

The sun rises in the east: China rising

By Gustavo Medeiros

Chinese aggregate lending soars. Brazil's parliament approves an extraordinary budget and grants powers to the central bank to purchase assets. Ecuador requests the extension of coupon payments until August. Thailand approves a massive fiscal package. Argentina increases support to small companies. Malaysia extends the shutdown to the end of April. Venezuela gets aid and looks to privatise the gasoline market.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	10.4	–	3.48%
MSCI EM Small Cap	8.7	–	5.32%
MSCI Frontier	7.6	–	1.89%
MSCI Asia	11.0	–	3.16%
Shanghai Composite	9.5	–	0.69%
Hong Kong Hang Seng	7.5	–	2.99%
MSCI EMEA	8.7	–	4.17%
MSCI Latam	9.8	–	6.24%
GBI-EM-GD	5.28%	–	3.75%
ELMI+	3.51%	–	1.92%
EM FX spot	–	–	2.28%
EMBI GD	6.78%	598 bps	2.53%
EMBI GD IG	4.08%	324 bps	1.71%
EMBI GD HY	10.92%	1,016 bps	3.65%
CEMBI BD	6.42%	575 bps	1.68%
CEMBI BD IG	4.39%	372 bps	0.88%
CEMBI BD Non-IG	9.69%	902 bps	2.91%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	16.1	–	11.01%
1-3yr UST	0.26%	–	-0.02%
3-5yr UST	0.46%	–	-0.12%
7-10yr UST	0.77%	–	-1.01%
10yr+ UST	1.41%	–	-2.93%
10yr+ Germany	-0.35%	–	-1.50%
10yr+ Japan	0.00%	–	-0.51%
US HY	8.17%	747 bps	6.94%
European HY	8.18%	781 bps	3.40%
Barclays Ag	1.17%	40 bps	1.31%
VIX Index*	41.17	–	-5.63%
DXI Index*	99.24	–	-1.45%
EURUSD	1.0945	–	0.49%
USDJPY	107.71	–	-0.97%
CRY Index*	127.94	–	-0.02%
Brent	31.9	–	-3.60%
Gold spot	1715	–	4.11%

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

Emerging Markets

- **China:** There was a big rebound in lending in March with aggregate funding surging to CNY 5.2trn versus far more modest expectations of CNY 3.1trn. Household lending responded positively to fewer movement restrictions in March. Policy support boosted corporate and local government demand. Bank lending rose to CNY 2.9trn in March from CNY 0.9trn in February. Corporate bonds issuance surged to CNY 1.0trn from CNY 0.4trn in January and February, while government bond issuance rose to CNY 0.6trn in March from CNY 0.2trn in February. China is prioritising liquidity to the economy in order to avoid defaults over cutting policy rates. By keeping policy rates far from negative levels, the authorities are keeping dry their powder for a situation, where demand is in a position to respond positively to monetary policy, which is not the case in a coronavirus shock. The trade surplus is USD 19.9bn, roughly in line with expectations (USD 20.0bn). Exports and imports are both much stronger than expected: Exports down 6.6% vs -13.9% expected, while imports down 0.9% versus -9.8% yoy expected.

In other economic news, energy usage stalled at around 80% of normal levels in early April, thus highlighting the fact that demand bottlenecks persist in spite of the government's push to normalise the economy. Also, consumer prices index (CPI) inflation dropped to 4.3% on a yoy basis in March from 5.2% yoy in February, which was a surprise relative to the median consensus expectations by 0.6%, or one standard deviation. China's currency reserves dropped by USD 46bn to USD 3.06trn. About one-third of the drop was due to the rise in the US dollar over the period.

- **Brazil:** CPI inflation declined to 3.3% on a yoy basis in March from 4.0% in February. Central Bank President Roberto Campos said they could intervene in larger size after selling USD 10.7bn in spot and futures markets during March. The Supreme Court issued a ruling guaranteeing the right of individual states to determine their own quarantine measures in response to coronavirus, which was a setback to President Jair Bolsonaro, who insists on reopening the economy sooner rather than later. Bolsonaro's position is opposed by his own Minister of Health, Luiz Henrique Mandetta, as well as state governors. In other news, Brazil's Lower House approved a constitutional amendment, which allows for a temporary increase in the fiscal deficit in order to fight

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coronavirus. This means that the primary deficit in 2020 is likely to increase from BRL 124bn to BRL 420bn (or 6% of GDP). All the increases in expenditures are extraordinary and linked to the coronavirus. Brazil's debt to GDP ratio is likely to rise to above 85% of GDP, but the low policy rate of 3.75% combined with the fact that approximately half of the federal government's debt is in floating notes reduces the impact on the overall debt burden. The constitutional amendment also grants permission to the Central Bank to purchase government bonds in both local and international markets, both in the primary and secondary markets.

- **Ecuador:** Ecuador's Ministry of Finance issued a consent solicitation to bondholders for postponement of the repayment of coupons due between now and 15 August. The country maintains a strong willingness to pay and conditioned the proposed coupon delay on entry into a new IMF programme to be negotiated over the course of the summer. Ecuador has been heavily affected by coronavirus, thus putting intense pressure on medical facilities and morgues, particularly in Guayaquil, which is the country's main business centre. The Minister of Finance Richard Martinez estimates the impact of revenues from lower oil at USD 4.1bn or 11% of total revenues. Martinez correctly emphasised Ecuador has a temporary liquidity mismatch that needs addressing to avoid turning into a solvency problem.¹ In other news, former president Rafael Correa was found guilty of bribery and convicted to eight years in prison. He is currently in exile in Belgium. He has the right to appeal, but the court ruling is a setback to his ambition of returning to Ecuador to contest next year's presidential election.
- **Thailand:** The Cabinet approved a fiscal package worth 11% of GDP, including THB 1trn, or 6% of GDP, in new government borrowing until 2021. The package also includes THB 0.9trn of support from Bank of Thailand (BoT). The package includes health-related measures and the equivalent of USD 150 per month in cash handouts for approximately 9 million people until September. BoT will purchase corporate debt and provide soft loans to banks to extend loans to small companies at a rate of 2%. In other news, CPI inflation declined to negative levels at -0.5% on a yoy basis in March from +0.7% yoy in February.
- **Argentina:** The state-owned oil company YPF announced a 50% cut in production in the Loma Campana field, which is one of the largest within the Vaca Muerta shale area. The decision to cut production was motivated by lower demand for product and scarcity of storage facilities. The decision to cut production prompted fears of layoffs in the coming months. President Alberto Fernandez announced a package worth ARS 120bn (USD 1.8bn) to assist provinces as he extended the quarantine until 26 April. A survey by the Fundacion Observatorio Pyme (FOP) showed that 25% of small and medium companies will not be able to pay wages and fixed expenses in April, even with government support. However, only 6% are so far considering halting operations.
- **Malaysia:** Prime Minister Muhyiddin Yassin announced an extension to the ongoing shutdown over coronavirus from 14 April to 28 April, thereby increasing the likelihood of a mild economic contraction in 2020. Selected sectors, such as machinery and equipment, will be allowed to reopen in stages. The government also announced an additional stimulus of MYR 10bn, or 0.7% of GDP, to boost the wage subsidy programme. In other news, industrial production in February surprised on the upside by rising by 5.8% on a yoy basis from 0.6% yoy in January.
- **Venezuela:** The United States (US) Office of Foreign Assets Control (OFAC) extended until 22 July the stay, which prevents holders of the defaulted PDVSA 2020 bond from enforcing their collateral claim (50.1% of shares on CITGO). The stay was first imposed in October and has since been replaced twice. In other news, the Venezuelan government announced that it is studying the possibility of privatising the gasoline market. This market is not subject to economic sanctions. Shortages of fuel in Venezuela have taken gasoline prices above USD 2 per litre, which is a major departure from the past, where gasoline was sold at less than USD 0.01 per litre. The United Nations sent a plane with medical supplies and kits for health workers in the country.

Snippets:

- **Angola:** The government unveiled a cabinet reshuffle, which saw the number of ministries reduced from 28 to 21. The Ministry of Finance also issued a statement reiterating its commitment to the reform agenda currently under implementation within the IMF programme.
- **Colombia:** Consumer confidence dropped to -23.8 in March from -11.2 in February. The government announced new measures to buffer the impact of coronavirus, including payroll support for small companies and a freeze on pension fund contributions.
- **Egypt:** FX reserves declined by USD 5.9bn in March, mostly driven by portfolio outflows. However, FX reserves remain high at USD 40bn, which is equivalent to seven months of imports.
- **Hong Kong:** The government pledged an additional HKD 137.5bn in fiscal measures. This takes total fiscal support to HKD 287.5bn, or approximately 10% GDP. The new measures include a 50% payroll subsidy across industries as well as loan guarantees.
- **Hungary:** The National Bank of Hungary hiked the 1-week lending rate by 95bps to 1.85% in order to provide support for HUF, while at the same time announcing purchases of bonds on the secondary market to provide liquidity and keep yields low at the long end of the curve. The overnight deposit rate was unchanged at -0.05%.

¹ See: *'The merits of Ecuador's approach'*, Market Commentary, 9 April 2020.

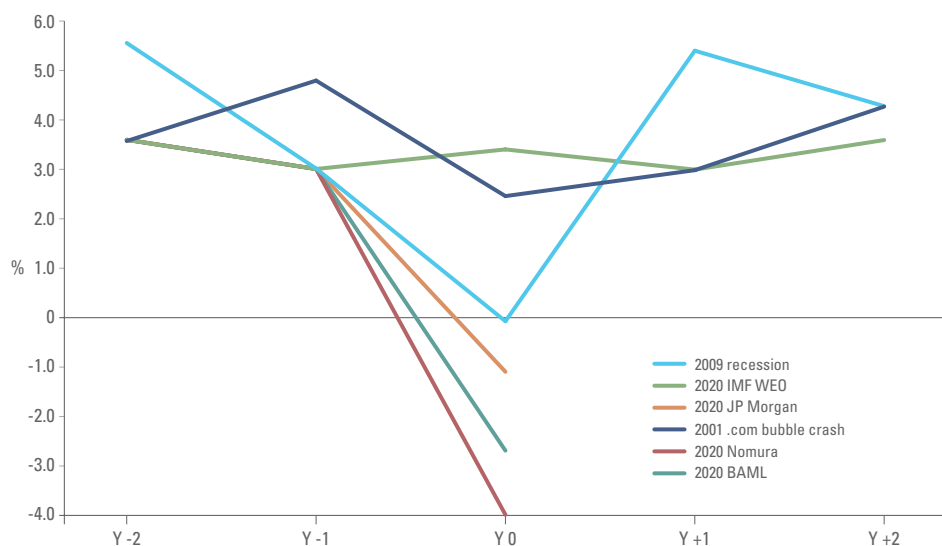
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- **India:** Industrial production expanded at a yoy rate of 4.5% in February from 2.1% yoy in January. Industrial production may now enter a temporary decline as the national lockdown started in 24 March. Meanwhile, CPI inflation declined to 5.9% on a yoy basis in March from 6.6% yoy in February, mainly due to lower food prices.
- **Kazakhstan:** The National Bank of Kazakhstan (NBK) cut the policy rate by 250bps to 9.5% in an emergency meeting. The rate cut follows a rate hike just one month ago. The about face reflects NBK's shifting objective from inflation control and financial stability to growth. The Ministry of Finance announced a fiscal stimulus totalling KZT 5.9tn, or almost 9% of GDP.
- **Mexico:** The Mexican government committed to cutting oil production by just 100,000 barrels per day, or 5.5% of total production as part of the agreement reached with the Organization of the Petroleum Exporting Countries (OPEC) at the weekend. In other news, the yoy rate of CPI inflation declined to 3.3% in March from 3.7% in February.
- **Pakistan:** The Executive Board of the IMF is scheduled to meet on 16 April to decide on a USD 1.4bn extra loan to Pakistan for budgetary purposes under the Rapid Financing Instrument (RFI). The World Bank is working on repurposing USD 2bn of loans to build a safety-net programme to support employment through public works and to enhance food security.
- **Peru:** The central bank cut the policy rate by 100bps to 0.25%, which is the lowest rate in Latin America.
- **Philippines:** CPI inflation declined marginally to a yoy rate of 2.5% in March from 2.6% yoy in February.
- **Poland:** A 'Financial Shield' programme of loans worth PLN 100bn (4.3% of GDP) to non-financial corporations was unveiled by the government. Under the programme, after one year firms that have kept open maintained current employment levels will be exempt from repaying the loan. The National Bank of Poland cut the policy rate by 50bps to 0.5% and pledged to provide funding towards the 'Financial Shield' by directly purchasing government bonds.
- **South Africa:** President Cyril Ramaphosa extended the national lockdown to the end of the month and said the government was developing an extensive package of economic measures to deal with the coronavirus crisis and its aftermath. The mining sector is negotiating a partial normalisation of operations from 16 April.
- **South Korea:** The Bank of Korea (BOK) kept the policy rate unchanged at 0.75%. Two out of six members of the monetary policy committee voted for a 0.25% cut. BOK announced that it will actively buy development bank bonds and treasury bonds.
- **Taiwan:** Exports declined by a modest 0.6% on a yoy basis in March after surging 24.9% yoy in February. The stronger than expected performance was due to the tech sector with exports particularly to China and Hong Kong expanding. Imports rose 0.5% on a yoy basis after a 44.7% yoy growth in February. The slowdown was mainly due to weaker capital goods imports.

Global backdrop

- **Turning tide:** Asset prices rebounded quite strongly over the last three weeks. Prior to that, the main sell-off took place from 19 February to 23 March when MSCI World declined by 34.1% and MSCI EM was down 31.3%. These were the fastest sell-offs on record. Since then, MSCI World rebound 23% and MSCI EM recovered 17.1%. The rebound have been accompanied by unprecedented fiscal and monetary stimulus across both developed markets (DMs) and Emerging Markets (EM) as well as lower daily coronavirus cases and declining fatality numbers, first in Europe and more recently in the US. Last week, the Fed announced an additional USD 2.3trn facility to buy private credit, including high yield assets. In the United Kingdom (UK), the Bank of England (BOE) announced an overdraft facility ('Ways and Means') to provide liquidity to the government via purchases of government bonds. Debt monetisation has become necessary, given the enormous expansion in government spending. Between direct fiscal measures and loans, taking the whole world into account, we estimate that fiscal stimulus equivalent to 8.75% of world GDP has been announced so far.
- **Size of GDP contraction:** The current global recession is unique in terms of its suddenness and concomitant supply and demand shocks. As such, it has greater resemblance to a natural catastrophe, such as a hurricane, than to a typical economic recession. The global economy now looks likely to contract in real terms between 1.1% and 4.0% in 2020 versus IMF's original forecast of 3.4% real GDP growth from October last year (Figure 1). IMF is due to unveil its new forecasts at the World Economic Outlook, which starts this week. The size and speed of the rebound is difficult to quantify as it is unlikely that all countries (and even regions within countries) will be able to open up at the same time, thus leading to spill-overs between regions. Furthermore, the extent to which the slowdown persists will depend on the degree of permanent impairment due to bankruptcies of businesses and increases in unemployment.

Global backdrop **Fig 1: World GDP Growth: 2020 growth estimates versus previous sell-offs**



Source: Ashmore, IMF, Bank of America Merrill Lynch, Nomura, JP Morgan. Data as at 14 April 2020.

- Coronavirus normalisation:** In the long term, there are two ways in which countries become comfortable with the ideas of lifting lockdowns and opening borders, namely by: (a) achieving universal immunity, meaning that more than 50-60% of the population has already been contaminated, wherefore the spread of the disease slows down sharply; (b) developing a vaccine. A vaccine may become a reality faster than expected, but is unlikely to be widely available until mid-2021. In the absence of these solutions, the most realistic scenario is a gradual and partial normalisation of activity levels in order to avoid a resurgence of the number of cases, although the pressure on politicians to lift lockdowns will intensify sharply once infection rates begin to decline quickly.

Gradual normalisation can be implemented far more effectively if mass testing is introduced to better isolate groups most at risk and if doctors and scientists find better treatments, thus reducing the bottlenecks on the healthcare system. Chinese doctors from Wuhan say evidence of the effectiveness of chloroquine (a malaria drug touted by US President Donald Trump) to treat coronavirus is inconclusive. However, with tests of many treatments taking place concurrently across the world, we believe it is premature to discard the possibility that new therapies will emerge as short term solutions over the coming months.

Meanwhile, in Europe, a number of countries have already announced plans to start normalising economic activity, including Denmark, the Czech Republic, Norway and Austria. Italy announced two more weeks of lockdown (until 27 April). In the UK and US, the normalisation may take longer as the shutdowns came in later. New York Governor Andrew Cuomo said it was too early to speculate whether schools and business would have to remain closed through the month of June.

- Oil:** After a considerable struggle, OPEC agreed to cut production by 9.7m barrels per day (bpd). Other producers (US, Canada and Brazil) agreed to cut output by 3.7m bpd, while other G-20 members will cut output by 1.3m bpd. Most of these cuts have already taken place. Indeed, the cut in supply is unlikely to compensate for the sharp 19m bpd average decline in demand due to coronavirus. Oil prices may therefore fail to return to previous levels, and could even fall further in the short term. However, OPEC agreed to a longer-term output reduction of 8m bpd from June to December and 6m bpd until April 2022. This could lead to an under-supplied market when global economic activity rebounds, implying a sharp jump in oil prices, perhaps around Q4 2020.
- US Data:** CPI inflation declined by a yoy rate of 0.4% to just 1.6% yoy. Core CPI inflation rate declined by 0.1% in March, taking the yoy rate to 2.1% from 2.4% yoy in February. The number of initial jobless claimants increased by another 6.6m in the week to 4 April. Continuing claims have now reached 7.5m people, which means that 5.1% of the work force is now on unemployment benefit. It is possible that the number could be even higher as states struggle to process jobless claim applications. Unemployment may spike as high as 20% by April, in our view. Unsurprisingly, consumer sentiment declined from 89.1 in March to 71.0 in April, the lowest level since 2011.

Global backdrop

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	4.16%	4.16%	-20.42%	-16.49%	-0.12%	-0.51%
MSCI EM Small Cap	5.93%	5.93%	-27.27%	-26.06%	-7.76%	-5.24%
MSCI Frontier	2.54%	2.54%	-24.77%	-18.06%	-3.83%	-2.80%
MSCI Asia	3.59%	3.59%	-15.46%	-12.53%	2.32%	0.91%
Shanghai Composite	1.19%	1.19%	-8.76%	-10.60%	-3.10%	-5.59%
Hong Kong Hang Seng	2.25%	2.25%	-12.15%	-13.80%	2.38%	-2.92%
MSCI EMEA	8.41%	8.41%	-28.33%	-25.69%	-5.53%	-4.54%
MSCI Latam	6.08%	6.08%	-42.27%	-37.35%	-10.90%	-5.58%
GBI EM GD	1.52%	1.52%	-13.92%	-6.70%	-0.49%	0.30%
ELMI+	0.63%	0.63%	-7.90%	-5.51%	-0.30%	0.24%
EM FX Spot	0.92%	0.92%	-13.52%	-14.10%	-6.70%	-5.89%
EMBI GD	2.00%	2.00%	-11.65%	-4.90%	0.81%	2.87%
EMBI GD IG	1.15%	1.15%	-4.35%	5.46%	4.43%	3.94%
EMBI GD HY	3.16%	3.16%	-19.99%	-15.95%	-3.37%	1.61%
CEMBI BD	1.57%	1.57%	-8.76%	-2.20%	1.89%	3.26%
CEMBI BD IG	1.01%	1.01%	-5.10%	1.89%	3.10%	3.27%
CEMBI BD Non-IG	2.43%	2.43%	-13.71%	-7.74%	0.22%	3.36%

Global Backdrop	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
S&P 500	6.93%	6.93%	-14.03%	-3.12%	7.95%	7.88%
1-3yr UST	0.02%	0.02%	2.78%	5.56%	2.63%	1.83%
3-5yr UST	-0.07%	-0.07%	5.30%	9.58%	3.93%	2.84%
7-10yr UST	-0.28%	-0.28%	9.84%	17.03%	6.40%	4.26%
10yr+ UST	-0.11%	-0.11%	20.77%	35.85%	12.46%	7.41%
10yr+ Germany	-0.95%	-0.95%	4.09%	8.81%	5.63%	3.11%
10yr+ Japan	-0.20%	-0.20%	-1.04%	0.54%	2.09%	3.48%
US HY	4.74%	4.74%	-8.54%	-3.55%	2.21%	3.53%
European HY	3.94%	3.94%	-12.85%	-9.34%	-1.02%	1.02%
Barclays Ag	0.71%	0.71%	0.38%	5.27%	3.48%	2.86%
VIX Index*	-23.10%	-23.10%	198.77%	242.80%	157.96%	201.17%
DXY Index*	0.19%	0.19%	2.95%	2.33%	-1.25%	0.51%
CRY Index*	5.05%	5.05%	-31.14%	-32.08%	-31.87%	-41.59%
EURUSD	-0.78%	-0.78%	-2.40%	-3.18%	3.12%	2.72%
USDJPY	0.16%	0.16%	-0.83%	-3.86%	-0.80%	-9.79%
Brent	40.11%	40.11%	-51.73%	-55.47%	-43.00%	-45.47%
Gold spot	8.76%	8.76%	13.06%	33.19%	33.42%	43.82%

*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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