

ALTERNATIVE EmergingInvestor

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One of the main components to the volatility of emerging and frontier markets is uncertainty. Not having any idea what the future of a region will look like gives most investors pause. While this is generally understood and accepted, we are now seeing the same kind of uncertainty within the developed markets; between the Brexit and Trump's surprisingly resilient campaign, attack in Nice, outcomes for the developed world are anyone's guess.

What does this mean for developing markets? I believe global markets are coming to a crossing point of perception. Allow me to explain: When there is new interest in a particular region, country, IPO, etc, I find investors are highly motivated by not an actual change, but rather one of perception. Argentina, for example, is fundamentally the same as it was prior to new Macri administration, however, the maligned Southern Cone nation is now at the top of many investor lists, receiving substantial bond allocations in addition to a flood of interest in the country. This new impetus was solely created by a change of perception and renewed hope for the future.

In the developed markets we are seeing the opposite where the perception is becoming increasingly negative. I'm reminded of taking the Trans-Siberian railroad from Beijing to Moscow in 2002; China was a bit of a disaster, but things were getting better day by day, massive investment and improvements swept through the country. Russia on the other had, was falling from its days of opulence, but the two nations seemed to be at a crossing point...this is where I see the world today. While the short-term might see more EM allocations and openness to consider emerging markets, the global economy requires stability within its most developed markets. This will be an extremely interesting year, as we watch how this dynamic between developed and developing markets unfolds.



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The Counterintuitive African Opportunity

 EMIA (The Emerging Markets Investor's Association)

What is Africa's economic outlook, and what solutions are there to roadblocks slowing growth such as soft commodity prices, tumbling oil prices and weakening of African currencies? How are they affecting the continent's capital inflows?

For the past decade, Africa has been a hotspot for emerging and frontier market investors with a high-enough risk tolerance and excellent local on-the-ground knowledge. It has even proven to be a hotspot for those without local expertise.

Riding the developing market wave of a growing middle class, with ever-increasing amounts of disposable income investors, has

been pursuing sectors across the board, consumer goods, energy, infrastructure, real estate and agribusiness. In a continent that is lacking in many ways, opportunities still abound. While African investment has been—and most likely will always be—plagued with global headline risk, highlighting the most negative aspects of the region, and planting seeds of doubt across the investment universe, the huge demand for investment along with rapidly increasing regulation have led to an inundation of capital and the growth of local funds and global allocations to the region. However in more recent years, the largely irrelevant (to investment specifically) news has become more relevant.

Devaluations of local currencies and the crash of oil prices have hit many petroleum-producing nations hard. But what does this mean for investors?

We spoke with Olutoyin Oyelade, the managing partner and chair for the Management Investment Committee at InVcap, an investment manager that provides accredited investors access to investment opportunities in the frontier markets of Africa.

The answer seems somewhat counterintuitive yet springs from the wisdom within, “necessity is the mother of invention.” The mix of decreasing capital, historic GDP growth and consumer demand has forced African nations to enter the

global financial markets on a scale they never have before.

Oyelade comments, “With improvements to financial infrastructure and strong fundamentals, Ghana, Zambia and Rwanda have raised capital through bond issuances with interest rates between 7% and 10%. Africa is becoming more and more accepted by international financial markets.” The softening of commodity prices causing budget deficits for many net exporters is a driving factor in these nations seeking funding from outside the continent, which has become a key driver in expanding the ability for investors to access the African market.



This unique combination of softening commodity prices, local currency devaluations and budget deficits has been instrumental in providing opportunities for investors. As governments face capital constraints, privatization has opened many doors to investors who were previously unwilling or unable to invest in public companies.

According to Oyelade: “We’ve seen a lot of growth in Africa, which has been supported by positive fundamentals, which has dovetailed into the GDP of the region.” Despite a dip in regional GDP growth, there has been a spike in consumer spending and infrastructure devel-

opment. An excellent example of the former is the smartphone penetration, which is expected to hit 50% by 2020, up from just 2% in 2010.

“A lot of restructuring in terms of public spending and increased accountability have been implemented to maximize local government revenue in addition to tax incentives for investors, particularly Egypt, Nigeria, Ethiopia and Angola,” Oyelade points out, continuing, “More than this, nations are trying to make investors comfortable—not just to bring money into the country but also having confidence they can get it out.”

When there’s blood in the street, buy property, Baron Rothschild said. While there isn’t literal blood on the streets, in most cases, the sentiment is still valid now. Opportunities are ripest when things are going from bad to slightly better. Africa has ridden a wave of positive sentiment for the past decade, with the recent depression in growth, global perception and capital; this does not change the fundamental potential for investment and in fact makes the market more attractive due to the government’s need for capital and their willingness to improve local investment environments to attract investors.

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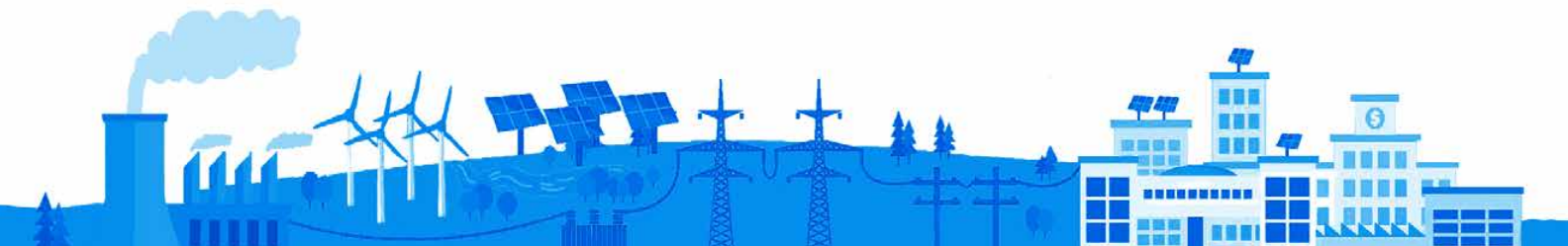
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Gold: The Most Precious of Metals

It is widely accepted that gold is a truly precious metal. In this article we explore why gold is so valuable by explaining how it is mined and processed and discuss how its unique physical properties make it one of the most useful metals. Finally, we end this piece with a section on gold's importance to the global economy, the factors that set it apart from all other commodities and how it can be classed as both a commodity and a monetary asset.

How Does Gold Mining Work?

Before one can start the mining and production process of gold, one must actually find the gold. Many of the great historic gold rushes began with a story of someone stumbling upon gold in a riverbed or backyard while strolling along. However, finding gold at a corporate level, as you might imagine, is a bit more sophisticated.

Gold is concentrated in the earth's crust all over the world, and while

one can, in theory, fairly easily go to a stream in places like California or Canada and find placer gold, what large mining corporations try to do is find higher concentrations in the earth's crust to produce at higher volumes. This is tricky because finding gold in high volumes is not an easy task. There is approximately 0.004 grams of gold per ton of the earth's crust, meaning that it is sort of like finding a needle in a haystack.

Finding gold starts with geologists who study the rock formations and types of rock in a certain area by taking samples of the earth, which are called diamond drill cores. They are called this because, as you might guess, a diamond-tipped drill is used to cut through the rock to obtain the samples. Gold is normally found mixed in with many other elements, metals and mineral in rock called ore, and based on their sample analyses through assays and other processes, geologists are able to determine where the ore is as well as its composition.

The grade of the ore and the size of the deposit dictate the type of mining necessary to get to the ore and whether or not it will be cost-effective to mine it. Obviously, the higher the grade of the ore, the more cost-effective it will be to mine it. However, more cost analysis is needed to determine if the mining process will be worth it.

There are a few different terms used to describe the gold deposits found,

but in general they are the following: proven reserves and probable reserves. A geologist may determine from sampling that a probable reserve exists, meaning that gold exists; however, the type of mining necessary to get to the ore may not prove to be profitable. Proven reserves, on the other hand, basically mean what you might think: The geologists have determined that gold exists, and engineers have decided that there is an economically viable way to mine the gold. These terms usually appear on annual reports of gold-mining corporations and provide the company's best estimate as to the total gold that can be mined. These numbers do not, however, actually guarantee that the gold can or will ever be mined.

Types of Gold Mining

There are a few different mining processes that can be used. Two of the most common for large mining corporations are open-pit mining and underground mining.

Open-Pit Mining Process

Open-pit gold mining is used when the ore is close to the surface of the earth. As you might guess, an open-pit mine is basically just a massive hole in the ground that has roads along the walls of the pit so that huge trucks can get in to carry ore back out.

The extraction process involves the use of explosives and heavy machinery to haul the ore out of the huge mines. There are heavy costs associated with this process, according to Mineweb. About 25% of the total cost of mining is spent on diesel fuel.

Mineweb also estimates that for each ton of ore hauled out of a mine, it might contain a tenth of an ounce of gold. Crunching a few numbers, we can estimate the amount of gold in US dollars that one haul of ore can yield. In the latest FocusEconomics Consensus Forecast Commodities report, the spot price of gold on April 15 was USD \$1,230 per troy ounce (a troy ounce is slightly different from an ounce and is a common unit of measurement for precious metals, however, it is only slightly heavier than a standard ounce). That means for every ton of ore excavated from the mine the yield would be USD \$123 of gold, which is not a whole lot. However, the trucks that are used to haul the gold out of the pit can hold up to 300 tons, which means that a good haul could yield USD \$36,900 worth of gold. In reality, however, the chances of this happening are slim, and many times the amount of gold in a truckload can end up yielding little to no gold at all.

Underground Mining Process

Sometimes it is determined that an underground mine makes more

sense, usually when the gold deposits are located much farther from the surface of the earth. Underground mining, also known as underground hard rock mining, utilizes long winding tunnels and shafts that are dug out of the ground with other tunnels branching off in different directions. Although you might imagine an underground mine with workers slaving away with picks, axes and shovels, those days are largely in the past, at least in the commercial mining anyway. Today, the mining process basically involves drilling holes for explosives, setting off the explosives and then hauling out the debris from the explosion.

In terms of the costs involved with underground mining, they are largely the same as those associated with open-pit mining. However, there is one very important aspect that must be taken into consideration for underground mining: electricity. There is little to no air underground, so electricity must be used to pump air into the mine so that the miners can breathe. Transportation of miners and hauling out the ore would also not be possible without

electricity powering the machinery needed for this. Of course, this can be quite costly, so some mining corporations have found more

cost-effective means of powering the mines by setting up wind farms and solar-energy panels near the excavation sites.

What is Cyanide Used for in Gold Mining?

Once the ore is excavated from the mine, the gold will need to be separated from the ore. The cyanide leaching process makes use of a mild cyanide solution to dissolve and separate the gold from the ore. The use of cyanide for this process was first developed in the late 19th century in Scotland, and since the 1970s it has been the primary gold-extraction method used in commercial gold production. First the ore is pulverized until it reaches a sandy consistency then a cyanide solution is added to the sandy ore. Without getting too technical, the cyanide dissolves and separates the gold from the ore. Further processes of crushing and milling are used to squeeze out as much gold as possible before the smelting process begins to refine and convert the recently liberated gold into gold bullion bars.



How To Determine And Test The Purity Of Gold

It is pretty safe to say that since the human race became aware of the concept of possession, gold has been sought after, and therefore determining the purity of gold has been extremely important.

What Is The Purpose Of A Fire Assay?

A metallurgical assay is a composition analysis of ore and can be used to determine the purity of gold. The fire assay was first used by the Babylonians more than 3,000 years ago and is still one of the most accurate methods to do this. Basically, the process involves taking a sample of melted impure gold from a larger portion of gold or ore. Then the sample is weighed precisely and the amount recorded. The sample along with a given quantity of pure silver is then wrapped in assay lead foil and placed in a furnace in a cupel, which is a special kind of disposable crucible. Eventually all the non-precious metals are absorbed into the cupel and the precious metal forms into a button shape inside the

cupel. Once the cupel is removed from the furnace, it is hit with a hammer and the button pops out. Then it is brushed to remove any residue hanging around from the cupel. Then the button is hammered flat and rolled thin and heated again in a porcelain crucible that contains a solution of nitric acid, which removes the silver. What you are left with is gold, which is then rinsed in distilled water to remove any residual acid and left to dry. The result

If it weren't for its density, gold may not have ever been discovered in streams and rivers, as its high density to water made it easy to spot on the river bottom.

is a sample of 99.999% pure gold. The original weight of the impure sample taken at the beginning is then divided into the weight of the new pure gold sample, which tells you how pure the original sample was.

Gold Density to Determine Purity Gold is an extremely dense material with a density of 19.3 g/cm³. Another way of stating gold's density is that it has a specific gravity

of 19.3. All this basically means is that it is 19.3 times heavier than water, so it sinks pretty fast in water. If it weren't for its density, gold may not have ever been discovered in streams and rivers, as its high density to water made it easy to spot on the river bottom. The density of gold has been very important to mining in the past, especially during the California gold rush, as it could easily be seen at the bottom of a pan. Prospectors also realized that gold was dense enough that when dropped into water it would sink to the bottom fairly fast. To determine whether or not they had found a piece of genuine gold, prospectors would use a piece of real gold and drop it into the water along with another piece of possible gold and compare how long it took for both to sink. If the questionable piece of gold took a while to fall to the bottom in comparison with the real gold, they knew they had "fool's gold." The density of gold basically made it possible to eliminate fancy equipment to determine its purity, another distinguishing characteristic of gold.

Gold Karat System and Millesimal Fineness

Two measurement systems used to represent the purity of gold are the karat system and millesimal

fineness. With the karat system, 24-karat gold denotes pure gold, whereas with millesimal fineness, as the name suggests, the purity is expressed in parts per 1,000. Twenty-four karat gold is equivalent to 990 millesimal fineness or higher. Pure gold is not usually used for jewelry because it is too soft. Therefore, gold used in jewelry is normally alloyed with other metals, such as copper and silver, to make it stronger. The highest purity for gold used in jewelry is normally 18 karats or 750 fineness.

Normally the purity of the gold is stamped on the jewelry, and there are actually organizations that reg-

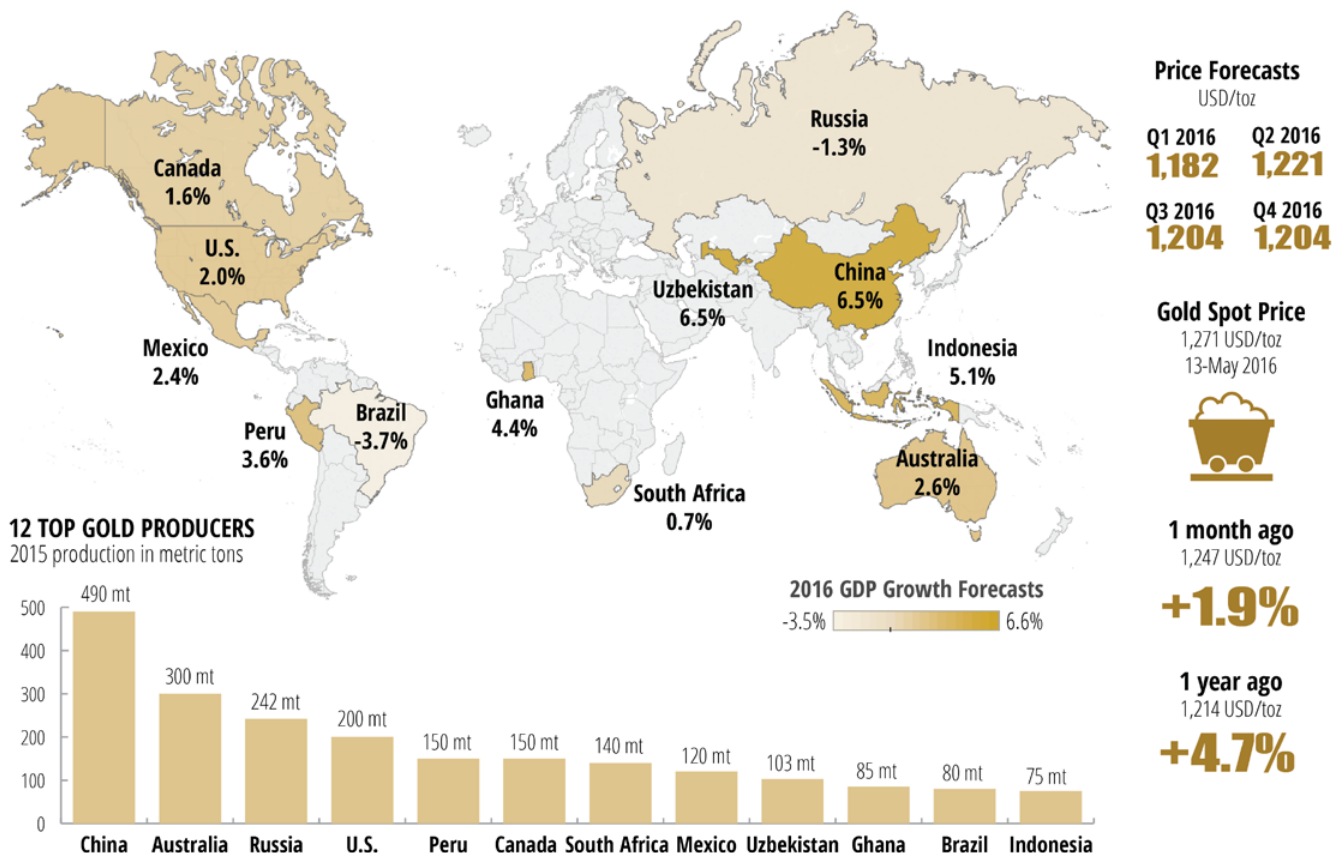
ulate this. The Hallmarking Convention is an international treaty between countries that seeks to standardize the marking of precious metals like gold and to facilitate their cross-border trade. They have a zero-tolerance policy with regard to purity. If gold is 749 parts per 1,000 fine, it cannot be marked with a 750 quality mark.

What is Gold Used For?

Besides the obvious use of gold in jewelry, you may ask yourself, does it have any practical applica-

tions? Does it have any industrial or technological application similar to some other metals? The answer is yes. Gold is used in a multitude of capacities. It is arguably the most useful metal because of its many unique properties. It is extremely malleable, allowing it to be pounded, hammered, melted down and cast in extremely detailed shapes. It is so malleable that one ounce can be drawn into 80 kilometers of wire. It is also a great conductor of electricity and heat, it is basically indestructible, it does not rust and it can easily be alloyed with other metals. All of these factors and more make it very useful beyond jewelry making, and many of its uses may surprise you.

How Will Top Gold Producers Perform in 2016?



Electronic Devices and Computers
Solid-state electronic devices, which are basically those with inner workings that are based on semi-conductors, use gold because it does not tarnish and conducts electricity well. These devices include cell phones, calculators, GPS systems and other smaller electronic devices.

As with small electronic devices, computers use gold because of its electric conductivity. Gold is used in the edge connectors to mount microprocessors and memory chips onto the motherboard.

The challenge with using gold in these types of devices is the potential for the loss of gold. Gold is a very scarce material and costly to boot. According to the World Gold Council, each cell phone contains around 50 milligrams of gold, which equates to about USD 50 cents worth of gold. With more than 1 billion cell phones produced a year, this results in a lot of lost gold and, consequently, lost money. One might theorize that electronic recycling programs have a lot more to do with gold recovery than being environmentally friendly, but we'll leave that one for you to ponder.

Dentistry

If you have ever needed dental work done that required some kind of metal, what type of metal do you think would work best? Probably the kind that doesn't rust, right?

How do you think iron would work as a filling? It would be rusted before you know it, and you'd have the taste of iron in your mouth for the rest of your days. Gold is one of the most widely used metals for dentistry because it does not rust. Pure gold is a bit too soft, not to mention expensive, so normally gold alloys are used for things such as crowns, fillings, bridges and caps. Besides the fact that it does not rust, gold also looks nice. Joe

Pesci from Home Alone comes to mind immediately.

Health Care

Gold is also used in a variety of ways in medicine and health care. In 1927, a French study was published documenting gold's use in the treatment of rheumatoid arthritis. It is still sometimes used to treat the disorder with injections of a solution of sodium aurothiomalate

Gold

- The chemical symbol for gold is Au.
- Gold's atomic number is 79 and its atomic weight is 196.967.
- Gold melts at 1064.43° Centigrade
- The specific gravity of gold is 19.3, meaning gold weighs 19.3 times more than an equal volume of water.

.....

WEIGHT EQUIVALENTS

1 troy ounce	=	1,097 ordinary ounces
1 troy ounce	=	480 grains
1 troy ounce	=	31.1 grams
1000 troy ounces	=	31.3 kilograms
1 gram	=	.03215 troy ounces
1 kilogram	=	32.15 troy ounces
1 tonne	=	32.150 troy ounces
1 ordinary ounce	=	.9115 troy ounces
1 ordinary pound	=	14.58 troy ounces

.....

Percent Gold	=	European System	=	Karat System
100 %	=	1000 fine	=	24 karat
91.7 %	=	917 fine	=	22 karat
75.0 %	=	750 fine	=	18 karat
58.5 %	=	585 fine	=	14 karat
41.6 %	=	416 fine	=	10 karat

or aurothioglucose. Sometimes radioactive gold isotopes are implanted in parts of the body to aid in the treatment of certain cancers. It is used to treat people with a disorder called lagophthalmos, in which the person is unable to close their eyes properly. Small bits of gold are sewn into the eyelids of the person suffering from the disorder in order to weight the eyelids down, aiding them in the ability to close their eyes completely. Gold salts can be injected into patients to reduce swelling, bone damage as well as to relieve joint pain and stiffness.

Aerospace

When building a spaceship, NASA needs to use materials that are extremely reliable. If they didn't use reliable materials and something went wrong in outer space, who would be around to fix it? This is where gold comes in. Similar to electronics, gold is used in the circuitry of the spaceships because of its dependability as a good conductor of electricity. Gold-coated polyester film is used throughout the spaceship because it helps stabilize the temperature of the ship in space. Gold is also used, believe it or not, as a lubricant between mechanical parts of the ships. Lubricants one might use in machinery on earth are ineffective in space as radiation outside of Earth's atmosphere would evaporate them. Gold, however, under intense radiation pressure can serve as a lubricant between moving parts.

Glass Making

Gold is also used for glass making as a pigment to tint glass, but it is also used as an insulant. As the world "goes green" to make the world more sustainable for future generations, modern buildings are constructed with gold coatings on the glass to help insulate them. In the summer the gold on the glass keeps the heat out by reflecting the radiation from the sun outward, and in the winter it reflects the internal heat inward, keeping the building nice and warm without using much energy on internal heating systems.

The Future Use Or Nonuse Of Gold
The use of gold for things outside of jewelry has increased quite a bit since the U.S. abandoned the gold standard in the 1970s. The malleability, dependability, the fact that it does not tarnish and that it is a good conductor of electricity make it ideal for many different uses. Normally gold is only used when there really is no other substitute, and because gold is so useful, it is rarely abandoned once it is found to be useful for something. However, due to its cost and scarcity, as technologies improve and substitutes are found, the industrial and technological use of gold may diminish. Nonetheless, gold's importance to the modern global economy as not only a commodity but a monetary asset will likely continue.

Gold's

Importance to the Modern Economy

Now we can finally delve into gold as a traded commodity. As mentioned previously, gold no longer backs any currency, however it is still vital to the global economy, which is demonstrated by the fact that almost all central banks hold substantial international reserves in gold.

Gold has many similarities with other commodities, but it also behaves similarly to a currency and can be thought of as monetary asset. Even today after the abandonment of the gold standard, if you went anywhere in the world, you could probably exchange gold for goods and services. One probably wouldn't be able to do that with most other commodities. However, like most other commodities it is taken from the earth, and it has an inverse relationship with the U.S. dollar.

Although gold shares some characteristics with other commodities, it certainly stands out from the rest for a variety of reasons. According to the World Gold Council, gold truly is a commodity like no other, stating that: "Gold is less exposed to swings in business cycles, typically exhibits lower volatility, and tends to be significantly more robust at times of financial duress."

How Does Gold Compare And Contrast To Other Commodities?

We will start with the laws of supply and demand, also known as the fundamental drivers, which tend to affect commodities heavily. The fundamental drivers are exposed often and influenced by risks associated with geopolitical issues, wars, disease and weather, among other factors, which can impact commodity prices heavily. Most commodities are subject to some or all of these risks. Take oil, for example, which is similar to gold in that it is a very liquid commodity. However, it is heavily influenced by the business cycle for industrial purposes. It also tends to be extracted in certain geographical regions, leaving it more exposed to the potential for idiosyncratic risks, such as some of those outlined above.

Gold is not exposed to the same risks from the fundamental drivers, especially supply. Think about agricultural and energy commodities. These commodities are generally one and done. Metals, in general, can be reused, which means there is another massive avenue for supply that other commodities do not have. The fact that gold production is

geographically diversified, meaning that it can basically be mined anywhere in the world, also makes it unique. Gold's geographical diversification is actually a massive differentiating factor from other commodities. If we take a look at other commonly traded commodities, according to the World Gold Council, 47% of global oil production comes from the Middle East and Eurasia, platinum is primarily mined in South Africa (80%) and

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Russia (11%), while corn, an important agricultural commodity, is produced mainly in the U.S. (39%). Silver, a metal that is possibly the most similar to gold in terms of its

status as a commodity and monetary asset is primarily produced in Latin America. Because of this supply characteristic of gold, the price of gold is primarily and almost exclusively influenced by demand.

Perhaps comparing gold to other metals would be a fairer comparison to make. Transportation of metals is fairly easy being that there is little need for specialized infrastructure such as those that are needed for many energy commodities. Metals, especially gold, have a much longer shelf life than other commodities, as was mentioned above, because they can be reused. However, this is generally speaking where the similarities between gold and other metals stop. Gold is nearly indestructible, meaning the recycling of previously used gold makes it much less susceptible to production shocks and shortages, and the stocks of annual flows ratio is much higher for gold than other metal, not to mention other commodities. Although, as mentioned previously, gold is used in the technological sector for electronic devices and computers, there is less demand for it in these sectors than for other metals, meaning that other metals are highly exposed to the business cycle in comparison to gold. Gold's status as a "noble metal," meaning that it does not tarnish, oxidize or corrode, makes it unique to many other metals, while at the same time it is extremely malleable and easy to work with.

Liquidity, Depth And Breadth Of The Gold Market

The gold market is very liquid, but it is also extremely large even when comparing to not only other commodities but other currencies and debt markets. According to the London Bullion Market Association (LBMA), in 2010 the daily net amount of gold that was transferred between accounts averaged USD \$21 billion. However, this does not necessarily account for all the trades between bullion dealers that are simply recorded in trading books. Taking this into account, it is estimated that global trading volumes could be between USD \$63 billion and USD \$211 billion, which is actually larger than many sovereign debt markets. It

must be noted that these numbers were taken at the height of the financial crisis in 2010, when gold may have been highly traded as a hedge against low currency values and volatility in financial markets. However, it will still give you an idea of the scale of the gold market around the world.

Gold As A Monetary Asset

Its role as a monetary asset also differentiates it from most other commodities. Although the gold standard has long been abandoned, gold's long history as a standard of value in monetary systems, and its history of obsession for more than 5,000 years, has left a lasting legacy and relevance in today's international monetary system. Central

banks still hold substantial international reserves of gold for national wealth preservation and as a hedge against economic instability.

Not only is gold not subject to many of the supply-side risks that most other commodities are subject to, but it is actually safer than most currencies and asset classes and used by investors as what is called a safe haven. At times of economic and political uncertainty, investors usually buy gold to preserve their wealth. Historically speaking, it has been the case that those who have survived economic and political shocks were those who had gold. When the economic landscape becomes a bit rocky, values of currencies tend to fall. One thing that remains constant is the purchasing power of gold.

To demonstrate how gold can preserve wealth, we can use a great example from Investopedia. Think about it this way: Forty years ago you probably could have bought yourself a nice suit for USD \$35 or an ounce of gold for the same amount of money. Fast-forward to today, USD \$35 would not buy you a suit, but if you had that ounce of gold you bought 40 years earlier and sold it, you could probably go and buy yourself a pretty nice suit. Besides using gold as a short-term safe haven, it can also be invested in the long-term. The purchasing power of currency diminishes over time because of inflation and other factors, whereas the value of gold is



inversely related, continuously increasing in the long run, preserving its purchasing power. This makes gold a hedge against rising inflation. As inflation rises, typically so does the value of gold. Gold preserves wealth because it also benefits from a declining U.S dollar.

It is safe to say that gold is neither just a commodity nor just a monetary asset, sharing many characteristics of different asset classes. Its unique characteristics in terms of aesthetics, chemical properties, history as a currency, depth and liquidity of the gold market, its geographical diversification, as well as its propensity to preserve wealth make it a hybrid of the best of both worlds.

Concluding Remarks

If you read all the way through Part 2 of this series on gold, you will now have a better idea of how gold is mined and produced, an idea of how its properties make it such a useful metal, as well as its industrial and technological uses. You will also have a better idea of what sets gold apart from all other commodities, as well as gold's unique role as both a commodity and monetary asset. All of the above, albeit a bit disconnected, serves to further explain how gold truly is the most precious of metals.

If you missed Part 1 of this series on the history of gold and the gold standard, don't forget to check that out. If you want to learn more about gold, stay tuned for Part 3 of our series.

Gold: The Most Precious of Metals (Part 3)

Gold production in many countries, especially in developing or emerging markets, has declined in the past few years, as the depressed price level of gold has led many mining operations to shut down or downsize significantly. In Part 3 of our series on gold, we begin with a section explaining why the price of gold has been trending upward since the turn of the year. This is followed by a section on the history and news on gold production in each of the top gold-producing economies globally in 2015 according to the United States Geological Survey, as well as the economic outlook for each according to the FocusEconomics Consensus Forecast.

Why Gold Prices Are Rising

In Part 2 of this blog post series, we included a section on how gold is used to preserve wealth. Because

of gold's history as a standard of value in monetary systems, it has left a lasting legacy in today's international monetary system. Historically speaking, those who have held gold have been able to survive crises. This is something that still rings true to this day. During times of economic or financial turbulence, individuals and even foreign central banks look to acquire gold for risk aversion because, unlike most other commodities and asset classes, gold tends to preserve its value.

People generally don't lose confidence in gold, but they do lose confidence in economies and currencies. As a result, the price of gold tends to give us an idea of when a financial crisis is about to hit. As uncertainty begins to fester and sentiment begins to turn negative, confidence in currencies is lost and investment in hard assets increases. Gold's price, unique to most other commodities, is almost exclusively driven by demand. As demand for gold increases, so does the price.

During the global financial crisis the price of gold skyrocketed. The average price of gold per troy ounce in 2007 was USD \$696.77, and by 2012 it was USD \$1,668.69. As global economies began to slowly but surely come out of the crisis the price of gold decreased. In 2015, the average price of gold was USD \$1,159.8 marking a 30% drop in four years. However, volatility in stock markets and uncertainty over the health of the world econ-

omy since the beginning of 2016 has seen prices creep up once again as safe haven investments have increased.

According to a Wall Street Journal report, gold tallied its best quarterly gain in more than 30 years in Q1, as the global economy grew at its slowest pace in almost three years. Weaknesses that plagued emerging markets in 2015 carried over into this year while dynamics among developed countries remained weak. The global economy expanded 2.5% annually in Q1, which was below the 2.6% expansion tallied in Q4. According to the FocusEconomics Consensus Forecast Commodities, in March of this year the price of gold rose to more than USD \$1,250 per troy ounce, which marked the highest price in more than a year after falling to a multi-year low in December. The price hit an over one-year-high at the beginning of this month, and on May 13, gold closed the trading day at USD \$1,271 per troy ounce, which was up 1.9% from the same day in April. In addition, the price was 19.6% higher on a year-to-date basis and was up 4.7% from the same day last year.

Since gold pays nothing to its holders and struggles to beat yield-bearing

assets when borrowing costs are high, low interest rates tend to support gold prices. Shifts in the value of the US dollar also tend to influence the price of gold, as it is globally priced in US dollars. After

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the US Federal Reserve left rates unchanged in April, it was believed that the Fed would hold rates again in June. The value of the US dollar

began to fall, making gold cheaper for foreign investors and consequently helped drive up the price of gold.

Macquarie Group analyst Matthew Turner, as quoted in a Reuter's report, stated that the increase in the gold price is down to, "the shift in the Fed stance, the weaker dollar and the prospect of inflation."

Speculation in the market of late is that the Fed may raise rates in the June after all, which has seen the value of the dollar rise and the price of gold fall slightly. However, Boris Schlossberg of BK Asset Management isn't so sure that the gold price rally is over.

Our forecasts project the price coming down slightly later this year. However, the higher price should see an uptick in gold production in the coming future. As was mentioned previously, if the price continues to rise this could mean a crisis is on the horizon.

With that in mind, let's take a look at the world's top gold-producing economies according to the USGS, including history and news on gold production in each country, followed by their current economic outlooks for 2016.

Top Gold Producing Countries 2015

History
and
Economic
Outlook



Australia

The discovery of gold played a large role in Australia's history starting with the Bathurst Gold Rush in 1851. Gold finds in other parts of Australia following the Bathurst Gold Rush brought millions of migrants to Australia. In the 1890s gold was found in Western Australia in Coolgardie and Kalgoorlie. According to The Australian Atlas of Mineral Resources, Mines, and Processing Centres, 60% of gold mined in Australia today comes from that region. Gold is also mined in all of the other Australian states, as well as the Northern Territory.

Mining is a significant primary industry in Australia and a major contributor to the country's economic growth. During the commodities super cycle starting last decade, Australia thrived, but since the commodity bubble burst, the economy and specifically the mining sector has suffered considerably. According to The Australia Institute, 22,000 mining positions were axed between 2013 and 2015, and according to the Sydney Morning Herald, a further 2,000 were cut earlier this year. The job cuts in the sector give an idea of the state of the mining sector in Australia, and as the country's third-largest export earner after iron ore and coal, gold mining plays a big part. Australia is the world's second highest producer of gold, mining an estimated 300 metric tons in 2015 according to the USGS.

Economic Outlook

In Q4, the Australian economy grew 0.6% over the previous quarter. The print was less than the 1.1% recorded in Q3 2015; however, it beat market expectations of a 0.4% increase. Although Australia's economy defied expectations in the last quarter of 2015, so far 2016 could be going better Down Under. An economic slowdown has been able to be avoided thanks in part to strong growth in the housing market, which supported the construction industry and lifted consumer sentiment. However, housing price growth slowed in Q1 2016, and homeowners are feeling less optimistic about the future value of their homes. This is evident in weak consumer sentiment, which fell again in April in the most recent reading. Consumers' confidence is likely to take another hit in the coming months as Prime Minister Malcolm Turnbull stirred economic uncertainty when he stated that he would call for a double dissolution election—an extraordinary measure designed to remove deadlocks in Parliament—which will likely be held on July 2. The potential for another change of government may have an impact on business and consumer confidence, which could negatively affect business investment and retail sales at a pivotal point in Australia's economic rebalancing act.



Brazil

Gold mining in Brazil stretches as far back as the 1690s when the Brazilian Gold Rush began. Unlike most gold rushes, the Brazilian Gold Rush lasted more than 200 years until the 1900s. Brazil's gold-mining activities, like many other countries, played a large part in the development of the country and its economy. Although gold has been and continues to be a very important driver for the Brazilian economy, the many years of exploitation has exhausted Brazilian gold mines. However, it is still the 11th highest gold producer in the world with an estimated 80 metric tons in 2015.

Economic Outlook

Brazil's economy sank into the deepest recession in recent history last year amid low prices for key exports, soaring inflation and depressed confidence levels. Moreover, as the economy plummeted so did President Dilma Rousseff's political career. A wide-spread corruption scandal and the economy's abysmal performance caused approval levels to fall to all-time lows and resulted in the commencement of impeachment proceedings last year. On May 12, the Senate voted to continue with these proceedings, forcing Rousseff to step down for a maximum of 180 days while a trial is conducted. Vice President Michel Temer took over as interim president, and his first task will be to find a way to halt the sinking ship. However, a number of daunting challenges lie in Temer's path, and recent economic data remain poor: Retail sales returned to contraction in March, and the manufacturing PMI fell to the lowest level in more than seven years in April. A change in leadership will not be a magic bullet for Brazil's economy, and FocusEconomics expects the recession to continue throughout this year.



Canada

Gold in Canada is found all across the Laurentian Plateau, in British Columbia, Nunavut and Newfoundland. Gold was first discovered in Canada in 1823 along the Chaudiere River in Quebec. Many years later the legendary Klondike Gold Rush in 1896 sparked a massive migration of prospectors to the Yukon River basin in search of gold with the dream of striking it rich. It has been called the last great gold rush.

Since then, Canada has been a Steady Eddie in terms of gold output, especially for the past decade, as it has been at the top of the rankings for gold production by country. In 2014 Canada achieved a record for gold output at 152 metric tons, which marked the first time

Economic Outlook

Although economic growth in Canada beat market expectations last year, business investment in Canada contracted in 2015 and represented a sizable drag on GDP growth over the year. Collapsing investment is one of the main avenues through which last year's drop in commodities prices is affecting economic activity. In more recent indicators of growth in Canada, GDP contracted in February after strong growth in January. However, a recent upswing in the price of oil has provided a glimmer of hope for the economy and lifted the value of the Canadian dollar. Should the rally in oil prices continue, some investment may trickle back into the Oil Patch, which would provide much-needed relief for oil-dependent provinces. Although the strengthen-

that it caught up to South Africa in annual output. The estimated output for 2015 by the USGS is expected to be slightly lower at 150 metric tons. As for this year, the rally in gold prices has Canadian gold mining shining bright in 2016.

ing dollar signals improving confidence in the Canadian economy, it may compromise the gains made by export-oriented industries in recent months, which have grown markedly thanks to the competitive currency as well as a steadily increasing demand from the U.S.

Canada's economy is expected to gradually recover, with growth accelerating this year and next as commodity prices pick back up and an expansionary fiscal policy takes hold. The Bank of Canada will also provide support for the economy as it is expected to keep rates at historic lows over the forecast period.



China

China is the number-one producer of gold in the world. The USGS estimates that China mined 450 metric tons of gold in 2015. Since gold began to be mined in the 1970s, gold production in China has rapidly increased. China finally overtook South Africa in 2007 as the world's top gold producer. China's major gold production regions are generally located in the east of the country, in the eastern provinces of Shandong, Henan, Fujian and Liaoning. Most of the gold mined in China stays within its border to produce jewelry. The demand for gold in the west over the past decade has decreased, while Chinese demand has increased dramatically. In 2014, China was the top gold consumer in the world at 27.9% of global consumption, just ahead of India at 26.5%.

Although China is the world's top gold producer, it is expected that Chinese mining companies will begin to explore potential acquisitions of international gold producers to meet demand and reduce dependency on international gold producers. China's insatiable appetite for gold also led to a new price fix in Shanghai a few weeks back in an attempt to start a regional benchmark priced in Yuan to increase its influence in the global gold market.

Economic Outlook

China's economic slowdown over the last year or so has been well documented with final 2015 growth falling to a 25-year low. Economic activity has continued to decelerate at the outset of the year, as authorities have begun to promote a more balanced economic model at the expense of weaker short-term growth. The key question regarding China's economy is whether the economic slowdown is related to structural macro-economic imbalances or if, on the contrary, it reflects a genuine shift to a more sustainable growth path.

In Q1, China's GDP increased 6.7% annually, which came in marginally below the 6.8% expansion observed in Q4. The print represented the weakest expansion since the height of the global financial crisis in Q1 2009 and was in line with market analysts' expectations. However, more recent indicators indicate that strong policy support and improved credit conditions fostered growth at the end of Q1 and helped to stabilize economic activity in the first three months of 2016. Some indicators have signaled recently that China's gradual transition toward a more sustainable growth path is in the works and a loose monetary stance, rising investment and improved dynamics in the property sector indicate that the pickup observed in March will likely continue in the coming months.

While policy support is expected to shore up the economy in the short-term, government-led credit growth presents significant downside risks to China's outlook from a somewhat longer-term perspective. Particularly, cheap credit has the potential to further exacerbate domestic imbalances.



Ghana

Ghana has been a major producer and exporter of gold dating all way back to precolonial times when gold was exported from present-day Ghana to Europe via trans-Saharan trade routes. Gold mining was mostly alluvial until the 1860s when modern mining techniques were first implemented to extract gold.

Many years later, Ghana is now Africa's second-largest producer of gold behind South Africa. Southern Ghana is considered to be one of the world's best regions for gold mining. However, despite still being one of the world's top gold producers, output of the mineral has dropped significantly in recent years. Much of this has been attributed to the fall in gold prices, as the global economy began to look healthier following the crisis. With the decline in mining activities followed increasing layoffs in mining operations while even illegal gold miners in the country have begun to give up. Nonetheless, Ghana is still the 10th largest producer of gold globally. The USGS expects the country to have produced 85 metric tons in 2015.

Economic Outlook

Economic growth in 2015 in Ghana was subdued at 4.1%, and significant macroeconomic imbalances persisted even though it was the second year under the IMF's stabilization and reform program. Sliding commodity prices restrained exports—Ghana principally exports cocoa, gold and oil—and caused the currency to plunge by nearly 20%. On top of this, recurrent power shortages hampered economic activity. While the current account deficit shrank somewhat and the fiscal deficit narrowed due to the government's fiscal consolidation efforts, elevated public debt and financing costs remain a concern.

Following 2015's turbulence, GDP growth will likely tick up this year, as private consumption and fixed investment should increase. The opening of new oil fields and developments in the gold sector as the price has begun to rise should also prop up growth. However, external imbalances, the struggling power sector, elevated public debt, tight financing conditions and high inflation remain challenges. Uncertainty surrounding November's elections adds to the downside risks.



Indonesia

Indonesia is home to one of the largest gold mines in the world, the Grasberg Mine. It did not technically open until the 1980s, but its origins can be traced with the Ertsberg mine, which was first discovered in

Economic Outlook

Indonesia's economy lost steam last year as rising government spending failed to compensate for falling exports and lackluster private consumption. While surging government consumption should boost growth

the early 1900s but didn't officially open until 1973. The mine is thought by some to hold the largest gold reserves in the world and contributes the majority of Indonesia's gold production. The Grasberg mine has been the site of numerous attacks by the Free Papua movement beginning in the 1970s. Papua, Indonesia's eastern-most province, has been a hotbed for an independence movement among inhabitants of the province, which has prompted the Free Papua Movement to make numerous attacks on the mine over the years. The mine is owned by a foreign company, which has many Papuans resentful because they believe it profits disproportionately from the region's natural resources without giving much back. Nonetheless, the mine employs more than 19,500 people in the area. Pollution and environmental harm are another source of resentment toward the mine, which many believe is contributing heavily to pollution to surrounding rivers, land surfaces and groundwater.

Apart from the Grasberg Mine, Indonesia is in the midst of a modern gold rush, where it is estimated that, quite remarkably, illegal gold mining is producing more within the borders of the country per year than the estimations of Grasberg's yearly output. According to a New York Times report, corruption and even more pollution are at the heart of the illegal gold mining in Indonesia. The crucial ingredient in the purification process of the gold by illegal mining operations is mercury, which has environmentalists and other health experts concerned around the world. Many of the small-scale illegal gold-mining operations are funded by businesses located in the country's capital city, Jakarta, which pay local authorities off to allow them to continue the practice. Although illegal gold mining is not taken into account in the USGS survey, Indonesia's estimated gold output in 2015 by the USGS is thought to be 75 metric tons, making it the 12th highest producer in the world by yearly volume.

this year, high-frequency data suggests other economic drivers are stuck in the doldrums. The trade surplus more than halved in March, and growth in real retail sales moderated in February. Meanwhile, the government unveiled its 11th economic stimulus package at the end of March. The latest measures to boost growth, including lower taxes on real estate investment and measures to cut red tape at Indonesian ports, should boost the economy this year.



Mexico

Although Mexico has historically been known for its silver mining, it is also a major player in gold production. Gold has been mined in Mexico for more than 500 years, and although the country has a long history of mining for precious metals, there are still large deposits of precious metals that have gone untouched. Recent developments in mining technologies are now making it possible to get to some of those untapped deposits, while Mexico's political environment is largely considered to be favorable to mining activities, meaning that Mexico will likely be one of the top gold-producing economies for the foreseeable future.

However, gold mining in Mexico has not been without controversy. Many mining corporations that are present in Mexico are foreign, such as McEwen Mining Inc., which recently had a refinery robbed and looted by armed gunmen late last year. This was the third attack of this kind in 2015. Kidnappings are also an issue, with workers disappearing and turning up dead days later. This recent flurry of attacks highlights the perils of mining in Mexico, and the security issues may present downside risks to the mining sector in Mexico in the future.

Mexico is still a world leader in gold production with an estimated volume of 120 metric tons in 2015.

Economic Outlook

Mexico's economy was more resilient to external headwinds at the beginning of the year. Preliminary data shows that GDP growth picked up from 2.5% year-on-year in Q4 2015 to 2.7% in Q1. The result, which exceeded expectations, was driven by faster growth in all three of the main sectors of the economy. Agriculture and services expanded robustly in Q1, while growth in the industrial sector was surprisingly faster, considering cutbacks in oil production and a slowdown in the U.S. economy in Q1. Moreover, manufacturing gauges in April suggest that the sector is off to a positive start to Q2. On a negative note, consumer confidence slipped further in April, suggesting that sentiment is losing traction, despite strong consumption fundamentals. In response to Moody's warning in March that it could decide to downgrade Mexico's rating, the government announced new expenditure cuts together with the guidelines for next year's budget.

Economic growth will be supported by strong private consumption this year. However, Mexico is facing a painful adjustment to low oil prices and weak demand for its manufactured exports.



Peru

There is no question that Peru is a mining country, with the country's mineral deposits having been mined going back more than 1,000 years. One drawback to Peruvian mining is that many of the mineral deposits are located in the areas that are fairly inaccessible in areas of high elevation in the Andes. Peru's government is pro-mining and open to foreign investment, playing a limited role in the oversight of the country's mining

Economic Outlook

The latest polls for the June 5 runoff presidential elections indicate a nip-and-tuck race. Regardless of the winner, policies are expected to remain business-friendly, which both candidates claim to be. Peru's economy gained steam in the fourth quarter of last year, as the economy weathered external headwinds. More recent data related to the external sector show that the trade deficit improved notably in March due to larger exports

industry. Much like the mining industry of Indonesia, pollution is a big concern in Peru, especially from illegal mining, which is rampant. Similar to illegal gold mining and production in Indonesia, the use of mercury is widespread. According to the USGS, Peru is the seventh-largest producer of gold annually, having produced an estimated 150 metric tons in 2015.

of traditional Peruvian shipments. Moreover, business sentiment turned optimistic in April for the first time since July 2015. This upswing in confidence is also likely due to the first round of elections held in April, since markets praised the outcome.

Despite continued external headwinds emerging from economic crises in the region, the economy is foreseen maintaining healthy growth this year.



Russia

Russia is a massive country geographically and consequently, as one might imagine, it has a wealth of natural resources. This includes gold, and although the country has been mined for gold going back many centuries, gold production actually hit an all-time low as recently as 1998.

Russia's economy was in a shambles leading up to and after the breakup of the Soviet Union. After the fall of the Soviet Union, the first president of the Russian Federation, Boris Yeltsin, sought to restore Russia to its former glory by privatizing large parts of the economy and dismantling the economy's central planning mechanism, which didn't work out too well. The economy plunged into despair, culminating in the 1998 financial crisis and Bank Rossii defaulting on its debt. Yeltsin finally resigned on New Year's Eve in 1998 and put a man in charge whose name many will probably recognize: Vladimir Putin.

Since Putin has been at the head of the table, Russia's mining sector has gradually developed, reaching a booming period between 2008 and 2009. In fact, since the late 1990s, Russia's gold production increased two-fold. Although the Russian mining sector largely contributed to the economic resurgence the country saw during the last decade, it is currently at a loss for foreign investment, something it relied on heavily in the

Economic Outlook

Following a strong contraction Q4 2015, Russia's economic activity decreased in Q1, though the drop is expected to be less severe than in the previous quarter. Industrial production took a step back from an incipient recovery in March as output contracted following February's modest expansion. Moreover, a continuous deterioration in economic conditions prompted unemployment to rise in March. On the external front, weakness in global demand coupled with the country's deep recession prompted exports to contract at a double-digit rate again in March. Heading into Q2, leading indicators suggest that the economy is still fragile. In April, the manufacturing PMI fell to an eight-month low, while the services PMI continued to improve. These results highlight the diverging performance between Russia's goods producers and services providers once again. FocusEconomics expects the economy to remain in recession this year. Weak private consumption is expected to be the main drag on growth in 2016 as high inflation, low wages and rising unemployment will continue to hit households' spending. However, a gradual rise in oil prices and the stabilization of the currency will provide some support to growth.

past. Low commodities prices have made the mining industry, especially for gold, less attractive for investors. Geopolitical issues with the west and Ukraine as well as macroeconomic uncertainties have also significantly hurt investment in the sector. Since gold mining is geographically diversified, investors can turn to any number of less-risky countries for investment.

Russia is still one of the world leaders in gold production. The USGS estimation of 2015 gold output is 242 metric tons, making it the third top gold producer in the world.



South Africa

In 1886, when George Harrison stumbled across gold in South Africa, he set off a chain reaction starting with the Witwatersrand Gold Rush that changed South Africa from a largely agricultural society to one of the largest gold-producing nations in the world. This was important at the time, as the gold standard was still in its golden age.

So many migrants came to South Africa with the dream of striking it rich that some of South Africa's biggest cities sprung up as a result of the gold rush, including the capital, Johannesburg. The gold discovery led to the widespread construction of infrastructure like roads, railroads, buildings and towns and made it the richest country on the continent of Africa. Gold has continued to be a massive contributor to South Africa's economy, and as mentioned earlier, the country was the king of gold production until China overtook it as the number-one gold-producing economy just a few years ago.

As is a theme with many commodity-driven economies, the low-commodity-price environment has hurt South Africa's gold mining industry of late. Although many of South Africa's mines have become depleted of their proven reserves, they are still located on top

Economic Outlook

Recent data shows that South Africa's economy likely recorded another weak growth rate in Q1. Manufacturing production expanded in February; however, the PMI deteriorated and hit the lowest level in nearly two years in March. The country's outlook remains fragile as electricity and water supply constraints coupled with low commodity prices will weigh on growth. Moreover, failure of the government to push forward with fiscal consolidation reforms might provoke a downgrade of the country's credit rating to junk territory.

of possible reserves. Unfortunately, the nature of the low-commodity-price environment has meant that mining for that gold is no longer economically viable. Investment in mining activities has been an issue as it has been in Russia, as macroeconomic issues have left the country in a precarious position. Power outages and drought have hurt the agricultural sector and manufacturing respectively, leading to unemployment and a depreciating rand. South Africa is still a leading producer of gold, producing an estimated 140 metric tons in 2015, the fifth-highest mark in the world.



United States

In 1799, Conrad Reed found a 16-pound gold nugget in a creek that ran through the family farm located in North Carolina. The nugget served as a doorstop for three years until a jeweler recognized the rock on Reed's porch and very slyly asked him to name his price. Conrad asked for USD \$3.50 for the nugget. Shortly thereafter, the first commercial gold find and subsequent gold rush in the United States began. Following the North Carolina Gold Rush, of course, was the famous California Gold Rush, which led to a massive migration of people from all over the world to the West Coast of the United States in search of riches in the form of gold, hastening the settlement of the great Wild West of the United States. More than 150 years later, the United States is still a top producer of gold globally with the state of Nevada supplying close to 70% of the country's gold output itself. Gold production in the States has been on the decline since 2000, as demand for gold has decreased within its borders, but the country can still count itself among the elite with an estimated 200 metric tons of output in 2015, making it number four on the list of top gold producers.

Economic Outlook

An advance estimate showed that the U.S. economy slowed at the outset of the year. In Q1, GDP increased at a seasonally adjusted annualized rate of 0.5%. The result came in below the 1.4% expansion registered in Q4 and reflected weak growth in domestic demand, which was dragged on by a contraction in fixed investment as energy businesses reacted to the renewed slump in oil prices at the beginning of the year. In addition, a strong dollar at the start of the year took a heavy toll on exports, which contracted for a second consecutive period in Q1. Private consumption, the key engine of the economy, moderated but remained resilient in Q1 despite the heightened financial volatility registered in the first few months of the year.

Despite ongoing challenges at home and abroad, the economy is likely to grow at a steady rate and be one of the major drivers of global growth this year.



Uzbekistan

Economic Outlook

Mineral mining and especially gold production plays an important role in the economy of Uzbekistan. Gold is primarily found in the Kyzylkum Desert and is home to the Muruntau Gold Deposit, the largest single open-pit gold mine in the world. The gold deposits were first found in the area in 1958 with the mine opening a few years later. The mine has produced around 1,500 metric tons of gold to date, and the deposits of gold in the area are expected to last until 2032. Many experts believe that Uzbekistan may be on top of the world's largest gold reserves with experts quoting figures ranging from 2,500 to 5,300 metric tons of gold yet to be mined. Uzbekistan is expected to have produced 103 metric tons of gold in 2015 as estimated by the USGS.

According to official indicators, Uzbekistan's economic activity grew by 7.5% in Q1 2016. While the recession in Russia and slowing activity in China, Kazakhstan and Ukraine—all major trading partners—weighed on growth, economic activity was supported by strong public investment. Moreover, a seven-year-old feud between Russia's energy giant Gazprom and Turkmenistan recently culminated with the dissolution of an agreement regarding the delivery of natural gas. Gazprom is set to substitute Turkmen gas with deliveries to Uzbekistan, with contracts already signed amounting to 140 billion cubic feet of natural gas to be delivered in 2016.

As external headwinds continue to weigh on the economy, government spending is set to remain the strongest driver of economic growth.

The Future of Gold

As the demand for gold increases globally, especially as economies in Asia continue to develop, we may have to ask: What does the future of gold look like? Gold is scarce and costly to mine. However, almost all of the world's gold that has ever been mined is somewhere in the world at the moment, but it's likely that most of it is locked away in a vault somewhere, as government and individual investors increasingly "bar hoard." As more sophisticated technologies are developed to detect the presence of gold in areas that were previously thought

to not hold gold or to be depleted, the better for top gold-producing economies. However, environmental concerns over the mining and production of gold will have to be taken into account as these technologies progress. Will gold mining continue at profitable rate...on Earth? The high demand for gold used for jewelry, risk aversion and for industrial and technological uses, will probably not be surpassed in the near future by a substitute, leading many scientists to look toward heavens. Asteroids that have passed by Earth have been studied, and indications are that there are high deposits of metals and minerals present on them. The question perhaps is, will human's historic

obsession with gold lead to mining it in outer space? How could this affect the price of gold in the future? Who will be the top gold-producing economies once we start landing on asteroids? Only time will tell.

FOCUSECONOMICS

About the Author

FocusEconomics is a leading provider of economic analysis and forecasts for 127 countries in Asia, Europe, Africa and the Americas, as well as price forecasts 33 key commodities. The company provides reliable and timely information to help companies make the right business decisions. FocusEconomics' extensive global network of economists, coupled with its position as an industry leader, are indications of the company's solid reputation as a reliable source for business intelligence among the world's major financial institutions, multinational companies and government agencies. www.focus-economics.com

A Work in Progress: *Are Emerging Markets Becoming More Investable?*

 **Andrew Burrell**

The rise of emerging markets has been a key global trend of recent economic history, highlighted by the ascent of the BRIC countries in the past 10 years or so but established well before. Although activity in these immature markets—where higher returns are accompanied by greater risk and volatility—remains undeveloped, the potential is clear, and it is no surprise investor interest has increased.

The ongoing search for returns in the current low-interest-rate environment is only likely to reinforce this.

Recently, Investment Property Forum conducted a research project focusing on emerging-market investment in a real-estate context. The related survey was aimed at understanding

the scale and balance of activity between established and emerging markets, as well as gauging whether these underdeveloped markets are more investable than a decade ago. In addressing these questions,

it was hoped to gain insights into the factors that determine the developmental status of real-estate markets and the structures that are most conducive to their future growth.

Key trends in emerging-market investment

Using previous global research on market evolution as a starting point, the 50 most important global investment destinations were categorized into developed, emerging and frontier markets, based on their investment flows, transparency and GDP levels. These aggregate groups formed the basis for the quantitative analysis in the rest of the research.

As noted, economic evidence indicates a shift in the balance toward emerging and frontier markets since 2004. The advanced grouping in this survey showed roughly a 10% loss in GDP share over the period, to the benefit of the emerging world, though these economies still accounted for about 60% of the world total. The relative decline was marked by past standards and is explained by the China-led surge in BRIC growth after 2000 and the severe impact of the global financial crisis on growth in the advanced markets.

Real-estate investment data shows inflows to these dynamic emerging and frontier economies also outstripped those in the developed world. Inflows rose by 40% on an underlying basis (the past three years compared with the 10-year average), compared with an increase of 18% in the established markets.

A US-led recovery during the recent past has closed the gap, but the share of total investment flows into emerging markets remains well up on 2004. Not only this, but individual emerging markets now are appearing in the global rankings, most notably China, with the seventh-largest inflow overall; South Korea, Russia and Brazil also rank in the top 20 global destinations.

*...data suggests
neither the open
(high levels of cross-
border flows) nor the
domestic focus (low
levels) has resulted in
stronger performance
over the longer term*

The picture varied widely among markets and regions. Progress has been strongest in BRIC and the Asian Tigers, with China, Mexico, South Korea and Russia most buoyant.

With the exception of Poland, investment in European emerging markets generally was much weaker. Declines were recorded in Portugal and Greece, for example, rep-

resenting a rapid fall from grace for Euro zone member states regarded as “close to developed” in precrisis times. Other markets in Central Europe and Eastern Europe also fared less well.

Investment activity remains highly concentrated in the developed world, however, with emerging and frontier groups combined accounting for only one-tenth of the total in 2014. While trailing the economic contribution, this lag is not surprising. It is broadly in line with experiences in other assets, notably equities, where market capitalization accounts for a similar share in emerging markets. It also should be remembered investment flows are disproportionate even in the developed world, with the United States and the United Kingdom alone accounting for almost half of the total.

A challenging assessment

Assessment of emerging-market investability was one of the challenges of this research. Ideally, a measure of the invested property stock relative to the total is required, but this data is rarely available. To overcome these limitations, JLL Research uses an alternative “investment intensity” measure, which compares the past three years’ average capital inflows with current GDP levels. This provides a gauge of how well inflows are captured by



markets, relative to their size, with GDP acting as a proxy for the property stock in each market and volumes smoothed for an even comparison.

The measure provides some interesting results. A wide disparity exists across countries and cities on this metric, but, on average, we saw a clear gap between emerging and established markets. National results were not conclusive, with developed markets seeing a slightly stronger rise over the past decade. But intensity within the major cities of the emerging markets (arguably a more appropriate standard) showed a clear increase relative to

movements in more developed centres. Overall, it appears these markets have become more investable.

Global investment data also allow us to examine shares of cross-border transactions and concentrations of sector activity within emerging markets. On average, cross-border shares are higher in emerging and frontier economies. But data suggests neither the open (high levels of cross-border flows) nor the domestic focus (low levels) has resulted in stronger performance over the longer term, as, for example, South Korea and Poland have grown successfully through very different routes. Although office purchases

were regarded as a potential base for real estate development, no set sectoral pattern appears in the emerging world either.

Explaining emerging-market trends

The scale of emerging-market property investment has grown in both absolute terms and relative to the developed world over the past cycle, and evidence shows these markets are becoming more investable too. This raises questions

regarding whether this progress is an inevitable consequence of economic development and if it will continue, as well as why some markets have been more successful in attracting inflows than others. To understand this, we need to identify the drivers of performance. In this research, quantitative analysis of the emerging-market benchmarks and comparison with a variety of possible drivers was the main approach.

Economic variables were the obvious place to start, as these are regarded as the most important influences on commercial real-estate performance. Correlations of GDP and population growth with investment flows were high, with output measures explaining 90% of the movement in emerging-market inflows at both the city and national levels—much higher than for mature markets. This strongly suggests, with economic and demographic progress continuing to outstrip the mature markets, investment will continue to expand in emerging markets.

Many other factors also were identified for the development of emerging investment markets, including rule of law, taxation, political freedom and infrastructure. But even where these influences could be quantified easily—for example, qualitative measures, such as credit and political risk indicators—the relationship with property investment was much weaker than

for economics. This may, in part, reflect the data limitations, particularly the relatively short time series for capital flows. These factors may well be important modifiers of long-term development despite relatively weak results over the past decade, so this is an important area for further study.

*It (survey) highlights
the strong trends
in capital inflows
outside of established
markets and how
the emerging world
has become more
investable over the
past decade or so.*

Emerging markets or emerging cities?

In the wider debates on the evolution of emerging markets, the role of urbanization is a focal point. The shift from rural to city living is creating new conurbations each year, and evidence shows economic growth is becoming ever more concentrated in these urban clus-

ters of high value-added service industries. As the developed world is relatively mature in this regard, the bulk of this change is occurring within less-established markets.

Even without this trend, city dynamics are fundamental to commercial real estate. The retail and office sectors are integral to urban areas, and a concentration of other property types exists within cities, including hotels and apartments. Outside of the developed world, major cities are seen as key to opening up less-transparent markets, as investors will seek a foothold in these centers before exploring other opportunities. This research focused on these larger cities, the so-called gateways.

Given these priors, results from the city analysis added less to the overall insights than was hoped. Economic growth again was highlighted as the key driver of urban investment performance at the national level. But major city growth did not always lead whole-economy trends as widely expected, casting doubts on the gateway hypothesis. The trend in the developed world was the opposite; the top cities were more dynamic, on average, with inflows holding up better than in the outlying economy.

Even more unexpected, the pattern of gross returns in emerging markets was surprisingly similar to that in the developed world. Not only are the aggregate series highly cor-

related, but also there is a concern investors are compensated only marginally for the greater risk and volatility encountered outside the established markets. Although the evidence on the role of gateway cities was not conclusive, further clarification of their role in attracting property investment should be a focus for additional work in this area.

In conclusion

Overall, the survey threw some new light on emerging-market investment in real estate, as well as generating many ideas for further study. It highlights the strong trends in capital inflows outside of established markets and how the emerging world has become more investable over the past decade or so. In terms of drivers, economic growth emerges as a clear differentiator of performance, which reinforces the view significant future potential exists for investors as these markets mature.

The analysis was less successful in establishing general models for real-estate development. This may be because, as previous research has hinted, the importance of market specifics is such that general theories are elusive. Further detailed work to isolate structures and institutions that have been successful in promoting emerging real estate development would be a major step.

Improved data also would be helpful. The constraint of working with a historic perspective of less than one complete cycle was particularly

limiting in drawing out quantitative trends. This aspect, at least, should improve with time.



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About the Author

Since 1987, Institutional Real Estate, Inc. (IREI) has been a leading force in industry knowledge, providing institutional real estate and infrastructure investors with decision-making tools via its publications, conferences and consulting services.

Andrew Burrell is head of forecasting at JLL, based in London. This article is based on research undertaken as part of the research programme of the Investment Property Forum. The IPF research program is financed through commercial sponsorship from a cross-section of key UK market participants and publishes regular papers and surveys on property investment topics. Further information on the IPF and its research program can be found at www.ipf.org.uk.

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Rodrigo Duterte's Economic Vision:

The Punisher's Plans for the Philippines

 **Alexander Chipman Koty**

As Philippine president-elect Rodrigo Duterte prepares to take office on June 30, investors and business people both at home and abroad are wary of how the audacious politician will impact the country's booming economy. Under President Aquino, the Philippines enacted several liberal macroeconomic reforms and experienced an average GDP growth rate of 6.2%, leading the Oxford Business Group to name the country the best economy in South East Asia. However, widespread anger over elitism, corruption, inequality and crime catapulted the controversial politician to the country's highest office despite little explanation of his economic policies.

Duterte has made international headlines for his crude and seemingly off-the-cuff anti-establishment remarks while drawing anxiety from some corners due to his uncompromising tough-on-crime approach and implicit support for extrajudicial vigilante killings, giving him the monikers “Duterte Harry” and “The Punisher.” His populist campaigning, self-description as a socialist, lack of commitment to the rule of law and remarks that he does not know much about economics or care about the stock market have unnerved investors who fear a reversal of the previous administration’s liberal economic reforms.

To allay these anxieties, Duterte recently announced an eight-point economic plan setting out his agenda to maintain the Philippines’ vigorous growth. The plan addresses rural development, tax reform, corruption, education, tourism, ease of doing business, foreign investment and public-private partnerships.

Despite Duterte’s fiery and unpredictable rhetoric, he appears set to continue former president Benigno Aquino’s reforms and further open up the Philippines to foreign investment. While Duterte’s presidency promises to be eventful and campaign pledges may not ultimately be wholly fulfilled, investors can take solace in his reassurances to the business community and commitment to attracting foreign investment.

Law and Order

Duterte’s principle campaign promise to strengthen law and order features prominently in his economic plans. Duterte contends that eliminating gangs and organized crime will reassure investors wary of entering the Philippines due to concerns over their own personal safe-

*The Philippines
ranks 95th in
Transparency
International’s
Corruption
Perception Index,
showing the
pressing need for
reform in this area.*

ty. He touts his experience as mayor of Davao, where rampant lawlessness once earned the city the designation the “Nicaragua of Asia,” but now boasts the lowest crime rates in the country and strong foreign investment.

In addition to expunging urban crime, Duterte has pledged to quell

ongoing conflicts and insurgencies with Islamist and Communist rebels in the south, principally on the island of Mindanao. While Duterte is notoriously ruthless on crime, even admitting to killing criminals himself, he has signaled his openness to enter peace talks with rebels. If successful, he plans to promote the area—the Philippines’ second largest island and home to more than 20 million people—for tourism, agriculture and infrastructure investment.

Corruption and Ease of Doing Business

As part of his efforts to cleanse the Philippines of crime and elite entitlement, Duterte stresses the importance of eliminating government corruption. The Philippines ranks 95th in Transparency International’s Corruption Perception Index, showing the pressing need for reform in this area. Duterte asserts that stamping out corruption will give greater guarantees and predictability to investments while safeguarding investors from unexpected fees and extortion.

Eradicating corruption ties in with his plans to improve the country’s feeble ease of doing business standards, as he says government red tape is “what investors don’t like.” Indeed, the country rates an unimpressive 106th for ease of doing business, according



to the World Bank Group. To remedy this, Duterte aims to apply his “Davao model,” which he instilled as mayor of the city. He boasts that in Davao, processing government documents must be done within 72 hours and failure to do so must be justified to the Office of the Mayor. To further reduce corruption and government inefficiencies, he is also reducing the number of signatories required to issue a permit.

Lifting Foreign Investment Restrictions

Many of Duterte’s economic policies follow his well-known campaign commitments to wipe out crime in its various forms. Not to be overshadowed, though, is the potential for significant liberalization of foreign investment. Duterte has

expressed interest in granting foreign investors access to sectors currently restricted to Philippine nationals and allowing them to own at least 70% and possibly up to 100% of companies they establish in the country, up from the current limit of 40%. Getting rid of the so-called 60:40 rule should pose a challenge, however, as it requires amending the country’s 1987 constitution.

Sectors that are currently heavily restricted to foreign access include:

- Mass media and broadcasting
- Retail trade
- Domestic shipping
- Pharmaceuticals
- Advertising
- Public services
- Small-scale mining
- Private security
- Utilization of marine resources

While there is no guarantee that all or even many currently restricted

industries will be opened to foreign investment if Duterte successfully amends the constitution, there could still be significant opportunities on the horizon in these largely untapped sectors. Further, Duterte has also indicated support for joining the TPP, which in itself could require altering the constitution due to foreign ownership restrictions. However, it appears that he will maintain restrictions on foreign ownership of land, which is currently limited to long-term leasing.

Infrastructure Spending and Other Initiatives

Duterte’s team has put forward a variety of other measures to boost the economy, as outlined in the eight-point plan. To address the country’s infamous infrastructural deficits and

congestion issues, Duterte has committed 5% of annual GDP to infrastructure spending. It is hoped that increased spending will improve tourism through upgraded transportation and stimulate the Philippines' IT industry by enhancing the nation's internet connectivity. Additional focus on education and the struggling agricultural sector are other target areas.

Tax reform is another goal, though the specifics remain vague. To wit, Duterte stated that, "We need to be aligned with the tax system of our ASEAN neighbors. We need to be competitive. If investors see the tax system here is too punishing, they're not going to invest here." Duterte has expressed interest in pursuing a more progressive income tax system and more transparent bank secrecy laws, and these comments potentially open the door to lower corporate income tax as well. However, it remains to be seen what shape tax reform will specifically take.

Going Forward

Despite Duterte's often incendiary rhetoric, the economic proposals he has put forward are largely a continuation of the previous regime's liberalizations and are generally pro-business. Many of his proposals ultimately might not succeed: Eliminating crime in a nation of

more than 100 million, ending decades-old insurgencies and amending the constitution are not tasks that can be done overnight. Further, his economic policies remain vague and lack timelines and strategies for implementation. Even if he does not attain all his goals during his six-year term, however, investors can heed his advice for the business community to "relax" due to the policy continuity he has put forward.

Still, there remains potential for political instability during Duterte's tenure as president. Although he stresses the importance of law and order and creating a stable environment, he himself has threatened to skirt the rule of law. Reintroducing the death penalty, supporting extrajudicial killings, transitioning the country into a federal parliamentary system and amending the constitution could all introduce serious political crises. Indeed, Duterte has threatened to dissolve parliament and create a revolutionary government if MPs do not follow his orders, giving credence to his critics' fears of dictatorial strongman rule. Separating rhetoric from policy, as well as awareness of jokes and cultural references that could be lost in translation, is crucial to decipher Duterte's proposals. Although it might not be a smooth presidency, Duterte may very well attract foreign investment into his country

that, while growing steadily, has traditionally lagged behind its ASEAN peers in that area.



ASIA BRIEFING

About the Author

Established in 1999, Asia Briefing Ltd. is dedicated to providing individuals and enterprises with the latest business and regulatory news as well as expert commentary relating to conducting business in emerging Asia. The publishing house is a fully-owned subsidiary of Dezan Shira & Associates — a specialty foreign direct investment consulting firm with offices in China, Hong Kong, India, Vietnam and Singapore, alliances in Indonesia, Malaysia, the Philippines and Thailand, as well as liaison offices in Italy, Germany and the United States.

Puerto Rico Control Board Short List Includes George Pataki, David Chafey

✍️ **Xavira Neggers Crescioni and Andrew Scurria**

Former New York Governor George Pataki and David Chafey, former president of the Government Development Bank for Puerto Rico (GDB) and past president and COO of Popular Inc., are among the candidates for Puerto Rico’s fiscal control board, two sources close told Debtwire Municipals.

Four additional sources familiar with the situation confirmed Chafey’s candidacy. Two of these sources questioned whether Chafey, as former GDB president, would have a conflict of interest in overseeing the institution responsible in part for Puerto Rico’s debt crisis.

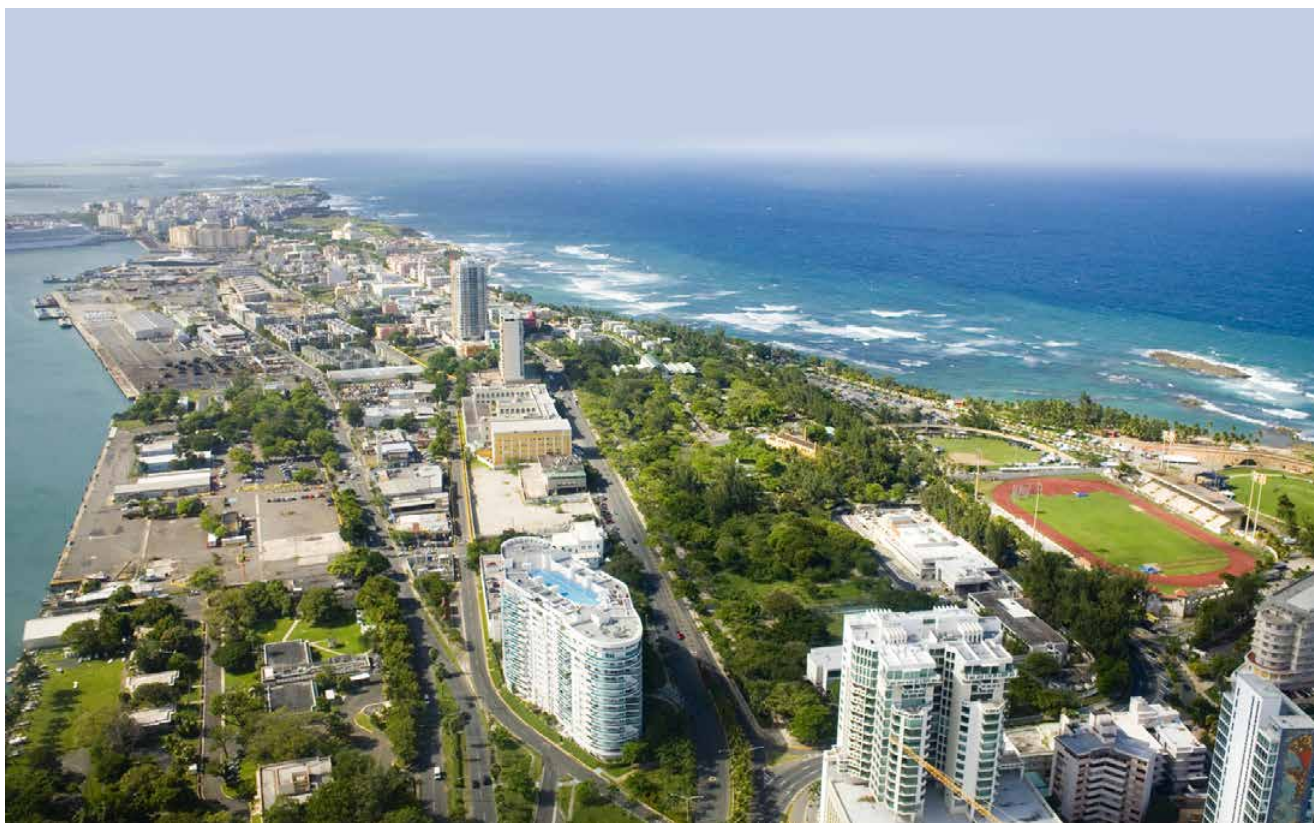
Pataki owns a home in the island’s municipality of Vieques and is

friends with various island governors, including Alejandro Garcia Padilla. Ana Matosantos, former California finance director who grew up in Puerto Rico, said the first and second sources.

The White House and Congress have been quietly conducting this search so the fiscal control board under the Puerto Rico Oversight, Management and Economic Sta-

bility Act (PROMESA or H.R. 5278) can hit the ground running, the first source close said.

“We are already working on day one of the control board,” the first source said. “I don’t think people realize that once PROMESA is enacted the board will be operational. It’s not going to be a question of 30 or 60 days.”



This source spent the last week meeting with various players on the island and reviewing potential office spaces for the control board. The House is scheduled to vote on the bill tomorrow, and board supporters hope President Barack Obama can pass the legislation before commonwealth's USD \$1.9 billion debt service payment July 1.

"Right now the most important thing is a stay [on litigation]," the source said.

The fiscal control board will head negotiations with creditors, as well as oversee a streamlining of commonwealth's operations. The fiscal control will not retain Cleary Gottlieb Steen & Hamilton or Millstein & Co. as advisors. As part of its

oversight of commonwealth's restructuring, the fiscal control board may hire chief restructuring officers to financially troubled public agencies, the first source said.

An official at Cleary declined to comment, while an official Millstein did not return requests for comment.

Heavy hitters and friendlies

The short list of potential candidates for Puerto Rico's control board contains a host of heavy hitters from the political arena and municipal market. Candidates also include people with prior knowledge of Puerto Ri-

co's fiscal problem and/or would be sympathetic to local residents and on-island creditors.

Among the heavy hitters is Kevyn Orr, partner at Jones Day and former emergency manager of Detroit, said a seventh and eighth source. Former Mayor of Washington, DC, Anthony Williams, special counsel at Dentons who also served as independent chief financial officer of the district, is also on the list, according to the second source close. As Detroit's emergency manager, Orr restructured city's USD \$18 billion in debt, which reduced overall debt by USD \$7 billion and implemented a multiyear USD \$1.7 billion revitalization plan for city services and operations. Under the restructuring, Orr streamlined city

operations and avoided drastic cuts to pension and related retiree benefits.

Williams was elected mayor of Washington, DC, after steering the district's fiscal control board and is credited with the city's financial comeback. During his two terms as mayor (1999 to 2007), Williams improved the performance of the district's government agencies, lowered taxes and invested in infrastructure and human services.

Other heavy hitters on the short list are New Mexico Governor Bill Richardson, said the seventh source close. Retired bankruptcy Judge Thomas Bennett, who oversaw USD \$4.2 billion bankruptcy case of Jefferson County in Alabama, and Ron Stack, head of public finance and managing director at Wells Fargo & Company, are also in consideration, according to the first source close.

Richardson is a power player in the Democratic National Party. Prior to his two terms as governor (2003–2011), he served as US Ambassador to the United Nations and Energy Secretary under President Clinton. He also served special envoy to the Organization of American States and as elected chairman of the DNC and the Democratic Governors' Association in 2004.

While not as widely known, Stack is a veteran of public finance. Prior to heading Wells Fargo's public

finance division, he also was head of public finance Barclays Capital and Lehman Brothers. He has more than two decades of experience in the public-finance arena. Stack has also chaired the Municipal Securities Rulemaking Board.

Under PROMESA, The Speaker of the House gets to submit six names, from which the President will pick two members. The Senate Majority Leader will submit four names, yielding another two selections. Lastly the House and Senate Minority leaders also submit lists of three names each, from which the President will select the last two members.

The President can pick outside the lists, but those selections would

require the consent of the Senate. It would allow the President to “pack” the board if the Democrats retake the Senate in the November elections, according to a June 3 Republican Study Committee bulletin on PROMESA.

The USD \$3.5 billion tranche of 2014 Series A general obligation bonds maturing in 2035 and issued at 93 and 8.727% yield last traded today in round lots at 65.75% and 12.853%, according to Electronic Municipal Market Access.

Chafey and Orr declined to comment, while spokespersons for the other potential candidates did not return requests for comment.



About the Author

Debtwire Latin America PLUS provides actionable intelligence on event-driven equity in addition to the distressed and high-yield markets in Latin America. With an on-the-ground team of journalists based in Sao Paulo, Buenos Aires and Mexico City, Debtwire Lat-Am PLUS closely tracks special situations throughout the LatAm market, providing real-time coverage of primary equity issuance and alerting subscribers early-on to restructuring events and key credit situations. Please visit www.debtwire.com.

Why Africa's Electronic Payments Market is Booming

 **Tom Stein, Privcap**

A successful exit
from electronic
payments company
Emerging Markets
Payments shows
profitable deals are
there to be found.

Sub-Saharan Africa skipped
landlines and went directly
to mobile phones, allowing
Africans to leapfrog into the digital
age. Now, the same thing is happen-



ing with commerce. Africans are skipping the checkbook and going straight into various forms of electronic payments.

And there is plenty of room for growth. Only about 20% of the African population has a bank account, according to a World Bank survey, and 98% of all transactions in Nigeria—Africa’s largest economy—are in cash, according to MasterCard Advisors.

“In a generation’s time people will still be talking about the growth opportunities in payments,” says Rick Phillips, a partner at London-based Actis Capital.

Another positive indicator is the continent’s youth; a third of all Africans are 14 years of age or younger. “So you have a strong secular drive of demand, apart from the ups and downs of the macro economy, GDP and oil prices,” Phillips says. “The next generation wants to have a phone, they want to be on the Internet, they want to be in the banking system. They don’t want to walk around with cash that can get stolen or lost.”

Rick Phillips, Actis Capital

In March, Actis, which invests heavily in financial services in Africa, sold electronic payments company Emerging Markets Payments (EMP) to payments-solutions con-

glomerate Network International for \$340 million, exiting its original investment of \$90 million.

The deal could serve a playbook for investing in electronic payments. From the start, it intended to create a payments platform that adheres to international standards and has sufficient scale and management talent to make it attractive to potential buyers. Actis built EMP’s continent-wide platform by acquiring

*“Mobile payments
are also a growth
story in Africa.
Kenya, for instance,
has one of the most
advanced mobile
payments systems on
the planet.”*

a number of regional companies. With its buy-and-build strategy, Actis constructed an electronic payments platform with the largest footprint in the region. It delivers services to more than 130 banks, 35,000 retailers, governments and consumer finance institutions

across 45 countries in the Middle East and Africa.

“The trick was not reading the market because we knew the demand would be there,” Phillips says. “The challenge was making a series of acquisitions and stitching together a business that had coherence across different geographies and payment disciplines.”

Of course, investing in the African payments space is not a slam dunk. “Challenges for private equity investment in Africa include negative perceptions about investing in Africa, an information gap about the opportunities available on the continent, regulatory constraints and a shortage of talent in this field,” according to a KPMG report.

What’s more, the value of private equity deals in Africa fell by 69% in 2015, to \$2.5 billion, according to the African Private Equity and Venture Capital Association, and some observers worry it will take years for Africa-focused funds to find a home for the money they’ve raised, given the relative scarcity of strong companies in which to invest.

Still, Phillips believes that the payments market in Africa has some very attractive characteristics. “You have high growth, secular demand, high margins, stickiness and resiliency to economic shocks,” he says. “For instance, in the middle of our venture, the Arab Spring

happened, but we still managed to grow through it all.”

Mobile payments are also a growth story in Africa. Kenya, for instance, has one of the most advanced mobile payments systems on the planet. For example, M-Pesa, the country’s largest mobile-network operator, boasts more than 19 million subscribers and processes about a quarter of Kenya’s gross national product. “So there are huge examples of the population leapfrogging ahead of where most western markets are,” Phillips says.

But he predicts it might be a few more years before the mobile-payments space becomes a true bonanza for private equity investors on the continent. “Many deals still lend themselves more to the venture cap-

ital market than to traditional private equity,” Phillips says. “That’s

because the assets themselves are not hugely high scale.”



About the Author

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MARKET ENTRY AND THE PITFALLS OF AFRICA'S POOR REGULATORY FRAMEWORKS

 **Chijioke Mama**

Across many markets in developing countries, compliance is often overseen by poorly developed institutions. This often constitutes a new learning curve for new entrants and investors, especially those coming from more mature markets. Africa in particular remains a major frontier of investment opportunities, holding six of the 13 fastest-growing economies in the world according to the World Bank.

However, one of the most conspicuous challenges of doing business in Africa is the poor state of infrastructure. Energy, efficient transport and basic amenities are grossly absent in many countries. But the pitfall of poor and faulty compliance frameworks and the risks that arise from it will arguably have the greatest impacts on business performance indices. From market stabilization for new entrants to growing market share and ultimately improving margins, the poor quality of regu-



latory systems can have measurable impacts. Despite this obvious risk, organizations have found it possible and sometimes easy to navigate and overcome these challenges. The keys lie squarely within an organization or investor's capacity to understand the nature of the problems, followed by applying carefully crafted strategies that reflect this deep understanding.

Managing a Continuing Flux

Despite the massive changes recently in the quality of governance and institutions across many African countries, the challenges of implementing consistent business policies and lowering political risks are still many. Often, nations looking to attract Foreign Direct Investment

(FDI) into different areas of competitive advantage (mainly natural resources) will develop long-term plans and programs for improving the ease of doing business.

However, one major challenge for investors is that the reforms/plans characteristically (and sadly too) may be too broad, in addition to having a slow pace and limited clarity. In Nigeria, power sector reforms have been ongoing for about 15 years now; this prolonged duration adds an additional layer of risk to the multibillion-dollar investment of many foreign and local investors. In spite of this, organizations that understood this made adequate provision for the continuing flux and have managed to report some good margins. Rigid organizational systems that work in more organized regions traditionally do not work in these

kinds of environments. Organizational hierarchy has to be haircut with decision-making quick and less rigorous to rebound with expected changes. In Nigeria, many international oil companies operating in the oil and gas industry adopt decision-making processes that often require active input from global headquarters, in cities such as London and Houston. This has side effects that can translate to more costs and greater exposures to risks. But those organizations (often smaller organizations) that reduce the pathway to final decision, as well localizing it through strategic empowerment of local staffs in leadership roles, have built more responsive decision-making systems. This enables them to adapt and respond quickly to internal and external environmental changes.

Rigorous Monitoring of Business Compliance Environment

Given that changes and reforms are likely to continue for too long in these markets, a viable strategy for investors is to create systems and mechanism that rigorously monitor the business environment. The level of details required is often ridiculous, if you juxtapose it with an organizational compliance-monitoring program in a similar-size project within a developed country. But this is the level of detail that works. In some cases conflicting and confusing guidelines may be arising from a single agency. Political interference may also see an excessive change in the leadership of an institution that directly interfaces with investors. For example, between 2010 and 2015, state-owned oil and gas company Nigerian National Petroleum Corporation (NNPC) had five Group Managing Directors (GMDs). In these kinds of settings, each change (sometimes in a matter of month's intervals) brings a new set of rules, depicting the absence of decision documentation and institutional memory. The flux, regulatory uncertainty and the consequent risks are very organic. They are often made worse by general political uncertainties, except in nations where political instabili-

ty and wanton regime changes have been long overcome.

The long-term nature of these uncertainties often combines to provide a risk pattern that is distinctly associated with each market in view. It is most challenging for new entrants and potential investors who are evaluating the market to make a Final Investment Decision (FID). In many cases, it altogether constitutes a deterrent to market entry. However, emerging markets by their very definition hold a lot of opportunities for foreign investors.

Foreign technical capacity and financial muscle often mean foreign investors have better chances than many local players, who may lack these two critical qualities required to successfully establish a business. This condition is the precursor to the now rampant market-entry strategy of floating a Joint Venture (JV) with a capable local partner. With proper due diligence, local businesses provide a very viable tool for new, foreign entrants to navigate market uncertainties. This is especially true in Africa where local laws may limit the allowable equity for foreign companies. Africa's abundant natural resources, infrastructural deficits and exploding population provide great opportunities for investors from mature markets—if they have proven capabilities in their choice sectors.

From power generation infrastructures to mass transport systems, mining, financial services, telecommuni-

cations and agribusiness, Africa holds massive opportunities for financially and technically capable investors who understand the uncertainties and are willing to monitor it rigorously.



About the Author

Chijioke Mama is a senior energy analyst, strategy consultant and syndicated columnist, one of the leading voices in Africa's energy and strategy discourse, with more than 40 research-based and investment-focused publications on strategy and energy matters in Sub-Saharan Africa. His analytical works are syndicated across top business publications in the UK, US and Africa with diverse advisory and consulting engagements for energy and infrastructure firms in these same regions.

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ECONOMIC ANALYSIS

Ten Emerging Markets Of The Future

Just as China, India, Brazil and Russia have become important markets for investors over the past two decades, many less-developed emerging markets will emerge as the next set of key investment hotspots over the next decade.

NEXT EM INVESTMENT HOT SPOTS - KEY FACTORS TO CONSIDER	
Criteria	Rationale
Large Domestic Market	A large domestic market implies strong growth opportunities for consumer industries. Moreover, large populations will provide significant opportunities for infrastructure and construction as urbanization rates rise.
Strong Enough Economic and Political Institutions	Stronger institutions are typically associated with better policymaking, the protection of property rights and reform, which help to underpin growth
Rapid Economic Growth	Countries that experience strong economic growth will provide strong investment opportunities and returns
Room for Infrastructure Investment	This suggests significant room for infrastructure-led productivity growth and, given the increasing reliance on PPP models of funding, provides investors with significant opportunities

KEY EMERGING MARKETS OF THE NEXT DECADE						
Per Capita GDP, USD				Nominal GDP, USDbn		
	2016f	2025f	Will Be Similar To*	2016f	2025f	Will Be Similar To*
Indonesia	3,570	7,848	China	861	2,213	India
Nigeria	2,514	4,577	Albania	470	1,069	Mexico
Philippines	3,019	6,347	Bulgaria	312	756	Netherlands
Bangladesh	1,337	3,242	Indonesia	218	581	Argentina
Egypt	3,535	5,724	Thailand	299	549	Taiwan
Vietnam	2,112	5,256	Thailand	199	525	Taiwan
Pakistan	1,384	2,201	Vietnam	267	500	Sweden
Myanmar	1,274	3,415	Indonesia	70	197	Portugal
Ethiopia	678	1,464	India	69	183	Greece
Kenya	1,346	2,863	Phillipines	65	170	New Zealand

Note: *In 2025, country x will be similar to how country y is in 2016. Source: BMI, f = BMI forecast

Source: BMI

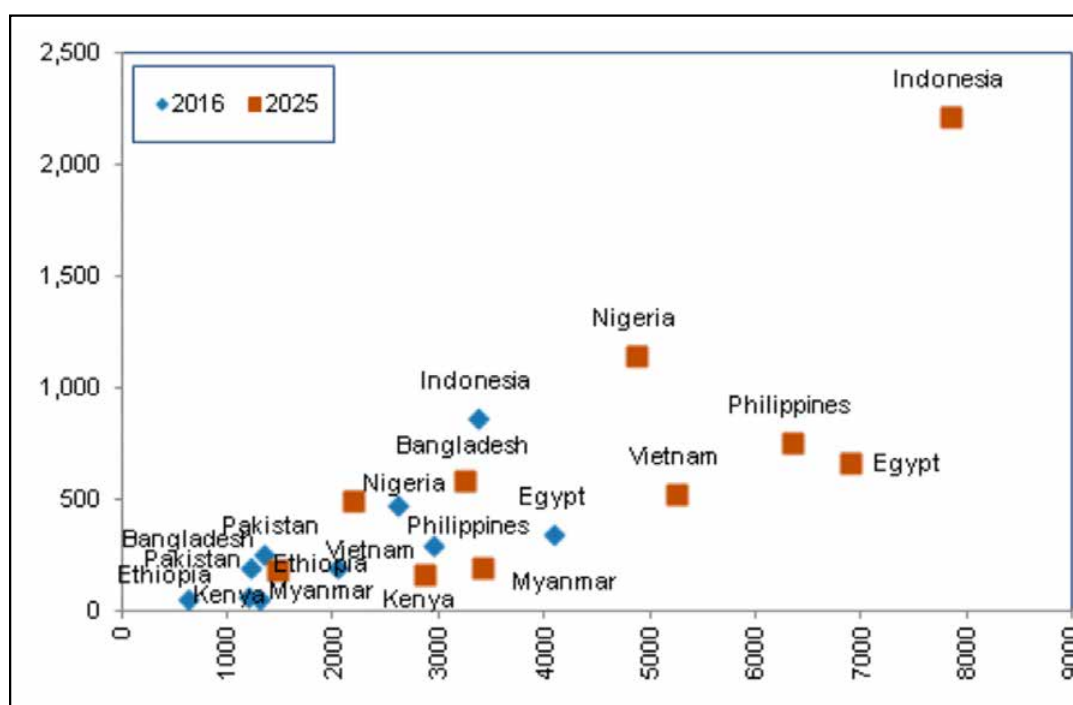
In order to shortlist these countries, we considered those with per capita income of about USD \$3,500 and below that enjoy strong enough economic and political institutions to enact reforms, are

set to enjoy rapid economic growth, boast a potentially large domestic market and have an infrastructure deficit that will lead to productivity-enhancing investment.

The preceding 10 countries have the potential to transition into key emerging markets and will cumulatively add USD \$4.3 trillion to global GDP (roughly the equivalent of Japan's economy) by 2025, pro-

Huge Potential Ahead

GDP Per Capita (USD, horizontal axis) vs. Nominal GDP (USD billion, vertical axis)



viding significant opportunities for investors. Six of the 10 are found in Asia, which chimes well with our house view that Asia will remain one of the fastest-growing regions globally, driven in large part by the performance of the less-developed emerging markets as well as various frontier markets. We also identify opportunities in Africa and the Middle East given strong demographic trends and improved macroeconomic fundamentals for some countries in these regions. The criteria of a country having a per capita income of about USD \$3,500

and below means that several large emerging markets in Europe and Latin America are excluded from the list.

Asia: Indonesia, Philippines, Vietnam, Bangladesh, Pakistan And Myanmar Stand Out

Indonesia: This is Asia's sixth largest economy and boasts the world's fourth-largest population of almost 260 million people. Given that its per capita GDP is only about USD \$3,500 suggests significant room for growth as well as the develop-

ment of a large internal market for investors to benefit from. Although the Indonesian economy has underperformed its potential in the past few years, we believe it is starting to turn a corner and will see growth accelerate over the coming five to 10 years underpinned by greater government-led infrastructure investment, an improvement to the business environment, rising foreign direct investment and greater macroeconomic stability. We forecast real GDP growth to average 6.0% annually over the next decade, which will raise the country's GDP per capita

Rising Importance Globally Indonesia: Share of Global GDP, %



from USD \$3,570 to USD \$7,848, which is roughly China's current level. In terms of market size, these growth rates imply that Indonesia's nominal GDP will almost triple over the next 10 years to reach USD \$2.2 trillion, which is similar to the current size of India's economy.

The biggest risk to this bullish view is the ability for the country's leaders to maintain current economic reform momentum. We expect Joko Widodo's current government to deliver significant results on reform across the economy to boost productivity and rising incomes, and we caution that any stagnation of

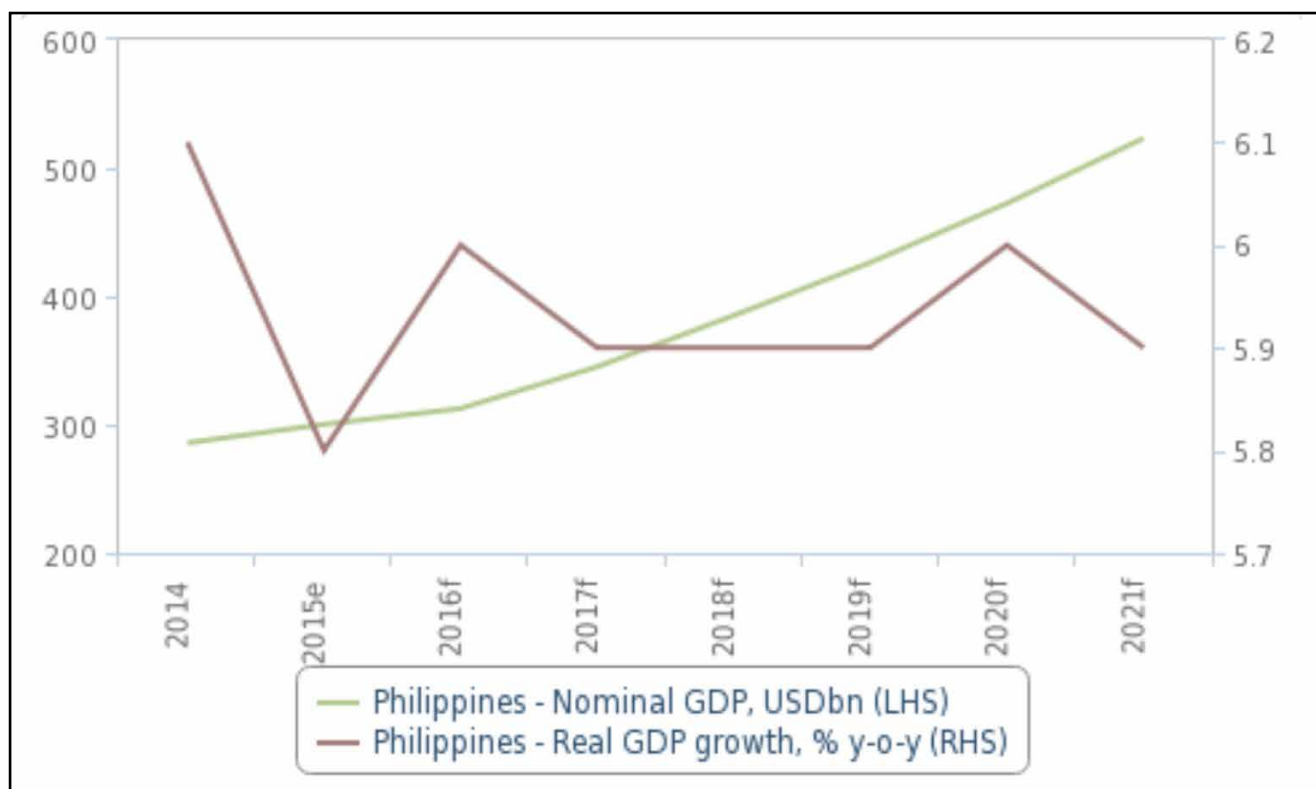
reforms could deal a blow to investor sentiment and hence growth.

Philippines: The economy has seen a huge improvement in its macro-economic fundamentals in the past six years, and we forecast average annual growth of 5.8% over the next decade. This means the economy will more than double in size from USD \$312 billion in 2016 to USD \$756 billion by 2025, which is similar to the current size of the Netherlands. On a per capita basis, GDP will more than double from about USD \$3,000 in 2016 to USD \$6,347 over the next decade, which is similar to the level seen in Bul-

garia currently. The Philippines has the world's 12th largest population of 101 million and benefits from strong remittance flows from expatriate workers, forming the foundation of a large domestic market. Given these dynamics, we believe that the Philippines will become an increasingly important market for investors.

The main risk to this view is once again policy continuity. President-elect Rodrigo Duterte poses some risks to policy continuity and has not yet revealed a comprehensive economic plan. Any large deviation from the prudent and

Fast Growth Ahead Philippines: Real GDP Growth, %



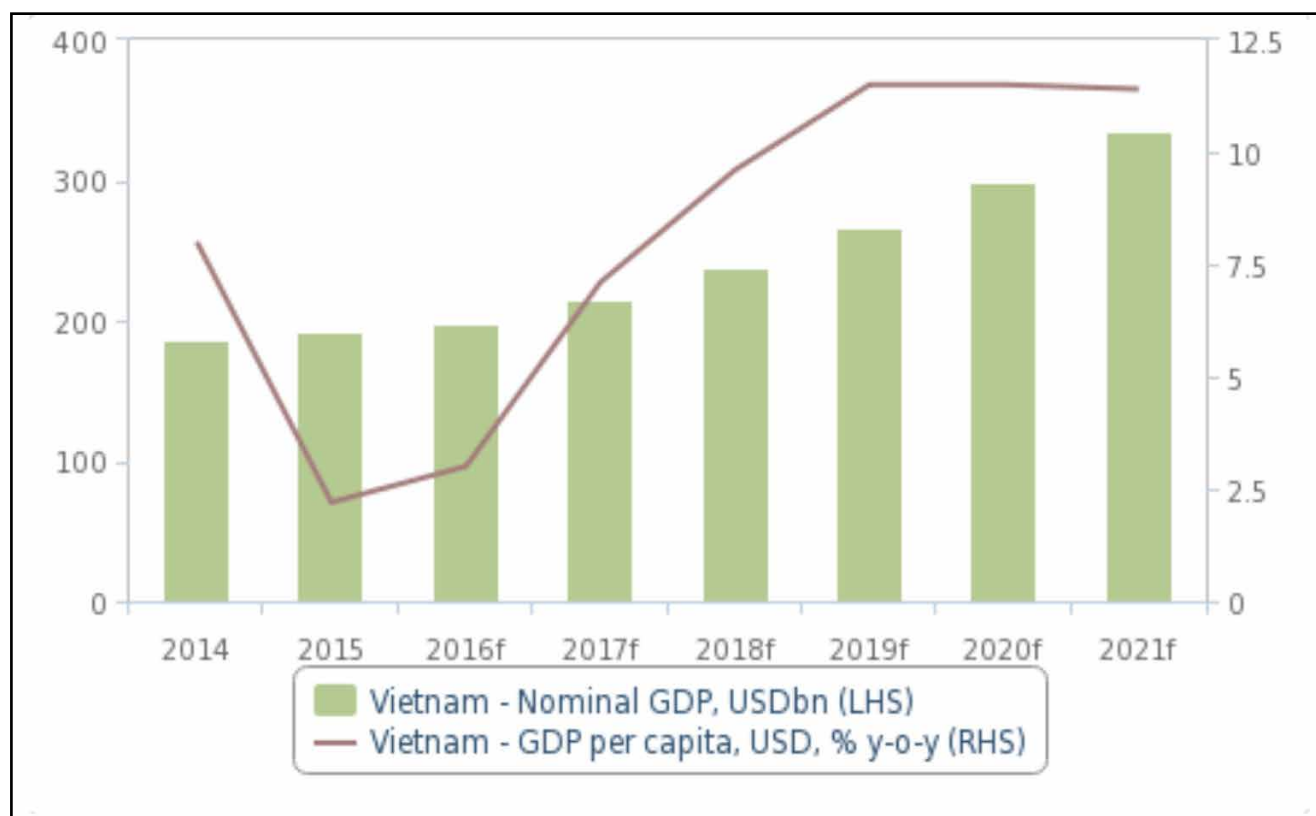
business-friendly macroeconomic policies of the outgoing Aquino administration could pose risks to investment into the Philippines, as well as domestic business confidence, which would weigh on growth.

Vietnam: This is one of the shining economic stars of Asia and will see real GDP expand by an average of 6.2% per annum over the next decade. As a result, GDP per capita will rise from USD \$2,100 to USD \$5,300 (similar to that of Thailand today), and the total size of the economy will grow by 160% to US \$525 billion by 2026, which is sim-

ilar to the current size of Taiwan's economy. With a population of close to 100 million, this means that there will be a significant domestic market developing over the coming years. Underpinning this strong performance is a combination of a continuously improving business environment and regulatory framework (which has led to a surge in investment into the manufacturing sector), political stability and policy continuity, as well as an increasingly diversified economy in terms of output and trade. Given these dynamics, we believe that Vietnam will progressively become a more important market within ASEAN.

There are two key risks to this positive story. First, although the Communist Party has substantial support and has generally been able to deliver on economic growth, social pressures continue to build within the country. Should these growing calls for increased participation be ignored, it could result in a rise in political risk. Second, Vietnam and China remain in dispute over territorial issues around the South China Sea. Although we believe that a military escalation is unlikely, further discord between the two countries could result in political and economic risk, given China's dominant position in the region.

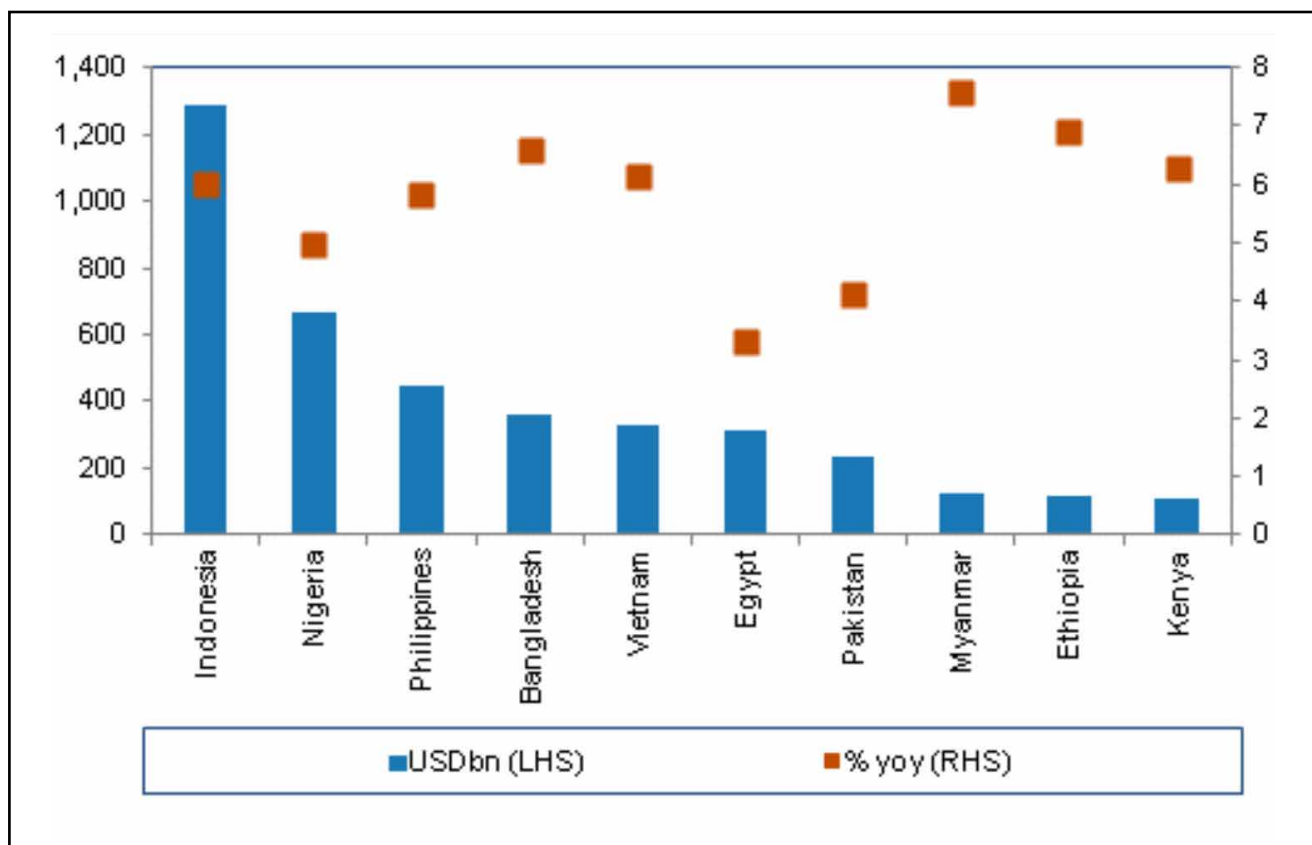
Catching Up Again Vietnam: Per Capita GDP Growth, % & GDP, USD billion



General Statistics Office/Asian Development Bank

Indonesia Stands Out

Select Countries: Increase In Nominal GDP Over 2016–2025, USD billion & Average Annual Real Growth (RHS)



Source: BMI, National Sources

Bangladesh: The country has seen a significant improvement in its political risk profile since the street protests that crippled the economy in 2015. At the same time, the macroeconomic outlook is also improving with strong remittances and a robust manufacturing sector boosting external earnings, while the government has embarked on a strong infrastructure investment drive to help boost productivity. Given these positive dynamics, we forecast that Bangladesh's economy will grow by an average of 6.6% per annum over the next decade,

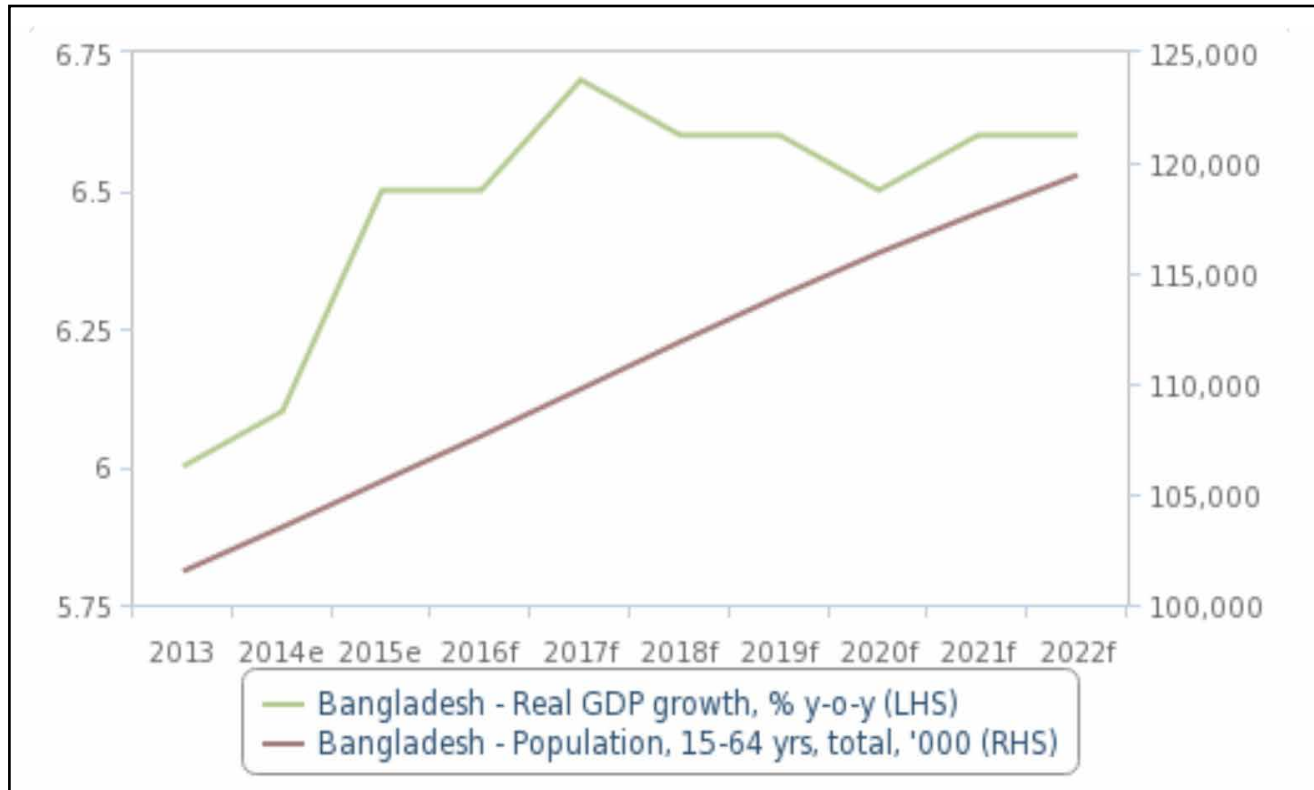
which will see GDP per capita rise by 142% to USD \$3,242, putting it on a similar level to Indonesia today. Given the large population of over 160 million people, this means that Bangladesh's economy will grow by about 170% over the decade to USD \$580 billion, which is roughly the size of Argentina today, presenting significant opportunities for consumer goods, manufacturing and infrastructure investors.

There are two key risks for Bangladesh. The first is the ongoing security threat, which has seen a rise of

Islamist violence and religiously motivated killings. Second, Bangladesh's banking sector remains very weak and underdeveloped, and a failure to implement reforms could weigh on the development of the domestic market.

Demographics A Tailwind

Bangladesh: Population & GDP Indicators



National Sources/BMI

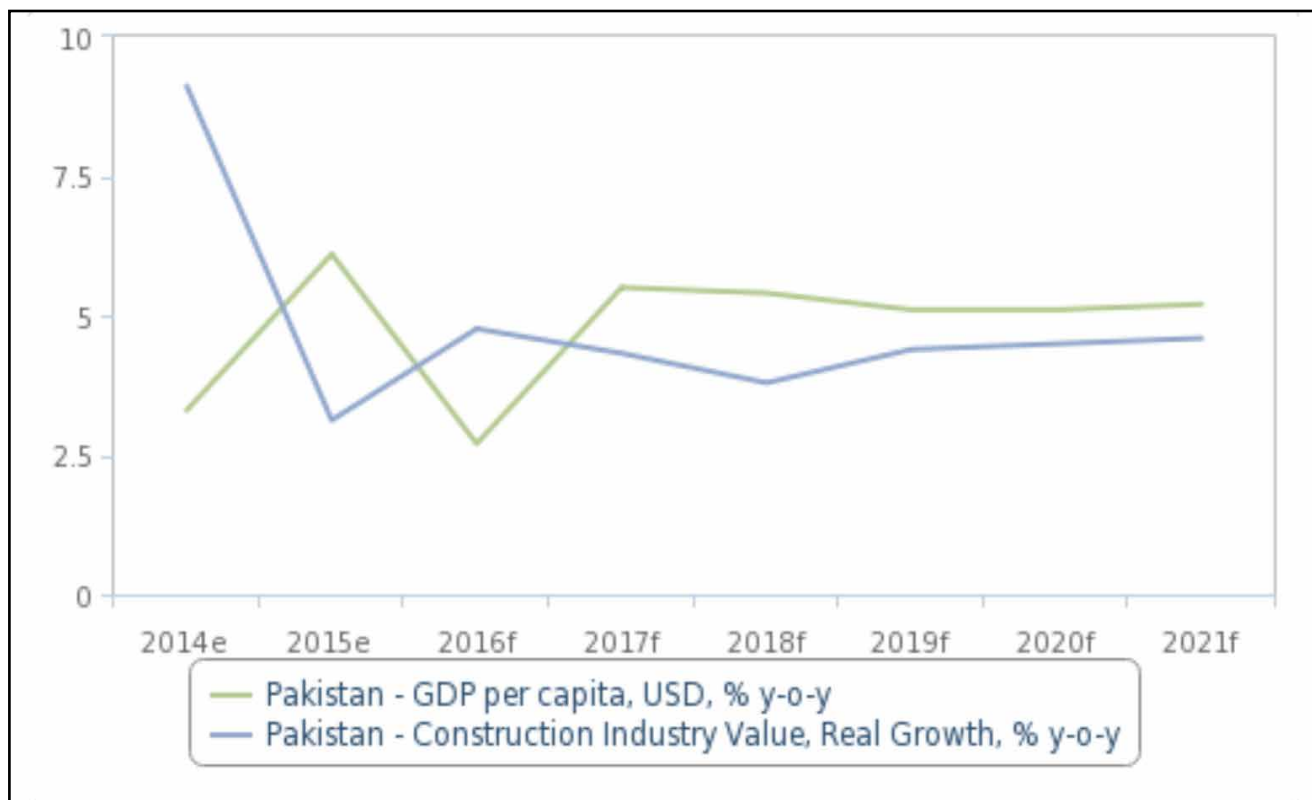
Pakistan: The country has the world's sixth-largest population of 190 million people and, as such, could become a very important market for international companies looking to access a large and relatively young consumer base. A number of favorable domestic and internal dynamics, including improved energy supply, strong remittances and an improving manufacturing outlook, should support real GDP growth in Pakistan over the coming years, and we forecast real GDP growth to average 4.1% over the next decade. While our growth forecasts are relatively conservative compared with the government and the IMF's expectations, the

successful implementation of the China-Pakistan Economic Corridor (CPEC) would have the potential to propel growth above 5.0% over the coming years. Although growth rates in Pakistan are relatively low given the country's level of economic development, the market potential is still large. Over the next decade, we forecast GDP per capita to rise by almost 70% to USD \$2,201 (similar to Vietnam today) and for its economy to almost double to USD \$500 billion, which is the same size as Sweden's economy today. Given that our estimates are conservative, we believe that the risks are to the upside for Pakistan, particularly if the country can suc-

cessfully address its long-standing security situation, pervasive energy shortages and a very low savings rate.

Huge Opportunities Ahead If Policy Improves

Pakistan: Key Economic & Sector Indicators



BMI/Pakistan Bureau of Statistics

Myanmar: The country will achieve the fastest average growth rate (7.6% real GDP growth per annum) in Asia over the next decade as the country continues to open up. This will take GDP per capita from USD \$1,274 to USD \$3,415 by 2026, a similar level to what Indonesia enjoys currently. Given the relatively large population of 54 million, this means that the economy will almost triple in size to USD \$200 billion, which is the current size of Bangladesh's economy. Myanmar's economy has a lot of catching up to do given its low level of economic development, high levels of inequality and large agrarian sector, which accounts for almost 35% of GDP.

As such, we expect a significant economic transformation over the next decade whereby the secondary and tertiary sectors of the economy will develop rapidly, potentially giving rise to huge opportunities in the manufacturing, construction and service sectors of the economy.

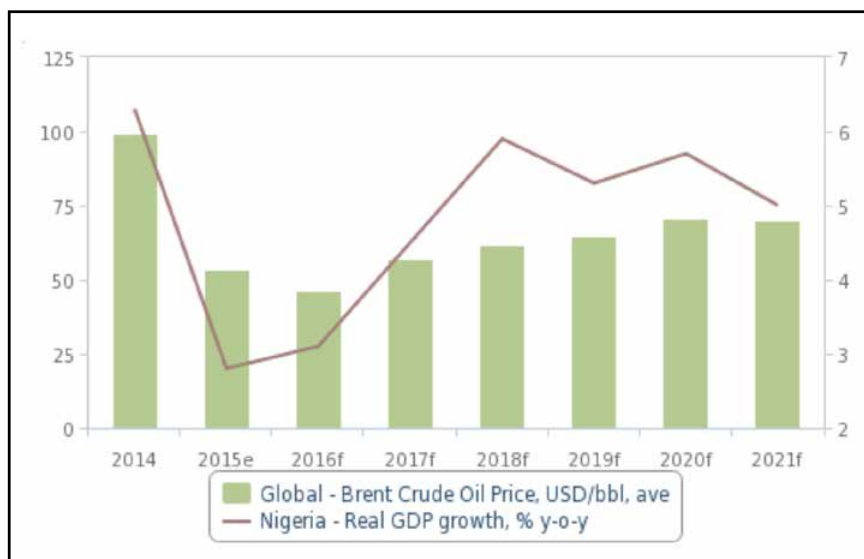
Although there are key political risks related to the country's nascent democratic transition, a significant number of reforms were initiated under the military government, which means that even if there is a risk to the country's fragile democratic institutions, we believe that economic reforms will be sustained given the broad consensus on how

the economy needs to evolve. That said, any weakening of the political institutions or the flaring up of ethnic tensions could weigh on investor sentiment. Moreover, many of the country's largest businesses are connected to military officials, which could pose a risk to the rise of competitive forces within the economy and may present conflicts of interest with regard to some economic reform goals.

Africa: Nigeria, Ethiopia & Kenya Will Continue To Emerge As Important Markets

Nigeria: Growth will be weak in 2016. We forecast a 3.1% expansion

Suffering From Oil Short-Term Nigeria: Economic & Commodity Indicators



National Sources/BMI

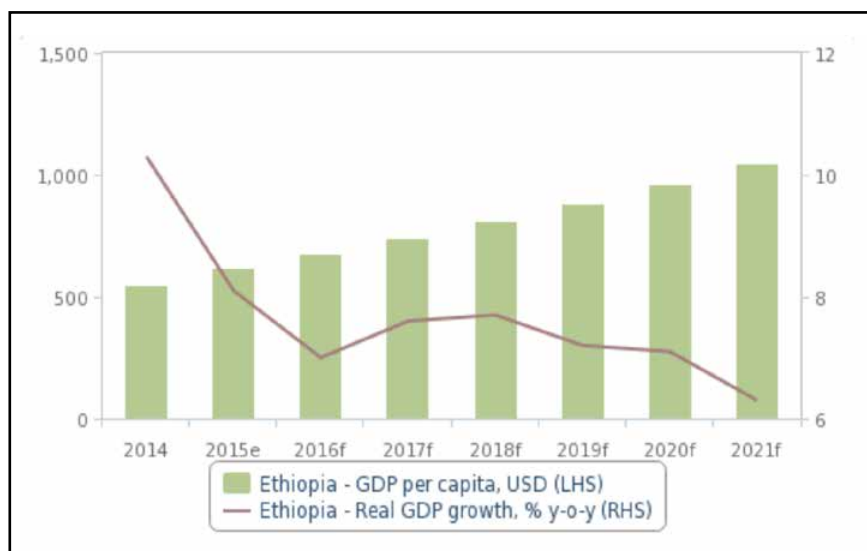
sion, as the naira peg and capital controls will continue to weigh on economic activity through the course of the year, exacerbating the global oil price slump's effects on the economy. However, from a longer-term perspective, we forecast average annual real GDP growth of 5.0% for Nigeria, which will see per capita incomes rise from USD \$2,517 in 2016 to USD \$4,577, putting it on a par with a country like Albania. More impressive, however, is the fact that the Nigerian economy will extend its lead as Africa's largest economy by more than doubling in size to USD \$1.07 trillion, similar to the size of Mexico's economy today. President Muhammadu Buhari's impressive victory in 2015 provides him and his All Progressives Congress (APC) with a strong platform from which to implement his ambitious reform agen-

da. Using its commanding majority in both the upper and lower houses of Nigeria's bicameral National Assembly we expect government to

make progress on areas such as petroleum industry reform, boosting fiscal accountability and reforming the power sector. Such reforms are critical if Nigeria is to have any hope of overcoming the major structural challenges it faces, namely an overreliance on oil exports a dearth of productive capacity and to help transform the economy from an elite-driven consumption model to one driven by investment and more broad-based consumption.

Ethiopia: By far the poorest of the countries mentioned in this list, Ethiopia nonetheless has experienced impressive and relatively broad-based economic growth over the past 10 years, growing at a rate of around 10.3% on average, and we believe that the economy will continue to post strong growth

Rising From A Very Low Base Ethiopia: GDP Per Capita & Real GDP Growth, %



BMI/Ministry of Finance and Economic Development

in the years ahead. Although still robust by regional standards, we believe that real GDP growth in Ethiopia will moderate, and we are forecasting average growth of 6.9% between 2016 and 2025. Ethiopia's economic trajectory will continue to be largely shaped by the state-led model that has been responsible for a decade of spectacular growth. This has been characterized by heavy public investment into priority sectors such as infrastructure, agriculture and manufacturing, as well as accompanying measures aimed at boosting human development. GDP per capita will rise from a very low USD \$678 in 2016 to USD \$1,464 by 2025, which given the large population of 99 million translates to GDP of USD \$183 billion over the next decade and will see the economy reach the size of that of Greece currently.

The government's involvement in regional counterterrorism efforts will increase the risk of retaliation from Somali-based wings of militant groups such as al-Shabaab and Islamic State. However, we do not anticipate this will have a significant negative impact on Ethiopia's economic development, with any new attacks likely

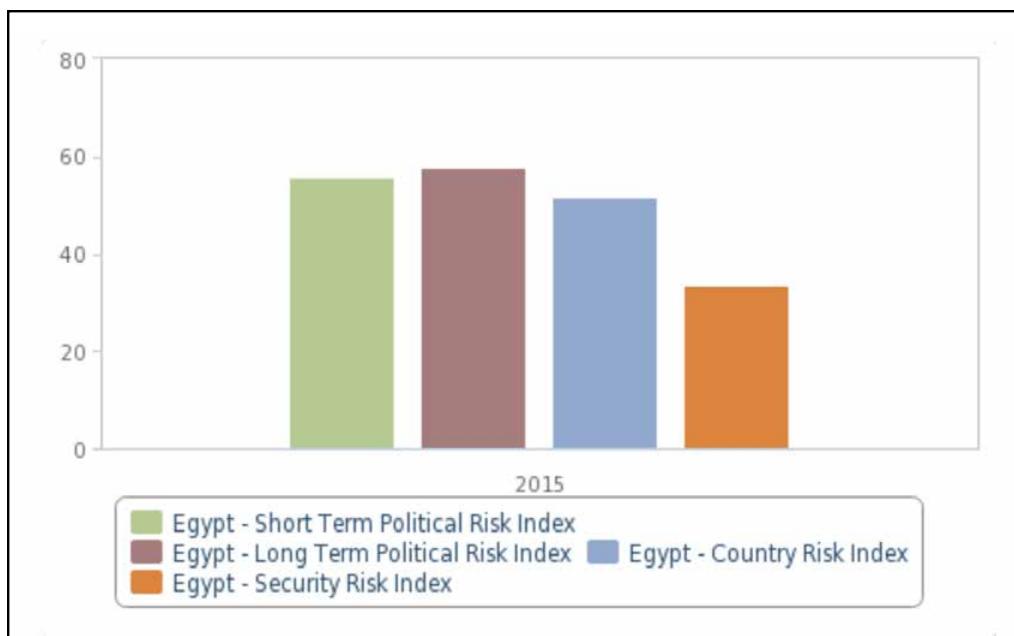
to occur in the more rural regions of the country.

Kenya: The economy will expand robustly in the coming decade, and increasing access to technological and financial services will ensure Kenya remains among Sub-Saharan Africa's most dynamic and innovative markets. The Kenyan economy is set to strengthen in the coming decade, largely due to infrastructure investment and services growth. We currently forecast annual real GDP growth to average 6.3% between 2016 and 2025, a step higher than the 5.2% average growth seen between 2006 and 2015. A pipeline of major infrastructure projects will significantly improve the country's logistical networks, allowing the

economy to solidify its position as the region's economic hub. The strong economic performance will see GDP per capita more than double from USD \$1,346 in 2016 to USD \$2,863 over the next decade, putting it on a par with the Philippines today and, given the sizeable population of 46 million people, will see a near-tripling of GDP from USD \$65 billion to USD \$170 billion over the same period, making it the same size as New Zealand currently.

Despite the strong growth rates, politics will pose the biggest risk to the country's long-term economic growth as the country's fight against the al-Shabaab militant group in Somalia weighs on eco-

Much Hinges On Political Stability Egypt: BMI Political Risk Index



BMI



conomic activity in the north and high levels of corruption weigh on fiscal revenues.

Middle East: Egypt & Morocco Will Provide Opportunities

Egypt: The country will be one of the Middle East's outperformers over the next decade. Pent-up demand through four years of political turmoil, a growing population and rising productivity all bode well for long-term growth. We expect to see the Egyptian economy continuing to modernize, with the private sec-

tor taking an increasingly dominant role and foreign direct investment (FDI) continuing to flow in accordingly. In addition, the longer-term growth picture is bolstered by a huge increase in gas exports (and decrease in imports) from development of Zohr gas field, the largest gas field in the Mediterranean. Given the size of the economy and population, this means that Egypt will still offer significant opportunities for investors. GDP per capita will rise from USD \$3,535 in 2016 to USD \$5,724 over the next decade (an increase restrained by rapid population growth), reaching a level similar to that of Thailand today and will add USD \$150 billion to GDP to reach USD \$550 billion, which is roughly the same size as Taiwan's economy currently.

Given some of the structural constraints currently in place, which include continued political uncertainty, high unemployment and rising levels of sovereign risk, we forecast that Egypt's economy will struggle over the next few years, before potentially picking up, and we forecast real GDP growth to average 3.3% over the next decade, which pales in comparison to that of other emerging markets.

Reform Risks And Other Countries To Consider

Although we believe that these economies could become increas-

REAL GDP GROWTH %											
Country	10 Year Av	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Myanmar	7.6	8.0	7.8	7.8	7.5	7.7	7.5	7.6	7.2	7.3	7.3
Ethiopia	6.9	7.0	7.6	7.7	7.2	7.1	6.3	6.4	6.4	6.5	6.7
Bangladesh	6.6	6.5	6.7	6.6	6.6	6.5	6.6	6.6	6.6	6.6	6.6
Kenya	6.3	6.2	5.8	6.3	6.5	6.2	6.5	6.4	6.4	6.4	6.3
Vietnam	6.2	6.3	6.4	6.4	6.3	6.2	6.2	6.0	5.9	5.9	5.9
Indonesia	6.0	5.2	6.0	6.1	6.1	6.1	6.1	6.1	6.1	6.1	6.1
Philippines	5.8	6.0	5.9	5.9	5.9	6.0	5.9	5.8	5.7	5.6	5.7
Nigeria	5.0	3.1	4.5	5.9	5.3	5.7	5.0	5.0	5.2	5.0	5.0
Pakistan	4.1	4.3	4.2	4.1	4.1	4.1	4.1	4.1	4.1	4.1	4.1
Morocco	3.7	2.0	3.3	3.8	3.8	3.9	3.9	4.0	3.9	4.0	4.0
Egypt	3.3	2.6	3.2	3.3	3.3	3.3	3.8	3.6	3.4	3.3	3.2

ingly important markets over the coming decade, there are many risks as highlighted above. Reform momentum aimed at encouraging greater private sector participation and investment, diversification of the economy as well as a continued focus on the improving both the macroeconomic fundamentals business environment will be crucial to unlocking growth in these economies.

Moreover, there are other economies, which were very close to making the list of the top 10 economies that could become important markets over the next decade for investors. These include Morocco and Tanzania, both of which will benefit from strong demographic tailwinds, reasonably strong growth and an improving business environment.

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About the Author

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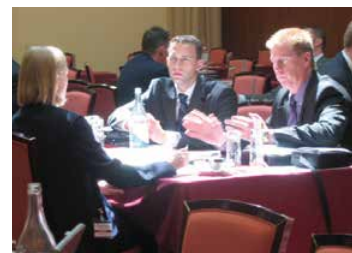
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