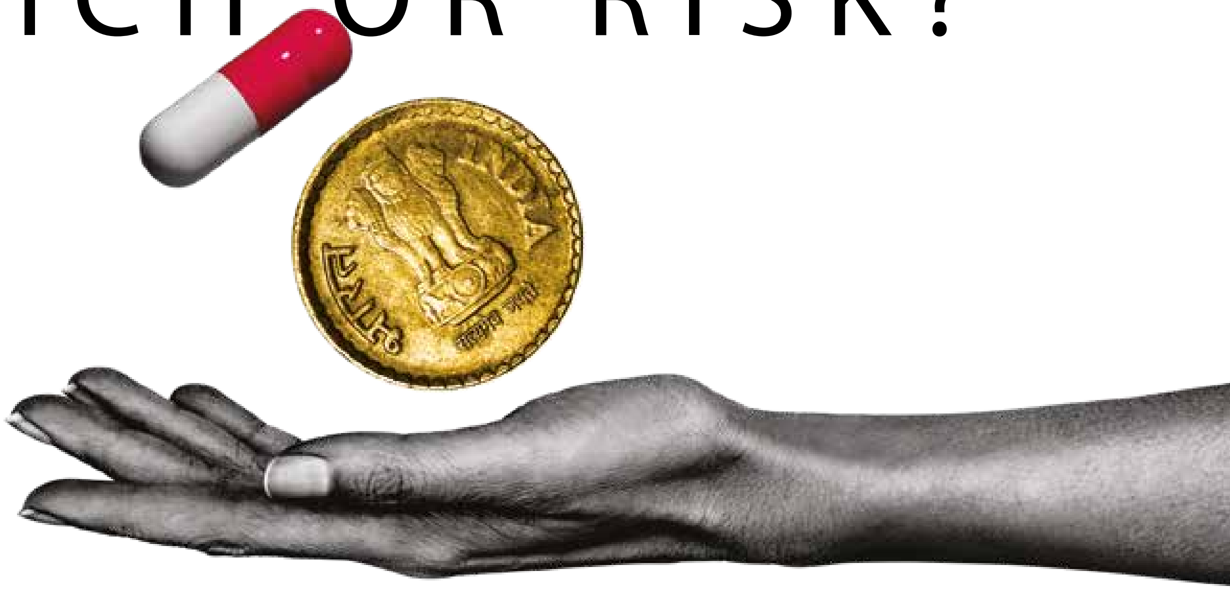
RICH OR RISK?



CHANGING ECONOMIC CONDITIONS HAVE GIVEN EMERGING MARKETS UNIQUE GROWTH POTENTIAL BUT ALSO EXPOSED THEM TO RISKS

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Most research indicates that there are positive expectations for emerging markets. Stimulus with monetary and fiscal policies worldwide by central banks and governments should support global trade. On the other side, emerging markets as a whole experienced fewer economic stimulus programmes but their economies stabilised faster. Emerging markets present lower valuations, on average, compared to the developed countries, while simultaneously experiencing a higher growth rate. China's recovery after lockdown is progressing at a faster pace compared to the rest of the world, and it looks like the country has managed its fight against the coronavirus well.

Research also points to a lower USD, which is usually good for emerging markets. Nevertheless, in uncertain or stressful times, capital usually flows towards the US. With the exception of the election period and any potential time spent recounting votes, a stronger USD in the mid-term means we should look for which emerging market countries can handle this environment better.

Overall, emerging markets are more resilient to external shocks and crises than in the past. This does not mean, however, that all of them have a great outlook.
We have to consider the debt burden of emerging countries – and companies – to see which countries have a lower debt to GDP ratio and which ones have better refinancing conditions.

It is still assumed that emerging markets are driven by commodities, but we have to differentiate. Some countries benefit from higher commodity prices, and some do not. Within commodities, we can differentiate between soft and hard commodities and energy. The USD influences commodity prices, but it depends which cycle we are in. Different asset classes can move in the same direction as the USD, against textbook theories. The interactions and correlations are complex.

EMERGING CHANGES

Some emerging market countries need time to develop and adopt legal rights to gain investor confidence and attract capital flows.
I am convinced that this long-term goal will be achieved by some of the players. With the trade war between China and the USA, both countries have to find ways to handle access to technology and build up a new value chain to compensate for the relocations. However, they are each other's largest trading partner so they have to find political agreement.

A positive feature of emerging countries is that they have a younger demographic and a much larger middle-class base. This will continue to be a driver for consumption in future and will make them less dependent on exports. On the other side, we have to assess which sectors and topics this consumption will flow in. I can imagine that the performance dispersions will be wide, not only from country to country but also from sector to sector.
IT and BTC platforms, healthcare, digital healthcare, consumer discretionary, gaming, online education and online entertainment should all benefit.

I think higher valuations are justified in the case of well-run companies that have strong balance sheets and little debt. Companies that are still growing have an even higher valuation in relative terms. Cheap valuations, where the catalyst is higher commodity prices, are also an opportunity. In any case, you have to be selective and an increased level of volatility should be expected globally.