EMERGING MARKETS

BRAZIL: 3.5 STARS – ATTRACTIVE

- Manufacturing PMI stood at 45.2 in Dec 16, down from 46.2 in Nov 16
- Services PMI came in at 45.1 in Dec 16, up from 44.4 in Nov 16
- Composite PMI at 45.2 in Dec 16, down slightly from 45.3 in Nov 16
- Retail sales fell by -3.5% y-o-y in Nov 16, from an upward-revised -8.1% decline in Oct 16
- Industrial production declined -1.1% y-o-y in Nov 16 compared to the -7.3% fall in Oct 16
- IPCA inflation came in at 6.29% y-o-y in Dec 16, easing from a 6.99% y-o-y increase in Nov 16
- Selic rate at 13.00% as of 31 January 2016

RUSSIA: 4.0 STARS – VERY ATTRACTIVE

- Industrial production grew 3.2% y-o-y in Dec 16, up from a 2.7% growth in Nov 16
- CPI came in at 5.4% y-o-y in Dec 16, down from the 5.8% increase in Nov 16
- PPI came in at 7.4% y-o-y in Dec 16, up from a 4.3% increase in Nov 16
- Retail sales fell -5.9% y-o-y in Dec 16, down from a -4.1% decline in Nov 16
- CBR rate at 10.0% as of 31 January 2016

MARKET OUTLOOK

In South America, the earnings outlook of the Bovespa Index this year rose over the month of January (as at 27 January 2016), with estimated earnings for 2017 and 2018 revised upwards by 26.7% and 23.7% respectively. As of 27 January 2016, the earnings of Brazilian companies are expected to increase by 26.7% in 2017 before increasing by 19.9% in 2018. Mixed companies were seen at the top and at the bottom of the table in terms of earnings revisions over the month. Companies with the greatest upward earnings revisions over the month include public investment firm Bradespar SA, pharmaceutical manufacturer Hypermarcas SA, and Banco Santander Brasil SA bank. Meanwhile, companies which saw the largest downward earnings revisions in the month include personal products producer Natura Cosmeticos SA, food conglomerate BRF SA, and steel producer Metalurgica Gerdau SA.

Across the Atlantic in Russia, the RTSI$ Index saw upward revisions in estimated earnings over the month of January (as of 27 January 2017), with the estimated earnings for 2017 and 2018 revised higher by 12.1% and 13.4% respectively. As of 27 January 2017, the earnings of Russian companies are expected to rise 12.1% in 2017 before growing further by 12.4% in 2018. Over the month, the 2017 estimated EPS of the heavy weight materials and the energy sectors have been revised downwards by an average -1.1% and -9.2% respectively. Some of the companies with the largest upward revisions in earnings over the month were Magnit PJSC from the Consumer Staples sector, Rosneft Oil Co PJSC from the Energy sector and Acron PJSC from the Materials sector; while companies with the greatest earnings downgrades were largely from the energy sector and included LUKOIL PJSC, Bashneft PJSC and Surgutneftegas OJSC.

Amid slower-than-expected economic recovery and an encouraging downward trending inflation, the central bank of Brazil had cut the Selic rate by an aggressive -75 basis points in mid-January to 13.00% in an attempt to boost economic recovery. While the country had continued to show improvement with 3Q 2016's decline coming in at a smaller -2.9% compared to 2Q 2016's -3.6% decline, growth in the quarter had disappointed with a -0.8% quarter-on-quarter contraction, the largest seen in 2016. Although the risk of a slower-than-expected recovery remains, the latest economic data released had largely continued to suggest improvement. Apart from the steady decline in inflation to 6.29% in December 2016, retail sales, although volatile, had presented an overall upward trend rather than a downward one. Also, industrial production saw its smallest decline in 2016 (-1.1% year-on-year) in December 2016 and is forecast by economists to see positive growth in January 2017. Furthermore, the impact of Brazil's aggressive rate cut has yet to fully materialise. As of 13 January 2017, a weekly survey of about 100 economist conducted by the Brazilian central bank revealed that the consensus is expecting the economy to grow 0.5% in 2017 before expanding 2.2% the following year.

Over in Russia, economic data released over the month continued to show good progress towards economic recovery. The Markit manufacturing PMI showed an expansion for the fifth consecutive month in December 2016 with a 53.7 reading, and December's Markit services PMI extended its improvement from the previous month, with a 56.5 reading. Recent readings seem to suggest some stabilisation in manufacturing and services PMIs. Industrial production had continued to improve, registering a 3.2% growth in December 2016, its highest in 2016. Additionally, the country's trade surplus had widened 2.2% year-on-year in November 2016 to USD 9.1 billion amid the strongest export growth thus far in 2016. Oil prices have gradually increased through 2016 and given the recent agreement amongst OPEC members and some non-OPEC oil producers, including Russia, to lower oil production starting January 2017, the recovery of oil prices seems to be further encouraged. This comes in positively for Russia, as it is an oil exporter. As at 30 January 2017, the consensus is expecting Russia's economic growth to turn positive in 2017 with a 1.2% GDP growth.

As at 27 January 2017, the Bovespa Index has risen 9.6% year-to-date and currently trades at estimated PE ratios of 13.1X and 10.9X for 2017 and 2018 respectively as compared to its fair PE ratio of 11.5X. This represents a discount from its fair PE ratio when looking at the metric from a longer term perspective (2018 PE ratio). Continued signs of recovery as well as a stabilisation in commodity prices have led us to be slightly less pessimistic about the Brazilian economy which is still struggling at this juncture. As such, **we believe that a star rating of 3.5 Stars "Attractive" continues to be warranted for Brazil's equity market at this juncture**. On the other hand, Russian equities have posted a 3.8% gain thus far as at 27 January 2017 in USD terms and the Russian RTSI$ index currently trades at estimated PE ratios of 7.0X and 6.2X for 2017 and 2018 respectively as compared to its fair PE ratio of 7.0X. Volatility is still expected in the near-term as investment and business sentiment is still weighed down by geopolitical tensions as well as the overall direction of crude oil prices. While **we retain Russia's star ratings at 4.0 Stars "Very Attractive", we are keeping an eye on overall valuations should there be continued gains in stock prices without overall improving fundamentals.**

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