EMERGING MARKETS

BRAZIL – 3.0 STARS (ATTRACTIVE)

- GDP declined -3.8% y-o-y in 2Q 16, after a -5.4% y-o-y contraction in 1Q 16
- Manufacturing PMI stood at 46.0 in Jul 16, up from 43.2 in Jun 16
- Services PMI came in at 45.6 in Jul 16, up from 41.4 in Jun 16
- Composite PMI at 46.4 in Jul 16, up from 42.3 in Jun 16
- Retail sales declined -5.3% y-o-y in Jun 16, after a -9.0% plunge in May 16
- Industrial production fell -6.0% y-o-y in Jun 16, after an upward-revised -7.5% slump in May 16
- IPCA inflation came in at 8.74% y-o-y in Jul 16, slowing from a 8.84% y-o-y increase in Jun 16
- Selic rate remained unchanged at 14.25% in Aug 16

RUSSIA – 4.0 STARS (VERY ATTRACTIVE)

- Industrial production fell -0.3% y-o-y in Jul 16, down from a 1.7% increase in Jun 16
- CPI rose by 7.2% y-o-y in Jul 16, down from a 7.5% increase in Jun 16
- PPI increased by 4.5% y-o-y in Jul 16, down from a 5.1% increase in Jun 16
- Retail sales fell -5.0% y-o-y in Jul 16, up from a -5.9% decline in Jun 16

MARKET OUTLOOK

In South America, the earnings outlook of the Bovespa Index was downgraded over the month of August, with estimated earnings for 2016 and 2017 revised downward by -1.8% and -0.7% respectively. Meanwhile, earnings for 2018 was uplifted by 1.5% (as of 29 August 2016). There were notable downgrades in the consumer staples and energy sectors, while the materials sector saw improvements in its earnings outlook. A surge in feed costs and the BRL, both of which have slashed profit margins of Brazilian meat producers, have led analysts to revise the estimated earnings of JBS SA and BRF SA downward over the month. The estimated earnings of troubled oil giant Petrobras was also revised downward in August as the company's 2Q 16 earnings missed analyst expectations by a huge margin. Meanwhile, mining giant Vale SA saw its estimated earnings revised upward by 11.7%, with the firm's profit prospects bolstered by improved business fundamentals arising from its cost cuttings and margin enhancement strategies. Across the Atlantic in Russia, estimated earnings of Russian companies (as represented by the RTSI$ Index) on aggregate saw slight upward revisions over the month of August, with 2016's estimated earnings revised 0.4% higher month-to-date, while 2017's estimated earnings were revised 0.04% higher (as of 29 August 2016). With the recent revisions, Russian companies are expected to see their earnings grow by 8.6% this year, before growing by 16.3% in 2017. Some of Russia's energy titans like Novatek and Lukoil saw minor upgrades to their estimated EPS month-to-date, while banking giant Sberbank continued to see earnings upgrades once more, as the consensus has started to price in a recovery in economic conditions, amelioration of asset quality as well as prospects for further interest rate cuts.

Following a -5.4% decline in 1Q 2016, Brazil's Gross Domestic Product (GDP) fell for the ninth consecutive quarter by -3.6% year-on-year in 2Q 2016, slightly below market expectations for a -3.7% year-on-year contraction. Brazil's consumer price inflation came in at 0.52% month-on-month in July, accelerating from the 0.35% inflation in June and was above market expectations for a 0.45% increase in consumer prices. On a year-on-year basis, inflation in July was at 8.74%, a slowdown from the 8.84% seen in June. As Brazil's inflation remains stubbornly high above the government's 6.5% inflation ceiling, the central bank has held the country's benchmark Selic rate unchanged at 14.25% for the thirteenth consecutive month in August, a decision that was widely anticipated. Meanwhile, retail sales in Brazil declined for the fifteenth consecutive month by -5.3% year-on-year, while industrial production also extended its slump by -6.0% year-on-year in May. On a brighter note, consumer confidence in Brazil has also shown a marked improvement in recent months, with the FGV Consumer Confidence Index coming in at a 79.3 reading in August, up from a previous 76.7 reading and is the highest since January 2015. Over the month in the political space, a line was finally drawn under the impeachment saga in Brazil as Dilma Rousseff was officially removed from office. With increasing optimism in the ability of the interim government to steer the economy out of recession, economists have made upward adjustments to their forecasts for Brazil's economic performance this year over the course of August, with GDP growth for 2016 expected to come in at -3.16%, as compared to a -3.24% contraction forecasted in end July.

Over in Russia, PMI readings continue to suggest a gradual improvement of economic conditions in the country. Although the manufacturing PMI came in below consensus expectations (49.5 reading, down from a prior 51.5 reading), services beat expectations in July, clocking a 55 reading that is higher than June's 53.8, and is the highest reading in three years. Additionally, various consumer sentiment readings also suggest that consumer confidence has been picking up in recent months, and should this trend continue, a gradual improvement in domestic consumption could be seen in the near-future. In July, industrial production fell slightly but has been gradually picking up year-to-date, and retail sales data showed signs of improvement, declining -5.0% year-on-year as compared to a prior -5.9% year-on-year decline (retail sales rose 4.2% month-on-month). CPI data also continued to display disinflationary trends, and should it continue, policy-makers are expected to continue easing monetary policy (via interest rate cuts) in order to stimulate economic conditions.

On current forecasts, the Bovespa Index trades at estimated PE ratios of 15.1X and 12.3X for 2016 and 2017 respectively (as of 29 August 2016), as compared to its fair PE ratio of 11.5X. With markets having priced in a change of government and looking beyond the political turmoil, the investment case for Brazil now hinges upon its economy. While there are tentative signs of a recovery, it may be premature at this juncture to call a bottom to Brazil's economic troubles. We **maintain a 3.0 Stars "Attractive" rating for the Brazilian market**. The Russian equity market, like its Brazilian counterpart, has also rebounded strongly from its January-lows, posting a year-to-date return of 22.2% (in SGD terms) as of 29 August 2016. The Russian RTSI$ Index currently trades at estimated PE ratios of 7.3X and 6.3X for 2016 and 2017 respectively as compared to its fair PE ratio of 7.0X. Valuations have risen over the past few months, and the market's expected total returns are now lower than before, hence **we lowered Russia's star ratings from a prior 4.5 Stars "Very Attractive" to 4.0 Stars "Very Attractive"** in mid-July, while we expect a gradual improvement in fundamentals as policy-makers continue to ease monetary policy and as business and consumer sentiment returns.

RECOMMENDED FUND:
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