ABROAD

«Yes, the opportunities are still there.»

A legendary and veteran guru analyses the outlook for Asia, Latin America, Africa and East Europe.

By Vincenzo Sciarretta

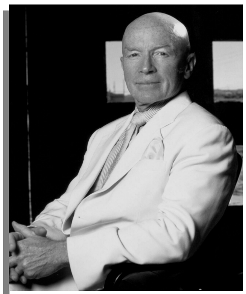
It is said that Mark Mobius spend over 200 days a year all over the world looking for opportunities in developing countries. He got the title of <number one global emerging market manager> and he was praised as part of the exclusive club of the "ten top money managers of the 20th century." *The European Side* talked to him on the prospects of the emerging markets and he sounded quite bullish. "The opportunities are still there", he said.

In the past, we have occasionally seen some emerging markets soaring 10 to 20 times in a few years or a decade. Do you sense anything of that magnitude in the next future?

"In the last five years the MSCI Emerging Markets index has nearly doubled. Some regions such as Latin America and South Africa have experienced even higher returns, while the MSCI EM Europe was up about 160% (in euros) in the five years to end November 2005. Despite these numbers, we continue to see significant opportunities in all these regions. We expect companies to continue to grow earnings and further strengthen their balance sheets. Yet, overall, valuations are still below the levels seen in the past. Fundamentals remain sound. China, India, Brazil, Eastern Europe and Russia are set to continue their high GDP growth rates."

Let's start from Asia. What's the outlook?

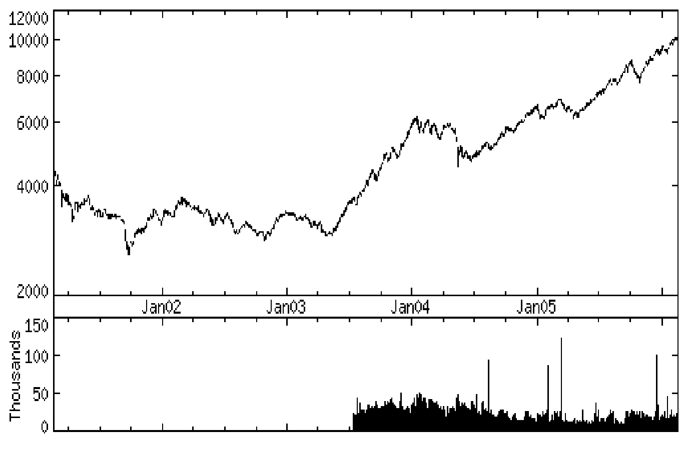
"It's amazing to see how markets and prices have gone up over the last three years in Asia, but still price-earnings ratios are very reasonable. That's because earnings have kept pace with these price increases. So we see more bullishness ahead, especially as money continues to pour in from the U.S. and Europe. American investors especially have been disappointed by their domestic markets - hence their heightened interest in emerging markets surfaced and was reinforced."



Dr. Mark Mobius, managing director of Templeton Asset Management LTD, Singapore.

The Indian stock market has recently broken out beyond the 10,000 level. By the way, it's up 4 times from the bottom. Should investors buy, hold or sell Indian stocks?

"There are many reasons for the strong performance of Indian stocks. An improving geopolitical environment - including a lessening of tensions with Pakistan - Reforms in key sectors like banking, power and telecommunications, privatizations and stable economic policies should also continue to favour Indian stocks, while India's booming software and pharmaceutical sectors continue to move the economy up the global value chain. India also has sizable dollar reserves - an important consideration for global investors when evaluating an emerging market - and it has made important strides in corporate governance, coming in third after Singapore and Hong Kong in a recent CLSA survey. The return on invested capital (ROIC) of publicly listed Indian companies has been consistently above that registered in most other emerging markets, a situation that is expected to continue."



The Indian equity index has surged as a lot of other emerging markets.

Yet, one cannot deny that there are some problems. India's fiscal deficit and its current account deficit are major concerns for global investors. Inflation too has been rising. The country is highly exposed to hikes in imported oil prices, and attract much less FDI than China. Moreover, it has become fashionable to say that infrastructure is a disaster there…Aren't you worried about?

"Yes, I am worried about all of that and more. Yet the country's fast-growing and increasingly affluent workforce will be good for savings and investment in the coming decades. In particular, India's growing economy should encourage local investors to look increasingly at equities as savings instruments, providing a sound underpinning for the continued growth of the Indian stock market in the years ahead."

Then there's that other giant named China. Many are disappointed by its stock market…

"Yes, for the past number of years, the domestic Chinese market has done very badly. By contrast, H shares and Red Chips have done fairly well, although in valuation terms they have not moved much."

Are you optimistic?

"I am inclined to think that as they allow more foreigners to come into that domestic market, it will be very interesting. There is still a lot of room for upside in the Chinese market."

There's a widespread fear that government-controlled banks may get into terrible trouble. What do you think about?

"It is easy to see that if they were run on private equity terms, they would be bankrupt. The government will not allow them to go bankrupt, but it is now trying to reform them by allowing some foreign investors to come in. In essence, there is recognition that the banks are in trouble and they have to be reformed. But the Chinese are being very careful because foreclosing on too many loans would see a lot of people out of work. So they are reforming the state banks gradually by cautiously opening up to foreign know-how."

You speak of a medium-term process.

Do you see any shorter-term implications?

"Yes, stability in the banking sector is key to avoiding a hard landing of the economy. Chinese banks' non-performing loans are very dangerous, which is why the government will probably not institute large interest rate hikes in the near future because default rates for mortgages and loans to overheated sectors might get higher."

How do you judge the valuation of the equity market?

"Well, I'll give you an anecdote: we are seeing some very big IPOs launched at reasonable prices in China. And that's tending to keep market price levels overall from going though the roof. In other words, we are seeing reasonable growth in prices, but without the sort of bubble we had in past years in developing countries."

What about risks? I mean big risks?

"The big political risk in Asia, of course, is the tension between China and Japan. Also, if the conditions in China deteriorate, then Taiwan is at risk because the Chinese would want to get people's mind off what's happening domestically and look at Taiwan for a takeover. But those risks are far too removed to have any implications in current investment decisions."

You mentioned Taiwan. One notes some optimism for the Taiwanese bourse centred on high dividends, low interest rates and a China-led export boom. Do you share the consensus opinion?

"Yes, I do. Taiwan continues to benefit from the tremendous growth in mainland China. We particularly like Taiwanese technological firms. Many Taiwanese electronic companies have been transformed from just being OEMs (original equipment manufacturers ed. note) to real brand names. A number of Taiwanese companies are well on the way to becoming leaders in international markets."

Let's change area: many markets in Latin America have taken off. What's the outlook and what's the story?

"We continue to see significant upside potential in Latin American stocks. Currently, we find more opportunities in stocks that have exposure to the region's domestic economies, and a number of industries should continue to fare comparatively well."

Any examples?

"Brazil. I like Brazil. The country has a huge consumer market and world class export companies with very low production costs. Recent political corruption scandals have not affected either the economy or the stock market in any significant way, as the government continues its austere fiscal and responsible monetary policies. Elections this year should not change the economic landscape, therefore maintaining Brazil on the right track. Interest rates are trending down and consumer credit availability continues, growing thus sustaining growth."

Do you have another example?

"Mexico. In Mexico, GDP growth expectations for 2005 have come down after the strong growth registered in 2004, but growth should still be well above the low levels experienced in the preceding years. Growth outlook for 2006 is solid, helped by the performance of the U.S. economy. Mexican consumer demand remains robust, fuelled by the higher availability of consumer credits among other reasons. Fiscal accounts continue to benefit from high oil prices, as Mexico is a net oil exporter. Political concerns ahead of the 2006 presidential elections may lead to some volatility in the markets, but our investment philosophy will not change due to short-term political noise. Indeed, any volatility should present buying opportunities."

In my interviews with gurus and money managers, I never record a story about Africa. Are there any opportunities here?

"We do have investments in South Africa and see significant opportunities there. On the domestic front, rising consumer spending - especially in the retail sector as a result of the government's black empowerment plans - have resulted in putting more money in the hands of a larger part of the community. And at the same time, the best South African companies are expanding into countries north of its border. We are invested in Old Mutual (one of the largest financial services companies in South Africa, predominantly focused on insurance) and have had interests in the South African brewing company SABMiller. In all, South African companies accounted for about 10% of Templeton Emerging Markets Fund (SICAV) assets at end-2005."

Are there any opportunities left in eastern Europe? What are the opportunities?

"The outlook for Eastern European markets is positive. Companies are expected to record earnings growth and further strengthen their balance sheets. Overall, valuations are still at reasonable levels and fundamentals remain sound. The key, however, is to find undervalued companies that are well capitalized and have a unique and competitive product range. We are also looking out for companies that are paying solid and sustainable dividends."

Mr. Mobius, you sound quite sanguine. Many thank for your comments.