Market Intelligence

September 2011

Shift in Power

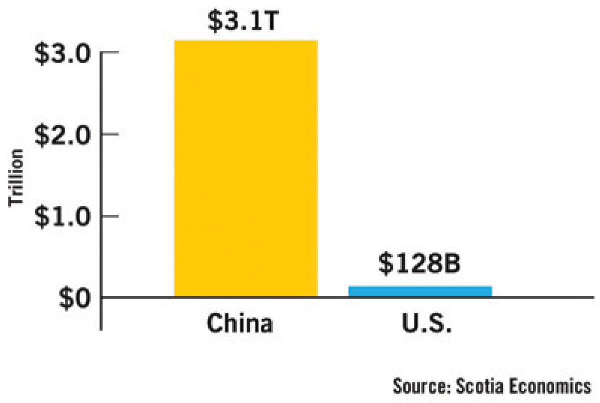
By Kevin Dehod
Vice President & Portfolio Manager

As the United States and Europe struggle with anaemic economic growth and a future of fiscal austerity, where can investors find sustainable economic growth and improving government balance sheets?

Emerging market economies are only emerging by name, and given the crisis evolving in most developed market economies, their economic dominance and political power will only increase. These are nations with a dominant and growing consumer class, powerful demographic trends and governments that in most cases have proven to be fiscally responsible, and have now amassed tremendous foreign exchange reserves. Emerging economies should now be considered GPP's or "global power players."

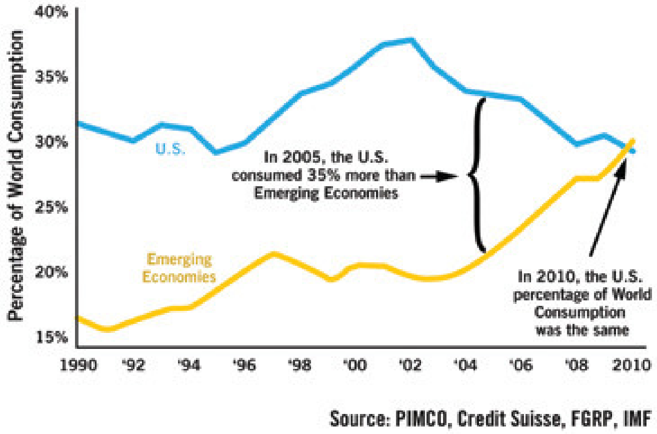
According to the International Monetary Fund (IMF), foreign exchange reserves held by developed countries were $3.16 trillion at the end of the first quarter of this year. By comparison, the GPP held $6.53 trillion in global currency reserves. As you can see from Figure 1, China by itself has over $3 trillion in foreign currency reserves vs. $128 billion for the United States. Recently, Moody's upgraded the credit rating of Brazil to Baa2 from Baa3 and both Moody's and Standard & Poor's assign a "positive" outlook on Brazil's sovereign credit rating. This is in sharp contrast to recent events in the United States and Europe. While emerging nations account for 46 per cent of world retail sales, 52 percent of all motor vehicles purchased, and consume 55 per cent of the world's oil output, they are only responsible for 17 percent of all the outstanding government debt.

FIGURE 1: Global Foreign Exchange Holdings Chart



From a consumption perspective there are a number of shifts occurring on the global economic stage. As Figure 2 shows, in 2010 the emerging economies percentage of world consumption matched that of the United States and has made up significant ground since 2002. Going forward with China and India alone having 1.4 billion middle-class consumers by 2020, this trend of accelerating global consumption remains very strong.

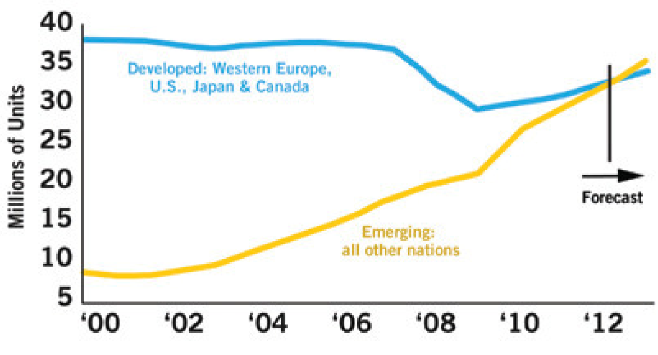
FIGURE 2: Percent of World Consumption – U.S. vs. Emerging Economies



With regard to the oil industry, the continued economic dominance of the emerging nations should be supportive of oil demand going forward. The factors that drive the oil price on a day-to-day basis have changed a lot in the last 10 years. It used to be fundamentals (supply and demand) and a small premium for country and or political risk. Today, fundamentals still matter and they always matter in the long term. However, in the short term, speculative commodity investors and political/country risk factors have taken on a much bigger role with regard to the short-term movements in oil prices.

Another area related to oil demand where a shift is occurring relates to global auto sales. By 2013, emerging nations will buy more new cars annually than developed nations. Later this decade, Brazil is forecast to become the world's third-largest car market, overtaking Germany. From a demographic perspective, the Brazilian population under 35 years of age is four times greater then Germany's. Industry estimates suggest that China alone will purchase 25 million cars a year by 2020. So over the long term, the demand for Canada's oil reserves based on the consumption trends of the emerging nations looks pretty solid. Just be prepared for the speculators to create tremendous amounts of volatility in the oil price over the short term.

FIGURE 3: Emerging Nations' Car Sales Set to Surpass Developed Countries by 2013



Source: Scotia Economics

The power shift that has occurred between the emerging and developing nations has numerous investment implications when it comes to building your portfolio for the future. The fundamentals argue that the gap will continue to grow on a number of fronts between the new global power players and the mature economies. Fundamentals also indicate that the perceived risks of investing in emerging nations may be much less than developed nations, given the more sustainable growth outlook and better financial position with regard to government debt and fiscal austerity.

If you would like to discuss how to incorporate the Emerging Markets into your portfolio, please call us at (403) 234-6103. Our Portfolio Managers are here to act as a sounding board at any time.

McLean & Partners
WEALTH MANAGEMENT

801 10th Avenue SW Calgary, Alberta T2R 0B4

Phone: (403) 234-0005 Toll Free: (888) 665-0005 Email: solutions@mcleanpartners.com Web: www.mcleanpartners.com