Title: Emerging Markets Update 2Q2025

Description: Portfolio Manager Akhil Subramanian provides an update on the second quarter for our Emerging Market strategies.

Transcript:

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Hello, I'm Akhil Subramanian. I'm one of the portfolio managers here at Pzena Investment Management and I'm here to give you an update on the second quarter of 2025.

Now, the second quarter was quite volatile because it included all of the announcements around Liberation Day and the subsequent fallout. But despite all of that, EM was actually up approximately 12% in the quarter.

Again, just like it is every quarter, there was a fair amount of dispersion between countries. South Korea, Greece, and Taiwan, for example, were up more than 25%, and then Thailand and China were more of the laggards—up very, very modestly—and that has to do with a little bit of macro uncertainty in Thailand as well as some potential political instability.

And on the China front, as we all know, China has been one of the countries that has pushed back against some of the Liberation Day tariffs, and that has continued to present a little bit of uncertainty on Chinese valuations.

Now we are by no means out of the woods yet. We're currently in the tariff pause, so there still is time for additional developments on the tariff front. But what we have seen is company-specific volatility, especially around tariffs.

And what we do at Pzena is try to take advantage of that—try to look through on a five-year horizon and ideally buy a business that is trading at a low multiple of mid-cycle earnings.

In terms of our contributors and detractors:

Our top contributor was TSMC—Taiwan Semiconductor Manufacturing Company. This was more of a reversal of what had happened in the first quarter after the news of Deepseek. The company continues to produce good results. Its chips are in strong demand. Despite the prevalence of Deepseek, there still continues to be strong demand for GPUs and other kinds of semiconductor chips. And the company continues to widen its lead between Samsung and Intel.

The next three contributors were all Korean financials—so DB Insurance and then two of our banks: KB and Shinhan. This is a combination of valuations being very, very compelling in Korea and some lifting of the uncertainty around some of the news flow that happened at the end of last year, where the president had enacted martial law and was subsequently impeached. Korea had elections, they've elected someone who's a bit more business-friendly, and as a result, you've seen some of the valuations of these companies re-rate.

In terms of detractors:

Our top detractor was Alibaba. This has been one that has sort of bounced around over the last six to twelve months—it's either been a strong contributor or a strong detractor. The reason around Alibaba detracting was sort of an okay set of results and then the lingering uncertainties in the Chinese economy, especially around domestic consumption, given that China sort of engaged more aggressively in the trade war and the tit-for-tat tariffs with the U.S. We don't believe anything has meaningfully changed to the Alibaba franchise. We still think it's a very compelling valuation as things stand today, and we're excited to see the progress that they've been making in their e-commerce and cloud efforts.

Another detractor in Brazil was Banco do Brasil. This is one of the leading banks in Brazil. The bank is currently just facing some elevated non-performing loans in its ag book—its agriculture book. Again, this will continue to weigh on results for the next quarter or two. But when it comes to the business itself, the bank is pretty well-capitalized and can navigate through this period of elevated credit losses. And at the end of the day, we don't believe anything has directly harmed its franchise. It still is a leading bank in Brazil with low-cost deposits and really strong franchises across personal, consumer, corporate, and ag.

The last detractor was Beijing Oriental Yuhong. This is a waterproofing company that we own in the EM portfolio. Yuhong is just facing a little bit of additional competitive dynamics in the waterproof coating sector. There's been sort of a mild price war over the last three to six months, but this company is very nimble and has navigated a very challenging property segment over the last three to four years and has really grown its retail business.

Yuhong, going back in history five or six years, really focused on the property developers in China. But since then, it has expanded to have more of a retail presence—so more about personal home renovation and the builder channel and things like that. And so we believe that the company is well-equipped to navigate through this sort of uncertainty in the Chinese macro landscape.

In terms of activity, we had two new buys in our portfolio.

The first one was Arcos Dorados. Arcos Dorados—for those of you who speak Spanish—means “Golden Arches.” This is the McDonald's franchisee in Latin America. So they have exclusive rights to distribute and run the McDonald's restaurants in Latin America across 20 countries. And this is a good example of Pzena’s investment discipline. We looked at this business last year and we actually passed on it because, as much as we liked the business, the valuation just wasn't cheap enough for us to get comfortable.

What's happened in the last three to four months is there's been uncertainty on the macro front in Latin America. And so visitation to quick-service restaurants in Brazil—which is their largest market—was down in Q1. On top of that, there's been elevated beef prices, which has pressured their cost of goods sold and their gross margins. We believe ultimately these things will end up being temporary, and the company has a really dominant position in the QSR space and continues to see a very long runway of store potential opportunities.

So this is an example of us liking a business, having to pass on it because of our strict valuation criteria, and then getting an opportunity to buy it further down the line.

The second business we bought in the portfolio is an Indian outsourcing company—WNS.

WNS has been plagued by the losses of three customers over the past couple of years, and generally people seem to link that to some kind of AI disruption. While we believe that there is a real threat from AI, WNS is not like your traditional IT services company. They focus on much smaller-ticket and much smaller businesses and are really helping think about process refinement and outsourcing of an entire process—not just something BPO like a call center.

We believe that this is a good business that is going to continue to benefit from clients trying to harness technologies like cloud and AI. And they are the go-to for their clients in very specific verticals such as insurance and travel. We believe that the company continues to have a really good runway despite this idiosyncratic loss of a couple of customers. And so we were excited to add that one to our portfolio because it really speaks to our investment process—a company going through what we believe is a temporary period of disruption, but at the end of the day still has pretty strong fundamentals and a very unique value proposition for the clients that it serves.

So in a nutshell, that's what happened in the second quarter of 2025. I think despite the strong performance of EM, there continue to be a lot of uncertainties—especially on the tariff front and the subsequent knock-on effects for what might happen to economic growth.

We're keeping a careful eye on our portfolio as we think about potential tariff developments, and also looking outwardly into the world of EM to look for interesting investment opportunities—companies such as Arcos Dorados or WNS that may be unfairly punished by the market.

So, we look forward to giving you an update next quarter.

Thank you.

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