

Kyklos Capital

The Current State of Frontier Markets

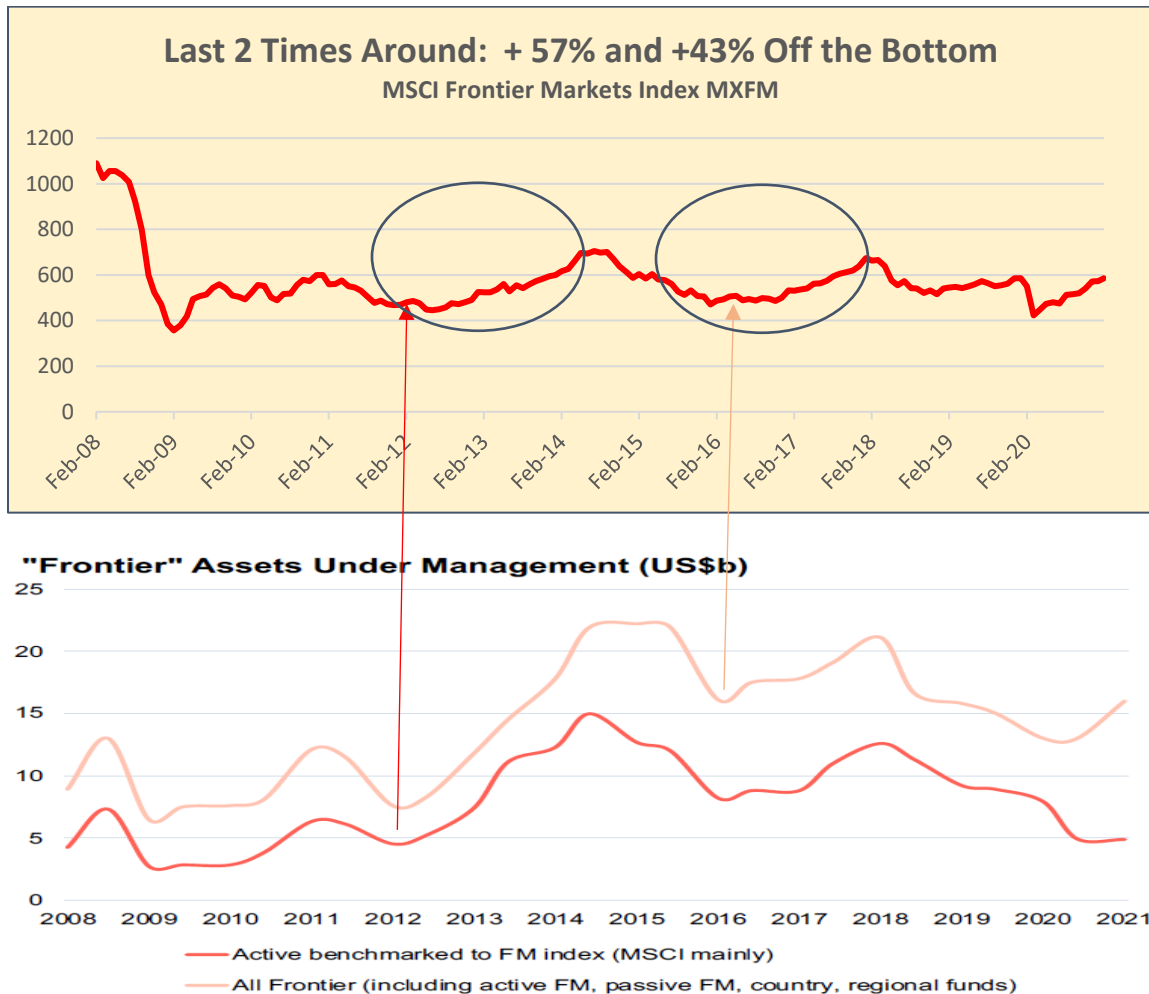
"History does not repeat itself, but it often rhymes." Mark Twain

Foreign investors come and go in Frontier equity markets, because they can, unlike local individuals and institutions that tend to focus on their home market. As a result, foreign buying and selling in Frontier equities drives prices. So what is the latest state of play for foreign investors in Frontier?

Foreign equity investors have already sold their Frontier market assets. Foreign-owned Frontier equity assets total about \$16 billion, including active, passive, ETF and other funds. This is tiny, equivalent to about ½ the assets in a single Emerging market fund, the iShares MSCI Emerging Markets ETF, or about a single day's trading volume in Apple. Even smaller is the portion run by the active managers, who pick stocks as well as countries, at only about \$5bn. Rubbing salt into the wound, the investors in those funds have continued to sell through late 2020 despite strong returns in the second half of the year.

Of course, investing at the *end* of a long selloff is usually a good strategy. An investor who bought the MSCI Frontier Markets Index the last time ownership by active funds was this low, in 2012, would have pocketed +57% over two years. Buying back in 2016, when the total of all foreign fund assets last matched current levels, would have earned +43% over two years (below). Past returns do not guarantee future returns, but we see continue to see opportunity.

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Source: EPFR, Tellimer Research

A Quick Followup on Sri Lanka: As we mentioned in our January letter, we exited our last Sri Lanka position after its strong performance, and we pointed to the disconnect between Sri Lanka's bullish local equity investors and bearish bond investors. As it happens, the MSCI Sri Lanka Index returned a negative -11% in February. We are on the sidelines for now.

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