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New virus strain risks more stringent lockdowns ahead of vaccines

By Gustavo Medeiros

The new strain of the coronavirus in the UK threatens a second global lockdown before mass vaccinations. Chinese leadership pledged to keep simulative fiscal and monetary policies during 2021. The Brazilian congress approved the 2021 budget guidelines. A South African court dismissed unions appeal to enforce wage increases. Peru announced measures to mitigate the impact of the pension fund withdrawals. Mexico kept policy rates unchanged but signalled rate cuts in 2021. Singapore eased mobility restrictions. Russia kept policy rates unchanged. Colombia reported they are reaching a consensus to hike taxes in 2021. The US named Vietnam a currency manipulator. Argentina GDP rebounded in Q3 2020. Serbia re-joins the JP Morgan sovereign debt index, the 74th country in the benchmark.

This is the last 2020 edition of the weekly research. We will resume our publication on 4th January 2021. We hope our readers enjoy happy and healthy holidays and all the best for 2021!

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	14.9	–	0.90%
MSCI EM Small Cap	13.7	–	1.84%
MSCI Frontier	12.2	–	1.29%
MSCI Asia	15.9	–	0.55%
Shanghai Composite	13.3	–	1.43%
Hong Kong Hang Seng	9.3	–	0.31%
MSCI EMEA	11.2	–	1.96%
MSCI Latam	13.5	–	2.39%
GBI-EM-GD	4.22%	–	1.20%
ELMI+	1.10%	–	0.42%
EM FX spot	–	–	0.60%
EMBI GD	4.59%	357 bps	0.62%
EMBI GD IG	2.73%	166 bps	0.48%
EMBI GD HY	7.03%	606 bps	0.79%
CEMBI BD	4.05%	328 bps	0.35%
CEMBI BD IG	2.80%	203 bps	0.12%
CEMBI BD Non-IG	5.82%	504 bps	0.66%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	21.5	–	1.29%
1-3yr UST	0.11%	–	0.00%
3-5yr UST	0.36%	–	-0.05%
7-10yr UST	0.91%	–	-0.35%
10yr+ UST	1.66%	–	-1.31%
10yr+ Germany	-0.61%	–	-1.14%
10yr+ Japan	0.00%	–	-0.04%
US HY	4.39%	376 bps	0.33%
European HY	3.42%	404 bps	0.18%
Barclays Ag	0.85%	-6 bps	0.32%
VIX Index*	24.25	–	-0.47%
DXY Index*	90.52	–	-0.20%
EURUSD	1.2199	–	0.34%
USDJPY	103.55	–	0.44%
CRY Index*	166.45	–	5.20%
Brent	50.5	–	0.50%
Gold spot	1898	–	3.75%

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

Emerging Markets

- **Coronavirus:** The UK announced a tougher 'tier 4' lockdown policy for many regions, including London after a more contagious new strain of the coronavirus significantly increased the number of cases in some regions. Several countries announced bans on travellers from the UK in order to contain the more contagious virus mutation. Germany also imposed restrictions after cases per million rose to 295 on a 7-day moving average basis, the highest level since the beginning of the pandemic. The Netherlands will shut non-essential shops until at least 19 January. In the US, New York is moving to a second lockdown due to higher cases and hospitalisations. The US remains the worst affected amongst major countries with 650 daily cases per 1m people. Cases are also on the rise in South America where 160 people for every 1m people got infected on a daily basis last week, driven mostly by Brazil and Colombia as most other countries still have cases on a declining trend. On the other hand, the number of cases per 1m people are still declining in India.
- **China:** Chinese top policymakers recognised the need to keep stimulus policies going in 2021 due to an uncertain external environment caused by the pandemic at the annual Central Economic World Conference. The document said that macroeconomic policy "should be continuous, stable and sustainable, maintain the necessary support for the economy recovery and avoid a policy U-turn". In quantitative terms, M2 growth should

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Emerging Markets

be aligned with nominal GDP growth, implying a soft reduction from the current 13.5% yoy M2 growth level. China also committed to reduce their carbon dioxide emissions by 65% by 2030, an ambitious goal that implies massive investments in renewable energy. Economic data surprised to the upside in November as retail sales, industrial production and fixed asset investment rose 5.0%, 2.3% and 2.6% on a yoy basis respectively and property investment rose 11.5% on a yoy basis. In corporate news, the Chinese regulator fined companies owned by Alibaba and Tencent for monopolistic behaviour adding further concerns after ANT group IPO postponement.

- Brazil: Congress approved the 2021 budget guidelines with a BRL 247bn (c. 3.1% of GDP) primary fiscal deficit target, a marked improvement from an estimated deficit in 2020 of 11.5% of GDP. The budget will also allow the government to avoid a shutdown. Brazilian airline companies suggest 80% normalisation on domestic flights as leisure flights have resumed to pre-pandemic levels. However, the rebound in mobility has been leading to a resurgence of the virus over the last few weeks.

- South Africa: In a major positive surprise for the fiscal outlook, the Johannesburg Labour Court dismissed the appeals from unions to enforce the 2020 wage increase, which may save the Treasury an estimated ZAR 37bn. The yoy rate of PPI inflation rose 3.0% in November from 2.7% yoy in October mostly due to higher food prices. In other positive news, ANC secretary Ace Magashule was asked to step down pending the outcome of investigations on fraud and corruption cases.

- Peru: The Central Bank announced measures to smooth the impact of the second wave of withdrawals from pension funds (AFPs) which are estimated at PEN 15bn (USD 4bn), including purchasing Dollars and long end local bonds directly from AFPs, as well as borrowing local currency using Treasury bonds as collaterals. Economic activity rose 3.2% on a seasonally adjusted basis in October after a 2.0% rise in August and September. The unemployment rate declined to 15.1% in November from 16.4% in October. In other news, Fitch affirmed Peru's BBB+ rating, but changed its outlook to negative from stable.

- Russia: The central bank kept monetary policy unchanged at 4.25% in line with consensus expectations, but struck a cautious tone on inflation developments, when it stated that inflation would have a more significant and prolonged upward pressure. The yoy rate of industrial production declined by 2.6% in November, about half of the level expected by consensus analysts.

- Mexico: The Central Bank (Banxico) kept policy rate unchanged at 4.25% but 2 out of the 5 members of the monetary policy committee voted for a 25bps cut, signalling a higher likelihood of cuts in 2021 while the yield curve implies slightly more than one 25bps rate cut. The minimum wage commission agreed on an increase to MXN 141.7 (USD 7.15) from MXN 123.22 currently, a 15% increase starting in January 2021 taking the cumulative hike since President Andres Manuel Lopez Obrador came to power to 60%.

- Singapore: Prime Minister Lee Hsien Loong announced that the economy will proceed to phase three of its three-stage reopening plan on 28 December, easing most of the mobility restrictions. At the same time, Singapore will have vaccines available to immunise the whole country by Q3-2021.

- Colombia: Finance Minister Alberto Carrasquilla Barrera said there was consensus across stakeholders for a tax reform, which could result in a closure of VAT loopholes or outright increases in the rate of VAT. In other news, the central bank kept policy rates unchanged at 1.75%.

- Vietnam: The US Treasury Department named Vietnam and Switzerland as currency manipulators as both countries 'achieved' the three quantitative criteria of: (a) bilateral trade deficit of at least USD 20bn; (b) a current account surplus of at least 2% of GDP and; (c) Foreign exchange (FX) interventions with net purchase of at least 2% of GDP in the previous 6 months.[1] The Vietnamese trade surplus with the US increased 25% to USD 58bn last year as the country benefited from supply chain migration from China as a result of the trade war. The designation has no specific impact or consequence, but requires the US to engage with the countries to address the perceived FX imbalance.

- Argentina: Real GDP growth rebounded 12.8% in Q3 2020 from a 16.0% decline in Q2 2020, still leaving the economy 10.2% smaller on a yoy basis. The rate of unemployment declined to 11.7% in Q3 2020 from 13.1% in Q2 2020. CPI inflation declined to 3.2% (35.8% yoy) in November from 3.8% (37.2% yoy) in October, however core CPI inflation rose 3.9% from 3.5% over the same period.

- Index matters: Serbia will re-join the JP Morgan Emerging Markets Bond Index – Global Diversified (EMBI GD) with an estimated 0.2% weight at the end of December, after the issuance of a new 10-year benchmark bond in November. This will take the total number of countries in the EMBI GD to 74. The weight of Peru will rise to an estimated 2.4% from 1.6% in November. JP Morgan also announced new debt issued by Chinese companies sanctioned by the US via executive order will not be included in the index.[2]

1 See: https://home.treasury.gov/news/press-releases/sm1212

2 See: https://www.whitehouse.gov/presidential-actions/executive-order-addressing-threat-securities-investments-finance-communist-chinese-military-companies/

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Emerging Markets

Snippets:

- **Angola:** Parliament approved the 2021 budget with a modest 2.2% of GDP deficit containing conservative estimates for oil production (1.2m barrels of oil per day) and prices (USD 39 per barrel).
- **Czech Republic:** The central bank kept policy rate unchanged at 0.25% in line with consensus expectations.
- **Ecuador:** The National Assembly unanimously approved the anti-corruption bill, a necessary condition for the next disbursement under the IMF programme.
- **Egypt:** The IMF has allowed Egypt to withdraw another USD 1.67bn from its Stand-By Arrangement (SBA), bringing the total borrowed on the facility to USD 3.6bn with one last disbursement remaining.
- **Ethiopia:** The EU suspended a USD 108m budget support to Ethiopia due to the conflict in the Tigray region.
- **Gabon:** Fitch has affirmed Gabon's rating at CCC (stable) due to external funding needs and uncertainty on financing sources. At the same time, Fitch does expect a new IMF agreement in early 2021 which means that Gabon may not issue Eurobonds next year.
- **Hungary:** The central bank kept policy rate unchanged at -0.6% in line with consensus expectations.
- **India:** The yoy rate of CPI inflation declined to 6.9% in November from 7.2% yoy in October due to favourable base effect and a small decline in perishable food prices.
- **Indonesia:** Bank Indonesia (BI) kept policy rates unchanged at 3.75%, in line with consensus expectations, albeit some market participants expected BI to cut policy rates by 25bps. The trade balance registered a USD 2.6bn surplus in November from USD 3.6bn in October.
- **Pakistan:** The opposition coalition said that opposition parliamentarian will be tendering their resignation due to Imram Khan's economic policies and the conflict in Kashmir.
- **Philippines:** The central bank kept policy rates unchanged at 2.00% in line with consensus expectations.
- **Poland:** The yoy rate of CPI inflation declined by 0.1% to 3.0% in November.
- **Saudi Arabia:** The country suspended all international flights out of fear of the new strain of covid-19.
- **South Korea:** Unemployment rate declined to 4.1% in November from 4.2% in October, as the labour participation rate rose to 62.7% from 62.4%. The first 20-day exports rose by 4.5% on a yoy basis from 7.7% in November after adjusting for the number of working days.
- **Sri Lanka:** The yoy rate of GDP growth rose 1.5% in Q3 2020 from -16.3% decline in Q2 2020.
- **Taiwan:** The central bank kept policy rate unchanged at 1.125%, in line with consensus expectations.
- **Turkey:** The central bank meeting on the 24 December will be carefully monitored as markets scrutinise the ability of recently appointed Governor Naci Ağbal to rein in inflation expectations. Most market participants expect a rate hike of 150bps to 200bps after inflation surprised to the upside in November.
- **Uruguay:** GDP growth rebounded 7.8% in Q3 2020 after contracting 10.4% in Q2 2020.

Global backdrop

- **US:** The Fed said that the current pace of its quantitative easing (QE) programme will be maintained until they make "substantial further progress" towards reaching their dual mandate of inflation and growth. The Fed refrained from extending the maturity of bonds targeted on its QE programme, which may keep the long end of the yield curve under upward pressure. In fiscal policy news, the leader of the Congress, Nancy Pelosi, and the leader of the Senate, Mitch McConnell, reached a deal to extend another USD 900bn package to fight the effect of the coronavirus in the economy. The agreement encompasses USD 300 weekly unemployment programme until 5 April 2021 and USD 600 payment per family member from households with up to USD 150k of income. Small companies will benefit from USD 325bn to be granted mostly via the Paycheck Protection Programme which will cover up to eight weeks of payroll and employees' benefits as well as interest on mortgages, rent and utilities. The deal was reached a few days after McConnell congratulated President elect Joe Biden for winning the election. In other news, the US Treasury added India, Taiwan and Thailand to the currency manipulation monitoring list which previously featured China, Japan, Korea, Germany, Italy, Singapore and Malaysia.[3] Vietnam and Switzerland were the only countries explicitly cited as currency manipulators as China was removed from the explicit list.

US economic data was mixed with better than expected housing, but weaker employment, sales and manufacturing data. Initial jobless claims rose to 885k in the 12 December week from 862k in the previous week, while continuing claims declined to 5.5m in the 5 December week from 5.8m in the previous week. The Philadelphia Fed manufacturing survey declined to 11.1 in December from 26.3 in November as retail sales declined 1.1% in November from -0.1% in October. Industrial production slowed to 0.4% in November from 1.0% in October. Housing starts rose 1.2% and housing permits rose 6.2% in November.

[3] See: https://home.treasury.gov/news/press-releases/sm1212

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Global backdrop

- **Brexit:** Another deadline was missed as negotiators continued to haggle about the remaining sticking points in fisheries and other areas. If a deal is not reached by the end of December, UK trade with the EU will be subject to WTO-negotiated tariffs on goods and services.
- **EU:** The Euro Area manufacturing PMI rose to 55.5 in December from 53.8 in November while services PMI rose to 47.3 from 41.7 over the same period, most likely due to better expectation of economic normalisation owing to the vaccine developments. CPI inflation rose by 0.1% in November, leaving the yoy rate stable at -0.3%, while core CPI rose 0.1% keeping the yoy rate unchanged at 0.2%.
- **Japan:** CPI inflation declined by 0.9% on a yoy basis in November from -0.4% in October due to lower food and electricity prices.

Benchmark performance

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	5.32%	17.46%	16.37%	17.27%	6.79%	12.96%
MSCI EM Small Cap	5.98%	20.27%	17.60%	20.37%	3.72%	8.56%
MSCI Frontier	4.04%	9.45%	0.00%	2.28%	0.00%	6.40%
MSCI Asia	4.13%	15.66%	22.17%	23.01%	8.39%	13.61%
Shanghai Composite	0.10%	5.54%	13.92%	15.17%	3.72%	1.20%
Hong Kong Hang Seng	-0.58%	11.61%	-2.41%	-1.13%	1.04%	5.80%
MSCI EMEA	7.29%	17.31%	-5.90%	-4.57%	-1.24%	7.00%
MSCI Latam	12.44%	35.50%	-13.20%	-12.51%	-0.71%	9.02%
GBI EM GD	3.71%	9.87%	2.93%	4.33%	3.41%	6.66%
ELMI+	1.93%	5.82%	1.59%	2.31%	1.34%	3.55%
EM FX Spot	2.59%	7.08%	-4.88%	-3.98%	-4.25%	-1.55%
EMBI GD	1.59%	5.48%	4.94%	5.24%	4.96%	7.06%
EMBI GD IG	0.57%	2.74%	8.69%	8.68%	7.32%	7.62%
EMBI GD HY	2.82%	8.88%	0.39%	1.02%	2.28%	6.33%
CEMBI BD	1.23%	4.19%	6.88%	7.23%	5.98%	7.08%
CEMBI BD IG	0.60%	2.49%	7.22%	7.44%	6.30%	6.17%
CEMBI BD Non-IG	2.11%	6.60%	6.33%	6.84%	5.56%	8.57%

Global Backdrop	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
S&P 500	2.51%	10.71%	16.87%	18.37%	13.45%	15.34%
1-3yr UST	0.04%	0.03%	3.15%	3.35%	2.76%	1.90%
3-5yr UST	-0.01%	-0.16%	6.05%	6.41%	4.23%	2.95%
7-10yr UST	-0.59%	-1.62%	9.64%	9.87%	6.23%	4.33%
10yr+ UST	-2.22%	-4.02%	16.46%	16.15%	9.53%	7.25%
10yr+ Germany	0.09%	1.10%	8.54%	7.20%	7.28%	5.64%
10yr+ Japan	0.40%	0.32%	-1.54%	-1.31%	1.66%	2.71%
US HY	1.30%	5.84%	6.50%	6.77%	6.10%	8.67%
European HY	0.80%	5.46%	1.87%	2.09%	2.88%	4.67%
Barclays Ag	0.98%	2.91%	8.80%	9.38%	4.83%	4.69%
VIX Index*	17.89%	-8.04%	75.98%	93.84%	152.08%	29.68%
DXY Index*	-1.47%	-3.59%	-6.09%	-7.34%	-2.96%	-7.98%
CRY Index*	4.00%	12.08%	-10.41%	-10.05%	-11.34%	-3.46%
EURUSD	2.05%	4.07%	8.64%	9.99%	2.79%	11.80%
USDJPY	0.71%	1.91%	4.86%	5.64%	9.57%	16.98%
Brent	6.20%	23.42%	-23.42%	-23.59%	-22.13%	39.04%
Gold spot	6.72%	-0.02%	24.61%	27.86%	49.74%	75.60%

*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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