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MUFG Bank, Ltd.
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Global recession risks and emerging markets

Macro focus: 2022 has witnessed a lot and we are only half way. From an EM perspective, the outlook is in a state of flux. EMs were already pricing in a long streak of stagflationary shocks and these have grown louder as months have gone by on a combination of commodity shocks, supply disruptions and a tepid post-COVID demand recovery. Our EM 2022 outlook theme we catalogued in January (see here) was centred on "stagflation trepidation" gaining traction. Persistent inflation, recession concerns and reverberations of the war in Ukraine reinforces this narrative.

FX views: EM FX have staged a modest relief in recent weeks but the underlying bearish trend remains in place. Whilst the USD has corrected lower over the past week in part by the scaling back of Fed rate hike expectations, we expect the FOMC to stick to its hawkish policy this week even as growth risks are increasing.

Trading views: A short term correction in EMFX looks possible with worst case US picture being priced out and risk indices oversold – but we have been here before.

Week in review: Russia eased rates by 150bp to 8.0%. South Africa accelerated its pace of tightening by delivering a 75bp hike to 5.5%. Turkey kept its rates unchanged with negligible changes to guidance. Saudi's inflation rate moderated (2.3% y/y in May) as pricing rigidities and FX gains guard against import price shocks.

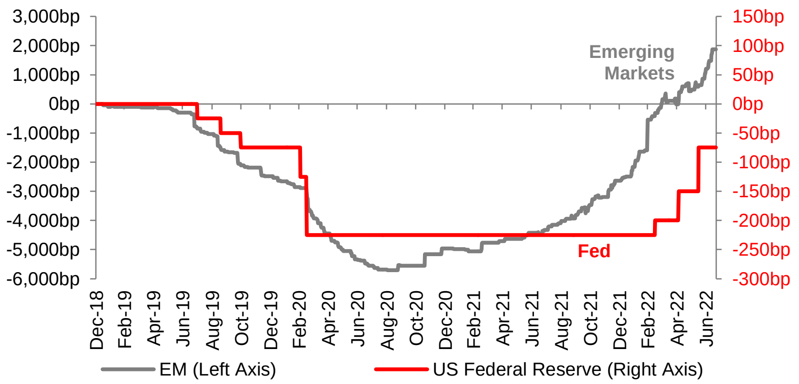
Week ahead and calendar: In the coming week, we have Hungary rates (MUFG: +100bp to 10.75%) and Czech Q2 2022 GDP (MUFG: 3.5% y/y)

Forecasts at a glance: Headwinds facing EMs are getting stronger as persistently high inflation prompts more hawkish monetary policy responses leading to further tightening of financial conditions and more sacrifices from growth.

Core indicators: EM securities suffered an outflow of USD4.0bn in June – the fourth consecutive month of outflows with mounting global recession risks weighing on EM flows as apprehensions builds over geopolitical events, tighter monetary conditions, elevated volatility and realised inflation (see here).

CHART OF THE WEEK: FED TIGHTENING ELIMINATES EM POLICY OPTIONS

MAJOR EMERGING MARKETS INTEREST RATE CHANGES, CUMULATIVE (DECEMBER 2018 = 0 BP)



Fed funds target rate remains 75bp below its prior cycle peak of 2.5%, as the process of US interest rate normalisation has only just begun, leaving EM central banks with little choice other than to tighten monetary policy even further.

Source: Bloomberg, MUFG Research

Macro focus

Global recession risks and emerging markets

Sequencing of the global economic slowdown will matter for EM performance

We are in a global interest rate and high inflation shock. Large swathes of the global economy are likely to be in recession at some point over the next 18 months. Sequencing matters however. Two out of the three global economic powerhouses – the US and EU – are likely to witness two consecutive quarters of declining GDP (a technical recession), albeit not at the same time, with the third titan, China, also set to experience the lowest annual growth in over 30 years (bar 2020) this year. We view the precise order of deterioration points to a unfavourable outlook across the EM space. That is, if the US were to enter recession first, it would yield a more dovish Fed as well as a China that acts to offset the spillovers with a more aggressive stimulus programme. The challenge this time around is that the current global downturn is most evident outside the US, with Europe – the centre of global volatility – holding the recessionary baton. EMs will eventually encounter a more favourable combination of external demand and US monetary easing again, but getting there may take longer than historically the case with the Fed seeking to regain inflation credibility whilst China's structural pivot towards a less EM-responsive operating model gains traction.

It is our concern that EMs are facing a synchronised slowdown in both the US and China that warrants an unfavourable EM outlook this time around from a sequencing perspective with both weak external demand growth and tightening US monetary conditions

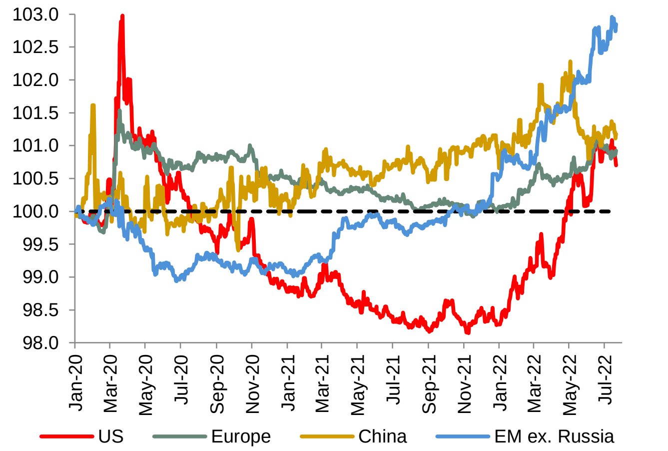
Historically, China has driven current accounts across EMs whilst the US through the Fed has driven EM capital accounts. A combination of weak growth (or outright recession) in the US and stronger growth in China is favourable for many EMs as their current accounts are bolstered by strong import demand from China, whereas a more dovish Fed drivers capital towards EM. Vice versa, when growth is weak in China and strong in the US, the opposite is the case. The other two cases wherein both countries have concurrently weak or strong growth is seldom, as authorities, tend to offset each other. Out of these various scenarios, it is our concern that EMs are facing a synchronised slowdown in both the US and China that warrants an unfavourable EM outlook this time around from a sequencing perspective with both weak external demand growth and tightening US monetary conditions.

EMs positive real rate differentials towards DMs is set to ease noticeably

The current global downturn is most evident outside the US. Over the last quarter, China has been as close to a recession as it has ever been bar Q1 2020, with a q/q contraction of 2.6%. Meanwhile, inflation numbers in the US remain high, labour markets tight and wage growth strong, prompting an ever more aggressive reaction by the Fed. Our house view is for a 60% probability of a US recession over the next 12 months which has largely a consequence for Fed reaction. Some EMs look more

GLOBAL FINANCIAL CONDITIONS ARE TIGHTENING WHICH IS A CORE EM RISK (CAPITAL FLIGHT) IN 2022

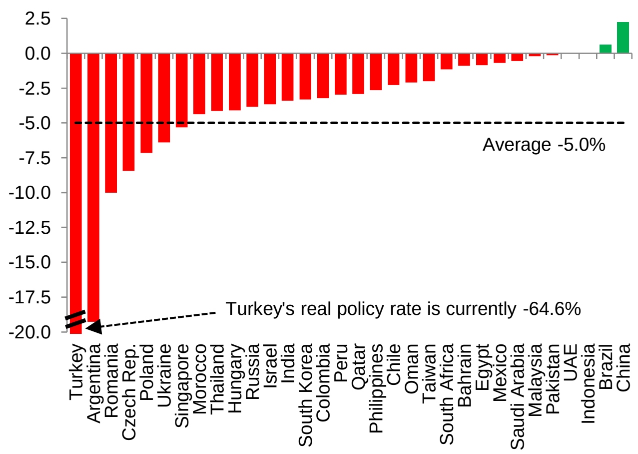
FINANCIAL CONDITIONS INDICES (FCI) BY COUNTRY/REGION, REBASED 100 = JANUARY 2020



Source: Bloomberg, MUFG Research

IN REAL TERMS, THE ROOM FOR MANOEUVRE IS LIMITED WITH NO REAL RATE BUFFER IN MOST EM'S

EM REAL POLICY RATES (%)



Source: Bloomberg, EM Central Banks, MUFG Research protected from this than others, because of their large real policy rate differentials to DMs, though this is likely to change. As such, EMs face a deteriorating external demand picture, while the rate differential towards the US changes in a way that tends to lead to capital outflows. The expectation of this might well be what has been leading to a renewed decline in foreign ownership of EM local currency bonds, as this asset class is particularly sensitive to the confluence of low growth, tighter US monetary conditions and global risk aversion.

Three key transmission channels of a stronger USD on EMs

As we recently catalogued, the strong US dollar (USD) environment also heralds additional pressures for the EM complex (see here). We examine three transmission channels in which a strong USD – a constituent or consequence of tight US monetary conditions – affects EMs. First, a strong USD propagates a negative trade shock due to dominant currency pricing (as large shares of global trade are invoiced in USD, a USD appreciation makes traded goods (and services) more expensive to purchase, depressing demand for them). Second, a stronger USD weakens EM creditworthiness as USD liabilities become more costly to service. Third, a strengthening USD places a more damaging effect on inflation expectations. As a result, EM policy – both monetary and fiscal – is more limited in the support it can provide even as largest parts of the global economy enters recession.

The composition of Chinese stimulus leads to less EM spillovers this time around

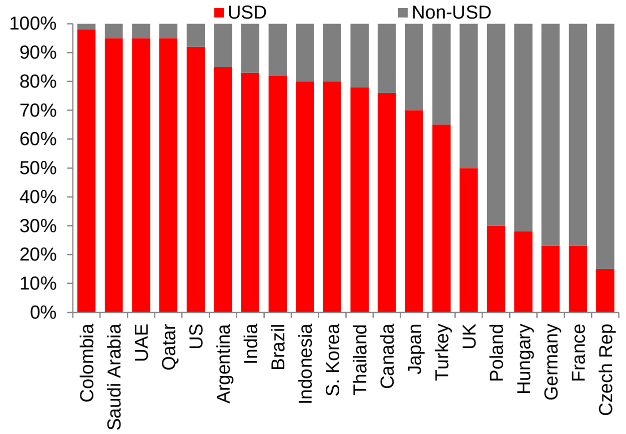
Meanwhile, whilst markets have kept a laser focus on China's reopening strategy to gauge prospects for EMs, we believe that China is playing an increasingly less pivotal role in the EM outlook relative to the past. Granted, Chinese policymakers are once again making use of a large array of fiscal levers which will augment the Chinese fiscal deficit this year. Though, the nature of the current stimulus is set to be less EM-centric, as whilst a sizable share is attributed to infrastructure investment, by and large, this is being geared to large tech and public services shares such as upgrading 5G networks, the construction and improvements of datacentres and strengthening public health facilities. Thus, Chinese stimulus may be markedly less import and commodity intensive than in the past with fewer EM spillovers.

EMs will eventually encounter a more favourable combination of external demand and US monetary easing again, but getting there may take longer than historically the case

Looking ahead, whilst markets are increasingly signing from the same hymn sheet when it comes to recessionary voices, this cycle will eventually turn and prospects for EMs will become more favourable. If the US enters a recession before year-end, then markets will start pricing a more dovish Fed, and hence give other central banks some policy space too. The concern however is that getting there may take longer than historically the case with the Fed seeking to regain inflation credibility, especially in the context of longer-term persistent inflation pressures such as deglobalisation and decarbonisation. Thus, they may be less willing to loosen policy early than in the past, whilst equally a US recession could itself create a drop in external demand for EMs, especially if China does not act as a circuit-breaker for transmission.

THE OVERWHELMING SHARE OF EM EXPORTS ARE INVOICED IN USD

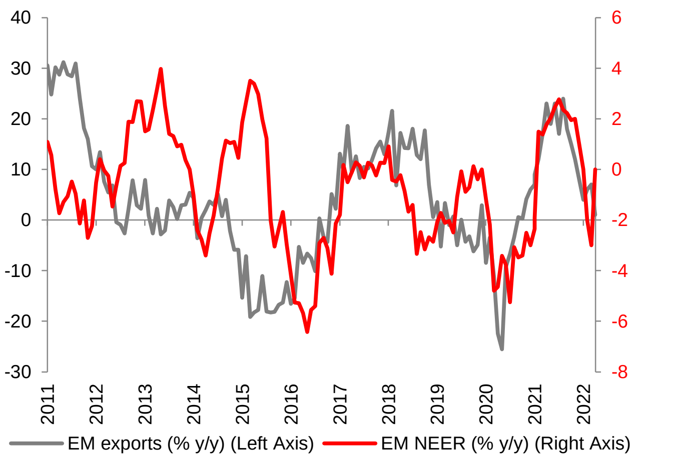
SHARE OF EXPORTS INVOICED IN USD AND NON-USD (%)



Source: Bloomberg, MUFG Research

EM EXPORTS ARE WITNESSING WEAKNESS WITH THE USD STRENGTH AS THEY BECOME MORE COSTLY

EM EXPORTS (% Y/Y) AND EM NEER (% Y/Y)



Source: Bloomberg, MUFG Research

FX views

EM FX: Hawkish Fed & global slowdown fears continue to weigh on EM FX

EM FX stages relief rebound in recent weeks but bearish underlying trend remains in place

It has been a tough year for emerging market currencies. Our MUFG EM FX index has fallen sharply to new record lows against the USD this month. At the worst point on 12th July our EM FX index had fallen by -9.0% year to date. EM currencies have since staged a modest relief in recent weeks but the underlying trend remains lower. The CLP (+6.4% vs. USD), RUB (+6.1%), HUF (4.4%), COP (3.6%) and PLN (3.6%) have rebounded the most since the USD peaked on 12th July. It has provided some short-term term relief for the CLP, HUF, COP and PLN after they were all hit hard as the USD regained upward momentum in June.

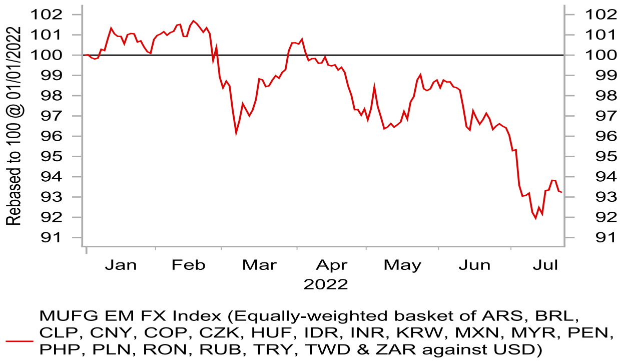
Pullback for US yields & global equity market rebound trigger correction lower for USD. We expect Fed to stick to hawkish policy message this week even as growth risks are increasing

The USD has corrected lower over the past week driven in part by the scaling back of Fed rate hike expectations. The US rate market is now more confident that the Fed will deliver a 75bps hike this week after initially pricing in a much higher probability of a larger 100bps hike immediately following the release of the hot US CPI report for June. Comments from Fed officials including Governor Waller still backing a 75bps hike, and the release of softer US data (Philly Fed & PMI surveys for July) and inflation expectations (UoM survey for July) have dampened expectations for more front-loaded Fed tightening. Nevertheless, we still expect the Fed's update communication to strike hawkish tone and keep alive expectations for another 75bps hike in September. We believe it is too soon to expect the Fed to make a dovish policy pivot this week and signal a slower pace of hikes while elevated inflation remains the main focus. The combination of intensifying fears over a sharper global slowdown/recession and the Fed's still hawkish policy action creates an unfavourable backdrop for EM FX. As a result, we believe the recent relief rebound for EM currencies will prove short-lived.

EMEA central banks stepping up rate hikes to provide more support for domestic currencies. Larger hikes on their own unlikely to be sufficient to trigger reversal of bearish underlying trends

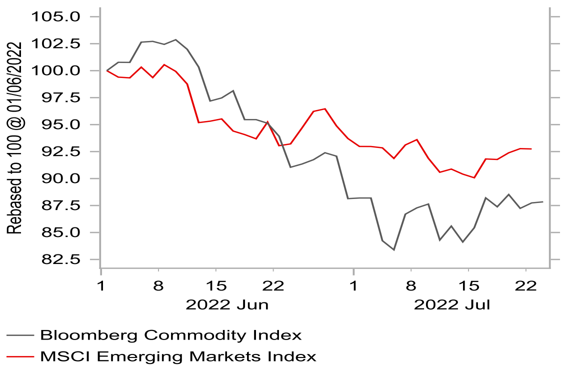
Weak domestic currencies have been one factor that has been increasing pressure on EMEA central banks to deliver larger rate hikes. Over the past week, the SARB became the latest central bank to deliver a hawkish surprise when it hiked rates by 75bps. After hitting a year to date high earlier this month at 17.306, USD/ZAR has just fallen back below the 17.000-level although the larger SARB on its own is unlikely to be sufficient for sustained reversal lower. In the week ahead, we expect the NBH to hike rates again by 100bps. It follows the 200bps hike earlier this month when EUR/HUF was threatening to break above the 410.00-level. It has since fallen back below the 400.00-level. We continue to believe that the HUF remains one of the most sensitive EM currencies to tighter global financial conditions.

BEARISH TREND FOR EM FX REMAINS IN PLACE



Source: Bloomberg, Macrobond & MUFG Research

SLOWDOWN FEARS CONTINUE TO WEIGH ON EM FX



Source: Bloomberg, Macrobond & MUFG Research

Trading views

Disclaimer: "Trading views" offers an overview of what our professional traders and desk analysts are watching in the markets, their commentary and views are theirs alone and are not intended to be construed as investment advice. This material is intended to be of general interest only and should not be considered a recommendation or solicitation to buy, sell or hold any security or to adopt any investment strategy. The information provided in this material is not intended as a complete analysis of every material fact regarding any country, region or market.

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Correction looks possible in EMFX but we have been here before

A short term correction in EMFX looks possible with worst case US picture being priced out short term and risk indices in oversold territory but we've been here before, with nothing new

After a break away we come back to markets not too dissimilar to where we were before. The positivity coming from Chinese stimulus is now being offset by increased concerns on the housing market. The fundamental backdrop for the USD is still strong on a medium term level but post last week's data and fed speak may see "just" a 75bps hike this week. This alongside a feel of oversold on risk indices suggests that some strength in EMFX could continue perhaps. However we've been here before and proved wrong with corrections being much more like pauses before the underlying trend continues. .

The pickup in EM CBs acting in ways that support their currency is notable

One thing that is notable over the last weeks is the significant pick up in EM Central banks actively looking to, if not outright support their currency, at least lean against the trend somewhat. You have the more overt support where CLP is clearly leading the charge. Candidates here also include BRL and in Asia INR. Others CBs are supporting through tightening liquidity or outright rate hikes where FX is now playing an active role. The former being popular in CEE while the latter is starting to become more commonplace as the rates hikes in South Africa and Philippines the week before showed. While lastly you have some CB starting to lean on local institutions to slow outflows or at least hedge the FX more and more.

Maybe not enough to change the trend but will make it harder

While this is notable, does this mean that they will turn the trend in EM? In itself we think not. The fundamental reasons for USD strength are too widespread and from a CB perspective justifiable. There is little speculation in EM right now to see this actions as having a significant turnaround. In fact we would argue the biggest driver behind local EM weakness is coming from BOP story and onshore are much better buyers of USD than offshore. In such a scenario unless you are tackling the actual import/export transactions it is very hard to stop the trend. While for example India may be looking at this with its move on gold tax it needs to be much more significant for it to have a real impact on the currencies.

And presents RV opportunities in EM space going forward

However what all this does do is make the default proposition of a higher USD tougher going forward. Maybe the hurdle rate won't be high enough to change things immediately but it does mean there will need to be more done on the US side as the EM side will get support now. As we have mentioned before the carry gap with the US is closing further and CBs will now make it easier to be long than short their respective currencies where it helps them. The latter point is key as it will open up good RV opportunities over summer. You want to have EM longs in places where CBs are credible and are now looking to support their currency. Against this places where valuations do not look as stretched or we have not seen CBs care too much about currency weakness will be our preferred shorts. In Asia this means that relative intra-Asia plays with RMB as a funder look attractive to us especially as you know get paid to short RMB.

Week in review

EM capital flows: investors sharply reduced exposures to EM assets last week

EM sentiment remains woeful

Investor sentiment across the EM space remains gloomy with indicators pointing to an ever sharper slowdown of growth momentum. Prospects of further rate hikes by global central banks given sticky inflation will keep financial conditions tight. It was the turn of the ECB last week with a 50bp hike – its first rate rise since 2011. Asian central banks have also accelerated their pace of tightening over the past month, having initially been slower than global peers to join the tightening bandwagon. As monetary policy turns restrictive, this is likely to weigh on global economic activity over the next 12 months and with the health of the global economy being a major driver of EM returns, this is a large part of our thesis behind our cautious EM view (see here). A key component worth highlighting is the real effective exchange rate (REER), which has turned quite negative across the EM space, as higher inflation readings out of EM have led to a real appreciation of the currencies. Given the lagged relationship between financial conditions and EM economic activity, this implies some significant slowdown in EM economic activity in H2 2022.

EMs witnessed a sharp week of outflows (USD-7.6bn – week ending 20 July), led by both outflows of equity (USD-5.4bn) and debt (USD-2.1bn), with investor apprehension continuing to linger

According to IIF data, EMs witnessed a sharp week of outflows (USD-7.6bn – week ending 20 July), led by both outflows of equity (USD-5.4bn) and debt (USD-2.1bn), with investor apprehension continuing to linger, stemming from geopolitical events, tighter financial conditions, realised inflation and anxieties that some EMs will not recover quickly enough from COVID (see here, here and here). Following the latest IIF estimates, the 52 week rolling cumulative outflows into EM bond and equity funds declined to USD-73.3bn from USD-70.4bn a week ago. This figure is the lowest since December 2020, and we expect this trend to continue given the ongoing deterioration in the global liquidity backdrop. From an asset markets perceptive, EM credit historically outperforms into Fed lift-offs, but this time around EM local rates is doing better.

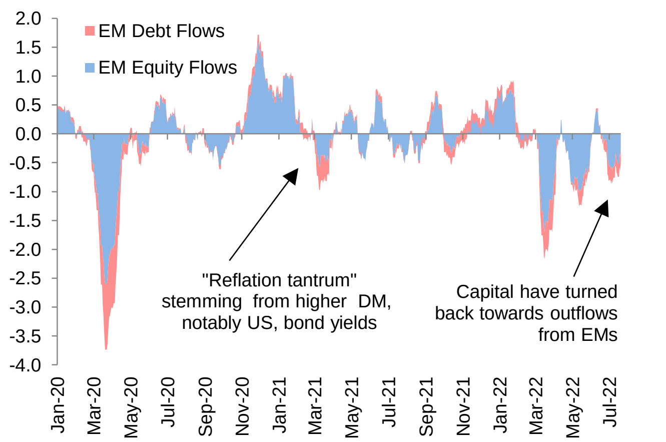
Russia: CBR cuts by 150bp to 8.0% in a dovish move – now below pre-war levels

Russia eases rates to below pre-war levels with further to go

The Central Bank of Russia (CBR) eased the repo rate by 150bp to 8.0%, more than the 50bp markets were anticipating (MUFG forecast was for a hold at 9.5%). The cut brings the cumulative easing to 1,200bp since the initial emergency rate hike of

CAPITAL CONTINUES TO FLOW OUT OF EM'S ON A 28 DAY ROLLING BASIS GIVEN ELEVATED RISK AVERSION

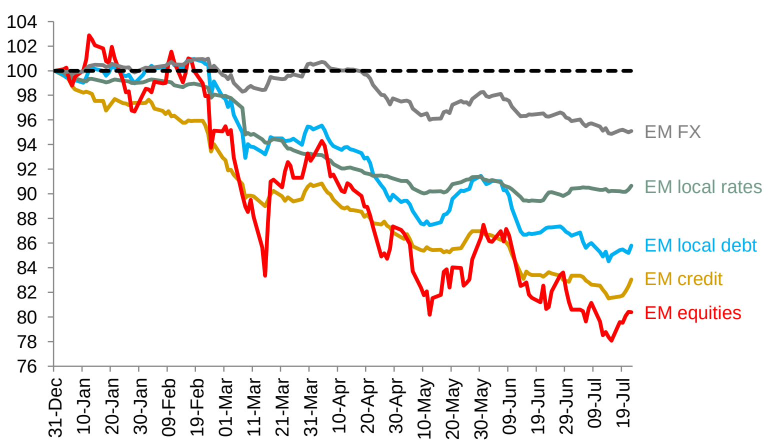
EM EQUITY AND DEBT FLOWS (USD BN), 28 DAY ROLLING AVERAGE



Source: IIF, MUFG Research

SELL-OFF ACROSS ALL MAJOR EM ASSET CLASSES CONTINUES GIVEN THE WAR AND THE HAWKISH FED

EM EQUITIES, FX, RATES, CREDIT AND DEBT (1 JANUARY 2022 = 100)



Source: Bloomberg, MUFG Research

1,050bp on 28 February in reaction to capital flight and financial market turbulence following Russia's invasion of Ukraine. The CBR reconfirmed that inflationary pressures have eased owing to a stronger Rouble (RUB) and that economic activity had declined less than expected. The CBR left it open during the press release that it will consider the necessity of further rate reductions at its upcoming meetings. At face value, rate cuts appear more geared to buttress domestic demand rather than weaken the RUB which appears artificially low owing to ongoing hard currency inflows and thin FX liquidity. Finally, the CBR announced updated forecasts to which it sees inflation and the key rate lower and growth higher against its previous April projections – key estimates are:

1. Inflation (average, y/y) adjusted from 18.2-20.9% to 13.8-14.7% in 2022, from 6.8-10.4% to 4.3-7.5% in 2023.
2. Repo rate (average) adjusted from 10.8-11.4% to 10.5-10.8% in 2022, from 7.0-9.0% to 6.5-8.0% in 2023.
3. GDP growth (y/y) adjusted from (-8.0)-(-10%) to (-6.0)-(-4.0%) in 2022, from (-3.0)-0% to (-4.0)-(-1.0%) in 2023.

Bid-ask spreads are wide and offshore funding rates remain high, supporting our low liquidity view. On economic activity, we believe that this is the main focus of the CBR's rate cuts. According to the CBR, inflow of household funds continued though lending remained moderate. Moreover, consumer activity started to pick up as evidenced by high frequency spending data but appears to be constrained by subdued lending activity. In our view, this is the main transmission channel the CBR tries to focus on in order to bring consumer demand back and reduce the propensity to save, with less focus on inflation.

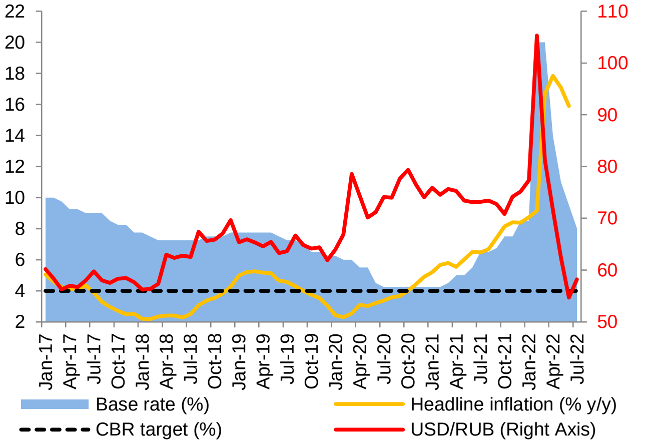
South Africa: SARB accelerates its pace of tightening to 75bp with more to come

South Africa hikes by 75bp with our expectation of another 100bp in hikes to come before year-end

The South African Reserve Bank (SARB) accelerated its pace of policy tightening by delivering a 75bp hike to 5.50%, responding to higher inflation, upside risks to the CPI outlook, and in a move to curb rising inflation expectations. The decision was in line with our forecast (consensus 50bp), with three of the five Monetary Policy Committee (MPC) members preferred 75bp, one favoured a 100bp hike, and another wanted a 50bp increase. The SARB lifted its headline inflation forecasts markedly to 6.5% for 2022 (5.9% previously) and to 5.7% in 2023 (5.0%), while it was unchanged at 4.7% in 2024. Even with these revisions, the SARB still sees a confluence of upside risks to the inflation outlook, including ongoing upside surprises to global

RUSSIA HAS NOW LOWERED RATES BY 1,200BP SINCE THE WAR, REVERSING THE 1,050BP EMERGENCY HIKE

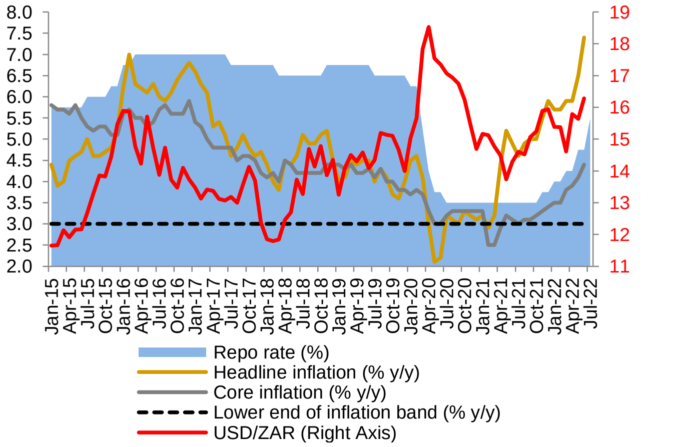
RUSSIA INFLATION AND TARGET (% Y/Y), RATES (%) AND USD/RUB



Source: Bloomberg, CBR, MUFG Research

SOUTH AFRICA HIKES RATES BY 75BP AND WE EXPECT ANOTHER 100BP IN HIKES BY YEAR-END

SOUTH AFRICA INFLATION (% Y/Y), INTEREST RATES AND USD/ZAR



Source: Bloomberg, SARB, MUFG Research producer price and food inflation, pressures on energy prices, risks from electricity and other administered prices and higher wage demands. This is what prompted the acceleration in policy tightening in our view, against the backdrop of higher inflation expectations and currency depreciation. Recent inflation and currency developments imply upside risks to our forecast for a further 100bp of tightening to a 6.50% terminal rate by year-end.

Turkey: CBRT maintains rates as widely expected but pressure continues to build

Turkey maintains rates as expected with emphasis on heterodox policies

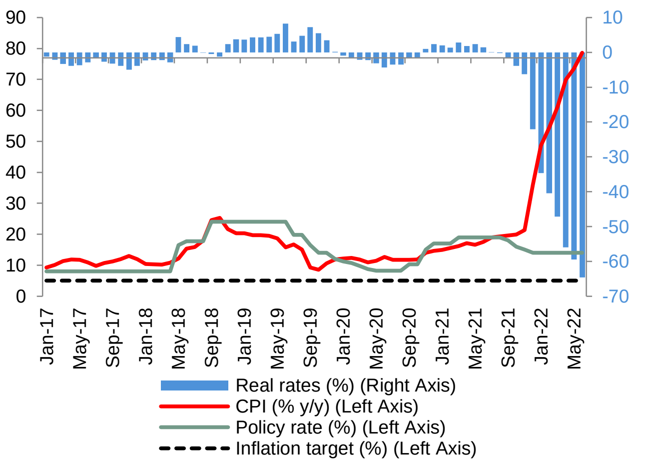
The Central Bank of Turkey (CBRT) kept the key rate unchanged at 14.00% last week in line with our (and consensus) expectations. Among the negligible changes to the press release was the Monetary Policy Committee's (MPC) statement on the increased likelihood of slower external growth. The CBRT acknowledged the risk to the current account from a possible global recession, alongside the broader ramifications of elevated commodity prices. The MPC's view on the current account has pivoted from surplus expectations to the recognition of more downside risks from external factors in light of a widening current account deficit throughout 2022. More broadly, we believe that the current macro backdrop remains exceptionally untenable and see real rates moving deeper into negative territory in the remaining months of the 2022, fuelling headline inflation further and considerably derailing inflation expectations. We estimate inflation rising to 92% y/y by September and now only falling to 75% y/y by end-2022 (with strong support from favourable base effects in the final month of the year). Beyond inflation, Turkey's current account deficit has been widening precipitously this year, while FX inflows have slowed, leading to a deterioration in the CBRT's reserve positon, causing pressure on the Lira (TRY).

Our base case is that the CBRT will reluctantly change course with a pivot back to conventional policy

Looking ahead, we reiterate our conviction that the CBRT will likely change course and tighten policy in an orthodox manner but do so reluctantly – our base case is for the CBRT to raise rates from a trough of 14% to 20% by year-end (see here and here). Our rationale is centred on the premise that the acute deterioration in the inflation outlook, in tandem with the fragility of the TRY, as well as the risk premium since the inception of the rate cuts in September 2021, necessitates a significantly tighter monetary policy stance to anchor expectations and promote price stability. With real policy rates so deeply negative (-65%), the current monetary policy stance is unambiguously unsustainable and the pressure on the TRY is likely to continue in the absence of a policy U-turn.

TURKEY CONTINUES TO MAINTAIN RATES AT 14% BUT DEEPLY NEGATIVE REAL RATES ARE UNSUSTAINABLE

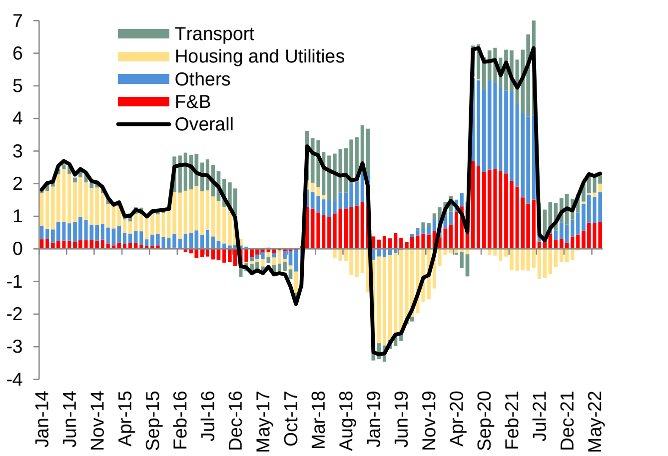
TURKEY INFLATION AND TARGET (% Y/Y) VS RATES (NOMINAL/REAL) (%)



Source: Bloomberg, CBRT, MUFG Research

SAUDI INFLATION REMAINS LOW AS PRICE RIGIDITIES AND FX GAINS GUARD AGAINST IMPORT PRICE SHOCKS

SAUDI ARABIA HEADLINE CPI AND CONTRIBUTION TO INFLATION (% Y/Y)



Source: Bloomberg, CBRT, MUFG Research

In the interim, we acknowledge that a host of heterodox policies will continue to be adopted to help stabilise the TRY

Whilst our core scenario is that the policy adjustment will be in an orthodox fashion, we acknowledge that a continuation of heterodox measures could materialise over the near-term to encourage de-dollarisation, bolster reserves and manage other aspects of the economy (even if this has negative reverberations on the budget or adds significantly to the government's contingent liabilities). Ultimately, we see the CBRT's reaction function likely being geared by adverse shocks that could intensify the prevailing challenging dynamics in the FX market. A taxing external financing outlook due to the weakness in the current account, in tandem with the increase in the risk premium, suggests a more restrictive policy stance going forward. Though recent evidence signals that the authorities are content on unconventional measures such as the FX protected deposit scheme, revenue indexed bonds and other macroprudential measures, rather than convention rate hikes.

Saudi Arabia: inflationary pressures continue to remain moderate relative to peers

Saudi Arabia's inflation rate remains benign with SAMA likely to hike less than the Fed once again

Compared to most EM peers, Saudi Arabia's inflationary pressures continues to remain moderate. In June, headline CPI remained broadly stable at 2.3% y/y from 2.2% y/y in May. We continue to expect headline to peak between July and August before gradually moving lower. Our forecast remains unchanged for CPI to average 1.7% in 2022 and 3.4% in 2023. From a monetary policy perspective, the Saudi Central Bank (SAMA) did not fully match the Fed in June, and was alone in the GCC in hiking by 50bps rather than 75bps. The divergence highlights the tension between Saudi Arabia's policy needs and those of the US where inflation is much more pronounced. However, we view the move as fine tuning, not the start of a break from the dollar-peg. As a result, we expect rates to rise with the Fed over H2-22, but look for the authorities to use other tools to support credit conditions (SAMA deposited USD10bn in the banking system in June to boost liquidity) and to draw on their fiscal strength to support growth if required.

Week ahead

Czech Republic: Q2 2022 GDP likely to print flat

Czech economic growth likely muted in Q2 2022 owing to counterbalancing forces

The Czech Statistical Office will release its flash estimate for Q2 2022 GDP on 29 July. We expect GDP growth to have slowed to 3.5% y/y (consensus 3.4% y/y) owing to counterbalancing forces. Industrial production was relatively strong in the quarter, offset by relatively weak retail sales. Though tourism-related sectors has remained relatively robust, given an ongoing boost from post-COVID normalisation despite the war in Ukraine.

Hungary: MNB to continue hiking owing to elevated inflation and currency pressures

Hungary to tighten policy further

The National Bank of Hungary (MNB) is set to meet on 26 July and we forecast the Monetary Policy Committee (MPC) to raise its base rate and the one week deposit rate by 100bp to 10.75%, in line with consensus expectations. Over the past month, the MNB has been under marked pressure, raising the base rate from 5.90% before the June MPC meeting, to a current level of 9.75% (over the same period the one week deposit rate was raised from 7.25% to 9.75%). While challenging inflation dynamics called for further rate hikes, the aggressive tightening was due to significant exchange rate depreciation pressures. The Hungarian Forint (HUF) weakness partly reflects the weak external position, as the current account deficit widened over the course of 2021 and into 2022. Part of the widening was driven by significant fiscal spending leading up to April's election and since then the government has announced a number of fiscal consolidation measures. However, in recent months, the country has faced additional negative terms-of-trade shocks, which has pushed the external position into a greater deficit and it is unclear whether fiscal policy will be sufficiently tight to stabilise external balances. Looking ahead, we anticipate a terminal rate of 13.00% before year-end, reflecting FX concerns as well as guidance from the MNB that it will continue to tighten policy until inflation peaks.

Weekly calendar

	Country	Day	GMT	Indicator/Event	Period	MUFG Forecast	Consensus	Previous	Market Moving
	Hungary	26/07/2022	13:00	Monetary policy meeting (%)	---	10.75%	10.75%	9.75%	!!!
	Russia	27/07/2022	17:00	Industrial production (% y/y)	Jun	---	-9.3%	-10.1%	!!
	Kenya	29/07/2022	---	CPI (% y/y)	Jul	---	---	7.9%	!!
	Czech Rep.	29/07/2022	08:00	Real GDP (% y/y)	Q2-22	3.5%	3.4%	4.9%	!!!
	Poland	30/07/2022	09:00	CPI (% y/y)	Jul	---	15.7%	15.5%	!!!

Source: Bloomberg, MUFG Research

Forecasts at a glance

EM EMEA economic growth, fiscal balance and current account balance

	Real GDP (%, y/y)			Fiscal balance (% of GDP)			Current account (% of GDP)		
	Latest	2021	2022	Latest	2021	2022	Latest	2021	2022
Bahrain	19.66	6.00	3.50	-10.61	-8.00	-8.02	-2.06	-2.90	-2.87
Czech Rep.	4.90	2.90	3.00	0.27	-8.03	-5.47	5.02	1.57	0.82
Egypt	0.91	3.30	5.50	-7.41	-7.33	-6.33	-4.17	-3.88	-3.66
Greece	15.39	6.50	4.30	0.57	-10.25	-4.29	-2.70	-7.41	-5.14
Hungary	8.20	7.30	4.30	-2.05	-6.60	-5.94	-4.59	0.60	0.88
Iraq	4.43	3.60	6.70	0.86	-1.55	-2.53	1.12	6.16	4.00
Israel	9.60	7.00	5.00	-3.91	-6.81	-4.33	5.61	4.46	3.82
Jordan	1.96	2.00	2.20	-5.98	-7.69	-5.94	-8.59	-8.93	-4.45
Kenya	5.37	5.50	5.60	-7.73	-8.01	-6.67	-5.82	-5.04	-5.10
Kuwait	0.43	4.50	6.40	5.38	-1.47	0.99	3.06	15.51	13.27
Lebanon	-6.90	-5.20	2.00	-10.50	---	---	-27.45	---	---
Libya	9.89	123.20	5.30	2.19	6.77	12.46	-0.30	19.23	15.39
Morocco	0.30	5.70	3.10	-4.13	-6.49	-5.91	-3.95	-3.07	-3.25
Nigeria	3.11	2.50	5.60	-4.76	-6.11	-5.96	-3.49	-3.22	-2.25
Oman	-0.83	2.70	0.90	-7.06	-2.57	1.11	-4.38	-5.75	-0.94
Poland	8.50	5.00	4.50	-0.74	-4.25	-1.90	1.08	2.26	1.56
Romania	6.43	7.60	3.00	-4.56	-6.70	-5.59	-10.07	-5.71	-5.53
Qatar	2.50	2.90	6.00	4.93	2.78	5.68	-27.67	8.20	11.56
Russia	3.97	4.40	-7.00	1.92	-0.56	0.02	1.11	5.74	4.41
Saudi Arabia	9.94	4.50	11.20	-4.45	-3.05	2.79	-0.39	3.87	3.79
South Africa	3.00	5.10	1.60	-2.27	-8.44	-6.99	1.22	2.88	-0.86
Turkey	7.34	9.80	1.60	-5.65	-4.92	-5.58	0.00	-2.42	-1.61
Ukraine	-15.10	4.00	-28.00	-2.04	-4.50	-3.50	1.35	-0.69	-2.44
UAE	5.30	5.00	5.00	-0.76	-0.54	-0.22	2.44	9.67	9.37

EM EMEA inflation, interest rates and FX

	Inflation (% y/y, average)			Policy interest rates (%)			FX (against USD)		
	Latest	2020	2021	Latest	End-2021	End-2022	Latest	End-2021	End-2022
Bahrain	3.50	3.90	1.90	3.75	3.75	3.00	0.377	0.377	0.377
Czech Rep.	17.20	3.90	11.30	7.00	3.75	5.50	24.578	24.886	21.380
Egypt	13.20	5.40	7.90	11.25	7.75	11.50	18.904	15.723	15.420
Greece	12.09	-0.10	0.40	0.50	0.50	0.40	1.021	1.137	1.132
Hungary	11.70	4.90	7.80	9.75	2.40	5.50	388.7	324.5	314.70
Iraq	5.40	6.40	5.00	4.00	4.00	5.00	1460	1460	1460.000
Israel	4.44	1.50	2.80	1.25	1.25	0.50	3.439	3.103	3.100
Jordan	4.39	1.60	2.00	4.50	4.50	2.00	0.709	0.709	0.709
Kenya	7.90	6.00	5.90	7.50	7.50	9.50	118.710	113.140	113.040
Kuwait	4.52	2.90	3.40	2.25	2.25	3.00	0.307	0.303	0.303
Lebanon	210.08	124.10	85.00	2.75	2.75	7.75	1509.640	1512.330	1512.330
Libya	4.56	21.10	8.00	3.00	3.00	3.00	4.877	4.597	4.597
Morocco	7.20	1.40	1.20	1.50	1.50	1.50	10.221	9.252	9.250
Nigeria	18.60	17.30	12.00	14.00	14.00	14.00	423.460	424.830	440.500
Oman	2.85	1.30	2.00	1.23	1.23	14.00	0.385	0.385	0.385
Poland	15.50	4.90	10.00	6.50	1.75	5.50	4.640	4.035	3.948
Romania	15.05	5.30	11.90	4.75	4.75	5.50	4.829	4.353	4.388
Qatar	5.41	1.60	4.00	2.50	2.50	2.50	3.641	3.642	3.642
Russia	15.90	6.60	16.60	8.00	5.75	15.00	118.690	74.679	71.130
Saudi Arabia	2.31	3.10	2.20	1.75	1.75	2.50	3.757	3.755	3.755
South Africa	7.40	4.50	6.20	5.50	3.50	4.75	16.828	15.937	15.800
Turkey	78.62	17.90	62.00	14.00	14.00	20.00	17.727	13.317	14.250
Ukraine	21.50	9.40	15.30	25.00	25.00	14.00	36.751	27.285	29.800
UAE	2.50	0.10	1.20	0.65	0.65	2.00	3.673	3.673	3.673

Core indicators

EM EMEA sovereign bond yields (%)

	Maturity	24-Jun	01-Jul	08-Jul	15-Jul	22-Jul	Change in yield (basis points) Week	MTD	YTD
Bahrain	10 years	5.24	5.36	5.26	5.62	5.54	-7.59	30.47	300.69
Czech Rep.	10 years	5.34	4.88	4.92	4.93	4.83	-9.55	-30.63	174.94
Egypt	9 years	12.30	13.70	13.84	15.91	15.22	-69.68	142.57	805.52
Greece	8 years	3.37	3.18	3.32	3.25	3.04	-20.70	-25.28	193.19
Hungary	8 years	8.18	8.18	9.34	10.14	9.44	-70.17	119.54	497.62
Israel	8 years	2.79	2.72	2.68	2.65	2.58	-6.82	-20.93	236.44
Jordan	5 years	8.29	8.58	8.63	9.31	8.28	-103.61	-59.32	400.56
Kenya	7 years	13.57	14.47	15.15	16.92	15.29	-162.42	72.95	958.77
Kuwait	6 years	3.53	3.30	3.41	3.37	3.27	-10.42	-26.96	157.20
Lebanon	9 years	82.39	87.94	88.80	91.14	92.24	110.37	336.84	2823.94
Morocco	11 years	5.72	6.21	6.21	6.71	6.34	-37.27	4.70	394.07
Nigeria	9 years	13.00	13.21	13.52	14.81	13.29	-151.60	-2.50	590.29
Oman	9 years	6.34	6.53	6.55	7.19	6.38	-80.91	-26.04	163.16
Poland	8 years	2.79	2.73	2.78	2.78	2.71	-6.58	-9.70	254.12
Romania	7 years	5.65	5.53	5.67	5.90	5.61	-29.21	-16.03	406.13
Qatar	9 years	3.94	3.81	3.87	3.81	3.78	-3.26	-14.49	152.99
Russia	5 years	61.86	51.15	43.51	43.21	35.81	-740.28	-1113.23	-73.07
Saudi Arabia	8 years	4.10	3.97	3.89	3.89	3.71	-17.57	-33.73	156.59
South Africa	9 years	6.85	7.27	7.53	7.77	6.96	-81.36	-50.32	274.04
Turkey	7 years	9.82	10.63	11.06	11.67	10.75	-92.33	-6.51	353.17
Ukraine	8 years	43.46	46.51	54.55	58.15	56.58	-157.38	906.20	4,709.52
Abu Dhabi	6 years	3.52	3.33	3.32	3.32	3.18	-13.27	-37.34	143.22
Dubai	8 years	4.16	4.11	4.10	4.10	4.09	-1.87	-4.90	150.54

EM EMEA equity market (index)

	17-Jun	24-Jun	01-Jul	08-Jul	15-Jul	22-Jul	Change (%) Week	MTD	YTD
Bahrain	1,850	1,829	1,825	1,869	1,872	1,887	0.76	2.55	4.97
Czech Rep.	102,807	98,080	98,542	100,730	97,881	98,925	1.07	0.39	-5.63
Egypt	9,981	9,698	9,180	8,658	8,764	9,276	5.84	0.55	-22.37
Greece	839	836	822	779	803	830	3.32	2.41	-7.09
Hungary	39,225	40,036	39,900	39,352	38,903	42,328	8.80	7.87	-16.55
Israel	1,822	1,834	1,865	1,826	1,854	1,915	3.29	4.69	-3.21
Jordan	2,435	2,412	2,460	2,548	2,568	2,602	1.34	5.10	22.83
Kenya	128	120	118	132	138	137	-1.36	9.72	-17.96
Kuwait	7,401	7,217	7,397	7,384	7,360	7,662	4.10	3.42	8.78
Lebanon	658	658	658	658	658	658	0.00	-2.18	36.03
Morocco	12,359	12,026	12,058	11,632	11,742	11,924	1.55	-0.71	-10.74
Nigeria	52,775	51,377	51,802	51,557	51,339	51,980	1.25	0.31	21.69
Oman	4,113	4,137	4,125	4,124	4,141	4,318	4.26	4.73	4.55
Poland	1,707	1,681	1,733	1,655	1,656	1,702	2.78	0.34	-24.93
Romania	12,076	12,301	12,571	12,286	12,022	12,230	1.73	-0.53	-6.37
Qatar	12,627	11,943	12,237	12,061	11,868	12,751	7.44	4.59	9.68
Russia	2,319	2,374	2,379	2,222	2,074	2,097	1.11	-4.90	-44.64
Saudi Arabia	11,979	11,320	11,727	11,417	11,163	11,975	7.28	3.92	6.15
South Africa	61,163	59,415	61,554	59,703	60,032	61,767	2.89	2.76	-7.88
Turkey	2,531	2,574	2,402	2,408	2,408	2,517	4.50	4.62	35.47
Ukraine	519	519	519	519	519	519	0.00	0.00	-0.68
Abu Dhabi	9,584	9,302	9,408	9,251	9,244	9,662	4.52	3.07	13.83
Dubai	3,336	3,236	3,246	3,062	3,154	3,257	3.27	1.04	1.91

EM EMEA FX against USD*

	17-Jun	24-Jun	01-Jul	08-Jul	15-Jul	22-Jul	Change (%) Week	MTD	YTD
USD Index	103.631	104.431	104.685	107.130	108.063	106.730	-1.23	1.95	11.56
Bahrain**	0.379	0.379	0.379	0.379	0.379	0.379	-0.05	0.00	0.18
Czech Rep.	23.546	23.434	23.760	24.197	24.316	24.039	-1.14	-1.82	-8.98
Egypt	18.762	18.762	18.797	18.868	18.868	18.904	0.19	0.57	20.23
Greece***	1.050	1.055	1.041	1.019	1.008	1.021	1.32	-2.58	-10.18
Hungary	380.760	380.500	384.380	398.190	397.730	388.740	-2.26	-2.73	-16.54
Israel	3.454	3.403	3.520	3.464	3.468	3.440	-0.78	1.53	-9.80
Jordan**	0.710	0.710	0.710	0.710	0.710	0.710	0.06	0.01	-0.18
Kenya	117.647	117.647	0.009	0.009	0.008	0.008	0.00	1.19	4.76
Kuwait	0.307	0.307	0.307	0.307	0.307	0.307	0.00	-0.15	-1.51
Lebanon	1,511.15	1,510.75	1,509.75	1,509.64	1,509.64	1,509.64	0.00	-0.13	0.18
Morocco	10.091	10.022	10.051	10.164	10.420	10.221	-1.90	-1.43	-9.49
Nigeria	417.180	416.880	418.080	424.780	423.040	423.460	0.10	-0.61	0.32
Oman**	0.385	0.385	0.385	0.385	0.386	0.386	0.00	-0.05	0.23
Poland	3.756	3.755	3.755	3.755	3.754	3.750	-0.12	0.13	0.11
Romania	4.711	4.685	4.748	4.855	4.902	4.829	-1.48	-2.32	-9.87
Qatar**	3.661	3.661	3.659	3.659	3.659	3.661	0.07	-0.07	0.35
Russia	57.500	53.480	55.807	63.927	57.000	58.190	2.09	-6.07	29.18
Saudi Arabia**	3.756	3.755	3.755	3.755	3.754	3.750	-0.12	0.13	0.11
South Africa	16.018	15.802	16.415	16.873	17.075	16.828	1.47	-3.26	-5.29
Turkey	17.331	16.926	16.750	17.259	17.362	17.731	-2.08	-5.82	-24.97
Ukraine	29.538	29.528	29.403	29.547	29.403	36.751	24.99	-20.00	-25.76
UAE**	3.673	3.673	3.673	3.672	3.672	3.672	0.00	0.01	0.05

Note: * Exchange rate quoted as amount of USD per currency in line with market convention, other exchange rates are amount per USD; ** 12 month forward given pegged against USD; *** EUR per USD

EM EMEA 5 year CDS spreads (basis points)

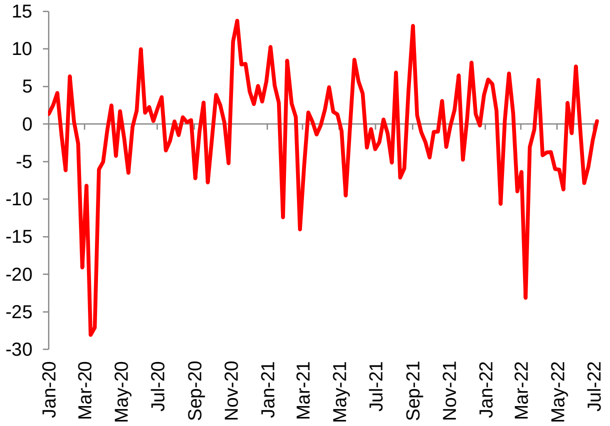
	17-Jun	24-Jun	01-Jul	08-Jul	15-Jul	22-Jul	Change in yield (basis points) Week	MTD	YTD
Bahrain	309.92	338.07	317.20	314.82	314.82	312.87	-1.95	21.15	19.04
Czech Rep.	39.73	39.97	39.69	38.10	38.10	33.70	-4.40	-5.99	-1.92
Egypt	864.13	922.60	751.43	778.14	924.42	943.00	18.58	191.57	444.96
Greece	155.29	172.61	165.17	174.12	174.12	167.87	-6.25	2.70	55.88
Hungary	120.76	125.00	128.20	129.97	129.97	160.50	30.54	32.31	115.78
Israel	41.94	45.49	46.09	46.45	46.45	48.27	1.83	2.18	8.06
Kenya	855.37	927.71	695.06	813.38	1,013.97	1,060.63	46.66	365.57	653.75
Kuwait	62.73	66.75	69.76	69.37	67.89	68.44	0.55	-1.32	23.73
Morocco	117.27	201.56	205.95	207.84	231.57	241.75	10.19	35.80	146.36
Nigeria	620.36	811.73	811.44	700.65	894.66	893.92	-0.74	82.49	438.85
Oman	257.77	267.27	259.93	261.75	259.95	260.73	0.78	0.81	4.92
Poland	103.48	107.39	100.00	104.53	107.60	108.45	0.85	8.45	68.87
Romania	217.70	244.47	240.93	219.95	263.30	264.22	0.92	23.30	189.40
Qatar	67.70	68.20	60.36	62.04	62.54	62.69	0.16	2.33	18.94
Russia	5,377.20	10,121.04	14,418.18	9,954.09	14,413.29	10,195.04	- 4,223.14	- 4,223.14	10,070.62
Saudi Arabia	67.67	69.01	61.36	66.35	66.35	62.75	-3.60	1.39	13.37
South Africa	263.35	275.53	233.66	242.93	242.93	65.60	-177.34	-168.06	-137.43
Turkey	711.58	719.02	711.43	715.33	715.33	278.45	-436.88	-432.98	-284.31
Ukraine	5,708.78	4,812.47	3,615.89	5,108.84	7,710.87	11,106.86	3396.00	7490.98	10495.97
Abu Dhabi	67.01	68.01	59.42	60.71	61.09	123.85	62.76	64.43	80.95
Dubai	118.59	123.42	119.46	118.18	122.26	123.85	1.59	4.39	29.79

Source: Bloomberg, MUFG Research

EM capital flows

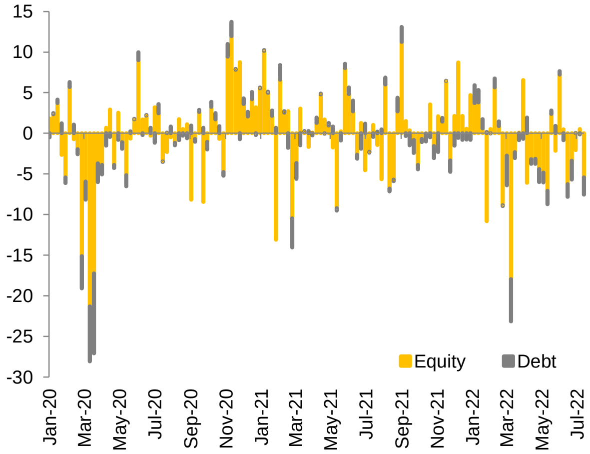
WEEKLY TOTAL EM OUTFLOWS OF USD-7.6BN – 15 JULY

TOTAL WEEKLY PORTFOLIO FLOWS (DEBT AND EQUITY) (USD BN)



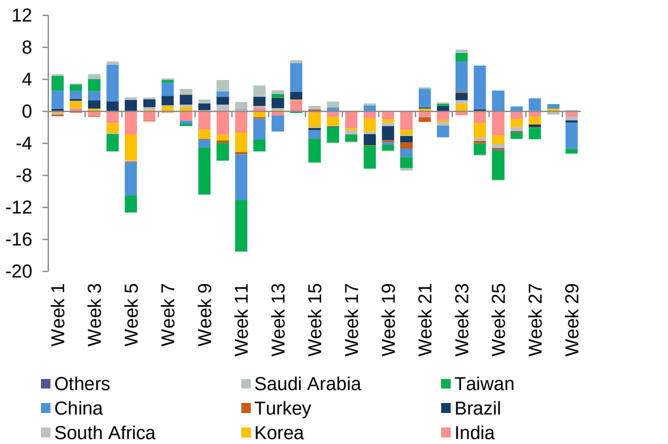
WEEKLY EM OUTFLOWS FROM EQUITY (USD-5.4BN) AND DEBT OUTFLOWS (USD-2.1BN) – 15 JULY

WEEKLY DEBT AND EQUITY FLOWS (USD BN)



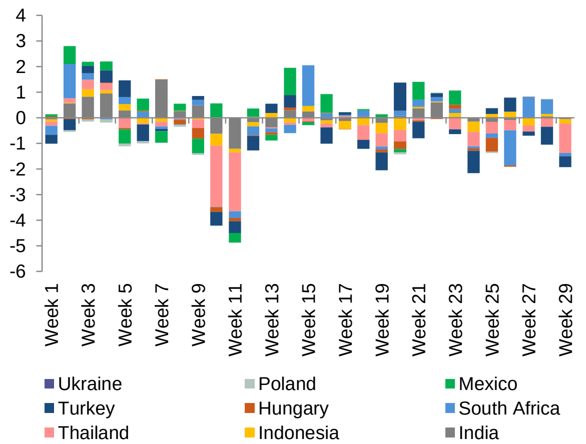
CHINA (USD-3.2BN) AND INDIA (USD-0.6BN) LED WEEKLY EM EQUITY OUTFLOWS – 15 JULY

WEEKLY PORTFOLIO FLOWS BY COUNTRY, WEEK 1 = JANUARY 2022 (EQUITY) (USD BN)



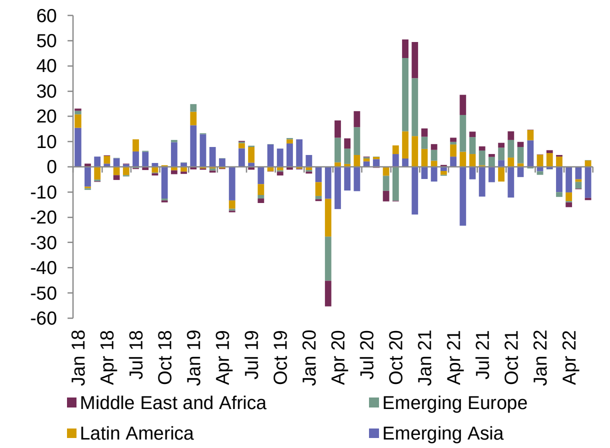
THAILAND (USD-1.1BN) LED EM DEBT OUTFLOWS LAST WEEK – 15 JULY

WEEKLY PORTFOLIO FLOWS BY COUNTRY, WEEK 1 = JANUARY 2021 (DEBT) (USD BN)



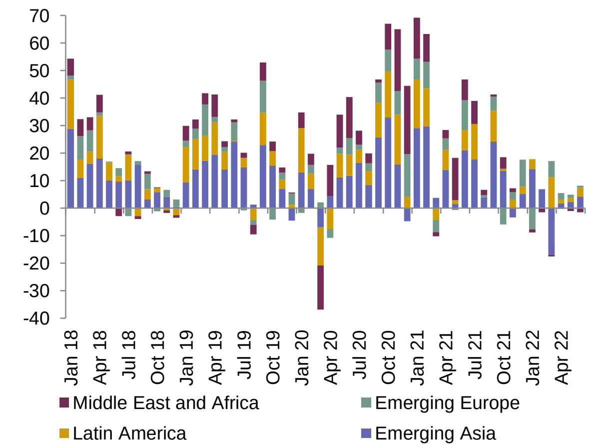
EM EQUITY OUTFLOWS TOTALLED USD-10.5BN IN JUNE, LED BY EM ASIA (USD-12.3BN)

MONTHLY PORTFOLIO FLOWS BY COUNTRY (EQUITY) (USD BN)



EM DEBT INFLOWS TOTALLED USD6.6BN IN JUNE, LED BY EM ASIA (USD4.4BN)

MONTHLY PORTFOLIO FLOWS BY COUNTRY (DEBT) (USD BN)



Source: Bloomberg, IIF, MUFG Research

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