ROBECO
The Investment Engineers

Emerging markets sell-off driven by fear rather than fundamentals

- Volatility may continue for some weeks
- Valuations nearing historical lows
- Buying opportunities in countries like China, India and Korea

Today's global financial markets were marked by great volatility. As for emerging markets, we expect this to continue for some weeks. Buying opportunities are emerging, though.

Once the dust will have settled in a few weeks' time, we might be in a situation in which US interest rates are no longer at zero, the Chinese economy is still expanding, albeit at a slower pace, and the Chinese currency is trading in a way that allows for a bit more market force. The latter is a good development in the long run, but adds to uncertainty in the shorter term. Emerging countries that buy a lot of - ever cheaper - commodities enjoy a much smaller bill for energy, copper, iron ore et cetera. This applies to countries such as China, India, Korea, Taiwan and Turkey. For now markets focus mostly on the exit and the ongoing market action is more reminiscent of a panic-driven final sell-off than the beginning of a structural bear market.

Debt has been built up in Asia over the past few years but is not sizable enough to justify a crisis. Currencies are well supported by foreign reserves. Most countries in Asia don't need foreign capital to sustain themselves thanks to current account surpluses.

Buying opportunities

The situation in large non-Asian emerging countries might be at its worst in Brazil and Russia with commodity prices declining rapidly and political turmoil at a peak. We don't know what the future holds but as top-down investors we do see good buying opportunities in markets like China, India and Korea. India, for instance, saves a staggering amount of USD 80 billion this year, with oil prices at USD 45 against over USD 100 last years. This is a lot of precious money the Indians can spend on infrastructure, education and health care instead.

Almost all of the commodity-buying nations have an overweight position in Robeco's Emerging Markets Equities portfolio, whereas the commodity-exporting nations such as Brazil, Russia, Malaysia and South Africa are among the largest underweights in the portfolios. We do not see a lot of upside in today's commodity prices, even after the recent decline.

The average valuation in emerging markets is approaching historical lows, both in absolute terms and in terms of discount to developed markets. The expected 2015 price/earnings ratio is well below 10 times and price/book stands at 1.2 times. These levels match the ones reached during the Global Financial Crisis in 2008/2009.

Focus on the fundamentals

What could put a stop to the uncertainty in this sentiment-driven market? A hike in US interest rates in

September would end the uncertainty on that front, which might redirect global asset allocators' attention back to economic fundamentals. This would be a good thing, as today's world economy certainly looks better than seven years ago.

Wim-Hein Pals, Head of Emerging Markets Equities