

Building with BRICs and more too

Construct an emerging market portfolio

In our last issue, we provided a chart showing the overseas exposure of FTSE 100 companies. This time, Graham Spooner, Investment Adviser, looks at ways of gaining exposure to emerging markets.

The four fastest growing and leading emerging markets are those of Brazil, Russia, India and China, commonly known as the BRIC countries. Their markets are built on strong fundamentals and growing consumer demand and there is a general view that these countries will grow in importance as contributors to the world economy in the years ahead. Recently, there have been two high profile events that have supported this view: Prudential's acquisition of AIG's Asian operations and Anthony Bolton's (Fidelity's well respected fund manager) postponement of his retirement in order to launch a China investment trust, which is expected to start on 19 April.

Although emerging markets were impacted by the global financial crisis, a recent KPMG-backed survey suggests that emerging markets broke free of the recession quicker than developed markets. Statistics show that companies in the emerging universe increased acquisitions into developed markets in the second half of 2009 against a fall the other way. The table opposite shows the growth in the main indexes of emerging market countries since 2006. It's interesting to note that some countries flip between the top and the bottom of the table: a clear indicator of their potential for increased volatility.

Emerging markets are regarded as higher risk. However, they have proved popular in recent years with investors who are happy to take on that greater risk for the potential of greater reward. Please remember that past performance is not a reliable indicator of future performance and that the value of investments and the income from them can go down as well as up.

The easiest route to invest in these markets is via funds or ETFs. You can find out more about these types of investments on our website at www.share.com or in

	2006		2007		2008		2009	
Top three emerging market countries by annual return in sterling								
1	China	60.4%	Peru	91.1%	Morocco	23.1%	Brazil	103 %
2	Indonesia	52.4%	Brazil	76.5%	Colombia	3.7%	Indonesia	101.4%
3	Morocco	47.3%	Turkey	71%	Israel	-2%	Russia	81.8%
Bottom three emerging market countries by annual return in sterling								
1	Jordan	-39.3%	Argentina	-5.6%	Pakistan	-64%	Morocco	-15.7%
2	Turkey	-18.6%	Taiwan	6.5%	Russia	-63.8%	Czech	12.6%
3	Israel	-16.9%	Mexico	10.2%	India	-51%	Egypt	24.4%

Source: MSCI factsheet

The Fundholder. If you prefer to invest in shares, then you can also benefit from emerging markets by buying shares in some of the well-known or small, niche companies listed on the London Stock Exchange (LSE). You can do this in one of two ways: by buying shares in companies that operate exclusively in emerging markets or by buying shares in companies that are expanding into new markets.

Followers of emerging markets see the countries' economic success as a long-term story geared to the growth of the middle class, which brings with it an increase in internal consumer demand. For example, the middle-class population in Brazil is estimated to have risen by 30 million since 2003, boosting demand for white goods and luxury products — which in turn boosts demand for raw materials — and developing financial markets. Brazil could also benefit in the longer-term from its raised profile when it hosts the FIFA World Cup in 2014 and the Olympics in 2016. One beneficiary is maritime services group Ocean Wilson Holdings, which is listed on the LSE. It provides harbour & ocean towage, container terminal operations, ship building and support services in Brazil. The share price has

rebounded strongly over the past year leading to a market cap of around £320 million.

China has attracted most investor interest and there are a number of Chinese companies listed on the LSE as well as UK groups keen to break into this burgeoning market place. With China's annual GDP growth forecast to be around 10% over the next few years, a number of companies are prepared to face up to the challenges — which should not be underestimated — associated with gaining a foothold in China's markets in order to grab a share of the growth. One such company that features on our higher risk buy list is Hutchison China MediTech which is involved in developing, manufacturing and selling health products from its Hong Kong base into China. In their latest update the group reported a 25% rise in sales. Demand for health products in China is growing rapidly and this trend is set to continue.

Another successful share which highlights the spread of opportunities available is Asian Citrus, which is China's largest orange grower. Although not on our buy list its success is an example of the

classic growth story seen throughout the emerging regions. In this example, as standards of living improve, consumer spending grows (in this case on oranges) but consumption is still well below other countries and should therefore continue to grow. Output is set to grow (the trees are young) and earnings visibility will also grow (in this case, as the increasing number of supermarkets place contracts for the oranges).

With western economies faltering there has been a notable push by UK companies to try and tap into the emerging markets growth story, as indicated in trading statements during the recent reporting season. For example, AstraZeneca hopes to get a quarter of its revenue from emerging markets by 2014. Our preferred choice in the sector is GlaxoSmithKline; they achieved sales growth of 16% in emerging markets and are making a

strategic shift away from western markets. In the banking sector HSBC has refocused eastwards and the sector bellwether is Standard Chartered who generates 90% of its earnings from emerging markets.

Other companies on our preferred list include: Reckitt Benckiser who saw emerging markets sales rise by 19% to £388 million, compared to a 1% rise in Europe; Experian the credit checking group, who reported a 49% rise in third quarter revenue in Latin America and described business in the region as being robust (they also announced a new joint venture in India); and Vodafone who enjoyed a 16% rise in revenue in Asia and the Middle East. Other companies looking to expand eastwards include Aviva, Tesco, G4S, & Rolls Royce.

Investing in emerging markets is higher risk than investing in developed markets and ventures into new countries are not always

a success as evidenced by Kingfisher, whose move into China turned into a loss-making venture which has had to be restructured. That said, our main theme for 2010 has been to go overweight on companies that have exposure to overseas earnings and it's likely that an increasing amount of that will be in emerging markets. Yes, that may increase the risk and there will be setbacks, but on balance we think it's worth taking if you're an investor who is happy to include high-risk investments in your portfolio as part of your investment strategy.

If you want more information on any of the companies mentioned or on emerging markets in general just contact our Advice team on 01296 41 43 45 or visit our website at www.share.com.

