

China and the US to work together in fight against climate change

By Gustavo Medeiros

China and the United States (US) agreed to collaborate in the fight against climate change. The US sanctioned Russian local currency bonds. The Peruvian election delivered a fragmented Congress and far-left and far-right candidates will dispute the presidential run-off. Colombia unveiled a new fiscal rule to rein in public debt. The Brazilian Supreme Court annulled indictments against former President Lula. Indian inflation rose by more than expected due to base effects. Ecuadorian President-elect Guillermo Lasso said he will form a national-unity government.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	13.4	–	0.77%
MSCI EM Small Cap	11.5	–	1.09%
MSCI Frontier	10.5	–	2.56%
MSCI Asia	14.5	–	1.01%
Shanghai Composite	11.5	–	-0.70%
Hong Kong Hang Seng	9.8	–	0.46%
MSCI EMEA	10.0	–	2.94%
MSCI Latam	11.3	–	3.18%
GBI-EM-GD	4.85%	–	1.25%
China GBI-EM GD	3.21%	–	0.94%
ELMI+	2.52%	–	0.80%
EM FX spot	–	–	0.82%
EMBI GD	4.99%	335 bps	1.44%
EMBI GD IG	3.25%	155 bps	0.81%
EMBI GD HY	7.23%	564 bps	2.15%
CEMBI BD	4.39%	302 bps	0.25%
CEMBI BD IG	3.15%	179 bps	0.25%
CEMBI BD HY	6.05%	467 bps	0.24%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	20.8	–	1.39%
1-3yr UST	0.16%	–	0.01%
3-5yr UST	0.81%	–	0.11%
7-10yr UST	1.56%	–	0.60%
10yr+ UST	2.25%	–	1.22%
10yr+ Germany	-0.26%	–	-0.62%
10yr+ Japan	0.65%	–	0.40%
US HY	3.99%	293 bps	0.20%
European HY	3.05%	353 bps	0.16%
Bloomberg-Barclays	1.11%	-45 bps	0.58%
VIX Index*	16.25	–	-0.44%
DXY Index*	91.51	–	-0.63%
EURUSD	1.198	–	0.56%
USDJPY	108.54	–	-0.77%
CRY Index*	193.2	–	6.47%
Brent	66.6	–	5.20%
Gold	1,780	–	2.72%
Bitcoin	57,322	–	-4.43%

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

Emerging Markets

- **China:** The US climate envoy John Kerry and his Chinese counterpart Xie Zhenhua issued a joint statement saying their countries will collaborate with each other and with other countries to fight climate change “with the seriousness and urgency that it demands.”¹ The statement shows that the two countries can work together in areas of common interest ahead of a Leaders’ Summit on Climate in the US on 22/23 April.

In Chinese economic news, electricity consumption increased at a yoy rate of 19.4% in March from 23.4% in January. The deceleration is due to base effects as electricity consumption actually rose 17.5% in March from 13.3% in January-February when comparing 2021 versus 2019 data. China’s trade surplus narrowed to USD 13.8bn in March from USD 37.8bn in February, due to a 27.7% yoy increase in imports versus a 20.7% yoy increase in exports. Total aggregate financing nearly doubled to RMB 3.3tn in March from RMB 1.7tn in February. Retail sales, fixed asset investment and industrial production rose in March at a yoy rates of 33.9%, 25.6% and 24.5% respectively.

In spite of the strong economic performance, Chinese assets underperformed due to concerns over the state-owned company Huarong Asset Management. We believe China will continue to allow some mismanaged state-owned enterprises (SOEs) to fail to avoid moral hazard and as part of the broader policy shift towards allowing market forces a greater role in resource allocation.

¹ See <https://www.politico.com/f/?id=0000178-e597-d112-a97e-f7bf37200000>

Emerging Markets

The problems facing Huarong are company specific, namely:

- **Asset-Liability mismatch:** Huarong expanded unsustainably and in the process acquired poor assets which, if written down, will make liabilities untenable.
- **Ownership:** The Ministry of Finance may control Huarong, but it is not within the most strategically important sectors for the government.
- **Capital structure:** Huarong Eurobonds sit in an offshore holding company, which can default without adversely affecting the domestic business.

- **Russia:** US President Joe Biden announced sanctions against Russia over its alleged tampering with US elections. The sanctions prevent US investors from buying Russian local currency bonds in the primary market, but US investors can still hold and trade local bonds in the secondary market. JP Morgan said local currency bonds will also remain in its main benchmark index, the GBI-EM GD since liquidity in the existing bonds is likely to remain satisfactory for index tracking purposes. The sanctions did not lead to a meaningful sell-off in Russian fixed income as they were somewhat expected. Rather, the announcement lifted to a certain extent the cloud of uncertainty hanging over Russian assets. Nevertheless, the situation remains fluid. Russia may retaliate, by raising tensions in Ukraine, for example, which in turn could trigger further measures from the US. Furthermore, the health of opposition figure Alexei Navalny deteriorated over the weekend. Navalny was arrested at the beginning of the year (for missing parole meetings) when returning from Germany where he had spent five months recovering from poisoning. The US government said there would be consequences if Navalny dies in prison.
- **Peru:** A second round of presidential election will take place on 6th June between far-left candidate Pedro Castillo, who won 19.1% of the votes in the first round and Keiko Fujimori, daughter of former right-wing dictator Alberto Fujimori, who received 13.4% of first round votes. Regardless of who wins, Peru's next president will struggle to approve meaningful reforms, as the parliament remains deeply fragmented. Three diverse leftist parties will hold 45% of Congress' seats with several centrist parties controlling 21% and three right wing parties holding 34%. The first run-off poll by IPSOS showed Castillo leading with 42% of voting intentions, against 31% for Keiko Fujimori. Front-runner Castillo gave the first signs that he will seek to win the centre last week by pledging not to nationalise companies in the primary sector (mining). Mining investment has been the main source of investment in Peru for the past few decades. In other news, the unemployment rate rose to 15.3% in March from 14.5% in February.
- **Colombia:** The government unveiled changes to the Fiscal Rule in the form of primary deficits of 1.8% of GDP in 2022, 0.7% of GDP in 2023 and 0.2% of GDP in 2024. Previously, the Fiscal Rule targeted the overall deficit. By changing to the primary deficit, the Fiscal Rule is improved, since it allows for better management of the fiscal accounts. The government will seek to pass legislation to boost tax revenues by around 2.2% of GDP, mostly by raising taxes on the wealthy individuals. At the same time, the reform extends social safety nets for the poor. Specifically, new tax revenues will come from eliminating some value-added tax exemptions, increasing income and dividend taxes for wealthy individuals and creating a national tax on fossil fuels and single-use plastics. The bill also creates a monthly payment for the poorest Colombians and proposes to eliminate the 5% withholding tax for foreign investors in local government bonds. With the new tax proposal, the Colombian government aims to stabilise public debt at 65% of GDP.
- **Brazil:** The Supreme Court annulled the indictments on former President Luis Ignacio Lula da Silva, which means he is free, for now, to run for public office in 2022. However, Lula faces trial on the same corruption and embezzlement charges at the Federal Court in Brasilia. It is unclear if the Federal Court will rule on these cases before the deadline for registration for the next presidential election, so Lula's participation in the next election remains unclear. In economic news, the yoy rate of retail sales improved to -1.9% in February from -3.1% yoy in January, driven by higher vehicle sales. The trade surplus also increased to USD 2.1bn in the week of 11 April from USD 1.1bn in the previous week.
- **India:** The yoy rate of consumer prices index (CPI) inflation rose to 5.5% in March from 5.0% yoy in February, while wholesale price index (WPI) inflation rose to 7.4% yoy from 4.2% yoy over the same period. Adverse base effects are the main source of price pressure, driving fuel and manufacturing prices higher. In other economic news, the yoy rate of industrial production (IP) declined 3.6% in February from -0.9% yoy in January. Cases of coronavirus infections in India are rising sharply, but it is important to put India into global context. As of 17th April, India has had roughly 179k deaths, or 129 death per million of population. This compares to 127k death in the UK and 581k deaths in the US. UK and US deaths per million of population are 1867 and 1747, respectively.
- **Ecuador:** President-elect Guillermo Lasso opened negotiations with opposition parties to form a government of national unity. Lasso also confirmed he will send a tax reform, which will cut taxes and reduce tax exemptions. President Lenin Moreno pledged to vaccinate 2m Ecuadorians by the time his government ends its term in office in May 2021. So far, Ecuador has only been able to vaccinate 460k out of a total population of 17 million, but the country received 1m vaccine doses in April, so the pace of inoculations is likely to rise in the coming weeks.

Emerging Markets

Snippets:

- **Argentina:** CPI inflation rose 4.8% in March after increasing 3.6% in February with the yoy rate rising to 42.6% from 40.7%. A concomitant increase in regulated and seasonal prices explain the bulk of the increase as education prices rose 28.5% during the month.
- **Chile:** The House of Representatives approved a third withdrawal from pension funds with 120 votes in favour, 18 against and 2 abstentions. The strong support in favour of the withdrawal sets a high bar for President Sebastián Piñera to challenge the bill at the Constitutional Tribunal.
- **Cuba:** Raul Castro resigned as the Communist Party leader, ending six decades of control of Cuba by his family. The Communist Congress will vote for Castro's successor at the end of a debate, which is expected to last four days. The front-runner is Miguel Díaz-Canel, who was the interim president in 2018.
- **Egypt:** The current account deficit widened to USD 4.8bn (4.5% of GDP) in Q4 2020, which is the widest quarterly deficit since the start of the International Monetary Fund (IMF) programme in 2016. Low tourism revenues and a large current account deficit were the main reasons for the deterioration.
- **Indonesia:** The trade surplus narrowed to USD 1.6bn in March from USD 2.0bn in February. Exports and imports rose by more than the consensus expectation, signalling a solid economic rebound. Auto sales surged to 85K in March from 49K in February – close to the average since 2016.
- **Qatar:** The government has removed the limit on foreign ownership of assets. Foreign investors will be able to hold up to 100% of shares in local companies, from 49% today. Higher foreign ownership is likely to trigger increases in index weights. Specifically, if all companies raise their foreign ownership limits to 100%, Qatar's weight in the MSCI EM could increase by approximately 25bps to 0.9%.
- **Romania:** S&P ratings revised the outlook on Romania's 'BBB-' sovereign credit rating to stable from negative. Prime Minister Florin Citu fired his health minister over his handling of the coronavirus pandemic. The decision is likely to ensure that the coalition government survives, for now.
- **Sri Lanka:** Foreign exchange reserves declined to USD 4.1bn in March, excluding a USD 1.5bn swap with the People's Bank of China (PBOC). At this level, reserves only cover three months of imports.
- **Taiwan:** The Chinese military will hold live-fire drills off the coast of Taiwan as a delegation of former American officials, including Mike Pompeo visits President Tsai Ing-wen in Taipei.
- **Turkey:** The Central Bank of Turkey (CBT) kept its policy rate unchanged at 19%, in line with consensus expectations. CBT said it will use all available instruments in pursuit of the primary objective of price stability until the medium-term inflation target of 5% has been reached. Yet, at the same time CBT removed a pledge of further tightening from its statement.
- **Ukraine:** The central bank increased its policy rate by 100bps to 7.5%, higher than 50bps consensus expectations. Concerns over capital outflows due to the escalation of the conflict with Russia in the East may have influenced the decision.
- **Vietnam:** Citing lack of evidence of manipulation of exchange rates, the US Treasury removed Vietnam (and Switzerland) from the list of foreign-exchange manipulators just three months after adding them to the list.

Global backdrop

- **Coronavirus:** The US Food and Drug Administration and the Centre for Disease Control and Prevention called for Johnson & Johnson (J&J) vaccines suspension after six people (out of 7m) developed a rare blood clot disorder. Some 100m people were expected to receive J&J shots by July of this year. Yet, the pace of vaccinations increased at the fastest pace in the European Union, which is now on track to vaccinate 75% of its population by the end of the year. This percentage has increased from 51% just last week and 40% a month ago, according to the UBS vaccination tracker. Germany, France and Spain are the main contributors to the acceleration. EM is now on track to vaccinate 38.5% of its population by year-end, or 2.2% more than last week. The pace of vaccinations improved in every EM country, except for Hungary, Turkey, Singapore, India and South Africa. Brazil improved the most in April and now is on track to vaccinate 73% of its population by the end of the year compared to 51% last week and 32% two weeks ago. Argentina, Kazakhstan, Chile, Poland and Czech Republic also improved significantly over the last two weeks.
- **Commodities:** The International Energy Agency (IEA) increased its forecast for global oil demand by 230k barrels a day to 5.7m in 2021 due to the stronger economic outlook for both the US and China. The new projection implies a recovery of two-thirds of the demand lost in 2020. Oil prices rose 5% last week and broad commodities were up more than 6% last week.

Global backdrop

- United States:** Economic data was stronger than expected. The yoy rate of CPI inflation rose to 2.6% in March from 1.7% yoy in February, which is the highest level since July 2008, but only slightly higher than consensus expectations. The yoy rate of CPI ex-food and energy rose by a more modest 0.3% to 1.6%. Retail sales rose 9.8% in March after falling 2.7% in February, while industrial production was up 1.4% from -2.6% over the same period. Leading surveys were also strong with the University of Michigan sentiment survey rising to 86.5 in April from 84.9 in March, while the Empire Manufacturing index hit 26.3 after 17.4 last month and the Philadelphia Fed index reached 50.2 from 44.5 over the same period. Housing starts rose to 1.7m in March from 1.5m in February, the highest level since July 2006. Lastly, card expenditure data from Bank of America was up 59% on a yoy basis and 14% higher than the corresponding time in 2019, as of the week ending in 10 April.
- Eurozone:** The yoy rate of CPI inflation rose to 1.3% in March from 0.9% yoy in February, in line with consensus expectations, while core CPI was unchanged at 0.9% yoy. Industrial production declined 1.0% in February after gaining 0.8% in January and retail sales rose 3.0% from -5.2% over the same period. New passenger car registrations rose to 1.1m in March from 0.8m cars in February, an impressive 87% increase in yoy terms, but still below the March average of the previous five years of 1.4m cars. In the coming two weeks, attention will likely shift to who will succeed Angela Merkel as Germany's Chancellor, CDU's Armin Laschet, CSU's Markus Söder, or Annalena Baerbock from the Greens.

Benchmark performance

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	2.53%	2.53%	4.79%	56.02%	7.93%	12.76%
MSCI EM Small Cap	3.53%	3.53%	11.49%	80.55%	6.33%	10.26%
MSCI Frontier	5.62%	5.62%	6.47%	42.43%	0.99%	7.59%
MSCI Asia	2.27%	2.27%	4.93%	54.26%	9.90%	14.37%
Shanghai Composite	-0.44%	-0.44%	-1.33%	24.38%	5.76%	4.48%
Hong Kong Hang Seng	0.51%	0.51%	2.70%	18.53%	1.04%	7.83%
MSCI EMEA	3.03%	3.03%	11.40%	50.19%	1.97%	6.12%
MSCI Latam	4.80%	4.80%	-0.72%	52.76%	-3.78%	4.81%
GBI-EM-GD	2.54%	2.54%	-4.31%	13.96%	0.30%	3.43%
China GBI-EM GD	0.89%	0.89%	1.19%	7.22%	na	na
ELMI+	1.26%	1.26%	-1.34%	9.92%	0.03%	2.31%
EM FX spot	1.46%	1.46%	-2.19%	8.07%	-5.66%	-2.99%
EMBI GD	2.43%	2.43%	-2.22%	16.46%	4.90%	5.27%
EMBI GD IG	1.45%	1.45%	-3.93%	9.22%	6.89%	5.36%
EMBI GD HY	3.57%	3.57%	-0.22%	25.88%	2.69%	5.12%
CEMBI BD	0.52%	0.52%	-0.28%	15.29%	6.32%	6.02%
CEMBI BD IG	0.44%	0.44%	-1.26%	10.41%	6.45%	5.12%
CEMBI BD HY	0.63%	0.63%	1.04%	22.39%	6.15%	7.43%

Benchmark performance

Global Backdrop	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
S&P 500	5.41%	5.41%	11.91%	52.01%	18.24%	17.24%
1-3yr UST	0.01%	0.01%	-0.04%	0.24%	2.84%	1.71%
3-5yr UST	0.30%	0.30%	-1.04%	-0.53%	4.30%	2.28%
7-10yr UST	1.25%	1.25%	-4.56%	-5.45%	5.59%	2.53%
10yr+ UST	2.68%	2.68%	-11.20%	-16.32%	7.12%	3.46%
10yr+ Germany	-0.51%	-0.51%	-6.74%	-4.94%	5.35%	2.53%
10yr+ Japan	0.39%	0.39%	-0.38%	-1.04%	0.97%	0.17%
US HY	0.91%	0.91%	1.77%	18.53%	6.72%	7.82%
European HY	0.66%	0.66%	2.51%	17.73%	3.57%	4.64%
Bloomberg-Barclays Agg	1.27%	1.27%	-3.25%	4.97%	3.23%	2.78%
VIX Index*	-16.24%	-16.24%	-28.57%	-57.40%	1.82%	22.73%
DXY Index*	-1.85%	-1.85%	1.75%	-8.29%	1.75%	-2.62%
CRY Index*	4.46%	4.46%	15.15%	56.07%	-4.28%	8.59%
EURUSD	2.11%	2.11%	-1.96%	10.27%	-2.98%	5.46%
USDJPY	-1.97%	-1.97%	5.12%	0.85%	1.09%	-0.60%
Brent	4.77%	4.77%	28.51%	137.07%	-9.77%	51.19%
Gold	4.23%	4.23%	-6.24%	4.97%	32.28%	42.37%
Bitcoin	-2.78%	-2.78%	97.69%	734.61%	596.17%	13,149.27%

*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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