corporates are focusing on profitability.

Down south in India and Indonesia, domestic demand has shown relative strength. India’s economy has continued to produce robust broad-based momentum supported by cyclical and structural tailwinds. On the back of government capex on infrastructure, there is emerging evidence of a pick-up in private sector capex cycle and for the first time in a decade it appears that India’s economy is being driven incrementally by investment rather than consumption. Our boots-on-the-ground research recently uncovered a strong outlook for higher-end discretionary growth while mass and mid-segment consumption remains weak, due to a weak job market, bad monsoons in recent years impacting agricultural incomes and high inflation. Staples companies are showing some stability but recovery may take a few more quarters. India’s general election results came in with BJP stopping short of parliamentary majority, but with its allies, it would still be able to form the government. This means the direction of reforms should continue and investors are looking toward cabinet allocations this month and the Budget in early July for more clarity.

In Indonesia, the macroeconomic environment remains stable given well-supported domestic demand and a healthy commodities trade surplus. We believe the economy will continue to be supported by reforms, such as the Job Creation Omnibus Law, instituted by the Jokowi administration as well as supply chain diversification. Public finances in Indonesia are the healthiest among key Emerging Markets economies, with low fiscal deficit and public debt to GDP. There have also been initiatives to build out the EV supply chain given Indonesia’s nickel ore supply. Financial health of corporates and households remains robust which should support domestic demand recovery. There are some jitters on a smooth and easy transition to the new government at year-end but we are waiting to see the direction of the new administration. Meanwhile we had already trimmed our Indonesian holdings after elections as we thought there may be a lull in economic activity during the transition.

Outside of Asia, while the macro backdrop for potential rate cuts is favorable given the level of high real rates, it hasn’t fully materialized yet. Brazil was among the first to cut rates back in August 2023. However, given the worse than expected fiscal deficit, rates are likely to stay high for longer. The outlook for Mexico is similar albeit for different reasons. The backdrop of political noises makes it difficult to cut rates in a meaningful way. Only market so far that has delivered on rate cuts is Hungary.

Beyond potential rate cuts, election outcome has been a key driving force behind the markets. Investors are worried about the latest election results in Mexico where the incumbent party seems to have secured the constitutional majority. There has already been some pressure on the equity markets and on FX. Similarly, there is uncertainty around who will be forming the next government in South Africa following the incumbent party’s loss of majority. We are monitoring the situation closely as it’s important to distinguish what is sentiment and what is fundamentally driven.

Structurally speaking, we see changes happening in select markets. In Mexico, we see a strong trend of nearshoring, especially in the north, resulting in higher investment and employment. In addition, the Middle East should continue benefiting from structural reforms, the volatility in oil price notwithstanding. Last, we are also monitoring closely the geopolitical risk around the current conflict in the Middle East.

Over the longer term, we see the following attractive drivers for Emerging Markets: 1) The evolution of Asian consumers: a rising middle class likely to drive higher consumption, premiumization and a shift towards discretionary spending and financial deepening, 2) De-globalization and geopolitics: reconfiguration of manufacturing and supply chains/“China Plus One” diversification, 3) Artificial intelligence and digital transformation: growing strategic importance of semiconductors with large parts of the value chain in Asia, 4) Energy transition: electric vehicle supply chain, from raw materials (e.g. nickel ore) to electric vehicles and 5) structural changes/reforms: better institutions, reforms and macro conditions in countries like India and Indonesia.

With respect to our portfolio, we believe that we can continue stabilizing performance and add value for our clients with our active approach.

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