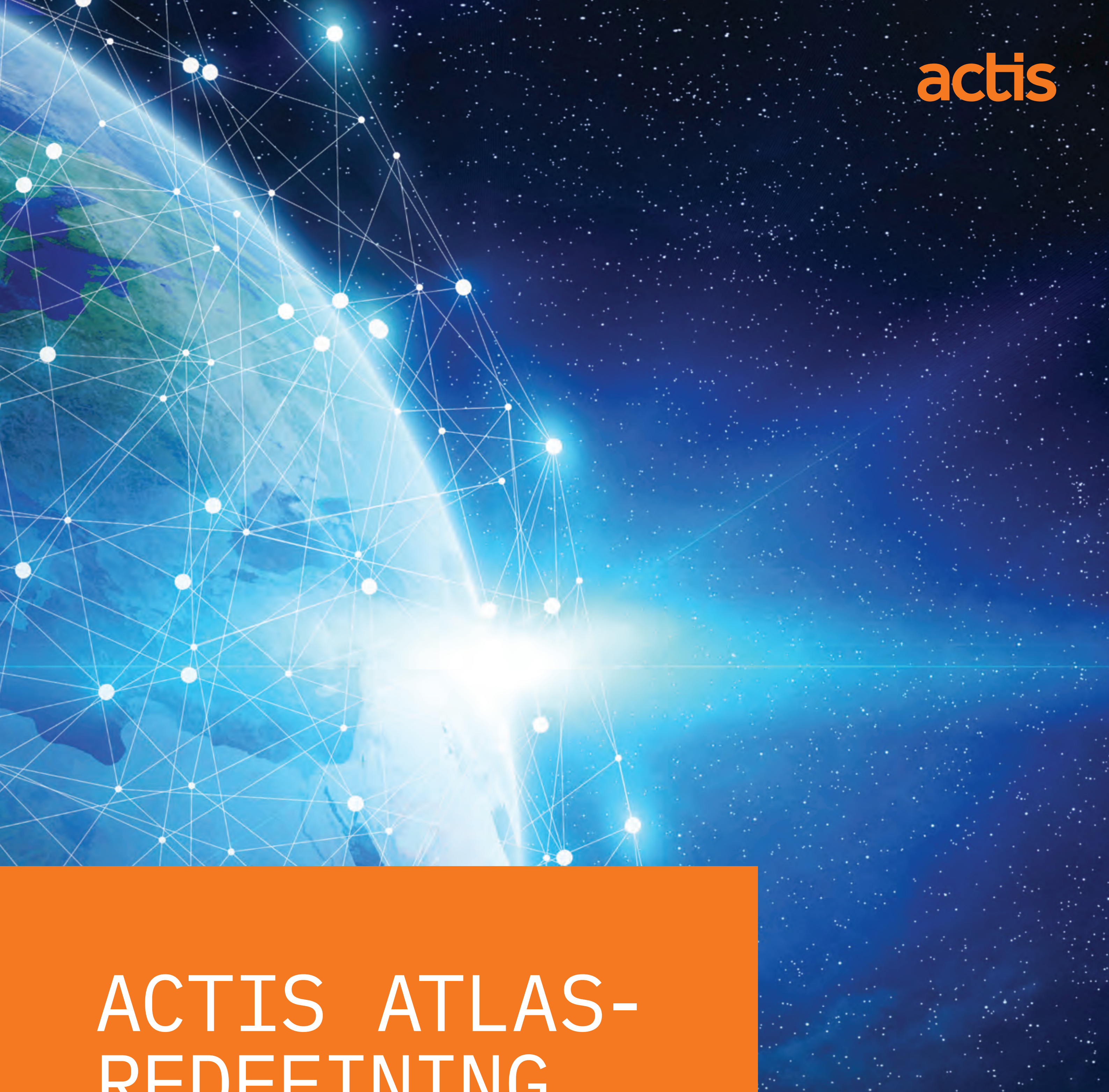

ACTIS ATLAS- REDEFINING GLOBAL INVESTMENT OPPORTUNITY

THE STREET VIEW

JUNE 2023

CONTENTS

SUMMING UP

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Why We Wrote This Report

- Commonplace labels applied across global markets substitute simplicity for opportunity.
- Labels including Developed Markets ('DM'), Emerging Markets ('EM') and Frontier Markets ('FM') assume a non-existent homogeneity of investment and macroeconomic risk.
- Labels are fine but there are too few of them to allow for genuine opportunity.
- As a major, global, long-term, thematic investor with a focus on hard assets, Actis and our clients have real skin in the game.

What We Recommend

- We introduce six categories which we feel allow for more equitable assessment of opportunity.
- Countries are assigned to a single basket each, as an initial screen and limited to those where Actis either has invested or may do so in the near future.
- These assessments are based on a variety of criteria, including financial stability, macroeconomic and societal fundamentals and drivers of currency risk.

"COMMONPLACE LABELS APPLIED ACROSS GLOBAL MARKETS SUBSTITUTE OPPORTUNITY FOR SIMPLICITY."

The Six Buckets

1. **Global Influencers** are major economies which are givers rather than takers of global investment risk. These are **China, Japan and USA.**
2. **Big Middles** are G20 members with substantial financial resource and resilience. These are **Brazil, India, Mexico and South Korea.**
3. **Supply Chain Heroes** are materially exposed to non-resources targeted FDI, so-called China plus One, and generally operate orthodox policies. We nominate **Malaysia, Philippines, Thailand and Vietnam.**
4. **Stable but Small.** Size means these countries, despite having sensible policy mixes are exposed to risks from larger economies. We include **Bulgaria, Lithuania, Morocco, Romania and Uruguay.**
5. **Natural Resource Winners** are materially net exporters of one or more commodities. We include **Chile, Colombia, Gulf Cooperation Council (GCC) members, Indonesia, Peru and South Africa.**
6. **Structurally Challenged** are countries where past policy decisions and/or income levels have created material macroeconomic and currency volatility. We include **Egypt, Ghana, Kenya, Nigeria and Türkiye.**

Investment Conclusions

- Establishing the main risks allows for asset pricing, selection and where appropriate effective risk mitigation.
- This is not a framework for rejection or selection, rather a series of working titles to allow effective investment and portfolio management.
- There is no consistent link between categorisation and level of return.
- Capital flows towards effective risk return opportunities. Lower risk tends to attract more capital and potentially lower returns via crowding out.
- A successful investor can manage selection, mitigation and opportunities given a clear initial framework.

How the Report is Organised

- **Section 1** 'Definition and Proposition' describes the six categories and the basis for each selection.
- **Section 2** 'Proving the Case' is a deeper dive into the factors and risks for each categorisation.
- **Section 3** 'So What?' states our basic conclusions from the paper.

"A SUCCESSFUL INVESTOR CAN MANAGE SELECTION, MITIGATION AND OPPORTUNITIES PROVIDED A CLEAR INITIAL FRAMEWORK."

DEFINING THE INVESTMENT OPPORTUNITY

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The investment world is becoming more complex. Many of the traditional guidelines which have helped investors make sense of the economic and political environment in different countries are no longer useful when allocating capital. Investors who treat the 80+ Emerging Markets in particular as a single, homogenous group risk misjudging their strategies as a result. What is needed is a new lens through which investors can compare and contrast the risks and opportunities they face.

At Actis, we have therefore grouped the countries we invest in into six new categories through which we believe investors should view the world. They are Global Influencers, Big Middles, Supply Chain Heroes, Stable but Small, Natural Resource Winners, and the Structurally Challenged. The countries within each category have a number of similar characteristics which can help investors make more informed decisions than taking a one-size-fits-all view of the Emerging Markets.

Our objective in creating this framework is to help investors think more coherently about those markets. This means we are able to make better investments with clearer objectives, using a common language both internally and externally with our own investors.

"THIS FRAMEWORK IS TO HELP INVESTORS THINK MORE COHERENTLY ABOUT OUR MARKETS. IT MEANS WE ARE ABLE TO MAKE BETTER INVESTMENTS WITH CLEARER OBJECTIVES, USING A COMMON LANGUAGE BOTH INTERNALLY AND EXTERNALLY WITH OUR OWN INVESTORS."

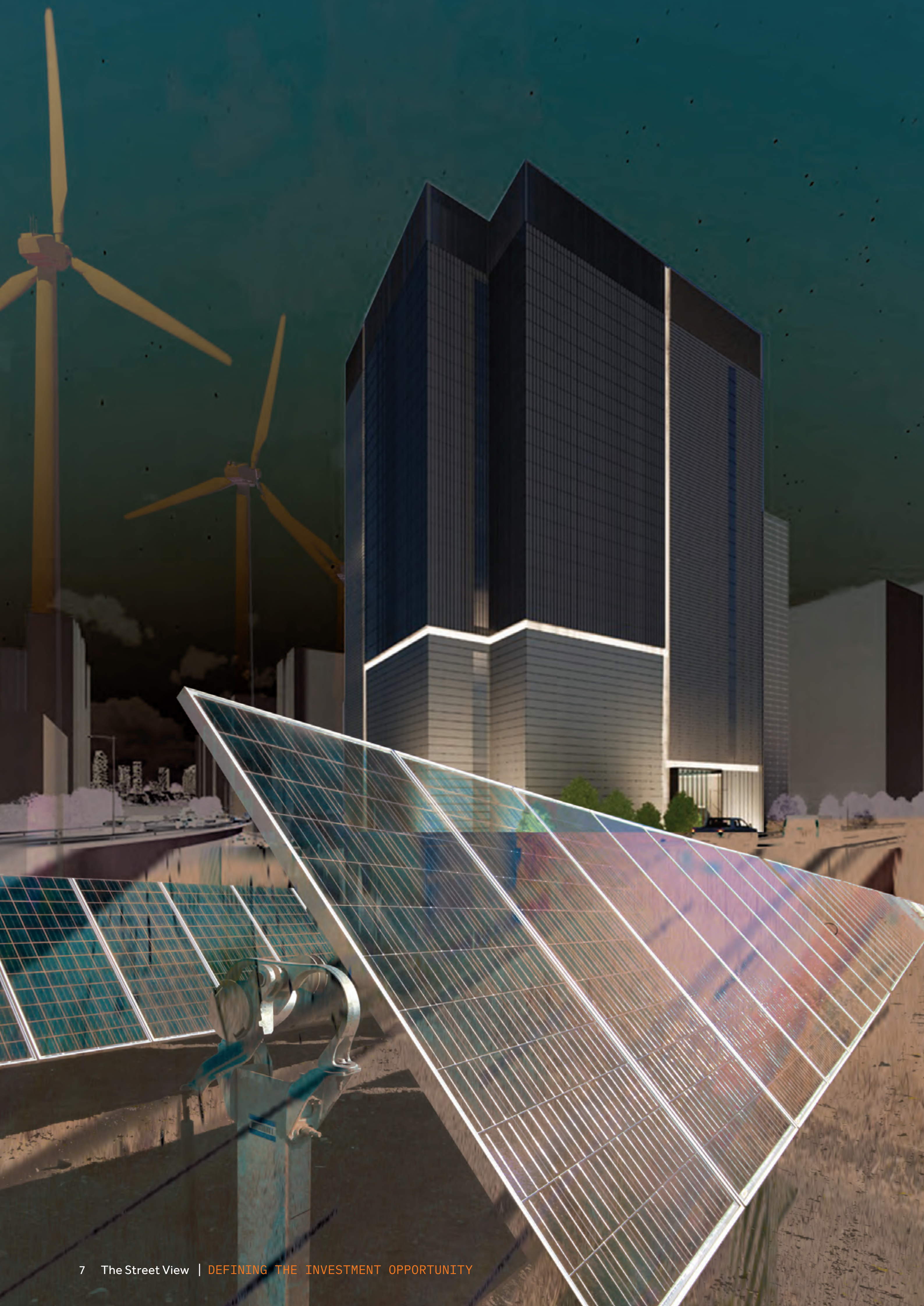
As a global allocator of capital, we are always looking for the best risk-adjusted returns. How do we do this? We look at secular tailwinds: the energy transition, digital transformation and new economy real estate. We call on our deep understanding of our markets, thanks to our 75-year heritage across more than 40 countries. We take a long-term perspective, which enables us to look beyond the headlines to deliver solid returns over many years. And we look at the investment thesis of each opportunity, analysing the risks and potential returns behind each business we assess.

Our new framework enables us to make deeper, more considered decisions when using these criteria. This helps us better assess both market volatility and the risk-return opportunities we face. It also helps us understand the structural changes that may be going on around the world, and how we can benefit from them. When looking at natural resources for example, thanks to net-zero and electrification, mineral resource producers are replacing oil and gas owners as the most significant winners. Our framework gives us an overview of which countries these changes may affect, guiding our decision-making.

The framework also helps us decide whether a trend in one country means other countries in the same group will benefit. And it also allows us to take decisions with greater conviction. We have, for example, decided to invest in Mexico in part because of the high level of domestic savings, a key feature of countries in the 'Big Middles' category.

Our framework allows us to better assess the countries and businesses we invest in, and how we can take advantage of the opportunities they offer. We believe it will help investors around the world to see the Emerging Markets in a clearer way and provide a better understanding of the potential they offer.

WATCH VIDEO



ACTIS ATLAS: MEASURING THE INVESTMENT WORLD

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WATCH VIDEO

Why we Wrote This Report

Investors love labels. Developed, Emerging and Frontier Markets are the most common groupings applied to economies, asset allocation and risk budgeting. Like it or not, these labels exist and are widely employed in investment decision making.

Consensus can blur reality and obscure opportunity. Within these major categories, wide differences exist. A global thematic investor like Actis seeks out opportunities wherever they exist. The homogeneity implied by broad categorisation has limited utility in assessing specific country risk. Fortunes have been lost rather than made in pursuit of consensus.

"CONSENSUS CAN BLUR REALITY AND OBSCURE OPPORTUNITY. WITHIN THESE MAJOR CATEGORIES WIDE DIFFERENCES EXIST. A GLOBAL THEMATIC INVESTOR LIKE ACTIS SEEKS OUT OPPORTUNITIES WHEREVER THEY EXIST."

"Emerging Markets" as a catch-all label is a major culprit in creating misconceptions based around assumed similarity. Covering most of the global population, geography, resource production, and foreign exchange reserves, the 80 countries or more in this bucket have less in common with each other than the 25 or so developed markets. How is South Korea like Peru? Or Estonia and Qatar? Or South Africa and India? Yet they are all lumped into the one classification.

Equally, there are profound structural differences between many developed markets. Resource winners such as Canada and Australia clearly differ from France, Spain and the UK.

These broad characterisations have become increasingly misleading since first employed in the mid-1980s. In this, the hand of indexation and risk budgeting hang heavy. Today, the idea of a 100-page report on the Nepal stock market as was written in 1992 (top tip Yak and Yeti Holdings) is quaint. More to the point, homogeneity has suffocated opportunity, with a handful of countries representing over 80% of most indices.

Across 80 plus countries, wide differences of opportunity are obvious. Yet common and lazy investment and media shorthand ignores this point. The weakest countries frequently dominate the dialogue. The case of Sri Lanka – a wonderful country with woeful macroeconomics – overwhelms the attractions of India just to the north in the mantra that EM is too risky, too corrupt and unable to deliver returns. 'Four legs good, two legs bad' to quote Snowball the pig in George Orwell's classic "Animal Farm".

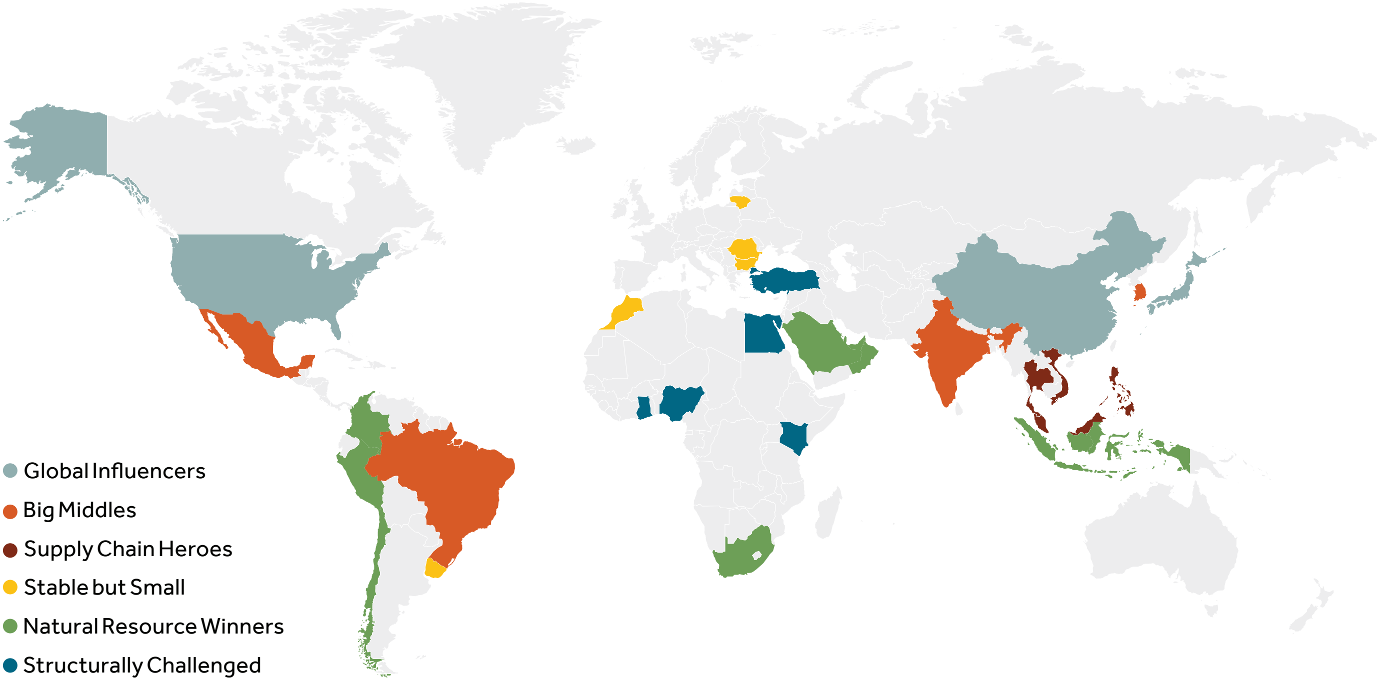
Over the 40 years since the Emerging Markets label was first employed, other taxonomies have been tried. The investment graveyard is stacked with BRICS, MINTS, Next 11, Fragile 5 and other whims. Some struggled because the premise imploded (BRICS), others were more temporal or pejorative (Fragile 5). Most of all, the relentless march in liquid markets towards indexation obliterated incentives to differentiate. Worth noting that even the plethora of single country ETFs attract a fraction of the flows that go to the broader categorisations.

Given this, why bother to distinguish? Is there real investment opportunity in embracing diversity? We believe so.

Actis is a global investor with a particular heritage in the Emerging Markets. We have, as they say, real skin in the game. Our entire investment history – over 70 years, US$ 25 billion capital raised, and 43 countries – speaks to the value of diversity of opportunity. We are used to staring beyond the headlines to spot opportunity, whilst operating a disciplined approach to individual investment evaluation and managing risk.

"WE ARE USED TO STARING BEYOND THE HEADLINES TO SPOT OPPORTUNITY, WHILST OPERATING A DISCIPLINED APPROACH TO INDIVIDUAL INVESTMENT EVALUATION AND MANAGING RISK."

EXHIBIT 1: ACTIS ATLAS: A COUNTRY TAXONOMY



Discipline ensures consistent, objective, risk aware decision making. Our footprint is truly global, increasing the need for sub-categorisation as we seek opportunity. Our LP community and other stakeholders ask us to differentiate between countries in a consistent fashion and be able to explain decisions and outcomes using meaningful frameworks. Some of the larger and more diversified asset owners are also seeking categorisations to shape their own strategic and tactical decision making. Hence, we present here our new taxonomy of global investing.

Let's be clear – we don't expect that EM or DM will die as labels. We don't expect the process we have applied to be infallible or immune to criticism. We have applied a limited series of judgements, conscious of the virtue of simplicity over complexity.

In consequence, we have placed countries in a single bucket even when they obviously span more than a single category (see Exhibit 1).

In short, this report helps unpack global investment opportunities beyond the two big, over simplistic, labels of Developed and Emerging Markets. We strongly assert that broad brush judgements which have no justification beyond simplicity, do not drive successful investment outcomes for longer term investors. We do recognise that some categorisation is essential to allow for appropriate benchmarking of opportunity and disciplined risk budgeting. We don't hate labels; we simply think there are too few to be useful these days. Extrapolation can harm your wealth.

This report now falls into three sections. First, we outline our definitions and allocations. Second, in a longer and more detailed section we explain our methodology and provide proof statements. Finally, we summarise a few brief conclusions.

"HOW IS SOUTH KOREA LIKE PERU? OR ESTONIA AND QATAR? OR SOUTH AFRICA AND INDIA? YET THEY ARE ALL LUMPED INTO THE ONE CLASSIFICATION."

SECTION 1:
DEFINITION AND PROPOSITION

DISSECTING THE GLOBE

Our taxonomy allocates the major countries where Actis invests into one of six separate buckets. We explore the methodology below. These working titles are designed to focus that investment debate and risk taking. Our analysis targets sources of financial risk including currency drivers, liquidity, inflation and how these trends may evolve during our investment holding periods, typically five years as a minimum.

We have worked closely with Cross Border Capital ('CBC'), a London based research boutique with over 30 years' experience analysing currencies and liquidity. Their quantitative approach to FX forecasting acknowledges that exchange rates and liquidity are driven by different factors depending on the time horizon. Actis employs CBC as our key partner in generating FX forecasts for use in investment decision making. We have incorporated a peer review process including input from DSG Asia, a respected Hong Kong based consultancy and long-time Actis Adviser.

Some countries are difficult to fit into any one group. We have struggled to reflect countries where policy unorthodoxy has created increased risk – **Türkiye** being a prime example (spoiler alert we put it in 'Structurally Challenged'). We have excluded countries where we have not yet invested, most notably **mainstream EU countries**. We also recognise that there will be sensitivities about where some countries are allocated.

We believe most countries can be allocated to one of the following six buckets. Remember that in the interests of simplicity, we have opted for one label per country, even though very obviously countries may fall into several categories.

1. Global Influencers

These are countries which, by virtue of their size, are global price fixers in goods and services. They typically have large and material shares of trade volumes in goods and services. Crucially, by virtue of size, they are givers rather than receivers of investment and macroeconomic risk.

Our nominations are

- China
- Japan
- USA

2. Big Middles

These economies are often classified as EM, yet their economic and financial systems are usually sizeable, and well developed. Generally, the countries in this category also have significant domestic savings institutions (which helps smooth volatility as explained later in this paper). They also enjoy substantial foreign exchange reserves. They are all G20 members and recognised as significant players in the global economy. Their increased institutional maturity has led to better macro management and improved currency resilience. We don't include mainstream Europe or the UK as we don't invest there yet but they would naturally fall into this area.

Our nominations are

- Brazil
- India
- Mexico
- South Korea

3. Supply Chain Heroes

In general, these are countries who have seen significant and sustained levels of foreign direct investment beyond natural resources and are increasingly embedded in global supply chains. This group benefits from "China Plus One". Our nominations in this category exclude countries with volatile exchange rates or unorthodox monetary policies, because we believe such choices undermine the concept of investment led stability.

Our nominations are

- Malaysia
- Philippines
- Thailand
- Vietnam

4. Stable but Small

Not exactly the catchiest title, but useful for differentiating from what we label 'Big Middles'. These countries may run structural deficits or have negative net international investment positions. The key factor by virtue of the size of their economies, is that they are price and policy takers, not givers.

Our nominations are

- Bulgaria
- Lithuania
- Morocco
- Romania
- Uruguay

5. Natural Resource Winners

The title says it all. These are countries where natural resource cycles are material drivers of financial and economic stability. They generally have currencies, which if free floating, reflect price swings in natural resources. Those with fixed exchange rates reflect these swings in current accounts and fiscal conditions. Energy transition has the longer-term potential to redistribute the spoils within this category, favouring minerals and new material providers over fossil fuel based economies.

Our nominations are

- Chile
- Colombia
- GCC
- Indonesia
- Peru
- South Africa

6. Structurally Challenged

These countries have debt servicing issues or have adopted unorthodox policy mixes. Financial and/or macroeconomic volatility seem to be a way of life. With one important exception (Türkiye) these countries have low tax revenues to GDP, narrow domestic financial systems and have borrowed in currencies other than their own.

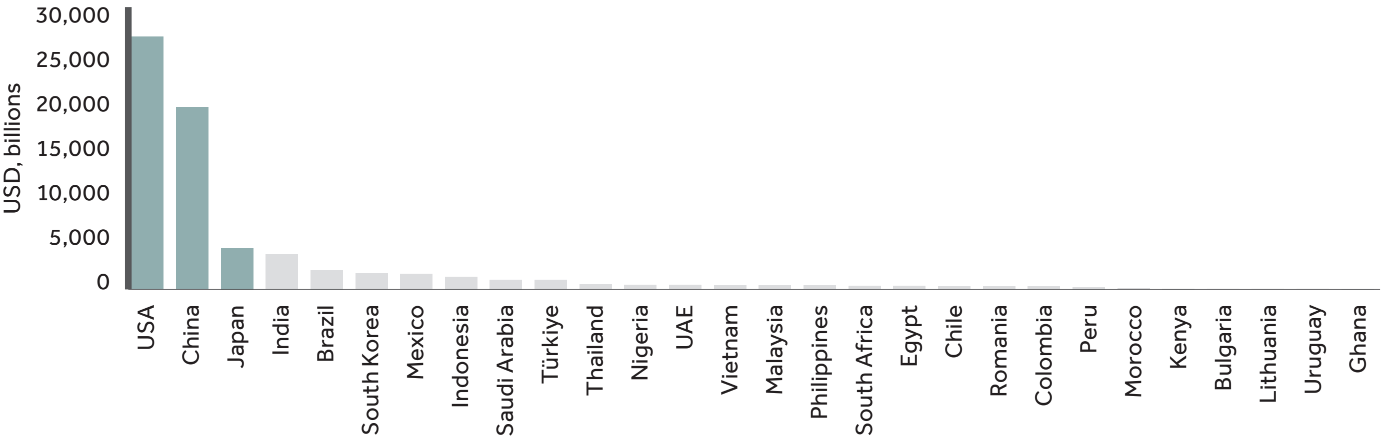
Our nominations are

- Egypt
- Ghana
- Kenya
- Nigeria
- Türkiye

GLOBAL INFLUENCERS

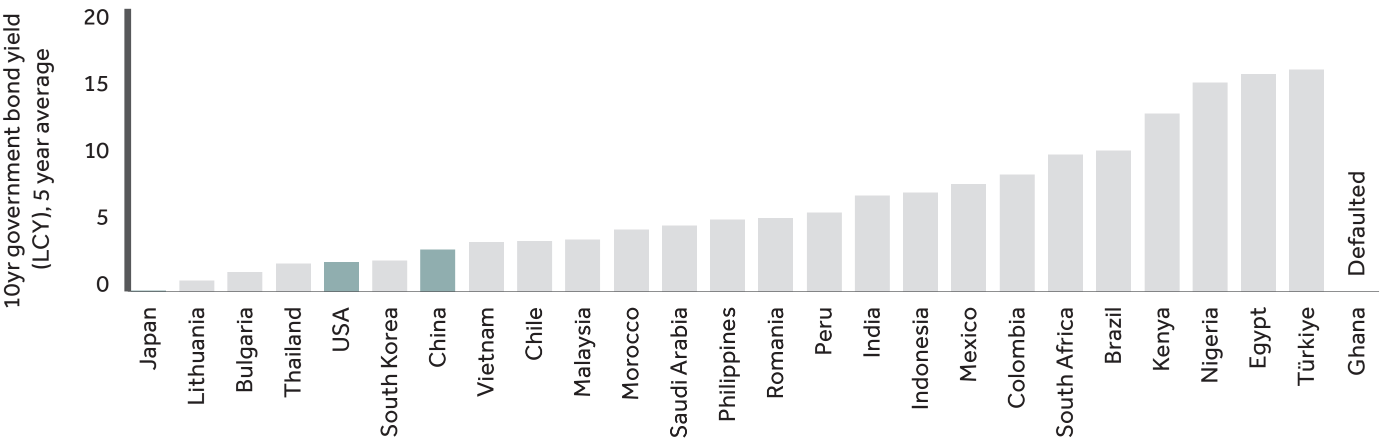
WHAT	• Major economies • Large share of world trade and/or services • Givers not receivers of risks • High productivity • High scores for human capital • Structural budget deficits • Deep financial systems • Higher (but mixed) political stability
WHO	• China • Japan • USA
CHARACTERISTICS	• Economic size • Floating currencies • Financial depth • Wide opportunity spread • Peaking inflation • Low currency and bond volatility

NOMINAL GDP SIZE, 2023

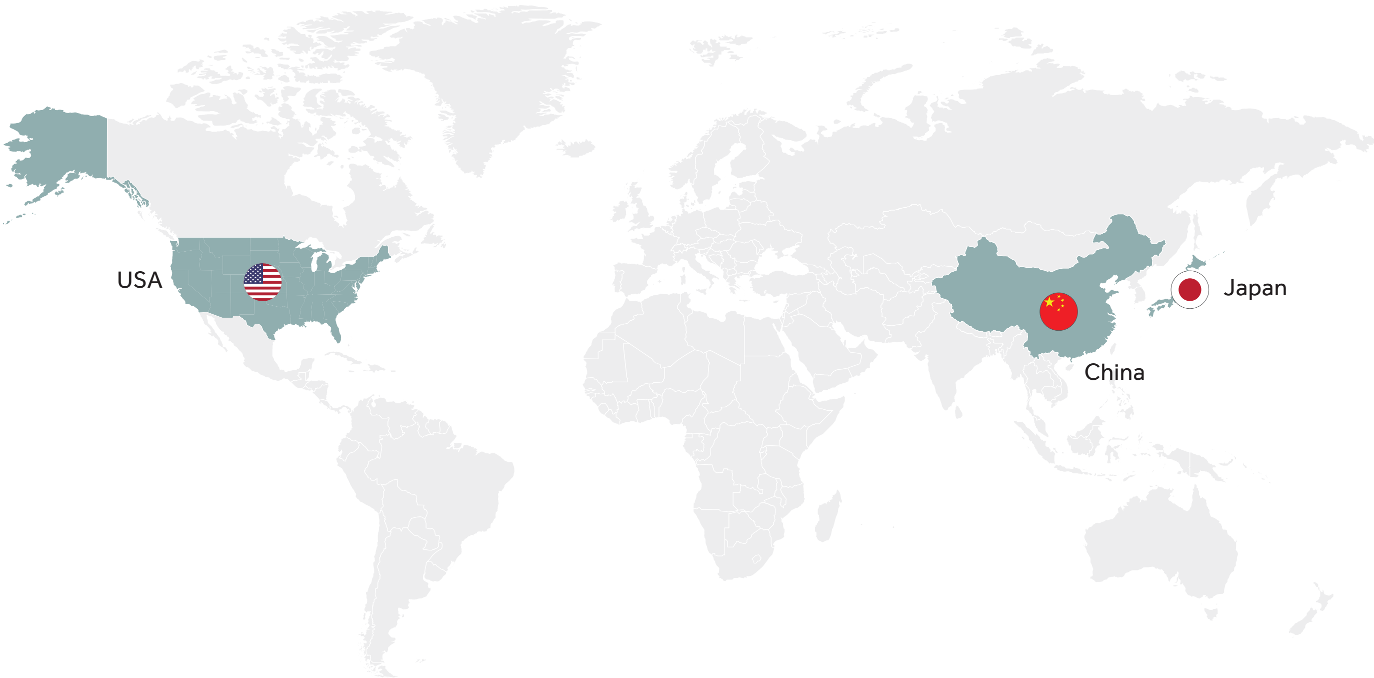


Source: International Monetary Fund, World Economic Outlook database, April 2023.

10YR GOVERNMENT BOND YIELD (LOCAL CURRENCY), LAST 5-YEAR AVERAGE



Note: Data was not available for UAE and Uruguay. Data represents the average yield between June 8, 2018 and June 7, 2023.
Source: Bloomberg LP, 2023.



WHERE WE STAND TODAY

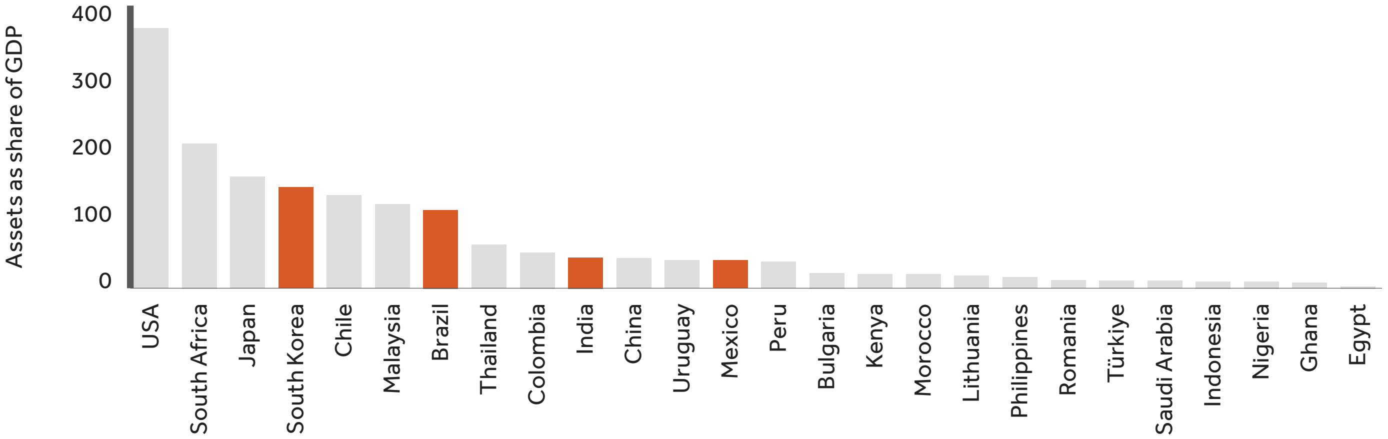
CHINA	• April 2023 inflation 0.1%, down from 2.8% in September 2022 • Interest rate 3.65%, down 15bps since January 2022 • Real GDP growth 3.0% in 2022, and accelerating this year • Renminbi trading at 7.00 per USD, 4% weaker than a year ago • Growth slowly recovering post Covid led by consumption. Investment rebound more muted as confidence yet to be fully restored
JAPAN	• April 2023 inflation 3.5%, down from 4.3% in January 2023 • Interest rate -0.1%, no change since January 2022 • Real GDP growth 1.1% in 2022, and accelerating this year • Yen trading at 138.1 per USD, 10% weaker than a year ago but off recent lows • Growth accelerating at the margin as companies reshore activities. Capital flow back and BoJ action have stabilised currency. Macro generally constructive
USA	• April 2023 inflation 4.9%, down from 9.1% in June 2022 • Interest rate 5.25%, up 500bps since January 2022 • Real GDP growth 2.1% in 2022 • US dollar Index (DXY) 103.2, flat compared to a year ago • Activity yet to slow materially despite Fed actions. Inflation remains on a gradual downward path and outlook for rate rises has softened

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund, World Economic Outlook database (April 2023) for real GDP growth figures in 2022 and 2023f. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

BIG MIDDLES

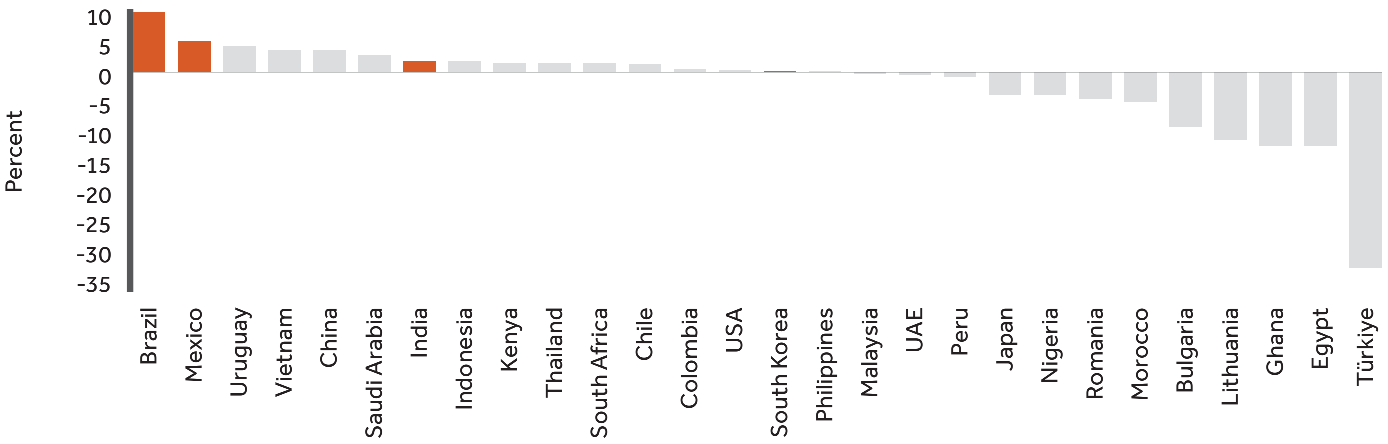
WHAT	• G20 Members • Large, diversified economies and populations • Financial stability / depth • Low currency volatility • Substantial FX reserves • Risk receivers
WHO	• Brazil • India • Mexico • South Korea
CHARACTERISTICS	• Floating currencies / falling volatility • Domestic capital market depth • Higher but variable Human Capital Index • Wide range of investment opportunity

RATIO OF ASSETS OF PENSION FUNDS, MUTUAL FUNDS AND INSURANCE COMPANIES TO GDP, 2020 OR LATEST



Note: Data was not available for UAE and Vietnam.
Source: The World Bank, Global Financial Development Database, 2022.

REAL INTEREST RATE, JUNE 2023



Note: Real interest rate is interest rate minus inflation rate. Data as of June 7, 2023.
Source: Bloomberg LP, 2023.

WHERE WE STAND TODAY

BRAZIL

- April 2023 inflation 4.2%, down from 12.1% in April 2022
- Interest rate 13.75%, up 450bps since January 2022
- GDP growth 2.9% in 2022
- Real trading at 4.96 per USD, flat compared to a year ago
- Despite political noise and volatility, stable economic fundamentals and growth backdrop

INDIA

- April 2023 inflation 4.7%, down from 7.8% in April 2022
- Interest rate 6.5%, up 250bps since January 2022
- GDP growth 6.8% in 2022
- Rupee trading at 82.7 per USD, 6% weaker than a year ago
- Continuing stability from macro and political standpoint

MEXICO

- April 2023 inflation 6.3%, down from 8.7% in September 2022
- Interest rate 11.25%, up 575bps since January 2022
- GDP growth 3.1% in 2022
- Mexican peso trading at 17.6 per USD, 11% stronger than a year ago
- Material beneficiary of nearshoring and FDI inflows

SOUTH KOREA

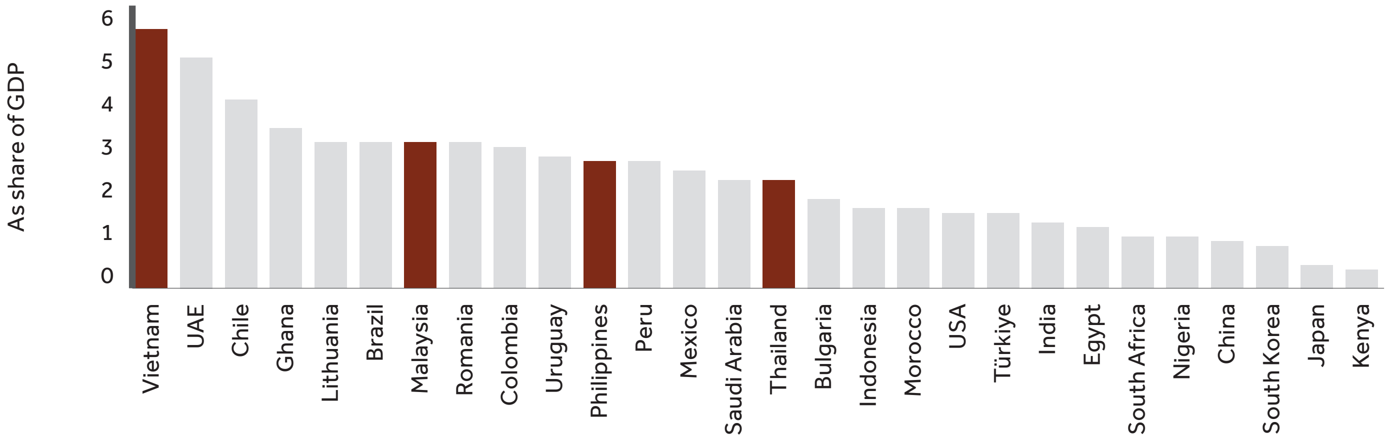
- April 2023 inflation 3.7%, down from 6.3% in July 2022
- Interest rate 3.5%, up 225bps since January 2022
- GDP growth 2.6% in 2022
- Won trading at 1327 per USD, 4% weaker than a year ago
- Macro generally sound with won slowly appreciating alongside yen

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund World Economic Outlook database (April 2023) for real GDP growth figures in 2022. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

SUPPLY CHAIN HEROES

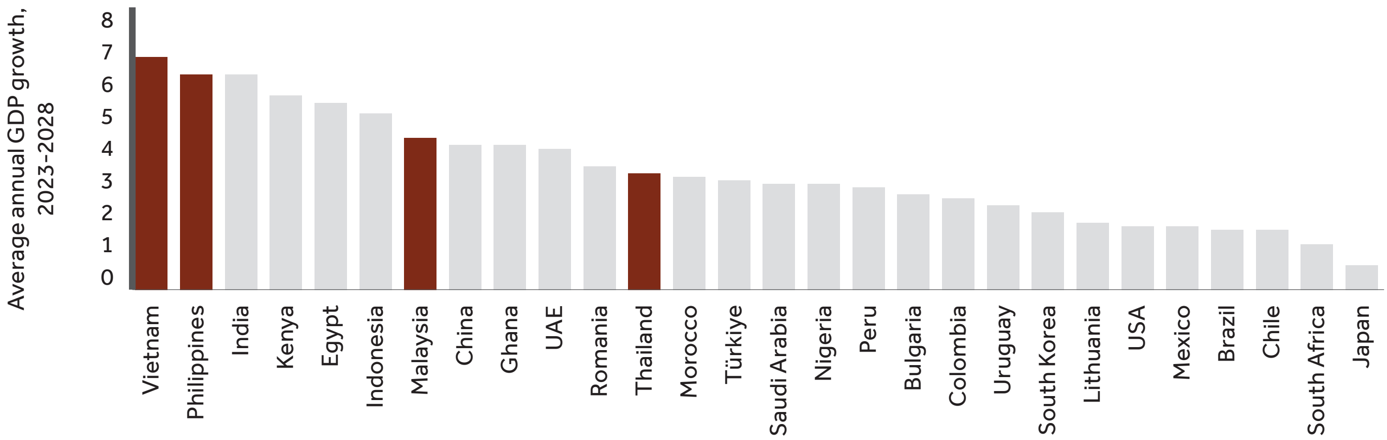
WHAT	• Significant and sustained non-natural resources FDI • China+1 winners • Increasing role in supply chains • Lower volatility FX • Financial systems deepening
WHO	• Malaysia • Philippines • Thailand • Vietnam
CHARACTERISTICS	• Rising investment opportunity set • Fast growing population • Improving educational attainment • Declining currency and bond volatility • Deepening financial systems

RATIO OF INWARD FDI FLOWS TO GDP, 2021

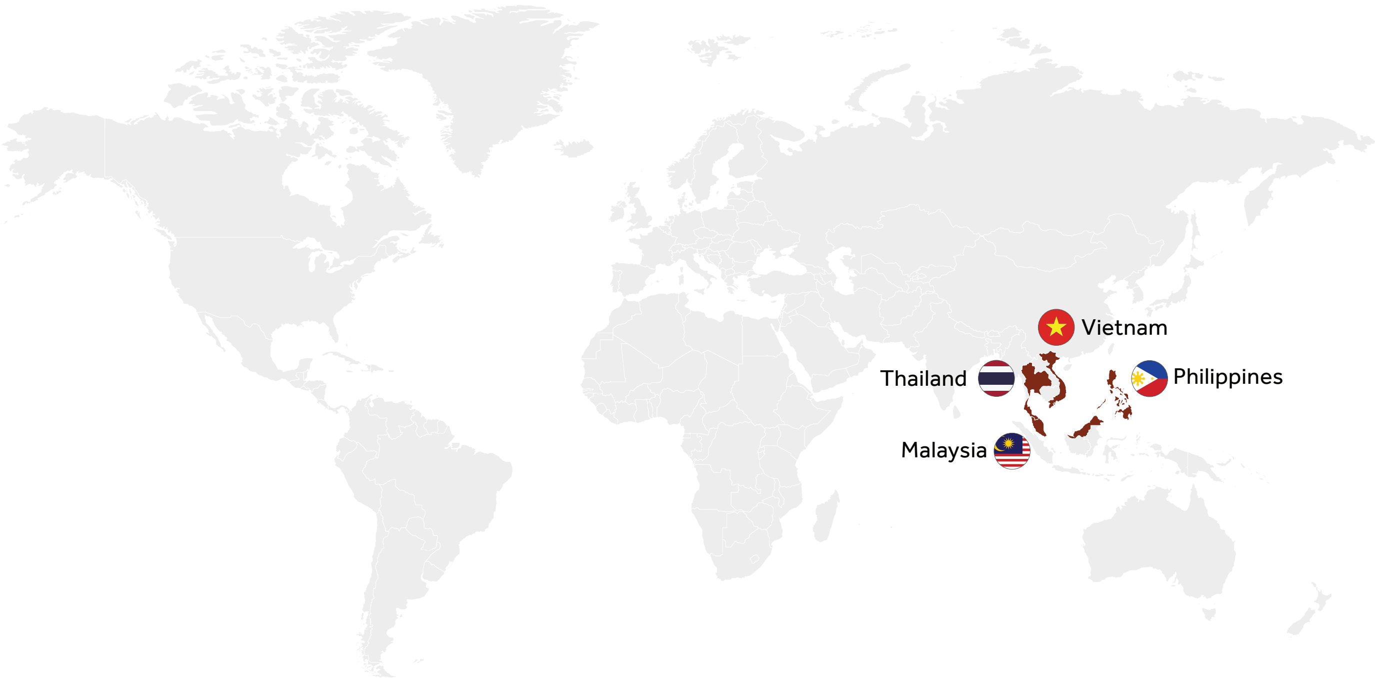


Source: UNCTADstat database, 2023.

REAL GDP GROWTH OUTLOOK, 2023-2028



Note: The columns on the graph represent average annual real GDP growth between 2023 and 2028.
Source: International Monetary Fund, World Economic Outlook database, April 2023.



WHERE WE STAND TODAY

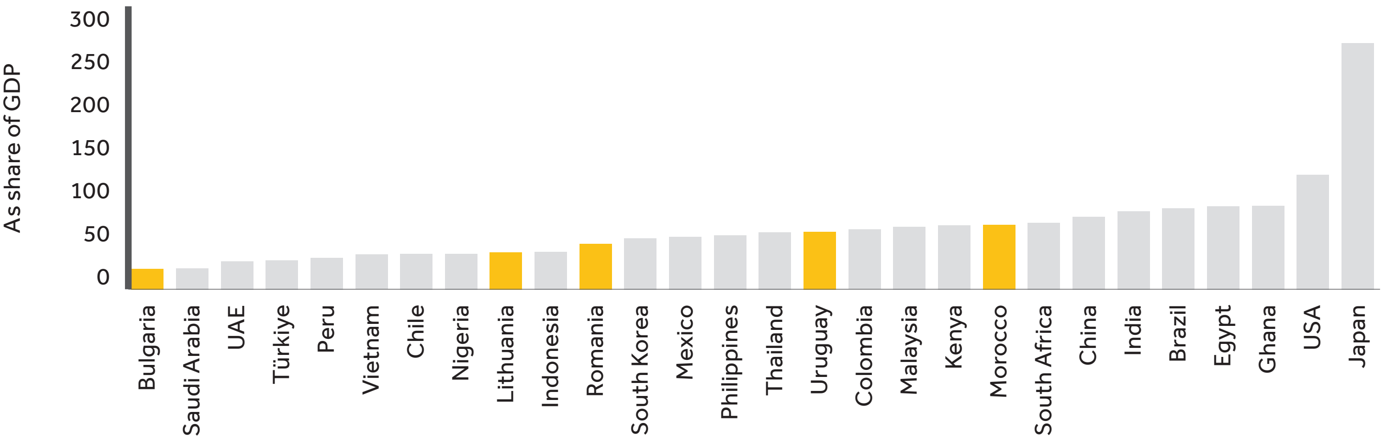
MALAYSIA	• March 2023 inflation 3.4%, down from 4.7% in August 2022 • Interest rate 3.0%, up 125bps since January 2022 • GDP growth 8.7% in 2022, an outperformer • Ringgit trading at 4.54 per USD, 3% weaker than a year ago • A relative success over last decade with sound banking and financial institutions
PHILIPPINES	• April 2023 inflation 6.6%, down from 8.7% in January 2023 • Interest rate 6.25%, up 425bps since January 2022 • GDP growth 7.6% in 2022, an outperformer • Philippine peso trading at 55.68 per USD, 6% weaker than a year ago • Relatively stable macro picture despite some balance of payment constraints
THAILAND	• April 2023 inflation 2.7%, down from 7.9% in August 2022 • Interest rate 2.0%, up 150bps since January 2022 • GDP growth 2.6% in 2022, and accelerating this year • Baht trading at 33.7 per USD, 3% stronger than a year ago • Well-positioned to benefit from China+1 with a long export manufacturing tradition; baht is a fairly stable currency, tipped to benefit from tourism recovery
VIETNAM	• April 2023 inflation 2.8%, down from 4.9% in January 2023 • Interest rates 6%, up 200bps since January 2022 • GDP growth 8% in 2022, an outperformer • Dong trading at 23,469 per USD, flat compared to a year ago • Key winner of China+1 story with a low volatility, slowly depreciating currency. FDI inflows of $1.5-2.5bn every month

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund World Economic Outlook database (April 2023) for real GDP growth figures in 2022 and 2023f. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

STABLE BUT SMALL

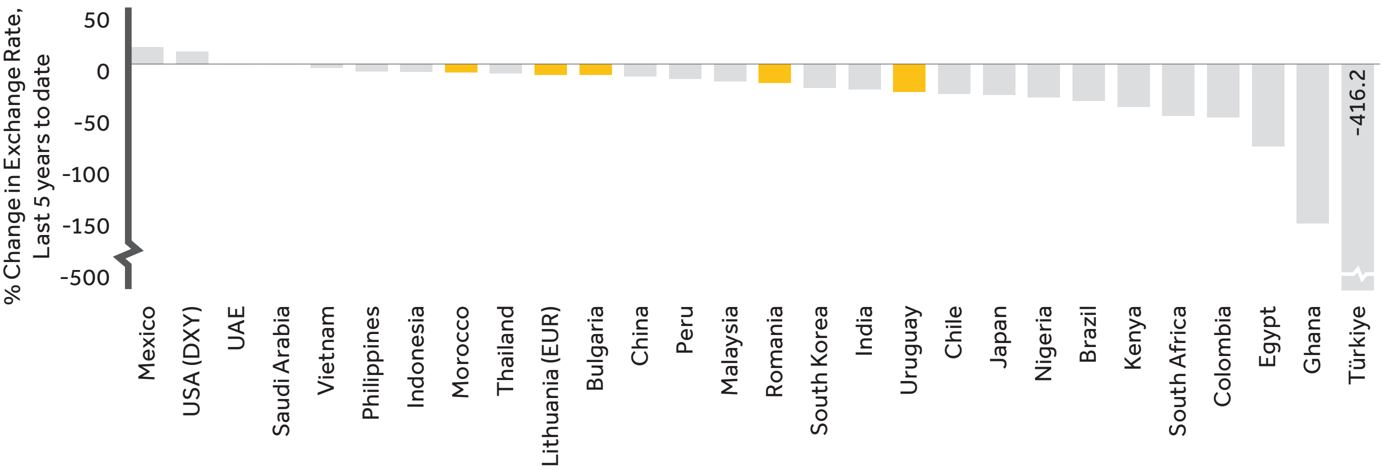
WHAT	• Smaller GDP size • Negative net international investment position • Lower currency volatility • Higher debt service costs • High inflation • High scores for rule of law/transparency • Risk receivers
WHO	• Bulgaria • Lithuania • Morocco • Romania • Uruguay
CHARACTERISTICS	• Structural deficits • Falling currency volatility • Rising bond yields

RATIO OF GENERAL GOVERNMENT DEBT TO GDP, 2022



Source: International Monetary Fund, Fiscal Monitor database, April 2023.

FOREIGN EXCHANGE RATE PERFORMANCE, LAST 5 YEARS TO DATE



Note: All exchange rates are against the USD; except for the United States, which is against DXY. Minus sign equals depreciation, plus sign is appreciation against USD. UAE and Saudi Arabia currencies are pegged to USD. Lithuania has euro and Bulgaria's currency is pegged to euro. Morocco's currency is pegged to a weighted basket of 60% euro and 40% USD. The columns represent the change in exchange rate from June 8, 2018 to June 7, 2023.
Source: Bloomberg LP, 2023.

WHERE WE STAND TODAY

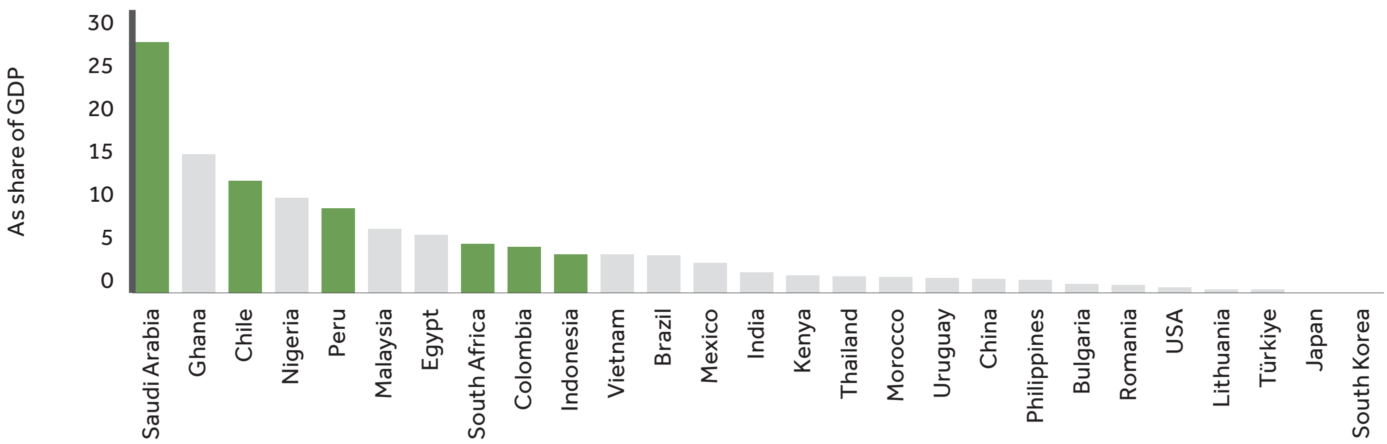
BULGARIA		• April 2023 inflation 11.6%, down from 18.7% in September 2022 • Interest rate 2.96%, up 296bps since January 2022 • GDP growth 3.4% in 2022 • Lev trading at 1.81 per USD, 2% stronger than a year ago • Negative real rates support activity
LITHUANIA		• April 2023 inflation 14.5%, down from 24.1% in September 2022 • ECB interest rate 3.75%, up 375bps since January 2022 • GDP growth 1.9% in 2022 • Euro trading at 0.93 per USD, 2% stronger than a year ago • Macroprudential policies, pro-business environment and openness to EU trade/risks
MOROCCO		• April 2023 inflation 7.8%, down from 10.1% in February 2023 • Interest rate 3%, up 150bps since January 2022 • GDP growth 1.1% in 2022, and accelerating this year • Dirham trading at 10.22 per USD, 2% weaker than a year ago • Flexible economy with currency tracking euro peg
ROMANIA		• April 2023 inflation 11.2%, down from 16.8% in November 2022 • Interest rate 7%, up 500bps since January 2022 • GDP growth 4.8% in 2022 • Leu trading at 4.62 per USD, flat compared to a year ago • Macro backdrop is improving as energy and headline inflation are easing. Activity holding up well, but twin deficits make it vulnerable to any rise in euro risk
URUGUAY		• April 2023 inflation 7.6%, down from 10.0% in September 2022 • Interest rate 11.25%, up 550bps since January 2022 • GDP growth 4.9% in 2022 • Uruguayan peso trading at 39.0 per USD, 6% stronger than a year ago • A track record of sound macroeconomic policies, with limited fiscal risks

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund World Economic Outlook database (April 2023) for real GDP growth figures in 2022 and 2023f. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

NATURAL RESOURCE WINNERS

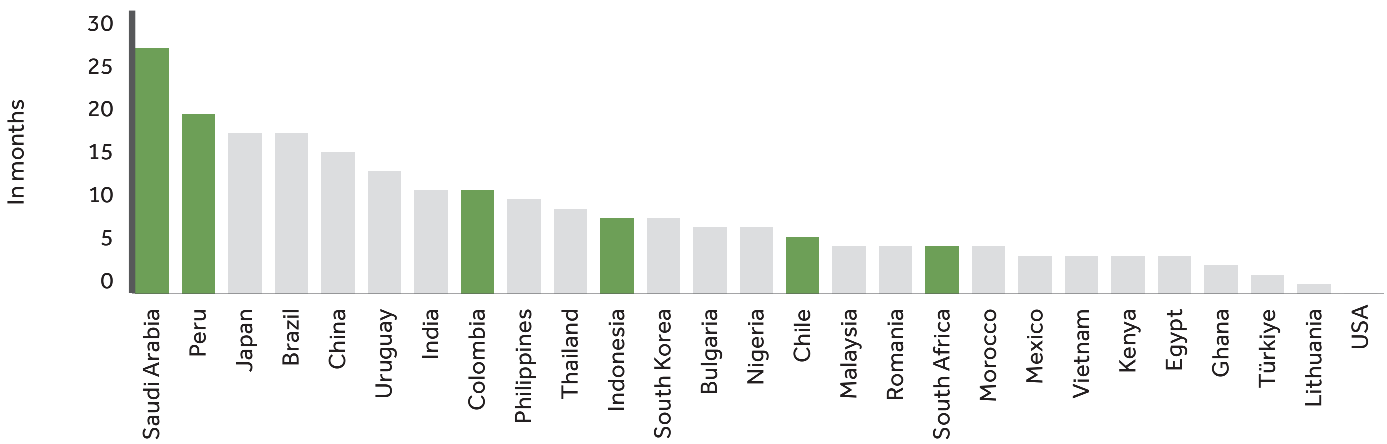
WHAT	• Major commodity exporters • High but variable FX reserve cover • Relatively undiversified economies • Young and fast-growing population
WHO	• Chile • Colombia • GCC • Indonesia • Peru • South Africa
CHARACTERISTICS	• Currencies higher volatility unless fixed exchange rate regimes • Higher GDP per capita • High but variable import cover ratios

RATIO OF TOTAL NATURAL RESOURCES RENTS TO GDP, 2018 OR LATEST

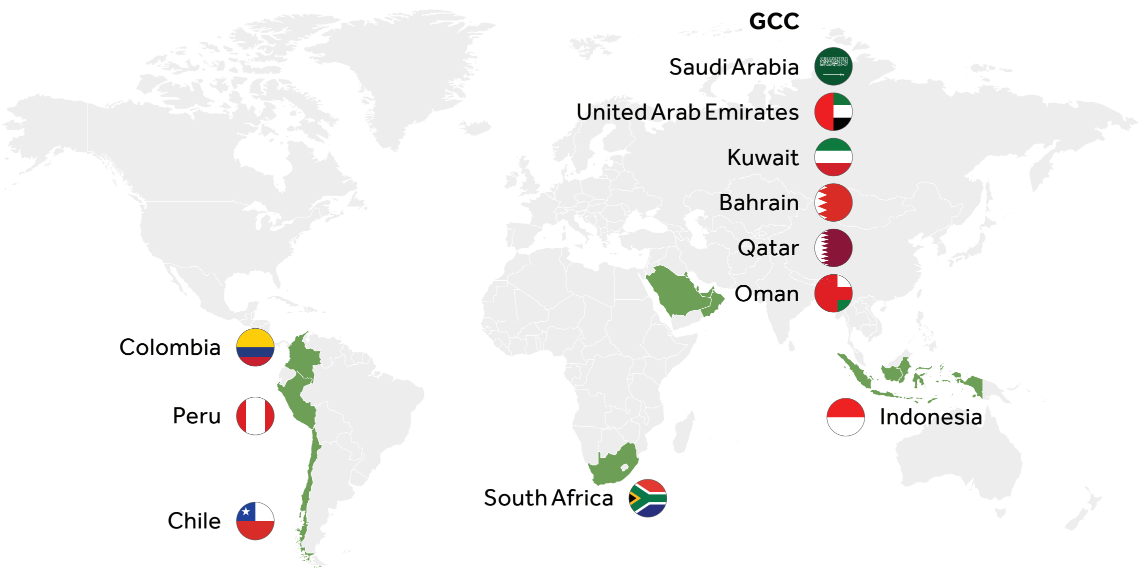


Note: The World Bank staff estimates of natural resources rents are calculated as the difference between the price of a commodity and the average cost of producing it. These rents are then multiplied by the physical quantities countries extract or harvest to determine the rents of each commodity as a share of GDP.
Source: State of Commodity Dependence 2021, by Alexandra Laurent/ Janvier Nkurunziza / Commodities Branch UNCTAD, ©(2021) United Nations. Used with the permission of the United Nations.

RATIO OF FOREIGN CURRENCY RESERVES TO IMPORTS (IN MONTHS), Q2 2023



Note: No data was available for UAE (peers in the GCC for whom data is available have substantial reserves and import cover). Data as of June 7, 2023.
Source: Bloomberg LP, 2023.



WHERE WE STAND TODAY

CHILE

- April 2023 inflation 9.9%, down from 14.1% in August 2022
- Interest rate 11.25%, up 725bps since January 2022
- GDP growth 2.4% in 2022
- Chilean peso trading at 793 per USD, 5% stronger than a year ago
- Despite higher economic volatility recently, long term copper and lithium outlook very benign

COLOMBIA

- April 2023 inflation 12.8%, down from 13.3% in March 2023
- Interest rate 13.25%, up 1,025bps since January 2022
- GDP growth 7.5% in 2022
- Colombian peso trading at 4,567 per USD, 12% weaker than a year ago
- The president's reform agenda is colliding with slower growth and efforts to bring down CPI

INDONESIA

- April 2023 inflation 4.3%, down from 6.0% in September 2022
- Interest rate 5.75%, up 225bps since January 2022
- GDP growth 5.3% in 2022
- Rupiah trading at 14,925 per USD, flat compared to a year ago
- Growth to stay solid as resilient domestic demand buffers receding commodity tailwind

PERU

- April 2023 inflation 8.0%, down from 8.6% in September 2022
- Interest rate 7.75%, up 525bps since January 2022
- GDP growth 2.7% in 2022
- Sol trading at 3.70 per USD, flat compared to a year ago
- Political instability a way of life but growth and currency performing well

SAUDI ARABIA

- April 2023 inflation 2.7%, down from 3.4% in January 2023
- Interest rate 5.75%, up 475bps since January 2022
- GDP growth 8.7% in 2022, an outperformer
- Riyal trading at 3.75 per USD, flat compared to a year ago (pegged)
- Fiscal position remains strong, liquidity plentiful and OPEC action supportive

SOUTH AFRICA

- March 2023 inflation 7.1%, down from 7.8% in July 2022
- Interest rate 8.25%, up 450bps since January 2022
- GDP growth 2.0% in 2022
- Rand trading at 19.4 per USD, 23% weaker than a year ago
- Despite inflation starting to soften, power shortages pose a material challenge to outlook

UAE

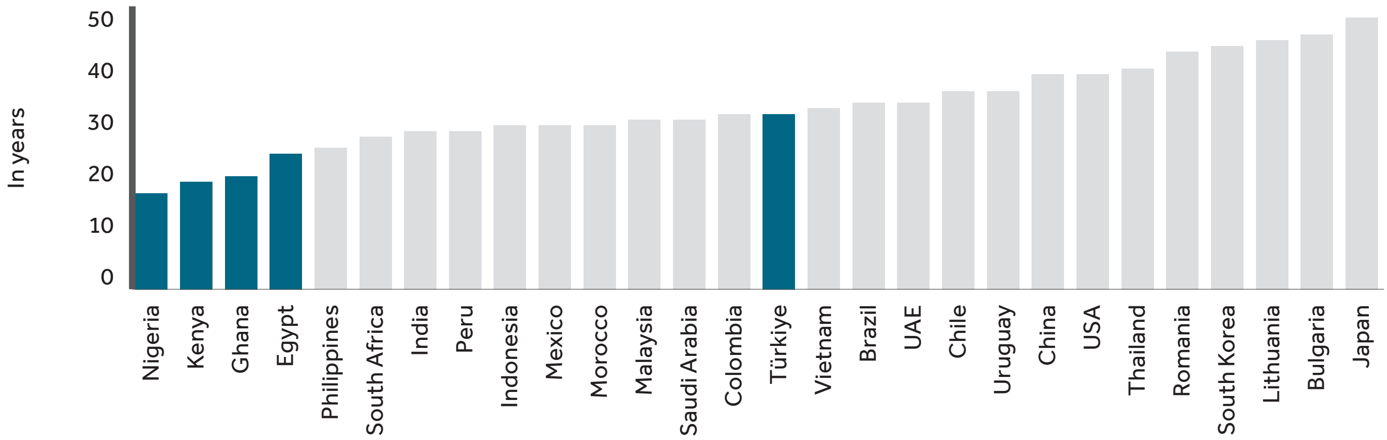
- April 2023 inflation 3.3%, down from 7.1% in July 2022 (Dubai)
- Interest rate 5.15%, up 365bps since January 2022
- GDP growth 7.4% in 2022, an outperformer
- Dirham trading at 3.67 per USD, flat compared to a year ago (pegged)
- Huge benefits from oil price and strong tourist inflows; economic activity going very well

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund World Economic Outlook database (April 2023) for real GDP growth figures in 2022. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

STRUCTURALLY CHALLENGED

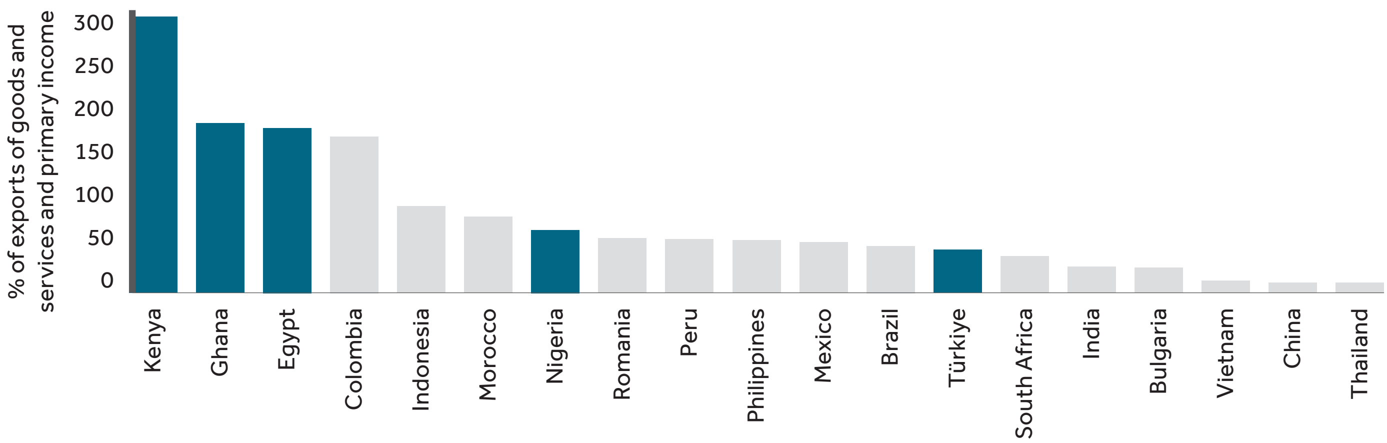
WHAT	• Heavily indebted countries with limited debt service capabilities • Small financial systems (excl. Türkiye) • Young fast-growing population
WHO	• Egypt • Ghana • Kenya • Nigeria • Türkiye
CHARACTERISTICS	• High nominal debt costs • Negative real rates • Higher inflation • Domestic currency distrusted as store of value • Low import cover • Low transparency / rule of law • Misery Index high

MEDIAN AGE, 2021



Source: World Population Prospects 2022, Department of Economic and Social Affairs Population Division, United Nations © (2022). Used with permission of the United Nations.

RATIO OF EXTERNAL DEBT TO EXPORTS AND PRIMARY INCOME, 2021



Note: This metric measures the present value of external debt as share of exports of goods, services and primary income, according to officially recognised international sources compiled by The World Bank. Data was not available for Chile, Japan, Lithuania, Malaysia, Saudi Arabia, South Korea, UAE, Uruguay and USA.
Source: The World Bank, International Debt Statistics database, 2023.

WHERE WE STAND TODAY

EGYPT		• April 2023 inflation 30.6%, down from 32.7% in March 2023 • Interest rate 18.25%, up 1,000bps since January 2022 • GDP growth 6.6% in 2022, a relative outperformer • Egyptian pound trading at 30.9 per USD, 68% weaker than a year ago • In the middle of a structural adjustment programme with IMF. Still needs to show credible commitment to reform and FX flexibility
GHANA		• April 2023 inflation 41.2%, down from 54.1% in December 2022 • Interest rate 29.5%, up 1,500bps since January 2022 • GDP growth 3.2% in 2022 • Cedi trading at 10.7 per USD, 38% weaker than a year ago • Effectively defaulted on debt with IMF negotiations ongoing. Elevated government and external debt ratios
KENYA		• April 2023 inflation 7.9%, down from 9.6% in October 2022 • Interest rate 9.5%, up 250bps since January 2022 • GDP growth 5.4% in 2022 • Shilling trading at 137.6 per USD, 18% weaker than a year ago • Domestic funding challenges remain material but relationship with multilateral agencies constructive
NIGERIA		• April 2023 inflation 22.2% and yet to peak this cycle • Interest rate 18.5%, up 700bps since January 2022 • GDP growth 3.3% in 2022 • Naira official trading at 462.5, 11% weaker than a year ago • Record rates and inflation levels but little relief in sight. Productive capacity is constrained and oil price decline could spell more trouble
TÜRKIYE		• April 2023 inflation 43.7%, down from 85.5% in October 2022 • Interest rate 8.5%, down 550bps since January 2022 • GDP growth 5.6% in 2022 • Lira trading at 19.6, 28% weaker than a year ago • After Erdogan's victory the strategy of promoting nominal GDP is likely to continue; further devaluation and domestic currency banking system risks remain material

Source: Bloomberg LP for consumer prices, interest rates and exchange rates. International Monetary Fund World Economic Outlook database (April 2023) for real GDP growth figures in 2022. Exchange rates as of May 22, 2023 and interest rates as of June 7, 2023.

SECTION 2: PROVING THE CASE

We now explore these key metrics. We show the different fundamental market, macro and political risk characteristics using the above taxonomy. This allows us to map out our exposure to different types of risk and investment opportunity on a global basis.

We focus on market, macro, currency and governance risks. We decided to calculate simple unweighted averages for our metrics across the buckets.

We test our categories using the same set of country nominations as highlighted before. The resulting country universe is summarised in six buckets.

WHAT MATTERS?

1. Size Matters

A large economy, population or growth rates say nothing about investment returns. But market size parameters are useful to give a rough indication of investment opportunity.

'Global Influencers' and 'Big Middles' clearly stand out (see Exhibit 2). As expected, 'Stable but Small' and 'Structurally Challenged' groups have smaller economies on average. However, the picture alters somewhat once we drill down into GDP per capita; here 'Global Influencers', 'Stable but Small' and 'Natural Resource Winners' stand out, followed by 'Big Middles'.

"A FAMILIAR MANTRA TO LONG HORIZON, CROSS BORDER INVESTORS ASSESSING CURRENCY RISK. UNDERSTANDING DRIVERS HERE MATTERS A LOT. THIS APPLIES IN OUR BUCKETS REGARDLESS OF WHETHER A CURRENCY IS FIXED OR FLOATING – THEY ALL REFLECT CAPITAL FLOW VOLATILITIES THROUGH LIQUIDITY, BANKING, AND FISCAL DYNAMICS."

2. Population Matters

In terms of demographics, 'Global Influencers' and 'Big Middles' are a class of their own. As the name indicates, our 'Stable but Small' bucket is clearly the least sizeable group. In terms of median age and population growth prospects, the picture is more nuanced. Here we have the emergence of 'Structurally Challenged', 'Natural Resource Winners' and 'Supply Chain Heroes' as the buckets with rapidly growing populations.

3. Trade Matters

Highlighting share of global exports shows whether countries are likely to be price takers or givers. 'Global Influencers' stand out on this metric as price givers and therefore less risky versus the rest.

4. Financial Resilience (really) Matters

Financial depth – think of this as shock absorption which should vary with per capita income. Deep domestic savings and natural incentives to hold assets onshore smooth volatility created by offshore investors selling local assets. Pension funds in Latin America and East Asia, sovereign wealth funds in MENA and insurance companies in South Africa all have local currency liabilities. As such, they are net buyers of local currency assets and so smooth economic and financial system volatility. A build-up in credit to GDP is frequently a precursor to financial crisis through reversal of funding. Battle scarred veterans such as one of your authors recall the 1980's and 1990's and think this factor is materially underappreciated. **The nature of funding really matters.**

Analysing assets of non-bank financial institutions to GDP shows that 'Global Influencers', 'Big Middles' and 'Natural Resource Winners' (including South Africa) have the deepest financial systems measured as the total assets of pensions funds, mutual funds and insurance companies as share of GDP.

THE SIX BUCKETS

Global Influencers
- China
- Japan
- USA

Big Middles
- Brazil
- India
- Mexico
- South Korea

Supply Chain Heroes
- Malaysia
- Philippines
- Thailand
- Vietnam

Stable but Small
- Bulgaria
- Lithuania
- Morocco
- Romania
- Uruguay

Natural Resource Winners
- Chile
- Colombia
- GCC
- Indonesia
- Peru
- South Africa

Structurally Challenged
- Egypt
- Ghana
- Kenya
- Nigeria
- Türkiye

Source: Actis

5. Remittances Matter

Amongst the 'Structurally Challenged', 'Supply Chain Heroes' and 'Stable but Small', remittances act as an important source of additional flows, compensating for a limited domestic savings pool. They tend to be countercyclical and consistent, moving up during domestic downturns at a time when private capital tends to flee.

6. Foreign Direct Investment Matters

Foreign Direct Investment (FDI) brings in stable capital from abroad, increasing the overall investment and funding available within the country. FDI has many advantages. Long-term capital commitments are more stable and hence sustainable than short-term portfolio flows ('hot money'). The latter leaves economies vulnerable to shifting investor sentiment and sudden outflows: Egypt is right now learning the hard way. FDI flows are also associated with technology transfer and increased export earnings.

Data shows 'Supply Chain Heroes' are clearly also FDI Heroes. In terms of annual FDI inflows as share of GDP, 'Supply Chain Heroes' rank as the highest, with Vietnam leading the pack across all our economies covered (5.5% of GDP). This makes sense, as FDI typically stimulates trade activities by integrating the host country into global supply chains. Foreign investors often establish export-oriented industries. Other prominent performers on this metric include 'Natural Resource Winners' (where FDI is linked to commodity cycles, hence more volatile) and 'Stable but Small'. For the rest, FDI represents a smaller share of GDP.

EXHIBIT 2: KEY MARKET DESCRIPTIVES

Metric	Global Influencers	Big Middles	Supply Chain Heroes	Stable but Small	Natural Resource Winners	Structurally Challenged
Average GDP *(US$bn, 2023f)*	16,879	2,301	478	149	616	422
GDP per capita *(US$, 2023f)*	43,047	14,585	7,486	17,556	17,389	4,430
Average population *(mn, 2023f)*	624	459	79	14	70	100
Median age *(in years, 2021)*	41	33	31	39	30	22
Share of world exports *(%, 2022)*	8.6	2.1	1.1	0.2	0.9	0.3
Assets of pension funds, mutual funds and insurance companies *(% of GDP, 2018 or latest)*	190	84	66	22	74	11
Migrant remittance inflows *(% of GDP, 2022)*	0.1	2.0	4.1	2.8	0.9	4.2
Inward FDI flows *(% of GDP, 2021)*	1.0	2.0	3.4	2.5	2.8	1.5
Human Capital Index *(scale 0-100, higher=better, 2020)*	72	61	61	60	58	50

Note: All figures in this and subsequent tables are simple unweighted averages of individual country figures in each group. For example, the share of world exports for 'Global Influencers' equals China (14.4%) + USA (8.3%) + Japan (3%) / 3 = 8.6%.
Source: International Monetary Fund, World Economic Outlook (April 2023) for GDP size and GDP per capita. World Population Prospects 2022, Department of Economic and Social Affairs Population Division, United Nations, © (2022) for demographics data. Used with permission of the United Nations; UNCTADstat for world exports share and FDI flows; The World Bank Global Financial Development Database for non-bank financial assets; The World Bank KNOMAD (November 2022) for migrant remittances; The World Bank Human Capital Project for Human Capital Index, June 2023.

"TRADITIONAL RESEARCH FOCUSES ON MACROECONOMIC VARIABLES INCLUDING INFLATION, INTEREST RATES AND FISCAL TRENDS. WHILST WE ACKNOWLEDGE THE IMPORTANCE OF THESE VARIABLES, THEY SEEM OFTEN TO US TO BE SYMPTOMS RATHER THAN CAUSES OF INVESTMENT RISK."

7. Institutional Maturity Matters

Mature institutions reduce uncertainty and foster economic stability by minimising the risks associated with volatile policy changes or political interference. Institutional maturity and operational independence of economic institutions helps untie investment cycles from electoral ones. This should lead to more rational policymaking.

Here the 'Big Middles' and 'Supply Chain Heroes' stand out in terms of improvements. In both groups current account deficits, share of debt denominated in foreign currency and non-resident holdings of government debt are lower than a decade ago. Their central banks have become credible and independent. Countries, such as Brazil and Mexico, have been hiking prudently this cycle and getting ahead of the curve. Their economies have the largest ever FX reserves and no longer the type of currency mismatch or pegged exchange rates that have amplified past crisis (e.g. Asian Financial Crisis of 1997-98). Amongst both groups it has supported the reduction in currency volatility in the past decade and FX outperformance versus DM majors in the last years. The spread of volatility between the US dollar and 'Big Middles' currencies has dropped significantly in recent years (see Exhibit 3). Notably, the 'Big Middles' currencies have been less sensitive to extreme market events now than previously (see Exhibit 4).

To put these achievements in perspective: in the early-1990s hyperinflation plagued Brazil whilst the Bank of Thailand was a serious contender for the worst run central bank in the world (Bank Indonesia won that particular prize).

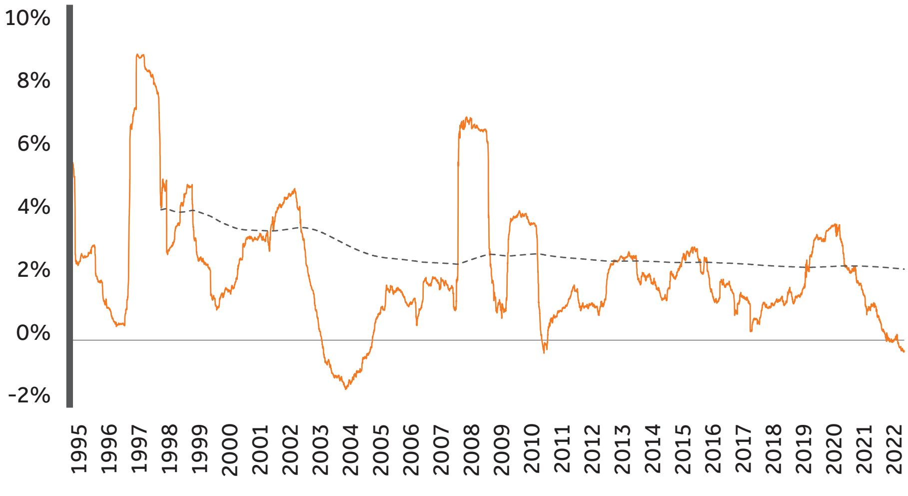
"UNDERSTANDING AND DIFFERENTIATING THE RISKS BEING TAKEN AND PRICING THEREOF IS VITAL."

8. Human Capital Matters

The intuitive linkage between financial depth, educational attainment and productivity can be complex. **We show that financial development is lowest for the 'Structurally Challenged' bucket, which is also characterised by lower levels of human capital development.**

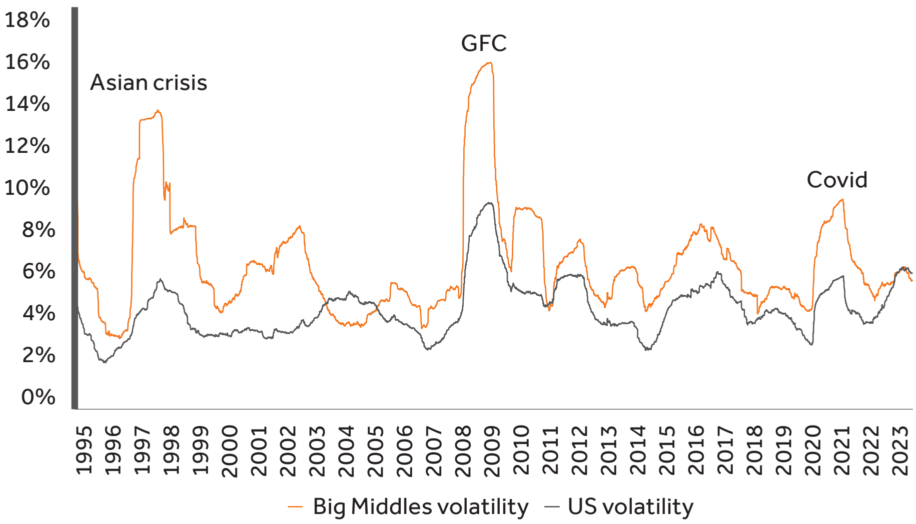
Looking at The World Bank's Human Capital Index, which measures expected years of school, harmonised test scores and basic health, 'Global Influencers' perform the best, followed evenly by all other groups except 'Structurally Challenged'. The relatively solid and even human capital picture across most of our investment universe is encouraging (although it masks some within group differences). It is one foundation of future economic sophistication and productivity growth.

EXHIBIT 3: BIG MIDDLES BECOMING LESS VOLATILE



Note: Spread between 'Big Middles' NEER rolling 1-year volatility and US NEER rolling 1-year volatility. 'Big Middles' NEER represents the unweighted average of Brazil, India, Mexico and South Korea. Nominal Effective Exchange Rate (NEER) represents the value of a country's currency relative to its trading partners' weighted basket of currencies (rather than just one bilateral exchange rate). Average measures expanding window average. Data as of June 7, 2023.
Source: Cross Border Capital, June 2023.

EXHIBIT 4: SURVIVING CRISES



Note: Rolling 1-year annualised volatility in nominal effective exchange rate (NEER). 'Big Middles' NEER represents the unweighted average of Brazil, India, Mexico and South Korea. NEER represents the value of a country's currency relative to its trading partners' weighted basket of currencies (rather than just one bilateral exchange rate). Data as of June 7, 2023.
Source: Cross Border Capital, June 2023.

CURRENCY IS CRUCIAL

A familiar mantra to long horizon, cross border investors assessing currency risk. Understanding drivers here matters a lot. This applies in our buckets regardless of whether a currency is fixed or floating – they all reflect capital flow volatilities through liquidity, banking, and fiscal dynamics.

Currency risk matters both as a cause and symptom of diverse investment outcomes. Hence, it is important to understand and, whenever possible, diversify exposure to different currency drivers across our portfolio.

Our FX partner CBC analysed currency drivers across our buckets. CBC's approach identifies through quantitative analysis a subset of currency drivers that impact each currency. They focus on a 2-year forward horizon as back testing shows that events rather than inflation differentials have a higher explanatory function at short horizon. We assume, as they do beyond two years, that PPP differentials take over given that events become less forecastable at longer horizons. All Actis deals, including exits, use this framework now. The key take-aways:

Global Influencers

Domestic monetary policy accounts for almost half of the variation in this subset (see Exhibit 5). Interest rate decisions, open market operations, liquidity management, Yield Curve Control (YCC) and exchange rate mechanisms drive most event-driven volatility in this bucket's currencies. Crises tend to be endogenous not exogenous – these are risk givers not takers. Domestic economic activity particularly affects the USD and CNY.

EXHIBIT 5: WHAT DRIVES CURRENCIES

Currency Drivers (in %)	Global Influencers	Big Middles	Supply Chain Heroes	Stable but Small	Natural Resource Winners	Structurally Challenged
Capital Flows	15.3					
Domestic Economic Activity	19.1	7.3				
Trade Balance	18.4	17.9	13.9	26.5	15.3	23.0
Monetary Policy	40.6	9.5	12.9	13.8	13.1	
Inflation	6.5					
Agricultural Prices			17.5			
Precious Metal Prices		7.4	10.4		11.1	4.2
Industrial Metal Prices		12.0	10.4		13.9	9.2
Energy Prices		18.7	9.4		25.3	14.9
FDI		6.3	21.2	35.5		
US Activity		16.3	4.5	18.1	14.7	6.7
Global Sentiment		4.6		6.1	6.7	8.9
FX Reserves						23.8
Remittances						9.2

Note: Percent figures represent the share of variation in the subset's indexed currency explained by a given factor.
Source: Cross Border Capital, June 2023.

Big Middles

Trade balance, energy prices and US activity dominate, accounting for close to 20% of the currency variation each. But some nuances caveat this general conclusion. Some 'Big Middle' countries are large energy importers, making them sensitive to shocks in energy prices (India). Industrial metal prices have a greater impact on the currencies of Brazil and South Korea due to their reliance on manufacturing. Currencies across this bucket, in particular the Mexican peso, are sensitive to US economic activity as the US is a key trade partner for these countries. India's rupee is, relatively speaking, more sensitive to global risk sentiment.

Natural Resource Winners

This group is highly sensitive to commodity prices, with energy and metals prices driving half of the currency movements. This sensitivity is no surprise given the significance of oil, gold, platinum, and copper to these economies. The South African rand has a significant beta (33%) to major precious metal prices. Energy prices drive 41% of GCC currency sensitivities. Middle Eastern currencies are mostly dollar-linked so volatility comes through fiscal, credit and inflation variables rather than FX values. US economic activity and industrial metal prices heavily influence the Chilean peso and Peruvian sol, but also the Colombian peso. The Indonesian rupiah is more sensitive to energy prices (32%).

One aside – energy transition has the long-term potential to create winners and losers in this area. Think declining fossil fuel demand and rising renewables driven industrial materials demand. This is probably a while away but worth flagging.


▼ 4.62%
▼ 4.62%
▲ 9.12%
▲ 3.45%
▲ 3.45%
▲ 9.12%

Supply Chain Heroes

Important drivers for this bucket are foreign direct investment, agricultural prices and trade balances. 'Supply Chain Heroes' currencies are primarily driven by foreign direct investment (21%), which has become increasingly important in recent years. Vietnam is a case in point. Benefiting from the relocation of manufacturing bases from China, FDI inflows are a key driver of the currency 'explaining' over 30% of movements in the dong. FDI is also a key driver of the Thai baht. Relatedly, these currencies are also reliant on export and import performance, with trade balances accounting for 14% of the bucket's drivers. Trade balances are the primary driver of Philippine peso. The economies that rely more on agricultural exports like palm oil, rubber, and rice (Malaysia, less so Vietnam) are also sensitive to agricultural prices.

"WE SHOW THE DIFFERENT FUNDAMENTAL MARKET, MACRO AND POLITICAL RISK CHARACTERISTICS USING THE ABOVE TAXONOMY. THIS ALLOWS US TO MAP OUT OUR EXPOSURE TO DIFFERENT TYPES OF RISK AND INVESTMENT OPPORTUNITY ON A GLOBAL BASIS."

EXHIBIT 6: CURRENCY METRICS

Metric	Global Influencers	Big Middles	Supply Chain Heroes	Stable but Small	Natural Resource Winners	Structurally Challenged
FX rate change against USD *(%, last 5 years to date, official rate)*	-9	-15	-8	-13	-20	-139
FX realised volatility *(%, last 5 years to date, annual average realised vol)*	6	10	4	7	11	10

Note: In the calculation of average currency volatility for Natural Resource Winners, the currencies of UAE and Saudi Arabia were excluded as they are pegged. All exchange rates are against the USD; except for the United States, which is against DXY. Minus sign means depreciation against USD. Average annual FX realised volatility is measured against USD. Data as of June 7, 2023.
Source: Bloomberg LP for exchange rates; PMC Treasury for realised volatility, June, 2023.

Stable but Small

The currencies in this bucket are sensitive to the economic activity, monetary policy and flows of 'Global Influencers' (assuming EU taken together is also one). Lithuanian, Romanian and Bulgarian economies are influenced by their close economic ties to the EU. Foreign direct investment and trade balances, for which the EU plays a significant role, contribute to 62% of the bucket's drivers and EU monetary policy a further 14%. Export and import measures contribute 30%, 35% and 34% to the overall variation in the Moroccan dirham, Romanian leu and Uruguayan peso, respectively. Uruguayan peso is more sensitive to the US economic activity (27%).

Structurally Challenged

This bucket is particularly sensitive to FX reserves (24%) and trade balances (23%), and to a lesser extent energy prices and remittances. The currencies in this bucket heavily rely on export and import performance and maintaining sufficient FX reserves to meet external obligations, as large shifts in reserves can lead to significant currency fluctuations. Türkiye is a case in point. FX reserves 'explain' almost third of lira's moves, followed by energy prices and trade balance. FX reserves and trade balances also account for 40% of the variation in the Kenyan shilling. Unlike other buckets, remittances play a significant role in this subset. Remittances are particularly meaningful drivers of the Egyptian pound (19%) and Ghanaian cedi (20%). Energy prices also have a material impact on the Nigerian Naira and Ghanaian cedi due to their reliance on oil exports.

One stress factor is when citizens distrust their own currency as a store of value. Gresham's Law whereby bad money (local currency) is spent quickly, and foreign exchange is hoarded as a source of value applies. And offshore investors demand an unsustainable premium for substituting for local interest.

Currency risk is manifested in both currency levels and volatility. This goes partly back to the currency drivers' analysis above, as some drivers tend to be more volatile than others. For example, economies more exposed to commodity price swings also tend to have, on average, more volatile currencies, unless their currencies are credibly pegged with solid FX reserves (e.g. UAE, Saudi Arabia) (see Exhibit 6).

Lower currency volatility implies lower investment risk, all else being equal. A country with low or improving FX volatility not associated with capital controls, is attractive for new investment flows. Why? If FX volatility is low, the chances of domestic cash flows accruing at a faster rate than the currency depreciates boosts hard currency returns. (It tends to mean lower inflation volatility as well).

Average FX volatility has come down across most of our investment universe over the past 15 years or so. This finding applies in particular to 'Supply Chain Heroes', 'Stable but Small' and 'Big Middles' groups. Some star performers are highlighted in Exhibit 7.

Despite the recent crisis and dollar strength, currency volatility is lower across these buckets than in the previous decade (which also covers the GFC shock). The ability of currencies to weather external shocks, manifested as historically low FX volatility, is an obvious harbinger of reduced risk.

By contrast artificially induced low volatility (sometimes associated with administrative actions) is a red flag.

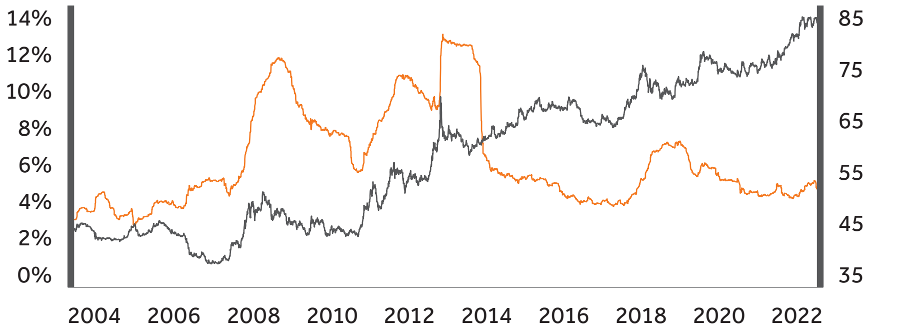
Some country differences are worth mentioning. It is justified to look at group averages when mean and median converge. Hence with the 'Big Middles', whilst the realised currency volatility has substantially declined over the past decade, and has halved in India and South Korea, Brazil and Mexico have seen more volatile outcomes. This results in a somewhat less impressive group level average for the 'Big Middles'.

Understanding currency drivers helps make better long term investment decisions. Drivers do differ between countries – see the heatmap – which further supports our distaste for homogeneous judgements.

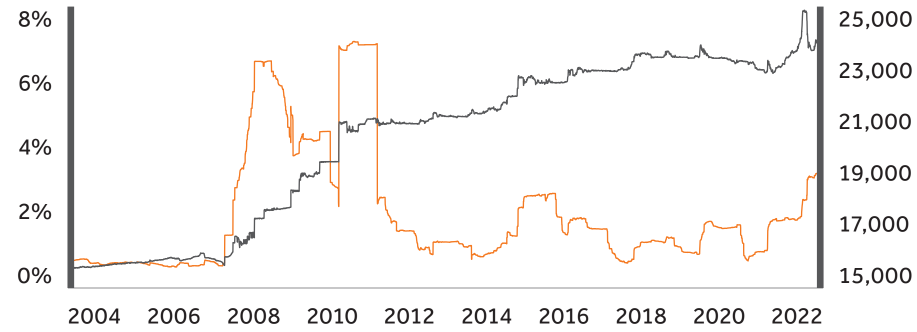
Currency drivers are central to debate at Actis. We are often able to mitigate it through tariff or revenue indexation to the dollar. In some jurisdictions local finance is freely available which reduces the need to worry about asset liability mismatch. In the event of known flows, we can manage short term risk through financing and hedging strategies.

EXHIBIT 7: TRACKING VOLATILITY LOWER

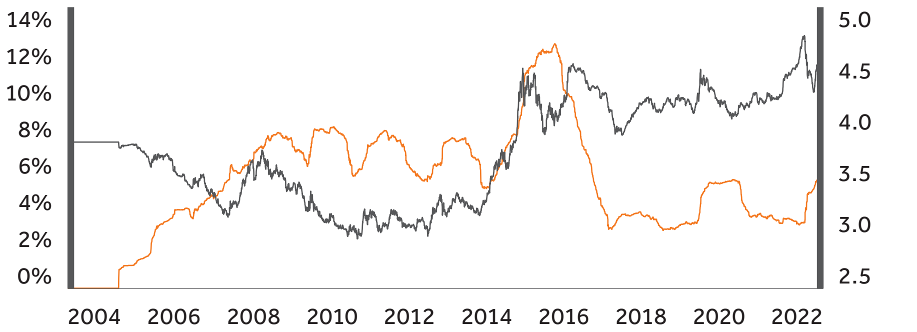
India annual realised volatility and spot exchange rate



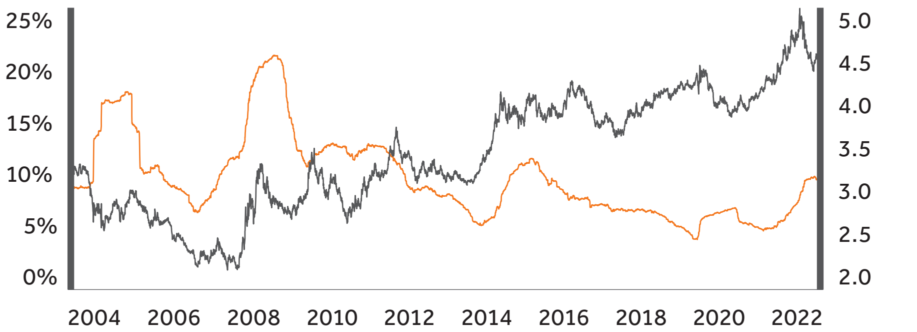
Vietnam annual realised volatility and spot exchange rate



Malaysia annual realised volatility and spot exchange rate



Romania annual realised volatility and spot exchange rate



— Annual volatility (left axis) — Spot versus USD

Source: PMC Treasury, June 2023.

MACROECONOMIC FUNDAMENTALS

Traditional research focuses on macroeconomic variables including inflation, interest rates and fiscal trends. Whilst we acknowledge the importance of these variables, they seem often to us to be symptoms rather than causes of investment risk (see Exhibit 8).

An appropriate interest rate is important for balancing investment, consumption, and inflation in an economy. Negative real or low nominal rates can incentivise borrowing and discourage savings, as money is being lost on investments in real terms.

Stubbornly high inflation and deeply negative real rates remain, above all, a challenge amongst 'Structurally Challenged' and 'Stable but Small' (largely EM Europe) countries. Even so, as we go to print, headline inflation appears to have peaked. The IMF forecasts inflation will decline amongst 'Stable but Small' economies over the next two years, but inflation will remain above target amongst most 'Structurally Challenged' economies. Across other buckets, CPI pressures have already been softening, albeit slowly.

"OUR LP COMMUNITY ASKS US TO DIFFERENTIATE BETWEEN COUNTRIES IN A CONSISTENT FASHION AND BE ABLE TO EXPLAIN DECISIONS AND OUTCOMES USING MEANINGFUL FRAMEWORKS. SOME ARE ALSO SEEKING CATEGORISATIONS TO SHAPE THEIR OWN STRATEGIC AND TACTICAL DECISION MAKING. HENCE, WE PRESENT HERE OUR NEW TAXONOMY OF GLOBAL INVESTING."

EXHIBIT 8: THE MACROECONOMIC FUNDAMENTALS

Metric	Global Influencers	Big Middles	Supply Chain Heroes	Stable but Small	Natural Resource Winners	Structurally Challenged
Real interest rate *(%, latest)*	0	4	1	-5	1	-11
Inflation *(yoy %, last reported)*	3	5	3	10	7	28
Real GDP growth *(%, 2023f-2028f, average annual growth rate)*	2	3	5	3	3	4
Government revenue as % of GDP *(2021)*	31	25	20	30	25	16
Government debt (gross) as % of GDP *(2022)*	153	70	55	48	43	63
External debt as % of exports *(2021)*	11	44	26	55	88	152
Total reserves *(in months of import, Q2 2023)*	11	10	7	6	13	4
NIIP as % of GDP *(2022)*	8	-12	1	-28	0	-35

Note: 'External debt as % of exports' measures the present value of external debt as share of exports of goods, services and primary income, according to officially recognised international sources compiled by the The World Bank. Data was not available for Chile, Japan, Lithuania, Malaysia, Saudi Arabia, South Korea, UAE, Uruguay and USA. NIIP refers to Net International Investment Position. Data as of June 7, 2023.
Source: Bloomberg LP for interest rates, inflation and import cover; International Monetary Fund World Economic Outlook (April 2023) for GDP forecast; International Monetary Fund Government Finance Statistics for government revenue; International Monetary Fund Fiscal Monitor (April 2023) for government debt; International Monetary Fund BOP/IIP Statistics for NIIP (ratio calculated using nominal GDP in 2022); The World Bank International Debt Statistics for external debt, June 2023.

Real rates, on average, are highest in the 'Big Middles'. This implies room for stimulating activity should the need arise. It also suggests that these economic systems are robust enough to absorb orthodox policies and, in some cases, get ahead of the curve. This is a virtue not a vice.

In terms of the real GDP growth outlook across the next half decade, the most impressive country bucket is 'Supply Chain Heroes'. The IMF GDP forecast is aligned with this bucket's recent track-record – think Vietnam and other ASEAN countries' remarkable past decade. Buckets other than 'Supply Chain Heroes' will grow at a relatively similar rate; 'Global Influencers' economic growth will be slower.

General government revenues to GDP – especially tax take to GDP – reveal why some countries are structurally more vulnerable to shocks than others. Here, the 'Global Influencers' and 'Stable but Small' countries stand out, whilst 'Structurally Challenged' have lowest government revenues – and tax intake – relative to GDP. Government debt to GDP ratio is problematic in the latter group (excl. Türkiye), implying limited fiscal scope and possible debt distress scenarios if either global or domestic conditions worsen.

A key solvency ratio is external debt to exports. It is useful as a trend measure indicating the repayment capacity of an economy. Data limitations apply but calculating bucket averages for the economies where data is available yields a very clear-cut result: 'Structurally Challenged 'economies are, on average, three times worse off than any other bucket. In fact, this indicator is flashing red in regard to solvency concerns across this group. These fears have proven warranted in the case of Ghana, which earlier this year effectively missed coupon payments on its Eurobond.

Another important macro stability benchmark is the import coverage ratio. It measures the number of months that a country's foreign currency reserves could cover its total import bill. Too low import cover implies vulnerability to external shocks, such as a sudden rise in commodity prices or economic slowdown. This metric shows how 'Natural Resource Winners' are currently sitting on a fiscal bonanza; whilst at the opposite extreme are the 'Structurally Challenged' economies. 'Global Influencers' (including China) and the 'Big Middles' occupy the second and third most favourable spots.

In the case of the 'Big Middles', there has been a clear trend towards more sound policymaking, central bank independence and FX reserve building in the past decade.

The net international investment position (NIIP) is the difference between a country's stock of foreign assets and a foreigner's stock of that country's assets; a material negative NIIP suggests more vulnerability to developments in the global financial markets.

On this metric, 'Global Influencers', 'Supply Chain Heroes' and 'Natural Resource Winners' are the best positioned. The former group is driven by Japan which runs the biggest total net creditor position in the world in US dollar terms (and one of the largest as a share of GDP). The latter is driven by the GCC economies, but South Africa also performs well. 'Big Middles' (including South Korea with a material positive NIIP) are in the middle of the spectrum. 'Stable but Small' and 'Structurally Challenged' are the worst positioned. All economies in the latter two groups are debtor nations vis-à-vis the rest of the world.

GOVERNANCE AND POLITICAL STABILITY

Political risk appears in varying guises including corruption, rule of law, ease of doing business or political instability.

For long horizon investors, rule of law is critical. A predictable and reliable legal system fosters and protects investments. Think property rights or contract enforceability. A reliable and transparent legal system and equal application of law tend to reduce corruption.

There is a plethora of indices measuring these variables (see Exhibit 9). These cover rule of law, corruption, political stability, ease of doing business and misery. The last, devised by economist Arthur Okun, combines inflation and unemployment and can posit social unrest risk levels.

In general, 'Global Influencers' score positively in these areas; 'Stable but Small' show well, reflecting their European heritage. 'Structurally Challenged' score worst of all.

The Misery index seems most indicative. It is currently the highest amongst the 'Structurally Challenged' countries, followed by 'Stable but Small' and 'Natural Resource Winners'. This is also perhaps why street protests – so far mostly peaceful – have been the most prominent in EM Europe ('Stable but Small'), Latin America ('Natural Resource Winners') and Africa ('Structurally Challenged').

'Supply Chain Heroes', 'Global Influencers' and 'Big Middles' stand out as having relatively low levels of "Misery". In fact, 'Big Middles' and 'Supply Chain Heroes' have seen material improvements in this metric since post GFC.

EXHIBIT 9: GOVERNANCE AND POLITICAL STABILITY

Metric	Global Influencers	Big Middles	Supply Chain Heroes	Stable but Small	Natural Resource Winners	Structurally Challenged
Corruption Perceptions Index *(rank out of 180, 2022)*	36	84	89	55	69	115
Rule of Law Index *(rank out of 192, 2021)*	41	93	93	66	83	115
Political Stability and Absence of Violence/Terrorism Index *(rank out of 194, 2021)*	84	120	122	68	124	155
Ease of Doing Business *(rank out of 190, 2019)*	22	63	50	56	62	90
Misery Index *(inflation + unemployment, latest)*	7	10	6	19	18	40

Note: Misery Index is calculated as last reported inflation rate + latest unemployment rate (in ppts). Rule of Law and Political Stability rankings are based on The World Bank's Worldwide Governance Indicators which is a research dataset summarising the views gathered from several survey institutes, think tanks, NGOs, international organisations and private sector firms. This dataset covers microstates affecting overall rankings. Data as of June 7, 2023.
Source: Transparency International Corruption Perceptions Index 2022 for corruption;
The World Bank Worldwide Governance Indicators 2022 for rule of law and political stability;
The World Bank Ease of Doing Business 2020 (latest available, discontinued since) for regulatory burden; Bloomberg LP for inflation and unemployment, June 2023.

MARKET PERCEIVED COUNTRY RISK

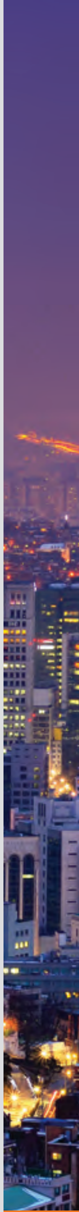
A higher yield on sovereign debt generally indicates that investors perceive greater risk associated in that country. This could be due to concerns about ability or willingness to repay debt or uncertainties regarding the economic or political situation in the country.

Unsurprisingly, markets see the highest risk in 'Structurally Challenged' and lowest for the 'Global Influencers' group. The rest sit somewhere in the middle, although 'Stable but Small' are in the less risky end of this middle spectrum. 'Natural Resource Winners' are on the riskier side of this mid-range, although this is partially driven by the current high perceived riskiness of South Africa.

Market perceptions can change rapidly in response to new information or events, making it more helpful to look metrics over a longer horizon. The 5-year average figures reveal similar bucket differences – barring 'Stable but Small' that emerge more clearly as having lower market perceived risk levels (after 'Global Influencers' and ahead of 'Supply Chain Heroes'). This makes sense, given the recent energy shock from the Russia-Ukraine war has hit EM Europe particularly hard, who make up the bulk of our 'Stable but Small' bucket.

We have chosen not to focus on variables such as credit ratings or CDS spreads. The former are reactive, the latter heavily influenced by illiquidity.

"ANALYSING ASSETS OF NON-BANK FINANCIAL INSTITUTIONS TO GDP SHOWS THAT 'GLOBAL INFLUENCERS', 'NATURAL RESOURCE WINNERS' AND 'BIG MIDDLES' HAVE THE DEEPEST FINANCIAL SYSTEMS MEASURED AS THE TOTAL ASSETS OF PENSIONS FUNDS, MUTUAL FUNDS AND INSURANCE COMPANIES AS SHARE OF GDP."



SECTION 3:
SO WHAT?

PULLING IT ALL TOGETHER

Categorising the world this way gets beyond the perception that all Emerging Markets are the same. Investors do differentiate between developed markets – think of the perennial comparisons between the US and Europe as an example or indeed Northern vs Southern Europe. Why not do so for EM?

Our proposals are one of the 'arrows' in a risk assessment 'quiver'. They do not of course necessarily tell you which the best places are to invest or deals in which to invest – the variables we have employed are easily observable and therefore discountable. In any case with long investment horizons, we expect some turbulence en route. Capital tends to flow to locations where risk is perceived to be lowest or declining and with compelling risk adjusted returns. Such flow can dilute potential returns through excessive competition for assets. But understanding and differentiating the risks being taken and pricing thereof is vital. That above all is the point of this exercise.

THE TEN CONCLUSIONS

1. 'GLOBAL INFLUENCERS' will continue to drive risks, rather than be dictated to.
2. 'BIG MIDDLES' are natural destinations provided inappropriate policy does not dilute investment opportunity.
3. 'SUPPLY CHAIN HEROES' will vary in attraction with their ability to absorb capital and the global economic cycle. However, for those who succeed, investment opportunities can be multi year.
4. 'STABLE BUT SMALL' countries reflect the risks and opportunities of their surrounding client economies by virtue of their size. As an example, CEE has been impacted by Russia/Ukraine and remains observant to developments in mainstream Europe and the euro.
5. 'NATURAL RESOURCE WINNERS' vary enormously, not least in the cycles for their product. Efforts to diversify their economies are long term. Energy transition has the potential to alter this landscape.
6. 'STRUCTURALLY CHALLENGED' countries require considerable fortitude to navigate. Investment is best concentrated in sectors with strong risk protection including credit enhancement, political risk insurance and FX/inflation indexation.
7. Don't confuse financial resilience with debt levels. Resilience derives from savings not credit flows.
8. Excess homogeneity and lazy decision making have obscured these important differentiators.
9. If investors (ourselves included) can appreciate risk segmentation they can also plan potential mitigation strategies. What looks too risky can become rewarding with good management.
10. Mitigation strategies exist. Understanding what you are addressing and why is the stock in trade of portfolio management excellence.

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