Charlemagne Capital

Latin America:

Much More Than Just A Commodity Story

Latin America's relationship with international equity investors has not always been a happy one over the last few decades. Indeed many investors have often regarded the region as secondary to other emerging market countries in Asia or the EMEA region. Often the perceived wisdom has been that Latin America offers investors little apart from commodities and political uncertainty and that domestic politicians were incapable of creating sufficient stability to allow disciplined economic policies to succeed.

Whilst in the past some of this thinking may have been correct, investors now risk missing out on one of the great emerging market stories by continuing to ignore Latin America and in particular the continent's dominant market, Brazil. Supported by strong democracies and disciplined economic policies in all the region's main markets, Latin America has weathered the global downturn remarkably well with countries such as Brazil not only entering the downturn later and at a less severe pace than many developed economies, but also now emerging into recovery at a much quicker pace.

Solid banking systems

One of the key supports for the region's economies during the downturn has been the strength of the banking systems. With virtually no exposure to subprime loans and low loans to deposit ratios, banks have continued to lend to both corporates and individuals throughout the crisis. In addition, state funded development institutions such as Brazil's BNDES or Mexico's Infonavit have provided additional financing into strategically important sectors. BNDES loans to Brazilian companies reached an all-time high of BRL 130 billion last year whilst Infonavit in Mexico has continued to support mortgages for low income households to help overcome the structural housing deficit in the country, which has reached 4 million homes. Particularly in Brazil investment in infrastructure spending has taken on additional urgency after the country won the rights to stage the football World Cup and the Olympic Games.

Commodity wealth supports consumption growth

Of course commodities have played a key part in providing a solid platform for the region from which to develop growth in other sectors. Mexico and Brazil are already self-sufficient in oil and Brazil is leading the way currently in the discovery of significant new oil fields. Chile is the world's leading copper producer and Peru has enjoyed one of the fastest growth rates in recent years based on its ample natural resources.

This however does not mean that Latin America is purely a commodity story. Whilst commodity stocks retain heavy weightings in Brazil's Bovespa index for example, commodities themselves make up only 50% of Brazilian exports which in themselves only account for 13% of GDP with China now being the main export partner.

Brazil's economy remains relatively closed and it is in the domestic sectors and consumer-related industries where the best performing stocks have been found over the last 12 months. The Magna Latin American Fund has been focussed on exploiting this domestic growth story by being overweight stocks that provide exposure to the increase in domestic consumption and the changing demographics of the region. Indeed it is the growth of the middle class and the accompanying increase in spending power which provides much of the support for the region's exciting prospects. Between 2006 and 2008 the B and C social groups grew by an estimated 18 million, with an accompanying increase in purchasing power.

With overall consumer credit penetration still low, falling interest rates, disciplined inflation targeting and an increased formalisation of the economy, we believe that the scene is set for sustained growth in consumer spending over the coming years.

/ continued

Charlemagne Capital

/ continued

Magna Latin American Fund favours Brazil and consumption stocks

This positive outlook on the Brazilian market in particular and consumer stocks is also reflected in the portfolio of the Magna Latin American Fund, with Brazil making up 65% of the Fund and consumer discretionary stocks carrying a 6% overweight relative to the benchmark. Our focus has been on retailers such as Lojas Renner which will benefit from the expected increase in spending power and the increased penetration of consumer financing which should continue to support strong sales growth. Of course the Fund also continues to find attractive opportunities in some commodity stocks such as Brazil's OGX, an oil exploration company which continues to trade at a substantial discount to its peers despite significant success in discovering new reserves. In Mexico, the Fund has gained exposure to the infrastructure story via homebuilder Homex and PVC producer Mexichem.

Whilst valuations are no longer at significant discounts to other emerging markets, the growth prospects of the region justify a further re-rating.

Stefan Herz
Portfolio Advisor, Magna Latin American Fund
December 2009

Marketing & Sales Department
Tel: + 44 (0)20 7518 2100 Fax: + 44 (0)20 7518 2199
Email: marketing@charlemagnecapital.com Website: www.charlemagnecapital.com

Issued by Charlemagne Capital (UK) Limited, 39 St James's Street, London SW1A 1JD
A company authorised and regulated by the Financial Services Authority