Wellington Emerging Market Development Fund

WELLINGTON MANAGEMENT®

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MARKET REVIEW

Emerging markets equities fell in October. Asia led the decline, followed by Europe, the Middle East, and Africa (EMEA), and Latin America.

In Asia, China's third-quarter GDP grew 4.6% annually, its slowest pace since early 2023 and down from 4.7% in the second quarter. The sharp property sector downturn, alongside weakening export growth and deflationary pressures, continued to weigh on the economy. The government announced more support for the struggling economy, while the central bank cut key lending rates by 25 bps. India's central bank tweaked its policy stance to "neutral", opening the door for potential rate cuts amid early signs of moderating economic growth. Taiwan's GDP expanded at a higher-than-expected annual pace of 4.0% in the third quarter, as robust AI demand boosted exports.

In EMEA, Saudi Arabia's Ministry of Finance slashed its 2024 GDP forecast to 0.8%, from a previous estimate of 4.4%, and raised its budget deficit estimates for fiscal years 2024 — 2026. In the United Arab Emirates, second-quarter economic growth of 4.1% was driven by a 6.6% increase in the non-oil sector. South Africa's inflation dropped sharply to 3.8% in September, increasing the prospect of another rate cut.

In Latin America, Brazil's inflation accelerated to 4.5% in the 12 months to mid-October, driven by higher residential electricity costs due in part to a major drought. In Mexico, third-quarter GDP surprisingly rebounded at the fastest quarterly pace in more than a year, although economic growth this year has been disappointing.

FUND PERFORMANCE AND ATTRIBUTION

Over the month, the portfolio delivered negative absolute returns but outperformed the MSCI Emerging Market index. Two out of eight themes delivered positive returns, led by the Energy Efficiency and Digital Connectivity themes, while the Social Empowerment and Financial Market Deepening themes detracted from total returns.

At the issuer level, our top two absolute contributors were Advantest and Flat Glass Group, while our top two absolute detractors were Mahanagar Gas and AU Small Finance Bank.

Shares of Advantest, a Japan-based semiconductor testing equipment maker, rose during the period. The company announced fiscal 2Q 2024 results with profits above consensus estimates. Driven by the robust demand for high-performance semiconductors, particularly those related to AI technologies, Advantest has revised its full-year sales forecast upwards and announced a share repurchase program. Shares of Mahanagar Gas declined during the period alongside fellow Indian gas distribution companies. The company reported a second quarter profit decline of 16.5% driven by a surge in fuel costs. Revenues rose 8.6%, but expenses rose 18% year-over-year. Lower production of natural gas that was being sold under a government-set pricing framework has caused the company to obtain gas from the open market, driving up costs.

FUND POSITIONING AND OUTLOOK

In terms of positioning, our investment process, which relies on both fundamental inputs as well as proprietary quantitative models, is currently most constructive on Social Empowerment and Financial Market Deepening. Both themes are currently exhibiting positive momentum, earnings revision trends and attractive valuations relative to historical levels. On the other hand, we are less constructive on Automation & Robotics where all four indicators are looking challenged. Valuations appear lacklustre for Health Care Provision, which leads us to be underweight this theme as well.

Whilst there was weakening sentiment ahead of the US elections, we continue to anticipate a soft-landing scenario with steady economic growth and low recession risk. Coupled with improving corporate earnings and steep valuation discounts, our outlook for Emerging Markets equities remains positive, with increasing alpha opportunities as the upside equity participation broadens. We believe that our capabilities in identifying diverse thematic opportunities, strong fundamental bottom-up security selection, and our risk aware portfolio construction methodology will allow us to capitalise on areas of growth. In times of volatility, we believe that our diversified portfolio positioning across themes – and lack of concentrated single stock positions – should position the portfolio well.

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