4 Reasons Investors Should Boost Their Exposure to Emerging Markets

Description

Emerging markets have performed poorly in recent years, weighed down by weak commodity prices, a stronger U.S. dollar, political crises and excessive debt. While these markets are typically associated with volatility, corruption, and political instability, recent data shows that they are more resilient and stable than investors believe. Emerging markets are attracting considerable attention from investors, as evidenced by the **iShares Core MSCI Emerging Mkts IMI ETF** (TSX:XEC) surging by 35% over the last year.

Despite that massive rally, there are signs of further gains ahead, which, when combined with the advantages of investing in emerging markets, makes now the time for investors to boost their exposure.

Now what?

Firstly, emerging markets are outperforming developed markets.

According to a report released by investment bank UBS, emerging markets' gross domestic product for the first half of 2017 has expanded at double the rate of that for developed markets. That can be attributed primarily to firmer commodity prices, particularly for base metals, coal, and precious metals, all of which are important exports for many developing economies.

The World Bank expects the recovery and stabilization of commodity prices to drive further growth among developing economies into 2018. This will be supported by improving economic sentiment as well as by increased political stability and reforms across a diverse range of emerging markets, including Brazil, Argentina, China, and India.

According to analysts from global fund manager Fidelity, emerging markets are attractively priced and growth remains robust, which, after almost a decade of weakness, makes them an appealing investment.

Secondly, emerging markets are not as volatile or unstable as many investors believe.

Data collated by *Bloomberg* shows that between 1999 and 2016, the best-performing markets annually were emerging markets; that was even after factoring in currency swings. That proves they are far more resilient and less volatile than investors believe.

Thirdly, they possess characteristics that are supportive of higher rates of economic growth.

These include favourable demographics and rapidly expanding wealth, which boosts consumption and business confidence. That means faster earnings growth for companies operating in those markets, which, in turn, helps to further boost GDP. This becomes quite apparent when examining the results from **Bank of Nova Scotia** (TSX:BNS)(NYSE:BNS), which has built a significant presence among emerging markets in Latin America. Its solid third-quarter 2017 results benefited from a 13% year-over-year increase in loans in Latin America and a 16% bump in the bottom line of its international banking business.

Finally, by investing in emerging markets, investors can obtain greater diversification, thereby reducing risk and enhancing returns.

One of the greatest problems with solely investing in the TSX is that the index is heavily weighted to financials and energy stocks, making up 34.5% and 20% of the index respectively. That leaves investors overly vulnerable to macro events such as the protracted oil slump, which now sees many upstream energy stocks trading at a fifth or less of their pre-slump prices.

So what?

There are significant benefits that come from investing in emerging markets that enhance returns and reduce risk for investors. This makes them an important consideration when it comes to portfolio construction. The easiest means of gaining diversified exposure to emerging markets is by investing in the iShares Core MSCI Emerging Markets ETF**,** which offers exposure to China, Taiwan, South Korea, Brazil, South Africa, and Mexico.

Another option is to invest in **Brookfield Infrastructure Partners L.P.** (TSX:BIP.UN)(NYSE:BIP), which owns a diversified portfolio of hard infrastructure assets across developed and emerging countries, including India, Brazil, Colombia, and China. The rapid growth of those nations, which is exacerbating significant domestic infrastructure shortages, will enhance Brookfield Infrastructure's earnings growth, sustaining further dividend hikes and its tasty 4% yield.

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