GIB Asset Management Emerging Markets Active Engagement Strategy

Value unlock!
How active engagement can make a difference

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The GIB AM Emerging Markets Active Engagement Strategy is a core, scalable and differentiated investment strategy aiming to maximise risk-adjusted returns through its proprietary approach to truly active emerging markets investing. Our investment philosophy is shaped by the belief that active management must fully integrate engagement across the portfolio to unlock and drive greater recognition of fundamental value.

This is of particular importance in Emerging Markets.

The strategy is underpinned by a proprietary two-pillar process that both identifies undervalued businesses through its fundamentally driven bottom-up approach and partners with all portfolio companies to generate additional alpha from material ESG and operational improvements.

Engagement action points

Turning back to this quarter, we have seen some important engagement outcomes materialising to drive portfolio returns. Our engagement process with companies is typically a 36-month process and begins prior to our point of initial investment. We believe that each incremental step compounds to help drive the wider company transformation. We have outlined some highlights below:

One of our portfolio companies, a leading Chinese online recruitment platform, has faced significant market pressure due to deteriorating macroeconomic conditions in China and their implications for its business outlook. We have recommended several improvements to the company, including addressing excessive stock-based compensation and the lack of a granular framework for performance evaluation through key performance indicators (KPIs). Moreover, we believe that during times of increased market volatility and share price pressure, companies with substantial net cash reserves should proactively revisit their capital allocation policies and consider introducing an upsized buyback program. We are confident that rectifying these issues will immediately enhance shareholder returns and strengthen market perceptions of the company's governance practices.

Another portfolio company, a leading Chinese online travel service provider, experienced prolonged share price weakness throughout 2024, driven by challenging market conditions and subdued domestic travel demand. Despite a buyback program in place, which repurchased approximately 6 million shares in 2024, we identified further potential for capital returns, given the company's strong cash reserves. Our engagement emphasized the benefits of expanding the buyback program to enhance long-term compounding value. Consequently, the company announced plans for an expanded capital return program for 2025, pending board approval.

A Chinese food retailer in our portfolio has also faced valuation pressures due to weak domestic consumption. Our engagement focused on encouraging the company to accelerate and scale its franchising business, which, given its asset-light nature, has the potential to significantly improve return on invested capital (ROIC). Over time, this strategy can unlock shareholder value by enabling greater scalability and improving profitability, likely triggering a positive re-rating of the company's valuation. Following our recommendations, the company has increased its focus on franchising and has communicated the long-term benefits of this strategy to stakeholders.

In Saudi Arabia, a gym operator in our portfolio lagged peers in implementing sustainability initiatives. Our engagement outlined a three-step sustainability framework, beginning with a materiality survey to assess key environmental, social, and governance (ESG) issues among shareholders. Addressing these sustainability priorities can lower the company's implied cost of capital, attract sustainability-focused investors, and diversify the shareholder base. Following our engagement, the company initiated a materiality assessment to identify and address critical ESG concerns, marking a significant step forward in its sustainability journey.

GIB AM Analysis, 31.12.2024
No representation is being made that any account will or is likely to achieve profits or losses similar to those shown. Past performance is not indicative of future performance. Views, opinions, statements, forecasts and projections are as of date and subject to change without prior notice. There is no guarantee they will be met.

Sustainability engagement at a portfolio level

Our portfolio companies have demonstrated a strong commitment to advancing governance and sustainability practices, consistently outperforming the MSCI Emerging Markets Index on key engagement metrics. Since the inception of our fund, we have actively engaged with portfolio companies, driving significant achievements in board independence, diversity, sustainability, and capital allocation.

Board Independence

A key focus has been increasing the independence of boards of directors. Since our fund's launch, 13 of our portfolio companies, representing 28%, have enhanced their board independence. This helped bring the average Board independence ratio of the portfolio to 54.4% vs. 44.7% average for the benchmark. This improvement in board composition has led to better oversight, accountability, and more robust decision-making processes. Notably, three of our portfolio companies have exceeded the 50% board independence threshold, reflecting a commitment to strong governance practices and the importance of independent boards providing unbiased guidance and oversight.

Diversity

Diversity on boards is critical for fostering varied perspectives and inclusive decision-making. Our proactive engagement has driven significant progress in this area, with 35% of our portfolio companies, increasing the share of female representation on their boards. As a result of this improvement the average female board participation for the portfolio increased to 19.35 vs 17.1% for the benchmark. This commitment to gender diversity underscores the positive impact of our engagement on governance practices.

Sustainability

Following our Net Zero engagement, 20% of portfolio holdings have introduced SBTI net zero targets, showcasing a dedication to sustainable practices.

Capital Allocation

Additionally, 32% of portfolio companies increased their dividend payout ratio during our investment period, reflecting a more focused and enhanced approach to capital allocation.

These efforts have not only improved corporate governance, sustainability, and capital allocation but have also contributed to the enhanced ESG ratings of our portfolio companies. During this period, 33% of our holdings have registered MSCI ESG ratings upgrades, with 15% achieving at least a double upgrade. While our primary engagement goal is not to improve ESG ratings, we believe these improvements can significantly help companies reduce their implied cost of capital, ultimately serving as a source of return for our fund.

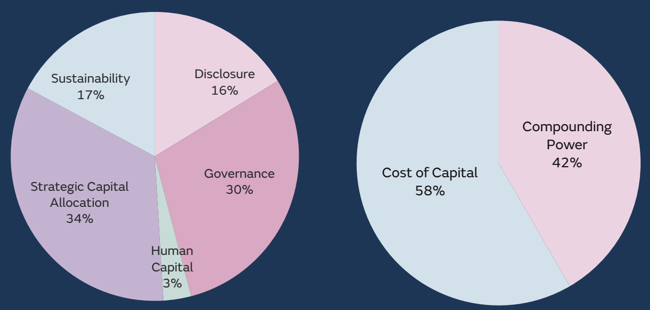
These achievements highlight our dedication to active management, reinforcing shareholder returns through purposeful and sustained engagement.

Our engagement outlook ahead

We are particularly excited about the inbuilt latency that exists in the portfolio today. We were successful with 67 Engagement Action Points since inception with each having an impact on improving the Compounding Power or reducing the market implied Cost of Capital for their respective business.

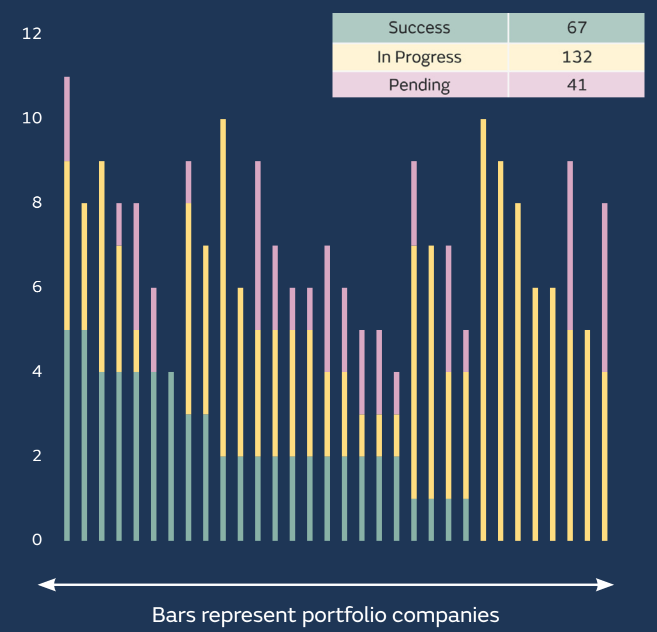
Looking ahead, there remain 173 outstanding Action Points across the portfolio, which we believe can help drive future incremental returns. Of these Action Points, 58% are focused on reducing the market implied Cost of Capital whilst 42% aim on improving the business' Compounding Power. 30% of our Action Points center on improving Governance; 34% on Strategic Capital Allocation; 17% on incorporating Sustainability as a source of returns, 16% on improved Disclosure and 3% on material improvements in Human Capital.

Chart 1[1]: Engagement snapshot since inception



The chart bellows illustrates the remaining Action Points we have for our 34 companies in the portfolio. 66 Action Points have been successfully resolved (shaded green) however, the yellow and purple shaded areas point to the outstanding unresolved Action Points that represent unaccounted inbuilt latency.

Chart 2[2]: Engagement latency - outstanding suggestions in our current portfolio



As these bars turn incrementally green over the subsequent months and years ahead, this can be a strong predictor of future shareholder returns to come.

This update is an extract from our GIB AM Emerging Markets Active Engagement Quarter 4 letter. ***If you would like to read the report or hear more from our team, please email info@gibam.com.***

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[1& 2] GIB AM Analysis as at 31.12.2024.
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