CITY OF LONDON
Investment Management Company Limited

Emerging Markets Quarterly Outlook

April 2019*

Overview

What to Expect After a Bumper Quarter

Asset markets experienced a bumper performance year-to-date, rolling back much of the sharp sell-off of late 2018. While bonds have delivered decent returns this year, risk assets (credit, commodities and equities) did extraordinarily well. Developed market (DM) equities led the charge, gaining 12.5% in Q1 in net total return terms (ex-US 10.5%). Emerging market (EM) equities performed strongly too, but lagged DM somewhat, with a return of 9.9% or 6.5% excluding China.

The overall market rally doubtlessly owed much to the Fed's unexpected pivot on rates. This was less a change in its reaction function as some have touted than an acknowledgement of a changed reality. Data releases had taken a sharp turn for the worse in Q4 and markets accordingly first priced out the chance of rate hikes in 2019 in December 2018 and in February 2019 began pricing as many as two rate cuts. However, the differential performance between DM and EM may appear odd in light of some developments which occurred over the same period. First, while the economic data stream in both had been disappointing in Q1, it generated much deeper negative surprises in DM than EM. Second, the improvement in risk sentiment that accompanied the more dovish Fed stance would normally be expected to create stronger demand for the higher-beta asset, all else equal.

So why the lagging performance of EM? It could have to do with initial market positioning, but evidence suggests a significant market underweight in EM equities in late 2018 and proportionately greater flows into EM than into DM markets. It could also reflect the scale of the sell-off in Q4, which was much sharper for DM at 18% vs. a mere 9% for EM. However, EM equities were sliding for most of 2018 and from their February peak, they had declined a full 25%.

Hence, the lagging EM performance either implies a significant potential for catch-up or else, markets are correct in pricing more limited upside potential for EM than for DM. Indeed, the three issues that dominate the outlook for 2019 could be most consequential for EM: 1) the risk of higher US rates and tighter financial conditions, 2) slowing growth, in particular in the US and China and 3) rising trade tensions. There has been respite on all three fronts recently: both the US and China have held off from further policy tightening or reignited stimulative policies (in the case of China also on fiscal policy); activity indicators have taken a turn for the positive, with PMIs in particular returning to expansionary levels, and hopes for a breakthrough in trade talks have been rising (albeit admittedly on thin evidence other than continued delay in imposing punitive measures).

That said, these changes are still tentative and the absence of a full resolution of these concerns weighs more heavily on EM than on DM. Emerging markets are more indebted and thus more sensitive to rate changes than DM, they are less domestic-consumption driven/more export-oriented and hence more dependent on foreign demand growth. Finally, their economies are more open and thus more vulnerable to disruptions to world trade than DM.

This interpretation is also consistent with the return patterns within EM, where above-average returns were concentrated in China (and Russia) in Q1. MSCI China returned 18% during Q1 (China A Inclusion Index 30%), significantly outpacing all other countries in the asset class. China, of course, is the economy at the centre of investor focus, where the growth slowdown and trade conflict are most pronounced. Any easing on these fronts due to stimulative measures and progress in negotiations thus benefits it disproportionately.

Market Strategy

While slowing activity and policy stimuli will likely continue to wage battle throughout the year, valuation changes during the recent rally have opened up some significant opportunities. They give rise to the following changes in our allocation:

- **China**: We upgrade China to *neutral* as recent policy stimulus has stabilised the economy and signals have emerged that the trade conflict with the US may be defused (although not resolved).
- **South Korea**: Downgraded to *neutral* as plunging memory chip prices and weakening foreign demand weigh on export prospects.
- **Thailand** is downgraded to *neutral* on political developments, while Indonesia and the Philippines are upgraded to *overweight* on an improving economic outlook.
- We maintain *overweights* to **Russian** and **Mexican** equities as valuations remain compelling and stay *underweight* in **Turkey** and **India** where fundamentals and policymaking are deteriorating and political risks have risen, respectively. **Brazil** also remains *underweight* as approval of pension reform is likely to prove lengthy, while the economic recovery has been tepid.

**The publication reflects asset performance up to March 29, 2019, and macro events and data releases up to April 5, 2019, unless indicated otherwise.*

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Asia

China

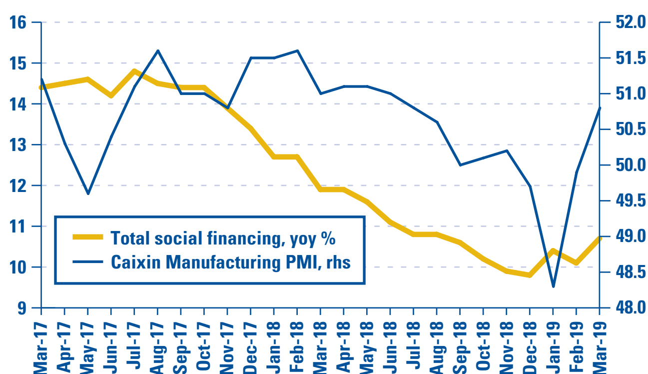
Neutral (↑)

The Chinese economy tentatively stabilised against the background of domestic policy easing and progress in the Sino-US trade talks.

China and the US have achieved meaningful progress this year with regards to trade negotiations, including postponing tariff increases. The US announced a 25% tariff rate on $50bn of Chinese goods in August 2018, followed by a 10% rate on another $200bn of goods in September. Yet, the Trump administration decided to postpone raising the tariff rate from 10% to 25% previously scheduled for March 1st, as the Chinese government offered to increase US imports and step up efforts on issues to protect intellectual property, as well as prevent forced technology transfers. Consensus expects a trade deal to be reached sometime in Q2, though the exact timing and terms remain unclear. One sticking point seems to be how to design an enforcement mechanism that is robust enough from the US point of view that warrants the lifting of US tariffs on Chinese goods.

GDP continued to moderate over the course of the year, slowing from 6.7% yoy in Q2, to 6.5% in Q3 and 6.4% in Q4 2018. Full-year GDP growth declined to 6.6% in 2018 from 6.8% in 2017, as fixed asset investment slowed to 5.9% from 7.2% in 2017. While the Chinese New Year distorted January-February data, tentative signs of stabilisation are emerging. For the first two months of the year, retail sales stabilised at 8.2% yoy, while fixed asset investment recovered to 6.1% yoy from 5.9% in December. Industrial production also picked up to 7.8% yoy from 6.7% in December, while the Caixin Manufacturing PMI rose to 50.8 in March from 49.9 in February. More importantly, credit growth has stopped falling as total social financing, a broad measure of credit supply.

Chart 1: Chinese Credit and PMI



Source: Bloomberg, The People's Bank of China, Markit

That said, activity in certain sectors remains sluggish. Residential property sales, for example, a leading indicator of real estate investment, contracted by 3% yoy in January-February. Another weak spot seems to be the car industry, where passenger vehicle sales contracted by 17% yoy for the first two months of the year. Upstream sectors (e.g. petroleum, steel and chemical) also suffer from weak demand and overcapacity. Autos and upstream sectors thus remain the key drag on industrial profits, which contracted by 14% yoy in January-February, the steepest decline since the global financial crisis.

Looking ahead, policymakers will likely prioritise growth over financial stability, a reversal from a year ago. First, fiscal policy is set to become "more forceful" – according to Premier Li - with planned cuts of close to RMB 2.0 trn in taxes and fees, including VAT tax cuts for manufacturing, construction and transport sectors. The quota for local-government bond issuance has also increased to RMB 2.2 trn this year from RMB 1.4 trn in 2018. Second, credit growth is likely to pick up modestly this year on the back of cuts in required reserve ratios (RRR) as well as the PBoC's efforts to help commercial banks replenish capital and increase their lending capacity. Third, the RMB has strengthened significantly this year, inching further away from the psychologically important level of 7.0 (versus the USD) and giving policy makers more room to ease if growth falters again. Fourth, growth-supporting policies are unlikely to be scaled back until China and the US formally reach a trade deal that restores the confidence of Chinese manufacturers and consumers. Overall, consensus expects growth to remain weak in H1 and pick up in H2 on the back of policy stimulus, resulting in full-year GDP growth of 6.2%, in line with the government target of 6.0-6.5% for 2019.

Market Strategy: MSCI China gained 17.7% in USD terms in Q1, outperforming EM equities by 7.8% points. Chinese A shares, as measured by CSI 300, staged a strong rally of nearly 30% in RMB terms, recouping almost all of the loss in 2018. The trailing P/E ratio of the MSCI China trades at a 5% premium to that of MSCI EM, a moderately expensive level when compared to the five-year average of a 12% discount.

We upgrade Chinese equities from underweight to neutral. Company earnings may look weak in the near term (particularly for autos and upstream sectors), but tentative signs of economic stabilisation, policy stimulus and progress in the Sino-US trade talks warrant a neutral position.

South Korea

Neutral (↓)

Plunging memory chip prices and weak DM manufacturing activity weigh on Korean equities. Chinese stimulus may provide support.

Negotiations on North Korean denuclearisation have become more tense this year despite three successful summits between the two Koreas last year and the first summit between the US and North Korea in June 2018. Political uncertainty increased when a summit between Donald Trump and Kim Jong-un in February was abruptly cut short and no agreement was announced.

Meanwhile, Q4 GDP rebounded to 1.0% qoq from 0.6% in Q3, lifting the yoy rate from 2.0% to 3.1%. Accelerating public consumption and a smaller contraction in private investment offset sluggish exports. However, the economy may have decelerated again in Q1 as DM manufacturing activity continued to slow, weighing on exports and industrial production. Indeed, exports contracted by 8.2% yoy in March after an 11.4% fall in February. Industrial production declined by 2.7% yoy in February, while manufacturing PMI recovered marginally to 48.8 after declining to 47.2 in February. Consensus expects Q1 and full-year GDP growth to moderate to 2.6% yoy and 2.5%, respectively, marginally lower than 2.7% in 2018.

Monetary conditions remain accommodative though as the Bank of Korea (BoK) maintains a gradual tightening cycle. It kept the base rate at 1.75% in February, after increasing it by just 50bps in the last two years. The BoK sounded less dovish than major DM central banks and low domestic inflation (headline and core inflation at 0.5% and 1.3% yoy, respectively, for February), reflecting its concern over financial instability and high household leverage. Consensus expects tighter policy over the next 12 months.

Market Strategy: MSCI South Korea gained 4.9% in USD terms in Q1, underperforming EM equities by 5.0% points. Its trailing P/E ratio trades at a 30% discount to the MSCI EM P/E, compared to the five-year average of a 20% discount. That said, Korea's forward P/E ratio is at 10.5 times, close to its five-year peak as the market has substantially revised down earnings estimates and expects a 10% fall in EPS for the next 12 months.

The earnings outlook remains challenging. On the one hand, the Chinese stimulus and progress in the Sino-US trade talks suggest that the fall in Korean exports may ease later this year. On the other hand, plunging memory chip prices significantly weigh on Korean I.T. firms. For instance, DRAM prices fell by 20-30% in Q1, losing 40-60% of their value compared to the 2017 peak, due to industry-wide overcapacity. Samsung and SK Hynix are two of the top three producers of memory chips in the world, with Samsung deriving 80% of its operating profit from memory sales. Overall, we downgrade our view on Korean equities from *overweight* to *neutral* due to the challenging environment for the I.T. sector (40% of MSCI South Korea).

Taiwan

Overweight

Taiwan's manufacturing and export cycle may bottom in the next few months. A substantial downward revision in earnings has already occurred.

Taiwanese Q4 GDP slowed to 1.8% yoy from 2.4% in Q3 against the background of a synchronised global slowdown. Exports grew by 1.2% yoy but slowed on a sequential basis. Still, private consumption remained solid while government consumption rebounded to 3.6% yoy from a contraction in Q3. Full-year GDP growth moderated from 3.1% in 2017 to 2.6% in 2018.

The manufacturing and export sectors remained tepid in Q1. Manufacturing PMI plunged to 46.3 before recovering to 49.0 in March, while industrial production contracted by 1.8% yoy in February. Both tech and non-tech exports remained sluggish for the first two months of the year, on the back of weak foreign demand globally (the US, the EU and China/HK). Looking ahead, however, consensus expects growth to bottom out in Q1 at 1.7% yoy before accelerating for the rest of the year, resulting in full-year growth around 2.1%. The sequential reacceleration could be driven by a bottoming of the semiconductor cycle, the government's infrastructure investment program and solid private consumption.

The Taiwanese central bank has maintained a "moderately loose" stance. It kept the policy rate at 1.375% in March, unchanged since June 2016. Consensus expects the central bank to remain on hold for the rest of the year. While low inflation (CPI inflation at 0.2% yoy in February) argues for a rate cut, the central bank seems concerned about its negative impact on banks' margins. Meanwhile, the labour market remains stable, with moderate growth in employment.

Market Strategy: Taiwanese equities gained 9.0% in USD terms in Q1, slightly underperforming EM equities by 0.9% point. Its trailing P/E is at a 6% premium to that of EM, in line with its five-year average. With regards to the earnings outlook, the market prices in a 7% EPS contraction for the next 12 months, even though forward EPS estimates have already been revised down by 13% over the past six months. We think the downward revision – which is mostly due to the recent semiconductor downturn - is largely behind us for several reasons. To start with, we are already two quarters into the current semiconductor downturn. We may see the cycle bottom out over the next few months as a typical I.T. recession lasts for 2-3 quarters given its short product cycle. In addition, demand for logic/computing chips – the semiconductor subsector that Taiwanese I.T. companies are mostly exposed to - appears more resilient than other subsectors, such as memory. Indeed, J.P. Morgan expects flat growth in logic device shipments in 2019, compared to a contraction in the whole semiconductor market. All in all, we remain *overweight* Taiwanese equities on the back of sequential economic recovery, conservative earnings growth estimates and undemanding valuations.

Malaysia

Underweight

Growth is likely to moderate in 2019 as exports and investment remain weak. Malaysian equities look expensive given sluggish earnings growth.

Malaysia's Q4 GDP grew by 4.7% yoy, slightly better than expected. On a sequential basis, however, GDP slowed to 1.4% qoq from 1.6% in Q3 against the background of a synchronized global slowdown. Public investment continued to contract while private consumption moderated after a tax holiday.

Economic activity remained sluggish in Q1. Exports weakened to 3.1% yoy in January from 4.8% in December, while industrial production moderated to 3.2% yoy from 3.4% in December. Manufacturing PMI declined further to 47.2 in March, as the downturn in global capex spending continues to weigh on Malaysian manufacturers. Meanwhile, the government is set to embark on fiscal consolidation to maintain its current credit rating. Public spending is forecast to contract by 1.8% in 2019 versus flat growth in 2018. Overall, consensus expects GDP to moderate further to 4.5% in 2019, compared to 4.7% in 2018 and 5.9% in 2017, respectively.

Malaysia is experiencing disinflation amidst tepid activity. Indeed, headline CPI contracted by 0.4% yoy in February while core CPI was just 0.3% yoy. The central bank cut its 2019 inflation forecast to 0.7-1.7% from 2.5-3.5% previously, signalling a benign inflation environment. While domestic disinflation and a more dovish Fed may warrant monetary easing, the Malaysian central bank is likely to stay put for the near term to maintain financial stability. Indeed, a rate cut would risk renewed currency depreciation given large foreign ownership of Malaysian debt. Consensus expects the central bank to remain on hold for the rest of 2019, with only a small chance of a rate cut only in H2.

Market Strategy: The Malaysian ringgit appreciated by 1.3% in Q1 versus the USD as higher oil prices provided support to trade and fiscal balances. The ringgit may remain resilient for the rest of 2019, as the Fed likely keeps its key rate unchanged this year and the interest rate gap between Malaysia and the US stops shrinking.

MSCI Malaysia gained 0.3% in USD terms. The index significantly underperformed EM equities by 9.6% points, as defensive sectors (e.g. utilities, consumer staples and healthcare) constitute a large part of the Malaysian market. The trailing P/E ratio trades at a 56% premium over that of EM, two standard deviations above the long-term average of 26%. Meanwhile, consensus expects EPS to contract again in 2019, the third consecutive year of contraction. Equity valuations look unattractive given the slowing economy, declining company earnings and lack of domestic policy support. We remain *underweight* Malaysian equities.

Indonesia

Overweight (↑)

President Jokowi seems poised for re-election while growth is likely to remain healthy and inflation controlled.

Indonesian GDP expanded by 5.2% yoy in Q4, matching the pace in Q3. Fixed investment growth fell from Q3, whereas household consumption accelerated. Decelerating investment reflects a slowdown in infrastructure-related spending and is set to continue this year as elections in April delay implementation, as other government projects also decelerate. Improving household consumption is expected to compensate for falling investment this year, with consensus projecting GDP growth of 5.1% in 2019 from 5.2% in 2018. Bank Indonesia's (BI) consumer confidence index has fallen this year, but is close to historical highs, while manufacturing PMI is in expansionary territory (51.2 in March).

The rupiah has strengthened by some 7% against the US dollar since October, which is set to exert downward pressure on prices via the import channel in H2. Headline CPI fell to a post-financial crisis low of 2.5% yoy in March, but core price pressures have been slowly rising (3.0% in March, 0.3% point up from a year earlier). Inflation is expected to accelerate to 3.5% yoy this year, the midpoint of BI's 2.5-4.5% target range. BI is likely to keep its key policy rate at 6.0%, where it has been since November, in order to maintain rupiah stability. At the same time, Governor Warjiyo stated at the February meeting that macroprudential policy would be eased in order to support growth.

Meanwhile, the current account deficit is projected to shrink to 2.6% of GDP in 2019, 0.5% point down from 2018. Falling capital goods imports due to slowing infrastructure-related demand are set to support an improved trade balance. The 24% decline in the oil price in rupiah terms since October should also lower import costs. Exports are expected to fall by less than imports as tailwinds from the Chinese stimulus should stabilise external demand in H2.

Presidential and general elections scheduled for 17 April are expected to lead to victory for the incumbent, President Joko Widodo (Jokowi), who maintains a double-digit lead over opposition candidate Prabowo Subianto in opinion polls. Policy continuity should allow for rupiah stability, while fiscal management is expected to remain prudent (the 2019 budget deficit is forecast to match that of 2018 at 1.9% of GDP).

Market Strategy: Valuations are more attractive now than three months ago, with the trailing P/E at a 30% premium over EM and close to its long-term average. This is down from 48% at end-2018 when the premium was over two standard deviations above the long-term average. Given stable economic and political conditions, we raise Indonesia to *overweight*.

Philippines

Overweight (↑)

Economic conditions are set to remain benign this year, allowing the peso to stabilise.

GDP in the Philippines stabilised in Q4, with growth of 6.1% yoy. This followed a deceleration from 7.2% yoy in Q3 2017 to 6.0% in Q3 2018. Government expenditure remained supportive (11.9% yoy), as did net exports. Investment slowed from a double-digit pace in the first three quarters of the year to a still robust 5.5% yoy. This was largely due to a slowdown in equipment investment, whereas construction investment accelerated as the property sector remained strong. Consensus expects growth this year to match that of 2018 (6.2% yoy) due to continued government spending ahead of the May 13 midterm elections and strengthening household consumption amid healthy nominal wage growth (4.8-5.2% yoy in Q1).

Falling inflation should also be growth supportive, with headline CPI decelerating from a post-crisis high of 6.7% yoy in October 2018 to 3.3% in March. Inflationary pressures have decelerated, with core inflation falling from 5.1% yoy in November to 3.9% in February. Both are within the government's 2-4% target range. Moreover, the Rice Industry Modernization Act is set to improve the supply of rice (10% of the CPI basket) and help limit food price inflation. This backdrop suggests that the central bank (BSP) is likely to keep its policy rate unchanged. At the same time, given that M3 growth is at its lowest since 2012 (7.1% yoy in February), BSP is likely to cut the reserve requirement ratio in the coming months to support growth. The Bank has played down the urgency of doing this and may wait until Q3 to ensure inflationary pressures remain controlled.

Meanwhile, the current account deficit is expected to remain wide by historical standards and similar to that in 2018 (2.4% of GDP) after widening from 0.7% in 2017. This is partly due to robust domestic demand, which has pushed up imports, but should ease somewhat this year amid slower project implementation in H1 due to the May elections. Indeed, the 2019 budget had not been approved as at end-March, though a deficit of 3.0% of GDP is projected (vs. 3.2% in 2018). The fall in the oil price since October could also reduce import costs. Overseas foreign worker remittances are also supportive, having recovered from contracting by -0.9% yoy in August to a rise of 4.4% in January. Controlled twin deficits should stabilise the peso after it fell 5.4% against the USD in 2018.

Market Strategy: MSCI Philippines underperformed EM by 2.4% in Q1, while the premium over EM (47%) is below the long-term average (53%). This is better value than at end-2018 (64%). Combined with healthy economic fundamentals, this leads us to upgrade the Philippines to *overweight.*

Thailand

Neutral (↓)

The economy faces numerous headwinds this year, including slowing external demand and political risks.

The first valid general election since 2011, long delayed, was held on March 24. Initial results indicate that the opposition Pheu Thai party (PT), that of exiled former PM Thaksin Shinawatra and the last democratically elected party, won an estimated 130 seats. The incumbent military-backed Palang Pracharat Party (PPRP) won a similar number. At this stage, PPRP appears more likely than PT to secure a majority coalition. This should maintain the status quo, but the situation remains fluid and final results are not due until May. In any case, policy implementation for the next government is likely to become more difficult as the governing coalition is set to have only a slim parliamentary majority.

Thailand's economic growth has continued to accelerate though, rising to 3.7% yoy in Q4 from 3.2% in Q3. This was a broad-based expansion, with growth in household consumption and investment accelerating. Full-year 2018 growth was 4.1%, up marginally from 4.0% in 2017. However, GDP is set to slow this year as the economy faces a number of headwinds ranging from slowing tourist numbers to lower export growth. Consensus projects a 3.8% expansion this year, falling to 3.7% in 2020.

Headline CPI rose by 1.2% yoy in March, just above the lower bound of the Bank of Thailand's (BoT) 1-4% target range, while core CPI moved up by 0.6% yoy. Moreover, the Bank reduced its 2019 core inflation projection in March to 0.8% (headline projected at 1%). However, concerns over financial stability mean the BoT is set to keep a hawkish tilt after raising its key rate by 25bps to 1.75% in December.

Meanwhile, the current account surplus is projected to shrink further, from 7.4% of GDP in 2018 to 6.2% this year as export growth decelerates amid slowing global demand and reduced tourism. The surplus remains substantial and provides a buffer against external shocks. The budget deficit is expected to remain around 3.0% of GDP, not especially high by historical standards and still growth supportive as infrastructure spending, such as build-out of the Eastern Economic Corridor, remains a focus.

Market Strategy: Valuations for the MSCI Thailand are above average (20% premium over EM, up from 16% a year ago and compared to a long-term average of 17%). At the same time, while economic fundamentals remain healthy, downside risks to growth remain. Given heightened political and policy risks, we downgrade Thailand to *neutral.*

India

Underweight

The governing BJP has to contend with a slowing economy and popular discontent about unemployment as it seeks re-election in April/May.

India is gearing up for another round of national elections on April 11, to last until May 19 (results are to be announced on May 23). The Bharatiya Janata Party (BJP) is seeking re-election, but after five years in office, only some of the promised reforms have been implemented and the record on the bigger projects is mixed. The "demonetization" move of 2016 was widely viewed as a disaster that delivered an unnecessary shock to the economy. Other decisions, such as the overhaul of the tax system (introduction of the GST) and the new bankruptcy law are seen as important successes. Yet, more controversial topics such as reform of land rights and labour markets, the privatisation of inefficient state enterprises and the non-performing loan problem of the banking system have so far been eschewed. The BJP's biggest problem remains its economic record. Even though the economy grew by 6.6% yoy in the most recent quarter, job creation continues to lag the number of new entrants into the labour force (0.5 million per month) as Prime Minister Modi failed to deliver on his promise to create 10 million jobs. As a result, the BJP recently lost power in several state elections and its standing in the polls has waned.

But despite being mired in corruption allegations and facing a march by disgruntled farmers on the capital, the BJP has bounced back following a terrorist attack in Kashmir and its subsequent airstrikes on Pakistan. Although the BJP has been able to regain momentum with the electorate, it is unlikely to be able to repeat its stunning victory of 2014 when it secured an outright majority for the party (a first since 1984). While it still remains on track to win a plurality, the next election will likely signify a return to the tradition of a coalition government, reliant on regional parties. Unfortunately, coalition governments, which often encompass extremist parties, are notorious for corruption and the slow pace of reform.

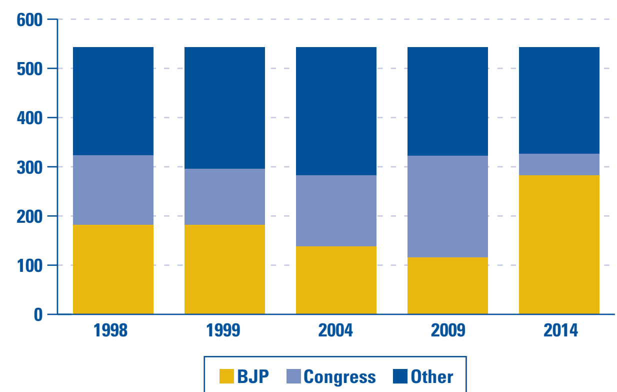
A different political front was opened up by the US recently, which announced that it would terminate preferential access for India (and Turkey) to its markets unless India provides free and fair access of its own markets to the US. The announcement is to take effect 60 days after the notification to Congress. While India has insisted that it would not impose retaliatory tariffs, a deterioration of trade relations could weigh heavily on the economy as the US represents a key export destination (16.5% share of total exports) and is a key strategic ally.

GDP growth slowed to 6.6% yoy in Q4, further extending the deceleration from the downwardly revised 8.0% yoy in Q2 and 7.0% yoy in Q3. Fixed investment remained strong (contradicting other high-frequency data), while consumption slumped, mostly on account of tightened government spending intended to meet budgetary limits. Other indicators, such as PMI remained robust, staying above 52 between last November and the latest March release. Actual industrial production readings remain as uneven as ever, but registered a modest expansion of 1.7% yoy in the latest release for January following an abrupt deceleration in November.

Inflation has been on a downward trend since mid-2018 and while printing marginally above expectations in February, it remains benign and significantly below the RBI's 4% inflation target, at 2.6% yoy. Food prices, which account for 40% of the basket, drove the recent uptick, but have been on a secular downtrend over the past six years. On the other hand, core prices have remained relatively sticky. This creates a dilemma for the RBI policy decisions. Nevertheless, stable oil prices, relative exchange rate stability and the previous monetary tightening together with weakening activity suggest limited inflationary pressures in the near term.

Against this backdrop, the RBI decided to cut the benchmark repo rate by 25bps at the April policy meeting to 6% (after cutting it by 25bps in February). However, the RBI revised its CPI forecast for the second half of the year to 3.5-3.8%, implying a reacceleration in inflation. Therefore, further rate cuts may be limited if any.

Chart 2: India's General Elections*



**Number of seats out of 543-seat lower house.*

Source: Bloomberg

Market Strategy: India underperformed the broader market in Q1, returning 2.8% points less than the MSCI EM. Nevertheless, the Indian market remains one of the most expensive in this space with a P/E of 27, a 104% premium over the market average, equivalent to 2.4 standard deviations above its medium-term average. While the Modi administration has achieved some reform success during its first term in office, it has also blundered and veered toward the authoritarian. The 2019 election outcome will likely see its ambitions more constrained if it has to form a coalition in the absence of a single-party majority (as is expected). This would likely further curtail the reform momentum and open the door to increased corruption. While market participants may prefer BJP rule over that of the disgraced Congress Party, we maintain our *underweight* allocation through the election.

Latin America

Brazil

Underweight

The government submitted the linchpin pension reform but will likely have to endure a long approval process. The economic recovery has continued to disappoint.

The success of the Bolsonaro Presidency (at least in the near term) critically depends on his ability to achieve meaningful reform of the social security system, a prize that has eluded many of his predecessors. While a consensus has emerged both in the wider population and in Congress that reform was necessary, the views on the nuances of such reform differ widely. What is more, Presidents much less confrontational and with much more Congressional support than the 10 seats Bolsonaro's PSL commands have failed to garner sufficient support to pass such significant legislation.

As a result, Bolsonaro's strategy to enter the process with an ambitious reform proposal is understandable, as it is highly likely to be whittled down over the course of the process. The proposed reform is set to generate savings worth BRL1.1trn over 10 years, significantly more than the original proposal by former President Temer, which aimed to save BRL780bn over 10 years and was eventually reduced to BRL466bn (before losing momentum in Congress due to corruption allegations against President Temer and the ensuing erosion of his political capital). As stated previously, most of the savings are to come from changes in the retirement age (62 years for women, 65 for men) as well as the benefit calculation, the minimum contribution period and the transition rule. In addition, the new system is to be applied to public sector workers as well and extend to the military in a separate bill. Observers expect savings from the final bill to amount to just BRL500-700bn and any cutbacks should thus not be market-moving.

However, sending a new constitutional amendment to Congress rather than relying on and amending the earlier Temer proposal ensures that the bill is likely to take a long time to make its way through the legislature. Introduced in this form, it must first be approved by the Constitution and Justice Committee which votes in up to five sessions. Once accepted, a Special Committee is created that will discuss the details of the bill in 11 to 40 sessions. It eventually votes on it and if the bill achieves a simple majority it moves to the Lower House floor, where it needs to obtain approval by 60% of deputies in two separate voting sessions. A similar process then repeats in the Senate (see Table 1) and if any amendment is introduced at this stage, the bill will return to the Lower House, where it restarts the process at the Special Committee level. If the bill fails to gain the required majority at any stage, it is terminated. Consensus currently expects the bill to pass the Lower House by mid-year and to emerge from the Senate in Q3 2019. In light of the cumbersome nature of the process and the high risk of upsets, these expectations are highly ambitious and (market-negative) delays are thus a strong possibility.

Table 1: Brazil Social Security Reform Process

	Sessions	Votes required
Lower House		
CCJ	5	
Special Committee	11-40	
Interval	2	
First vote		60%
Interval	5	
Second vote		60%
Senate		
Senate CCJ	max. 30 days	
Interval	min. 5 days	
First vote		60%
Interval	min. 5 days	
Second vote		60%
Presidential sanction (if no changes)		

Source: J.P. Morgan

One potential hiccup on the path towards approval could be the recent arrest of former President Temer on corruption charges, together with former Energy Minister Moreira Franco. Their party could interpret the move as vindictiveness and refuse cooperation on the reform. What is more, Bolsonaro's approval rating has recently plunged to 34% from 49% in January.

Similarly, economic activity data have not kept pace with the lofty expectations that emerged following Bolsonaro's election. GDP growth decelerated after a bump in Q3 and recorded mere 1.1% yoy gain in Q4, compared to 1.3% the previous quarter. Although PMI has risen from 47.3 in September to 52.6 by February, actual industrial production has declined for three consecutive months, most recently by 2.6% yoy in January. Unemployment ticked up slightly to 12.3% as well.

Inflation has stabilized below 4% after a slight rise from mid-2018 and thus remains well within the central bank's target range (mid-point 4.25%). Economic slack, well-behaved inflation expectations and relative exchange rate stability imply limited inflationary pressures for now. Upside risks include the effects of increased wholesale petrol prices, rising food prices and exchange rate instability if the pension reform bill encounters hiccups in Congress. Unsurprisingly, the central bank has thus left the Selic rate unchanged at 6.50% since March 2018 after a series of cuts. It expects inflation at 4.1% by year-end 2019 and recently turned more dovish at its March meeting, suggesting that the outlook had become more balanced. Barring any external or domestic shocks, rates are thus expected to remain on hold through the year.

Market Strategy: The absence of the eagerly awaited 'Bolsonaro Bounce' in Brazil's economy comes as a disappointment to investors who had hoped that the clearing of uncertainty after the election could bring Chile-style policy efficiency to Brazil. However, Bolsonaro's party has only a very small representation in Congress and his dealmaking ability is limited, partly as a matter of choice. Like most markets in EM, Brazil underperformed during Q1, lagging MSCI EM by 1.8% points. With an anaemic economic recovery and likely delays in pension approval, we maintain our *underweight* allocation.

Mexico

Overweight

President AMLO continues to tread a fine line between his populist instincts and more orthodox policies. But investors remain overly skeptical.

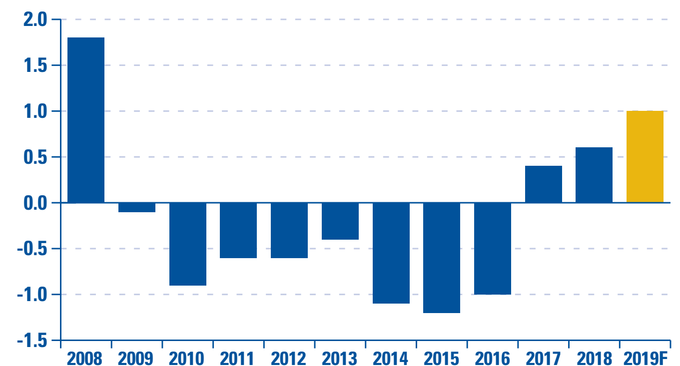
Mexico's new President continues to tread a fine line between his populist instincts and more conventional, orthodox policy moves. The former category includes AMLO's recent decision to go ahead with the tender for building the new Dos Bocas oil refinery for Pemex. Indeed, the 2019 budget allocated $2.5 bn for the refinery, which is to wean Mexico off its dependence on foreign (refined) oil imports (as it mostly extracts heavier grade crude). The total cost of construction is estimated at $6-8 bn.

Pemex certainly is in need of help. As part of the austerity drive by the Pena Nieto administration, it has been subject to chronic underinvestment, mounting losses and a fall in production capacity to half the level of 2004. It is now weighed down by a debt burden of $106 bn plus $66 bn of pension liabilities. While the previous administration was content to see Pemex shrink as it expected the sector to be liberalized and opened up to private enterprise, AMLO has put Pemex back at the centre of his energy policy. Accordingly, the government has budgeted a bail-out package worth $5.5 bn, of which $1.3 bn consists of direct recapitalization and some is tax relief. However, rating agencies fear that additional government support will be required and have downgraded Pemex to their lowest investment grade rating. What is more, most analysts agree that it would be more cost-efficient to refine Mexico's crude in Texas rather than build another local facility.

While Pemex, public pension liabilities and general under-investment represent important long-term challenges for Mexico's fiscal management, the government remains committed to the consolidation course set out by the previous administration. Under President Pena Nieto, the government vigorously cut (capex) spending, increased tax collection and broadened the tax base (reducing the share of oil revenues from 40% to 20%). By 2017, it had turned primary deficits into a surplus and the public debt had declined from a peak of 50% of GDP in 2016 to 44.8% of GDP in 2018. The recent budget aims to boost the primary surplus to 1% of GDP, thus keeping debt in check, and significantly scaled back the various social programs promised by AMLO during his campaign. What is more, many projects involve private sector partnerships, limiting the budgetary impact.

Meanwhile, sluggish activity could complicate the fiscal effort. GDP growth slowed to a mere 1.7% yoy in Q4, from 2.5% yoy the quarter before, bringing annual growth for 2018 to 2%. The slowdown in the US, as well as domestic developments such as fuel shortages and blockades of railways, will likely keep a lid on growth in 2019. Indeed, the Banco de Mexico revised the outlook for growth this year from 2.2% to 1.6% in its February Inflation Report. Recent indicators have witnessed manufacturing PMI fall back to 49.8 in March after a temporary surge to 52.6 in February. Actual industrial production continues to decline, even if the contraction eased to -0.9% yoy in January from -2.5% yoy in December. Manufacturing grew a modest 1.3% yoy, benefitting from a recovery in construction following the contraction in the wake of the airport project cancellation whereas the oil sector remained in free-fall with an 18.3% yoy decline.

Chart 3: Public Sector Primary Balance, % of GDP



F - forecast.

Source: J.P. Morgan

Inflation has been on a downward trend since reaching a peak of 6.8% yoy in December 2017, but at 3.9% yoy in February it remains some distance from Banxico's 3% target. What is more, the central bank is becoming concerned that persistently high core inflation and rising inflation expectations could complicate attainment of the target. It expects headline and core inflation to reach its target only by mid-2020, at current interest rates. After raising rates twice in 2018, the Board left them unchanged at 8.25% in February. With growth slowing, the US raising rates but Mexican inflation proving sticky, Banxico faces a difficult decision. Nevertheless, consensus expects it to start cutting rates by mid-year.

Market Strategy: Mexico underperformed the broader market by 4.4% points during Q1 and is now one of the cheapest markets in the EM space with a P/E premium of just 31%, compared to a medium-term average of 55%. AMLO continues to cultivate a confrontational style with the private sector and has proceeded with some decisions that conflict with standard economic arguments (airport cancellation, revision of gas pipeline contracts, oil refinery decision, etc.). Nevertheless, markets are overly skeptical of the overall outlook as the government still targets a primary surplus for 2019, even if the actual outcome could be less than the 1% of GDP projected in December. Bond markets too are wary and already price in a one/two-notch downgrade in Mexico's credit rating. As a result, we believe that most of the negative news has been priced in and the market offers upside. We maintain our *overweight* allocation.

Emerging Europe and Africa

Russia

Overweight

The global environment becomes more adverse for Russia's economy, which is set to slow again in 2019, prompting the central bank to turn more 'dovish'.

Russia faces a series of headwinds but has so far weathered them well. In particular, the fiscal and current account positions are the best in a decade as both record a sizeable surplus. However, this also reflects the weakening of domestic demand over the course of the past year. The level and volatility of oil prices, geopolitical tensions and a strained relationship with the US, as well as the increase in the VAT rate from 2% to 20% from January 2019, are set to weigh on overall growth this year. Indeed, retail sales remain sluggish despite picking up from 1.6% to 2.0% yoy in February while wage growth slows. By contrast, Russia's Manufacturing PMI has picked up further to 52.8 and industrial production has also surprised to the upside, in particular in February when it accelerated to 4.1% yoy. Nevertheless, consensus expects growth to slow from an estimated 2.3% in 2018 to 1.5% in 2019.

Inflation has been on an upward trajectory since mid-2018 and peaked at 5.2% yoy in February, after rising successively from 2.3% yoy in June of last year. Nevertheless, the acceleration was less pronounced than feared and with a likely moderation of food prices and the effect of the VAT increase fading, the outlook is more sanguine than recent history suggests.

Indeed, inflation has remained significantly below the central bank's forecast and could well undershoot its year-end expectation of 5.0-5.5%. Accordingly, the central bank has not only left its policy rate unchanged at 7.75% in its latest meeting (after hiking in September and December by 25bps respectively), but also turned more dovish in its rhetoric, removing a reference to potential hikes. Instead, it moved the expected timing of rate cuts from "late 2019/early 2020" to simply "2019." This represents a material change and may be indicative of the bank's concern about the domestic economic outlook.

Market Strategy: Russia was the only market other than China to outperform the EM index in Q1, gaining 2.3% points more than the MSCI EM. Nevertheless, it remains cheap with its 5.1 P/E. The outlook remains dominated by weak growth, which faces additional headwinds due to the VAT hike as well as ever-present geopolitical tensions. Nevertheless, the market represents a good diversifier in the portfolio due to its oil exposure. We retain our *overweight* allocation.

Turkey

Underweight

Financial instability remains, and the effects of last year's crisis are increasingly being felt in the real economy.

The economic fallout from last year's crisis that followed President Erdogan's contested re-election is becoming ever clearer. Indeed, after a boost to exchange rate volatility and inflation readings, the impact of the shock to confidence and the reversal in capital to Turkey is now most visible in activity readings. GDP growth in Q4 2018 declined by 3.0% yoy as private consumption and investment collapsed by 8.9% and 12.9% yoy respectively. Only net trade cushioned the blow somewhat, contributing to full-year growth of 2.6% in 2018, compared to 7.4% the prior year. Q4 may have represented the bottom of the downturn as more recent indicators such as economic confidence and manufacturing PMI have already picked up. However, industrial production contracted another 7.3% yoy in January and still-depressed loan growth will likely keep any recovery of private consumption in check. Consensus expects a slight contraction for the full year.

The exchange rate came under renewed depreciation pressure this year, losing 6% against the USD. This followed a 23% appreciation from its August low to the end of 2018. Indeed, the weakening of the lira might have been more dramatic had it not been for what appears outright market intervention by the central bank (CBRT), which witnessed a decline of foreign reserves by over $6 bn in March after they had been rebuilt since last October. The previous accumulation reflected the narrowing external deficit which in turn owed to depressed domestic demand.

In tandem with the sell-off in the exchange rate, CPI rose to a peak of 25.2% yoy in October and subsequently moderated to 19.7% yoy as of March. In addition to relative lira stability, low domestic demand and a series of tax cuts introduced by the government helped keep inflationary pressures at bay. Despite changes at its helm, the central bank has resisted government pressure to lower interest rates, keeping the one-week repo rate unchanged at 24.0%. If inflation declines further (e.g. mid-2019), the CBRT can be expected to cut rates decisively (500bps or more in 2019) in order to keep real rates from rising too fast and impairing investment activity further.

Market Strategy: Turkey has taken no steps towards eliminating the distortions that increasingly dominate its policy mix and, in addition to facing an economic contraction, has witnessed renewed pressure on its currency. This has forced the central bank to (unsuccessfully) intervene in the market. What is more, President Erdogan suffered a string of setbacks in local elections, which could yet prompt a populist tilt in policymaking. With no change of course in sight, we remain *underweight*, despite Turkey's cheap valuation metrics.

Romania

Neutral

Economic uncertainty is rising at a time of slowing growth and ongoing inflationary pressures.

Economic growth in Romania has continued to expand healthily, rising by 4.1% yoy in Q4 compared to 4.2% in Q3. An acceleration in household consumption from 4.0% yoy to 5.8% compensated for a deceleration in government consumption. GDP growth is expected to decelerate to 3.2% this year from 4.1% in 2018 as the impact of the 'greed tax' and slowing growth in key export markets in the Eurozone weigh on activity.

Inflation, after briefly falling within the central bank's (NBR) 1.5-3.5% target range from November through January, rose to 3.8% yoy in February. Core prices also rose to 2.7%, the highest in almost five years. Real wages continue to grow at close to double-digit rates, which should boost growth and keep upward pressure on consumer prices. However, the NBR has left its key policy rate at 2.5% since the last hike in May 2018.

Fiscal policy remains expansionary and poses an upside risk to inflation, but is also a key source of uncertainty that will potentially weigh on economic activity. The 2019 budget was approved by parliament in February, with a targeted 2.8% of GDP deficit against 2.9% in 2018. However, this may be unrealistic since it is based on GDP growth of 5.5%. The government also watered down its so-called "greed tax" on banks (down from 1.2% to 0.4% and on only 20% of assets), which means tax revenues from this source are less likely to compensate for rising expenditure. Backing down on this issue allowed the government to avoid a credit rating downgrade. S&P decided in March to affirm the 'stable' outlook on the country's BBB- rating.

Meanwhile, the current account deficit widened by 1.4% points to 4.6% of GDP last year. This was largely due to a deterioration in the trade balance as imports rose by more than exports amid robust domestic demand. The pattern is likely to repeat to some extent this year, with a marginal widening to 4.7% of forecast GDP. A longer-term concern is the funding of the shortfall, with FDI covering around half of this in 2018 compared to 82% in 2017. The watering down of the "greed tax" could prevent FDI from falling further, but widening twin deficits remain a downside risk for the leu.

Market Strategy: The valuations for MSCI Romania remain unchallenging, with the trailing P/E at a 45% discount to EM compared to a long-term average of 19%. This is counterbalanced by an uncertain economic outlook, political risk given the presidential election in Q4 and downside currency risk. We therefore stay *neutral*.

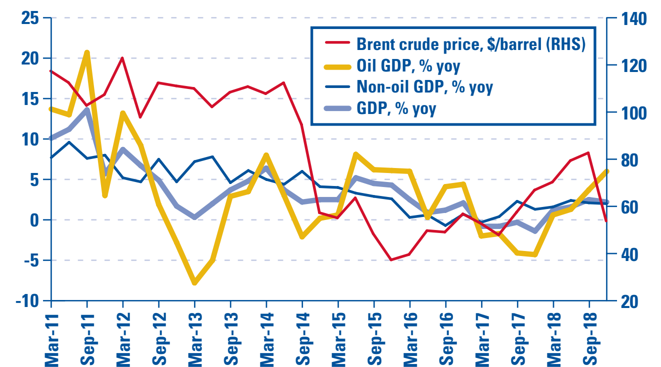
Saudi Arabia

Neutral

Stable economic fundamentals belie an economy undergoing substantial changes.

Saudi Arabia's economic backdrop improved last year, with GDP recovering from a 0.7% yoy contraction in 2017 to a 2.2% expansion in 2018. The fall in 2017 was driven both by lower oil production and government austerity measures, while the recovery in 2018 was aided by a partial reversal of these factors. A growth rate around the 2018 level is expected for this year and next. The economy remains highly dependent on the oil sector, with petroleum accounting for 42% of GDP, 68% of budget revenues and 90% of export earnings, while the state plays a big role in the economy, with government expenditure accounting for around one third of GDP. As a result, the key determinants of growth are the oil price and fiscal policy.

Chart 4: Oil Price and GDP



Source: General Authority for Statistics Kingdom of Saudi Arabia, Bloomberg

Saudi Vision 2030 aims to change this over the medium term. The program, launched in 2016, aims include diversifying the economy, developing public services and increasing the role of the private sector and foreign investment. An investment program led by the Public Investment Fund (PIF), the sovereign wealth fund, is likely to support growth in the medium term. The $500 bn Neom economic zone broke ground in Q1 and is set to include wind and solar energy projects. Reforming Saudi Arabia, both economically and socially, appears to be a key goal of Crown Prince Mohammed bin Salman, the heir to King Salman and the de facto ruler.

The program also includes so-called 'Saudization', which aims to raise the employment of Saudi nationals. This is beginning to have an impact. Hiring of Saudi nationals doubled in 2018, according to a survey by recruitment specialist Robert Walters. This is in line with companies meeting requirements to raise the proportion of nationals in the workforce. The government is targeting a

reduction in the unemployment rate from 12.8% in Q3 2018 to 9.0% in 2020. This target is ambitious, but policy implementation means that the trajectory is likely downwards. The expected rise in employment should help boost household consumption.

The inflationary backdrop has been mixed, with the 5% value-added-tax introduced in January 2018 pushing the cost of living index up to 3.0% yoy in that month. This led to an average monthly rise of 2.5% last year, up from -0.8% in 2017. Deflation has returned this year (-2.2% yoy in February) due to the base effects of the VAT rise. Potential additional cuts in fuel price subsidies provide upside risks to inflation, but any rise is expected to be gradual. Monetary policy is conducted by the Saudi Arabian Monetary Authority, a government agency. Its aim is to "maintain monetary and financial stability", with a number of targets including money growth.

The 2019 budget was announced in December, with the rise in revenues (9% yoy) projected to outpace that of spending (7%). This is set to reduce the budget deficit to 4.2% of GDP from 4.6% in 2018. The oil price assumption is not disclosed, but is estimated to be around current levels ($65-70/barrel). Spending is set to be driven by a 20% yoy rise in capital expenditure. However, project awards will need to improve to meet these goals. Capex was down 1% yoy in 2018 and project awards were unchanged from 2017 despite ambitious spending plans. The expected narrowing of the budget deficit is likely to keep growth stable absent a large change in the oil price. An oil price of $83 is required to balance the budget and with the government's increasingly fiscally conservative stance, aiming to eliminate the budget deficit by 2023, additional revenue from rising oil prices would not necessarily be spent. Thus, growth risks appear to be biased to the downside.

Saudi Arabia's economy is fairly open, with imports and exports accounting for over 60% of GDP, similar to that of the UK, France and Spain. Despite its exposure to movements in the oil price, it has substantial buffers to defend the exchange rate and maintain financial stability. It has a large current account surplus (estimated to be around 8.0% of GDP this year) and substantial sovereign wealth fund assets (120% of GDP), both of which help to dampen external shocks. This enables the authorities to maintain the exchange rate peg at 3.75 Saudi riyal per US dollar, maintained since 1986.

Market Strategy: The upgrade of Saudi Arabia to EM status by MSCI and FTSE has led to increased flows into the market, with the market up by 20.5% in the year to end-March, outperforming EM by 27.9%. However, valuations may leave investors cautious, with the MSCI Saudi Arabia's trailing P/E at a 34% premium to EM compared to a five-year average of 11%. An above-average valuation in the year leading up to an upgrade to EM has been typical, before falling away after inclusion (e.g. Qatar, UAE, Pakistan). We believe downside risks are counterbalanced by some attractive metrics, diversification benefits and healthy economic fundamentals. On balance, we therefore regard a *neutral* weight within an EM portfolio as appropriate.

South Africa

Underweight

Growth risks remain to the downside amid ongoing electricity supply issues and an upcoming election.

South African GDP expanded by 1.1% yoy in Q4, recovering from a two-year low of 0.1% in Q2. A recovery in agricultural output and a healthy services sector have been key drivers. This year's prospects are lacklustre though, with the manufacturing PMI in contractionary territory (below 50) in January and February and falling consumer confidence. GDP growth is forecast to accelerate from 0.8% in 2018 to 1.5% this year, but this is still below the potential rate of 2% estimated by the South African Reserve Bank. (SARB). Growth risks are biased to the downside given ongoing energy issues (60% of installed capacity was available to meet demand in March, down 10% points yoy).

Headline inflation has fallen by over 1% point, from 5.2% yoy in November to 4.1% in February, driven by a sharp fall in fuel prices. However, this is set to reverse this year amid a recovery in the oil price. Core inflation was also stable at 4.4%, suggesting that inflationary pressures remain. This is likely to keep the SARB hawkish, while the Bank will also be cognizant that recent rand weakness may push up inflation. Headline inflation is expected to be within the SARB's 3-6% target range this year and the key rate unchanged at 6.75%.

The 2019 budget was announced in February and a key element was conditional, rather than unconditional, support for public electricity company Eskom over the next few years. This support is counterbalanced by cuts in the public sector wage bill and additional taxes. The result is a projected widening of the budget deficit from 4.3% of GDP in 2018/19 (year to end-March 2019) to 4.7% in 2019/20 and down to 4.5% in 2020/21. Downside growth risk pose upside risks to both deficit borrowing projections.

Political risks are likely to be in focus in Q2, with the general election scheduled for May 8. Opinion polls suggest that the ruling Africa National Congress (ANC) have 55-60% support, a 30-40% point lead over the opposition Democratic Alliance. If the ANC gains this support in the election, President Cyril Ramaphosa would be better positioned to push through reforms. Meanwhile, the current account deficit is projected to remain close to 3.7% of GDP, as in 2018. Funding the shortfall in the medium-term could become less of an issue if Ramaphosa is able to implement structural reforms.

Market Strategy: The MSCI South Africa's P/E premium over EM is now is line with the long-term average of 38%. This is more reasonable than six months ago when the premium was two standard deviations above the average. However, we do not view this as sufficient compensation for downside growth and political risks, so we stay *underweight*.

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KEY ECONOMIC AND FINANCIAL INDICATORS

	Emerging Market	Macroeconomic Data: % change on year ago: Annual GDP Growth*	Industrial Production*	Consumer Price Index*	Latest 12 months: Trade Balance*	Current Account Balance*	Foreign Reserves 2019 Latest*	Foreign Reserves 2018 Year ago	Currency vs $ 2019 Latest*	Currency vs $ 2018 Year ago	Short-Term Interest Rates*	Sovereign Rating S&P*	Market Data: Performance: % S&P/EM Frontier Super Composite BMI	Stock Market Index S&P/EM Front. Super Comp. BMI US$	Change since 12/31/18 US$	Change since 12/31/18 Local Currency	Forecast (Bloomberg)†: 2019 P/E Forecast*	EBIT Margin 2019 Forecast*	6 month Stock Market Index Estimate (Front Super Comp. BMI) US$*	3 month Currency vs $ +/-*
		%	%	%	$ Bns	$ Bns	$ Bns	$ Bns			%		Mar. 29, 2019	Mar. 29, 2019	%	%		%		
Overweight	MEXICO	1.7	-0.9	3.9	-13.8	-26.5	169.39	166.90	19.18	18.20	8.5	BBB+	2.33	398.95	6.65	5.06	13.7	15.7	406	-
Overweight	PHILIPPINES	6.1	-4.1	3.8	-42.0	-7.9	72.41	71.06	52.09	52.05	5.1	BBB	1.13	861.02	7.41	7.26	17.1	22.6	890	-
Overweight	INDONESIA	5.2	5.2	2.5	-8.4	-31.1	114.10	125.72	14176.00	13763.00	6.3	BBB-	2.07	1482.07	4.93	3.92	15.3	25.8	1527	+
Overweight	RUSSIA	2.7	4.1	5.2	0.2	113.8	376.60	357.56	65.16	57.65	7.9	BBB-	3.39	508.41	12.61	7.69	5.8	17.5	520	-
Overweight	TAIWAN	1.8	-1.8	0.2	49.4	68.3	464.08	457.19	30.81	29.15	0.7	AA-	11.02	277.63	9.89	10.19	15.4	6.8	283	+
Neutral	ARGENTINA	-6.2	-13.3	51.3	-1.2	-28.0	61.41	56.32	42.72	20.18	42.3	B	0.58	596.05	28.80	48.46	10.7	21.2	554	-
Neutral	BAHRAIN	4.6	n.a.	0.9	n.a.	n.a.	1.80	1.99	0.38	0.38	3.6	B+	0.11	159.32	15.10	15.13	n.a.	n.a.	164	uc
Neutral	CHILE	3.6	-3.6	1.8	3.6	-9.2	37.77	37.65	666.80	603.38	2.9	A+	0.97	503.87	4.66	2.62	15.6	14.9	509	+
Neutral	CHINA	6.4	5.7	1.5	339.2	49.1	3090.18	3134.48	6.71	6.30	1.1	A+	27.69	883.80	16.74	16.97	12.3	12.3	907	+
Neutral	COLOMBIA	2.9	-0.8	3.0	-8.0	-12.7	47.82	45.20	3128.56	2780.25	4.3	BBB-	0.48	6205.97	23.87	21.50	12.1	22.9	6374	+
Neutral	CZECH REP.	2.6	-1.1	2.7	18.2	0.4	142.45	150.58	22.88	20.65	1.9	AA-	0.13	928.62	3.66	5.92	13.6	n.a.	967	+
Neutral	EGYPT	5.3	1.6	14.4	-43.5	-6.0	39.06	37.41	17.33	17.60	15.8	B	0.20	1616.73	19.27	15.67	10.6	n.a.	1766	-
Neutral	GREECE	1.6	3.4	0.6	-25.2	-6.9	1.83	2.38	1.12	1.23	0.1	B+	0.32	26.83	13.74	15.58	14.9	12.0	27	+
Neutral	HUNGARY	5.1	5.0	3.1	6.4	0.8	28.82	28.57	284.78	254.21	0.1	BBB	0.27	584.34	5.84	8.03	10.1	n.a.	600	+
Neutral	KENYA	6.0	n.a.	4.4	-11.4	-45.9	8.55	7.54	100.70	101.10	7.4	B+	0.12	738.89	15.12	13.87	9.5	23.7	775	-
Neutral	KUWAIT	-3.5	n.a.	0.6	57.2	-4.9	35.27	32.57	0.30	0.30	1.5	AA	0.74	94.01	10.69	10.86	8.3	n.a.	97	+
Neutral	MOROCCO	2.9	-6.1	0.0	-21.9	-5.6	22.21	23.65	9.65	9.23	3.0	BBB-	0.20	550.73	-5.36	-4.47	16.9	25.8	561	-
Neutral	NIGERIA	2.4	n.a.	11.3	16.4	5.3	40.42	38.97	360.25	360.10	10.3	B	0.18	171.00	1.01	0.31	6.0	n.a.	182	-
Neutral	PAKISTAN	5.4	-10.2	9.4	-35.2	-15.2	9.55	13.51	141.37	115.72	7.8	B-	0.13	582.96	4.22	5.68	7.5	n.a.	611	-
Neutral	PERU	4.8	8.2	2.3	6.6	-3.3	57.79	61.46	3.30	3.23	0.3	BBB+	0.38	2255.98	10.59	10.46	15.1	n.a.	2307	-
Neutral	POLAND	4.9	6.9	1.7	-5.4	-3.9	106.91	112.11	3.82	3.42	1.6	A-	1.03	340.27	0.61	2.66	11.9	15.1	350	+
Neutral	QATAR	0.3	n.a.	-1.4	46.9	14.1	28.38	16.15	3.66	3.66	2.7	AA-	0.81	276.26	-1.03	-1.04	12.6	n.a.	288	uc
Neutral	ROMANIA	4.1	0.8	3.8	-18.2	-61.7	35.67	41.58	4.23	3.80	3.3	BBB-	0.11	116.83	4.70	9.44	9.2	27.6	119	+
Neutral	SAUDI ARABIA	3.6	n.a.	-2.2	87.3	18.5	479.72	484.36	3.75	3.75	2.7	A-	1.26	144.09	13.27	13.25	14.7	n.a.	146	uc
Neutral	SOUTH KOREA	3.1	-2.7	0.4	66.3	76.5	394.32	384.95	1134.92	1055.98	1.9	AA	13.49	490.58	4.33	6.13	10.8	9.5	497	+
Neutral	SRI LANKA	1.8	4.3	4.3	-10.3	n.a.	7.75	6.69	174.70	155.80	11.0	B	0.05	208.07	-5.89	-9.71	13.6	10.5	214	-
Neutral	THAILAND	3.7	-1.6	1.2	21.8	33.2	203.82	204.11	31.75	31.21	2.5	BBB+	2.49	1283.37	9.68	6.95	14.9	11.5	1328	-
Neutral	UAE	0.8	n.a.	1.1	80.9	27.5	97.44	92.21	3.67	3.67	2.6	AA	0.60	125.41	7.20	7.19	9.5	n.a.	129	uc
Neutral	VIETNAM	6.8	9.1	2.7	-1.1	12.5	56.32	38.11	23190.00	22795.00	4.7	BB-	0.47	226.33	10.92	10.97	19.0	18.7	238	-
Underweight	SOUTH AFRICA	1.1	0.3	4.1	2.4	-52.2	42.58	41.93	14.14	11.81	6.7	BB	5.31	701.02	3.96	4.16	15.1	15.2	709	-
Underweight	BRAZIL	1.1	2.0	3.9	58.7	-13.9	368.93	367.99	3.85	3.32	4.8	BB-	6.83	766.38	8.80	9.22	11.7	20.7	770	+
Underweight	INDIA	6.6	1.7	2.6	-179.2	-64.9	374.64	395.84	68.51	65.01	6.3	BBB-	11.27	1116.48	6.74	5.92	22.4	12.8	1172	-
Underweight	MALAYSIA	4.7	3.2	-0.4	30.3	8.4	98.75	100.18	4.08	3.87	3.2	A-	2.18	382.64	2.63	1.39	16.4	19.9	397	-
Underweight	TURKEY	3.1	-7.3	19.7	-44.8	-21.6	77.58	87.86	5.62	3.99	29.0	B+	0.63	255.34	-2.22	3.84	6.3	12.0	241	-

Note: All data shown are as at 29 March 2019 unless stated otherwise. UC is unchanged (currency versus US dollar). S&P sovereign rating shown is long-term foreign currency rating. UAE sovereign rating shown is for Abu Dhabi. Data for countries in the Middle East and North Africa region are the latest available, but in certain cases relate to periods more than one year ago. The 34 countries shown in the table accounted for 99.0% of the S&P/EM Frontier Super Composite BMI on 29 March 2019. An additional 22 countries accounted for the remaining 1.0% of the index on the same date. These countries, which can be accessed via City of London's Frontier Markets strategy, are: Bangladesh, Botswana, Bulgaria, Cote d'Ivoire, Croatia, Cyprus, Ecuador, Estonia, Ghana, Jamaica, Kazakhstan, Latvia, Lebanon, Lithuania, Mauritius, Namibia, Panama, Slovakia, Trinidad & Tobago, Tunisia, Ukraine and Zambia.

†Any forecasts are based on Bloomberg consensus forecasts, where available, and assumptions. Actual results may vary from any such statements or forecasts. Past performance is no guarantee of future results.

**Key Criteria*

Source: Bloomberg, City of London Investment Management

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