

Mirae Asset Global Investments



Seven Reasons to Consider Emerging Markets

About Mirae Asset Global Investments

Mirae Asset Global Investments manages investment strategies for clients across the globe. With approximately \$45 billion in total assets under management (as of September 30, 2011), we are driven by a global network of on-the-ground investment professionals, engaging in a fundamentally driven, research-intensive investment approach. Our global team of over 650 employees includes over 125 investment professionals based in Hong Kong, Korea, India, Brazil, Taiwan and the United States.

Seven Reasons to Consider Emerging Markets

Summary

Emerging markets offer more investment opportunities than developed economies in terms of economic growth potential. We believe there are seven reasons for this:

- **Higher personal savings rates:** Higher rates enable self-financing of capital expenditures to enhance economic productivity and encourage private consumption expansion in the future.
- **Demographic opportunities:** A higher youth dependency ratio, a lower elderly dependency ratio and a higher working-age ratio predict significant demographic dividends.
- **Undervalued currencies:** Currencies that are undervalued increase the competitiveness and profitability of emerging market products and companies, while also allowing future currency appreciation gains from investing in emerging market assets.
- **Healthier public-sector balance sheets:** A low government debt-to-gross-domestic-product (GDP) ratio allows for the use of additional instruments to boost economic growth, which is in sharp contrast to the current situation in developed market economies.
- **Enhanced sovereign credit quality:** Increased transparency and significantly lower country risk have led to sovereign debt ratings upgrades, many to investment-grade status.
- **Growth potential in equity markets:** Equity market capitalization-to-GDP ratios have been lower than in developed markets, despite the significant outperformance of emerging markets during the last decade.
- **Underrepresented equity markets in global portfolios:** Underdeveloped equity markets in emerging economies have been significantly underweight in global investors' portfolios.

Slow growth and heightened uncertainties in the developed world may reduce the appetite for emerging market investments, although we believe this trend will be short-lived. In the long run, strong economic fundamentals and underrepresentation in global financial markets should attract investors to the asset class.

Seven reasons to consider Emerging Markets

THE TERM “EMERGING MARKETS” HAS BECOME COMMON in the investment world as a conceptual tool used to describe countries sharing similar characteristics in economies and financial markets over a certain period of time. Yet there is no one, commonly accepted definition of an emerging market, although index providers MSCI and FTSE each use a distinct set of criteria to classify certain countries this way.

For us, a true emerging market is an underrepresented country in the global financial markets with extraordinary economic growth potential. The list of emerging market countries is ever-evolving, as economies continue to mature and expand. Some investors may associate the asset class with higher economic growth rates, while others may reference higher volatility in emerging equity markets. In the long run, we believe that global financial markets will fully reflect the fundamentals of the emerging market economies.

In this paper, we present seven defining characteristics of emerging markets: higher personal savings rates, demographic opportunities, undervalued currencies, healthier public-sector balance sheets, enhanced sovereign credit quality, growth potential in equity markets and underrepresented equity markets in global portfolios. These fundamental and structural factors are common across emerging markets, with few exceptions. Short-term and tactical investment decisions may be influenced by cyclical or idiosyncratic factors, but we believe that these seven factors will continue to be reasons why individuals should consider investing in emerging markets.

In the long run, we believe that global financial markets will fully reflect the fundamentals of the emerging market economies.

An increase in capital expenditures can help produce a higher capital-to-labor ratio, faster labor productivity growth and, ultimately, economic growth, all other things being equal.

Higher Personal Savings Rates

More savings means less consumption. While this may decrease economic growth in the short term, a strong, positive correlation exists between higher savings rates and economic growth. This phenomenon has been widely observed and accepted¹ across countries globally.

In the long run, higher savings rates are crucial for economic expansion because they enable more capital investment, which is imperative for a developing economy.² An increase in capital expenditures can help produce a higher capital-to-labor ratio, faster labor productivity growth and, ultimately, economic growth, all other things being equal. Countries can finance their capital investments from international financial markets, rather than by increasing domestic savings, but this presents a risk of currency instability and devaluation, thus increasing systematic risk of the economy. In a poor country with limited advanced technology, domestic savings are essential for technological innovation. Local banks are able to monitor local projects that adapt such technology, which eventually leads to faster economic growth.³

As shown in the top graph on page 5, the average personal savings rate in emerging markets is 18.9%, much higher than the developed market average of 9.7%. Some argue that high personal savings rates in emerging markets may reflect the lack of a social security system, thereby creating a higher dependence on “self-insurance.”⁴ While this is true to some extent, it is also true that increased savings rates can lead to an acceleration of capital formation, higher labor productivity, more technological innovation and faster economic growth.

Furthermore, higher savings indicate higher household consumption in the future, yet another reason why we believe that higher personal savings rates are crucial for future economic expansion. Emerging market countries with high savings rates will enjoy higher private consumption-to-GDP ratios in the future.

The developed world, however, does not enjoy the higher personal savings rates and lower ratios of private consumption to GDP of emerging markets, although Brazil and Russia are anomalies, as seen in the bottom graph on page 5. Consumers in developed markets are struggling to deleverage their household balance sheets via higher saving rates.

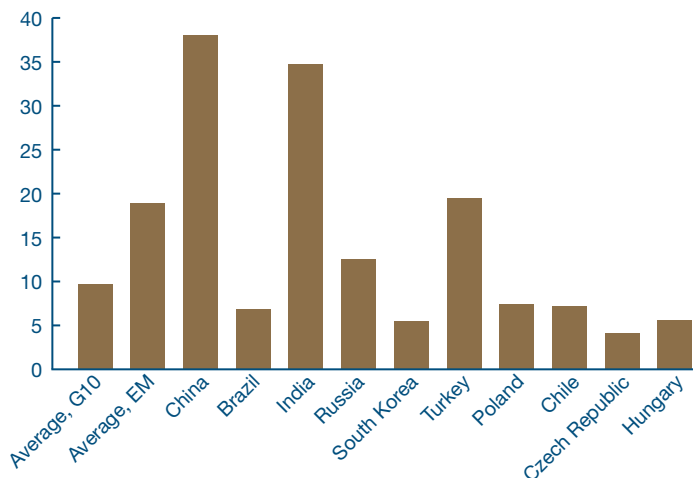
¹Some say that higher expected economic growth induces higher savings rates, and not the other way around, but a long-term, positive relationship between savings and growth is still accepted. “Savings and Growth with Habit Formation,” Carroll, Overland and Weil, *American Economic Review* (2000).

²Economic theory states that higher savings rates allow for increased levels of investment. Income that is not being spent on consumer goods and services can instead be invested in fixed capital, such as land or machinery, which ultimately contributes to economic growth.

³“When does domestic saving matter for economic growth?” Aghion, Comin, Howitt and Tecu, Harvard Business School Working Paper 09-080.

⁴“The puzzle of China’s rising household saving rate,” Prasad, Liu and Chamon, www.voxeu.org, January 2011.

PERSONAL SAVINGS RATE

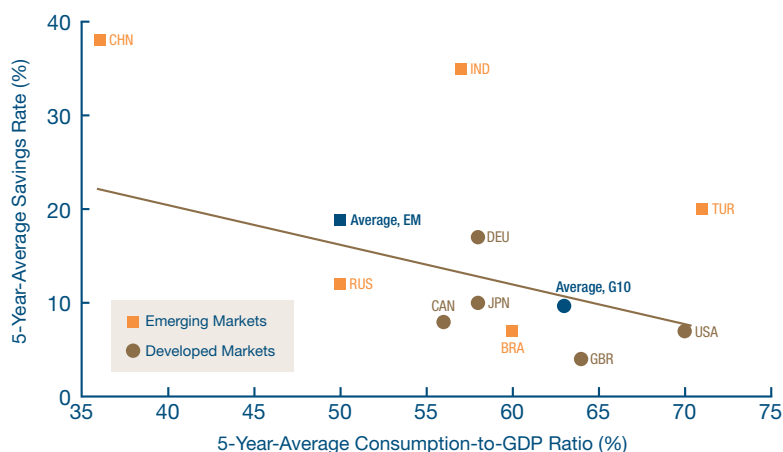


Source: Bloomberg Businessweek, OECD

5-year-average savings rate is calculated using the most recent 5 years of data available for each country. G10/EM average personal savings rate is the GDP-weighted average of those countries that provide annual personal savings rates.

G10 Countries: Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Switzerland, UK, and U.S.

PERSONAL SAVINGS vs. CONSUMPTION



Source: Bloomberg Businessweek, OECD, World Bank

5-year-average savings rate is calculated using the most recent 5 years of data available for each country. Consumption-to-GDP ratio uses the most recent full year of available data. Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

	5-Year-Average Consumption-to-GDP Ratio (%)	5-Year-Average Personal Savings Rate (%)
G10 Countries	63.2	9.7
Emerging Markets	50.0	18.9

Higher savings indicate higher household consumption in the future, yet another reason why we believe that higher personal savings rates are crucial for future economic expansion.

Countries with larger working-age populations are also likely to have higher-than-average household savings rates, which facilitate the financing of domestic investments in fixed assets and social infrastructure.

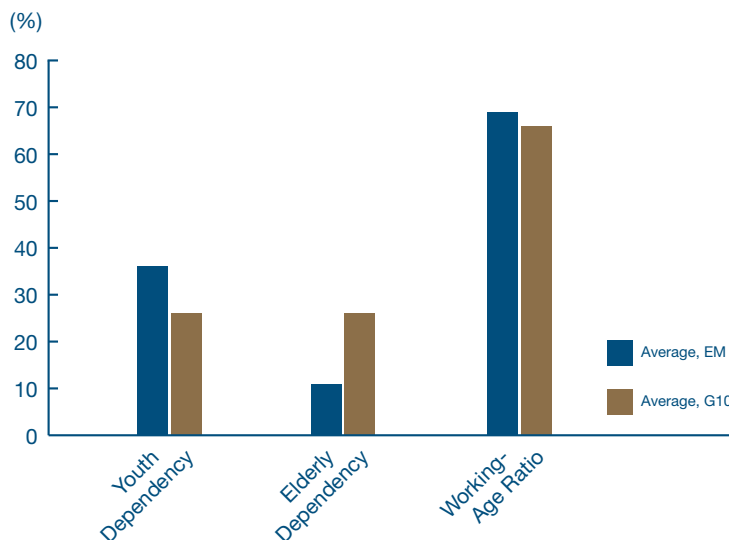
Demographic Opportunities

In a previous white paper entitled “Demographics in Emerging Markets: Hope or Hype?” (April 2011), we discussed the opportunities that emerging market countries have in terms of demographic structure. In this paper, we introduce three statistical measurements that we believe are relevant when discussing the long-term relationship between demographics and economic growth, and how emerging market countries are positioned in terms of these measurements.

The demographic advantage, in this case, is not population size or growth. Rapid population growth by itself neither promotes nor impedes economic growth. Instead, the key is the age structure of a population.⁵ We believe that countries with a 1) higher youth dependency ratio, 2) lower elderly dependency ratio and 3) higher working-age ratio are well-positioned for future consumption and economic productivity. These metrics indicate what is known as the “demographic dividend.”⁶

A person's propensity to save is highest during the working years of his or her life. Both the young and the elderly are forced consumers due to the lack of a regular income that can contribute to savings. Therefore, countries with larger working-age populations are also likely to have higher-than-average household savings rates, which facilitate the financing of domestic investments in fixed assets and social infrastructure. This further supports economic and per capita income growth.⁷

DEMOGRAPHICS



Source: CIA World Factbook, 2010
Averages are population-weighted.

⁵“The Demographic Dividend – A new perspective on the economic consequences of population change,” Bloom, Canning and Sevilla, RAND, 2007.

⁶The demographic dividend is a theory proposing that as countries transition from largely agrarian societies with high fertility and mortality rates to more urban societies with lower fertility and mortality rates, the working-age population will grow more rapidly than the population dependents, creating resources for investment in economic development and, all other things being equal, increasing per capita income growth. Source: *What is the Demographic Dividend?* Lee and Mason, International Monetary Fund, 2006.

⁷Source: “Demographics in Emerging Markets: Hope or Hype?” Mirae Asset, April 2011.

In addition, youth dependency plays an integral role in shaping a future labor force. An increased youth population implies higher future labor input, as the overall size of the workforce will increase as the youth reach working-age status. As the size of the labor force of a country increases, the productivity of its economy should also increase, as there are fewer dependents to support and more working-age people who are productive, both of which drive economic growth. In our view, labor input should increase with a younger population, as youth are better able to adapt new education and technology to increase efficiency.

As shown in the graph on page 6, the populations of emerging market countries generally have higher youth dependency and working-age ratios, while less of a dependency on the elderly. This is in sharp contrast to the structure of populations in developed nations.

Undervalued Currencies

It is widely accepted in the financial industry that emerging market currencies are fundamentally undervalued relative to developed market currencies.⁸ In our July 2011 white paper entitled “The Global Middle+ Class in the Emerging Markets: The Growth Has Only Begun,” we introduced purchasing power parity (PPP) rates of emerging market currencies and the magnitude of market exchange rate mispricing when compared to the actual purchasing power of those currencies.

The merits of undervalued currencies are twofold. First, an undervalued currency helps local products compete in global markets because their prices are attractive relative to the prices of other countries’ goods. This often leads to a trade account surplus on the macroeconomic level and high profitability of local exporters, all other things being equal. Undervalued currencies can also act as a catalyst for higher economic growth rates, particularly in developing countries via higher profitability of their exports.⁹ As shown in the graphs on page 8, emerging market currencies are undervalued¹⁰ by an average of 38%, while the corresponding countries are enjoying trade account surpluses and high economic growth.

From an investor’s perspective, the other advantage of market exchange rate mispricing is the potential gain from currency appreciation, as undervalued emerging market currencies will likely strengthen going forward. Emerging market currencies, of course, can go through periods of high volatility, given the low risk appetite for the asset class in times of turmoil across developed markets. If the so-called “flight to safety”¹¹ trend prevails, emerging market currencies may even depreciate further against major hard currencies, such as the U.S. dollar. That being said, emerging market currencies are likely to appreciate in the long run, barring sustained domestic inflation, because they are deeply undervalued.

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⁸See <http://www.marketwatch.com/story/most-emerging-market-currencies-undervalued-2011-07-18>.

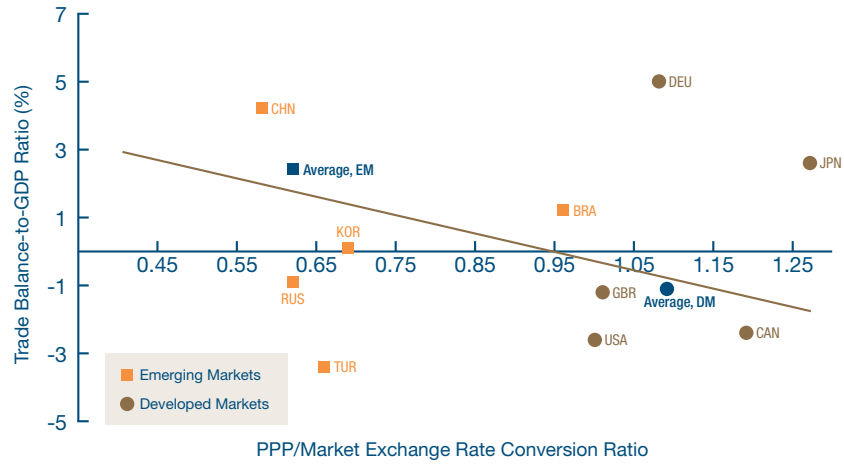
⁹“The real exchange rate and economic growth,” Dani Rodrik, Brookings Papers on Economic Activity, October 2008.

¹⁰One exception is Brazil, where nominal exchange rates against the U.S. dollar declined almost 40% since December 2008 before turning around in August 2011.

¹¹Investors move capital into assets that are perceived to be less volatile during a period of market uncertainty.

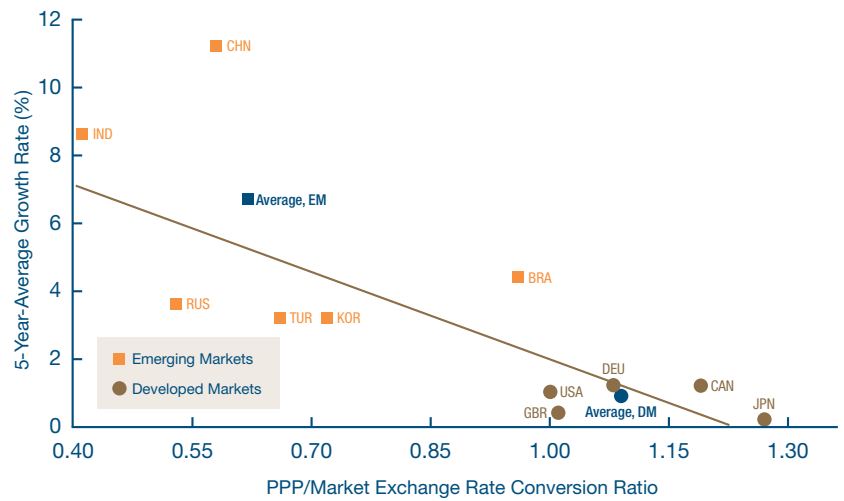
An undervalued currency helps local products compete in global markets because their prices are attractive relative to the prices of other countries' goods.

EXCHANGE RATE vs. TRADE BALANCE



Source: IMF, World Bank, most recent full-year available data
 Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.
 Note: The lower the PPP/market exchange rate conversion ratio is, the more the currency is undervalued.

EXCHANGE RATE vs. GDP GROWTH



Source: IMF, World Bank, most recent full-year available data
 Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

	PPP/Market Exchange Rate Conversion Ratio	Trade Balance-to-GDP Ratio (%)	5-Year-Average Growth Rate (%)
Developed Markets Average	1.09	-1.1	0.9
Emerging Markets Average	0.62	2.4	6.7

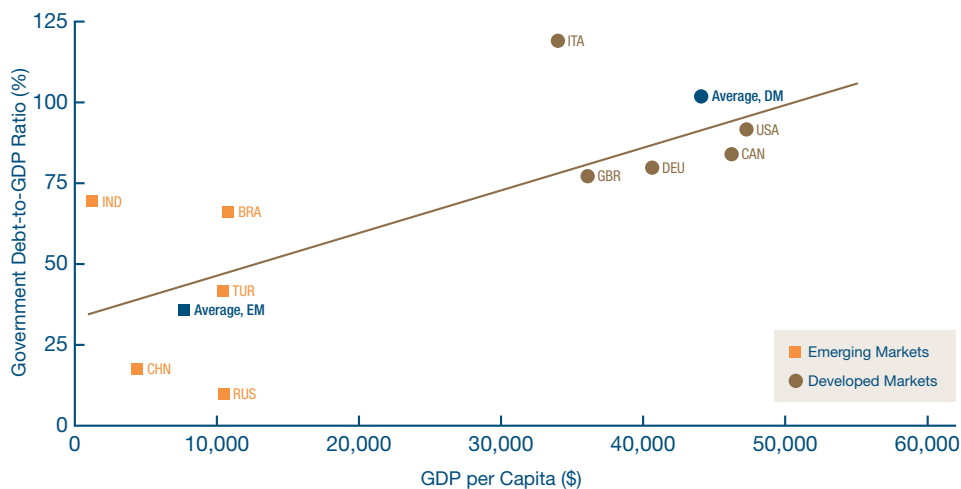
Healthier Public-Sector Balance Sheets

One of the greatest difficulties that developed economies are facing now is the deteriorating fiscal situation of their governments. If a nation's balance sheet is not healthy, whatever the reason, it can create an extra burden for the already struggling economy. According to empirical research conducted by the European Central Bank (ECB), if a government debt-to-GDP ratio is above the threshold of 90-100%, it will have a negative impact on economic growth.¹² In fact, the detrimental effects may even begin at levels as low as 70-80% of GDP. On the contrary, government can help promote, or at least avoid hampering, economic growth with sound fiscal policy and a healthy balance sheet. There are various routes administrations can take to achieve fiscal health, such as introducing incentives for increasing entrepreneurship, providing social infrastructure and financing long-term projects.

Emerging market countries have much healthier balance sheets than their counterparts in developed markets. As shown in the graph below, the average government debt-to-GDP ratio in emerging market nations is only 35.8%, compared with the developed market average of 101.7%. Using developed markets as a benchmark, the demand for social security will increase as emerging markets mature, and the debt-to-GDP ratio will inevitably increase in the long run as a result. However, this shift will take time. Over the next few decades, at least, we expect stronger fiscal conditions across the emerging market countries relative to the developed world.

There are various routes administrations can take to achieve fiscal health, such as introducing incentives for increasing entrepreneurship, providing social infrastructure and financing long-term projects.

GDP vs. GOVERNMENT DEBT



Source: IMF, World Bank, most recent full-year available data

Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

¹²"The impact of high and growing government debt on economic growth – An empirical investigation for the euro area," Working Paper series No. 1237, August 2010, European Central Bank.

Equity investors are most concerned with the fundamentals of specific companies and not merely with the probability of default of the country in which the companies operate or are domiciled.

	GDP per Capita (\$)	Government Debt-to-GDP Ratio (%)
Developed Markets Average	44,078	101.7
Emerging Markets Average	7,744	35.8

Enhanced Sovereign Credit Quality

Traditionally, investing in emerging markets has been associated with substantial risks, such as default, increased volatility, low transparency, geopolitical instability and less convertibility of local currencies. Such risks were often reflected as low credit ratings of emerging market sovereign debt.

In the past, there was a vast difference between the credit ratings of developed market economies and those of emerging market countries. In 1990, all of the 24 MSCI developed world constituents had investment-grade credit ratings,¹³ compared with only five out of 21 MSCI Emerging Markets Index members. However, sovereign ratings of emerging economies have improved significantly, as shown in the table on page 11. In the year 2000, 11 of the MSCI Emerging Markets Index members could claim investment-grade status, but today the number has increased to 17. Sovereign ratings improved in 81% of MSCI Emerging Markets Index member countries over the past decade.¹⁴ While credit quality in developed market countries is still higher, on average, than in emerging market countries, the debt ratings of seven developed nations have been downgraded since 2000, including those of the United States and Japan.¹⁵

Of course, a higher sovereign rating does not automatically encourage more equity investment in that specific emerging market country, nor does it guarantee higher equity returns. For instance, research finds that the flow of international equity tends to respond sharply to sovereign credit rating downgrades, but investors have not been particularly enthusiastic to upgrades.¹⁶ This phenomenon is not especially surprising. Equity investors are most concerned with the fundamentals of specific companies and not merely with the probability of default of the country in which the companies operate or are domiciled.

That being said, the enhanced credit ratings of emerging market countries reflect the fact that the risks involved in emerging market equities have been significantly reduced during the last decade. This is a nontrivial conclusion, as higher sovereign credit ratings will make global investors feel more secure in these markets.¹⁷ It is particularly important that the sovereign debt ratings of 17 of the 21 MSCI Emerging Markets Index member countries have reached investment-grade status, as this is critical in reducing the financing costs of emerging market governments and companies.¹⁸

¹³Credit rating must be BBB- or higher to be considered investment grade.

¹⁴Standard & Poor's, August 31, 2011.

¹⁵As of August 31, 2011, Greece, Ireland, Italy, Japan, Portugal, Spain and the United States were all downgraded relative to their ratings in the year 2000.

¹⁶"Sovereign credit ratings, transparency and international portfolio flows," Gande & Parsley, April 2007. The authors analyzed sovereign credit rating changes in 85 countries between 1996 and 2002.

¹⁷There is no guarantee that any strategy will be successful. All investing involves risk, including potential loss of principal.

¹⁸"Sovereign credit ratings and spreads in emerging markets: does investment grade matter?" IMF Working Paper, WP /11/44, March 2011.

S&P LONG-TERM FOREIGN CURRENCY SOVEREIGN DEBT RATING

	1990	2000	Current
Brazil	NR*	B+	BBB-
Chile	NR	A-	A+
China	NR	BBB	AA-
Colombia	NR	BB	BBB-
Czech Republic	NR	A-	AA-
Egypt	NR	BBB-	BB
Hungary	NR	BBB+	BBB-
India	BBB	BB	BBB-
Indonesia	NR	SD**	BB+
South Korea	A+	BBB	A
Malaysia	A-	BBB	A-
Mexico	NR	BB+	BBB
Morocco	NR	BB	BBB-
Peru	NR	BB	BBB+
Philippines	NR	BB+	BB
Poland	NR	BBB+	A-
Russia	NR	SD	BBB
South Africa	NR	BBB-	BBB+
Taiwan	AA	AA+	AA-
Thailand	A-	BBB-	BBB+
Turkey	NR	B+	BB

Source: Standard & Poor's, August 31, 2011

*NR: not rated

**SD: selective default

Description of Standard & Poor's rating system may be found in the Appendix on page 16.

Growth Potential in Equity Markets

The connection between the size of equity markets and the size of the economy is complex. A higher economic growth rate does imply a larger market capitalization over the long term, but various factors can affect this relationship. For one, different countries have different compositions of equity and fixed income markets, based on their national institutions. For instance, the stock market in Germany has a relatively small market capitalization of \$1.38 trillion,¹⁹ which is due in part to the well-developed commercial banking industry and bond market in that country. In addition, companies may choose to list on a foreign stock exchange,²⁰ a common practice in emerging markets. Foreign-listed companies will contribute to the growth of domestic economic activities, as measured by GDP, but the company

¹⁹Bloomberg; U.S. market capitalization currently \$14.76 trillion.

²⁰The percentage of overseas companies is high in the Hong Kong, Switzerland and Singapore stock exchanges. "Alternative measures of the size of the stock market," Research paper 27, Nov 2005, SFC, Hong Kong.

If the situation in developed markets can be used as a benchmark, we can expect the market capitalization-to-GDP ratio to increase in emerging markets as those economies mature.

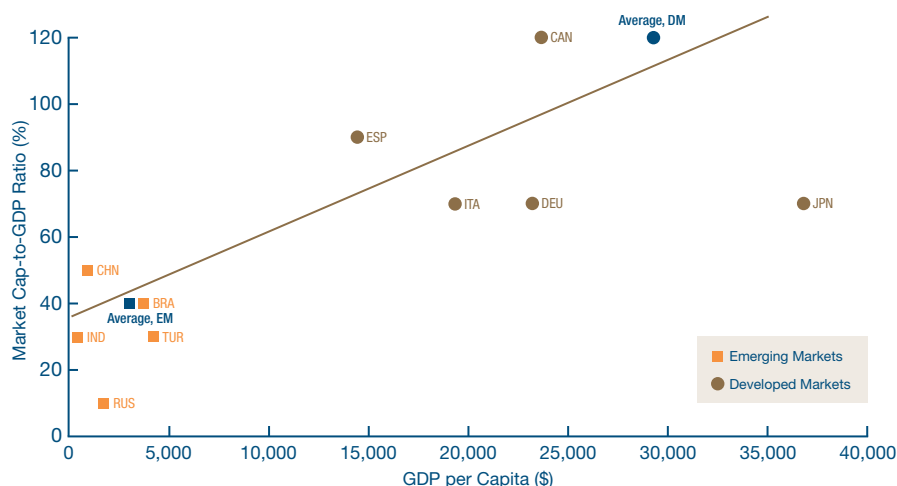
will not be represented in the country's market capitalization. Chinese companies, for example, often list some of their shares on the Hong Kong Stock Exchange, while simultaneously floating their shares on mainland Chinese exchanges. In 2010, H shares²¹ and red chip²² stocks accounted for more than 45% of the Hong Kong Stock Exchange market capitalization.²³

Similarly, new public stock issuance and the privatization of national companies can increase market capitalization significantly, although there is no corresponding effect on the contribution to positive GDP growth.

Even after taking into consideration factors that may skew the equity market capitalization-to-GDP ratio, there are two conclusions. First, the ratio is significantly higher in developed markets, despite the significant outperformance of emerging equity markets over the last decade. The MSCI Emerging Markets Index has returned 13.6% per annum over the past ten years, versus 1.7% per annum for the MSCI All Country (AC) World Index during the same time period.²⁴ Second, if the situation in developed markets can be used as a benchmark, we can expect the market capitalization-to-GDP ratio to increase in emerging markets as those economies mature.

	Market Cap-to-GDP Ratio — 2000 (%)	Market Cap-to-GDP Ratio — 2011 (%)
Developed Markets Average	119.7	87.1
Emerging Markets Average	37.2	70.0

MARKET CAP-TO-GDP RATIO vs. GDP PER CAPITA, 2000



Source: IMF, World Bank, 2011

Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

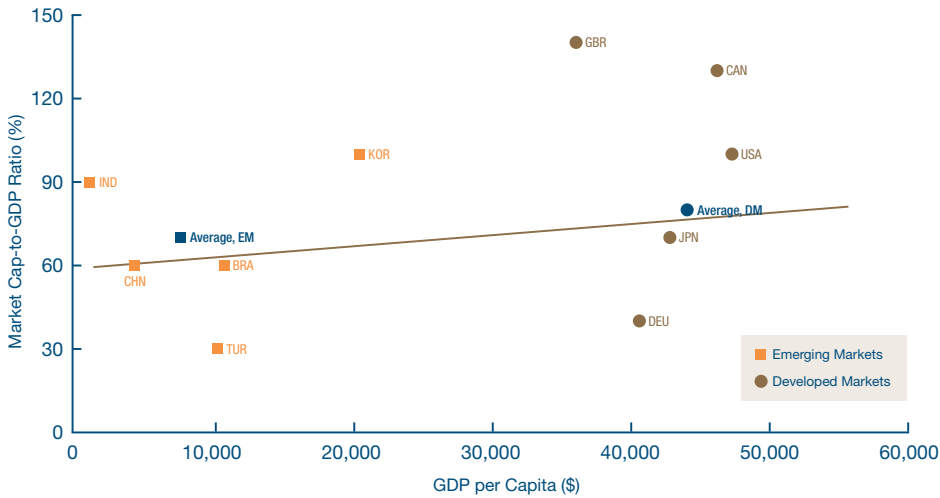
²¹Shares of mainland China-incorporated companies that are traded on the Hong Kong Stock Exchange.

²²Shares of Chinese-affiliated companies that are incorporated outside of mainland China.

²³Source: Hong Kong Stock Exchange.

²⁴As of September 12, 2011.

MARKET CAP-TO-GDP RATIO vs. GDP PER CAPITA, 2011



Source: IMF, World Bank, 2011

Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

A mathematical example helps to illustrate the potential growth of emerging market equity markets. Suppose the market capitalization-to-GDP ratio in both developed and emerging markets converges to 100% in five years.²⁵ This means that the ratio should increase 2.5% and 5.5% annually in developed and emerging markets, respectively, given the market cap-to-GDP ratio of 87.1% in developed markets and 70.0% in emerging markets. If average, nominal GDP growth rates in developed and emerging markets over the next five years are 4% and 10%, respectively, then equity market capitalization in developed markets should increase by 6.5% each year, and the equity market capitalization in emerging markets should increase by 15.5%. The gap in ratios between the two regions is still significant considering the faster nominal GDP growth in emerging market economies.

Global investors seeking exposure to emerging market equities may accelerate the convergence process between the market capitalization-to-GDP ratios of developed and emerging economies, as increased demand in emerging market equities should lead to market maturation. As shown in the graphs on page 12 and above, the current market capitalization-to-GDP ratio in emerging markets is only 70%, on average, compared with 87% in developed countries.²⁶ The expected convergence here does not necessarily mean that emerging market investors are guaranteed higher returns, but the growth potential for these markets is strong. As discussed, higher market capitalization-to-GDP ratios may be reached via more listings of new companies and the issuance of additional stock by existing companies, in lieu of an increase in stock prices. New investors benefit from IPOs and new issues, as it provides them with an opportunity to enter the marketplace.

The implication stands that emerging market equities have room to grow via a stock price increase or the listing of new equities, or both. The maturation of equity markets increases liquidity and simultaneously attracts new investment, all of which illustrate the potential investment opportunities in the equity markets of emerging economies.

²⁵This is not a particularly aggressive assumption because the ratio in developed markets reached 120% in 2000.

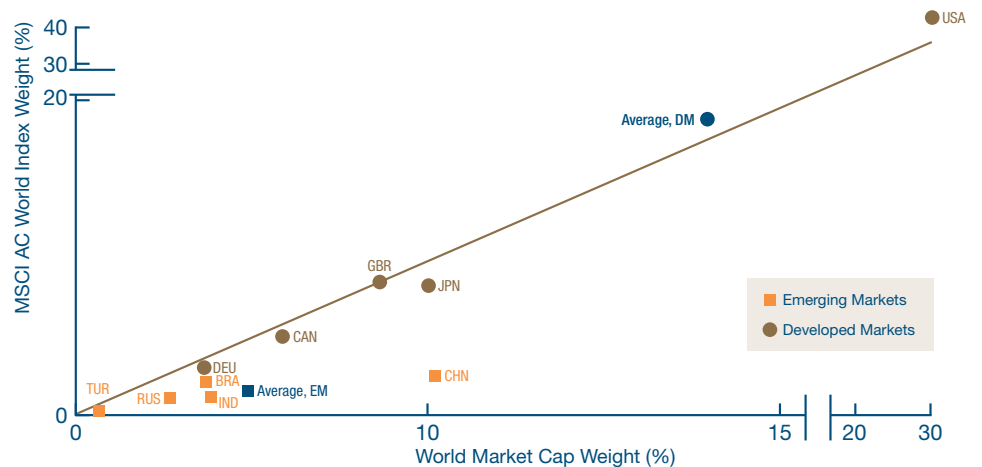
²⁶As of August 31, 2011.

The implication stands that emerging market equities have room to grow via a stock price increase or the listing of new equities, or both.

Underrepresented Equity Markets in Global Portfolios

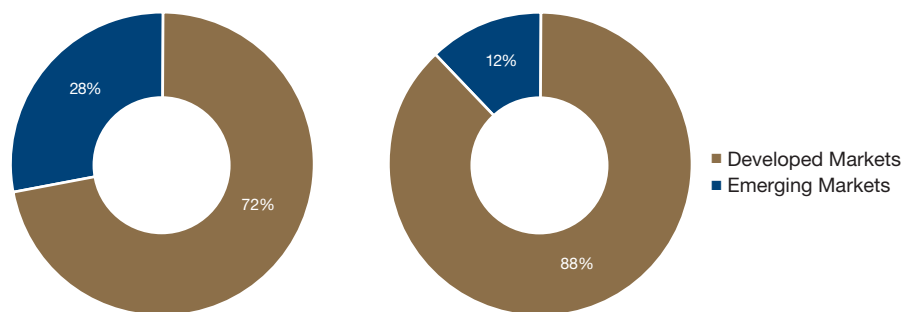
Emerging equity markets, on average, are underdeveloped and often underrepresented in investors' portfolios. Precise figures vary on how much institutional and retail investors allocate to emerging market equities, but a rudimentary calculation computes the weight of emerging markets in a global index. Our analysis in the graph below compares the percentage of emerging market equities in the global equity market capitalization to the percentage of emerging market equities in the popular global equity benchmark.²⁷

MSCI AC WORLD INDEX vs. WORLD MARKET CAP



Source: Bloomberg, MSCI, August 31, 2011
Averages are GDP-weighted. List of UN country code abbreviations may be found in the Appendix on page 16.

WORLD MARKET CAP WEIGHT vs. EQUITY† INDEX WEIGHT



†MSCI AC World Index, August 31, 2011.

²⁷As of August 31, 2011.

We are not necessarily suggesting that optimal asset allocation should be as much as any asset's market capitalization. But if there is a significant gap between the market capitalization of emerging market equities and the average asset allocation to those countries, the trend is not likely to continue given the strong fundamentals of emerging markets.

As shown in the pie charts on page 14, market capitalization of emerging markets accounts for 28% of the world equity market capitalization.²⁸ Emerging equities are given an allocation of only 12% of the MSCI AC World Index. The opposite holds for developed market equities, however, where market capitalization explains 72% of world equity markets but is given 88% of weights in the benchmark. Therefore, by our calculation, emerging market equities are underrepresented by 57% and developed market equities are overrepresented by 22% in the benchmark index. This is likely the case in the actual asset allocation of many global investors, as well. Again, market capitalization is not the only factor when determining benchmark weights or asset allocation, but, in our view, this large gap simply cannot be sustainable. We believe that weights of emerging markets in benchmarks will increase continuously and, as a result, global investors will allocate more to emerging market equities going forward.

Conclusion

Investment opportunities across emerging markets are especially attractive given the seven advantageous characteristics we highlight in this piece. Higher personal savings rates, demographic opportunities and healthier public-sector balance sheets indicate strong, potential economic growth of emerging economies. Undervalued currencies and enhanced sovereign credit quality also underpin future economic growth, reflecting the likelihood of gains from currency appreciation and reduced investment risks. Small equity market capitalization-to-GDP ratios, along with fundamentally underrepresented emerging equity markets in globally benchmarked indices, also point to significant growth potential in emerging markets.

Investors are now faced with an environment of increased risks and uncertainties, such as sluggish economic growth in the U.S. and sovereign debt crises in Europe, as well as seemingly less ammunition on the part of many governments and central banks to deal with these problems. Inevitably, the risk appetites of investors may shrink and, as a result, asset allocation to emerging markets may be reduced or even reversed. But with a long-term perspective, and regardless of short-term trends or tactical investment themes, investors can expect the global shifts we outline in this paper to persist. In the long run, we believe that emerging markets still have strong growth capabilities as well as underdeveloped, underrepresented equity markets, and that global financial markets will fully reflect these fundamentals.

Higher personal savings rates, demographic opportunities and healthier public-sector balance sheets indicate strong, potential economic growth of emerging economies.

Peter Lee, PhD, CFA
Head of Emerging Market Strategy

Meredith Farber
Research Analyst

²⁸We use MSCI indices.

APPENDIX

IMPORTANT INFORMATION

Glossary Of Terms

The Consumer Price Index (CPI) is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care.

Gross Domestic Product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

Index Definitions

The MSCI All-Country (AC) World Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed markets. The MSCI AC World Index consists of the following 24 developed market country indices: Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Israel, Italy, Japan, Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, the United Kingdom and the United States.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. As of June 2010, the MSCI Emerging Markets Index consisted of the following 21 emerging market country indices: Brazil, Chile, China, Colombia, Czech Republic, Egypt, Hungary, India, Indonesia, Korea, Malaysia, Mexico, Morocco, Peru, Philippines, Poland, Russia, South Africa, Taiwan, Thailand and Turkey. Investing in an index is not possible.

Country/Area Name	UN Country Code	Country/Area Name	UN Country Code
Australia	AUS	Italy	ITA
Austria	AUT	Japan	JPN
Belgium	BEL	Malaysia	MYS
Brazil	BRA	Mexico	MEX
Britain	GBR	Morocco	MAR
Canada	CAN	Netherlands	NLD
Chile	CHL	New Zealand	NZL
China	CHN	Norway	NOR
Colombia	COL	Peru	PER
Czech Republic	CZE	Philippines	PHL
Denmark	DNK	Poland	POL
Egypt	EGY	Portugal	PRT
Finland	FIN	Russia	RUS
France	FRA	Singapore	SGP
Germany	DEU	South Africa	ZAF
Greece	GRC	South Korea	KOR
Hong Kong	HKG	Spain	ESP
Hungary	HUN	Sweden	SWE
India	IND	Switzerland	CHE
Indonesia	IDN	Thailand	THA
Ireland	IRL	Turkey	TUR
Israel	ISR	U.S.	USA

Source: United Nations

About S&P Credit ratings

The general meaning of our (S&P) credit rating opinions is summarized below.

'AAA' — Extremely strong capacity to meet financial commitments. Highest Rating.

'AA' — Very strong capacity to meet financial commitments.

'A' — Strong capacity to meet financial commitments, but somewhat susceptible to adverse economic conditions and changes in circumstances.

'BBB' — Adequate capacity to meet financial commitments, but more subject to adverse economic conditions.

'BBB-' — Considered lowest investment grade by market participants.

'BB+' — Considered highest speculative grade by market participants.

'BB' — Less vulnerable in the near term but faces major ongoing uncertainties to adverse business, financial and economic conditions.

'B' — More vulnerable to adverse business, financial and economic conditions but currently has the capacity to meet financial commitments.

'CCC' — Currently vulnerable and dependent on favorable business, financial and economic conditions to meet financial commitments.

'CC' — Currently highly vulnerable.

'C' — Currently highly vulnerable obligations and other defined circumstances.

'D' — Payment default on financial commitments.

An obligor rated 'SD' (selective default) or 'D' has failed to pay one or more of its financial obligations (rated or unrated) when it came due. A 'D' rating is assigned when Standard & Poor's believes that the default will be a general default and that the obligor will fail to pay all or substantially all of its obligations as they come due. An 'SD' rating is assigned when Standard & Poor's believes that the obligor has selectively defaulted on a specific issue or class of obligations, excluding those that qualify as regulatory capital, but it will continue to meet its payment obligations on other issues or classes of obligations in a timely manner. A selective default includes the completion of a distressed exchange offer, whereby one or more financial obligations is either repurchased for an amount of cash or replaced by other instruments having a total value that is less than par.

Note: Ratings from 'AA' to 'CCC' may be modified by the addition of a plus (+) or minus (-) sign to show relative standing within the major rating categories.

Source: Standard & Poor's, October 11, 2011

Risks: Investing in international markets may involve additional risks, such as social and political instability, market illiquidity, exchange-rate fluctuations, a high level of volatility and limited regulation. In addition, single-country and sector funds may be subject to a higher degree of market risk than diversified funds because of concentration in a specific industry, sector or geographic location. Investing in small- and mid-size companies is more risky than investing in large companies as they may be more volatile and less liquid than large companies. **Emerging Markets Risk** — The risks of foreign investments are typically greater in less developed countries, which are sometimes referred to as emerging markets. For example, political and economic structures in these countries may be changing rapidly, which can cause instability and greater risk of loss. These countries are also more likely to experience higher levels of inflation, deflation or currency devaluation, which could hurt their economies and securities markets. For these and other reasons, investments in emerging markets are often considered speculative.

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