

Frontier Hurdles

Leopard Capital Fund Manager, Thomas Hugger of Leopard Asia Frontier Fund and Managing Partner of Leopard Capital LP, goes through some of the major difficulties faced in various frontier markets in Asia.

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In the frontier markets, even though you have electronic data services such as the internet, social media, and Bloomberg, it is very difficult to get financial papers or balance sheet papers, and other fundamental papers for some of the companies in these locations. Even if you go to Bloomberg and search on Bangladesh, you don't have the balance sheet there. If you go into Bloomberg and look at Mongolian stocks, you will often find the price, but the description says, "The company currently has no available information on their current line of business as of 08/2008". These are often blue-chip companies, and sometimes we have visited them or we have networks there, but there is limited information available.



But this is frequently because business is based on a more personal note, and I would say physical representation gives a big advantage. Our strategy on the private equity side complements this, so everywhere we have firms, we have offices. So we have an office in Cambodia, we have an office in Laos, we have an office in Haiti. When we are successful in fundraising for Myanmar and Bangladesh, we will have offices there too.

For private individuals it is still very difficult to invest in these markets. Go to a private bank in Hong Kong or Singapore, tell them you want to buy stock in Laos or even Vietnam and they will often tell you "Oh we are sorry, we cannot execute".

Even for the institutional funds, including the bigger ones in some of the smaller markets, many still cannot trade because there are some restrictions, one of the main issues is they have no international custodians. That's why the big guys often cannot invest in Laos, Cambodia, Mongolia or Papua New Guinea.

Principal difficulties

The hurdles start from very basic things, when last year I made my first trade in Mongolia, I called up the firm I wished to trade with. It was very difficult to reach a person because the fixed line was poor. So I had to call a mobile. I placed the order and I had to confirm it by email. There are some rules in Mongolia that mean that the broker can only place the order in the system if he has it written and signed, and it has to be on an order slip and the client has to sign it. So the broker sent me print-outs of the order sheet, which was in Mongolian. Then I had to sign it and to scan it and email it back and then the order was placed. In some markets people compete for nano-seconds, and this trade took me hours.

An execution in Papua New Guinea takes sometimes two, three days. I often need to call the local broker to chase them up. Sometimes the brokers don't execute orders and say "Oh no, it was not done today". So I have to wait for a week or even sometimes a month just to execute small tiny purchases. Of course in Papua New Guinea don't call them in the afternoon; they are probably not in the office.

Then also in Mongolia, the fee I paid for the first broker was somewhere around 5% in commission and government fees. So I went there found another broker who gave me considerably cheaper executions. In international terms it is still outrageously expensive. Then it took me about four months until I had all the papers process done and when I asked for trade reports I would just get an email saying what I had bought. In this situation there was no contract, nothing, so I requested a contract note. I was probably one of the first foreign institutions for them, so I sent them examples of contract notes and what I expect for my fund, and within 24 hours I had the notes.

Execution pains

In Mongolia, I don't have live prices on Bloomberg, so I found a website that has a five minute delay. I always check the prices online and I always place limit orders because the spreads can be more than 100%.

The daily turnover in Mongolia is less than US\$100,000 and there are maybe one or two liquid stocks and the rest are just super illiquid.

There are also some capital controls, for example in Vietnam, before the broker can execute a trade he calls my custodian and determines a limit. Then the custodian will give the broker his limits and then he can execute. For each broker I have to designate the people, the name and phone number, ID number or fax number of who can ask for the limits in order to get the approval from their custodians.

In Mongolia or Vietnam or in other markets, I cannot sell stock and then buy with the profits, as I am required to wait until the money hits the account again.

One big hurdle is that, for foreign investors it is not easy to access these markets. For me as an emerging fund it is worth it and I went through the pain. It takes months until we have all custodians and brokerage accounts set up.

There is also a problem with ID markets, because if you go to London or New York, you don't need an ID, you just have an account somewhere and your bank will get a broker and so on. But it is an administrative hurdle and I don't understand why these exchanges add this pain for foreign investors. Although I think it is also not only the exchange, it is flowing down from the regulator.

Difficulties in opening accounts

In Vietnam it took me seven months to get a trading licence. There is no standardisation of the process between any of these markets. When you have to go back and forth it can take a long time.

For example, to open an account for Pakistan I went to the Pakistani Consulate here in Hong Kong with all the documents and they said they cannot do it because my firm is registered in

the Cayman Islands. I went about 10 times to the Pakistan Consulate and finally they made an exception.

Some of the brokers have asked for extensive information to open an account and this can prove very time consuming.

On the other hand, a Pakistani guy with a brokerage, one of the leading companies, came to my office and he asked, "Do you mind opening an account with me?" I said, "Hey listen I'm going through this with such a pain with all the brokers. I don't want to do this process again I'm nearly at the end of the tunnel". Then he said, "Okay, listen give me your certificate of incorporation and the MMA of the funds and I promise you it will take two days". And two days later the brokers account was opened.

In Vietnam, the document has to go to the Cayman Islands, they have to be notarised. Then they have to be sent to the Vietnamese embassy in London to be consularised. It then goes to Singapore to the custodian and the custodian sends it to Vietnam. So the whole process costs \$2,000 for two stamps.

Now my fund administrator gives a lot of pain to some of the brokers, because the fund needs a monthly statement of my transactions which is proving to be quite a lot of work. and it is a big learning curve.

Chances of reform

Look at Laos, it's a communist country. Laos and Cambodia, Cambodia has one stock at the moment and Laos has two. People go to Thailand where it's a free country. You don't need an ID, but in Cambodia and Laos, you do. So they are investing a lot of money in technology and people and they don't make money. Then you consider the ASEAN link and from a commercial point of view, those countries don't have a stock exchange. It took Cambodia three or four years to get it off the ground. I don't know how much money they sunk into this project and with the link it could limit trading in this market.

The big stock exchanges are in Thailand and Singapore. But even Thailand today has currency restrictions so you can put money in easily, but if you try to move money out it's very difficult, especially in large amounts. It also makes it more difficult for people in Laos to trade stocks in Thailand or in Singapore, because they need to buy the local currency.

Lately Emerging and Frontier Markets have underperformed Developed Markets and this provides an excellent entry point since these markets are historically seen as not expensive.

The trading facilities are often inefficient, but when you look at the stock market valuations: some stocks are overpriced but also a lot of stocks are trading below our "fair value model" or even below net cash (most of these companies are growing faster than listed companies in developed markets).

However, while some of the trading facilities are inefficient, in terms of stock market valuations: some stocks are overpriced, but a lot of stocks are trading below our "fair value model" or even below net cash (most of these companies are growing faster than listed companies in developed markets), which is a clear opportunity.