Disruption Week 2024 Misunderstood markets and emerging opportunities

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From semiconductors enabling AI to raw materials making renewables possible, hunger-inducing hotpots to branchless banks, investment manager Ben Durrant reveals some of the companies with great growth potential that have caught his eye in this Disruption Week discussion.

Your capital is at risk.

Leo Kelion (LK): 14 years ago, TSMC's founder, Morris Chang, invited Apple's Jeff Williams to his Taiwan home for dinner. Chang was already legendary in semiconductors for pioneering foundries, in which TSMC solely manufactures other companies' chip designs, rather than its own.

Even so, the plan the two cooked up that night was high-risk for both parties. Apple shifted all production of its iPhone and iPad chips to TSMC, and TSMC committed $9bn and 6,000 workers to get the required factory up and running in a record 11 months.

As Williams later commented, there was no fallback, and the execution was flawless. The achievement burnished TSMC's reputation, helping it become one of the world's 10 most valuable listed firms. And it proved that an emerging market company can be best in class.

Today, I'll be speaking to investment manager, Ben Durrant. He'll discuss other high-calibre emerging market firms and reveal why now is the time to reconsider the asset class. Welcome to Disruption Week.

New horizons of growth

Hello and welcome. This webinar is about 45 minutes, and we'll take questions from you, the audience, during the last 15. We'd love to hear what you want to know, so, please, use the Ask a Question tab on your screen to send your requests.

Ben, thanks for joining me. Great to have you with us.

Ben Durrant (BD): Hi, Leo.

LK: It's probably a good idea to start with some definitions. So, when you're considering emerging markets, which countries qualify?

BD: Of course. So the big ones are China, India and Brazil, but you also have places like South Korea and Taiwan, which, while smaller and more advanced, also qualify because they are less easy to access for investors.

Really, you can think about it from, at least a Western investor's perspective, as anything outwith the mainstream, but still important. Or it's the potential that really matters, and so you should be invested in that.

There are third-party classifiers, such as MSCI or FTSE, which create indices that many clients look at, but these are quite basic and rules-based in some ways. We think about it more philosophically sometimes because there are countries that don't technically fall into those indices, but we think, have tremendous potential, such as Vietnam, for example.

LK: So, large parts of Latin America, Asia, but you don't focus much on Africa, is that right?

BD: No. So, about 80 per cent of emerging markets come from Asia, and then you've got another 10 per cent from Latin America and from the Middle East and a select part of Africa, such as South Africa and Egypt. But sadly, much of the rest of Africa isn't yet at that economically developed stage for foreign capital to make a return there.

LK: And the Emerging Markets team invest in frontier markets. Can you just explain what they are?

BD: Yes, selectively, as part of our emerging markets and Asian strategies, we do. Frontier markets are the next tier down. So, you've got developed, emerging and then frontier, which are even more difficult to access. And many of those, we don't think, have those kind of attractive traits.

That alignment of long-term economic growth with shareholder returns. [There are] a couple of exceptions, as I mentioned, [like] Vietnam and also a couple of places like Kazakhstan as well. We do invest [here], but selectively.

LK: So, I imagine there'll be some in our audience who question the appeal of emerging markets. As an asset class, it's disappointed over recent years. So, why should the future be different?

BD: Yes, it's intriguing in a way because you should expect these highest-growth parts of the world to deliver you the highest returns, and that has been the promise for emerging markets. If you were to look back over the 30-odd-year history, you've had that, but over the last decade, you haven't.

And that's intriguing because you ask yourself why, because you have seen GDP growth, but you haven't seen shareholder returns. And so, the question is, is that going to continue in future? And there are plenty of reasons for optimism, which we can go into.

There's also some sources of concern that many people raise, but fundamentally, when we look at the companies that we're investing in, look at the strength of the companies and the valuation starting points we're being asked to pay for them, then I think, actually, we're in a very good place here. It's almost because of that pain, that patience that people have had to endure over the last decade, that does set you up well for the future.

LK: So, am I right to think, then, that the case for emerging markets isn't just that there's an increasing number of high-calibre companies there, but also that macroeconomic factors are lining up in their favour?

BD: Exactly. So, you've got valuations, [which] we talked about. Then you've got macro resilience, and then you've got growth, both from the big-picture side of things, but also just great-quality companies that are essential for global progress.

LK: Okay, that gives us lots to talk about. Let's start with valuations. What's the evidence that emerging market stocks are excessively undervalued, compared to those in the US and other developed markets?

BD: Yes, sure. Maybe we just start with the real basics? There are two very strong factors for predicting returns going forward. The first is growth. If a company or a sector delivers strong growth, you're far more likely to outperform.

And the second is valuations. If you're cheap at the start, again, statistically speaking, you're more likely to outperform. If you look at emerging markets, relative to developed markets, and especially the US, there are historic discounts there. The US is on about 37 times cyclically adjusted earnings, which is at 1999 or 1929 levels of valuations and optimism there.

There [are] reasons for that, perhaps, but it's certainly more demanding. By contrast, emerging markets are on about 12 times earnings, so one-third of that. So, all else being equal, you should expect, emerging markets [to] deliver three [times] the kind of returns that you'd be getting from developed markets there.

We don't expect those valuation disparities to close altogether, but it's certainly a much more comfortable starting point. You can think about it from a growth perspective as well.

Over the last decade, [in] the US, for every unit of GDP growth, you've had five units of shareholder return growth, which, of course, is great if you can get it, right? But by contrast, in EM, say, China, for every unit of GDP growth, you only have 0.3 of stock market growth.

LK: And by EM, emerging markets?

BD: Yes. And so, when we're looking at this, we're saying, okay, does that economic progress ever come back to shareholders? And we think it does.

LK: Okay. When you look at your portfolios, are there standout examples then, of companies where you think the markets are really underappreciating their value at present?

BD: Yes, sure. So, I suppose, when we look at our portfolio, we think everything's too cheap because otherwise, we wouldn't own it, really. And remember, we're growth investors, so typically speaking, we're prepared to pay up for quality, pay up for future prospects.

So, many of our companies wouldn't tend to look, optically, cheap in today's terms. We think the future more than compensates for that. But even so, businesses like Sea Limited [which] owns Shopee and Garena Free Fire, the games business (so an ecommerce business in Southeast Asia and Brazil), that business has grown revenue about 15-fold over the last five/six years. And yet it's still at big discounts from its previous market caps two/three years ago.

And so, you've seen tremendous operational progress, but you've not seen that being rewarded in today's share price. We think that's just too cheap, and we think the prospects of that are better than they were in the past, as well. Another example that people will be familiar with is TSMC.

So, this powers practically every leading-edge bit of electronics manufactured today, and it is behind much of the progress of AI as well. It manufactures Nvidia's logic chips, for example, and anything else you may consider really important, yet it is on valuations literally an order of magnitude lower than its customers, the NVIDIAs, the Apples of the world.

And again, we think that it's arguably more important than them. So again, just too cheap there. And maybe finally, and it speaks to the breadth of the kind of things we invest in, a Mexican Bank, Banco Banorte. That's paying a 10 per cent dividend yield, 12 per cent more recently as well.

This isn't a business in distress. We think Mexico does very well actually, over the next four/eight years. Yet you're paying very attractive returns just for staying still. We think there's growth there as well.

LK: So, let's move onto macro resilience. Historically, emerging markets have been associated with economic crises, financial instability, outflows of foreign capital. What's changed?

BD: Well, I suppose, what's changed is that emerging markets have recognised that as well. They know there's crises named after them, the 1980s LATAM debt crisis, for example, the 1997 Asian financial crisis. They've realised, painfully, that they can't rely on foreign investment to fund a lot of the growth that happens in emerging markets.

That would make sense though, because you'd expect the richer slower-growing parts of the world to fund the growth that has very high returns in the emerging markets. But the problem is, many of

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those foreign funders are good-times lenders. They come in, they fund, and when times get tougher, they all rush out, which actually precipitates those crises.

So, instead, what's happened in these emerging markets countries, is, they've learned a form of self-sufficiency. They have far higher foreign reserves, relatively lower debt levels, more stable fiscal positions.

The challenge with this kind of country-level austerity, [is that] it's a bit like a diet, but across an entire country. It's painful, and it takes time, and you're not really enjoying yourself while it's going on. But the outcome, though, is that you're actually a far stabler foundation.

And when we look at macroeconomics today, actually, some of the unorthodox policies that you saw in emerging markets of old, you see in developed markets today, really.

LK: So, that's the countries becoming more resilient. Are the companies themselves becoming more resilient too?

BD: Yes, absolutely. So, the old story was that you had very low-cost labour or simple minerals/materials to extract from emerging markets and sell to developed market countries. However, now you've got world-class companies that just integrate it in their supply chains or for companies and for economies as a whole. Take Indian IT, for example.

This was an industry that came about in the early 2000s. You may remember the Y2K bug, where you just needed a code from two-digit years to four-digit years. That was a long and painful process. There was a lot of cheap Indian labour that could do that.

And so, you used it for that, and then, when you were done, you just dropped it. But now, companies like Infosys, Tata Consultancy Services, that were born out of that era, are some of the most capable at doing any kind of large-scale implementation of IT in the world.

And so, businesses like BT, for example, here in the UK, just can't operate without them. So, this is no longer a discretionary source of labour, but instead, just a key part of the global economy. And so, any AI implementation that any companies are really looking to do at scale will use businesses like this.

Then, maybe on the product side, businesses like Shenzhou International that make many of the clothes for Nike and Puma, Adidas, this isn't just low-cost labour again. Historically, China was the cheapest place to manufacture a lot of this, and they came about there.

Brilliant economies of scale, but as labour in China got more expensive, they moved to the rest of the world. What we're seeing now is, when these developed world companies want to shift their supply chain, they actually take these emerging market suppliers with them because they have the knowhow, the skillset.

So, when Nike moves from China to Indonesia or Vietnam or Bangladesh, they bring these suppliers with them because they have tremendous potential that way.

LK: So, that brings us to growth, [which] is the other factor that you talked about. Baillie Gifford, of course, is a long-term investor. When we buy a stock, we look to hold it for five to ten years or longer. Over that timespan then, what do you think are going to be the main growth drivers of emerging markets and their companies?

BD: Yes, I suppose, I'll start with just a lot of great growth companies. EM, for better or worse, is about 10 per cent of global indices. So, 90 per cent is really the west, developed markets, 10 per cent is EM.

But EM contributes half of the high-growth companies over the next three to five years across those global indices there. So, you have an outsized proportion of just great growth companies because these are faster-growing economies, and so there's plenty of nascent opportunities there. But the top-down trends as well, I think, are really supportive.

If you look at the biggest challenges that we're dealing with, and the biggest opportunities as well, the energy transition has to be up there. That's a $100tn CapEx investment programme, and guess where the vast majority of the materials and the manufacturing is coming from? It's coming from EM.

It's coming from places like China that have had the ambition, perhaps, to invest really heavily in solar, wind and the like. And then places like Indonesia or Latin America that are endowed with a lot of those minerals as well. So, we think that that drives a boom there.

LK: And sorry, CapEx, that's capital expenditure, isn't it?

BD: Yes. Investment that is recorded on the balance sheet, rather than expensed immediately. The second big change, of course, that we're all familiar with, is AI, or high-performance computing.

And to our earlier point, TSMC is manufacturing the vast majority of the world's leading logic chips, and then Samsung is the other one there. And the memory, again, that all comes, well the vast majority comes from Asia as well. And so, I think, if you want to have anything there, you're going to need to have a lot of investment from Asia.

And these aren't discretionary choices. You've seen the troubles Intel has had in the West as well. Emerging markets, Asia has won the right to be leading, and these are some of the biggest top-down trends. And then, finally, there's just the growth of the emerging middle class.

Where do you think the next billion consumers come from? It's not coming from the West, almost arithmetically, because they're already spending lots.

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It’s coming from places like India and China that are moving up that prosperity curve and also places like Taiwan, South Korea, that are relatively wealthy but haven’t spent yet because they’ve saved so much and then invested in their businesses, rather than being able to, frankly, enjoy life. And so, I think you see an awful lot more consumption there, and so we’re invested in that as well.

LK: If I play devil’s advocate though, emerging markets have been amongst the chief beneficiaries of the wave of globalisation that began in the 1980s. President-elect Trump comes back to power in January, and he’s talking about introducing tariffs of 60 per cent on Chinese imports, 10 to 20 per cent on those from other countries. Is there a risk that you then get tit-for-tat action, and as a result, deglobalisation?

BD: I think there’s absolutely a risk, and to be clear, I don't think tariffs on both sides would be good news. It would be painful, and certainly, in the short term, detrimental for all. The question there is, who suffers most?

But that’s not really an avenue we want to go down. I’d argue that those positions are, most likely, opening bargaining positions, and it makes much more sense for a happy compromise to be met. But even so, I think it’s important to remember that globalisation isn’t just China selling to the US. It’s much more than that.

And what the US wants is, arguably, a designification, rather than a deglobalisation. And so, if they’re looking to achieve that, the biggest beneficiaries there are the rest of the emerging markets, Mexico, Vietnam and the like.

And then, [with] emerging markets, [when] you look at trade there, actually, 70 per cent of trades from emerging markets is to other emerging markets as well. So, again, they will adapt. And finally, while we look at good companies in China and the rest of the world, a lot of them are hamstrung by having even better, more established businesses that will sell the same products tariff-free from the US to them.

And so, they’ve not been able to succeed because they’ve had very advanced western competitors. But these threats of deglobalisation have actually given an impetus to prioritise domestic manufacturers, [and] domestic innovators.

So, you’re actually seeing a boom in innovation in many sectors that we think [is] really intriguing. And from our perspective, as emerging markets investors with pretty depressed starting valuations, actually could drive tremendous growth there in the long term, despite, as you say, a relatively pessimistic or negative reason for that [at] the outset.

LK: Okay, and then if I introduce the theme that, I think, has been woven through a lot of this, the increasing number of world-class companies in emerging markets to pick from. I talked about TSMC right at the start. Can you give us another example?

BD: Yes, sure. So, maybe one that we can all relate to would be a business like Coupang. So, this is an ecommerce business in South Korea. I'd say, the best ecommerce experience in the world. So, you can order anything you want, food/groceries by midnight, and it'll be at your door by 7am the next morning.

They've out-Amazoned Amazon there, and there's still so much more room for them to go as well. Then in China, you've got the internet platforms, which offer a far superior experience, again, than we can, as consumers, too.

The payments, the delivery, the communications, the seamless work of WeChat to interconnect everybody and every business together there, I think that is tremendous and underappreciated.

Then maybe at the macro scale, look at businesses like BYD or Hyundai. These are some of the best cars in the world. You saw the Ford CEO admitting recently that he'd been driving a Chinese car, a Xiaomi car, for the last six months and doesn't want to give it up. And that's a remarkable statement by a competitor CEO there.

So, I think you're seeing underappreciated quality and innovation that means these businesses are world-class and aren't so reliant on the whims of global trade and western sentiment.

LK: You mentioned China there. I checked before we sat down. You've visited there three times this year on investment trips. Can you tell us about some of the companies that you met that you think have the potential for strong long-term growth?

BD: Sure, yes. I think China, throughout our universe, is the most useful place to visit because it's so misunderstood. And there [are] plenty of positives and negatives, to be clear. But the companies are fascinating.

One would be SG Micro, which relates to what I was talking about there, the shift towards import substitution, being able to get an elbow into what was previously a very closed market. So, they make analogue semiconductors. These aren't the digital ones that you'd be familiar with, with logic and memory, but they convert heat, noise, radio signals and the like, into a digital form there.

Previously, a domain dominated by the likes of Texas Instruments in the US. But this company's doing great things and taking Chinese expertise and actually putting that throughout the electronic supply chain in China. I think they're tremendously driven.

This is a company that, a couple of years back, was traded at fantastic valuations by the domestic market. But as you've seen, a bit of a cycle there, both in terms of semiconductors and in sentiment in the Chinese market. It's now at very attractive valuations, and because some of the things we've talked about are coming to pass there, in terms of global trade, I think the prospects for them are even stronger.

More prosaically, one business I really like is Luckin Coffee. So, [the] clue's in the name, [it's a] coffee company. [It] had a bit of a scandal a couple of years ago, but we think it's the best coffee business in China and has outcompeted Starbucks in practically every aspect.

20,000 stores in China now and still growing very strongly. You can't go up to one of their stores and order a coffee. Everything is done through the app, which means they have tremendous data, and they can plan, and they can also understand what people might like.

So, they'll know someone like you might be ordering an Americano at midday, and so they'll have one premade. It's more likely a jasmine tea coffee or something like that, or a coconut latte actually.

But I think they have real innovation there, both in digital expertise, and also a fresh perspective on what coffee is. As I said, jasmine tea latte. Apple Americano [has] been very popular as well recently. But they bring out 100 new flavours a year, just to see what works. And then what works, they continue, and what doesn't, they quietly drop there. So, I think that's got tremendous potential as a business.

From a more traditional Chinese perspective, perhaps, a company I like is Haidilao, [which] is a hotpot restaurant. So, you have a very communal way of eating. You have a hot soup base in the middle, and you cook your own food in that. So, celebrations, birthday parties, that kind of thing.

What would be a traditionally, very competitive industry, the Chinese restaurant industry, they've done very well. A result of, I think, a founder-led business and a culture that's empowered their people. And so, it's not just about these big-picture trends, but just really finding excellent businesses that are tremendously well run that have great growth opportunities.

LK: So, that's quite a range of companies in China. How about somewhere a little bit more off the beaten track that you've visited, to meet companies on their home turf?

BD: Yes, sure. So, one recent example is going to the frontier markets, [like] Kazakhstan. One of my colleagues and I went to Kazakhstan for a week to see Kaspi, which is, I'd contend, the world's best super app.

So, this is a business that practically every adult in Kazakhstan has downloaded on their phone. It's an app that does ecommerce, payments, all sorts of other things, such as travel booking and banking as well. And so, it's that breadth of offering that we're, perhaps, unfamiliar with in the west. But it's that level of trust and uniquity that they have that gives them a real advantage there.

We'd understood it from afar, met the founder a few times over Zoom, but really wanted to go and meet them in person and understand other perspectives in Kazakhstan because it just looks almost too good to be true from afar.

And so, we wanted to figure out what the growth opportunity was and whether the business would continue to thrive in a relatively small economy there, which was really reassuring. We met the sovereign wealth fund, met the regulator, competitors, customers and the like. And that's the kind of work that, I think, when you have that five [to] ten-year horizon, is worth doing to really understand the long-term operational prospects of a company, rather than just trying to second-guess quarterly earnings.

LK: And moving on to Latin America, I spoke to Alexander Nicolier from the Private Companies team earlier in the week about a trip that he'd taken to Brazil and Colombia, and of course, on the public markets, Baillie Gifford's the biggest institutional investor in Mercado Libre, the fintech and ecommerce giant. Can you tell us about some other companies in the region that our audience should be aware of?

BD: Yes, sure. So, I suppose, Alex has the most exciting companies in Latin America, but I get some of the bigger ones, maybe, or the ones that work for the mass economy. One example, perhaps, would be Raizen, which is a second-generation ethanol producer.

So, this company grows enormous amounts of sugar in South America. And historically, the sugar cane from that, the waste that isn't processed into cane sugar, was just burned in the fields, but now, they're producing what's called second-generation ethanol.

So, first-generation ethanol is when you take corn or sugar and produce that into ethanol that's then used, often as a fuel additive. The problem is that competes with food supplies. This is taking that waste material I mentioned and converting that into a form of fuel, which I think, has tremendous potential.

It's taking advantage of something, which would otherwise go unused and indeed, pollute the atmosphere, into something that actually is environmentally beneficial. At the moment, mainly just added to domestic fuels, but increasingly exported at a premium because it's sustainably sourced for use in western countries. And a good source stock for sustainable aviation fuel as well.

Another one would be Nubank, a financial services business, an online fintech that has done tremendous things there in creating financial inclusion, a bit like what Mercado Libre's done on the side as well, but in a much more mass market in Brazil and now Mexico as well.

They, I suppose, just by taking a positive view on humanity and trusting people and treating customers in a far more open way than the state-owned banks did in Brazil, have built up a very strong customer base and actually have seen very good return metrics for a bank.

Their customers pay them back far more than they expected, and that customer quality is getting better as well. So, that's something that we're really optimistic about too.

LK: Exciting-sounding companies. Thanks, Ben. We'll be coming to audience questions soon, so if you haven't already done so, please, do submit one via the *Ask a Question* tab on your screen.

But before we do that, I want to talk about India, the world's fifth biggest economy, 1.5 billion people, and that scale works to the advantage of its domestic companies. So, can you give me an example of one that excites you?

BD: Yes, sure. So, one that I quite like that's maybe unexpected, is a business called PolicyBazaar, which looks a lot like Compare the Market here in the UK, but just so much better. This connects Indian insurers with people who buy insurance in India, which is actually a very large market because it's a traditional source of savings as well.

But in a low-trust economy where you have less-capable state-owned insurers often, there is tremendous value for a business like this to sit in the middle, digitise and increase trust and awareness.

The traditional model would be on-the-ground Indian insurance agents, [who] often do it part-time and sell to their relatives or their friends and family in their locality there. But people don't really know what they're signing. They don't have the financial acumen to figure it out.

PolicyBazaar has been very disruptive in saying, no, here's a better way. And I think that that business has tremendous network effects and very long-term growth from here. So, that's one I'm particularly excited about.

LK: And its chief executive's quite a force of nature, isn't he?

BD: Yes, that's a fair characterisation. In an industry that, traditionally, was quite chummy, he's really shaken things up by criticising the behaviours of the past and saying, look, we can do so much better.

In health insurance, for example, now, he's gone, look, I've got a lot of health insurance here, but I can do even better than that. I'm going to start building, in partnership, my own hospitals as well, so I can create that full lifecycle experience for a customer.

LK: So, that's insurance and PolicyBazaar. Can you give us another example, maybe in a different sector?

BD: Yes, sure. So, let's go to logistics. A business called Delhivery, which is a terrible pun, Delhi-very, Delhivery, is the name of the company there. But they've, I'd argue, the best logistics network in India. They've been lucky in some ways.

They started late, and the founder is very data-oriented as well. The result of starting late means that India's moved from a place of 50-odd different tax jurisdictions to one nationalised jurisdiction under GST, a kind of VAT-equivalent legislation that came in about eight years ago there. This meant, they've been able to build a genuinely national network for everyone else. Their older competitors are very much state-based.

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This has let them build an unusual form of network, a mesh network, rather than a hub-and-spoke network, which is far more efficient.

LK: And I think we can bring up a graphic, showing the difference between a mesh network and a traditional hub-and-spoke model. For those who aren't familiar, can you just contrast the two?

BD: Yes, sure. So, hub-and-spoke is what you'd see in an airline, for example. You've got a big hub like Heathrow or Atlanta in the US, and then you fly to and from there, and connecting through that hub if you're going to any of the spokes.

That's very efficient, to start with, and if you don't have critical mass on every single one of your interjoining networks, it works pretty well. But a mesh network is much more like the internet, for example, where you follow the most efficient route you possibly can.

And initially, that's pretty difficult because you might not have enough scale to go direct from, say, Maharashtra or Mumbai to Gujarat, and instead, it's more efficient to go Mumbai to Delhi and then Delhi to Gujarat.

But when you get scale, then being able to go direct is far more efficient and lower cost there. But it is these kinds of things that, building up over years, create competitive advantage. And this is the kind of thing that we're excited about, the willingness to think long-term and push for a more efficient model.

And this is what we see, that, again, isn't apparent in short-term results, but in long-term advantage, we think it's actually something quite special.

LK: It's a great example of long-term thinking. Thank you. Time for some audience questions now. Let's see what you've sent in.

Your questions answered

LK: So, just having a look to see what's here on the iPad. Let's have a look here. The fundamentals in emerging markets often look good, as you've said, but isn't the challenge about capital flows? When there's uncertainty, everyone runs to the dollar, and emerging markets get skint?

BD: Yes, I think that's a fair challenge. I'd make, maybe two points in response. Firstly, EM's been a pariah for a decade really, from a capital flows perspective. You've seen outflows over the last 10 years. The flipside of that is that you've had emerging markets funding themselves.

We talked about, what that means is, you're less vulnerable to those foreign outflows, both in debt and in equities. There aren't that many foreign investors left really in places like China, for example. And when returns have been weak, no one's really that incentivised to put money into these places, but when they start seeing returns getting stronger, I think you see very strong flows coming back in there.

The second point would be that emerging markets and equity markets are increasingly reliant on domestic flows. There is a lot of private capital sitting on the sidelines in China. In India, which has been strong, it's been domestic investors that have been making the market there.

So, we think that actually, the weakness of foreign capital flows is a positive feature now, but that transition has been quite painful over the last year. Picking that turning point, I agree, is incredibly difficult, but I don't think capital flows is the reason to be invested in emerging markets going forward. Instead, it's that quality of growth that would be funded and recognised by domestic investors.

LK: Okay, a question here about the opportunity in China. Given China's stimulus talks and actions by the Chinese Government and agencies over the last two months, what's the team's view? Have they done enough? What opportunity or risks do you see there?

BD: Yes, I think Chinese macro and stimulus is incredibly intriguing. They haven't done enough to turn around the economy. The fundamental driver of the economy over the last decade, be it exports, infrastructure, property, those have come to natural, or for tariffs, premature, ends in the case of exports there.

And Chinese stimulus hasn't been sufficient to do anything near turn those around. This is stimulus in the order of a couple per cent of GDP. You'd need 50/60 per cent of GDP to really change the game there. But perversely, I don't think that is necessary to make China a very attractive place for investment.

Historically, in China, you'd have two countervailing forces, domestic investors in the equity market or foreign investors. Domestic investors [are] momentum, enthusiasm-based. Foreign investors [are] much more rational. And they tend to offset each other quite well.

Now, both have been incredibly pessimistic, and so, Chinese markets are at very low valuations, and because of the failures of stimulus, because of the challenge of the Chinese economy, they will keep interest rates very low in a closed capital account, which means that you have this perverse situation where you get 1 per cent in a bond or in a current account, but you can get 5/6 per cent yields on these very strong-growing businesses.

I think those businesses' valuations should double, should triple. And so, if you're able to look through the weakness in the Chinese economy, then I think these become very attractive investments.

And stimulus, while not enough to fix the economy, is certainly enough to fix the stock market, to encourage growth there, because you can't make property prices double, but you certainly can make equity prices double. And that brings enthusiasm, wealth-effect back into the economy, which is what they're trying to achieve.

LK: Okay, I've got a question here from an audience member who's perhaps looking for a bit more reassurance. Are emerging markets at a place of increased risk, due to uncertain politics and economies in developed markets? How do they mirror one another?

BD: So, I think it is, maybe as the question was coming to, the challenges of politics in developed markets really that concern us most. And to your point, it is the aggressive policies of people like Donald Trump that worry us really.

And so, in the short term, I think it is incredibly uncertain, but markets are forward-looking, and I think a lot of that is reflected in valuations, as we've talked about. In the long term, it's that force for self-sufficiency that I think is really positive.

And because you're not reliant on capital flows, I think you can look through some of that. We're investors in that long-term progress, where I'm looking at companies on the operational progress and how that business can grow, rather than trying to worry too much about the three-/six-month outlook.

That is our advantage, being able to look through that. The flipside of that, though, is that we're not particularly good at timing, and that means accepting a degree of volatility. But remember what, I think, practically all of us are trying to do.

We're trying to invest on time horizons here, measured in years, decades, probably generations for many of us as well. And on those time horizons, I think that emerging markets, given starting valuations and given the underlying stronger growth, actually look pretty compelling here.

LK: Okay, a question picking up on some of your earlier comments about the chip manufacturer, TSMC. On TSMC, why do you think it attracts a significant discount, compared to the customers it serves? An invasion of Taiwan would impact those customers just as much as their most important supply.

BD: Yes, I think it's a fair challenge. You can go to the behaviours of investors as well. Obviously, the clue is in the name. It's in Taiwan. And frankly speaking, if you saw some kind of action between China and Taiwan and, for whatever reason, TSMC became uninvestable and their customers were hit just as well, you would get berated by your clients for investing in TSMC when this was obvious. Whereas you wouldn't get berated if you were investing in Apple, for example. So, there's a degree of, no one ever gets fired for buying IBM, for example.

But really, I think that it is because it's capital-intensive because it doesn't have the same degree of hype, this business isn't going to double over a year, whereas NVIDIA has doubled revenue over those kind of time horizons.

But over the longer-term perspective, I think it's actually a far stronger business because it chooses to deliberately, I suppose, avoid indulging in [the] short term.

They don't profit maximise in the short term, and that gives them a tremendous stability in the long term, which means that no one can get that excited, and it's a very large company and a pretty small market in Taiwan as well.

So, we think it is structurally undervalued and will always remain structurally undervalued, which we really like, from our perspective. But to your point, I suppose, it means that you need to have that long-term perspective because you can't get in and out for just a quick turn.

LK: And a follow-up on India. Do you think it's now become too expensive?

BD: The short answer would be yes. We found this difficult because, as I said earlier, a lot of the valuations were driven by domestic flows. You've seen very large foreign outflows, and so it's almost easy to say, oh, we're cleverer than you. We understand what's going on, paying 130 times for a supermarket chain, isn't this bonkers?

But actually, it's continued to do very well there. I think that, as we talked about earlier, prospect of returns in India are pretty low at the overall market level. It's corrected quite a bit over the last few weeks, few months, and I think, will have further to go.

Those domestic flows are driven by systematic investment plan flows, sticky, pretty price-insensitive flows from people who are often first-time investors. I think, when those go away, or at least abate, it'll be very positive for the market.

But our funds are relatively underweight India. We're much more enthusiastic about growth prospects elsewhere in Asia, and undervaluation [in] places like Brazil and China, to earlier comments.

LK: We're nearly out of time. We've got lots of questions here, so I want to get through a couple of them quickly. Back to definitions, at what point do emerging countries become developed countries? We seem to have classified the same group of countries as emerging for more than 30 years.

BD: Yes, good question. You've seen places like Israel that have been promoted, places like Greece that were promoted, and then went straight back in again, post the euro crisis, back into EM. There's a degree of classification choice by the MSCI.

You need to have complete English language disclosure, which is why Korea isn't there. You need to have access to foreign flows as well, but I think it is an arbitrary decision. Korea has higher GDP than Italy, for example. From my perspective, they're places that are just difficult to invest in, which, I think, is why they are still kept as EM, but are tremendously important.

And you need a specialism to be able to invest there. So I think, in a way, it's a benefit for these countries that they are still an EM because they get focused on by people like ourselves, rather than ignored by DM investors that just focus on the US or Europe.

LK: And one very last question. Can you tell us about which holdings in Vietnam excite you, and keep it brief?

BD: Sure, I'll give you two. Mobile World, the best retailer there and electronics, and now grocery. And then FPT, a leading IT services company that is servicing people in Japan and the US, that is doing tremendous things and far cheaper than those in India.

LK: That's great, Ben. Feels like we've done quite the world tour. We haven't had time to answer all your questions, but we'll aim to respond to some of those that we didn't get to on our Disruption Week website. Details of that coming up in a minute. Ben, we're nearly out of time, but before we go, could you leave the audience with one final thought?

BD: Sure, and I suppose to some of the questions, there's plenty of behavioural biases and uncertainties when you're investing far from home, particularly when you haven't been paid for that the last few years. Newspaper headlines do nothing to reassure as well because that sells.

But what goes underreported really is that steady, silent march of human progress, and that's what drives returns in the long run. That's what's led to the success of the whole world, and EM is not an exception there. And given these starting valuations, we think the returns are incredibly compelling because those fundamentals are there, and that's what will drive future progress.

LK: Ben, it's been great talking to you. Thank you.

BD: Thank you, Leo.

LK: And that brings us to the end of our final topic for this Disruption Week. I hope you've enjoyed this and the past day's events. You may be aware we had to postpone our session on the Age Wave, but we still intend to record the conversation, and we'll let you know when you can get the briefing about companies taking advantage of us living longer but having fewer children.

In the meantime, if you want to refresh your memory about our earlier events on the US's infrastructure renaissance, investing in private companies, or indeed, this emerging markets discussion, please visit bailliegifford.com/disruptionweek.

If you have any follow-up questions or suggestions for future Disruption Week topics, please get in touch with your client contact or email us at disruptionweek@bailliegifford.com. And if you haven't already done so, please, also check out our podcast, Short Briefings on Long Term Thinking, where I quiz our investment managers throughout the year. But for now, that's it. Thank you and goodbye.

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