News & Views

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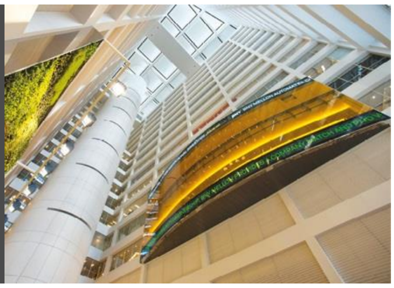
For Professional Clients and, in Switzerland, Qualified Investors

BNY MELLON



ARE YOU INVESTED IN THE RIGHT EM ‘BUCKETS’?

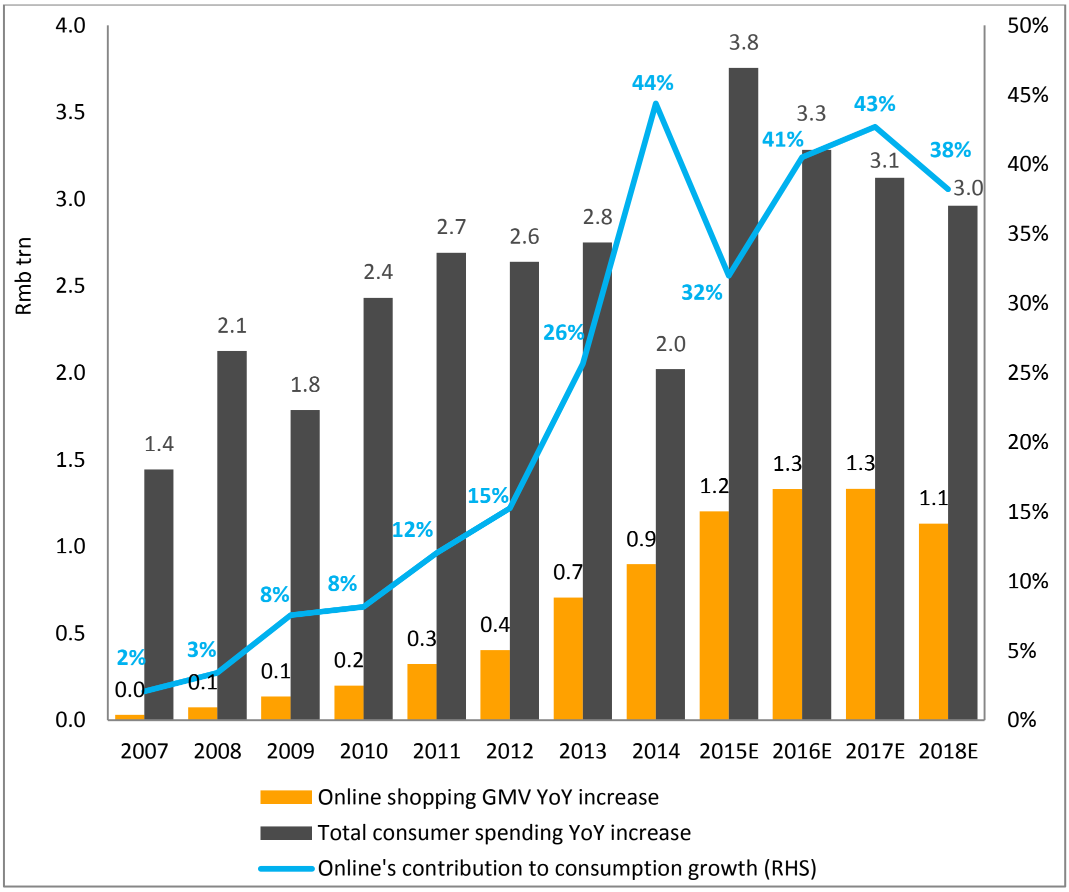
A decade ago, investors just wanted to be in emerging markets, no matter where, according to Rob Marshall-Lee, leader of Newton’s Emerging and Asian Equity teams, adding that there are now hugely diverse outcomes for the very different constituent countries, sectors and companies.

“Tracking error is not your friend,” he says. As has been the case for emerging-market investors for the past two to three years, selectivity is the key to capturing growth and will remain so for the next five years.

Moreover, in a world where growth is getting ever scarcer, the emerging markets still have a lot to offer. However, there is significant differentiation in terms of GDP growth, says Marshall-Lee.

Across the emerging markets where retail is much less sophisticated than in the developed markets, consumers are benefiting from access to the mobile internet. Whereas consumers in the developed world have long enjoyed PC-based broadband, hundreds of millions of emerging-market consumers now have personal access to the internet for the first time. This is thanks to Android smartphones costing as little as US$50 and to fast expanding 3G and 4G connectivity. In China, eCommerce is increasing as a percentage of consumption as a result of increased mobile connectivity.

Contribution to China's total consumer spending by online shopping



Source: NBS, iResearch, March 2016

Telecoms may be benefiting from data usage but are losing revenue from voice as well as facing increased competition and the burden of heavy capital expenditure (capex), says Marshall-Lee. In contrast, internet companies are benefiting from improving technology and their capex is light.

Healthcare is also a significant growth area as government provision in the emerging markets has often been very poor but, as individuals earn more, they can dedicate a greater proportion of their disposable income to spending on health.

Demand for autos is a good indicator of the robustness of consumer sentiment and auto sales paint a clear picture of divergence across the emerging markets, says Marshall-Lee. If a consumer is confident about his or her personal circumstances and not burdened by debt, there is greater willingness to go out and buy ‘big ticket’ items, such as a car.

Looking at individual markets, China’s economy is decelerating, while, India’s is accelerating, comments Marshall-Lee. The Chinese economy is “a big beast, driven by industrialisation” and in the mid ‘noughties’ “put the pedal to the metal,” he adds. The Chinese government knows it is on an unsustainable path and is now actively seeking to rebalance the economy towards the consumer.

Marshall Lee says that with c.70% of the Chinese market state controlled, the c.30% in private ownership, in contrast, offers attractive opportunities – especially among internet and healthcare companies..

Investing by anecdotes in China can mislead, says Marshall-Lee. Chinese ghost cities may make engaging newspaper copy but vacant properties are used as store of value and leaving them empty rather than fitting them out is a way of avoiding taxes. A similar misallocation of capital can also be said to apply to some London property investments. China, in contrast to, say, the UK, has many levers it can apply to stimulate its economy.

India is expected to have significant population growth in the future – good for productivity, whereas China’s population is expected to decline largely as a consequence of its previous ‘one-child policy’, observes Marshall-Lee. Economic reforms being undertaken in India will be good for growth as well as the low levels of personal debt. There is pent-up demand for consumer durables after an earlier slowdown. India still has pockets of debt and needs to clear out the infrastructure bottlenecks concentrated in the power sector.

For Marshall-Lee, the Philippines (significant working age population) is one of the most exciting areas of potential growth and its 15 years of de-gearing has laid the foundations for future growth.

The fiscal positions of emerging-market commodity-centric markets, such as Brazil and Russia, are rapidly deteriorating and are due a “painful reset”, comments Marshall-Lee. Brazil, now undergoing a credit crunch, had grown like a weed on China’s industrialisation. In addition, the potential change in Brazilian politics could accelerate austerity with pain for consumers and corporates, he observes.

Important Information