CITY OF LONDON
Investment Management Company Limited

Emerging Markets Quarterly Outlook

April 2017

Overview

Belated Honeymoon for Emerging Markets

Brimming with optimism, markets have risen to new record highs as the financial crisis recedes in memory, cyclical indicators increasingly point to a gathering global recovery and the Trump administration has proven unable/unwilling to make good on its most disruptive campaign promises. This has particularly benefitted emerging market (EM) equities, which enjoyed the additional boost of strengthening exchange rates as the dollar weakened during Q1. Similarly, sovereign bond issuance by EMs hit an all-time quarterly record in the first quarter, while flows of portfolio capital into EM stocks have also been strong. Whereas investors withdrew nearly $30bn from EM stocks and bonds in November 2016, the month of Donald Trump's election victory, outflows slowed to a mere $1.2 bn in December and reversed to the tune of an estimated $12 bn in January.

To be sure, signs of improvement abound, not only in the context of the dismal recent years. True, Russia and Brazil are merely exiting a painful recession and remain hostage to the vagaries of local politics and global commodity prices. Political flashpoints also exist from Turkey to South Africa to Thailand. But robust economic readings elsewhere, be it in South Korea or Mexico, suggest that the broader growth downtrend of the past years may be about to be broken. Some countries, such as India and Indonesia, also enjoy large domestic economies and ambitious economic reform programs. And finally, while EM inflation is ebbing away, global trade is witnessing its fastest growth rate in seven years.

But what of the threat of rising US rates? Their impact is likely to be less damaging than in past episodes. First, the tightening cycle only responds to (and in fact, deliberately lags) the recovery of the US economy. Second, it is the most telegraphed series of rate increases in Fed history, and they are set to be both small and slow. The Fed continues to see the equilibrium real rate as near zero and has not changed its view of the terminal rate of 3.0%. Third, at the same time China's economy is stabilising and delivering a positive growth impulse to the global economy. And finally, as pointed out previously, emerging markets possess much improved national balance sheets and more competitive exchange rates compared to previous episodes of rising US rates.

But is buying into risk at this stage in the market cycle picking up pennies in front of a steamroller? Potentially. The shock value of last year's two seminal events – the 'Brexit' vote on June 23rd and Donald Trump's election on November 8th – may have faded, but the long term repercussions of these events have yet to make themselves felt. At a minimum, the increasing scepticism about trade, financial integration and international cooperation amongst policymakers does not warrant market volatility levels near historic lows and stock markets near historic highs. While low volatility can partly be explained by record low bond yields which support appetite for alternative assets, the long term consequences of these political risks appear insufficiently discounted. While the old adage holds that 'in the long term we are all dead', any upsurge in US trade protectionism, in particular with respect to China, has the potential to severely disrupt appetite for EM assets.

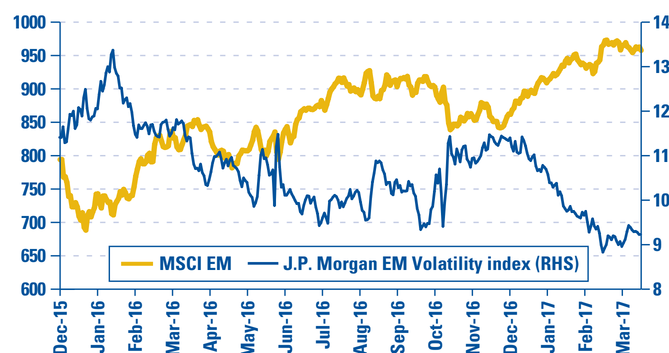
Market Strategy

Against this backdrop, our approach remains to acknowledge both the fundamental and cyclical improvements in emerging markets, but to stay wary of current market exuberance, which relies excessively on the notion of 'Trumpflation'. In other words, while the MSCI EM outperformed the MSCI World by a strong 4.9% in Q1, we do not indiscriminately ramp up risk exposure in our allocation. Instead, we add risk where we see value and make some other adjustments.

Specifically, we have upgraded Mexico from *underweight* to *neutral* given both the proactive stance of Banxico in stemming peso weakness and rising inflation expectations and the receding threat of a wholesale dismantling of NAFTA by the US. We upgraded Korea to *overweight* as the ouster of President Park opened the door to a more certain and promising outlook, while valuations remain attractive. Similarly, we moved Taiwan and Malaysia from *neutral* to *overweight*, the former on the basis of an uptick in external demand and the latter on the basis of a recovering domestic outlook.

By contrast, after a spectacular but short-lived run, we downgrade Russia from *overweight* to *neutral* as there has yet been little fundamental improvement, political tensions, both domestic and international, are intensifying again and valuations have become unattractive.

Chart 1: EM Performance and Volatility



Source: Bloomberg

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Asia

China

Neutral

Policymakers are fine tuning their policy levers to keep the economy on even keel during a year of political transition.

Policymakers managed to stabilise the economy in 2016 through pro-active fiscal policy, while shifting monetary policy towards a more neutral stance as the year ended. At the National People's Congress, the government recently lowered its 2017 growth target to "around 6.5%" (compared to "a range of 6.5-7%" in 2016 and "around 7.0%" in 2015). Yet, this is likely to be regarded as a lower bound given that this is a year of political transition. The government also announced a series of other economic targets for 2017, including M2 and total social financing growth of 12% yoy, down from a planned 13% in 2016 (actual 11.3% and 12.8%, respectively). The fiscal deficit target remained unchanged at 3% of GDP, but the local government special bond issuance quota was doubled to Rmb800 billion and the debt swap program is set to continue.

Meanwhile, GDP slightly beat expectations with a 6.8% yoy gain in Q4, up from the 6.7% yoy recorded in each of the previous three quarters (full year 6.7% in 2016). More recently, manufacturing and services PMI remained on expansion course, at 51.8 and 55.1 respectively in January-February. FAI expanded by 8.9% yoy in January-February, the fastest rate since June. Importantly, the private sector component has begun to make a recovery, after it had been in decline for several years and exerted a significant drag on growth. On the other hand, domestic demand remains lacklustre amid slowing consumption as retail sales rose by just 9.5% yoy on the back of weak auto sales during the same period, the slowest pace since 2004.

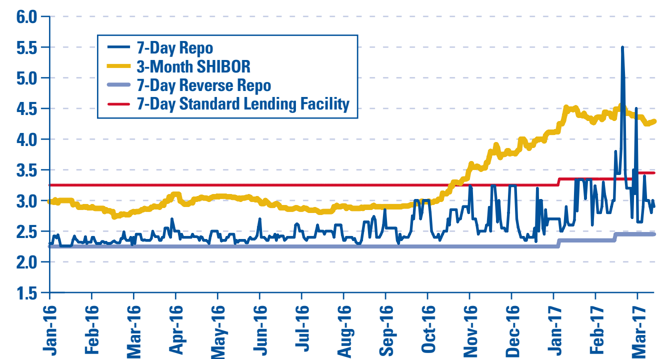
In February, export growth turned negative despite a favorable base effect and a regional export rebound, leading to the first monthly trade deficit in almost three years. However, early year data are typically distorted by the Lunar New Year effects and averaging the first two months suggests robust export growth of 4% yoy, whereas import growth jumped by over 26% yoy in Jan-Feb, a sign of robust industrial if not retail demand. In addition, after two years of capital outflows and seven consecutive months of foreign reserve declines, outflows reversed as capital controls gained traction, driving reserves back above the $3 trillion mark.

Price developments diverged starkly at the beginning of the year, suggesting that domestic pricing power remains weak. Indeed, PPI rose to 7.4% yoy in January-February (average), from 5.5% yoy in December. Yet, CPI decelerated to 1.7% yoy in January-February from 2.1% yoy in December. Core CPI remained stable though at 2.0% yoy during the period. Global commodity prices may keep upward pressures on PPI alive for several more months, but CPI is likely to hover around the 2% mark, thus comfortably below the 3% official 2017 target.

The PBoC raised market-based policy rates for a second time in 2017 in March, lifting rates by 10 bps (rates on 7-day, 14-day, and 28-day reverse repos rose to 2.45%, 2.60%, and 2.75% respectively and rates on the 6-month and 1-year medium-term lending facility (MLF) moved to 3.05% and 3.20% respectively). However, the central bank has developed a variety of policy tools to address these different objectives and is keen to differentiate between policy moves aimed at monetary stability and those aimed at financial stability. As such, it does not regard the recent changes as a tightening of monetary policy and consequently it also left the benchmark deposit and lending rates on hold (unchanged since October 2015). Together with stable credit growth, the PBoC will likely target a neutral stance in both monetary and FX policy over the year.

It is worth noting though that tighter wholesale funding conditions and financial regulation could negatively impact regional banks, which have relied heavily on such funding to support the expansion of their balance sheets. In the event, these banks could be forced to shrink their balance sheets via asset sales or reduced lending, causing asset price fluctuations and reduced credit growth to the economy.

Chart 2: Interest Rates



Source: Bloomberg

Market Strategy: Chinese equities rallied in Q1, with Hong Kong listed shares (MSCI China) posting a strong gain of 12.9% and outperforming the index by 1.5% points. However, the Chinese housing sector is set to decelerate yet again as the government implemented restrictive measures and constrains land sales, exerting a drag on overall growth. With a P/E of 14.4, valuation metrics remain favourable, but a current 11% discount to the MSCI EM P/E has become much less compelling than the one of 44% a year ago. What is more, the likelihood of a more adversarial relationship with the US, be it on trade or on North Korea, keeps us on hold with a *neutral* allocation.

South Korea

Overweight (↑)

Following the ousting of President Park, Jae-in Moon leads the polls for the election due in May. He stands for more redistributive policies and a more dovish foreign policy.

After parliament voted to impeach President Park on corruption charges in early December 2016, her term came to an early end on March 10th when the constitutional court upheld the motion. Ms Park was subsequently arrested on March 31st. Her ouster triggered a new presidential election, due to be held on May 9th. Currently leading the polls is Jae-in Moon, the leader of the Minjoo party until last January, who Ms Park defeated in the 2012 election. His party is more socially liberal and currently enjoys its highest ever support, at over 50%. Mr. Moon's personal support is at 35%, the highest in a crowded field. He appears more down to earth to the electorate than Ms. Park and vows to tackle the state's corruption, nepotism and its close relationship with the country's chaebols, while being more dovish in dealings with North Korea. Indeed, geopolitical issues could become the defining issues for any presidency as North Korea continues its belligerent behaviour by firing four ballistic missiles in the East Sea toward Japan in March and claiming to conduct exercises for a strike on US bases in Japan (following two nuclear tests and a submarine launched missile in 2016). At the same time, China has instructed a travel ban for tour organisers to Korea in protest against the deployment of the US THAAD (Terminal High Altitude Area Defense) anti-missile system in South Korea. But regardless of who wins the presidency, the next government will have a minority in parliament, limiting the scope for radical policy changes. Broadly speaking, Moon favours more redistributive policies and a tightening of lending standards in order to limit household debt (currently at 150% of GDP).

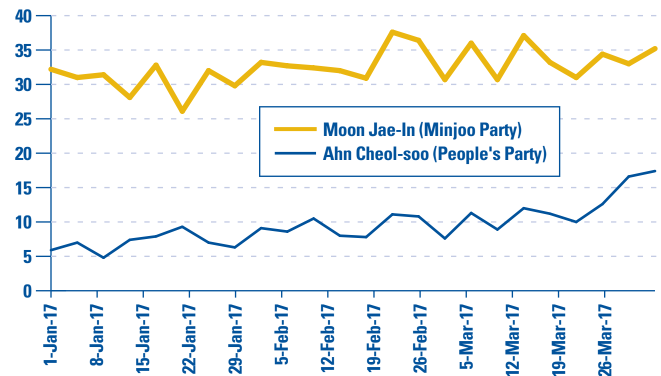
Meanwhile, political uncertainty weighed on private consumption in Q4, which decelerated from 2.7% yoy in Q3 to 1.5% yoy and dragged overall GDP growth down from 2.6% yoy to 2.4% yoy in Q4. More recently, industrial production bounced 2.9% mom in January, but dropped precipitously by 3.4% mom in February. Given the typical volatility in output figures around the lunar holidays, IP subsequently rebounded in March. Yet, sentiment remains muted and PMI readings hover around a contractionary 49 point index level.

Consumer sentiment improved for a second consecutive month in March, recovering from the dip in November, but remaining below the level prevailing before the impeachment vote. The final ruling by the Supreme Court and the presence of a clear frontrunner in the upcoming elections are likely to further reduce consumer concerns about the economic outlook in the upcoming months.

On a positive note, exports staged a better-than-expected recovery in February, expanding 20.2% yoy on the back of a broad-based improvement in manufacturing goods exports. Imports also rose at double-digit rates on the back of capital goods imports, pointing to a rise in investment expenditures. On the other hand, receipts from tourism expenditures have begun to edge down as a result of the restrictive policy measures implemented by China in 2016. The additional measures introduced in March this year have the potential to reduce tourist inflows even further. Private forecasters expect GDP growth to slow from 2.7% in 2016 to less than 2.5% in 2017 as weak domestic expenditures offset improving external performance.

Consumer prices ticked up from 1.3% yoy to 2.0% in January, but edged back to 1.9% yoy in February. Some slight gains are expected on the back of the government's hike of utility prices but softening oil prices will likely keep headlines rates in check. In this context, the Bank of Korea is likely to remain on hold for now, in particular as it awaits the outcome of the presidential election and the possible implementation of more stimulative fiscal policies. The adoption of a supplementary budget looks particularly likely given the restrictive nature of the current 2017 budget, which is based on expenditure growth of just 0.5%.

Chart 3: Presidential Election Polls



Source: Wikipedia

Market Strategy: The reduction of political uncertainty with the ouster of President Park and the likely victory of Mr. Moon will likely support sentiment and bolster private consumption. Stimulative fiscal policies and a supplementary budget are set to add further tailwind to the economy.

South Korea has outperformed the MSCI EM by 1.7% over Q1, but valuations remain attractive, with a P/E of 12.5, a 23% discount to the MSCI EM P/E. We shift back to an *overweight* allocation, but remain wary of the increasing tail risk any flare-up of tensions with North Korea represents.

Taiwan

Overweight (↑)

Robust external demand and rising investment are set to push growth up this year.

Taiwan's economic data has recently surprised to the upside. The export sector, a key bellwether for activity, has shown significant strength, with export orders up by 22% yoy in February against an expected 16.1%. Although this may have been boosted by the impact of the Lunar New Year, the combined rise in January and February was still 12.7%, the fastest expansion since 2010. This suggests that global demand is accelerating, with non-tech orders surging as Chinese growth remains robust.

Meanwhile, tech exports ytd are up by 17.5% yoy and the sector is likely to be supported by several new smartphone launches this year. The manufacturing PMI suggests an acceleration in activity ahead, with the March figure at 56.2 against 51.1 a year earlier. Revenue grew for the first time in six quarters in Q4 and the TIER survey has also shown rising optimism in the manufacturing sector over the outlook for the next six months.

GDP rose by 1.4% yoy is 2016 as fixed asset investment increased by 11.8%, the strongest since 2010. Growth accelerated over the year as the economy emerged from recession in Q2 to grow by 1.1% yoy and the expansion accelerated to 2.9% in Q4. GDP growth is forecast to rise to 2.0% this year, supported by robust external demand and rising investment.

The Taiwanese dollar is up by 6.2% ytd on a trade-weighted basis and by over 10% since the low in June. This is likely to keep downward pressure on already low inflation (0.2% yoy in March versus 2.4% a year earlier). Underlying inflationary pressures are muted, with core inflation at 1.0% in March, up marginally from 0.8% 12 months earlier.

A backdrop of rising growth and low inflation should keep the central bank (CBC) on hold. Indeed, the Bank kept its key policy rate at 1.375% in March for a third consecutive quarterly meeting, which followed cumulative easing of 50 bps in the previous four meetings. Moreover, the country's large external surplus reduces pressure on the central bank to raise rates as the Fed tightens, unlike some other EMs. The expanding trade surplus supports external finances, with the current account surplus projected to be 13% of GDP this year.

Market Strategy: Taiwan's improving economic backdrop coincides with attractive valuations: its P/E is below the long-term average and is at a 2% discount to EM versus a long-term average of a 26% premium, while its dividend yield (4.0%) is the second highest in EM. We therefore upgrade our weight to *overweight*.

Malaysia

Overweight (↑)

The cyclical upturn in the economy coincides with a neutral central bank and stable external accounts.

Malaysia's cyclical recovery gathered momentum in Q1. Both Statistics Malaysia's leading economic indicator and the manufacturing PMI rose to the highest levels since 2015 in February, though the latter remained in contractionary territory (below 50) at 49.4. This built on 2016 momentum, with GDP growth accelerating from a post-crisis low of 4.0% yoy in Q2 to 4.3% in Q3 and 4.5% in Q4. Strong increases in private consumption (6.2-6.4% yoy) supported the recovery over the period. Economic growth is forecast to rise marginally to 4.5% this year from 4.4% in 2016.

Bank Negara Malaysia (BNM) left its key rate unchanged at its March meeting despite a spike in headline inflation to a post-crisis high of 4.5% yoy in February, up from 1.8% in December. However, this was largely driven by a rise in transport costs and in fuel prices, reflecting higher commodity prices. The stabilisation of the oil price and controlled core inflation (2.5% against 2.1% in December) suggest BNM will look through the rise in the headline rate and keep policy unchanged. High household debt (90% of GDP) further justifies a cautious stance towards tightening.

BNM has also managed portfolio outflows prudently, reducing the need for hikes to prevent ringgit weakness. This is evidenced by stable interbank rates and bond yields amid 3.2% of GDP worth of fixed income outflows from August to February. The fall in the FX reserves was smaller than during previous outflow episodes as BNM intervened in the FX market using forwards, which gave it US dollar funds in exchange for a temporary local currency liquidity boost for domestic banks. Meanwhile, all transactions by residents must now be settled in ringgit, which should alleviate downward exchange rate pressure.

These measures and a recovery in commodity prices have helped stabilise the current account surplus, which had fallen from 5.7% of GDP in Q2 2014 to 1.9% two years later. In Q4, the surplus was 2.0% of GDP and projected to remain around this level for full-year 2017. The balance of payments and FX reserves are likely to be bolstered by the requirement that exporters convert 75% of exports earnings into ringgit, thereby improving resilience to external shocks.

Market Strategy: Malaysia's cyclical upturn and improved external buffers are concurrent with unchallenging valuations. The P/E premium over EM is one standard deviation below its long-term average. Profit margins are also the second highest in EM and earnings estimates are being revised upwards. We upgrade Malaysia from *neutral* to a small *overweight*.

Indonesia

Overweight

The growth outlook benefits from improving terms of trade but awaits the much-heralded increase in infrastructure spending. Rising inflation is likely to be transitory.

Indonesia's external balance has strongly benefited from the recent rise in commodity prices, notably in coal and palm oil. While the oil and gas balance has deteriorated of late, this too is likely to recover once the supply disruption due to a refinery shutdown is resolved.

While rising raw material prices provide an income boost to the economy, the resumption of higher growth will depend on the deployment of greater capital investment by both the private and the public sector. So far, indications from auto or cement sales are still soft and data on public infrastructure spending is not readily available. Indeed, in Q4 2016 GDP contracted 1.8% qoq, implying a softening of the headline rate from 5.0% yoy in Q3 to 4.9% yoy.

CPI moderated slightly in March as weaker food prices offset the increase in non-food prices, leaving the monthly change flat. In turn, this implied a decline of the headline rate from 3.8% yoy in February to 3.6% yoy in March. Higher commodity prices as well as a planned hike in electricity tariffs are set to keep upward pressure on CPI. This is expected to push the headline rate above the midpoint of Bank Indonesia's 3.0-5.0% target but keep it well below its ceiling. The mooted delay in the electricity price hike would reduce the likely inflation peak as readings would benefit from a higher comparison base a year earlier.

Consequently, Bank Indonesia has kept its policy rate unchanged at 4.75%, in line with expectations. The accompanying statement suggested that the central bank expects growth to recover in 2017 on the back of stronger domestic demand, amid a still-uncertain external environment. After six rate cuts in 2016, BI will likely remain on hold throughout 2017, all else equal.

Market Strategy: Indonesia has underperformed the MSCI EM by 4.5% in Q1 and its 19.2 P/E is at an 18% premium to EM. However, an improving external environment and firmer commodity prices will likely support the external balance. We maintain our *overweight* allocation.

Philippines

Neutral

Softer growth combines with firming inflation and a weakening external balance. However, to a large extent, these developments are signs of strength.

The growth momentum slowed somewhat towards year-end in the Philippines, although it beat market expectations once again and remains ahead of regional peers. At 6.6% yoy (1.5% qoq) in Q4, GDP decelerated from the (revised) 7.0% yoy pace recorded in Q3 and points the way towards a year of consolidation following the pre-election fiscal spending boom in 2016. Q4 growth continued to benefit from strong consumption and investment growth. Full year growth came to 6.8% and is expected to be somewhat softer, near 6.5%, in 2017.

But while the unemployment rate inched up to 6.6% in January, compared to 5.8% a year ago, the proposed income tax cut, the broadening of the VAT base and the planned rise in excise taxes bode well for a pick-up in 2018 growth and lay the foundations for an ambitious medium term infrastructure program.

Consumer prices continued their uptrend, rising to 3.4% yoy by March, up from 2.6% yoy in December. Rising commodity prices pushed up fuel prices, which are subject to further upside pressure from rising excise taxes as part of the tax reform plan. All told, inflation is expected to average close to the mid-point of the central bank's 2.0-4.0% target range in 2017. The BSP has kept its reverse repo rate on hold at 3.0% since early 2016, but its rhetoric has become more hawkish given the rise in the headline rate, a weakening external balance and the risks this implies for the exchange rate. If CPI readings start skirting the upper bound of the target range, the BSP could shift back towards tightening. Indeed, money market rates (91-day T-bill) have started to rise towards the BSP's new, narrow interest rate corridor.

The ongoing surge in capital goods imports - up 33% yoy in Q4 – have pushed the trade balance further into deficit (12% of GDP), leaving the current account balance slightly in the red (1.2% of GDP) for the quarter as a record high services surplus could not compensate for the large trade gap. The small current account deficit is likely to persist and rising capital outflows have undermined the balance of payments position despite strong remittances.

Market Strategy: Despite its strong economic performance, the Philippine market has strongly underperformed the MSCI EM since mid-2016 and recorded 5.3% points less than the index in Q1. The radicalised political landscape, the vanishing external surplus and the perennially expensive market (P/E of 20.5, equivalent to a 26% premium over the market) prompt us to maintain a *neutral* allocation.

Thailand

Neutral

Elections are planned for 2018, but the junta intends to retain a permanent role in national politics. Stimulus supports the economy, but structural reform remains absent.

With little sign of the military junta planning to relinquish power, it has instead released a 20-year National Strategy of economic priorities. While the junta may eventually hand over the day-to-day running of the government to civilians, the new constitution it has drafted and which has been approved by referendum, grants it a pivotal role into the far future. Elections are planned for 2018, but the junta will retain control over the Senate and several important committees. The "national priorities" are vaguely formulated, but will provide the junta cover should it decide to intervene when the government is seen as deviating from them. However, King Vajiralongkorn has not yet signed the constitution, demanding repeated amendments. His exact stance on the army's role remains as of yet unclear although an upcoming reshuffle will give him a chance to clear out potentially less supportive ranks.

While the junta has done little to advance the structural reforms it advocates in its National Strategy, it has been able to prop up the economic cycle through fiscal stimulus. As a result, GDP growth maintained the Q3 pace of 0.4% qoq, even though that meant a drop in the headline rate from 3.2% yoy to 3.0% yoy in Q4. In early 2017, the economy was supported by a rise in agricultural incomes thanks to rising commodity prices and subsidies, a key support for private consumption in the Thai economy. In addition, tourism revenues remained solid during Q1. In turn, a strong current account surplus, coupled with a moderation of capital outflows has pushed the balance of payments back into surplus and contributed to the regional outperformance of the Thai baht.

Inflation picked up in January to 1.6% yoy from the December reading of 1.1% yoy, but defied market expectations and moderated to 1.4% yoy in February. While oil prices pushed up the headline rate, softer food prices counteracted the impact. If commodity prices strengthen, CPI could head towards 2%, but is likely to remain below. The BoT has so far left its interest rate unchanged, at the low 1.50% level

Market Strategy: Thailand's market performance has oscillated in a +/- 3% point range relative to the index performance over the past three quarters (Q1 -2.9% relative to EM). While the cycle is likely to experience an uptick in the short term, the long term outlook remains as unclear as ever (with the junta's role seemingly becoming more entrenched). With valuations in line with the market, they do not provide an argument either way. As a result, we maintain our *neutral* allocation.

India

Overweight

Activity has remained resilient despite the demonetisation shock, while the BJP's election victory in Uttar Pradesh augurs well for reform implementation.

Despite the blunder of the November demonetisation which nullified the value of 86% of the currency in circulation, the BJP achieved a key victory in state elections in Uttar Pradesh, India's largest state, winning a 3/4 majority in the state assembly. The two developments taken together raise the question whether India is embarking on an era of decisive reform or instead risks falling prey to an illiberal autocrat.

The government is also proceeding on the introduction of a nationwide Goods and Services Tax (GST), which is to replace more than a dozen state taxes. It made further strides towards implementation in March, when four supplementary pieces of legislation were approved by the Lower House of parliament. These are now set to be discussed in the Upper House, but no further votes are required. The most recent bills indicated that there will be four separate rates set at 5% (for essential goods such as healthcare), 12%, 18% (luxury goods) and a 28% 'sin tax' on alcohol and tobacco. While the new system may seem unnecessarily complex, most food items will remain exempt from GST. Accounting for 50% of the CPI basket, this suggests that the inflationary impact of the tax will be limited. The legislation is currently only binding for five years, leaving scope for improving the regime in the future.

On the monetary side, the economy has begun to recover from the November demonetisation shock. Rising food prices and global commodity prices in general led to a sharp turnaround of inflation in February, with WPI surging to a three-year high of 6.6% yoy (from 5.3% yoy in January) and CPI, which is more insulated from global price movements, rebounding for the first time since the demonetisation move to 3.7% yoy (from 3.2% yoy the month prior).

Despite the demonetisation shock, activity remained resilient, with GDP growth recording a 7.0% yoy gain in Q3, only slightly down from 7.4% yoy posted in Q2. More recently, manufacturing and services PMIs have been on the rise for the two months up to March. Auto sales, which slumped during the November-December period, bounced back during January-February.

Market Strategy: India outperformed the index by 5.7% during Q1 and with a 22.6 P/E is one of the most expensive emerging equity markets. However, the economy appears to be overcoming the disruptions of the currency reform quicker than expected and India remains one of the few economies truly committed to undertaking positive structural reform. In addition, the government has bolstered its political support, thus becoming increasingly able to carry out its plans. We maintain our *overweight* allocation.

Latin America

Brazil

Neutral

The economy is on the path of recovery and declining inflation facilitates rapid rate cuts. But an unsteady political backdrop could derail much-needed reforms.

The political situation in Brazil remains febrile, with new revelations emerging every week. Only in March did the Prosecutor General in the 'carwash' probe open investigations into 83 politicians, six of which reportedly part of President Temer's cabinet. Separately, a new scandal involving 21 meatpacking plants said to have bribed health officials erupted.

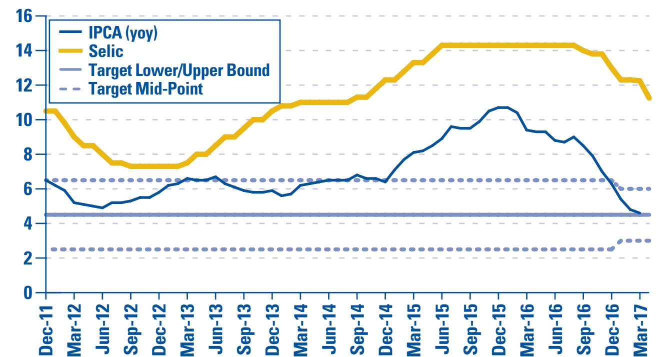
Yet, in the meantime the government successfully auctioned off four airports (at a higher price than expected) and Congress approved the outsourcing bill, which allows unrestricted outsourcing of jobs in the private sector and of most jobs in the public sector. However, the bill passed by a tight margin of 43 votes only, suggesting that support for reforms is waning and imperilling the passage of the pension system reform. The government already announced that it would not include state and municipal employees in the reform, in an apparent attempt to shore up support for the bill. It will be crucial to move the bill to the Senate within Q2 and the government will likely compromise rather than lose time.

GDP contracted a stronger than expected 0.9% qoq in Q4, but the slower pace of decline helped the headline rate, which posted a contraction of only 2.5% yoy, compared to -2.9% yoy in Q3. The contraction ranged across most sectors, with private consumption at -2.9% yoy, gross fixed investment at -5.4% yoy and exports down 7.6% yoy. Nevertheless, there are signs of improvement more recently: industrial production gained 1.4% yoy in January, up from -0.1% yoy in December, the first positive print since early 2014. Auto production has been rising strongly and sentiment data also firmed recently. However, unemployment has kept rising, recording 12.6% in January.

Headline CPI has surprised to the downside for six successive months, with the latest CPI reading slowing to 4.8% yoy in February, compared to 10.4% yoy a year earlier. The downward surprise stemmed from food prices, but with the disinflation process generally being broad-based, market analysts have marked down their expectations for year-end inflation to just above 4%, that is, below the midpoint of the BCB's target range.

As a result, the benchmark Selic rate, which was as high as 14.25% in mid-2016, was cut twice by 75bps during the past quarter, bringing it to 12.25%. Disinflation, together with a tightening of monetary conditions through the 10% appreciation of the real against the USD since early December 2016, will likely prompt the BCB to continue and perhaps accelerate its easing cycle. Private forecasters expect as much as 300bps in cuts by July (at a 100bps pace) and anticipate a year-end rate as low as 9%. However, the central bank has also explicitly made its actions contingent on progress with the government's structural reform plans. Recent signs of popular resistance and the widening of the corruption probe pose a material risk to the reform agenda, most notably on pensions.

Chart 4: Inflation and Selic Rate (%)



Source: Bloomberg

The government recently provided updated estimates on the performance of its 2017 budget, suggesting that it may fall Brl 58 bn short of plan. This partly reflects a downward revision of the 2017 GDP growth forecast from 1.6% to 0.5%, which implies a decline of projected tax revenues by Brl 34 bn. The government is contemplating a range of taxes to fill the gap but has not announced any measures yet.

The current account deficit remained contained to a 1.2-1.3% of GDP range during the past quarter as imports remained restrained, while exports have begun to benefit from strong agricultural output. Portfolio flows remain net negative on a 12-month basis, but net FDI inflows totalling 4.6% of GDP more than cover all financing needs and provide broad support for the currency.

Market Strategy: The Brazilian stock market's performance over the past quarter closely matched that of the MSCI EM, giving up much of the outperformance in the first half of the quarter during the second half. Nevertheless valuation metrics suggest that the market remains expensive as its 21.3 P/E runs 31% above the EM P/E (although this is less than the five-year average of 26.6). But the possible upside from political developments is receding given last year's ousting of President Rousseff and the current watering down of the pension reform. Instead, the maelstrom of corruption investigations continues to widen and candidates are set to begin jockeying for the 2018 presidential elections, with no clear market-friendly frontrunner visible yet. We thus maintain our *neutral* allocation.

Mexico

Neutral (↑)

The economy, led by a recovery of the peso, has begun to stabilise as the threat of disruptive trade measures by the Trump administration has begun to recede.

Mexico's economic and market performance have come to exemplify the turnaround in investor sentiment towards EM. To some extent, this reflects the general notion that the Trump presidency would turn out to be less disruptive in deeds than it is in words and specifically, that the threat to Mexico from a tearing up of NAFTA (say, in the form of a US withdrawal) has receded significantly. While some 'rebalancing' of the treaty remains on the cards, the tone of US officials has become much less adversarial recently. Indeed, Secretary of Commerce Ross Wilbur has indicated that negotiations would only begin at the end of the year and could take an indeterminate length of time (one year is seen as minimum). In turn, after declining by some 20% against the USD between November and late January, the peso has appreciated by 14% in the two months since, outperforming its EM peers.

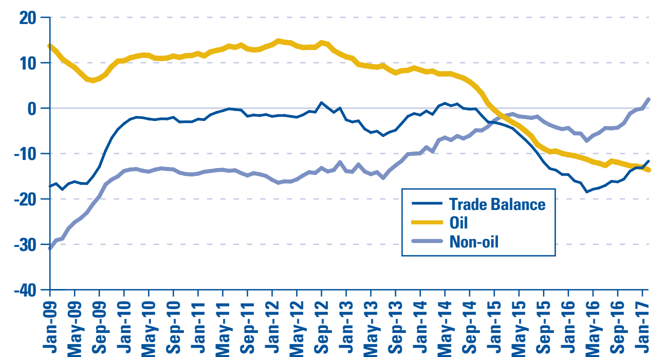
In response to the earlier peso slide, the central bank raised its key policy rate by 50bps in February and by another 25bps in March to 6.5%, for a total tightening of 175bps since the US election and bringing the policy rate to a post-crisis high. Together with calmer political rhetoric, this has helped stabilise the peso and lower inflation expectations. Inflation itself had increased significantly in the face of peso weakness as CPI rose at its fastest pace since 2010 in February, at 4.9% yoy, up from 3.4% yoy as recently as December. Pressure on consumer prices will likely prevail for some time as PPI prices are running at a high 9.5% yoy. These pressures could trigger further Banxico tightening but they are seen as transitory and are likely to dissipate soon. The central bank is therefore likely to begin signalling a formal decoupling from the US policy cycle.

Meanwhile, GDP growth picked up to 2.4% yoy in Q4, from 2.1% yoy in Q3, led by private consumption and export growth. More recent indicators suggest that industrial production remains lacklustre, but this mostly owes to the decline in mining output. Whereas domestic consumption softens against a background of higher inflation, the recovery of external demand (e.g. US factory orders) bodes well for non-manufacturing output. Auto production has been particularly robust and manufacturing PMIs have remained solidly in expansionary territory, with the March figure rising to 51.6.

Consumer sentiment experienced some of the sharpest declines on record early in the year. While stabilising energy prices and a recovery in the peso could change this sentiment, retail sales remain weak, declining in both December and January and prompting a drop in the headline rate from 9.0% yoy to 4.9% yoy in January.

Presidential elections are due by mid-2018 but until then three gubernatorial elections have to take place, including in the State of Mexico, the largest state, containing 13% of the population. The president's approval is currently at an all-time low, creating an opening for the opposition to push the PRI off its top spot, which it has held in the state since the1990s. Moran, the party led by two-time leftist presidential candidate Andres Manuel Lopez Obrador (AMLO) trails the PRI by only one percentage point in the polls.

Chart 5: Mexico's Trade Balance ($bn, 12-Month Rolling)



Source: Bloomberg

Market Strategy: The turn in investor sentiment benefitted the battered Mexican market significantly and led to a 4.6% point outperformance of the index during Q1 (after falling by nearly a fifth from November's US election through mid-January). Yet, the Mexican market remains vulnerable with a P/E of 24, both compared to its peers and relative to its own track record, with the five-year average running at a lower 22.6. Nevertheless, the recovery in external demand, the pre-emptive stance taken by Banxico and the receding threat from punitive trade measures prompt us to upgrade Mexico from *underweight* to *neutral*.

Emerging Europe and Africa

Russia

Neutral (↓)

Amidst a recovering economy and robust enough oil prices, the central bank remains decidedly on an easing course.

After two consecutive years of recession, Russia is expected to return to growth in 2017. During this difficult period, Russian policymakers responded with a tightening of fiscal and monetary policies, while letting the exchange rate adjust to the negative supply shock. As a consequence, following a steep fall in 2014, the ruble began to stabilise and appreciated some 45% against the USD from its low in January 2016. The economic contraction has continued to lessen, but year-end figures for 2016 are not available yet. What is more, industrial production figures have been subjected to sizeable revisions and now suggest a 0.8% decline in 2015 (compared to a previously reported 3.4%) and a 1.3% increase in 2016 (versus 1.1% before). Recent data points remain mixed and indicate a rebound in industrial production by 2.3% yoy in January, up from 0.2% yoy in December. By contrast, manufacturing PMIs remain elevated even though the February reading softened to 52.5 from 54.7 in January. In line with its conservative planning, the government projects 2017 growth of 0.6%, based on an average oil price of $40/brl. However, with oil prices above $50/brl, growth could accelerate to 2%.

Headline inflation has extended its steep descent, with February CPI recording 4.6% yoy, down from 5.0% yoy the month prior. While food prices exhibited the largest decline, the CPI slowdown is broad-based. After a six-month hiatus the CBR judged that low inflation momentum and the strong RUB allowed further monetary easing, cutting the key rate by 25bps to 9.75%. This now almost fully unwinds the emergency hikes of late 2014. However, if favourable conditions continue to prevail, the CBR could eventually return to the levels prior to 2014 at 6% or less. For now, it tries to temper expectations and suggested future steps would be undertaken in 25bps increments and be data-dependent. Another 100bps or more of total easing appear nevertheless likely this year.

Market Strategy: The Russian market gave up a good deal of its 22.3% gains of Q4 and posted a 16.1% loss in Q1. With additional gains in oil prices likely limited (if not reversed) and foreign relations again beginning to tense up, any upside is limited. We revert our temporary *overweight* allocation back to *neutral*.

Turkey

Underweight

The economic outlook for Turkey remains hostage to domestic political developments and the prospect of rising US rates.

Against the background of strong market performance in Q1 2017, Turkey stands out from many of its EM peers. Its currency weakened sharply over the past year and missed out on this year's market rally, while inflation recently moved back above 10%. And even though domestic growth remained languid, this has forced the central bank to keep tight tabs on liquidity, further strangling activity.

In addition, political tensions both domestically and abroad remain high as Turkey is gearing up for its April 16th referendum that is to pave the way to a shift to a presidential regime. In the run-up to it, the government continues to interfere with domestic media outlets, tried to mobilise Turkish citizens abroad to support a 'Yes' vote and soured relations with its EU partners. While polls point to a majority of 'No' vote, the large share of undecided voters makes it difficult to predict the ultimate outcome. A presidential system under Erdogan would likely subsume economic policies under political priorities and lead to more populist policies.

Following a sharp GDP contraction of 1.8% in Q3 in the wake of the failed coup attempt which dented already fragile consumer sentiment, activity picked up again in Q4 as industrial production gained 4.2% yoy at the latest reading in January and capacity utilisation stood at 75.2%. Similarly, the central bank's real sector confidence index rose sharply in February. Exports recovered strongly and the government's tax cut on consumer durables and furniture as well as the cancellation of social security payments for newly employed helped stabilise and revive domestic demand.

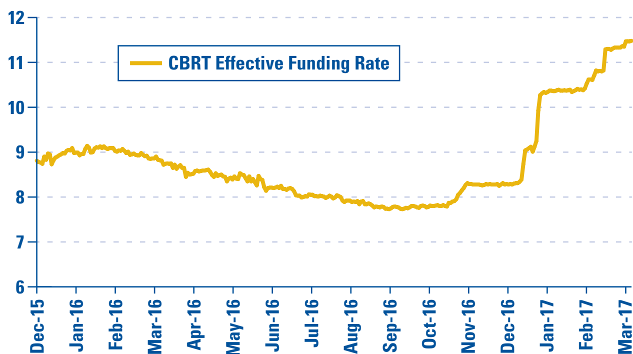
On the other hand, these stimulative measures have undermined budget performance, which is witnessing a sharp drop in tax revenues and a rise in primary spending, leading to the highest February deficit since 2009. As a result, the full year outcome appears headed for a deficit near 3% of GDP, up from an estimated 1.1% of GDP in 2016, PM Yildirim's assurances that this would not be the case notwithstanding.

Inflation remains beyond the central bank's grasp as it continues to surprise on the upside and even moved into double digit territory for the first time in five years. After ending the year at 8.5%

in 2016, CPI moved up to 10.1% yoy in February, partly due to adverse base effects. But in addition to rising food prices, core prices have also begun to shift upwards in response to exchange rate pass-through. While relative lira stability during the first quarter (given a weakening US dollar) will benefit inflation dynamics compared to 2016, CPI could still end the year near the 10% mark, sharply above the central bank's 5% target.

As a result, real policy rates have moved into negative territory, giving the central bank plenty of scope to tighten policy. Yet, the CBRT has left its key one-week repo rate unchanged since it raised it to 8.0% in November 2016, tightening only its other monetary policy instruments such as the late liquidity window (LLW) rate, which it raised by 75bps to 11.75% in March. Having stopped providing funding through the other facilities and tightening the LLW rate successively over the past months, the CBRT has driven the effective funding rate up more than 200bps since the start of the year.

Chart 6: CBRT Effective Funding Rate



Source: Bloomberg

Market Strategy: Turkey has underperformed the MSCI EM for four successive quarters. While the market remains cheap at a 9.7 P/E, rising political uncertainty domestically paired with the risk of even more populist policies, its strategic entanglements in the Middle East, souring relationships with EU partners and rising international interest rates pose a significant challenge to achieving anything more than temporary market outperformance. We maintain our *underweight* allocation against that context.

Romania

Neutral

Growth is likely to remain strong, but slow from the post-crisis high in 2016. Meanwhile, fiscal deterioration is likely to push the central bank towards tightening policy.

Romania's GDP rose by 4.8% yoy in Q4, up from 4.3% in Q3. The main growth driver continued to be household consumption (6.3% yoy), while export growth (10.9%) outpaced that of imports (8.6%) for a second consecutive quarter. However, net exports are expected to act as a drag on GDP this year as EU demand wanes and imports stay strong, pushing down growth to 3.7% from last year's post crisis high of 4.9%. Meanwhile, the current account deficit more than doubled from 1.2% of GDP in 2015 to 2.5% in 2016 and a further deterioration to 3.0% is projected for 2017.

Household consumption is supported by robust wage growth (14.7% yoy in February). Real wages have risen by double digits since November 2015 amid deflation. Consumer prices have begun to rise this year, but yoy changes remain close to zero (0.1% yoy in January and 0.2% in February). National Bank of Romania project inflation to rise to 1.7% in Q4 as the 2016 VAT cut drops out of calculations, moving within the 2.5% +/- 1% target range in Q1 2018. This means that the Bank is likely to become increasingly hawkish during the rest of 2017.

Fiscal loosening and its likely inflationary impact is also set to push monetary policy towards a hawkish tilt. Parliament passed the 2017 budget in February, with the IMF forecasting the deficit to widen by 1.3 percentage points this year to 3.7% of GDP. The IMF recommended a moderation in wage and pension growth and limiting tax cuts in order to prevent Romania from breaching the EU's 3% of GDP limit. At present, the government appears more likely to keep its fiscal easing in place in order to appease the population following mass protests in January.

Market Strategy: Romania's favourable economic backdrop of strong growth and low inflation is likely to remain in 2017. The P/E discount to EM of 18% is also below its long-term average of 9%. However, the risk of fiscal slippage is significant and in our view counterbalances the positive factors, so we keep our *neutral* weight.

South Africa

Underweight

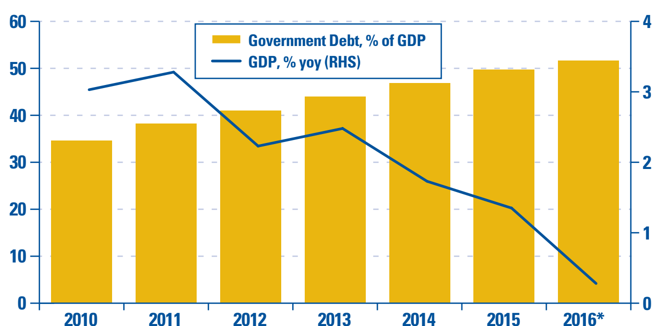
President Zuma's cabinet reshuffle raises the risk of economic mismanagement even as economic indicators began to improve.

President Jacob Zuma undertook a significant cabinet reshuffle in March, with the main casualty being the well-respected Finance Minister Pravin Gordhan. The reshuffle was broad-based, including replacements for the ministers of energy, transport, police, home affairs, public works and tourism and six deputies. The lack of experience in the new administration and the maintenance of underperforming cabinet members does not augur well for future policy, in our view.

S&P subsequently downgraded South Africa's long-term foreign currency rating to non-investment grade (BB+) and the outlook was left as 'negative', implying that further downgrades remain a risk. The reshuffle has been called the "Gupta coup" as the changes are seen as a way to facilitate previously blocked policies that would benefit the Indian-South African family, who have a close relationship with the president. Indeed, the ratings change was driven by the consequent increased likelihood of a rise in contingent liabilities for the government.

Meanwhile, political risk has risen on a number of fronts: 1) the reaction of key groups within in the ANC network has been negative, including the trade union group COSATU which has been a key ally and support in the ANC's campaigns and Cyril Ramaphosa, frontrunner to lead the party into the 2019 election. This raises the risk of a split within the ruling party; 2) opposition parties have called for a 'no confidence' vote and are likely to push reformist ANC members to support the motion when parliament returns in April/May and 3) President Zuma has chosen to exert his power via the reshuffle, a potential signal that he is determined to get his chosen candidate to win the ANC leadership in December's election. As the president tries to secure support, the risk of policy mismanagement through to year-end has risen. Under Zuma's leadership, since his election in 2009, conditions have deteriorated (see chart).

Chart 7: Economic Performance Under Zuma



Source: Bloomberg

Amid the political drama, economic conditions have improved in South Africa. Manufacturing PMI has been in expansionary territory (above 50) year to date having been in contraction for most of 2H16. BER Business Confidence also rose to 40 in Q1, implying that 40% of businesses are satisfied with current conditions, up from 36% a year earlier and driven by an 11 point rise among retailers to 45.

External accounts have also improved, with the current account deficit narrowing to 1.7% of GDP in Q4 against 4.9% a year earlier. This was driven by a sharp narrowing of the trade deficit from 4.1% of GDP to 0.3% over the period. The trend is set to continue as the monthly trade balance moved into surplus for the first time 2012 in January and February. South Africa's export sector has benefited from the recovery in commodity prices over the past year, with exports rising by 16.9% yoy in February.

However, domestic demand remains weak and this was reflected in a 22.1% yoy fall in imports in February. Personal consumption is being hampered by a weak labour market. Unemployment remains elevated at 26.5% in Q4 and the youth jobless rate is above 50%. Households have also deleveraged since the global financial crisis. Debt to disposable income has fallen each quarter for the past three years and was 73.4% in Q4 from a peak of 87.8% in 2008. These factors are strong headwinds to household consumption, which accounts for 60% of GDP and has shown signs of further deterioration recently. Retail sales fell by 2.3% yoy in January, the steepest decline since crisis and well below the projected 1.1% expansion. This was followed by a 1.7% fall in February, the first time since the crisis that retail sales have declined for two consecutive months.

The South African Reserve Bank (SARB) has kept its key policy rate at 7.0% for the past year as inflation fell from a peak of 7.1% yoy in February 2016 to 5.9% in August, within the Bank's 3-6% target range. Although inflation has risen to 6.3% in February this year, strength in the trade-weighted rand (+14% yoy) is set to reduce inflationary pressures and core inflation also remains under control at 5.2%, the lowest level in over a year. It therefore seems likely that the SARB will keep its policy rate unchanged in Q2. However, further tightening could be forthcoming if the rand continues to weaken materially, which would push up the central bank's inflation projections.

Market Strategy: South Africa's improved economic backdrop would justify an upgrade to *neutral*, in our view. However, we keep our *underweight* at least on a tactical basis as we see how the political situation unfolds over the coming months. President Zuma's government reshuffle risks jeopardising the economic progress made so far and we see further downside relative to EM as South Africa's P/E premium is close to its long-term average and the potential deterioration in governance could warrant a higher risk premium. ◆

Michael Hart and Lyndon Barreto, CFA, April 2017

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KEY ECONOMIC AND FINANCIAL INDICATORS

		Macroeconomic Data											Market Data							
		% change on year ago			Latest 12 months								Performance				Forecast			
	Emerging Market	Annual GDP Growth	Industrial Production	Consumer Price Index	Trade Balance	Current Account Balance	Foreign Reserves 2017 Latest	Foreign Reserves 2016 Year ago	Currency vs $ 2017 Latest	Currency vs $ 2016 Year ago	Short-Term Interest Rates	Sovereign Rating S&P	% S&P/EM Frontier Super Composite BMI	Stock Market Index S&P/EM Front. Super Comp. BMI US$	Change since 12/31/16 US$	Change since 12/31/16 Local Currency	2017 P/E Forecast	EBIT Margin 2017 Forecast	6 month Stock Market Index Estimate (Front. Super Comp. BMI) US$	3 month Currency vs $ +/-
		%	%	%	$ Bns	$ Bns	$ Bns	$ Bns			%		Mar. 31, 2017	Mar. 31, 2017	%	%		%		
Overweight	INDIA	7.0	2.7	3.7	-99.8	-11.9	339.94	326.63	65.05	66.06	6.5	BBB-	10.46	953.15	19.79	14.64	20.7	14.1	830	-
Overweight	INDONESIA	4.9	4.5	3.6	10.4	-16.3	111.31	96.70	13329.00	13144.00	6.4	BB+	2.23	1364.72	5.82	4.66	16.2	22.4	1351	-
Overweight	SOUTH KOREA	2.4	6.6	1.9	85.7	96.8	364.58	357.86	1118.21	1152.45	4.6	AA	15.05	469.14	16.44	7.89	9.5	10.7	407	-
Overweight	TAIWAN	2.9	10.6	-0.0	48.7	70.9	437.66	428.82	30.39	32.38	0.7	AA-	11.69	246.11	13.17	6.58	13.3	8.3	217	-
Overweight	CHILE	0.5	-7.6	2.7	3.9	-3.6	39.54	37.21	658.12	669.74	3.8	AA-	1.32	477.96	15.59	14.26	17.8	13.9	409	-
Overweight	MALAYSIA	4.5	3.5	4.5	20.9	5.9	91.73	92.49	4.43	3.90	2.9	A-	2.39	351.71	9.67	8.18	16.8	19.3	324	-
Neutral	ARGENTINA	-2.1	-6.0	14.3†	2.0	-15.1	45.59	23.12	15.45	14.75	18.1	B-	0.60	590.52	32.63	28.90	15.4	17.6	414	-
Neutral	BAHRAIN	3.9	n.a.	0.4	n.a.	n.a.	2.65	3.08	0.38	0.38	1.5	BB-	0.14	154.48	21.88	21.87	n.a.	n.a.	128	uc
Neutral	BRAZIL	-2.5	1.4	4.8	51.0	-22.8	360.51	350.74	3.12	3.59	8.0	BB	6.64	629.56	11.17	8.45	12.3	18.3	566	-
Neutral	CHINA	6.8	6.0	0.8	465.0	196.4	3005.12	3202.32	6.88	6.48	1.1	AA-	24.41	702.37	11.92	12.12	12.7	11.6	633	-
Neutral	COLOMBIA	1.6	-0.2	5.2	-11.2	-12.5	45.27	44.81	658.12	669.74	6.7	BBB	0.58	5575.74	5.27	1.48	12.5	n.a.	5134	-
Neutral	CZECH REP.	1.9	9.6	2.5	19.9	2.0	110.21	68.77	25.39	23.73	0.1	AA-	0.14	699.02	6.97	5.50	14.9	n.a.	668	+
Neutral	EGYPT	3.8	-1.1	30.2	-34.9	-19.4	21.69	12.07	18.07	8.88	14.8	B-	0.19	1264.34	6.24	5.78	11.9	n.a.	1247	+
Neutral	GREECE	-1.1	7.2	1.3	-18.6	0.0	1.62	1.41	1.07	1.14	0.1	B-	0.37	26.28	2.46	1.23	21.5	18.6	26	-
Neutral	HUNGARY	1.6	1.6	2.9	11.0	6.2	26.11	34.06	289.70	273.97	0.1	BBB-	0.24	424.41	-0.39	-1.78	11.2	n.a.	420	-
Neutral	KENYA	5.7	n.a.	10.3	-8.4	-47.6	7.85	7.14	103.25	101.55	7.3	B+	0.11	555.64	-0.62	-0.15	10.1	23.1	585	-
Neutral	KUWAIT	1.8	n.a.	3.2	57.2	5.9	28.78	26.00	0.31	0.30	1.3	AA	0.55	71.25	10.53	10.33	13.0	n.a.	63	-
Neutral	MEXICO	2.4	-0.1	4.9	-11.7	-26.5	170.07	169.74	18.72	17.44	6.9	BBB+	3.11	437.20	15.84	5.97	18.0	14.6	364	-
Neutral	MOROCCO	0.9	0.8	1.6	-18.3	-7.8	23.73	21.87	10.06	9.61	3.3	BBB-	0.25	522.67	-2.49	-3.32	17.5	25.8	548	-
Neutral	PAKISTAN	5.7	0.8	4.9	-29.2	-3.6	17.62	16.44	104.84	104.75	4.5	B	0.37	1034.84	-0.85	-0.42	10.8	n.a.	1101	-
Neutral	PERU	3.0	3.9	4.0	1.8	-5.5	59.92	59.99	3.24	3.36	0.5	BBB+	0.46	1600.21	5.46	4.92	12.8	n.a.	1471	-
Neutral	PHILIPPINES	6.6	9.3	3.3	-24.2	0.6	72.14	72.05	50.20	46.21	2.5	BBB	1.29	819.98	5.98	6.96	18.0	23.0	799	-
Neutral	POLAND	2.7	1.2	2.0	1.9	-1.4	105.64	93.74	3.98	3.72	1.7	BBB+	1.14	308.51	18.21	12.21	12.1	13.3	259	-
Neutral	QATAR	1.7	n.a.	0.7	27.6	-5.4	32.46	35.53	3.64	3.64	1.7	AA	0.70	254.81	0.91	0.91	12.8	n.a.	245	uc
Neutral	ROMANIA	4.7	5.5	0.2	-11.2	-24.3	35.22	33.61	4.27	3.92	0.8	BBB-	0.11	101.41	15.04	13.70	10.0	14.5	90	-
Neutral	RUSSIA	0.3	-2.7	4.6	0.1	25.0	320.92	313.47	56.34	68.37	10.0	BB+	3.69	426.29	-1.97	-8.10	6.2	16.6	425	-
Neutral	SLOVENIA	2.6	3.3	1.9	0.8	3.0	0.25	0.37	1.07	1.14	0.3	A	0.05	353.69	6.60	5.12	12.5	12.3	337	-
Neutral	SRI LANKA	5.3	-3.4	7.3	-9.1	n.a.	4.53	5.42	152.00	145.20	11.4	B+	0.07	258.67	-3.24	-1.73	10.5	15.3	269	-
Neutral	THAILAND	3.0	-1.5	0.8	34.0	44.5	174.80	159.82	34.37	35.25	1.5	BBB+	2.46	1076.74	7.35	3.04	14.9	11.3	997	-
Neutral	UAE	3.8	n.a.	1.9	89.4	21.6	78.88	80.50	3.67	3.67	1.0	AA	0.80	120.42	1.36	1.36	11.7	n.a.	120	uc
Neutral	VIETNAM	5.1	5.5	4.7	-2.5	6.4	37.24	30.63	22715.00	22296.00	4.8	BB-	0.31	148.37	12.05	11.97	19.1	19.5	136	-
Underweight	SOUTH AFRICA	0.7	0.8	6.3	1.1	-39.7	39.08	37.94	13.64	14.71	7.2	BB+	5.68	696.48	4.51	2.47	17.3	11.3	630	+
Underweight	NIGERIA	-1.3	n.a.	17.8	-1.9	-1.4	28.59	27.61	306.60	199.25	10.4	B	0.19	137.98	2.00	-0.89	7.2	-10.4	124	-
Underweight	TURKEY	3.1	2.6	11.3	-57.0	-33.2	89.47	92.23	3.64	2.81	11.9	BB	1.04	360.18	10.15	14.03	8.5	12.6	331	-
	OUT OF INDEX																			
	SAUDI ARABIA	1.2	n.a.	-0.1	28.8	-1.2	514.09	589.65	3.75	3.75	1.3	A-	0.00	106.57	-2.28	-2.32	15.6	16.6	108	uc

Note: All data shown are as at 31 March 2017 unless stated otherwise. †Unofficial estimates suggest annual inflation is between 40% and 50%. UC is unchanged (currency versus US dollar). S&P credit 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 98.8% of the S&P/EM Frontier Super Composite BMI on 31 March 2017. An additional 24 countries accounted for the remaining 1.2% 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, Jordan, Kazakhstan, Latvia, Lebanon, Lithuania, Mauritius, Namibia, Oman, Panama, Slovakia, Trinidad & Tobago, Tunisia, Ukraine and Zambia.

Source: Bloomberg, City of London Investment Management

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