



## Global Emerging Markets

### Monthly commentary

April, 2011

#### Market review

Emerging markets gained 3.1% in April, slightly lagging the overall MSCI World return. This was against a backdrop of disappointing economic data out of the US suggesting economic activity is slowing. We continued to see efforts by emerging markets policymakers to control inflation with several central banks continuing to tighten monetary policy during the month.

EMEA was the best region, gaining 3.8%, as some of the smaller markets like Hungary and Poland rallied over 10% on the back of a strong Euro. Asia followed with a 3.6% gain led by 7% gains in export intensive countries Taiwan and Korea. Latin America was flat on the month, with Peru falling 6% as left-wing presidential candidate Ollanta Humala unexpectedly won the first round of the presidential election.

At the sector level, consumer discretionary, staple and industrials did well with gains of 5-8%. Energy (-1%) was the main laggard, despite a 7% gain in oil prices over the month. Gold breached the \$1500 per oz level.

#### Market outlook

Another month of seemingly negative headlines and yet markets continued to rise in April! On April 18th S&P downgraded the long-term outlook for US debt to negative from stable, with the agency citing US policymakers' failure to attack long term fiscal stability. (Perhaps this kind of "shot across the bows" can begin to galvanise some action from US policymakers?). Europe saw credit rating cuts and an 80 billion Euro aid programme for Portugal; a credit rating cut for Ireland and an increasing consensus in the market that Greece will likely have to restructure its debt – despite having received an aid package one year ago. It seems that cheap and abundant money continues to support asset prices in equity, bond and commodity markets over this wall of worry.

The commodity sell off of recent days (writing in mid May) again highlights the markets' sensitivity to fears of potential slowdowns in economic growth be they in the West or the large emerging economies. Any sign of inflation in China seems to be met with the fear of the authorities having to "hard" land the economy. As mentioned last month we remain of the view that the Chinese authorities have the will and the tools to cool current inflation without crunching the economy. Since August 2010, China has let the Renminbi appreciate versus the US dollar, and whilst not at as fast a pace as some in Washington would like, this is another tool to help fight domestic inflation. Indeed several other Emerging economies (e.g. Brazil) have stepped back from the 2010 rhetoric about currency wars and let their currencies quietly appreciate as another weapon to fight their own inflation.

For the emerging world, any sustained sell off in commodity prices is likely to help reduce the immediate pressure on food and fuel price inflation (food and fuel often represent a much higher component of the inflation basket in EMs compared with developed economies). Even without this help, we would expect to see a peak in inflation expectations in many countries over the summer. However, this does not mean that central banks can stop tightening yet as strong growth in emerging economies necessitates interest rates moving up to normal levels.



## Strategy

The strategy is overweight Russia and Turkey, funded by under weights in South Africa, Mexico and Taiwan. There are more significant divergences at the sector level. The strategy is overweight the materials and consumer discretionary sectors and underweight consumer staples and energy.

In keeping with our core philosophy, we are seeking to maintain a fully invested, fully diversified exposure to the asset class. This does not mean we are looking to take risk out of the strategy, rather that we are trying to diversify that risk by country and sector.