FitchSolutions

Emerging Markets Key Themes For 2023

Wednesday, November 23 2022

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Agenda

1 EMs Headed For Slowdown

2 Commodity Prices Will Weaken

3 Inflation Will Ease

4 Hiking Cycle Almost Over

5 Industrial Policy Is Back

6 No Return To EM Golden Age

1

Economic Growth

Most EMs Headed For Slowdown

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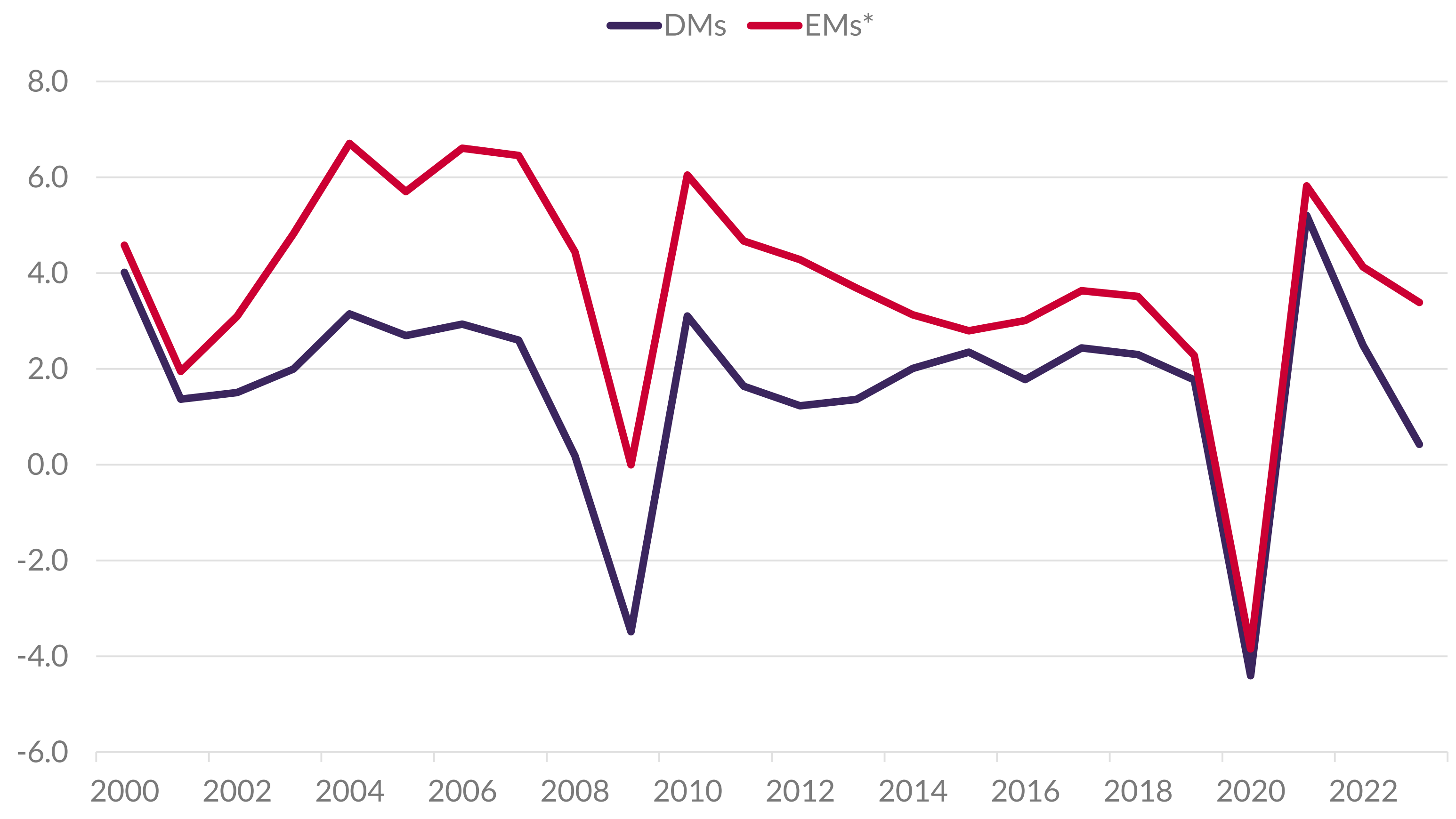
Growth: A Very Weak Outlook

Deceleration Will Continue
Global – GDP Growth, % (2000-2022)



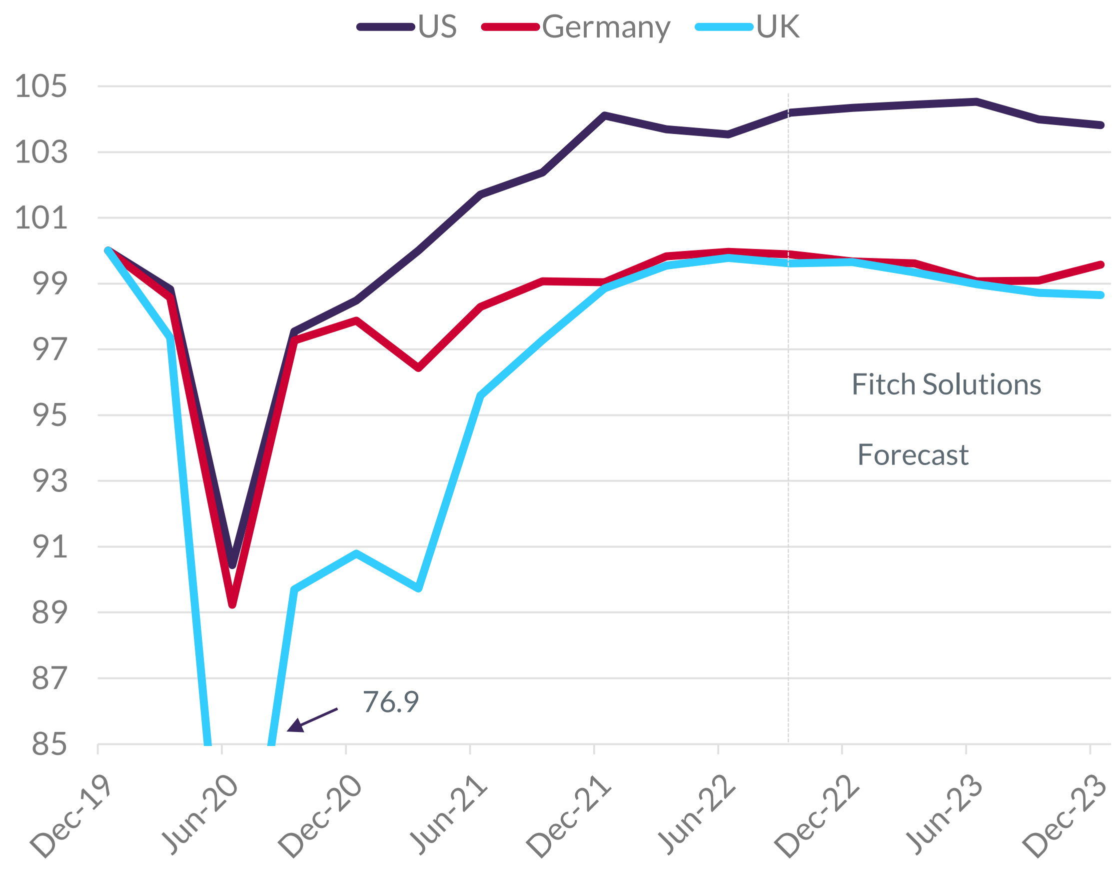
*Note:*EM figure excludes Mainland China, 2022 & 2023 = Fitch Solutions Forecast Source: Fitch Solutions*

- After briefly rebounding in 2021, emerging market (EM) growth slowed sharply in 2022.
- We expect that growth in most EMs will be even weaker in 2023 due to:
  - Lower commodity prices
  - Recessions in key developed markets (DMs)
  - Increased barriers to trade and investment
- Latin America and EM Europe will be the worst-performing regions.
- Mainland China will be a key exception.

Growth: DMs Will Drag Down EMs

DMs Set For Slowdown

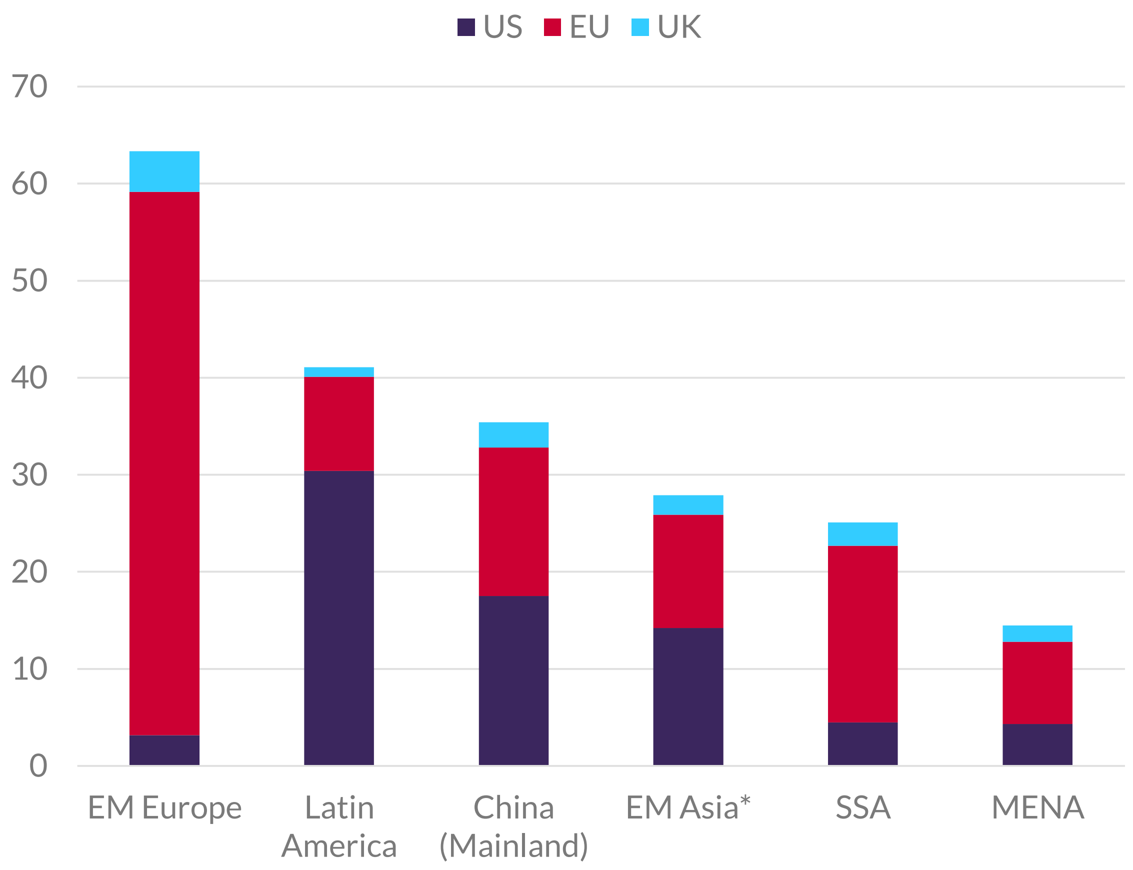
DMs – Real GDP Index, 100 = Q4 2019



Source: Fitch Solutions

DM Slowdown Most Painful In EM Europe, Latin America

EMs – Exports to DMs, % of total exports



**Note: Excludes Mainland China. Source: Fitch Solutions*

Growth: EM Europe, Latin America Will Lag Other EMs

Slowdown Will Be Broad-Based

EMs – Real GDP, %

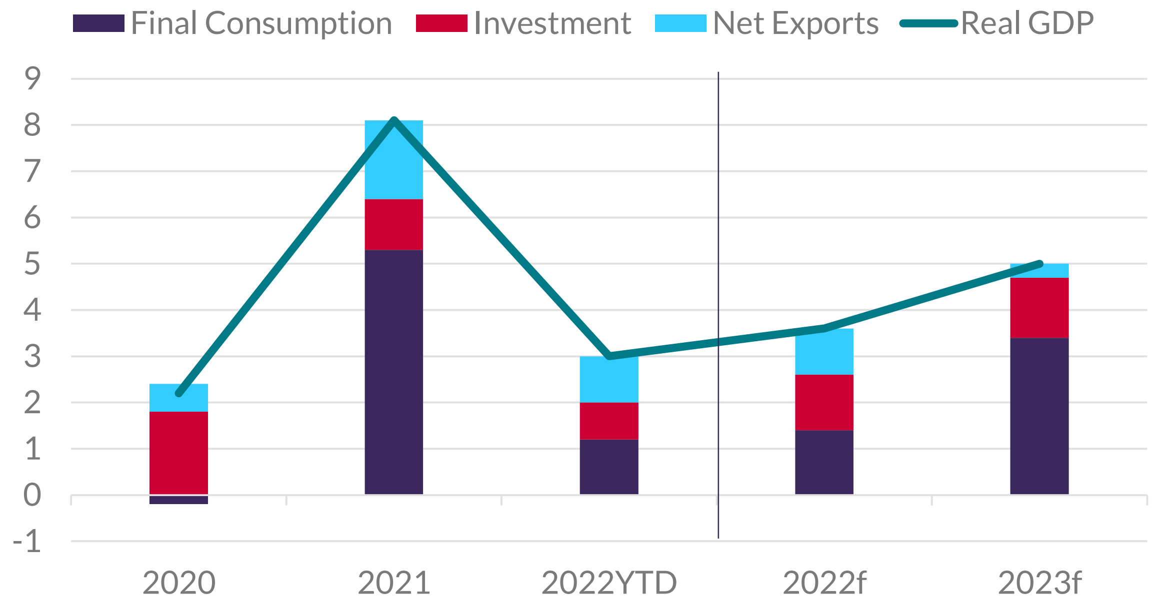
*Note:*Excludes Mainland China **Excludes Russia, Ukraine. e/f = estimate/forecast. Source: Fitch Solutions*

- We expect that almost all EM regions will perform worse in 2023 than they did in 2022
- The sharpest decelerations will be in Latin America and EM Europe
- Sub-Saharan Africa (SSA) and Mainland China will be the key exceptions
- In SSA, we expect slightly faster growth in South Africa and in East Africa.

Growth: Mainland China Will Pick up

Economic Recovery To Continue Into 2023

China (Mainland) – Real GDP Growth, %, & Expenditure Contribution, pp

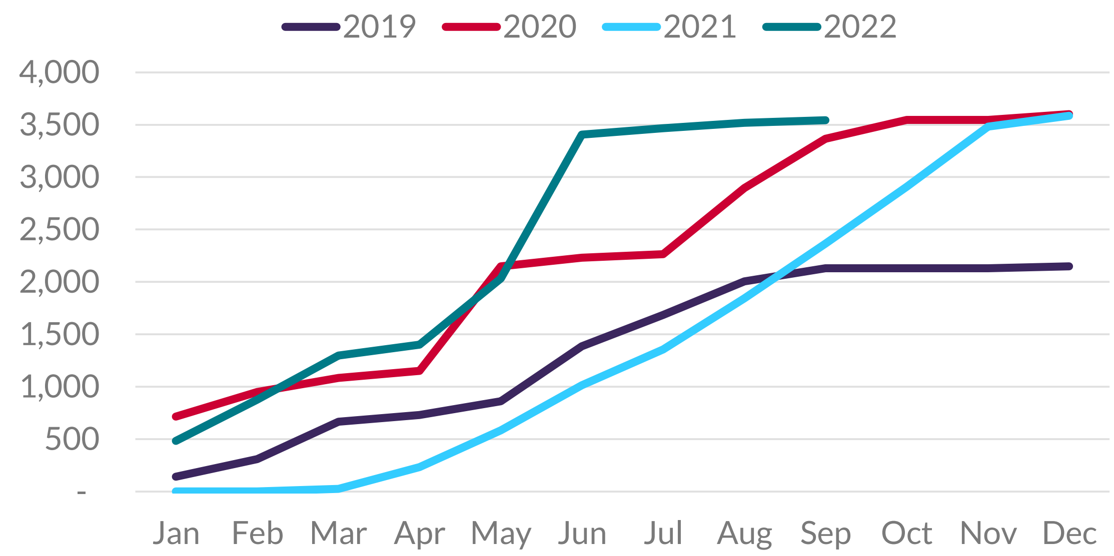


- Real GDP growth rebounded to 3.9% y-o-y in Q3, mainly driven by an improvement in investment and final consumption.
- Taking the latest figures into consideration, we are maintaining our growth forecast for 2022 at 3.6%. We expect real GDP growth to accelerate to 5.0% in 2023.

f= Fitch Solutions forecast. Source: National Bureau of Statistics, Fitch Solutions

Special Local Government Bond Issuance Accelerated

China (Mainland) – – Issuance Of Special Local Government Bonds, CNYbn ytd



- Growing headwinds stemming from a weakening external sector could potentially weigh on growth.
- However, this will be somewhat mitigated by a pickup in domestic economic activity as Covid-19 restrictions are eased and on the back of strong government measures to support the economy.

Source: Wind, Fitch Solutions

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Commodity Prices

Headed Down

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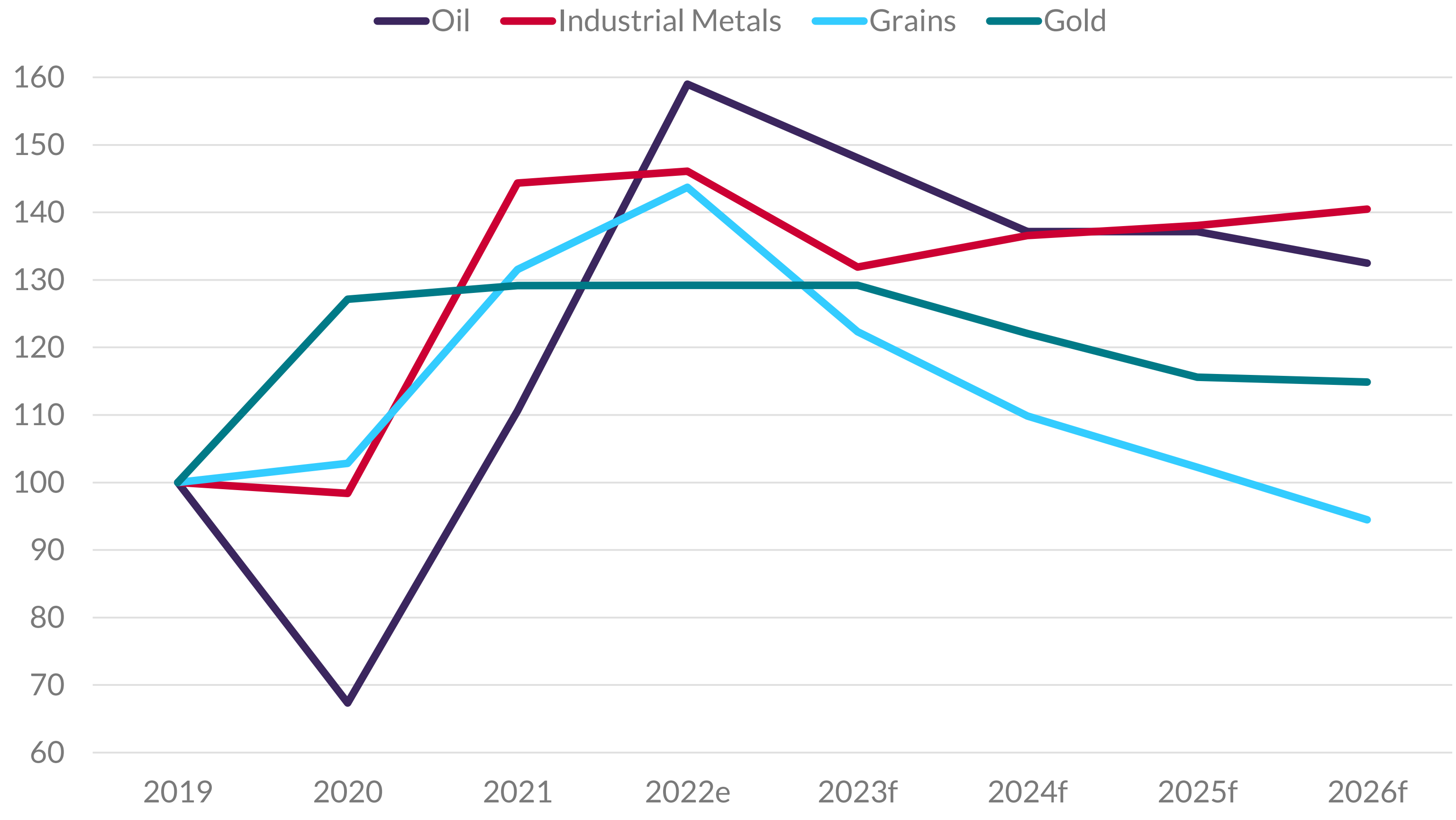
Commodities & Energy: Prices Have Peaked

Heading Down

Global – Commodity Price Indices, 100 = 2019 Average (2019-2024)



e/f = estimate/forecast. Source: Fitch Solutions

- Commodity prices have been highly volatile in recent years.
- Based on our core macro forecasts, we expect that most commodity prices have peaked, and will now gradually decline.
- The decline will be most pronounced for grain prices. Industrial metals, by contrast, will remain higher for longer.
- Lower prices will hit many EM exporters.

Commodities & Energy : Oil Pressures Will Weaken

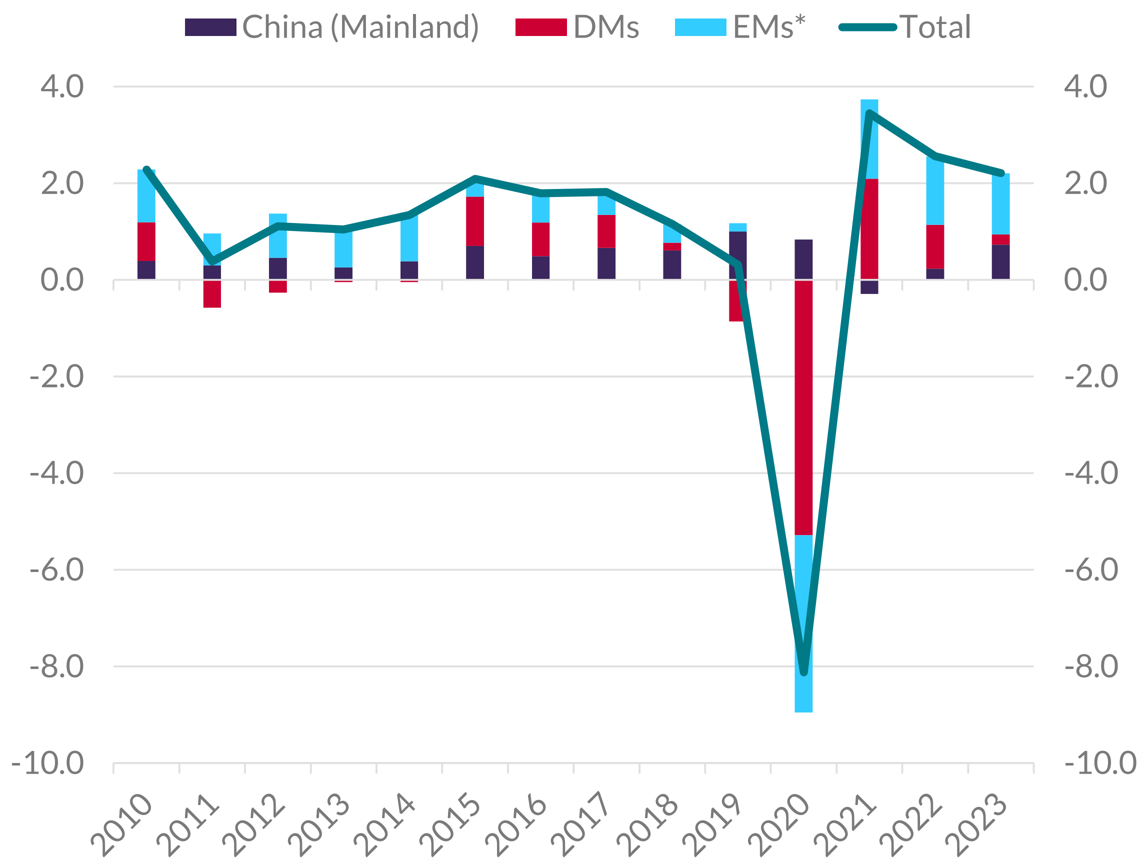
Oil Price Will Weaken…

Global – Brent, USD per barrel

Source: Fitch Solutions

…As Demand Growth Softens

Global – Change In Global Oil Demand, mn barrels

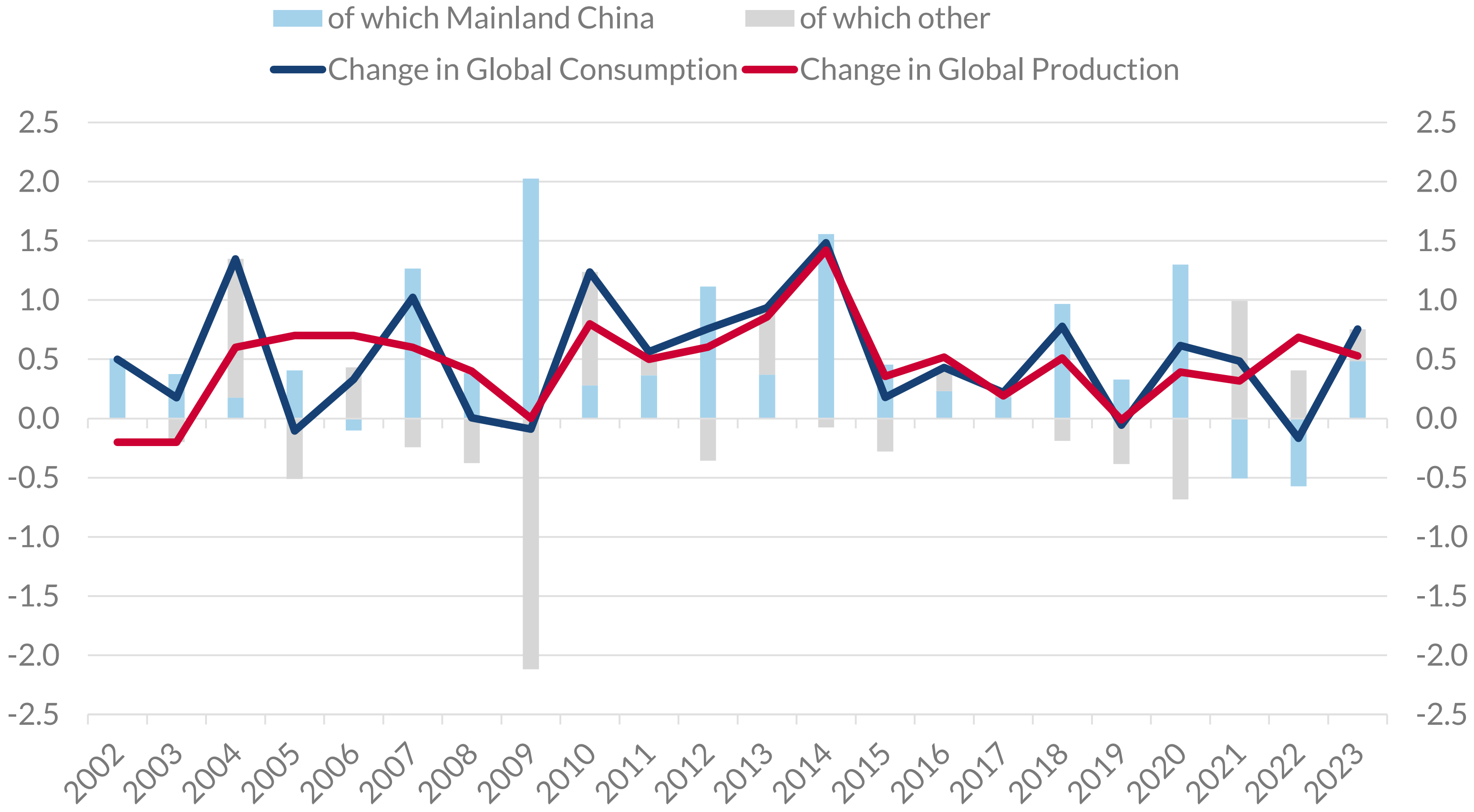


**Note: Excludes Mainland China. Source: Fitch Solutions*

Commodities: Industrial Metals Prices Will Ease Gradually

Mainland Chinese Growth Will Boost Copper Consumption

Global – Annual Change In Copper Production & Consumption, mn Tonnes



- Industrial metals prices will be supported by two key factors:
  - – Stimulus driven demand in Mainland China.
    - This is particularly important for copper and iron ore
  - – Supply constraints caused by limits on Russian exports
    - This is particularly important for nickel

3

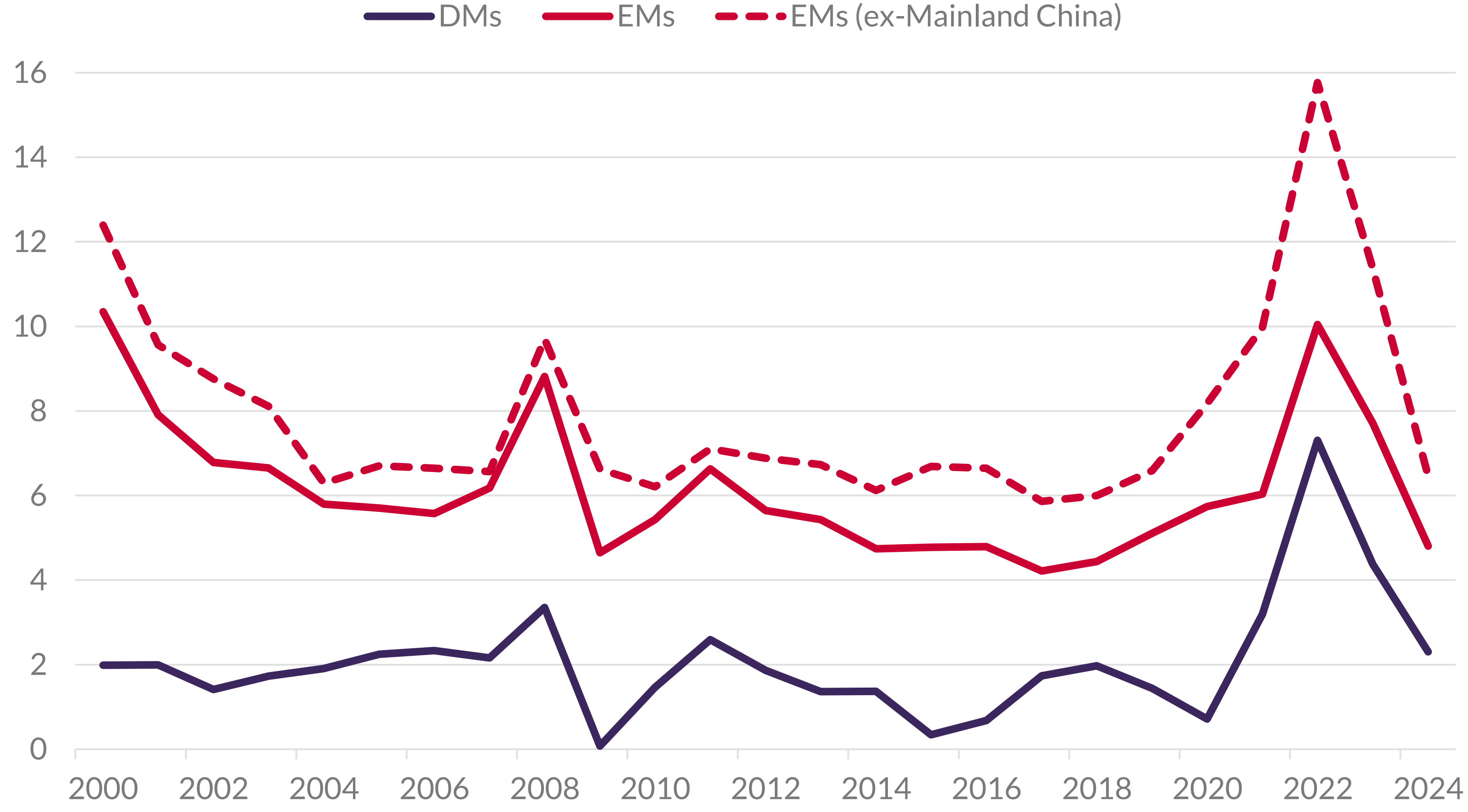
Inflation

Finally Easing

Inflation: Price Growth Has Peaked

Inflation Set to Ease In 2023

Global – Inflation, % (2000-2024)



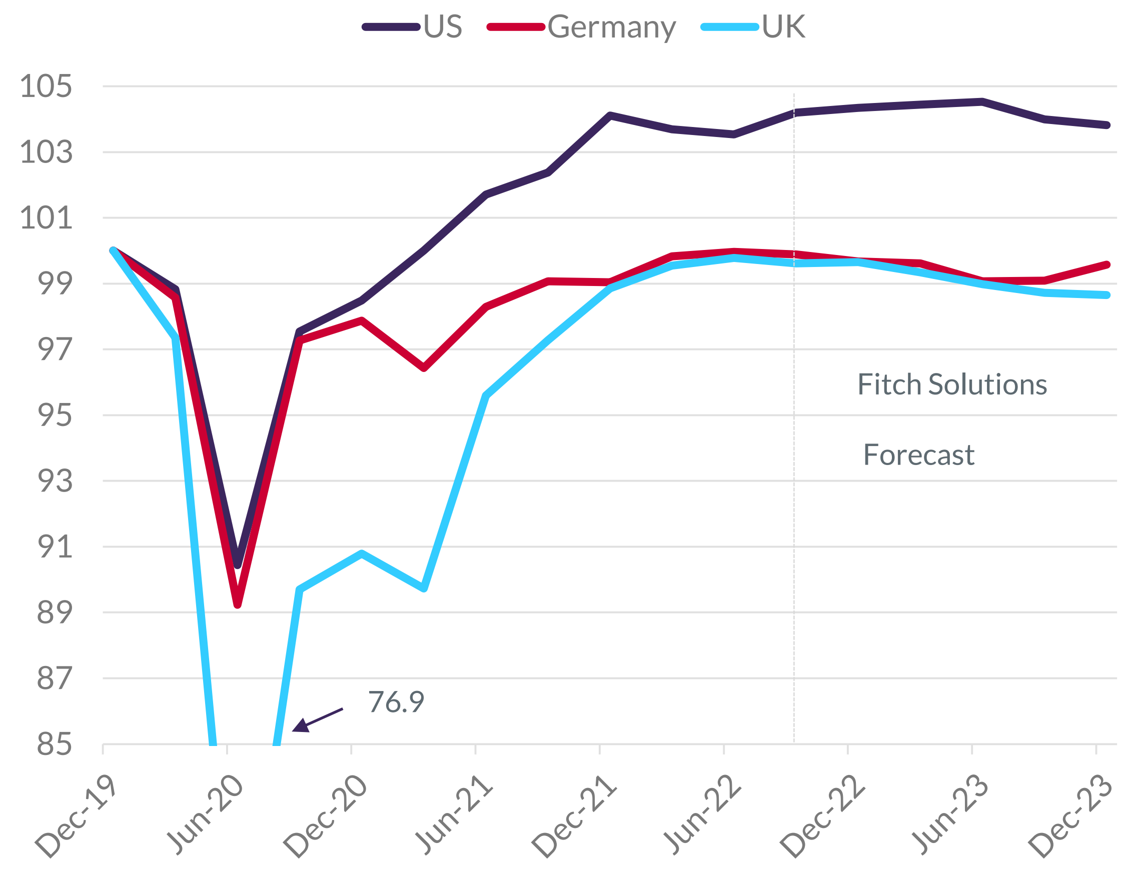
Source: Fitch Solutions Note: 2022, 2023, 2024 = Fitch Solutions Forecast

- We expect that inflation will ease across almost all EMs in 2023.
- There are key reasons for this view
  - Lower food & energy prices
  - Weaker demand
  - Reduced supply chain problems
  - A softer USD
- That said, the pace of deflation will differ across the EM world, with low income economies and EM Europe facing inflation for longer.

Inflation: Weaker Demand, Supply Chain Problems Will Ease

DMs Set For Slowdown

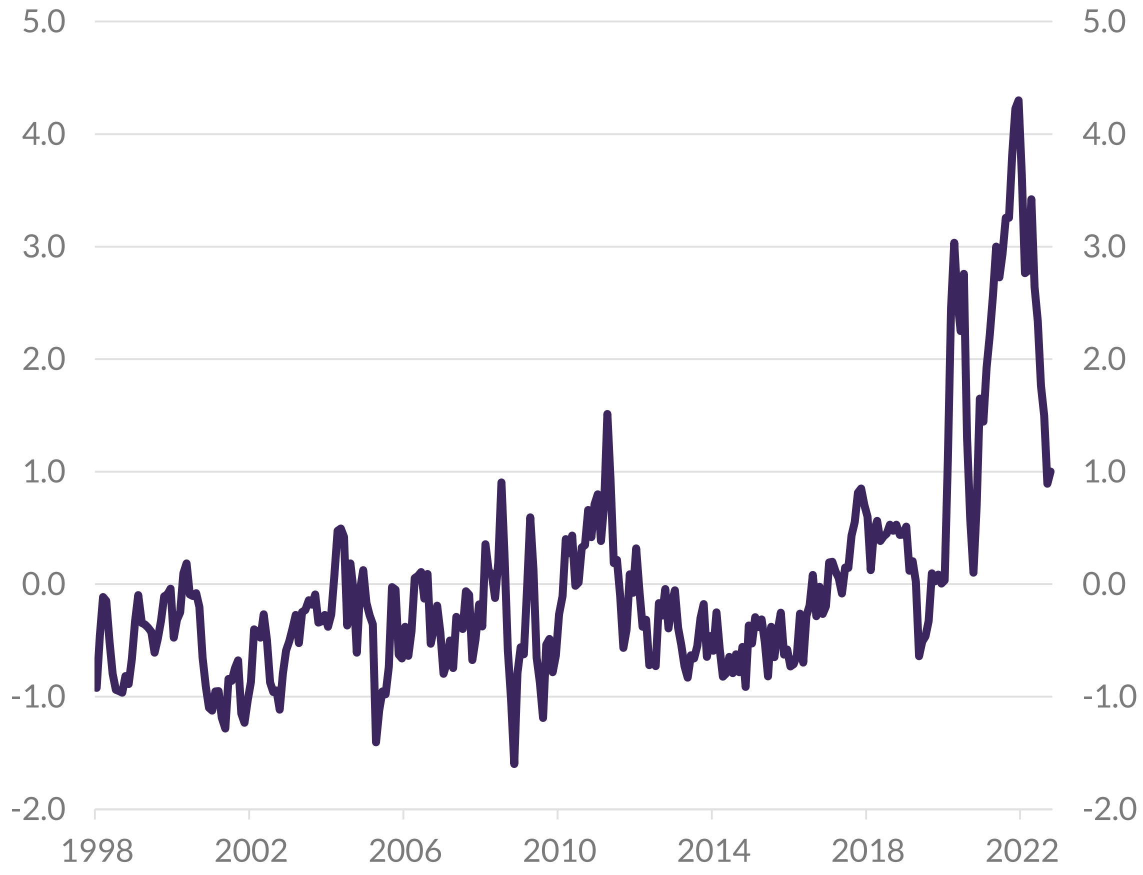
DMs – Real GDP Index, 100 = Q4 2019



Source: Fitch Solutions

Supply Chain Issues Fading

Global – Global Supply Chain Pressure Index

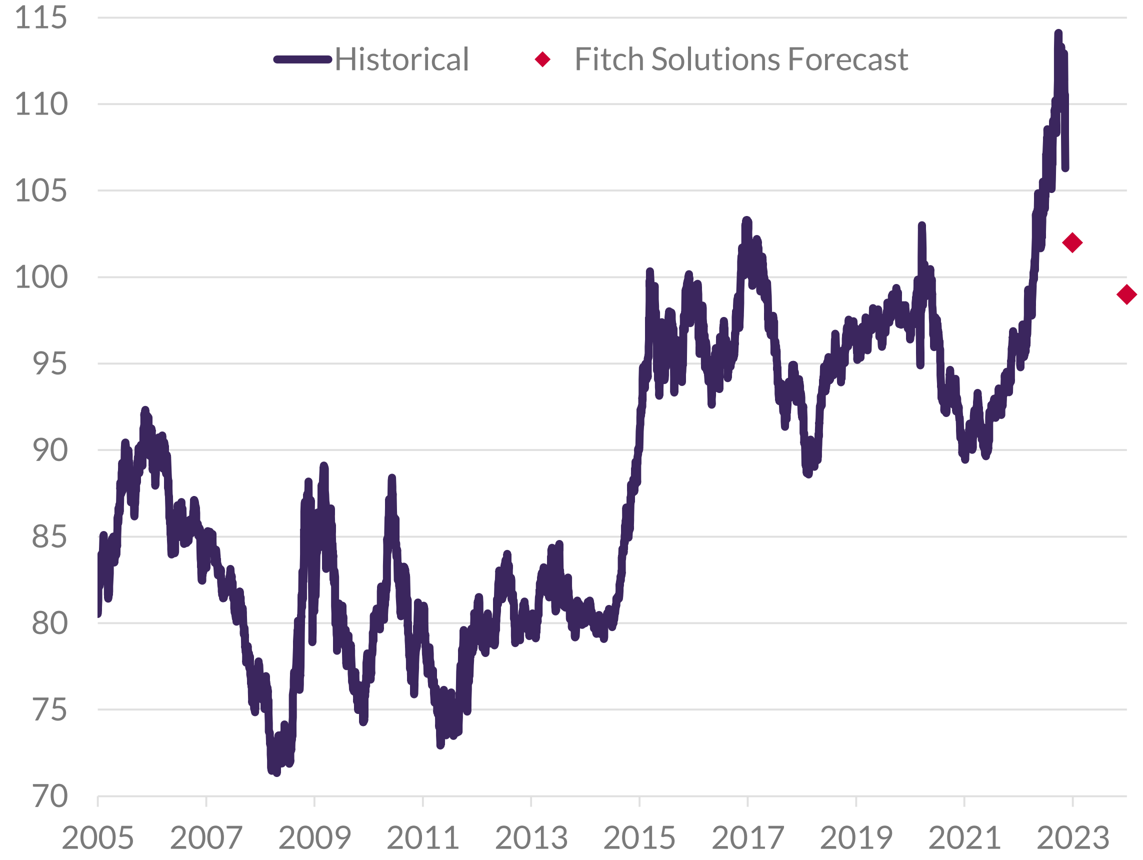


Source: Fitch Solutions

Inflation: External Factors Will Ease Up

Greenback Has Peaked…

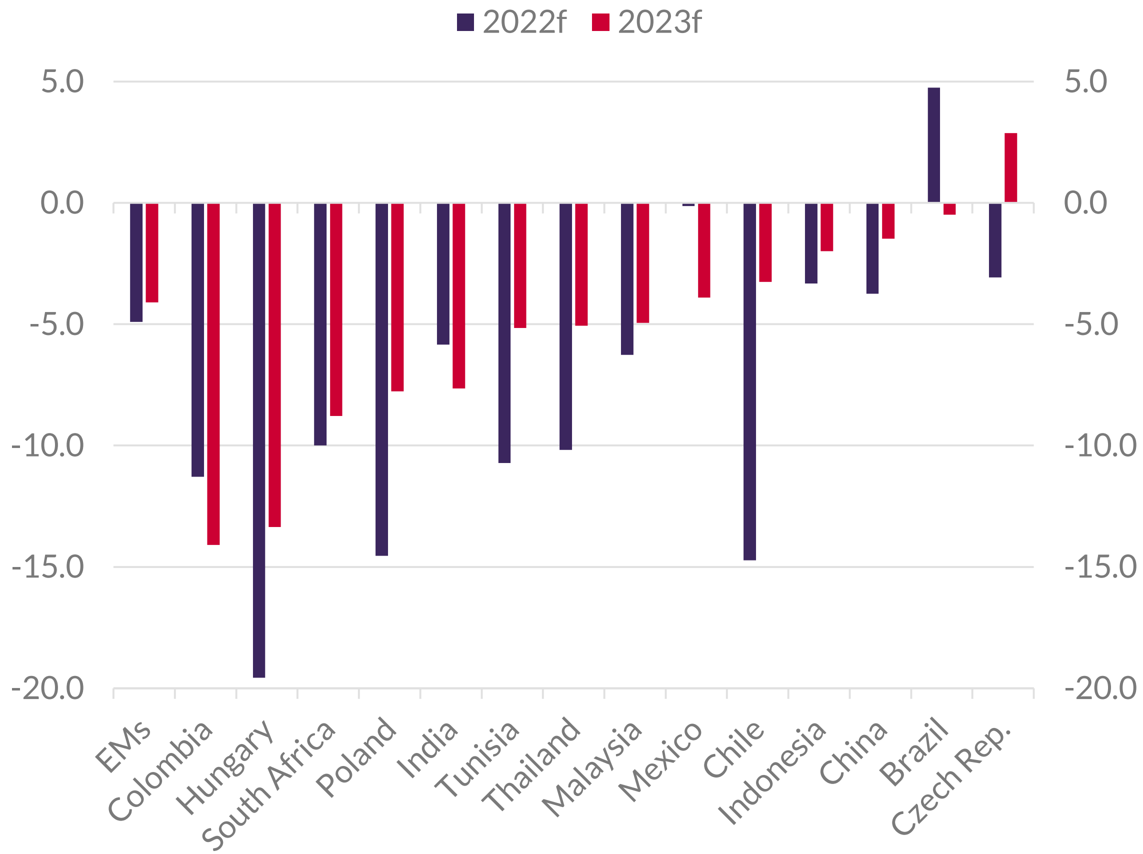
US – DXY Index



Source: Fitch Solutions

…Taking Pressure Off EM Currencies

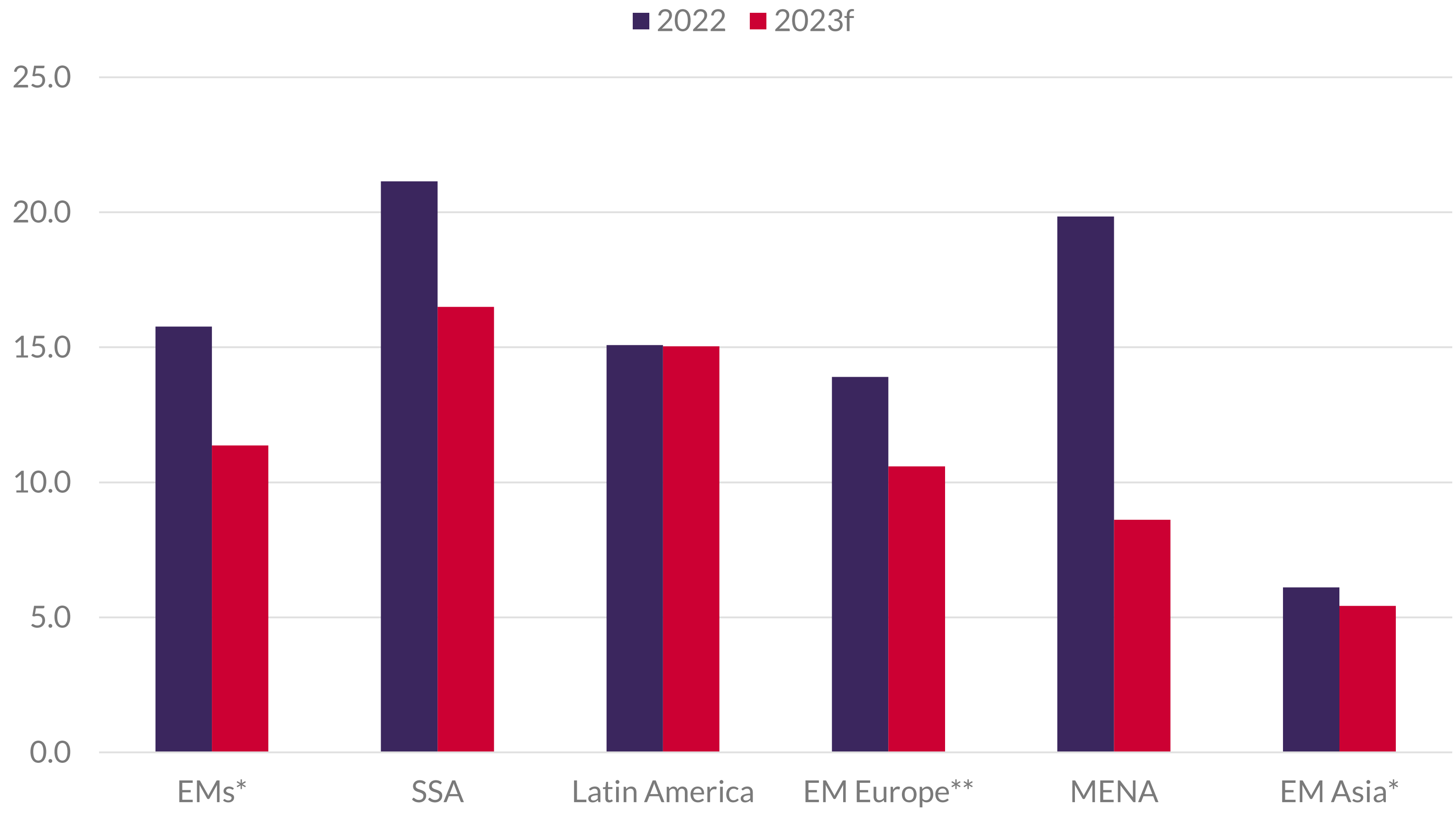
EMs – Average Exchange Rate vs USD, % Change



Source: Fitch Solutions

Inflation: Significant Regional Variation

Pace Of Disinflation Will Vary
Global – Inflation, %



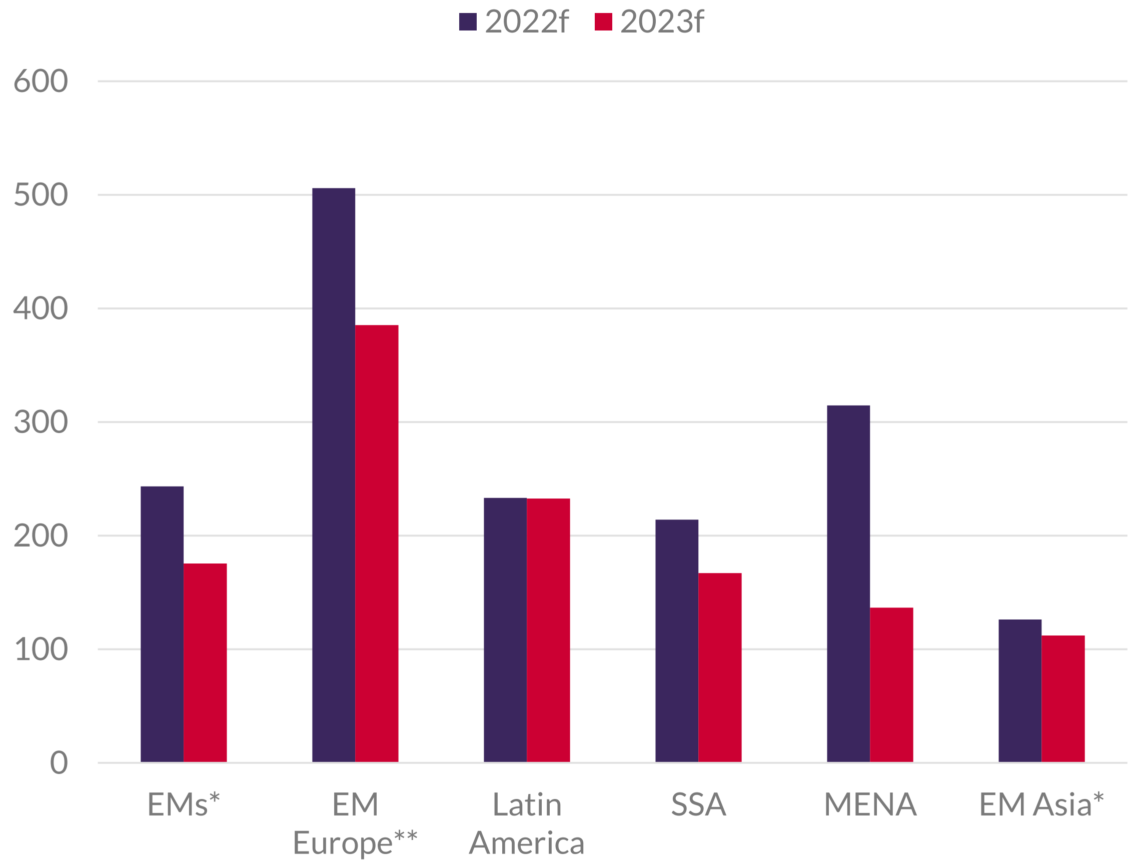
*Note:*Excludes Mainland China, **Excludes Russia, Ukraine, and Turkiye. f = forecast. Source: Fitch Solutions*

- We expect that inflation will ease in almost all EM regions.
- If Mainland China is excluded, EM inflation will slip from an average of 15.8% in 2022 to an average of 11.4% in 2023.
- The pace of the deceleration of price growth will vary significantly, with price growth slowing fastest in Middle East and North Africa.
- Inflation will remain fastest in SSA.

Inflation: Lasting Inflation Challenges In Europe

Inflation Remaining Farther Above Trend

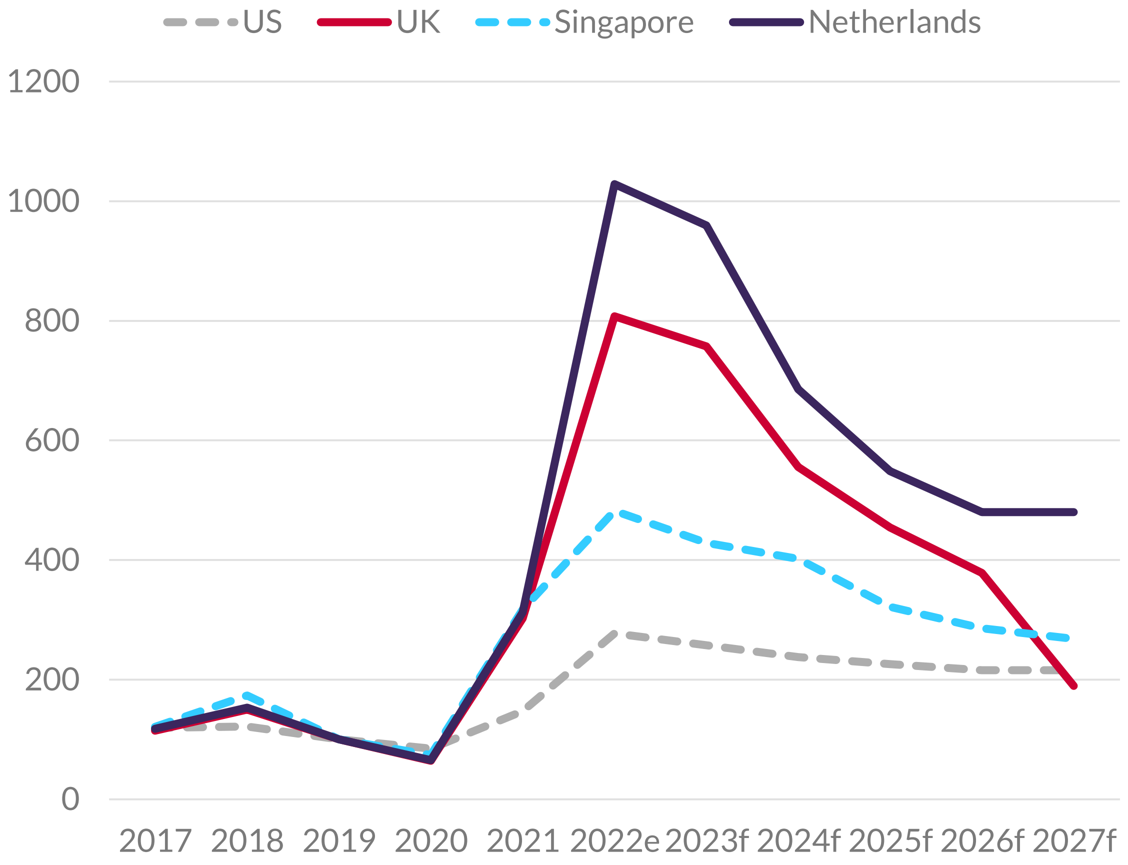
EMs – Average Inflation Compared, 100 = 2010-2019 Average



*Note: *Excludes Mainland China, **excludes Russia, Ukraine, and Turkiye. f = forecast. Source: Fitch Solutions*

European Energy Prices Will Be Higher For Longer

Global – Natural Gas Price Index, 100 = 2019 Average



f = forecast. Source: Fitch Solutions

4

Policy Rates

Hiking Cycle Ending

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Policy Rates: Cycle Nearing Its End

EM Rates Now Near Their Pre-Crisis Peak

EM Interest Rates – GDP-Weighted Index, 2010 = 100

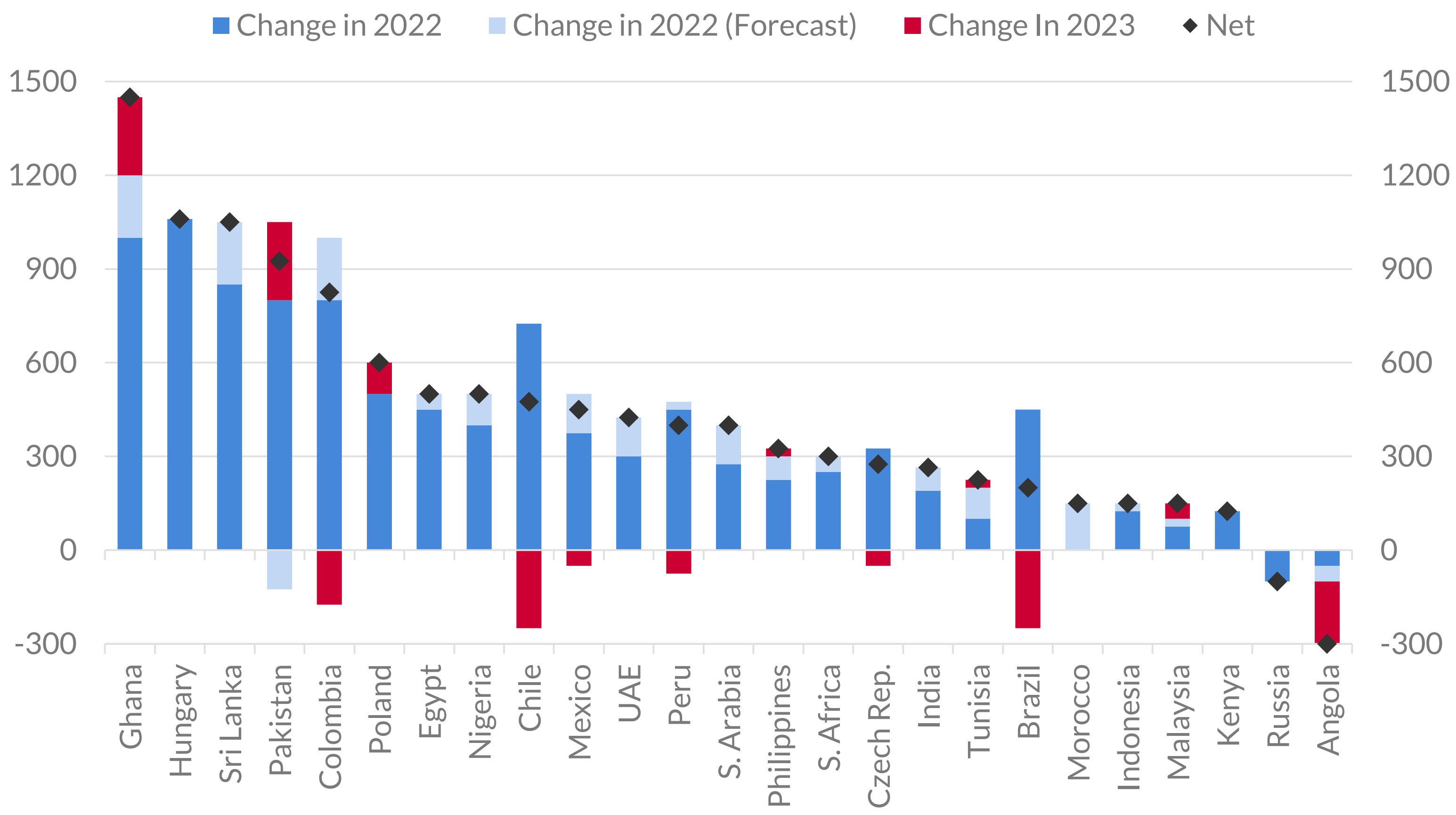
Source: Macrobond, Fitch Solutions

- EM central bankers cut their policy rates sharply in 2020 in an effort to provide stimulus.
- Starting with Latin America, EMs then began an aggressive sharp hiking cycle in 2021.
- In aggregate, rates are now almost as high as they were before the crisis.
- We expect that most banks are near the end of their cycle.
- A few EMs will begin loosening policy next year.

Policy Rates: Cycle Nearing Its End

Hiking Cycle Mostly Over

EMs – Change In Policy Rate Since Jan 1 2022, Basis Points



Source: Macrobond, Fitch Solutions

- EM policymakers are almost all of the way through their hiking cycle.
- We expect more hikes in a few economies, including Poland, Egypt, South Africa, and the USD-pegged economies of the GCC.
- Most rates will be kept on hold in 2023.
- In a few markets – mostly in Latin America – we expect that policymakers will actually begin to cut their key rates in 2023.

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Industrial Policy

More Interventions

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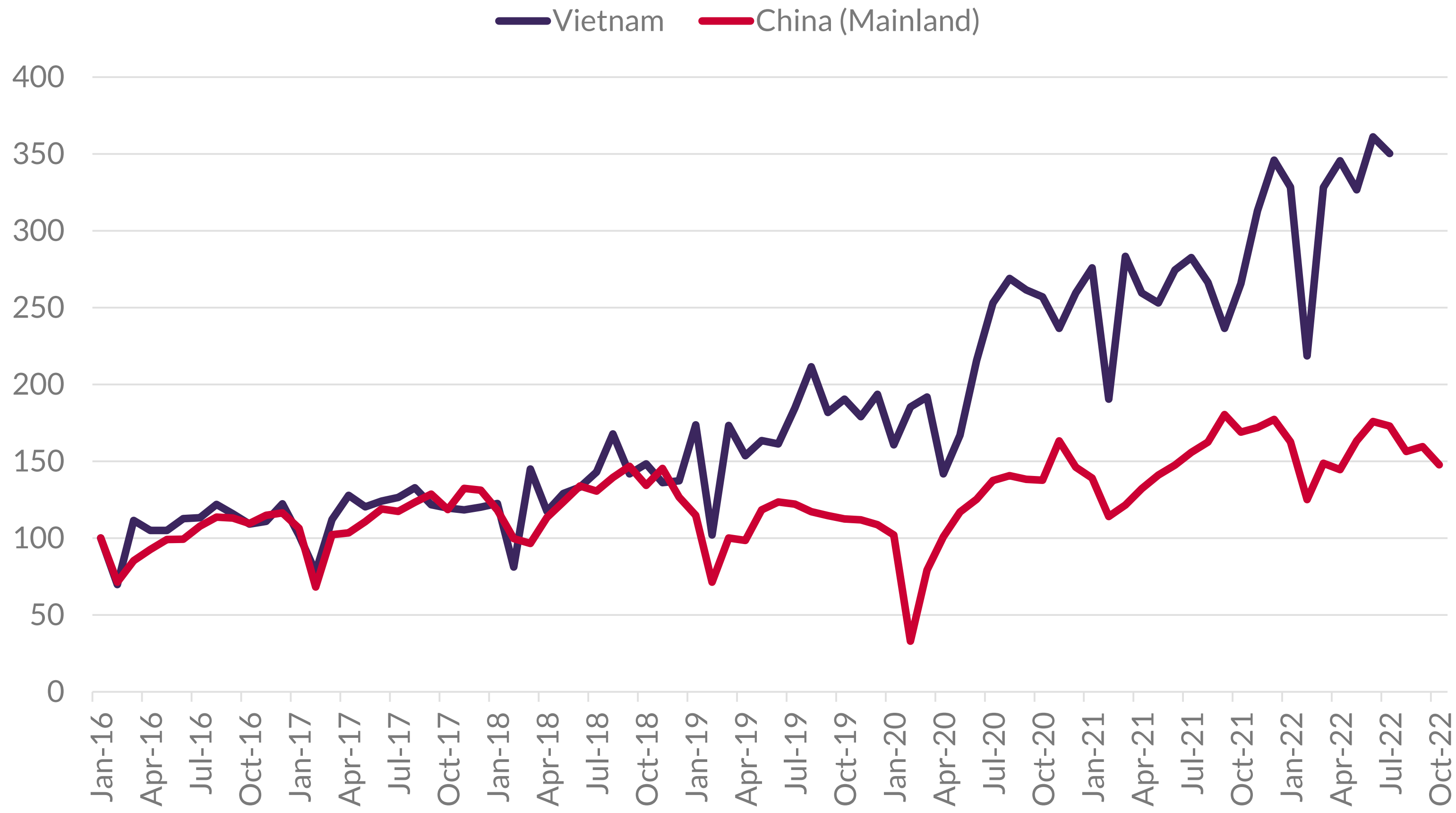
Industrial Policy: The Visible Hand Reaches In

Someone Always Wins

EMs – Index of Exports To US, January 2016 = 100

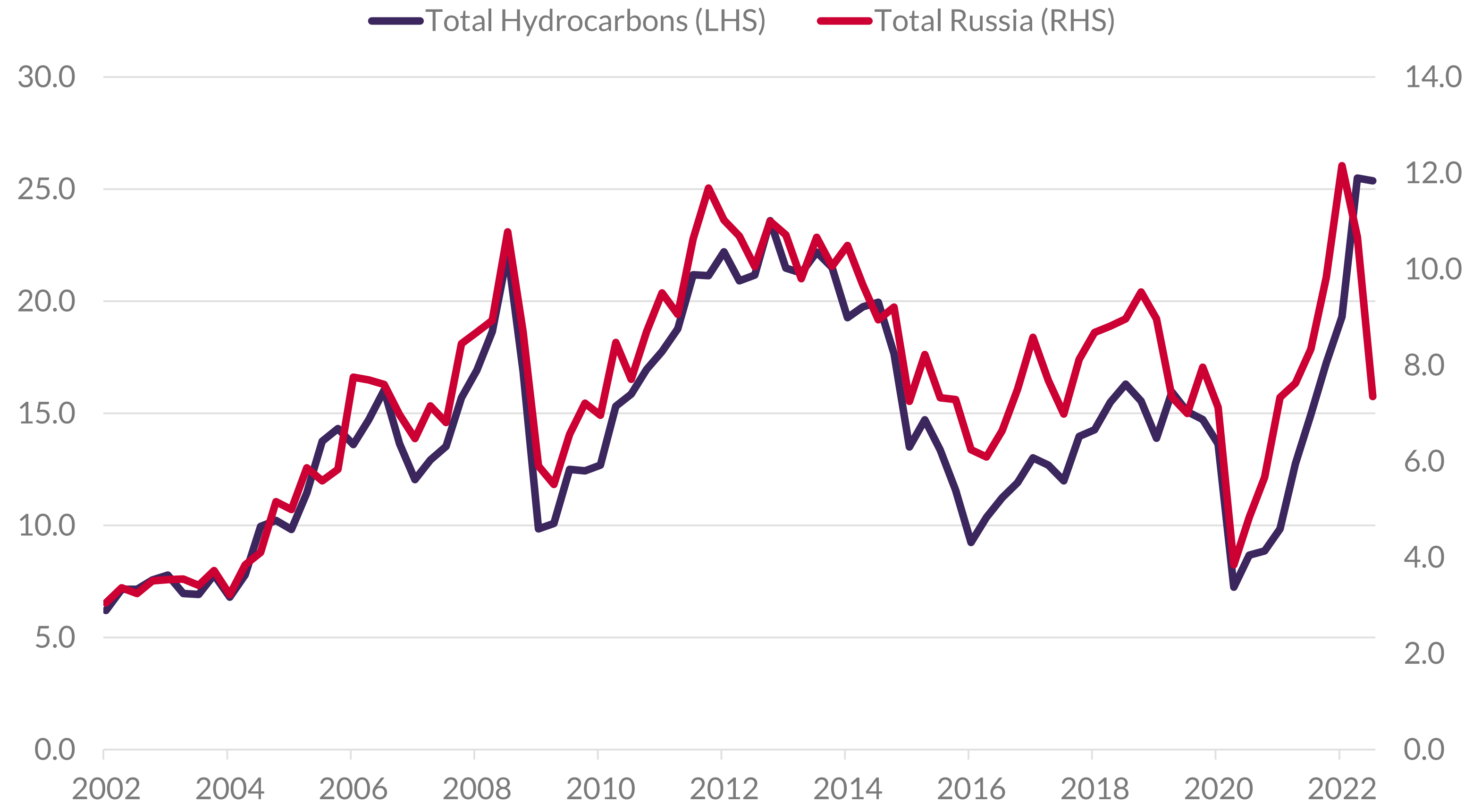


Source: Macrobond

- Worries about sourcing key inputs and increased tension between major economies will increase protectionism across DMs and EMs.
- Western sanctions and trade barriers will create headwinds for Mainland China and Russia.
- The displacement effects of these measures may have both positive and negative spill-over effects for other EMs.

Industrial Policy: A Different Sort Of Energy Transition

Conscious Uncoupling
Germany – Monthly Imports, EURbn

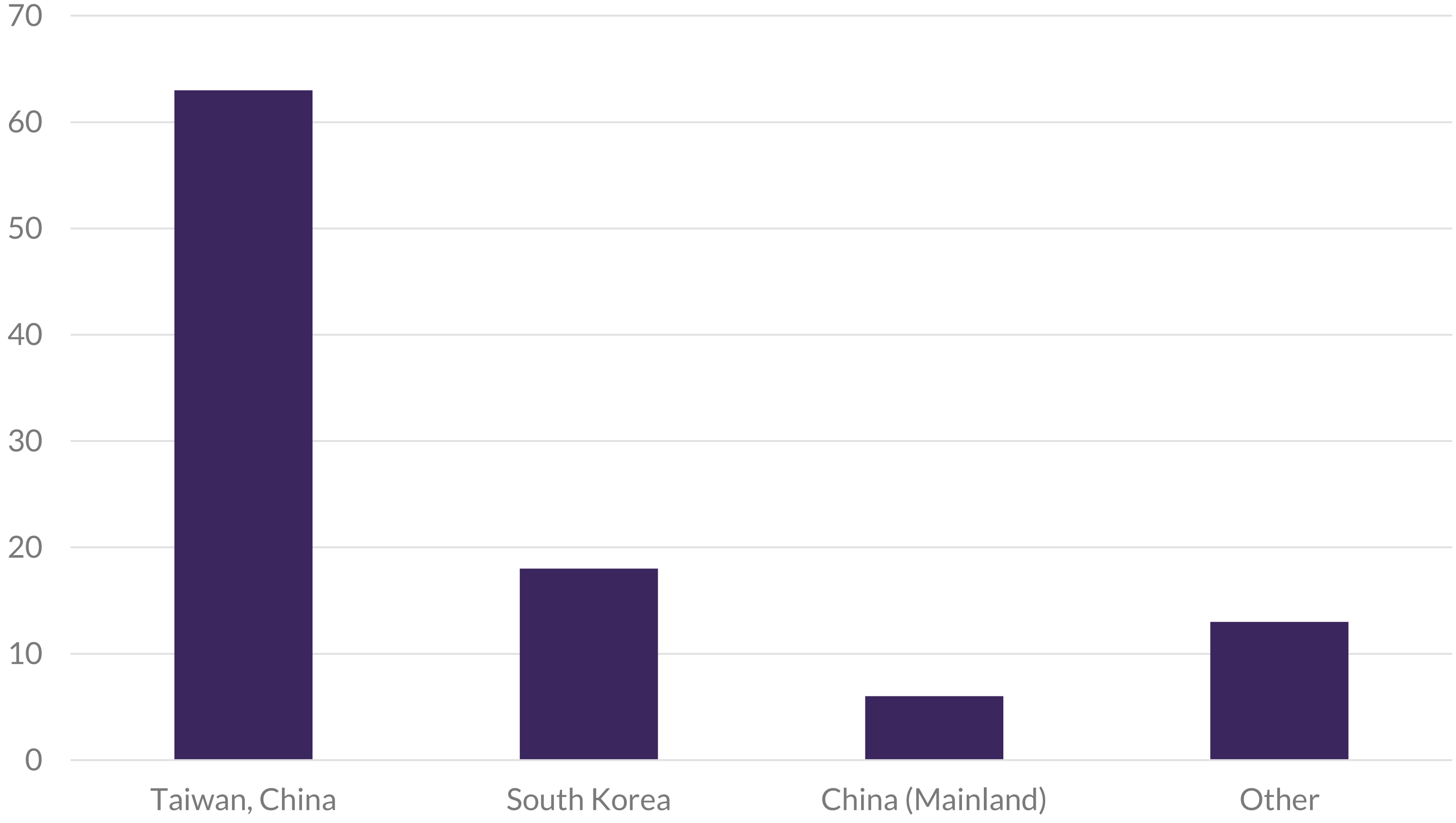


Source: Macrobond

- One key driver of policy-driven trade disruption will be the EU's move away from Russian energy exports.
- The bloc has already made significant progress, and we expect that this will accelerate.
- This transition has potentially significant benefits for other oil and gas suppliers, notably in Africa.
- However, LNG importers elsewhere will face a more competitive market. This poses risks for EMs like Turkey and India.

Industrial Policy: The Battle Over Chips

A Crucial Industry, Concentrated
EMs – Global Semiconductor Revenue, %



Source: TrendsForce, Fitch Solutions

- Political tensions between Washington and Beijing will have a significant effect on the technology sector.
- We expect that more governments will attempt to source key components domestically, or at least from friendly countries.
- This will reduce efficiencies from trade.
- Trade policies usually have unintended consequences.

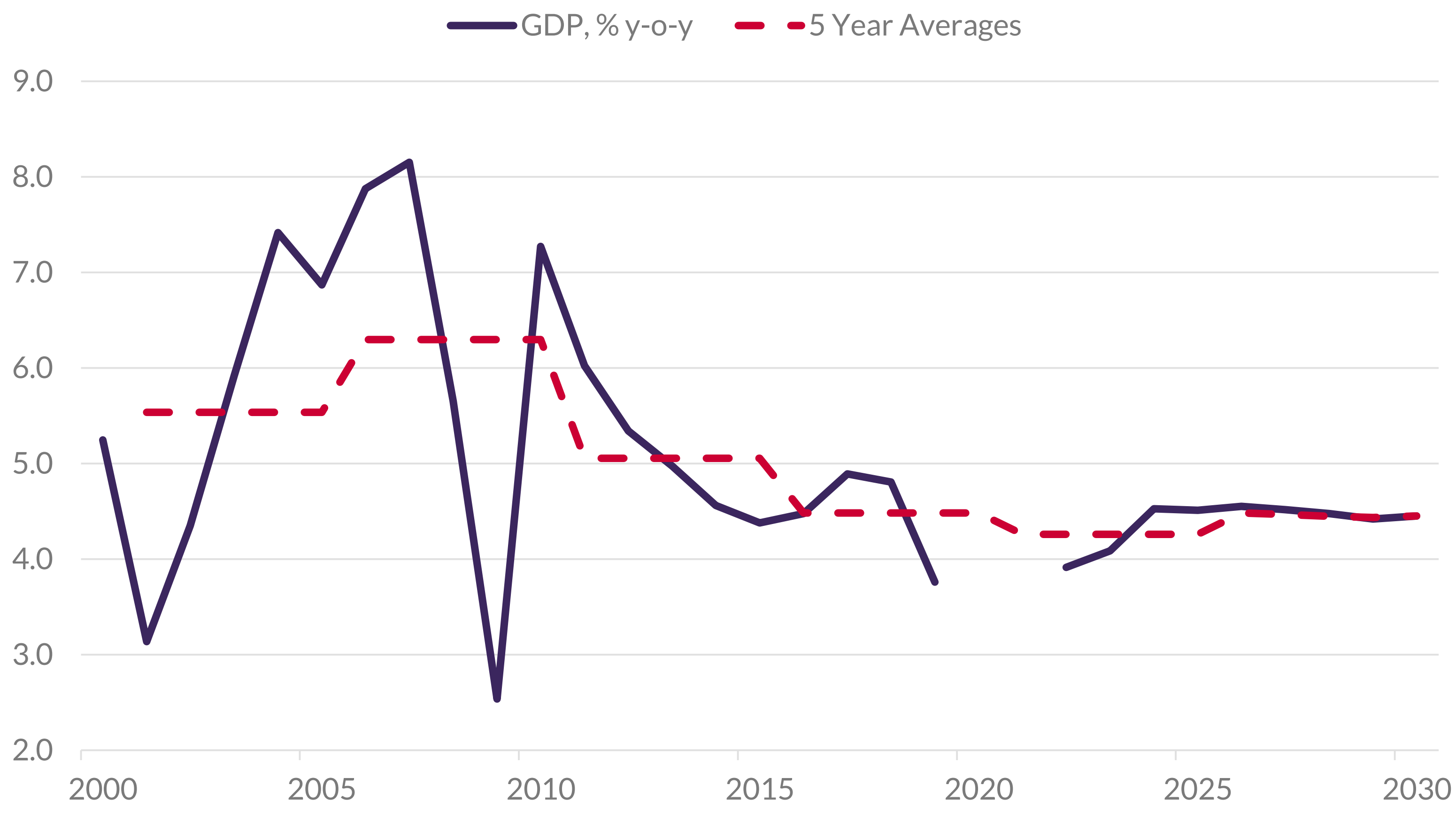
6

Structural Headwinds

Building

Structural Headwinds: EM Growth Has Peaked

EM World Will Gradually Slow
EMs – Real GDP, % y-o-y



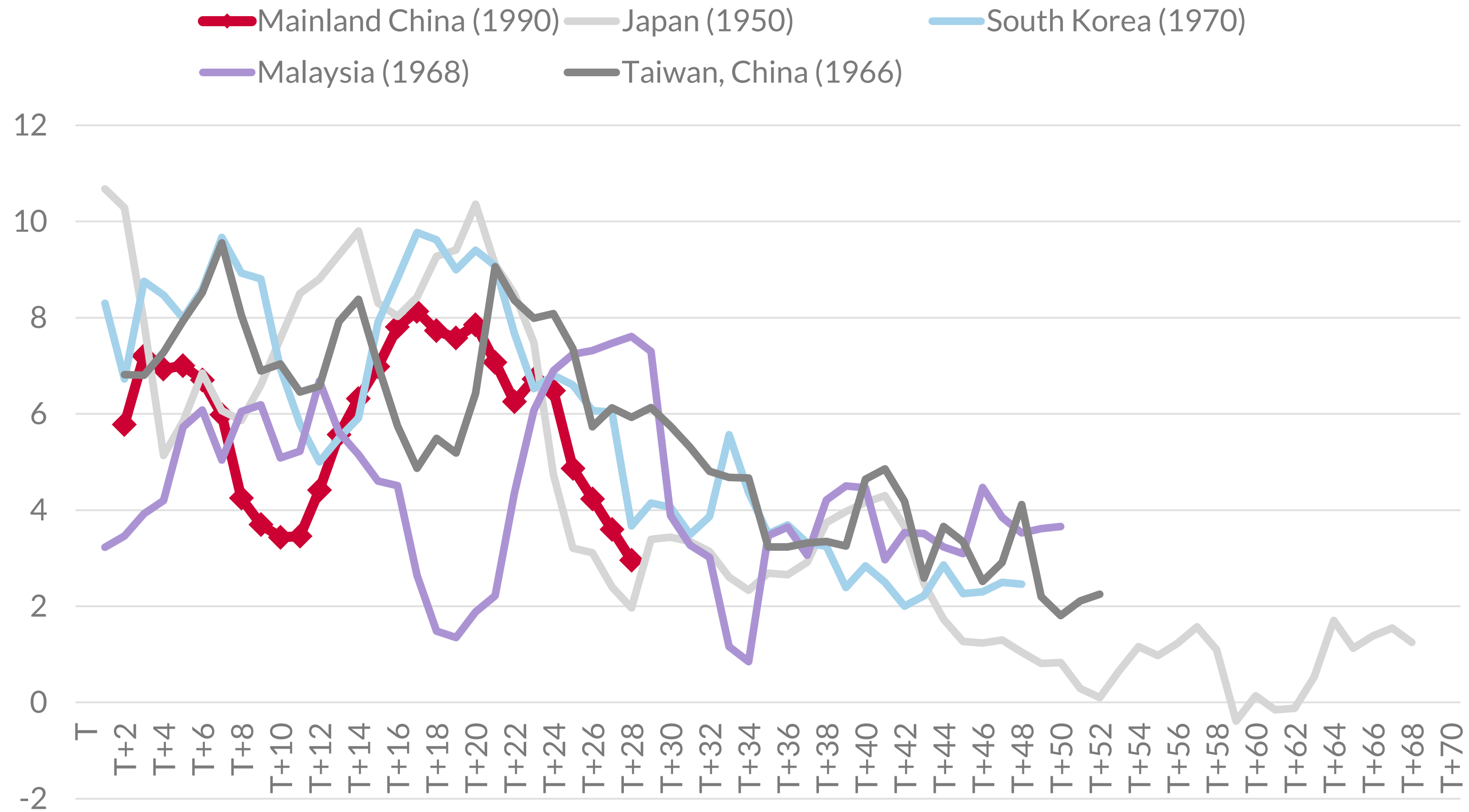
Source: Macrobond, Fitch Solutions (Note: Fitch Solutions Forecasts, 2020 & 2021 excluded for scale)

- While we expect that headline EM GDP growth will accelerate in 2024, we do not think that it will regain its pre-crisis pace.
- The structural slowdown that began in 2010 will continue over the coming decade.
- Several key factors will drive this:
  - Slower growth in China
  - Reduced commodity demand
  - Convergence with DM income levels
  - Weakening demographic tailwinds

Structural Headwinds: China, Other EMs Converging

Best Days Behind Them?

EMs – Real GDP Per Capita, % y-o-y (Rolling 5-year Average)

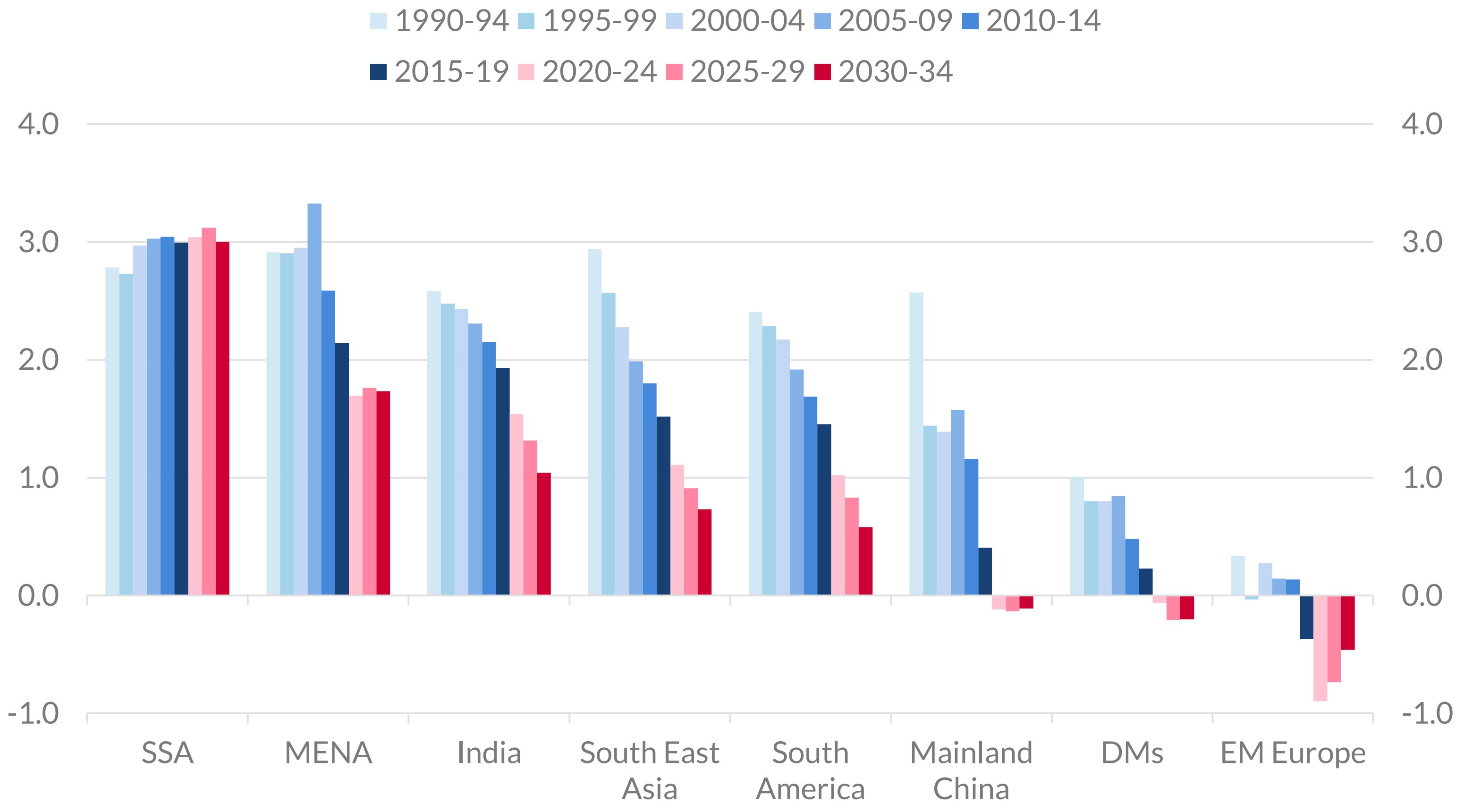


Note: Figures are show in Years since T; when GDP/capita = USD3,000 per capita in 2011 prices. Source: Angus Maddison Database

- While Mainland China's scale makes its rise unique, the economy is following a well-worn path.
- As incomes rise, potential growth is slowing, as it did in other rapidly-developing Asian economies.
- Similar trends are also at play in other EMs, though their transitions will mostly be slower.
- Potential growth will remain higher in SSA and parts of South Asia.

Structural Headwinds: Demographic Tailwinds Fading

Best Days Behind Them?
EMs – Working Age Population Growth, %



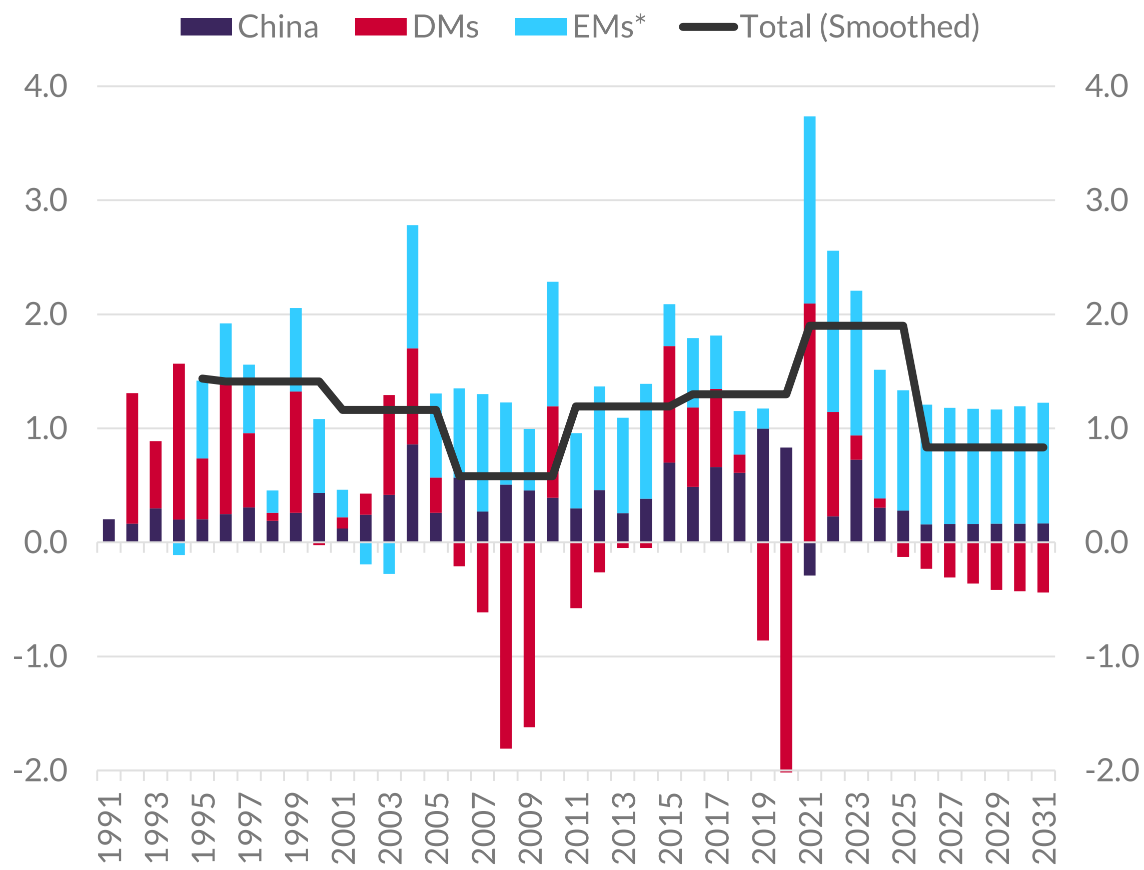
Source: UN Population Report

- Demographic tailwinds boosted EM growth in the 1990s and early 2000s.
- In most regions, the growth of the working-age population has already slowed, and will now slow further.
- In Mainland China and EM Europe, the working age population will begin to fall.
- While short-term measures can boost the labour force, this will create a significant tailwind and leave growth dependent on rising productivity.

Structural Headwinds : Commodity Demand Will Ease

Oil Transition Will Be Painful For Many EMs

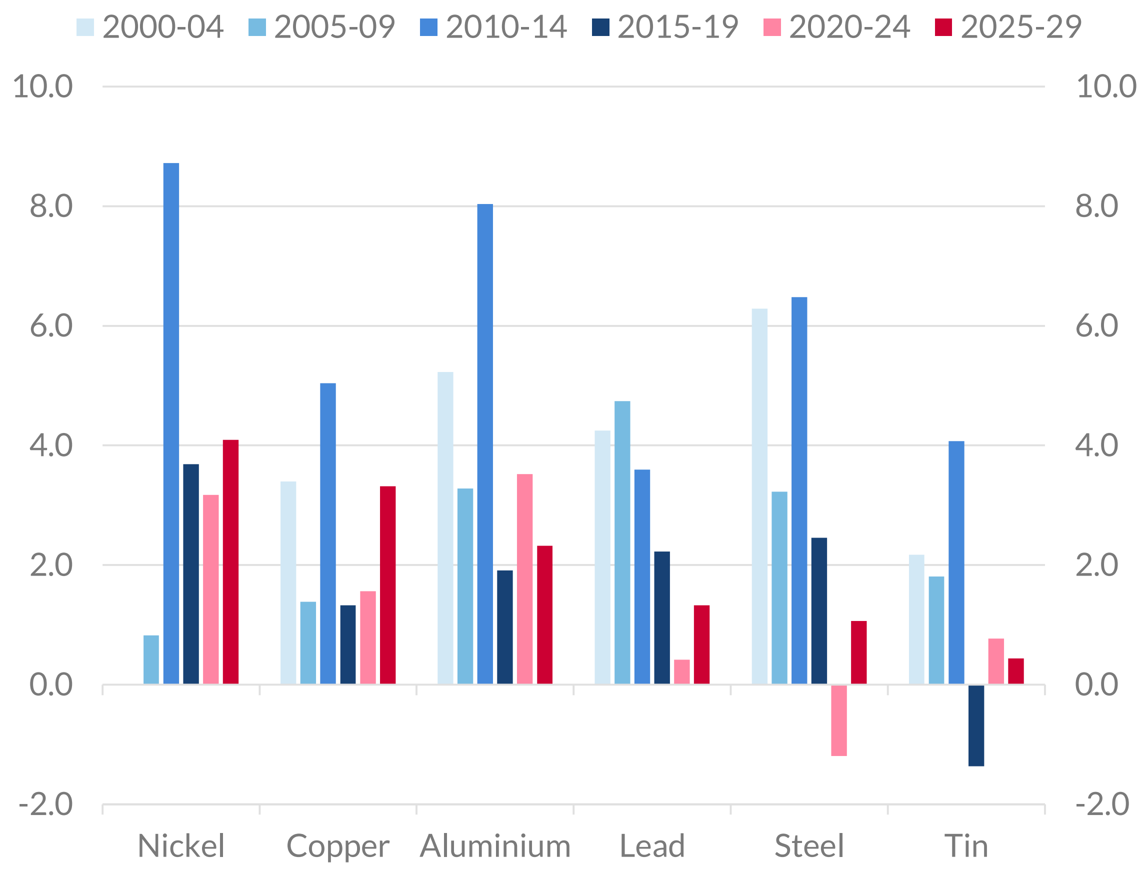
Global – Change In Oil Consumption, mn b/d



*Note: *Excludes Mainland China, *Source: Fitch Solutions, Fitch Solutions Forecasts*

China's Building Boom Will Not Be Repeated

Global – Commodity Demand, % y-o-y



Source: Fitch Solutions

Q&A

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