A blueprint for success

AWEM can look to India for inspiration...

Update
21 November 2024

It's not often that when a new investment trust is launched there's already a blueprint for success, but one could argue that is the case for **Ashoka WhiteOak Emerging Markets (AWEM)**.

Manager Prashant Khemka has demonstrated that his approach to investing can yield spectacular results via **Ashoka India Equity (AIE)**, the top-performing India trust it launched in 2018. Recognising the broader opportunity set in emerging markets and subsequent growth potential, Prashant and his team launched AWEM in May 2023.

AWEM provides access to a multi-cap portfolio of emerging market equities and has many attributes in common with its more established stablemate, including focusing on small- and mid-cap (SMID) opportunities – a segment of the market that remains largely under-researched. It also employs the same performance-first culture, designed to maximise alpha through stock selection, while minimising volatility.

Prashant brings a wealth of experience from his 17-year tenure at Goldman Sachs Asset Management and founded WhiteOak Capital Partners, the advisor to AWEM, in 2017. He is supported by two investment directors, Fadrique Balmaseda and Lim Wen Loong, alongside one of the largest and best-resourced investment teams in the emerging markets sector.

The team's on-the-ground presence enables regular access to company management, a close connection with domestic markets and a greater understanding of the companies within their investment universe.

The WhiteOak team aims to strip out businesses with poor governance, high debt levels and those lacking a sustainable competitive advantage. This distils a universe of c. 2,800 companies down to c. 750.

The high-quality companies eligible for inclusion in the portfolio must be able to deliver superior returns, have scalable business models, possess a sustainable competitive advantage that others in the industry struggle to replicate and be well-managed both operationally and in terms of governance.

Analysts:
David Brenchley
david.b@keplerpartners.com

Unique frameworks

The team then assesses the businesses' fundamentals and valuations using a unique analytical framework called OpcoFinco, developed by Prashant during his tenure at Goldman Sachs.

OpcoFinco nets off the cost of capital of a business in order to identify the self-sustaining, recurring cash-revenue growth of a company. Essentially, it's a more sophisticated cash-flow valuation model designed to help differentiate quality businesses from those whose current high returns may not be sustainable without substantial future capital injections.

The team uses another internally developed framework called ABLEx, which is designed to help avoid companies with inherently poor governance, and to strengthen their ESG risk assessments. The framework includes a sector-specific list of ESG risks and opportunities, against which companies' practices, policies, and disclosures are assessed and rated. The results of this analysis are then integrated into the overall valuation of each business.

There's a reasonably high degree of turnover in the portfolio (approximately 30% per year) because the team rigorously assess their holdings' valuations, selling when it aligns with the team's assessment of fair value. This allows them to reallocate to other high-conviction opportunities with greater upside potential.

At the moment, the team believes that large-cap valuations tend to be more closely clustered around fair value. They find more inefficiencies in SMID segments. AWEM currently has 35% invested in SMIDs, versus 16% for the benchmark. Over time, Prashant expects the split between large and SMID stocks to be around 50/50.

The case for emerging markets

On an absolute basis, compared to their average valuations, one could argue that emerging markets are neither cheap nor expensive. Indeed, the 12-month forward price-to-earnings (PE) ratio of the MSCI EM Index is c. 12.1x, narrowly higher than the index's 30-year mean average of 12x. The 12-month forward price-to-book (PB) of the index is 1.6x, bang on the 20-year average.

Yet, on a relative basis, the case for investing in emerging markets becomes much more compelling. The MSCI EM Index is trading on a c. 36% discount to the MSCI World Index on the forward PE metric, the biggest discount seen in about 20 years. On a forward PB basis, the discount is 47%, again a level not seen for more than 20 years.

This looks attractive when you consider that emerging markets were valued at a double-digit premium on the forward PB measure as recently as 2011.

Then, there's the fundamental investment case, which is centred on the fact that emerging markets house some of the fastest growing economies in the world. Emerging market economies generate 65% of global growth.

GDP growth in emerging market and developing economies is expected to be 4.2% in both 2024 and 2025, according to the International Monetary Fund (IMF), ahead of global GDP growth of 3.2% and almost two and a half times faster than advanced economies, which are predicted to grow by 1.7% in 2024 and 1.8% in 2025.

There's plenty of scope for growth, too. As an example, India has 800 million people aged under 35; by contrast, 2024 is expected to be the first year there are more people over the age of 65 than under the age of 15 in the US. Even in Mexico, 64% of the population is aged under 39, versus 51% in the US (in India, it's 66%).

The emerging market complex is one of the few areas where finding a good-quality active manager can pay clear dividends. This is particularly true in the SMID-cap segments, which often harbour strong, alpha-rich companies that have not yet been fully recognised by investors.

An active manager can make a number of calls that gives them an edge over a passive emerging market strategy. In particular, it can decide to shy away from the less democratic and over-regulated countries, investing only where the opportunity to make money is the most attractive.

Indeed, the average net democracy score of the MSCI EM Index is 3.6, with its large weighting to China a big drag, as well as modest positions in Saudi Arabia, UAE and Thailand. AWEM, by contrast, has a net democracy score of 6.2 due in part to its underweight call on China (on a direct exposure basis). AWEM is 13.6% underweight the least democratic emerging market nations and 12.7% overweight the most democratic countries.

Similar is true when it comes to state-owned enterprises (SOEs), which are common within emerging nations' stock markets but are often run for the good of the government that part-owns them, rather than outside shareholders. The MSCI EM Index has 19% invested in SOEs, versus just 3% for AWEM, a 16% underweight.

The blueprint

For many, putting their trust in a new strategy is a risk, but Prashant and the WhiteOak team's success with AIE gives confidence that AWEM can thrive.

AIE's net asset value (NAV) and share price total returns since IPO have been 194.5% and 173.4% respectively, to 09/10/2024. The share price total return for the Morningstar India Index in that time is 131.6%.

It's clearly early days for AWEM, but the early signs are encouraging. Although only a relatively short period, it's encouraging that since inception in May 2023, AWEM has outperformed its benchmark, and has done so in rising and falling markets in all but two quarters, and both of those involved only modest underperformance, as the table below shows. The outperformance during declining markets is particularly striking.

Quarterly Performance Since Launch

PERIOD	NAV (%)	MSCI EM (%)	EXCESS RETURN (BPS)	MSCI EM ETF (%)	EXCESS RETURNS (BPS)
Q4 2024 to-date	0.3	-2.3	257	-1.2	149
Q3 2024	1.8	2.5	-71	1.6	18
Q2 2024	5.6	5.2	35	4.3	131
Q1 2024	3.9	3	85	3.3	60
YTD 2024	11.9	8.5	101	8.1	385
Part 2023*	7.4	4.8	260	4.6	279
Q4 2023	4.7	3.3	138	3.3	137
Q3 2023	0.7	1.1	-38	-0.1	80
Part Q2 2023	1.8	0.3	151	1.3	53
Since inception	20.2	13.7	645	13	715

Source: WhiteOak, as of 14/11/2024 (*Inception Date: 03/05/2023)

As with AIE, AWEM charges no management fee, instead levying a performance fee earned only if the portfolio demonstrates relative outperformance of its benchmark over discrete three-year periods and is capped at 12% of the time-weighted assets over the three-year period. Any performance fee due is paid entirely in shares, 50% of which are subject to a further three-year lock-up period.

This incentivises the team to remain focused on delivering alpha through stock selection, which one can certainly see has worked with AIE. The managers have achieved a 'hit rate' of c. 65%, well above the c. 55% that is considered a high standard in the industry.

If that can be translated to AWEM, the future looks positive. For now, AWEM's differentiated process, unique charging structure, large research team and strong recent performance positions it as a standout option for capitalising on opportunities in many of the under-researched emerging markets.

Trusts in focus: Ashoka WhiteOak Emerging Market **Watch on youtube**

View the latest research note here

Click here to add AWEM to your watchlist

Click here to read related research

Disclaimer

This report has been issued by Kepler Partners LLP. **The analyst who has prepared this report is aware that Kepler Partners LLP has a relationship with the company covered in this report and/or a conflict of interest which may impair the objectivity of the research.**

Past performance is not a reliable indicator of future results. The value of investments can fall as well as rise and you may get back less than you invested when you decide to sell your investments. It is strongly recommended that if you are a private investor independent financial advice should be taken before making any investment or financial decision.

Kepler Partners is not authorised to make recommendations to retail clients. This report has been issued by Kepler Partners LLP, is based on factual information only, is solely for information purposes only and any views contained in it must not be construed as investment or tax advice or a recommendation to buy, sell or take any action in relation to any investment.

The information provided on this website is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject Kepler Partners LLP to any registration requirement within such jurisdiction or country. In particular, this website is exclusively for non-US Persons. Persons who access this information are required to inform themselves and to comply with any such restrictions.

The information contained in this website is not intended to constitute, and should not be construed as, investment advice. No representation or warranty, express or implied, is given by any person as to the accuracy or completeness of the information and no responsibility or liability is accepted for the accuracy or sufficiency of any of the information, for any errors, omissions or misstatements, negligent or otherwise. Any views and opinions, whilst given in good faith, are subject to change without notice.

This is not an official confirmation of terms and is not a recommendation, offer or solicitation to buy or sell or take any action in relation to any investment mentioned herein. Any prices or quotations contained herein are indicative only.

Kepler Partners LLP (including its partners, employees and representatives) or a connected person may have positions in or options on the securities detailed in this report, and may buy, sell or offer to purchase or sell such securities from time to time, but will at all times be subject to restrictions imposed by the firm's internal rules. A copy of the firm's Conflict of Interest policy is available on request.

PLEASE SEE ALSO OUR TERMS AND CONDITIONS

Kepler Partners LLP is authorised and regulated by the Financial Conduct Authority (FRN 480590), registered in England and Wales at 70 Conduit Street , London W1S 2GF with registered number OC334771.