

China's vaccine to be distributed to EM countries

By Gustavo Medeiros

China said it will share a China-made coronavirus vaccine with other EM countries, such as Brazil, Indonesia, and Turkey as soon as the vaccine is fully developed. FTSE Russell approved Chinese government bonds for inclusion in the World Government Bond Index (WGBI). Colombia cut the policy rate and announced an increase in its precautionary credit line with the International Monetary Fund (IMF). Mexico cut its policy rate by 0.25%. The Malaysian government was challenged by the opposition, but seems to have secured enough support to remain in place for now. Turkey's central bank hiked the policy rate by 200bps to contain TRY depreciation. Hungary increased the policy rate by 15bps to provide stability to HUF. Brazil's current account posted a large surplus. Romania's parliament approved a 40% increase in pensions. Zambia issued a consent solicitation to defer coupon payments on its bonds until April 2021. Costa Rica unveiled a fiscal adjustment programme. The Azerbaijan and Armenian armies clashed on the Nagorno-Karabakh disputed area.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	13.1	–	-4.42%
MSCI EM Small Cap	11.4	–	-6.34%
MSCI Frontier	12.6	–	0.84%
MSCI Asia	14.0	–	-4.14%
Shanghai Composite	12.3	–	-3.52%
Hong Kong Hang Seng	8.1	–	-5.09%
MSCI EMEA	9.9	–	-4.87%
MSCI Latam	12.1	–	-5.62%
GBI-EM-GD	4.47%	–	-3.35%
ELMI+	2.01%	–	-2.30%
EM FX spot	–	–	-3.21%
EMBI GD	5.16%	442 bps	-1.87%
EMBI GD IG	2.98%	220 bps	-1.04%
EMBI GD HY	8.16%	747 bps	-2.89%
CEMBI BD	4.59%	407 bps	-0.83%
CEMBI BD IG	3.05%	253 bps	-0.45%
CEMBI BD Non-IG	6.84%	632 bps	-1.35%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	19.8	–	-0.61%
1-3yr UST	0.13%	–	0.01%
3-5yr UST	0.27%	–	0.07%
7-10yr UST	0.66%	–	0.25%
10yr+ UST	1.40%	–	0.91%
10yr+ Germany	-0.53%	–	0.88%
10yr+ Japan	0.00%	–	-0.06%
US HY	6.02%	537 bps	-1.53%
European HY	4.82%	563 bps	-1.52%
Barclays Ag	0.90%	24 bps	-1.02%
VIX Index*	26.38	–	0.55%
DXI Index*	94.48	–	0.83%
EURUSD	1.1635	–	-0.90%
USDJPY	105.28	–	-0.51%
CRY Index*	148.36	–	0.54%
Brent	41.5	–	0.14%
Gold spot	1859	–	-2.28%

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

Emerging Markets

- Coronavirus developments in EM:** The Chinese vaccine developer Sinovac Biotech said that those EM countries, which are participating in its final-stage clinical trials, including Brazil, Indonesia, and Turkey will get access to the vaccine at the same time as China. Sinovac is expecting interim results from its phase 3 trials of almost 10,000 people in Brazil as early as November. China's National Health Commission said that China would be able to produce 610m doses of vaccine by the end of 2020. Three Chinese companies (Sinovac, CNBG and CanSino) already have vaccines approved for emergency use for doctors, nurses, and members of the military. China's emergency vaccination programme has the blessing of the World Health Organisation (WHO), according to China.
- China:** FTSE Russell will include Chinese government bonds in the World Government Bond Index (WGBI) starting in October 2021 with a subsequent 12-month phase-in period. The WGBI index is the benchmark for nearly USD 2.5tn of assets and an allocation to Chinese bonds in the 4-6% range should generate some USD 100-150bn of inflows. The announcement will further increase the attractiveness of Chinese bonds,¹ leading to even larger inflows from both EM and DM investors, in our view. In other news, China posted the largest current account surplus since 2009 at USD 110bn in Q2 2020 from a deficit of USD 34bn in Q1 2020. Errors and omissions accounted for an outflow of USD 75.7bn in Q2 2020 after recording an inflow of USD 22.6bn in Q1 2020. In other news, state owned companies' net profits rose by 25.8% on a yoy basis in August from 14.3% yoy in July. Industrial profits rose 19.1% on a yoy basis in August, a similar improvements as in July.

¹ See: '*Chinese bonds deliver in bear markets*', Market Commentary, 26 February 2020 and '*Chinese bonds in Developed Markets bond portfolios*', The Emerging View, 18 May 2018.

Emerging Markets

In corporate news, Bloomberg reported that the construction company Evergrande sent a letter to the Guangdong government on the 24 August warning of risks of potential default if the regulators fail to approve its listing in on the Shenzhen stock exchange. The company denied this, and said the letter was fabricated and reported the case to public security authorities. On Friday last week, Evergrande issued a statement that operations are stable and healthy, that debts and financing costs are lower than in March, and that the company has never missed a payment.

- Colombia:** The Central Bank of Colombia cut the policy rate by 25bps to 1.75%. The monetary committee was split as four out of seven board directors voted in favour of a cut, while three members opted for no action. In the press conference following the meeting, Governor Juan Jose Echavarria said there was "very little space remaining" for further rate cuts. In other news, the IMF increased the size of the Flexible Credit Line agreement by USD 6.2bn to USD 17bn. The Minister of Finance announced the government's intention to tap USD 5.3bn of the credit line to secure this year's funding needs.
- Mexico:** The central bank cut the policy rate by 25bps to 4.25%, largely in line with consensus expectations. Retail sales rose by 5.5% in July from 7.8% in June, but remain 12.5% lower on a yoy basis. The monthly real GDP growth proxy declined at a yoy rate of -9.8% in July from -13.2% yoy in June, surprising consensus expectations of a 10.1% yoy decline to the upside.
- Malaysia:** Last week, opposition leader Anwar Ibrahim said he had the backing of a majority of lawmakers to form a new government. However, at the weekend Prime Minister Muhyiddin Yassin's Perikatan Nasional (PN) coalition won 38 out of 73 contested seats in the Sabah state election. An early election now looks quite possible. In other news, the government announced another MYR 10bn in expenditure to support the economy, thereby increasing the total size of the economic stimulus to MYR 55bn (c. 3.9% of GDP). Lastly, inflation measured by the consumer prices index (CPI) declined at a yoy rate of -1.4% in August from -1.3% yoy in July, while core CPI inflation was unchanged at 1.1% yoy.
- Turkey:** The Central Bank of Turkey (CBT) hiked its one week repo policy rate by 200bps to 10.25% in a move, which was not expected by most market participants. CBT said that the hike was needed as large credit expansion and TRY depreciation posed risks for the inflation outlook. Market participants have been worrying about inflation risks for months. As such, the hike is welcome news, but risks weakening the economy further.
- Hungary:** The National Bank of Hungary increased its policy rate by 15bps to 0.75% in a surprise inter-meeting decision that came just two days after the committee had originally opted to keep the policy rate unchanged. Moody's affirmed Hungary's sovereign debt rating of Baa3 and revised the outlook to positive from stable.
- Brazil:** The current account surplus widened to USD 3.7bn in August from USD 1.4bn in July, thus bringing the 12-months cumulative deficit down to 1.6% of GDP from 2.0% of GDP in July. The yoy rate of CPI inflation rose to 2.7% in the first 15-days of September from 2.3% in the same period in August, largely due to an acceleration on food prices. In other news, the rating agency S&P said that a change in the spending cap provided under the Constitution would not lead to an immediate review of the country's sovereign debt rating outlook. The statement is unlikely to change Finance Minister Paulo Guedes's position that the spending cap should be maintained, in our view.
- Romania:** Romania's parliament approved a 40% increase in pensions and other expenditures as part of its review of the government's budget. The Liberal Party-led minority government lacks resources to implement the pension hike and is likely to dispute it in the Constitutional Court. Parliamentary elections are scheduled for 6 December 2020. In other news, which will be welcomed by the Liberal Party, Nicusor Dan won the election for the position of mayor of the capital city of Bucharest. Dan ran as an independent with backing from the Liberal Party and a newly formed anti-corruption party called 'Save Romania Union'. The ruling Liberal Party currently commands a minority position in parliament, but claims that it now controls close to half of local government heads as well as the mayors of Romania's largest cities, the strongest position in the party's history.
- Zambia:** The government launched a consent solicitation for all Eurobond holders to defer USD 161.2m of coupon payments until April 2021, when the Zambian government says it will have more clarity about a possible IMF deal. Zambia has been mulling an IMF deal since 2016, but never undertook the fiscal policy adjustment required to bring the Fund on board. The IMF classifies Zambia's debt as at high risk of distress and demands that the government cancels several contracted loans which remain undisbursed. The IMF also demands that Zambia consolidates the unstable fiscal situation. Fitch downgraded Zambia's sovereign rating to 'C' after the news about the consent solicitation.
- Costa Rica:** The President's Economic Council disclosed the fiscal consolidation that will be presented to the IMF. The initial plan is to reduce the fiscal deficit by an average of 6% of GDP over the next four years, which should place the debt-to-GDP ratio on a trajectory to fall to 50% of GDP by 2034. However, under the government's proposal more than two-thirds of the reduction in the fiscal deficit is expected to be achieved through temporary taxes on financial transactions and income over the first two years of the programme. This is opposed by members of the opposition in parliament. Meanwhile, international reserves declined to USD 7.9bn in August, taking the total drop in 2020 to USD 1.0bn.

Emerging Markets

- **Azerbaijan:** The US, France, and Russia are working towards a cease-fire as intense fighting continued on Monday in the disputed Nagorno-Karabakh area between Armenia and Azerbaijan. Azeri President Ilham Aliyev pledged to “put an end” to the occupation of the Nagorno-Karabakh by Armenian forces.
- **Armenia:** Prime Minister Nikol Pashinyan declared martial law and ordered a general mobilisation against the Azeri attack. Russia holds a mutual-defence pact and holds a military basis in Gyumri, Armenia, next to the northern border with Turkey and Georgia.

Snippets:

- **Angola:** Net foreign exchange reserves declined to USD 9.60bn at the end of August from USD 10.26bn in July.
- **Argentina:** The trade surplus declined to USD 1.4bn in August from USD 1.5bn in July as both exports and imports rose marginally to USD 4.9bn and USD 3.5bn, respectively. Poverty increased to 46% of the urban population in August from 36.4% in the same period of 2019, representing an increase of 4m people.
- **Czech Republic:** The central bank kept the policy rate unchanged at 0.25%, thus matching consensus expectations.
- **Ecuador:** A poll from CEDATOS, a local pollster, revealed that more than 80% of the population distrusts the National Electoral College, the President, and parliament, while only 25% of the population is interested in next year’s presidential election.
- **Egypt:** The Central Bank of Egypt cut its policy rates by 50bps, taking the deposit rate to 8.75% and the lending rate to 9.75%. Most analysts surveyed by Bloomberg had expected no change.
- **Kuwait:** Moody’s downgraded the sovereign credit rating by two levels to A1 citing increasing concerns over liquidity risks. The government has nearly depleted funding in its General Reserve Fund following fierce opposition in parliament against amending the government’s debt ceiling.
- **Nigeria:** The Central Bank of Nigeria cut the policy rate by 100bps to 11.5%, surprising the consensus expectation for no change.
- **Peru:** In a positive development for long term macro stability, the economic committee in Congress rejected a proposed second withdrawal from private pension funds.
- **Poland:** The ruling Law & Justice Party agreed to hold more talks with a junior coalition partner in a bid to keep the ruling bloc together and avoid a potential snap election.
- **Singapore:** Core CPI inflation declined 0.3% on a yoy basis in August from -0.4% yoy in July. Industrial production surged 13.9% in August from 2.3% in July.
- **Taiwan:** Industrial production (IP) rose by 3.6% in August from -0.2% in July due to strong performance of the semiconductor industry.
- **Thailand:** The trade surplus increased to USD 4.3bn in August as exports declined at a yoy rate of 7.9% and imports contracted 19.7% yoy. The Bank of Thailand kept its policy rate unchanged at 0.5%.
- **Ukraine:** Industrial production declined 4.5% in August (-5.3% on a yoy basis) after advancing 3.9% in July (-4.2% yoy).

Global backdrop

- **US:** In a testimony before Congress, Chicago Federal Reserve President Charles Evans said the Fed would maintain an accommodative monetary stance until inflation is on the path to average slightly over 2% over time. His communication was broadly in line with statements by Federal Reserve Vice Chairman Richard Clarida and Federal Reserve Chairman Jay Powell, but contained a contradictory statement as well: “...we (FOMC) could start raising rates before we start averaging 2%...”. This led to confusion and market price volatility last week, which illustrates how challenging the communication process associated with the new average inflation targeting regime has already become. Uncertainty over the effectiveness of a coronavirus vaccine also increased after a poll undertaken by Axios-Ipsos showed that six out of every ten Americans do not want to take the first version of any coronavirus vaccine.

In economic news, new home sales rose to 1,011K in August from 965k in July. Mortgage applications rose 6.8% in the week of 18 September after declining 2.5% in the prior week, while median home prices increased at a yoy rate of 11.4%, which is the strongest since 2013. The pickup in housing activity likely reflects both pent up demand and supply due to lockdowns earlier in the year, which means that activity could subside soon. Labour market data disappointed as initial jobless claims rose to 870k in the week ending on 19 September.

Global backdrop

In political news, President Donald Trump picked Judge Amy Coney Barrett to replace the liberal Ruth Bader Ginsburg on the Supreme Court. Barret is a conservative judge, who previously worked for ultra-conservative Judge Anthony Scalia. Most Republican senators, including often dissenting Mitt Romney, announced their intention to vote in favour of Trump's Supreme Court nominee, making it virtually impossible for Democrats to challenge it. The decision could produce some political headwinds for Trump as polls show that most Americans believe that a Supreme Court replacement should be picked by the new president. Polls suggest that the Biden lead in Florida is getting smaller, but growing in other important swing states, such as North Carolina, Pennsylvania, Michigan, and Wisconsin.² Disagreement over the Supreme Court nomination is also likely to be an obstacle to a new fiscal stimulus, which now looks likely only to be approved after a new president has been inaugurated.

- **EU:** The manufacturing PMI survey rose to 53.7 in September from 51.7 in August, but Europe's services PMI slowed to a three-month low 47.6 from 50.5. Manufacturing seems to be holding up due to demand from Europe's main export partners, such as the US and China, whereas service are declining mainly due to lower mobility within Europe due to rising coronavirus cases. If this pattern continues then Europe is likely to run up an even larger trade surpluses with the rest of the world.
- **UK:** After subsidising 50% of mid-week meals to get British restaurants back in business, Prime Minister Boris Johnson announced that restaurants and bars will have to close by 10pm. He also requested that businesses continue the current practice of letting staff work from home where possible. These announcements followed a sharp rise in coronavirus cases. Chancellor Rishi Sunak was forced to announce a new GBP 3bn wage subsidy scheme to replace the furlough scheme, which ends in late October. Sunak also announced another GBP 1bn to extend 15% VAT tax cut for the hospitality sector.

Benchmark performance

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	-3.71%	7.31%	-3.07%	8.05%	1.83%	8.98%
MSCI EM Small Cap	-4.06%	9.20%	-4.64%	4.10%	-1.42%	4.25%
MSCI Frontier	2.01%	9.77%	-7.50%	-1.70%	-0.95%	3.84%
MSCI Asia	-3.64%	8.36%	3.32%	15.20%	4.30%	10.48%
Shanghai Composite	-5.13%	9.09%	7.99%	11.48%	1.15%	3.10%
Hong Kong Hang Seng	-6.64%	-2.94%	-13.48%	-4.95%	-1.45%	3.55%
MSCI EMEA	-4.72%	-0.32%	-21.52%	-14.45%	-5.23%	1.31%
MSCI Latam	-3.93%	-0.01%	-35.14%	-28.23%	-11.43%	2.64%
GBI EM GD	-2.51%	0.11%	-6.79%	-2.11%	-0.32%	4.65%
ELMI+	-1.58%	0.84%	-4.55%	-1.10%	-0.54%	2.33%
EM FX Spot	-2.70%	-0.84%	-11.69%	-8.91%	-6.97%	-3.24%
EMBI GD	-1.89%	2.27%	-0.55%	1.36%	3.46%	6.02%
EMBI GD IG	-0.88%	2.30%	5.50%	6.63%	6.53%	7.12%
EMBI GD HY	-3.13%	2.24%	-7.57%	-4.86%	-0.05%	4.66%
CEMBI BD	-0.61%	2.61%	2.45%	4.84%	4.70%	6.16%
CEMBI BD IG	-0.21%	2.58%	4.56%	5.59%	5.48%	5.64%
CEMBI BD Non-IG	-1.16%	2.66%	-0.49%	3.70%	3.62%	7.08%

² <https://projects.fivethirtyeight.com/2020-election-forecast/>

Benchmark performance

Global Backdrop	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
S&P 500	-5.66%	6.82%	3.53%	12.63%	11.88%	13.55%
1-3yr UST	0.01%	0.08%	3.09%	3.76%	2.62%	1.83%
3-5yr UST	0.03%	0.18%	6.23%	6.59%	4.02%	2.90%
7-10yr UST	0.36%	0.38%	11.55%	10.70%	6.53%	4.68%
10yr+ UST	1.16%	0.89%	22.29%	18.61%	11.52%	8.63%
10yr+ Germany	2.66%	1.47%	7.43%	-0.36%	7.57%	5.70%
10yr+ Japan	0.53%	0.28%	-1.84%	-3.42%	1.62%	3.02%
US HY	-1.75%	3.84%	-0.11%	2.33%	4.02%	6.37%
European HY	-0.79%	2.32%	-3.74%	-1.74%	1.13%	3.67%
Barclays Ag	-0.71%	2.30%	5.35%	5.78%	3.76%	3.91%
VIX Index*	-0.11%	-13.31%	91.44%	53.19%	176.23%	-4.52%
DXY Index*	2.54%	-2.98%	-1.98%	-4.67%	1.50%	-1.61%
CRY Index*	-3.17%	7.53%	-20.14%	-15.57%	-18.92%	-23.05%
EURUSD	-2.59%	3.49%	3.62%	6.71%	-1.26%	3.53%
USDJPY	0.51%	2.42%	3.13%	2.73%	6.81%	13.79%
Brent	-8.35%	0.85%	-37.12%	-32.97%	-27.71%	-12.34%
Gold spot	-5.70%	4.25%	22.11%	26.45%	44.43%	63.96%

*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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