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FINANCIAL MANAGEMENT



Emerging Markets and You

Many global economists believe that rising commodity prices are more a result of increased demand than of market speculation or inflation.

Fed Chairman Ben Bernanke notes that “Rising commodity prices are a result of the rising demand of emerging economies”.

[The changing face of emerging economies](#)

As developing nations such as Brazil, Russia, India and China (collectively “BRIC”) continue to grow and develop, they have witnessed:

1. The migration of citizens from rural areas to cities.
2. A transition from poverty to a large freshly-minted middle class with disposable income that they eagerly spend on all manner of goods – cars, refrigerators, flat-screen TVs, laptops, cell phones, jewelry, branded goods, food, cosmetics, clothes, and more.
3. Huge investments in infrastructure – roads, subways, airports, telecom, technology, and farmlands lost to malls, apartment buildings, hotels, golf courses and office parks.
4. Heavy demand for energy (coal, nuclear, petroleum), water, financial services, capital markets, colleges, etc.

Developing economies are driving a real and urgent demand for all commodities - cement, iron and steel, copper, gasoline, chemicals, wheat, gold, silver and so on - with businesses outbidding each other to keep their factories humming.

Economics 101 – this voracious demand has led to an inevitable rise in commodity prices worldwide, leaving developed nations to cope - with higher prices at the pump, for food and just about everything else.

[Aging workers](#)

On the one hand, emerging economies are growing like there's no tomorrow. On the other, their aging workforce raises questions about the sustainability of this growth.

Census numbers show that China's elderly population has grown rapidly while its 14-and-under population has plummeted. Basically, there aren't enough youngsters to replace older folk who are moving into retirement.

According to Harvard Professor, Richard Cooper, China's median age will go from 35.2 to 47 between 2010 and 2040, Russia will go from 38.5 to 47, and India and Brazil's median population will remain current to the U.S.

Which begs the question, how long can China maintain its strong manufacturing growth and exports if it just does not have the human capital to replace aging workers?

[Investing opportunities](#)

Emerging growth is driving up sales, profits and share prices of companies catering to this huge demand.

So how can you as an investor participate in this?

Fortunately, it's not that difficult. You can invest in:

- Emerging market ETFs (Exchange Traded Funds)
- Shares of Blue Chip companies with a large footprint in emerging markets
- American Depositary Receipts (ADRs are shares of non-American companies traded in dollars on U.S. exchanges)
- Mutual funds that invest in foreign companies

Many large-cap companies draw a substantial chunk of their earnings from foreign operations. Foreign operations contributed to:

- 50% of the revenue of large global S&P 500 companies in 2010
- 28% of the revenue for companies in the S&P 500 as a whole, up from 24% in 2009

[Know the risks](#)

While emerging economies are growing, they are also facing a lot of concomitant problems.

For example, in China, there's been an unprecedented rise in wages that has made its products less competitive, debt levels have grown much too fast and banks have no real idea about the number of bad loans, and housing prices have risen to bubble levels.

50% of China's GDP is driven by capital spending on unnecessary airports, roads and high-rise apartments.

If the economy slows, a lot of this demand could fizzle out almost overnight – ghost towns with half constructed towers, a reverse exodus back to villages, social unrest... and an inevitable drop in demand and commodity prices.

In many of these markets, the economic “car” is moving so fast that if there is a blowout it could lead to a big crash.

So investors should consult their financial advisors, be cautious, and carefully invest only a small portion of their portfolio, preferably in blue chip companies that have globally diversified earnings, that are not overly exposed to emerging markets, with products that would still be in demand were a crash to come... soaps, shampoos, computers, burgers, pizza, mobile phones, colas... you get the picture. Bon voyage!