TCW

INSIGHT

MONTHLY COMMENTARY

May Emerging Markets Update

ANISHA GOODLY | 7 JUNE 2019

We continue to be in a period of uncertainty until we get more clarity on the direction of both U.S./China and U.S./Mexico trade negotiations. G20 meetings at the end of the month should also provide more clarity. In the short term, the trade disputes are likely to result in a reduction in global trade, leading to a deferral of investment and encouraging precautionary savings. The market is certainly pricing in a slower growth scenario, moving U.S. rate cuts forward, and Powell's more dovish comments suggest that the Fed will remain accommodative.

Emerging Markets (EM) sovereigns are in a better place to weather the current environment, given a combination of solid balance sheets, high real rates, and room to cut rates if needed. Chinese growth has also recovered somewhat off the 4Q18 lows and stimulus measures have provided a further buffer as well.

EM sovereign spreads widened out to approximately 385 basis points (bps) in this recent downtrade, partially on the back of outflows in May. Spreads have tightened over the last few days to around 365bps, which is around 20bps cheap to long term averages. Barring any meaningful changes in fundamentals, if spreads widened meaningfully beyond 400bps, a level which has historically been an attractive entry point with a 6-12 month view, we would look to incrementally add some risk. As for local currency debt, we believe EMFX will be driven by trade-related headlines. Longer-term, we believe that the dollar is likely to turn on the back of growing fiscal and current account deficits in the U.S., and/or a stabilization in growth internationally relative to the slowing U.S. economy. In light of the uncertain environment, we continue to focus on those sovereigns that we believe will benefit from a better policy mix and corporates that have a deleveraging path. ■

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Ms. Goodly is the Portfolio Specialist for the TCW Emerging Markets and International Equities Groups. In this role, she serves as the primary liaison between TCW's Emerging Markets investment team and TCW's client relations and marketing professionals and is responsible for communicating investment strategies, performance and outlook to clients. Prior to joining TCW in 2013, Ms. Goodly spent eleven years at Morgan Stanley, most recently as an EM Fixed Income institutional salesperson. At Morgan Stanley, she also served as the Asia Credit Product Manager, marketing Asian credit products globally to the firm's largest institutional clients. In addition, she spent several years working as part of Morgan Stanley's Institutional Investor-ranked U.S. Credit Strategy research team. Ms. Goodly currently serves on the board of Consano and is an Ambassador for Girls Who Invest. Ms. Goodly graduated with a BA in Economics from Stanford University.