Emerging Markets Equity Newsletter

Executive summary

The portfolio outperformed its benchmark by 890 basis points, net of fees, in Q2 2026. Our overweight exposure to Korea was the principal driver, led by SK Hynix and Samsung Electronics, while MediaTek, Chroma and several less conventional holdings broadened the contribution. The quarter reinforced our focus on high-return businesses whose earnings expectations are still rising despite strong share-price performance.

QUARTER IN REVIEW: KOREA LEADS, STOCK SELECTION BROADENS

SK Hynix (000660 KS) was the portfolio's largest contributor. We first added the company to institutional portfolios more than three years ago, attracted by its technology leadership, balance-sheet strength and ability to generate high returns on capital. Those qualities are increasingly evident: the company continues to produce substantial free cash flow and, on our estimates, trades at only 2.8 times next year's expected EV/EBITDA.

Following their first-quarter results, SK Hynix and Samsung Electronics (005930 KS) indicated that memory supply remains insufficient to meet rapidly growing demand for advanced products. The imbalance is most visible in high-bandwidth memory, where SK Hynix remains the industry leader. Together, the two Korean producers account for approximately 80% of the global DRAM market.

Recent management commentary has extended the industry's earnings visibility. SK Hynix's chief executive officer suggested that shortages could intensify beginning in 2027 and that the supply-demand imbalance may persist well beyond 2030. While long-range forecasts require caution, current customer commitments support our view that consensus earnings estimates for 2027 and 2028 are likely to continue rising.

The companies' substantial capital-expenditure plans nevertheless require close monitoring. They could affect free cash flow and returns on invested capital in the short and medium term. For now, stronger pricing power, greater product complexity and disciplined capacity expansion distinguish this environment from a conventional memory recovery. At roughly four times current EV/EBITDA and five times forward earnings, valuations appear to discount a much shorter cycle than current fundamentals imply.

MEDIATEK: CUSTOM COMPUTING EXPANDS THE OPPORTUNITY

MediaTek (2454 TT) was another important contributor. The Taiwanese semiconductor designer is becoming less dependent on smartphones as it expands into custom computing, enterprise networking, edge platforms and automotive semiconductors.

Our industry research indicates that MediaTek's TPU v8 platform is ramping faster than previously expected, with Google expected to deploy it for AI training workloads during the second half of 2026. MediaTek is also pursuing additional cloud ASIC programs that could materially broaden its addressable market.

Macquarie now estimates that the custom ASIC market could reach approximately US$40 billion in annual revenue by 2028, versus its earlier US$18 billion estimate. Future TPU generations should migrate to more advanced manufacturing processes, potentially more than doubling MediaTek's average selling prices. Although new programs may initially pressure gross margins, we expect scale and operating leverage to support a meaningful increase in operating profit.

CHROMA: TESTING COMPLEXITY SUPPORTS GROWTH

Chroma (2360 TT), a leading supplier of semiconductor testing equipment, also contributed positively. The company continues to report gross margins above 60% and a return on equity exceeding 30%, while earnings per share are expected to grow by more than 30% annually for at least the next three years.

Since we initiated the position in late 2024, management has consistently exceeded our expectations and consensus forecasts have continued to move higher. Chroma combines disciplined execution, high returns on invested capital and exposure to increasing semiconductor testing intensity - precisely the combination we seek for client portfolios.

PORTFOLIO IMPLICATIONS

Q2 performance demonstrates the value of combining structural themes with company-specific research. Leadership from SK Hynix and Samsung was complemented by MediaTek, Chroma and other specialized holdings. We remain constructive on advanced memory, custom computing and semiconductor testing while monitoring capital expenditure, capacity and valuation risk.

We are also identifying opportunities among equipment manufacturers and specialty chemical suppliers serving the semiconductor and memory industries. These companies should benefit as the investment programs announced by Samsung Electronics and SK Hynix move through the supply chain.

890 bps

Q2 portfolio outperformance, net of fees

2.8x

SK Hynix estimated next-year EV/EBITDA

~80%

Combined SK Hynix and Samsung share of global DRAM

MMI perspective

The quarter's performance was led by Korea, but contributions broadened across specialized semiconductor holdings. Rising earnings estimates - rather than multiple expansion alone - remain central to our conviction.

China: Q2 slowdown sharpens the divide

LATEST DATA: GROWTH MODERATES AFTER A STRONG FIRST QUARTER

China's economy grew by 4.3% year over year in Q2 2026, slowing from 5.0% in Q1 and bringing first-half growth to 4.7%. The moderation reinforces the imbalance between resilient production and weak domestic demand. Manufacturing expanded by 4.8% in Q2 and services by 5.1%, while real-estate activity remained slightly negative. Official data also show that information technology services grew by 10.8%, highlighting the strength of newer growth drivers even as the broader economy decelerated.

The latest figures refine, rather than reverse, our China thesis. Export-oriented manufacturing remains competitive, but household demand and property continue to limit the recovery. April's 14% year-over-year export increase and 44% rise in automobile exports demonstrated the strength of external demand. Domestic automobile sales, by contrast, declined 15%, while retail sales excluding autos rose only 1.8%.

With Q2 growth falling below the first-quarter pace, incremental policy support has become more likely. We still do not expect a broad consumption stimulus while exports and industrial production keep full-year growth within an acceptable range. A durable consumer rerating will require clearer evidence of stronger household demand and greater support for private enterprise.

CHIP IPO SIGNALS CAPITAL-MARKET DEPTH

Since quarter-end, Chinese DRAM producer CXMT completed the largest mainland semiconductor IPO on record, raising approximately RMB57.9 billion (US$8.6 billion). The transaction provides China with capital to narrow the gap with the Korean and Taiwanese chip leaders, but its relevance extends beyond domestic self-sufficiency. It demonstrates that emerging-market capital markets can finance semiconductor infrastructure at global scale and that the region's technology ecosystem remains active, strategically important and relevant to investors. The strong debut also warrants valuation discipline, given the limited initial free float and the industry's cyclicality.

MANUFACTURING ADVANTAGE: SCALE, ENGINEERING AND AUTOMATION

China's manufacturing leadership increasingly rests on economies of scale, sophisticated human and physical capital, and local-government support rather than low labour costs alone. Engineering expertise, robotics and capital intensity are allowing companies to raise productivity and compete globally.

Shuanghuan Driveline (002472 CH), one of our holdings, illustrates the shift. The company can produce approximately one million gear sets annually across three production shifts with a team of only about 70 operators. This level of automation demonstrates how technology and capital investment are replacing labour-intensive production as sources of competitive advantage.

LATIN AMERICA AND CHILE

Latin American equities continued to perform well during the quarter. Strong commodity prices and generally more market-friendly political developments remain supportive, although slower progress on inflation has reduced expectations for additional rate cuts, particularly in Brazil.

In Chile, anticipated pro-investment reforms could strengthen business confidence. Combined with copper prices that we expect to remain supportive, these measures may provide an additional tailwind for Chilean equities. We maintain an overweight position through a concentrated group of companies generating substantial free cash flow, high and improving returns on equity, and above-industry growth.

INDIA: PREPARING TO INCREASE SELECTIVELY

Our three- to five-year thesis for India remains intact. The country may be the only major economy capable of sustaining real GDP growth of approximately 6%-7% for several years without excessive leverage. Near-term earnings revisions and a valuation of roughly 20 times forward earnings nevertheless justify continued discipline.

Following substantial gains in Taiwan and Korea, we are evaluating opportunities to reallocate a portion of those gains and selectively reduce our India underweight. Any increase will focus on companies whose earnings outlook and valuation provide an appropriate margin of safety.

OUTLOOK

China's manufacturing strength, Chile's improving investment environment and India's long-term growth potential require distinct portfolio approaches. Our emphasis remains unchanged: durable competitive advantages, high returns on capital, strong balance sheets and the ability to convert structural growth into sustainable free cash flow.

4.3%

China Q2 2026 real GDP growth, year over year

US$8.6B

CXMT's record mainland semiconductor IPO

China lens

Q2 growth slowed, but the composition remains uneven: manufacturing, technology services and exports are resilient, while household demand and property remain weak.

Source: National Bureau of Statistics of China, July 2026.

Positioning snapshot

Positive: Korea memory and semiconductor suppliers.

Overweight: Latin America.

Selective: China manufacturing and consumer leaders.

Underweight: India; assessing additions.

Disclaimer

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