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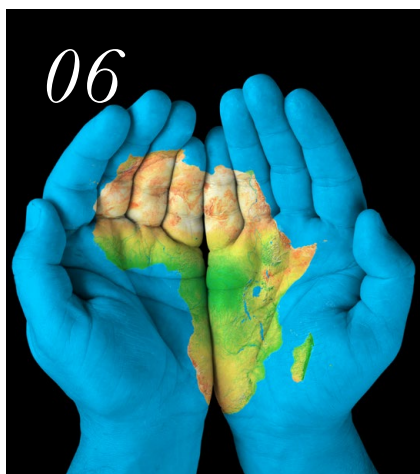
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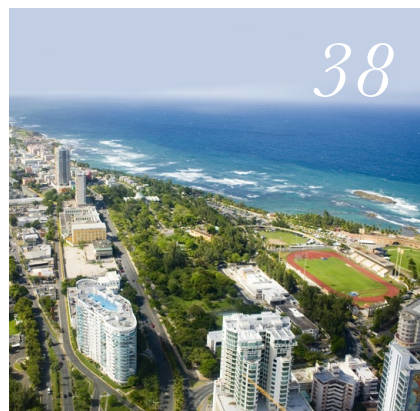
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Sharing Economy: Africa Finds Its Share in the Market

The concept of sharing economy has become a global phenomenon and after capturing several markets across Northern America, Europe, and Asia, it is now finding its way in Africa.

The pre-existing sharing culture in several African countries makes this business concept gain good momentum across the continent. In addition to global companies, such as Uber and Airbnb, which have witnessed exponential growth in their limited years of business in this region,



there are a host of home-grown players that are offering niche and country-specific services in this space.

At the same time, sharing economy business does face a great deal of challenges in Africa's complex markets. Safety concerns as well as limited availability and use of technology are two of the largest roadblocks for a thriving sharing economy business model. Although companies seem to find their way around these issues on their corporate drawing boards, the challenges are more intense and impactful in reality. Therefore, while the concept of sharing economy is likely to boom in the continent, it remains to be seen which companies manage to best adapt to local dynamics and thrive, and which players will fail in navigating the complexity of the regional markets.

Sharing economy businesses have been growing at an accelerating rate globally with leaders such as Airbnb and Uber taking over their traditional hospitality and travel competitors and becoming the largest players in the tourism and passenger transport sectors, respectively. After gaining huge market in several mature economies, the asset-light collaborative economic model is now making its presence felt in Africa. With vast youth population and a growing middle class, several markets in the African con-

tinents offer a huge growth potential for companies operating the sharing economy model. In 2016, Airbnb alone witnessed a 95% rise in the number of house listings in the continent, which increased from about 39,500 in 2015 to 77,000 in 2016. Moreover, the number of users of its online platform reached 765,000

While global companies are at a strong position to capitalize on this opportunity, there are a host of local players across the African subcontinent that are also looking for a share in the pie.

in 2016, witnessing a 143% y-o-y rise, and is expected to further expand to reach 1.5 million registered users by the end of 2017. Similarly, Uber, which entered Africa in 2013 through Johannesburg, has expanded into 15 cities across eight African countries in a span of just four years and has over 60,000 partnering drivers across the continent.

This remarkable growth is underpinned by a burgeoning middle class that is looking for (and increasingly can afford) convenient and reasonable solutions. Moreover, the sharing economy concept helps Africans bridge service gaps created by inadequate resources and infrastructure present in the continent. For instance, with increasing number of tourists and a limited number of high-end and mid-tier hotels or resorts, companies such as Airbnb are in a perfect position to fill such a demand-supply gap without much investment. In addition, sharing economy companies also help ease the unemployment and underemployment issues faced across several countries in Africa. The sharing economy model helps channelize a work stream for people who are unemployed or work in the informal sector, and provide them with a formalized platform where they can sell and market their services. Sharing economy is largely dominated by workers aged 18-34, which is also the age group largely affected by unemployment in Africa.

However, the key reason for the sharing economy model to have eased so well into the African lifestyle is the pre-existence of a sharing culture, which has been prevalent informally here for many years. Unlike in many developed regions, the concept of sharing economy is not new to Africa and the main task for global players entering this market was to formalize

Sharing Economy in Africa – Leaders and other players

Accommodation



4,000

Airbnb listings in 2016

Ride-sharing



1 million

rides within first 15 months of operations

GLOBAL

LOCAL

Ride-sharing



2,500

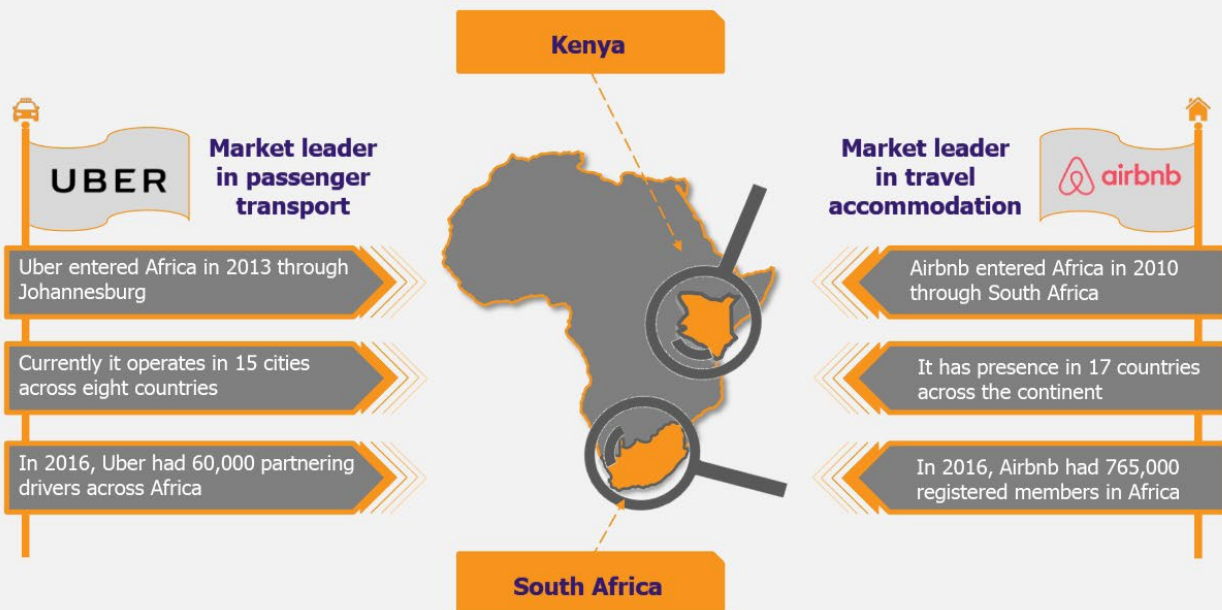
drivers by the end of 2016

Professional Services



400

registered service-providers in 2015



Accommodation



394,000

guests used Airbnb listings in 2016

Ride-sharing



2 million

rides in H12015

Wi-Fi Sharing



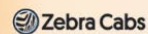
52,000

community generated hotspots in 2015

GLOBAL

LOCAL

Ride-sharing



Accommodation



afristay

Medical



medici



**These lists are indicative and not exhaustive*

it through tech-based platforms. Therefore, despite being one of the least developed regions globally, Africa comes as a good fit to the sharing economy model. As per a survey conducted by AC Neilson in 2014, 68% of respondents in the Middle East and Africa region are willing to share their personal property for payment, while 71% are likely to rent products from others. These numbers are much higher in Africa than in Europe and North America, wherein only 54% and 52%, respectively, are willing to share their possessions for pay and even fewer (44% and 43%, respectively) are interested in renting others' products.

While global companies are at a strong position to capitalize on this opportunity, there are a host of local players across the African subcontinent that are also looking for a share in the pie. Although these companies have come up across Africa, they are somewhat clustered in the more developed regions of South Africa, Kenya, Nigeria, and Uganda.

South Africa

Being one of the most developed economies in the subcontinent, South Africa has openly embraced the global sharing economy phenomenon and has been the entry point into the continent for several leading international players such as Uber, Airbnb, and Fon. Uber has

received great acceptance in South Africa with the first 12-month growth rates in Cape Town and Johannesburg superseding the growth experienced in other cities globally, such as San Francisco, London, or Paris (during their first year of operations). Uber provided 1 million rides in 2014, which was its first year of operation in South Africa, rising to 2 million rides by the first half of 2015. The company has also created more than 2,000 jobs in the country where unemployment levels are as high as 30%. Likewise, Airbnb boasts of similar growth in the country. In 2016, about 394,000 guests used Airbnb listings for their stay in South Africa, in comparison to 38,000 guests in 2014. During that year, Airbnb's users generated US\$186 million (ZAR2.4 billion) worth of economic activity in the country, of which about US\$148 million (ZAR1.9 billion) was attributed to Cape Town, Johannesburg, and Durban. Fon, an unused bandwidth sharing company, also enjoyed success in the South African market and more than doubled its community hotspots from 21,000 (at the time of its launch in 2014) to 52,000 community-generated hotspots in 2015. Taxify is another global player in the ride sharing space. Launched in 2015, Taxify is an Estonian company offering similar services as Uber. The company has managed to acquire 10% of South Africa's ride sharing market by offering 15% lower fares compared with Uber, while providing a higher driver payout (Uber

takes a 20-25% cut from drivers while Taxify takes a 15% cut).

These international players are challenged by several local companies, which, despite being much smaller in size, are competing on both price as well as local expertise. In the ride sharing market, there are several smaller domestic players, such as Zebra Cabs, Find a Lift, and Jozibear. Similarly, in the accommodation sharing market, acting as a direct competitor to Airbnb is South Africa's local, Afristay (formerly known as Accommodation Direct). The company has applied a country-specific approach and has succeeded in providing more varied and cheaper options as compared with Airbnb in South Africa. Having a single country focus, Afristay has close to 20,000 listings across 2,000 locations in South Africa. Airbnb on the other hand has 35,000 listings in the country.

Another emerging space of sharing economy concept adoption in South Africa has been seen in the medical sector, wherein players, such as Medici and Hello Doctor, are connecting patients with medical practitioners. Hello Doctor currently services around 400,000 patients in South Africa. Medici, which launched in May 2017 has partnered with the Hello Doctor and aims at connecting rural and less developed regions to remote access medical advice and consultations.

Kenya

Owing to a burgeoning middle class as well as an increasing access to education and the Internet, Kenya is a strong market for the digital sharing economy. Airbnb witnessed significant growth in Kenya, increasing its listings in the country from 1,400 in 2015 to 4,000 in 2016. The number of guests choosing to stay in an Airbnb accommodation have also expanded three-fold during the same period. Uber has received a similar response in the country, completing 1 million rides in its first 15 months of operations (beginning 2016), and having 1,000 drivers registered with them in the beginning of 2016. However, a local Kenyan company, Little Cabs, which is owned and operated by the country's leading telecommunication players, Safaricom in partnership with Craft Silicon, a local software firm, is a stiff competition to Uber. The company, which began operations in July 2016, managed to acquire 2,500 drivers and 90,000 active accounts by the end of the year, owing to more attractive pricing and driver-payout in comparison to Uber. Moreover, it offers several services, which have not been introduced by Uber in Kenya yet. Having the backing of the leading mobile network operator, Little Cabs is attracting customers by offering them discounted mobile recharge along with trips, free Wi-Fi for passengers, and the option to process payments using M-Pesa – Safaricom's mobile money service,

which has two-third share in mobile market in the country. However, despite a smaller fleet size and less attractive services, Uber continues to be the market leader in Kenya for now, with a revenue share of about 30% (in comparison to Little Cabs, which has a revenue share of about 10%) primarily due its global brand value and first mover advantage.

Airbnb witnessed significant growth in Kenya, increasing its listings in the country from 1,400 in 2015 to 4,000 in 2016.

Another newcomer to the sharing economy market in the country is Lynk, which aims at connecting service providers across about 60 categories to customers in Kenya. These include services such as plumbing, beauty works, tuition, or party planning. Having started operations in 2015, the company

identified and recruited about 400 workers across 60+ service categories, who provided 800+ services to paying customers within its first year of operation.

All of that being said, the sharing economy concept has not had that easy of a ride in the continent and has faced one too many challenges on its way up. The main issue challenging the success of this concept has been the limited use of smartphones, which are inherent to this business model. While the use of smartphones in today's time is taken for granted in most economies across the globe, this is not the case in Africa. In many cases, these service providers (especially drivers) are using smartphones for the very first time in their lives. Although the youth population is expanding in the continent, elevating the demand and use of smartphones, the numbers still remain extremely low – both at the consumers' as well as service providers' end. In 2015, only 24% of Africans used Internet on their mobiles and e-commerce penetration was mere 2%. This makes it imminent for companies looking to excel in the sharing economy space to provide training and workshops to help service providers adapt to and embrace the smartphone technology. Companies aiming to build a stronger position in the market over their existing competitors should also look at providing cost effective and easily accessible financing for the purchase of smartphones for service provid-

ers interested in registering in their sharing apps. In the African scenario, such a move would incentivize service providers to join the company's sharing platform, potentially choosing it over other competitors present in the market, while the company would be able to expand its supply-end of the business by growing the registered service providers' base.

The other issue that is key to operating in Africa is safety. Since the entire concept of sharing economy is based on trust, ensuring safety becomes a very important aspect in this line of work. Considering the high number of cases of theft and vandalism as well as weak regulatory system, African customers' trust in service providers in their region is naturally lower than the western market customers' trust in their local service providers. This impedes the service use growth and forms one of the largest barriers for sharing economy to reach its full potential in the continent.

In the transportation segment of the sharing economy market, the issue of safety is increasingly addressed by several players. To ensure safety of passengers, drivers undergo a rigorous background check that includes a multi-level verification. Companies also undertake innovative approaches to ensure only verified drivers work under the company logo in attempt to improve safety. In one such case, Uber introduced a 'selfie protec-

tion' feature, in Kenya, wherein a driver is required to take a selfie in the Uber app once in a while, before accepting a ride request from a customer. In case the photo does not match the one registered with the account, the account is blocked. In a market such as Africa, while safety precautions are a necessity, if marketed correctly, they can also be a differentiating and marketing factor. Along with general information and ratings, companies can also show driver's verification details and training credentials on their app before a consumer selects a ride. In case of other services, they can also include details of the certifications undertaken by the service provider.

In addition to this, the limited use of plastic money – which is the main form of payment in sharing economy-based businesses globally – is another speedbump in the operation of such a business model in Africa. While several ridesharing companies are tackling this issue by introducing cash payments, it remains a limiting factor for companies whose services nature leaves a limited scope for introducing cash payments option, e.g. Airbnb.

Regulatory barriers and outburst of traditional competitors is another challenge, however these issues are common for players across markets globally, though in various intensity. We have talked about it in more detail in our article in October 2016, *Sharing Economy Needs Regulator Support*. Companies such as Uber

have had to face several regulatory roadblocks, the latest of that being a July 2017 lawsuit ruling recognizing Uber drivers as employees (instead of the company-preferred 'driver partners') as per South Africa's labor laws. While the company does have plans to work around this ruling as it currently only applies to the seven drivers who filed the lawsuit, such issues have the potential to disrupt the companies' smooth operations in the country. There have also been severe protests from traditional taxi companies and Uber has faced several safety-related problems with Uber drivers being attacked and cars being burnt in Kenya, as well as cases of smashed windscreens at railway stations in South Africa. To counter this, the company has posted security guards outside railway stations in Johannesburg for the security of the drivers.

EOS Perspective

While the concept of sharing economy seems to fit perfectly in the African lives, it does require the companies to follow a very localized approach accounting for specific regional dynamics in order to blend with the countries' local fabric. While this gives an advantage to the local companies that better understand customer needs, it becomes difficult for them to match the scale of global leaders who have hefty marketing budgets.

Although sharing economy has largely captured the travel and passenger transport, with medical, education, and several other vocational services also seeing new businesses entering with sharing economy model, it is the crowd financing segment that might see the next boom in Africa. African region houses several dynami-

cally emerging economies, with huge hunger for capital, and digital crowd funding platforms can help SMEs connect with potential investors, and help African start-ups with seed capital. In addition to basic investment, these platforms can also offer mentoring opportunities to small start-ups. While there already are a couple of companies,

such as VC4Africa, that are operating in this space, crowd financing as a sharing economy business still has great potential to be tapped in Africa, especially beyond the Tier 1 cities of Johannesburg and Cape Town, where ideas are in abundance but there is lack investment and support.

EOS intelligence

incisive research. actionable insights.

About the Author

Established in 2010, EOS Intelligence is a professional services firm that delivers decision-enabling research and analysis solutions targeted at corporate, consulting and investment organisations. EOS Intelligence was founded with the objective of supporting emerging market -focused growth and optimisation strategies of both global and small and medium enterprises.

www.eos-intelligence.com

Look Before You Leap Into LatAm: AG3 Consulting

Would you dive into a lake without knowing its depth? You might, when the water is cool and the stone is burning your bare feet. Rational people do make bold choices, and sometimes they get in over their heads. That's why we have lifeguards. For the purposes of this metaphor, that cool water is Latin America—enticing, yet fraught with hidden hazards. The lifeguard is AG3 Consulting. And the hazards? You'll have to ask AG3—unless you prefer to discover them the hard way.

AG3 Consulting is a marketing intelligence company. But what does that mean? Put simply, marketing intelligence is practical, actionable information about your market that empowers you to make educated, rational decisions. Without it, you're flying blind. You're taking a leap of faith and hoping that the water is deep enough. AG3's job is to take faith out of the equation.

Think of it as your sonar, your periscope, your spy satellite, your surveillance drone. Sometimes it's a squad of professional statisticians compiling and synthesizing survey results from a representative sample of your target demographic. Sometimes it's a guy shoveling the contents of your competitor's dumpster into a rented pickup truck for later analysis. Of course, that's not what AG3 Consulting is suggesting when they talk about using "traditional and innovative techniques" for collecting market research data—but don't think it never crossed their minds.

In precise terms, AG3 Consulting offers market studies to help companies better understand three critical elements that will determine their success in Latin America: 1) external competition environment, 2) image among stakeholders, and 3) the unique, unpredictable challenges facing companies who want to enter the Latin American market. In broad terms, AG3 are your eyes

and ears in Latin America. Their job is to tell you whether you should get in, how you should get in, and what to do once you're in.

AG3 Director Geisa Rodrigues understands Latin America. Most importantly, she understands that Latin America is not a monolith; profound cultural and economic divides exist not just between, but also within its constituent countries. And after twelve years in business, AG3 has cultivated contacts everywhere, across an array of industries, who have the answers you need before you take your next step—whatever you're planning. Want to know what Costa Rican dentists are gossiping about right now? AG3 will have that report on your desk before you have time to say you were kidding.

"We started our business twelve years ago. We started by doing competitive intelligence projects, which are focused on understanding competitors. We started in tele-



communications doing competitive intelligence projects, understanding how competitors were planning to launch some services and their position in the market. We have expanded to market research because this is a wider field and we can understand more things additional to the competition.”

AG3 started out in Brazil, where their headquarters are, and they have since expanded their scope of their research to include nearly every country in Latin America. Their focus, however, is usually on the principal powerhouses in the region: Mexico, Peru, Argentina, Chile, and Colombia—and of course, Brazil. “For the last eleven years we have focused primarily on

market research and market studies which include market entry studies, customer satisfaction, image position, helping clients who are interested in entering some specific country or understanding the market size of this particular country, helping them to do that before they really do some action and really spend some money.” So if you’re thinking about

getting your feet wet in any of those countries, it's worth waiting for AG3 to give you the all-clear.

The good news is: they usually will. "Most of the time market research confirms that the service or the project is OK, but needs to be changed somehow," says Rodrigues. "But the client can keep going." Other times, though, they've had to blow the whistle. "We feel sorry when the client has some ideas to launch in some country, and they have to pay for market research, and market research does not give them a positive answer. But it happens."

Rodrigues remembers one such instance involving frozen salmon. It was a fishy case: the client wanted to have a go at importing frozen salmon for the Brazilian market, and they had done some investigation themselves. In fact, they already possessed the most important quantitative data of all: in order to turn a profit, they would have to sell their frozen salmon at a higher price than that of the fresh salmon from Chile

that was already quite freely available in supermarkets. That naked fact alone would be enough to stop most people in their tracks, but this particular client was canny enough, and determined enough, to realize that they were still missing an equally critical piece of qualitative information: "Who cares?"

Already well aware of the most self-evident obstacle to selling their overpriced, frozen salmon in a country awash in cheaper, fresher salmon, the client—undeterred—hired AG3 to hit the streets and ask the most important questions: Will people care about the difference? Will enough people care about the difference? Will enough people care—enough—about the difference? In this case, says Rodrigues, their findings were less than shocking: "Yes. Enough people will care—enough—about the price and the quality, which means that not enough people will buy your salmon." Maybe you don't need a PhD and mountains of data to reach that conclusion. But in this case, that's

what it took to stop one very bold client from breaking their neck on the rocks.

In their own words, AG3 is in the business of "shielding the company from threats and making it prosper," and the most important aspect of that mission may just be protecting clients from themselves (though perhaps AG3 would put it differently). Giving the go-ahead to an eager client, even when it comes with caveats, warnings, or constructive criticism—that's the fun part of the job. Ultimately, they're paid to blow the whistle, wag the finger, and deliver bad news. Like a lifeguard, AG3 is there to stop you from doing anything you'll regret and to warn you against hungry new competitors in the water, ominous political stormclouds on the horizon, or the ever-shifting tides of consumer whims. But unlike a lifeguard, AG3 Consulting can't drag you to back to shore if you get out of your depth, and they don't do CPR. AG3 looks—you leap.

About the Author

AG3 Consulting is a 12-year established full market research agency covering Latin America, with headquarters in Brazil and local teams in many countries (Mexico, Chile, Argentina, Colombia, Peru, Costa Rica, Guatemala, Panama, etc.). They offer full service market research or select services (recruitment only, field work, etc.) for global/marketing strategic consulting agencies such as Deloitte, PWC, Fuld & Company as well as brand/communication/AD agency such as IDEO, among others, offering them either local field work or full service when required. Their expertise covers qualitative, quantitative and competitive intelligence studies among different industries, using diversified methodologies and segments (B2B, B2C).

Afghanistan: Exploring the Untapped Potential

Few people would place the words “Afghanistan” and “investment opportunity” in the same sentence. But Ehsan Bayat, the Founder and Chairman of the Bayat Group, is working hard to develop his homeland—and its image abroad—to reflect the vast potential of its people and resources.

An Afghan native who emigrated to the United States during the Soviet occupation, Bayat returned to Afghanistan in 1998 armed with a Western education, nearly twenty years of entrepreneurial experience, and invaluable ties to the land and

its culture. Today, the Bayat Group is the largest diversified services company in Afghanistan, as well as its largest private employer. In the last twenty years, the Ehsan Bayat has weathered regime change, war, and insurgency while developing the infrastructure—and the relationships—necessary to get things done in what he prefers to call a “misunderstood” market.

What they do, specifically

The story of the Bayat Group began with an exclusive license to establish computerized telephone exchanges in Kabul and Kandahar in 1998. Bayat has been on the ground in Afghanistan since before the US intervention in 2001 which overthrew the existing regime, and has adapted and flourished amidst all that came afterward. That telephony business became Afghan Wireless, was the first telecommunications company in Afghanistan and today delivers wireless and broadband solutions

to more than 5,000,000 people. AWCC was not only the first telecom provider in Afghanistan, it established Afghanistan's wireless communications sector, which today, is the largest and profitable part of Afghanistan's economy.

In addition to bringing cell phone and internet service to millions of Afghans, Bayat Group owns and operates Ariana Television and Radio (ATN), Afghanistan's largest private media organization. With two television channels and two radio channels, ATN's coverage reaches all 34 provinces and more than 25,000,000 Afghans. Since the early years, Bayat Group has branched out in a big way, building on the success of their telecom ventures, which by connecting Afghans to one another—and the wider world—enables businesses of all types to be established and to prosper. Monty Simus, VP of Business Development, called their initial focus on wireless communication an “enabling investment” for a country that still lacked vital infrastructure.

The Bayat Group has expanded and established a portfolio of the expected variety of security, logistics, and infrastructure companies necessary for its operations all over the region, but the next big step for Afghanistan (and Bayat Group) is the development of the country's energy resources—specifically, its oil and natural gas reserves. “Afghanistan is one of the least self-sufficient countries in the world in terms of power,” Mr. Bayat has said. Decades of warfare have taken a toll on Afghanistan's power grid, and nobody has built a new gas-to-energy power plant in the country since the Soviet invasion.

Enter Bayat Energy. With an initial focus on “the exploration and production of the large undiscovered oil and gas reserves in the northern region of the Islamic Republic of Afghanistan,” Bayat Energy aims to harness the resources and build the infrastructure needed to power Afghanistan for decades of future development. Presently, Afghanistan imports the vast majority



of its energy from the neighboring countries of Uzbekistan, Turkmenistan, and Iran. In December 2016, Bayat Energy recently signed a \$250,000,000 memorandum of understanding with the national government to build a 200-megawatt gas power plant, Bayat-1, in the north of the country. “Our hope is that it will catalyze change in the power network and the laws and make it easier to come and invest in this field,” says Mr. Bayat.

The third pillar of Bayat’s vision for Afghanistan’s future is an investment in its most valuable resource: the Afghan people themselves. The Bayat Foundation, Afghanistan’s largest charitable initiative in the country, has contributed to more than 300 projects that improve the quality of life and opportunity for the most disadvantaged in Afghan society: 14 hospitals (and counting), thousands of eyeglasses (with protective cases) for the visually impaired, thousands of hearing aids, countless schools erected or refurbished, food and clothing for orphans, clean drinking water...name a need, and the Bayat Foundation is already working on it. Of course, businesses around the world frequently engage in charity (often with a publicity budget to match), but Bayat’s motivations go well beyond tax credits or good optics. He is investing in the future of an entire country and

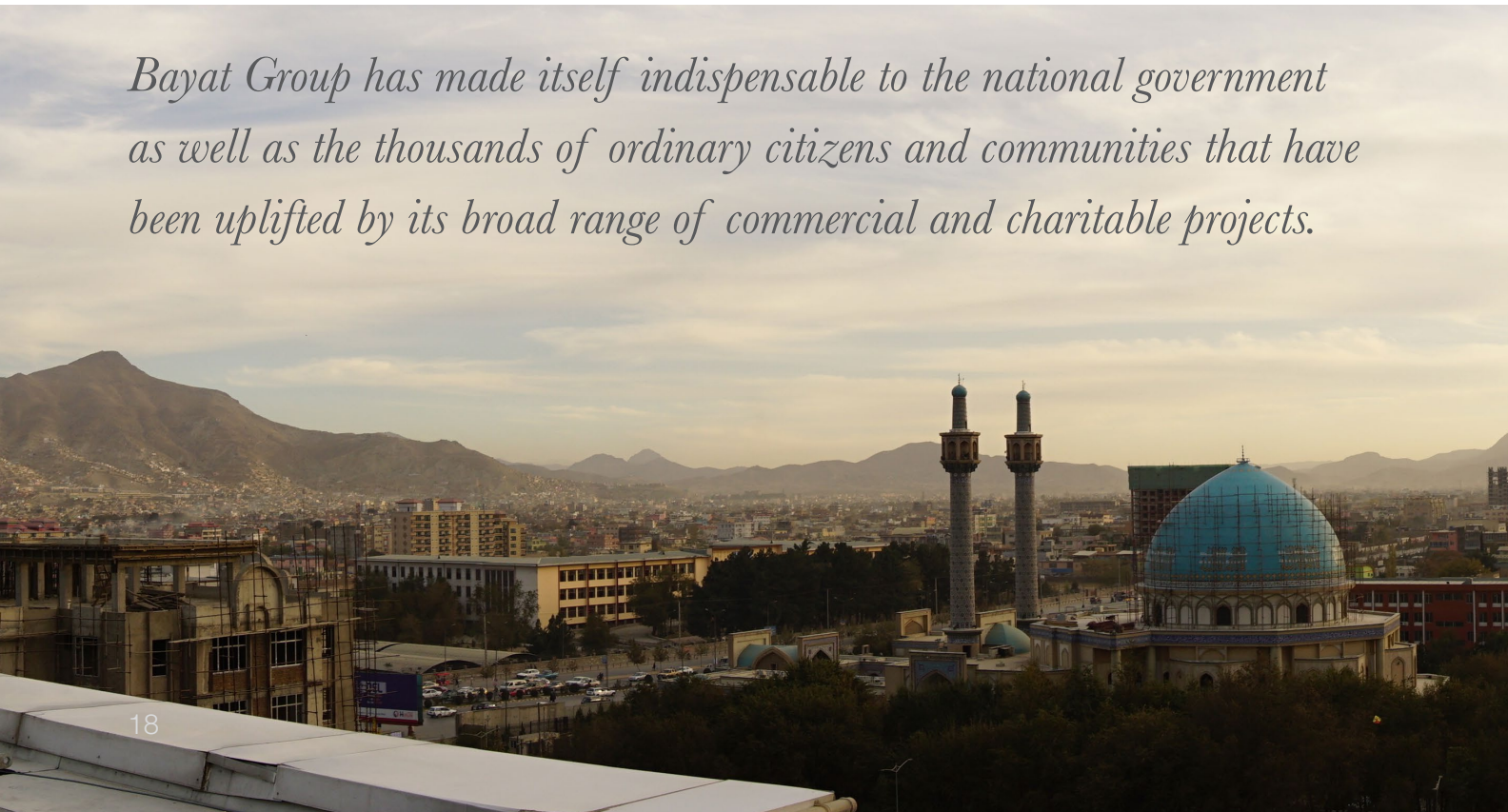
there can be no future for his enterprise if there is no future for the people. And to be perfectly blunt, if you want to get anything done in Afghanistan, you need the people on your side.

Why they’re good at it

Outsiders are wary of Afghanistan—that’s no secret. Many billions of dollars have vanished there without a trace. So if the story of Bayat Group, one of success and optimism, doesn’t sound like the Afghanistan you know, that’s because it isn’t. This is Bayat’s Afghanistan. Bayat Group doesn’t owe its success to pioneering cutting-edge technologies, or to “disrupting” the status quo, or “changing the paradigm.” The Bayat Group has managed to make itself welcome in what is arguably the most forbidding region on the planet. That didn’t happen overnight, nor is it something that everyone can hope to achieve.

Common wisdom dictates that anyone considering investment in a so-called “emerging market” must have a local partner. But Afghanistan isn’t your typical emerging market, so Bayat Group is more than your

Bayat Group has made itself indispensable to the national government as well as the thousands of ordinary citizens and communities that have been uplifted by its broad range of commercial and charitable projects.



typical “local partner.” As the country’s largest private employer, largest charitable organization, and one of its largest taxpayers, Bayat Group has made itself indispensable to the national government as well as the thousands of ordinary citizens and communities that have been uplifted by its broad range of commercial and charitable projects. Mr. Bayat explains: “By employing locals for projects – building roads, hospitals, cell towers – you minimize risks to your network, because it is now their livelihoods and they have a vested interest in making sure it’s successful.” And as Monty Simus points out, Bayat Group has even received formal recognition from the ruling establishment for their company’s contributions: “We got the award for being one of the largest tax payers in the country, so we have been privileged to grow alongside the government in its regulatory understanding and responsible development of that sector.”

But the fundamental difference is that for Ehsan Bayat, investment in Afghanistan’s future isn’t just about business; it’s personal, too. Without the ties that drove Mr. Bayat to return to Afghanistan, and to adapt and persevere through daunting levels of challenge and transformation, no outsider would have been willing to

take the early risks that were necessary to establish a foothold and build on it. As Simus recognizes, “Other investors that maybe don’t have as much vested interest as Dr. Bayat does in rebuilding his country might be reluctant to come, but we are quite happy to welcome other players.” Bayat Group has already taken the big risks, and the rewards have been commensurate.

Description of the opportunity they are capitalizing on/developing

So what comes after Bayat Energy? “We are quite proud that we gave rise to this entire sector,” says Simus. “Yes, in the first market we accumulated sort of competitive benefits and advantages, but this is a nation of 35 million people that need lots of services. This is a nation that needs dozens of power plants—and wouldn’t it we love to be the only company for over 15 years? Absolutely, but it’s not realistic. We continue to build out our space, our segment of the market, and we’d love to apply our investment in other sec-



tors or other countries around the world.” Not one to put the cart before the horse, Bayat Group are still focused on developing the energy generation and distribution infrastructure that Afghanistan so sorely lacks. Solar power and other renewable ventures have been duly considered, but Simus is pragmatic: “Whether the country is trying to launch mining or agribusiness, it’s going to need power, and the fastest way to get power is by using the natural gas in the ground.”

In Afghanistan, time is indeed of the essence. Nearly 50% of the population is under 15 years old, and the future of Afghanistan’s youth, and the future success and stability of their country—even the region as a whole—depends on giving them opportunities. “The second vector for what we’ve looked at is more of a response to what the nation truly needs—and that is lots of jobs,” says Simus. “I’ve got a roster of ten different businesses, which I call our social businesses, which have been modeled and are ready to launch anytime. We want to launch these businesses so they revolve in the space like agribusiness, sanitation and health, off-grid solar power, etc.” Food and medicine are always in fashion, but nothing is off the table when you’re starting from scratch—there are far worse alternatives, as Simus is bold enough to recognize: “It’s better for the world. In the future it will reduce the number of obligations that people might think of—financially, militarily or otherwise.”

Since 2002, Afghanistan’s GDP has rocketed from just \$2.2 billion to more than \$22 billion in 2015, yet its imports still exceed its exports by a factor of 13. Bayat Group’s vision is for a more self-sufficient Afghanistan—not just in energy, but in other crucial areas like pharmaceuticals and agriculture, which will spawn what Simus calls “ecosystems” of parallel employment and productivity: “With agribusiness you give rise to groups doing the transportation, or they give rise to marketing and distribution companies. Or in the world of pharmaceuticals, you prove that the nation doesn’t need to import all its medical equipment or medical supplies, and you move quickly from IV fluids to pro-

ducing the rubber gloves, and then all of a sudden you build the thematic.”

No one can predict exactly what the future of a more developed and prosperous Afghanistan will look like. All that is certain is that Bayat’s intertwined business and humanitarian initiatives will continue to play a leading role. And thanks to changing perceptions and attitudes engendered by the successes they have had there, Bayat Group won’t have to go it alone. “I think it’s early in the game,” says Simus. “I think we need more great success stories. Dr. Bayat is a very modest guy, so we don’t like to toot our own horn too much, but we are tooting the opportunity that the nation has. Let’s do good while we’re making money at it.” No one but Bayat Group could have looked at Afghanistan and see a “win-win” scenario, and no one but Bayat Group could have gone there, and made it so.

About the Author

The Bayat Group of companies has more than fifteen years of experience building highly profitable enterprises in Afghanistan in the telecommunications, media, industrial infrastructure, energy, and financial services sectors, and we have a proven ability to work successfully with government officials/organizations at both national and regional levels in order to help build out industries that generate profitable returns and also set the base for long term economic growth for the nation.

Spotting Opportunities in Brazil at Times of Economic Recession

 **An Hodgson, Income & Expenditure Manager**

Brazil's economic recession and socio-political turmoil is the story of a major emerging market in crisis, with implications for many consumer goods companies.



In the face of rising unemployment and falling wages, compounded with rising inflation and currency depreciation, consumer expenditure per household fell by

9.3% between 2014 (the year Brazil's economic recession began in its earnest) and 2016. As well as spending less, Brazilian households are also changing their con-

sumption habits with a shift away from the culture of 'consumerism' towards a greater focus on value for money. Insights into Brazil's consumer spending in times of eco-

conomic recession can help businesses adjust and adapt as well as identifying opportunities in the country.

Between 2011 and 2016, Brazil's consumer market as measured by total consumer expenditure expanded by 7.8% in real terms, equivalent to an average rate of only 1.5% per year. During this period, Brazilians made the largest spending cutbacks on communications and leisure and recreation while spending on clothing and footwear and transport saw no real increase;

Interestingly, alcoholic beverages and tobacco was the fastest-growing spending category, consumer expenditure on which grew by 23.6% in real terms between 2011 and 2016. However, the volume

sales of alcoholic drinks in Brazil has been declining steadily since 2012. This indicates that Brazilian consumers across the income spectrum had opted to purchase less in quantity but better in quality.

Brasil Kirin: Tapping the trend of consumers trading up in beer

Recognising the trend of consumers trading up in beer, Brasil Kirin invested heavily to add two premium brands, Baden Baden and

Eisenbahn, to its existing portfolio of domestic mid-priced beers;

Despite the recession, Baden Baden and Eisenbahn have performed well, as they enjoy high brand-awareness and respect from consumers especially in the south and southeast regions. In 2015, the company opened an internet retailing channel for its premium brands, aiming to reach those that do not live in the key areas of operation. In 2015, Brasil Kirin ranked third in Brazil's alcoholic drinks market, a position achieved thanks to its strong performance in the beer category.

Brasil Kirin was sold to Heineken in early 2017 as Kirin's Japanese owner shifts their strategic interest



Retail Sales Value of Brasil Kirin: 2008 - 2015

Actuals and Growth, Retail Value, GBO, US\$ mn, fixed ex rates

Growth Decline ■ 2008 ■ 2015 Sort by: Last Year ▼

Brazil

Other Latin America

Uruguay



Source: Euromonitor International's Competitor Analytics

to Southeast Asia, but the company's expansion hitherto was a case study of a business understanding the changing consumption pattern and successfully spotting opportunities amid a difficult economic climate.

Brazil's real consumer expenditure is forecast to grow by 1.9%

household disposable income is not expected to overtake its 2014 level before 2025. In this context, companies will need a granular approach to pinpoint pockets of growth, because opportunities in Brazil will be uneven between different consumer spending categories, age cohorts and income bands, as well as across cities and regions.

For more analysis please read the full report: Brazil's Consumer Spending in Times of Economic Recession

About the Author

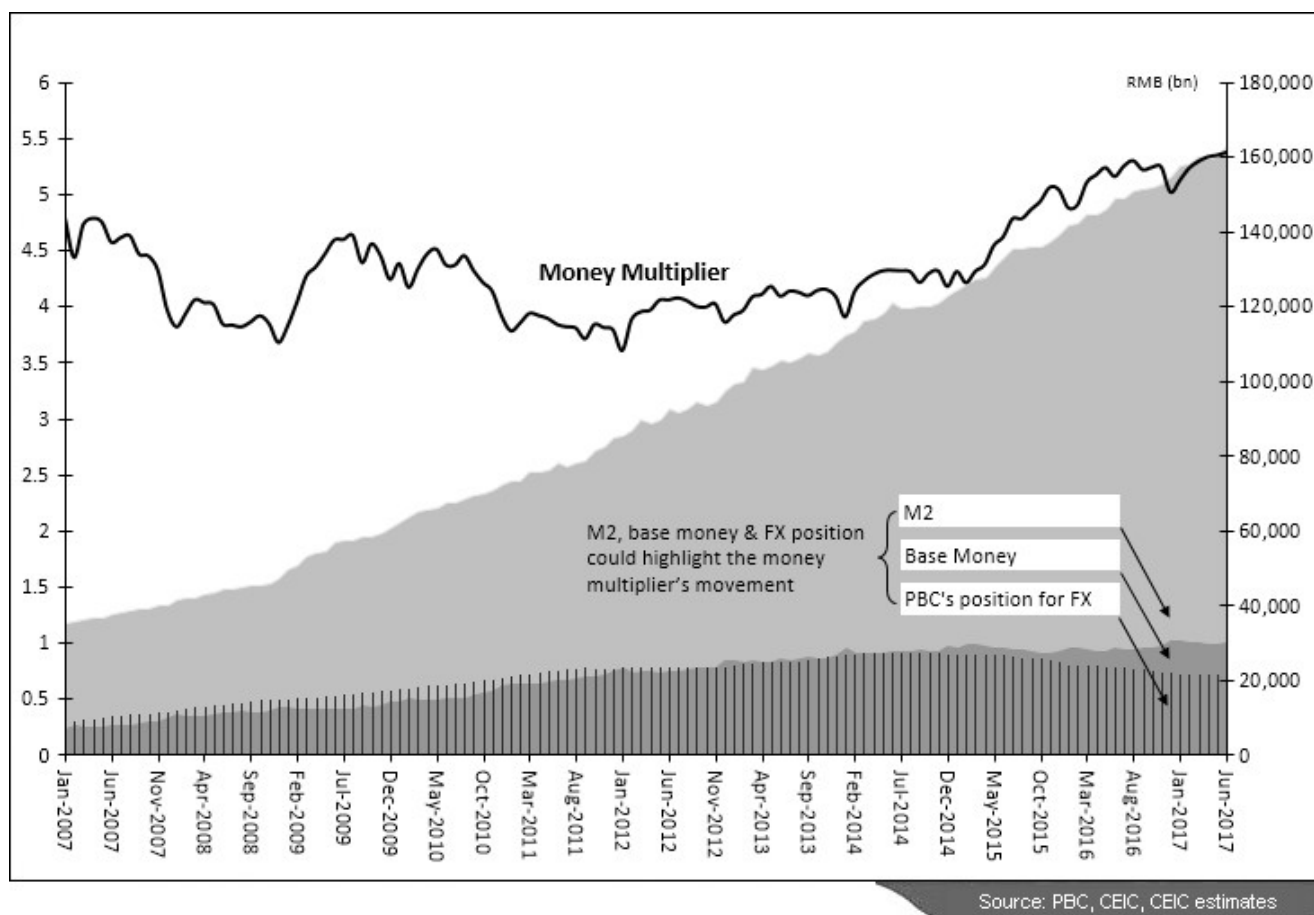
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China's Money Creation

The forecasting ability of the money multiplier is becoming increasingly non-indicative as the call for more supervisory policy is becoming more prevalent.





Source: PBC, CEIC, CEIC estimates

The potential money multiplier is equal to $1/RRR$ in which RRR refers to the required reserve ratio of the whole banking system. The actual money multiplier is equal to the ratio of money supply (M2) to base money. Normally, the actual money multiplier is lower than the potential money multiplier because of the following factors:

- Households and businesses hold cash and in turn, set the foundation of the money creation process
- Banks hold excess reserves to meet cash withdrawal needs

The increase in the size of the money multiplier reflects the recovery of

market confidence. It implies a higher willingness of financial institutions and investors to engage in lending and borrowing activities. Thus, the money multiplier could potentially act as a leading indicator with forecasting ability. China's money multiplier reached 5.37 at the end of June, which was the highest level ever recorded. In fact, M2, base money and foreign exchange position could highlight the money multiplier's movement.

In the first quarter of this year, alongside the passive shrinking of PBC's balance sheet, base money declined and M2 kept on rising. These both contributed to the increase in the

money multiplier. In June, PBC tried to maintain financial stability by expanding its balance sheet in order to improve liquidity. With the slight increase in base money and the continuous rising trend of M2, the money multiplier was further boosted up.

Nowadays, shadow banking is gaining significant influence on money derivatives. Foreign exchange positions at the same time also affects money issuance directly. As a result, the effectiveness of monetary controls in China are under a lot of pressure and thus related forecasting ability has become very ambiguous.



A Euromoney
Institutional
Investor Company

About the Author

Founded in 1992 by a team of expert economists and analysts, CEIC Data www.ceicdata.com provides the most expansive and accurate data insights into both developed and developing economies around the world. A product of Euromoney Institutional Investor, we are now the service of choice for economic and investment research by economists, analysts, investors, corporations, and universities around the world.

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The Small Country Effect:

What research says about whether small-country stocks generate bigger returns

 **Gregg Fisher, Ronnie Shah And Sheridan Titman**

Are foreign stocks finally emerging into the sunlight from hibernation? From January 2010 to December 2016, overseas stocks (as measured by the MSCI World ex USA Index) returned just 3.64 percent annualized, compared to 12.83 percent for the S&P 500 Index. The cumulative return for U.S. stocks during those seven fat years was 133 percent, more than 100 percentage points ahead of the meager reward investors earned for their patience with foreign stocks. But in 2017, year-to-date to July 31, 2017, international equities returned 17.1 percent versus 12.1 percent for the S&P 500 Index.

In connection with that, let's discuss a distinct approach to investing in foreign stocks around which my

firm and co-authors Ronnie Shah and Sheridan Titman have conducted considerable research. Whether we are investing in foreign or U.S. securities, we practice multi-factor investing, in which equity portfolios are tilted away from a passive index to security characteristics such as value, smaller size, momentum and profitability.

Most passive indexes, such as the S&P 500 or MSCI EAFE Index, are market capitalization-weighted, thus allocating the bulk of weight to the largest companies and creating an inherent large-cap bias in the portfolio. We decided to study whether investors can in fact improve their risk-adjusted returns in foreign stocks by eschewing country-capitalization weightings and,

instead, shifting some allocation from the largest countries to smaller countries — in other words, whether there is a small country effect worth tilting toward in a foreign stock portfolio.

Hitting Above Their Weight

For the study, we took a universe of the 19 developed-country markets in the MSCI EAFE Index and constructed monthly cap-weighted portfolios that we divided into three categories: 1) the largest country's weight, 2) the sum of the next four largest countries' weights, and 3) the sum of the next 14 countries' weights. The trend over the long

term has been for the larger countries to represent less of the index (Japan ranked as the largest single country during our entire 20-year study) and for small countries to grow in weight. Yet, as of the end of 2016, the top five countries still accounted for 67 percent of the market, which hints at the difficulty of achieving adequate portfolio diversification (one of the major benefits of international investing) by adhering strictly to an index-based approach.

Next, we calculated returns in the three country groupings by creating cap-weighted portfolios that we rebalanced annually. The 14 smallest countries outperformed the largest country in the market, returning 7.1 percent annualized over the 20-year period against just 2.3 percent for Japan. The small countries also outperformed the next four largest countries by a considerable margin, 2.7 percentage points annually. The small country returns come with higher annualized volatility than for the larger countries (18 percent vs. 17.1 percent), but a much better Sharpe ratio (a measure of risk-adjusted returns): 0.28 versus 0.02 and 0.14 for the largest and next four largest markets, respectively.

Country or Firm Size?

Careful readers might surmise that small country outperformance could be linked to the firm-size ef-

fect, which is the well-known tendency for small-company stocks to outperform large stocks. After all, it seems logical for small country equity markets to contain a relatively high proportion of small-cap companies. To test this hypothesis, we delved into the relationship between the small country effect and firm size. Within all three capitalization ranges, the returns of small countries exceed those of their larger counterparts. For instance, within large caps the largest-country portfolio returned only 0.82 percent annualized, compared to 3.8 percent for the next four largest countries and 5.5 percent for the remaining 14 smaller markets. These

results would seem to indicate that the small-country and firm-size effects are independent.

Conclusion

What we conclude from the study is that stocks from smaller countries (of any market-cap size) tend to have higher average returns than stocks from large countries over time. Therefore, investors can meaningfully improve expected risk-adjusted returns and enhance diversification by reducing weights for large countries and reallocating to smaller countries in a multi-country equity portfolio.

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About the Author

Gregg Fisher is founder and head of quantitative research and portfolio strategy at Gerstein Fisher. Research partners Ronnie Shah and Sheridan Titman contributed to the article.

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Real Assets Adviser is the first publication dedicated to providing actionable information on the real assets class and facilitating important business connections for registered investment advisers (RIAs), wealth managers, family offices and independent broker/dealers. Coverage includes real estate, infrastructure, energy, commodities/precious metals, agriculture and timberland. To learn more, visit www.realassetsadviser.com.

Emerging Markets Kicked Into High Gear In 2017

 FocusEconomics



With emerging market economies looking as though they are coming out of their slump, we've got a new emerging markets outlook and infographic for you in this article. You can also get a free Emerging Markets report download [here](#).

Brazil

President Michel Temer survived the vote on 2 August in Congress and avoided the possibility of being tried for corruption. An interruption of the government's reform agenda was thus sidestepped for now, although political noise is still high. The government is trying to pass a critical pension reform by October and a tax overhaul by the end of the year, two badly needed measures to correct imbalances in the hobbled economy. However, Temer is not off the hook yet and is facing abysmal approval ratings along with the likelihood that the public prosecutor's office will file more corrup-

tion-related cases against him in the coming months. Meanwhile, economic data has been mixed in recent months, suggesting that the recovery remains shaky. Industrial production growth stuttered in June and the manufacturing PMI fell in July, although a recent increase in commodities prices bodes well for exports.

Read more on the [Brazilian economy](#).

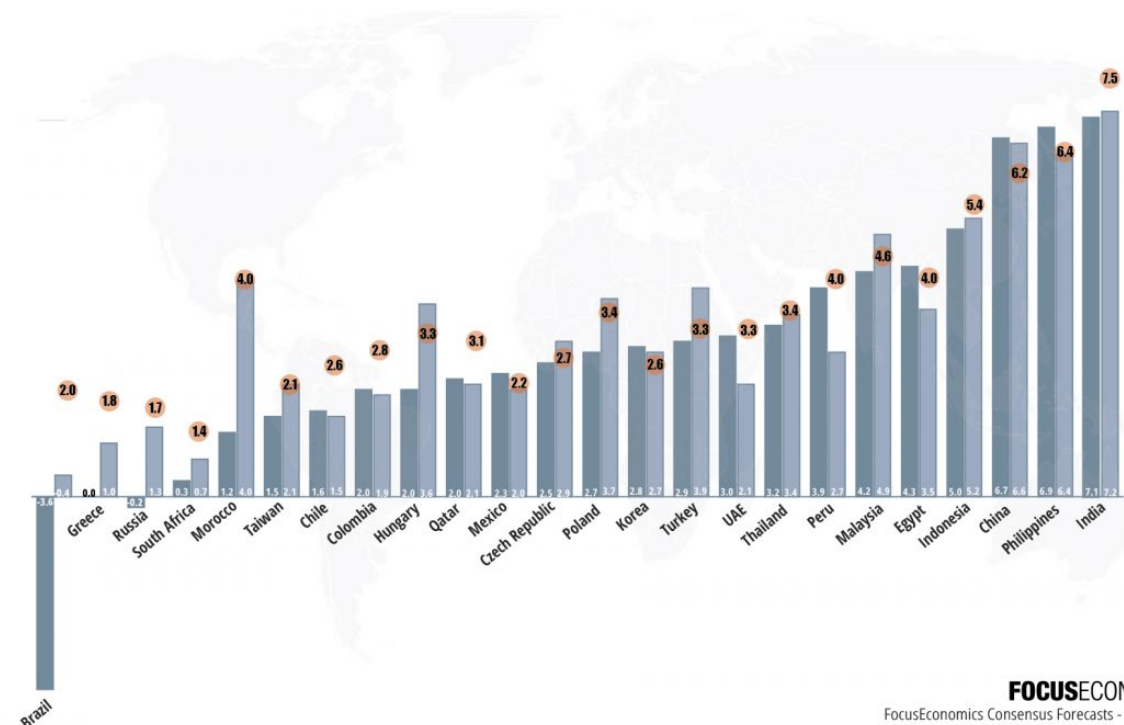
Greece

After a stronger-than-expected first quarter GDP figure, the economy is

expected to have grown for a second consecutive period in Q2, although at a weak pace. Industrial production picked up in May and the manufacturing PMI returned to expansionary territory in June for the first time since August 2016. In addition, the tourism industry—the economy's lifejacket throughout the crisis—performed strongly in April. Moreover, the country received EUR 8.5 billion in funds from its creditors in July, avoiding a summer showdown over reform requirements and ensuring that the government will be able to fulfill short-term debt commitments. As the economic picture becomes slightly more stable, the country

EMERGING MARKETS KICKING INTO HIGHER GEAR

2016 2017 2018 GDP for 2017 and 2018 are forecasts.



FOCUS ECONOMICS

FocusEconomics Consensus Forecasts - August 2017

received another piece of good news in recent weeks. The European Commission recommended that the European Council should end the country's excessive deficit procedure in July, removing special oversight over the government's spending. The move highlights improving government finances, after the country recorded a fiscal surplus in 2016. Meanwhile, the country returned to international financial markets after a three-year absence on 25 July selling a five-year bond, an important step for the government towards gaining financial independence.

Read more on the [Greek economy](#).

Russia

The economy's recovery likely kicked into a higher gear in the second quarter and growth is seen coming in at the highest reading since Q4 2013. Data remained bright despite oil prices having fallen throughout the period. In May, exports soared by nearly 30% and unemployment edged down in June. Moreover, consumer confidence stood at the highest level in nearly three years in Q2, aided by the improving economic situation. While the economic picture is becoming brighter, recent events are casting a shadow on the country's outlook. The U.S. Congress voted in July to step up sanctions on Russia, a move that could undermine confidence in the economy

and investment and possibly put a lid on the pace of economic recovery in the long-term. In addition, the low-oil-price environment is weighing on the economy's growth trajectory and shows little chance of improving, as a production cut deal by petroleum-exporting nations has failed to boost prices.

Read more on the [Russian economy](#).

South Africa

President Jacob Zuma narrowly survived another no-confidence vote on 8 August despite having introduced secret voting in the legislative body for the first time ever. The victory, although important, is short-lived and shows how support for Zuma's battered image continues to erode due to multiple scandals involving graft and mismanagement. The ultimate test for the embattled president, however, is the December ANC convention where the party will choose a new leader for the 2019 presidential elections. Furthermore, Zuma's persistent political debacles are causing collateral damage in the economy. South Africa entered a technical recession in Q1 and an uncertain political landscape is keeping investment at bay. Muted investor appetite bodes badly for the economy since it is crucial to rekindle growth as the latest stream of data has been bleak. The unemployment rate was 27.2% in Q2, manufacturing output was

stagnant in June and survey-based data was disappointing at the outset of Q3.

Read more on the [South African economy](#).

Morocco

GDP growth accelerated markedly in Q1 on the back of a hearty recovery in the agricultural sector, coming in at a five-quarter high of 3.8%. Improved household spending and investment in Q1 were the result of healthier dynamics in the domestic economy and came despite the uptick in unemployment. Moreover, leading indicators suggest that the economy kept up the pace in Q2. Notably, trade data from the January-May period suggests that the external sector's negative contribution to growth narrowed as higher imported energy costs were outstripped by robust growth in phosphate exports, which explains the jump in mining output in May. In early July, the IMF noted definite progress on the country's ongoing fiscal and structural reforms.

Read more on the [Moroccan economy](#).

Taiwan

Taiwan's economy lost some steam in Q2 according to recently-released figures, although it still expanded at a moderate pace thanks to

a strong external sector and robust private consumption growth. The economy has seemingly kicked off the third quarter on a solid footing, with exports motoring ahead in July thanks to healthy demand abroad, particularly from mainland China. The uptick in the global economy also benefited July's PMI reading, with firms reporting increased sales overseas. The economy should also benefit from the government's forward-looking infrastructure development program. The USD 3.3 billion budget for the first stage of the plan passed its first reading in Parliament in mid-July, and there are hopes that the budget can clear the house entirely before September in order to allow work to commence on shovel-ready projects.

Read more on the [Taiwanese economy](#).

Chile

The economy looks to have staggered back to its feet after receiving a body blow in Q1 due to a fall in mining activity. The economic activity indicator (IMACEC) expanded for the fourth consecutive month in June thanks to greater services and trade activity. In addition, consumer confidence reached its highest level in over two years in July; this bodes well for private consumption, which has been key to supporting growth in the face of lower fixed investment. However, firms remain cagey with presidential elections just around

the corner, as business confidence dipped again last month. On the political scene, Beatriz Sanchez from the leftist Frente Amplio coalition has recently emerged as a contender to reach the second round. Although her manifesto is not yet finalized, measures previously touted include universal health insurance, higher taxes on mining firms and an end to the AFP (private pension providers).

Read more on the [Chilean economy](#).

Colombia

Leading indicators suggest that the economy accelerated only marginally in Q2, a disappointing possibility following tepid growth in Q1. In May, industrial production contracted for a second consecutive month as the textile industry suffered from competition from cheaper products coming from Asia. However, other indicators paint a more optimistic picture: consumer confidence edged up and unemployment fell in June, both of which bode well for a much-needed boost to household spending. On the external side, exports recorded an almost flat reading in June after a stellar expansion in May, hinting that the prolonged slump in commodity prices could weigh on exports growth into Q3. Finally, H2 was ushered in by good news: coffee production soared by 25% year-on-year in July as harvests impressed to the upside.

Read more on the [Colombian economy](#).

Hungary

2017 is shaping up to be a spectacular year for the Hungarian economy as it is being supported by ambitious pro-cyclical policies and a resumption of EU investment funding. All evidence suggests that growth in Q2 remained robust. In May, both industrial production and retail sales expanded solidly and unemployment declined again. The external sector also performed robustly in the same month, hinting that the economic upturn is broad-based. Adding to the mounting good news, survey-based data reached all-time highs at the start of the third quarter, underscoring the strength of the country's economic fundamentals.

Read more on the [Hungarian economy](#).

Qatar

The political clash with several Arab states led by Saudi Arabia, which has resulted in the economic blockade of Qatar, has left some visible scars on the economy. In June, foreign deposits at Qatar's banks dropped significantly, prompting the Qatar Investment Authority, the country's sovereign wealth fund, to step in and inject billions of dollars into local banks in order to avoid a

liquidity crunch. Moreover, Qatar's decision to amend its anti-terrorism laws was deemed insufficient by the Saudi-led alliance, and the mediation attempt by U.S. Secretary of State Rex Tillerson has thus far proved fruitless. The crisis hits the country at a moment of relative economic weakness, with oil production at a multi-year low and GDP growing unimpressively in Q1, pushing credit rating agency Moody's to change Qatar's rating outlook to negative on 4 July.

Read more on the [Qatari economy](#).

Mexico

The economy expanded at a markedly slower pace in Q2, although positive momentum was largely retained and growth prospects remain relatively upbeat. While private consumption has shown signs of cooling off heading into Q3—auto sales were down in both June and July—upbeat manufacturing output and sentiment, a strong labor market and soaring remittance inflows continue to support economic activity. Along with positive economic momentum, the government's successful efforts to control the fiscal deficit and debt levels led both S&P Global Ratings and Fitch Ratings to upgrade the outlook of Mexico's sovereign credit rating to stable while maintaining the country's BBB+ grade. These upgrades come only weeks before talks to renegotiate NAFTA officially start on 16

August. Mexico recently disclosed its goals for a new agreement, prioritizing free access for goods and services and greater labor market integration.

Read more on the [Mexican economy](#).

The Thai economy defied expectations and picked up steam in the second quarter, growing at the fastest pace in over four years, chiefly driven by a buoyant external sector.

Czech Republic

The Czech economy is growing robustly, buoyed by a favorable external environment and strong household spending. After falling somewhat in April, exports jumped in May, with a greater trade surplus recorded for motor vehicles on the

back of stronger demand from European Union countries. The jump in exports was behind the rebound in industrial production recorded in the same month and PMI readings suggest that both domestic and external demand are creating expansionary conditions in the manufacturing sector. The positive momentum is also being felt in the labor market, with unemployment falling to a fresh multi-year low in June, which, together with rising wages, is underpinning private consumption. In addition, recently-published data shows that public finances are benefiting from robust growth, as in Q1, the fiscal balance recorded a small surplus—reverting the deficit registered in Q1 2016—thanks to revenue growth, especially from income taxes, outpacing spending growth.

Read more on the [Czech economy](#).

Poland

Heightened uncertainty and market volatility abound in the wake of 24 July's two presidential vetoes that halted much of the PiS-led judicial overhauls that had prompted nationwide protests. In the days since, the EU has filed court proceedings against the country in what promises to be a drawn-out legal squabble over the direction of Polish democracy. Although investor confidence is likely to be tested in the near term, a strong economy and sound fundamentals are sure to cushion

much of the blow—that is, a tightening labor market and healthy retail sales through June bode well for resilient consumer spending at the end of H1. Moreover, survey-based data showed a pronounced optimism heading into H2: the manufacturing PMI recovered solidly in June on improved output growth and business confidence was once again upbeat in July.

Read more on the [Polish economy](#).

Korea

The country is in the eye of the storm amid escalating geopolitical tensions in the Korean Peninsula. Preliminary data show that a contraction in exports caused GDP growth to decelerate in the second quarter. The decline in exports largely reflects China's ban on group tours following the deployment of a controversial anti-missile system in the country earlier this year. Despite the slowdown, the government is fairly optimistic about the country's growth outlook and raised its 2017 forecast to 3.0% in late July, the highest in three years. The revision reflects the view that the approval of an almost USD 10 billion supplementary budget will give the economy the extra boost although it is uncertain how the government could actually implement concrete measures without a parliamentary majority. The upward revision came despite an escalating war of

words between the United States and its rival in the North which could dampen fixed investment and private consumption in the short-term.

Read more on the [Korean economy](#).

Turkey

The economy has surged so far this year thanks to an expansionary fiscal policy and healthy export growth fueled by the weaker lira. In April, the unemployment rate dropped to a ten-month low, continuing the positive trend observed since the start of the year and highlighting the positive impact of the government's employment campaign. In addition, conditions in the manufacturing sector are upbeat, with the capacity utilization rate remaining elevated in July and the PMI staying firmly in expansionary territory in the last few months. In a bid to rejuvenate the political scene in the same way, the Prime Minister reshuffled his cabinet in July. Most key positions are unchanged, and the reappointment of Mehmet Simsek as the sole economy minister is likely to calm investors' nerves; he is widely regarded as a safe pair of hands and a fiscal moderate, in contrast to other big spenders in the cabinet.

Read more on the [Turkish economy](#).

United Arab Emirates

The non-oil sector continues to hum along, with the PMI remaining well within expansionary territory so far this year thanks to solid domestic demand and strong growth in output and new orders, although employment growth has been anemic due to pressure on margins. In contrast, the oil sector is looking peaky; even though the UAE complied with oil production cuts in May and June, and despite the OPEC deal extension until November, prices remain fairly depressed. However, the country is still navigating the choppy economic waters of low oil prices better than GCC neighbors, thanks to a rock-solid fiscal position and a relatively diversified economy. In order to boost revenues and broaden the tax base, from 2018 VAT will be implemented for the first time at 5.0%. The specificities of the policy are gradually crystalizing, with the government recently announcing exemptions for residential real estate, some financial services and local transport.

Read more on the [Emirati economy](#).

Thailand

The Thai economy defied expectations and picked up steam in the second quarter, growing at the fast-

est pace in over four years, chiefly driven by a buoyant external sector. Exports grew at a double-digit rate nearly throughout Q2 on the back of healthy global demand, with firms brushing off fears about a strong baht harming competitiveness. Imports also grew strongly over the same period, signaling a fairly robust domestic market, with consumer spending likely boosted by lower inflation. However, the third quarter seems to have gotten off to a slightly less auspicious start. The PMI dipped below the crucial 50-point mark in July due to falls in output and employment, indicating a deterioration in business conditions, while business confidence also declined marginally in the same month.

Read more on the [Thai economy](#).

Peru

Emerging data for Q2 suggests an upturn in growth dynamics for the economy, which since the start of the year has been severely disrupted by domestic political turmoil—spearheaded by the Odebrecht corruption scandal—and devastating floods triggered by the “coastal El Niño” phenomenon in the north-western part of the country. Economic activity surged in May after dwindling at subdued levels, led by a robust expansion in the manufacturing sector. Exports growth strengthened in June, widening the trade surplus. Furthermore, the business

confidence indicator ticked up in July as efforts to improve political conditions were stepped up by the government. President Pedro Pablo Kuczynski focused his 28 July Independence Day speech on his government’s plans to get the econ-

*On a positive note,
a brighter economic
outlook, a weaker
U.S. dollar and the
People’s Bank of
China’s (PBOC)
controls led capital
outflows to ease and
international reserve
to stop falling.*

omy back into shape, affirming his commitment to speed up delayed investment in infrastructure projects through the introduction of a bill. He pledged to resume large projects, such as the Southern Gas Pipeline and the Lima Airport expansion—the projects were put on hold due to corruption or inadequate financing arrangements—in a bid to restore confidence in his

political mandate amid rapidly-declining approval ratings.

Read more on the [Peruvian economy](#).

Malaysia

The economy surprised on the upside in Q2, accelerating thanks to a notable expansion in private consumption. A healthy manufacturing sector and solid momentum in services supported growth in the quarter, along with a positive push from the external sector. On the political front, while the recent positive economic momentum had led analysts to speculate that elections could be brought forward, the July-August session of Parliament came to an end without having taken any steps toward calling a vote. A delay in approving new electoral boundaries for the state of Sabah are likely impeding the government’s ability to call early elections, as typically the state’s vote is held at the same time as the national vote for cost reasons. The country is scheduled to hold a general election by August 2018 at the latest.

Read more on the [Malaysian economy](#).

Egypt

The government’s bold economic strategy was vindicated in mid-July, with the IMF formally signing

off on the second tranche of bailout funding worth USD 1.25 billion. In its first review of the Extended Fund Facility (EFF), the Fund gave a fairly ringing endorsement, lauding the progress on the reform agenda, with new investment and industrial licensing laws recently approved and a new insolvency law currently in Parliament. Nevertheless, consumers could be forgiven for not sharing the IMF's enthusiasm, as recent hefty fuel and electricity subsidy cuts have the potential to further stoke already-high price pressures in the coming months. They can however take some solace from plans to phase out energy subsidies more gradually than previously expected and a social package announced by the government in June. In the face of higher inflation, the Central Bank is taking no chances, pulling up the monetary drawbridge further at its most recent meeting despite the fragile economy.

Read more on the [Egyptian economy](#).

Indonesia

Economic activity was disappointing in the second quarter, as growth stalled at Q1's 5.0% year-on-year, contrasting expectations of an acceleration. Plummeting government consumption limited the economy's momentum, while the external sector's performance was lackluster. However, invest-

ment was a bright spot in the data and gained speed. Early data for the third quarter suggests subdued activity: the manufacturing PMI pointed to a sharper contraction in July and the trade balance recorded the first deficit since December 2015. On 16 August, President Joko Widodo presented a draft budget for 2018 to Parliament. The budget aims to increase spending to USD 165 billion to jumpstart growth and projects the fiscal deficit to narrow to 2.19% of GDP on the back of higher revenues.

Read more on the [Indonesian economy](#).

China

Incoming data for July suggests that momentum is moderating in H2 following the stellar performance in H1 driven by strong property sales and export activity. July's slowdown reflects weather-related disruptions, supply adjustments in some sectors and lower property sales. On a positive note, a brighter economic outlook, a weaker U.S. dollar and the People's Bank of China's (PBOC) controls led capital outflows to ease and international reserve to stop falling. Authorities' success in curtailing capital flight prompted the yuan to strengthen in recent months. With the economy sailing smoothly and risks to growth broadly balanced, the government tightened fiscal expenditure in

July after H1's strong growth in spending. Moreover, a report from the PBOC released on 11 August showed that effective lending rates are gradually increasing as a result of tighter financial conditions related to the Bank's effort to promote financial deleveraging.

Read more on the [Chinese economy](#).

Philippines

Economic activity remains buoyant, underpinned by solid macroeconomic fundamentals and an accommodative monetary policy. The health of the economy was reflected in the national accounts for Q2, which showed that GDP had extended its streak of solid expansions on the back of further remarkable performance in domestic demand. Robust inflows of remittances and healthy credit expansion have contributed to supporting household spending, while the ramping-up of infrastructure spending by the government, ample liquidity and favorable financing conditions have translated into upbeat business sentiment and rising fixed investment. Against this backdrop, the annual drop in FDI in the first five months of the year following the Fed's tightening cycle is not too alarming, especially considering that the country's ample foreign reserves provide protection from potential external shocks.

Read more on the [Philippine economy](#).

India

Incoming data points to a disruption in economic activity following the 1 July implementation of the new GST. Both the manufacturing and services PMIs fell into contractionary territory in July, while no relief came from abroad as exports growth slowed in the same month. Confusion over the new tax procedures and how to price products are chiefly behind the slowdown, but the blip in momentum is expected to be short-lived overall. Meanwhile, the government presented its Economic Survey to Parliament in August. Chief Economic Advisor Arvind Subramanian warned that fiscal

About the Author

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slippages could interfere with the economy's momentum and voiced concerns over farm loan waivers by states, while at the same time reiter-

ating the government's commitment to hitting budget targets.

Read more on the [Indian economy](#).

Puerto Rico bonds trade down on Trump 'wipe out'

✍ Maryellen Tighe, Simone Baribeau and Seth Brumby

Bonds across the Puerto Rico credit complex generally traded down following President Donald Trump's (R) comments to "wipe out" the commonwealth's debt, said two traders and an analyst tracking Puerto Rico.

Trumpp's comment, made last night (3 October) after his visit to Puerto Rico to survey damage done by Hurricane Maria, drove prices down on general obligation (GO), Puerto Rico Electric Power Authority (PREPA), Puerto Rico Aqueduct and Sewer Authority (PRASA), Employees Retirement System (ERS) and Puerto Rico Sales Tax Financing Corporation (COFINA by its Spanish acronym) bonds this morning, according to Electronic Municipal Market Access (EMMA).

"I don't think Trump can make that [a wipe out of Puerto Rico's debt] happen, this is in bankruptcy court [governed by] the Puerto Rico

Oversight, Management and Economic Stability Act (PROMESA)," said an analyst. "No matter what Trump said, that doesn't change the continuing deterioration, likely population loss, and the years and years of hopefully recovery."

The floor is somewhere above zero, the analyst said, but in three months trading will probably be even lower as reports of damage continue.

The benchmark commonwealth USD 3.5bn Series 2014 GO bonds due in 2035 underwent heaving trading today amidst its selloff, dipping into the low 30s from yesterday's close of 44, according to EMMA.

Legacy GO bonds, though less liquid than the benchmark, also took a hit today. The USD 304m 5.75% Series 2011 GO bonds due in 2041 dropped into the mid-30s today after the last round lot of 46 on 27 September, according to EMMA.

This is higher than the projected average annual payouts of 24 cents on the dollar through FY26 contemplated by the fiscal economic growth plan filed by the government this spring.

Trump's comments are intended to show that any aid will not help bondholders, said a trader. The bondholders have been described

as hedge funds or opportunistic buyers, providing an easy target. Following Hurricane Maria it was only a matter of time until someone, the Financial Oversight and Management Board (FOMB), Governor Ricardo Rossello or another player, said that the debt should be eliminated.

Keeping electric improvements from bondholders

The carnage didn't spare revenue debt as both PREPA and COFINA

also traded down. PREPA's USD 588m 5.25% Series 2011XX revenue bonds due in 2040 also traded down in the low 30s today from round lots of 42 on 2 October, according to EMMA.

The question of bondholders benefiting from federal investment especially comes into play with PREPA, said the trader. The Army Corps of Engineers is coming to rebuild the system, which was in desperate needs of upgrades before the storm.

"My guess is that there will be a strong push to modernize the system, it's now going to be on whose back," said the trader. "Ultimately,



the government will provide a lot of financial support but the government doesn't want the bondholders to get a higher recovery because we're paying it."

The government doesn't want to be perceived as helping bondholders, said the trader.

Meanwhile, COFINA's USD 325m 5.25% Series 2011C senior sales tax revenue bonds due in 2040 traded down to 45 this morning in round lots from round lots of 52 at yesterday's close, according to EMMA.

A USD 100m tranche of Series 2012A PRASA bonds which mature in 2047 traded in odd lots today at 54.4 to yield 11.4%, down from round lots at 76 yielding 8.2% on 20 September, according to EMMA.

And a USD 200m tranche of Series 2008A ERS bonds due in 2023 last traded in round lots today at 33, yielding 30.914%, according to EMMA. That's lower than their last round lot trade on 14 September at 41.5, yielding 25.114%, according to EMMA. Bonds declined over that time period, in the wake of Hurricane Maria, even before Trump's comments. Yields on the S&P Municipal Bond Puerto Rico Index climbed to 5.59% yesterday from 2.76% on 14 September.

At least one of Puerto Rico's bond insurers has suffered, shares for Assured Guaranty, which insures roughly USD 5bn in Puerto Rico debt (over USD 8bn if including

capitalized interest) were down 2.5% in intra-day trading today to a low of USD 37.00 per share after yesterday's close of roughly USD 38.60.

Low prices at the bargaining table

The PROMESA process and the FOMB have been focused on sta-

*The government
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said the trader.*

bilizing the Puerto Rico economy, not helping bondholders, said the trader. This takes that rhetoric up a notch.

"It's given the board political cover to go hard after bondholders," said Johnny Ceffalio, a municipal credit analyst at AB Global.

The trade may rebalance who is in the Puerto Rico credit complex and change negotiations, said the trader. Now that the 2014 GO bonds are trading in the 30s, a 50-cent recovery looks pretty good, especially as they may go down further.

"It's a pretty concentrated holder base on this debt, I think it's going to recalibrate and just go back and start negotiating again," said the trader.

As far as actually writing off the entire debt, Puerto Rico will need to return to the public market at some point, said the trader.

"[Trump] doesn't know what it means either, using the language he uses, it's pretty hard to think that it's well thought through, [it seems to be] just an off-the-cuff comment, that has everybody going crazy," said a second trader also tracking Puerto Rico.

Presidential finger on the scales

This isn't the first time a president has used the bully pulpit in a high-profile bankruptcy. In the Chrysler bankruptcy, then-President Barack Obama (D) blamed the automaker's bankruptcy on "investment firms and hedge funds" that refused to make sacrifices when others did. He had reportedly pressured banks receiving troubled as-

set relief program aid and Chrysler debt to agree to haircuts.

Likewise, Trump's comments yesterday "essentially short-circuit" the Title III process, said Richard Epstein, a law professor at New York University who has a client interest in the litigation.

"[His comments are] putting a very big chip on a very complex scale," Epstein said, adding that Trump's lack of respect for institutions threatens the process. "He's a bull in a china shop...[he's] completely ignorant about the uses and the limits of his role."

PROMESA is set up to be a very elaborate process which is already under intense scrutiny, Epstein said.

"The whole point about this is to create a process in which no one man can change unilaterally," Epstein said. "You don't give federal

aid by waving the claim for someone else. The changes in prices [of debt] should affect the market realities, not the presidential influence."



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