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Emerging markets' new generation of tech firms

Over the last decade, the role and prominence of technology companies in emerging markets has increased markedly. Emerging markets economies have proven themselves capable of producing truly world-leading tech firms. And as smartphone penetration has surged, the positive impact of technology on daily life in emerging markets has been very significant.

At one point in the past, 'technology' in emerging markets meant hardware assembly in Taiwanese factories and the outsourcing of repetitive data entry to India. It was a paradigm based mostly on wage arbitrage, in which technology leadership sat firmly in developed markets.

That world has been turned on its head.

'...today it is more often the case that America's tech giants imitate features first developed in China.'

World's largest pool of engineering and entrepreneurial talent

Now, the most advanced manufacturing companies in the world are just as likely to be located in Taiwan and Korea as they are in Germany and Japan. Semiconductors are the archetypal example: the cutting edge chips can only be made in emerging markets¹. And this isn't only a phenomenon pertaining to hardware.

The leading edge of online innovation has migrated from Silicon Valley to Chinese tech hubs like Shenzhen and Hangzhou¹. Whilst in the past Chinese internet companies were berated for shamelessly copying the innovations of companies headquartered in California, today it is more often the case that America's tech giants imitate features first developed in China.

In hindsight, perhaps this was always a likely outcome. Developing countries contain the world's largest pools of both engineering talent and of highly motivated entrepreneurs. The combination has been a potent recipe for the creation of innovative globally competitive businesses.

Eastern Europe is a case in point: its education system has been the bedrock on which the region has produced a number of truly world-leading software companies. For instance, Prague-headquartered Avast² is one of the world's largest cybersecurity companies. It uses machine learning to continuously tweak its software and prevents 1.5bn attacks per month on its 435 million users around the world¹.

Similarly impressive Eastern European software and internet companies have grown up in Minsk, Bucharest, Warsaw, and Moscow.

An evolving opportunity set

Very often companies from these countries choose to list in London or New York rather than their home markets – underlining the need for investors’ to place economic reality above place of listing in defining the emerging markets opportunity set¹.

The emergence of these kinds of companies has fundamentally changed the Global Emerging Markets asset class. Years ago, the important companies were larger banks and resource companies, and the universe was overwhelmingly cyclical. Today, these have been replaced by advanced manufacturers and online platform businesses. Rather than commodity prices and macroeconomic fluctuations, these companies’ earnings are driven by long-term structural trends.

Reducing inequality of income and of opportunity

Many of these secular shifts are continuously improving the lives of people in emerging markets and contributing positively to sustainable development outcomes.

Argentine internet company Mercado Libre² is a fantastic example. Its core business is an e-commerce platform on which 11.6 million entrepreneurs across Latin America are able to reach a pan-continental market¹. Their slogan “democratizing commerce” captures the impact well: these small companies would otherwise be unable to reach such large audiences and scale up over time.

Mercado Libre has built a number of adjacent businesses around its marketplace, many of which are tailor-made for the challenges facing small businesses in Latin America. For instance, historically in Latin America bank fees have been very high and small businesses have been unable to access sufficient finance. So in order to support its clients, Mercado Libre launched its own payments business which is now expanding into lending to SMEs.

The alignment of all stakeholders is clear: the better that their clients are able to grow their businesses, the more throughput that occurs via Mercado Libre’s various business lines. The net effect is the creation of thousands of additional jobs at the bottom of the pyramid in a region of the world that sorely needs ways to reduce inequality of income and of opportunity.

An exciting future

The prospects for companies like Avast and Mercado Libre over the next decade give us great optimism for the future of emerging markets, their ability to produce new world-leading companies, and the delivery of tangible development benefits in poorer countries. We hope to continue to generate such exciting investment ideas in coming years.

¹ Source for company information: Stewart Investors investment team and company data.

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Jack Nelson

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