How to Get Your Share Of Emerging Markets

Looking beyond established markets can yield success, writes **Colin Bloodworth**

Japan has a 9 percent weighting in the MSCI Developed Markets Index. AFP Photo/Kazuhiro Nogi

It is widely accepted that if you want your savings to grow in real terms, a portion should be allocated to the world's capital markets. Governments do not make money — they spend it. While your money in the bank may be feeding the capital markets, your share of the proceeds at current interest rates will not even keep up with inflation. So for your money to grow, you have to invest.

How do you access and allocate savings to the world's stock markets? It's not too difficult as you can buy shares directly through a stockbroker or enter the markets through managed funds, life insurance products and regular savings plans.

But how do you determine which markets to buy into? Should you buy global stocks, US stocks or local stocks? Up to a few decades ago there were limited opportunities to invest in freely traded stocks outside the US, Europe, Japan and a few Commonwealth countries. These are still considered the major markets of today. Gradually, however, a number of other countries came on to the scene, realizing that stock markets were a means of attracting capital and increasing prosperity. These became known as "emerging markets."

More recently, stock markets have been established in many more countries, some of which might raise the eyebrows of experienced investors. These have become known as "frontier markets."

Major markets

The biggest market in the world in terms of capitalization is, by a large margin, the United States. It is the home of eight out of 10 of the largest companies in the world, some of which, including Apple, Exxon, General Electric and Chevron, are worth more than the entire stock market capitalizations of smaller countries.

Some companies also hold cash reserves greater than those of many sovereign countries. If you invest in a global major market fund today you are likely to find yourself with a spread of countries close to that of the MSCI Developed Markets Index. The investment would be

The US share market has the world's highest capitalization. AFP Photo/Stan Honda

allocated roughly in the following proportions: US (52 percent), UK (10 percent), Japan (9 percent), Canada (5 percent), Australia (4 percent) with the remaining 20 percent spread around European countries, New Zealand and Singapore and Hong Kong.

Emerging markets

A fund following the MSCI Emerging Markets Index today would have roughly the following spread: China (18 percent), South Korea (15 percent), Brazil (12 percent), Taiwan (10 percent) and South Africa (8 percent) with the remainder (37 percent) allocated to a dozen or so countries including India, Indonesia, Malaysia, Mexico, Russia and Thailand. Some fund managers try to "beat the index" with different focuses.

One manager coined the acronym BRIC (Brazil, Russia, India and China) and committed investment to these four rising stars alone. Other funds focus on specific regions such as Asia, Latin America and Africa. Others again concentrate on single country funds.

Frontier markets

This is a fairly recent development and shows how quickly the rest of the world is trying to catch up. Frontier markets are not sufficiently mature to be fully considered emerging markets but some of them are rapidly improving access and liquidity and can expect to become more attractive to investors as well as to speculators.

At the same time the line between emerging and frontier will be more difficult to draw. The leaders in this field are Kuwait, Qatar and the United Arab Emirates but there are some interesting participants such as Kenya, Bangladesh, Pakistan, Romania, Serbia, Sri Lanka and Vietnam. Note that Cuba and North Korea, the last true bastions of communism, are not included as they have continued to resist the capitalist model.

One fund manager is offering single-country funds for Mongolia and Iraq. They may appeal mostly to investors who are looking for excitement, but there are some very strong fundamentals. Iraq, for example, is sitting on the world's fifth largest oil reserves and its oil is very cheap to extract. It does not need to incur the huge costs of deep water drilling, extracting from tar sands or the process of fracking.

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