J O Hambro Capital Management Group

Emerging Markets Spotlight

James Syme, JOHCM Global Emerging Markets Opportunities Fund

One of the reasons we believe it is crucial for emerging market investors to be knowledgeable about the history of the asset class and the countries in it is the dynamic nature of different emerging markets as they grow and develop (or, occasionally, fail to). There is possibly no country in the EM universe that has undergone a greater shift in its macroeconomic fundamentals and the relationship of its capital markets to those fundamentals than Thailand.

The Asian crisis of 1997 was one of the great landmark events in the history of EM. Whereas the 1994/5 'Tequila crisis' in Latin America was confined to a group of countries with a history of economic volatility (see: Latin American debt crisis, 1982), the Asian crisis tore through a regional economic miracle. Thailand was in fact the first domino to fall in 1997, with the default of major property developer Somprasong marking the beginning of the crisis.

Looking back, in the late 1990s, Thailand was as capital-deficient, liquidity-driven and high-beta as Turkey, Argentina or Russia, and the turn in global liquidity in 2002 would set in motion an economic and stock market boom of similar magnitude to those other countries. However, a genuine transformation of the economy occurred at this time, with Thailand developing deep and widespread capability in exports of electronic products and processed foodstuffs, as well as a highly successful tourism industry. As well as driving GDP growth, this shift massively strengthened the Thai current account balance, which has moved from a deficit of over 8% of GDP in 1995 and 1996 to a surplus that has averaged nearly 9% of GDP in the last three calendar years. This has in turn led to a 180 degree turn in the policy objectives of the Bank of Thailand (BoT), which went from holding the baht up (to keep imports cheap and hard-currency denominated debt affordable), to holding the baht down (to maintain export competitiveness). This BoT has pursued the latter strategy as single-mindedly as any other mercantilist EM.

What is more, Thailand is approaching some challenges as the limits to conventional interventionist-mercantilist policy are reached. These include disquiet among trading partners at the suppressed valuation of the currency, and the zero lower-bound to policy (policy rates in Thailand have just been cut to 1.25% but are likely to continue to fall). Unconventional monetary policies such as asset purchases, directed lending and negative rates could be employed, but the large current account surpluses will continue to pose a problem for Thai policymakers.

The upward pressure on the baht does not make Thailand particularly attractive for equity investors. The hit to competitiveness from the stronger currency has an overall drag on the economy, while the central bank's sterilisation of capital inflows limits liquidity growth. Domestic demand in other late stage-mercantilist-interventionist Asian economies like South Korea and Taiwan has consistently disappointed, while returns on capital (particularly in the financial system) have trended lower and lower. This also has echoes of the Eurozone, which has also chosen to suppress demand in order to run huge current account surpluses; indeed, a current account surplus can be thought of as representing a country's deficiency of demand relative to productive capacity. As we have seen in Europe, South Korea and Taiwan, equity market opportunities tend to be concentrated in export sectors during global upswings.

We continue to see the potential for US Federal Reserve accommodation to improve global US dollar liquidity and weaken the dollar in the coming year. This has the potential to drive very strong economic uplift and equity market returns in the capital-deficient, liquidity-driven and high-beta emerging markets. Thailand was one in 1999; it isn't 20 years later.

JOHCM Global Emerging Markets Opportunities Fund
5 year discrete performance (%)

Discrete 12 month performance (%):

	31.10.19	31.10.18	31.10.17	31.10.16	31.10.15
A GBP Class	8.93	-10.66	20.86	32.21	-3.41
Benchmark	10.84	-9.75	16.53	37.58	-10.78
Relative return	-1.72	-1.01	3.72	-3.91	8.26

Past performance is no guarantee of future performance.

Source: JOHCM/MSCI Barra/Bloomberg, NAV of Share Class A in GBP, net income reinvested, net of fees as at 31 October 2019. The A GBP Class was launched on 30 June 2011. Benchmark: MSCI Emerging Markets NR (12pm adjusted). Performance of other share classes may vary and is available on request.

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