

## Emerging Markets: Pockets of vulnerability

Turkey and Argentina remain under pressure from firm US interest rates



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### USD: Firm US yields continue to stress test emerging market vulnerabilities

US interest rates have stayed firm at the start of the week and the focal point for investors is increasingly switching to emerging markets. Here the two most exposed G20 countries to higher external borrowing costs, Argentina and Turkey, remain under pressure. Argentina has applied for an IMF deal (meeting due Friday), with the IMF apparently happy to let the currency float (Argentine peso down 7% yesterday) and focus more on fiscal tightening. For today, the focus is on what rates (40%+?) Argentina's central bank will have to pay to roll the US\$26bn of maturing short-term Lebac securities. The Turkish lira (TRY) also remains under pressure, not helped by overnight remarks from President Erdogan that 'he'll take more responsibility for monetary policy'.

Investors have been seeking a 100-150bp emergency CBT hike to stabilise the TRY, which may now be in doubt. So far there has been little contagion to other emerging markets, but with lots of external debt outstanding, Argentina and Turkey together comprise nearly 10% of popular EM hard currency debt indices. With these challenges unresolved, investors may have little appetite to put more money to work in EM and be happy to keep funds in cash – namely USD paying 2.35% for 3-month annualised. In the developed markets space, US retail sales should come in relatively strong and probably keep the dollar supported today. The US dollar index to drift back to 93.00.

## EUR: Learning to live with the 1Q18 slowdown

Germany has just released 1Q18 GDP, which slowed to 0.3% quarter-on-quarter. Strikes, weather and flu have been blamed here and the market will want to see a rebound in 2Q data. 1.1890/1900 looks intraday support for EUR/USD, below which the lows could be retested. Certainly how EUR/USD reacts to President Trump's trade agenda (is the EUR a safe haven?) has become a little cloudier – especially with Washington unlikely to extend EU steel tariff relief on 1 Jun. Look out for the German ZEW today, though any impact on the EUR should be fleeting.

## GBP: Decent earnings data should keep possibility of August rate hike alive

We look for another reasonable UK earnings figure today, supporting the Bank of England's position that tighter labour markets are finally feeding through to wages. This could generate a little GBP out-performance today – EUR/GBP to edge to 0.8760.

## PLN: Slight downside risk to Polish GDP

Our team is slightly below consensus with its forecast for Polish 1Q18 GDP today. With emerging markets under pressure, it wouldn't be a surprise to see the Polish zloty take a little of the strain today and EUR/PLN push back to the 4.30 area.

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