

DEVELOPING MARKETS INSIGHT

5th September 2018

Market summary

August saw a return to the negative tone which has prevailed in much of 2018, with a decline of 2.7%. Considering the 23 trading days, 14 were in negative territory. The principal cause of the weakness was currency depreciation, versus US dollar in a handful of countries.

MSCI Emerging Asia was largely untroubled, registering a backtrack of 0.8%. Only two of its constituents retreated: Pakistan and China falling 6% and 3.8% respectively. The latter saw currency volatility, prompting government intervention to halt the renminbi's slide. It has depreciated 4.9% this year, over concerns regarding trade wars. The Philippines was the best market, adding 2.5%, as the ASEAN underperformers from the beginning of the year have started to see money rotating into them.

EMEA lost 7.7%, its worst month since May 2016. Turkey plummeted 29%, thanks to a 34.9% slump in the lira. The market has been spooked by the Turkish Central Bank's apparent reluctance to raise interest rates sufficiently to combat inflation. It was the worst month since the financial crisis of 2008. A similar, albeit less dramatic, situation was repeated in South Africa, where the market stumbled 10% because of an 11.9% rand depreciation. Egypt managed a gain of 3%, helped by the announcement of prospective privatisations of state-run housing and tobacco companies.

Latin America was the worst region, shedding 8.4%, all markets were negative, with Brazil being the worst, losing 11.3%, including a currency rout of 9.7%. The country continues to be beset by concerns over the upcoming presidential elections. There was some relief at the month end, with a court ruling that former president Lula could not stand, owing to his imprisonment. Mexico was the relative winner, only losing 3.2%. There was expectation of a revised NAFTA deal with USA.

The worst sector was Utilities, down 6.1%, as the Brazilian Electricity Sector gave back recent gains. The best sector was Health Care, up 3.3%, boosted by Pharmaceuticals.

Currency weakness

August witnessed some exceptionally large currency depreciations. For background it needs to be remembered that emerging market currencies were strong in 2017, advancing 11.4% against the US dollar, as measured by the MSCI Emerging Currency Index. This year has been different, with US Federal Reserve tightening and Trump's growth policies boosting the greenback and leading to a 5% slippage in the Index. The two most dramatic losers have been the Turkish lira and the Argentine peso, which have plummeted 42% and 50% (both year to date) respectively against the US dollar. A common feature to both countries has been a reluctance to adopt difficult policies to tackle problems, because both governments had an eye on elections.

Turkey went to the polls in June, returning President Erdogan. He had allowed excess credit to buoy the economy to keep the electorate on side. President Macri in Argentina is seeking re-election in October 2019. He has therefore been pursuing a measured approach to curbing inflation and removing subsidies. The tightening of global credit sentiment has blown away this strategy, leaving the International Monetary Fund calling the shots in Buenos Aires. The most likely outcome in both cases will be elevated interest rates (although Turkey has shown considerably less vigour in hiking, compared to Argentina), high inflation and a recession to clear the imbalances. The perils of economic populism using other people's money in a different currency has always proven to be a toxic combination.

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4th July 2018

Big Brother is watching (out for) you

For better or worse, governments around the world are exerting their influence in the internet space or using technology to influence our lives.

- On 31 Aug 2018, China's top legislators passed an e-commerce law aimed at improving regulation over the e-commerce market, which will take effect on 1 Jan 2019. The law requires that e-commerce platforms bear the responsibility to ensure the quality and authenticity of products, especially those that affect the lives and health of consumers. The law also noted consumers' privacy and rights to complain, and operators must follow related laws and regulations when collecting and using consumers' personal data.

- Monday (2nd September) is the first day that French schoolchildren under 15 cannot use their mobile phones at any point during the school day, thanks to a new nationwide law. The ban, passed in July following a campaign pledge made by French President Emmanuel Macron, will affect elementary and junior high schools across the country as they return from the summer break. The new law, which went into effect on August 5, bans all types of mobile phones, as well as tablets and smartwatches. While a ban on mobile phones during class hours was already in place since 2010, the new law extends to breaks and mealtimes.

- China will limit videogame releases and set new restrictions on play time for youths, further punishing companies in the world's largest game market. The action followed increasing government scrutiny of videogames in China, which have been criticized in state media for graphic violent content as well as the amount of time young people spend playing them. The new measures were announced by China's Ministry of Education as part of a broader plan to combat vision problems among schoolchildren and adolescents. The new restrictions reflect officials' concerns that youths are spending too many hours playing videogames and neglecting their studies, analysts say.

- The US Army is taking wireless recharging to new heights, by using lasers to power small drones in mid-air. Drones have proven valuable to the military for intelligence gathering, but they are incredibly power-hungry, meaning their flying time is limited to half an hour or less. Now the US Army's Communications-Electronics Research, Development and Engineering Center based in Maryland are developing a power beaming system with a combination of modern lasers and efficient photovoltaic cells which would, in theory at least, mean the drones never have to land making cheap 24-hour surveillance easily achievable.

- One in every four schools in China is quietly testing a powerful machine that uses artificial intelligence to mark pupils' work, according to scientists involved in the government programme. The technology is designed to understand the general logic and meaning of the text and make a reasonable, human-like judgment about the essay's overall quality. It then grades the work, adding recommended improvements in areas such as writing style, structure and theme. The technology, which is being used in around 60,000 schools, is supposed to "think" more deeply and do more than a standard spellchecker. For instance, if a paragraph starts trailing off topic, the computer would mark it down. Scientists insist the technology is designed to assist, rather than replace, human teachers. It could help to reduce the amount of time teachers spend on grading essays and help them avoid inconsistencies caused by human errors such as lapses in attention or unconscious bias. It could also help more students, especially those in remote areas with limited access to resources, improve their writing skills more quickly. The machine is similar to the e-rater, an automated system used by the Education Testing Service in the US to grade prospective postgraduate students' essays.

For a long time 'tech' was able to follow a trajectory largely unhindered by the state. As investors we need to be increasingly aware of the impact of government policy in these areas.

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