EMERGING MARKETS

BRAZIL: 3.0 STARS – ATTRACTIVE

- Manufacturing PMI stood at 52.4 in Dec 17, down from 53.5 Nov 17
- Services PMI came in at 47.4 in Dec 17, up from 46.9 in Nov 17
- Composite PMI was recorded at 48.8 in Dec 17, down from 48.9 in Nov 17
- Retail sales rose by 5.9% y-o-y in Nov 17, up from a 2.6% y-o-y increase in Oct 17
- Industrial production rose 4.7% y-o-y in Nov 17 down from a 5.5% y-o-y increase in Oct 17
- IPCA inflation came in at 3.0% y-o-y in Dec 17, rising from a 2.8% y-o-y increase in Nov 17

RUSSIA: 3.5 STARS – VERY ATTRACTIVE

- Industrial production fell -1.5% y-o-y in Dec 17, up from -3.6% in Nov 17
- CPI came in at 2.5% y-o-y in Dec 17, in line with that in Nov 17
- PPI came in at 8.4% y-o-y in Dec 17, up from a 8.0% increase in Nov 17
- Retail sales at 3.1% y-o-y in Dec 17, up from a 2.7% increase in Nov 17

MARKET OUTLOOK

Over the course of January as of 29 January 2018, the 2018 and 2019 earnings estimates for Brazilian corporations were revised upwards by 2.4% and 1.2% respectively. For the whole of 2018 and 2019, the earnings of Brazilian companies are expected to grow 18.9% and 17.5% respectively. Companies which saw the largest earnings upgrades over the month were mixed, and included companies from the materials, utilities, and consumer discretionary sectors. Meanwhile, the earnings estimates of Brazilian banks remained largely unchanged. Pulp and paper companies such as Suzano Papel e Celulose SA, Fibria Celulose SA and Klabin SA, which were also part of the materials sector, saw some of the largest earnings downgrades over the month.

Over in Eastern Europe, the earnings estimates of Russian corporations for the years 2018 and 2019 were revised upwards by 4.5% and 3.9% respectively over the course of January. As of 29 January 2017, the earnings of Russian corporations are expected to rise 15.9% in 2018 before growing 2.9% 2019. Energy companies such as Surgutneftegas OJSC and Rosneft Oil Co PJSC saw some of the greatest earnings upgrades over the month alongside the 8.1% rise in oil prices, although not all energy companies saw similar earnings upgrades, as companies like TMK PJSC and Novatek PJSC were met with earnings downgrades. The earnings revisions of Russian financials too were mixed. Meanwhile, the consumer discretionary and materials sectors saw some of the largest earnings downgrades over the month.

Brazil's economic growth had turned positive in the second quarter of 2017 (0.42% year-on-year) since having fallen into its recession in 2014 and in 3Q 2017, the economy had expanded a greater 1.42% year-on-year. Additionally, economic data released over the month in Latin America's largest economy suggests continued progress towards economic recovery. Industrial production growth and manufacturing PMI, while slightly lower than that their last reported figures, generally continued to suggest a strong pickup in the nation's manufacturing sector. However, in October and November 2017, retail sales had grown by 5.9% and 2.5% year-on-year respectively, softening from the country's high of a 6.2% year-on-year growth in September. This is unsurprising given the uptick in consumer price inflation (CPI) since September on the back of higher power costs. Nonetheless, the nation's CPI continues to be near historical lows, while its unemployment rate has steadily dipped over the last 8 months to 12.0% in November, suggesting an environment that continues to be supportive of consumption. Additionally, the central bank had, in its last policy meeting in December, slashed interest rates by another -50 basis points to a historical low of 7.00%. While the bank had expressed that it "views an additional moderate reduction in the magnitude of easing at the next meeting", borrowing costs are likely to remain near historically low levels over the coming quarters, thus lending further support to economic growth over the near term. Current expectations are for the Brazilian economy to have grown 1.0% in 2017 and to grow 2.5% and 2.8% in 2018 and 2019 respectively.

Over the course of January, economic data released over in Russia continued to point to continued economic improvement. On a year-on-year basis, Russia's industrial production contracted for the second month in a row in December 2017, although its -1.5% year-on-year contraction was up from prior month's -3.6% year-on-year contraction. All 4 sectors (mining; manufacturing; electricity, water & gas; and water supply) had seen production contract on a year-on-year basis in December and November. On a whole, industrial production expansion has softened from its pace in mid-2017. While manufacturing PMI has also softened (from its highs at the beginning of 2017), it has consistently remained above the 50.0 neutral reading through 2017, boding well for manufacturing expansion ahead. At the same time, services PMIs have also trended at levels above that seen in 2016, suggesting a robust pace of expansion. Retail sales had posted a strong uptrend through 2017, and in December 2017 had expanded 3.1% year-on-year, just below the nation's high in the recent quarters (3.2% year-on-year in September 2017). Consumer price inflation had posted a consistent downward trend in recent times while the central bank had continuously lowered interest rates, supporting consumption appetites. In December 2017, the central bank had once again slashed its key rate by another -50 basis points to 7.75%%, its lowest level in more than 3 years.

Over the course of January, the Bovespa Index has risen 10.9% in local currency terms and currently trades at estimated PE ratios of 13.7X and 11.6X for 2018 and 2019 respectively as compared to its fair PE ratio of 11.5X. At this juncture, we **believe that a star rating of 3.0 Stars "Attractive" remains warranted for the Brazilian equity market, given its stretched valuations**. Over in the land of Tsars, the Russian equity market rose 10.5% over the course of January, and was trading at estimated PE ratios of 6.7X and 6.5X for 2018 and 2019 respectively when the year ended, relative to its 7.0X fair PE ratio. We are keeping a lookout for fundamental changes in global oil markets and would adjust the star ratings of the Russian equity market accordingly if appropriate. At this juncture, **we believe that a star rating of 3.5 Stars "Attractive" remains warranted for the market.**

RECOMMENDED FUND:
WELLS FARGO EM EQUITY INCOME A USD ACC
PARVEST EQ RUSSIA EUR