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WEEKLY INVESTOR RESEARCH

Ashmore

Summer is over, liquidity returns to global markets

By Alexis de Mones

After a nervous start last week markets welcomed the dovish tone of Fed chair Jay Powell's speech at the Jackson Hole Symposium. His sanguine assessment of the inflation risk, and patient attitude with respect to the tapering of asset purchases, were the green light that equities and credit investors awaited to overcome their concerns about global growth, which had prevailed through most of August. Friday's market rally carried over into the start of this week, with EM equities, commodities and EM FX doing particularly well. Spreads narrowed across the board and the EM sovereign debt index is now in positive territory for the year. Now that those dreaded summer markets are firmly behind us, and the green light is on for the cyclical trade, investors are facing an avalanche of economic data releases this week, including the US payroll report on Friday. In EM, China dominated headlines with an abundance of micro policy announcements, but local equities are participating in the rebound; Hungary and South Korea hiked rates, and Chile will likely hike again this week; Peru' cabinet passed the confidence.

Emerging Markets	Next year forward PE/Yield	Spread over UST	P&L (5 business days)
MSCI EM	12.4	–	4.28%
MSCI EM Small Cap	11.6	–	4.33%
MSCI Frontier	12.4	–	1.11%
MSCI Asia	13.6	–	4.11%
Shanghai Composite	11.5	–	2.78%
Hong Kong Hang Seng	8.7	–	2.61%
MSCI EMEA	9.8	–	2.65%
MSCI Latam	9.4	–	5.27%
GBI-EM-GD	5.00%	–	1.70%
China GBI-EM GD	2.96%	–	0.26%
ELMI+	2.89%	–	1.20%
EM FX spot	–	–	1.44%
EMBI GD	4.85%	348 bps	0.41%
EMBI GD IG	3.04%	162 bps	-0.08%
EMBI GD HY	6.96%	563 bps	0.91%
CEMBI BD	4.24%	307 bps	0.14%
CEMBI BD IG	2.90%	174 bps	0.01%
CEMBI BD HY	5.84%	466 bps	0.30%

Global Backdrop	Next year forward PE/Yield/Price	Spread over UST	P&L (5 business days)
S&P 500	20.4	–	1.54%
1-3yr UST	0.22%	–	0.05%
3-5yr UST	0.80%	–	0.03%
7-10yr UST	1.31%	–	-0.33%
10yr+ UST	1.92%	–	-0.72%
10yr+ Germany	-0.42%	–	-1.65%
10yr+ Japan	0.65%	–	-0.09%
US HY	3.94%	294 bps	0.70%
European HY	3.10%	349 bps	0.04%
Bloomberg-Barclays	1.03%	-28 bps	0.17%
VIX Index*	16.39	–	-2.17%
DXY Index*	92.69	–	-0.81%
EURUSD	1.180	–	0.83%
USDJPY	109.84	–	0.05%
CRY Index*	219.2	–	12.22%
Brent	72.7	–	11.54%
Gold	1,818	–	2.05%
Bitcoin	48,534	–	0.39%

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

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Argentina: After much delay, the province of Buenos Aires has completed its debt restructuring, with the exception of two bonds that remain in default. The restructuring achieves large cash flow savings via coupon haircuts, but no principal haircut.

Brazil: The yoy rate of CPI inflation rose to 9.3% in the first half of August from 8.6% in the prior bi-weekly period, 0.1% above consensus. The current account widened to a USD 1.6bn deficit in July from a USD 3.0bn surplus in June, but foreign direct investment (FDI) surged to USD 6.1bn in July from USD 0.2bn in June.

China: A number of policy announcements have made headlines in the last few weeks, and created uncertainty and confusion among investors, already rattled by recent government intervention (or so-called' regulatory tightening') in the private education and property sectors, notably. The leadership's insistence on 'achieving common prosperity', a phrase that has appeared more frequently in President Xi's addresses, and was mentioned again on August 17th at 10th Central Finance and Economic Committee (CFEC) Meeting of the CCP, led to fears of a radical move towards egalitarianism and imminent changes in the treatment of capital. So it was useful to hear last week the Deputy Head of the CFEC Mr. Han Wenxiu clarified the committee's intention by linking the aspiration to 'common prosperity' to China's long-term goal of becoming a prosperous society by 2035, set out in the 5th Plenum of the CCP last year. Thus, the government's intention is not to overhaul the

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system of capitalism with Chinese characteristics, but to correct some of the excesses of the system and make sure that the better-offs pay their fair share. The move is related to President Xi's anti-graft policy playbook, in our view: we note that the eastern province of Zhejiang, home to Alibaba Group was designated as a pilot zone for the new regulatory initiatives, and the top CCP official in Zhejiang's main city (Hangzhou) top CCP official was investigated over the week for unspecified violations of party discipline, which may be related to his closeness to regional entrepreneurs.

After a long delay since its credit problems came to light in March, government-owned Huarong, the country's largest 'bad debt' asset management company, announced a record loss of USD 16bn for FY 2020, but announced that five SOEs including CITIC would recapitalise the company by subscribing to new equity from the company, allowing it to meet the regulatory capital threshold. The company also said that it had no plan to restructure its debt. This is a clear example of government support for a systematically important company, and welcome news for the bondholders: the company's offshore bonds have recovered to par after trading at 70 cents for a few months.

There was no such breakthrough for real estate company Evergrande last week, but it was reported by REDD Intelligence that Beijing had asked officials in Guangdong province to resolve China Evergrande Group's debt through a 'market-oriented' approach, while maintaining stable operations for its real estate projects. It was also reported that Guangdong province governor Ma Xingrui was in favour of a rescue plan, but that opinions among provincial officials varied. One of the company's assets, a subsidiary called Evergrande NEV involved in the Electric vehicles space, reported a net loss of 4.8bn Yuan for the first semester, and saw its market capitalisation fall sharply amid speculation of a fire sale.

China's official manufacturing PMI fell to 50.1 in August from 50.4 in July, slightly weaker than market consensus of 50.2; However, the main disappointment came from the fall in non-manufacturing PMI plunged to 47.5 in August from 53.3 (Consensus was 52.0), posting its first sub-50 reading February 2020.

The People's Bank of China (PBoC) vowed to stabilise credit growth after total social financing growth moderated to 10.7% yoy in July 2021 from 13.7% yoy in October 2020 due to tightening on property lending and shadow banking. Covid-19 cases were close to zero last week after lockdowns and mass testing across provinces.

Colombia: Finance Minister Jose Manuel Restrepo said the government is working with the central bank to use the USD 2.8bn SDR allocation from the IMF for budget support. The SDR allocation would be equivalent to approximately 10% of 2022 budget needs with interest rates of only 0.05% per year. Restrepo also said the tax reform would not eliminate the 5% withholding tax for foreign investors holding local currency bonds.

Czech Republic: Business confidence declined 1.2 to 7.2 while consumer confidence rose 3.8 to -1.5.

Gabon: The ratings agency Fitch upgraded Gabon credit rating to 'B-' with a stable outlook, reflecting an improvement in the external environment, thanks to higher oil prices and a 3-year IMF loan worth USD 0.6bn agreed in late July. The fiscal deficit is likely to widen to 3.3% of GDP in 2021 but improve to 1.4% of GDP in 2022, higher than the IMF forecast by 1.1% of GDP.

Hungary: The National Bank of Hungary (NBH) hiked its policy rate by 30bps to 1.5%, in line with consensus, and announced a reduction on its weekly government bond purchases to HUF 50bn from HUF 60bn by reducing purchases of short-term securities. The NBH said it would review its quantitative easing programme quarterly from September 2021. HUF rose by 1.5% against the USD on the week.

Turkey: The trade balance for July came in at USD -4.28bn, in line with expectations and with the monthly average over the last 12 months.

Indonesia: President Widodo Jokowi confirmed Indonesia will start reopening restaurants, malls and churches in Jakarta and other areas after new Covid-19 cases declined and vaccinations rose. The Bank Indonesia announced it plans to purchase IDR 439trn (c. USD 30.5bn or 2.7% of GDP) in government bonds between 2021 and 2022. The announcement came after the Finance Minister said it expects to issue IDR 1,020trn in 2021 from IDR 958.1trn forecasted in July, taking the budget deficit to 5.8% of GDP.

Malaysia: The yoy rate of CPI inflation declined to 2.2% in July from 3.4% yoy in June, 0.7% lower than consensus.

Mexico: The yoy rate of CPI inflation declined to 5.6% in the first two weeks of August from 5.9% yoy in the previous bi-weekly period while core CPI rose 0.1% to 4.8% yoy, led by higher core good prices. The yoy rate of real GDP growth rose 19.6% in Q2 2021, 0.1% below consensus and Q1 2021. Retail sales declined 0.6% in June after rising 0.6% in May, 0.7 below consensus. The current account balance swung to a USD 6.3bn surplus In Q2 2021 from a USD 5.5bn deficit in Q1 2021, USD 2.5bn higher than consensus. In other news, oil production from 125 wells were taken offline after a gas leak caused a fire which caused five fatalities leading to a drop in oil production of 421k barrels a day (c. 1/4 of total oil production in Mexico).

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Peru: The Congress voted confidence in the Bellido cabinet, with 73 votes in favour and 50 against; The government presented the 2022-25 fiscal projections: they target a headline fiscal deficit reduction of 1.0%-pt per year in the period 2022-24, converging to 1.0% of GDP by 2025, with the structural balance also converging to -1.0% by 2025.

Philippines: President Rodrigo Duterte said he will run for vice-President in the May 2022 presidential election, saying that he "will continue the crusade" as he is "worried about the drugs, insurgency". In economic news, the balance of payments moved to a USD 0.6bn surplus in July from a USD 0.3bn deficit in June as the budget deficit improved to PHP 121bn in July from PHP 150bn in June.

Poland: the unemployment rate declined 0.1% to 5.8%, in line with consensus.

South Africa: The unemployment rate rose to 34.4% in Q2 2021 from 32.6% in Q1 2021.

South Korea: South Korea Central Bank (BoK) today announced the first pandemic-era rate hike in Asia, increasing its base rate from 50bps to 75bps, to control rising inflation, household leverage and property prices. The BoK left the door opened for more hikes in the next few quarters.

Taiwan: The yoy rate of industrial production declined to 13.9% in July from 18.0% yoy in June, 3.7% below consensus. The unemployment rate declined to 4.4% in July from 4.8%, 0.3% below consensus.

Thailand: Thailand relaxed Covid-19 restrictions by allowing dining-in at restaurants and the reopening of department stores. Car sales declined to 52.4k in July from 62.8k in June, the lowest level since May 2020.

Zambia: President Hakainde Hichilema, referred to as 'HH' in Zambia, was sworn in last week following his surprise majority win at the August 12th presidential election. He pledged to restore macroeconomic stability, and the market is expecting conversations with the IMF to start this fall, leading to a new programme possibly being agreed next spring. The country's Eurobonds are in default and the fiscal challenges are material, but the economic adjustment is made easier by the improvement in the country's external position: owing to the twin effects of high copper prices (up 24% YTD) and weak domestic demand, the country's current account surplus jumped to USD 920m in Q1, or close to 20% of GDP. The market reaction to HH's election has been very positive this far, judging by spot rate of the Zambian Kwacha, which is trading 17% stronger since the date of the election.

Global backdrop

Covid-19: The Covid pandemic is not going away and is gaining grounds in the United States, in particular, where confirmed cases continue to increase, albeit at a slightly slower clip than last month. The number of new daily cases per million rose to 480 last week from 420 the previous week (7-day moving average). In comparison, the number reached 650 during the last big wave in the US last January. In Europe, cases have been stable at c. 170 cases per million, but the UK stands out with confirmed cases close to 500 (per million, 7 day-moving-average) and very little restrictions in place. Conversely, Latin America has been the clear out-performer in recent weeks, with the number of cases below 90 per million, and declining rapidly. In Asia, the average has been relatively stable c. 55 per million, thanks to progress in India and Indonesia, but a few countries are going in the wrong direction and have to impose restrictions: Japan, Thailand, Malaysia, Philippines, S Korea, Pakistan all showing signs of being in a wave.

United States: at the Fed's annual policy symposium in Jackson Hole, Wyoming, which once again took place online, Fed chair Jay Powell delivered a very didactic lecture on the recent drivers of inflation, laying out five reasons why it would be temporary, in the Fed's assessment. In terms of policy announcement, he stuck with the language of the July FOMC minutes, stating that for 'most participant, if the economy evolved broadly as anticipated, it could be appropriate to start reducing the pace of asset purchases'. He made no commitment with respect to the timing, preferring to postpone the decision to one of the three FOMC meetings taking place before year-end. So the FOMC retains full flexibility to accommodate any negative surprise, and the speech was more dovish than expected. He was also keen to stress that the timing of the tapering 'will not be intended to carry a direct signal' regarding the lift-off in Fed Funds rate, which depends on a substantially more stringent test with respect to maximum employment notably. This will be the Fed's next communication challenge. For now, market participants were happy to move past their Jackson Hole worries, and they celebrated a dovish statement with a relief rally across asset classes.

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Benchmark performance

After selling off 10 basis points to 1.36% earlier in the week, the US 10-year treasury yield retraced by 6 basis points to 1.30% following Powell's speech. In addition, as the 10-year breakeven yields widened back to 2.40% in response to the dovish messaging, the 10-year treasury *real* yield fell 9 basis points on Friday to -1.09%. The USD index was down 0.8% on the week, of which 0.4% came on Friday following.

In economic news, the US manufacturing PMI dropped 2.2 to 61.2 and the services PMI dropped 4.7 to 55.2 in August, both below consensus. Housing data improved with existing home sale rising 2.0% to 6.0m in July from 5.9m in June and mortgage applications rose 1.6% on the week of 20 August from -3.9% on the previous week. Durable goods orders declined 0.1% in July after rising 0.8% in June while capital goods orders was flat in July after rising 1.0% in June.

Eurozone: Germany's preliminary HICP inflation for August rose to 3.4 yoy from 3.1, in line with expectations. The German IFO business climate index declined 1.3 to 99.4 in August led by a 3.5 drop in the expectations component to 97.5 (2.5 below consensus) while the IFO current assessment rose 1.0 to 101.4. The Eurozone Manufacturing PMI declined 1.2 to 61.5 in August while services PMI was down 0.7 to 59.5, both slightly below consensus.

Japan: The Jibun Bank composite PMI survey declined 2.9 to 45.9 as services dropped 3.9 to 43.5, while manufacturing was down 0.6 to 52.4.

United Kingdom: The market services PMI declined 4.1 to 55.5 in August (59.1 consensus) while the manufacturing PMI was 0.3 lower at 60.1 (59.5 consensus).

Australia: The Markit services PMI declined 1.1 to 43.3 in August while the manufacturing PMI dropped 5.2 to 51.7, the lowest level since June-2020.

Benchmark performance

Emerging Markets	Month to date	Quarter to date	Year to date	1 year	3 years	5 years
MSCI EM	-0.20%	-6.88%	0.08%	16.43%	8.75%	9.95%
MSCI EM Small Cap	-0.97%	-2.25%	17.18%	41.57%	12.01%	10.18%
MSCI Frontier	2.86%	2.60%	17.98%	33.55%	10.05%	9.76%
MSCI Asia	-0.54%	-7.97%	-2.08%	13.27%	9.32%	11.06%
Shanghai Composite	3.79%	-0.94%	3.45%	7.36%	10.71%	5.12%
Hong Kong Hang Seng	-2.78%	-15.21%	-14.64%	-9.82%	-3.46%	2.36%
MSCI EMEA	1.55%	1.67%	18.12%	31.84%	6.69%	6.44%
MSCI Latam	-0.18%	-4.22%	4.45%	33.56%	2.63%	3.70%
GBI-EM-GD	-0.32%	-0.75%	-4.10%	4.25%	4.64%	2.56%
China GBI-EM GD	-0.30%	1.38%	4.52%	10.90%	–	–
ELMI+	-0.08%	-0.59%	-1.19%	4.41%	2.21%	1.88%
EM FX spot	-0.35%	-1.51%	-3.06%	2.33%	-2.81%	-3.37%
EMBI GD	0.58%	1.00%	0.33%	4.25%	6.57%	4.30%
EMBI GD IG	0.57%	1.05%	-1.43%	0.85%	7.62%	4.69%
EMBI GD HY	0.60%	0.95%	2.38%	8.33%	5.29%	3.81%
CEMBI BD	0.58%	0.79%	2.08%	6.16%	7.63%	5.34%
CEMBI BD IG	0.35%	0.91%	0.77%	3.36%	6.98%	4.61%
CEMBI BD HY	0.85%	0.63%	3.85%	10.10%	8.43%	6.43%

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