

While emerging markets may only represent 29% of the allocation of the international index, it deserves a far larger percentage of a manager's attention. These markets are too large, diverse, and complex to be managed as an afterthought. Equally, the cost in terms of forgone alpha¹ potential is too high.

An Impossibly Large International Universe

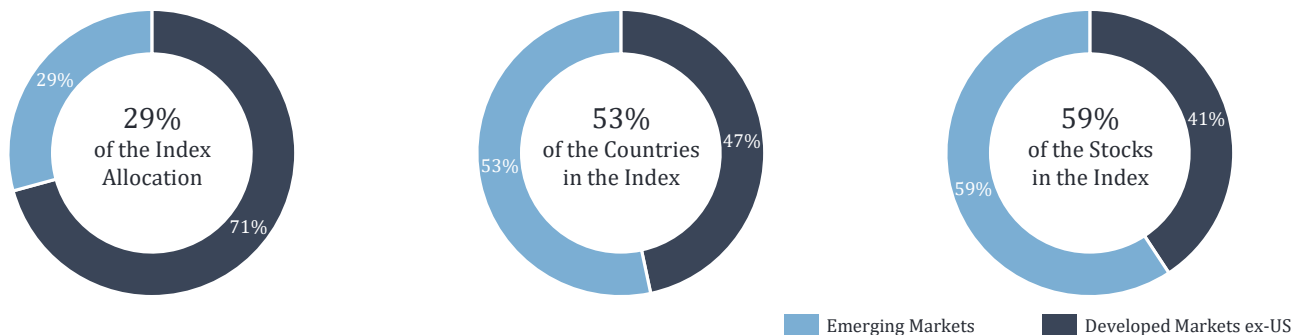
45 countries. 2,237 stocks². The international equity universe as defined by the MSCI AC World ex-US Index leaves investors with an impractically large universe. The natural question is whether it is possible for even an experienced investor to cover such a large universe in appropriate depth. Faced with this dilemma, allocators are encouraged to rethink the universe and split it into more manageable sub-segments: emerging and developed markets.

Emerging Markets: An Increasing Part of International Markets

The steady growth in the size and importance of emerging markets should not be overlooked. As recently as 2004 these markets represented only 10% of the international index. The allocation has grown almost three times since then³. Similarly, the number of stocks within these markets have multiplied over four times in the past 20 years⁴. While emerging markets today represent just under 30% allocation within the MSCI AC World ex-US index, they represent more than half of its countries and 59% of its stocks.

Each country has its own economic, political and market dynamics to be analyzed and each stock their own fundamentals to be dissected. So, while emerging markets have rapidly grown as a segment within international markets, managers trying to cover the full universe have generally struggled to expand their coverage at the pace of this evolution.

Emerging Markets as a Share of MSCI AC World ex-US Index



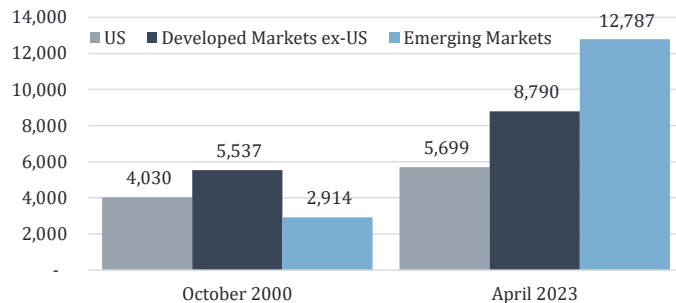
Source: MSCI and Bloomberg as of May 31, 2023.

Growth of Emerging Markets in the MSCI AC World ex-US Index



Source: MSCI and Bloomberg as of May 31, 2023.

Stock Universe with over \$100M Market Cap: 2000 vs 2023



Source of October 2000 Data: MSCI, FactSet as of October 31, 2000. Includes all stocks by country with market caps over \$100M. Source of April 2023 Data: MSCI, Bloomberg. Country weights as of April 30, 2023. Data based on Bloomberg EQS screen that includes all stocks by country with market caps over \$100M as of April 30, 2023. Developed and Emerging Market country definitions based on MSCI classifications.



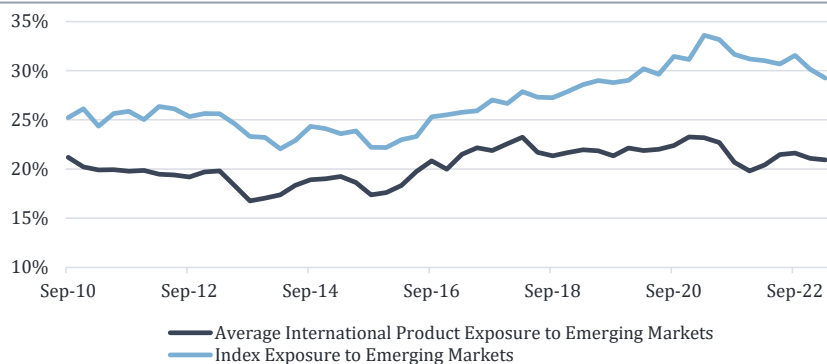
Emerging Markets Inefficiency & the Alpha Opportunity

It is generally accepted that emerging market equities are priced more inefficiently than developed market equities. Not only are information asymmetries more significant, but in many cases the large presence of retail investors creates further opportunities. This backdrop makes emerging markets fertile ground for skilled active managers to generate substantial alpha via stock selection. However, for this inefficiency to translate into value, investors must have the time, focus and mandate to scour this large and complex universe to find these opportunities.

Pitfalls of a Combined Allocation

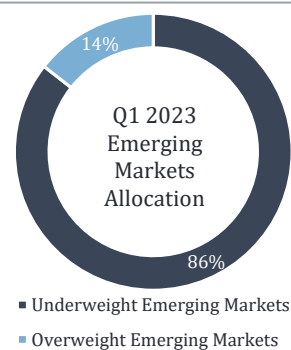
Without the bandwidth to perform appropriate diligence, many international strategies “make do”. In the past, we found that approximately 80% of international products were underweight emerging markets⁵. Although all these strategies were benchmarked to an index that includes emerging markets, they were on average underweight the asset class by 28%⁶. Further, when these products were able to generate alpha within emerging markets, it tended to be driven by style, country and/or sector bets, rather than stock selection.

International Products Consistently Underweight Emerging Markets



Source: eVestment as of Q1 2023. Universe defined as all active products within eVestment’s “All ACWI ex-US Equity” universe with over \$100M in AUM. Universe filtered to include only products with a preferred benchmark of MSCI ACWI ex-US Equity, MSCI ACWI ex-US Growth Equity, MSCI ACWI ex-US Value Equity and MSCI ACWI ex-US Small Cap Equity

International Products by Emerging Markets Allocation



Conclusion

Once an afterthought for most managers focused on international markets, emerging markets have grown to become a core part of the non-US equity universe. Their diversity and inefficiency offer active managers an excellent opportunity for alpha generation, however, the magnitude and complexity of underlying markets require dedicated resources. Moreover, the rapid growth of these markets suggests that the challenges of covering the full suite of international countries in one mandate will continue to grow. We believe the best way to extract alpha and outperform in these markets is to separate developed from emerging countries, and to partner with local specialists who can take advantage of the inefficiencies within their home markets.

ABOUT ABS GLOBAL INVESTMENTS

ABS Global Investments is a global investment firm, focused on fundamental equity strategies around the world. Our investment process consists of sourcing specialized managers, conducting continuous due diligence, and providing our investors with transparent access to our strategies and team. Currently ABS manages over \$6 billion, mostly on behalf of Pension Funds, Endowments and Foundations.

Our emerging markets strategies aim to generate alpha within an asset class recognized for its inefficiency and return potential. The core of our approach is a focus on local specialists who have a geographical and cultural advantage in identifying alpha opportunities within these highly diverse markets. With almost two decades of experience investing in emerging markets, we have cultivated a global network to source and diligence talented specialists. The resulting alpha generation is not dependent on style biases or country selection, but rather on the stock picking of local specialists in their own markets.



GREENWICH
537 Steamboat Road, 4th Floor
Greenwich, CT 06830
+1-203-618-3700

ZURICH

HONG KONG

www.absinv.com

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¹ Alpha is the measurement of the performance of an investment compared to a certain benchmark, usually a stock market index.

² Number of countries and stocks within the MSCI AC World ex-US Index as of May 31, 2023.

³ Emerging Market countries as a percent of MSCI AC World ex-US Index as of May 31, 2023.

⁴ Refers to stocks within each stock market defined as an emerging market by MSCI, with at least \$100M in market capitalization. As of April 30, 2023

⁵ Data based eVestment as of Q1 2023. Universe defined as all active products within eVestment's "All ACWI ex-US Equity" universe with over \$100M in AUM. Universe filtered to include only products with a preferred benchmark of MSCI ACWI ex-US Equity, MSCI ACWI ex-US Growth Equity, MSCI ACWI ex-US Value Equity and MSCI ACWI ex-US Small Cap Equity. Considers data from Q1 2019 through Q1 2023.

⁶ IBID

