



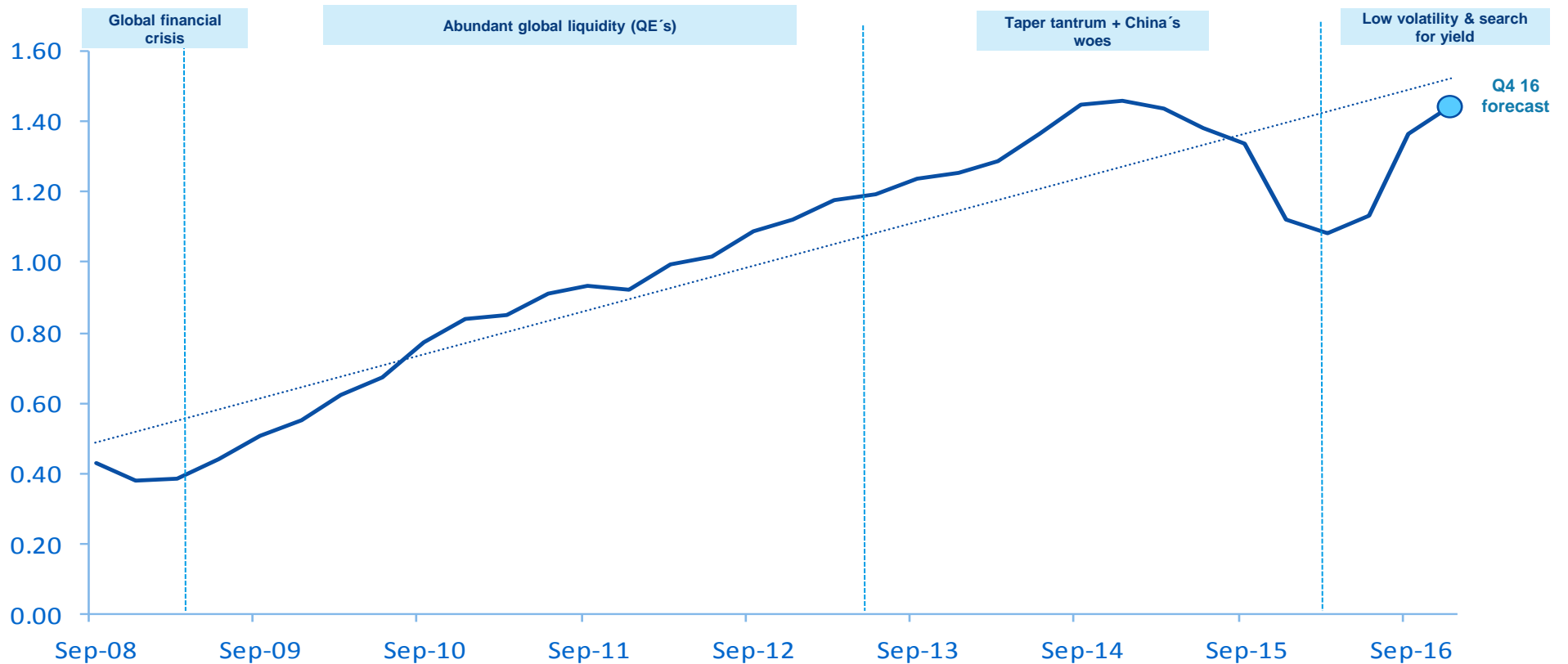
Harness Investor Forum

Jorge Sicilia, Chief Economist BBVA
Geneva- November 2016

Portfolio flows to EM: three stages

Cumulated Portfolio flows to Emerging Markets using high frequency data

Flows in US\$ Tn, cumulated from January 2005

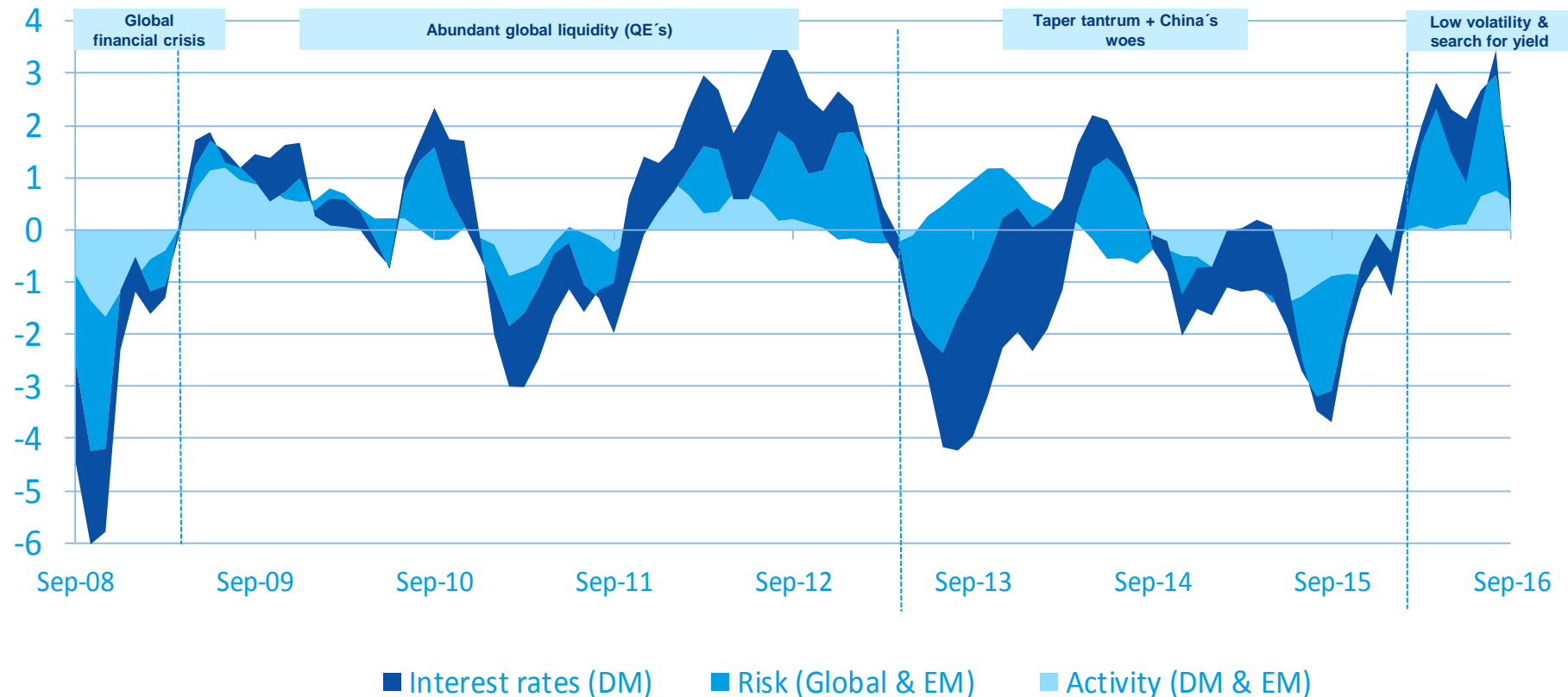


Portfolio flows to EM: The importance of global factors, particularly monetary policy in DM

BBVA Global Factor of Portfolio Flows Decomposition

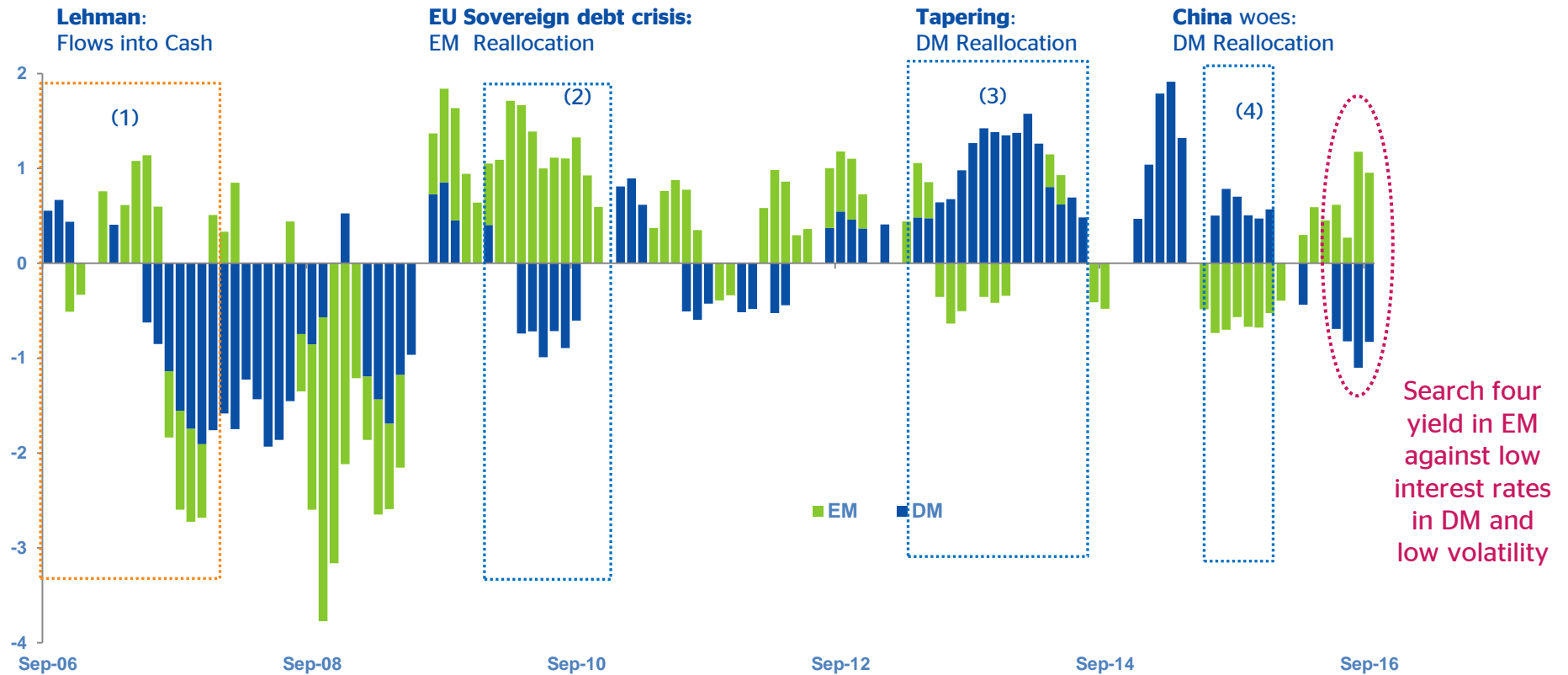
(First Factor from Flows using BBVA's DFM/FAVAR Model represents the main driver of flows, 6M moving average)

Source: BBVA Research



Portfolio flows reallocation: Where are we?

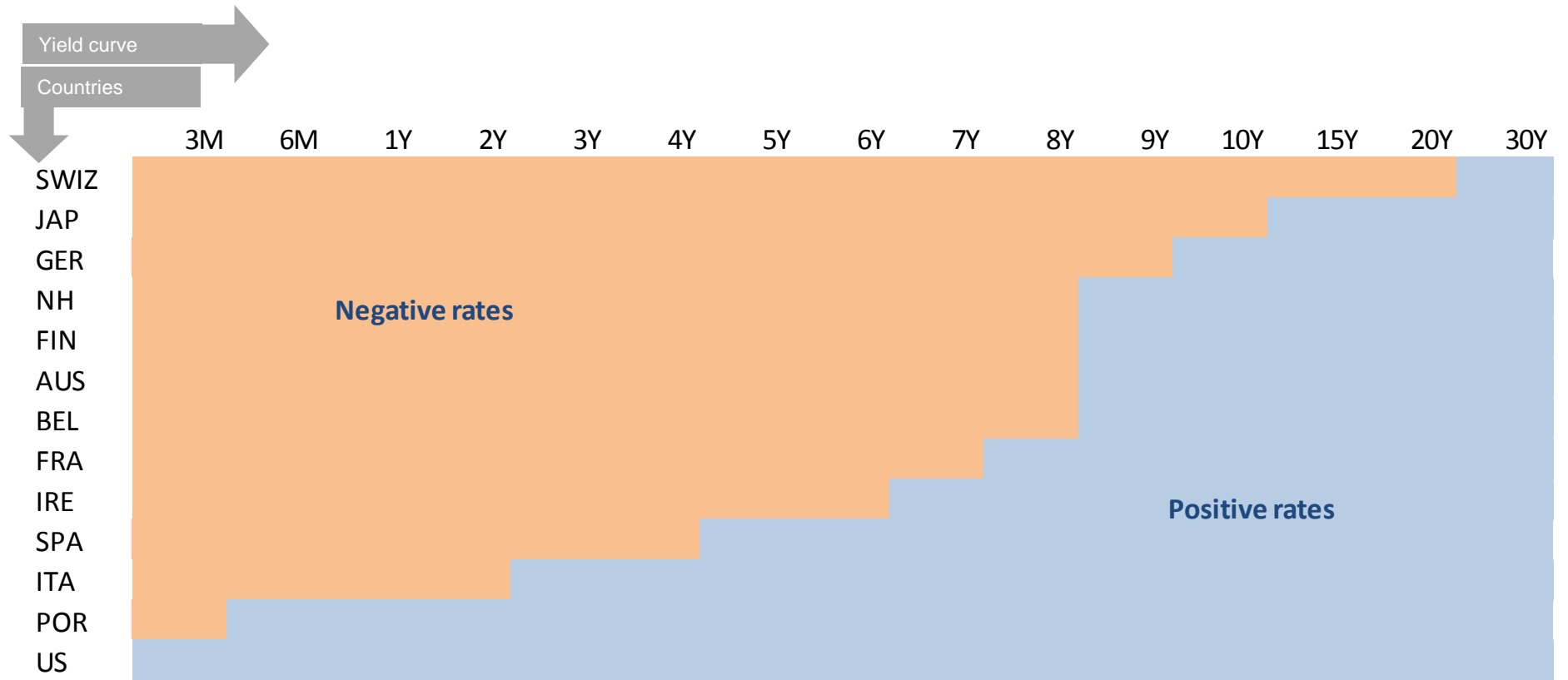
BBVA Developed vs. Emerging Market Portfolio Flows Reallocation Indicator* Source: BBVA Research



(*) Bars represent 1σ-significant events where the regional DM and EM factor contributed to Developed Markets and Emerging Market Flows. Sign of the contribution is given by the direction of the bars, Values are normalized. Reallocation events are there where DM/EM factor contributions have opposite signs (events: 2, 3, 4)

Low (and negative) interest rates are spreading across DM

The negative interest rates have spread across countries and yield curve



Source: BBVA Research

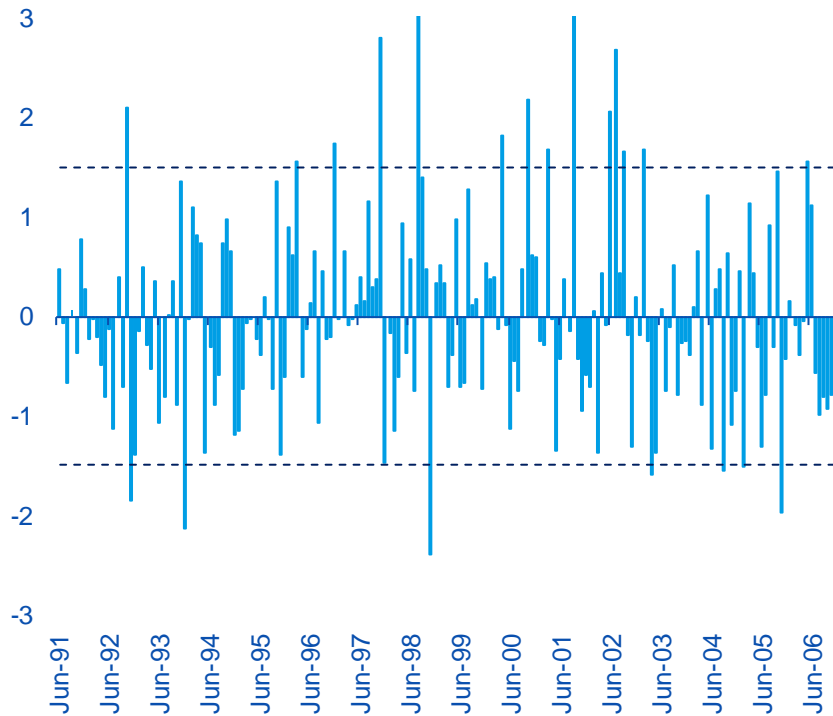
* Central banks that have entered in negative territory: ECB, Denmark, Switzerland, Sweden, Japan (but not the BoE or the Fed)

Volatility: Big shocks of volatility are more frequent, but less persistent (New normal?)...

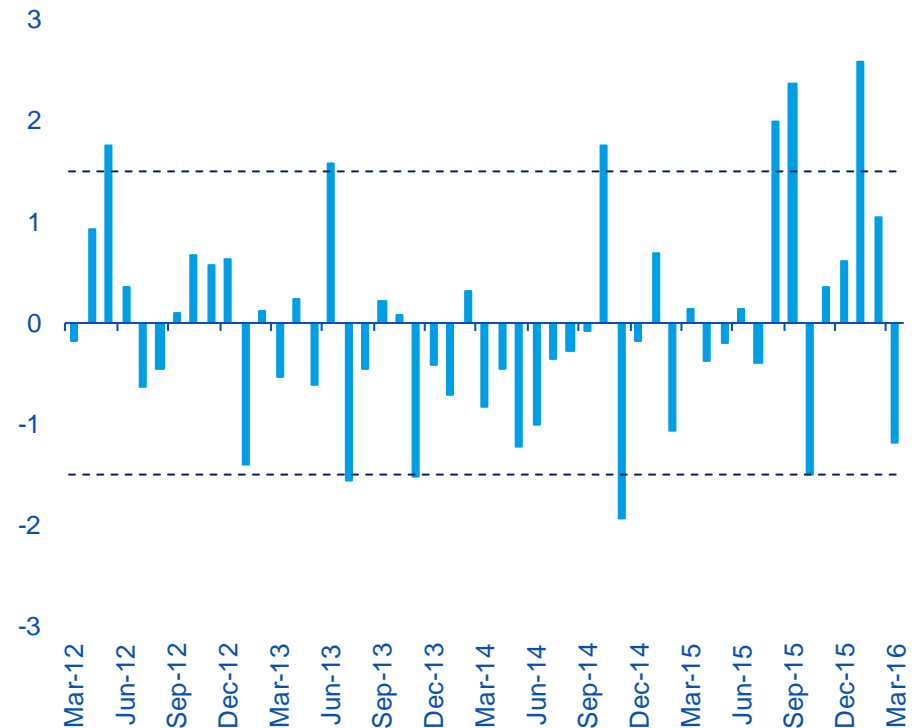
Uncertainty shocks

Source: BBVA Research

Sample 1 of “normal times”, “big shocks”: 10%



Sample 2 of “normal times”, “big shocks”: 20%

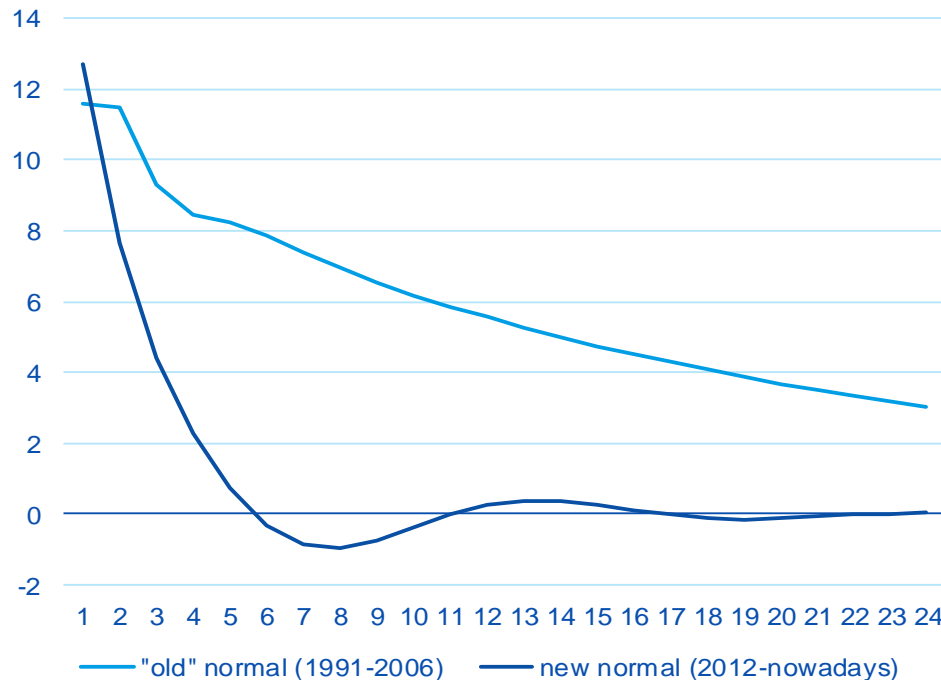


“Big shock” = a shock that is higher/lower than 1.5 std. deviation

... with higher impact on activity in the short-run, but shorter lived (due to central bank support?)

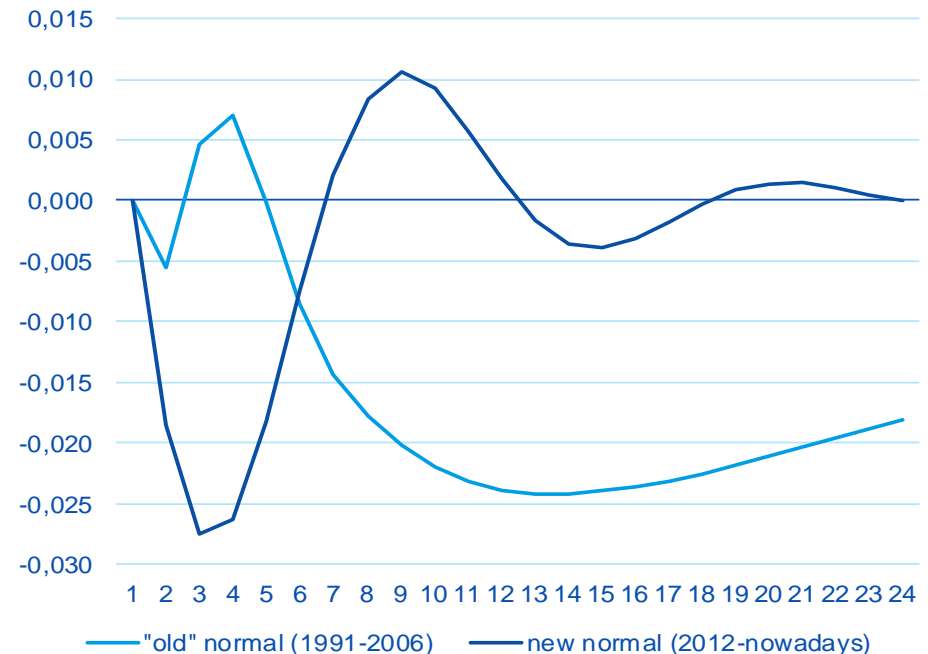
VIX response to a shock that increases uncertainty (bp)

Source: BBVA Research



GDP growth response to a shock that increases uncertainty (%)

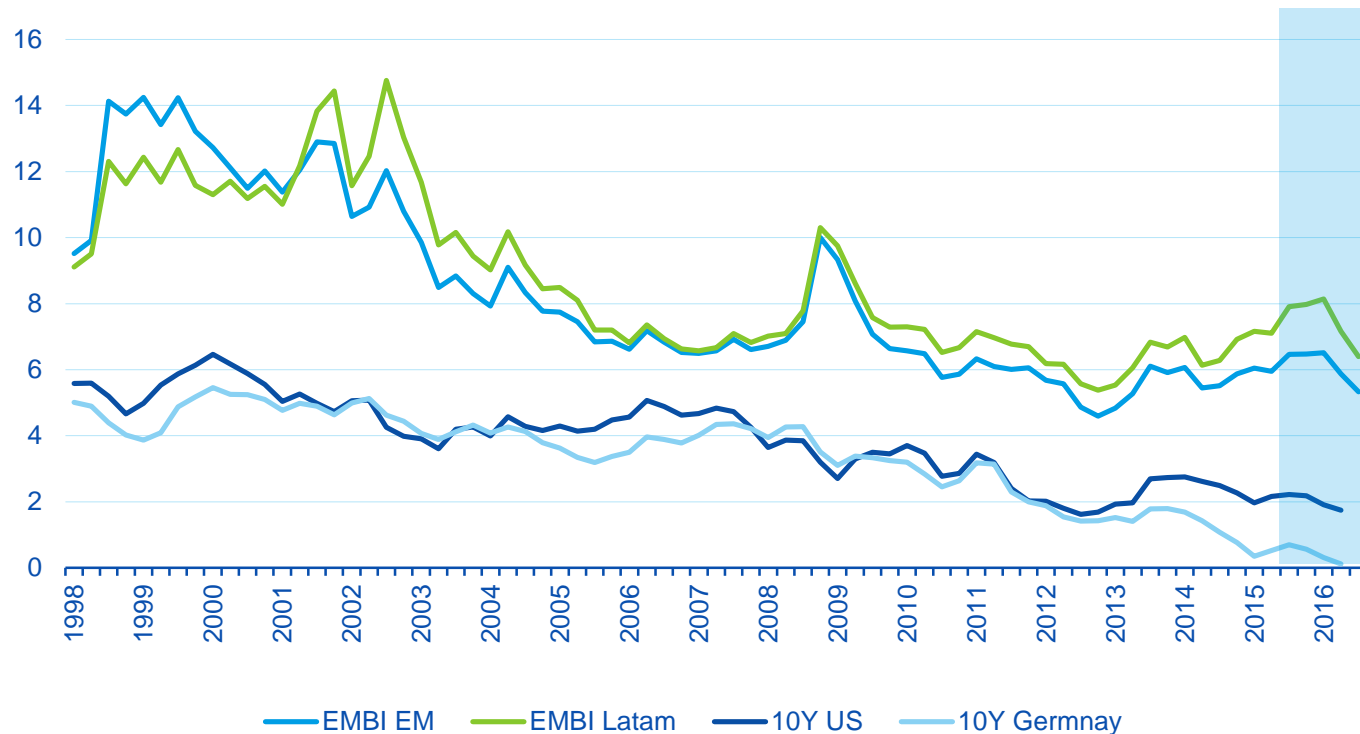
Source: BBVA Research



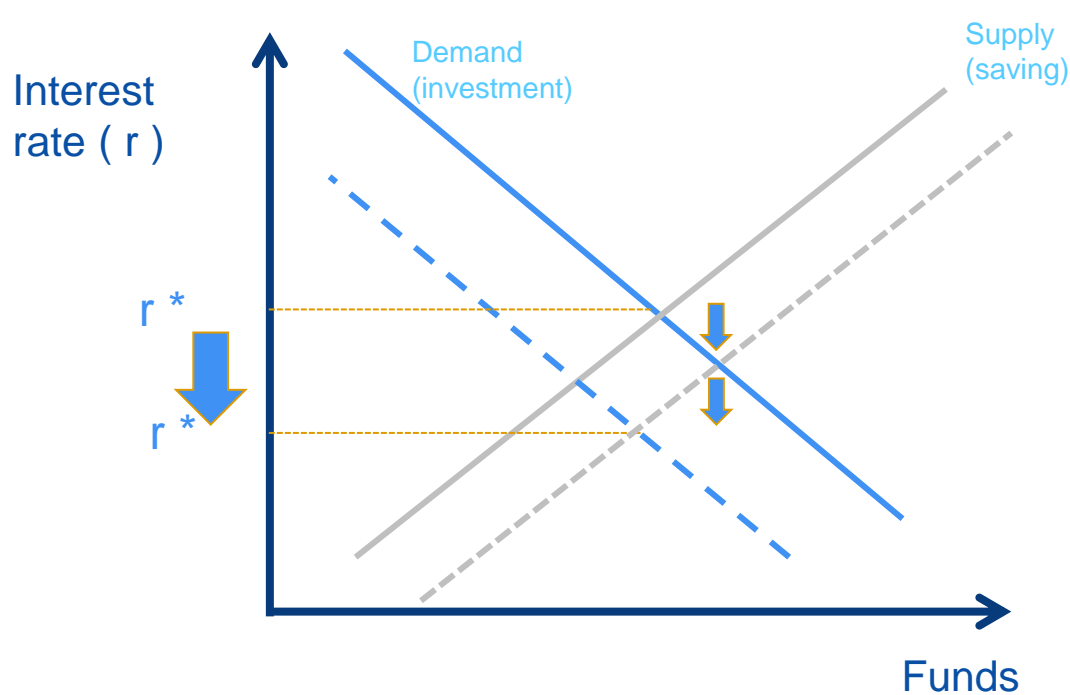
x-axis = months after the shock

Low interest rates, a global phenomena; is there an end to it in sight? What for emerging markets?

Interest rates in DM and EM (%)



Interest rates in the medium to long term (r^*) are determined by structural factors



Structural factors behind low interest rates

Increasing supply (saving)

Saving in Emerging markets

Demographics in DM

Greater inequality

Increasing uncertainty (risk aversion)

Decreasing demand (investment)

Drop in productivity (and growth)

Lower price of capital goods

Lower public investment (DM)

Deleveraging

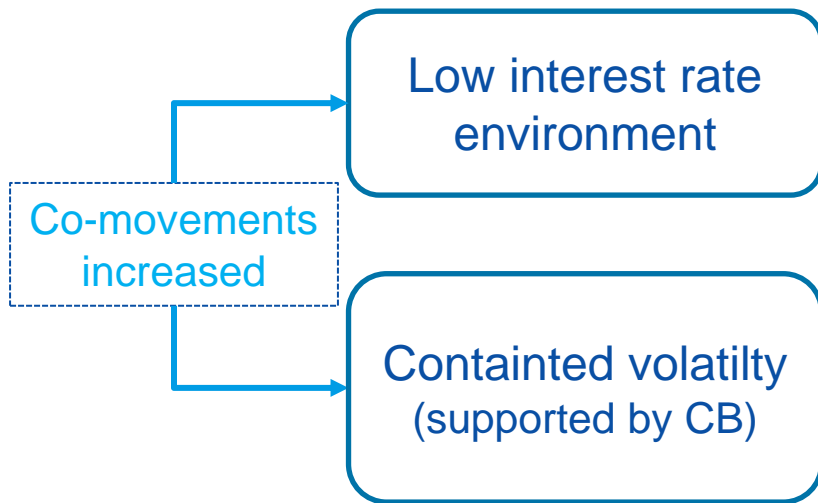
High uncertainty

Financial intermediation

Financial repression (non-standard monetary policy and forward guidance i.e. low term premium)

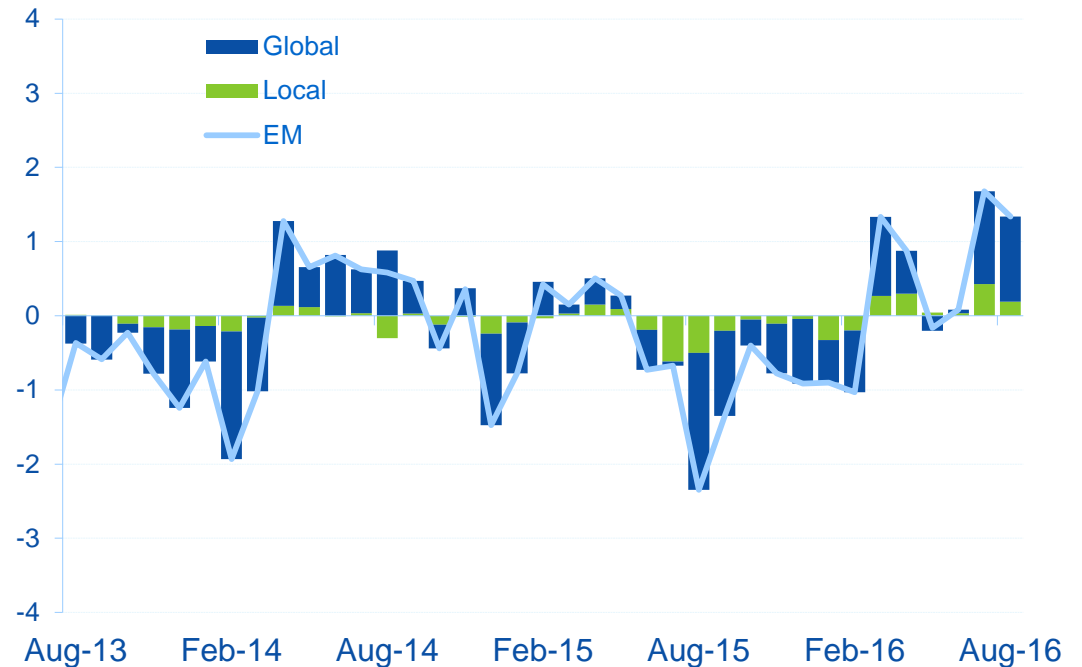
Shortage of safe assets (due to regulatory compliance)

Global trends (low interest rates and volatility) are the main drivers. Local factors are secondary



Portfolio flows to EM, global vs local factors

(Median EM Portfolio Flow Decomposition, monthly change in %)



Source: BBVA Research

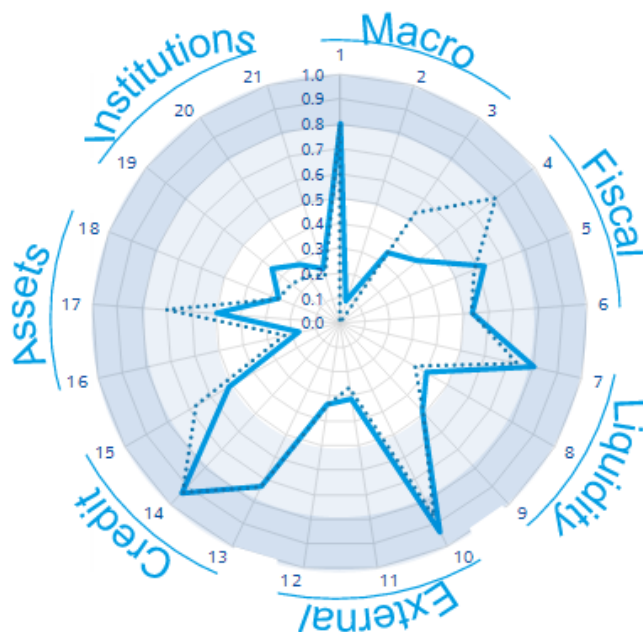
While EM vulnerabilities have declined, differentiation still matters and will come back

Emerging countries: vulnerability radar 2016

Relative position for the emerging developed countries. Max risk=1, Min risk=0. Previous year data is shown as a dotted line.

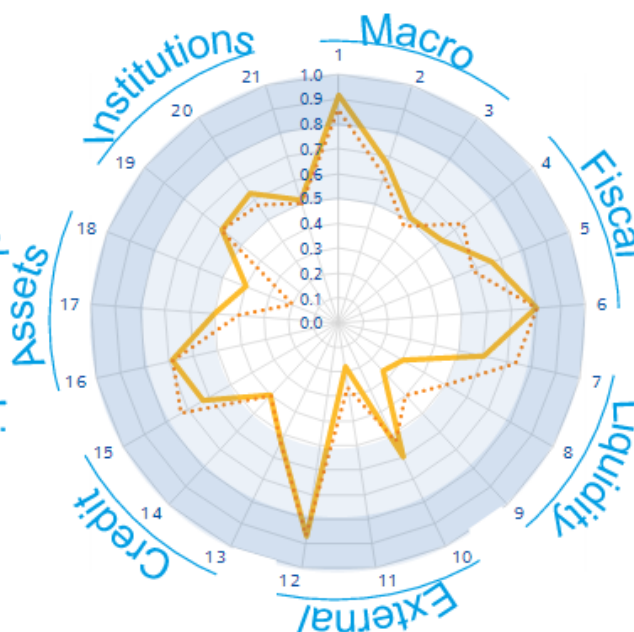
Source: BBVA Research

Emerging Europe



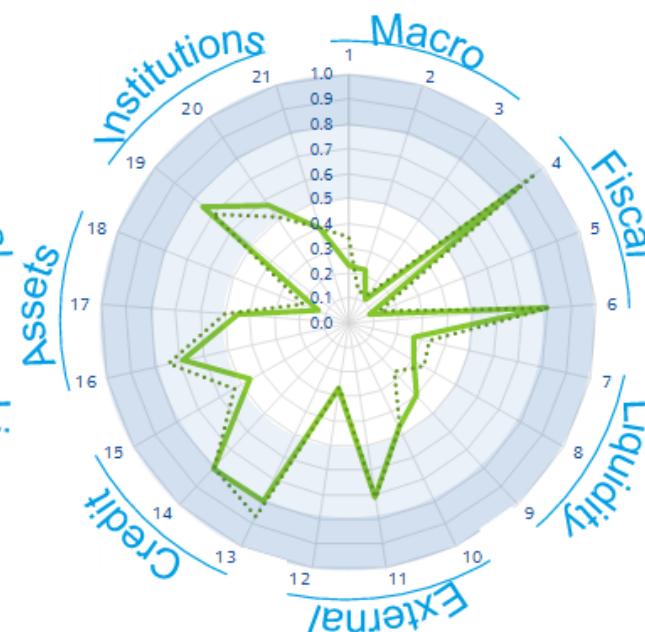
Significant improvement in public primary balances. High levels of corporate and external debt

LatAm



GDP growth and external vulnerabilities worsening with respect to 2015. Improvement in liquidity vulnerabilities

Emerging Asia



Public balances still the main vulnerability. Private leverage (households & corporates) also at risky levels



- Macro:** (1) GDP (%YoY) (2) Prices (% YoY) (3) Unemployment (% LF)
- Fiscal:** (4) Structural balance (%) (5) Interest rate – GDP % YoY (6) Public debt (% GDP)
- Liquidity:** (7) Debt by non-residents (% total) (8) Financial needs (% GDP) (9) Financial pressure (% GDP)
- External:** (10) External debt (% GDP) (11) RER appreciation (%YoY) (12) CAC balance (% GDP)

- Credit:** (13) Household (%GDP) (14) Corporate (% GDP) (15) Credit-to-deposit (%)
- Assets:** (16) Private credit to GDP (% YoY) (17) Housing prices (% YoY) (18) Equity (%GDP)
- Institutional:** (19) Political stability (20) Corruption (21) Rule of law

Potential source of risk: leverage and profitability in non-financial corporate sector

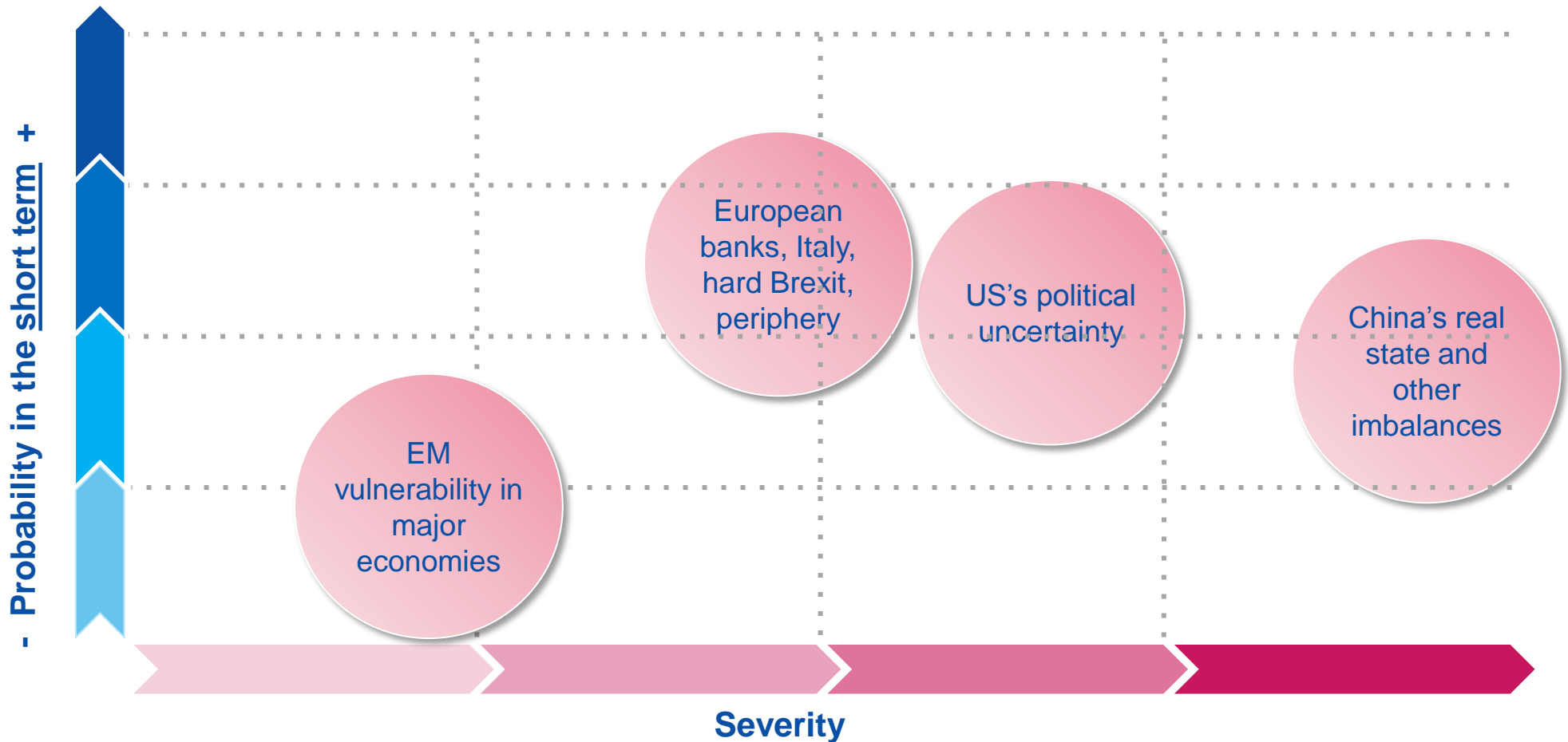
Corporate Vulnerability Dashboard: explanatory variables

	Corporate Debt (% GDP, last available data)	ROE change, % (2015 vs. average 2010-13)	Net Debt to EBITDA (last available data)	Industry Diversification Index (last available data)
China	Very High	Very Low	Very Low	Very High
Chile	High	Very Low	Very High	High
Brazil	Very Low	Very Low	Very High	Very High
Argentina	Very Low	Very High	High	High
Colombia	Very Low	Very Low	Very High	High
Turkey	High	Very Low	High	High
India	Very Low	Very Low	High	High
Peru	Very Low	High	High	High
Russia	High	Very Low	Very Low	High
Poland	Very Low	Very Low	High	Very High
Mexico	Very Low	Very Low	High	High
Indonesia	Very Low	Very Low	Very Low	High

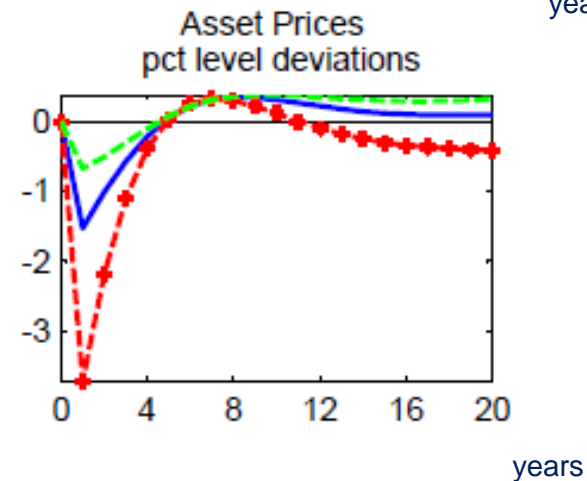
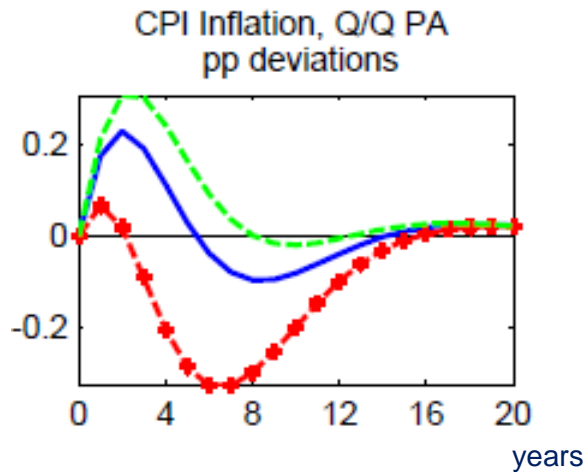
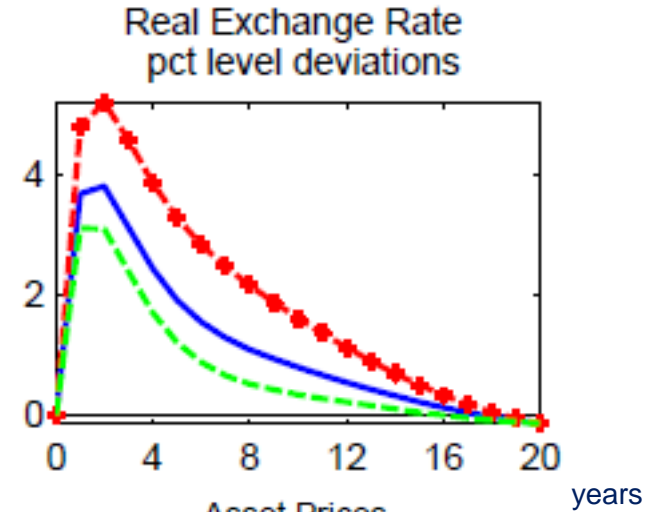
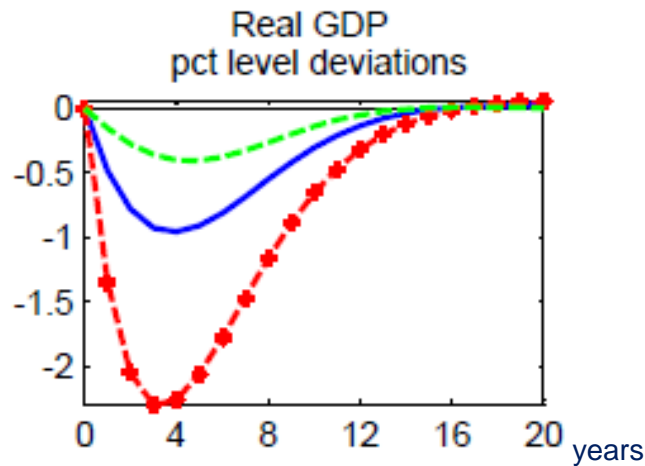
Level of risk Very high ■ ■ ■ ■ Very Low

Source: BBVA Research

Mapping the global risks in a two year horizon



The impact in EM of a shock in global risk premium



— EM Economy (35% FX Lending) - - - + Vulnerable Economy (65% FX Lending) - - - 10% FX Lending

C D E

55.45

100%

12.55

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