

MONEY & INVESTING

EMERGING MARKETS

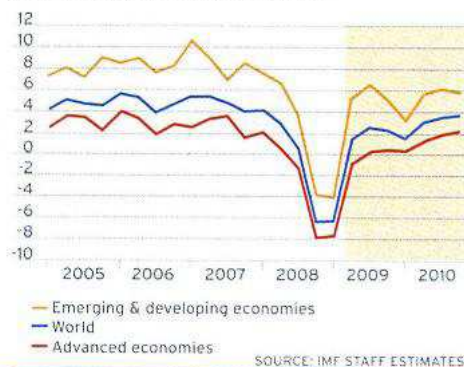
Going strong

Equities in many emerging markets have recovered strongly from their steep declines in the past two years. In many cases they fell further than markets in developed economies, but they have so far shown quicker and stronger recoveries. Their recoveries have also been quicker than they were after previous deep falls in emerging markets, in 1997-1998 and earlier in that decade.

These markets are still exposed to

HIGHER GROWTH

Global GDP growth (%) quarter/quarter, annualised



substantial risks. The MSCI US\$ emerging markets index has risen by 60% from its lows of October last year, but remains 4.4% lower than at its record high in 2007 — and some international analysts say certain emerging markets may now be expensive, based on earnings prospects. Other investors disagree.

“Broadly speaking, emerging markets are more attractive than developed markets because the earnings growth is going to be higher yet the ratings are similar,” says Coronation Fund Managers portfolio manager Gavin Joubert, who heads a team that specialises in emerging market portfolios. Joubert says emerging markets should be seen as a “five to 10-year story”.

Franklin Templeton emerging markets investment guru Mark Mobius says in his latest update that the outlook for emerging markets remains “positive”. He adds that valuations remain attractive.

Citigroup, in its latest global strategy review, says it generally favours emerging over developed markets.

The recovery in emerging markets is significant when seen in the context of previous bear markets and the deeply negative investor sentiment in the fourth quarter of last year. It reflects the change in risk aversion, and recognition of improved economic fundamentals, with higher growth rates still expected in many developing economies.

The trends in these markets are important for several reasons. They are a reminder that much of the world still has better growth prospects than the developed economies of the US, Japan or Europe, though the problems in the latter regions capture greater attention.

The JSE should be seen in the context of emerging markets, which are often influenced by international capital flows. Emerging markets may also offer specific opportunities for local investors who want to diversify globally.

The correlation between emerging markets — or between these and developed markets — can be high in the short term, but they should be considered individually, as they vary greatly.

Some of the strongest equity market recoveries (in dollars) from last year's lows have been in Brazil (up 79%), China (67%), India (90%) and Indonesia (119%). The JSE all share has risen by 80% in dollars and 24% in rand. Russia's market has risen, in dollars, by 79% since early February, but is 65% below its high in May 2008.

These figures are affected significantly by the renewed weakness in the dollar and recoveries in many developing economies' currencies after last year's panic. In local currencies, some of the emerging market recoveries are less impressive, but the pattern is similar. Almost all are still well below earlier highs, which at least partly discounts the weaker earnings outlook.

In the latest update of its world economic outlook, the IMF estimates that emerging and developing economies will

grow at 1,5% in 2009 and 4,7% in 2010. The 2010 figure is 0,7 percentage points higher than the IMF's previous estimate. It says these economies are expected to regain growth momentum in the second half of 2009, though with notable regional differences.

The best growth is still expected to come from emerging Asia. The IMF has revised its earlier growth projections for this region upward to 5,5% in 2009 and 7% in 2010. The upgrade is based on improved prospects in China and India, in part reflecting substantial macro-economic stimulus; and a faster than



Gavin Joubert

RECOVERY TREND

Share prices based to 100



expected turnaround in capital flows.

Joubert points out many high-growth companies in these economies are domestic businesses that do not depend on international trade.

Earnings of many emerging market domestic stocks, such as telecom providers and retailers, are still growing well. Some of these, such as MTN and Shoprite, are listed locally. However, other emerging markets offer many other choices in these sectors, including companies at earlier stages of development and at similar or lower valuations.

Longer term, emerging markets should gain in importance for global investors because of growth and demographic trends. They now account for 30% of global GDP, up from 20% several years ago. Joubert expects this will rise to 50% in 15 years. They account for 24% of world equity market capitalisation, up from 16%-17% late last year and much less a decade ago. The JSE represents just 0,9% of the world equity market.

Populations in most developing economies are younger and potentially more productive than the ageing populations of the US, Japan and Western Europe. A growing middle class and infrastructural investment helps support growth in developing economies, which account for more than 80% of the world's population, says Mobius.

Moreover, people in the slower-growth, developed economies may increasingly have to take a more global view when investing for retirement.

Provided valuations do not become stretched, and political and economic management remains stable, this should remain a positive dynamic for emerging markets, including the JSE.

Andrew McNulty