11. May 2017

https://blog.en.erste-am.com/impressions-fromn-imf-meeting-washington-emerging-markets-alive-kicking/

# My impressions from IMF meeting in Washington: Emerging markets “alive and kicking”

Gast-AutorIn / Guest Author




*Felix Dornaus, Senior Fund Manager Emerging Markets Bonds*

**Author: Felix Dornaus**
**Senior Fund Manager**

The spring meeting of the International Monetary Fund was held in Washington from 20th to 23rd April. This event was the reason for an investor conference that I attended in order to get an idea of the status quo of the global economy as well as of risks and opportunities.

**The core message to the participants, published in a joint communiqué of all states: the global economic growth is picking up speed, but downside risks, especially of a political nature, cannot be ruled out.**

### Tasks of the International Monetary Fund

The International Monetary Fund (IMF) was established in 1945 with the goal of the member states (currently 188) cooperating in international monetary policy and offering mutual financial support to overcome balance of payment-related difficulties. According to the bylaws, further tasks of the IMF are the promotion of international trade and exchange rate stability (source: www.bmf.gv.at).

### Semi-annual meetings to analyse the global economy

The most important committee is the International Monetary and Financial Committee (IMFC). It convenes semi-annually, as it did this spring.

### Hope for “politics of the middle way” in the USA

The discussion revolved to a large degree around the question of how the USA and President Trump would position themselves in trade and tax policies. The US equity markets had anticipated most of the “America first” statements. Now expectations are for Trump’s policies to even out in the middle and investor-friendly plans to be realised that further boost economic growth.

### USA-China-North Korea

China’s economy is expected to grow by 6.7% in 2017. A trade war between the USA and China should not materialise. Communist Party General Secretary Xi Jiping seem to have agreed at their meeting at Mar a Lago (US state of Florida) off the records that China would reduce its balance of trade surplus with the USA and the USA would expand its high-technology exports. In the conflict with North Korea, China should step up its pressure on the neighbouring country to abandon its nuclear arms tests. In “return”, the USA could enter into peace talks and even open an embassy.

### Expectation with respect to monetary and interest rate policy and oil price

The politics of two additional interest rate hikes by the Fed is expected to continue. Some 46% of the participants expect the US Treasury bond at 2.5-3.0%, 39% envisage it in a bandwidth of 2 to 2.5%. The euro should appreciate relative to the US dollar: 45% expect to see an exchange rate of 1.0 to 1.10, while 44% expect 1.10 to 1.20.

According to 52% of the participants, US economic growth should even out at 1.5 to 2.0%, and at 2-2.5% for 39%. As far as the oil price is concerned, 31% expect a price and of USD 50-55, and 29% envisage a band of USD 55-60.

In the Western industrialised nations, the low interest rates should remain low for some time. The sanctions against Russia will probably not be loosened any time soon. That being said, the country has adjusted quite well to the measures.

### Capital inflow into emerging markets increases

In this environment, the capital inflows into the emerging markets should continue at current levels or even pick up. Most participants of this conference are overweighted in emerging markets. The growth differential between the emerging markets and the developed economies should expand, which all emerging markets asset classes will benefit from, especially equities in local currencies. The majority of participants expect the emerging economies to grow by 4.5%, while 34% expect growth of 3.5 to 4%. The interest rate differential between emerging markets government bonds and global government bonds is expected at 2.75% to 3%. The level of debt of largely privately-held emerging market companies, which has been an issue in recent years, is not seen as a threat by the majority of participants anymore.

### Comeback of frontier markets

In order to improve the diversification of the portfolio, investors will increase their focus on frontier markets – i.e. countries that fall short of the level of development that emerging markets have attained. When Xi Jinping gets re-elected as General Secretary of the powerful Chinese Communist Party in November, this should translate into the biggest problems being dealt with – on the basis of a restructuring of government-owned companies, a recapitalisation, and the tightening of the financial system.

### Potential for interest rate cuts

As always, the attractive growth figures come with political risks, especially from countries like Venezuela, South Africa, and Turkey. These risks should be balanced by the story of interest rate cuts across all emerging markets. In Brazil for example, the potential for a rate cut is particularly high, given that the fundamental data have improved significantly and the social and labour market reforms have started to gain traction. The outlook for Argentina is positive as well. In Central and Eastern Europe, the development of Romania is the main problem that is worrying investors.

Author:
**Felix Dornaus** joined ERSTE-SPARINVEST/ Erste Asset Management in 2009, where he now manages global emerging markets hard currency fixed income portfolios. He holds a degree in political economy from the Vienna University of Economics and Business and completed part of his studies in Sao Paulo.




## Gast-AutorIn / Guest Author