Emerging Markets Strategy

MONTHLY COMMENTARY | AUGUST 2021

Our global listed infrastructure strategy outperformed infrastructure indices and equities for the month.

Economic activity continued to be robust during the month, despite increasing infections caused by the COVID-19 variant strains. The effectiveness of vaccines in preventing hospitalisations has allowed mobility restrictions to begin to ease globally. Countries with lower vaccination rates, however, have continued to struggle.

Government policy remained supportive, continuing to implement previously announced stimulus. Bond rates stabilised, with real bonds declining, while the view that the inflation spike is largely transitory continued, albeit with risk to the upside. Strong labour and wage data, combined with large increases in commodity prices, highlight the risk of higher inflation. However, significant slack in labour markets is expected to contain inflation risk. Markets performed solidly on the back of strong economic data.

Meanwhile, the government's regulatory intervention in pushing common prosperity has caused significant pullback in many large-cap stocks in China, mostly in the tech sector.

Portfolio Performance

On a regional basis, Asia Pacific was the top contributor to monthly performance (+1.99%), of which Philippines port operator International Container Terminal Services (+0.99%) and Malaysian airport operator Malaysia Airports (+0.53%) were the lead performers.

International Container Terminal Services is a Philippines-based port operator that operates terminals through long-term concession agreements with local port authorities and governments. Shares rose on strong first-half results, which significantly beat market expectations on both volume growth and unit yield (per 20-foot container equivalent unit or TEU).

Malaysia Airports is one of the world's largest airport operators by passenger numbers. Based in Kuala Lumpur, it operates all but one airport in Malaysia and also has a 100% stake in Istanbul's Sabiha Gokcen airport. Share prices rallied as the reopening narrative started to play out in Malaysia.

Turning to Latin America, Brazilian electric utility CPFL Energia (+0.35%) also performed strongly.

CPFL Energia (CPFE) is a Brazilian integrated electric utility. It is one of Brazil's largest distribution and generation companies, with a 13% market share in distribution and a 3% market share in generation. CPFE's distribution assets include eight separate concessions that are federally regulated and generation assets consisting of a mix of hydro and renewable assets that are underpinned by long-term take-or-pay contracts. CPFL Energia decided to move to a 100% payout ratio for their 2020/2021 dividend, which was a large incremental positive for the stock. This decision hopefully signals higher dividends for the coming years. This announcement has also dampened the perceived risks surrounding unwanted M&A.

Chinese gas utility ENN Energy (-0.36%) was the largest detractor from monthly performance.

ENN Energy is a major listed gas distribution utility in China with a nationwide portfolio of last-mile city gas concessions and the longest operating track record amongst the listed players. ENN Energy was down as first-half results broadly met expectations while the full-year guidance of gas sales dollar margins came in slightly below consensus. There was also profit-taking by investors after a strong year-to-date rally.

All returns are in local currency.

Positioning and Outlook

This strategy is invested in high-quality companies benefitting from structural drivers, with strong cash flow and dividend yields. We have strong conviction in the long-term opportunities within emerging markets listed infrastructure. At the regional level, the strategy is split between Asia Pacific EM (70%) and Latin America (28%), with the remainder in cash. At the sector level, the strategy is split between economically sensitive user pays infrastructure (61%) and regulated and contracted utilities (37%).

For the **Global Infrastructure Emerging Markets Strategy**, the primary quantitative tool in portfolio construction is Excess Return, on which our stock-ranking system is based. As such, driven by valuation, the Investment Committee initiated a position in Chinese electric utility China Resources Power Holdings.

The strategy also used the opportunity to crystallise some gains by exiting Indian energy infrastructure company Petronet LNG and Chinese airport operator Shanghai International Airport.

Monthly Stock Highlight

This month we review Mexican communications company Telesites (SITES).

Telesites is a Mexican communications company with communication towers distributed across Mexico.

SITES rent space on its towers on long-term contracts with duration of 5–7 years. Most of the company's contracted communication towers distributed so far have been with Telcel (owned by Mexico America Movil). These contracts are adjusted for Mexican inflation and, given the financial strength of mobile carriers, the revenue stream is highly predictable.

We believe that SITES is well-positioned to take advantage of both the potential increase in tower densification in Mexico and the gradual conversion of their tower portfolio into a FIBRA structure. A FIBRA structure has significant tax benefits for Telesites whereby local investors are exempt from paying tax on distributions. Over the last year Telesites began the gradual process of ceding towers into a FIBRA, thereby generating significant value for shareholders. This theme is expected to continue over the coming year.

gas consumption (across vehicles, industrial usage, heating and cooking fuel).

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