T. Rowe Price

Three key themes to watch out for in emerging markets

From the Field
September 2024

Key Insights

- **Growth and fiscal:** Economic growth is fairly steady overall at present, but this resiliency will likely be tested in the coming months given the slowdowns taking place in China and the U.S.
- **Monetary policy:** The Federal Reserve moving to a cutting cycle should open up the opportunity for a new group of emerging market countries to also cut interest rates.
- **Rates, credit, and currencies:** The outlook for local rates is constructive, while currencies are mixed, with the U.S. presidential election expected to stoke volatility.

Chris Kushlis
Chief Emerging Markets Macro Strategist

What does the rest of 2024 have in store for emerging markets (EM)? It will be important to keep an eye on developed market economic growth and whether the slowdown turns into a recession that drags down EM and weighs on investor sentiment. For now, EM growth is fairly steady overall, while inflation has moved into the rear view mirror as a concern for investors.

On the monetary policy front, the U.S. Federal Reserve moving to a cutting cycle is likely to open up the opportunity for new EM countries to also begin easing over the coming months. This should be supportive for EM local currency bonds, but the outlook for currencies is mixed, with uncertainty over the U.S. presidential election likely to stoke volatility.

Growth and fiscal

Resiliency of EM growth to be tested

The focus in markets has shifted from inflation concerns to economic growth worries. Although EM growth is fairly steady overall at present, there are divergences. Central and Eastern Europe, for example, is lagging other regions, while the two powerhouses of Latin America—Mexico and Brazil—are going in different directions with

“The focus in markets has shifted from inflation concerns to economic growth worries.

the former slowing while the latter is growing. Going forward, EM growth will likely be tested, especially as the economies of both China and the U.S. are slowing. How that evolves could be important for EM and broader risk sentiment. As the impact is most likely through the export channel and demand for EM goods, it will be important to monitor this area.

On the external front, current account balances are in relatively good shape in major EM countries. Deficits are not as out of control as they are in some developed economies, although there's a risk of some fiscal deterioration in nations where elections have taken place this year that resulted in surprise outcomes. In Mexico, for example, the ruling party won with a landslide victory, and despite pledges of fiscal responsibility, it will likely be challenging to adhere to fiscal rules given promises made not to raise taxes and increase social and infrastructure expenditures.

Monetary policy

Potential for more countries to start cutting interest rates

EM countries can largely be split into two groups when it comes to monetary policy this year—those that have been able to cut interest rates and those that have not. The group that has been easing monetary policy, which includes Chile, Hungary, and the Czech Republic, are nearing the end of their cutting cycles. The second group is yet to start, but that could change soon.

The Federal Reserve kicking off its easing cycle is expected to open up the opportunity for those EM countries that have been waiting on the sidelines—due to either currency concerns or sticky inflation—to also begin cutting interest rates. This group could include Mexico and South Africa, as well as some Asian countries. However, the cutting cycle in the Asia region is likely to be shallower than for EM peers as the inflation problem was not as deep in Asia. One country that bucks the broader easing trend is Brazil—where the central bank looks set to begin hiking again soon amid stronger growth.

Rates, credit, and currencies

U.S. presidential election could stoke volatility

The outlook for EM local rates remains constructive as there's potential for a new wave of countries to start easing monetary policy. For EM external debt, the backdrop is less positive as valuations are expensive versus history. But an encouraging year-to-date development in this area has been the progress made in key debt restructurings. Zambia, for example, reached an agreement with bondholders, while Ghana is also close to finishing its debt restructuring.

Within currencies, the outlook is mixed. Although medium-term fundamentals are well anchored in EM, their currencies may struggle with uncertainty surrounding the U.S. presidential election. There's potential for volatility as the race is tight and both presidential candidates have staked out vastly different economic plans.

Global backdrop matters for EM

(Fig. 1) How EM could perform in different global economic scenarios

Growth Stabilization

Positive tilt for risk sentiment

This scenario could drive U.S. Treasury yields higher and be positive for EM high-yielding currencies and mostly neutral for EM local rates.

Soft landing

Neutral for risk sentiment

This scenario could see more volatility initially but overall should be favorable for EM local rates and EM low-yielding currencies.

Recession

Negative tilt for risk sentiment

This scenario may weigh on risk sentiment, leading to weakness in EM currencies, but high-quality EM local rates could find some support.

As of September 2024.
For illustrative purposes only. This is not intended to be investment advice or a recommendation to take any particular investment action. Actual future outcomes may differ materially.
Source: T. Rowe Price analysis.

INVEST WITH CONFIDENCE™

T. Rowe Price identifies and actively invests in opportunities to help people thrive in an evolving world, bringing our dynamic perspective and meaningful partnership to clients so they can feel more confident.

DISCLOSURE CONTINUES ON THE FOLLOWING PAGE.

Important Information (cont.)

Australia—Issued by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 28, Governor Phillip Tower, 1 Farrer Place, Sydney NSW 2000, Australia. For Wholesale Clients only.

Brunei—This material can only be delivered to certain specific institutional investors for informational purpose only. Any strategy and/or any products associated with the strategy discussed herein has not been authorised for distribution in Brunei. No distribution of this material to any member of the public in Brunei is permitted.

Canada—Issued in Canada by T. Rowe Price (Canada), Inc. T. Rowe Price (Canada), Inc.'s investment management services are only available to Accredited Investors as defined under National Instrument 45-106. T. Rowe Price (Canada), Inc. enters into written delegation agreements with affiliates to provide investment management services.

Colombia, Chile, Mexico, Perù, Uruguay—This material is prepared by T. Rowe Price International Ltd - Warwick Court, 5 Paternoster Square, London, EC4M 7DX which is authorised and regulated by the UK Financial Conduct Authority - and issued and distributed by locally authorized distributors only. For professional investors only.

DIFC—Issued in the Dubai International Financial Centre by T. Rowe Price International Ltd which is regulated by the Dubai Financial Services Authority as a Representative Office. For Professional Clients only.

EEA—Unless indicated otherwise this material is issued and approved by T. Rowe Price (Luxembourg) Management S.à r.l. 35 Boulevard du Prince Henri L-1724 Luxembourg which is authorised and regulated by the Luxembourg Commission de Surveillance du Secteur Financier. For Professional Clients only.

Hong Kong—Issued in Hong Kong by T. Rowe Price Hong Kong Limited, 6/F, Chater House, 8 Connaught Road Central, Hong Kong. T. Rowe Price Hong Kong Limited is licensed and regulated by the Securities & Futures Commission. For Professional Investors only.

Indonesia—This material is intended to be used only by the designated recipient to whom T. Rowe Price delivered; it is for institutional use only. Under no circumstances should the material, in whole or in part, be copied, redistributed or shared, in any medium, without prior written consent from T. Rowe Price. No distribution of this material to members of the public in any jurisdiction is permitted.

Korea—This material is intended only to Qualified Professional Investors. Not for further distribution.

Mainland China—This material is provided to qualified investors only. No invitation to offer, or offer for, or sale of, the shares will be made in the mainland of the People's Republic of China ("Mainland China", not including the Hong Kong or Macau Special Administrative Regions or Taiwan) or by any means that would be deemed public under the laws of the Mainland China. The information relating to the strategy contained in this material has not been submitted to or approved by the China Securities Regulatory Commission or any other relevant governmental authority in the Mainland China. The strategy and/or any product associated with the strategy may only be offered or sold to investors in the Mainland China that are expressly authorized under the laws and regulations of the Mainland China to buy and sell securities denominated in a currency other than the Renminbi (or RMB), which is the official currency of the Mainland China. Potential investors who are resident in the Mainland China are responsible for obtaining the required approvals from all relevant government authorities in the Mainland China, including, but not limited to, the State Administration of Foreign Exchange, before purchasing the shares. This document further does not constitute any securities or investment advice to citizens of the Mainland China, or nationals with permanent residence in the Mainland China, or to any corporation, partnership, or other entity incorporated or established in the Mainland China.

Malaysia—This material can only be delivered to specific institutional investor. This material is solely for institutional use and for informational purposes only. This material does not provide investment advice or an offering to make, or an inducement or attempted inducement of any person to enter into or to offer to enter into, an agreement for or with a view to acquiring, disposing of, subscribing for or underwriting securities. Nothing in this material shall be considered a making available of, solicitation to buy, an offering for subscription or purchase or an invitation to subscribe for or purchase any securities, or any other product or service, to any person in any jurisdiction where such offer, solicitation, purchase or sale would be unlawful under the laws of Malaysia.

New Zealand—Issued by T. Rowe Price Australia Limited (ABN: 13 620 668 895 and AFSL: 503741), Level 28, Governor Phillip Tower, 1 Farrer Place, Sydney NSW 2000, Australia. No Interests are offered to the public. Accordingly, the Interests may not, directly or indirectly, be offered, sold or delivered in New Zealand, nor may any offering document or advertisement in relation to any offer of the Interests be distributed in New Zealand, other than in circumstances where there is no contravention of the Financial Markets Conduct Act 2013.

Philippines—ANY STRATEGY AND/ OR ANY SECURITIES ASSOCIATED WITH THE STRATEGY BEING DISCUSSED HEREIN HAVE NOT BEEN REGISTERED WITH THE SECURITIES AND EXCHANGE COMMISSION UNDER THE SECURITIES REGULATION CODE. ANY FUTURE OFFER OR SALE OF THE STRATEGY AND/ OR ANY SECURITIES IS SUBJECT TO REGISTRATION REQUIREMENTS UNDER THE CODE, UNLESS SUCH OFFER OR SALE QUALIFIES AS AN EXEMPT TRANSACTION.

Singapore—Issued by T. Rowe Price Singapore Private Ltd. (UEN: 201021137E), 501 Orchard Rd, #10-02 Wheelock Place, Singapore 238880. T. Rowe Price Singapore Private Ltd. is licensed and regulated by the Monetary Authority of Singapore. For Institutional and Accredited Investors only.

South Africa—Issued in South Africa by T. Rowe Price International Ltd (TRPIL), Warwick Court, 5 Paternoster Square, London EC4M 7DX, is an authorised financial services provider under the Financial Advisory and Intermediary Services Act, 2002 (Financial Services Provider (FSP) Licence Number 31935), authorised to provide "intermediary services" to South African Investors. TRPIL's Complaint Handling Procedures are available to clients upon request. The Financial Advisory and Intermediary Services Act Ombud in South Africa deals with complaints from clients against FSPs in relation to the specific services rendered by FSPs. The contact details are noted below: Telephone: +27 12 762 5000, Web: www.faisombud.co.za, Email: info@faisombud.co.za

Switzerland—Issued in Switzerland by T. Rowe Price (Switzerland) GmbH, Talstrasse 65, 6th Floor, 8001 Zurich, Switzerland. For Qualified Investors only.

Taiwan—This does not provide investment advice or recommendations. Nothing in this material shall be considered a solicitation to buy, or an offer to sell, a security, or any other product or service, to any person in the Republic of China.

Thailand—This material has not been and will not be filed with or approved by the Securities Exchange Commission of Thailand or any other regulatory authority in Thailand. The material is provided solely to "institutional investors" as defined under relevant Thai laws and regulations. No distribution of this material to any member of the public in Thailand is permitted. Nothing in this material shall be considered a provision of service, or a solicitation to buy, or an offer to sell, a security, or any other product or service, to any person where such provision, offer, solicitation, purchase or sale would be unlawful under relevant Thai laws and regulations.

UK—This material is issued and approved by T. Rowe Price International Ltd, Warwick Court, 5 Paternoster Square, London EC4M 7DX which is authorised and regulated by the UK Financial Conduct Authority. For Professional Clients only.

USA—Issued in the USA by T. Rowe Price Associates, Inc., 100 East Pratt Street, Baltimore, MD, 21202, which is regulated by the U.S. Securities and Exchange Commission. For Institutional Investors only.