

September 2017



Emerging Markets Outlook

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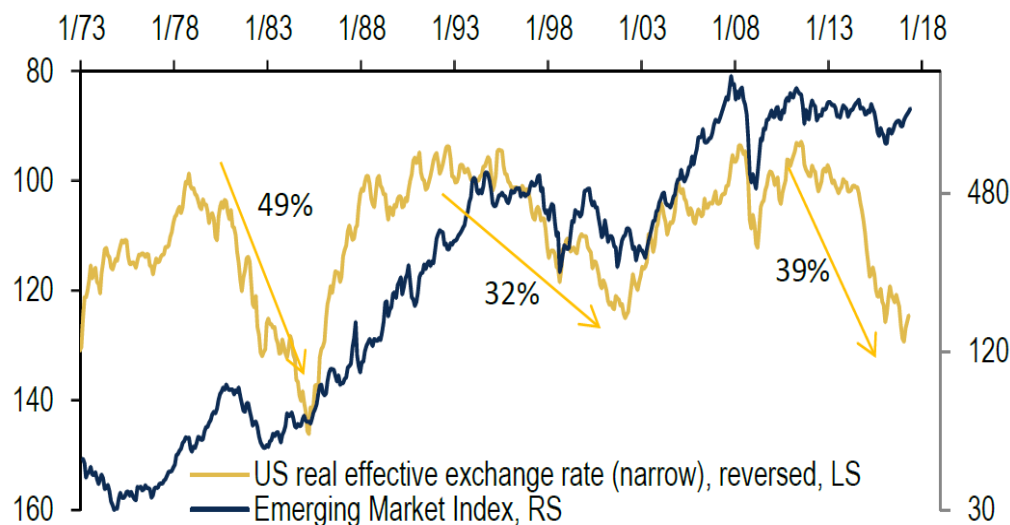
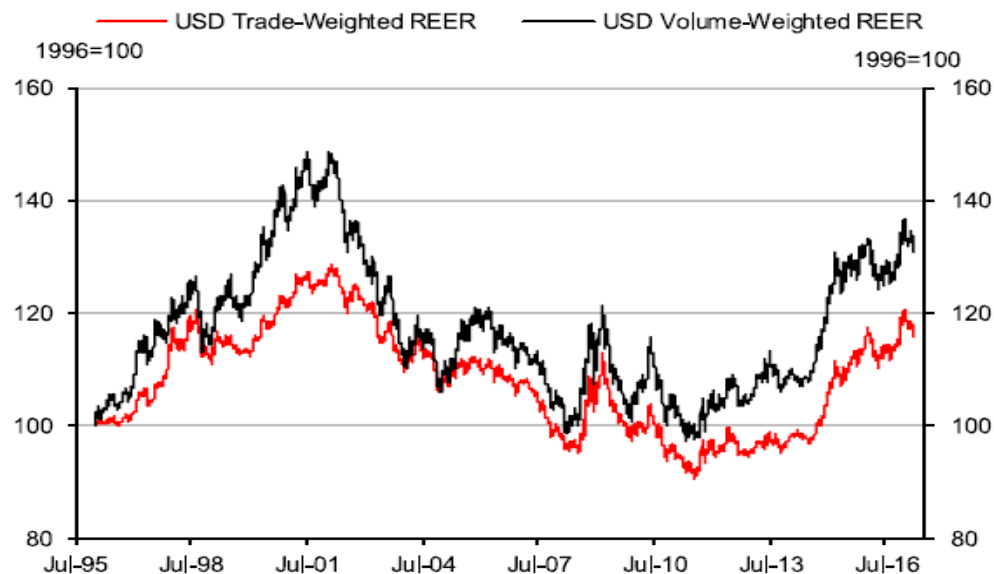


Growth Driving EM: Headwinds Abate



Global Fears: The U.S. dollar fully valued?

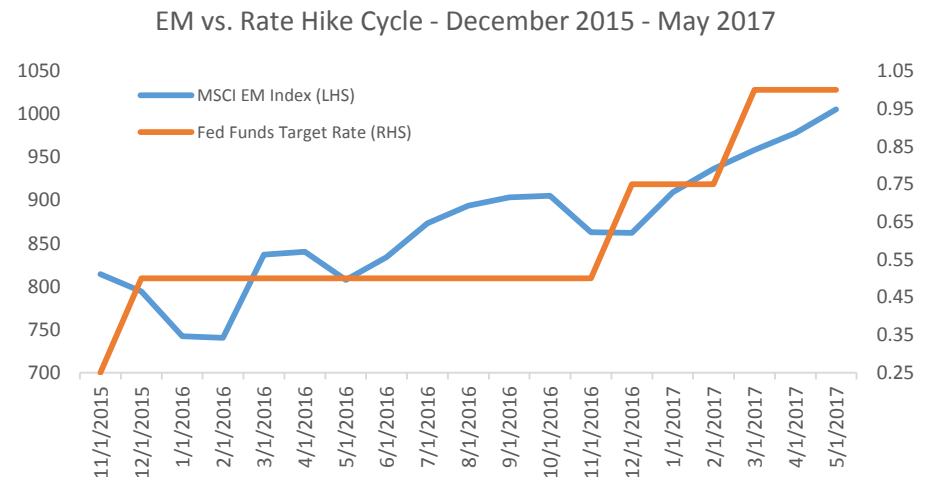
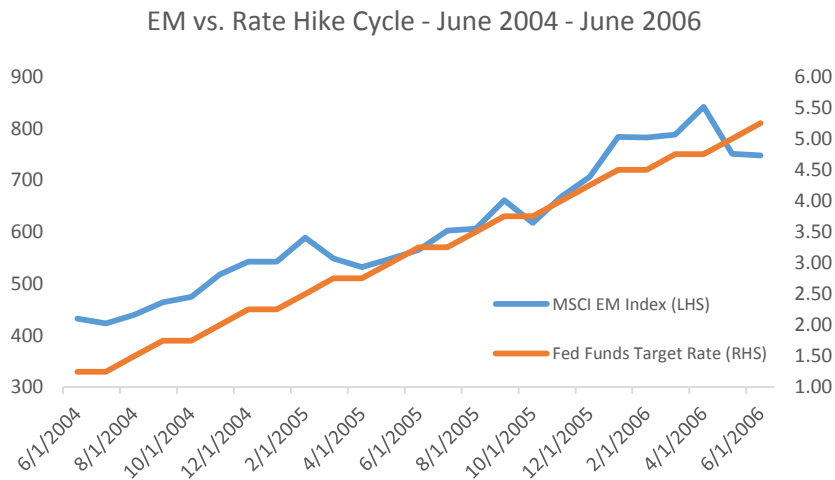
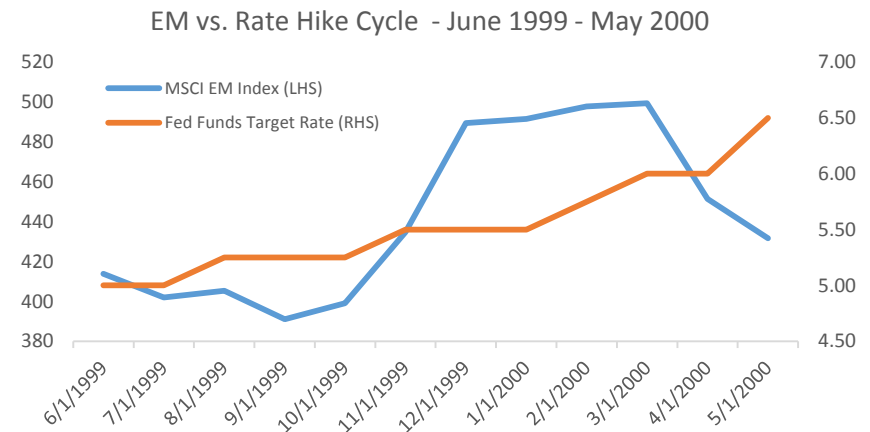
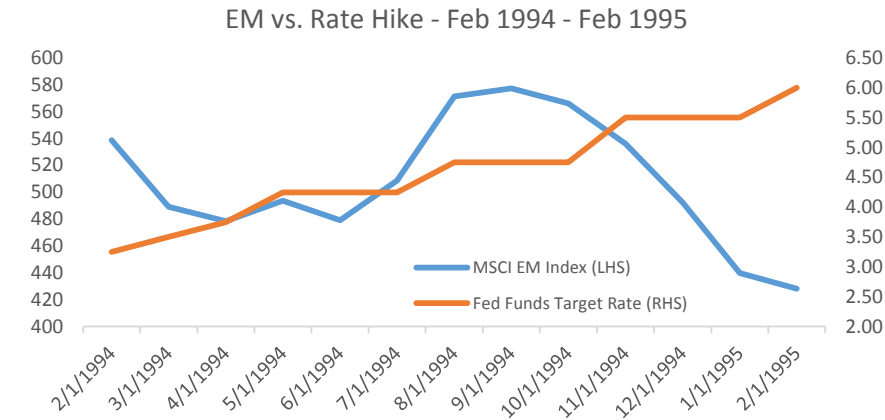
- The U.S. dollar has strengthened 39% since 2011; in prior periods of dollar strength (most of the early 1980s and in 1997-1998), emerging markets were in crisis, but not this time around



Source BAML; HSBC. Data as of June 2017 (low chart) and March 2017 (upper chart).
See disclosures on page 2.

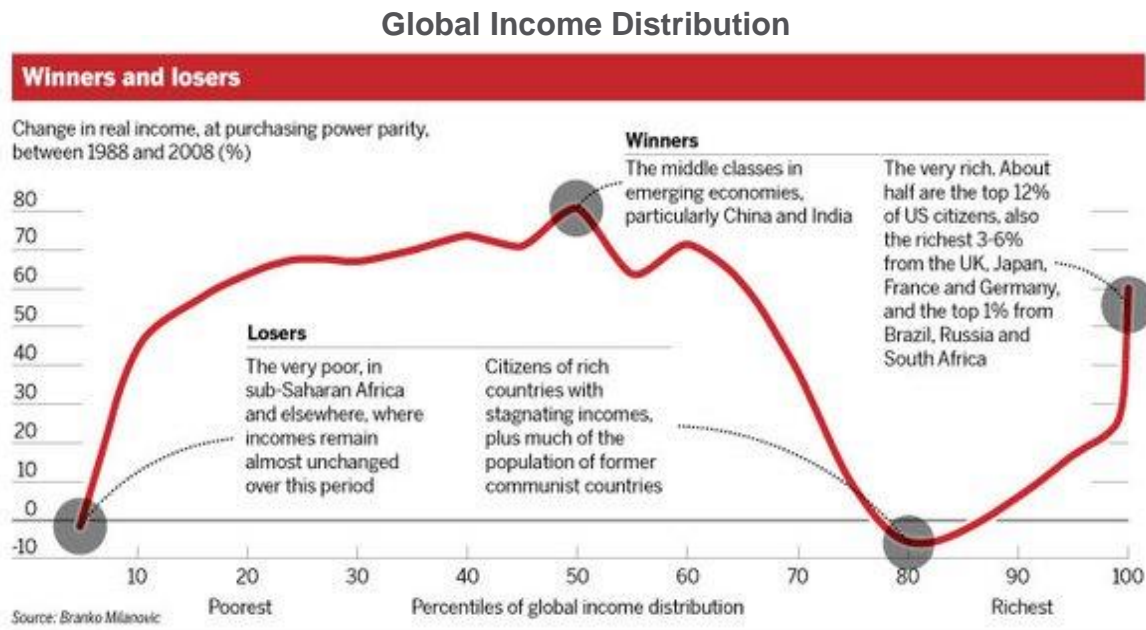
Global Fears: EM equity performance during U.S. rate hike cycles

- Emerging markets equity have historically reacted favorably during U.S. rate hike cycles

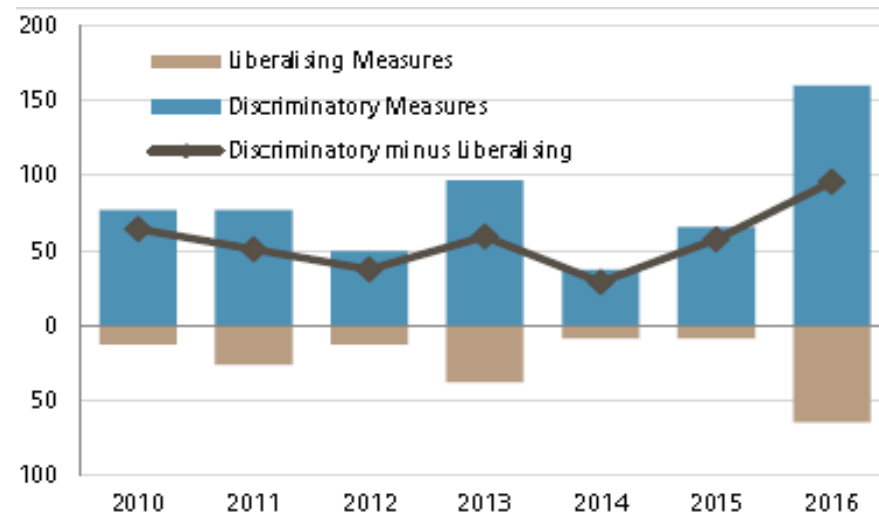


Source VanEck, Bloomberg.
See disclosures on page 2.

Global Fears: Populism and protectionism on the rise



- State aid is a key mechanism for trade discrimination
- Includes local procurement legislation, tax benefits for export and domestic industry subsidization, heightened regulatory standards, and public procurement discrimination
- Over the long haul, technology is a much bigger driver of trade than government policy
- Zero sum game – China steps into the vacuum

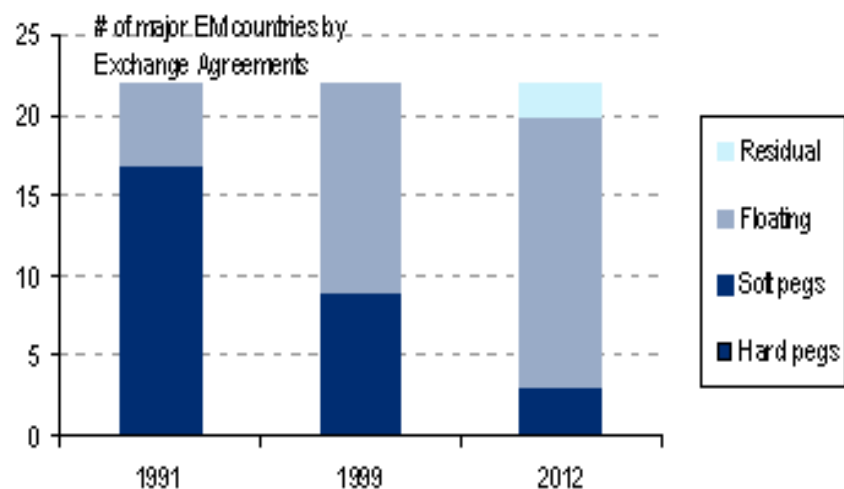


Source: Branko Milanovic (top chart). Merrill Lynch (bottom chart). Data as of December 31, 2016. See disclosures on page 2.

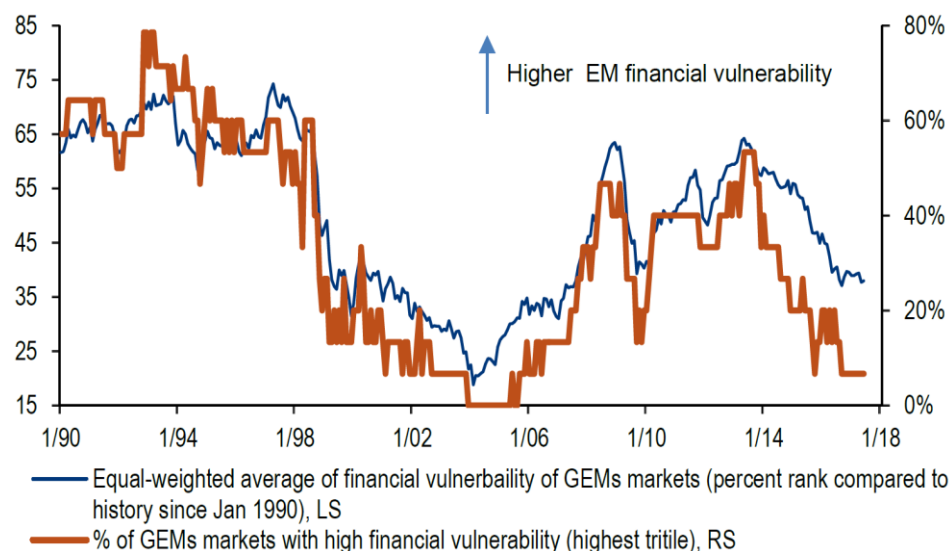
EM Macro: Emerging markets have less financial vulnerabilities

- Most emerging economies (with the exception of China) have floating currency exchange systems
- Currency flexibility is a natural progression from mercantilism and gives central banks more control over monetary policy
- Emerging economies are less vulnerable today due to major economic and financial reforms in the past decade
- External and fiscal accounts have significantly improved from the “taper tantrum” period

Number of EM countries by exchange agreements



Financial Vulnerability in EM

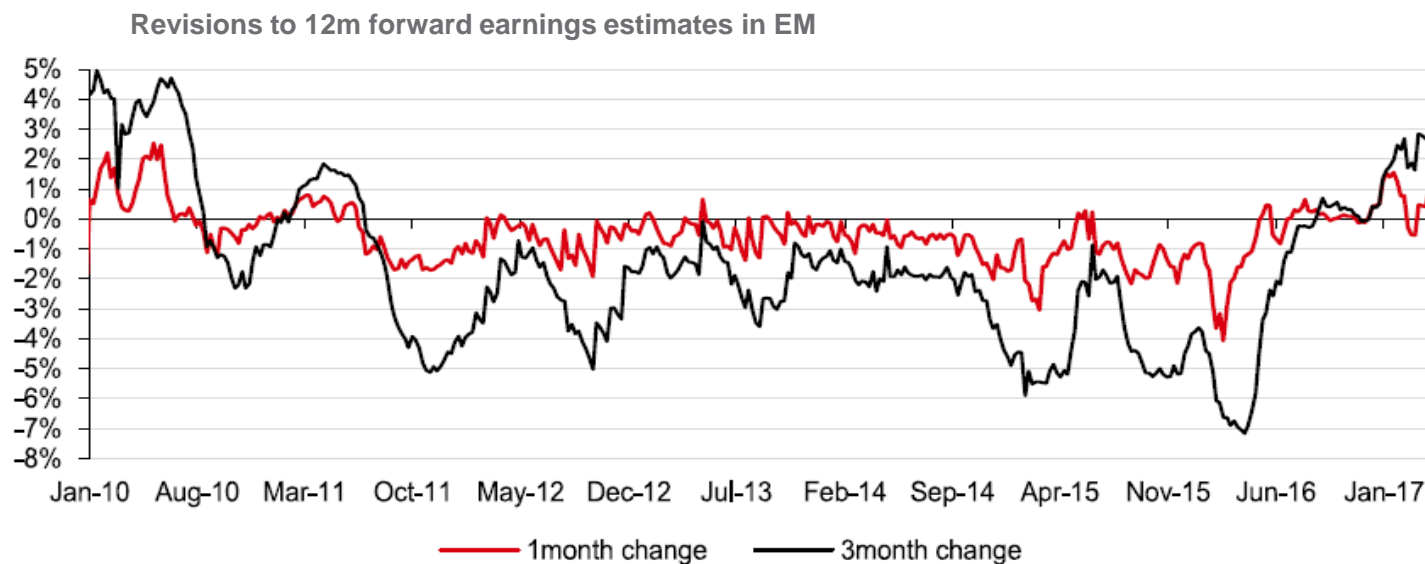


Source: UBS (left chart) and Merrill Lynch (right chart). Right: Chart Data as of June of 2017.
See disclosures on page 2.

EM Micro: EM companies' earnings are exceeding expectations



- Often wrong, but never in doubt; 2017 a rare example of analyst EPS growth optimism coming true? BAML research suggests yes.
- EM 12m forward earnings estimates revisions accelerate

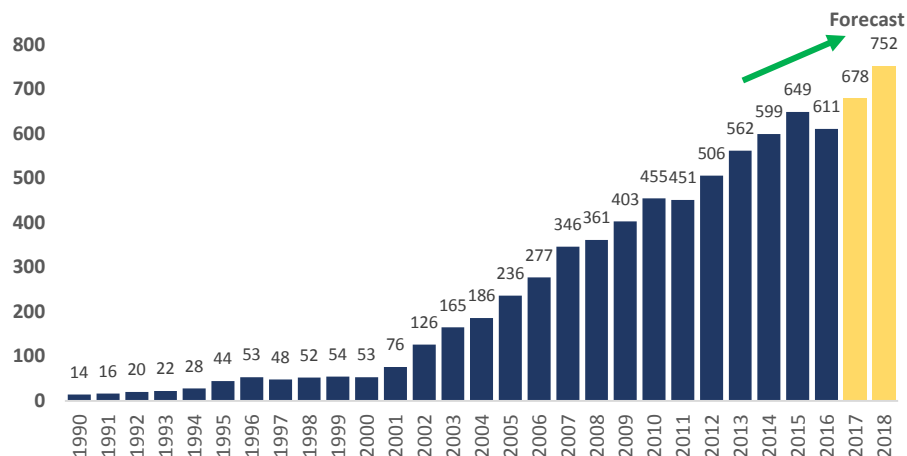


Source: BAML, HSBC. Data as of March 2017.
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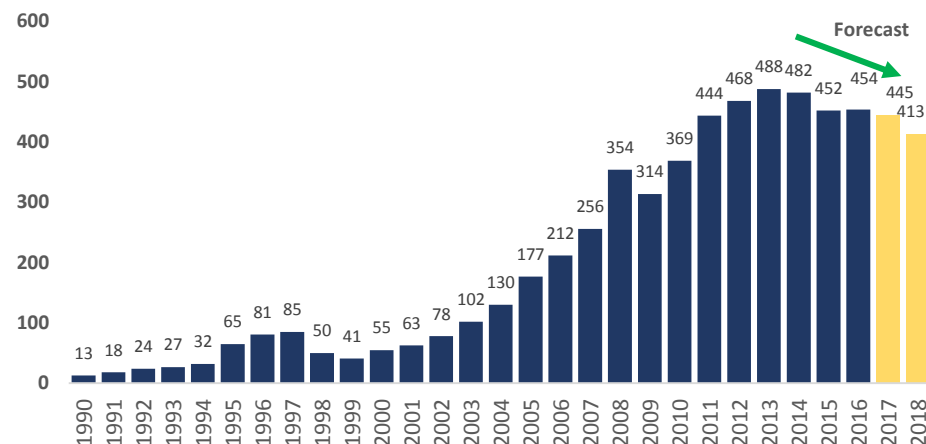
EM Micro: Capex declining and free cash flow galore

- BAML predictions – all time high free cash flow in Asia ex-Japan

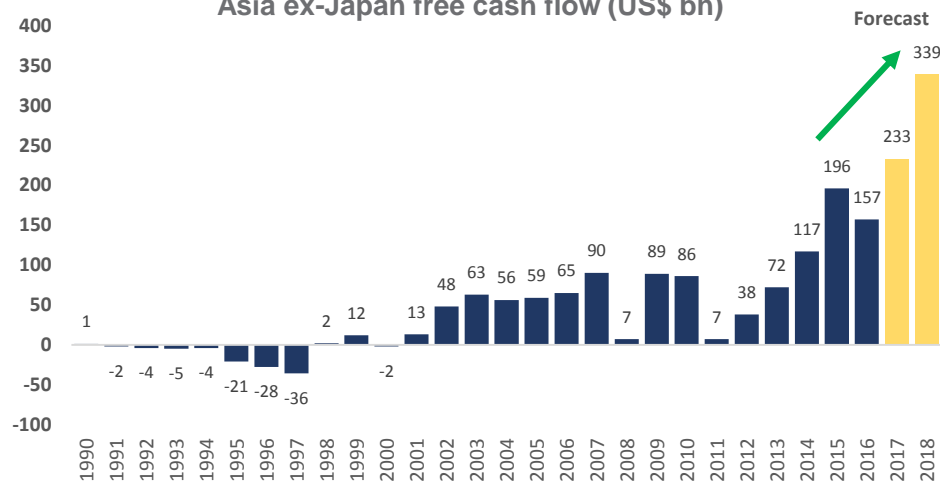
Asia ex-Japan operating cash flow (US\$ bn)



Asia ex-Japan capital expenditure (US\$ bn)

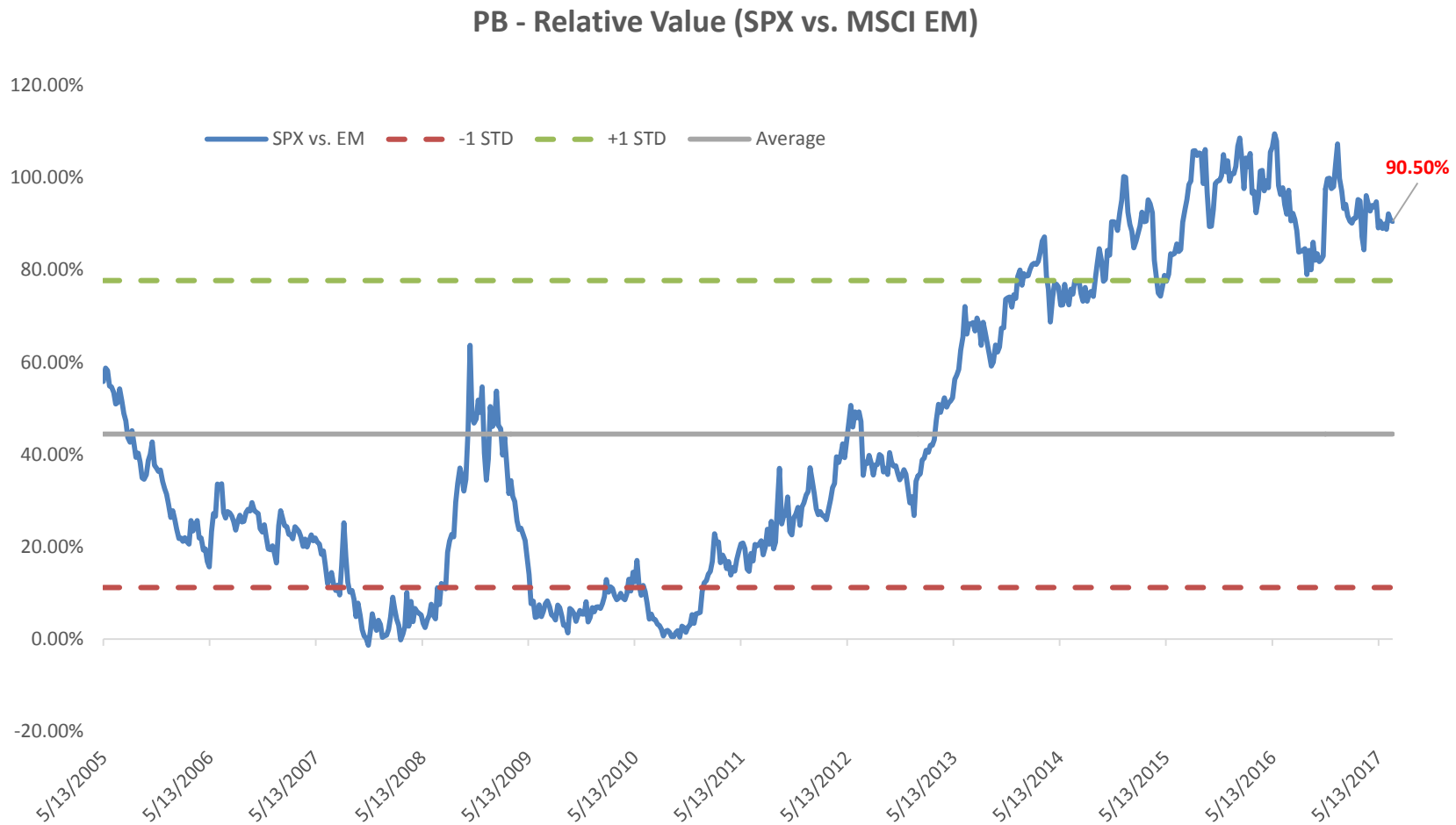


Asia ex-Japan free cash flow (US\$ bn)



Source: CLSA. Data as of December 2016.
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EM Micro: EM selling at a 90% discount compared to the U.S.

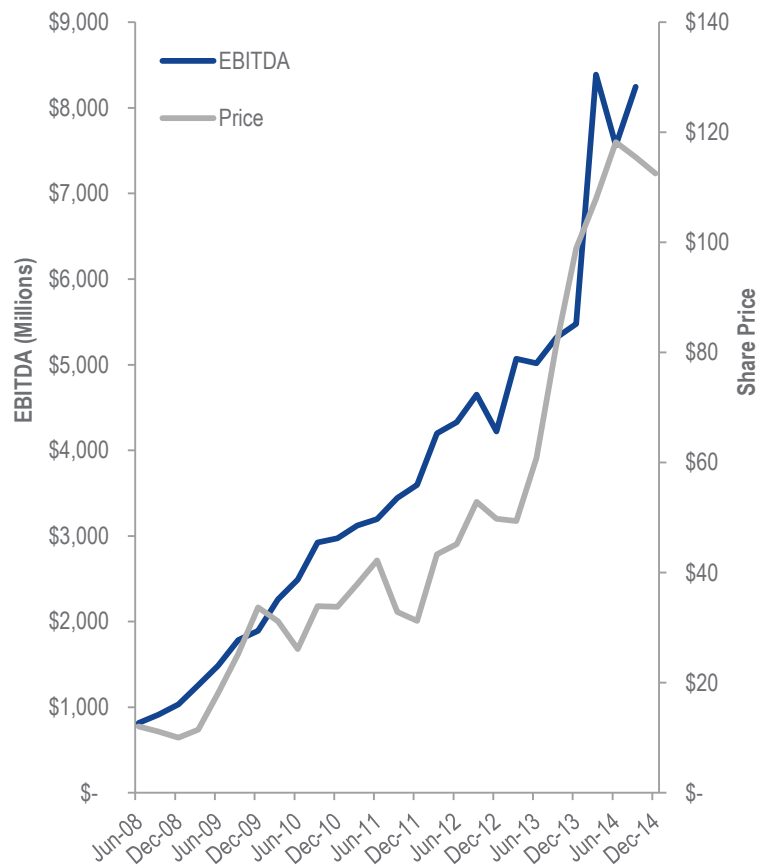


Source: Bloomberg, MSCI. Data as of June 2017.
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Structural growth versus cyclical growth



Structural Growth



Cyclical Growth



Source: VanEck. Data as of December 31, 2014.

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