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A brighter outlook for emerging markets

While the first half of 2022 witnessed a harsh sell-off in emerging markets (EM), the period ended with hope for the second half as EM stocks, bonds and currencies started to outperform global peers in the second quarter. SKAGEN Kon-Tiki outperformed its benchmark index in the quarter.

As the US withdraws its extraordinary policy support, its growth outlook is deteriorating; macro data has continued to wane with softer consumer spending, deteriorating sentiment and subdued manufacturing, suggesting that the US economy now has a more fragile foundation. As we pivot away from higher inflation to weaker global growth and looming recession risk as the dominant market drivers, most commodities nosedived towards the end of the period.

As the largest economy in EM, the Chinese stock market has decoupled from the US market recently due to diverging monetary policies and economic cycles. With a gradual easing of Covid restrictions, various activity indicators are bouncing back. We may be through the worst for the property sector as a new mortgage rate-cutting cycle finally kicked off towards the end of the quarter. China has started dialling back regulatory measures while also ramping up policy support.

With the global business cycle set to slow over the next few quarters, relative growth differentials are starting to point in EM's favour again. A trough in the China cycle, still resilient labour markets in many EMs and fiscal policies should help to cushion the slowdown.

Attribution

As the country's largest producer of offshore crude oil and natural gas, the China National Offshore Oil Corporation (CNOOC) is benefiting from high energy prices due to Russian sanctions and the supply-chain shock. Its strategic focus on boosting natural gas production is critical to the success of efforts to reduce the country's carbon emissions. This is an added bonus to the investment case.

Prosus and Naspers' decision to start selling down their Tencent holding and buy back their own shares was a welcome U-turn which led to a significant rerating at the end of the quarter. Also promising is management's comment that they are supportive of going beyond this to reduce complexity combined with a new incentive KPI which ties the management payout directly to a reduced discount.

The largest detractor in the quarter was Atlantic Sapphire. At the end of the period, the company raised USD 125m in a widely expected private placement. At the same time, DNB confirmed almost the same amount as committed debt which means Atlantic Sapphire should now be fully funded for their phase 2 expansion and to reach steady state phase 1 harvest. Nordlaks, one of the largest private salmon farmers in Norway, participated in the private placement.

Other detractors in the quarter included our South Korean holdings LG and Samsung Electronics. As the global economic downturn and inflation have intensified, there is now a built-in expectation that demand for home appliances and TVs will continue to slow and adversely affect profitability combined with a more muted semi-cycle.

Portfolio activity

Three new companies entered the portfolio in the quarter. Cosan is a Brazilian sugar and energy conglomerate in which we have previously been long-term shareholders. They have reduced the holding complexity, the company trades at an attractive valuation, and they are now ready for a new growth phase within some of their well-run holding companies. One of these is Raizen, which is the second company we invested in. Raizen is Brazil's largest sugar and ethanol producer. The company is now expanding heavily in the greener/renewable side of the energy equation with some exciting growth projects. Lastly, we now have a small holding in Sibanye Stillwater, which offers differentiated exposure to precious metals and therefore portfolio diversification.

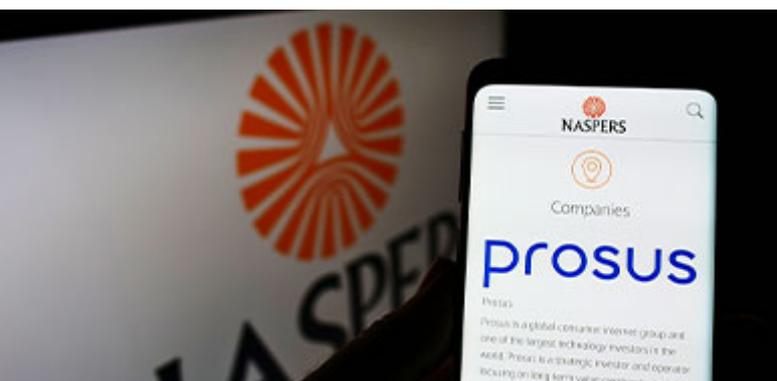


Photo: Shutterstock

We exited Orbia as we are concerned that their newly announced investment plan may be coming at the peak of the cycle, with most being invested in highly cyclical assets at a time when the cycle as well as the cost of capital seem to be heading in the wrong direction. We also exited Sinotrans, a Chinese logistics company, as we have been disappointed by the scant operational progress over the past few quarters.

We continue to be cautiously optimistic that some value can eventually be recovered from our Russian holdings which continue to be priced at 0. There have been no trading activities in the Russian holdings during the quarter.



Photo: Shutterstock

Outlook

Even though Emerging Markets continue to battle rough seas for now, we believe that the portfolio consists of very attractive and robust companies trading at a significant discount. Given where we stand in the interest rate cycle globally, the odds should be stacked in favour of our value-based investment philosophy. The portfolio is highly diversified and consists of companies with strong prospects. It trades at a heavily discounted 6x 22x P/E, which is more than a 40% discount to EM in general. The historically high discount of EM versus DM started to reduce this quarter, and we are cautiously optimistic that this could continue.

The fund selects low-priced, high-quality companies, mainly in emerging economies. The objective is to provide the best possible risk adjusted return. The fund is suitable for those with at least a five year investment horizon. Subscriptions are made in fund units and not directly in stocks or other securities. The fund has risk profile 6. The benchmark reflects the fund's investment mandate. Since the fund is actively managed, the portfolio will deviate from the composition of the benchmark.

Historical performance (net of fees)

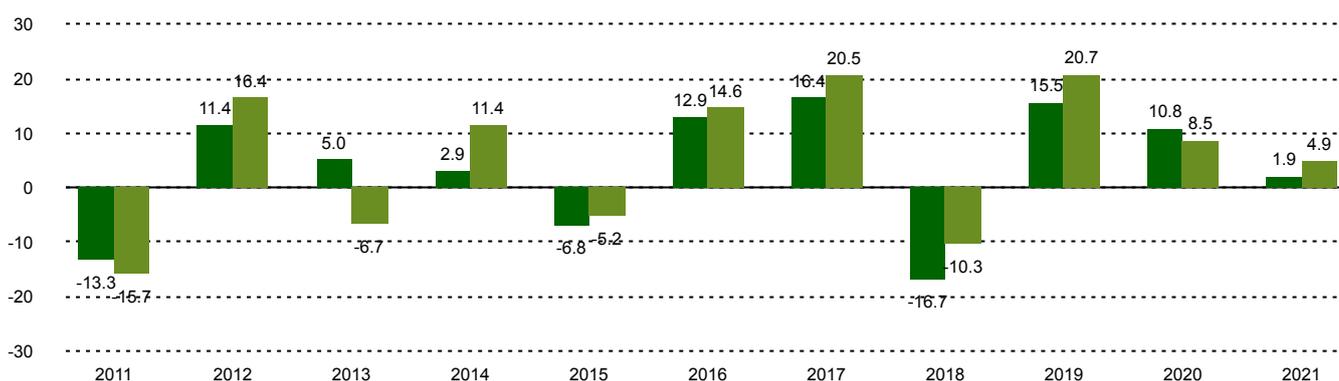
| Period | SKAGEN Kon-Tiki A | Benchmark index |
|-----------------|-------------------|-----------------|
| Last month | -6.2% | -4.3% |
| Quarter to date | -4.7% | -5.8% |
| Year to date | -13.3% | -10.4% |
| Last 12 months | -22.0% | -15.2% |
| Last 3 years | -0.3% | 3.4% |
| Last 5 years | 0.2% | 4.0% |
| Last 10 years | 3.0% | 5.1% |
| Since start | 9.9% | 6.9% |

Fund Facts

| | |
|----------------------------|-------------------------------------|
| Type | Equity |
| Domicile | Norway |
| Launch date | 05.04.2002 |
| Morningstar category | Global Emerging Markets Equity |
| ISIN | NO0010140502 |
| NAV | 88.14 EUR |
| Fixed management fee | 2.00% + performance fee* |
| Total expense ratio (2021) | 1.67% |
| Benchmark index | MSCI EM NR USD |
| AUM (mill.) | 1245.22 EUR |
| Number of holdings | 48 |
| Portfolio manager | Fredrik Bjelland Cathrine Gether |

*10.00% performance fee calculated daily and charged annually if the fund's value development is better than the benchmark. The total management fee charged represents a maximum of 4.00% p.a. and a minimum of 1.00% p.a. The performance fee may be charged even if the fund's units have depreciated in value if the value development is better than the benchmark.

Performance last ten years



■ SKAGEN Kon-Tiki A ■ MSCI EM NR USD The benchmark is MSCI EM Index. This index did not exist at the fund's inception, consequently the benchmark prior to 1/1/2004 was MSCI World AC Index. This is not reflected in the graph above which shows MSCI EM Index since the fund's inception.

Historical returns are no guarantee for future returns. Future returns will depend, inter alia, on market developments, the fund manager's skill, the fund's risk profile and management fees. The return may become negative as a result of negative price developments. There is a risk associated with investing in the fund due to market movements, currency developments, interest rate levels, economic, sector and company-specific conditions.

Contributors in the quarter



Largest contributors

| Holding | Weight (%) | Contribution (%) |
|-------------------------|------------|------------------|
| CNOOC Ltd | 5.89 | 1.20 |
| Prosus NV | 2.89 | 1.06 |
| WH Group Ltd | 2.26 | 0.79 |
| Ping An Insurance Group | 7.42 | 0.70 |
| China Life Insurance | 2.32 | 0.60 |



Largest detractors

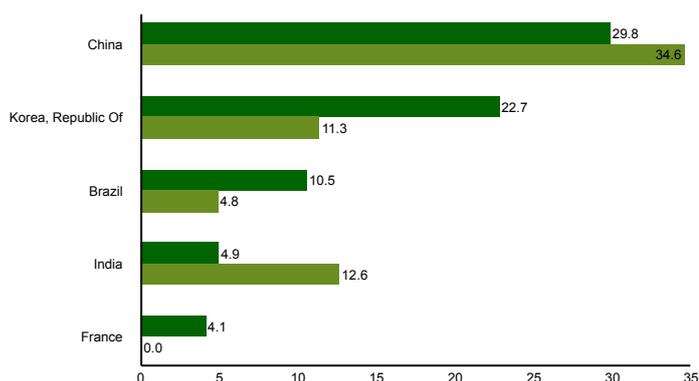
| Holding | Weight (%) | Contribution (%) |
|----------------------|------------|------------------|
| LG Electronics | 7.07 | -1.65 |
| Samsung Electronics | 5.87 | -0.75 |
| Atlantic Sapphire | 1.02 | -0.66 |
| Ivanhoe Mines | 1.63 | -0.53 |
| Sendas Distribuidora | 4.20 | -0.39 |

Weights shown are the average for the period. Absolute contribution based on NOK returns at fund level.

Top ten investments

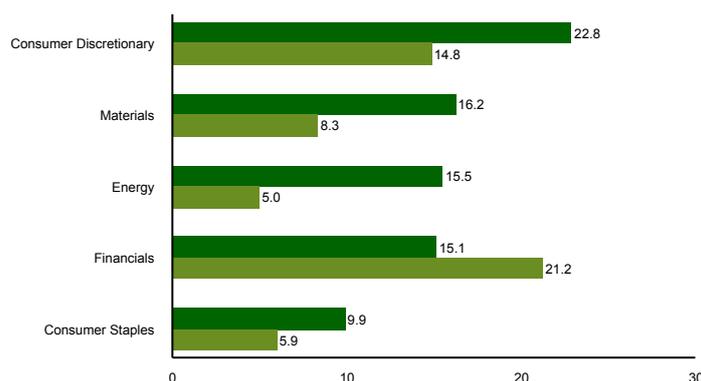
| Holding | Sector | Country | % |
|---|------------------------|--------------------|------|
| Ping An Insurance Group Co of China Ltd | Financials | China | 7.8 |
| LG Electronics Inc | Consumer Discretionary | Korea, Republic Of | 5.4 |
| Samsung Electronics Co Ltd | Information Technology | Korea, Republic Of | 5.1 |
| Cnooc Ltd | Energy | China | 5.1 |
| TotalEnergies SE | Energy | France | 4.1 |
| Shell PLC | Energy | Netherlands | 4.0 |
| Suzano SA | Materials | Brazil | 3.9 |
| Hyundai Motor Co | Consumer Discretionary | Korea, Republic Of | 3.9 |
| Prosus NV | Consumer Discretionary | China | 3.8 |
| Sendas Distribuidora SA | Consumer Staples | Brazil | 3.7 |
| Combined weight of top 10 holdings | | | 46.8 |

Country exposure (top five)



■ SKAGEN Kon-Tiki A ■ MSCI EM NR USD

Sector exposure (top five)



■ SKAGEN Kon-Tiki A ■ MSCI EM NR USD

Important information

This report is intended for investment professionals only. All information is based on the most up-to-date data available. Unless otherwise stated, performance data relates to class A units and is net of fees. AUM data as per the end of the previous month. Except otherwise stated, the source of all information is SKAGEN AS. SKAGEN AS does not assume responsibility for direct or indirect loss or expenses incurred through use or understanding of this report. Employees of SKAGEN AS may be owners of securities issued by companies that are either referred to in this report or are part of a fund's portfolio.



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