



C A M B R I D G E A S S O C I A T E S L L C

GLOBAL MARKET COMMENT

ASIAN CAPITAL MARKETS PRIMER; PART I

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Asian Capital Markets Primer; Part I

This month marks the first in a series of primers designed to introduce investors to the characteristics of Asian capital markets. Among the topics to be covered, we will examine country and regional risk/return profiles, intra-regional correlations and correlations with other equity markets, sector weightings, valuations, and currency regimes. This month, we compare the weight of Asia's economies and equity market capitalizations with those of the world. Complementing this series, we have launched a new "Asian" section in our monthly publication, *Market Update: Returns and Valuations*.

Japan and Developed Asia

While Japan's GDP is clearly much larger than those of the other "developed" Asian economies, its dominance in size is not fully reflected in its market-cap weighting¹ in developed markets equity indices.² The world's second largest economy currently accounts for 15.5% of global developed markets GDP (as measured by the sum of the GDPs of MSCI World's 23 constituents), yet MSCI Japan's market-cap weight is only 9.7% of the MSCI World Index's total market cap (all economic figures are denominated in US\$). Japan's current market cap is down substantially from 1988, when at the height of its bubble, MSCI Japan made up a full 44.1% market-cap weight in MSCI World. (See Table A.)

Similarly, the combined GDP of developed Asia accounts for 18.6% of the global economy, yet only 13.1% of the market cap of MSCI World. Without Japan, the relationship between economic and market-capitalization weights is almost identical: MSCI Pacific *ex Japan* constituents account for 3.6% and 3.8% of the combined GDP and market cap of MSCI World *ex Japan*, respectively.

China and Developing Asia

Developing Asia is by far the largest emerging markets subregion, accounting for 54% of both the aggregate GDP and market capitalization of emerging markets. As was the case for developed Asian countries, developing Asian countries have a mismatch between their economic and market-cap weightings that is primarily attributable to one constituent country.³ Developing Asia's combined GDP accounts for 10.2% of the size of global (both developed and emerging) economies, but only 2.8% of global equities (Tables B and C). The main reason: China. China's economy accounts for 4.1% of global GDP, compared to only 0.4% of market capitalization. China's GDP accounts for 21.7% of the combined economies of MSCI Emerging Markets Index constituents, while its market-cap weight is only 7.7%. Its overall GDP is 40.2% of the combined size of Asia's nine developing economies, while China's total market cap is 14.3% of the MSCI Emerging Markets Asia Index.

¹ Market-cap weightings refer to the float-adjusted market capitalization used by MSCI in its index construction.

² "Developed" Asia is represented by the MSCI Pacific Index, which includes Japan, Hong Kong, Singapore, Australia, and New Zealand. Global developed equities are represented by the MSCI World Index.

³ "Developing" Asia is represented by the MSCI Emerging Markets Asia Index, which includes China, India, Indonesia, Korea, Malaysia, Pakistan, the Philippines, Taiwan, and Thailand. The aggregate of developed and emerging global equities is represented by the MSCI All Country World Index.

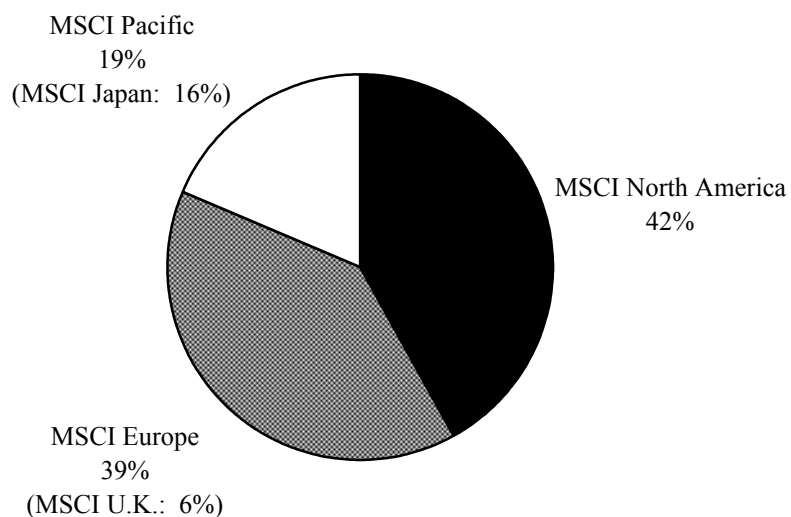
Table A

MSCI WORLD REGIONAL GDP AND MARKET CAPITALIZATION

(US\$ Trillion)

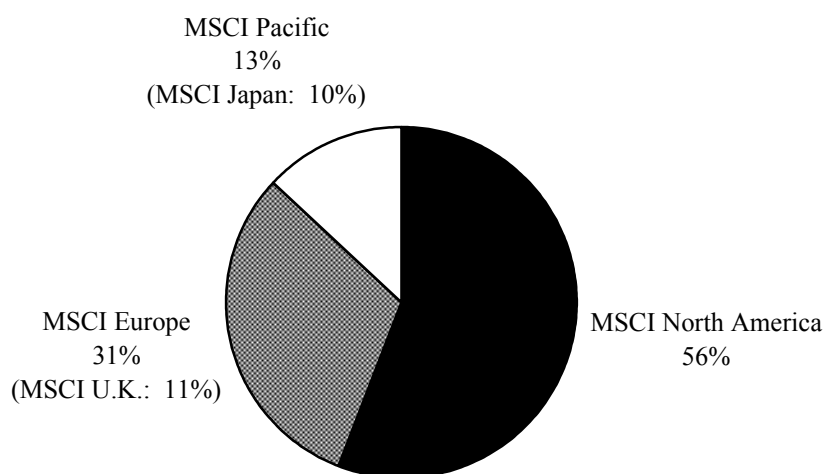
December 31, 2003

Total GDP: \$27.9



December 31, 2004

Total Market Capitalization: \$20.3



Sources: Morgan Stanley Capital International, Thomson Datastream, and The World Bank. MSCI data provided "as is" without any express or implied warranties.

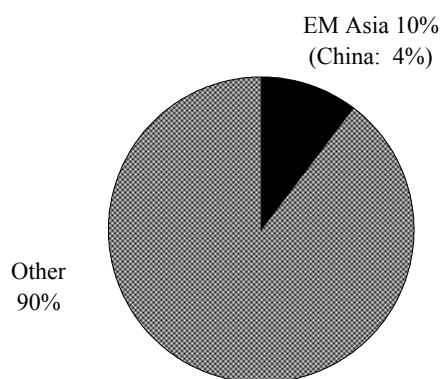
Note: Market capitalization is float-adjusted.

Table B

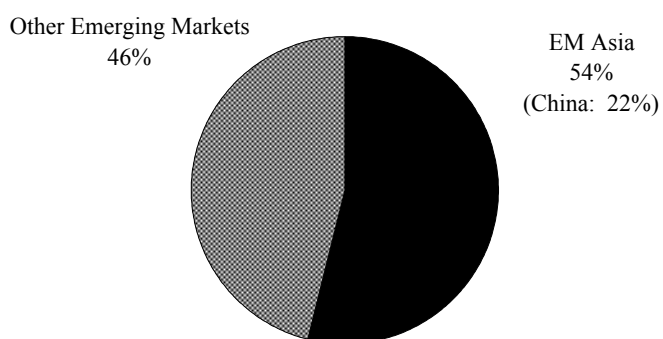
**MSCI EMERGING MARKETS ASIA GDP AND MARKET
CAPITALIZATION WEIGHTINGS
(US\$ Trillion)**

December 31, 2003

EM Asia GDP as a % of World GDP
Total World GDP \$34.4

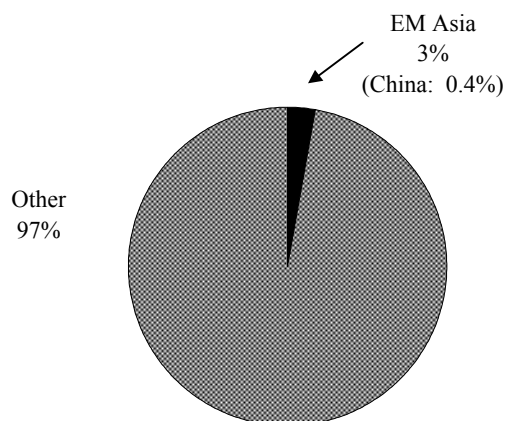


EM Asia GDP as a % of EM GDP
Total EM GDP \$6.5

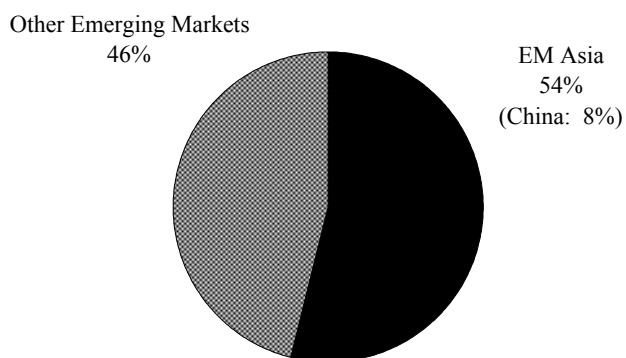


December 31, 2004

EM Asia Market Cap as a % of World Market Cap
Total World Market Cap \$21.4



EM Asia Market Cap as a % of EM Market Cap
Total EM Market Cap \$1.1



Sources: Deutsche Bank, Morgan Stanley Capital International, Thomson Datastream, and The World Bank. MSCI data provided "as is" without any express or implied warranties.

Notes: World GDP and market capitalization are based on the MSCI All Country World Index. Market capitalization is float-adjusted. Figures may not total due to rounding. Israel's GDP dates back to 2002.

Table C

DEVELOPED AND EMERGING MARKETS COUNTRY ALLOCATIONS
U.S. Dollars
December 31, 2004

	Percent (%)	
	<u>GDP</u>	<u>Market Capitalization</u>
Developed & Emerging Markets		
All Country World Index	100.0	100.0
All Country Asia Pacific	25.2	15.3
All Country Asia Pacific ex Japan	12.7	6.1
Developed Markets		
Pacific	15.0	12.4
Pacific ex Japan	2.5	3.3
Australia	1.5	2.1
Hong Kong	0.5	0.7
New Zealand	0.2	0.1
Singapore	0.3	0.3
Japan	12.6	9.2
Emerging Markets		
EM Asia	10.2	2.8
China	4.1	0.4
India	1.7	0.3
Indonesia	0.6	0.1
Korea	1.8	0.9
Malaysia	0.3	0.2
Pakistan	0.2	0.0
Philippines	0.2	0.0
Taiwan	0.8	0.7
Thailand	0.4	0.1

Sources: Deutsche Bank, Morgan Stanley Capital International, and The World Bank. MSCI data provided "as is" without any express or implied warranties.

Notes: Market capitalization is float-adjusted. Israel's GDP dates back to 2002, and remaining GDPs date back to 2003.