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## INVESTING IN EMERGING MARKETS



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Economist

September 2010

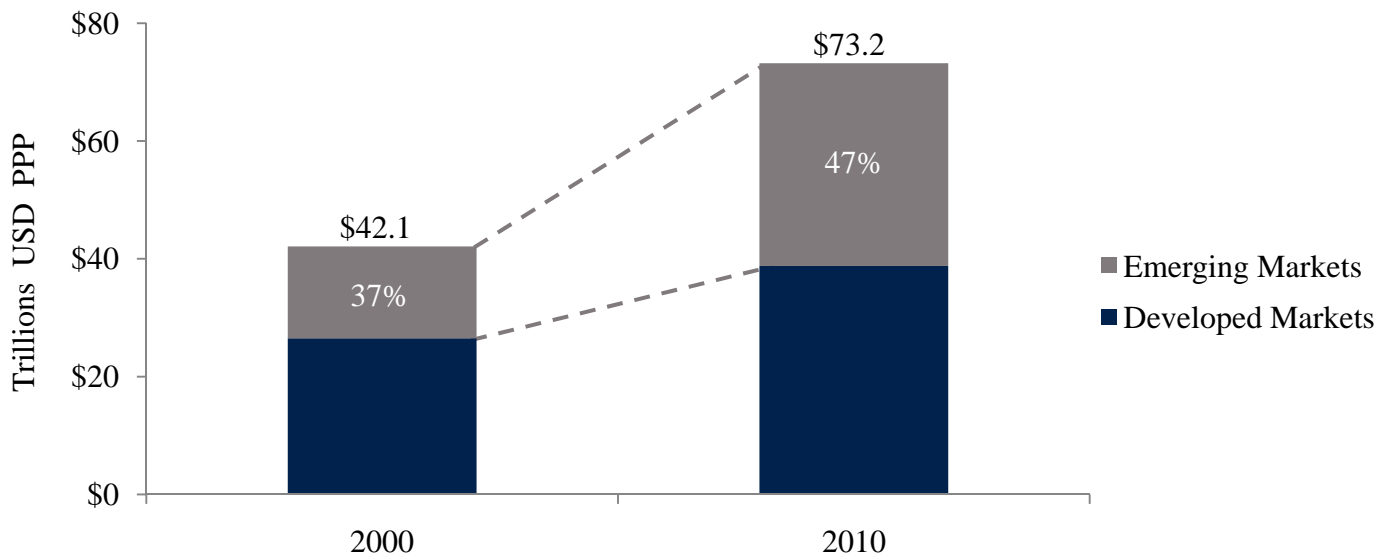
**Investing In Emerging Markets**  
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*A*t William Blair & Company, we believe that emerging markets are an important part of the global opportunity set. Emerging markets will be global growth drivers over the years to come, as more emerging markets consumers attain middle class status and industrial production continues to grow. These trends are important not only for those that invest directly in emerging markets, but also for investors in multinational companies as a number of these companies are focusing on emerging markets demand as their growth drivers for the future.

Emerging Markets investing is a broad topic. Following a brief discussion on why everyone should be looking at emerging markets, we'll focus on what drives GDP (Gross Domestic Product) growth and why it suddenly accelerates in some places and not in others. Next, we will make the case for three of the popular emerging markets – Indonesia, India and China. We'll highlight the “magic of number eight” and discuss why investors should be paying attention to whether these three countries can grow at an approximately 8% annual rate moving forward.

Over the past decade, emerging markets became the drivers of global growth, rather than just its beneficiaries. What that means in practice is that today close to half of the world's GDP is produced outside of Europe, North America, and Japan. This is a big change that occurred in a short period of time.

**Chart 1: Share of Emerging Markets in Global GDP**



Source: International Monetary Fund, World Economic Outlook Database, April 2010

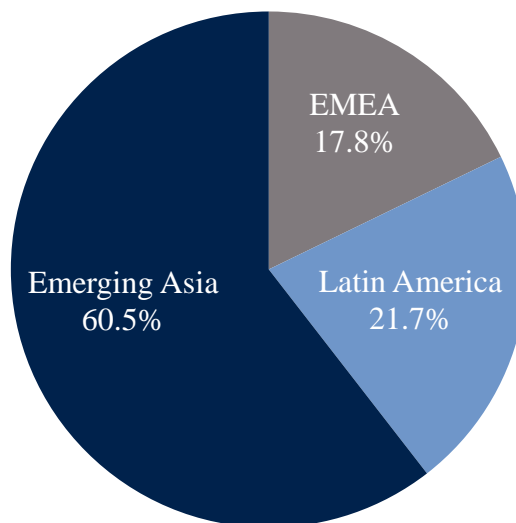
Chart 1 reflects that as early as ten years ago the ratio of emerging markets GDP to world total was less than 40%. If we go back to the early 1980s, that number was around 10%, so in a very short period of time, these countries have become the drivers of world output. The way they are able to capture the ever bigger share of world GDP is through growth differentials. These countries are growing at a much faster rate than the world in general; and obviously at an even faster rate than developed markets.

As emerging markets countries are becoming more important economically, their share of global equity markets is also rising. Today that share stands at around 14%. Now with 47% of global growth and only 14% of equity markets, there is a tremendous scope for more companies in these countries to become public and to be more investable. As a result, the investable opportunity set is going to grow even faster than headline GDP numbers.

Another factor that propels these markets forward is the demographic dynamic. As early as 1950, the global population was about 2.5 billion people, give or take a few million. Today that number is 6.5 billion, so that is a three-fold increase in the span of approximately 60 years. In that time frame, the share of world population that lives in emerging markets has increased from just under 70% to over 80%. Not only are these countries the drivers of GDP growth, but also where most of tomorrow's consumers live. These are underpenetrated and very large markets. The opportunity is exciting, not just for companies that are operating in the regions, but for companies that are operating almost anywhere else in the world.

When we talk about emerging markets, who are we talking about? EMEA is Europe, Middle East, and Africa, which includes some of the North African countries and a number of the Eastern European countries that are trying to modernize. Emerging Asia includes countries that in the 1980s and 1990s were known as the Asian Tigers, but that set is now much broader. Emerging markets also include countries in Latin America.

**Chart 2: Primary Emerging Markets**



Source: FactSet as of 6/30/10

Driven by China, the share of Emerging Asia in world GDP has grown quite a bit. Unsurprisingly, given the diversity of the emerging markets universe, growth has not been distributed evenly. In fact, China, India, and Indonesia account for about 40% of emerging markets output.

**Chart 3: Growth Within Emerging Markets Has Been Distributed Unevenly**

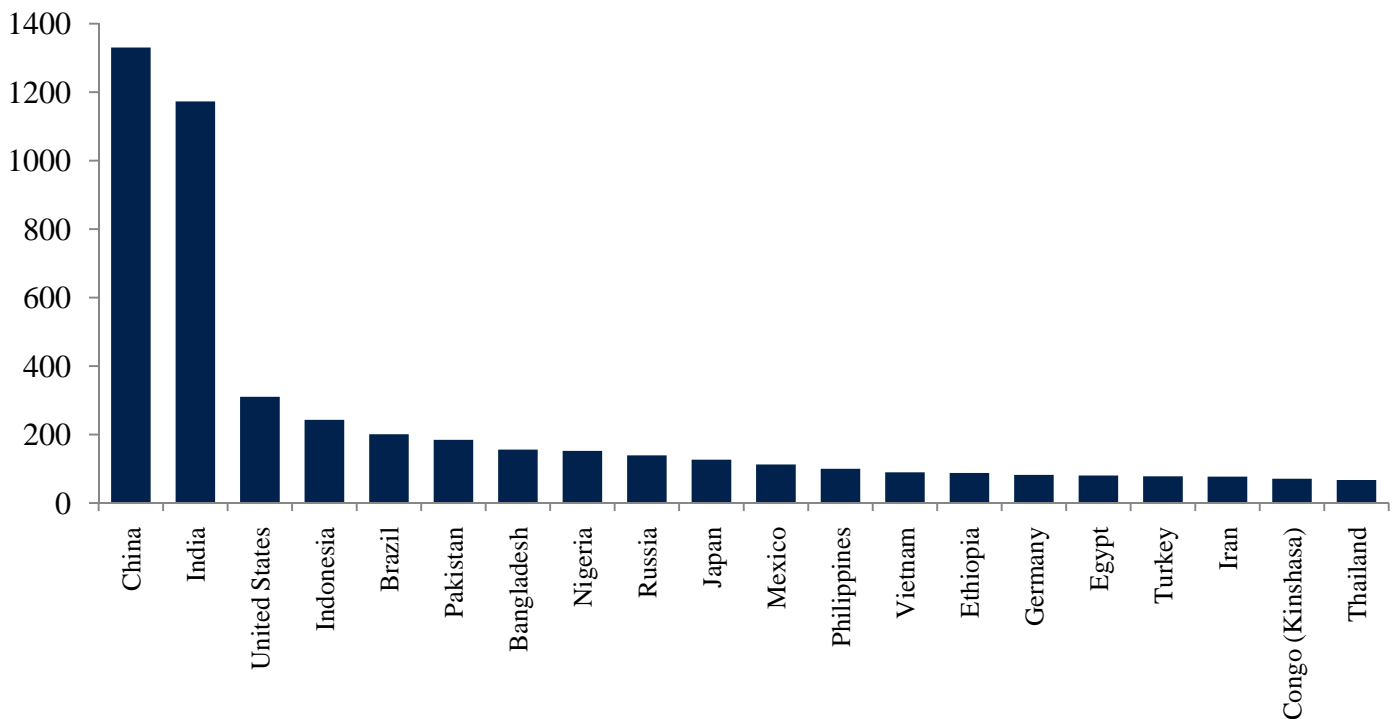
% Share of Emerging Markets GDP			
	1990	2000	2010
China	10%	19%	28%
India	8%	10%	11%
Indonesia	3%	3%	3%

Source: International Monetary Fund, World Economic Outlook Database, April 2010

In 1990, China accounted for only 10% of emerging markets GDP, and today it is probably close to one-third.

The key questions for investors, following three decades of what has, by any measure, been unprecedented growth are: a) can China slow down enough but still to continue on its growth trajectory? And, as importantly, b) can India and Indonesia now pick up the slack? Population-wise, these countries are very important. Forty percent of the world's population live in India, China, and Indonesia. The opportunity to serve those consumers is tremendous should they one day become consumers.

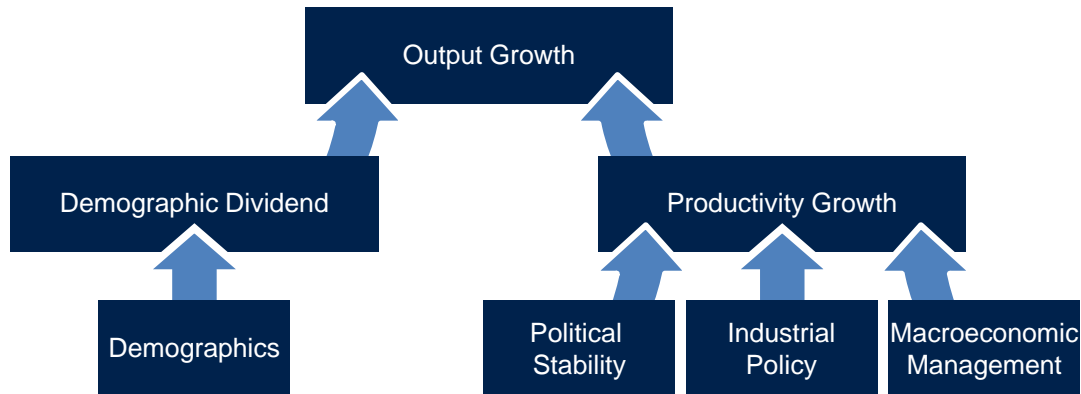
**Chart 4: Population Distribution by Country, 2010 (in millions)**



Source: US Census Bureau, 2010

What drives output growth acceleration? Why, all of a sudden, is a country that has been growing at about 2% to 3% per year able to grow at 8% to 12% per year? There are four key drivers.

**Chart 5: Key Determinants of Output Growth Acceleration**



The first driver is favorable demographics. Demographers refer to something called the population bonus, which is effectively a ratio of working age population to the non-working-age population. If that ratio is around 2, or is rising very rapidly, that means there is a pool of capable workers that can produce relatively more compared to the size of the overall population. Supplemented by proper industrial policies, favorable demographics can lift GDP growth by 2% to 3% per year.

Political stability is also a prerequisite. This does not necessarily mean democracy. Political stability in this context refers to pro-growth policies by the government and, more importantly, some transparency and some continuity so that there is not a new regime every two years, so businesses can plan, invest, and really think about a five- to ten-year horizon.

Industrial policy is a broad basket. It can include any number of things such as favorable tax regimes that influence growth in particular sectors or at least not undermine it at the expense of other sectors (e.g. services versus manufacturing). This factor is particularly relevant for India, for example. It could be labor policies: how easy or difficult it is to hire and fire new workers, how easy or difficult it is to expand into a neighboring state or a province, etc.

Macroeconomic management usually incorporates fiscal policy and monetary policy. Businesses require a relatively low and, more importantly, constant rate of inflation to accelerate investment. The rate of inflation impacts lending rates and required return on investment (ROI) for a long-term project to be undertaken. Low and constant inflation reduces uncertainty, lending rates, and ultimately, ROI, making more projects attractive. Government policies to facilitate private investment along with public investment stimulate sustainable acceleration of growth.

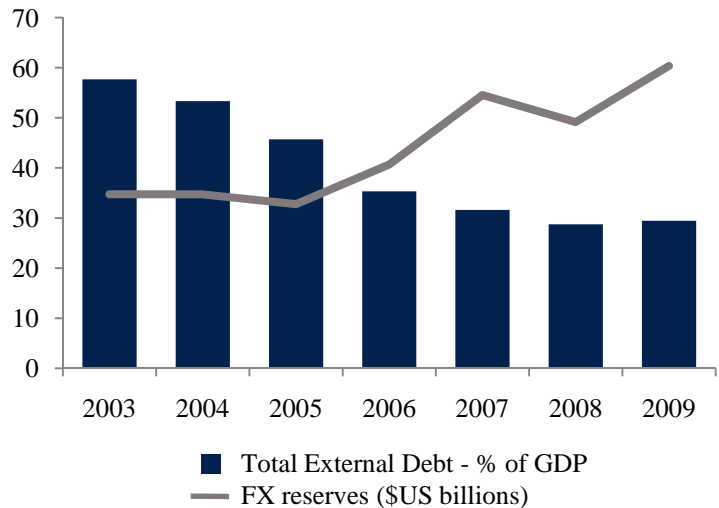
Moving up the chart, initial conditions accelerate two components of growth: a labor input that is now bigger and rising faster from the demographic dividend, and faster productivity growth resulting from growing capital stock. Productivity is really what drives a country's wealth. That is what determines whether consumers are able to consume and, if so, how much. Together those two components comprise GDP or output growth, and acceleration in one or both of them and preferably both of them, accelerates output growth.

Let's now turn to the experiences of three popular emerging markets – Indonesia, India, and China.

**Indonesia**

Let us focus on the first country, Indonesia. Indonesia grew fairly rapidly before the Asian Crisis of 1998 - 1999, and that crisis really set the country back. Its macroeconomic stability was undermined. Overnight, the government found that it was sitting on massive piles of foreign denominated debt that it could no longer service. Growth plummeted. Since 2000, the Indonesian government has worked hard to restore macroeconomic stability, both on the fiscal and on the external side. External debt as a share of GDP (both private sector and public sector) has been declining steadily, while FX reserves have risen steadily, as shown on Chart 6.

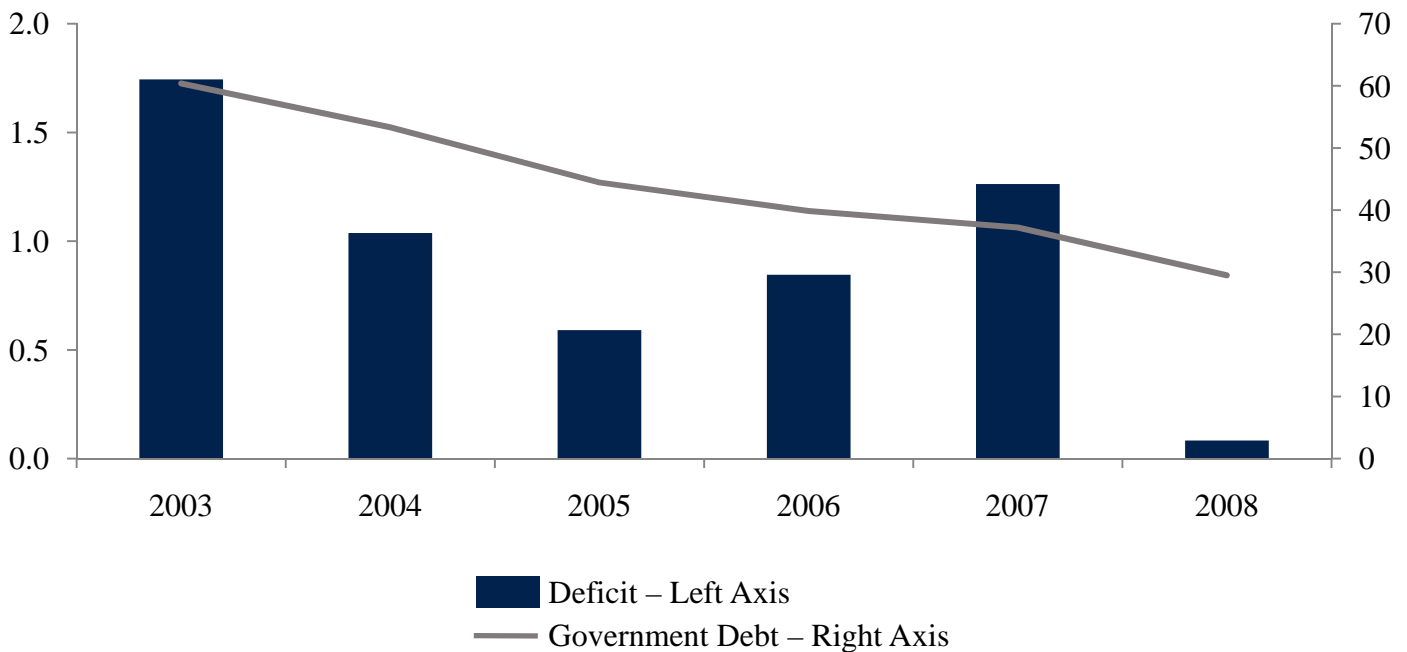
**Chart 6: Indonesia – Total External Debt**



Source: FactSet as of 12/31/09

Obviously, 2009 was a bit of a challenging year for everyone. But even in that environment, Indonesia managed to grow by a healthy 4.5% - 5% per year. The Indonesian government has shown remarkable discipline in controlling public finances. As Chart 7 shows, public deficits have been kept to under 2% of GDP, and the stock of public debt has declined to around 30% of GDP.

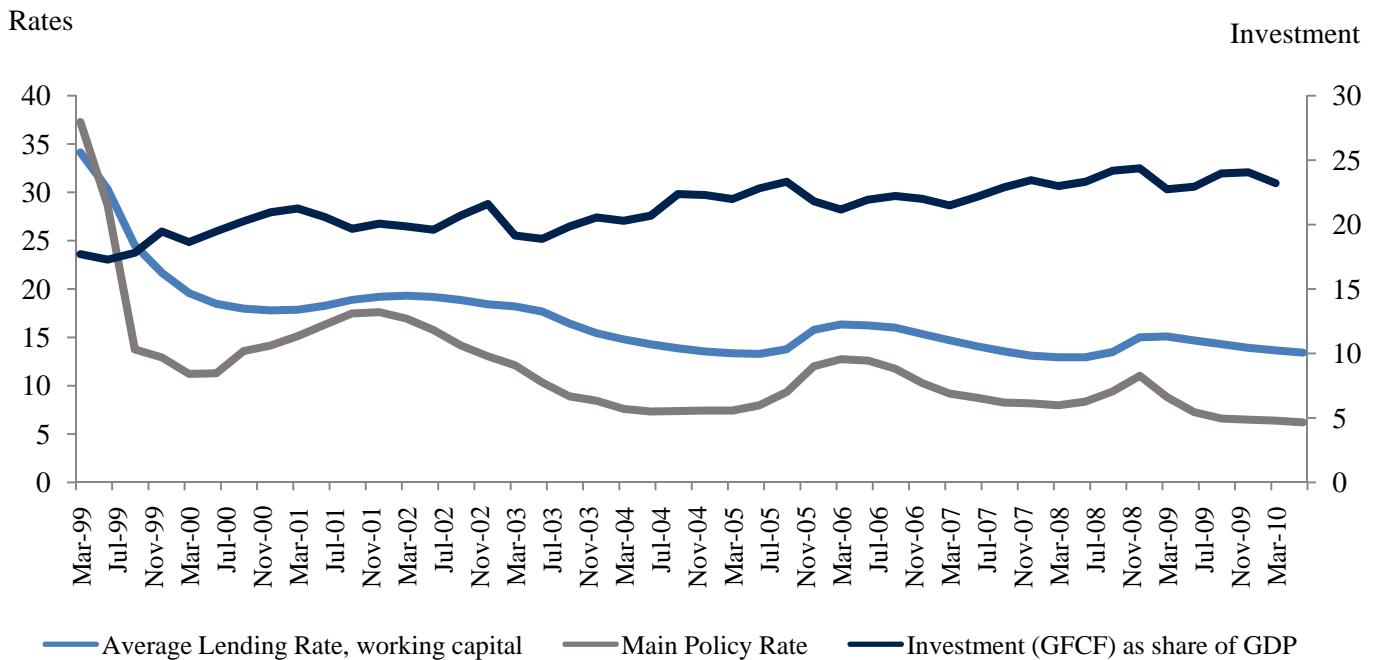
**Chart 7: Indonesia – Government Finances, share of GDP**



Source: FactSet as of 12/31/08

As a result of prudent macro policy, the cost of capital is beginning to decline. Chart 8 shows the average lending rate as a function of the main policy rate that is set by the central bank. The right axis measures investment as a share of GDP, which is beginning to rise. The current government, which has shown remarkable continuity, was just re-elected in October 2009 with an even stronger mandate. As a result, there is more hope that Indonesia will continue its pro-growth policies moving forward.

**Chart 8: Indonesia - Supportive Environment for Growth to Accelerate**



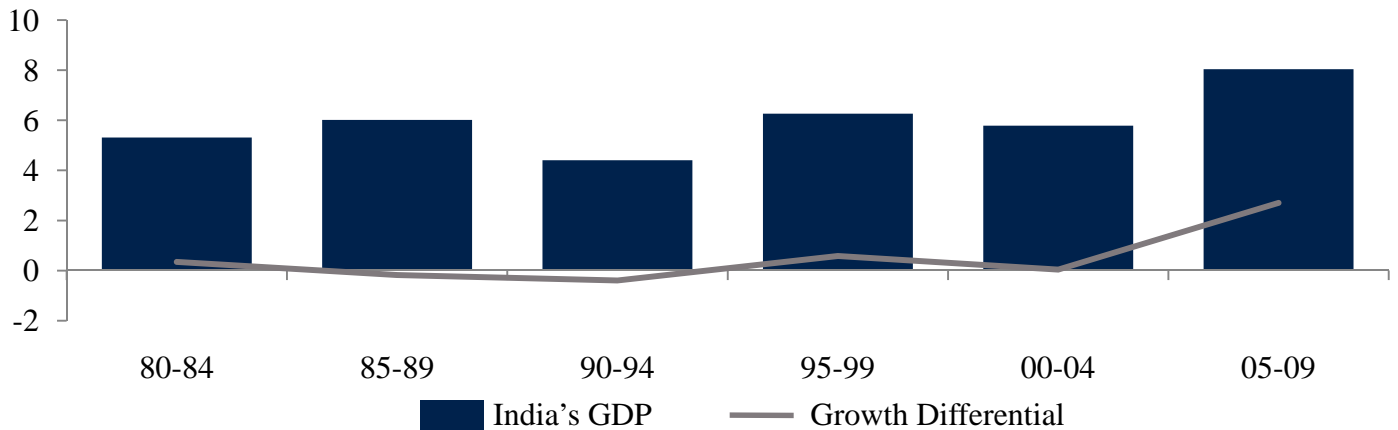
Source: FactSet as of 6/30/10

Indonesia's key ministerial positions are being occupied by capable, Western-educated technocrats who know what they are doing and, more importantly, know what they need to do to remove barriers to faster growth. The political environment is much improved, and the government has shown for the past ten years that they have the discipline, in fact, to do what is necessary to accelerate growth. The Indonesian government is aware that investment, particularly investment in infrastructure - both road and railway, but also power infrastructure - needs to increase and is implementing specific policies to make sure that happens. Because Indonesia still relies to a large extent on foreign capital, the government is seeking to improve public/private partnerships. They have used these structures in Indonesia in the past, but the rules of operation have been so cumbersome that very few private companies have been willing to invest. The government is now looking to change the bidding process, to change the incentives, to increase the return on capital that these companies can have so that investment is increased. On the macroeconomic policy side, if the Bank of Indonesia can increase its relatively weak inflation credibility, we could really see an acceleration of growth in Indonesia on a sustainable basis. They are hoping to announce as early as 2012 a clear inflation target which would go a long way toward policy transparency and keep inflation in the 4% - 6% range. If this is implemented, we could see an acceleration in growth in Indonesia on a sustainable basis.

**India**

What about India? India has been a democracy since 1948, but has not grown above average world growth rates for much of that period. Chart 9 reflects not only India's average growth rates over five-year periods since the 1980s but also its growth differential, adjusting for demographics, vis-à-vis the world.

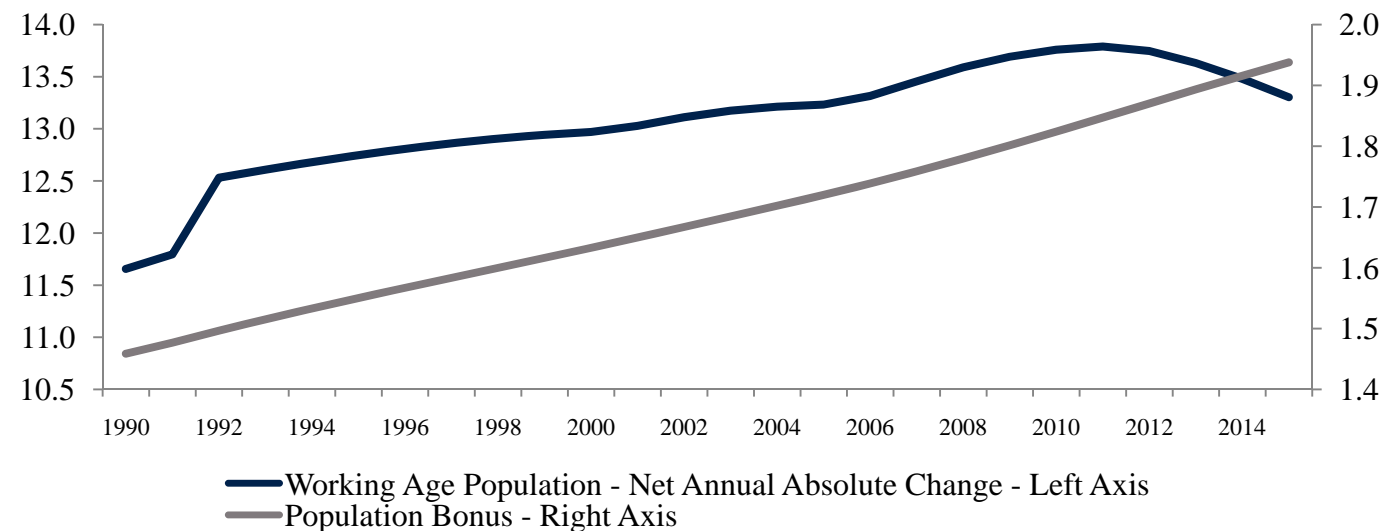
**Chart 9: India – GDP Growth: Actual and Relative to Global Growth Adjusted for Population Growth (%)**



Source: FactSet as of 12/31/09

Only in the 2005-2009 time period has growth in India meaningfully outpaced the world average by about 2.5%. Demographics are looking favorable as well.

**Chart 10: India's Demographic Dividend and Its Growth Impact**



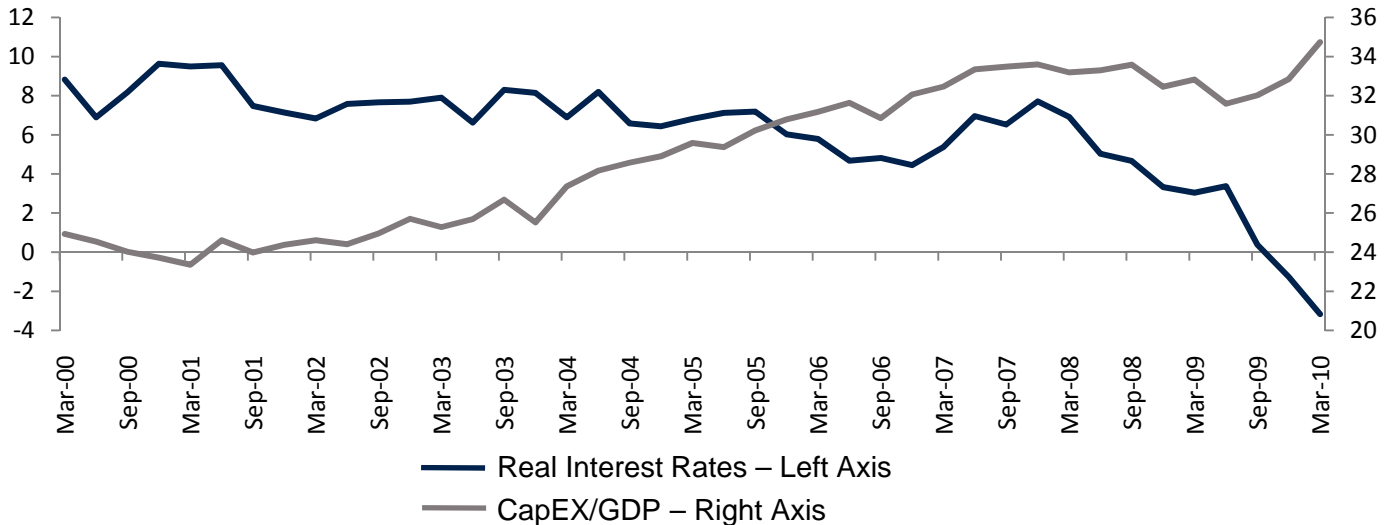
Source: US Census Bureau, 2010

There are many young people in India and that proportion is rising relative to the overall population. If those resources are channeled properly, this could create a boost to growth.



India's macroeconomic policy has also been supportive of growth. There is currently a lot of talk about the Reserve Bank of India being behind the curve and not raising interest rates more aggressively, etc. We would argue that they have actually been quite diligent in keeping real interest rates not only low but negative to facilitate a pickup in investment, which is exactly what has occurred.

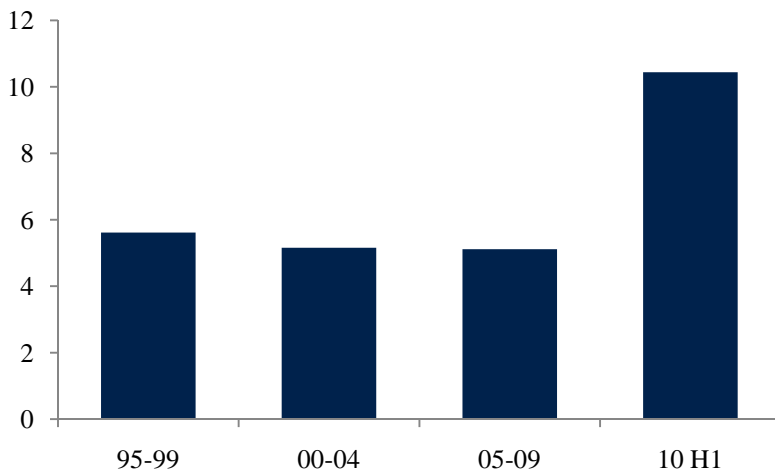
**Chart 11: India – Interest Rates & Investment**



Source: FactSet as of 6/30/10

Investment as a share of GDP over the last six to seven years has increased by about 10%. Now it is closer to 35%, and that is really the driver of growth acceleration. You could argue whether India has reached the point where it can grow at 8% to 9% per year on a sustainable basis because of the inflation situation. As economic capacity expands, that kind of growth rate need not result in ever-higher inflation; but that has not been the case in India yet.

**Chart 12: India – Producer Product Index, Annual Change (%)**



Inflation in India is captured most accurately by producer/wholesale price data. Inflation in India is highly volatile, so to get a sense of trends, we show annual price change in India as 5-year averages on Chart 12. While inflation has fluctuated between 5% - 6% on average over the past 15 years, it accelerated to double digits since 2009, as the Indian economy gained momentum.

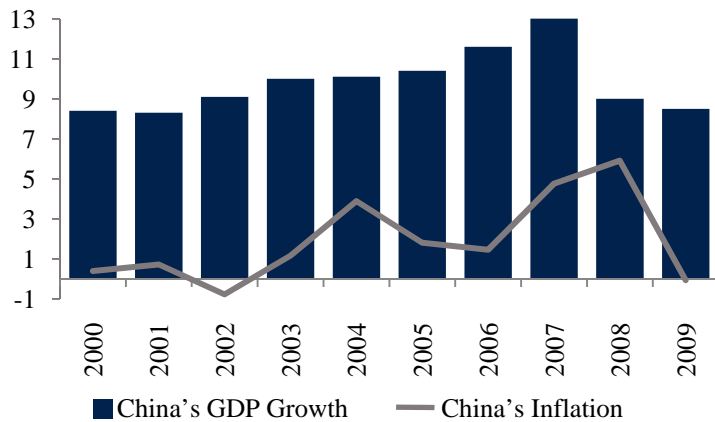
Source: FactSet as of 6/30/10

What is the Indian government doing to sustain rapid growth? Everyone who has traveled to India knows that infrastructure, particularly transport infrastructure, is dreadful. In order to connect a country as large as India, roads need to be built. The government now has explicit targets of how many kilometers of roads per day they want built, and they are moving closer to meeting these targets. Incentives have been put in place to enable private companies to participate in this endeavor meaningfully so that they make decent returns out of building infrastructure in India. That has not been the case until recently. Similarly, the government is trying to encourage investment in renewable energy because India, like China, is largely dependent on coal, and to produce electricity for 1.2 billion people using nothing but coal would be very dirty.

**China**

In China, the case is almost the opposite of India and Indonesia. China has enjoyed more than three decades of unprecedented growth.

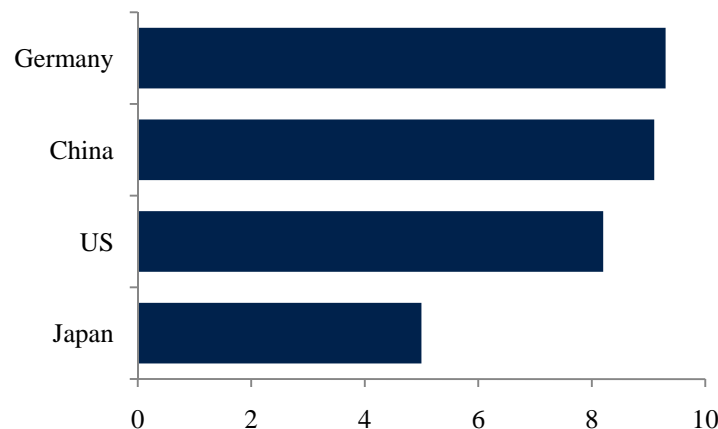
**Chart 13: China – GDP Growth and Inflation (%)**



In the entire period, but particularly since 2000, growth has outpaced inflation. That is almost unheard of in emerging markets. That has not happened anywhere else in the world — not in Latin America, not in Asia, not anywhere. As a result, China's macroeconomic management and its industrial policies deserve a lot of credit for this kind of growth, regardless of what you think of its quality. In the same timeframe, since 1983 to 2008, China became the world's largest exporter.

Source: IMF, World Economic Outlook, 2010

**Chart 14: World's Largest Exporters, Share of Total in 2008 (%)**

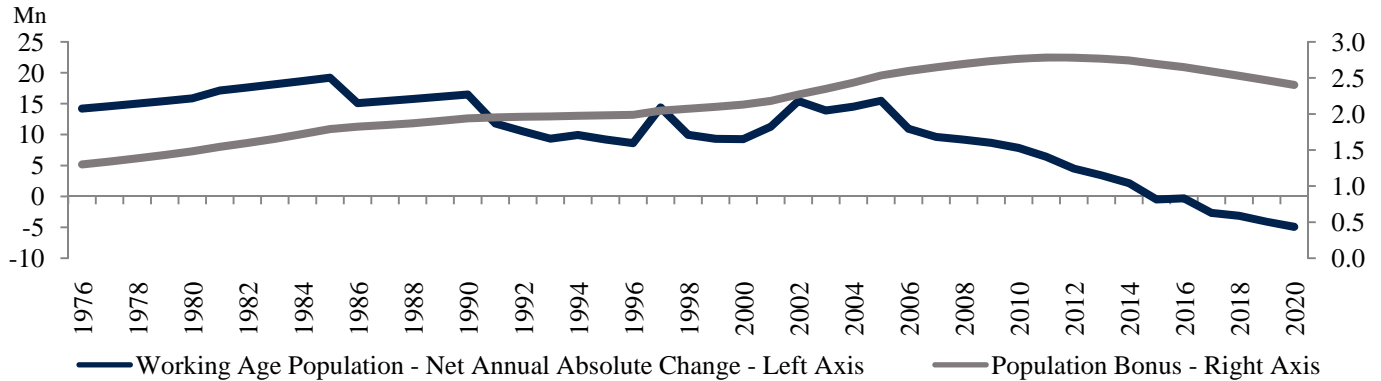


China has recently overtaken Germany as having the largest share of total exports in the world. This is World Trade Organization-based data and; therefore, not controversial. No one is saying that China has achieved the same wealth status as Germany, but given where China has come from in the early 1980s, this progress is pretty remarkable.

Growth in China has been underpinned by favorable demographic trends.

Source: World Trade Organization, 2010

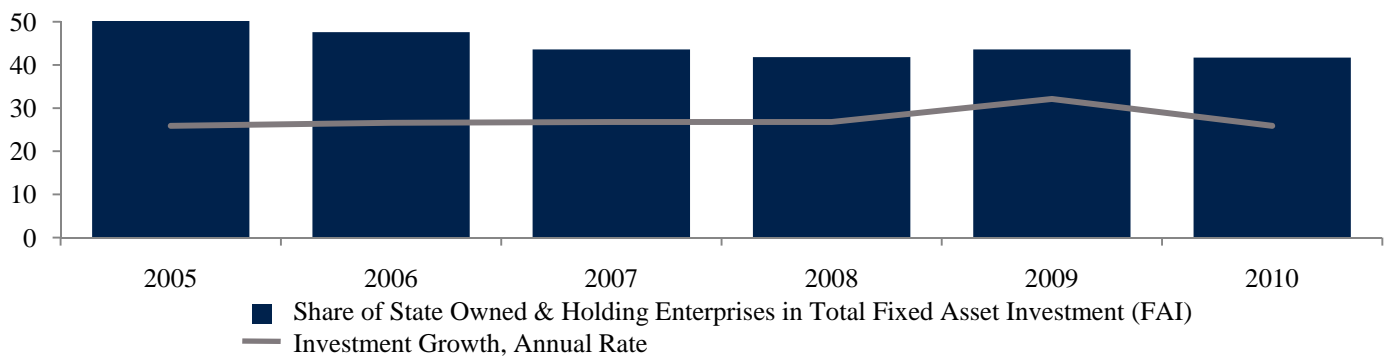
**Chart 15: Demographic Trends in China**



Source: US Census Bureau, 2010

Chart 15 references the net additions of working age population in millions of people per year. The population bonus - the demographic dividend – rose sharply through the 1980s, stabilized, and then in the 2000s picked up again. There was a mini Baby Boom in the early 1980s, and that is what created that uplift in the population bonus in the early 2000s. That also has helped to boost GDP growth and keep wages down: little inflation and high growth. But as evidenced on these charts, these demographic trends are set to reverse. If you are a Chinese leader and you are looking at this, you are not terribly complacent because this spells a slowdown in growth. There have been articles discussing whether or not China can get rich before it gets old, and this is what they are talking about. Because of that, there is a real sense of crisis in the Chinese elite political and economic decision makers. They are not taking anything for granted in order to ensure that China can grow sustainably at about 7.5% to 8.5% per year. Whether they can achieve this kind of transition from 10% + growth to about 8% growth and change the composition of that growth remains to be seen, and we are watching that very carefully. There are some encouraging signs that they are moving in the right direction.

**Chart 16: Who is Investing in China?**

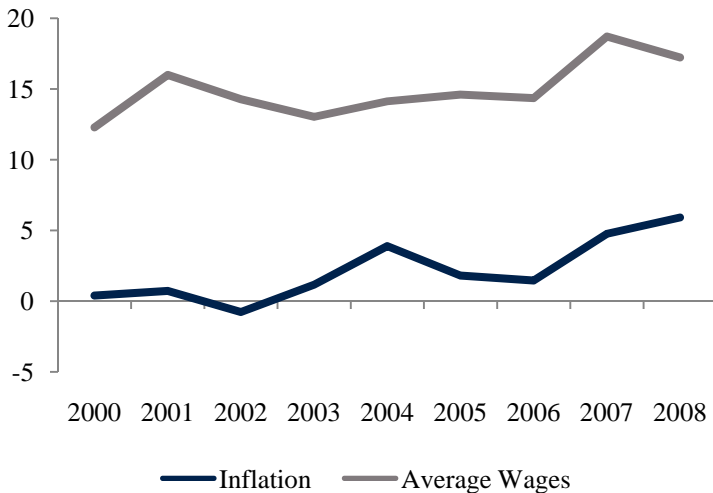


Source: National Bureau of Statistics China

Chart 16 indicates that apart from last year's massive stimulus, by and large the share of private sector investment has been rising as the share of state-owned (SOE), in total fixed investment has been falling, from over 50% in the early 2000s to just over 40% today. This may not seem significant on a year-over-year basis, but over time these effects accumulate.

Similarly, there has been an increasing push to award a larger share of GDP growth to labor at the expense of capital.

Chart 17: China – Annual Price Changes



Income inequality has been rising, and it is partly why consumption in China has lagged. If someone is not making any money, he/she cannot really spend anything. This is not a new phenomenon, as real wage growth in China has lagged productivity growth for quite some time; and this trend, we believe, is set to change if the decision makers are to achieve the transition that they are aiming to achieve. Whether China can transition will remain a dominant theme for the next 12 to 18 months or so, until the markets are beginning to see some results. Currently, the signs are favorable.

Source: National Bureau of Statistics China

In conclusion, emerging markets contribute to just under half of the world's GDP. They represent over 80% of the world's population and only 14% of the global equity markets. The opportunity is pretty sizeable. Over the past decade, Indonesia has successfully restored its macroeconomic environment. It brought down its external and fiscal debts and increased its foreign exchange reserves. That has paved the way for it to potentially lift its growth rate on a sustainable basis. India has begun to finally grow considerably faster than the world average, and its investment as a share of GDP has been on the rise. China has experienced a remarkable decade of over 10% average GDP growth and very low inflation.

In the near to medium term, investors are evaluating whether India's economy can reach 8% annual GDP growth sustainably: in other words, 8% growth with lower or at least moderating inflation. We are evaluating whether Indonesia can see its GDP growth accelerating to 6.5% - 7.5% and sometime down the road to maybe even 8%, and whether China can engineer slower but still very high growth of 8%. Eight is quite a magic number. In Chinese culture, in Mandarin, the word for eight very closely resembles the word for fortune and for money. It is the same thing in Cantonese, so perhaps it is not a coincidence that we are looking for 8% growth in all of these countries.

What are these countries doing to make sure that they get there? India is finally changing its tax and infrastructure investment policies to facilitate growth in the manufacturing and industrial sectors, which have been suffering at the expense of the services sector. The government is hoping to create a favorable environment for productive investments, specifically in infrastructure but really in any kind of investment. Indonesia is likewise investing in infrastructure and is doing so slightly differently. It is creating incentives for private companies to participate and have a bigger share of infrastructure investment spending. China is hoping to address its lagging wage growth with more rapid wage growth than productivity growth and a shift away from export-led growth towards domestic-demand growth. We should still see heavy investment in China but hopefully a bit more consumption as well. The key question for these economies, and to the extent that they represent so much of emerging markets, is whether these countries that represent over 40% of the world's population can grow at about 8% per year.



*The previous content is derived from the transcript of a presentation given by Olga Pomerantz. The Question and Answer portion and Olga's biography are contained on the following pages.*

**Question: What is the availability or lack of the actual natural resources in each of these countries and how will it contribute to or hurt their growth?**

*Olga Pomerantz:* China is notoriously poorly endowed in almost every resource except coal, where it has plenty, and, more recently, in rare earth minerals. China's policy toward resources is commonly linked to what Japan did in the 1980s, but I would argue that it is fundamentally different. China is not just going abroad to secure a supply of resources. It is doing it by securing the resources themselves – they are buying mines. They are building infrastructure to get deposits out of those mines into China, etc. These are long-term national priorities, and that is how they are going about securing resources. They are also trying to find oil in places that we typically do not think of as oil producing countries, and that is true of every other resource as well — iron ore, oil, mineral deposits, gas. China has just secured a massive deal with Kazakhstan to build a LNG pipeline that will deliver gas from Kazakhstan, which is very LNG-rich, directly into China. This is a long-term investment. It does not mean that in ten years time China will be awash with natural gas, but it will contribute probably close to 5% of its electricity needs up from currently about 1% to 2%. India, because it is just literally starting this very rapid industrialization phase that requires a lot of commodities, has really not been the same mover on the international markets for commodities as China has to date. The more that India is growing at 8% rate, the more this is likely to change and sooner. India is rich in coal, but not as rich as China. India is better endowed in resources like water. China has very little water. China has 22% of the world's population and only 7% of the freshwater reserves, so water is a big issue for China. It is not for India, critically, although some are beginning to argue that unabated industrialization will change that. How these two countries vie for resources and commodities will be an important theme moving forward.

Indonesia is very rich in geothermal coal and in other resources. In fact, Indonesia has been an exporter of commodities for many years and more recently even a coal exporter to China. China has only recently started exporting coal. Whether that is going to be a permanent trend or just for a few years remains to be seen. Indonesia's resource situation is a lot better than I would argue either India or China. And while China has formulated a coherent policy to move ahead to acquire these resources, either in developed or developing markets and build the infrastructure necessary to bring them home, India does not yet have a coherent resource policy. It still is buying things on the open market, but that may change.

**Question: Is there any other country that strikes you as particularly attractive or unattractive?**

*Olga Pomerantz:* To me these are by far the most attractive. In general, I think East Asia is a very exciting region. Following the Asian Crisis, it has taken a lot of these countries that have not had much to do with the crisis per se to get out from underneath the piles of debt and debt servicing burdens to get back on track. I think we're starting to see that now. I think Malaysia is starting to wake up. It is showing some tentative signs. Philippines & Thailand (political coup notwithstanding)- I think in the next several years we are likely to see a lot more out of these countries than we have in the past ten years.

**Question: What are your comments about Brazil?**

*Olga Pomerantz:* Brazil is growing, but not as fast as it should given its GDP per capita. Brazil is suffering from chronically poor productivity growth, but it has deep, liquid equity markets which are attractive, which is not the case for a lot of Asian markets. Brazil is rich in natural resources. A tremendous part of Brazil's growth over the past ten years has been supplying resources to rapidly industrializing Asian countries, specifically China. To the extent that story is set to continue, assuming Brazil can invest in things like ports and infrastructure, that tie-in, that coupling, will continue.

**Question: China's growth over the last 10 – 20 years has been the result of manufacturing and outsourcing. That has really improved return on capital to develop all these things. It cuts developed market company costs, but that return on capital has not contributed to local Chinese companies. Do you see that changing in the future?**

*Olga Pomerantz:* This is more relevant for China, but it will become increasingly relevant for India as well. I think Chinese growth may have been a little bit misunderstood. China started at such a low level of development (its GDP per capita in 1978 was something like \$300 per person) and they had virtually no capital stock. To build that kind of capital stock, whatever you think of quality, over 30 years is a massive achievement by any means. So the first 30 years of growth was really all about building capacity to be able to finance China's investment in capital building. Well, they now have done that.

Now the next phase is China 2.0 and what does that mean? It is really going to be about moving up the value chain - not improving the amount of stuff you can make, but the quality of that stuff that you are making. I mean that on every level, from toys to agricultural equipment to heavy machinery. For example, five years ago, China was not installing ultra-supercritical boilers to make electricity. This is at the forefront of technology, and it is now over half of what they are installing. They are moving up the value chain very rapidly, but installed capacity is not going to grow very much from here on out.

The fundamental structural change in the composition of that growth will not only drive the returns on capital of Chinese capital owners but also returns on labor because it requires much more productive, much more high value labor, much better educated labor, etc.

India has really suffered, because of the different tax systems within the different provinces and regions, which is really like having 30 countries in India. If a company exported from one province to the next, it had to pay excise tax at the border. It has taken the government a very long time to change that. They are now moving to one tax policy, which is going to greatly reduce expenses. But more importantly, the old regime really punished the manufacturing sector at the expense of services. This is partly why, apart from the fact that they speak English, which is a nice benefit, India's service industry has really taken off before truly we have seen a manufacturing upsurge. That is going to change. Some of the barriers they have already removed and are in the process of removing and the investment that they are encouraging with negative real interest rates will start to change that. It takes a couple of years to start really seeing that. It will take a little bit longer to see it on the ground, but I think the excitement is already there. Companies are already revising their capital expenditure plans. Small manufacturers are already finding it a lot easier to really get going and to possibly build another plant in a neighboring province, something they would not have contemplated 20 years ago.

It is fashionable to talk about China and India in the same breath. They are not the same, but to the extent that India can continue on its path, I think investors will hear a lot more coming out of India.

**Question: One of the differences that I would like to ask you about between China and India has to do with the Rule of Law. India incorporates British common law, and whether we like the laws or not, there are common law protections for property and you can make investments there relatively safely. China does not have that. The law is much more complicated, and the potential to retain assets once earned is more problematic in China. We constantly see a lot of capital exported to Singapore and places like that. What role do you think this plays into investment in these countries?**

*Olga Pomerantz:* I would argue that China does have a Rule of Law, and it does have some protection of capital for the simple reason that I think the Chinese government has shown itself to be quite pragmatic. While the revolutionary rhetoric is all fine, what they are actually doing is quite different from that. The government understands that its staying power and the degree to which it is able to perpetuate itself will depend on wealth accumulation - more importantly, on wealth distribution so that there is not a situation where 1% of the population controls 90% of the assets. They need the private sector to do that. So to that end, they have been quite good at guaranteeing that you keep what you have earned - on the capital side that is, but in ways that we in the West (a) can not readily see, and (b) do not necessarily identify with. We have a fundamentally different political system. We have a different understanding of what the Rule of Law means, what a contract means, etc. I would argue, however, that just because their system is different does not necessarily mean it does not exist.

They have different rules to be sure, but local players know those rules. It is a little bit more difficult for foreigners, and they do need to hire a lot of local help to be able to navigate both the legal and the political system, but those rules are in place, and they have been guaranteed. I would argue that this is a longer-term challenge - but sometime over the next 20 years, China has to address its legal system. I know that they are aware of that. They are studying legal systems around the world, and they are trying to figure out what would work for them and how to move in that direction incrementally but consistently.

In India it is a lot more transparent and a lot closer to what we would identify as the Rule of Law. It is more similar to our norms, as they inherited the British system of government effectively. There is a degree of debate as to how suitable that has been for India because in effect what exists is 100 to 150 or so million people for whom that system really works and about 900 million or so who are completely outside of it. While we understand its principles, for a developing country that is as poor as India, you could easily argue that it is just as inappropriate as the Chinese system is for us. Both have their issues; and I think they will both evolve with their economies. If they do not evolve, then forget 8% growth. We are going to have bigger problems. However, I would broaden it a little to say that the Rule of Law has different interpretations and different implementation in different cultures.

**Question: Please comment on the imbalance in gender demographics in China and its implication.**

*Olga Pomerantz:* I purposely did not address it because it is quite scary. Sometime over the next ten years there are going to be 30 to 40 million more Chinese men than women. This has tremendous social implications. How they are going to address that is anybody's guess. I can tell you already just anecdotally, in Northern China there is a tremendous push to emigrate north into Eastern Russia and to seek brides there. Some people settle there, form new families. Some come back into China with their Russian wives. We may see more of that, but the question is of magnitude. There is just not that big of a supply of excess women in Mongolia or in Russia, so this is going to be a problem. How they are going to address it, I have no idea, and I do not think they do either.

**Question: Along the same lines, if there is a gender problem, there is a population growth problem. Their culture is such that the generation that is able to work supports the older. If there is one child and he is supposed to support two parents and possibly some grandparents, now there are 30 million excess men, where are you getting your workforce? How is this economy going to continue to grow or are they going to begin to call in their debts?**

*Olga Pomerantz:* The demographic problem is not imminent. This is from 2035 or so onwards. Some of it is a question of timing, and it goes back to that question, can China become wealthy before it grows old? This is why the leadership is really approaching this issue as a crisis. They are not complacent by any means on any level of government. Beyond that, as the economy in China is growing and is becoming wealthier, provision of social services will become better. Last year they had an 800 billion renminbi, rural healthcare plan rolled out. The first impression is that it has been quite successful.

Obviously, in order to have that, you need to build a certain number of hospitals, you need to have a certain number of doctors. So this is another value-creating part of the economy. They are investing very heavily in R&D and in schooling, so more and more people are going to have college and beyond educations. It is becoming mandatory for both boys and girls to attend the first 9 years, but now they are moving into even a K-12 grade system. They have a different education system, but basically one comparable to something like that. They are aware of these problems, and they are doing something about them. But, yes, I would say provision of social services, both in healthcare and education but then also on the other end, in pensions, etc. is going to be very important.



### **Olga Pomerantz**

Olga Pomerantz joined William Blair & Company in 2009. She is responsible for economic research across all regions and sectors. Prior to joining the firm, Olga was a Senior Economist at the National Institute of Economic and Social Research in London, UK, where she was responsible for macroeconomic forecasting and thematic research projects for international organizations and government bodies. Education: B.A., University of Chicago; M.S.c Economics, London School of Economics and Political Science.

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