Ashmore

Weekly Investor Research

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Summary: Global market sentiment continued to be very volatile leading into the year-end on account of the 'fiscal cliff' issue in the United States, rising tensions in the Middle East due to the situation in Syria, and slow progress in Europe in dealing with Greece and Spain. The problems in the HIDCs generated collateral volatility in Emerging Market asset prices but fundamentals remain healthy in Emerging Markets, where the economic indicators suggest that a modest upswing is now underway. We believe that year-end HIDC-related volatility presents an excellent opportunity to add Emerging Market exposure, just like previous HIDC panics.

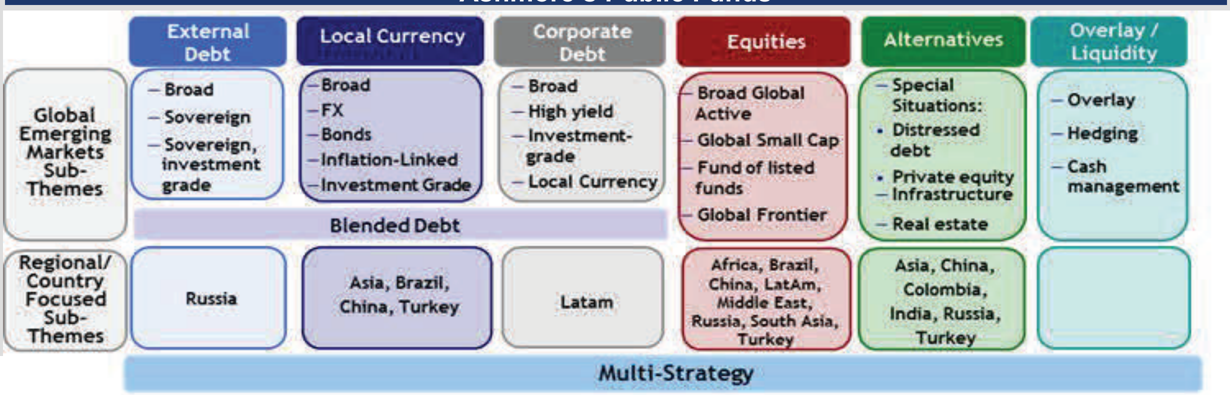
Global: The market's main focus remains the fiscal cliff issue in the United States. This week Republican members of Congress and President Obama began negotiations to seek to resolve their differences before the 'cliff' - a 4.1% of GDP fiscal contraction— comes into effect starting on 1st January. The key to a solution is reconciliation of the Republican commitment not to raise tax rates for the rich with a desire on the part of the Obama administration to raise revenues from the rich. Such a compromise could involve closing loopholes and broadening the tax base, but we expect brinkmanship and it is quite possible that the US has to go past the 1st January deadline before the political pressure rises sufficiently to produce a compromise. Uncertainty arising from the fiscal cliff issue is weighing heavily on US stock markets, which declined 2.8% over the past week, while US 10 year treasury yields declined from 1.65% to 1.59%. Another development worth noting is that both the FOMC minutes and Janet Yellen re-affirmed that the Fed is struggling with the question of how to exit QE, but that an exit is still a very distant prospect. Indeed, it seems very likely that the Fed will engage in open-ended bond purchases to replace the so-called "Twist" operation, which expires in December. In Europe, officials approved the Greek fiscal program, but continued to struggle with the question of how to divvy out the cost of bailing out the Greeks again. In our view, the Greek sovereign debt burden is completely unsustainable and the best policy would be to implement a credible haircut immediately. Support for Spain was also held up by disagreement between Germany and France over how to regulate banks. These unresolved issues continue to expose Europe to speculative attacks. Spanish 10 year bond yields rose from 5.67% to 5.94%, but EURUSD managed to end the week largely unchanged, aided in part by signs that the ECB is not about to cut rates, in part by the dovish commentary from Fed officials. In the UK, the Bank of England transferred QE profits to the treasury—pure monetary financing. Mervyn King, Bank of England governor, also said that the strength of the pound undermines UK competitiveness as inflation came at 2.7% versus 2.3% expected. It seems clear that the UK aims to reduce fiscal deficits via negative real interest rates and currency weakness. Opposition politicians in Japan also called for an explicit inflation target of 2%-3%. We believe that a major currency alignment in favour of Emerging Market currencies is likely to come about over the coming years. Finally, tensions within Syria spread to Israel over the past week, having previously affected both Lebanon and Turkey. We expect a cycle of escalating unrest in the region. Oil prices reflected this risk by rising $3 to just below $110 per barrel.

Latin America: In **Brazil**, September retail sales continued to expand at the August pace of 8.9% yoy on the back of credit expansion and a tight labour market. The September GDP proxy suggested that Q3 growth is running at a pace of 4.7% annualised. In **Argentina**, attention is now focused on how Judge Griesa will implement the pari passu ruling. His decision is expected before 2nd December. In **Mexico**, industrial production rose more than expected in September (0.9% mom, seasonally adjusted). In another positive development, the labour reform was passed by the Senate and should now become law barring any legal objections. Speculation increased about devaluation and new bond issuance in **Venezuela** following an increase in the parallel exchange rate premium as a result of recent election related spending. **Uruguay** announced a bond exchange to achieve significant maturity extension.

Asia: In **China**, the new leadership was announced with no major surprises. The 7-person Standing Committee is a finely balanced entity comprising reformers and conservatives, but with the two most powerful members in the pro-reform camp. We expect China's transition from export to consumption-led growth to accelerate now that the political transition is drawing to a close. USDCNY fixed sharply lower last week. **South Korean** unemployment fell from 3.1% in September to 3.0% in October. **Indian** WPI inflation dropped to 7.45% yoy versus 7.9% expected and 7.81% in the previous data release. **Philippines** exports rose a whopping 22.8% yoy in October versus 4.6% yoy expected.

Eastern Europe, Middle East: Ghana's October CPI declined to 9.2% yoy from 9.4% yoy in September. **South African** retail sales declined to 4.3% yoy from 6.4% you last month. President Ouattara reshuffled his cabinet in **Ivory Coast**. **Poland** released inflation data for October in line with expectations (3.4% yoy). **Zambia** announced that it is removing three zeros from its currency—the move has no implications for macro policy or the exchange rate, in our view. **Hungarian** inflation was lower than expected at 6% yoy versus 6.3% expected. **Russia's** head of the stock exchange announced that OFZ bonds will be Euroclearable by January 2013.

Ashmore's Public Funds



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