



BARINGS EMERGING EMEA OPPORTUNITIES PLC

Istanbul, Turkey

Emerging EMEA: The developing tech region you can't ignore



Adnan El-Araby, Portfolio Manager on the Barings EMEA Equities Team, explains why it's time to take a serious look at emerging EMEA's homegrown technology companies.

When it comes to choosing technology companies to put in a portfolio, investors may immediately think of big-name stocks from the US or Asia. Global giants such as Microsoft, Alphabet (parent company of Google), Amazon from the US or Tencent, Alibaba and Samsung Electronics in Asia dominate their market indices. They can therefore seem the natural choice for either a global diversified or technology-focused strategy.

Of course, these big names still have the potential to deliver attractive earnings. But focusing on established tech names and markets can mean missing out on new opportunities that are equally (or sometimes even more) compelling. In particular, a focus on the US and Asia can lead investors to overlook the dynamics that are making technology players in Emerging Europe, the Middle East and Africa of interest to informed investors.

Here I want to take a look at a few of the reasons why ‘emerging EMEA tech’ deserves close attention.

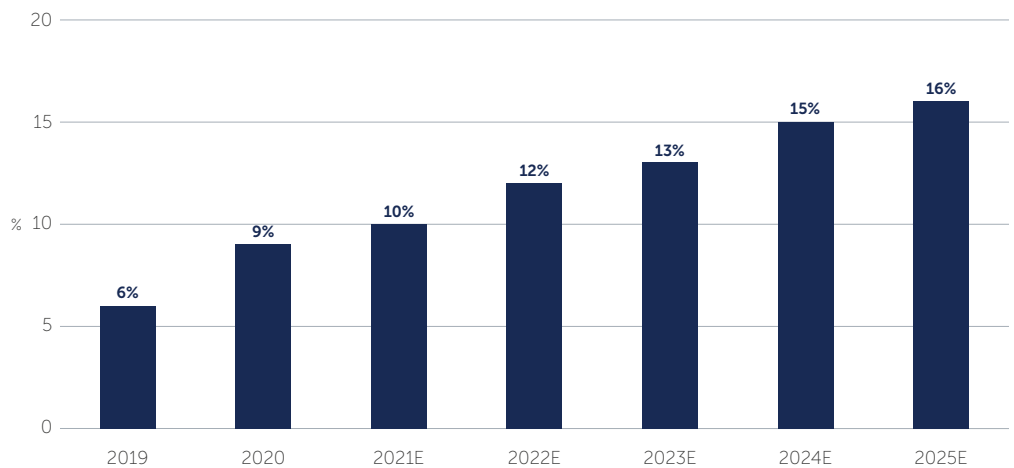
Emerging EMEA consumers are embracing e-commerce rapidly...

Right now, across Eastern Europe, Russia, the Middle East and down to South Africa, we are seeing a seismic shift in behaviour as consumers pivot from offline to online living...

Alongside sectors like infrastructure and consumer discretionary goods, technology has long been a key beneficiary of any emerging market’s growth story. For example, right now, across Eastern Europe, Russia, the Middle East and down to South Africa, we are seeing a seismic shift in behaviour as consumers pivot from offline to online living, including online banking, food delivery, transport services and gaming.

Like everywhere else, this trend has been accelerated by the Covid-19 pandemic. In Poland, for example, the proportion of total retail sales accounted for by e-commerce leapt from 5.6% in January 2020 to almost 10% a year later. Russia’s online penetration rates as a percentage of retail sales have also accelerated after years of meagre growth caused by low consumer awareness and inefficient logistics – and is on course to grow from 10% in 2021 to 16% in 2025 – see Figure 1.

FIGURE 1: Forecasts for e-commerce penetration in Russian retail



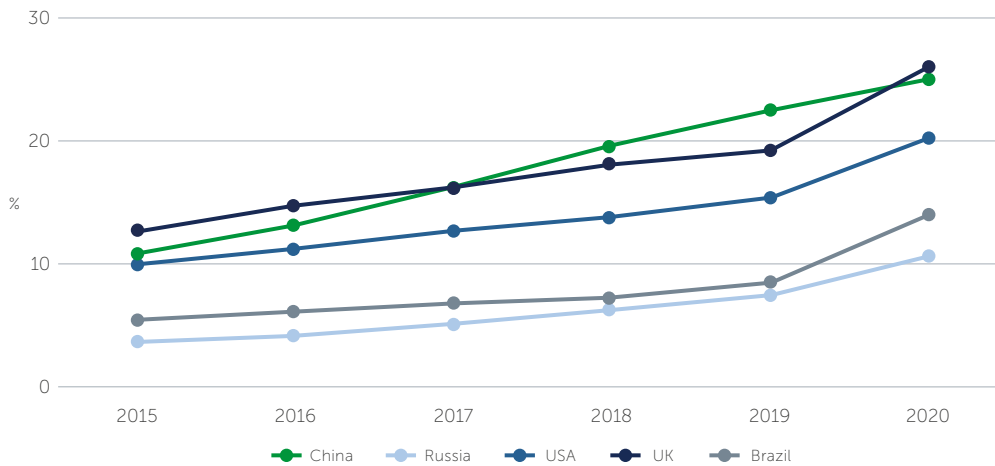
Source: InfoLine, company data, UBS estimates, as of January 2021.

...and the region is at a much earlier stage of its tech journey

The shift to e-commerce is, of course, happening globally. But emerging EMEA is at a much earlier stage of that journey, thereby offering greater potential for further growth.

For example, even given the pandemic-related rise, e-commerce penetration in Russia and Brazil stands at 10% and 14% respectively, compared to 20% in the US, 25% in China and 26% in the UK – see Figure 2. Turkey is expected to see e-commerce adoption within its retail markets more than double in the next five years to 22%, thanks to its young population (46% of which are under 30) and rapid shift to urbanisation.

FIGURE 2: Growth in e-commerce penetration rates over time



Source: Euromonitor, ONS UK, HSBC, as of June 2021.

Homegrown tech is often preferred to – or more accessible than – global names

Another compelling aspect is that the companies benefitting from this growth aren't necessarily the ones you might expect. Instead of turning to established global brands, 'local champions' are often the preferred providers.

This is sometimes because overseas companies have limited access but also because local players have the right infrastructure. For example, Amazon's full retail offering is only now in the process of being launched in Poland. In its place, local e-commerce platform Allegro has flourished. As well as offering the right product mix for its local audience, Allegro is far better geared up for Poland's pick-up boxes/locker delivery system to serve its largely apartment-living population.

Sometimes home-grown stocks do better because they have a greater understanding of their market. In Russia, the most popular internet search engine is home-grown Yandex, accounting for 60% of the digital advertising market. Commentators suggest Yandex's enduring edge against Google is its superior ability to interpret Russian-language searches. Like Google, Yandex has also diversified into other services, such as online payments, cloud services, music streaming, e-commerce and even taxi services. It is now the biggest technology and media company in Russia.

Emerging EMEA tech valuations supported by expected growth

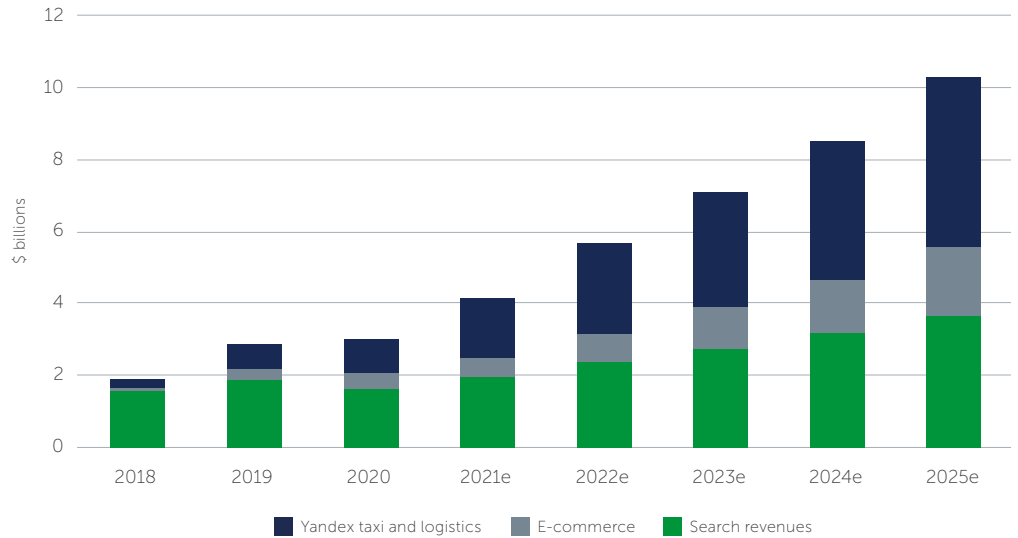
The gravity-defying ability of the world's 'Big Five' tech companies – Apple, Microsoft, Amazon, Alphabet and Facebook – to keep rising in market value, including through the Covid-19 pandemic, has been well documented. In some cases, structural growth drivers such as the accelerated global shift to digitisation can justify their stratospheric share prices. But nonetheless, investors would do well to keep their tech portfolio diversified, given there is little room in the Big Five's share prices for negative surprises.

Emerging EMEA technology stocks, conversely, could see their share prices supported by two major considerations: first is their superior growth rates relative to developed market peers. Second is the 'scarcity premium' they enjoy from being the few stocks that global investors can allocate to in order to achieve tech exposure in the region.

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Russian search engine leader Yandex, for example, is on course for substantial year-on-year growth as taxi and logistic services account for a growing proportion of its diversified revenue streams – see Figure 3. Plus, profit margins on both taxi services and e-commerce are on the rise for the company. Its fellow Russian e-commerce player Ozon – often dubbed the Amazon of Russia – is forecast to see gross merchandise value (GMV) growth on its platforms that dwarfs other stocks in the sector – see Figure 4.

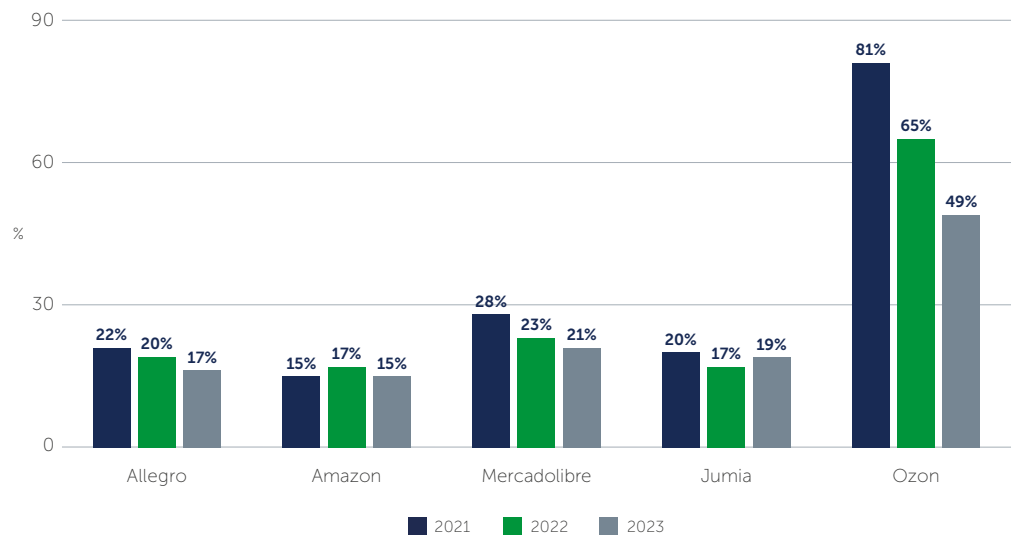
FIGURE 3: Diversified revenue streams are supporting growth for Yandex...



Source: Yandex, Barings, as of June 2021.

Russian e-commerce player Ozon is often dubbed the Amazon of Russia...

FIGURE 4: Ozon’s forecast gross merchandise value (GMV) growth rate dwarfs the competition...



Source: Morgan Stanley Research estimates as of February 2021.

A final plus-point for emerging EMEA tech stocks, in terms of their valuations, is their low levels of debt compared to many of their developed market peers. The reopening of economies in recent months has created inflationary pressures as pent up demand is released, leading to expectations of interest rate rises. The less indebted tech stocks across emerging EMEA are better placed to withstand any increase in the cost of borrowing as interest rates trend upwards.

Local opportunity demands local insight

The emerging EMEA region offers a fresh means to harness the investment opportunities being shaped by the global shift to life online.

But emerging EMEA markets have their own idiosyncrasies, preferences and behaviours. Identifying the most attractive opportunities, therefore, demands deep local knowledge and access. We invite you to learn more about Barings Emerging EMEA Opportunities PLC to see how it can put you at the heart of this region's tech story.

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Finding quality companies from Emerging Europe, the Middle East and Africa

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