RBC Vision Fossil Fuel Free Emerging Markets Equity Fund

Commentary as at December 31, 2023

Emerging-market equities rose in 2023 to halt two years of declines, after subsiding inflation triggered interest-rate cuts and their promise of faster economic growth. The Information Technology sector drove emerging and developed markets, following the U.S., on expectations that advances in artificial intelligence (“AI”) would spur demand for computer chips and other technology needed to fuel AI.

China, the largest constituent of the emerging-market benchmark, was a significant exception to the upbeat story for emerging markets. The removal of the country’s remaining pandemic restrictions was taken by investors as a positive in early 2023, but consumers and businesses did not spend and invest as had been expected, holding back Chinese equity markets. Overall, emerging markets underperformed developed markets.

Stock and sector selection aided the Fund’s relative returns during the period. Stock selection in the Consumer Staples and Real Estate sectors had a positive impact, as did underweight exposure to Consumer Discretionary and Communication Services. At the country level, stock selection in South Korea, Mexico and Chile bolstered relative returns, but was negative for China’s market. Below-benchmark exposure to China and Thailand benefited returns.

The top contributors to the Fund’s relative performance during the period were SK Hynix, Fomento Economico Mexicano, Phoenix Mills and Dr. Reddy’s Laboratories. The Fund also benefited from the absence of Meituan in the portfolio. Portfolio stocks that limited relative returns the most were Samsung Electronics, AIA Group, Yum China, Ping An Insurance and Hong Kong Exchanges.

Emerging-market returns are based largely on movements in the U.S. dollar, and the U.S. dollar’s strength over the past decade has limited the performance of emerging-market equities. There are, however, reasons to believe that this trend may reverse. The first is that U.S. Federal Reserve (the “Fed”) may be embarking on interest-rate cuts in 2024, which tend to coincide with a weakening U.S. dollar. Moreover, further declines in emerging-market currencies should be limited by their attractive valuations, relatively high inflation-adjusted interest rates and strong current accounts.

Aside from currency considerations are two factors that should support emerging-market performance over the medium term. First, emerging-market corporate earnings and economic growth look set to improve from cyclically low levels, driven by improved productivity, structural reforms and growth-friendly fiscal policies. Second, emerging-market stocks are attractively valued, particularly relative to developed markets, following the significant underperformance of recent years.

Sustainalytics conducted a review covering the Fund’s holdings during 2023. In the opinion of Sustainalytics and RBC GAM, all holdings in the Fund were eligible in the latest review based on the Fund’s ESG exclusion criteria. During 2023, no companies were removed from the Fund for failing to meet the ESG criteria.

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