A flood always starts with a trickle…

By Jan Dehn

In the global backdrop section we discuss Japan's return to debt stimulus. What started as a trickle in Tokyo is likely to become a flood across developed economies and the ramifications are not good for holders of fixed income in those countries. Meanwhile, in EM the big story last week was the Indian Senate's approval of a major tax reform, which, to all intents and purposes, creates a single market in that country. In China, financial reforms continue with the planned launch of CDS markets and issuance in SDRs ahead of China's inclusion in the global reserve currency basket in October of this year. Indonesia gears up for reforms following the appointment of Sri Mulyani as Finance Minister and Thailand's voters approve a new constitution that puts the country on track for a return to democracy next year. In Brazil, the impeachment of President Dilma Rousseff is set to kick off in the Senate this week, while formal inflation targeting is just around the corner in Argentina. The Venezuelan Cabinet reshuffle was a setback to reformers, but probably does not change the government's willingness to pay. Finally, we discuss South Africa's local elections, which delivered a bloody nose to the ANC.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	11.7	–	1.44%
MSCI EM Small Cap	12.2	–	1.18%
MSCI Frontier	9.4	–	-1.03%
MSCI Asia	12.2	–	1.40%
Shanghai Composite	12.4	–	-0.06%
Hong Kong Hang Seng	7.3	–	0.55%
MSCI EMEA	10.0	–	0.42%
MSCI Latam	13.8	–	1.28%
GBI-EM-GD	6.23%	–	0.43%
ELMI+	3.39%	–	–
EM FX spot	–	–	0.22%
EMBI GD	5.11%	351 bps	0.52%
EMBI GD IG	3.87%	221 bps	0.55%
EMBI GD HY	6.89%	539 bps	0.49%
CEMBI BD	5.05%	360 bps	0.24%
CEMBI BD IG	3.88%	244 bps	0.18%
CEMBI BD Non-IG	6.99%	553 bps	0.33%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	16.4	–	0.49%
1-3yr UST	0.73%	–	-0.13%
3-5yr UST	1.13%	–	-0.35%
7-10yr UST	1.58%	–	-0.87%
10yr+ UST	2.30%	–	-2.23%
10yr+ Germany	-0.06%	–	-1.29%
10yr+ Japan	-0.04%	–	-1.68%
US HY	6.66%	528 bps	0.35%
European HY	4.30%	476 bps	0.39%
Barclays Ag	–	243 bps	-0.38%
VIX Index*	11.43	–	-1.01%
DXY Index*	96.35	–	0.63%
EURUSD	1.1089	–	-0.65%
USDJPY	102.27	–	-0.12%
CRY Index*	181.80	–	0.78%
Brent	44.8	–	6.36%
Gold spot	1331	–	-1.60%

Note: Additional benchmark performance data is provided at the end of this document. *See last page for index definitions.

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- **India:** India's Senate approved the Goods & Services Tax (GST) reform bill last week. The reform has already passed the Lower House. The GST bill must now be passed by at least 50% of India's state governments, but we do not expect this to present a major obstacle. Implementation is likely to start in 2017. GST is by far the most important tax reform in India for decades. It creates a national sales tax to replace a state-based tax system that created major distortions, inefficiencies and internal barriers to trade. GST creates a single market within India from a tax perspective. The Indian government estimates that the reform can add 2% to GDP.

Longer-term, the reform may lead to economies of scale in production, lower transport costs and ultimately higher growth and as such the reform supports both equities and bonds in India. However, there may be short-term challenges, such as temporary inflationary effects and noise at local level. After all, all tax reforms have winners and losers. However, once these teething problems have been overcome the only ones not to benefit from GST would be those who enjoy quasi-monopolistic fiefdoms behind high state taxes and trade barriers at the expense of the large silent majority. With the passage of GST, Prime Minister Modi has now delivered on his most important reform promise. His administration has already cut red tape and made other efficiency enhancing measures. India has also been returned to strong growth with low inflation and acquired a healthy external balance with more than USD 360bn in reserves. With the passage of GST, India becomes the latest in a long line of EM countries to engage successfully in structural reforms, including Colombia, Mexico, Argentina, Brazil, Indonesia, Peru, Romania, China, Thailand, Pakistan, Saudi Arabia, Ghana, El Salvador, Costa Rica, Morocco, etc.

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EM countries tend to reform far more than developed economies, because they are rarely given the benefit of the doubt in the markets. This feature sets EM countries quite apart from developed economies that tend to address most macroeconomic problems – structural or otherwise – with monetary stimulus and/or deficit financing, or both, but rarely reform. In other Indian news the government announced that the new inflation target for the next five years will be 4% +/-2%. Currently, inflation is sitting close to the top of this band (5.77%). Going forward, if the central bank misses the target, it must report to the government on a quarterly basis with an explanation and a list of steps it intends to take in order to bring inflation back to the target range.

- China: China continues to push forward aggressively with financial sector reforms. Firstly, China's industry body which represents domestic institutional investors are preparing to launch a full credit default swap market in China, which, in principle, would allow for investors to take both long and short positions. This development should significantly increase the liquidity in the Chinese corporate bond market, in our view. Also, China's inclusion in the IMF's SDR basket, which is scheduled for October this year, means that a number of institutions are currently preparing to place SDR-denominated bonds within China.

The World Bank, China Development Bank (CDB), ICBC Asia and others are among the institutions issuing bonds in China in SDRs. The SDR market is likely to remain small, however. We think the real significance of China's inclusion in the SDR basket is that it will increase investment in China's local bond market. The RMB's weight in the SDR basket will be 10.9% compared to 8.33% for JPY and 8.09% for GBP. We believe the bulk of the world's central banks and indeed other institutional investors are under-exposed to China. Standard Chartered Bank estimates that each 1% allocation to RMB by central banks alone will increase demand for Chinese bonds by USD 78bn and that total central bank holdings could reach USD 1trn within 10 years. In addition, the bank estimates that demand from International Financial Institutions alone could reach USD 65bn. However, the largest demand is ultimately going to come from pension funds and insurance companies, in our view, particularly when Chinese domestic markets are included in benchmark indices. Institutional investors have generally been too myopic when it comes to China. We think they ought to be heavily invested already. After all, Chinese bonds have outperformed US bonds in Dollar terms since 2014 and China is the only country in the SDR basket, whose bonds pay positive nominal and real yields. Equally importantly, we believe China per capita GDP will equal that of the US by the middle of this century at which point China's economy – and hence her markets – will be 4.5 times greater than the US (due to a bigger population). That implies that Chinese government bonds will replace US Treasuries and the RMB will replace the USD as the main global bond and currency benchmarks exactly the same way that the USD replaced the GBP in the interwar years.

In other news, China's Q2 2016 current account surplus increased sharply to USD 59.4bn from USD 39.2bn in Q1 2016. July's trade balance suggests this trend may be continuing. Due to a better performance on exports than imports China's trade surplus rose from USD 48.1bn in June to USD 52.3bn in July. Note that positive trade balance numbers enter positively into GDP. China's FX reserves were broadly stable at USD 3.2trn (down USD 4bn since last month). A new study by Citigroup shows that China's reserve adequacy is now 177%, which is far above the reserve levels recommended by the IMF.[1]

Finally, we note that a new report by Fitch, the ratings agency, finds that China will need to build 800 million square meters of residential housing in order to meet demand in the next 15 years.

- Indonesia: The economy expanded at a faster than expected clip in Q2 2016. Real GDP growth was 5.2% yoy, a meaningful acceleration from 4.9% yoy in Q1 2016. The qoq rate of growth is accelerating, up 1.4% in Q2 versus 0.7% in Q1. Indonesia's current strength is not likely to be a flash in the pan. Newly appointed Finance Minister Sri Mulyani Indrawati has already announced new reform measures that further improve the economic outlook. She said that the government will expand the tax base and ensure better tax enforcement. On the spending side, the government will step up the execution of infrastructure projects and target spending at improving the business climate and eradicating poverty.

- Thailand: More than 60% of Thailand's voters approved the new constitution put forward by the military government. The approval of the new constitution is an important step on the road back towards full democracy in Thailand. A general election will now be held next summer. New rules governing the appointment of prime minister were also approved, which holds out the prospect of less populist rule in Thailand going forward. All this is positive news for Thailand, in our view. For more details see *"Thailand's Plebiscite"*, Weekly Investor Research, 1 August 2016. The Bank of Thailand kept the policy rate unchanged at 1.5%.

- Brazil: A special committee in the Senate approved by a 14-5 majority the resumption the impeachment proceedings against President Dilma Rousseff. A full vote on the Senate floor to formally approve commencement of the trial is scheduled to take place tomorrow. A minimum of 54 votes out of 81 is required for the trial to go ahead; we expect the trial to go ahead and be concluded as early as this month (during the height of the Olympic Games). Once the Dilma trial is out of the way the government will seek to pass a constitutional amendment that limits government spending for the next 20 years and radically alters Brazil's fiscal trajectory in a favourable direction. This reform, in our view, is far more important than the Dilma trial, which, in our view, has been a 'done deal' for some time. Meanwhile, there are further signs of green shots in

[1] *"China's encumbered FX reserve and reserve adequacy: a reassessment"*, Citigroup, China Economics View, 7 August 2016.

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the economy. Higher frequency economic indicators, such as PMI and industrial production, capacity utilisation and confidence in the manufacturing, services, construction and consumer sectors all picked up, albeit from low levels.

- Argentina: Expectations are increasing that the central bank will soon introduce a conventional inflation targeting regime, including a new policy interest rate. Hitherto the monetary policy rate has been set using the rate at which the central bank auctioned paper (Lebacs). However, as Argentina gradually normalises economic policies following the heterodoxy of the previous Kirchner regime the central bank will want to separate quantitative and qualitative instruments. Hence, the need for an explicit policy rate. Meanwhile, the central bank cut the 35-day Lebac rate by another 25bps to 30%. In other news, President Mauricio Macri announced that the government will give the private sector four years to wean itself off subsidies and other protection provided by the previous government. The removal of state protection from various industries is critical to ending rent-seeking, encouraging private sector investment and raising productivity growth. However, liberalisation has upfront political and economic costs, which is why the government is seeking a long adjustment period. The government also announced that that it expects to issue up to USD3bn of 2019 zero coupon Dollar bonds and USD 5bn (or more) of 1% coupon 2023 bonds as encouragement for Argentinians with unregistered cash abroad to settle their unpaid dues. The bonds will be paid to those who bring back cash, but they are not tradable until 2020. The repatriated funds will go to the state pension fund ANSES, which will then invest in infrastructure and other projects.

- Venezuela: President Nicholas Maduro's cabinet reshuffle last week weakened the reform-minded elements within his administration, but may not significantly alter the government's willingness to service debt. The removal of Vice President of Economic Policy, Miguel Perez, a reformer, has isolated PDVSA President Eulogio Del Pino, another reformer. Del Pino has argued vociferously in favour of liability management to push PDVSA's liabilities into the future. We do not think the cabinet reshuffle changes these plans. The government wants to stay current on PDVSA's debt in order to retain access to credit lines for the company, which is the country's only meaningful employer and source of Dollar revenues. The proposed liability management operation would be expensive, but has the potential to free up significant resources for the government next year. On the other hand, we think the cabinet reshuffle does reduce the odds of currency devaluation and changes in fuel price subsidies. Maduro does not appear to want to undertake any reforms of the type that can impact his popularity negatively in the run-up to a planned recall referendum next year. The National Electoral Council said last week that the Opposition has satisfied the requirement to collect the signatures of at least one percent of eligible voters, which means that the recall referendum process can push on to the next stage.

- South Africa: The ANC received a bloody nose from voters in the municipal elections last week. The ANC did win more than half of the votes, but with a much reduced overall majority (53.91% versus 61.95% in the 2011 election). ANC also lost overall control of key councils in several major urban centres, including Tshwane and Johannesburg. Nelson Mandela Bay saw strong gains for centrist opposition party DA. The radical populists in EFF also made inroads in their first council election, though their overall share of the vote remained below 10%. The result can be interpreted in different ways, but we see it as near-term negative. Clearly, it is good for democracy that ANC's de facto monopoly on power is challenged, because the party has been ineffective in restoring growth and is riven with deep internal divisions that go right to the very top of the party. Corruption has also become a major problem for the ANC. On the other hand, South Africa's near-term situation is not likely to improve as a result of this election. This was a local election, so there will be no changes at the top unless ANCs poor showing results in moves to replace President Zuma. The ANC remains the dominant force in South African politics despite the shift in power towards the DA and EFF. The fact that it is still impossible for other parties to challenge the moral right of the ANC to power in South Africa is one of the sad legacies of Apartheid; this legacy appears to be outliving ANC's capacity to deliver good governance.

Snippets:

- Cameroon: Moody's assigned B2 (stable) inaugural rating to Cameroon. S&P and Fitch have already rated Cameroon B. Cameroon entered the JP Morgan EMBI GD index in December 2015 as the 65th member of the index.
- Chile: Industrial production declined at a rate of 3.8% yoy in June due to declining mining output. This decline was sharper than expected. On the other hand, retail sales picked up 1.1% yoy in June, up from 0.5% yoy in May.
- Colombia: Inflation was higher than expected in July (0.52% mom versus 0.34% mom expected). This takes Colombian yoy inflation rate to 8.96%. The spike in inflation is partly related to industrial action by food transport workers and should revert next month. Indeed, core inflation declined marginally from 6.31% yoy in June to 6.26% in July yoy.
- Czech Republic: The central bank left both the policy rate and its FX policy unchanged. The policy rate is 0.05% and the central bank will continue to intervene to keep EURCZK at roughly 27.

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Emerging Markets

- **Ecuador:** Guillermo Lasso, a Guayaquil-based opposition politician, has characterised Ecuador's recent USD 1.0bn debt offering as "immoral debt". Lasso's comments echo President Rafael Correa's labelling of the Global 12 and 30 bonds as "illegitimate debt" ahead of defaulting on these bonds in 2008. Lasso is in no position to determine if the Ecuadorian government will service the new bonds, but if he becomes president the markets may question the government's willing to pay, in our view.
- **Malaysia:** The trade surplus surged to MYR 5.5bn in June from MYR 3.3bn in May. Exports and imports both rose, but exports in particular rose far quicker than anticipated by the market (+3.4% yoy versus -3.7% yoy expected).
- **Mexico:** The government released strong public finance statistics. The primary balance flipped from a deficit of 0.8% of GDP in H1 2015 to a 0.7% of GDP surplus in H1 2016 on the back of solid real growth in revenues (+11.4% yoy). Spending decelerated moderately in real terms. This is an impressive performance in an oil dependent economy, in our view. Gross fixed investment, however, slowed. It increased just 0.7% mom seasonally adjusted (sa) in May from 1.5% mom sa in April. Consumption was strong in May (+2.4% yoy)
- **Philippines:** Consumer prices rose at a 1.9% yoy clip in July versus 2.0% yoy expected. Core inflation is running at 1.9% yoy, unchanged from June. International reserves rose to USD 85.5bn, the highest ever level.
- **Russia:** Services PMI picked up strongly in June (55 versus 53.8 in May and 52.9 expected). Inflation dropped to 7.2% in July from 7.5% in June.
- **South Korea:** S&P raised South Korea's sovereign debt rating from AA- (stable) to AA (stable)
- **Taiwan:** PMI increased moderately to 51 in July from 50.5 in June.
- **Ukraine:** Retail sales and wages picked up smartly in June. Central bank reserves also rose (USD 14bn) as the current account swung into surplus (USD 900m) in Q2 2016. Another USD 2bn in inflows is likely after the IMF approves the most recent programme review (expected later this month).

Global backdrop

Bank of England's decision to further ease monetary policy is obviously a direct consequence of the economic damage underway as a result of UK voters' decision to leave the European Union. Normally one can blame politicians for making bad economic decisions, but this particular decision was the explicit wish of the people. This simple fact undoubtedly takes some of the pressure off Governor Mark Carney, but only for so long. As the economic downturn takes hold, blame will inevitably fall upon officials. Hence, it is worrisome that the Bank of England – like the other QE central banks – is running out of easing options. Carney stated that he is no fan of negative interest rates, so instead he upped corporate bond purchases. Corporate bond purchases are highly distortionary, however. Not only do they drive bond yields below the appropriate level commensurate with the riskiness of individual companies, but the policy also constitutes a subsidy that is only available for larger companies (i.e. those that can issue bonds).

The shrinking room to ease by monetary means strongly suggests that developed countries will once again turn to debt policies, the next phase in their crisis management. Indeed, this was the key message from Japan last week, where Prime Minister Shinzo Abe's announced a JPY 7.5trn fiscal stimulus.

We think Abe's announcement has significance far beyond Japan. Additional debt stimulus is also likely in other developed economies, including the US and the UK. In the US, we expect the next administration to engage in major fiscal spending targeted at infrastructure. Despite healthy gains in the US labour market, including last week's strong payroll number, stronger growth remains elusive. Indeed, a number of banks revised down their estimates for US growth for 2016 to less than 2% last week. The UK will also need to rely more on domestic demand until relations with the country's main trading partners have been clarified.

Why are developed economies still stimulating demand after so many years? The relentless focus on demand stimulus reflects a view on the part of policy-makers that private sector demand is inadequate. The private sector, so the story goes, bit a little too far into its future income in the years leading up to the Developed Market Crisis (DMC) of 2008/2009. Hence, a period of retrenchment can be expected during which governments can usefully fill the gap by easing monetary policy and running fiscal deficits, or both.

So far, there have been two distinct phases of stimulus. Between 2008 and 2012 governments nearly tripled their fiscal deficits, taking average government indebtedness up by an eye watering 48% (raising the average debt to GDP ratio in developed economies from 71% in 2007 to 106% in 2012).[2] Then, however, as the European debt crisis exploded into full bloom, policy-makers switched back to greater monetary stimulus. Their key instrument was bond purchases. This policy served two distinct purposes. One was to ease financial conditions by driving down long-dated yields. The other was to encourage institutional investors to restore capital flows back to the debt markets.

[2] Incidentally, government indebtedness in developed countries has outpaced EM government indebtedness by a mindboggling 353% since 2007. Average indebtedness in EM is expected to be just 47% of GDP this year, according to the IMF.

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Global backdrop

The policies worked well. A European debt crisis was avoided and asset prices went up, especially in European bond markets. Investors chased central bank purchases. Unfortunately, each successive round of stimulus became less and less effective as more and more bonds began to trade with negative yield.[3] This is why the pendulum is shifting back to fiscal stimulus– and it helps, of course, that bond yields are now so low, because governments can issue very cheaply indeed.

Unfortunately, the return to fiscal stimulus at this point in the cycle raises important concerns. The most fundamental is that private sector demand has *still* not taken off nearly a decade after the DMC. This suggests that demand stimulus may not be the right solution. Perhaps the problem is on the supply side. Worse still, perhaps the problem is stimulus itself.

It is likely that awareness of the potential dangers of excessive indebtedness on the part of private sector agents has skyrocketed following the DMC. Certainly, consumers have sought to de-leverage in spite of cheap and abundant credit. Corporates have preferred to pay dividends and buy back stock rather than making irreversible investments in their own capital stock. In light of these observations, the return to fiscal policy may actually make the demand problem worse if consumers and companies understand that government debt has to be repaid somehow, by somebody, at some point in the future.

Sadly, governments may not be able or willing to recognise this. Politicians face regular and frequent elections, so they tend to be far more myopic than other economic agents. They want to keep the wheels of the economy turning. Even a slow turning wheel is better than a wheel that does not turn at all, let alone one that turns backwards. Hence, politicians will always want another stimulus and will always try to avoid measures that have upfront costs, such as reform and more aggressive deleveraging. Note that they also have strong incentives to reassure citizens that their short term measures will solve all problems even if it is patently not true, so one should discount their reassurances heavily.

Another concern is that debt policies may also soon give rise to serious debt sustainability issues. The IMF expects that average government indebtedness in developed economies will rise to 107% of GDP this year, i.e. higher than in 2012, even before a new phase of stimulus has begun. Perhaps that is why the yield curve in Japan initially suffered a sharp sell-off following the stimulus announcement, a sell-off that spilled into global markets and pushed up US Treasury yields too. Stocks were hurt and the Dollar fell (while JPY got stronger).

Another concern is who is going to buy all the bonds. The market is unlikely to want to absorb all the issuance needed to finance a major ramping up of fiscal spending at current yields. Yet, even modest rises in yields can have serious negative ramifications for the economy and housing in particular as the aftermath of Bernanke's tapering announcement in May 2013 showed. Mortgage applications collapsed by 65% and the Fed was forced to retreat after real 10 year UST yields rose just 100bps.

What will policy makers in developed economies do if bond markets refuse to take the paper? There are two potential solutions. Either the private sector will be forced to buy the bond, say, through additional financial repression. Or the bonds will have to be sold to the public sector, particularly central banks. In other words, Helicopter Money. Ultimately, both solutions may have to be employed.

Helicopter Money is likely to be the more immediate market moving intervention. Helicopter Money differs from QE in that the government sells bonds directly to central banks, thus avoiding the inconvenience of having to place the bonds with the private sector first before the central bank buys them. Helicopter-funded fiscal stimulus clearly has the potential to stimulate demand. Governments would obtain freshly minted cash and could proceed to spend, creating a temporary boost to aggregate demand.

Unfortunately, Helicopter funded fiscal stimulus would also create more debt and hence add to future tax and/or inflation liabilities for the private sector. Helicopter Money would therefore likely have less of an impact on aggregate demand than governments hope. Moreover, the private sector's already dim view of the future would only darken further the more the policy was used. Clearly, this is a vicious circle of short-term stimulus that leads to excessive debt that in turn leads to private sector retrenchment and hence the need for more short term stimulus.

Is there a way out of this predicament? The only sustainable way out is to reduce the overall debt stock and to increase growth rates using methods that are not funded by debt, i.e. raising productivity. Unfortunately, it is extremely painful for politicians to enforce de-leveraging and to pass productivity enhancing reforms. This is precisely why they have not done this. Only a serious crisis would lead to such measures, in our view.

In the absence of an immediate crisis, policies are more likely to emphasise even more myopic, ineffective and economically costly measures, particularly protectionism. Protectionism is extremely powerful politically and extremely damaging economically. The reason why protectionism becomes a logical choice is that domestic companies will increasingly demand economic safeguards as the economy slows, particularly against foreign competition. Dishing out protection to domestic business is a bit like kissing babies – it looks good politically.

[3] *"China's encumbered FX reserve and reserve adequacy: a reassessment"*, Citigroup, China Economics View, 7 August 2016.

Global backdrop

But, obviously, it is well documented that protectionism has two seriously adverse consequences. First, it raises tensions between countries and therefore reduces odds of trade agreements and other types of international cooperation. It may even raise the perception of foreign threats resulting in greater defence spending. Secondly, it undermines growth because protectionism is inefficient and encourages rent-seeking. So, yes, your protectionist government will look after you, but it will hurt.

Ultimately, the underlying debt issue in developed economies will only be solved through non-payment of some kind. Barring outright default, one option is for central banks to buy up all the debt and governments then cancel it. A less blatant but economically equivalent policy would be to swap the central banks' debts into zero coupon perpetuals. Either way, this policy is equivalent to pure Helicopter money, whereby central banks print money – create liabilities – without backing from assets of any integrity on the balance sheet. The result is inflation and currency debasement.

What would cancellation of central bank assets do to private sector demand? Proponents of the policy argue that Ricardian Equivalence would immediately cease to be a problem.[4] After all, there is suddenly no more debt to repay. However, this is a weak argument. The debt has obviously not just suddenly and magically disappeared. Rather, it has been transformed into currency weakness and inflation. In a sense, that makes immediately current all the expected future losses from the unsustainable debt stock. This would be bad for demand. Inflation would decimate real income and real wealth, while currency weakness would drive up import prices and erode purchasing power. In addition, weaker currencies would likely encourage capital flight, so whatever positive effects are expected from exports they may be delayed, possibly for a long time.

Yet, inflation and currency debasement could turn out to be the least painful of the various adjustment options available. It is all about who pays. The first-best solution from a political perspective is to pass the cost of adjustment on to those who do not vote, while the second-best solution is to pass the cost onto weak minority groups. This is what makes inflation and currency debasement part of the solution. Inflation hurts future generations (who do not vote yet), while devaluation hurts foreigners (who do not vote either). As for the inevitable domestic pain, government will seek to deflect the damage onto scapegoats, while seeking to protect others. The scapegoats are likely to be the weakest in society, notably immigrants, while the most powerful will be protected because they wield enough influence to secure state support when things get tough. We note that the potential for currency weakness is ultimately greatest in the US. The Dollar is already overvalued and currency weakness is an obvious remaining easing option only available to the US. A weaker Dollar would also be good for global growth (but not for foreign savers in US dollars) due to the effect a weaker Dollar would have on capital flows.

Benchmark performance

Emerging Markets	Month to date	Year to date	1 year	3 years	5 years
MSCI EM	1.44%	13.57%	2.13%	0.21%	-0.40%
MSCI EM Small Cap	1.18%	7.06%	0.16%	1.38%	0.38%
MSCI Frontier	-1.03%	-0.27%	-9.08%	-1.15%	2.18%
MSCI Asia	1.40%	8.75%	0.89%	3.52%	2.93%
Shanghai Composite	-0.06%	-14.30%	-17.76%	15.92%	5.14%
Hong Kong Hang Seng	1.94%	-1.60%	-14.36%	1.79%	-0.56%
MSCI EMEA	0.42%	18.50%	-2.59%	-5.04%	-4.02%
MSCI Latam	1.28%	34.31%	11.09%	-6.08%	-6.09%
GBI EM GD	0.43%	15.19%	7.74%	-3.34%	-2.09%
ELMI+	–	–	–	–	–
EM FX Spot	0.22%	5.16%	-2.15%	-9.87%	-8.83%
EMBI GD	0.52%	12.88%	12.07%	7.59%	6.50%
EMBI GD IG	0.55%	12.19%	10.11%	6.99%	5.53%
EMBI GD HY	0.49%	13.52%	14.46%	8.18%	7.88%
CEMBI BD	0.24%	9.77%	7.34%	6.04%	5.34%
CEMBI BD IG	0.18%	7.86%	6.65%	6.03%	5.34%
CEMBI BD Non-IG	0.33%	13.07%	8.21%	5.80%	5.36%

[4] Ricardian Equivalence is the tendency for the private sector to cut spending as public sector debts rise.

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Benchmark performance

Global Backdrop	Month to date	Year to date	1 year	3 years	5 years
S&P 500	0.49%	8.19%	6.28%	10.84%	15.16%
1-3yr UST	-0.13%	1.44%	1.36%	0.74%	0.67%
3-5yr UST	-0.35%	3.35%	3.59%	2.52%	1.77%
7-10yr UST	-0.87%	6.93%	8.01%	5.43%	4.54%
10yr+ UST	-2.23%	15.06%	15.67%	12.15%	9.18%
10yr+ Germany	-1.29%	17.18%	18.52%	13.07%	10.92%
10yr+ Japan	-1.68%	12.68%	16.66%	9.17%	6.97%
US HY	0.35%	12.40%	5.51%	4.62%	6.64%
European HY	0.39%	6.61%	4.49%	6.85%	10.20%
Barclays Ag	-0.38%	7.85%	7.84%	5.45%	5.21%
VIX Index*	-3.71%	-37.23%	-14.64%	-10.21%	-76.19%
DXY Index*	0.85%	-2.32%	-1.25%	18.98%	28.82%
CRY Index*	0.43%	3.21%	-8.33%	-35.87%	-42.78%
EURUSD	-0.78%	2.15%	0.64%	-17.13%	-21.79%
USDJPY	0.20%	-14.82%	-17.94%	5.78%	31.52%
Brent	5.56%	20.23%	-7.80%	-57.99%	-56.80%
Gold spot	-1.44%	25.44%	20.55%	1.38%	-22.57%

*VIX Index = Chicago Board Options Exchange SPX Volatility Index. *DXY Index = The Dollar Index. *CRY Index = Thomson Reuters / CoreCommodity CRM Commodity Index.
Source: Bloomberg, JP Morgan, Barclays, Merrill Lynch, Chicago Board Options Exchange, Thomson Reuters, MSCI, total returns.
Figures for more than one year are annualised other than in the case of currencies, commodities and the VIX, DXY and CRY which are shown as percentage change.

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