ACADIAN

Acadian Asset Management LLC
Emerging Markets Portfolio
Third Quarter 2024

Performance

The Acadian Emerging Markets Portfolio returned 6.30% (net of fees) for the quarter, relative to a return of 8.88% for the MSCI Emerging Markets Equity Index. †

Commentary

Global equities climbed 4.7%, ending the third quarter on a high after building on momentum from the second quarter. After a mid-quarter slump, equity markets recovered when the U.S. Federal Reserve (Fed) slashed rates for the first time in four years and, later in the quarter, when the Chinese government announced a slew of stimulus measures to boost its economy and prop up the real estate sector. Chinese stocks surged after the announcement, outperforming all the major markets by the end of Q3. This late surge contributed to emerging markets outperforming their developed counterparts. In September, the European Central Bank (ECB) cut interest rates for a second time this year as inflation eased toward its target. The combination of cooling inflation and accommodative monetary policies renewed hopes of a potential soft landing in developed economies. In Asia, however, the Bank of Japan's (BoJ's) hawkish stance along with the unwinding of the yen carry trade, placed downward pressure on Japanese equities, leading to underperformance.

Against this backdrop, the Acadian Emerging Markets Portfolio underperformed its benchmark† by 258 basis points for the quarter ending September 30, 2024.

At the country level, stock selection detracted from return, while country allocations were also marginally negative. Key sources of negative active return included stock selection in China, a combination of stock selection and an overweight position in Taiwan, and a combination of stock selection and an underweight position in South Africa. The Fund experienced positive contributions from stock selection and an underweight position in South Korea, as well as stock selection in India.

From a sector perspective, key sources of negative active return included a combination of stock selection and underweight positions in consumer discretionary and health care, as well as stock selection in industrials. The Fund experienced positive contributions from stock selection and an overweight position in communication services, as well as stock selection in Energy and Financials.

Outlook

The global economy ended the second quarter of 2024 on a strong note as concerns over inflation and interest rates abated and hopes of a soft landing were revived. The momentum continued into the third quarter, buoyed by steadily slowing inflation and the beginning of the rate cut cycle by major central banks. The U.S. Federal Reserve (Fed) finally slashed rates by 50bps after holding steady for 13 months. Marking the first cut since March 2020, the decision lowered the federal funds rate to 4.75-5.0%. In China, the government announced the biggest stimulus package in years to shore up the country's ailing economy. The People's Bank of China slashed interest rates by 20bps and its reserve requirement ratio by 50bps to boost loan demand.

The Organization for Economic Cooperation and Development (OECD) believes that the global economic growth is in the process of stabilizing as concerns over interest rates ease with central banks' reducing rates and falling inflation, boosting household incomes. The OECD raised its growth outlook for the global economy recently, expecting it to grow 3.2% year-over-year both this and next year. The Paris-based organization had earlier projected the global economy to grow 3.1% in 2024. As central banks continue to lower rates, the lagged impact of monetary tightening will likely gradually fade. Additionally, falling inflation will likely boost consumer spending going forward. The OECD believes that if oil prices continue to fall, global headline inflation could drop 50bps more than it anticipated earlier.

Experts believe that a soft landing is in sight for the West. With fears of a new surge in inflation receding, central banks may cut rates more aggressively than previously thought. Consequently, looser monetary policies and a rally in real income growth are expected to remain the key growth drivers in advanced economies. However, emerging markets may suffer from a structural slowdown in China.

The U.S. Energy Information Agency expects oil inventories to fall in the fourth quarter of 2024 because of the recent announcement by OPEC+ to delay production increase until December. It expects Brent crude oil spot price to average $82/b in the fourth quarter and $84/b in 2025. Persistent uncertainty, due to geopolitical tensions, particularly in the Middle East, will likely lead to further hikes in oil prices. However, weak oil demand from China will likely remain a drag.

The OECD expects U.S. GDP to grow 2.6% in 2024 before slowing to a 1.6% increase in 2025. The slowdown will likely be accompanied by a rise in unemployment. The Fed is expected to slash rates by another 50bps in November as inflation inches towards its target. Meanwhile, the U.S. economy is likely to witness a soft landing in 2024, while the following year, annual inflation is expected to converge to 2%, due primarily to a cooling labor market, likely bringing down wage growth and unit labor costs.

The euro area is expected to grow slightly, up 0.7%, in 2024 as energy prices ease, allowing disinflation to continue. However, the OECD believes that growth will nearly double to 1.3% in 2025 as real income grows faster than inflation. Inflation is expected to return to the 2% target by mid-2025. The OECD also hiked its outlook for the U.K. economy, citing expected wage growth. It now projects the economy to expand 1.1% in 2024 and 1.2% in 2025.

The Reserve Bank of Australia expects the Australian GDP growth over the next year to be stronger than initially forecast, as domestic demand remains strong. Meanwhile, consumption is expected to increase steadily as real household disposable income rebounds thanks to cooling inflation. Meanwhile, unemployment is forecast to rise steadily but the expected recovery in the Australian economy will provide some relief to the labor market.

The OECD lowered its 2024 growth estimate for Japan to -0.1% from 0.5% earlier. However, it expects the Japanese economy to grow 1.4% in 2025, as inflation-adjusted real wages rise, due to wage hikes and solid bonuses. Meanwhile, the Bank of Japan policymakers remained unsure about how quickly the central bank should raise interest rates.

The OECD believes that the Chinese economy will slow from 4.9% growth in 2024 to 4.5% in 2025 as government stimulus spending is offset by falling consumer demand and the real estate crisis. While China recently announced a historical stimulus package to prop up its failing economy, experts believe that it may be too late to boost this year's growth, with economists speculating that the country may miss its 5% growth target for 2024.

India is likely to remain the fastest-growing economy in 2024, driven by, in the OECD's view, growth in the service sector, an improved macroeconomic policy framework, and strong domestic demand. The organization revised India's 2024 economic growth projection from 6.6% to 6.7%. In addition, it expects the country's economy to grow 6.8% in 2025.

The OECD now projects the Brazilian economy will grow 2.9% in 2024 on strong domestic demand, cooling inflation, and expanding oil output. However, growth is expected to slow to 2.6% in 2025.

South Korea's economy is expected to benefit from strong semiconductor exports, rate cut optimism, and a recovery in global demand. The OECD expects the country's economy to grow 2.5% and 2.2% in 2024 and 2025, respectively.