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Masterclass – Emerging Markets

The West vs. the Emerging Markets

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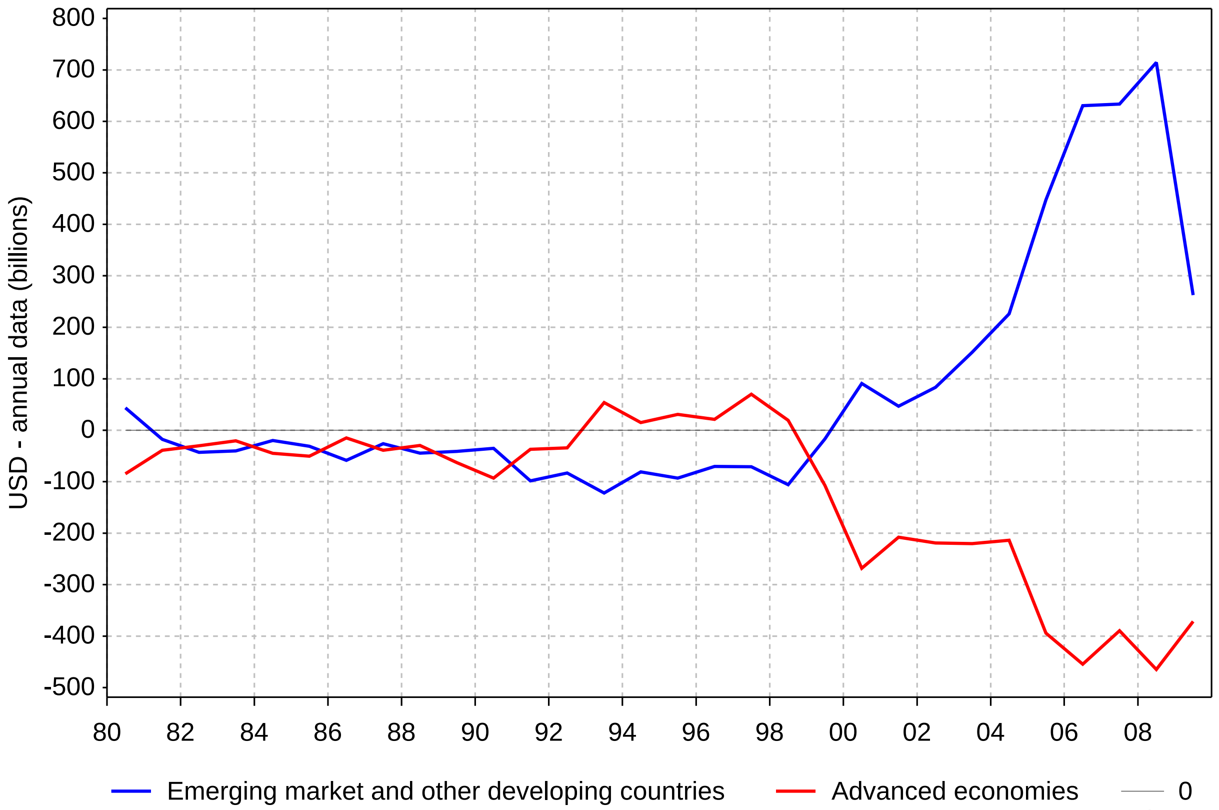
1a. Emerging Markets – Structural economic strength

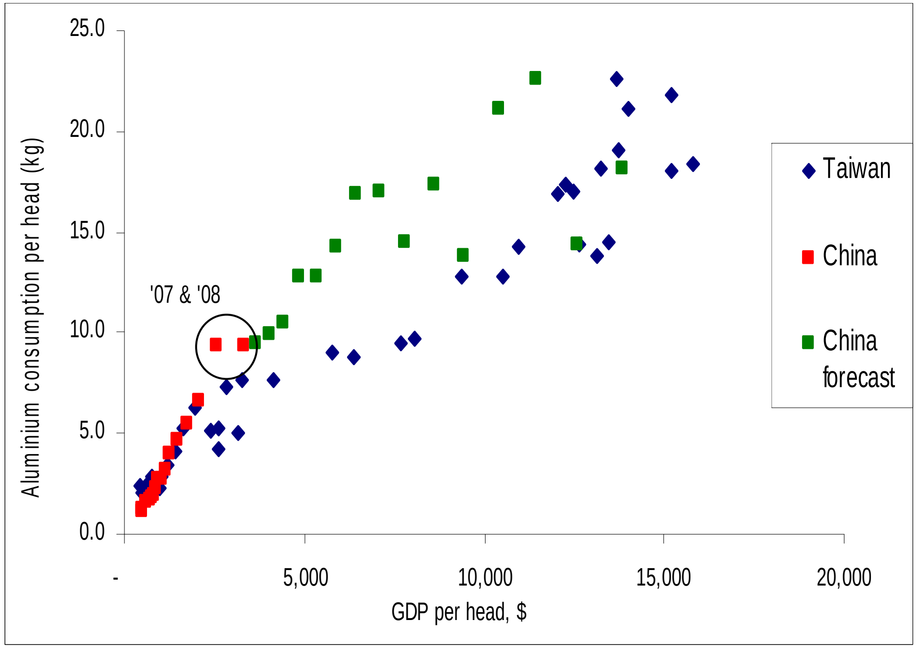


Source: Reuters EcoWin, IMF

Annual current account balance (in US$): Emerging Market vs. Advanced economies

1b. The Industrialisation Dynamic

Chinese pattern of industrialisation (1990 to today) vs. that of Taiwan (1970 – 2007) – shown with Aluminium consumption



1c. Emerging markets: Income Catch-up

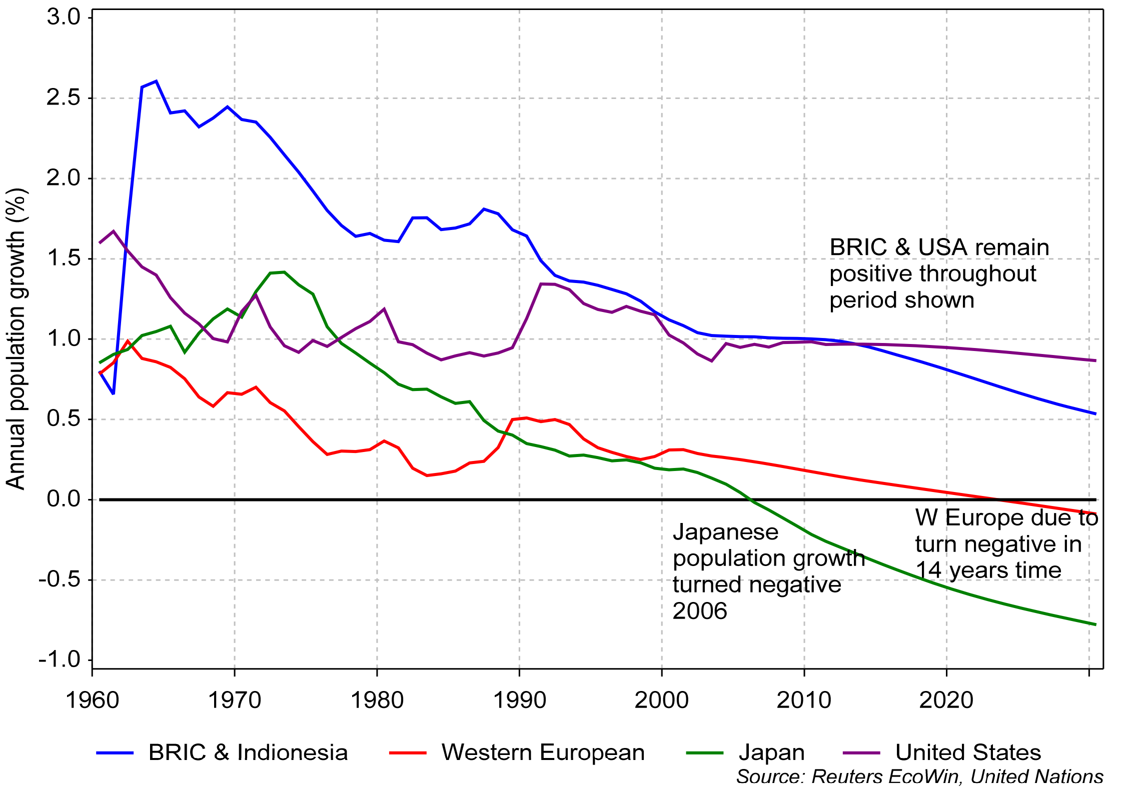
Long term average economic growth rates, shares of world economy, GDP per capita (US$) & share of world population

	1990 – 2010* (long term average real p.a. GDP growth)	Share of world economy on PPP basis	Share of world economy – nominal basis (US$)	GDP per capita (US$)	Share of world population
World GDP growth	3.47	100	100	6,910	100
United States	2.60	21.3	27.8	41,640	4.7
Euro area	1.84	15.01	22.4	32,130	4.9
G7	2.16	40.8	60.6	n/a	n/a
Newly Industrialised Asia**	5.36	3.64	3.2	21,032	1.3
Developing Asia*	7.73	22.70	n/a	n/a	52.9
China	9.93	10.8	5.0	1,700	20.4
India	6.47	4.6	1.8	730	18.0
Emerging & developing economies	4.93	n/a	n/a	n/a	84.8
Middle East	4.93	3.99	2.25	n/a	3.7

*Developing Asia = China & India & 14 other Asian countries; **Newly Industrialised Asia = HK, Taiwan, Singapore & S Korea

1d. EM – Better Demographic Profile

Total population growth (annual, %; 1960 to 2050)



Source: Reuters EcoWin, United Nations

2a. Preconditions for Relative Decline of leading world economic powers

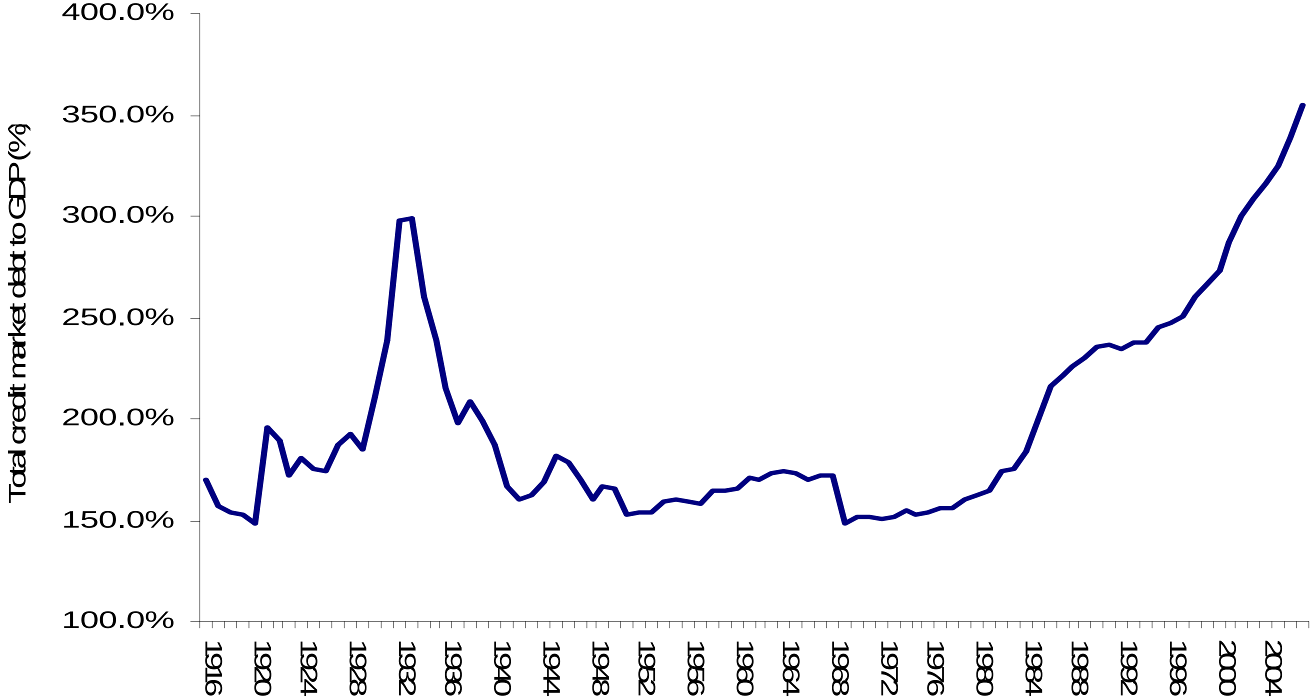
Kindleberger's preconditions

1. Overindebtedness
2. Foreign Policy overstretch – military overextension
3. Currency debasement
4. Energy dependency
5. Political corruption – "consolidation of groups looking after narrow parochial interests" Paul Kennedy
6. Financialisation of economy – deterioration of manufacturing base
7. Loss of technological leadership (?)

Source: CP Kindleberger, World Economic Primacy, 1500 - 1990

2b. Record Indebtedness (US & Western)

Total US debt as % of GDP (1916 – 2008)*



*includes financial sector debt,

Source:

2c. Shifting World Economic Primacy – a weakened USA (& west)

Rule of Thumb – World Economic Primacy; The 100 Year Cycle

Economic Primacy	
C15th	Italian City States
C16th	Portugal & Spain/Hapsburgs
C17th	United Provinces of Netherlands
C18th	France (?)
C19th	Great Britain
C20th	United States
C21st	???

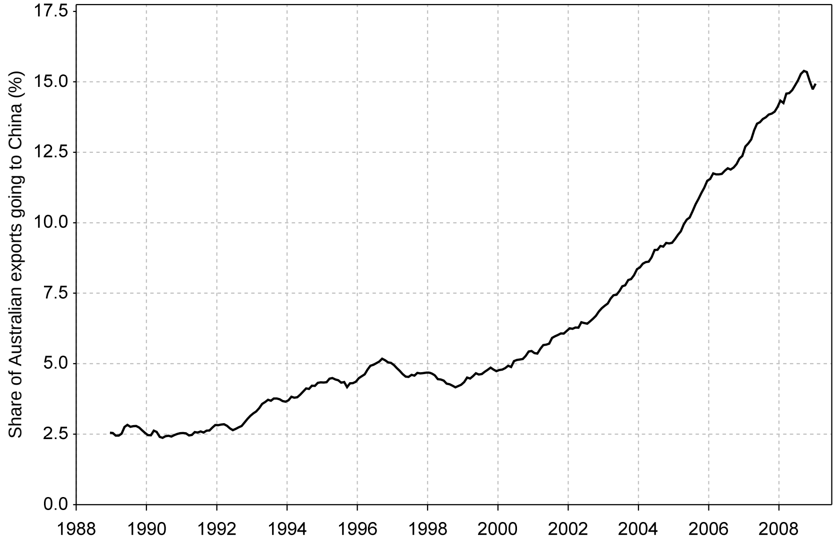
Source: Kindleberger

3a. China – Central to EM strength
Emerging 2nd Global Centre

Share of Brazilian exports to China
(% of total)

Source: Reuters EcoWin

Share of Australian exports to China
(% of total)



Source: Reuters EcoWin

3b. China's Growing Share of Commodity consumption (From G1 to G2)

	China's share of world consumption (% of total)		
	1998	2008	2020*
Copper	11%	28%	43%
Aluminium	11%	33%	45%
Oil	6%	9%	20%
Lead	9%	36%	n/a
Gold	8%	13%	n/a
Coal	29%	43%	50%+
Natural Gas	1%	3%	n/a

Source: Longview Economics, WMBS, BP world oil report

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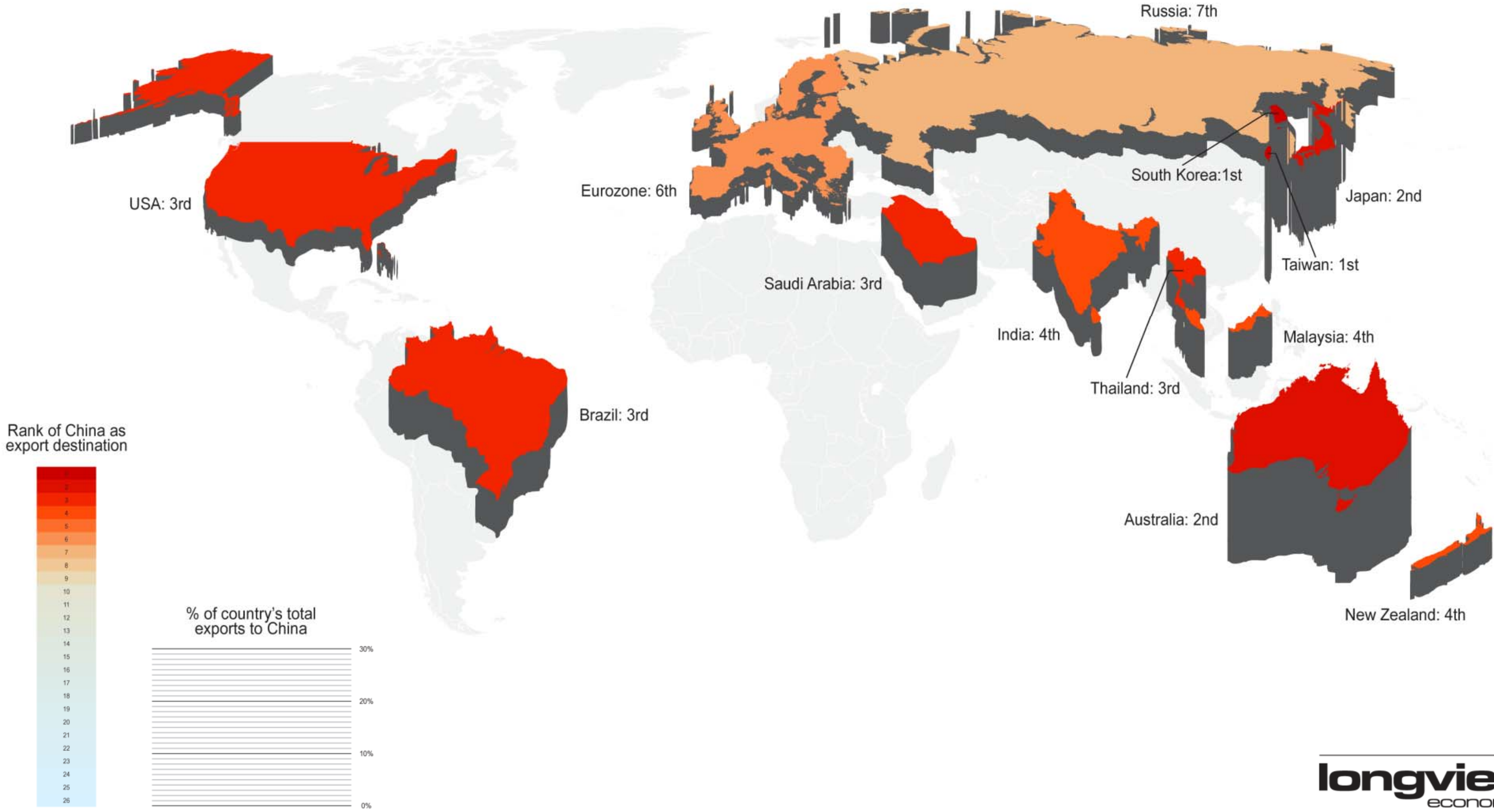
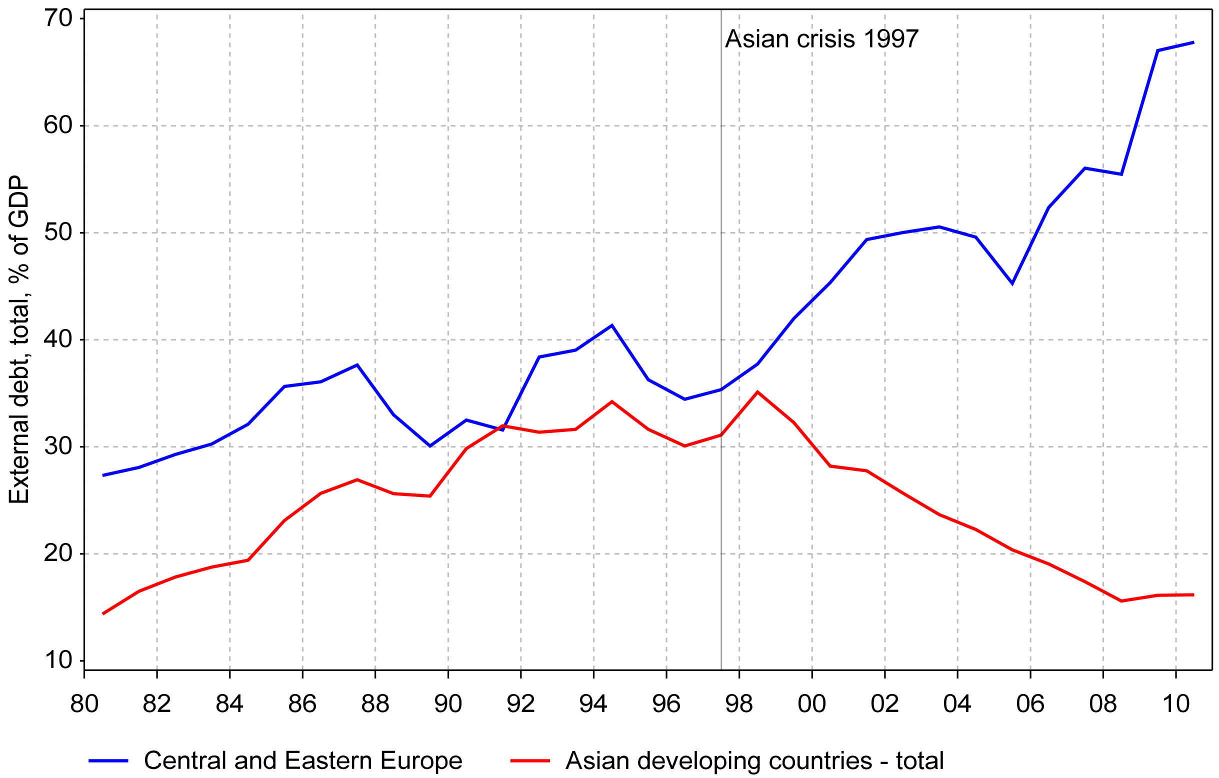
3c. China's Importance to Global exporters

EXPORTS TO CHINA IN 2008



4a. Eastern Europe – the exception

External Debt to GDP – Central & Eastern Europe vs. Asia (developing)



Source: Reuters EcoWin, IMF

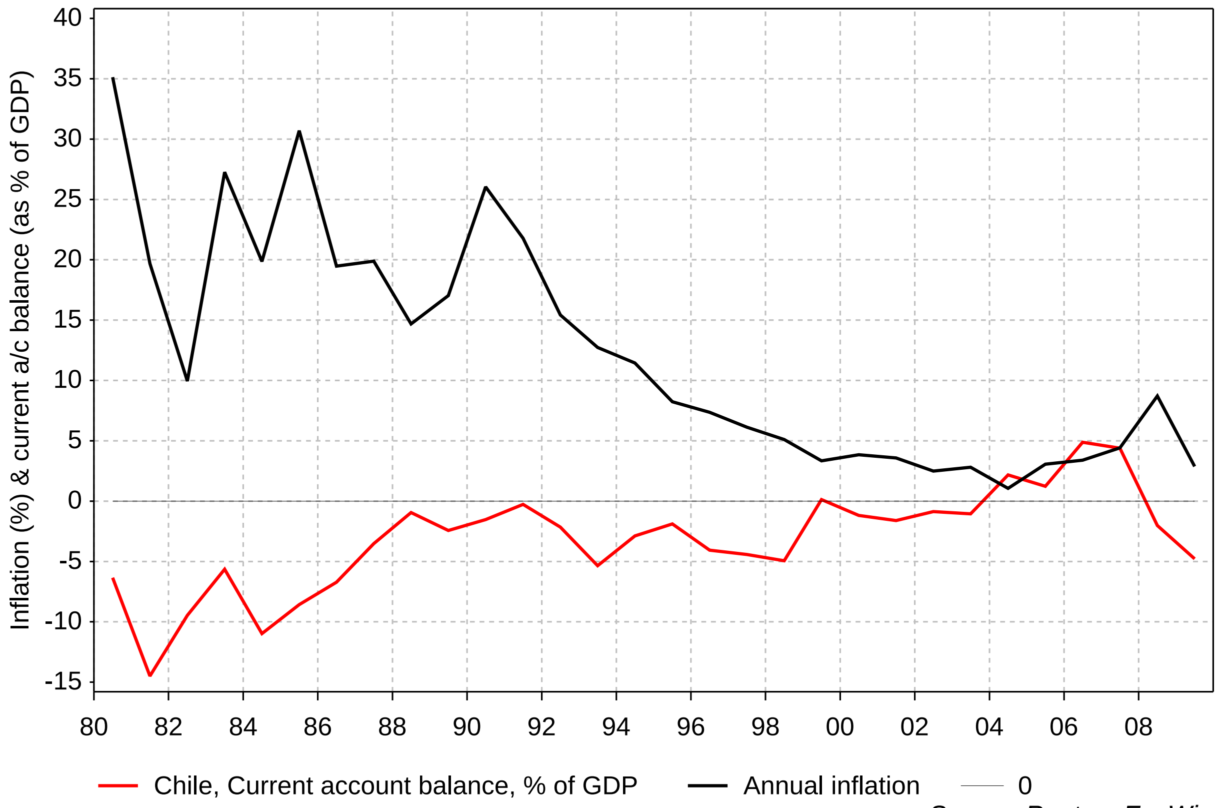
4b. Bulgaria: Unwinding a credit & asset price bubble

Household lending growth (Y-o-Y %)

Source: Reuters EcoWin

4c. Chile – Paragon of Virtue

Chilean current account balance as % of GDP & annual inflation (%): 1980 to current



Source: Reuters EcoWin

5a. Emerging Market Valuations – Attractive?

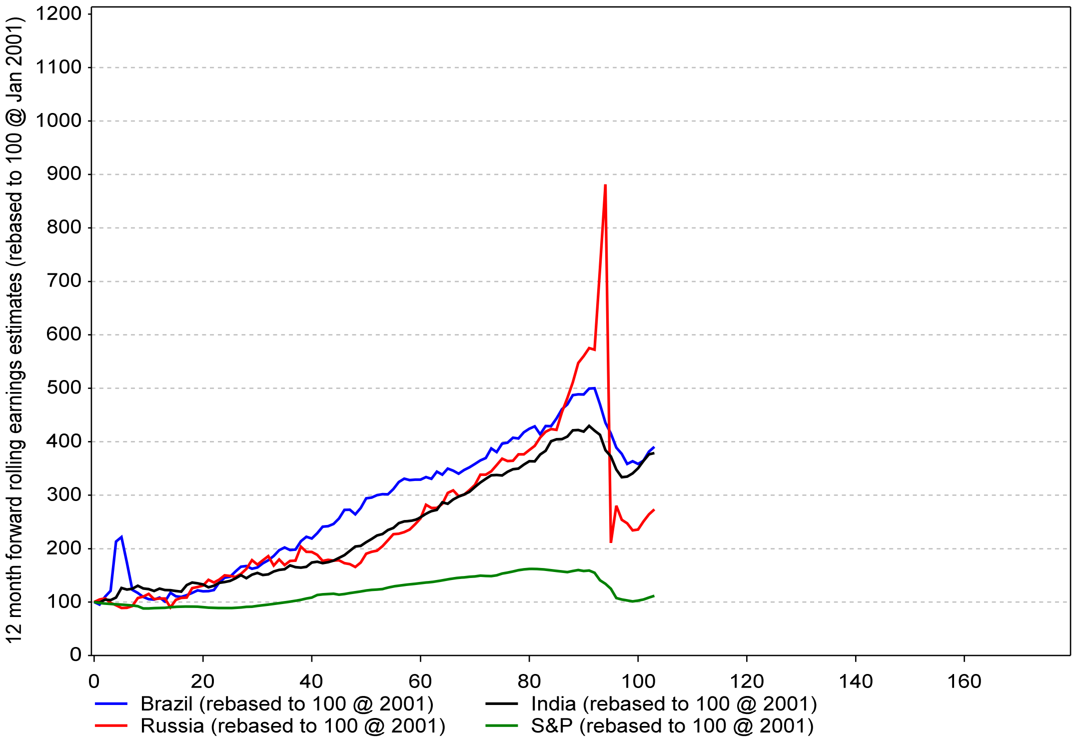
MSCI Emerging Market index country weightings & PERs (based on 12m forward consensus EPS)

Western B/marks	PER (12m fwd eps)		MSCI EM	PER (12m fwd EPS)	% index weighting
US	14.7		Israel	13.2	2.9
UK	13.3		Indonesia	14.4	1.8
Euro zone	13.4		Turkey	9.9	1.6
			Chile	17.0	1.4
MSCI EM	PER (12m fwd EPS)	% index weighting	Thailand	11.0	1.3
China	16.4	18.8	Poland	13.2	1.2
Brazil	12.1	15.3	Colombia	-	0.7
S Korea	12.5	13.1	Czech Republic	11.8	0.6
Taiwan	13.7	11.4	Eqypt	-	0.6
South Africa	12.7	7.2	Hungary	9.7	0.6
India	16.4	7.0	Peru	11.2	0.6
Russia	7.3	5.7	Phillippines	13.6	0.5
Mexico	14.7	4.7	Morocco	-	0.3
Malaysia	16.3	2.9			

Source: Longview Economics, JCF Aggregates; Ecowin

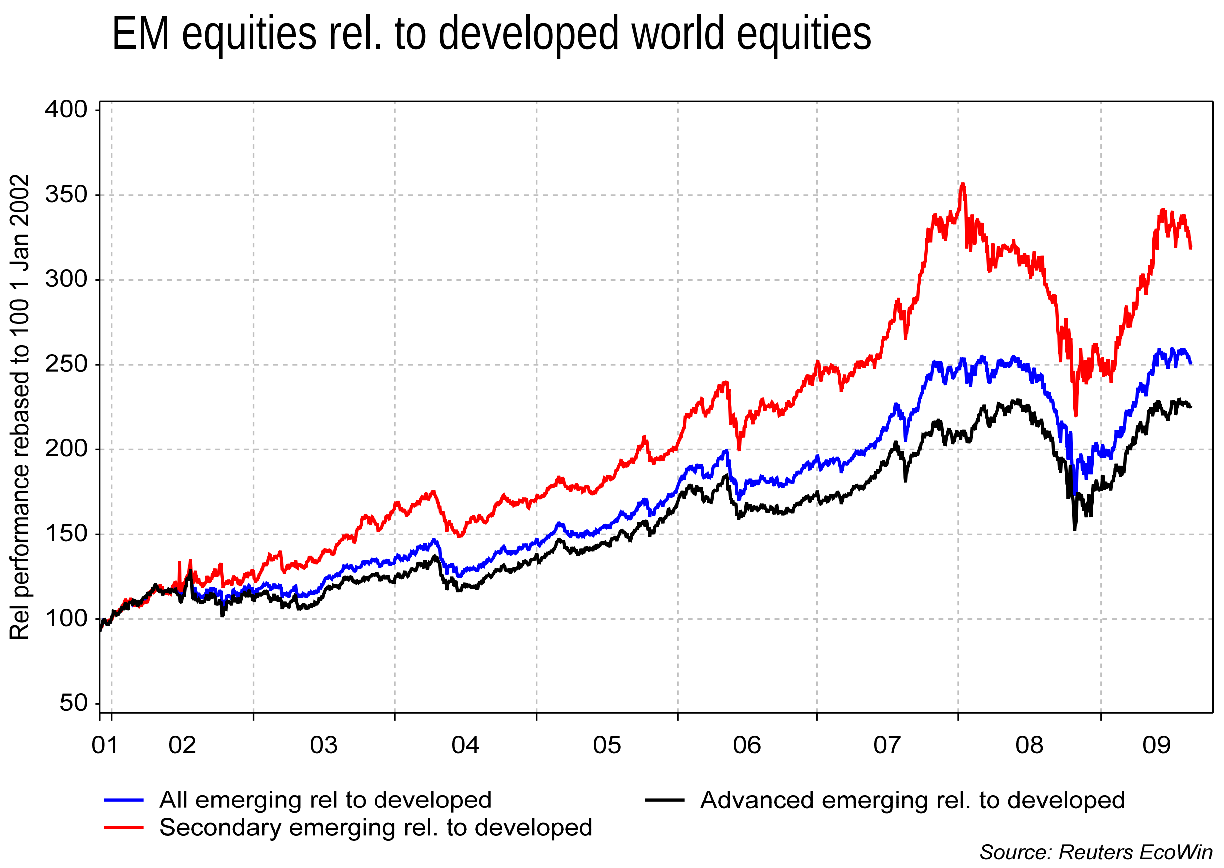
Outlook for EM Earnings (vs. S&P earnings)

Consensus Earnings growth (2001 to current) – Brazil, India & Russia (benchmarked against S&P EPS growth)



Source: Reuters EcoWin

MSCI Emerging Markets vs. Developed Equity markets



Conclusion

- Emerging markets – faster economic growth
- EM – driven by industrialisation & Income catch-up
- Emerging markets – structurally strong
- West – structurally weakened
- Small share of world GDP; large share of world population
- China – increasingly significant global trading partner
- Valuations – attractive?

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