Monthly Comments – Emerging Markets

MacroFinance Research – June 2021

Key Messages

Country Focus – Philippines: Economic recovery hinges on pandemic management

Philippines as one of the fastest growing emerging economies was severely impacted by Covid-19 witnessing a steep recession in 2020. The situation exposed deficiencies in its healthcare system and severe movement restrictions to curb the pandemic greatly stymied domestic consumption and industrial production. Moreover, the fiscal support, although large, failed to match the scale of pandemic impact to provide the necessary fillip to the economy. In 2021, the subsequent increase in daily Covid-19 infections and lack of effective vaccination policy continue to be a drag on economic performances. Given these factors, the mechanical economic rebound in 2021 is likely to remain modest. The enhanced currency competitiveness will support external trade and sovereign risks remain contained. However, high corporate vulnerabilities might lead to bankruptcies in weaker sectors, in turn impacting banking sector (asset quality, restructurations, …). Moreover, with Presidential elections less than a year away, near term political gains can overpower polices necessary for long term economic growth.

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RiskWatch – Vulnerable economies in a persistent pandemic

In 2021, the new and virulent mutations of the virus have increased the complexity of the pandemic management and infection levels have increased even among countries that witnessed lesser cases in the previous year. Meanwhile the rollout of the vaccinations has been favorably skewed toward high and upper-middle-income countries, leaving most of the low-income nations vulnerable. Hence, to combat the pandemic, most EMs have gone into repeated or extended lockdowns that have dented the economic activity. However, unlike the last year, the movement restrictions this time around have been targeted and less stringent, thereby reducing the brunt on economic activity. Unless the delay in vaccination is corrected (not until the end of 2022), the most vulnerable economies would be low-income countries (specially in Africa), also economies that are depended on tourism income (Egypt, Turkey). In addition, those countries that are currently in high epidemiological index, lesser stringency levels (India, Vietnam, Brazil) would require further lockdown measures in the future and on the contrary, countries with current high stringency (Philippines, Turkey) now face short-term pain, but the strategy might prove effective in controlling the pandemic.

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As always, readers are most welcome to come back to us for further details or clarifications.

Completed on June 15, 2021.

Country Focus – Philippines: Economic recovery hinges on pandemic management

Philippines as one of the fastest growing emerging economies was severely impacted by Covid-19 witnessing a steep recession in 2020. The situation exposed deficiencies in its healthcare system and severe movement restrictions to curb the pandemic greatly stymied domestic consumption and industrial production. Moreover, the fiscal support, although large, failed to match the scale of pandemic impact to provide the necessary fillip to the economy. In 2021, the subsequent increase in daily Covid-19 infections and lack of effective vaccination policy continue to be a drag on economic performances. Given these factors, the mechanical economic rebound in 2021 is likely to remain modest. The enhanced currency competitiveness will support external trade and sovereign risks remain contained. However, high corporate vulnerabilities might lead to bankruptcies in weaker sectors, in turn impacting banking sector (asset quality, restructurations, …). Moreover, with Presidential elections less than a year away, near term political gains can overpower polices necessary for long term economic growth.

Covid-19 steeply cuts down a strong economic growth story

At the onset of Covid-19 crisis, Philippines was a robust economy witnessing a stellar GDP growth (above 6% y/y for the past eight years). Since the pandemic, the country has however recorded one of the poorest performances (-9.6% y/y in 2020), exposing its ill-equipped health care system. It has been caught in a vortex of deteriorating health situation, severe movement restrictions, and inadequate policy support; each cumulatively undermining the economy.

The government imposed one of the strictest lockdown measures in 2020, leading to contraction in manufacturing (-10%) and increase in unemployment (10.4%). Moreover, the fiscal support (close to 4% of GDP), although large, has been insufficient to meet its pandemic needs, where the sanitary conditions and the economy required enormous support.

Pandemic déjà vu in 2021 and vaccination shortfall

The challenges with the pandemic have intensified in 2021. While the ebb and flow of infections and restrictions continue (over 200k daily infections at its peak in April 2021), only 2.3% of the population have received the first vaccine dose until mid-May. With the current vaccination shortage, the best-case scenario to vaccinate the planned 70% of the population will happen by June 2022, or by Jan. 2023 in the worst-case scenario.

Hence the worsening health situation in early 2021 has led to a fifth consecutive quarter of GDP contraction in 2021Q1 (-4.2% y/y); inflation has accelerated to +4.5% y/y in Mar. and April (temporary supply-side constraints and increase in transportation prices); while domestic demand and business conditions have remained mediocre.

Below potential economic recovery in 2021

For a strong economy like the Philippines, the recovery in 2021 will be below its stellar historical growth rate (+4.5% y/y in 2021 projected by ADB) despite a global economic recovery (supporting exports) and robust fundamentals:

(a) strong external trade performances as evidenced by the rebasing of our *exchange rate competitiveness* index. The moderate currency overvaluation has been corrected due to improvements in structural competitiveness;
(b) improving remittances (increased by +5.3% y/y in Feb. 2021 and contributing 10% of the GDP);
(c) historically low fiscal and low external debt, providing ample space for policy support.

However, the mechanical rebound would have been much higher (with a low base effect) if the budgetary support had been stronger and well directed. Nonetheless, the inherent structural weaknesses in political decision making (choosing political optics over necessary polices) led to misplaced and inadequate policy support.

Index of Sensitivity to Post-Covid Transition – Credit, Growth & Resilience
from 0 (best) to100 (worst)

	Philippines	Rank from worst out of 100 countries
Liquidity Index	16	88
Shock to corporates	48	44
Shock to Sovereign	34	87
Gross Credit Risk	33	87
Credit Sensitivity	**28**	**86**
Covid-19 Situation	69	10
Lockdown Stringency	53	29
Monetary support	50	43
Fiscal support	38	76
International transmission	86	6
Growth Sensitivity	**59**	**9**
Resilience Growth 2020	64	21
Timeline to recovery	66	6
FX rate and volatility	5	73
Resilience	**50**	**21**
Overall Index	**47**	**26**

Source: TAC ECONOMICS

Beyond 2021 – Opportunities and Risks

Assuming roll out of an effective vaccination and control of the pandemic, and the course corrected polices by the government (fiscal deficit to expand to -8.9%, new tax law friendly to attract investments), Philippines can be expected to be on a steady path to economic recovery.

Philippines will be supported by low Credit Sensitivity and low fx volatility. There is also an absence of Sovereign Risk (moderate fx obligations backed by strong foreign reserves).

However Corporate Risk is elevated- with the highly indebted corporates, increasing the chances of defaults and bankruptcies in fragile sectors, especially when the economic recovery is slow. As a ripple effect, this shall reduce asset quality in the banking sector. Finally, since R. Duterte's term will end in June 2022, the upcoming Presidential elections can increase the political heat that would dictate economic policies colored by short-term political interests.

RiskWatch – Vulnerable economies in a persistent pandemic

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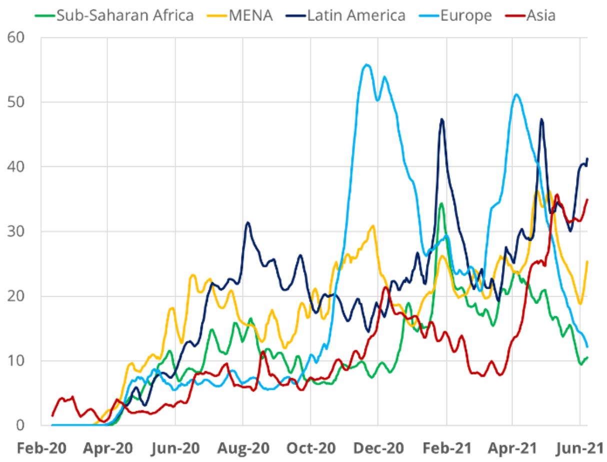
The long haul of Covid-19 pandemic

(a) Persistent infections: More than a year since Covid-19 has been declared a pandemic, the level of infections persists in repeated waves, most often than not, it has been larger and widespread than in the previous year. This tread is specially witnessed among the emerging economies, some of which have gone from very low case levels in 2020, to pronounced peaks of infection in 2021. The emergence of new variants (in UK, India, South Africa) are leading to a faster and a virulent spread. All of this has heightened the complexity and uncertainty of the pandemic.

Epidemiologic Stress Index by region
countries average by region, 7-day moving average



Source: TAC ECONOMICS

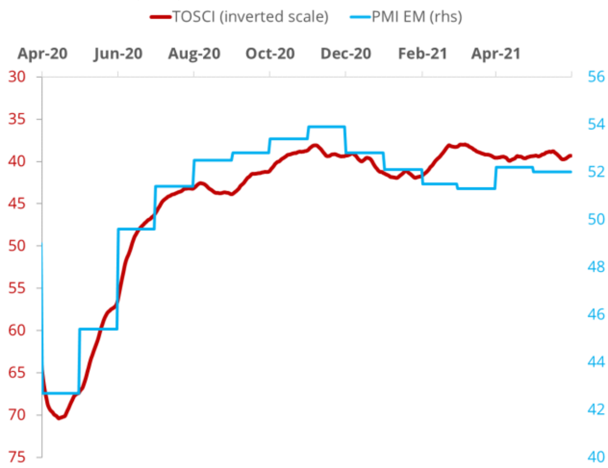
(b) The dream of herd immunity: Meanwhile, an effective vaccination strategy, one of the key factors for Covid-19 management has been disproportionately skewed. Among the 6% of the global population that has been fully vaccinated, close to 85% of them have been in high and upper-middle income countries. With the ongoing vaccination shortage, EMs aiming to vaccinate close to 60% of their population, will be able to achieve this in the best by end of 2022.

(c) Movement restrictions are to stay: lacking a faster rollout of the vaccination and with the newer mutations, governments have little choice than to repeatedly impose varying movement restrictions. At least 80 EMs have reintroduced some form of stringency in 2021. This alternating 'Hammer and Dance' – containment and activity - is likely to continue until economies reach a certain level of pandemic immunity.

Diminishing Economic Impact

While the movement restrictions adversely impact economic activity, in the recent confinements the severity of economic impact has been lesser. This is reflected in the graph below where the stringency has been lesser in the recent months, hence the PMI has not dropped sharply. The restrictions are more localized and targeted to specific geographic areas, and firms and households are adopting to production and consumption patterns that are less disruptive. Case in point, **India** (largest daily infections in the world in April-May 2021), maintained above average business conditions (manufacturing PMI above 50 in the same period). Similarly other countries like **Malaysia**, **Philippines**, and **Turkey**, while have imposed new rounds to lockdowns, the reduction in business conditions are not at the very low levels of 2020.

Stringency of Confinement (TOSCI) versus PMI



Source: TAC ECONOMICS, Oxford University, Datastream

Economies most impacted in a long-drawn pandemic

With the nebulous end in sight of the pandemic, some of the most affected would be

(a) countries with low on vaccination rate and who are largely depended UN's COVAX;

(b) low-income countries (most of them present in Africa) given their poor health infrastructure and low vaccination levels;

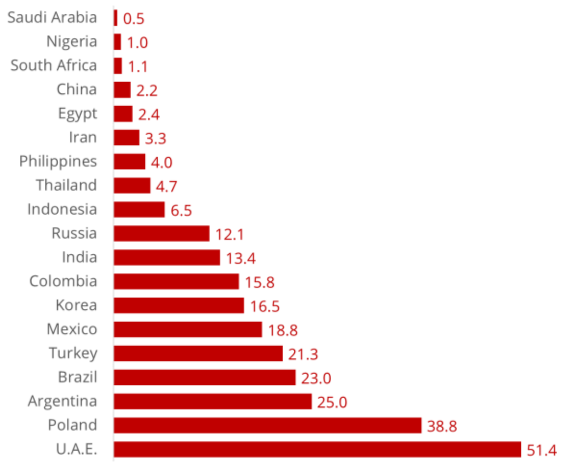
(c) countries with high dependence on tourism - **Egypt**, **Turkey**, **Caribbean islands**, as international travel will remain keenly restricted due to evolving Covid-19 mutations;

(d) countries that are demonstrating poor business conditions despite low stringency (**Colombia**, **Thailand** and **Mexico**);

(e) countries that have elevated epidemiological index, but low stringency, indicating the necessity for more lockdowns in the future that in turn might lead to persistently adverse business conditions (**India**, **Vietnam**, **Brazil**);

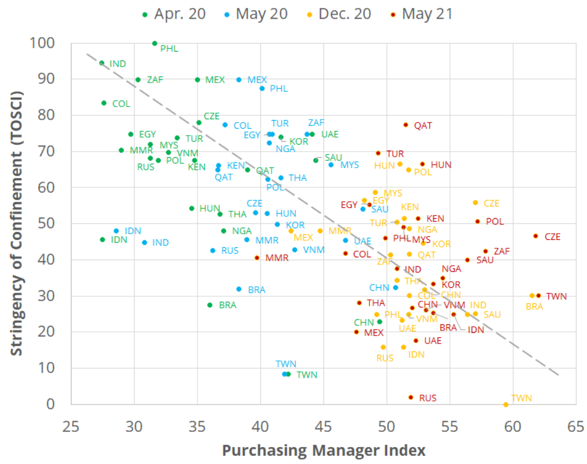
(f) intensified short-term pain for countries with current severe lockdowns (**Turkey** and **Philippines**), although this strategy might be useful in controlling the pandemic.

People who received at least one dose of Covid-19 vaccine
% population



Source: TAC ECONOMICS, Datastream

Stringency of Confinement (TOSCI) versus PMI



Source: TAC ECONOMICS, Datastream

Appendix 1: List of 100 countries monitored by alphabetical order of ISO3 Code

ISO 3 Code	Country Name
AGO	Angola
ALB	Albania
ARG	Argentina
ARM	Armenia
AZE	Azerbaijan
BEN	Benin
BFA	Burkina Faso
BGD	Bangladesh
BGR	Bulgaria
BHR	Bahrein
BIH	Bosnia
BLR	Belarus
BOL	Bolivia
BRA	Brazil
BRN	Brunei
CHL	Chile
CHN	China
CIV	Cote d'Ivoire
CMR	Cameroon
COD	DR Congo
COG	Rep. of Congo
COL	Colombia
COM	Comoros
CPV	Cape Verde
CRI	Costa Rica
CZE	Czech Rep.
DMA	Dominica
DOM	Dominican Rep
DZA	Algeria
ECU	Ecuador
EGY	Egypt
ETH	Ethiopia
GAB	Gabon
GEO	Georgia
GHA	Ghana
GIN	Guinea
GNB	Guinea Bissau
GTM	Guatemala
HND	Honduras
HRV	Croatia
HUN	Hungary
IDN	Indonesia
IND	India
IRN	Iran
ISR	Israel
JOR	Jordan
KAZ	Kazakhstan
KEN	Kenya
KHM	Cambodia
KOR	Korea

ISO 3 Code	Country Name
KWT	Kuwait
LAO	Laos
LBY	Libya
LKA	Sri Lanka
MAR	Morocco
MDG	Madagascar
MEX	Mexico
MKD	N. Macedonia
MLI	Mali
MMR	Myanmar
MNE	Montenegro
MNG	Mongolia
MOZ	Mozambique
MUS	Mauritius
MYS	Malaysia
NER	Niger
NGA	Nigeria
NPL	Nepal
OMN	Oman
PAK	Pakistan
PAN	Panama
PER	Peru
PHL	Philippines
POL	Poland
PRY	Paraguay
QAT	Qatar
ROU	Romania
RUS	Russia
RWA	Rwanda
SAU	Saudi Arabia
SDN	Sudan
SEN	Senegal
SLV	El Salvador
SRB	Serbia
SYC	Seychelles
TGO	Togo
THA	Thailand
TUN	Tunisia
TUR	Turkey
TWN	Taiwan
TZA	Tanzania
UAE	UAE
UGA	Uganda
UKR	Ukraine
URY	Uruguay
VEN	Venezuela
VNM	Vietnam
YEM	Yemen
ZAF	South Africa
ZMB	Zambia

Appendix 2: List of 100 countries monitored by region

Eastern & Central Europe, CIS (19)			
ALB	Albania	KAZ	Kazakhstan
ARM	Armenia	MNE	Montenegro
AZE	Azerbaijan	MKD	N. Macedonia
BLR	Belarus	POL	Poland
BIH	Bosnia	ROU	Romania
BGR	Bulgaria	RUS	Russia
HRV	Croatia	SRB	Serbia
CZE	Czech Rep.	TUR	Turkey
GEO	Georgia	UKR	Ukraine
HUN	Hungary		

Latin America (18)			
ARG	Argentina	SLV	El Salvador
BOL	Bolivia	GTM	Guatemala
BRA	Brazil	HND	Honduras
CHL	Chile	MEX	Mexico
COL	Colombia	PAN	Panama
CRI	Costa Rica	PRY	Paraguay
DMA	Dominica	PER	Peru
DOM	Dominican Rep	URY	Uruguay
ECU	Ecuador	VEN	Venezuela

Asia (18)			
BGD	Bangladesh	MNG	Mongolia
BRN	Brunei	MMR	Myanmar
KHM	Cambodia	NPL	Nepal
CHN	China	PAK	Pakistan
IND	India	PHL	Philippines
IDN	Indonesia	LKA	Sri Lanka
KOR	Korea	TWN	Taiwan
LAO	Laos	THA	Thailand
MYS	Malaysia	VNM	Vietnam

Middle East & North Africa (15)			
DZA	Algeria	MAR	Morocco
BHR	Bahrein	OMN	Oman
EGY	Egypt	QAT	Qatar
IRN	Iran	SAU	Saudi Arabia
ISR	Israel	TUN	Tunisia
JOR	Jordan	UAE	UAE
KWT	Kuwait	YEM	Yemen
LBY	Libya		

Sub-Saharan Africa (30)			
AGO	Angola	MDG	Madagascar
BEN	Benin	MLI	Mali
BFA	Burkina Faso	MUS	Mauritius
CMR	Cameroon	MOZ	Mozambique
CPV	Cape Verde	NER	Niger
COM	Comoros	NGA	Nigeria
COG	Rep. of Congo	RWA	Rwanda
COD	DR Congo	SEN	Senegal
CIV	Cote d'Ivoire	SYC	Seychelles
ETH	Ethiopia	ZAF	South Africa
GAB	Gabon	SDN	Sudan
GHA	Ghana	TZA	Tanzania
GIN	Guinea	TGO	Togo
GNB	Guinea Bissau	UGA	Uganda
KEN	Kenya	ZMB	Zambia

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