Emerging Markets Watch

The Graduate Program in International Political Economy & Development
Fordham University

IPED

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Alumni Profile: Mr. Joshua Post

Mr. Joshua Post is a Senior Consultant in the Transfer Pricing (TP) team of Ernst and Young. TP is part of EY's International Tax Services. The TP is a group which offers tax compliance assistance to multinational companies, as required by the Internal Revenue Service (IRS). In addition, the group also assists companies in restructuring their operations in order to minimize their global tax burden.

According to Mr. Post, "as emerging markets continue to increase in global prominence so too will the need for tax experts who understand the implication of local tax rules as it applies to cross border transactions". Recently the UN released TP guidelines for developing countries highlighting this topic as an important issue. During this time of global economic weakness, both developed and developing country governments will focus on TP as a means of generating tax revenues through enforcement of TP regulations.

As an example, two emerging markets recently implemented TP legislation: Brazil and China. Brazil's laws are interesting as they do not follow the generally accepted OECD TP guidelines but rather follow their own unique rules. Mr. Post has worked on projects where US companies were moving manufacturing operations to China. His work on these projects involves both transfer pricing as well as indirect tax issues such as VAT and Customs.

Mr. Post never imagined that he would be working as a tax consultant. His undergraduate training was in Biochemistry which was followed by serving as a volunteer with Peace Corps in Burkina Faso. IPED provided him the opportunity to follow his interest in development economics. During his studies, the global financial crisis occurred and the development job market became very competitive. As a result, IPED provided the opportunity for him to take classes in finance that ultimately led him to qualify for his current job. Although many of the courses in IPED are not directly related to tax, he believes that the training in economics prepared him well for the analyses that he currently undertakes.

Global Markets Fellowships

Designed to attract highly qualified full-time students who seek careers in the analysis of international commercial and financial markets into the IPED Program, the Global Markets Fellowship consists of a tuition scholarship combined with a graduate assistantship. Eligibility criteria are: relevant professional work experience, professional proficiency in English and another language widely used in international business, and strong cross-cultural skills. Students committed to a professional career in international business and finance with a focus on emerging markets may also apply for the Emerging Markets Travel Program. The application deadline is early January for the following fall semester. For further information, go to www.iped.fordham.edu and follow the link to "Financial Aid."

What is IPED?

IPED stands for the International Political Economy and Development Program at Fordham University in New York City: a program that trains graduate students in the advanced interdisciplinary analysis of global economic relations and international development issues. Graduates frequently work as financial analysts in the private sector, economists and policy analysts in the public sector, and project managers in the non-profit sector.

Emerging Markets Watch is a student-run newsletter of Fordham's IPED Program. It aims to share with prospective students and friends in the academic, non-profit, government, and corporate community IPED analysis in emerging markets and country risk analysis.

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Investment Prospects for Emerging Economies

EDITORS' NOTE: Fordham's *Summer Certificate Program in Emerging Markets and Country Risk Analysis* is an intensive 10-week program designed for international business professionals as well as current graduate students. The program offers students the opportunity to develop the political, economic, and financial analytical skills needed to evaluate the potential risks and rewards associated with the dynamic and volatile financial markets of Asia, Latin America, Africa, and Eastern Europe. On page 2 are abstracts of the papers completed during the summer of 2012. For more information about the program, please visit www.fordham.edu/iped/summer.

Brazil

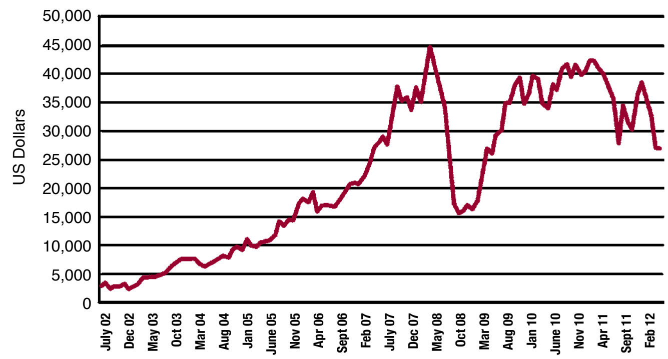
By Brittany Borg

The prospects for portfolio investment in Brazil are below normal for the next year. Lower than predicted growth, a slumping stock market, and concerns over inflation counter the few positives: an exceptionally high amount of foreign direct investment and newly discovered oil deposits. As Brazil prepares to be host to the 2014 World Cup and 2016 Olympics, prospects may perk up during those periods but unlikely within the next year.

Brazil is now the world's sixth largest economy but the OECD predicts growth of only 3.2% this year, considerably less compared to other emerging market economies. Inflation and policies towards it have been very unpredictable. The official inflation target is 4.5% ± 2%. Inflation rate fell below 5% in June this year for the first time in 2010. This suggests that the central bank's strategy of simultaneously reducing interest rates and prices is working. However it unexpectedly accelerated for the first time in ten months in July by 0.33% and is now expected to continue. This also suggests that the government will soon need to curb interest rates cuts.

The stock market was hit hard by the global recession, recovered and then plunged again in 2010. The Bovespa Index declined by 45% and is yet to recover. While Brazil's market has boasted very high gains over the ten-year period, the last year showed monthly losses of 2.5% and shows no indication of a turnaround.

Bovespa Index



FDIs into the economy were $64B over the last 12 months ending in May 2012. Inflows from foreign corporate investors have been more than enough to cover for its small current account deficit.

Petrobras has discovered large oil deposits off the coast of Brazil and the company CEO seems optimistic about this opportunity. However, Petrobras falls behind other emerging market energy options in all areas of growth.

Concerns over a sluggish economy, inflation and underperforming stocks make Brazil a less than ideal candidate for investment over the next year. Other emerging market equity opportunities will likely outshine the country in the very short term. ■

China

By Fan Zhang

The equity investment opportunity for a one-year time horizon in China is above normal. This is due to the stable exchange rate and recovering stock market, but poor GDP growth, rising inflation rate and unstable political environment are potential drawbacks.

The exchange rate is kept stable by the government at the 6.3 level by buying and selling US$. China caters to a huge export market and this resulted in a trade surplus in the current account and consequently, in the balance of payments. To balance this, China is holding a great amount of international reserves, which includes US dollars and T-bills.

The 2008 financial crisis caused the Shanghai Composite Index to lose 67% of its value since its peak in October 2007. It is now slowly recovering as seen from the increasing long-term returns. Over the past five years, the average monthly return of 0.84% outperformed the S&P, FTSE and N225. The higher return however is countered by its risk: it is three times more volatile than the other three.

GDP growth rate decreased from 14% in 2010 to 11.4% in 2011. Forecasted growth rate is 7.5%, the lowest in eight years. This stems from the government policy of divestment in technology development and production efficiency.

The government implemented lax monetary policies and moderately loose fiscal policies and this brought up the inflation rate: as high as 8% in early 2011 and eventually having a yearly average of 5.4%. The decrease in the value of money and the unfair distribution of wealth further causes discontent.

Whether China can strengthen itself in the future depends on the government's ability in achieving political reform and solving political differences with other states. The high risk in the equity market makes it less attractive but is countered by its high returns. ■

Shanghai Composite Index

Egypt

By Mohammed Ali Sergie

Egypt's prospects for portfolio investment are below normal. It has a large population which stimulates spending, stable exchange rate and rapid economic expansion over the past decade but the aftermath of the revolution stunted growth and worsened the current account and balance of payment deficit.

On February 11, 2011, President Hosni Mubarak resigned and transferred power to a military council that was tasked with assisting in the country's transition to democracy. The economy skidded to a halt for a few months and growth has remained lackluster.

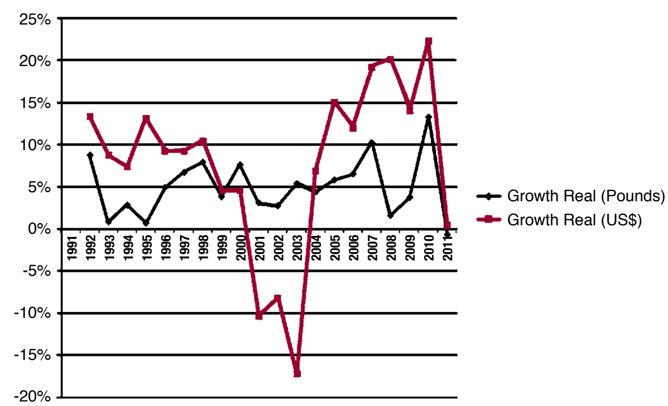
Egypt's economy is largely based on consumer spending by its population of 82.5 million and income derived from tourism to its ancient pyramids and shipping traffic through the Suez Canal. As a result, it is highly dependent on global economic cycles. Growth slowed to 2.82% in 2002 from 7.68% in 2001. The economy rebounded in 2003 and posted a 10.3% gain in 2007. However it slowed along with most of the world during the 2008 and 2009 global recession.

Egypt has been running twin current account and balance of payment deficits since 2003, and the situation has become more acute as international reserves plunged in order to defend the Egyptian pound. International reserves were steadily expanded over the past decade and more than tripled to $33.6B by the end of 2010 which allowed Egyptians to benefit from a corresponding rise in imports. But foreign reserves are now down roughly 60% to $15.5B thereby reducing the central bank's ability to maintain the value of currency.

Foreign aid appears to be the only solution to shore up reserves and the country held talks with the IMF regarding a $3.3B loan in 2011. In addition, Saudi Arabia deposited $1B in the central bank, following President Morsi's meeting with them. However, the Egyptian currency has lost about 10% of its value since 2005 but has been stable over the past year with a coefficient of variation of less than 1%.

The lingering power struggle between civilians and the military as well as pressures on foreign reserves indicate an extended period of economic uncertainty, even though the currency is currently stable.

Egypt Real Annual GDP Growth Rate



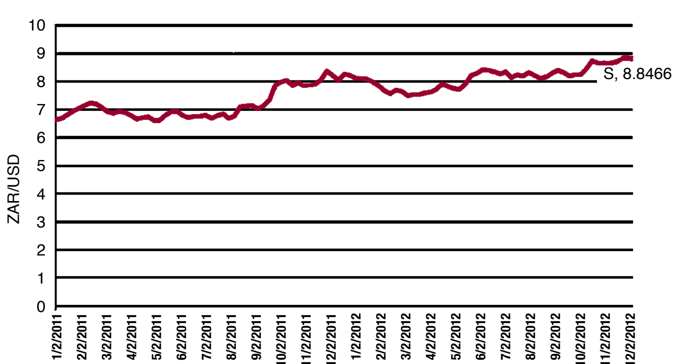
South Africa

By Ramon Fuentebella

The prospects for portfolio investment in South Africa in the next year are below normal. It faces a dual-headwind scenario of international economic slowdown and domestic volatility, offering no benefit of superior returns or effective diversification for American portfolio investors.

South Africa continues on a modest growth trajectory heavily influenced by the Eurozone crisis and economic slowdown. The economy grew 3.1% last year driven by low and stable interest rates, higher commodity prices and a weaker rand. It is forecasted to grow 2.5-2.7% this year. Given the exposure of the economy to trade and portfolio investments from developed regions and China, the continued volatility of international economy poses a serious threat to growth prospects.

South Africa Exchange Rate



The country's national accounts are also affected by the international economy. SA finds itself with decreased exports to Europe and China resulting in trade deficits as it continues to import materials for infrastructure building. One can also assume the period of international uncertainty to lessen investors' risk appetite for emerging markets. This puts a challenge to SA's international reserves which has been on a flattening trend since the first quarter of 2011. A closer look at the rand shows increased volatility: its standard deviation ranged from 0.8622 in the last five years to 0.322 in the last six months.

The return and risk profile of the stock market puts it between emerging and developed economies. Its average monthly return is higher than developed markets and it has slightly lower risk than emerging markets. In this case, there are long-term prospects for the stock market given it continues to have lower price-earnings ratio than other developed/emerging markets.

Indeed SA faces two reinforcing sources of risk in the next year: externally, the European crisis and China slowdown, and internally, nationalist economic policies, elections, labor unrest and declining business confidence. In this context, one must only tactically invest in industries that are cushioned from these risks and that can source growth from frontier African markets.

Faculty Interview: Dr. Ralf Hepp

Dr. Ralf Hepp is currently an Associate Professor in the Department of Economics. He teaches both undergraduate and graduate courses. Dr. Hepp completed his Ph.D. in International Economics from the University of California, Santa Cruz in 2005 with a focus on the consequences of debt relief initiatives.

Currently, Dr. Hepp is collaborating with Dr. Madhavi Bokil, Senior Economist for American International Group, to produce a paper titled Central Bank Preferences in Post-Crisis East Asia. This paper takes a closer look at the monetary policy objectives of Thailand, Indonesia, the Philippines and Korea, beyond traditional inflation and output stabilization. They have concluded thus far that policy-makers care more about exchange rate than interest rate volatility based on data from 1999 to 2007. The likely reason for this is that the growth of sectors heavily engaged in international trade is important to policymakers. Additionally, they believe these countries are no longer as dependent on advanced economies and that their trading activities with emerging markets such as China and India will become increasingly important.

When asked about what he thinks of IPED students, Dr. Hepp said “they often ask very insightful questions in class because they have a ‘foot in the real world’ ”. He believes this challenges him in the sense that students always want to know the real world application of a lecture. According to him, he has always been fascinated by the diverse backgrounds of IPED students: from all across the globe and very different life experiences.

Dr. Hepp applauds the IPED program for being well-established and having a wide alumni network. He reiterates the importance for IPED students to keep their focus internationally since this will aid students in attaining very good working opportunities either in the US or abroad. ■

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