# 2024 Emerging Markets Outlook

Local Views

**January 31, 2024**

## INTRODUCTION

Heading into 2024, we believe emerging market equities provide reasons for optimism. The asset class is set to benefit from a continued resilient macroeconomic standing, favorable monetary policies, and attractive valuations. However, we believe that the way these dynamics play out will vary greatly by country and, as always, these opportunities will be accompanied by risks. To navigate this environment, it is critical to have deep and detailed knowledge of local nuances. Specialists based in their market of expertise should continue to be well positioned to identify the many risks and opportunities and to invest accordingly.

To better understand the key topics that will shape the year ahead, we asked our local partners to share insights regarding one key opportunity and risk in their area of expertise.

## CHINA: LOCAL PERSPECTIVES FROM A HONG KONG BASED PORTFOLIO MANAGER

### Key Opportunity

*We believe the more established Chinese internet companies present a key opportunity for 2024. These companies offer a combination of value and growth fundamentals. If we look at the top 15 internet companies by market capitalization together as a group, their total market cap is about 8 trillion RMB with projected 600 billion RMB in total net income and 738 billion in total EBITDA for 2024. So, their aggregate forward PE ratio is about 13. Their total net cash is about 1.26 trillion RMB which is about 15% of total market cap, and they have low inventory and fixed assets compared to most other industries. They face reduced regulatory risks compared to the last few years and less competition from newer entrants due to fewer private equity and venture capital investments in many of their business areas in recent years. At the same time, they will continue to benefit from secular technology and consumer growth trends at the top line, scalability of their business models, and are expected to deliver low to mid-teens earnings and cash flow growth over the next 2 years.*

### Key Risk

*A key risk for Chinese equity markets in 2024 is a deficiency in the strength and/or timeliness of government policies to break the ongoing deflationary trends in asset (particularly housing) prices and weak consumer confidence. With housing accounting for about two-thirds of Chinese household net worth, continuing efforts to stabilize property prices and housing-related activities through fiscal, monetary, and administrative policies are important. Insufficient policy support would prolong the deflationary cycle, depress overall corporate profitability and market sentiment, and make the problem more difficult to solve down the road. While we believe domestic issues will dominate the outlook, geopolitical risks will continue to linger in the background and should be considered by investors. In particular, the US and China relationship could face increased pressure as US elections approach in 2024.*

## TAIWAN: LOCAL PERSPECTIVES FROM A TAIPAI BASED INVESTMENT TEAM

### Key Opportunity

*The emergence of AI has been transformative over the past year, unlocking robust growth drivers across all sectors and industries, most notably within the technology infrastructure supply chains. Taiwan, as the global leader from upstream integrated circuit design to midstream advanced foundry to downstream manufacturing, has been the major beneficiary of this secular product cycle, capturing a dominant leadership position within the AI ecosystem. In 2024, we project mid to high double-digit earnings growth for the region, led by technology, after the inventory correction of late 2022 into 2023. Specifically, we continue to see robust growth in the semi and hardware supply*

*chains as capex spending ramps up (across both chip-scale packages and enterprise) as more models are established and applications are built, driving the need for accelerated computing both on the cloud (AI servers) and at the edge (AI PCs).*

### Key Risk

*In our experience covering multiple technology product cycles over the past few decades (desktop computers, PCs, smartphones, etc.), the market tends to overestimate the speed of adoption for new technology but underestimate the magnitude of its impact over the longer term. The current AI wave will likely be similar. Factors that may introduce bouts of short-term volatility include 1) slower adoption speeds from the demand side as new applications are introduced and tested, 2) choppy or non-linear capex spending growth and 3) intensifying geopolitical tensions constraining industry TAM in the near term. Fortunately, with our supply chain-centric approach, we can quickly identify any changes to demand and order books through our channel checks of each component used to assemble AI servers and PCs.*

## SOUTH KOREA: LOCAL PERSPECTIVES FROM A SEOUL BASED INVESTMENT MANAGER

### Key Opportunity

*The semiconductor industry, mainly memory chips, will lead Korea's economic growth in 2024, as the sector is on a recovery path supported by production cuts and increasing AI-driven demand. The prices of memory chips, DRAM and NAND, have bottomed out and industry experts expect 40%+ price increases and 20% volume growth in 2024. In particular, the AI boom will accelerate a new memory segment called HBM (High Bandwidth Memory). HBM, an important factor for AI accelerators, will be a secular growth market, providing a highly profitable market for Korean semiconductor companies in 2024.*

### Key Risk

*China's souring economy, coupled with growing fears of its economy heading toward deflation, is triggering concerns over spillover effects that could rattle the global economy and eventually affect the Korean economy. Since the 2000s, China has been the single biggest contributor to South Korea's growing exports and trade balance surplus. Furthermore, against a backdrop of increasing geopolitical tensions between the U.S. and China, South Korea is vulnerable to their economic clashes over important issues ranging from trade policy and technology to Russia's invasion to Ukraine.*

## INDIA: LOCAL PERSPECTIVES FROM A MUMBAI BASED CIO

### Key Opportunity

*India is on a consumption super trend. The key drivers are demography (470 mn Gen Z population with ~27 years average working age), increasing digital intensity (~1.2 bn mobile users with per capita data usage of 20 GB/month), growing GDP per capita (of ~USD 2200+ USD), easy access to credit, and rising incomes. All of these drivers are creating multiple addressable cohorts at scale for serious long-term players to exploit. We expect consumption to grow at approximately 20% CAGR, over the next 8-10 years with an increasing share of discretionary spending. In addition, increasing access and improving affordability to consumer items, as well as rising aspiration, should result in a "premiumization" trend across consumer cohorts. As a result of this trend, we expect a long growth runway for segments like fashion, retail, home improvement, healthcare, leisure & entertainment, travel, and mobility to grab higher wallet share for the foreseeable future.*

### Key Risk

*India is heading into a national election in the second quarter of 2024. The current regime led by the Bharatiya Janata Party has done all the hard work to create building blocks for the economy to take off. It is therefore even more critical for the ruling regime to get re-elected. Currently, the market is optimistic given the favorable results of recent state elections. The market seems to have factored in the most favorable scenarios in terms of economic, political as well as corporate performance. This includes possible policy continuity, acceleration of next-generation*

*reforms post-election, and sustained better-quality, consistent earnings trajectory. Any adverse outcome differing from these expectations would disappoint the market.*

## SOUTHEAST ASIA: LOCAL PERSPECTIVES FROM A SINGAPORE BASED REGIONAL SPECIALIST

### Key Opportunity

*As a region, Southeast Asia is home to more than 670 million people, with an average GDP per capita income of less than US $5,000. Most of the population is still young, offering investors an opportunity to participate in its rising middle-class story. This demographic dividend translates into a powerful driver of economic growth, as the region consistently posts real GDP growth of 4-5% per year. Sectors poised to benefit from this rising consumer demand trend include consumer staples, consumer discretionary, healthcare, and financials. The average wage of the working class in Southeast Asia is still low, indicating further upside in the longer term.*

### Key Risk

*The biggest risk that could derail this secular growth trend is inflation, which would hurt the average consumer's wallet as purchasing power is eroded. Other notable risks that could jeopardize the Southeast Asia growth story include the slower-than-expected tourism recovery in Thailand, the weak property market in Vietnam, and the poor execution of the incoming new government in Indonesia to attract FDIs. Longer-term, the threat of artificial intelligence on the Business Process Outsourcing (BPO) sector in the Philippines could also impact unemployment rates.*

## MIDDLE EAST: LOCAL PERSPECTIVES FROM A SAUDI BASED PORTFOLIO MANAGER

### Key Opportunity

*Saudi Arabia has been focusing on transforming the country and boosting tourism numbers, (both religious and leisure tourism). They are enhancing connectivity by expanding and launching new airlines. More specifically, Riyadh Air is launching in 2024, and Saudia Airlines is expanding its fleet by 241 planes. The overall goal is to boost tourism numbers by 150Mn by 2030, and improvements are already being seen in several tourism enabling sectors, such as hotels, restaurants, events (music festivals, football games, etc.), transportation (including rail), and advertising natural attractions (such as Al Ula). We believe companies will benefit from this core objective for at least the next decade.*

### Key Risk

*Despite Saudi Arabia's notable efforts to diversify government revenues, with non-oil revenue rising from $44.3bn in 2015 to $117.5bn in 2023, oil revenues continue to play a key role when it comes to the mega project spending that the country is pursuing. Some examples of mega projects include NEOM and Red Sea developments. If the global economy slows down significantly in 2024, it could lead to lower oil prices putting further pressure on government funding and liquidity in the local system. Local liquidity is already limited given the government borrowing needs to fund mega projects. A lower oil price would further pressure liquidity and could lead to a slowdown in spending on these projects. While this would not be a favorable scenario, it could have some positives as it gives more time to re-evaluate the productivity output of some of the more ambitious projects. In addition, it is worth noting that the recent uptick in geopolitical tensions in the region is likely to be a source of uncertainty in the months to come for the region as a whole.*

## EASTERN EUROPE: LOCAL PERSPECTIVES FROM AN ESTONIA BASED PORTFOLIO MANAGER

### Key Opportunity

*Turkey is one of the most under-owned stock markets amongst foreign investors. The market was among the weakest in 2023 falling by 11.5% in USD-terms. Negative sentiment was driven in part by unwelcome results from*

*the presidential and parliamentary elections which cemented the political landscape for next 5 years. Increasing inflation combined with unorthodox monetary policy led foreigners to abandon the market en masse. The US$12 bn of foreign outflows since 2020 took the foreign ownership levels in several companies to historical lows which tends to be a good contrarian indicator. Currently, the Turkish market trades below 5x 2024E earnings. These levels represent close to a 50% discount to the 10-year average. For some, these low valuations may seem justified considering Turkey's high inflation level and 25% 10-year bond yields. However, there are plenty of companies in Turkey that benefit from Turkish Lira weakness, that have unlevered balance sheets, and offer growing free cash flow yields in the range of mid-twenties for the foreseeable future. If the highly regarded finance minister Mehmet Simsek and the new central bank governor Hafise Gaye Erkan are allowed to continue with orthodox monetary policy, having some Turkish exposure can be rewarding.*

### Key Risk

*Going into 2024 the key risk remains the war between two neighboring countries: Russia and Ukraine. The war risk premia shrunk considerably in 2023 as the war seems contained (as in, not spilling over into other countries as had once been feared), energy prices have fallen back to pre-war levels, and western support for Ukraine remains intact. However, at present, the Russian population seems more unified towards Putin than ever before, and Russian military spending has only increased. It can be argued that Russia's confidence to maintain the status quo (i.e., keep fighting) has only increased. While nearly impossible to guess where things go from here, it's quite possible that testing the NATO alliance is on the table, escalating the likelihood of a broader war. Aside from an increasing chance of a military escalation, risk of energy and food supply shocks remain, similar to what we saw in 2022. Indeed, some European economies remain highly dependent on Russia; Hungary for example still gets 50% of its crude oil through pipelines from Russia, which cannot be replaced by an alternative route.*

## SOUTH AFRICA: LOCAL PERSPECTIVES FROM A JOHANESSBURG BASED INVESTMENT MANAGER

### Key Opportunity

*The South African economy has been hampered by ongoing electricity outages, which have stalled overall economic growth and deterred both local and foreign investment. However, recent regulation changes have resulted in massive investment by the private sector in alternative energy sources which in turn has alleviated some of the strain on the grid and mitigated some of the economic impact of the electricity crisis. With significant additional power being added in the last 12 months – both by the state and private enterprises – South Africa should be poised for stronger growth as power outages become less frequent and businesses are able to reinvest in growth.*

### Key Risk

*2024 is an election year in South Africa and for the first time since the start of democracy, there is a strong likelihood that the African National Congress Party (ANC) will not achieve an outright majority. South African politics has historically been dominated by the ANC. However, due to increased corruption and slowing growth, the party is expected to fall below 50% of the votes for the first time in the democratic era. It is likely the ANC will form a coalition with a more centrist party which will be viewed positively for the South African financial markets. The risk is the ANC opts for more left leaning parties in a coalition. We view that scenario as unlikely.*

## LATIN AMERICA: PERSPECTIVES FROM A LONDON BASED REGIONAL SPECIALIST

### Key Opportunity

*One specific opportunity in Brazil is in healthcare, the worst performing sector in 2023. Prior to Covid, the Brazilian healthcare industry generated a return on equity (ROE) of 15% which increased to 20% during the pandemic as patients avoided going to doctors and hospitals, with many procedures delayed. As Covid abated, the backlog of procedures resulted in significant costs for the industry and profitability declined. The industry then faced the headwind of much higher inflation, which further pressured profitability. Given the weak economic recovery from Covid, the industry was slow to increase prices to offset higher costs. The industry went through almost a year of breakeven profitability, but recently we have seen price increases being implemented and*

*utilization of doctors and hospitals returning to normal. As price increases can only be implemented once contracts are renewed, we expect to see consistent improvement in profitability until the sector reverts to the 15% historic return levels. As the stock market continues to forecast weak earnings (albeit better than a few quarters ago), we are significantly more optimistic about the outlook for earnings and valuations.*

### Key Risk

*One risk to the Brazilian economy is a potential slowdown in the agricultural sector. Agriculture has been growing much faster than the rest of the economy, with tailwinds from increased Chinese animal feed and global biofuels demand, plentiful available land, improving logistics, rising crop yields and supportive government policies. This has happened as competing countries struggle with supply challenges including drought in Argentina, war in Ukraine and tensions between the US and China. A slowdown in this sector could be triggered by reduced farmer profitability as crop prices are falling significantly from those after the Ukraine conflict. China is also seeking to improve its own self-sufficiency, which may reduce the pace of export market growth. Brazil may also face weather issues and recent dry and hot conditions are already reducing expectations for upcoming harvests.*

## DISCLOSURES

Interviewees have had their names anonymized for purposes of confidentiality. All quotes and representations made in the white paper have been authorized and approved by such manager.

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