Confidence must be earned

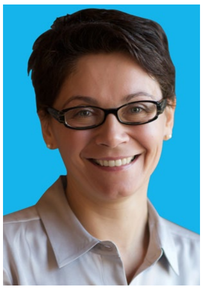
Amundi ASSET MANAGEMENT

INVESTMENT INSIGHTS BLUE PAPER | FEBRUARY 2021

Investors should look at EM for yield and growth in 2021, on the basis that fundamentals will make the difference

Yerlan SYZDYKOV
Global Head of Emerging Markets

- *Global investors are currently dealing with two key challenges: find decent yield for their fixed income portfolios in a world of ultra-low or negative interest rates and access some exposure to growth at a reasonable price.* ***EM market assets*** *may offer some opportunities in addressing these challenges and* ***have the potential, in our view, to outperform other asset classes both in equity and fixed income in 2021****. However, investors should be aware of the heterogeneity of the EM universe and the transformation occurring in EM. Each country has specific drivers, monetary and fiscal policies, and political landscapes. In a world of retreating global trade, domestic growth drivers are becoming increasingly important. The role of China and Asia in the geopolitical order, as a global growth engine and new centre of gravity, became even more significant in 2020, with Russia willing to play a stronger role as well. These elements have to be considered in building an allocation in EM. Deep expertise in assessing all these dynamics – macro and bottom-up – and looking at the opportunities from a cross asset perspective (where- and however they are emerging) are, we believe, the key means to gaining exposure to superior growth and yield premiums and at the same time mitigating idiosyncratic risks.*
- ***Looking in detail at the 2021 EM macroeconomic outlook****, the prospects for a widespread vaccination campaign are supportive for a global economic recovery in 2021. Markets have reflected this positive sentiment recently.* ***Emerging countries should be able to take advantage of this supportive global outlook and therefore our EM GDP growth forecast is 5.7-6.5% for 2021****. Such a rebound might be uneven across countries and regions, and we could see some 'stop-and-go' phases, depending on the speed of vaccine rollouts and the evolution of the virus and its new mutations. We do not expect to see inflationary tensions over the coming year and thus support an accommodative policy framework for central banks (CB). Some CBs may continue to use non-conventional tools, such as QE, although fiscal measures have little room to grow due to the recent new highs in indebtedness that some countries took on to address the pandemic.* ***The outcome of the US election is something to watch carefully for its implications on rates and the dollar, which is critical for EM assets.*** *Markets were not fully discounting a 'Democratic sweep' and we could see some overshooting in the short term of US rates. Also, despite the prospects of a weaker dollar in the medium term being confirmed, in 2021, we could see a widening GDP growth differential between the US and the rest of the world thanks to the upcoming fiscal boost that could support the dollar. On foreign policy, we expect to see a less aggressive attitude towards China from the Biden administration, although we still expect to see a tough stance from the new government.*
- ***Fixed income and FX views:*** *We expect to see some continuation of strong technicals and inflows in support of EM hard-currency debt.* ***We prefer the HY to the IG*** *space, as the former has more room to tighten and could benefit more from these conditions. EM local currencies have* ***all the ingredients to perform well in 2021****: low inflation, CBs in a low-rate environment, and a cyclical growth recovery. An area of attention should be the evolution of the dollar, the combination of local currency appreciation and potential spread compression will support this asset class. Asian countries are ticking more boxes than others. Commodities are rebounding from their recent lows, thanks to the projected global recovery. EM corporates* ***offer carry opportunities, although spreads appear tight*** *historically. Earnings have been recovering during the last quarter of 2020; investors need to be selective in terms of bond picking and pay attention to the measures that could be implemented by the new US administration and their implication for US rates.*
- ***Equity:*** *Markets should benefit from a reopening dynamic, economic recovery, and improvement in earnings. The market will monitor the vaccination process and availability within EM countries.* ***EM equity valuations are attractive*** *in the current global context, although some growth sectors look disproportionately expensive. Therefore, we favour some cyclical or value stocks.* ***Going in depth into country-specific features is critical, as the outlook and fundamentals are significantly different****. Frontier markets supported by China's recovery are an attractive area to look at, as well as India as a long-term growth story. The development around the New Silk Road theme, in our view, also represents an attractive investment opportunty for the medium term.*



Alessia BERARDI
Head of EM Macro and Strategy Research

Macroeconomic view

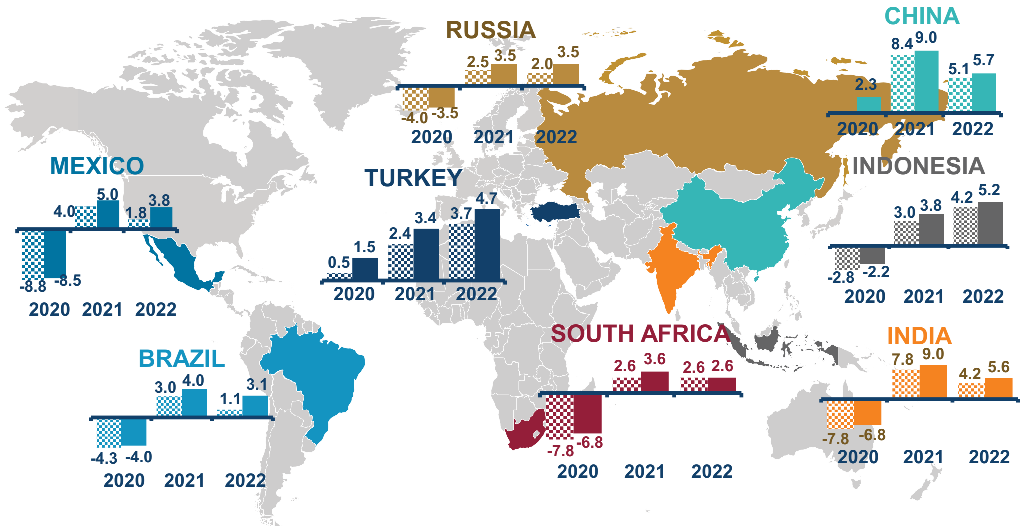
Growth: momentum to pick up in 2021

The outcome of the US elections and positive vaccine developments have boosted investor sentiment and resulted in a rally in risk assets, in particular for emerging markets. We have seen a rebound in growth, both in developed and emerging markets. In EMs, exports have rebounded sharply, led by a recovery in North Asian countries -- China, South Korea and Taiwan -- driven by the technology and healthcare (medical supplies) sectors.

We expect global growth momentum to pick up in 2021. Our current estimates are for developed markets to expand 4.0-4.5%, a trend that should support a sustained pick-up in trade and commodities. We expect EMs to benefit from this backdrop and grow by 5.7-6.5% in 2021. Notably, the **recovery may be uneven across EM regions given that EMs are a heterogeneous universe, with diverse growth levers to support economic recovery.**

"We expect EMs to benefit from the global recovery and grow by 5.7-6.5% in 2021".

Figure 1. Varied growth rates across EM countries



Source: Amundi Research. Latest forecasts are as of 29 January 2021. Bars represent real GDP growth (YoY%) forecast range: solid bars represent the best-case scenario, while shaded bars represent the worst-case scenario of the forecasting range. For EMs, we assume no new additional fiscal impulse in 2021 vs 2020, according to the national budget laws announced so far. National daily economic activity data and local lockdowns as of 15 January 2021 have been included, together with the boost to growth from the above fiscal packages and trade linkages.

Inflation: under control overall, with some exceptions

Inflation has been picking up in some countries, particularly due to higher food prices, a significant driver of inflation in EMs. In general, inflation remains within CB targets, with the exception of some countries, such as India and Turkey, where inflation is well above their targets. Meanwhile, some countries are close to the upper bound of CB targets (e.g., India), but inflation should converge to those targets soon. **Overall, we expect EM inflation to remain benign, barring some base effects kicking in** due to extremely low levels reached in 2020 (oil price collapse in 1H20). **Having said that, it is important to monitor inflation closely, given the highly accommodative policies followed by EM CBs and due to the fact that some CBs have been using unconventional tools (e.g., QE on the secondary market).**

Monetary and fiscal policies: different room of manoeuvre

We expect EM CBs to remain accommodative to support liquidity and financial stability, especially if the Fed and the ECB maintain their dovish stances. It should be kept in mind that EMs are a diverse universe: different EM countries have different room available regarding monetary policy. Some CBs that have the flexibility needed, could use QE to provide support, whereas others may still have some room of manoeuvre on rates, especially if inflation remains benign while growth rebounds. On the other hand, fiscal support in EMs remains relatively limited compared to DMs, especially given the fragile fiscal situations in some EM countries, which were already concerning before the Covid-19 crisis (e.g., Brazil, South Africa, and India). An important element to watch for Eastern EU countries is the approval of recovery fund, significant in terms of GDP of the area (See Box).

"A Democratic sweep could bring some pressure on US rates, and has to be closely monitoted for its impact on EM assets".

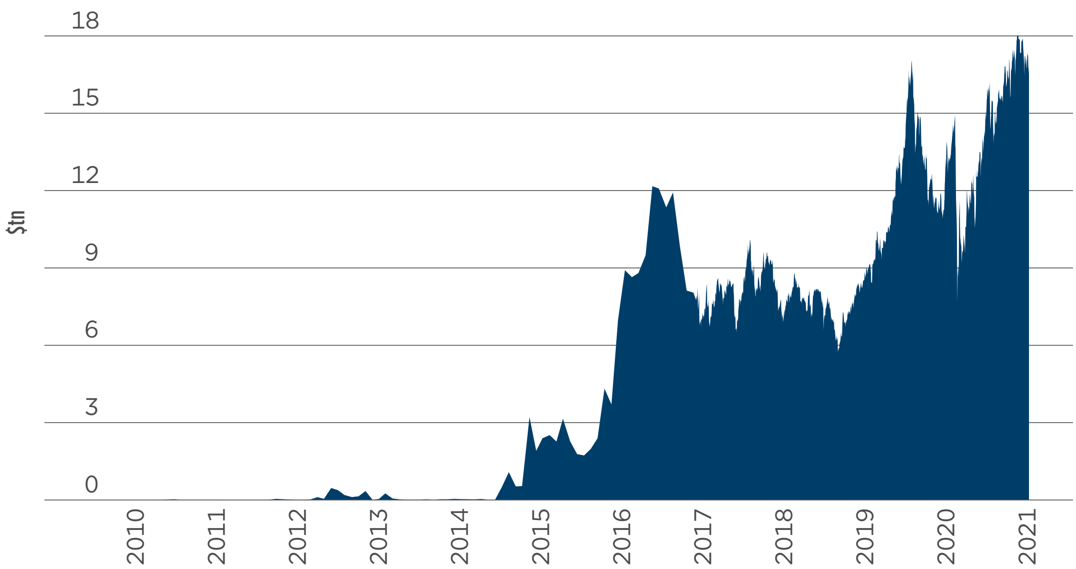
Prior to the US election, we had maintained that the outcome should support risk assets and EMs in particular. A Biden presidency removes the risks of geopolitical tensions such as those stemming from volatile US-China trade tensions. We expect the incoming US administration to be less aggressive in his rhetoric than Trump's and -- as such -- we expect fewer spikes in market volatility going forward. Nonetheless, the 'tough-on-China' stance should stay. **The Democratic sweep was not priced in by the market and has accelerated the reflation trade, with markets discounding a more aggressive US fiscal policy.** This is an area of attention for the coming months, that made us a bit more cautious after the vote in Georgia. **We do not expect a derailment of the benign conditions supporting EM assets, as the flows dynamics should support the asset class, but we think that a possible overshoot of US rates in the short term has to be monitored.**

For 2021, we expect some normalisation in global rates. **In the United States, we expect ten-year Treasury yields at 1.2-1.3% at end-2021.** On the other hand, we see lower market volatility given positive macro developments and expectations for oil prices to stabilise in the $45-55/bbl range.

Although EM spreads appear fairly valued in the short term against such backdrop as they are already discounting the positive developments on the vaccine and on the US election fronts, we believe that there is space for some further spread compression in the next twelve months, as macro and geopolitical uncertainty will fade in 2021. **Given the accommodative policy framework, the hunt for yield will remain and should provide a positive backdrop for EM debt in 2021.**

"Within an accommodative policy framework, the hunt for yield will remain and should provide a positive backdrop for EM debt in 2021".

Figure 2. Amount of negative-yielding debt at record level



Source: Amundi, Bloomberg. Index is Barclays Aggregate Negative-Yielding Debt Index. Data as of 2 February 2021.

EU budget and recovery package: an opportunity for CEE countries

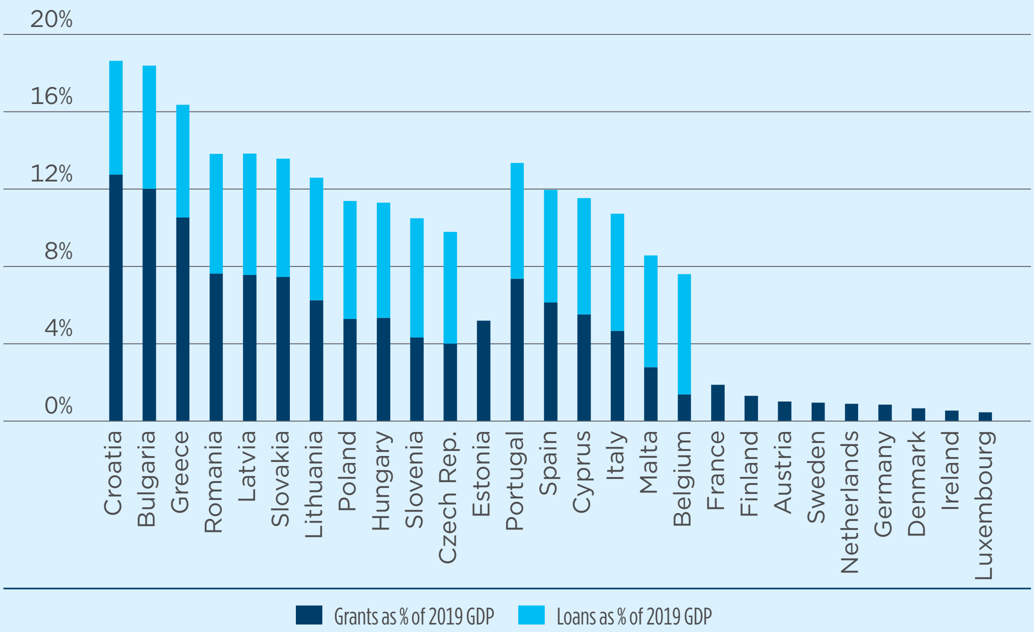
Long-term EU budget 2021-2027 and recovery package are a comprehensive financial package of €1.8tn for the coming years to tackle the socio-economic consequences of the pandemic and address the EU's long-term priorities.

This combines: 1) the new €1.1tn EU budget for 2021-2027 (multiannual financial framework) these funds will allocate more money to Southern and Eastern European countries, boosting the long-term prospects for investments; and 2) the European Union's €750bn recovery instrument (Next Generation EU Programme) aimed at economic transformation projects that should further accelerate economic recovery. The emergency fund will disburse €390bn in grants and €360bn in low-interest-rate loans to EU member states. This large plan was adopted and could eventually become a permanent economic crisis and convergence instrument. The plan has been described as a fourth major step in European integration after the Single Market, the euro, and banking union. It brings fundamental changes through joint EU debt, support to countries in the form of grants, and use of European solidarity funds for cyclical economic support (not just for convergence and long-term investment). Crises are catalysts that push the European project forward, not backward.

"CEE countries are big beneficiaries of the Next Generation EU programme".

Around 25% of Next Generation EU Programme funds will be allocated to CEE countries; the region represents around 11% of EU GDP. **These funds will be crucial to supporting recovery in Eastern Europe**, boosting the mid-to long-term economic pace, transforming the economic-growth mix (eg, innovation and digitalisation, green transition, sustainable infrastructure or education and research), and helping to limit populist parties' increasing ascendancy in the region.

Figure 3. NGEU grants and loans



Source: Amundi Research on Bruegel Institute estimates. Data as of November 2020.

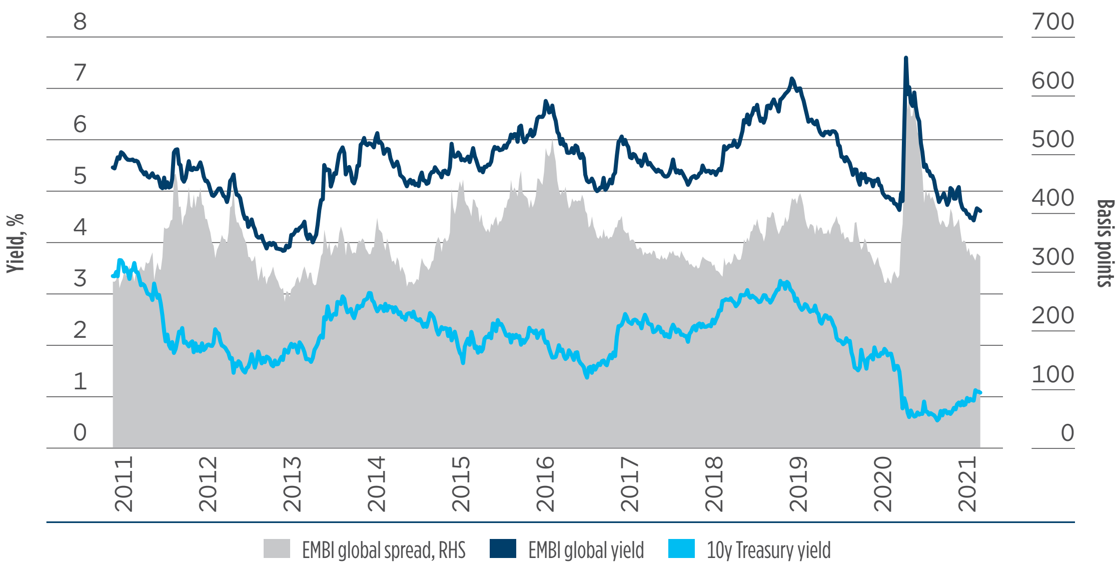
Sergei STRIGO
Co-Head of Emerging Markets Fixed Income

EM debt outlook

EM hard-currency sovereign debt: oppurtunities remain, especially in the HY space

Regarding EM hard-currency debt, we believe that valuations for IG are fair, considering the credit quality. We expect IG spreads to remain unchanged or tighten slightly in 2021, while there is more room for spread compression in the HY space. Even though we do not forecast a significant change in US Treausury yield in 2021, we do see the outcome of the US election -- with the Democratic sweep -- as a risk for the IG universe.

Figure 4. EM and US Treasury ten-year bond yields



Source: Amundi analysis on Bloomberg data as of 2 February 2021.

EM sovereigns are still in a default wave, but we expect default rates to be significantly lower in 2021 than in 2020, which registered a record 10.2% by year-end. EM debt restructurings have turned a corner, with Argentina's and Ecuador's having concluded. However, the situation in Lebanon continues to be drawn out, while Zambia has officially entered default. **The default concerns are more centred around solvency rather than liquidity risks**, which makes the analysis around fiscal and debt risks more pertinent than assessing external financing capacity.

The technical backdrop remains supportive for HC debt. We have seen strong inflows in HC debt and expect that flows for IG would remain strong, as investors chase income from high-quality sectors amid the low-yield backdrop. Technicals for HY are also supportive, as issuance was light in 2020. Against such backdrop, **we remain constructive on EM HC. In terms of specific opportunities:**

"We have seen strong inflows in HC debt and expect that flows for IG would remain strong, as investors chase income from high-quality sectors amid the low-yield backdrop".

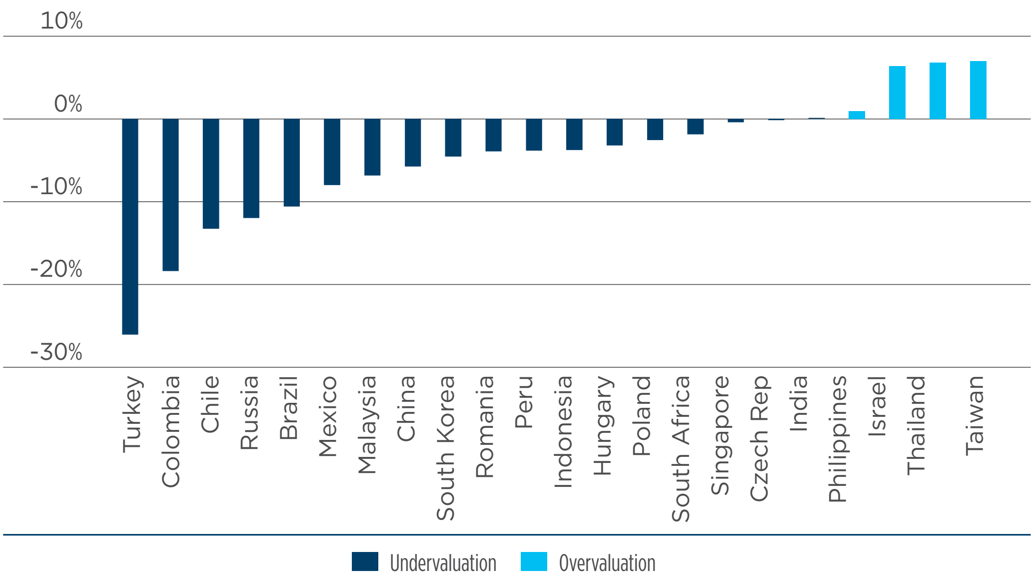
- **Latin America:** We like Mexico due to solid fundamentals given improving macro momentum and low fiscal spending, while valuations also appear attractive. We also favour Mexican quasi sovereigns due to attractive valuations and continuous state support. We are less constructive on Peru and Colombia, where the risk/return profile appears less attractive. Valuations in Panama look stretched, in our view.
- **CEEMEA:** We favour selected GCC countries -- UAE primarily -- as we believe that the economy benefits from strong fundamentals and is better positioned than regional peers given that it is a more diversified economy. On the other hand, we are cautious on Saudi Arabia, where the technical picture is weakening due to strong issuance in 2020. We also favour HY countries, such as Ukraine, Egypt, Ivory Coast, and Nigeria.

- **Asia:** Indonesia remains our favoured credit. We believe that bonds should benefit from continued investor flows considering the high credit quality and the CB credibility. We are less constructive on Philippines and Malaysia due to expensive valuations.

EM local-currency sovereigns: benefitting from a supportive outlook on EM FX

We head into 2021 less bullish on local rates, but with a more favourable view towards EM FX, which, we believe, appears undervalued. We believe there is upside potential for the asset class in 2021, after having lagged other EM fixed income sectors for a long time. The current environment is supportive for EM FX. CBs have eased policy around the globe, leading to a low-yield environment, while inflation remains benign. We expect to see more normality in policy making under the incoming US administration. **Furthermore, an early-cycle growth environment typically heralds EM FX appreciation**. An area of attention is the dollar after the recent vote in Georgia. In the medium term, the outlook is for a weaker dollar, but in the short term the prospect of an aggressive fiscal policy could drive some dollar appreciation.

Figure 5. FX medium-term fair value, valuation range



Source: Amundi Research. Data as of 25 January 2021. Amundi fair value is calculated by including rates and spreads, FX and CB metrics in a comprehensive model, whereas the first three histograms are based on mean reversion and specific angle assumptions. GREAT Framework: Global Risk Exposure Analysis Tool, developed by Amundi.

In this context, we remain positive on the expected returns of local-currency sovereign bonds, mainly driven by carry and EM FX appreciation, while we expect price returns to remain stable. EM FX returns should be driven by flows back into selective EM countries due to a post-Covid-19 recovery.

In 2021 we see some potential for risk premia to compress, mainly within EM FX and HY credit, and somewhat also in local rates. Our main investment themes in the local-currency universe are:

"The current environment is supportive for EM FX. CBs around the globe have eased policies, leading to a low-yield environment, while inflation remains benign".

- **We prefer high-yielding countries over low-yielding ones**, as they offer the potential for a better risk-adjusted performance. Although US yields are rising, we believe that high-yielding countries will see a relatively better performance on rates. In high yielders, we position for risk premium compression, **with a preference for countries such as Russia and Turkey**. In 2020, we were concerned about rising political risk premium. However, we believe that a corner has been turned and judge an imminent geopolitical escalation as unlikely. Russia should benefit from the expected commodity price recovery. In Turkey, also see value in local bonds following market friendly changed at the Central Bank, aggressive monetary policy tightening and very light positioning by international investors. Additionally, we expect high-yielding EM FX currencies to outperform.

- **We prefer countries with attractive real yields**, such as South Africa, Mexico and Indonesia.
- **In Asia, we are very positive on countries that should benefit from capital inflows, such as China**, where local bonds should be supported by global benchmark inclusion. We expect FX to outperform, supported by a weaker dollar, vaccine optimism fuelling broader EM reflationary trends, and reduced tariff threats.
- **We also like the candidate countries with good IMF or EU anchors which are expected to be included in the benchmark index, such as Egypt, Serbia and Kazakhstan.**

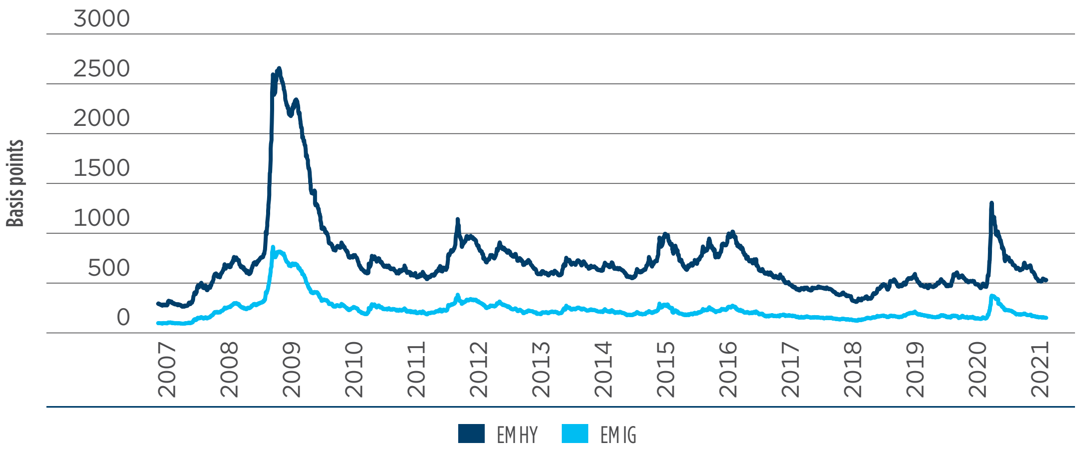
Colm D'ROSARIO
Co-Head of EM Corporate and HY

Maxim VYDRINE
Co-Head of EM Corporate and HY

EM corporates: resilient throughout the crisis

EM corpor ates delivered a more resilient performance this past year compared to EM FX and to global credit sectors. While we expect the global environment to remain supportive for EM corporate credit in 2021, spreads appear tight vs fundamentals from an historical perspective.

Figure 6. EM IG and HY credit spreads



Source: Amundi analysis on Bloomberg data as of 2 February 2021.

On a positive note, earnings for EM corporates started to turn the corner in Q3 2020. Given the extraordinarily accommodative monetary policies and the forecast of improving fundamentals in 2021 on the back of vaccine rollout, **we expect the improvement in credit metrics to continue over the next twelve months. This could lead to further spread compression over 2021, particularly in the HY universe.**

We expect to see stronger rebounds in sectors that were negatively affected by Covid-19. In terms of ratings, **we are positive on the single-B space**, as we expect to see greater deleveraging than among CCCs, leading to potential outperformance as a result. While we believe that EM defaults should stay limited, we remain selective and focused on seeking fundamentally strong corporates, especially when moving into lower-rated credits. **In terms of specific opportunities:**

"Earnings for EM corporates started to turn the corner in Q3 2020. We expect to see stronger rebounds in sectors that were negatively affected by Covid-19".

- **We favour higher beta and cyclical sectors**, as they could benefit from the positive macroeconomic momentum. In Latin America, we like Brazilian energy, financials, consumer and pulp & paper.
- **We see value in Mexican banks, metals & mining and energy**.
- **In Asia, Chinese real estate is our core preference**, albeit we believe investors shoud be selective on individual names.
- **Within EMEA, we believe Ukraine offers the best risk/reward** opportunity; we suggest playing it though consumer and utilities.
- **We are cautions on Asian IG credit**, as valuations appear stretched.

Overall, we are constructive on the EM corporate space. However, while the tide is rising, we do not expect it to lift all boats. Credit selection will remain key.

Patrice LEMMONIER
Head of EM Equity

EM equity: the potential for outperformance

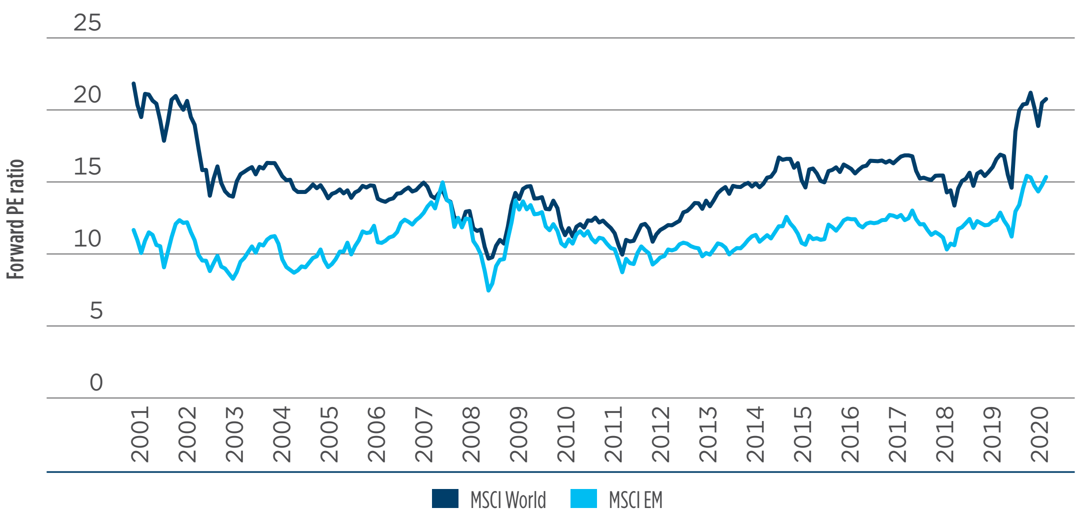
Economic and earnings momentum and relative valuations are bright spots

The backdrop looks positive for EM equities in 2021. Global equities should be supported by the reopening dynamic as well the limited upside of mainstream bonds. Large CBs appear to be willing to be accommodative for longer. Equities are more protected than bonds from any potential negative surprise on inflation.

Economic and earnings momentum are improving in EM. Any equity market correction should be relatively limited, as: (1) markets will focus on incipient mass vaccine availability, with 22 vaccines either in phase 2 or 3 trials or having been approved; and (2) the economic impact of new Covid-19 waves should be relatively muted as governments and doctors improve policies to cope with the pandemic (better management of mobility, improving treatments).

EM equity valuations are relatively attractive in the current global context. Although not historically cheap, EM equities are still trading within a normal historical valuation band when looking at cycle-adjusted earnings. In addition, sector-adjusted analysis shows that **EM equities are trading at their lowest point compared to DM in the last 15 years.** Finally, EM currencies should be stable or appreciate as the "blue-wave stimulus initated by President Biden will likely result in appreciaton of the USD vs the EUR (due to widening bond yield diferentals), but will be counter-balanced by a better growth outlook in emerging economies.

Figure 7. Attractive EM valuations compared to DM



Source: Amundi Research on Bloomberg data as of December 2020.

"EM valuations are relatively attractive vs world equities".

Four risks to watch

Outside of country-specific developments that we analyse in detail below, we see **four main risks for EM equities in 2021:**

- **The vaccine issue.** Vaccination of EM populations will definitely will be slower than for DM. At the time of publication, **the ratio of 'vaccine order book' to 'population size' was much lower in EM than in DM.** Only UAE, Chile and Mexico have, on paper, a large enough order book to vaccinate their entire population. Asia (especially North-East Asia) has efficiently controlled the spread of Covid-19, but that very success has set the region behind the US and Europe in the race for developing vaccines. In some countries with limited coronavirus outbreaks, regulators have relied on other countries to test the new vaccines first while the low level of Covid-19 cases means

"The evolution of the virus cycle as well as the vaccination campaign are key risks to watch in 2021".

that locally developed vaccines have sometimes struggled to complete clinical trials. **A slower vaccination process will probably cap the cyclical rebound of some countries in the short term and lead to some degree of de-synchronisation.** In such a scenario, the growth of some countries will fully normalise only in 2022, but, in our view, markets will anticipate recovery in sync with global markets and overlook this delay. We are also relatively relaxed regarding the vaccine issue as we believe that some vaccine candidates with less stringent temperature conservation requirements could prove their efficacy (this could include one of the four Chinese vaccines in phase 2 or 3, the Russian "Sputnik V", the AstraZeneca/Oxford vaccine or any other Western non-mRNA-based vaccine). As the logistics of those vaccines are easier to manage, this could potentially help many EM countries to reach herd immunity before or around the end of 2021.

- **Covid-19 mutations.** Although Covid-19 mutations will delay the speed of global recovery, we are hopeful than many governments will endeavour to limit the spread of more easily spread Covid-19 variants, as seems to be the case currently for the South African strain. In addition, mRNA technology should enable, if necessary, the fast development of vaccines (in six weeks, according to BioNTech, the company that designed the first available Western vaccine with Pfizer).
- **US/China trade relations.** Initially, the perception of US/China trade negotiations could cosmetically improve, as discussions will probably pass under the radar of investors: the fight against Covid-19 will be one of the key priorities of the new US administration and US/China dialogue will probably occur behind closed doors, without tweets. However, **under President Biden's leadership, the outcome of trade talks may end up being tougher than expected for China** as the new US president will probably try and set a common coherent approach with his partners in Europe and maybe among ASEAN countries (something that his predecessor was unwilling to do).
- **A potential tech/internet correction.** Both expectations and valuations are very high for most internet and/or technology stocks. Growth in the past 10 years has been driven by the increasing usage of smartphones, coupled with better telecommunications networks. This has boosted online markets (ads, game, social activity, e-commerce) and led to a huge cannibalisation of "offline". Today, however, both penetration and time spent are very high, with competition increasing and companies being scrutinised by many regulators. Risk of disappointment on growth exists while expectations on future drivers (self-drive electric vehicles, internet of things, augmented reality/virtual reality, etc) could be reset lower.

We believe that the risk of a spike in global inflation translating into a much higher cost of debt and equity for EM is not that significant, at least in the first half of this year and probably for the whole of 2021. Elevated unemployment, large output gaps, and still- accommodative CBs should prevent this inflation risk from becoming an issue quickly.

In addition, **China, Korea and Taiwan, which together account for close to 70% of the EM benchmark, should not be too prone to global inflation vagaries, thanks their economic and monetary stability.** After all, China's PBOC is almost the last remaining bastions of orthodoxy in the world of large central banking. Nevertheless, it is true that in the long term, the increasingly elevated indebtedness levels of many countries might become an issue for the global growth outlook, an issue that could appear once inflation spikes.

Play the rotation towards cyclical and value in EM

In the following pages, we analyse the rationales for country views and opportunities. However, on a broad level, we generally **shift our convictions on ex-China countries based on specific opportunities.**

"Growth: we are cautious regarding what look to be excessive valuations. Value: we maintain a positive view on stocks that are likely benefit from re-opening as we still see valuations as attractive".

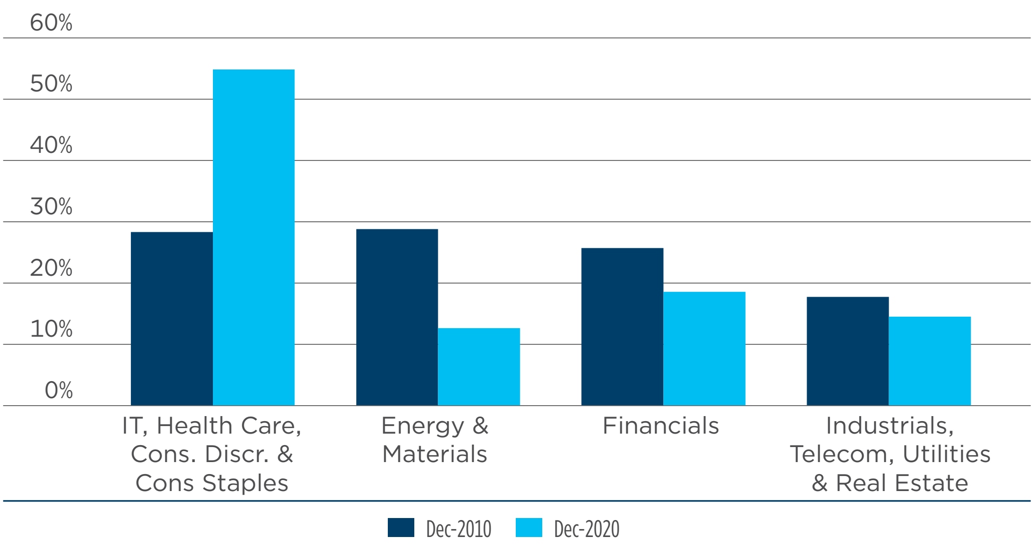
Regarding sectors classified as 'growth', **we are cautious regarding what look to be excessive valuations** for some 'hot' themes, like EV batteries/vehicles and health care. Assumptions for EV car penetration already look high while the risk of disappointment on margins are significant. Within the highest growth sectors, we maintain a preference for semiconductors, including memory chip makers, as the cycle should improve in the next two years and valuations still look very reasonable. We maintain a more cautious view on internet stocks, mostly in China, given regulatory risk, increasing competition, and the risk of disappointment regarding growth.

As for the more cyclical or value sectors, we maintain a positive view on stocks that should benefit from re-opening as we still see valuations as attractive — ie, mostly commercial shopping malls and travel agencies. Elsewhere, we continue to view intra-sector valuation discipline as critical:

- The cyclical commodity sector is no longer cheap;
- Within financials, most banks should see improving outlooks in terms of asset quality, but the speed of recovery is likely to be disparate; and
- Stock selection for utilities and telecoms will again be a function of the ability to navigate regulations and stock-specific drivers.

The resilience of domestic consumption will be another key theme to watch with regard to investment opportunties. Many EM are transforming their economic models, from export- and energy-dependent towards domestic demand-driven, and this is also reflected by equity index compositions which in the last 10 years has seen substantial transformations.

Figure 8. MSCI EM index sector weighting by market capitalisation



Source: Amundi Research analysis on Bloomberg data as of 1 December 2020.

Esther LAW
Senior Portfolio Manager - Emerging Markets Debt

Deirdre MAHER
Head of Frontier Markets Equity

With the contribution of
Hakan AKSOY
Senior Portfolio Manager - Emerging Markets Debt

Look for quality in Frontier markets

Given our view of a constructive EM debt backdrop as part of the global recovery story post Covid-19 while liquidity remains ample, inflation benign, and with global yields staying low for longer, **we think diversification into 'quality' frontier markets (FM) will remain an attractive proposition**. We must emphasise that investment in FM needs to be selective, as the weaker ones could remain volatile. With regard to quality, we are looking for countries with:

- A manageable debt matrix;
- Healthy FX reserves;
- Strong fiscal consolidation anchors;
- IMF programmes already in place or potential candidate and/or EU convergence angle;
- Index inclusion potential;
- Political stability; and
- Good liquidity.

On the local currency frontier front, we like Egypt, Kazakhstan, Ukraine and, to a lesser extent, Serbia, due to tight valuation on the latter. All these countries are potential candidates for GBI-EM Index inclusion with some other features mentioned above. For instance, Egypt bonds have recorded a stellar 15% total return in 2020, despite all the Covid-19-related volatility. It is also encouraging that there is clear **evidence of frontier market local bond liquidity improving,** as we are seeing many more quotes on a more regular basis which was not the case in the past. On the hard currency debt front, we also like Egypt, Ukraine and Ivory Coast, based on valution.

On the **equity markets** front, although we have seen a strong rebound in emerging equities, **frontier equities have lagged and are now trading at their widest discount to EM in the past five years**. Of course, this is not a homogenous segment and differentiation should be made between individual markets. **On that point, there are a couple of frontier equity markets tht are worth investors' attention.**

Vietnam is the largest equity market in frontier and it has successfully contained Covid-19, avoiding a recession. Due to its increasing position as a regional hub benefitting from supply chain shifts and also significant investment through both public investment and FDI (foreign direct investment), it should grow strongly this year based on expansion in the manufacturing and service sectors, and a resilient domestic consumer. The new Biden administration has signalled that it may join the TPP (Trans-Pacific Partnership) which would be a further, significant, boost to the economy. The currency is expected to remain strong due to the trade surplus and strong reserves. Given such a strong backdrop and as it is trading at a discount to regional peers, Vietnam is a market that is looking interesting for 2021.

Another market that equity investors should have on their radar in frontier markets is Kazakhstan, with its strategic importance in the New Silk Road initiative and its resilient economy. Kazakhstan is rebounding well from the impact of the pandemic and should show growth (about 4%) next year, supported by fiscal spending and a solid reserve buffer. The equity market is increasingly accessible to investors and offers an interesting and discounted alternative to other markets in the region.

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Regional and country assessment for investing in EM equities

ASIA

1 China - *neutral*
See page 15.

2 India - *positive*
See page 18.

8 Hong Kong - *neutral*
The valuation of the HK market is not cheap. However, a strong Chinese economy as well as an improving economic outlook post-pandemic would support the market.

9 Vietnam - *positive*
An economic rebound is expected to continue in 2021, mainly driven by internal consumption, state investment in infrastructure, and manufacturing. We remain positive on the market, now the largest in MSCI Frontier, which MSCI could put on the watch list for upgrade to EM status. Valuations are attractive vs the rest of the EM universe.

4 South Korea - *positive*
Korea is one of the few countries where Covid-19 had an overall limited impact. The economy has benefited from healthy exports thanks to companies that are competitive globally in growing industries. We remain optimistic on the Korean equity market for 2021. Valuations remain overall relatively attractive, mostly in the still-dominant technology sector.

5 Thailand - *cautious*
With ~14% of GDP coming from tourism, Thailand has been one of the ASEAN economies hit hard by the pandemic. The Thai economy remains in the doldrums, as witnessed by a slow pace of recovery (little fiscal and monetary policy space). We are cautious and prefer companies that are less reliant on tourism sector.

7 The Philippines - *cautious*
The country went through an eight-year upcycle prior to Covid-19 and the economic recovery should be lower than in other countries. One of our main concerns also continues to be the currency, which we view as relatively expensive and also very sensitive to commodities or energy prices. Overall, we maintain a cautious approach.

3 Taiwan - *cautious*
The relatively robust economic outlook must be viewed within the context of what are already quite elevated valuations within the region and the relatively less cyclical exposure that Taiwan offers. We are cautious on financials and positive on tech and industrials.

6 Malaysia - *cautious*
The 2020 rally brought forward much of the upside from this year. We remain cautious on sectors exposed to domestic consumption and investment (banks, construction, property, telcos, consumers); we are more constructive on exporters (IT, commodities) and selectively on REITs and utilities, which offer resilient and attractive yields in a low-interest-rate environment.

10 Indonesia - *positive*
We expect a strong cyclical rebound in 2021, thanks to stronger exports, with rising commodity prices and volumes, a good external balance, moderate inflation, and continued fiscal and monetary stimulus. We maintain a positive stance towards banks and the infrastructure sector.

Colours indicate Amundi equity view on the country for 2021

Cautious	Neutral	Positive

With the contribution of
***Nick McConway**, Head of Asia ex Jap. (Taiwan),*
***Deirdre Maher**, Head of Frontier Markets (Vietnam),*
***Lionel Knezaurek**, GEM PM (Indonesia),*
***Mickaël Tricot**, Head of GEM (Korea),*
***Andrew San**, Malaysian PM (Malaysia),*
***Hicham Lahbabi**, Deputy Head of Asia Ex Jap. (Philippines),*
***Gwen Tsui** and*
***Thomas Yeung**, China equity PM (Hong Kong) and*
***Manuele Moi**, Asia Ex Jap. PM (Thailand).*

Amundi
ASSET MANAGEMENT

1 **China** - *neutral*

***Claire Huang**, EM Macrostrategist and **Qian Jiang**, GEM Equity Portfolio Manager*

Shifting drivers of growth: the year of the consumer

Though having enjoyed "first-in, first-out" in most of 2020, China is not immune to the new winter outbreak. While the country's infection rate is relatively low compared with the rest of world, the stringent approach the government chose to handle the outbreak (mass testing, regional lockdowns and travel restrictions) has driven us to lower near-term growth expectation. **Looking ahead, transitory set-backs are likely, but are not expected to derail the overall recovery.**

Private consumption to lead the recovery in 2021. With the repairing of household balance sheets and the narrowing of excess savings, services activities are on track to return to normal. We expect private consumption growth to firm and lead the overall economic growth recovery. Meanwhile, as policy neutralises, public investments look set to cool.

Industrial production growth was exceptionally strong, running above trend till the end of 2020. This is in part attributable to the resurgence of demand for medical supplies and remote working equipment. Based on the upcoming vaccine supply to EMs, we expect China's export strength to last at least through 1H21, resulting in a continuous large current account surplus and driving the currency to appreciate further. **We have a target for USD/CNY of 6.45 by mid-2021** and then expect the exchange rate to largely stay stable or depreciate slightly as the BoP (balance of payments) advantage dissipates in H2.

Reflation insight

In light of a broad recovery led by the consumer sector, **we expect inflation to increase in 2021.** Services and core inflation have shown signs of bottoming since August. We expect both to climb to around 2% in 2H21 from the current subdued levels.

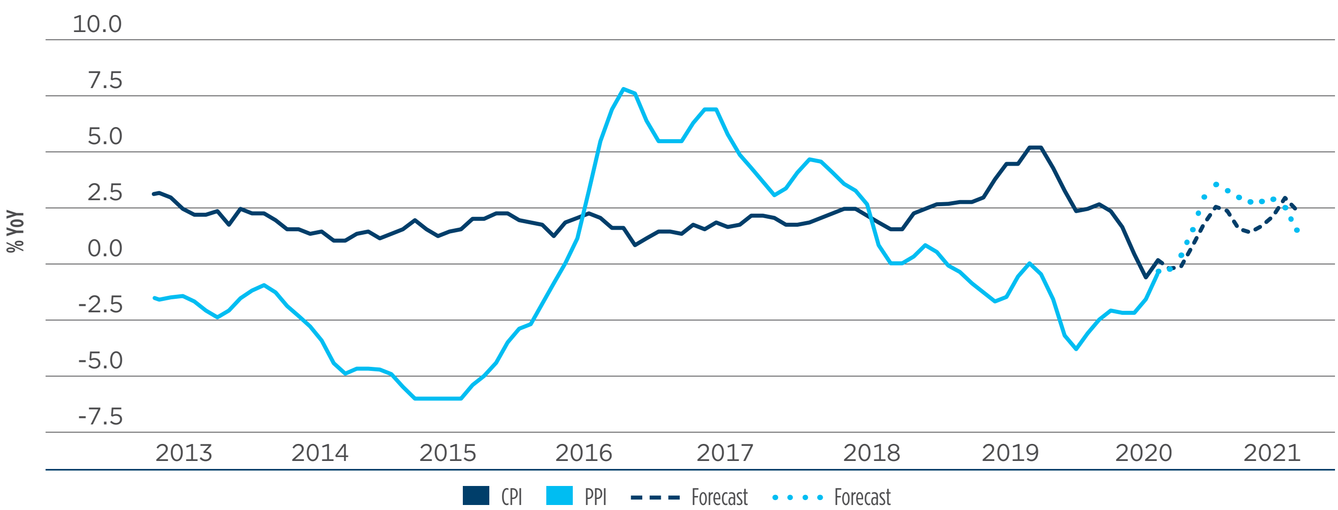
Negative headline CPI print, which was mainly driven by pork prices and supply factors, should be a temporary phenomenon. We also expect producer price inflation (PPI) to climb out of the deflationary zone, supported by the high domestic industrial capacity utilisation and global commodity price rebound.

	2021	2022
GDP	8.4;9.0	5.1;5.7
Inflation	1.6	2.0

Source: Amundi Research as of 29 January 2021.

> *"GDP growth should support corporate earnings. However, we remain cautious on China's mid- to long-term growth potential, as overall leverage remains high and productivity gains look more difficult."*

Figure 9. China inflation outlook



Source: Amundi Research on CEIC data as of 12 January 2021. CPI: Consumer price index, PPI: Producer price index.

Policy outlook: watch credit growth and targeted sector policies

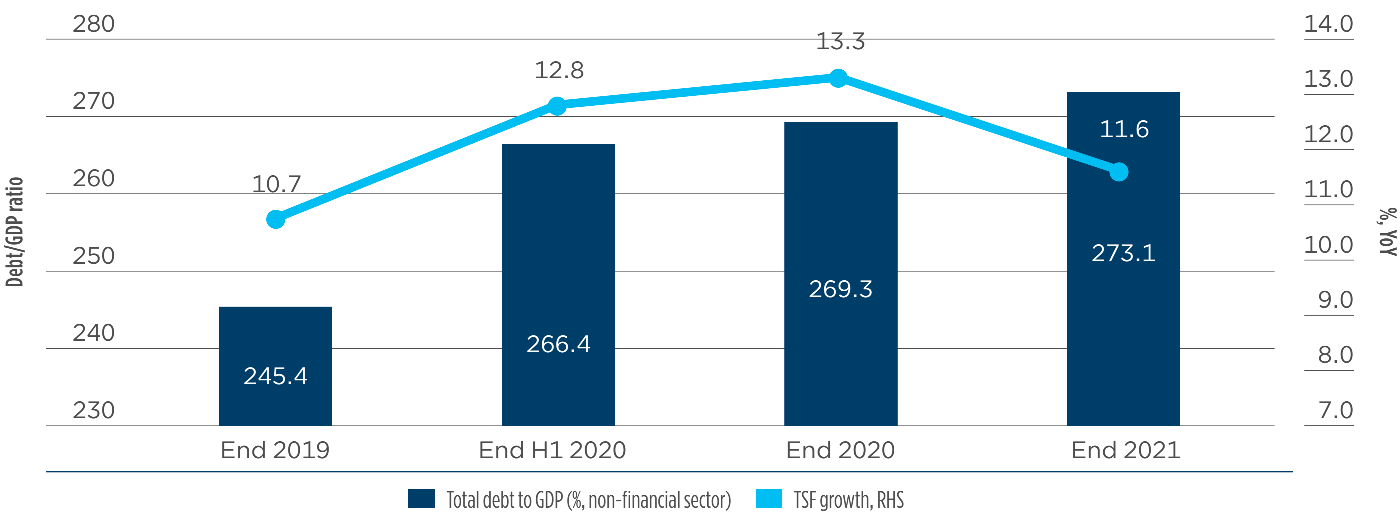
- The year-end Central Economic Work Conference confirmed that macro policy will continue to normalise, but the pace of adjustment will be gradual to avoid accidental over-tightening.
- **Policy rates, including the Loan Prime Rate (LPR) and RRR, will remain unchanged.** For the interbank market, the PBoC is expected to guide rates to hover around its anchors, including the seven-day reverse repo rate at 2.2% and one-year MLF rate at 2.95%. However, the unexpected liquidity tightening ahead of the Chinese New Year suggests concerns over asset bubbles outweighed economic recovery risks. The central bank is normalising its monetary policy with a tightening bias.
- **Macro leverage should hold stable, translating into slower credit growth.** We expect total social financing growth to slow to 11.6% at the end of 2021 from 13.3% at end-2020. Still, this would be notably faster than the pre-Covid 10.7%.
- **We expect to see less expansionary fiscal policy and a reduced quota for special government bonds.** Unlike in 2020, the need for fiscal stimulus to stabilise the economy has decreased. As a private sector recovery gains momentum, funding support for public investments will be dialled back. As a result, bond supply will likely decrease, starting with the reduction of RMB1tn of Special China Government Bonds.

"The fundamental picture for earnings is positive, but slower credit growth and sector-targeted or local-level policies are key things to watch in 2021."

Meanwhile, bigger policy tweaks at the sector level look inevitable. The top two targets for tightening, have been real estate and tech monopolies. At end-2020, financial regulators released new rules capping bank lending to developers and households. Antitrust regulations for tech companies have also gained momentum, following the cancellation of the Ant Financial IPO. On a positive note, tax cuts for SMEs (small and medium enterprises), tax relief for R&D, and a loosening of local car purchase restrictions look likely.

Given an improving macro backdrop, we are positive on China's earnings recovery in 2021. That said, as credit growth slows, sector-targeted or local-level policy catalysts could complicate the investment picture, despite improving fundamentals.

Figure 10. China debt-to-GDP ratio and related total social financing (TSF) growth



Source: Amundi Research on CEIC and China CNBS, data as of 19 January 2021.

Targeting productivity to thrive over the long term

2021 marks the 100th year of the founding of Chinese Communist Party, a critical year for the leadership to review achievements and set new long-term goals. In 2020, President Xi and the administration laid out goals for the next five years and visions through to 2035, with a detailed guideline to be released at the coming March NPC.

In the long term, policies look to be centred on the goal of boosting growth potential. Specifically, there are four areas we would highlight:

- **Growth targets:** Growth is envisioned to moderate to an average 5% between 2021 and 2035. A likely path could be a slowdown from 5.5% in the next five years to 4% in the early 2030s.
- **Policy sustainability vs stimulus:** A prolonged period of conventional monetary policy is likely. In the end, it has to be reforms, not stimulus, that resolves structural imbalances and supports growth potential.
- **Development priorities:** Under the dual circulation model, the domestic economy will be more important in driving growth. The nation will play a key role in leading innovation. Capital would be prioritised for strategically important sectors and be directed away from the housing market. AI, quantum information, integrated circuits, life science, brain science, breeding, aerospace, and deep earth & ocean exploration are named in the 14th Five Year plan.
- **Geopolitics:** Despite decoupling from the US, China will actively seek deepening integration with the rest of the world, including joining the CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership). Even with the US, doors are open in certain areas -- for instance, with regard to fighting global warming.

Investment view

While Chinese GDP growth should rebound strongly in 2021, which should support corporate earnings growth next year, we remain cautious on China's mid- to long-term growth potential, as overall leverage remains high and productivity gains look more difficult in light of less access to advanced technology.

We have a neutral stance on the country, with a negative view on expensive names, mostly in health care, consumer staples and new technology (electric vehicles, semiconductors, the cloud, etc). Most of these sectors have re-rated sharply, thanks to high levels of liquidity and retail participation. In most cases, valuations look too high to us. We maintain a preference for companies in the renewables, gaming and leisure sectors. These sectors should continue to benefit from Chinese policy in favour of a cleaner and more domestically oriented economy. We maintain a cautious approach regarding most value sectors, as they look structurally challenged, and our holdings mostly reflect stock selection with a focus on restructuring opportunities or cash flow generation/the ability to increase dividends.

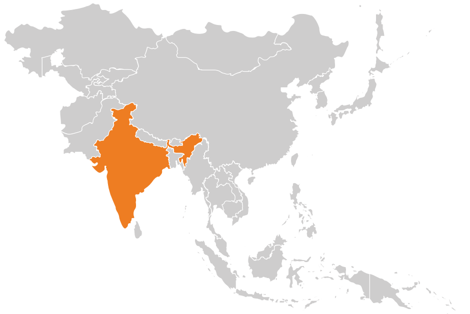
2

India - *positive*

***Mickaël Tricot**, Head of GEM Equity Funds*

Country Assessment

In line with most emerging economies, India's economic growth is expected to rebound in 2021 to 9.0% (fiscal year 2022) after a stringent lockdown which led to a strong contraction in 2020. The fiscal deficit at the central level does not look low at 7.2% in 2021, but fiscal support from the government has been measured. A strong pickup in economic growth in 2022 should be sufficient for the deficit to start to narrow and should not be a big concern. Lower interest rates, relaxation of recognition for non-performing loans (NPL), and healthy liquidity (thanks to a positive current account and a strong balance of payments) have provided most of the support to India's households and corporates.



	2021	2022
GDP	7.8;9.0	4.2;5.6
Inflation	5.6	6.2

Source: Amundi Research as of 29 January 2021.

The Indian equity market started to rebound in Q3, following signs that lockdown would not lead to a new massive spike in non-performing loans. It seems likely that a reasonable percentage of around 4-6% of total loans could become NPLs in 2022, a level most banks should easily digest.

The government has continued its **push towards structural reforms** by reforming the labour code and agricultural supply chains and price mechanisms. Finally, **the "Make in India" policy has been more formalized, with different incentives schemes** put in place to help companies to produce more locally or attract foreign companies to build manufacturing facilities in the country. A few Taiwanese electronic manufacturing services companies have applied and/or are committing capital to the country, which is welcome.

Following years of disappointment regarding economic growth, we think there are now good reasons to become more optimistic. Past NPLs have mostly been digested (thanks to the bankruptcy code put in place recently), real estate should no longer be a drag and could surprise positively (the RERA act has been cleaning up the sector), monetary conditions have eased a lot since the tight period of 2015-2018, and, finally, the balance of payments looks solid, with international reserves growing.

Inflation is a concern as it has rebounded to above 6%; our base case continues to be that fewer supply disruptions in 2022 should help in limiting upward pressure despite a cyclical upturn. The RBI maintained very tight monetary policy over 2015-2018 to reduce inflation expectations. A sustained increase in inflation would clearly be bad news as it would force the central bank to tighten sooner and faster.

> *"India's equity market is not cheap and partly discounts an improving profit outlook. Nevertheless, we remain constructive as the market is likely to rerate in line with profit growth and benefit from an economic upturn."*

Investment view

India's equity is one of our main convictions. India's market is not cheap and partly discounts an improving profit outlook for 2022. Nevertheless, we remain constructive as we think India has managed Covid-19 relatively well without excessive fiscal spending. The passing of structural reforms during Covid-19 to address key hurdles for economic growth is also obviously impressive. The market is likely to rerate in line with profit growth and expectations of a sustained improvement in growth. We favour private banks (mostly after 2H21), industrial companies that should benefit from higher domestic or foreign investments, and selected domestic cyclical stocks that are likely to benefit from an economic upturn. We are more cautious on expensive consumer staples and health care.

LATAM

2 Mexico - *neutral*
We expect Mexico's GDP to grow by 4-5% in 2021. About 40% of the its GDP is export-centric and will benefit from the expected resumption of US industrial activity. Mexico has one of the best vaccine order books among EM and we don't expect strong fiscal headwinds. We are neutral on Mexico and favour cyclicals and natural resources while we are cautious on consumer staples for regulatory reasons.

4 Peru - *cautious*
We are cautious and watch for political events, with general elections scheduled for April. Provided the political situation improves, Peru should continue to catch up in terms of income per capita and investments over the mid term. We are cautious on the country, but are watching vaccine and political events carefully to gauge when to re-focus on the banking sector.

6 Chile - *cautious*
General elections will occur in November. Chile is best placed in the region in terms of vaccine procurement. The country's GDP growth could near 6% in 2021. The market appears to anticipate some of these positive dynamics. Hence, our moderately cautious stance, focusing on some stock- specific investment cases that look interesting on risk/reward. Political volatility may open opportunities.

5 Argentina - *cautious*
The new government has managed to restructure 99% of its foreign debt. 2021 will be a pivotal year for Argentina, due to the confluence of a financial crisis and the impact of the pandemic. While we recognise the massive potential and extremely low dollar-based values, we are prudent. In 2021, we will watch carefully for developments and the resolution of chronic issues and a possible new agreement with the IMF.

3 Colombia - *cautious*
The sovereign credit rating could be downgraded to high yield due to a large increase in the public debt ratio and current account deficit trajectory. Monetary policy has space to stay on hold at 1.75% through 2021 as inflation continues to undershoot. We are cautious as even a moderately higher oil price would be insufficient to help solve the country's rising deficit and we do not expect any significant tax reform.

1 Brazil - *neutral*
See page 20.

Colours indicate Amundi equity view on the country for 2021

Cautious	*Neutral*	*Positive*

With the contribution of ***Patrice Lemonnier****, Head of EM Equity (Mexico and Peru),* ***Andrea Salvatori****, Head of ESG and Latin America Equity PM (Argentina and Chile), and* ***Lionel Bernard****, Latin America Equity PM (Colombia).*

Amundi
ASSET MANAGEMENT

1

Brazil - *neutral*

***Lionel Bernard**, Latin America Equity Portfolio Manager*

Country assessment

To mitigate the economic impact of the pandemic, in 2020, the government deployed the strongest fiscal stimulus in Brazil's history. The budgetary impulse added around 9% of GDP, leading to a GDP decline of around 4.0% for 2020. This was the lowest contraction among large Latin American countries, which are ranging from circa -6% of GDP in Chile to around -11% in Peru. The largest stimulus came from cash transfers to households ('Coronavoucher'), representing close to 4.5% of GDP in 2020. The set of measures was broad, including financial support to states and municipalities, extended government-backed credit lines to small businesses, and the introduction of employment retention schemes. The ~15% nominal fiscal deficit propelled Brazil's gross public debt/GDP to above 90%. It will be critical to see how the government complies with the budgetary spending cap from 2021 onwards. **This appears to be the main challenge for Brazil in the coming years, one that will require both moderation in government spending and structural reforms.**

	2021	2022
GDP	3.0;4.0	1.1;3.1
Inflation	5.4	3.8

Source: Amundi Research as of 29 January 2021.

We expect GDP growth of around 3.5% in 2021, including a carry-over effect of almost 3%. Growth should be supported by the reopening process in manufacturing and services activity while consumption and government spending should act as major headwinds. Together with a soft recovery of the labour market, this should translate into a contraction of wages in real terms.

> *While low interest rates and the expected economic recovery are positive for Brazil, the adoption of structural reforms calls for caution. We recommend a neutral stance, with a preference for cyclical stocks.*

The continuation of easy financial conditions should stimulate credit-led consumption growth. The government and the Congress may seek reform to create space for higher welfare transfers without breaching the constitutional spending cap. The recent pick-up in inflation was mainly food-related and should be temporary. Hence, **inflationary expectations should remain within the central bank's target range**. In our baseline scenario of anchored inflation expectations, robust external position (mild current account deficit, positive FDI, comfortable net external debt), and fiscal discipline, the CB should maintain an accommodative monetary stance with the lowest real interest rates on record for the country. **A scenario of a weaker USD and higher commodity prices should also be supportive for the BRL** (Brazilian real), which could result in a slow re-appreciation trend in 2021. Important reforms should be discussed in Congress in 2021: the emergency reform, the tax reform, the administrative reform, the public funds reform and privatisations. However, the reforms agenda lost momentum in 2020 and is expected to remain erratic and disappointing in 2021. We expect to see only mild adjustments. The most important threats to our rates, currency and fiscal outlook mainly relate to the risk of a second wave of infections and/or vaccination delays. **Brazil seems to have secured a sufficient number of doses to be able to reach herd immunity before year-end 2021.**

Investment view

We are **neutral on Brazil despite historically low interest rates and an expected economic recovery**. We acknowledge that this environment may prolong local investors' rotation from bonds to equities (although a large part of equity inflows is absorbed by an uninterrupted supply of IPOs and secondary issues) while the BRL and traditional sectors trade on relatively attractive valuations. However, a potential fiscal cliff in the context of uncertainty about virus eradication, as well as a painful adoption of structural reforms, still make us cautious. **We are positive on some discounted cyclical stocks, selected SoEs** (turnaround of profitability, potential privatisations), **selected consumption stocks** (omni-channel and food retail, fuel distribution, proteins) and banks (still discounted, although facing structural and Covid-19-related challenges). We are cautious on growth stocks (pure e-commerce, healthcare, IT), given their historically high valuation premiums.

EMERGING EUROPE

2

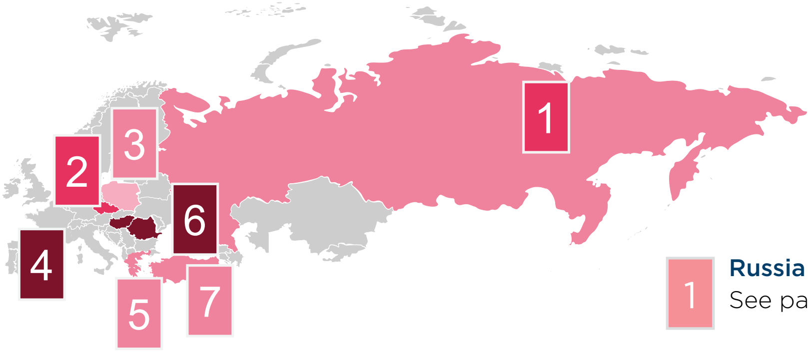
Czech Republic - ***neutral***
We expect to see significant recoveries in both domestic and foreign demand, supported by improved economic sentiment, loose fiscal and monetary policies, and EU funds. Gradual monetary policy tightening should help keep inflation within the tolerance band around the CB's target. Utilities and banks are among of our main preferences.

6

Romania - ***cautious***
The Romanian economy should start to recover in 2021, but at a slower pace than other CEE economies. Inflation is expected to remain inside the central bank's target range and should enable it to maintain easy monetary policy. We like sectors that could benefit from the expected EU infrastructure funds inflow. Overall, we maintain a conservative approach.

3

Poland - ***positive***
Poland should be one of the major beneficiaries of the EU budget and Recovery Fund, which should support investment and further modernisation of the economy. Low interest rates and a recovery in consumer confidence should also support an expected recovery in 2021. The market trades at a discount to past valuations. Among our preferences are consumer stocks and financials.



1

Russia - ***positive***
See page 22.

4

Hungary - ***cautious***
Hungary is likely to significantly benefit from the EU budget for 2021-27 and the Recovery Fund. Despite our optimistic short- to mid-term view, Hungary's economy shows some structural weaknesses, eg, economic reforms, falling population and corruption. Financials and oil are among of our favourite sectors.

5

Greece - ***positive***
Despite the pandemic, the improvement in the investment climate has attracted foreign companies to Greece. The Greek government aims to recover an IG rating for its sovereign bonds. We remain confident in the Greek turnaround story. Sectors such as banks, consumers and industrials, exposed to green investments, should be further supported by the EU Recovery Fund.

7

Turkey - ***positive***
Given the changes to macroeconomic policies (the Ministry of Finance and the governor of the CB have recently been replaced), Turkey should return to policy orthodoxy and sustainable growth. Inflation and forex are among the main risks to the recovery, as are sanctions. The investment case for Turkish equities is currently based on the value theme as the market trades at distressed valuations which are much lower than in the past. Banks, industrials and consumers should benefit from the reopening of the economy and tourism.

Colours indicate Amundi equity view on the country for 2021

Cautious *Neutral* *Positive*

With the contribution of ***Marcin Fiejka**, Head of CEEMEA Equity (Greece, Poland and Turkey),* ***Dan Karpisek**, CEE Equity PM (Czech Republic and Romania), and* ***Janos Kocsi**, CEE Equity PM (Hungary).*

Amundi
ASSET MANAGEMENT

1 **Russia** - *positive*

***Nikolai Petrov**, Russian Equity Portfolio Manager*

Country assessment

Russia's equity market was among the laggards in 2020, largely because the country is still significantly dependent on oil prices, which were very volatile due to the Covid-19 pandemic. In 2021, we expect to see a meaningful recovery of the global economy after significant pandemic-related losses, which should bode well for risky assets and commodity prices. **We expect to see a rise in the domestic retail investor base due to low rates, which should continue to provide support for the local market.** Vaccinations against Covid-19 with a domestically developed vaccine, Sputnik V, began in December 2020 and the pace will increase in 2021. We are hopeful that it will be as effective as seen in trials (above 90%).

Russia's economy has been less severely hit by the pandemic vs most other European countries, thanks to it having a relatively low proportion of services and small & mid-sized businesses. The GDP decline in 2020 is expected to be around 4%, and the recovery in 2021 is likely to be in a range of 2.5-4.0%. In our base scenario, we expect oil prices to fluctuate around USD50/bbl, which is a comfortable level for Russia's budget. The fiscal deficit should fall to around 2%, after almost 5% in 2020 (one of the lowest deficits in the world). Inflation is fluctuating around its target of 4%, and we do not expect to see any further significant moves in key rate in 2021 after the 2020 easing, as a weaker currency and strong global food prices put upward pressure on inflation, mitigating suppressed consumer demand. We forecast that real rates will remain in slightly positive or neutral territory in 2021.

As for geopolitics, sanctions remain one of the key risks for the Russian equity market. We expect the new US administration to develop a rather targeted approach to imposing sanctions and/or restrictions on the economy/specific sectors (as Russia is quite well integrated into the global economy through supply of commodities and a major hit to the Russian economy would not be welcomed by European allies). However, the headline risks are still material. At home, Russia has scheduled **parliamentary elections for September 2021**. While our base scenario is that the ruling party will confirm its strong majority, we notice the continued gradual decline of its popularity and thus expect to see a tightening of the grip on opposition, which might lead to some political turbulence.

	2021	2022
GDP	2.5;3.5	2.0;3.5
Inflation	3.9	3.8

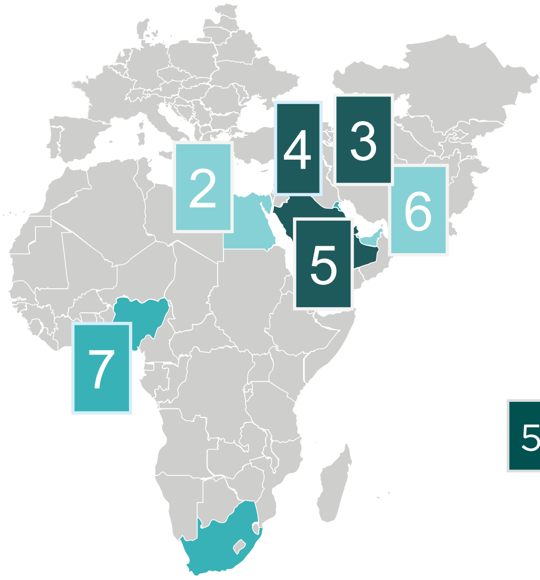
Source: Amundi Research as of 29 January 2021.

"The recovery in 2021 is likely to be in the range of 2.5-3.5%. Russia is quite well integrated into the global economic recovery through supply of commodities. Rotation from growth to value may continue for some time, supporting Russia's equity market."

Investment view

We think that rotation from growth to value that started in 2H20 may continue for some time, supporting Russia's equity market which has low valuations (the P/E for 2021 is around 8.3x in our base scenario) and high dividend yields (around 6.7%). Within the energy sector, we favour gas producers over oil companies, as the latter are potentially more prone to tax increases. Materials is in the sweet spot now after strong growth in most underlying commodities and a weaker ruble. Many issuers offer high-single-digit or potentially low-double-digit dividend yields. We remain positive on the financial sector which looks like it will see a recovery in EPS in 2021 and prefer industry leaders rather than potential recovery stories. Sanctions noise is clearly a risk, as banking is usually the most sensitive sector, although, in our base case, we expect sanctions to be limited to individuals. We continue to like the business models of key Russian listed technology names as they are generally leaders in their markets and are actively developing new services. However, sector valuations seem to be somewhat stretched. Consumer companies are becoming value plays, increasing dividend distributions, and are likely to continue to be solid defensive plays.

MENA AND AFRICA



2 Egypt - *positive*
Given the traction of IMF-backed reforms, its growing population, and strategic location at the gateway to Africa and the Middle East, the Egyptian market should offer long-term growth. With interest rates below 10% and inflation undershooting, monetary policy is needed to boost investment and productivity. We are positive on the market (banks, mid-cap companies exposed to consumers) and we believe it is a long-term growth story.

7 Nigeria - *neutral*
Looking into 2021, the IMF is forecasting a mild recovery of 1.5% growth for the Nigerian economy and a return to pre-crisis levels in 2022. Low oil prices have limited the scope for fiscal policy. The oil sector should start to recover from early next year as Nigeria's production quota rises. The market is trading at a significant discount. However, given the disconnect between economic fundamentals and capital controls, the discount is likely to remain in place.

1 South Africa - *neutral*
See page 24.

4 Kuwait - *cautious*
The recovery in 2021 is expected to be muted as OPEC+ supply cuts are still in place and consequently the oil sector (52% of GDP) is taking longer to recover. The authorities have been using the General Reserve Fund for liquidity, but this cannot be sustained. Given the weak macro fundamentals and a lack of catalysts, we do not expect the market to outperform in 2021. Selective stories could stand out and a number of individual names that will benefit from the re-opening of the local and global economy post-Covid-19 will warrant attention.

3 Qatar - *cautious*
In 2021, Qatar should be back to a twin surplus environment, with large current account and fiscal balance surpluses. Another positive catalyst should come from the end of the Qatar blockade Bahrain and Egypt). However, we maintain a slight defensive stance due to an expensive valuation and a low dividend yield. In terms of sector allocation, we prefer resilient and solid banks.

5 Saudi Arabia - *cautious*
The comfortable debt and FX reserves positions offer the Saudi government the opportunity to implement some mega projects as part of the 2030 vision which aims to diversify economy away from oil. We keep a defensive position on Saudi Arabia due to high equity valuations, with a very selective approach and a preference for banks and consumers.

6 UAE - *positive*
Looking into 2021, UAE should also benefit from structural reforms. Given the value profile and the cyclical profile of the index composition, we start 2021 with a positive stance on UAE. We favour industrials and real estate names.

Colours indicate Amundi equity view on the country for 2021

Cautious	Neutral	Positive

With the contribution of
Deirdre Maher*, Head of Frontier Markets (Kuwait and Nigeria),*
Marcin Fiejka*, Head of CEEMEA Equity (Egypt), and*
Rémy Marcel*, EMEA Equity PM (Saudi Arabia and UAE).*

1

South Africa - *neutral*

***Rémy Marcel**, EMEA Equity Portfolio Manager*

Country assessment

Like most investors, our focus for South Africa remains on the fiscal situation. Public debt/GDP has increased from 48% in 2015 to 84% in 2020, with the fiscal deficit likely above 14% of GDP for 2020.

The Covid-19 outbreak came at a particularly poor time for the country as it was already suffering from very weak growth (barely above 1% in real terms between 2014 and 2019). Given the lack of structural reforms before the Covid-19 crisis, the weak fiscal situation, and low household and corporate confidence, **our base case is that economic recovery in 2021 will be weak**, at around 3.0%, reinforcing concerns on debt sustainability. The overall fiscal balance may still be close to double digits in 2021. The fiscal consolidation plan announced by the government in October is a good sign, but is aimed at stabilising debt only in 2025-26. **In the absence of significant progress on debt stability, South Africa could face a funding and debt situation that might force the country to seek some form of support from the IMF.** This is a scenario that we do not exclude in the medium term.

Furthermore, it mostly relies on a freeze of public wages, which may not be that easy to get as the left wing of the ANC may oppose it. The lack of credibility with regard to adhering to fiscal plans meant Moody's and Fitch downgraded the sovereign to sub-IG.

On the positive side, thanks to a surge in export volumes (notably commodities) and moderate import dynamics, **South Africa's current account balance should turn to a surplus** in 2020 for the first time in many years. This year, we expect the current account to be broadly balanced. This environment is supportive for the local currency, the ZAR, which strengthened by approximatively 25% against the dollar since the lows seen last April.

On the political front, we identify other sources of optimism: one of the main opponents of President Cyril Ramaphosa in the ANC has been charged with corruption. This may reinforce the president's position in the ANC and help with implementation of the reforms agenda. The ANC will hold its National General Council meeting in May 2021. Local elections will take place in August 2021. President Ramaphosa's power in the party will be closely monitored during these political events with the ANC's key National Conference event of December 2022 in sight. **Apart from debt dynamics, other key reforms on the agenda relate to SOEs, public sector governance, power and infrastructure**. Note that some reforms unpopular with investors, eg, expropriation of land without compensation or nationalisation of the CB, remain on parliament's agenda. Mr Ramaphosa's position in the ANC will be key to removing overhang risks regarding such populist proposals identified as not market friendly and a source of concern for many South African corporates and individuals.

	2021	2022
GDP	2.6;3.6	1.6;2.6
Inflation	3.7	4.3

Source: Amundi Research as of 29 January 2021.

> *"Economic recovery is likely to be weak in 2021. South Africa could face a funding and debt situation that might force the country to seek some form of support from the IMF. We maintain a neutral stance on South African equities."*

Investment view

South African equities screen relatively well, with a next-12-months P/E relative to MSCI EM at discount of 30%. South Africa also offers a better 12-month-forward dividend of 3.2% compared to the MSCI EM index. In this context, we maintain a neutral stance on the country. Within the South African index, we remain cautious on domestic names even though we see attractive investments in the telecoms and industrials sectors. We maintain our preference for exporters, which tend to benefit from global cyclical upturns within the mining and internet spaces and are essentially privately owned.

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Definitions

- **Basis points:** One basis point is a unit of measure equal to one one-hundredth of one percentage point (0.01%).
- **Carry:** The carry of an asset is the return obtained from holding it.
- **CEEMEA:** Central and Eastern Europe, Middle East and Africa.
- **Correlation:** The degree of association between two or more variables; in finance, it is the degree to which assets or asset clas prices have moved in relation to each other. Correlation is expressed by a correlation coefficient that ranges from -1 (always move in opposite direction) through 0 (absolutely independent) to 1 (always move in the same direction).
- **Credit spread:** Differential between the yield on a credit bond and the Treasury yield. The option-adjusted spread is a measure of the spread adjusted to take into consideration possible embedded options.
- **Cyclical vs. defensive sectors:** Cyclical companies are companies whose profit and stock prices are highly correlated with economic fluctuations. Defensive stocks, on the contrary, are less correlated to economic cycles. MSCI GICS cyclicals sectors are: consumer discretionary, financial, real estate, industrials, information technology and materials, while defensive sectors are consumer staples, energy, healthcare, telecommunications services and utilities.
- **Diversification:** Diversification is a strategy that mixes a variety of investments within a portfolio, in an attempt at limiting exposure to any single asset or risk.
- **Dividend:** A sum of money paid regularly (typically annually) by a company to its shareholders out of its profits (or reserves).
- **FX:** FX markets refer to the foreign exchange markets where participants are able to buy and sell currencies.
- **Growth investment style** aims at investing in the growth potential of a company. It is defined by five variables: 1. long-term forward EPS growth rate; 2. short-term forward EPS growth rate; 3. current internal growth rate; 4. long-term historical EPS growth trend; and 5. long-term historical sales per share growth trend. Sectors with a dominance of growth style: consumer staples, healthcare, IT.
- **Quantitative easing (QE):** QE is a monetary policy instrument used by central banks to stimulate the economy by buying financial assets from commercial banks and other financial institutions.
- **Spread:** The difference between two prices or interest rates.
- **Volatility:** A statistical measure of the dispersion of returns for a given security or market index. Usually, the higher the volatility, the riskier the security/market.
- **Value style** means purchasing stocks at relatively low prices, as indicated by low price-to- earnings, price-to-book, and price-to-sales ratios, and high dividend yields. Sectors with dominance of value style: energy, financials, telecom, utilities, real estate.

Important Information

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