EM Growth Tracker
June 2019

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- EM Growth Tracker at 3.5% 3m/3m SAAR in June.
- Hard data and financial conditions drag growth down.
- Regional trackers in EM Asia and EMEA are weakening.

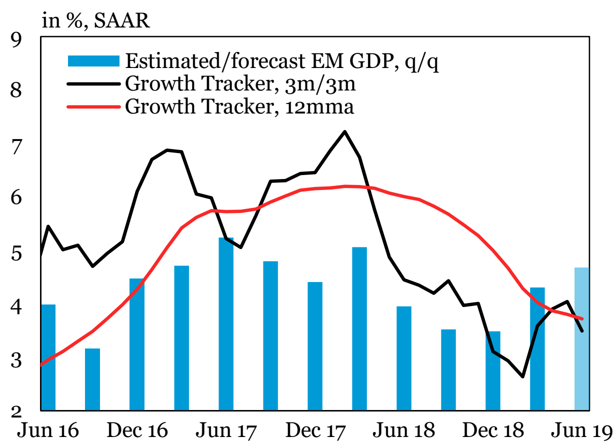
Tracker softens

Our EM Growth Tracker came in at 3.5% (3m/3m SAAR) in June, 0.3pp lower than the month prior (Exhibit 1). The deterioration in our tracker was mainly driven by weaker hard data (explaining more than half of the decline) but exacerbated by business surveys and financial variables (Exhibit 2).

The drop in our tracker, a sign that deteriorating manufacturing sentiment is becoming more broad-based globally, is notable for its speed and timing, given that it coincides with the latest escalation in China-US trade tensions. One-off events in specific countries, combined with the increased volatility in markets given the ongoing trade frictions, paint a challenging horizon for EMs.

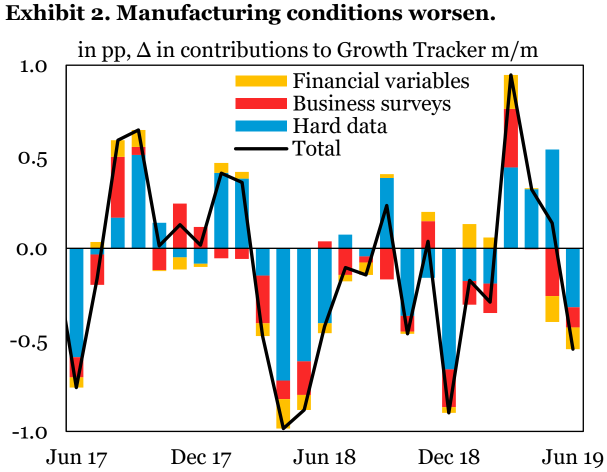
Trade actions and tensions have so far not significantly affected global current account imbalances, as trade has been diverted to other countries with lower or no tariffs. Instead, these trade tensions and related uncertainties are weighing on global investment and growth, especially in sectors most integrated into global supply chains. Lately, the response of monetary authorities to this scenario seems to be the most important driver of market sentiment. Over the past 12 months, market pricing for the Fed has shifted from 50 bps in hikes through end-2020 to 100 bps in cuts. Yet the dollar has refused to weaken; in fact, it has strengthened slightly over this horizon.[1]
Despite the challenges, we remain positive on growth. This benign growth view is constructive for risk assets, but emerging markets have not benefitted as much as might have been expected. We believe this relates to what we are calling the *EM Positioning Overhang*, whereby a decade of QE left investors overloaded with EM assets.

Exhibit 1. Tracker deteriorates.



Source: IIF

Exhibit 2. Manufacturing conditions worsen.



Source: IIF

[1] Our Global Macro Views, in-depth country reports and data contain detailed estimations and forecasts for EMs.

Weak outlook for manufacturing

The global economy has stumbled sharply in the first half of the year, with trade and investment flows between countries falling faster than expected. China's manufacturing activity weakened once again in the month of June. A downbeat reading, along with somber indicators seen in May and April, would suggest economic growth is likely to slow this quarter and increase the prospect of further policy easing in the coming months. Subdued global demand has also affected other EMs: manufacturing activity in Taiwan was in contraction for a second consecutive month in June. Singapore's PMI also fell for the second straight month after contracting by 0.3 point to 49.6 in June. This marks the lowest index reading for Singapore's PMI since August 2016. Brazil's manufacturing sector ended the second quarter on a stronger footing, avoiding slipping into contraction territory in June and breaking a three-month run of slowing growth. The Turkish economy remained on a rebalancing track in 1Q, with ongoing weakness in domestic demand despite strong public consumption and contributions from exports. The recent early indicators for Turkey give encouraging signals in June with improving consumer and business confidence indices, rising PMI to the highest level in a year.

IP growth with mixed signals

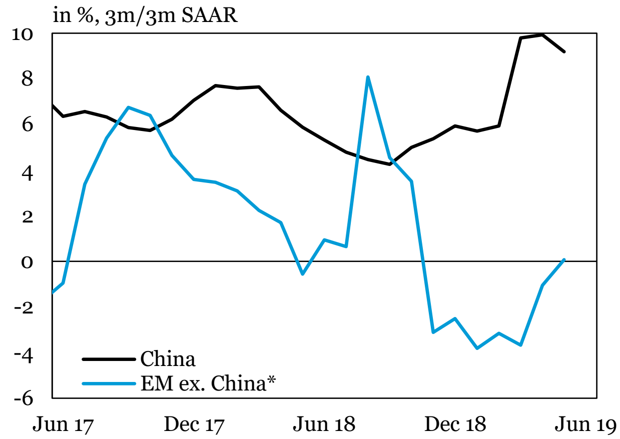
China's industrial output grew 6.3% in June from a year earlier, picking up from May's 17-year low. Fixed-asset investments for the first half of the year rose 5.8% from a year earlier. Private sector investment in fixed assets, which make up 60% of the country's total investments, rose 5.7% in January-June, compared with a 5.3% rise in January-May (Exhibit 3). During May, industrial production fell in Brazil (-0.2% with respect to April), Taiwan (-3%), Korea (-0.2%) and Singapore (-2.4%).

While China exports unexpectedly returned to growth in May, this could be attributed to front-loading of U.S.-bound exports to avoid new tariffs. Only three countries whose exports factor into our model expanded. Moreover, import growth rates were positive for only 4 countries in our sample, evidencing a slowdown in global demand (Exhibit 4).

Regional trackers mixed

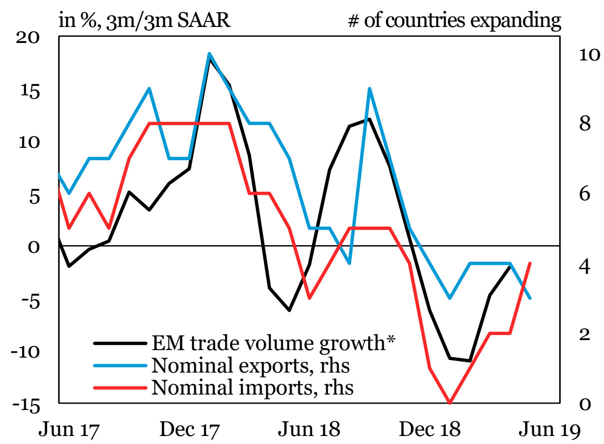
The regional tracker for EM Europe and Africa continues its decline, showing a slower pace of growth (1.3 pp in June), while Latin America saw its first positive reading in three months (0.18 pp). The regional tracker for EM Asia finished at 5.6 pp (Exhibit 5).

Exhibit 3. IP growth in EM ex. China continues to recover.



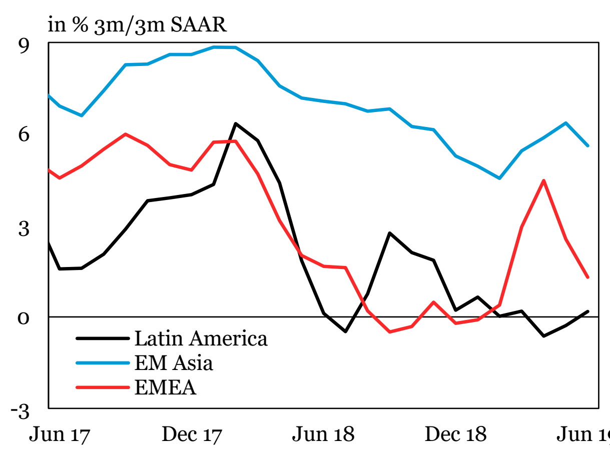
Source: IIF. BR, KO, PL, SG, TW, RU (GDP-weighted)
**Due to lagged IP release, we use May figures.*

Exhibit 4. Trade activity still weak.



Source: CPB Trade Monitor, Haver, IIF.
**Due to lagged Trade data release, we use March figures.*

Exhibit 5. Regional trackers weakening.



Source: IIF