

Russia launches 'Sputnik V' vaccine

By Gustavo Medeiros

Russia became the first country in the world to approve a coronavirus vaccine, named 'Sputnik V'. Argentina said a deal to restructure IMF debt could take months. China's credit expansion decelerated amidst strong real estate activity. Private banks stepped up lending in Brazil as the government's economic team suffered further casualties. Industrial production and inflation surprised to the upside in India. Turkey's external accounts deteriorated as the population increased gold purchases. The Peruvian parliament approved a new government. Czech Republic's labour market remained resilient. Popular protests continued in Belarus following a recent election.

| Emerging Markets | Next year forward PE/Yield | Spread over UST | P&L (5 business days) |
|---------------------|----------------------------|-----------------|-----------------------|
| MSCI EM | 13.5 | – | 0.40% |
| MSCI EM Small Cap | 11.9 | – | -0.15% |
| MSCI Frontier | 12.0 | – | 1.90% |
| MSCI Asia | 14.3 | – | 0.38% |
| Shanghai Composite | 12.6 | – | 0.21% |
| Hong Kong Hang Seng | 8.0 | – | 2.02% |
| MSCI EMEA | 10.4 | – | 2.71% |
| MSCI Latam | 12.5 | – | 0.53% |
| GBI-EM-GD | 4.42% | – | 0.12% |
| ELMI+ | 2.39% | – | 0.39% |
| EM FX spot | – | – | 0.33% |
| EMBI GD | 4.97% | 418 bps | -0.40% |
| EMBI GD IG | 2.75% | 191 bps | -1.34% |
| EMBI GD HY | 8.18% | 745 bps | 0.79% |
| CEMBI BD | 4.48% | 391 bps | -0.05% |
| CEMBI BD IG | 2.97% | 240 bps | -0.36% |
| CEMBI BD Non-IG | 6.61% | 604 bps | 0.38% |

| Global Backdrop | Next year forward PE/Yield/Price | Spread over UST | P&L (5 business days) |
|-----------------|----------------------------------|-----------------|-----------------------|
| S&P 500 | 20.5 | – | 0.69% |
| 1-3yr UST | 0.15% | – | -0.05% |
| 3-5yr UST | 0.29% | – | -0.22% |
| 7-10yr UST | 0.69% | – | -0.89% |
| 10yr+ UST | 1.42% | – | -3.72% |
| 10yr+ Germany | -0.42% | – | -1.68% |
| 10yr+ Japan | 0.00% | – | -0.84% |
| US HY | 5.60% | 498 bps | -0.47% |
| European HY | 4.81% | 531 bps | 0.48% |
| Barclays Ag | 0.90% | 21 bps | -0.58% |
| VIX Index* | 22.05 | – | -0.16% |
| DXI Index* | 92.99 | – | -0.59% |
| EURUSD | 1.1866 | – | 1.09% |
| USDJPY | 106.54 | – | 0.55% |
| CRY Index* | 149.21 | – | 1.63% |
| Brent | 45.1 | – | 0.33% |
| Gold spot | 1948 | – | -3.91% |

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

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- Russia:** The Russian government granted regulatory approval for a coronavirus vaccine for humans. The vaccine is called 'Sputnik V' in reference to the Russian pioneer space craft. An early vaccine would grant the developer a large amount of soft power. Western pundits questioned the speed at which the vaccine was approved. Instead of questioning the legitimacy of the achievement, western scientists should be looking to collaborate with the Russians, who have led the development of several vaccines in the past, including polio vaccine in the 1960s.¹ In other news, real GDP contracted at a yoy rate of 8.5% in Q2 2020, which was better than consensus expectations.
- Argentina:** After reaching a deal with bondholders, Finance Minister Martin Guzman said negotiations with the International Monetary Fund (IMF) to restructure the USD 45bn debt "will be difficult and take months". President Alberto Fernandez said the IMF will have to "trust them" as Argentina cannot cope with further macroeconomic adjustment. The government's inability to adjust spending is forcing the central bank to finance the fiscal deficit. The monetary aggregates are therefore continuing to expand at a highly inflationary 80% yoy rate with transfers from the central bank to the treasury rising to 7.5% of GDP over the last 12 months. Total monetary liabilities now stand at 18.6% of GDP. The large monetary expansion is putting pressure on the currency, which in turn has forced the central bank to sell USD 1bn from its stock of FX reserves over the last 30 days, in spite of strict capital controls, which limit Argentinians to purchase a maximum of only USD 200 per person per month. Gross FX reserves now stand at USD 43.3bn as of 12 August 2020, which is unchanged from July, mainly due to the rise in the price of gold and a Chinese swap line. The parallel 'blue chip' exchange rate depreciated to USDARS 131, which is now 80% higher than the official exchange rate of USDARS 73.

¹ See: <https://www.mos.ru/en/news/item/62002073/>

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Consumer Prices Index (CPI) inflation was 1.9% in the month of July, or 42.4% on a yoy basis, which was nevertheless a bit lower than expected. Tight capital controls and the economic recession are helping to keep inflation from getting out of control, but they are only a temporary fix. Argentina will free itself from its dependence on foreign currency debt only when it develops its own domestic capital market and when the government learns to live within its means. Only at that point can Argentinians start to believe that their currency will maintain its value rather than be inflated away as in previous episodes.

- **China:** Credit and other economic data posted small downside surprises last week. Total social financing (TSF) rose by RMB 1.7tn in July, or 12.9% on a yoy basis. Money supply as measured by M2 decelerated to 10.7% on a yoy basis in July from 11.1% yoy in June. Industrial production (IP) rose at a yoy rate of 4.8% and retail sales dropped 1.1% in July. The real estate market continued its recovery with sales of floor space in the 30 largest cities rising at a healthy yoy rate of 10.4% in July. Volumes of sales in tier-3 cities rose even more strongly at 15% yoy in July. In other news, the Dow Jones news agency reported that two Chinese semiconductor businesses supported by the Chinese government hired more than 100 senior engineers from TSMC in Taiwan. TSMC is the world's leading semiconductor company. This shows that China will work hard to reduce its dependence on US technology in particular in the years ahead.²

- **Brazil:** Data from the Central Bank shows that the largest private banks lent BRL 574bn from 16 March to 31 July. Private lending is therefore exceeding lending from public sector banks, which stood at BRL 331bn over the same period. The expansion of private sector lending in an economic downturn stands in contrast to previous economic downturns when public sector lending accounted for the bulk of credit creation. Meanwhile, retail spending appears to be responding to fiscal and monetary stimulus as retail sales rose by 12.6% in the month of June, taking spending by households close to pre-pandemic levels. In other news, two officials from the Ministry of Finance resigned due to the challenges in execution of the privatisation programme and in the implementation of other administrative reforms. Finance Minister Paulo Guedes and the Leader of Congress Rodrigo Maia gave a joint interview, where they defended a constitutional provision that caps government spending and anchors fiscal stability in Brazil. President Jair Bolsonaro's approval rating surged to 37% in July from 32% in June, while his disapproval rate dropped to 34% from 44%, according to Datafolha, a credible pollster. There is some evidence that the increase in the president's popularity is associated with news of a BRL 600 per month income replacement programme dubbed 'corona voucher', which, if confirmed, could lead to additional fiscal pressures ahead.

- **India:** IP declined at a yoy rate of 16.6% in June, which was better than the 21% yoy consensus expectation and the 33.9% yoy drop in May. Manufacturing activity in particular improved in sequential terms. The trade balance reverted to a USD 4.8bn deficit in July after recording a USD 0.8bn surplus in June. Different measures of inflation increased at different magnitudes as the Wholesale Prices Index (WPI) inflation rose to a yoy rate of 0.6% in July from -1.8% yoy in June, whereas the Consumer Prices Index (CPI) inflation increased to 6.9% in July from 6.1% in June, both yoy.

- **Turkey:** Turkey's current account deficit narrowed to USD 2.9bn in June from USD 3.8bn in May, thus bringing the 12 month cumulative deficit to USD 15bn or approximately 2% of GDP. Imports of gold played a large role in the slower improvement of the external balance, which would only have been USD 1.7bn on a 12 months basis without gold. Foreign direct investment is close to zero in Turkey and net portfolio outflows were USD 6.4bn over the last quarter leading to a large USD 7.7bn drawdown in FX reserves.

- **Peru:** Congress passed a vote of confidence in the cabinet of Prime Minister Walter Martos. Approval came after Martos signalled a more conciliatory tone with parliament and pledged to focus his attentions on limiting the spread of the coronavirus. Martos noted that a general lockdown is inappropriate, but proposed to prohibit family and social gatherings, while implementing all-day curfews on Sundays to fight the virus. Peru has more than 535,000 coronavirus cases. With 796 deaths per million, which is third worst death rate in the world, Peru is the only Emerging Markets (EM) country in the world in the top ten in terms of death rate. Brazil, ranked 11th, is the second worst hit EM country.

- **Czech Republic:** The unemployment rate rose to 3.8% on a yoy basis in July from 3.7% in June. The good performance in the Czech Republic labour market is explained by the government's antiviral programme, 'kurzarbeit', where the government pays the wages of employees, who would otherwise have been dismissed. In other news, CPI inflation rose to 3.4% on a yoy basis in July, which was higher than the consensus expectation. The current account accumulated a CZK 1.8bn surplus in June, which was far below the expectation of a surplus of CZK 8.0bn.

- **Belarus:** Protesters continued to clash with police in the streets across the country with hundreds of thousands of people gathering on the streets of Minsk. The protests are following in the wake of alleged rigging in a recent election. The state TV company staff started a strike on Monday, shutting an important government communication tool. Over the weekend, Russia pledged military support to President Alexander Lukashenko.

² For a discussion of US-China tensions and China's likely policy response please see: ['The China Witch Hunt'](#), The Emerging View, 10 June 2020.

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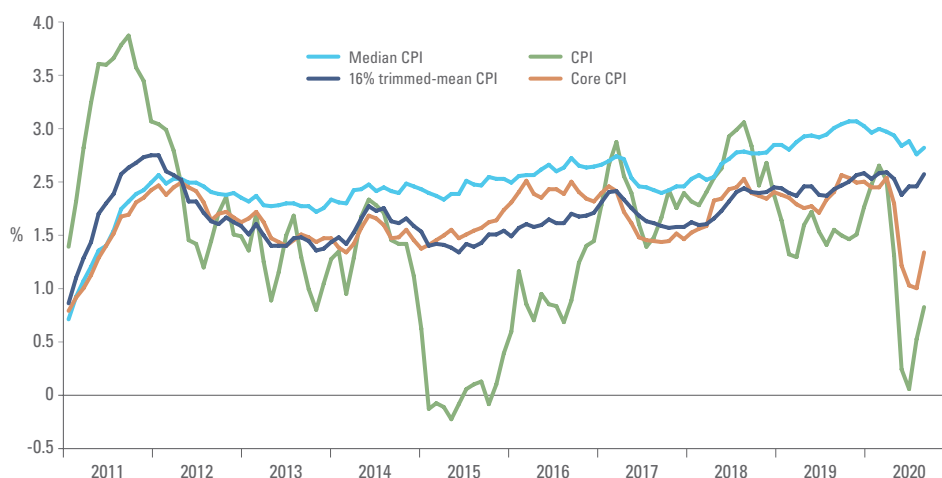
Snippets:

- **Egypt:** The Central Bank of Egypt kept the deposit and lending overnight policy rates unchanged at 9.25% and 10.25% respectively.
- **Indonesia:** The government proposed to reduce the fiscal deficit to 5.5% of GDP in 2021 from 6.2% of GDP in 2020. The primary deficit is expected to narrow to 3.4% of GDP in 2021 from 4.3% of GDP in 2020.
- **Lebanon:** The government resigned after intense popular protesters in the wake of an explosion in the port of Beirut.
- **Malaysia:** The real GDP growth rate was -51.3% qoq in Q2 2020, or 1-17.1% on a yoy basis.
- **Mexico:** IP rose 17.9% in the month of July due to a rebound in manufacturing and construction activity. However, IP remains some 17% below pre-coronavirus levels. The central bank cut the policy rate by 50bps to 4.5%, which was in line with consensus expectations and left the door open for further cuts.
- **Poland:** The rate of real GDP growth declined by 8.9% in Q2 2020. The yoy rate of CPI inflation was 3.0% in July.
- **Saudi Arabia:** State-owned oil giant Saudi Aramco generated USD 5.9bn free cash flow and USD 12.2bn cash flow from operations in Q2 2020. The company also confirmed USD 75bn in dividend payments for 2020. The company's gross debt increased by USD 84bn due to the acquisition of refiner SABIC, but net leverage remains below global peers at only half of annual EBITDA.
- **Singapore:** Q2 2020 GDP contracted 42.9% qoq, or 13.2% on a yoy basis.
- **South Korea:** Employment rose 0.3% in July, which reduced the yoy rate of employment to 1%, or 277k jobs.

Global backdrop

- **US:** The core US CPI index rose 0.6% in July, which took the yoy rate to 1.6% from 1.2% yoy in June. This means that core CPI inflation in the US over the last three months is now running at an annualised rate of 3.2%. Figure 1, using data from the Cleveland Federal Reserve, shows different measures of US inflation. They suggest that US inflation may eventually converge to the median rate of CPI inflation and the 16% trimmed-mean measure of CPI inflation (which excludes highest and the lowest eight percentile of the distribution). US Producer Prices Index (PPI) inflation also surprised to the upside with a rise of 0.6% in the month of July after declining 0.2% in June. Energy prices contributed the most to the increase in the PPI. Retail sales rose 1.2% in July after rising 8.0% in June and 18% in May, thus pointing to a slowing recovery as the number of coronavirus cases continues to increase. IP rose 3.0% in July, while nonfarm productivity spiked 7.3% in Q2 2020 amidst an increase in unit labour costs of 12.2%.

Fig 1: Cleveland Fed CPI measures (% change, yoy)



Source: Cleveland Fed. Data as at July 2020.

In other US news, presidential candidate Joe Biden announced that Kamala Harris will be his running mate in the November presidential election. Harris's appointment is in line with most pundits' expectations. She is seen as a competent "tough on crime" lawyer from South-Asian and African origins. In the primaries for the Democrat Party, she defended healthcare reform and a system of progressive taxation.

Global backdrop

In other election-related news, the level of political noise continues to rise amidst apparent efforts by the Trump Administration to decline additional funding for the US Post Office, which is likely to play a key role in the upcoming election on account of coronavirus infections.³

On the fiscal front, market participants continue to hope for new spending and/or tax cut pledges before the elections, but negotiations for a comprehensive bill now seem to be at a standstill. House Speaker Nancy Pelosi said she would not re-start negotiations until Republicans are prepared to accept a USD 2trn fiscal expansion. While substantially smaller than her initial USD 3.5trn demand, Pelosi's proposal is nevertheless still twice as large the USD 1trn proposed by the Trump Administration. The Democrats have an incentive to reach a deal before President Donald Trump's executive order comes into effect at the end of August. However, given that the Democratic National Convention takes place between 17 and 20 of August and the Republican National Convention takes place from 24 to 27 of August there is little time for further negotiations before the end of August. Another deadline looms on 30 September, when a new spending bill is required to prevent a partial shutdown of the US government. While a shutdown in the middle of a pandemic is undesirable for both parties, history has shown that they do happen. There have been no fewer than 21 government shutdowns in the US since 1976.⁴

On the trade front, US-China trade talks originally scheduled to take place on 15 August were postponed indefinitely due to scheduling complications. Tensions between the US and China are running very high as both the political parties in the US have opted to blame China for America's home grown economic and coronavirus-related problems.

- **Coronavirus:** The total number of coronavirus cases now exceeds 22 million with 14.5m recovered and 770k deaths as of Sunday evening. Half of the cases are concentrated in the US, Brazil, and India, where the case numbers appear to have stabilised at high plateaux of between 50k and 70k new cases per day. Cases are starting to increase in Spain, France, and Germany, where the relaxation of rules over the summer appears to have triggered a resurgence in the number of cases. Rising case numbers could slow the strong ongoing EU economic recovery if mobility restrictions are re-introduced. On the other hand, hopes are increasing that a vaccine could become widely available earlier than expected following the Russian breakthrough discussed at the top of this report.
- **EU:** Euro area IP rose 9.1% in June following a 12.3% gain in May. The level of IP is now just shy of 89% of the level seen pre-coronavirus. UK real GDP contracted by 20.4% in Q2 2020. This is the worst GDP print since the beginning of the series in 1955 and the worst across major economies. The UK economy had a particularly large concentration in consumer services.

Benchmark performance

| Emerging Markets | Month to date | Quarter to date | Year to date | 1 year | 3 years | 5 years |
|---------------------|---------------|-----------------|--------------|---------|---------|---------|
| MSCI EM | 1.41% | 10.55% | -0.15% | 16.41% | 4.05% | 7.74% |
| MSCI EM Small Cap | 2.24% | 11.74% | -2.42% | 10.07% | 0.47% | 3.13% |
| MSCI Frontier | 4.08% | 3.42% | -12.85% | -9.61% | -2.16% | 1.23% |
| MSCI Asia | 1.91% | 10.64% | 5.50% | 22.88% | 6.10% | 9.08% |
| Shanghai Composite | 1.58% | 13.72% | 12.58% | 22.49% | 3.69% | -1.06% |
| Hong Kong Hang Seng | 2.26% | 6.59% | -4.99% | 8.24% | 2.41% | 2.42% |
| MSCI EMEA | 2.50% | 5.82% | -16.68% | -5.70% | -2.86% | 0.83% |
| MSCI Latam | -2.38% | 8.31% | -29.74% | -19.87% | -7.29% | 1.74% |
| GBI EM GD | -0.78% | 2.22% | -4.83% | 0.56% | 1.13% | 3.84% |
| ELMI+ | -0.03% | 1.79% | -3.65% | 0.30% | 0.11% | 2.07% |
| EM FX Spot | -0.59% | 1.39% | -9.71% | -7.17% | -6.10% | -3.75% |
| EMBI GD | 0.91% | 4.66% | 1.77% | 4.35% | 4.72% | 6.27% |
| EMBI GD IG | 0.05% | 4.26% | 7.52% | 9.23% | 7.65% | 7.02% |
| EMBI GD HY | 2.00% | 5.16% | -4.92% | -1.44% | 1.38% | 5.38% |
| CEMBI BD | 0.72% | 3.05% | 2.89% | 6.12% | 5.23% | 5.85% |
| CEMBI BD IG | 0.39% | 2.71% | 4.70% | 6.38% | 5.80% | 5.45% |
| CEMBI BD Non-IG | 1.17% | 3.52% | 0.35% | 5.65% | 4.44% | 6.52% |

³ For a discussion of the mounting risks in the US election see the Global Backdrop section here: ['New highs for Chinese economic data and US anti-China hysteria'](#), Weekly investor research, 3 August 2020.

⁴ <https://www.vox.com/policy-and-politics/2018/1/19/16905584/government-shutdown-history-clinton-obama-explained>

Benchmark performance

| Global Backdrop | Month to date | Quarter to date | Year to date | 1 year | 3 years | 5 years |
|-----------------|---------------|-----------------|--------------|---------|---------|---------|
| S&P 500 | 3.20% | 9.02% | 5.65% | 21.05% | 13.19% | 12.27% |
| 1-3yr UST | -0.08% | 0.02% | 3.03% | 3.61% | 2.60% | 1.87% |
| 3-5yr UST | -0.28% | 0.00% | 6.03% | 6.06% | 3.93% | 3.00% |
| 7-10yr UST | -1.04% | -0.18% | 10.93% | 9.00% | 6.39% | 4.73% |
| 10yr+ UST | -4.20% | -0.15% | 21.02% | 14.15% | 11.52% | 8.13% |
| 10yr+ Germany | -2.07% | -0.47% | 5.38% | -3.17% | 6.76% | 5.28% |
| 10yr+ Japan | -0.96% | -0.29% | -2.39% | -5.39% | 1.59% | 3.18% |
| US HY | 0.09% | 4.78% | 0.80% | 5.25% | 4.75% | 6.18% |
| European HY | 1.18% | 2.72% | -3.37% | -0.36% | 1.52% | 3.34% |
| Barclays Ag | -0.63% | 2.54% | 5.60% | 5.21% | 3.92% | 4.02% |
| VIX Index* | -9.85% | -27.54% | 60.01% | 19.38% | 41.80% | 69.35% |
| DXY Index* | -0.38% | -4.52% | -3.52% | -5.25% | -0.67% | -3.94% |
| CRY Index* | 3.84% | 8.14% | -19.69% | -12.44% | -15.17% | -24.08% |
| EURUSD | 0.75% | 5.63% | 5.81% | 7.11% | 1.22% | 7.10% |
| USDJPY | 0.67% | -1.29% | -1.91% | -0.09% | -2.77% | -14.35% |
| Brent | 4.25% | 9.70% | -31.61% | -23.02% | -11.54% | -7.39% |
| Gold spot | -1.41% | 9.38% | 28.39% | 30.22% | 51.24% | 74.29% |

*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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