Emerging Quietly

Although down roughly 3.5% as of Nov. 30, the Seligman Emerging Markets Fund's manager, Daniel J. Barker, thinks that foreign markets are quietly emerging from a global slump and could outpeform the markets in developed countries if that growth perks up. A veteran with more than 10 years of experience in investments, primarily in growth companies within the developing markets arena, Barker leads a team responsible for the Seligman Emerging Markets Fund. A chartered financial analyst, Barker is a managing director of J & W Seligman and co-manager of the Global Investment Group. Ticker spoke with Barker to get his outlook on emerging markets in 2003.

Q: Several fund managers I've spoken with recently expect a pickup in the global economy in 2003. What is your view?

A: I'm probably more cautious on global growth. I think we've done a lot to either extend growth or keep growth at a minimal level through low interest and easy money. I think that game is about up. I'm concerned that we've gotten about as much out of the consumer as we can. We need business investment to kick in to provide what would be the next leg of growth. Given the capacity-utilization, which is quite low, I don't see the need for a tremendous uptick in business investment. Looking at Japan, I still see a lot of malaise there and a lot of continuing problems in the banking sector and restructuring of that economy. Europe, additionally, has a lot of structural issues to deal with, a central bank that is not nearly as aggressive in terms of promoting growth. My baseline expectation is that growth will be there but it will be muted and probably disappointing, relative to consensus.

Q: How weak must the dollar become to generate a massive flow of money overseas?

A: There are fundamental effects for companies and there are fundamental effects for portfolio flows into equity markets. Certainly from a portfolio flow standpoint, international investments have been swimming upstream for the last eight or nine years against a strong U.S. dollar. Any kind of equity return performance has been muted by losses in local currencies. That has switched in the past year. The dollar has been weakening, although not to any great extent. Overall, it's helped improve performance for international investment. If the dollar starts to fall 10% or 15%, then you will see the performance from foreign assets grow, and the appeal of foreign markets will grow with that. On the other hand, you have a lot of companies in all these other markets, which fundamentally don't really want the dollar to weaken. It's not a straight positive or negative. For domestic oriented companies outside the U.S., they're the pure beneficiaries; especially those in the markets that I follow that have dollar debts. A lot of companies have raised debt in U.S. dollars and when the dollar weakens, those debt obligations are reduced. That can be a major fundamental positive for specific companies.

TICKER'S CHOICE

Seligman Emerging Markets A

Fund Facts		
Symbol	SHEMX	
Website	www.seligman.com	
Address	Seligman Group, 100 Park Avenue, New York, NY 10017	
Tel. No.	800-221-2450	
Inception	05/28/96	
Portfolio		
Total Net Assets *		$24.50
Median Market Capitalization *		---
Average Price/Earnings Ratio		---
Average Price/Book Ratio		---
Turnover Ratio		133.56%
Investment Information		
New Investment		Open
Min Initial Investment		$1,000
Min Subsequent Investment		$100
Min Initial IRA Investment		$1,000
Risk (Against Std Index - 3-yr Average)		
	SHEMX	**Category Avg.**
Alpha	1.07	4.59
Beta	1.15	1.00
Returns vs. Category		
	SHEMX	**Category Avg.**
1 Year	- 3.00%	2.61%
3 Year Avg.	- 17.51%	- 0.47%
5 Year Avg.	- 8.80%	0.01%
Returns vs. MSCI EAFE NDTR_D		
	SHEMX	**Index**
1 Year	- 3.00%	- 12.50%
3 Year Avg.	- 17.51%	- 1.11%
5 Year Avg.	- 8.80%	- 0.05%
Fees and Expenses		
Max Sales Charge - Front		4.75%
Max Sales Charge - Deferred		0.00%
Redemption Fee		0.00%
Total Expense Ratio		3.14%
Portfolio Manager		
Daniel J. Barker		01/21/00

** millions*

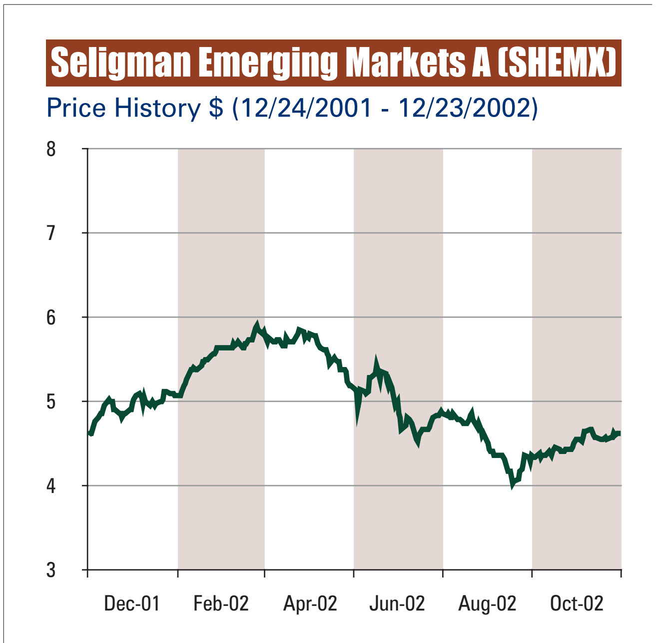
Source: Mutual Fund Company Documents

Q: How do global tax rates affect your stock selections?

A: We do a bottom-up stock picking with a top down overlay. As part of that overlay, tax rates are one of the hard variables we key in on. Seligman tends to be a supply-side-oriented place, and we do tend to look at tax rates as one of the key variables. In places like Korea, you're seeing taxes reduced. That's a positive. In Thailand, we're seeing taxes reduced. In general, the picture is more neutral than anything. The other positive is Russia. They've gone to a flat tax and to a lower tax and surprise, they've seen the economy grow more and tax revenues go up.

Q: The portfolio's allocation is roughly 50% concentrated in the Pacific region. What companies there interest you?

A: A wide variety. In Korea, it's anything from technology to industrial based companies. In China, it's the same thing. To give you specific names, in Taiwan, I would talk about a company like Ambit, which is a global leader in wireless LAN connectivity solutions and also broadband ADSL and cable modems. In Korea, companies like Samsung, which is our largest holding — you play them as conduits. They're competitive, just being in Korea. Even in Korea, they're outsourcing further to China for some of the more lower-value-added things they make. When it comes to the higher valued products, semiconductors or integrated circuits, that stuff is still made in Korea. But, the box building for them has been outsourced to China. While you don't necessarily play China directly, you're playing it indirectly, because these are the first movers into China using it as a production resource and they're well ahead of their U.S. and European counterparts, as well as the Japanese.



Q: When it comes to consumerism, what advantage do overseas companies have over the U.S. multinationals?

A: When you look at retail or consumer finance, we own a bank called Kookmin Bank. They have a significant share of the credit card market, 25% to 30% in Korea. Kookmin Bank is being run by people from Goldman Sachs and ING Bank, as well as local Koreans. There is a lot of Western expertise on the board and in the management of a bank like that. So, they're really at no disadvantage. They bring the expertise from the global multinationals and merge it with the local knowledge and the local management. When you look at the retailing side of things, it takes a fair amount of time for the Wal-Marts to get their formula right for the local market. Wal-Mart has oftentimes just taken the same store and just slapped it down in the middle of Korea and Mexico and had a very poor performance at the initial outset. In Korea, we own Shinsegae Corp., which is a discounter. It's vastly superior to Wal-Mart because they know how to localize.

Q: Turning to emerging markets in Western Europe, now that Russia has matched Saudi Arabia in terms of daily output, how oil dependent is the economy?

A: No doubt part of Russia's success is disguised as a sustainable high oil price and an increasing reliance on Russian oil, given OPEC and geopolitical considerations. I'm of the opinion that Russia has improved. The quality of governance of corporations is at a much higher standard. Like I said, some of the tax and policy changes have been real. That said, it's a little bit difficult to separate the true reform from the benefits of a high oil price. If oil stays in the 20-plus dollar per barrel range, I think you'll see a pretty healthy situation in Russia, at least in line or above average performance.

Q: Do you look at other raw materials there, nickel producers, for example?

A: We've owned Norelsk in the past. Like a lot of Russian companies, Norelsk is not the most transparent situation in the world. It's hard to understand their inventory situation. It's very much managed from above. The government has a strategic reserve of platinum and palladium, and they can play with how much supply it wants to put on the market. In the past it's had poor corporate governance. It's the world leader in nickel, platinum and palladium. It's a monster. If it's managed properly, it's worth a lot than it's valued at today. Given the corporate governance concerns, we don't find it attractive right now.

Q: The Balkan countries, Hungary, for example are due to join the EU in 2004 and adapt the common currency in 2006. Should we get in now or wait?

A: It's a complicated question. If you looked at euro conversion plays when you looked at Greece or Portugal, it was pretty straightforward. They were cheap markets; they had high interest rates. As they moved toward convergence with the EU, interest rates converged. You had a lot of growth driven by consumption on low interest rates and improving stability of the macroeconomic environment. Those things still apply, but I think to a lesser degree than they did three or four years ago. The EU is not as generous as it once was with incoming countries. There were significant transfers to help develop these underdeveloped economies. Those giveaways aren't going to be near what they were for some of the early entrants. The common agricultural policy, or the CAP as it's referred to in Europe, is a big headache. The farmers in Poland and Hungary are quite productive and quite low cost. If allowed to freely compete, they'll put the French and Germans and everybody else out of business. Again, line by line, there are benefits and in general it's positive, but I don't think it's going to be the boom as it was for the Greeces and Portugals and Spains when they entered the EU.

Q: Are you still cautious about the Middle East, particularly Israel?

A: We have a somewhat contrarian view. We're overweight Israel by a few percent. It's a deep valuation situation, most specifically in technology, where you can buy companies for less than their net current assets. In other words, you can buy a company with $2 in cash for $1.50. The situation, as we see it, is the businesses are stable. They're going to be survivors, and actually we think they're going to thrive in a better growth environment. A couple of names we have are Radvision, a leader in video conferencing, and Ceragon, which makes wireless broadband telecom equipment. They're both difficult sectors, but they're global leaders. Whenever we get to the other side of this abyss, we think they're going to grow quite strongly.

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>
> **Daniel J. Barker**

Q: Turning to China, how is the country deploying its huge trade surplus?

A: We like China a lot. You've seen growth there of about 8%. What we play there is a lot of domestic plays. Returning to our theme, it's a bit defensive. There are a lot of domestic companies that have been growing and I think will continue to grow at 20% to 30% that you can buy for seven or eight times earnings. We're excited about what we have there. We have things like Denway Motors, which sells Hondas. They have a 50-50 joint venture with Honda to sell the whole product line. They're expanding production aggressively, but at the same time there's a waiting list for cars. You're paying seven times earnings for what has historically been 25% to 30% growth, and with a good yield, too, of 4%. We also own CNOOC, which is China National Offshore. They have exclusive rights to all the offshore oil reserves. China is an oil importer, so they have every motivation to grow the domestic oil market. CNOOC is sitting on top of some very fertile ground. They're going to grow about 15% a year. We own Expressway, which operates toll roads running from Shanghai to the ports. They're seeing volume growing at 20% a year and again with a good 5% dividend yield. It's fairly simple business, but even simple businesses can be exciting in China.

Q: How do feel overall about emerging markets?

A: Very quietly, emerging markets have now outperformed developed markets for four years running. Nobody really knows that. That's reasonable because emerging markets have effectively gone nowhere and the rest of the world has fallen in the toilet in terms of performance. When you put it in perspective, it's significantly outperformed the rest of the world. When you look at the growth relative to developed markets and you still look at the valuation relative to developed markets, you have every reason to believe that the outperformance will continue. In my reading of quantitative data, I learned the ROE is 30% higher than the return in developed markets. You're paying about eight times earnings on the whole. You're paying about 14 times for the developed markets.

Q: So emerging markets look cheap right now?

A: They're always cheap relative to developed markets. But, even relative to their history, they're on the cheapest end of where they've been. What's different this time is that actually the companies are even better. You've never had a situation where the ROE in emerging markets was higher than the ROE in the developed. Now that you have better companies, it could be argued that, even in a tough market, I'm pretty optimistic that you're going to see continued outperformance. If global markets really perk up, then I think you'll see tremendous outperformance. At worst, you'll do OK, and at best you can do really well. I still think the risk reward still looks very favorable. ▮

Dave Jennings