CITY OF LONDON
Investment Management Company Limited

Frontier Markets Semi-Annual Outlook

August 2022*

Overview

In the Shadow of the War

With commodity markets upended by the Russo-Ukrainian war, rising inflation and tighter monetary policy have followed. The prospect of a synchronised slowdown points to softer growth in frontier markets (FM), where the post-pandemic recovery is still in its early stages. Dwindling foreign reserves mean that some FM are particularly vulnerable to a debt crisis.

Just as the post-pandemic recovery got underway, frontier markets (FM) have been hit by a surge in commodity prices in the wake of Russia's invasion of Ukraine in late-February. The pandemic had already left scars in many frontier markets due to their limited fiscal space to offset the economic hit. But with higher raw materials prices pushing up inflation across the world, developed markets (DM) have initiated an aggressive tightening cycle. This is likely to put pressure on central banks in other parts of the world to keep up, with higher rates dampening domestic demand.

Meanwhile, tighter global financial conditions are set to put pressure on FM reserves, which are already strained in food and energy importing nations. Additionally, due to the small and open nature of their economies, frontier markets are particularly exposed to the likely DM slowdown. All told, FM economies face significant headwinds.

While sharing many of the same challenges facing emerging markets (EM), FM are vulnerable in additional ways. For a start, low-income economies are less likely to borrow in domestic currency, which leaves them exposed to a stronger US dollar. For example, the IMF recently noted that 60% of low-income countries were in or at high risk of debt distress. Secondly, dependence on food imports and strained external balances mean that many FM are at risk of experiencing a food crisis, which could trigger social upheaval.

The flipside is that commodity exporters (Kazakhstan and Nigeria), countries with ample reserves (Morocco and Romania) and those in a strong fiscal position (Vietnam) face the best prospects.

Market Strategy

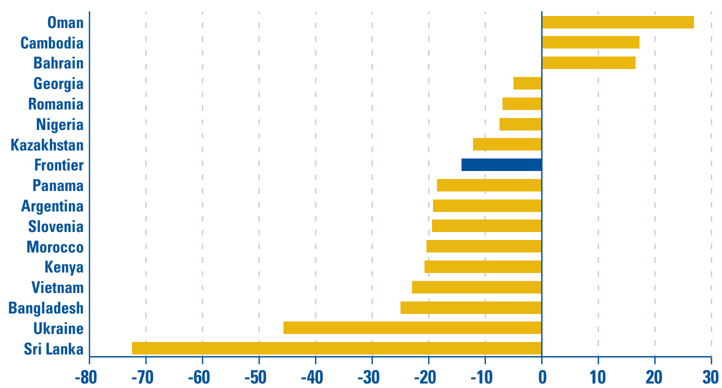
FM equities, as measured by the MSCI FM 100 Net TR Index, continued to slightly outperform EM equities (MSCI EM Net TR Index) over the past six months. Nonetheless, both trailed DM equities (MSCI World Net TR Index) over the same period.

Some valuation metrics for FM equities have improved. The discount of the 12M forward P/E of FM to EM has widened from 5% at the end of January to 11%, higher than its five-year average of 6%. On balance, considering that EPS for FM is expected to grow by 4.7% this year, much higher than the 4% contraction projected in EM, there is upside potential.

Bearing in mind each country's exposure to the various global headwinds, as well as equity valuations, we make only one change to our allocation:

- **Upgrade Kazakhstan to *overweight*.** With the economic fallout from the Russo-Ukrainian war offset by higher oil prices, Kazakhstan's economy appears to be performing better than initially feared. Against this relatively strong economic backdrop, valuations are attractive.
- To counterbalance the upgrade, we increase the *underweight* allocation in **Argentina** and reduce the *overweight* in **Slovenia**.

Chart 1: S&P Extended Frontier 150 Net Total Returns USD, Feb-Jul 2022, %



Source: S&P

Allocation Breakdown

	Chg	-2	-1	0	+1	+2
Latin America						
Argentina	-	■				
Middle East and North Africa						
Morocco	-			■		
Sub-Saharan Africa						
Nigeria	-		■			
Kenya	-		■			
Asia						
Vietnam	-					■
Bangladesh	-			■		
Kazakhstan	↑				■	
Europe						
Romania	-				■	
Slovenia	-				■	

Note: Up/down arrows indicate a positive/negative change in our asset allocation compared to the previous quarter. A dash indicates no change.

Source: City of London Investment Management

**The publication reflects asset performance up to 29 July, 2022, and macro events and data releases up to 11 August, 2022, unless indicated otherwise.*

Latin America

Argentina

Underweight

Macro imbalances and economic mismanagement weigh on Argentina's fortunes in the medium term.

	3Y history	Latest	
GDP, % yoy		6.0	Q1
CPI, % yoy		71.0	Jul
Policy rate, %		60.00	Jul
MSCI Argentina*		3.6%	Jul
EPS, % yoy		-17582.3	Jul
Trailing P/E		2.9	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

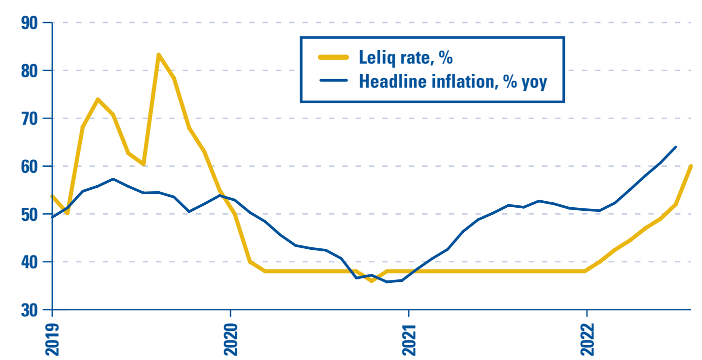
In contrast to its regional peers, the surge in commodity prices in the wake of the Russo-Ukrainian war has been of limited benefit to Argentina. As the world's sixth largest exporter of wheat, Argentina seemed primed to profit from the increase in wheat prices. Yet, a drought has meant that the country is facing its worst wheat planting conditions in 12 years. Moreover, high fertiliser prices and a government wheat export cap meant to rein in domestic inflation has created uncertainty. In addition, while home to the second largest shale gas reserve in the world, Vaca Muerta, government mismanagement and insufficient infrastructure mean that Argentina will miss out on the benefits of a changing energy landscape.

Looking ahead, Argentina's economic outlook is fragile, as consensus expects GDP growth to slow sharply from 10.4% in 2021 to 2.8% this year. The IMF recently approved the first review of Argentina's program, disbursing $4bn. The IMF program targets for this year are three-fold: reducing the primary fiscal deficit to 2.5% of GDP; limiting monetary financing to no more than 1% of GDP; increasing net international reserves by $5.8bn. None of these targets are likely to be met. For a start, elevated energy prices mean politically-sensitive social spending is unlikely to be cut, particularly as 40% of Argentinians have recently seen their incomes fall below the poverty line. This raises the risk of higher monetary issuance to meet fiscal needs. And accumulating net reserves is likely to be achieved by adopting tighter import restrictions, which could come at the expense of economic activity and inflationary pressures.

Highlighting the challenges faced by the economy, the recent measures unveiled by the new Economy Minister Sergio Massa were thin on details aside from a pledge to stop further monetary financing. Any real progress in meeting the IMF's targets could be hamstrung by ongoing political infighting, particularly leading up to next year's elections. In the space of a month, Argentina has had three Economy Ministers, which has done little to assuage market fears. Indeed, the spread between the official and parallel exchange rate remains high at 110%, while dollar bonds due in 2030 are trading at 24 cents on the dollar.

Meanwhile, inflation continues to accelerate, with the latest print showing that prices rose by 71% yoy in July. With inflation expectations unanchored and import controls in place, consensus projects inflation to trend higher, averaging 68.9% in H2. As such, following 22% worth of rate hikes since January, the BCRA is expected to continue tightening policy (see Chart 2). But the lack of fiscal consolidation plans means that sustainable disinflation is unlikely.

Chart 2: Argentina Policy Rate and Headline Inflation



Source: Bloomberg

Market Strategy: The 12M forward P/E for the Merval Index is trading at a 67% discount to FM, lower than the five-year average of 24%, but similar to its discount six months ago. But valuations for Mercado-Libre, which makes up 78% of the MSCI All Argentina Index, are still stretched despite the 20% year-to-date decline in price. The 12M forward P/E of the stock is trading at around 100x, while the EPS estimate has risen by 24% since the start of the year. Tighter global financial conditions are a headwind to such growth stocks. Additionally, a synchronised slowdown and the removal of most mobility restrictions does not bode well for e-commerce sales growth.

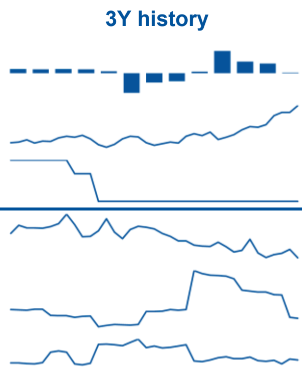
Argentina's economic backdrop is fragile and dependent on IMF funding. Meanwhile, exposure to the market is expensive given Mercado-Libre's valuations. As a result, we maintain our *underweight* allocation.

Middle East and North Africa

Morocco

Neutral

A drought-driven decline in agricultural output puts a drag on growth and on Morocco's external balances.



	Latest	
GDP, % yoy	0.3	Q1
CPI, % yoy	7.2	Jun
Policy rate, %	1.50	Jun
MSCI Morocco*	-7.5%	Jul
EPS, % yoy	-23.0	Jul
Trailing P/E	22.0	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

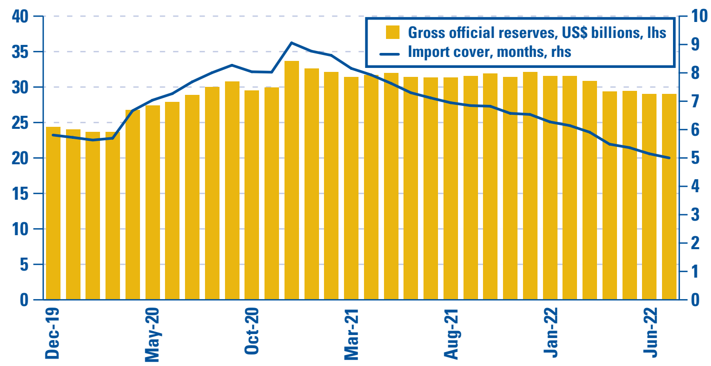
Morocco's economy had a soft start to the year, with GDP growth slowing sharply from 6.6% yoy in Q4 2021 to 0.3% in Q1. The slowdown can be attributed to weak agricultural production due to the drought. Indeed, the Ministry of Agriculture estimates total cereal production in 2022/23 to decline by 62% yoy. With agriculture accounting for 10% of Morocco's economy, a dry season is set to drag growth down. Consensus projects GDP growth to ease from 7.7% yoy in 2021 to 1.3% this year.

The drought has meant that Morocco has had to import higher volumes of cereals at a time of elevated commodity prices. In addition, Morocco also faces a higher energy import bill. The recovery in tourism and phosphate exports, which have gained importance amidst the current global fertiliser shortage, is not expected to be enough to offset the increase in imports. As such, consensus expects the current account deficit to widen from 2.9% of GDP in 2021 to 6.4% this year.

On the fiscal front, the budget balance is expected to remain in deficit this year as the government increases social spending amid high commodity prices. The government subsidises butane gas, wheat and sugar through a compensation fund. The government has also announced emergency measures to support the transport, tourism and agricultural sector. Such measures and the fact that Morocco's food imports are worth less than 20% of its goods exports mean that the likelihood of a food crisis and the associated social unrest is lower in Morocco than elsewhere in the region.

While Morocco is set to experience twin deficits this year, the risks usually associated with such a position are low given Morocco's ample reserves and therefore its ability to finance its current account deficit (see Chart 3). Moreover, 77% of Morocco's public debt obligations are dirham-denominated.

Chart 3: Morocco Foreign Exchange Reserves



Source: Bloomberg

Meanwhile, following average inflation of 1.4% in 2021, price pressures have picked up on the back of rising commodity prices. Consumer prices rose by 7.2% in June. The Bank Al-Maghrib (BAM) does not explicitly target inflation, and currently views the latest price shocks as temporary, allowing it to keep its benchmark interest rate at a historical low of 1.5%. Looking ahead, BAM has noted that it will review its options only if price pressures are found to be domestically generated. Markets are pricing in 50bps of rate hikes within the next year.

In the medium term, given its large agricultural sector and scarce water supply, Morocco's economic fortunes will continue to be linked to rainfall patterns, which are set to become more erratic as the climate changes. In the absence of infrastructure development and water demand management, droughts are likely to weigh on productivity and on Morocco's potential output.

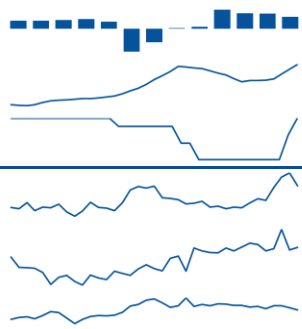
Market Strategy: Morocco's equity valuations have remained steady over the past six months, with the 12M forward P/E premium over FM at 79%, much higher than its five-year average of 58%. Moreover, the market offers a dividend yield of 3.5%, lower than FM's 3.9%. While the economic backdrop is not as fragile as elsewhere in FM, we think that this has been fully priced by the market. As a result, we stay *neutral*.

Sub-Saharan Africa

Nigeria

Underweight

Muted oil production means Nigeria is set to miss out on the benefits of higher oil prices, keeping a lid on growth.



	3Y history	Latest	
GDP, % yoy		3.1	Q1
CPI, % yoy		18.6	Jun
Policy rate, %		14.00	Jun
MSCI Nigeria*		14.8%	Jul
EPS, % yoy		13.8	Jul
Trailing P/E		7.4	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

In what should have been a year of robust growth due to higher oil prices, Nigeria's economy is set to slow as oil production remains depressed. GDP growth slowed from 4% yoy in 2021 Q4 to 3.1% in Q1 of this year, as the oil sector contracted by 26% yoy. Crude oil production in Nigeria has been hampered by security and technical problems, leaving the country short of its OPEC quota and thereby limiting the pass-through of higher oil prices to fiscal revenues. In addition, scant domestic refining capacity means that Nigeria is reliant on imported refined petroleum, which is subsidised by the government. Authorities estimate that 2% of GDP will be spent on fuel subsidies.

Coupled with Presidential elections in February 2023, Nigeria is unlikely to make much progress on fiscal consolidation in the coming months. Pre-election spending should support the services sector, which is set to be the key driver of economic growth. All told, consensus expects Nigeria's GDP to expand by 3% yoy this year, a slight pick-up from 2021's 2.8%, and the fiscal deficit to remain wide at around 4.3% of GDP.

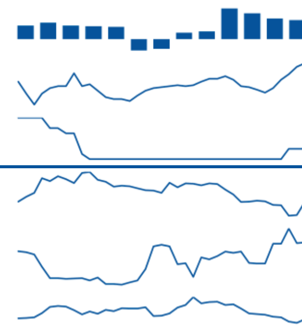
With the country facing double-digit inflation of 18.6% yoy in June, the Central Bank of Nigeria (CBN) has raised rates by a cumulative 250bps since the lift-off in May. Nonetheless, further pressure on the naira is likely amid dollar scarcity, which has pushed the parallel rate to trade at a wide discount.

Market Strategy: Elevated oil prices drove the outperformance of MSCI Nigeria to FM over the past six months. While oil prices are expected to remain elevated, depressed oil production suggests the benefits to Nigeria will be limited. With valuations neither expensive nor attractive, with MSCI Nigeria's 12M forward P/E trading at a discount in line with the five-year average, we stay *underweight*.

Kenya

Underweight

Increased social spending to combat commodity price rises threatens to derail fiscal consolidation efforts.



	3Y history	Latest	
GDP, % yoy		6.8	Q1
CPI, % yoy		8.3	Jul
Policy rate, %		7.50	Jul
MSCI Kenya*		-1.1%	Jul
EPS, % yoy		35.3	Jul
Trailing P/E		9.4	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Delayed rainfall and high fertiliser prices have hindered agricultural output, which, accounting for 33% of GDP, is a key driver of Kenya's economy. Indeed, the USDA projects lower coffee and sugar production for the 2022/23 marketing year. Inflation is set to dampen domestic demand, as evidenced by the further decline in Kenya's all-economy PMI in July. Consensus forecasts GDP growth to slow from 7.5% in 2021 to 5.4% this year. While the result of the recent election is yet to be announced, given both candidates' similar pledges, policy continuity seems likely.

Against the backdrop of elevated commodity prices, the government has continued to subsidise fuel to the tune of $64mn a month, which is expected to be phased out this fiscal year. The IMF has said that the country has the fiscal space from strong tax collections to temporarily provide such subsidies without missing the program's fiscal targets. Consensus projects the fiscal deficit to narrow from 8.1% in the previous fiscal year to 7.3% in FY22/23. In contrast, a higher import bill points to a widening current account deficit. Meanwhile, with food imports using up over 40% of export earnings and existing food insecurity, Kenya is at risk of a food crisis and the associated social upheaval.

Inflation rose for the fifth consecutive month in July to 8.3% on the back of food prices, leaving it uncomfortably above the 7.5% upper-bound target of the Central Bank of Kenya (CBK). After raising rates by 50 bps for the first time in nearly seven years at the May meeting, the CBK kept rates on hold in July due to signs of easing inflationary pressures. Nonetheless, consensus expects a further 50bps of rate hikes by the year-end.

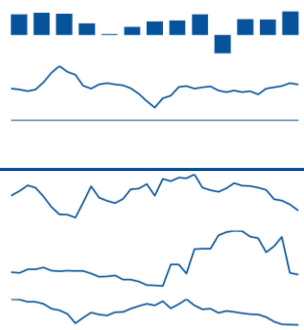
Market Strategy: With the economy vulnerable to higher commodity prices, Kenya's equity market does not appear attractive. The 12M forward P/E is at a 9% discount to FM, in line with the five-year average, so we stay *underweight*.

Asia

Vietnam

Overweight

While the Communist Party's corruption crackdown is a headwind to equities, the economic backdrop is robust.



	3Y history	Latest	
GDP, % yoy		7.7	Q2
CPI, % yoy		3.1	Jul
Policy rate, %		9.00	Jul
MSCI Vietnam*		-10.4%	Jul
EPS, % yoy		11.7	Jul
Trailing P/E		12.5	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Vietnam's economy is firing on all cylinders, as GDP growth picked up from 5% yoy in Q1 to 7.7% in Q2. The strong outturn can be attributed to both the strength of the household sector and of exports. The outlook for H2 has deteriorated in the past six months though. Rising inflation is likely to weigh on household consumption, despite the fact that the government introduced a cut to fuel tax last month.

Additionally, softer external demand suggests a slowdown in Vietnam's export sector, which has been a major driver of growth. Moreover, the potential for further lockdowns in China and the ensuing supply chain problems is a downside risk for the sector. Nonetheless, Vietnam's manufacturing sector appears to be holding up so far, as reflected in the above-50 PMI reading for July.

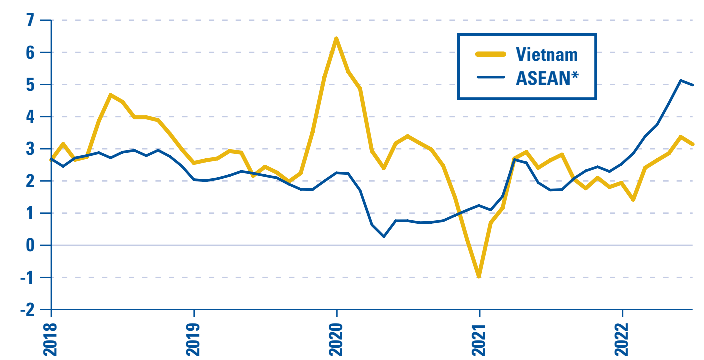
Further ahead, Vietnam's economy still benefits from some structural tailwinds, which should support growth in the medium-term. A productive labour force and weak wage growth mean that the reconfiguration of global supply chains is still in Vietnam's favour. Foreign direct investment in manufacturing grew by a solid 27% yoy in Q2. And Samsung recently announced plans to produce semiconductor components in Vietnam from July 2023.

All told, consensus projects GDP growth to rebound sharply from 2.6% yoy in 2021 to 6.8% yoy in 2022. This would mark a return to growth in line with the five-year average and leave it ahead of the government's growth target of 6-6.5% for this year.

Vietnam's external balance is expected to improve this year. The current account deficit is forecast to narrow from 0.7% of GDP last year to 0.3% as a recovery in tourism receipts should offset a higher energy import bill. On the fiscal side, with only 40% of planned total expenditure spent, the budget balance was in surplus during H1. Therefore, the government has the fiscal space to support the economy, as evidenced by the recent fuel tax cuts.

In contrast to its ASEAN peers, inflationary pressures in Vietnam have been contained thanks to stable local food production (see Chart 4). Inflation in July slowed from 3.4% to 3.1%, comfortably within the National Assembly's target of 4%. As such, the State Bank of Vietnam (SBV) is expected to keep rates on hold, sitting out the global tightening cycle.

Chart 4: Consumer Prices, % yoy



**ASEAN is GDP weighted Malaysia, Indonesia, Philippines and Thailand.*

Source: Bloomberg

The Vietnamese Communist Party has been cracking down on corruption since April, which has resulted in the arrest and dismissal of several high profile government officials. The government has also made headway in deleveraging the real estate sector by clamping down on private lender loans and curbing speculation. The anti-corruption campaign is part of the government's efforts to uphold the Communist Party's legitimacy and upgrade Vietnam from a frontier market to an emerging market (the country is on FTSE's EM watch list). While eliminating corruption would be a step in the right direction, Vietnam would also need to make regulatory changes such as increasing the cap on foreign ownership and liberalising its foreign exchange market to graduate to the EM index.

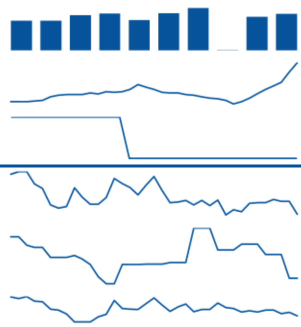
Market Strategy: MSCI Vietnam sold off sharply in the wake of the government's anti-graft drive, with equities dropping by 25% between February and July. As such, valuations appear attractive, with the 12M forward P/E trading at a 15% premium to FM, nearly two standard deviations below the five-year average. While the Communist Party appears intent on pressing on with its anti-corruption campaign, posing a downside risk to equities, we think Vietnam's economic fundamentals are strong. We remain *overweight*.

Bangladesh

Neutral

The outlook for economic activity is strong, but depleted foreign reserves are a key risk.

3Y history



	Latest	
GDP, % yoy	7.3	FY21-22
CPI, % yoy	7.5	Jul
Policy rate, %	4.00	Jun
MSCI Bangladesh*	-6.4%	Jul
EPS, % yoy	-4.3	Jul
Trailing P/E	11.5	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Bangladesh's economic recovery gathered steam through the fiscal year ending in June 2022, with GDP growth accelerating from 6.9% to 7.3%. But growth is expected to soften as exports moderate on the back of weak external demand. Meanwhile, although higher inflation is likely to drag consumption down, the increase in government fuel and fertiliser subsidies in the latest budget should blunt some of the impact. Consensus expects GDP growth of 7.1% for the 2022 fiscal year.

Similar to other frontier markets, Bangladesh's role as a net importer of energy and commodities has resulted in a deterioration of the country's external balance. As such, the Bangladesh Bank (BB) allowed the taka to float against the US dollar at the start of June to preserve foreign exchange reserves, which have been under pressure due to the country's rising import bill. The situation has been exacerbated by the weakness in remittances from abroad. Indeed, it appears that many expatriates have switched to using informal channels after using official channels during the pandemic, although the pick-up in remittances in July suggest a tentative turnaround.

The taka has depreciated by 6% since the start of June, which will add to inflationary pressures by increasing import costs. Consumer prices rose by 7.5% yoy in July, a nine-year high. In response, BB raised rates for the first time in a decade in May, bringing its cumulative tightening to 75bps.

Amid a shortage of reserves, Bangladesh has sought assistance of $1bn from the World Bank and the Asian Development Bank. This is in addition to the bailout requested from the IMF. While funding would provide a temporary reprieve, any assistance will come with conditions, which will weigh on growth.

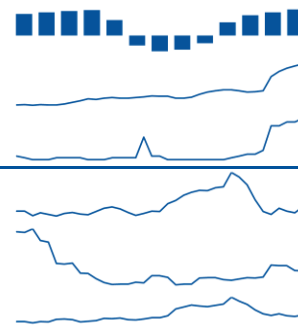
Market Strategy: MSCI Bangladesh's 12M forward P/E is at a 5% discount to FM, only slightly below its five-year average. Coupled with the challenging backdrop, we keep our *neutral* allocation.

Kazakhstan

Overweight (↑)

Resilient economic activity on the back of high oil prices offsets the hit from the Russo-Ukrainian war.

3Y history



	Latest	
GDP, % yoy	4.6	Q1
CPI, % yoy	15.0	Jul
Policy rate, %	14.50	Jul
MSCI Kazakhstan*	-9.9%	Jul
EPS, % yoy	3.9	Jul
Trailing P/E	7.3	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Economic activity in Kazakhstan has held up better than initially expected following Russia's invasion of Ukraine. With 30% of Kazakhstan's imported goods coming from Russia, Kazakhstan appeared vulnerable to a sharp Russian slowdown. But soaring energy prices and a smaller-than-expected contraction in Russia has blunted the negative impact of the invasion. GDP growth picked up from 4.1% yoy in Q4 to 4.6% in Q1. The composite PMI was unchanged at 53.6 in June, which signals private sector expansion, suggesting that momentum continued in Q2. All told, consensus projects GDP growth to ease only slightly this year, from 3.7% yoy in 2021 to 3.4%.

Accounting for 13% of GDP, the economy is deeply intertwined with the oil sector. In line with rising OPEC+ quotas, Kazakhstan has increased output. Latest OPEC forecasts show supply increasing by 120,000 b/d. But the recent reversal of a short-lived Russian suspension of the Caspian Pipeline Consortium (CPC), which transports nearly all of Kazakhstan's exports, has increased political pressure. As a land-locked nation, Kazakhstan has limited options outside the CPC.

The current account has shifted into surplus on the back of rising oil receipts, which means that the National Fund is well placed to step in to support the tenge in the event of financial outflows. Capital controls in Russia have meant that the tenge has depreciated against the ruble, which has pushed up imported prices. The National Bank of Kazakhstan (NBK) has raised rates by a cumulative 475bps this year to shore up the currency. With CPI at 15% yoy in July and the NBK expecting inflation to start easing only in Q1 2023, further rate hikes are likely.

Market Strategy: Valuations are attractive, with Kazakhstan's 12M forward P/E trading at a 42% discount to FM, significantly below the five-year average. Elevated energy prices should continue to bolster the Kazakh economy. Thus, we upgrade Kazakhstan to *overweight*.

Europe

Romania

Overweight

Despite the limited exposure to Russian energy, high prices are set to drag economic growth down.

	3Y history	Latest	
GDP, % yoy		6.4	Q1
CPI, % yoy		15.0	Jul
Policy rate, %		4.75	Jul
MSCI Romania*		11.2%	Jul
EPS, % yoy		74.1	Jul
Trailing P/E		6.7	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Romania's economy started the year on a strong footing, with GDP growth picking up from 2.4% yoy in Q4 2021 to 6.4% in Q1 on the back of investment and household spending. Growth momentum is set to slow this year, with private consumption and investment on the back of EU fund flows likely to be the biggest growth drivers. Moreover, Romania is less exposed to Russian energy, with only 37% of its oil imports and 16% of its natural gas imports coming from Russia. This minimises the economic shock in the event Russia cuts off oil supply.

Consensus projects GDP growth to ease from 6.2% in 2021 to 3.8% this year. On the fiscal front, government subsidies for households and firms to cope with higher inflation mean that the government is widely expected to overshoot its budget deficit target of 5.8% of GDP this year.

Inflation in July reached 15.0% yoy, as services inflation picked up, suggesting broadening price pressures. The National Bank of Romania (NBR) has so far raised rates by 425bps since October 2021. But the NBR eased the pace of its tightening at its August meeting, hiking by 75bps compared to the 100bps expected by the consensus, as the bank became more concerned about growth and does not expect a further increase in inflation. The market is nonetheless still pricing in a further 20bps this tightening cycle. The current account is set to remain in deficit due to higher energy imports, but tighter policy and strong international reserves should limit volatility in the leu.

Market Strategy: MSCI Romania's 12M forward P/E is at a 38% discount to FM, one standard deviation below its five-year average. Additionally, the dividend yield of 8.5% is significantly higher than FM's 3.9%. Therefore we stay *overweight*.

Slovenia

Overweight

Growth is set to moderate this year, with Slovenia's dependence on Russian energy another downside risk.

	3Y history	Latest	
GDP, % yoy		9.8	Q1
CPI, % yoy		11.0	Jul
Policy rate, %		0.50	Jul
MSCI Slovenia*		-7.9%	Jul
EPS, % yoy		21.4	Jul
Trailing P/E		5.5	Jul

**US$ total return relative to MSCI FM 100. Latest is six-month return.*

Source: Bloomberg

Slovenia's economy grew by a robust 9.8% yoy in Q1, driven by strong private consumption. GDP growth this year is expected to moderate as high energy and food prices weigh on households, although the tight labour market should continue to put upward pressure on real wages, providing some offset. In addition, EU fund inflows should continue to boost investment. Consensus expects GDP growth to slow from last year's 8.3% to 3.9%. Despite public transfers to households to combat rising energy prices, the budget deficit is projected to narrow.

The biggest risk to the outlook is Slovenia's dependence on Russian energy. The country imports 25% of its oil imports and 80% of its natural gas from Russia. The newly-elected Prime Minister Robert Golob has prioritised the transition away from Russian energy, yet has provided little detail on how the country would achieve this.

Much like in the rest of the eurozone, inflation in Slovenia has been ticking up on the back of higher food and energy prices. Consumer prices rose by 11% yoy in July, the highest pace of increase in 27 years. The European Central Bank (ECB) responded by raising rates by 50bps at its July meeting, bringing an end to its decade long accommodative monetary stance. The market is pricing in nearly 140 bps of hikes this cycle. However, with the ECB's tightening cycle trailing the US Fed and a looming Russian energy crisis, the euro is expected to remain on the backfoot.

Market Strategy: With MSCI Slovenia's 12M P/E trading at a 21% discount to FM, nearly a standard deviation below the five-year average, valuations are attractive. Combined with the fact that the forward earnings for the pharmaceutical firm Krka, which accounts for 73% of the index, are up by 16% on a six-month basis, we maintain our *overweight* allocation.

KEY ECONOMIC AND FINANCIAL INDICATORS *(All data shown are as at end-July 2022 unless otherwise stated)*

		Macroeconomic Data												Market Performance					Forecast (Bloomberg)†
		% change on year ago				Latest 12 months													
	Frontier Market	Annual GDP Growth YoY	Quarterly GDP Growth QoQ*	Industrial Production Growth YoY	Consumer Price Index YoY	Trade Balance	Current Account	Foreign Reserves 2022 Latest	Foreign Reserves 2021 Year Ago	Currency vs $ 2022 Latest	Currency vs $ 2021 Year ago	Sovereign Rating S&P	Budget Balance % of GDP 2022F	Short-Term Interest Rates	% S&P Frontier 150 Index**	Stock Market Index (S&P Frontier 150 Index) US$	Change since 12/31/21 US$	Change since 12/31/21 Local	Trailing P/E	6 month Currency vs $ +/-
		%	%	%	%	$ Bns	$ Bns	$ Bns	$ Bns					%	Jul. 29, 2022	Jul. 29, 2022	%	%		
Overweight	VIETNAM	7.7	n.a.	11.2	3.1	1.1	-6.0	102.9	101.3	23395.0	22809.0	BB+	-4.8	3.5	14.2	530.0	-27.6	-25.9	17.6	+
	SLOVENIA	9.8	3.2	0.8	11.0	-5.9	0.6	0.8	0.7	1.0	1.2	AA-	-4.7	0.1	2.7	1580.7	-22.5	-13.6	11.3	-
	ROMANIA	6.4	20.3	-3.7	15.0	-7.6	-24.4	40.2	42.4	4.8	4.2	BBB-	-7.0	7.8	8.5	2161.1	-6.9	3.4	6.5	+
	KAZAKHSTAN	4.6	n.a.	-1.3	15.0	29.7	-1.7	7.4	12.5	477.1	424.9	BBB-	-2.9	15.0	4.5	184.7	-25.8	-18.6	5.4	n.a.
Neutral	BAHRAIN	5.5	n.a.	n.a.	3.1	1.8	n.a.	3.3	3.5	0.4	0.4	B+	1.8	3.7	8.5	5097.8	18.1	18.1	13.3	uc
	BANGLADESH	7.3	n.a.	30.4	7.6	-50.8	-18.0	38.1	44.4	95.0	84.8	BB-	7.1	5.5	4.6	1572.9	-23.7	-15.7	11.5	n.a.
	CAMBODIA	3.0	n.a.	n.a.	7.9	n.a.	-12.4	16.2	17.2	4099.0	4076.3	NR	n.a.	1.6	2.4	1589.9	6.9	7.4	n.a.	n.a.
	GEORGIA	15.1	n.a.	0.2	1.2	-6.7	-2.0	3.7	3.7	2.8	3.1	BB	n.a.	n.a.	1.6	1020.0	-18.4	-27.2	21.0	n.a.
	ICELAND	7.3	4.4	n.a.	9.9	-14.9	0.2	5.8	6.6	136.8	126.1	A	n.a.	4.8	7.4	910.1	-9.0	-3.4	16.4	n.a.
	MOROCCO	0.3	n.a.	13.1	7.2	-17.0	-2.6	29.0	31.4	10.3	9.0	BB+	-5.9	2.5	11.3	1175.7	-20.3	-11.3	22.5	n.a.
	OMAN	-0.8	n.a.	11.2	2.9	17.7	-8.7	15.7	17.6	0.4	0.4	BB-	4.6	3.0	3.3	4540.7	37.4	37.4	33.2	uc
	PANAMA	13.6	n.a.	n.a.	5.2	-3.6	6.5	7.7	9.6	1.0	1.0	BBB	n.a.	1.6	2.9	3906.8	-17.9	-17.9	14.0	uc
Underweight	ARGENTINA	6.0	3.6	-13.3	71.0	11.1	5.1	42.2	42.8	134.5	97.1	CCC+	-4.6	55.7	13.3	3466.7	-26.2	-5.7	3.0	-
	NIGERIA	3.1	-58.6	n.a.	18.6	3.3	5.4	39.2	33.7	427.9	411.7	B-	-4.3	5.0	10.5	1102.9	-5.0	-2.2	7.4	-
	KENYA	6.8	4.8	n.a.	8.3	-13.2	n.a.	7.9	9.9	119.4	109.2	B	-7.3	6.6	2.9	3709.8	-23.6	-19.7	9.4	+
	UKRAINE	-15.1	-77.2	2.9	22.2	-0.5	-1.4	19.4	26.8	36.8	26.7	CC	-27.9	7.2	1.0	302.7	-54.6	-39.1	3.8	n.a.
	SRI LANKA	-1.6	n.a.	-2.3	60.8	-7.3	n.a.	4.4	6.5	361.6	199.5	SD	-11.3	12.6	0.2	1283.8	-73.9	-53.3	4.7	n.a.

*Note: S&P credit rating shown is long-term foreign currency rating. * % change in GDP on previous quarter, annual rate.**S&P/IFCG Extended Frontier 150 Net Total Return Index. Data are the latest available, but in certain cases relate to periods more than one year ago. †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.*

Source: Bloomberg, City of London Investment Management

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