What next for Argentina?

By Gustavo Medeiros

Alberto Fernandez was elected president in Argentina. Protesters took to the streets in Bolivia in anger at alleged election fraud. Brazil's pension reform was approved and should yield some USD 200bn in fiscal savings over the next 10 years. Chilean President Pinera sacked his Cabinet after large-scale protests. Indonesia's Jokowi reappointed reformist Indrawati as Finance Minister. In Lebanon, Prime Minister Saad Hariri announced sweeping budgetary reforms following protests. Hong Kong repealed a controversial extradition bill. Modi suffers setback in local elections in India. All sanctions against Turkey were removed after a permanent ceasefire was agreed in northern Syria.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	11.8	–	1.17%
MSCI EM Small Cap	11.0	–	0.81%
MSCI Frontier	9.2	–	0.24%
MSCI Asia	12.5	–	0.81%
Shanghai Composite	10.6	–	0.57%
Hong Kong Hang Seng	7.9	–	-0.70%
MSCI EMEA	9.3	–	1.87%
MSCI Latam	12.9	–	3.07%
GBI-EM-GD	5.12%	–	0.86%
ELMI+	4.95%	–	0.37%
EM FX spot	–	–	0.50%
EMBI GD	5.17%	334 bps	0.13%
EMBI GD IG	3.53%	167 bps	0.03%
EMBI GD HY	7.38%	558 bps	0.24%
CEMBI BD	5.08%	335 bps	0.27%
CEMBI BD IG	3.68%	195 bps	0.03%
CEMBI BD Non-IG	7.08%	534 bps	0.61%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	16.7	–	1.23%
1-3yr UST	1.63%	–	-0.09%
3-5yr UST	1.64%	–	-0.24%
7-10yr UST	1.81%	–	-0.37%
10yr+ UST	2.31%	–	-0.79%
10yr+ Germany	-0.36%	–	-0.05%
10yr+ Japan	-0.13%	–	0.08%
US HY	5.47%	360 bps	0.31%
European HY	3.85%	427 bps	-0.07%
Barclays Ag	1.40%	-41 bps	-0.17%
VIX Index*	12.65	–	-1.60%
DXY Index*	97.79	–	0.47%
EURUSD	1.1089	–	-0.55%
USDJPY	108.73	–	0.10%
CRY Index*	178.37	–	2.62%
Brent	61.9	–	4.94%
Gold spot	1508	–	1.57%

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

Emerging Markets

- Argentina: Alberto Fernandez was elected President of Argentina. With 97.9% of the votes counted, he led incumbent President Mauricio Macri by 48.1% versus 40.4%. The tighter than expected result was also reflected in a split parliament. Alberto Fernandez's first speech was conciliatory. He accepted Macri's invitation to a transition breakfast meeting today.

Attention will now shift to the composition of Fernandez's economic team, his choice of economic policies and negotiations with both the IMF and bondholders. Alberto Fernandez has pledged not to touch USD deposits in the banking system and ruled out a haircut on external debt in a future re-profiling. Due to the weak state of the economy, we expect Fernandez to have a short window to resolve the current economic problems.

We believe that over the last year Macri has achieved most of the macroeconomic adjustment required to stabilise inflation and the fiscal accounts. Therefore, a further year of adjustment should pave the way for a sustained economic recovery. We also believe that former President Cristina Fernandez de Kirchner will not have much influence over economic policy.[1]

Meanwhile, the Central Bank tightened capital controls last night, so that individuals can only buy USD 200 per month (compared to USD 10,000 per month until yesterday). Tighter capital controls reduce the pace of drawdown of FX reserves, which, for a period of time, can reduce the risk of non-repayment for bond holders. Central Bank reserves have continued to decline due to debt repayments and FX interventions. Reserves stood at USD 45.5bn as at 25 October, which is USD 22.8bn below the level prior to the primary election in early August. In other news, the current account surplus in September surprised on the upside at USD 1.74bn, which is the thirteenth consecutive month of surplus.

[1] For more details on Argentina's situation see: *'The path to averting a default in Argentina'*, Market Commentary, 14 August 2019, and *'Argentina Q&A'*, The Emerging View, 23 August 2019.

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Emerging Markets

- Bolivia: Riots broke out across the country after late changes in the election count showed a surprising surge in support for incumbent President Evo Morales who, according to the final official vote count, secured 47.08% of the votes versus 36.51% for the centrist candidate Carlos Mesa. A margin of 10% or more eliminates the need for a run-off second round. The Organization of American States (OAS) expressed deep concern over a "...dramatic and hard-to-explain change in the trend of preliminary results". The OAS alongside the European Union, US, Brazil, Colombia and Argentina all expressed support for a run-off. Morales has faced growing discontent after he ignored a referendum limiting presidential terms. He was first elected president in 2006 and this was his fourth re-election as President of Bolivia.

- Brazil: The landmark Social Security reform was approved in the second and final vote in the Senate. Under the reform, total savings of BRL 800bn (USD 200bn) will be achieved over 10 years by gradually increasing the retirement age of new public sector employees and reducing various benefits. In a new reform initiative, the government has also begun preparations for a reduction in import tariffs for industrial durable goods from a weighted average of 13.6% as of today to 6.4% over the next four years. Meanwhile, mid-month the consumer prices inflation (CPI) index increased 0.09% in the month to 15 October. The yoy inflation rate dropped from 3.22% in September to 2.72% in October due to base effects.

- Chile: President Sebastian Pinera dismissed all his ministers in a cabinet reshuffle and lifted a one-week curfew after more than one million people protested in Santiago yesterday. The protests have been ongoing for some weeks and some nineteen people are reported to have been killed and thousands injured. The protests are the largest since the Pinochet era. Last week, Pinera apologised for failing to anticipate the outbreak of social unrest and announced a package of social measures, which included a higher basic pension and higher minimum wages. He also cancelled a planned 9% increase in electricity bills and pledged to use state resources to help to cover the cost of expensive medical treatments. In other news, the central bank cut its policy rate by 0.25% to 1.75% and maintained an accommodative tone as the protests weighed on business confidence.

- Indonesia: President Joko Widodo (aka 'Jokowi') reappointed Sri Mulyani Indrawati as Finance Minister. This sends a strong signal of commitment to economic reform, including labour market reform. Jokowi also nominated his main political opponent, General Prabowo Subiano, for the post of defence minister, which is likely to increase political stability. In other news, Bank Indonesia (BI) cut the seven-day repo policy rate by 0.25% to 5.0%. Further cuts are likely as the economy grows slower than potential and inflation remains within the BI's 2.5%-4.5% target range.

- Lebanon: Last Monday, Prime Minister Hariri announced sweeping reforms aimed at reducing the country's fiscal deficit from 7.0% GDP in 2019 to 0.6% GDP in 2020. The reform includes halving the salary of ministers, levying a one-off USD 2.9bn tax on banks, cutting electricity subsidies by USD 1.0 bn per year and privatising state-owned telecommunication companies. Protesters remain on the streets. They are demanding an end to sectarian political disputes and corruption, which have undermined the quality of public services, such as electricity, telecommunications, health care and education.

- Hong Kong: The government officially removed a controversial extradition bill following months of social unrest. Media reports indicate that Prime Minister Carrie Lam may be replaced next year after failing to quell violent pro-democracy protests. In other news, CPI inflation declined to a rate of 3.2% yoy in September from 3.5% yoy in August as lower housing prices partially mitigated higher food prices.

- India: President Modi's BJP party lost ground in local elections in the highly industrialised Haryana and Maharashtra states. The results reflect the current economic slowdown and may add pressure on the government to accelerate economic reforms, including bank recapitalisation and privatisations.

- Turkey: Turkey and Russia agreed to create a safe zone in the area captured by the Turkish army in northern Syria following a recent decision by the United States to pull out troops. The agreement includes the withdrawal of Kurds from the 30-kilometre strip of land stretching to the Iraqi border and joint patrols across the area. US President Donald Trump lifted all sanctions imposed on Turkey after Turkish President Recep Tayyip Erdogan promised a permanent cease fire. In other news, the Turkish central bank cut the policy rate by 2.5% to 14%, which was larger than the expected 1% cut.

- Angola: The National Bank of Angola allowed the Kwanza to depreciate outside its crawling peg band and increased the reserve requirement ratio (RRR) for banks from 17% to 22% in a bid to contain inflation. The official exchange rate has depreciated by 32% this year. Currency weakness supports the ongoing macro-economic adjustment without impacting the government's ability to serve debt. The majority of Angola's revenues come from oil and are denominated in USD.

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Emerging Markets

Snippets:

- China: The People's Bank of China injected RMB 250bn (USD 35bn) into the banking system last week via seven-day repos. The injection was in response to tight conditions in the money market, which were caused by large tax payments from firms and households in the month of September.
- Colombia: The government awarded wind and solar power generation projects worth USD 2.2bn last week in a bid to diversify the country's energy sources. Hydroelectric power currently generates 70% of Colombia's energy.
- Costa Rica: Finance Minister Rocio Aguilar resigned from her post after a political attack from the country's Controller General. Mrs. Aguilar was instrumental in improving the profile of the government's debt stock and oversaw the approval of a fiscal responsibility law in 2018.
- Ethiopia: President Abdel Fattah el-Sisi of Egypt and Prime Minister Abiy Ahmed of Ethiopia agreed to resume negotiations over the Grand Ethiopia Renaissance Dam in a bid to resolve a disagreement over the pace at which the dam will be filled after its completion.
- Hungary: The National Bank of Hungary kept the main monetary policy target rate unchanged at -0.05% in line with expectations.
- Kenya: The government delayed the construction of a USD 3.5bn highway between Nairobi and Mombasa by two years in order to stabilise the government's debt levels.
- Malaysia: CPI inflation declined to 1.1% on a yoy basis in September from 1.5% yoy in the previous month, surprising on the downside due to lower food, communication and recreation prices.
- Mexico: The unemployment rate remained stable at 3.5% (seasonally adjusted) in September. Wages increased at a rate of 6.2% yoy in September, while CPI inflation rose by only 3.01% on a yoy basis in the first two weeks of October. Retail sales were 0.3% mom (sa) versus an expected contraction of 0.1% mom (sa).
- Mozambique: Incumbent President Filipe Nyusi was re-elected with 73% of the total vote. Nyusi's party Frelimo, which has been in power since the end of the civil war in 1992 also won the majority of the seats in parliament. The main opposition party Renamo rejected the results.
- Namibia: The Finance Ministry lowered Namibia's real GDP growth rate forecast from 0.2% yoy to -1.5% yoy for the 2019-20 fiscal year. However, the fiscal deficit was also revised sharply lower from 4.1% GDP to 0.6% GDP. Namibia has been adversely impacted by the slowdown in South Africa's economy, but prudent fiscal policies are likely to help to rekindle private sector investment.
- Oman: The fiscal dynamics deteriorated in August as the government's budget deficit increased to 7.5% of the 2019 estimated GDP on a 12-month basis from 6.2% of GDP in June.
- Philippines: The Central Bank cut the RRR for banks by 1.0% to 14% in a bid to stimulate the economy as the real GDP growth rate slowed to 5.5% on a yoy basis in Q2 2019.
- Poland: Retail sales expanded by 5.3% on a yoy basis in September versus 8.1% yoy expected. This compares to 6.0% yoy in August.
- Russia: The Central Bank of Russia cut the policy interest rate by 0.5% to 6.5%. More rate cuts are likely after staff revised the 2019 inflation forecast from a range of 4.0% to 4.5% yoy to 3.2% to 3.7% yoy.
- Singapore: The rate of unemployment inched higher from 2.2% in Q2 2019 to 2.3% in Q3 2019. Employment improved in construction but declined in manufacturing. Industrial production (IP) rose by 0.1% on a yoy basis in September and was better than expected (-4.8% yoy). IP was buoyed by stronger than anticipated output of semiconductors and biomedical equipment.
- South Africa: The National Assembly approved the Eskom Appropriation bill, which allocates ZAR 59bn (USD 4bn) to the ailing utility company. In other news, consumer prices rose by 4.1% on a yoy basis in September, down from 4.3% yoy in August. Softer home rental prices compensated upside surprises in food prices.
- Thailand: Tourist arrivals increased at a rate of 10.1% yoy in September, led by an increase in Asian visitors. The government announced a small increase in public expenditure as well as measures to support the property sector. Exports declined at a rate of 1.4% yoy in September and imports were 4.2% lower yoy over the same period. The trade surplus in the first nine months of 2019 rose to USD 7.4bn.
- Taiwan: IP declined at a rate of -0.75% on a yoy basis in September after rising at a rate of 2.35% yoy in August. Production of electronic and communication products are recovering, but low global capital spending is weighting on non-tech items, such as chemicals and machinery. Export orders contracted by -4.9% on a yoy basis in September.
- Ukraine: The National Bank of Ukraine cut the policy rate by 1.0% to 15.5% versus an expected cut of 0.5%. CPI inflation declined sharply from a rate of 8.8% yoy in August to 7.5% yoy in September.
- Uruguay: A run-off election will be held between Daniel Martinez and Luis Lacalle Pou on 24 November as neither candidate achieved the minimum 50% share of the vote required to be elected in the first round yesterday.

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Global backdrop

In the UK, Boris Johnson's European Union (EU) Withdrawal Agreement Bill was approved by the parliament, but Parliament demanded more time to scrutinise the bill. Attention this week will focus on the politics of the new deadline.

In news relating to the US trade war against China, China announced a new legal framework for intellectual property rights, which significantly improves the odds of a meaningful trade deal in mid-November, in our view. The new rules, which take effect on 1 January 2020 aim to protect trade secrets, forbid forced technology transfers and stop discrimination against foreign companies. Furthermore, China has offered a tariff-free quota for 10mn tons of US soybeans. A speech by US Vice President Michael Pence also struck a more conciliatory tone.

In the US, the risk of a recession continues to increase. Last week, a report from the National League of Cities revealed that two thirds of all finance officers in the 451 largest cities in the US now expect recession next year. While the flash PMI increased to 51.5 in October from 51.1 in September, durable goods orders declined 1.1% in the month of September with most of the decline attributable to strikes at General Motors and poor aircraft output from Boeing.

In the Eurozone, the composite PMI inched 0.1 points higher to 50.2 in October, signalling a stabilisation at low levels. German PMI rose 0.1 points to 48.6, while French PMI accelerated 1.7 points to 52.6. In Canada, the Liberal Party won a narrow victory, which enables Prime Minister Justin Trudeau to form a minority government.

Benchmark performance

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	3.60%	3.60%	9.96%	12.38%	7.00%	3.86%
MSCI EM Small Cap	3.22%	3.22%	5.31%	9.15%	2.69%	1.33%
MSCI Frontier	0.84%	0.84%	11.57%	11.12%	7.29%	-0.39%
MSCI Asia	3.26%	3.26%	9.34%	12.93%	7.57%	5.37%
Shanghai Composite	1.72%	1.72%	21.37%	16.28%	0.35%	7.34%
Hong Kong Hang Seng	2.61%	2.61%	7.28%	6.74%	6.13%	4.00%
MSCI EMEA	3.80%	3.80%	9.65%	12.84%	5.72%	0.46%
MSCI Latam	5.04%	5.04%	11.91%	8.69%	5.47%	1.30%
GBI EM GD	3.17%	3.17%	11.28%	14.84%	4.23%	0.83%
ELMI+	2.02%	2.02%	3.46%	5.25%	2.60%	0.19%
EM FX Spot	2.17%	2.17%	-0.37%	-0.21%	-2.92%	-6.02%
EMBI GD	0.35%	0.35%	13.38%	13.94%	4.82%	5.55%
EMBI GD IG	0.16%	0.16%	15.40%	16.81%	5.42%	5.32%
EMBI GD HY	0.57%	0.57%	11.32%	11.03%	4.20%	5.72%
CEMBI BD	0.74%	0.74%	11.46%	11.87%	5.23%	5.20%
CEMBI BD IG	0.21%	0.21%	11.77%	12.77%	4.83%	4.69%
CEMBI BD Non-IG	1.47%	1.47%	11.00%	10.64%	5.91%	5.92%

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Benchmark performance

Global Backdrop	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
S&P 500	1.64%	1.64%	22.54%	14.01%	14.41%	11.24%
1-3yr UST	0.11%	0.11%	3.19%	4.42%	1.60%	1.27%
3-5yr UST	-0.16%	-0.16%	5.02%	7.47%	1.89%	2.01%
7-10yr UST	-0.71%	-0.71%	9.07%	13.47%	2.45%	3.15%
10yr+ UST	-2.89%	-2.89%	16.31%	23.90%	4.07%	5.48%
10yr+ Germany	-3.61%	-3.61%	12.95%	15.72%	3.96%	6.51%
10yr+ Japan	-0.77%	-0.77%	5.37%	7.84%	1.55%	4.53%
US HY	0.53%	0.53%	11.99%	8.41%	5.81%	5.25%
European HY	-0.21%	-0.21%	8.48%	5.26%	3.68%	4.36%
Barclays Ag	0.05%	0.05%	6.38%	8.57%	2.45%	1.81%
VIX Index*	-22.11%	-22.11%	-50.24%	-47.64%	-21.87%	-12.09%
DXY Index*	-1.59%	-1.59%	1.68%	1.49%	-0.56%	14.50%
CRY Index*	2.55%	2.55%	5.05%	-8.77%	-5.73%	-34.44%
EURUSD	1.73%	1.73%	-3.31%	-2.50%	0.96%	-12.93%
USDJPY	0.60%	0.60%	-0.88%	-3.25%	3.82%	0.53%
Brent	1.79%	1.79%	15.00%	-20.29%	24.46%	-28.08%
Gold spot	2.41%	2.41%	17.58%	22.65%	18.22%	22.74%

*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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