OP

Oldfield Partners

Overstone Emerging Markets Equity Fund

2021 Investment Manager's Report

The Overstone Emerging Markets Equity Fund (A shares) returned +11.3% in US dollar terms (total return inclusive of dividends and net of all fees) in 2021 compared to a fall of -2.5% in the MSCI Emerging Markets Index (index used for illustrative purposes only). I shares returned +11.6%.

Emerging market equities were pressured by a slowing Chinese economy undergoing regulatory reset, the prospect of monetary policy tightening in the US, inflationary pressures and supply chain disruptions, and the global health crisis unfolding with new variants of the Covid virus. That said the outlook for emerging market equities is generally positive as they recover one-step behind developed markets on the roll-out of vaccines, and benefit from pent-up demand both domestically and internationally. We continue to favour the normalisation trade as economic life recovers around the world. Valuations for emerging market equities remain reasonable, and slightly below their long-term historic averages.

The top performers by contribution for 2021 were Embraer, Ternium, and Infosys. Embraer (Brazilian aircraft manufacturer) was a strong performer this year as demand for aircraft recovered and it bounced back from an unprecedently low valuation. It will continue to benefit from the ongoing recovery in the domestic and short-haul aviation market in the US. It is the near sole remaining manufacturer of regional jets for the key US market and a solid player in the business jet market. The icing on the cake is the prospect for its short-range electric flight vehicle (called EVE) as this market opens globally and orders prove its potential. Ternium (Latin American steel producer) benefited from buoyant US steel prices, a solid demand outlook, and good strategic positioning in the Mexican market. Mexico remains a growing manufacturing location and Ternium should benefit as an efficient low-cost operator. Infosys (Indian IT services provider) continued to execute well in a period of booming demand for IT services to boost and enhance corporate digital capabilities. Management has been able to steadily increased guidance throughout the year.

The bottom performers by contribution during the year were Buenaventura and Turkcell. Buenaventura (Peruvian mining company) reflected that gold has lost some of its historic safe-haven shine in this crisis and the political uncertainties for the mining sector in Peru following the close-run election. We believe that politics will moderate to reflect economic realities and the importance of the mining sector to the country. Turkcell (Turkish mobile telecom provider) was again impacted by the wider fallout from Turkish economic policy as the President intervened dramatically in monetary policy, rather than by anything company related. Turkcell continues to execute well. The company can inflation price, has an active currency hedging policy, and is well used to the vagaries of Turkish policy in structuring its balance sheet. Further economic disruption hurts the voter base favourable to the President, perhaps prompting a reconsidered economic approach.

There were four new holdings in the portfolio – SK Hynix, Alibaba, ASE Technology, and SK Square. SK Hynix (Korean semiconductor manufacturer) is the second largest DRAM producer globally (behind Samsung Electronics) and the second largest NAND player following its acquisition of Intel's NAND business. It is a pure play memory semiconductor company. There is scope to improve technology in 3D NAND ramp up, better NAND product mix, and adopting EUV technology in DRAM. We like the continued consolidation of the global semiconductor industry which has allowed key players to profit maximise. Alibaba (Chinese e-commerce & cloud provider) is the leading player in e-commerce and cloud services in China. The Chinese government has sought to reduce the strong market positions of the ‘super platforms’ and have greater access to the data being produced by the internet service companies. Many of the regulatory reforms on the sector are sensible long-term to prevent unwelcome monopolies developing. Despite this we see e-commerce continuing to grow in China and Alibaba remaining a leading player. The sharp correction in the share price since late-2020 provided a compelling opportunity to access the Chinese consumer. ASE Technology (Taiwanese semiconductor packaging & testing provider) is the world’s largest semiconductor assembly and testing provider. Based in Taiwan it benefits from proximity to some of the world’s largest semiconductor foundries. Advanced integrated chip packaging techniques play an increasingly important role in optimising systems of semiconductor performance in areas such as processing speed, scale reduction, energy efficiency and heat management. It is well positioned to benefit from both the broader trend of semiconductor demand growth and technological advancement in packaging techniques. SK Square (Korean technology holding company) was spun out of SK Telecom (Korean mobile telecom provider). The telecom company will continue to benefit from the growth of 5G and broadband in South Korea with a dependable dividend yield. SK Square holds a stake in SK Hynix that accounts for the bulk of its assets, but also an active portfolio of internet service companies in Korea that over time will be sold opportunistically.

Portfolio turnover for the year remained low, as in prior reporting years, and at the year-end the portfolio had 20 stocks. The weighted average of the price targets in the portfolio at year-end showed over 55% upside potential. We continue to be selective in picking stocks on a bottom-up basis for a concentrated portfolio that we believe should offer attractive upside potential for the patient investor.

Oldfield Partners LLP

April 2022

The value of all investments and the income from them can go down as well as up; this may be due, in part, to exchange rate fluctuations. Past performance is not necessarily a guide to future performance