

# Developing Markets Insight

## MARKET REVIEW

GEM equities remained friendless in September, with a decline of 3%, taking the quarterly and year to date losses to 17.9% and 15.5% respectively. This makes it the worst quarter since 2011, and the 7th worst in 101 quarters of benchmark existence.

Latin America continued its dismal performance, declining a further 7.7%, led by Brazil's 11.9% rout. The country was downgraded to "junk" by S&P, as it struggles to pass a budget to address its growing fiscal deficit. In the region most Central Banks are trying to control and moderate their currencies' depreciations. This month the Colombian peso and the Peruvian sol actually appreciated slightly.

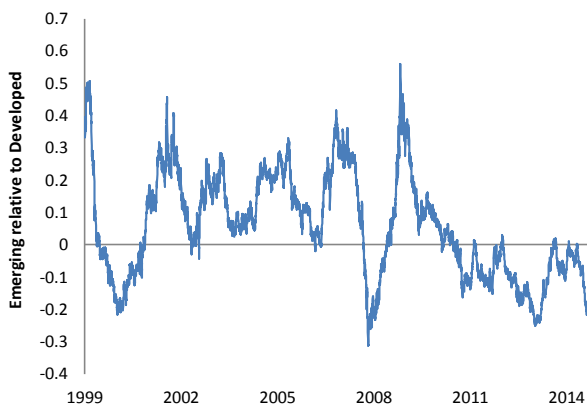
EMEA lost 5.1%, mainly attributable to South Africa's 6.7% slippage, and again the major factor being currency weakness. As a measure of this, one can observe the J P Morgan Emerging Market Currency Index (EMCI) which has lost 25% this year.

Asia was slightly more resilient, only losing 1.5%, supported by South Korea's 1.8% advance, and China generally trading sideways, after its substantial fall.

## STICK WITH THE U.S.?

Developing market equities is currently not a well-liked asset class. The last few years have seen poor performance relative to developed markets (which are dominated by the US).

12 month relative performance: MSCI EM vs MSCI Developed (USD NDTR)

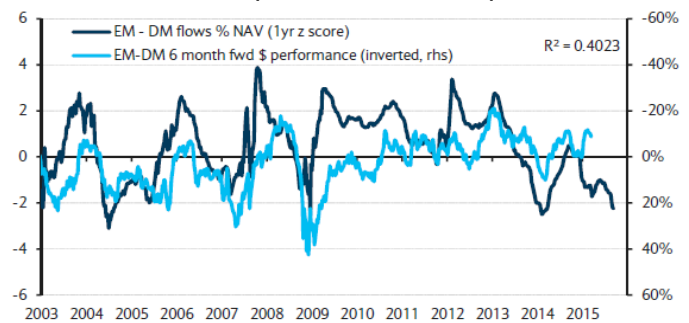


Source: Bloomberg

However, as we can see from the chart above, that performance versus developed markets is at levels where we have seen a reversal in the past.

Some interesting work done by Barclays looks at fund flows in both asset classes. The difference between flows to EM and DM is at extreme levels, only seen four times before in the last 12 years. On each previous occasion, emerging markets have subsequently outperformed developed by a sensible margin.

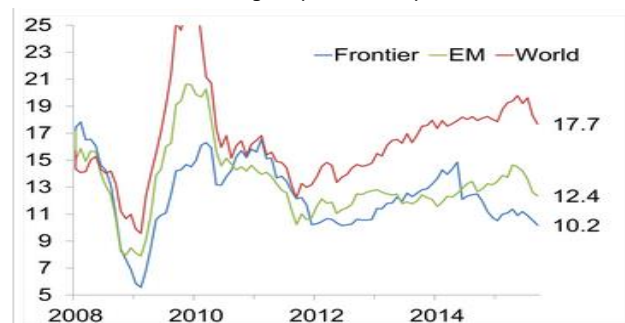
Fund flow to EM equities and forward relative performance



Source: EPFR, MSCI, Barclays Research

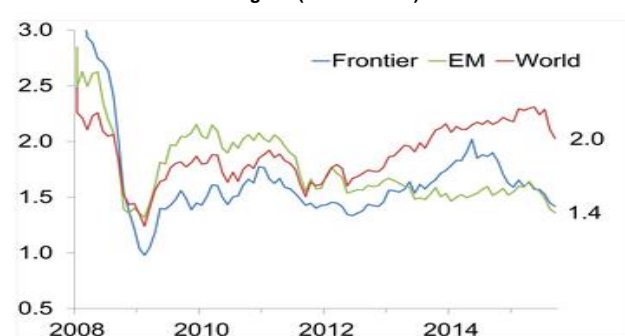
If we turn to valuation, then both trailing PE and PB look reasonable. We are not at the crisis levels seen post-Lehmans but are looking much better relative to developed markets so perhaps it is not unreasonable to find some support here.

Trailing PE (MSCI indices)



Source: Datastream

Trailing PB (MSCI indices)



Source: Datastream

There are 243 entities that make up developing markets. The likelihood of economic stress within this large sample is high but economic fundamentals are diverse and resorting to generalities can be a mistake. Even within difficult markets or sectors there can be companies that are doing well. We retain our selective, stock specific approach in these challenging times.

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