



Close correlationships

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ONE of the main motives for investing in emerging stockmarkets has been the desire to diversify risk. Yet share prices there have become much more closely correlated with Wall Street's over the past couple of years. As America's high-tech bubble has burst, share prices have tumbled, not only in Asia but throughout the developing world. Since March, the Nasdaq index has fallen by almost 45%, while emerging stockmarkets have fallen on average by about one-third.

Share prices have dropped particularly sharply in Asia, where the economic recovery has been driven largely by exports to America. But, contrary to popular perception, share prices in most Asian markets have tended to move less in step with Nasdaq than those of many other emerging markets.

The chart, based on figures calculated by The Bank Credit Analyst, a research group based in Canada, shows the correlation over the past year between the movements of individual emerging stockmarkets and Nasdaq. This tends to be influenced by two factors: the share of high-tech companies in a stockmarket's total capitalisation; and the importance of exports to the United States. Thus, the South-East Asian markets have moved less closely in line with Wall Street than those of Taiwan and South Korea, which depend more on electronics.

The markets with the highest correlation are mostly in Latin America and Eastern Europe. Mexico tops the league—hardly surprising since exports to the United States account for 25% of Mexico's GDP, compared with a more modest 7% of South Korea's and 4% of China's.

At the other extreme, Chinese and Venezuelan share prices are negatively correlated with Nasdaq—ie, prices have risen as Nasdaq has tumbled. Since the beginning of the year, Chinese share prices have risen by around 50% in dollar terms—by far the biggest gain of all the markets monitored by *The Economist* each week. China is still dominated by "old economy" manufacturing industries (56% of the Shanghai stock exchange) and so has been relatively immune to the flight from technology.

