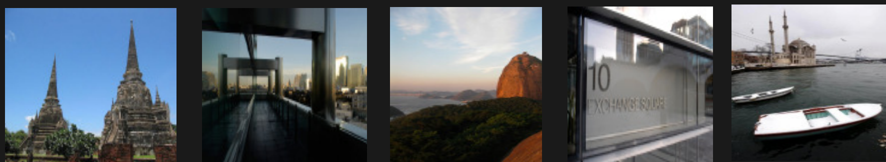
ESEMPLIA EMERGING MARKETS
Market Outlook
Q1 2010



The World economy remains on track to post above-trend growth over the first half of the year while we remain expectant that there will be a deceleration of growth over the second half of the year and possibly into 2011.

Emerging Economies are once again growing faster than the Developed World, largely as a result of strong tailwinds from global restocking and the reacceleration of global demand. Domestic demand also remains a key driver of economic growth in these markets, with the outlook for strong consumption and investment remaining favourable for the foreseeable future. Over the medium term, we expect the pattern of economic growth in the Emerging Economies to persist and growth in the Developed Markets to remain under pressure as consumers and governments struggle to rebuild their balance sheets.

Higher levels of economic growth across the Emerging Markets have resulted in some inflationary pressures and to date we have seen countries such as Israel, China, India, Brazil and Malaysia moving towards tighter monetary policy conditions. In the context of uncertainties which exist around the sustainability of the nascent recovery we are seeing in the Developed World, and in light of possible deflationary effects which could come about as a result of widespread excess capacity, moves by Central Banks have been careful and slow.

Looking forward, we expect that global rebalancing will once again become a major theme, as a protectionist backlash in the Western World has the potential to stem global trade and negatively impact the early recovery the global economy has been experiencing. We have however been witness to some encouraging signs to alleviate this risk. A significant growth in imports across many Emerging Markets and the expected appreciation of the Chinese Renminbi, we believe, should go a considerable way to assuage anti-trade instincts in the US and Europe.

In terms of market performance, we expect the Emerging Markets Equities asset class will continue on an upward trend, as valuations remain supportive and earnings growth robust. MSCI EM's PE currently stands at 12.1x, 10% below the asset class' long-term average of 13.3x and 13% below MSCI World's (the Developed Markets benchmark). On a Price-to-Book basis, MSCI EM trades at 2.1x, at a slight premium to its own historical average at 1.8x and to MSCI World's 1.9x. However, we believe these levels are more than justified by expected ROE from MSCI EM, which at 17.5% is much higher than the asset class' track record of 12.5%, and the expected ROE from MSCI World at 13.6%.

From a volatility standpoint, we expect to see further gyrations in market sentiment in coming quarters, similar to the ones we witnessed in 1Q10, when the Emerging Markets Equities asset class lost 10% in the first month and subsequently rebounded by 13% to close the quarter with a healthy 2.5% return. Such volatility is natural given the current environment, as markets are forced to digest:

- The end of ultra-loose monetary policy and quantitative easing,
- The prospects of fiscal consolidation in the West and scepticism around the ability of governments to deliver
- The transition from destocking into restocking across the world and
- The continuing uncertainties associated with regards to the sustainability of the recovery in Developed Markets.

Our portfolios remain overweight Mexico, Thailand, Indonesia and India and underweight Brazil, Malaysia and Israel. Sector-wise, over the quarter we reduced our overweight in Consumer Discretionary, as we believe the sector is poised to hit some turbulence due to a change in stance by Central Banks across the Emerging Markets. We have also initiated several positions in the insurance sector (Financials) as we believe it is poised to benefit from rising interest rates and yields. In general, in light of our positive expectations for economic growth and market performance, we continue to hold overweight positions in the cyclical sectors (Consumer Discretionary, Energy, Materials and Information Technology), funded with underweight positions in Industrials and the most defensive sectors –Consumer Staples, Utilities and Healthcare.

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