

VanEck

FUNDS

# Emerging Markets Shake Off Brexit

By David Semple, Portfolio Manager

## VanEck Emerging Markets Fund

GBFAX / EMRCX / EMRIX / EMRYX

### Performance Review

The VanEck Emerging Markets Equity Fund (the "Fund") returned 7.75% during the third quarter of 2016, underperforming the Fund's market index benchmark, the Morgan Stanley Capital International Emerging Markets (MSCI EM) Index, which returned 9.15% for the same period.

#### Average Annual Total Returns (%) as of September 30, 2016

	3Q16 <sup>†</sup>	1 Yr	3 Yr	5 Yr	10 Yr
Class A: NAV (Inception 12/20/93)	7.75	9.96	0.45	6.66	3.75
Class A: Maximum 5.75% load	1.58	3.62	-1.53	5.36	3.14
MSCI EM Index	9.15	17.21	-0.21	3.39	4.28
MSCI EM IMI Index	8.95	16.60	0.02	3.59	4.56

<sup>†</sup>Quarterly returns are not annualized.

Emerging markets continued to gather momentum and flows following the Brexit vote and, in the third quarter, outperformed most global indices including the S&P 500® Index. Large-caps outpaced small-caps, again extending the performance gap for the year. Growth stocks staged a modest comeback over value stocks.

After a couple of quarters of weakness, China was among the best performing countries in the third quarter, accompanied by Brazil (a familiar outperformer this year) and Hungary. India also advanced. Turkey, on the other hand, declined substantially during the quarter as a result of the power grab attempt by Turkish president Recep Tayyip Erdogan following the unsuccessful coup. Technology stocks pushed higher during the quarter to become the third best performing sector for the year following energy and materials. Utilities stocks performed the worst during the quarter.

### Fund Contribution

Stock selection added alpha, while asset allocation detracted from performance. On a sector level, selection in the telecommunications and consumer sectors led the way during the third quarter while selection and under allocation to the information technology sector hurt relative performance. On a country level, selection in Mexico, Taiwan, and India contributed most to relative performance while South Korea, China, and Jordan detracted from relative performance. The Fund's selection in the small-cap category detracted from performance most during the third quarter, while selections in large- and mid-caps aided performance.

**Expenses: Class A: Gross 1.46%; Net 1.46%.** Expenses are capped contractually until 05/01/17 at 1.60% for Class A. Caps exclude certain expenses, such as interest.

The table presents past performance which is no guarantee of future results and which may be lower or higher than current performance. Returns reflect applicable fee waivers and/or expense reimbursements. Had the Fund incurred all expenses and fees, investment returns would have been reduced. Investment returns and Fund share values will fluctuate so that investor's shares, when redeemed, may be worth more or less than their original cost. Fund returns assume that dividends and capital gains distributions have been reinvested in the Fund at net asset value (NAV). Index returns assume that dividends of the Index constituents in the Index have been reinvested. Performance information current to the most recent month end is available by calling 800.826.2333 or by visiting [vaneck.com](http://vaneck.com).

Please refer to index descriptions on last page. One cannot invest in an index.

Please note that the information herein represents the opinion of the portfolio manager and these opinions may change at any time and from time to time. Information herein should not be construed as investment advice.

Our top five contributor companies for the quarter included long-term portfolio position Chinese internet company Tencent Holdings (3.5% of Fund net assets\*) and Chinese e-commerce company JD.com (2.8% of Fund net assets\*), both of which rose during the quarter on the back of good earnings results.

In India, Yes Bank Limited (3.0% of Fund net assets\*), a high quality, private sector bank benefited from strong loan and deposit growth, outpacing peers, while at the same time maintaining a steady non-performing loans level. CP All (2.2% of Fund net assets\*), which operates close to 9,000 corporate, franchise, and sub-area license stores around Thailand reported strong second quarter results, resulting in earnings estimate upgrades.

Finally, Taiwan Semiconductor (2.8% of Fund net assets\*), the undisputed global leader in integrated circuit (IC) manufacturing, benefited from robust sales growth, and a strong 2017 demand outlook.

Our bottom five contributor companies in the third quarter were:

Hikma (0.7% of Fund net assets\*), a London listed pharmaceutical company with a mix of branded and non-branded generics, and in-licensed drugs, had a difficult quarter in stock performance terms, reversing a strong second quarter. The proximate cause was a downgrade to company guidance, specifically related to delayed product approvals, which lead most analysts to downgrade earnings for this year, and conservatively, also for 2017.

Robinson Retail (1.5% of Fund net assets\*), a Philippines-based retailer, with a variety of retail formats, also reversed relatively strong second quarter performance. In part this was due to a diminished enthusiasm for Philippines stocks generally, following on from the election of their new president. For the company itself, operations are robust, although there has been some frustration at the pace of deployment of capital, and concern about strong competition, particularly in Metro Manila.

Techtronic (1.4% of Fund net assets\*), a China-based producer of power tools that are sold mainly in the U.S. and Western Europe, declined due to weaker than expected quarterly revenue growth, and higher than expected promotional costs on new products, which depressed margins.

Credicorp (2.2% of Fund net assets\*), the leading bank in Peru, pared back gains from earlier in the year after it reported weaker than expected loan growth in the second quarter driven by

economic uncertainty caused by Peru's presidential election. Hence, loan growth for the full year is now expected to be lower than the market originally expected.

Rounding out the underperformers is Eva Precision (0.0% of Fund net assets\*), a position which has now been exited. Hopeful signs of better plastic molding orders did not, in the event, actually translate into orders, leading to worse than expected revenue and poorer gross margins.

## Market Review

Global markets have seen some significant challenges, including record low and negative bond yields and concern about the limits of quantitative easing. Markets have been challenged by Brexit, and concerns about the rise of "populist politics" – to name a few issues. Emerging markets specifically have seen some challenges, including political change in Brazil and an attempted coup in Turkey. Notwithstanding these risks, the summer was actually a period of restrained market volatility, which surprised many market participants.

Many factors combined to create the stronger relative performance from emerging markets during the quarter, and so far this year, compared to global indices. First, the rapid appreciation of the U.S. dollar appears to have faded as market expectation of a U.S. Federal Reserve (the "Fed") rate hike has been pushed back until the end of the year and possibly next year. Second, despite the febrile headline-grabbing comments of market pundits, China has not had any kind of "Minsky" moment, whether related to capital outflows or leverage. We certainly concede that there are some significant imbalances in the economy, but believe that the extra "stabilizers" available to authorities will be used to attempt to achieve a reasonably stable outcome over the medium term. Third, the supply and demand equation for commodities looks more balanced. Fourth, earnings are likely to be much less disappointing this year, partly because expectations have been reset to lower levels, and partly because corporates are gradually acclimatizing to a slower growth world and generating more efficiencies, rather than focusing predominantly on top-line growth.

Reform efforts have been uneven in emerging markets, but we are encouraged by the long-term impact of the passage of the GST tax in India. In China, some reform efforts are often opaque and sometimes seem like they are "two steps forward then one back". The outcome of tax amnesties in India and Indonesia appears to have been better than expected, and, finally, infrastructure projects seem to be developing greater impetus in a number of countries, for example, the Philippines.

## Outlook

We remain constructive on the continuing outperformance of emerging markets in a global context. After an extended period in the wilderness, emerging markets assets have shown considerable relative strength so far this year. We feel that there is reasonable evidence for that outperformance to continue for the asset class as a whole. Broadly speaking, a stable U.S. dollar, better commodities' prices, a more resilient earnings profile, and light positioning in the asset class ought to combine to increase the relative attractiveness of emerging markets.

One facet of the uptick in interest is that substantially all inflows into the asset class this year have come through passive fund offerings. While appreciating the convenience that ETFs offer, we caution that allocation of capital through market capitalization can be particularly pernicious in emerging markets.

We make this comment because, given the economic history of many emerging markets economies, there are many very large scale state owned companies in the emerging markets universe. The prominence of these companies we feel comes less from superior competence than from historically state sponsored systemic advantage which is unlikely to be sustained in the long run. In addition, we believe many of these large companies are essentially driven by global cyclical factors such as energy and materials. We will continue to implement our philosophy of structural growth at a reasonable price. We are not style agnostic, drifting into whatever appears to be working at any given time. We are style specific and we continue to find that there are many areas of superior, sustained growth that are essentially non-cyclical in nature and will likely provide reliable opportunities for well-managed companies to exploit.

While there may be some countries where economic growth has stabilized or even picked up, the evidence for a sustained, strong improvement in global GDP appears limited, at best. In a growth-challenged world, our philosophy of focusing on investment opportunities where strong, innovative management teams are able to capitalize on dynamic change and extract real value, ought to be rewarded over the medium term, despite the vagaries of commodity pricing and ETF flows.

Valuations for emerging markets equities and currencies are generally constructive, but not compellingly cheap. Expectations for earnings are much more realistic, and positioning in the asset class is cautious. Delayed expectations of further Fed tightening have also been positive for the asset class. Finally, it is perhaps hard to construct a case for alternative geographies and asset classes; arguably, the U.S. equity market looks overvalued, Japan is struggling with a strong currency, and Europe faces significant questions and uncertainties surrounding its political and economic future.

Consequently, we approach the remainder of this year, and the following years, with cautious optimism for the asset class. Much more importantly, we remain unabashedly enthusiastic about the companies that we actually own in emerging markets. As most investors know, we have a high active share and a healthy skepticism that the large emerging markets companies necessarily represent some of the best investable dynamics in emerging markets.

\*All country and company weightings as of September 30, 2016.

A State-Owned Enterprise (SOE) is a legal entity created by a government with the purpose to partake in commercial activities on the government's behalf.

All indices listed are unmanaged indices and include the reinvestment of all dividends, but do not reflect the payment of transaction costs, advisory fees or expenses that are associated with an investment in the Fund. An index's performance is not illustrative of the Fund's performance. Indices are not securities in which investments can be made. The Morgan Stanley Capital International (MSCI) Emerging Markets Index captures large- and mid-cap representation across 23 Emerging Markets (EM) countries. With 836 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. The MSCI Emerging Markets Investable Market Index (IMI) captures large, mid and small cap representation across 23 Emerging Markets (EM) countries. With 2,628 constituents, the index covers approximately 99% of the free float-adjusted market capitalization in each country. MSCI All Country World Index (ACWI) captures large and mid cap representation across 23 Developed Markets (DM) and 23 Emerging Markets (EM) countries. With 2,483 constituents, the index covers approximately 85% of the global investable equity opportunity set.

Diversification does not assure a profit or prevent against a loss.

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The Fund is subject to the risks associated with its investments in emerging markets securities, which tend to be more volatile and less liquid than securities traded in developed countries. The Fund's investments in foreign securities involve risks related to adverse political and economic developments unique to a country or a region, currency fluctuations or controls, and the possibility of arbitrary action by foreign governments, including the takeover of property without adequate compensation or imposition of prohibitive taxation. The Fund is subject to risks associated with investments in derivatives, illiquid securities, and small or mid-cap companies. The Fund is also subject to inflation risk, market risk, non-diversification risk, and leverage risk. Please see the prospectus and summary prospectus for information on these and other risk considerations.

Please call 800.826.2333 or visit [vaneck.com](http://vaneck.com) for performance information current to the most recent month end and for a free prospectus and summary prospectus. An investor should consider the Fund's investment objective, risks, and charges and expenses carefully before investing. The prospectus and summary prospectus contain this as well as other information. Please read them carefully before investing.



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