



NatWest

Emerging Markets

Desk Strategy

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1 February 2021

EMFX: Long USD bias, looking for RV

Over the past few sessions, **there has been a clear questioning of the overall bullish EM consensus that was pervasive at the end of 2020**. Most clients appear to be looking for decent shorts at least over the short term, rather than to fade the recent sell-off. The fact that EMFX has struggled both when US rates went higher and now as global growth expectations are being challenged has been particularly frustrating. And the volatility in many crosses (BRL for example) has made it particularly difficult to have conviction – in both directions.

We have continued to lower risk and have a long USD bias in our views, but concentrated mostly in relative value trades. While we remain overall constructive on EM on a quarterly basis, valuations in many places simply got ahead of themselves. Currencies that rely on portfolio vs real flows will remain challenged, and so will those that need positive catalysts to catch-up to fundamentals (such as RUB).

A summary of our current views:

- **Exited long ZAR and BRL at the beginning of the year** ([here](#)). We maintain long SAGBs (FX-hedged) as it offers the most attractive yield/vol pick-up ([here](#)), while the vaccine rollout poses dovish risks to the outlook ([here](#)). We find BRL attractive at the top of the range, but we are looking for better entry levels and decreased political noise.
- **Replaced TWD instead of KRW on our growth basket on Jan 15th** ([here](#)) given the KRW's higher beta and dependence on risk appetite, following a good run last year. Within our basket, we still expect CNH appreciation (which has quietly outperformed this year), and keep PLN given very strong export momentum ([here](#)).
- **Entered short CLP vs USD and PEN** ([here](#)) and kept half the position after taking profits following the BCChile reserve accumulation announcement ([here](#)). We expect CLP to head towards 760-770 given the much weaker flow dynamic and increasing political noise. We like the PEN as a cross because of its lower beta and better fundamentals. We also place a stop at entry.
- **More defensive on RUB and OFZs** as we find the political risks around protests and upcoming elections likely further increasing the risk premia, particularly with a more hawkish US administration. We also argue that local bonds are not particularly attractive within an EM portfolio ([here](#)).
- **Keep long TRY vs MXN, with higher conviction** ([here](#)) as we find MXN the best short to capture EM wobbles given its lack of domestic anchors. TRY, meanwhile, benefits from a relatively modest bar for the central bank to deliver its hawkish monetary policy, superior carry, and still-modest positioning. We recommend placing a stop at entry ([here](#)).
- **Expect ILS to test the Bol and recommended 6m put spreads** ([here](#)). The fundamental case for shekel appreciation continues to be underpinned by its CA surplus, strong net inflows and the best vaccine rollout program thus far ([here](#)). We

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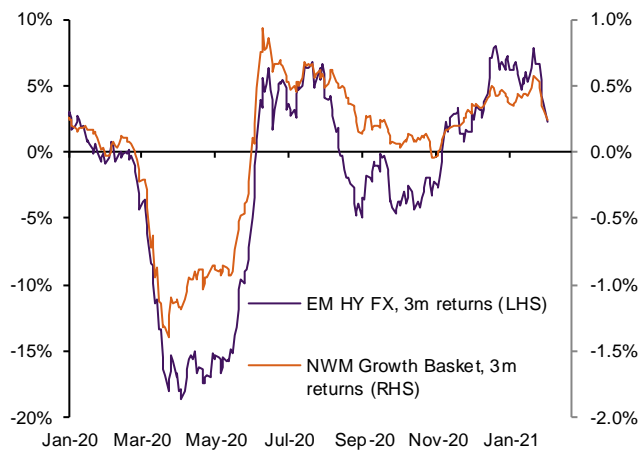
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think that the Bol will slow down the pace of appreciation rather than defend a particular level.

High-yield EMFX has pulled back in Jan, alongside growth-related assets

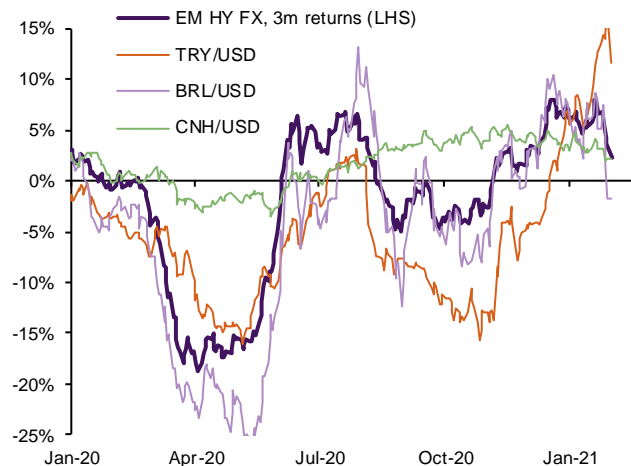
High-yield EM an equal-weighted basket of INR, IDR, RUB, TRY, ZAR, BRL, MXN, COP

Source: Bloomberg, NatWest Markets



We stay long TRY, expect more to come in CNH, and exited BRL

Source: Bloomberg, NatWest Markets



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Version 10.12.2020