KAMES CAPITAL

Emerging market backdrop

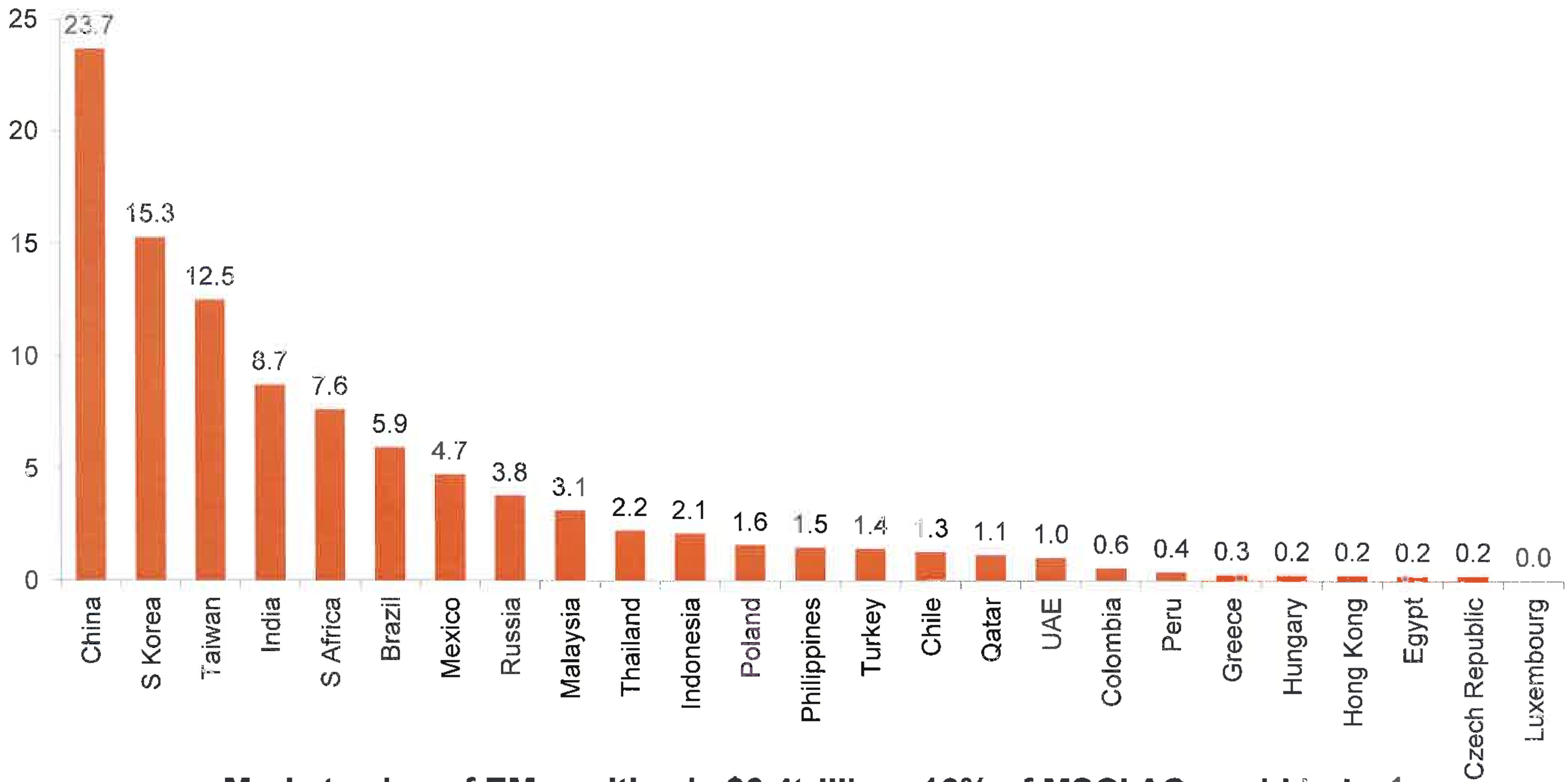
October 2015

Scott M Jamieson – Head of Multi-Asset Investing

an AEGON Asset Management company

Emerging equity markets – country composition

KAMES CAPITAL



▶ **Market value of EM equities is $6.4trillion; 16% of MSCI AC world index[1]**

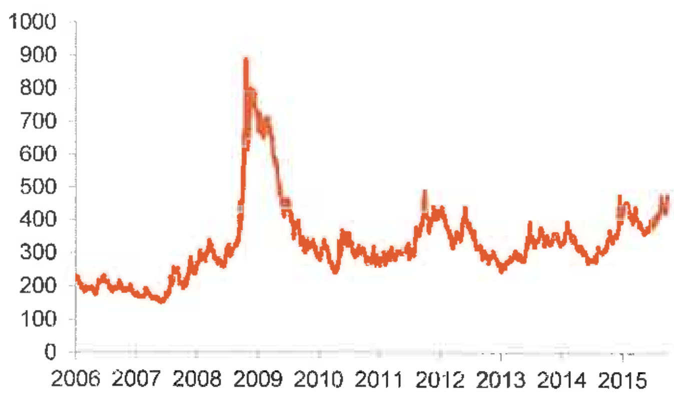
Source: iShares MSCI EM ETF. [1]based on MSCI data, source Bloomberg as at September 2015

Emerging market performance

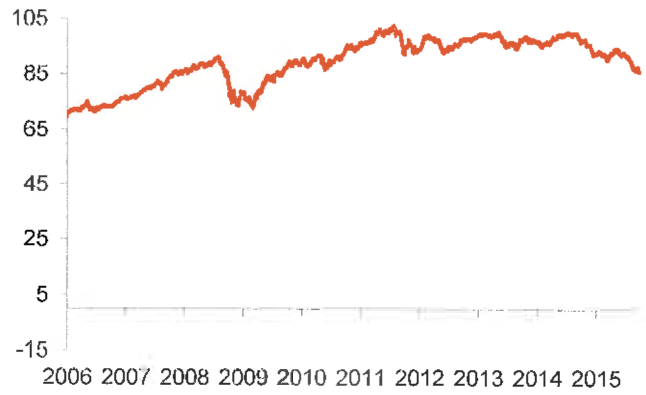
- **Emerging equity markets have underperformed developed markets badly**
  - More than unwinding the relative performance over past ten years
- **Emerging debt markets have seen yields spreads (over hard currency bonds) rise**
  - To levels only breached in the financial crisis
- **Emerging market currencies were last to slip**
  - Down 15% vs US$ over past year

EM vs DM equity (local FX)

JP Morgan EMBI Bond Spread (bps)



Emerging market currencies (vs US$)

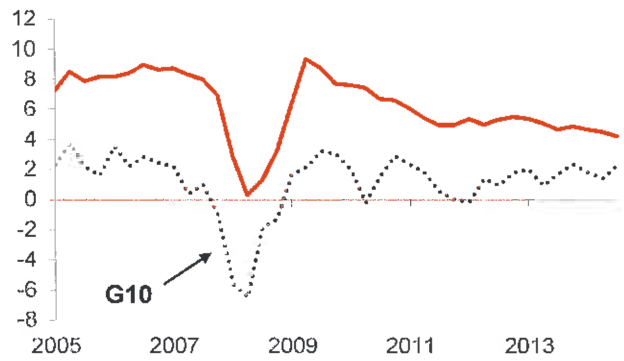


Source: Bloomberg and DataStream as at September 2015.

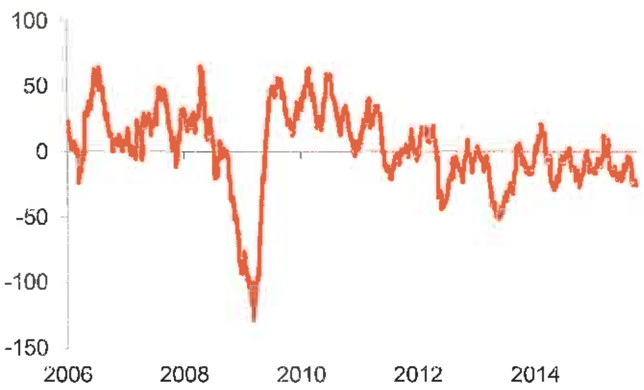
Emerging market economics

- Emerging equity market weakness coincides with downshift in economic growth
  - And a narrowing of the growth premium to developed markets
- Economic data continues to undershoot expectations
- Emerging market inflation has been declining
  - And faster than expectations

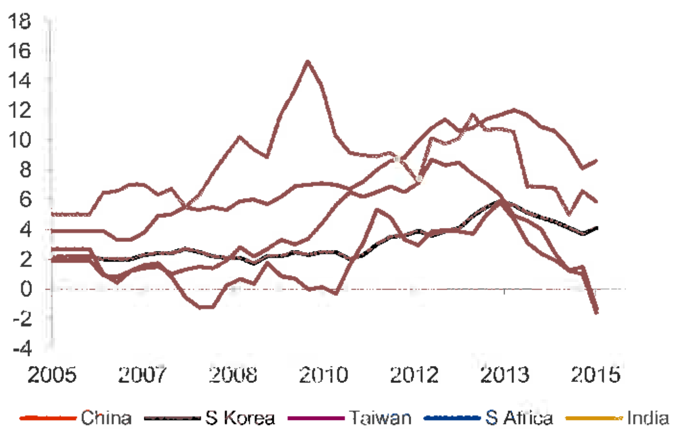
Emerging market real economic growth (% p.a.)



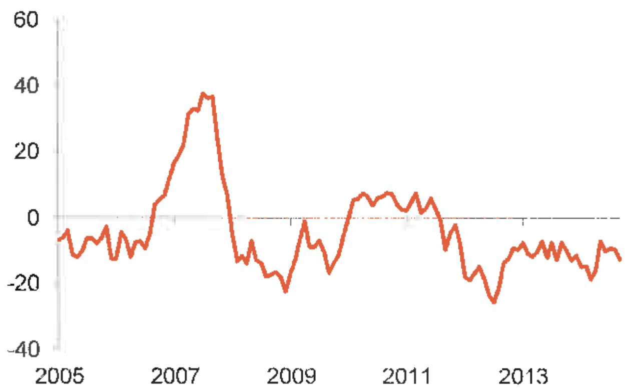
Emerging market economic surprises



Selected emerging market inflation rates (% p.a.)



Emerging market inflation surprise index

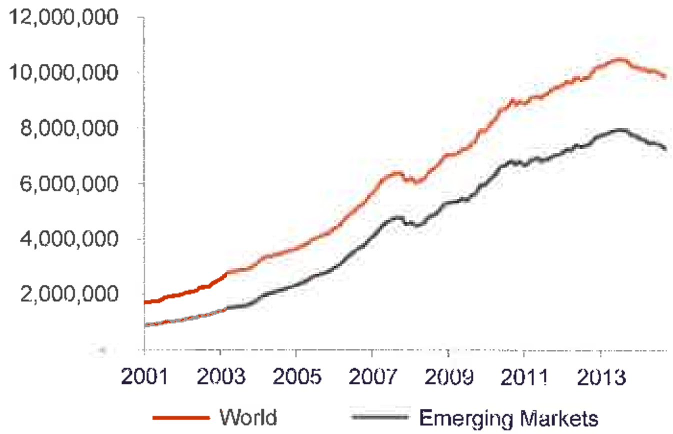


Source: Bloomberg as at August 2015

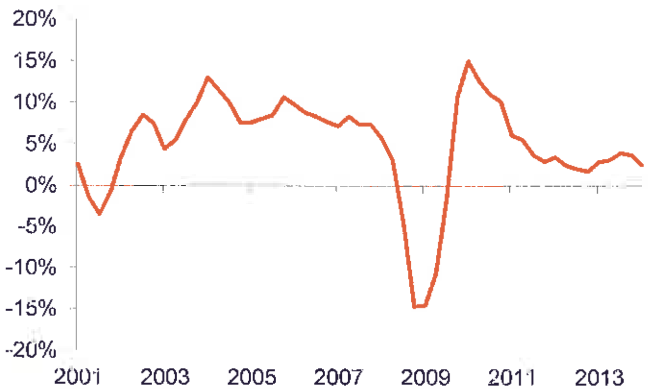
Reserve balances and trade flows

- **Emerging nations have tended to accumulate their trade profits in central bank reserves**
  - If used instead to fuel consumption then world's imbalances would be much less
- **World trade growth has fallen steadily since the financial crisis**
  - Putting pressure on trading nations
- **EM nations are starting to drawdown on their 'nest eggs'**
  - Adding to pressure on investment markets

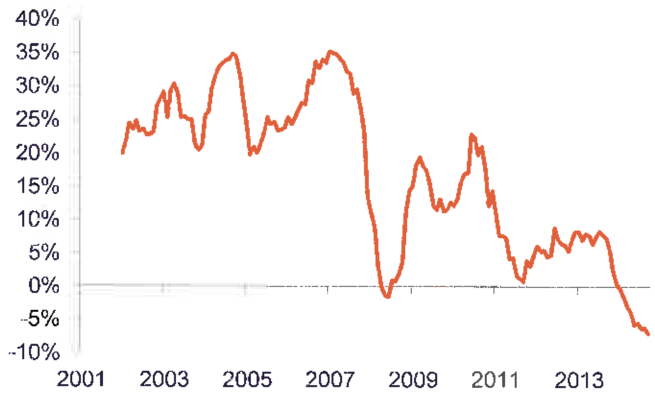
Central Bank Reserve Assets ($bn)



World Trade (%, yoy)



Change in EM Reserves (yoy)

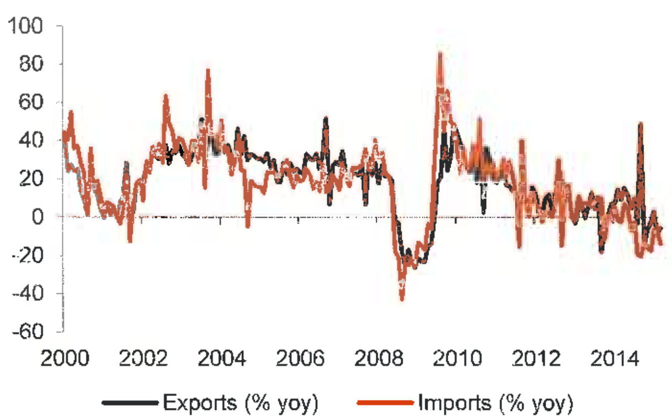


Source: Bloomberg as at August 2015.

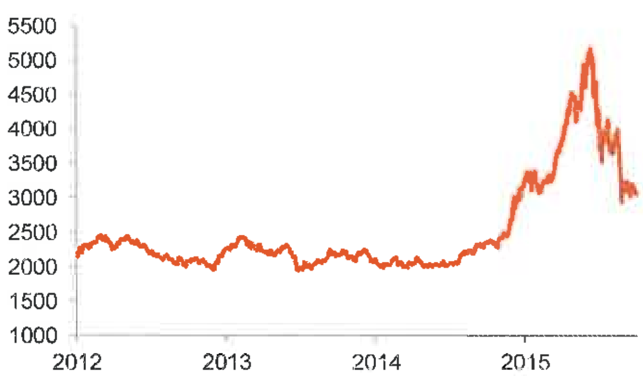
China

- **China has been hit by declining world trade**
  - And an appreciating currency
- **Chinese economic model is being transformed from investment focused to consumption led**
  - Putting pressure on its raw material 'suppliers'
- **Chinese policy being discredited**
  - The move to generate a wealth effect via the equity market has failed
- **Cutting interest rates too far risks capital flight**
  - So monetary conditions – everywhere – stay far too tight

Chinese trade flows



Chinese equity market



China real trade weight currency index

Source: Bloomberg and Datastream as at September 2015.

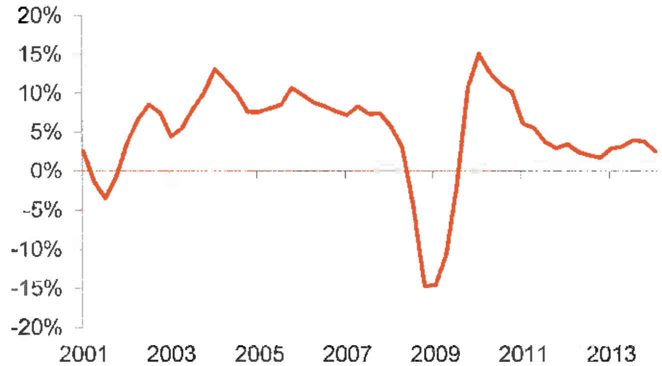
EM – a perfect storm?

KAMES CAPITAL

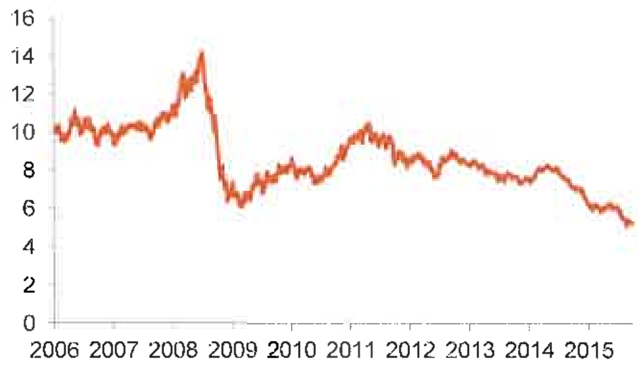
- In summary emerging markets are having to face:
- A resurgent US$
  - Keeping capital in the US and straining US$ borrowing lines (significant for EM corporates)
- A re-orientation of Chinese economy
- Weak world trade
- Slumping commodity markets

US trade weight currency index

World Trade (%, yoy)



Commodity markets (Bloomberg index)



Source: Bloomberg as at September 2015

EM – things can only get better?

KAMES CAPITAL

EM: Price to Book

EM PE Multiple

Perhaps, equities do look reasonably cheap

Improvement could come from:

- **A stabilisation of the US$**
  - Limited US interest rate hikes would help
- **Constructive use of the reserve balance**
  - To fuel much needed infrastructure investment across EM
- **A healthier world economy**
  - The goal of central bank policy everywhere

Source: Bloomberg as at 29 September 2015

Important information

KAMES CAPITAL

This document is not intended for retail distribution and is directed only at investment professionals. It should not be distributed to, or relied upon by, private investors.

All data in this presentation is sourced to Kames Capital unless otherwise stated.

The views expressed in this document represent our understanding of the current and historical positions of the market. They should not be interpreted as a recommendation or advice.

This document is accurate at the time of writing but can be subject to change without notification. Kames Capital is an Aegon Asset Management company and includes Kames Capital plc (Company Number SC113505) and Kames Capital Management Limited (Company Number SC212159). Both are registered in Scotland and have their registered office at Kames House, 3 Lochside Crescent, Edinburgh, EH12 9SA. Kames Capital plc is authorised and regulated by the Financial Conduct Authority (FCA reference no: 144267). Kames Capital plc provides segregated and retail funds and is the Authorised Corporate Director of Kames Capital ICVC, an Open Ended Investment Company. Kames Capital Management Limited is an appointed representative of Scottish Equitable plc (Company Number SC144517), an Aegon company, whose registered office is 1 Lochside Crescent, Edinburgh Park, Edinburgh, EH12 9SE (PRA/FCA reference no: 165548).