

Quick Take: EM Low Vol Equity as Risk Aversion Returns

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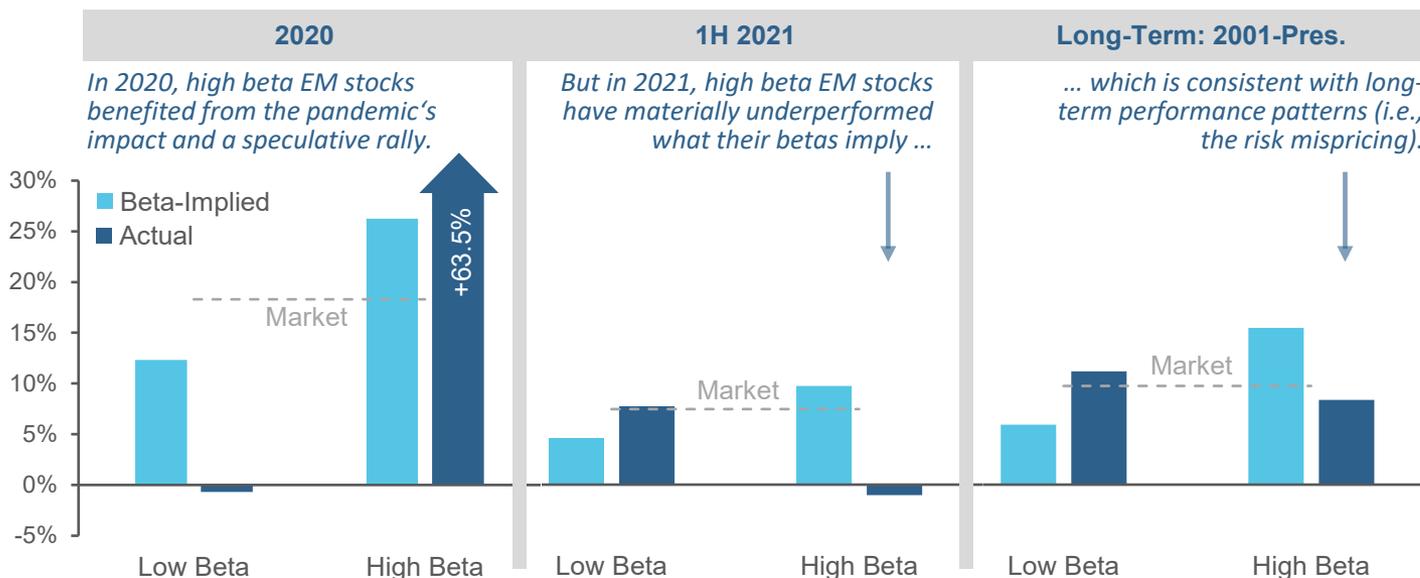
Emerging Markets low risk investing in 2021: Return to the norm

- In 2020 technology-driven mega-cap EM stocks enjoyed strong returns (left chart), dominating index performance and leading to a substantial increase in index concentration. Defensive EM strategies underperformed, particularly portfolios that underweighted the largest discretionary and media names.
- As we've commented elsewhere, low volatility performance in 2020 was peculiar, driven by the pandemic's specific economic consequences and a speculative global rally that resembled the TMT era.
- 2021 to date is a different story, and low-versus-high beta returns have more closely resembled our long-term expectation (right chart). Although MSCI EM rose another 7.4% in the first half of the year, high-beta stocks generated negative absolute returns. Low-risk stocks not only outperformed what their betas would imply, but the market as well (middle chart).

Looking forward: Own insurance if EM volatility persists?

- Broad geopolitical risks currently connected to China have dampened EM high-beta performance and present ongoing risk to EM large-cap investments. In late 2020 the U.S. imposed sanctions against a list of companies tied to the Chinese military, and in February China enacted antitrust rules targeting domestic tech giants.
- This cloudy geopolitical outlook reinforces the appeal of low-risk EM investments as a complement to benchmark-relative strategies. Historically, low-risk equity strategies diversify other portfolio tilts and have paid off when market multiples contract. In 2021, we've already seen such benefits, as sentiment has deteriorated, and overvalued, high-beta stocks have sold off.

EM Low and High Beta Stocks: Actual Returns versus Beta-Implied



Charts shows returns of high and low-beta quintile cap-weighted portfolios and the MSCI EM Index. Sources: Acadian based on data from MSCI. MSCI data: Copyright MSCI 2021. All Rights Reserved. Unpublished. PROPRIETARY TO MSCI. For illustrative purposes only. Results do not reflect transaction costs or other implementation frictions. It is not possible to invest directly in any index. Every investment program has the opportunity for losses as well as profits. Past results are not indicative of future results.



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