Market Overview

Emerging markets equities fell by 4.2%, in US dollar terms, during the third quarter as concerns over slowing global economic growth and trade tensions dominated the environment. Asian stocks finished the period 3.4% lower. Latin American shares fell by 5.6% and Eastern European stocks fell 2.6%.

In Asia, equities in China were range bound on continuing news concerning trade tensions and tariff increases between China and the United States. Indian stocks were aided by Prime Minister Modi’s re-election and a corporate tax cut, but this was more than offset by signs of a slowing economy. Korean equities were also impacted by concerns over economic growth. However, improving expectations over semiconductor prices helped share prices there and in Taiwan.

In Europe, a large interest rate cut by the central bank of Turkey bolstered the market considerably and especially helped bank stocks. Despite volatile crude oil prices, caused in part by a drone attack on a huge Saudi Arabian oil refinery, and an interest rate cut, Russian shares finished more than 1% lower. European Union tensions over Brexit and a weaker German economy hurt returns in Poland and the Czech Republic. Although Cyril Ramaphosa won a clear mandate as South African President, the market remained unimpressed at the government’s lack of urgency to establish a pro-growth economy.

Latin American markets finished lower during the quarter. Weaker copper prices helped to pressure Chilean share prices. Brazilian equities fell 4.6% despite pension reform legislation moving forward. Mexican equity prices fell despite a Banxico interest rate cut. An August primary election in Argentina favored Peronist candidate Alberto Fernandez over current reformist President Mauricio Macri, resulting in a very large collapse in local share prices. Fernandez is now the clear favorite in October’s presidential election.

By sector, information technology and consumer staples outperformed the index. Materials, real estate, health care, and financials all finished with negative returns.

Portfolio Review

The Lazard Emerging Markets Equity Portfolio outperformed the MSCI Emerging Markets Index during the quarter. Shares of SK Hynix, a Korean manufacturer of semiconductors, were boosted by positive trends in DRAM bit growth and rising NAND flash prices. The management of TSMC, a Taiwanese manufacturer of semiconductors, provided upbeat guidance for the second half of 2019 driven by rising demand for its 7nm chips from companies like Apple and Huawei. Tupras, a Turkish oil refining company, saw an improvement in its products spread in the third quarter of 2019. The management of CCR, a Brazilian toll road operator, provided optimistic guidance for a firming pipeline of potential future projects. ASM Pacific, a Chinese manufacturer of semiconductor assembly and back-end equipment, benefited from TSMC’s bullish outlook on 5G deployments and expectations that the semiconductor cycle had turned. Stock selection in Korea added value.

In contrast, shares of YPF, an Argentine energy company, fell sharply along with the entire Argentine market after the country’s surprising primary election result that indicated a strong likelihood for Fernandez/Kirchner to win the October elections. This was followed by announced 90-day price freezes by President Macri. Shares of Banco do Brasil, a Brazilian bank, corrected on the back of rumors of a potential stake-sale by a closed-end fund. Shares of China Construction Bank, a Chinese bank, declined due to concerns over the escalating trade tensions between the United States and China. Shoprite, a South Africa retail chain, was negatively impacted by its Sub-Saharan businesses due to currency depreciation in those countries. Shares of Bank Mandiri, an Indonesian bank, fell on concerns over slowing economic growth. A higher-than-benchmark exposure to Argentina hurt returns.

Recent Activity and Trade Rationale

During the quarter we purchased IRB Brasil Resseguros, a Brazilian reinsurance company, and Mondi, an integrated global paper and packaging company. We sold Woolworths, a South African supermarket and retail chain, YPF, an Argentine energy company, and Imperial Logistics, a South African provider of logistical services.

Outlook
While macroeconomic and political issues will continue to influence the asset class, we believe that emerging markets economic growth will endure despite the recent decline in global growth expectations. We also believe that there could be renewed confidence in some of the more economy sensitive stocks. Given the trouble spots as well as areas of great potential in the current markets, skilled stock selection remains essential.

Important Information

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The MSCI Emerging Markets Index is a free-float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. The MSCI Emerging Markets Index consists of 26 emerging markets country indices: Argentina, Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Pakistan, Peru, Philippines, Poland, Qatar, Russia, Saudi Arabia, South Africa, Taiwan, Thailand, Turkey, and United Arab Emirates. The index is unmanaged and has no fees. One cannot invest directly in an index.

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