Global debt flows
De-risking in Govies seen, but still long duration

We face into the 31 July FOMC meeting (and the ECB) with a market-place that is quite long duration. It is also long risk generally as evidenced from inflows built into long end governments, investment grade and high yield corporates and emerging markets. Risk assets have managed to command decent excess returns over the risk free rate YTD, and are being cushioned by a likely Fed easing policy that is seen to be anticipatory. This (plus inflation fund outflows) encapsulates the essence of the current market discount, one that in many circles incorporates excess return over (non-US) negative risk free rates as a first phase target.

Six things learnt from the latest flows data
1) We identify the market-place as being long duration based off a strikingly large build in longs in duration in the past quarter. Inflow to government long end funds shows this, marked by a 6.5% inflow there.

2) There have been some long end outflows seen in the past couple of weeks, but not dramatic. Moderate de-risking in duration space contracts with ongoing risk building on corporate space, albeit at a slower pace.

3) A recent spike in HY inflows has been mostly driven by an expected resumption of the European Central Bank’s (ECB) corporate sector purchase programme (CSPP). Risks that could come from a rise in default rates from recession is being contained by likely precautionary action from the Fed.

4) Meanwhile, inflation funds continue to see outflows. The biggest outflow has been from US inflation funds, while W Europe money funds outflows contrast with US money fund inflows.

5) In EM, we maintain a preference for local currency over hard currency in an environment where the Fed is on the cusp of cutting rates. This provides breathing space for EM central banks, to either cut rates or not be under pressure to hike rates (from a rates differential perspective).

6) Latest data confirm ongoing inflows to EM, with hard currency funds seeing the bulk of the inflows. But local currency funds are no longer seeing outflows, and are now outperforming hard currency funds in terms of total returns.
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Global debt flows July 2019

Global Manager (average) Allocations by Region

Fig 1  Global allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 2  EM allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 3  EM detailed allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 4  EMEA allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 5  Asia EM allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 6  Latam allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 7  Developed allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 8  Eurozone allocations one month ago (%)

Source: EPFR Global, ING estimates
Emerging Markets
Emerging Markets – Summary themes

- A look back at the past quarter shows a 3.2% increase in assets under management (AUM) for hard currency funds versus a 0.9% contraction for local currency funds. And indeed total returns in hard currency funds have been more impressive than in local currency funds as a theme so far in 2019.

- However, that contrast has begun to narrow. Emerging markets (EM) continue to see more inflows into hard currency funds, but local currency funds are also seeing a decent rump of inflows. Latest total returns data confirm an outperformance for local currency funds for the past month. We expect more of that ahead.

- The chart below shows EM weekly flows, and illustrates a decent run of inflows through the past number of weeks (the bars). The light blue line illustrates the value of AUM (including total returns), which is positive and rising (measured on the RHS). The Fed cut backdrop has helped sustain a decent tone for EM.

Fig 9  Feature Chart: Positivity underpinned by inflows and total returns performance

- Allocations data show that Emerging Europe and the Middle East has seen a fall in cash invested in the past number of months, countered by a rise in allocations to Latam and Africa. Allocation to Asia has also eased lower.

- In EMEA, a rise in allocation to Russia and S Africa has been countered by a fall in allocation to Turkey.

- In low beta space, allocation to Poland and Hungary is lower in the past month, while Romania is steady, and allocation to Czech in on the rise having hit prior lows.

- In a global context, allocation to Turkey is now at 3.6% compared with an average allocation of 5.7% and a high of 8.3%.

- See detailed allocations on a global scale on pages 7 and 8, country flows data is summarised on pages 9 and 10 and hard versus local EM flows on page 6.

**BOTTOM LINE:** We maintain a preference for local currency over hard currency in an environment where the Fed is on the cusp of cutting rates and core rates are testing lower in a slower growth but non-recessionary environment. This provides breathing space for EM central banks, to either cut rates or not be under pressure to hike rates from a rates differential perspective. Latest data confirm ongoing inflows to EM, with hard currency funds seeing the bulk of the inflows. But local currency funds are no longer seeing outflows, and are now outperforming hard currency funds in term of total returns (when translated back into USD).
Emerging Markets Net Fund Flows

Fig 10  Emerging Markets - Change in the past week (%)

% AUM  PAST WEEK

-0.10  0.00  0.10  0.20  0.30  0.40  0.50  0.60

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 11  Emerging Markets - Change in past week (US$m)

$ millions  PAST WEEK

-200  0  200  400  600  800  1000  1200  1400

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 12  Emerging Markets - Change in the past month (%)

% AUM  PAST MONTH

-1.00  -0.50  0.00  0.50  1.00  1.50  2.00  2.50

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 13  Emerging Markets - Change in past month (US$m)

$ millions  PAST MONTH

-1000  0  1000  2000  3000  4000  5000  6000

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 14  Emerging Markets - Change in past quarter (%)

% AUM  PAST QUARTER

-3.00  -2.00  -1.00  0.00  1.00  2.00  3.00  4.00  5.00

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 15  EM - Change in past quarter (US$m)

$ millions  PAST QUARTER

-4000  -2000  0  2000  4000  6000  8000  10000

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 16  Emerging Markets - Change in the past year (%)

% AUM  PAST YEAR

-15.00  -10.00  -5.00  0.00  5.00  10.00  15.00

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates

Fig 17  Emerging Markets - Change in past year (US$m)

$ millions  PAST YEAR

-15000  -10000  -5000  0  5000  10000  15000  20000  25000  30000

Total  Professional  Retail

EM Hard Currency Funds  EM Local Currency Funds  EM Blend Currency Funds  Total EM

Source: EPFR Global, ING estimates
Global EM Manager Asset Allocations

Fig 18  GEM allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 19  GEM detailed allocations one month ago (%)

Source: EPFR Global, ING estimates

Fig 20  GEM allocations two months ago (%)

Source: EPFR Global, ING estimates

Fig 21  GEM detailed allocations two months ago (%)

Source: EPFR Global, ING estimates

Fig 22  GEM allocations one quarter ago (%)

Source: EPFR Global, ING estimates

Fig 23  GEM detailed allocations one quarter ago (%)

Source: EPFR Global, ING estimates

Fig 24  GEM allocations one year ago (%)

Source: EPFR Global, ING estimates

Fig 25  GEM detailed allocations one year ago (%)

Source: EPFR Global, ING estimates

Africa, 9.6
Latin America, 33.3
Asia Ex-Japan, 21.5
Other, 1.3
Emerging Europe, 15.2

Source: EPFR Global, ING estimates

Africa, 9.1
Latin America, 32.6
Asia Ex-Japan, 22.2
Other, 2.3
Emerging Europe, 19.3

Source: EPFR Global, ING estimates

Africa, 8.9
Latin America, 32.8
Asia Ex-Japan, 22.1
Other, 4.3
Emerging Europe, 20.1

Source: EPFR Global, ING estimates

Africa, 9.7
Latin America, 34.2
Asia Ex-Japan, 20.4
Other, 13.3
Emerging Europe, 22.5

Source: EPFR Global, ING estimates

Figures 18-25 show the asset allocations for Emerging Market (EM) managers over different time periods: one month ago, two months ago, one quarter ago, and one year ago. The allocation percentages vary significantly across regions and countries, reflecting the dynamic nature of EM asset management strategies.
Regional EM Manager Asset Allocation

**Fig 26 EMEA allocations one month ago (%)**

- Czechrepublic, 3.5
- Russia, 20.5
- Poland, 12.2
- South Africa, 19.1

**Source:** EPFR Global, ING estimates

**Fig 27 EMEA allocations two months ago (%)**

- Czechrepublic, 2.9
- Russia, 21.5
- Poland, 12.4
- South Africa, 18.8

**Source:** EPFR Global, ING estimates

**Fig 28 Asia allocations one month ago (%)**

- Philippines, 8.2
- Thailand, 9.2
- Indonesia, 35.4
- Malaysia, 10.8

**Source:** EPFR Global, ING estimates

**Fig 29 Asia allocations two months ago (%)**

- Philippines, 7.4
- Thailand, 9.2
- Indonesia, 35.3
- Malaysia, 11.1

**Source:** EPFR Global, ING estimates

**Fig 30 Latam allocations one month ago (%)**

- Colombia, 12.1
- Mexico, 22.4
- Brazil, 22.7
- Peru, 9.0

**Source:** EPFR Global, ING estimates

**Fig 31 Latam allocations two months ago (%)**

- Colombia, 13.2
- Mexico, 23.3
- Brazil, 22.4
- Peru, 9.0

**Source:** EPFR Global, ING estimates

**Fig 32 Africa & ME allocations one month ago (%)**

- Africa & ME, 6.0
- Egypt, 14.6
- Nigeria, 9.6
- Gabon, 1.0

**Source:** EPFR Global, ING estimates

**Fig 33 Africa & ME allocations two months ago (%)**

- Africa & ME, 6.8
- Egypt, 16.4
- Nigeria, 9.4
- Gabon, 0.9

**Source:** EPFR Global, ING estimates
Selected EMEA and Latam Country Flows

**Fig 34** EMEA – Change in the past week (%) 

**Fig 35** EMEA – Change in the past month (%) 

**Fig 36** EMEA – Change in the past quarter (%) 

**Fig 37** EMEA – Change in the past year (%) 

**Fig 38** Latam – Change in the past week (%) 

**Fig 39** Latam – Change in the past month (%) 

**Fig 40** Latam – Change in the past quarter (%) 

**Fig 41** Latam – Change in the past year (%) 

Source: EPFR Global, ING estimates
High Yield
High Yield – Summary themes

- In proportional terms, inflows to corporate high yield (HY) had been lagging inflows into emerging markets (EM). That changed in the past month, with inflows to HY running at 2% of assets under management (AUM) compared with a 1.2% increase in EM AUM. The breakout shows a 0.9% rise in US HY vs 2.6% in W Europe HY AUM.

- The W European HY market is considerably smaller than that of the US market, but the spike in inflows to W Europe HY has been of particular note in the past number of weeks. A lot of this has been driven by a frenzy of interest in EUR corporate paper generally as a re-igniting of the ECB’s CSPP programme is cited.

Fig 50  Feature Chart: W Europe flows have spiked higher in the past 6 weeks

- Total returns are running at 8% YTD in W Europe HY and at 9% YTD in US HY, which are impressive. Compared with US Treasuries running on total returns of 5%, that represents an excess return of 4%. The equivalent excess in Europe is in the area of 2%. These compensations partly reflect a tame recession risk. Anything that elevates the recession risk would do the same for default risk, which would hurt HY generally. So far though the cushion being offered by likely Fed cuts is acting to dominant sentiment.

BOTTOM LINE: Even though inflows to HY have been choppy through 2019, returns have been impressive and generative of decent excess returns over the risk free rate. This is of the order of 4% in USD and 2% in EUR. A recent spike in inflows has been mostly driven by an expected resumption of the ECB’s CSPP programme, which we believe will extend out to the high yield space. The filter through of this along the credit spectrum has helped to improve prospects in the high yield space generally. Risks that could come from a rise in default risk from recession is being contained by likely precautionary action from the Fed (and the ECB).
Fig 51  Western Europe High Yield Weekly Flows

![Western Europe High Yield Weekly Flows graph]

Source: EPFR Global, ING estimates

Fig 52  US High Yield Weekly Flows

![US High Yield Weekly Flows graph]

Source: EPFR Global, ING estimates

Fig 53  Emerging Markets Weekly Flows – all currencies

![Emerging Markets Weekly Flows – all currencies graph]

Source: EPFR Global, ING estimates
Developed Markets
Developed Markets – Summary themes

- A striking contrast has emerged in terms of government bond flows in the past few months. On a 3mth view, assets under management (AUM) in long end funds are higher by an impressive 6.5%. But, in the past two weeks there has been a clear reversal, with long end funds seeing outflows, of some 1%.

- The past month is interesting as it capsulated a theme seeing outflows from government long end funds and short end funds versus inflows to corporate long end funds, and in the past week some decent inflows to corporate belly funds.

- Hence, there has been a clear de-risking in terms of duration exposure, but we’d assess that the market-place is still long duration by virtue of the longs set in the past quarter. Meanwhile, risk augmentation continues in investment grade and high yield corporates, albeit at a slower pace.

- In terms of other notable flows, inflation funds continue to see outflows, especially from US inflation funds where an outflow of 2.6% of AUM has been seen in the past quarter. At the same time, US money market funds are seeing moderate inflows, while W Europe money market funds are seeing outflows.

**Fig 54** Feature Chart: Prior inflow to long end funds is turning to outflows

- A notable trend in terms of allocation has been the distinct country inflow to the USA, which is now holding at 50% of developed markets (DM) allocation, up from 45% some 4 months back. These flows remain a support for US rates and the dollar generally, but look quite elevated right now. At the same time, DM allocations to the Eurozone (22.6%) and the UK (7.8%) are down for good reason (Eurozone-angst and Brexit respectively). In terms of choice of risk free rate, US Treasury yields may not be as high as they were, but at least they offer a positive coupon (in contrast to many other negative risk free rates).

**BOTTOM LINE:** We identify the market-place as being long duration based off a strikingly large build in longs in duration in the past quarter. Inflows to government long end funds encapsulate this, aggregating to a 6.5% rise in long end fund AUM. At the same time, there has been some long end outflows seen in the past couple of weeks as some of these longs have been shaved back, although not that dramatically. Some de-risking in duration space contrasts with on-going risk building in corporates (albeit at a slower pace). Meanwhile, inflation funds continue to see outflows. The biggest inflation-related outflow has been from US inflation funds, while W Europe money funds outflows contrast with US money fund inflows.
Developed Markets Country Flows

Fig 71  Eurozone – Change in the past week (%)  
- 0 0.05 0.1 0.15 0.2 0.25 0.3 0.35  
% AUM  
PAST WEEK  
Source: EPFR Global, ING estimates

Fig 72  Non Eurozone – Change in the past week (%)  
- 0 0.1 0.2 0.3 0.4 0.5 0.6 0.7  
% AUM  
PAST WEEK  
Source: EPFR Global, ING estimates

Fig 73  Eurozone – Change in the past month (%)  
0 0.2 0.4 0.6 0.8 1 1.2  
% AUM  
PAST MONTH  
Source: EPFR Global, ING estimates

Fig 74  Non Eurozone – Change in the past month (%)  
-0.6 -0.4 -0.2 0 0.2 0.4 0.6 0.8 1 1.2 1.4  
% AUM  
PAST MONTH  
Source: EPFR Global, ING estimates

Fig 75  Eurozone – Change in the past quarter (%)  
0 0.5 1 1.5 2 2.5 3 3.5  
% AUM  
PAST QUARTER  
Source: EPFR Global, ING estimates

Fig 76  Non Eurozone – Change in the past quarter (%)  
-2 -1 0 1 2 3 4 5  
% AUM  
PAST QUARTER  
Source: EPFR Global, ING estimates

Fig 77  Eurozone – Change in the past year (%)  
-3 -2 -1 0 1 2 3 4 5  
% AUM  
PAST YEAR  
Source: EPFR Global, ING estimates

Fig 78  Non Eurozone – Change in the past year (%)  
-8 -6 -4 -2 0 2 4 6 8  
% AUM  
PAST YEAR  
Source: EPFR Global, ING estimates
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