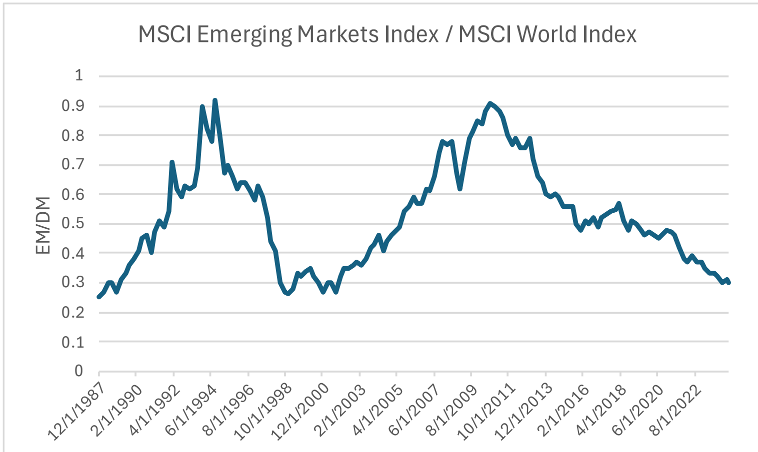
PERSPECTIVES – FROM THE MONTH IN REVIEW

JULY 2024 EDITION

As of July 31, 2024

***CHART OF THE MONTH* – Emerging vs. Developed Markets**

The chart below shows that emerging markets (represented by the MSCI EM Index) rallied during prior inflationary cycles – notably in 1994 and more recently in 2010. Emerging markets are also currently very inexpensive relative to developed markets (represented by the MSCI World Index). The last time the EM/DM ratio was so stretched was in the 2000 tech bubble.



Source: Bloomberg, Sophus Capital.

***QUOTE OF THE MONTH* – Closer to Cutting**

"If we were to see inflation moving down…more or less in line with expectations, growth remains reasonably strong, and the labor market remains consistent with current conditions, then I think a rate cut could be on the table at the September meeting."

- Federal Reserve Chair Jerome Powell in a press conference following the July Federal Open Market Committee Meeting in Washington.

***IN SUMMARY* – Political Tides Change & the Impact on EM**

GLOBAL ECONOMIC BACKDROP:

- The International Monetary Fund (IMF) published its latest World Economic Outlook update in July, with global growth expected to reach 3.2% this year and next, well below the 3.8% average established since the turn of the century until the pandemic.
- GDP growth differential expectations remain in emerging markets' favor over developed markets, 4.2% vs. 1.7% in 2024 and 4.2% vs. 1.8% in 2025. Standouts in EM include India, expected to maintain robust GDP growth of 6.8% in 2024 and 6.5% in 2025, as well as China, with IMF expectations falling below the Chinese guided 5% GDP growth target over the next two years (4.6% and 4.1%, respectively).
- Global headline inflation in June moved below 2.5%, only marginally above pre-pandemic levels, with food and energy running near or below historical averages, and global goods now close to zero. Softer pressures on goods sectors are also reflected in producer price indexes (PPI), with global PPI prices roughly flat over the last year. In contrast, global services inflation continues to trend downward though more slowly.
- Global export volumes and industrial production both expanded in May (latest month of data available as of July) and are at or near cycle highs, but overall performance remains modest relative to global real GDP growth. EM continued to drive much of the gains in global goods sectors. EM exports in May hit a new cycle high, with gains in China, Indonesia, and Mexico, while DM export volumes continued to move sideways, as they have for over a year. All in, the global manufacturing recovery continues to gradually gain steam, though tepid performance in DMs has limited the robustness and breadth of the recovery.

- The US economy continued to defy skeptics, growing by 2.8% QoQ annualized in Q2, with 1.6% of this coming from consumption. Likewise, US inflation continued to cool in June, with the three-month annualized rate fading to a six-month low of 2.3% (down from a 15-month high of 4.5% in March). The latest figures confirm the assertion that inflation is back on track towards the Fed's ~2% target, opening the door for potential rate cuts as early as September.

US ELECTIONS:

- At the start of July, Joe Biden stood on shaky ground following what he acknowledged to be a "bad night" at the first presidential debate of the current election cycle against former president Donald Trump. Nevertheless, Biden remained the Democratic party's nominee…until he wasn't.
- After weeks of pressure from top Democrats, donors, close allies, and friends alike, to withdraw from the race, Biden formally ended his re-election campaign, simultaneously endorsing his Vice President, Kamala Harris, to be his successor. Harris proceeded to rapidly consolidate support within her party well-beyond the delegate votes needed to win the Democratic nomination, while raising a record-breaking $200mn in her first week as merely the *likely* replacement to Biden, amassing more than $310mn in July alone.
- After surviving an assassination attempt, Donald Trump officially accepted the Republican nomination at the Republican National Convention in Milwaukee, where he named Ohio junior senator JD Vance as his running-mate and reaffirmed his tariff policies targeting China and the rest of the world.
- Trump took a commanding +3% lead over Biden in the polls following the debate and assassination attempt, but that was before Biden exited the race entirely, tapping Harris to take up the mantel in his stead. Since then, polls have been much tighter, with the latest favoring Harris by <1%.
- Global market volatility matched pace with US politics and preliminary polls in what promises to be an equally uncertain run-up to the presidential election in November.

IMPLICATIONS FOR EM:

- US macroeconomic and political cycles continue to send conflicting messages for EM equities.
- Positive optionality might build around EM equities as US macroeconomic conditions seem to be skewing towards US monetary easing, given slowing activity and cooling inflation, favorable EM-DM growth differential, low investor positioning, and valuation (with EM trading at a significantly wider discount than history to DM on forward P/E).
- The rising risk of a second Trump administration points to a bigger challenge for EM to navigate, most notably in the event of "America First" policy, which could asymmetrically support US equities. A Harris win would likely also favor trade policies that realign US relations away from rivals and prioritize advancing US leadership in high-tech industries (as seen under the current Biden administration, and to some degree the former Obama administration).
- However, there remain other headwinds to consider, including elevated geopolitical tensions, supply chains issues, US fiscal policy, NATO/Ukraine security issues, migration/drug trafficking in Mexico, and oil prices, to name a few.
- Contrary to the track record established during his first term in the white house, Trump-Vance, have signaled an interest in driving the US dollar (USD) lower, in an effort to increase the attractiveness of US exports, and bring manufacturing jobs back to the US. When coupled with lower taxes and higher government spending, such policy would drive US debt to GDP even higher. For context, the US debt-to-GDP ratio for Q1 2024 was 122%, and regardless of US election outcomes in November, any likelihood of this trend reversing is low.

IMPLICATIONS FOR CHINA:

- Irrespective of the election's outcome, most Americans view China as a threat, both economically and militarily, making "tough on China" policy one of few remaining bi-partisan agendas.
- <u>Tariffs</u>: If implemented, a full 60% tariff on China exports could lead to as much as a 250bp drag on GDP growth in China over the following 12 months. While the Chinese government could pass supportive policy measures to offset this negative effect, in reality there is little they could do to effectively neutralize such an offensive by the US.
    - As a reminder, China's share in the US market imports has fallen from 22% in 2017 to 14% in 2023. Mexico, Vietnam, Taiwan, Canada, and Korea were the top five export market share beneficiaries in the US. However, China's exports to these economies grew more than to the rest of the world, helping to keep its total share in global exports intact.
- <u>Supply Chain Reconfiguration</u>: Mexico and Vietnam's share gains in the US market are not just trade triangulation but rather supply chain shifts.
    - Global FDI into both Mexico and Vietnam has been substantial in recent years, but what is more interesting is the compounding nature of such investment when coupled up with messaging coming out of China (from CFOs, and other decision makers), revealing the vast majority of manufacturing exporters or suppliers have halved their production or capex spending overseas.

***MONTH/YTD THROUGH 7/31/24*: MSCI EM Index +0.3%+7.8%, MSCI EMSC Index -0.1%/+7.0%, and MSCI China Index -1.3%/+3.4%.**

REGION

Performances were more mixed by region in July, as the macro-outlook remains uncertain with a challenging combination of persistently high inflation and profit margin pressures. Emerging Europe, Middle East, and Africa (EEMEA) was the best performing region in the period, up 3.5%, led by Greece (+9.8%) and UAE (+6.8%). July was positive for MENA equities following three months of weakness. As 2Q results begin to trickle in, incoming results are indicating a less worrisome backdrop than initially feared. Rising tensions on the Israel-Lebanon border and the assassination of Hamas's lead negotiator, Ismail Haniyeh, nudged the region closer to a wider war, even if GCC and oil markets reacted little. Asia (-0.3%) was the worst performing region in the period, with Taiwan (-4.3%), China (-1.3%), and South Korea (-0.5%) weighing negatively given anxiety over US restrictions on chip sales to China. Concerns of heightened geopolitical tensions reverberated across Asian markets more broadly after the Biden administration floated tougher trade restrictions on China. Adding further to already negative sentiment following Donald Trump's comments on Taiwan taking away all of the chip business from the US.

SECTOR

Health Care (+8.4%) was the best performing sector, driven by broad-based market action in favor of more defensive assets as well as strong earnings results in several key markets, particularly South Korea. Information Technology (-3.0%) was the worst performing sector in the period, weighed down by broad-based profit-taking on valuation concerns and questions regarding the sustainability of the AI rally ahead of key corporate earnings, given the tech sector's big gains over the past year as investors position for the upcoming US election in November and potential Fed interest rate cuts, amid concerns over geopolitics and China's economy.

CURRENCIES/COMMODITIES

The US Dollar ended the month down 1.7%. The best performing EM currency versus the USD in July was the Peruvian Sol (PEN) up 3.1%. Conversely, the worst performer was the Argentine Peso (ARS) down 2.1%. Brent oil closed the month down 6.6%, with a falling geopolitical premium on the back of progress towards a ceasefire agreement between Israel and Hamas, though the outlook for that seems to have become murkier. This compounds with dwindling volume and volatility across the wider commodity space, partially impacted by the global tech outage, even as bullish signals remain.

STYLE

Small Caps ended the month mostly flat (-0.1%), marginally underperforming Large Caps, which ended +0.1%. Year-to-date, Small Caps have underperformed Large Caps by 186 basis points. Value rose 0.6% for the month, outperforming Growth, which ended flat (-0.0%). Year-to-date, Value has underperformed Growth by 131 basis points.

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WHY INVEST WITH SOPHUS CAPITAL?

Experienced team with long track record – the team, investment process, and philosophy date back to 2001, when Michael Reynal took over the EM strategy. Of the 10 members who currently make up the investment team, seven trace their origins back to the Victory Sophus Emerging Markets Fund's 2013 inception (with an average of 12 years on the team).

Invest across all market capitalizations – seek to exploit the inefficiencies in EM of bias, information, and access. Integrated approach allows us to capture growing companies down the cap spectrum, where inefficiencies are at their greatest, and alpha potential most significant.

Disciplined process – our process is bottom-up, with stock selection our biggest source of alpha, as the team believes that stock-picking is the most consistent alpha source in the emerging market space. Analysts combine quantitative signals with in-depth fundamental research to formulate high conviction alpha ideas. Portfolios are rigorously managed to emphasize stock selection as the key alpha driver, while controlling country, sector, factor, and other risks continuously.

Consistent results – our strategy was designed to provide a consistent return pattern over time. Our intention isn't to crush it in any one year, instead the discipline and consistency inherent to our process seeks to protect us from large swings in both directions.

Investment Performance (%)

Average Annual Returns as of July 31, 2024

Sophus Emerging Markets Strategy	QTD	YTD	1 - Year	3 - Year	5 - Year	10 - Year	Since Inception (3/31/13)
Gross of Fees	-2.07	8.76	7.37	-3.43	4.20	4.01	4.09
Net of Fees	-2.13	8.25	6.51	-4.20	3.37	3.16	3.23
MSCI Emerging Markets Index (Net)	0.30	7.81	6.27	-2.74	3.41	2.62	2.93
Differential (Gross of fees vs. Index) bps	-237	+95	+110	-69	+79	+139	+116
Sophus Emerging Markets Small Cap Strategy	**QTD**	**YTD**	**1 - Year**	**3 - Year**	**5 - Year**	**10 - Year**	**Since Inception (1/31/14)**
Gross of Fees	-1.65	6.46	14.50	3.02	10.05	7.11	7.78
Net of Fees	-1.73	5.84	13.37	1.99	8.95	5.96	6.61
MSCI Emerging Markets Small Cap Index (Net)	-0.05	6.99	12.63	2.97	10.30	5.07	6.03
Differential (Gross of fees vs. Index) bps	-160	-53	+187	+5	-25	+204	+175

Source: SEI
Past performance does not guarantee future results. Performance is preliminary and subject to change.
Returns greater than one year are annualized. Returns are expressed in U.S. Dollars. Returns reflect the reinvestment of dividends and other earnings.

Investment Performance (%)

Average Annual Returns as of June 30, 2024

Sophus Emerging Markets Strategy	1Q24	YTD	1 - Year	3 - Year	5 - Year	7 - Year	10 - Year	Since Inception (3/31/13)
Gross of Fees	5.81	11.06	15.60	-4.84	4.49	4.32	4.32	5.81
Net of Fees	5.67	10.69	14.75	-5.57	3.67	3.47	3.46	5.67
MSCI Emerging Markets Index (Net)	5.00	7.49	12.55	-5.06	3.09	2.79	2.93	5.00
Differential (Gross of fees vs. Index) bps	+81	+357	+305	+22	+140	+153	+139	+81
Sophus Emerging Markets Small Cap Strategy	**1Q24**	**YTD**	**1 - Year**	**3 - Year**	**5 - Year**	**7 - Year**	**10 - Year**	**Since Inception (1/31/14)**
Gross of Fees	7.42	8.24	22.40	3.04	10.35	7.25	8.02	7.42
Net of Fees	7.24	7.79	21.29	2.04	9.27	6.10	6.85	7.24
MSCI Emerging Markets Small Cap Index (Net)	5.93	7.04	20.04	2.54	9.98	5.15	6.09	5.93
Differential (Gross of fees vs. Index) bps	+149	+120	+236	+50	+37	+210	+193	+149

Source: SEI

Past performance does not guarantee future results. Performance is preliminary and subject to change.

Returns greater than one year are annualized. Returns are expressed in U.S. Dollars. Returns reflect the reinvestment of dividends and other earnings.

Past performance is no guarantee of future results. Composite and benchmark returns are net of transaction costs and gross of non-reclaimable withholding taxes.

Composite and benchmark returns are presented net of non-reclaimable withholding taxes. Gross-of-fees returns are presented before management and custodial fees but after all trading expenses. Net-of-fees returns are calculated by deducting 1/12 of the highest tier of the standard fee schedule in effect for the period noted (the model fee). Net returns prior to 1/1/2017 were calculated using actual fees. The composite model fee for each period is either the highest tier of the current fee schedule or a higher value, whichever is required to ensure the model composite net-of-fee return is lower than or equal to the composite net-of-fee return calculated using actual fees. Actual fees may vary depending on, among other things, the applicable fee schedule and portfolio size. The firm’s fees are available on request and may be found on Part 2A of its Form ADV.

Index returns are provided to represent the investment environment during the periods shown. Index performance does not reflect management fees, transaction costs or expenses that would be incurred with an investment. One cannot invest directly in an index.

All investments carry a certain degree of risk including the possible loss of principal, and an investment should be made with an understanding of the risks involved with owning a particular security or asset class.

The Sophus Emerging Markets representative account serves as the model against which each Sophus Emerging Markets strategy account is managed. The representative account is an actual portfolio and the information provided, including performance, will vary for other accounts. The representative account is being used solely as a tool to help demonstrate how performance can be attributed to the investment policies applied in the management of the Sophus Emerging Markets strategy.

The Sophus Emerging Markets Small Cap representative account serves as the model against which each Sophus Emerging Markets Small Cap strategy account is managed. The representative account is an actual portfolio and the information provided, including performance, will vary for other accounts. The representative account is being used solely as a tool to help demonstrate how performance can be attributed to the investment policies applied in the management of the Sophus Emerging Markets Small Cap strategy.

Chart of the month compiled utilizing Bloomberg.

This information is based on data obtained from recognized services and sources and is believed to be reliable. Any opinions, projections or recommendations in this report are subject to change without notice and are not intended as individual investment advice. The securities highlighted, if any, were not intended as individual investment advice. A complete list of all holdings for the previous 12 months, each holding's contribution to the strategy's performance, and the calculation methodology used to determine the holdings' contribution to performance is available on request. Victory Capital Management Inc., and its affiliates, as agents for their clients, and any of its officers or employees, may have a beneficial interest or position in any of the securities mentioned, which may be contrary to any opinion or projection expressed in this report.

The Sophus Emerging Markets Composite includes all discretionary accounts invested in the Emerging Markets Strategy. The Strategy employs an integrated investment approach whereby powerful proprietary quantitative screens are melded with deep fundamental analysis to capture the growth of emerging markets companies across the market-cap spectrum. The composite creation month is April 2013.

The Sophus Emerging Markets Small Cap Composite includes all discretionary accounts invested in the Emerging Markets Small Cap Strategy. The Strategy employs an integrated investment approach whereby powerful proprietary quantitative screens are melded with deep fundamental analysis to capture the growth of emerging markets companies across the market-cap spectrum. The composite creation month is February 2013.

The MSCI Emerging Markets Index is a free-float-adjusted, market-capitalization-weighted index designed to measure equity market performance in the global emerging markets.

The MSCI Emerging Markets Small Cap Index is a free-float-adjusted, market-capitalization-weighted index designed to measure the performance of small-cap stocks in the emerging markets.

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7/31/2024		6/30/2024	12/29/2023
		7/31/2024	7/31/2024
CRNCY		CUST_TRR	CUST_TRR
	Country	**Performance (USD)**	
		MTD	**YTD**
USD	**DM**	**1.61%**	**13.10%**
USD	**US**	**1.22%**	**16.69%**
EUR	**EUROPE**	**2.15%**	**8.08%**
JPY	**JAPAN**	**5.80%**	**12.43%**
USD	**EMLC**	**0.08%**	**8.85%**
USD	**EMSC**	**-0.05%**	**6.99%**
USD	**EM Growth**	**-0.01%**	**8.44%**
USD	**EM Value**	**0.63%**	**7.13%**
USD	**EM**	**0.30%**	**7.81%**
HKD	CHINA	-1.33%	3.35%
HKD	HONG KONG	0.42%	-10.45%
INR	INDIA	3.97%	21.54%
IDR	INDONESIA	3.82%	-7.11%
MYR	MALAYSIA	5.22%	13.16%
PKR	PAKISTAN	-0.54%	28.74%
PHP	PHILIPPINES	4.35%	-1.13%
SGD	SINGAPORE	2.98%	12.27%
KRW	SOUTH KOREA	-0.49%	-0.05%
TWD	TAIWAN	-4.28%	23.86%
THB	THAILAND	5.82%	-7.53%
CZK	CZECH REPUBLIC	2.61%	0.60%
EGP	EGYPT	6.06%	-28.56%
EUR	GREECE	9.80%	15.42%
HUF	HUNGARY	3.67%	13.72%
KWD	KUWAIT	4.72%	10.31%
PLN	POLAND	-4.33%	5.03%
USD	QATAR	3.51%	-0.53%
USD	RUSSIA	#N/A	#N/A
SAR	SAUDI ARABIA	3.65%	0.55%
ZAR	SOUTH AFRICA	5.18%	10.00%
TRY	TURKEY	-1.46%	37.04%
AED	UAE	6.79%	4.66%
USD	ARGENTINA	-2.53%	18.30%
USD	BRAZIL	1.28%	-17.67%
USD	CHILE	-0.47%	-6.18%
USD	COLOMBIA	2.26%	11.42%
USD	MEXICO	0.75%	-15.02%
USD	PERU	1.28%	19.63%
USD	**ASIA**	**-0.28%**	**10.73%**
USD	**EMEA**	**3.65%**	**6.41%**
USD	**LATAM**	**1.03%**	**-14.81%**
	SECTORS		
USD	COMM SERVICES	-0.79%	8.20%
USD	DISCRETIONARY	0.31%	4.94%
USD	STAPLES	2.56%	-4.73%
USD	ENERGY	-1.49%	8.76%
USD	FINANCIALS	2.77%	8.77%
USD	HEALTH CARE	8.44%	-0.95%
USD	INDUSTRIALS	0.75%	6.24%
USD	INFO TECH	-2.91%	18.67%
USD	MATERIALS	-0.28%	-6.61%
USD	REAL ESTATE	0.70%	-2.65%
USD	UTILITIES	3.07%	13.36%

Source: Sophus Capital, Bloomberg, Factset

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