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Emerging Markets gear up ahead of US elections and policy easing

Emerging Markets Charts and Views

OCTOBER 2024

Emerging Markets gear up ahead of US elections and policy easing

The global macroeconomic outlook is favourable for Emerging Markets (EM) assets, as global growth remains resilient and inflation is generally very close to or within target ranges. Although the growth premium for EM is nearing its peak, it still favours EM, with a significant growth differential expected for 2025 and beyond. Asia will continue to be a major driver of growth, with China's fiscal stimulus being a key variable to monitor.

The monetary outlook is generally favourable. EM Central Banks have already initiated the easing cycle and are expected to continue this trend, with few exceptions. The Federal Reserve provides less of a headwind for EM CBs.

On the risk side, one important theme to watch is the US elections and the impact of a potential new wave of tariffs. However, the uncertainty surrounding the election outcome makes it difficult to predict which policies will be implemented. Furthermore, rising geopolitical tensions in this multipolar world are significantly impacting EM. This shift may actually benefit certain EM by enhancing their bargaining power and political influence, underscoring the importance of assessing specific regions and country opportunities.

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Macro themes to consider for the EM outlook

Supportive macro backdrop 1

Global macroeconomic outlook is supportive for EM prospects, with global growth remaining resilient and inflation generally on a declining trend. EM appear more resilient.

Although the **EM growth premium** is peaking and moving closer to the historical average, it **still favours EM,** albeit with increasing fragmentation and divergence among countries.

Easier monetary policy 2

EM Central Banks adopted a more orthodox and agile approach in 2022 by raising interest rates and curbing inflation, positioning themselves **favourably for the current easing cycle**. The Fed's ongoing easing cycle creates a favourable environment for balancing growth support with vigilance against inflationary risks for more autonomous EM countries.

Winners & Losers: Asia in focus 3

Asia is playing a crucial role in shaping the future of the global economy, thanks to its **rapid economic growth and leadership in technology and innovation**. India's economic outlook remains solid and promising. Meanwhile, in China, new stimulus measures aim to reverse the structural economic slowdown. Meanwhile, Southeast Asian countries have strengthened their trade positions.

Risks to watch: US election 4

The key risks to watch are geopolitical risks and the US election. Possible Trump 2.0 is a significant factor influencing the outlook for EM. Idiosyncratic stories and internal vulnerabilities, which could increase EM fragmentation, are other topics that investors need to monitor.

Source: Amundi Investment Institute, as of October 2024.

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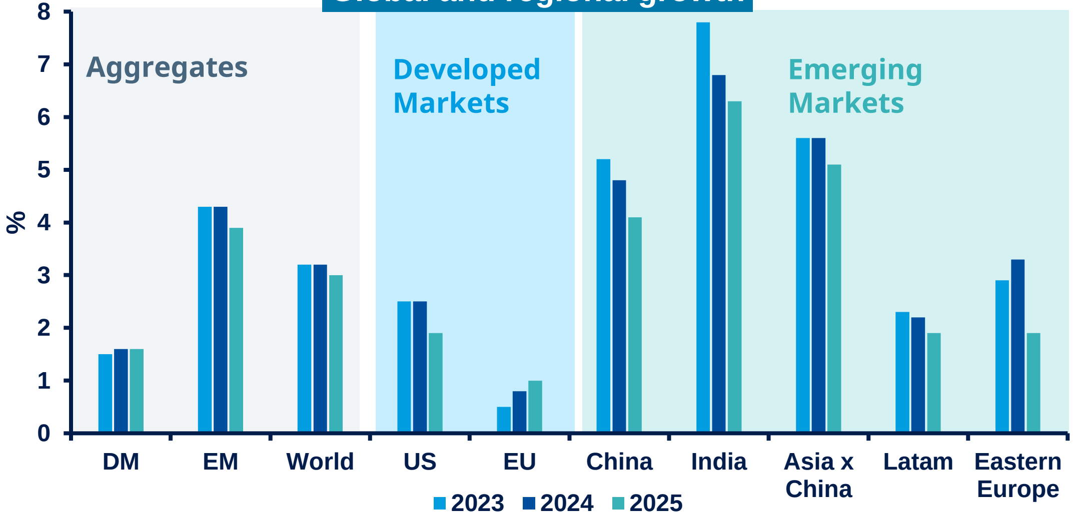
The rising role of EM in driving growth

The growth premium favours Emerging Markets, as developing economies are set to play a crucial role in driving global economic growth in 2024 and beyond. Asia will remain a key growth engine, with India shining as a standout performer.

Global and regional growth

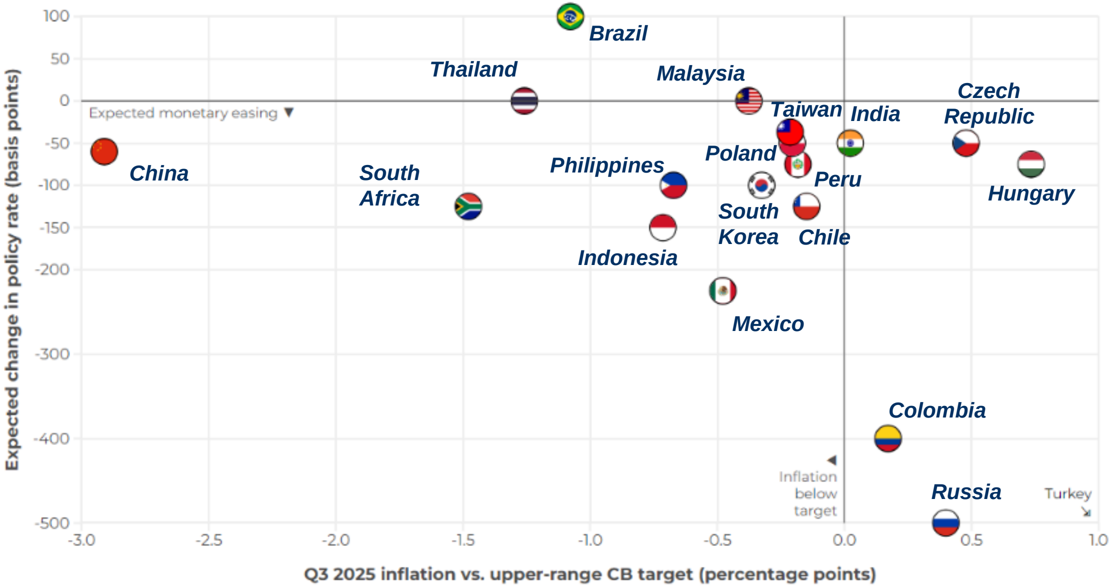


Source: Amundi Investment Institute. Data is as of 14 October 2024. Forecasts are by Amundi Investment Institute and are as of 14 October 2024. EM: Emerging Markets. DM: Developed Markets.

Favourable environment for EM Central Banks to continue the easing cycle

- Several Emerging Market Central Banks have already initiated their easing cycles with a gradual and cautious approach. This comes after they adopted a more advanced and orthodox stance during the significant inflation spike in 2022.
- Given that disinflation is expected to continue its trend, and the Fed has already started its monetary policy relaxation, some Central Banks could continue their easing cycles.
- However, not all countries are in the same situation; for example, Brazil is out of sync.

EM inflation and monetary policy trends by Q3 2025



Source: Amundi Investment Institute on Bloomberg Intelligence data. Data is as of 29 September 2024. EM includes CB from: Brazil, Chile, China, Colombia, Czech, Hungary, India, Indonesia, Israel, Malaysia, Mexico, Peru, Philippines, Poland, Romania, Russia, South Africa, South Korea, Thailand, and Turkey. DM: developed markets. EM: emerging markets. Fed: Federal Reserve. MP: monetary policy. Turkey's inflation is expected at 27.14% in Q3 2025, while Turkey's policy rate is expected to cut by 1750pbs in 1 year horizon. China's Q3 2025 inflation vs. upper PBoC target range is at 2.91%. Russia's policy rate is expected to cut by 500pbs in 1 year horizon.

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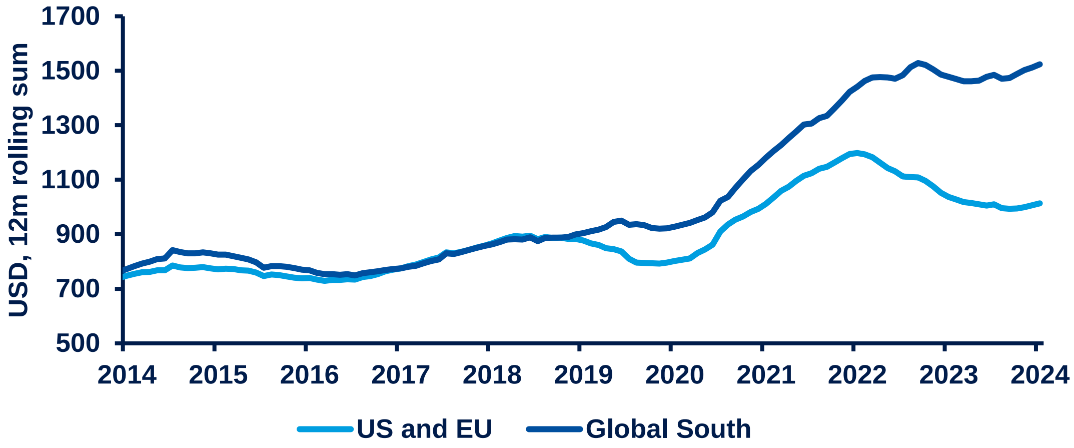
China: entering new markets amid geopolitical reordering

China is adapting its growth strategy. Chinese exports to the Global South have increased significantly, driven by rising geopolitical tensions and potential tariffs. Until the Covid crisis, the Global South market was comparable to the US and EU combined; it is now 50% larger.

China exports



Source: Amundi Investment Institute, CEIC. Monthly data, latest available data is as of August 2024. The Global South refers to Africa, Latin America and the Caribbean, Asia (excluding Israel, Japan, and South Korea), and Oceania (excluding Australia and New Zealand).

China's policy shift: a step to reverse the structural economic slowdown

- More Policy support is finally on the Chinese authorities' radar. The final size and the sectors targeted (housing and households) will be key.
- Our expectation is a potential fiscal package of RMB 6-7 trillion from Q4 2024 through 2027, with four spending priorities in the near term:

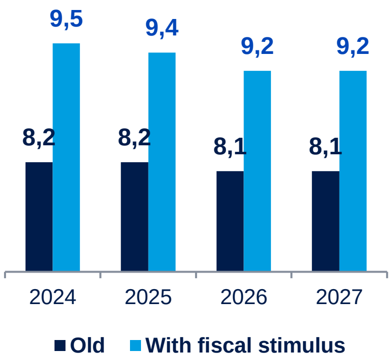
1. Support local governments,
2. Recapitalise large state-owned commercial banks,
3. Stabilise housing market, and
4. Strengthen vulnerable groups.

Note: for additional information about monetary and macroprudential policy adjustments see the recent Investment Talks: [China policy: short-term lift or long-term change?]

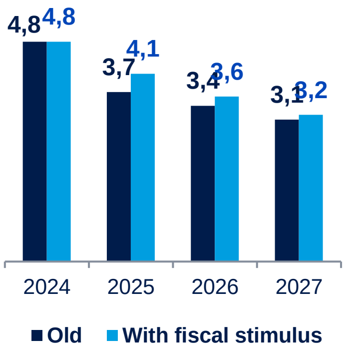
Hypothetical Fiscal Package

Impulse	Potential spending areas	Size
High	Direct subsidies to multi-child families (likely, not mentioned)	700bn
Moderate	Bank capital injection; direct transfers to vulnerable households	1trn
Low	Local govt debt restructuring; purchases of idle land/unsold but completed housing	5trn
	Total	**6.7trn**

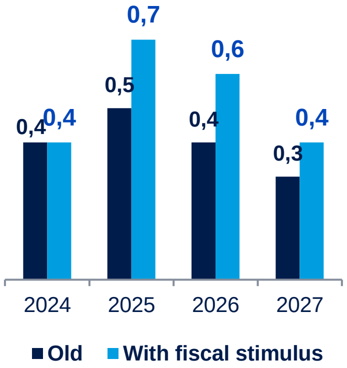
Fiscal deficit, % of GDP



GDP growth, %



Inflation, %



Source: Amundi Investment Institute, internal elaboration, data is as of 7 October 2024.

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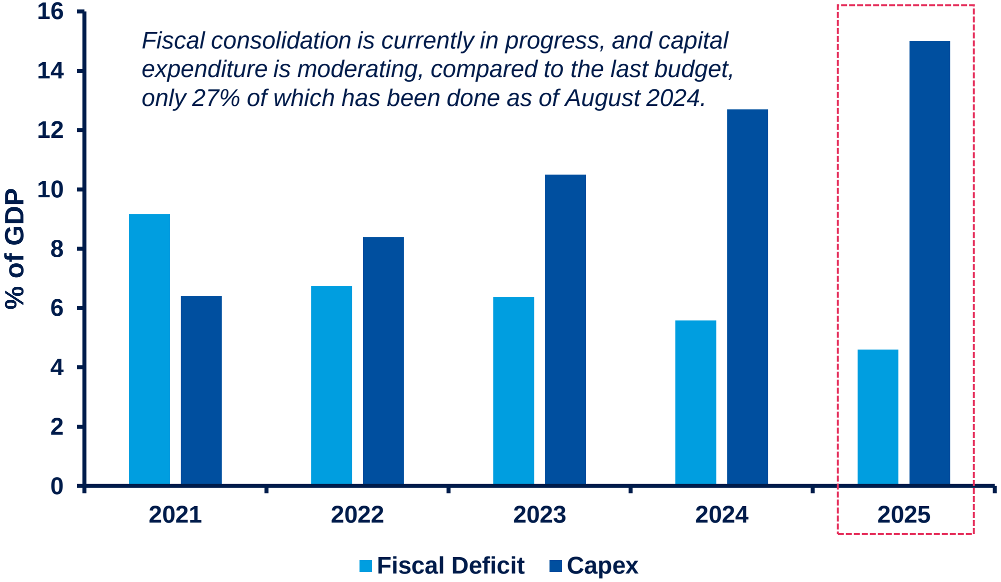
India: economic growth continues to be well sustained

- Robust economic growth is expected to continue, driven by domestic demand and investments. Some moderation in growth is anticipated after several years of high single-digit growth. Public Capex growth is moderating. Under Modi’s 3.0 administration, growth is becoming more inclusive, sustainable and resilient.
- The budget revision reinforces two important aspects: fiscal consolidation and capital expenditure (capex).
- Inflation is expected to remain well anchored in the upper band of the RBI’s target, allowing the Indian Central Bank to maintain a prudent approach to its monetary policy and initiate its easing cycle.

Between growth and macro financial stability

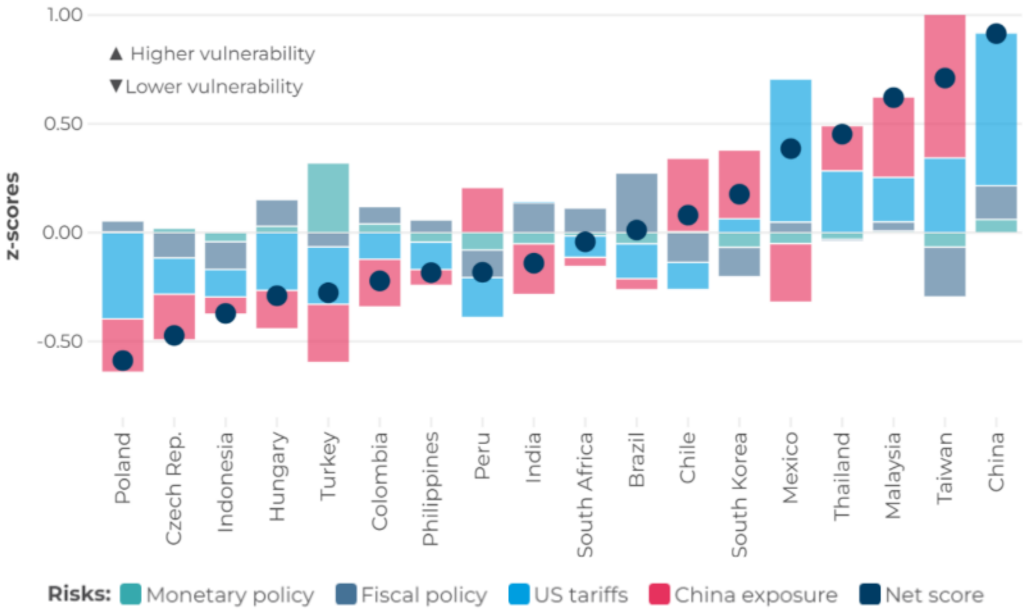


Source: Amundi Investment Institute, internal elaboration, data is as of 17 October 2024. Years refers to fiscal Indian year.

How the US election could impact on EM economies

- **Tariffs approaching:** Trump supports aggressive tariffs; Harris favours a more moderate stance, impacting EM differently.
- **Fiscal policy risks:** both candidates lack fiscal adjustments, potentially raising core yields and affecting EM valuations.
- **Growth projections:** Harris's policies may benefit EM growth compared to Trump from late 2025 to 2028.
- **Regional impact:** Trump's tariffs could harm Asian EM, while Mexico and Hungary may benefit; Harris's approach is expected to lower growth and inflation volatility.

EM exposure to US elections risks



Source: Amundi Investment Institute, CEIC, S&P, OECD. Data is as of 10 October 2024. Relative measure of vulnerability based on weighted z-scores.

How the US election could impact EM economies

- Under Harris, EM debt and equities are expected to have a neutral impact, while Trump's policies risk triggering inflation and volatility, posing challenges for Emerging Markets.

Summary table of market implications

Asset Class	Baseline	Harris	Trump
EM debt	GBI-EM (local currency): still downtrend in local yields. EMBI (hard currency): slightly wider spreads.	Modestly higher yields. Neutral, aligned with baseline.	Higher yields than baseline, especially in Asia. Wider spreads due to higher US Treasury yields.
EM equities	Neutral; favour valuation plays in EMEA, LatAm, and Asia.	Neutral.	Negative for Asian equities (tariffs), positive for LatAm.
EM FX	Neutral; favour valuation plays in EMEA, LatAm, and Asia.	Negative for Asia, overall, more negative than baseline.	Marginally positive for EMEA and LatAm, negative for Asia.

Source: Amundi Investment Institute, as of 10 October 2024. Views reflected on the table above are from Amundi Investment Institute.

Main investment convictions in EM

EM Debt

- Constructive on HC space amid a supportive macro backdrop and attractive yields, with a selective preference for HY over IG.
- Local Currency debt could also benefit from more dovish EM CBs. We remain focused on areas with appealing real yields.

EM Equities

- Mildly positive on EM equities, with focus on areas with attractive valuations, stronger economic growth and an earnings recovery that is on track.

EM FX

- Selective EM FX still offers good carry, and Fed's easing stance should lend support to EM currencies.
- Light positioning should offset uncertainty from core rates and geopolitics.

Source: Amundi Investment Institute, as of 14 October 2024.
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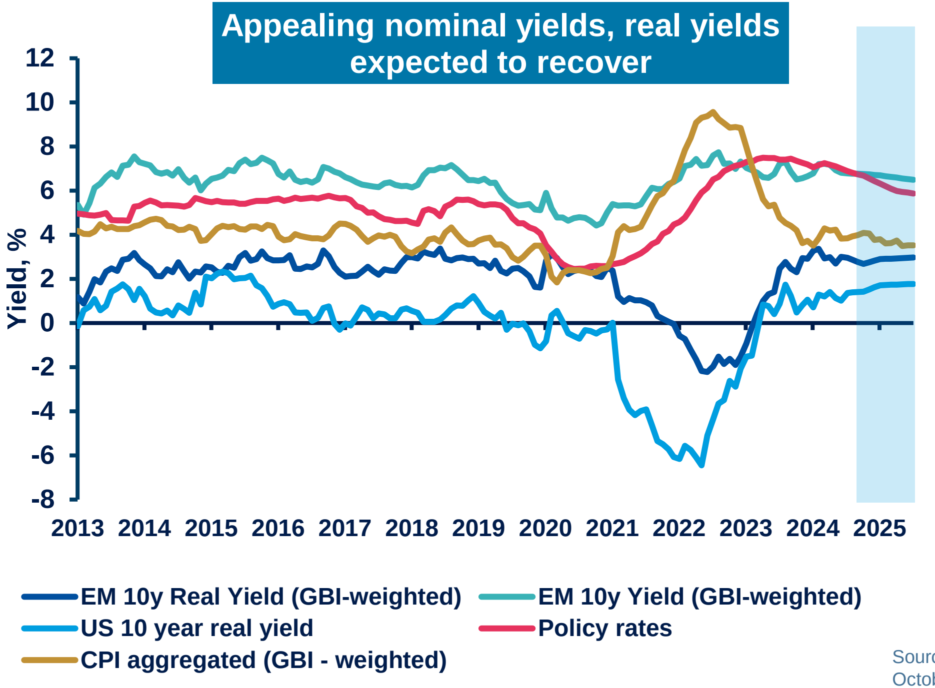
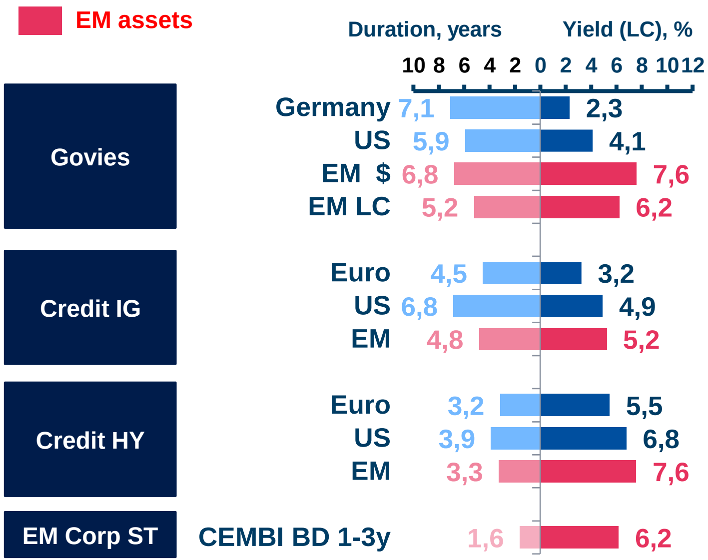
EM bonds: attractive yields, in absolute and relative terms

Appealing nominal yields, real yields expected to recover



Source: Amundi Investment Institute, Bloomberg. Data is as of 4 October 2024.

Duration and yield, local currency



Source: Amundi Investment Institute. Analysis on Bloomberg data. Data is as of 7 October 2024. Government and EM indices are from JP Morgan. Euro and US credit indices are from ICE-BofA. LC: local currency. IG: investment grade. HY: high yield. ST: short-term. Yield for EM Corp ST is JP Morgan CEMBI Broad Diversified 1-3 Year while duration is JP Morgan CEMBI IG+ 1-3 Years.

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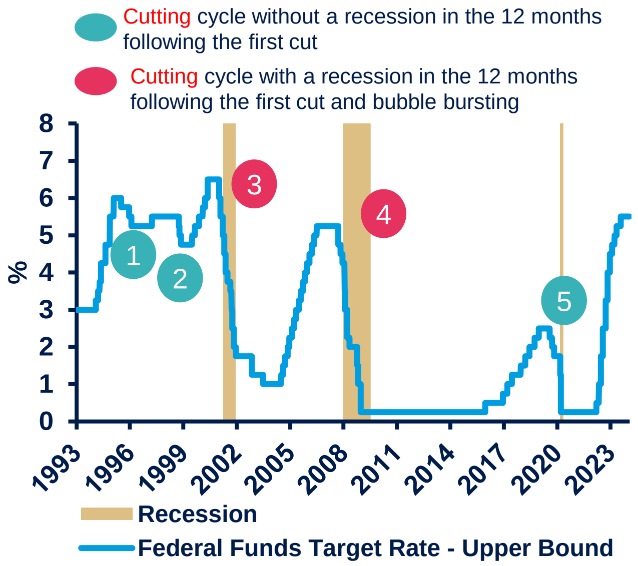
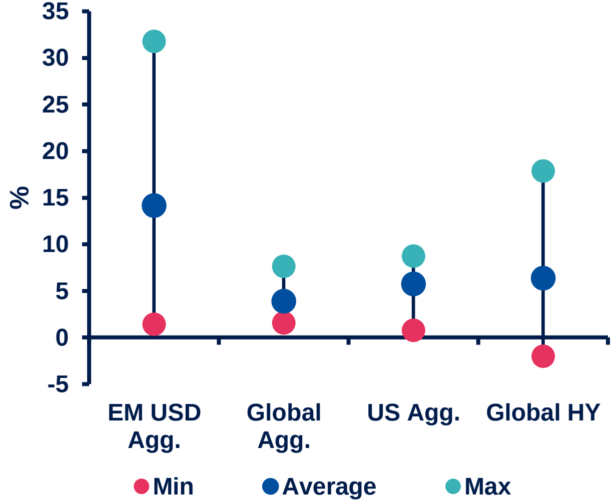
EM bonds outperformed other fixed-income assets during past Fed easing cycles

- During past rate-cutting cycles by the Fed, EM bonds have performed well, exhibiting a wide range of performance.
- As expected, the US economy is not falling into recession, while cuts are driven by falling inflation, EM USD Aggregate bond (EM bond) index could benefit.
- In past occurrences of Fed cutting cycles without a recession, EM bonds have on average outperformed vs other fixed-income assets.

Fed past rate cutting cycles



Fixed-income return 12 months after first Fed's rate cut for the last five easing cycles



Source: Amundi Investment Institute, Bloomberg. Data as of 16 October 2024. Analysis on monthly data and Total Return Net indices in local currency. Indexes from Bloomberg. EM USD Aggregate includes USD-denominated debt from sovereign, quasi-sovereign, and corporate EM issuers. **Past performance is not indicative of future returns.**

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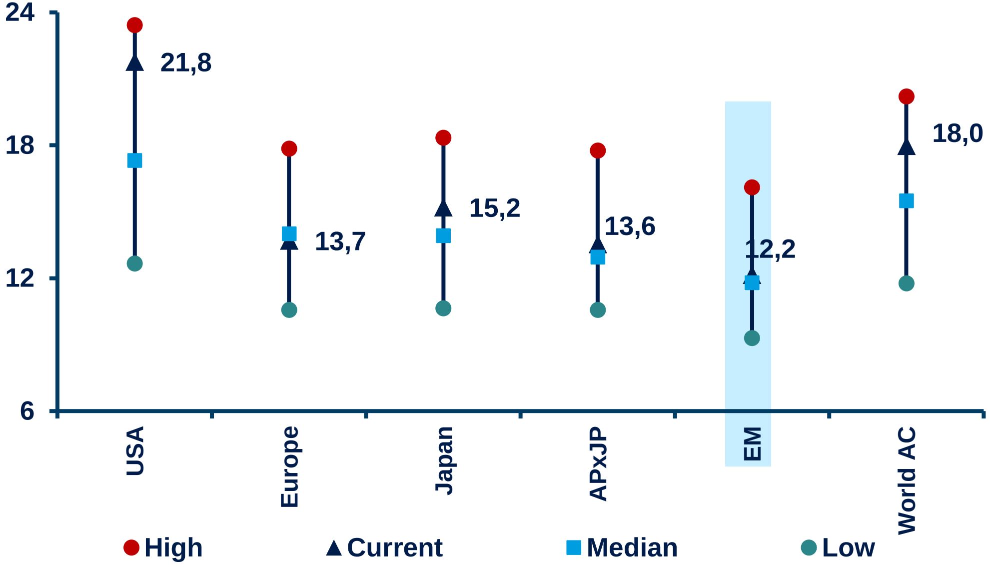
EM equity: constructive view driven by resilient global economic growth and valuations

- **EM equities**: Strong demand, a resilient global outlook, an earnings recovery projected for 2025, and attractive valuations support the case for this asset class. However, country-specific factors remain important
- **EM currencies**: further cut rates by the Fed will eventually support EM currencies. Moreover, some EM Central Banks are expected to ease policies at a slower pace than the Fed providing a cushion against further FX volatility in general.

PER 12m forward (over last 12 years)



Source: Amundi Investment Institute, Datastream. Data is as of 3 October 2024. MSCI indices.

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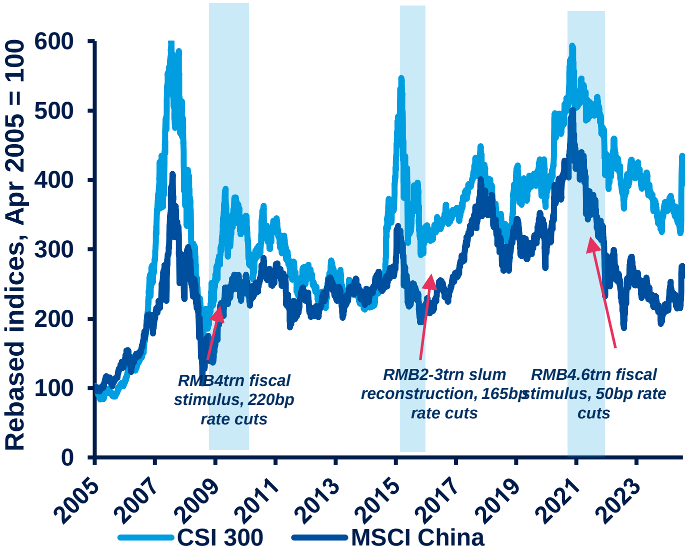
Exploring the dynamics of Chinese and Indian equity markets

- **China**: Recent supportive monetary policies are encouraging, but fiscal stimulus will be key to supporting Chinese equities further.
- **India**: Indian equities have seen rising interest from international investors as the market benefits from strong internal demand, the rise of the middle-income class, supply chain relocation and increasing financial inclusion.

Chinese equity : three out of the last five rallies were spurred by fiscal stimulus



Source: Amundi Investment Institute, Bloomberg, Gavekal. Data is as of 15 October 2024.

India is a bright spot

Source: Amundi Investment Institute, Bloomberg. Data is as of 15 October 2024.

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EM equity investors can benefit from new global trends

1/ FDI beneficiaries:
- Ability to leverage large domestic markets and produce at scale
  - boost productivity, limit trade dependency
- Competitive cost advantage to service largest global markets

2/ Owners of natural resources (an advantage if coupled with sound economic policy)
- Access to a wide range of commodities that are becoming critical (energy/sun, wind, copper, food etc.)

3/ Owners of technological expertise/advantage
- More companies will diversify their supply chains and look to substitute away from China

	FDI beneficiaries						Technology owners		Natural resources owners	
	India	Asean	Indonesia	Turkey	Eastern Eu.	Mexico	Korea	Taiwan	Brazil	Middle East
Large domestic economy	xxx	x	xx	xx	x	xx	x		xx	x
Proximity to end markets		x	x	xx	xxx	xxx				
Low geopolitical risk	xx	x	xxx	xx	x	xxx			xxx	
Ease of doing business	x	xxx	x	xx	xx	xx	xxx	xxx		xx
Structural reform	xxx		x		x		x		x	xx
Commodity independance	x		xx			xx			xxx	xx
Technological leadership	x						xxx	xxx	x	

Source: Amundi. Data is as of 15 October 2024.

Opportunities in Asia beyond China and India

1 **China –** ***neutral***
Deflation still ongoing and there is further downside risk to GDP and earnings growth due to housing sector and resulting weak consumption; this is offset by a policy shift (a pro-growth government stance with a willingness to support property and private sector) and significant excess savings accumulated during the Covid period. Valuation & positioning still attractive after recent rebound; Size and composition of fiscal support to be examined carefully regarding direction of earnings; the longer-term risk-reward appears more attractive for domestic vs offshore markets amid geopolitical risk.

2 **India –** ***positive*** Digital transformation, Made in India, financialisation of savings and increasing weight in indices with more IPOs to come in new economy sectors. A robust economic cycle helps mitigate high valuations, while we still find plenty of value in some sectors (financials/healthcare) and large caps.

3 **Taiwan –** ***neutral***
Constructive on semiconductors (logic and analog chips), with ongoing inventories normalisation in mature tech and ongoing strength in leading tech, both preventing earnings growth from decelerating. Valuation is stretched and hence opportunities are selective.

4 **South Korea –*positive***
Constructive with selective opportunities in semiconductors (on both leading and commodity memory chips, with a supportive earnings cycle and some valuation support after recent selloff) and among holdings companies benefiting from the "value up" programme.

5 **Thailand –** ***cautious***
Cautious on banks and chemicals. More constructive on tourism names.

6 **Malaysia –** ***cautious***
Cautious on demanding valuation relative to other Asean countries.

7 **The Philippines –** ***cautious***
Cautious on sectors exposed to domestic consumption, more constructive on banks.

8 **Hong Kong –** ***positive***
Focus on travel-related and defensive high-yield names Cautious on real estate.

9 **Vietnam –** ***positive***
Now the largest in the MSCI Frontier Index. It could benefit from an upgrade to EM status in MSCI indices and "China+1" opportunity. Favour banks and real estate.

10 **Indonesia –** ***positive***
Favour domestic names such as banks, but short term at risk of rotational flows to China.

Source: Amundi Investment Institute, data is as of 30 of September 2024. EM: Emerging Markets

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