Emerging Markets Spotlight

James Syme, JOHCM Global Emerging Markets Opportunities Fund

"Kospi-listed Firms' Dividend Surpasses 3 Trillion Won in First Half." — *Business Korea,* October 4, *2017*

We have been overweight South Korean equities since the end of 2012, finding the combination of strong corporate growth, attractive valuations and corporate-governance reform an attractive proposition. The portfolio has benefited from this, both through a modest contribution from country allocation as well as through effective stock selection.

We have focused on Korean exporters (that also meet our valuation and corporate-governance requirements), but that view is changing. At the end of 2016, a major corruption scandal in Korea led to mass protests, the impeachment of then-President Park Geun-hye and an election in May 2017. That election returned a more liberal/left-wing administration under President Moon Jae-in and is a significant contributor to our widened area of opportunity in the Korean equity market.

The stand-out feature of Korean equities is how cheap they are. On an industry-neutral basis, the cheapest markets on a price/earnings basis in the emerging world are Russia, Greece, Pakistan and Korea. Three of those face serious economic and/or political challenges; Korea does not. Korean equities are cheap because those earnings do not translate into dividends. Corporate Korea has the lowest payout ratio of any major market in the world because a lack of effective oversight allows company managers to simply hold cash back from shareholders.

To put some numbers on this, in 2016 the non-financial companies in MSCI Korea paid out KRW 15.7 trillion (US$13.5 billion at a 2016 exchange rate) in dividends on an earnings base of KRW 71.5 trillion, a 22% payout ratio. Those dividends look even less generous when one considers that those companies generated KRW 143.2 trillion in cash flow from operations and had a capital expenditure of KRW 95.6 trillion. The resultant KRW 47.6 trillion in free cash flow is potentially entirely available to pay out as dividends, which would increase the dividend yield on non-financial MSCI Korea from the current 1.4% to 5.0%. By comparison, five-year government bond yields in Korea are 2.0%.

Incredibly, there can and should be more. The net debt/equity of these companies is 10%, making Korea one of the least-levered markets in the world. The emerging-market average for non-financial companies is 27.8%, implying that a further KRW 167.6 trillion of dividends (representing 17.8% of market capitalization) could also be paid out through more efficient capital management.

The behavior of corporate Korea and the related lack of dividends have become an increasing issue in Korean politics, as an aging population needs income from its investments. We believe that both the Korean public's response to the corruption scandal and the resulting election of a left-wing administration will apply enormous pressure on Korean companies to reform, and that this will be the catalyst to unlock much of the hidden value in the Korean equity market.

Crucially, though, and in line with our investment process, we believe this creates opportunities within Korea rather than a case to own every stock in the market. First, financial companies have been excluded from this calculation as this is not a useful analysis. Second, Korea does contain a few horribly overleveraged businesses. As always in emerging markets, it pays to be selective.

An investor should consider the Fund's investment objectives, risks, and charges and expenses carefully before investing or sending any money. This and other important information about the Fund can be found in the Fund's prospectus or summary prospectus, which can be obtained at www.johcm.com or by calling 866-260-9549 or 312-557-5913. Please read the prospectus or summary prospectus carefully before investing. The JOHCM Funds are advised by J O Hambro Capital Management Limited and distributed through FINRA member BHIL Distributors, LLC. The JOHCM Funds are not FDIC-insured, may lose value, and have no bank guarantee.

RISK CONSIDERATIONS: The Fund invests in international and emerging markets. International investments involve special risks, including currency fluctuation, lower liquidity, different accounting methods and economic and political systems, and higher transaction costs. These risks typically are greater in emerging markets. Such risks include new and rapidly changing political and economic structures, which may cause instability; underdeveloped securities markets; and higher likelihood of high levels of inflation, deflation or currency devaluations. Emerging markets involve heightened risks related to the same factors, in addition to those associated with their relatively small size and lesser liquidity

The small- and mid-cap companies in which the Fund may invest may be more vulnerable to adverse business or economic events than larger companies and may be more volatile; the price movements of the Fund's shares may reflect that volatility.

The views expressed are those of the portfolio manager as of October 2017, are subject to change, and may differ from the views of other portfolio managers or the firm as a whole. These opinions are not intended to be a forecast of future events, a guarantee of future results, or investment advice.