EMERGING MARKETS

The latest meeting of the G20, hosted by India, was capped by an important US-Vietnam partnership deal, underscoring the importance of 'friend-shoring' and 'near-shoring' strategies pursued by the Biden administration. The Vietnamese government has wasted little time capitalizing on the attention the country has received. It has been actively working to stimulate the economy while the issues that overshadowed the market last year have largely been addressed. Much of this year's momentum has been driven by domestic retail activity whereas foreign premiums - where they exist - are still low. We believe there is still room for further upside, even in the face of a slowing global economy.

China continued to dominate headlines in the third quarter. Despite a modest reprieve in July, equity markets continued their poor form, reacting to negative economic data and piecemeal stimulus measures. Investors withdrew a record $15 billion out of Chinese stocks in August alone, the largest monthly outflow since 2015. Fixed income assets fared little better, with over $5 billion in outflows in August. Chinese banks and property developers continue to play the part of the bogey man for the country's growth prospects. While the government has taken steps to remedy some of the issues by lowering capital ratio requirements and the interest rate burden for first-time home buyers, the property sector has a long way to go before finding a footing. Just as indispensable is China's small business ecosystem, which makes up 60% of China's economic output and is responsible for 80% of new jobs. Small enterprises have been systematically stymied by government lockdowns and credit crackdowns, but China's youth unemployment problems and challenging demographics means making such businesses a part of the solution more eminent.

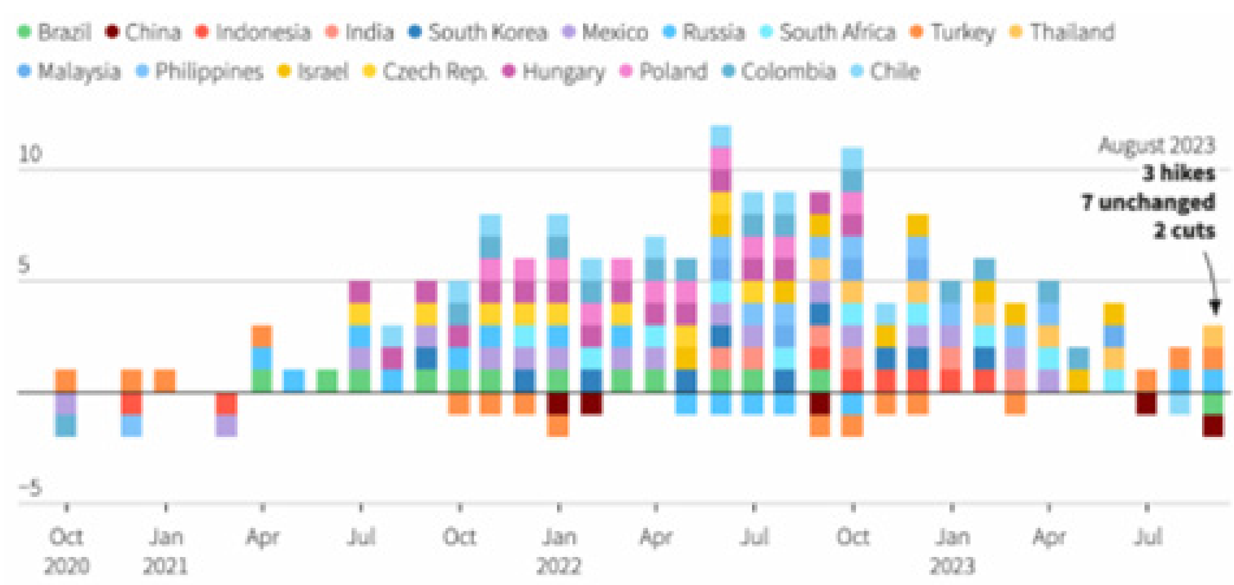
But it wasn't all bad news coming out of China. The quarter was capped by a speech by President Xi Jinping at a study meeting of senior leadership, where he emphasized the benefits of China's participation in the WTO and pledged to further open the country to foreign investors. More interestingly, the Chinese leader said relatively little on issues related to external and domestic security, a trademark of previous speeches. While nuanced, this shift in tone does serve as a belated acknowledgement that not all is well and that a course correction is badly needed. One source of confidence may come from third quarter corporate results which will begin their rollout later in October. We expect earnings to reflect strong consumption patterns on the back of the recent 'golden week' holiday, where both the Mid-Autumn Festival and National Day were celebrated in tandem. Data going into the holiday period looked promising. For instance, Chinese online travel operator Trip.com reported that airline booking volume rose nearly five times year-over-year and that hotel booking volume had increased by more than eight times. Similarly, China railway expected close to 200 million train trips would be taken over the extended holiday break. In a bid to boost consumption, many cities across the country issued 'consumption vouchers' at local shopping centers and markets. Even before this important holiday, there were signs the Chinese consumer was still open to spend, albeit differently, as evidenced by the impressive rally in discount online retailer Pinduoduo. Perhaps this is not surprising. The last time US consumers downgraded their spending habits, great companies like Walmart were born.

Elsewhere in emerging markets, a subset of central banks showed a willingness to cut rates after a series of aggressive hikes in 2021 and 2022 (Figure 7). Chile, Brazil, and Hungary began their rate cutting cycles during the quarter in the hopes of an uptick in economic consumption. Expectations were that other central banks would follow as inflation abated. However, in the face of the Fed's 'higher-for-longer stance', most EM central banks have opted to keep policy rates unchanged or have continued to hike, particularly those with currencies sensitive to higher US interest rates and higher energy prices.

Indeed, the USD has shown significant strength against EM currencies, clawing back losses from earlier in the year following the Fed's September FOMC. Predictions of broad-based monetary easing across emerging markets may prove an exaggeration, or at the very least premature.

It was also a summit heavy quarter in emerging markets. The annual BRICS summit drew headlines for expanding membership to Saudi Arabia, Iran, Ethiopia, Egypt, Argentina and the United Arab Emirates, a largely symbolic move meant to underscore dissatisfaction with the current dominance of the US in the global financial system but an important development, nonetheless. Talk of moving away from the USD as the de facto currency for trade and financial settlements, while impractical in the short term, is a further development to monitor. As we previously wrote, new members may help BRICS symbolic presence grow, but it is unlikely that they will help the bloc transform into an effective and coherent group any time soon.

Figure 7. Monthly count of Emerging Markets hiking or cutting rates



Source: Refinitiv Datastream.