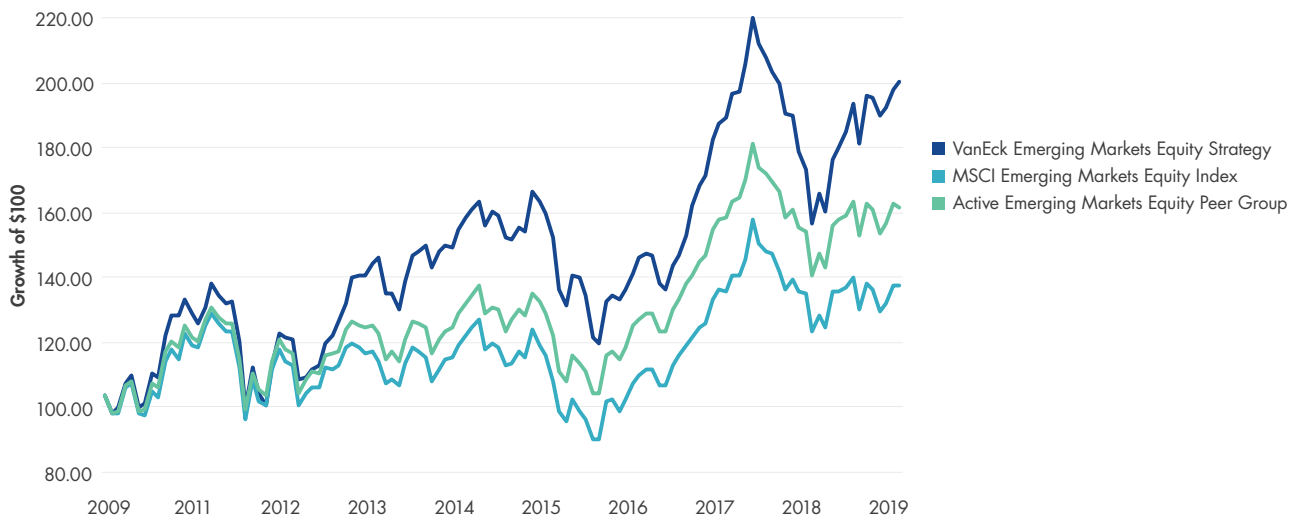


Our Active EM Solution vs. Passive Investing

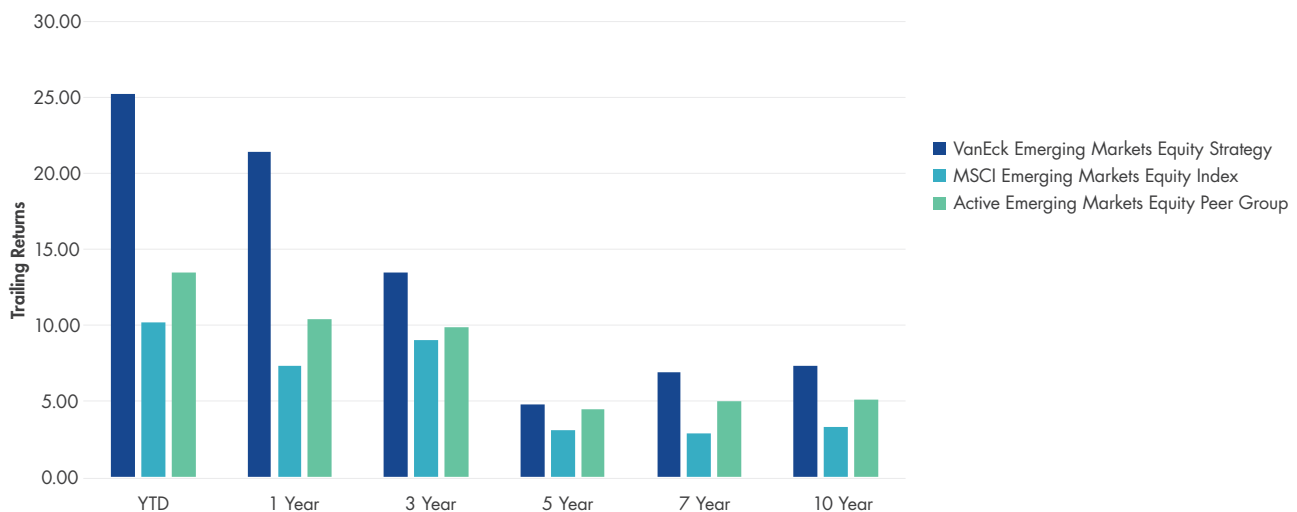
The rise of passive investing in emerging markets (“EM”) shows no signs of abating. Very many indices have been created and new ETFs are being proposed to further carve up the asset class. And yet, the **VanEck Emerging Markets Equity Strategy** continues to outperform a broad emerging markets index (“MSCI EM Index”) over multiple periods. The Strategy has also outperformed the Active Emerging Markets Equity Peer Group,¹ as outlined below. This has caused us to reflect again on the relative role, advantages and disadvantages of active and passive investing in emerging markets. This white paper aims to explain emerging markets index limitations and inefficiencies, and discuss the VanEck Emerging Markets Equity Strategy as an active solution and its fit within an investor’s total portfolio allocation framework.

VanEck EM Active Solution vs. Passive Investing – Growth of \$100 over 10 Years (2009-2019)



Source: eVestment. Data as of 11/30/2019.

VanEck EM Active Solution vs. Passive Investing – Historical Trailing Returns over 10 Years (2009-2019)



Source: eVestment. Data as of 11/30/2019.

¹ The Active Emerging Markets Equity Peer Group is defined as the Global Emerging Markets Equity All Cap Category in eVestment.

Inside the MSCI Emerging Markets Index – Its Limitations and Inefficiencies

Through many years of investment research, deep expertise and local knowledge of emerging markets around the world, our Investment Team² have identified the following limitations and inefficiencies of the broad emerging markets index, which we will address individually. We believe that the MSCI EM Index is:

- Backward Looking vs. Forward Looking
- Not Fully Representative of Emerging Markets as an Asset Class due to
 - Natural Bias and Significant Overweight in Large Cap, Often Cyclical Issuers
 - Corporate Governance Issues
 - Sector Dispersion
 - Under-Researched Opportunities in Small-Mid Capitalization Companies (“SMID”) as Future Business Model Disruptors
 - Index’s Liquidity Constraints

Backward Looking vs. Forward Looking Approach

Most widely used indices tend to poorly capture current EM trends, leading investors to potentially miss out on structural growth³ opportunities, as emerging markets continue to evolve.

Market-cap weighted indices tracking emerging markets tend to be backward-looking, influenced by the movement of companies that have succeeded in the past, without regard for future growth potential or risks. While this approach could work in mature and diverse economies with indices that tend to be more balanced and stable (i.e., the U.S. economy and the S&P 500 Index), it may not be appropriate for emerging markets. Because emerging markets are diverse and evolve at a much faster pace, passive vehicles may be at a structural disadvantage compared to active managers who have the flexibility to continuously evaluate and shift exposures to sectors and countries with the optimal risk-adjusted growth potential in mind.

To further illustrate how emerging markets equities have evolved, let’s examine the top ten holdings of the MSCI EM Index in December 1997 (as the Asian currency crisis unfolded and before Russia’s 1998 debt default), in August 2008 (prior to the global financial crisis) and more recently, in November 2019, as highlighted in the table below.

#	Top Ten 12/31/1997	Top Ten 8/31/2008	Top Ten 11/30/2019
1.	Centrais Electricas Brasileiras S.A.	Gazprom	Alibaba Group Holding Ltd.
2.	Telecomucacoes Brasileiras S.A.	China Mobile Limited	TSMC
3.	Telefonos de Mexico SAB de C.V.	Petroleo Brasileiro S.A.	Tencent Holdings Ltd.
4.	Oil Company LUKOIL PJSC	Samsung Electronics Co., Ltd.	Samsung Electronics Co., Ltd.
5.	Unified Energy System of Russia	Vale S.A.	China Construction Bank Corp.
6.	YPF S.A.	America Movil SAB de CV	Ping An Insurance Group Co. of China Ltd.
7.	Petroleo Brasileiro S.A.	Taiwan Semiconductor Manufacturing Co., Ltd.	Naspers Ltd.
8.	Tenaga National Bhd	Teva Pharmaceutical	Reliance Industries Ltd
9.	Wal-Mart de Mexico SAB de CV	Oil Company LUKOIL PJSC	Housing Development Finance Corp. Ltd.
10.	Genting Malaysia Bhd.	Sasol Limited	ICBC

Source: Bloomberg. Data as of 12/31/1997, 8/31/2008 and 11/30/2019.

² Portfolio Manager David Semple and his Team, which is dedicated to this Strategy, have an average of more than 20 years of direct and broad emerging markets equity experience. The Investment Team are all career emerging markets investors, who have lived and worked in emerging markets. Additionally, the Team leverages resources of the broader organizational research platform, including VanEck’s active equity traders, emerging markets fixed income team, quantitative research team and natural resource specialists.

³ Structural growth investment opportunities are defined as visible and persistent growth ideas that survive and thrive in a rapidly changing asset class such as emerging markets.

In 1997, transportation and utility companies from Latin America and Russia dominated the top ten. Some of the countries included in the list (e.g., Argentina) have since been recategorized to a frontier market status and some of the companies have been delisted.

By the turn of the century, many emerging nations progressed into a new phase of the financial reform, technological advancement and massive infrastructure building, which, naturally, changed the Index's composition. By 2008, the top ten list included companies such as China Mobile, Petrobras, Samsung, Vale and Taiwan Semiconductor.

Since the financial crisis of 2008, the top drivers of economic growth have shifted from infrastructure development that favored fixed asset companies to domestic consumption, which favors Internet and Internet-related technology companies, consumer electronics manufacturers and banks, among others – which are primarily dominated by China and India. Thus, the top ten list composition has changed again.

Not Fully Representative of Emerging Markets as an Asset Class

Natural Bias and Significant Overweight in Large Cap, Often Cyclical Issuers

The MSCI EM Index does not fully represent the universe of opportunity in emerging markets. As of today, it is dominated by large-cap companies, many of which are state-owned enterprises ("SOEs")⁴ that happen to be highly cyclical in nature, such as energy and materials; or low growth companies that comprise the utilities and telecommunications sectors. Many of these issuers grew not due to their superior competence and/or competitive advantage, but rather due to being systematically favored by their own governments through cheap capital, access to raw materials and preferential treatment.

Corporate Governance Issues

Two issues specific to the MSCI EM Index construction are:

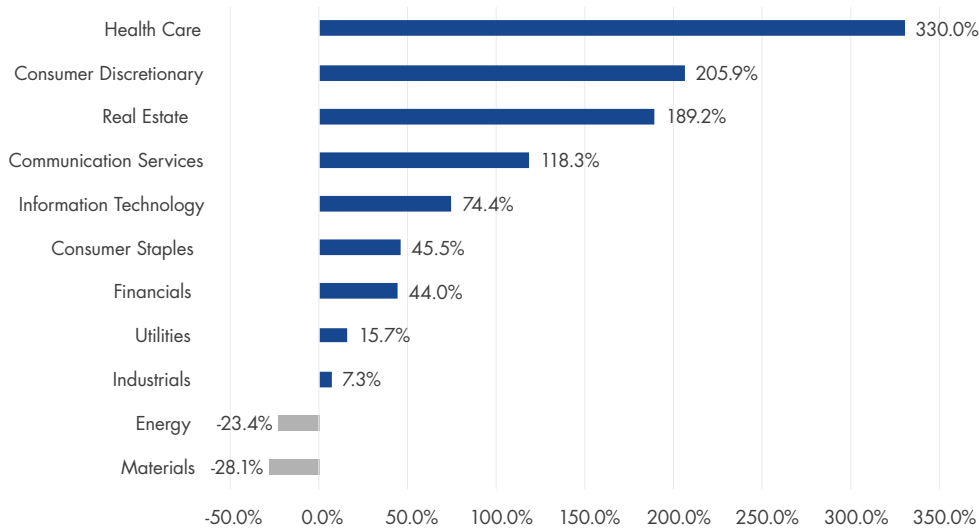
1. Corporate Governance: A significant number of companies, more often than not SOEs, included in the MSCI EM Index have significant corporate governance and ESG issues.
2. Areas of structurally lower growth: The current Index is heavily weighted towards structurally lower growth economies such as Korea and Taiwan. These countries are heavily exposed to global growth factors, as well as structurally low growth sectors, e.g., Utilities and Telecoms.

Sector Dispersion

The Index's inability to implement a forward-looking perspective leads to investor concentration in continuously shrinking, mainly cyclical sectors. For example, 2010 marked another inflection point in the evolution of emerging markets following the financial crisis of 2008. As the economic stimulus from monetary and fiscal easing slowed globally, emerging economies had to look for other ways to maintain their robust economic growth trends. For many governments, focus on domestic growth and consumer-led sectors and away from highly cyclical, fixed-asset infrastructure driven sectors was the answer. As a result, policymakers and investors turned their attention to the emerging markets domestic consumer, favoring sectors and industries influenced by local consumption and services. These sectors not only outperformed in the past few years but they also expanded substantially, especially when compared to some cyclical sectors that experienced a significant decline during the same period (as illustrated in the graph on the next page).

⁴ A state-owned enterprise ("SOE") is a legal entity that is created by a government in order to partake in commercial activities on the government's behalf. It can be either wholly or partially owned by a government and is typically earmarked to participate in specific commercial activities.

MSCI Emerging Markets Equity Index
Historical Market Cap Expansion by Sector (2010-2019)



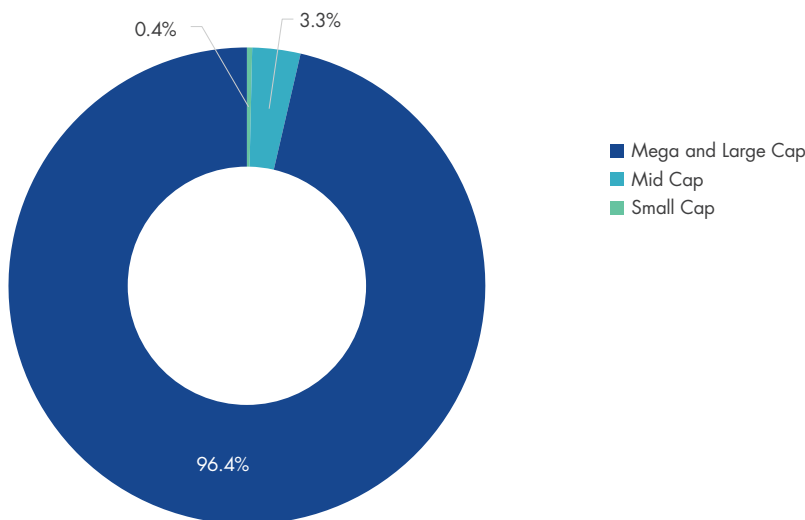
Source: FactSet. Data as of 12/31/2010 and 11/30/2019.

Under-Researched Opportunities in SMID as Future Business Model Disruptors

Due to its methodology, the MSCI EM Index does not fully capture structural growth companies that started small and grew larger through effective management and favorable business conditions. There is no shortage of such inspiring companies in emerging markets. In many cases, some of carefully selected and properly researched small caps (i.e., companies with market capitalizations below \$2 billion) can be the next generation’s disruptive force, often powered by new technologies.

Nevertheless, small and mid-cap companies are underrepresented in traditional emerging markets indices (see the chart below). As of November 30, 2019, small and mid-cap stocks comprised less than 4% of the MSCI EM Index.

MSCI Emerging Markets Equity Index
Market Cap Breakdown by Number of Stocks



Source: Bloomberg. Data as of 11/30/2019.

Index's Liquidity Constraints

Given the number of passive funds, investing in companies that trade in smaller quantities and/or infrequently, can be a challenge. Therefore, passive funds that track broad EM indices may deprive investors of exposure to stocks that may prove not only potentially rewarding but also less vulnerable to the unpredictability of global flows in and out of such funds.

For smaller active strategies, this represents a good investment opportunity with a potential bonus: less volatility and lower valuations, given that the liquidity premium is typically priced into such companies. An active strategy with the ability to invest in small and mid-cap companies may be more nimble and flexible in finding structurally growth businesses at a reasonable price. Additionally, it can also provide investors with access to rising companies before they become liquid enough for inclusion in large active and passive strategies.

VanEck Emerging Markets Equity Strategy as an Actively Managed Solution

We believe an active approach to investing in emerging markets has significant advantages over purely passive investing.

The VanEck Emerging Markets Equity Strategy offers the following:

- Its perspective is **always forward looking**, whereas any index (for example, the MSCI EM Index) typically focuses on companies that have done well in the past
- The Strategy can invest in the most attractive **structural growth opportunities in emerging markets**, while avoiding inefficient large cap and highly cyclical names
- Its investment universe can include stocks of **all market capitalization sizes**, whereas a market-cap weighted index historically and inherently will be dominated by large-cap names that tend to be driven and more responsive to global events
- The portfolio's built-in flexibility enables the Investment Team to identify, access and invest in emerging markets companies that are otherwise **excluded from the MSCI EM Index** due to liquidity requirements and/or other considerations (i.e., market capitalization size)

Allocation to Growth within Total Portfolio Framework

As investors evaluate their growth exposure (i.e., emerging markets equity exposure) as part of total portfolio allocation, the question they should be asking themselves is: "Am I efficiently accessing the best opportunities in emerging markets?" By "best opportunities," we mean fundamentally sound companies with visible and persistent growth that survive and thrive in a rapidly changing asset class such as emerging markets. And by "efficiently," we mean investments that generate acceptable risk-adjusted returns at a reasonable price over time.

Conclusion

It is difficult to reconcile concepts of "passive" and "emerging markets," as the essence of the former is dependent on maintaining the status quo; whereas the latter is a symbol of a dynamic, onward and upward movement. This thesis certainly holds true for emerging markets equities that are more dynamic, constantly changing and evolving by nature. As a result, an actively managed strategy, like the VanEck Emerging Markets Equity Strategy, outperformed the broad emerging markets index (i.e., MSCI EM Index), as well as the Active Emerging Markets Equity Peer Group over multiple periods ending November 30, 2019. While we, as the firm, have long supported both active and index-based passive management styles, our EME Investment Team's research concludes that an active approach to investing is the way to go in the context of emerging markets equities.

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Emerging Market securities are subject to greater risks than U.S. domestic investments. These additional risks may include exchange rate fluctuations and exchange controls; less publicly available information; more volatile or less liquid securities markets; and the possibility of arbitrary action by foreign governments, or political, economic or social instability.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of 24 emerging markets countries. The MSCI Emerging Markets Investable Market Index (IMI) is a free float adjusted market capitalization index that is designed to capture large-, mid- and small-cap representation across 24 emerging markets countries. Emerging markets countries include: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Greece, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Pakistan, Peru, Philippines, Poland, Russia, Qatar, South Africa, Taiwan, Thailand, Turkey and United Arab Emirates.

Standard & Poor's 500, often abbreviated as the S&P 500, is an American stock market index based on the market capitalizations of 500 large companies having common stock listed on the NYSE or NASDAQ. The S&P 500 index components and their weightings are determined by S&P Dow Jones Indices. The S&P 500 Index is a product of S&P Dow Jones Indices LLC and/or its affiliates and has been licensed for use by Van Eck Associates Corporation. Copyright © 2019 S&P Dow Jones Indices LLC, a division of S&P Global, Inc., and/or its affiliates. All rights reserved. Redistribution or reproduction in whole or in part are prohibited without written permission of S&P Dow Jones Indices LLC. For more information on any of S&P Dow Jones Indices LLC's indices please visit www.spdji.com. S&P® is a registered trademark of S&P Global and Dow Jones® is a registered trademark of Dow Jones Trademark Holdings LLC. Neither S&P Dow Jones Indices LLC, Dow Jones Trademark Holdings LLC, their affiliates nor their third party licensors make any representation or warranty, express or implied, as to the ability of any index to accurately represent the asset class or market sector that it purports to represent and neither S&P Dow Jones Indices LLC, Dow Jones Trademark Holdings LLC, their affiliates nor their third party licensors shall have any liability for any errors, omissions, or interruptions of any index or the data included therein.

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