Emerging Markets

Country Risk Analytics

MacroFinance Research

Quarterly - 2024Q1

TAC ECONOMICS

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Global Views on Emerging Markets

Executive Summary

→ **EM economic performances improved in 2023** thanks to post-zero Covid reacceleration in China and significant disinflation supporting domestic demand in other EM, with large divergence between underperformers (Poland, South Africa) and overachievers (India, Mexico, Turkey). Yet, persistent geopolitical tensions and US Fed policy tightening led to large pressures on EM interest rates' easing cycle and exchange rates.

→ **Drivers of economic growth will have an heterogenous impact on EM** depending on their resilience and interdependence. Reduction in inflationary pressures will become more gradual in line with more balanced global oil prices; spillover from China cyclical acceleration will be limited by the domestic focus on consumption and technology; and geopolitical tensions may be exacerbated by large political uncertainties as 34 out of 100 EM will have elections and/or referendums in 2024.

→ **Overall EM GDP growth should decelerate modestly in 2024** (to +3.0% y/y on average per quarter), **followed by a more convergent recovery towards 2025H1** (+3.8%). Differences across groups and regions will persist: weighted-average GDP growth for 10 Key EM will be 100pp higher, while Asia is expected to have stronger growth compared to Latin America and EM Europe. In parallel, most EM are expected to experience further albeit limited disinflation, with notable exception in China and Russia. Along with the expected turn in US Fed policy, EM central banks will start or continue to reduce interest rates in 2024, but at a slower pace than previously anticipated to lessen risks of financial volatility.

→ **Country risk measures steadily deteriorated in 2023** with increasing differentiation across countries, groups, and counterparties. In particular, Economic & Financial Risk ratings jumped and global risk aversion wedged at a high level, thus suggesting a cautious strategy in operating and/or expanding investments. Broad risks for corporate sector are generally higher in relatively larger economies because of lingering effects of mediocre cyclical performances, while relatively smaller economies display less favorable sovereign risks. Lastly, risks for the banking sector are concentrated in many Sub-Saharan African economies and Russia.

GDP Growth and Inflation in 10 Key EM
% y/y

	GDP Growth					Inflation				
	2021	2022	2023	**2024**	**2025H1**	2021	2022	2023	**2024**	**2025H1**
Brazil	4.8	3.0	3.1	**1.7**	**2.3**	8.3	9.3	4.6	**4.0**	**4.0**
China	8.4	3.0	5.2	**4.6**	**5.7**	0.9	2.0	0.5	**1.6**	**1.9**
India	8.9	6.7	7.0	**6.2**	**7.3**	5.1	6.7	5.7	**5.0**	**4.7**
Indonesia	3.7	5.3	5.1	**5.0**	**5.2**	1.6	4.2	3.7	**3.0**	**3.0**
South Korea	4.3	2.6	1.3	**2.1**	**2.4**	2.4	5.1	3.6	**2.3**	**2.2**
Mexico	5.7	3.9	3.4	**2.3**	**2.2**	5.7	7.9	5.6	**4.1**	**3.5**
Poland	6.8	5.5	0.1	**2.7**	**3.3**	5.2	14.3	11.6	**5.2**	**4.9**
Russia	5.6	-2.1	2.5	**1.5**	**1.2**	6.7	13.8	5.8	**6.5**	**5.0**
South Africa	4.7	1.9	0.5	**1.1**	**1.2**	4.6	6.9	5.9	**5.1**	**4.6**
Turkey	11.4	5.5	3.9	**2.5**	**3.1**	19.4	72.0	53.5	**55.4**	**32.0**
10 Key EM (GDP weighted)	7.5	3.3	4.6	4.0	4.8	3.2	6.6	4.0	4.3	3.6

Source: TAC ECONOMICS DataLab

1. 2023: normalization of post-Covid cyclical performances

2023: normalization of post-Covid cyclical performances

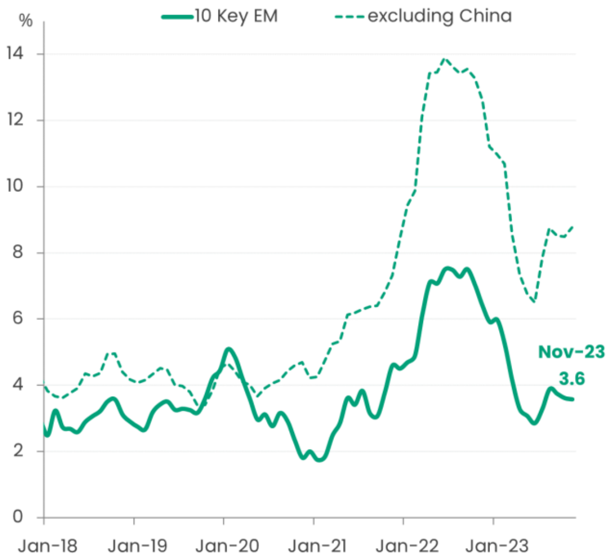
Cyclical developments in emerging markets and developing economies (EM) during the second half of 2023 were characterized by steady though unimpressive performances.

We estimate that GDP growth for all EM has stabilized at +3.8% y/y in 2023H2 after 3.9% in H1 and 4% in 2022. This is a result of much lower traction from China and international trade, and a stronger resilience of domestic demand, supported by the disinflationary trend and the end of the 2021-22 policy tightening.

Indeed, the soft growth profile, the stabilization / reversal in commodity prices, and the tighter monetary policies engineered in 2022 have allowed overall inflation rates in emerging markets to moderate in the second half of 2023. Divergences among large EM has remained huge, from China's closeness to deflation (+0.2% y/y increase in China's consumer price index estimated in 2023H2) to Turkey's battle against uncontrolled price spiral (+60% y/y in 2023H2). However, a positive development is the expected "convergence", i.e. China progressively exiting deflationary risk and Turkey applying orthodox breaks on runaway inflation.

EM activity: Industrial production, 10 Key EM
% y/y, weighted average

EM inflation: Consumer Price Index, 10 Key EM
% y/y, weighted average



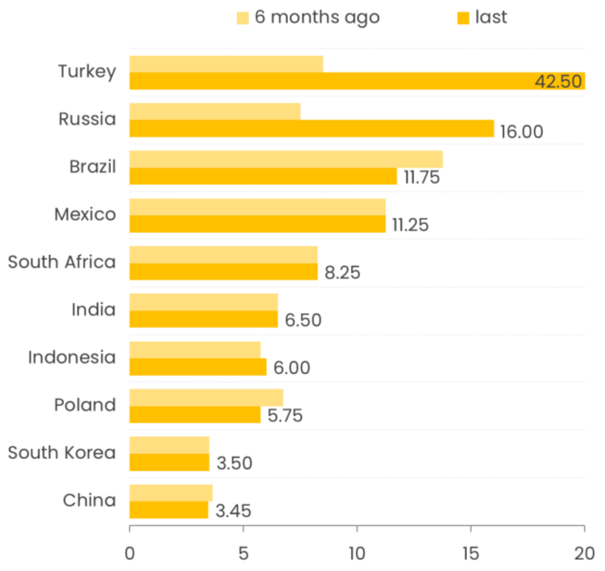
Sources: TAC ECONOMICS

Declining inflation and the announced pause in US / Eurozone tightening cycle has enabled the initial cuts in interest rates, particularly in countries where monetary reaction was earlier and/or stronger, e.g. Brazil, Chile, Hungary, and Peru. However, the decline in inflation remains insufficient to bring it within central banks' targets in many EM (with stronger stickiness for the politically sensitive food prices), while uncertainties on the 2024 timing of monetary easing in the US remain substantial, pointing therefore to greater caution in EM.

In a broad context of large volatility on international bond markets, abrupt swings in global markets' expectations, and persistent geopolitical disruptions, financial conditions in emerging markets remained volatile in the second half of 2023. Capital flows were substantially influenced by the combination of tense US-China relations (persistently large capital outflows from China) and a reappreciation of global risk (reduced aversion) favoring inflows into the other large EM, in particular India and Turkey. Using an average for the 10 Key EM[1], these developments led to a broad stabilization in exchange rates, coming after a cumulative 40% depreciation (against USD) since early 2022 and the beginning of the global monetary-tightening cycle.

EM policy interest rates, 10 Key EM

%



EM exchange rates, 10 Key EM

Overall index, against USD

Sources: TAC ECONOMICS

2. Complex combination of structural drivers

As always, the overall outlook for EM is dependent on critical assumptions on world / exogenous developments:

Cyclical and financial dynamics in mature economies

In 2024, the global economic landscape witnesses a deceleration in growth, with the United States displaying resilience despite consumer spending trends that fall short of preventing an economic slowdown. This resilience, however, is expected to confirm a mild recession scenario, with an anticipated trough in the first half of 2024.

In the Eurozone, GDP growth is projected to experience broad stagnation influenced by divergent forces, including a negative external environment, tightening conditions, and a potential rebound in real income. The prevailing trend indicates disinflation in 2024, with return to central banks' target by mid-2024. Base effects from energy and food prices and good deflation may contribute to disinflation, yet the inertia of service prices is anticipated to maintain elevated core inflation.

Central banks are expected to have reached peak interest rates, with a policy easing expected in Q22024. Anticipated weaker economic data, coupled with a shift in monetary policy direction and an expected softening in core inflation, suggest a potential easing of long-term yields in the coming months. This deceleration, however, is forecasted to be limited due to the looming risk of overheating in 2025. As 2024 unfolds, it emerges as a pivotal year setting the stage for a potential regime change.

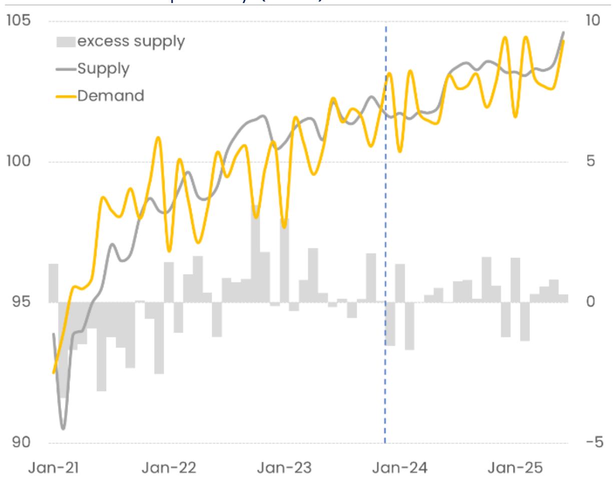
[1] The 10 Key EM are: Brazil, Mexico, Russia, Poland, Turkey, South Africa, India, China Indonesia, and South Korea. They account for approximately 70% of total GDP of all Emerging Markets and Developing Economies.

Oil and commodity prices

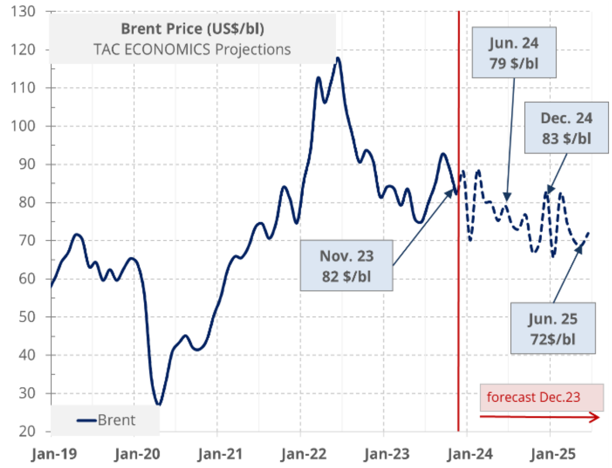
In line with our previous analyses on oil markets, supply restrictions have continued catching up with softening demand, itself a complex result of weak aggregate manufacturing and construction activity, and structural decline related to climate change issues. Despite repeated cuts in production by OPEC+ producing countries, the sharp increase in US production (+2 mbd over the past 18 months) and stabilizing demand have prevented prices from rising significantly despite the ongoing geopolitical crisis that followed Hamas attack in Israel and Israel retaliation offensive.

Overall, our quantitative models and our scenario for overall changes in demand and supply confirm our analysis of a market that remains "just balanced" with demand more volatile than supply, leading to occasional bouts of price pressures in a broad declining trend. Brent prices would move towards around 70$/bl during 2024, before larger oscillations around a trend stabilization in 2025H1.

Oil market balance: outlook for demand and supply
millions barrels per day (mbd)



Oil prices: projections to June 2025
Brent price, US$/bl



Sources: TAC ECONOMICS

Overall, both oil and other commodity prices are expected to become "more neutral" in broader inflationary pressures, with limited decline but no upward trend either.

Alber's comments on commodity prices[1]

Iron Ore: The outlook for iron ore prices in 2024 is expected to remain volatile, with prices largely dependent on Chinese policies and economic stimulus measures. The downside risk for iron ore prices in 2024 is if the stimulus effect is weaker than expected. However, with China ramping up investment in infrastructure and manufacturing, it should boost demand for steel and support iron ore prices. The outlook for 2025 is uncertain, as it will depend on factors such as China's economic recovery and government policies.

Aluminum: The global aluminum market is expected to be in a small surplus in 2024, with China driving most of the global production increase. However, restarts in Europe are not expected until 2025. The outlook for aluminum prices in 2024 is expected to be supported by China's green energy drive and the need for metals that are key to renewable energy-related manufacturing. Prices are expected to gradually recover in 2024 as demand begins to recover gradually.

Copper: The outlook for copper prices in 2024 is expected to be supported by a weaker US Dollar on the back of US Federal Reserve easing. The short-term demand outlook for copper remains weak

[1] Alber is TAC ECONOMICS virtual economic assistant, based on a comprehensive process combining information selection / information feed, and LLM tools trained on our own analytical process. Alber stands for "Artificial intelligence for Leveraging Better Economic Research".

amid recession fears, China's slowdown in the property sector, and weakening global manufacturing activity. However, the long-term fundamentals for copper are positive, with historically tight inventories and increasing demand due to its role in renewable technologies. Prices are expected to rise in the long term, but the market may remain volatile in the short term.

Wheat: The outlook for wheat prices in 2024 is expected to remain under pressure, as global ending stocks are projected to increase. Supply dynamics suggest that prices will need to send a signal to farmers to reduce corn acreage. The global demand for wheat is expected to rebound by a little over 3% in 2024, but prices are likely to remain under pressure for much of the year.

Corn: The outlook for corn prices in 2024 is expected to remain under pressure, as global ending stocks are projected to increase. Supply dynamics suggest that prices will need to send a signal to farmers to reduce corn acreage. Global demand for corn is expected to rebound by a little over 3% in 2024, but prices are likely to remain under pressure for much of the year.

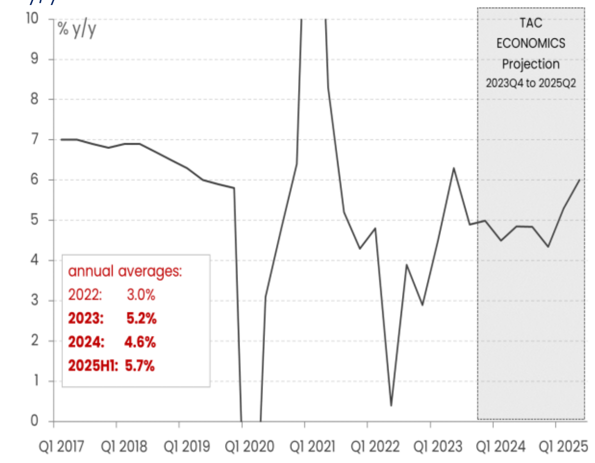
China's policy, structural changes, and overall traction

China continues to struggle in a complex combination of structural adjustments (ongoing crisis in real estate, excessive corporate and local governments' credit leverage, reinforcement of central / Party control, tensions with the US and implications for much tougher access to critical technologies, ageing population process, declining economic return on aggregate investment spending...) and post-zero Covid cyclical policies and support. It has become clear that Chinese authorities are not prepared to engage in massive stimulus policy if such policies create a reversal in structural adjustments, notably regarding leverage and the (too-large) role of construction in overall economic activity.

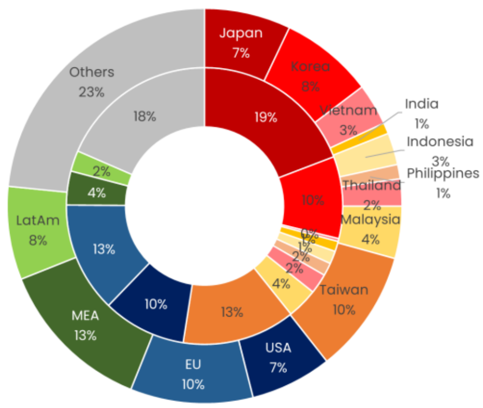
Policies have been therefore tuned to a complex management, with limited monetary easing, fiscal easing at central level aiming at supporting local governments, while engineering substantial debt restructuring and warning on a "long transition period" towards a new economic paradigm centered on domestic demand and technology.

This is translated by our quantitative models into a softer than expected growth in 2024 (4.6% y/y, after an estimated 5.2% in 2023 and 3.0% in 2022) and a more visible acceleration in 2025H1 (5.7% y/y). This would be accompanied by persistently low inflation (1.6% y/y on average in 2024, 1.9% in 2025H1, after 0.5% estimated for 2023), though avoiding the massive problems that a full-fledged deflation would create for indebted corporates.

China: GDP growth projections
% y/y



China's traction: China's imports by partners
% of total imports, inner circle: 2012, outer circle: 2022



Sources: UNCTAD, TAC ECONOMICS

Geopolitical issues and challenges

Geopolitics and related disruptions are here to stay: they reflect the fundamental competition for world leadership between the "incumbent" (US) and the "contender" (China), with the associated rise in the so-called 2nd order powers and the resulting expectations of a medium-term trend of rising episodes of tensions / violent flare-up. After the Russia War in Ukraine (getting entrenched with no expectations of an "Ukrainian victory and all difficulties in aiming at a negotiated settlement"), the Middle-East is once again the theater of acute / violent political tensions. We believe that divisions within the Arab / Muslim world are strong enough to prevent a "common front" with associated plausibility of oil embargo (OPEC) or oil sanctions (Iran). In parallel, diversion of shipping routes from the Suez Canal to rounding via the Cape of Good Hope would not per se create massive havoc, neither on delivery time (slightly less than 10 days difference for trip duration, from Asia to Europe) nor on cost (e.g. a few cents per barrels for oil)

Geopolitical hotspots include obviously Taiwan (with our view that a Chinese military intervention to forcibly annex Taiwan is highly unlikely as long as the US can be expected to intervene), but also Myanmar, Pakistan, the Great Lake region of Sub-Saharan Africa, Balkans, Central Asia.

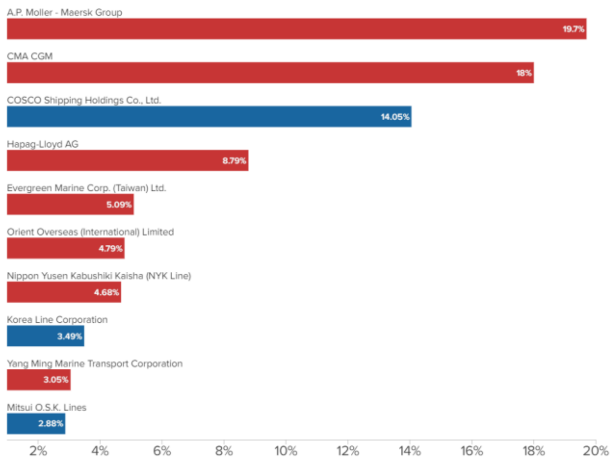
Such geopolitical uncertainties are reinforced in 2024 because of critical electoral consultation, starting in Taiwan next January and extending to the US at the end of the year.

War in Ukraine: situation as of December 20, 2023

Suspension of shipping routes via Suez Canal as reported by major shipping companies

red: suspension announced / blue: no suspension

as of Dec.20, 2023, % of total cargo shipping by company



Sources: Institute for the Study of War, Atlantic Council

3. Macroeconomic Outlook in 2024 and 2025H1: broadly steady performance but with divergence

Mixed perspectives for the next 18 months, with a visible time-sequence

Incorporating these assumptions into our quantitative tools for EM leads to a somewhat mixed perspective for the next 18 months, with a visible time-sequence.

GDP growth would continue a modest decline up to a cyclical trough in 2024H2, followed by a more convergent recovery in 2025H1, with persistent differences across regions. Asia is expected

Appendix: list of countries with ISO codes

(with corresponding region and size's group)

ISO3	Country	size group	region
ALB	Albania	50 Smallest	Europe
DZA	Algeria	Next 40	MENA
AGO	Angola	Next 40	Sub-saharan Africa
ARG	Argentina	Next 40	Latin America
ARM	Armenia	50 Smallest	Europe
AZE	Azerbaijan	50 Smallest	Asia
BHR	Bahrain	50 Smallest	MENA
BGD	Bangladesh	Next 40	Asia
BLR	Belarus	50 Smallest	Europe
BEN	Benin	50 Smallest	Sub-saharan Africa
BOL	Bolivia	50 Smallest	Latin America
BIH	Bosnia Herz.	50 Smallest	Europe
BRA	Brazil	10 Key EM	Latin America
BRN	Brunei	50 Smallest	Asia
BGR	Bulgaria	50 Smallest	Europe
BFA	Burkina Faso	50 Smallest	Sub-saharan Africa
CPV	Cabo Verde	50 Smallest	Sub-saharan Africa
KHM	Cambodia	50 Smallest	Asia
CMR	Cameroon	50 Smallest	Sub-saharan Africa
CAF	Centr. Afr. Rep.	50 Smallest	Sub-saharan Africa
CHL	Chile	Next 40	Latin America
CHN	China	10 Key EM	Asia
COL	Colombia	Next 40	Latin America
COM	Comoros	50 Smallest	Sub-saharan Africa
COG	Congo	50 Smallest	Sub-saharan Africa
COD	Congo DR.	50 Smallest	Sub-saharan Africa
CRI	Costa Rica	Next 40	Latin America
CZE	Czech Rep.	Next 40	Europe
DMA	Dominica	50 Smallest	Latin America
DOM	Dominican Rep.	Next 40	Latin America
ECU	Ecuador	Next 40	Latin America
EGY	Egypt	Next 40	MENA
SLV	El Salvador	50 Smallest	Latin America
ETH	Ethiopia	Next 40	Sub-saharan Africa
GAB	Gabon	50 Smallest	Sub-saharan Africa
GEO	Georgia	50 Smallest	Asia
GHA	Ghana	50 Smallest	Sub-saharan Africa
GTM	Guatemala	Next 40	Latin America
GIN	Guinea	50 Smallest	Sub-saharan Africa
GNB	Guinea Bissau	50 Smallest	Sub-saharan Africa
HND	Honduras	50 Smallest	Latin America
HUN	Hungary	Next 40	Europe
IND	India	10 Key EM	Asia
IDN	Indonesia	10 Key EM	Asia
IRN	Iran	Next 40	MENA
ISR	Israel	Next 40	MENA
CIV	Ivory Coast	50 Smallest	Sub-saharan Africa
JOR	Jordan	50 Smallest	MENA
KAZ	Kazakhstan	Next 40	Asia
KEN	Kenya	Next 40	Sub-saharan Africa
KOR	Korea	10 Key EM	Asia

ISO3	Country	size group	region
KWT	Kuwait	Next 40	MENA
LAO	Laos	50 Smallest	Asia
LBY	Libya	50 Smallest	MENA
MKD	Macedonia	50 Smallest	Europe
MDG	Madagascar	50 Smallest	Sub-saharan Africa
MYS	Malaysia	Next 40	Asia
MLI	Mali	50 Smallest	Sub-saharan Africa
MRT	Mauritania	50 Smallest	Sub-saharan Africa
MUS	Mauritius	50 Smallest	Sub-saharan Africa
MEX	Mexico	10 Key EM	Latin America
MNG	Mongolia	50 Smallest	Asia
MNE	Montenegro	50 Smallest	Europe
MAR	Morocco	Next 40	MENA
MOZ	Mozambique	50 Smallest	Sub-saharan Africa
MMR	Myanmar	Next 40	Asia
NPL	Nepal	50 Smallest	Asia
NER	Niger	50 Smallest	Sub-saharan Africa
NGA	Nigeria	Next 40	Sub-saharan Africa
OMN	Oman	Next 40	MENA
PAK	Pakistan	Next 40	Asia
PAN	Panama	Next 40	Latin America
PRY	Paraguay	50 Smallest	Latin America
PER	Peru	Next 40	Latin America
PHL	Philippines	Next 40	Asia
POL	Poland	10 Key EM	Europe
QAT	Qatar	Next 40	MENA
ROU	Romania	Next 40	Europe
RUS	Russia	10 Key EM	Europe
RWA	Rwanda	50 Smallest	Sub-saharan Africa
SAU	Saudi Arabia	Next 40	MENA
SEN	Senegal	50 Smallest	Sub-saharan Africa
SRB	Serbia	50 Smallest	Europe
SYC	Seychelles	50 Smallest	Sub-saharan Africa
ZAF	South Africa	10 Key EM	Sub-saharan Africa
LKA	Sri Lanka	Next 40	Asia
SDN	Sudan	Next 40	Sub-saharan Africa
TWN	Taiwan	Next 40	Asia
TZA	Tanzania	50 Smallest	Sub-saharan Africa
THA	Thailand	Next 40	Asia
TGO	Togo	50 Smallest	Sub-saharan Africa
TUN	Tunisia	50 Smallest	MENA
TUR	Turkey	10 Key EM	Europe
ARE	U.A.E.	Next 40	MENA
UGA	Uganda	50 Smallest	Sub-saharan Africa
UKR	Ukraine	Next 40	Europe
URY	Uruguay	Next 40	Latin America
VEN	Venezuela	Next 40	Latin America
VNM	Vietnam	Next 40	Asia
ZMB	Zambia	50 Smallest	Sub-saharan Africa

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