

*The views expressed in these posts are those of the authors and are current only through the date stated. These views are subject to change at any time based upon market or other conditions, and Eaton Vance disclaims any responsibility to update such views. These views may not be relied upon as investment advice and, because investment decisions for Eaton Vance are based on many factors, may not be relied upon as an indication of trading intent on behalf of any Eaton Vance fund. The discussion herein is general in nature and is provided for informational purposes only. There is no guarantee as to its accuracy or completeness.*

[EMERGING MARKETS DEBT](#) | [INTERNATIONAL/GLOBAL](#)

## IMF Spring Conference Focuses on Sticky Inflation and Accelerating Economic Fragmentation

By: *Emerging Markets Debt* | May 5, 2023

**Boston** - The April meeting of the IMF revealed an outlook made uncertain by financial sector distress and continuing high inflation levels, while policy debates focused on the risks of supply-chain disruptions, rising geopolitical tensions and increasing geo-economic fragmentation.

While inflation has fallen somewhat as global central banks have raised interest rates, hopes of a soft landing are fading. Labor markets remain tight, price pressures high and inflation sticky, forcing central banks around the world to keep rates up. It will be difficult to keep growth steady in the face of the side effects from these high rates, including banking weakness, potential turmoil and earnings pressures.

As a soft landing becomes less likely, the overall economic outlook has skewed to the downside. Nevertheless, there are individual positive stories in countries like the Dominican Republic, Armenia, Greece and others, and in regions such as Sub-Saharan Africa.

The following are regional observations from the Emerging Markets Debt team:

### **Macro**

The expectation of de-globalization and geo-economic fragmentation set a bearish tone for the meeting, despite the data not showing this trend playing out yet.

Central banks around the globe will likely continue to keep rates higher for longer on concerns that inflation is becoming more entrenched.

While there is a clear tightening of credit demand in the U.S., the consensus was the overall impact is uncertain as volatility in the U.S. financial sector continues.

The meeting revealed a hardening stance against China from U.S. foreign policy officials, reflecting a concerted foreign policy choice by the U.S. to counter China even if that approach requires increased ideological flexibility.

Africa may see some benefits from this shift, as the U.S. is increasingly allocating resources to Africa in order to counterbalance China.

### **Asia**

The participants expressed little interest about the economic situation in China, which came as a surprise. The consensus was that ending the country's "zero covid" policy would be positive in the short term, but that over the longer term the lack of economic reforms and demographic problems would create downward pressures.

While many were concerned about how China would interact with indebted countries under the Common Framework — a multilateral mechanism for restructuring sovereign debt in a way that ensures fair burden sharing — this issue wasn't explicitly addressed.

China faced political questions leading up to the Party Congress last year, but these are now settled, and the country is exiting its political cycle just as the U.S. is entering its 2024 election cycle.

The view on Pakistan's ailing economy improved after the meetings, as the country has started to implement slightly better policies. They still need to make these policies part of a more coherent plan, however.

### **G10**

In the U.S., Fed hikes are starting to seep into the economy, but they're doing so at a slow rate — the real economy remains quite hot.

Talk around the U.S. debt ceiling revealed a higher level of distress than in past years of debt-ceiling brinksmanship, as the political dynamics this year seem different, with more political volatility. Speaker McCarthy has relatively little power in the House compared to past speakers, which could lead to more political volatility. The government is expected to run out of cash over the summer, though there is still some uncertainty as to the exact timing of any potential default.

The narrative among central banks is that bringing inflation down close to target will be easy, but bringing it all the way back to target will be tough. Some central banks are placing the blame on corporate pricing behavior, which is said to be fueling inflation.

In Europe, smaller countries like Greece, Portugal and Cyprus are doing relatively well. Greece saw an upgrade to its fiscal outcome for this year along with a revision for last year. That sets them up for investment grade later this year, with an election in May.

Italy is likely to face growing fiscal pressures over coming quarters. Issuance is set to pick up given large deficits and quantitative tightening. The rating agencies are looking to EU recovery fund implementation as key to productivity growth.

## **Eastern Europe**

While Eastern Europe saw no downward revisions for medium term inflation, just up, several countries including Poland, Czech Republic and Hungary, saw growth revised downward. This is likely a reflection of the hiking cycle.

Armenia stands out with a big upward growth revision. A survey on how long Russians who migrated to Armenia plan to stay in the country revealed that most newly arrived Russians are highly educated IT workers, and about half indicated they intend to stay for at least one year. The IMF viewed this as encouraging for growth and combined with the macro policies of the authorities, the organization increased its confidence in the country.

Ukraine is the first country at war to receive an IMF program. While the program did not include preconditions on restructuring, significant reforms will clearly be needed. Conference participants emphasized that Ukraine's outlook and the terms of any restructuring will be crucially dependent on how the war evolves and, importantly, on the conditions of future support from the EU, U.S. and other partners. In that regard, the interest free loans from the EU and the grants from the U.S. are conducive for an investor-friendly restructuring in that they do not add to the gross financing needs of the country in the next few years.

## **Middle East and North Africa (MENA)**

Delays in the sale of state-owned assets in Egypt are leading to a negative outlook among investors. The country signed an IMF Extended Fund Facility program in January, which requires difficult reforms including floating the currency and selling state assets. These reforms haven't yet been implemented but some will need to happen before the first review in June.

In Turkey, polls suggest that the opposition may be in a position to win the May 14 presidential election and possibly Parliament as well, but the election race is very close. The IMF cut its growth projections due to the earthquake despite better-than-expected activity.

## **Sub-Saharan Africa (SSA)**

Growth expectations in the SSA region remain robust for 2023 and 2024, with many countries expected to see a pickup in growth driven by private consumption and investment. This growth is being driven by non-resource intensive countries like Kenya, Ivory Coast and Uganda. Agriculture is also picking up.

Many countries are looking at IMF programs as they seek to move away from commercial lenders and to other forms of financing, including the World Bank and other multilaterals.

In South Africa, the central bank is quite hawkish and serious about inflation. Quantified load shedding is expected to negatively affect growth by 2% of GDP.

In Zambia, the IMF team came out with a very positive staff-level agreement before the meetings, but the IMF wants to see decisions between Zambia and the official creditor committee before they make the disbursement. China co-chairs this creditor committee, and the mission chief was quite constructive on China.

## **Latin America**

In many of our meetings, we heard that reform agendas would be delayed until after key rounds of 2024 elections. Rising crime was another important theme for some Latin American countries. In Chile, crime is the top voter issue. In Ecuador, violence in proving difficult to stem and uproot — all in the midst of an impeachment trial against President Lasso. Both countries — and others in Central America — have an appreciation for the successful steps El Salvador took to combat gang-related crime. Removing gangs from the streets has become a key engine for growth in the economy.

Nearshoring was another big theme, as companies bringing production networks, closer to their domestic markets could be beneficial for long run growth. This is already happening in Northern Mexico, and other Central American countries are also hoping to position themselves to capitalize on this global trend.

The Dominican Republic is the current "darling" of the region. With an overall positive macro story, the country could be ready for a rate cut soon, its inflation rate is coming down and its economy is experiencing continuous upward growth. Its fiscal health looks good, though the country will eventually need a tax reform.

**Bottom line:** The global economy faces an increasingly likely prospect of a hard landing as inflation proves stickier than expected, forcing central banks to keep rates higher for longer. Meanwhile, the continuing trend of de-globalization is manifesting as regional economic fragmentation, creating new policy challenges. Nevertheless, there are pockets of good news in individual countries and regions, suggesting

a market that may reward an investing approach that is active, nimble and selective.

**Risk Considerations:** *The value of investments may increase or decrease in response to economic and financial events (whether real or perceived) in the U.S. and global markets. Investments in foreign instruments or currencies can involve greater risk and volatility than U.S. investments because of adverse market, economic, political, regulatory, geopolitical, currency exchange rates or other conditions. In emerging or frontier countries, these risks may be more significant. Investments in debt instruments may be affected by changes in the creditworthiness of the issuer and are subject to the risk of non-payment of principal and interest. The value of income securities also may decline because of real or perceived concerns about the issuer's ability to make principal and interest payments. Exposure to derivatives involves risks different from, or possibly greater than, the risks associated with investing directly in securities and other investments. As interest rates rise, the value of certain income investments is likely to decline. The value of commodities investments will generally be affected by overall market movements and factors specific to a particular industry or commodity, including weather, embargoes, tariffs, or health, political, international and regulatory developments.*



Emerging Markets Debt

"The narrative among central banks is that bringing inflation down close to target will be easy, but bringing it all the way back to target will be tough."



## Marketing Communication

To report a website vulnerability, please go to [Responsible Disclosure](#).

Eaton Vance is part of Morgan Stanley Investment Management, the asset management division of Morgan Stanley.

This website is operated by MSIM Fund Management (Ireland) Limited (MSIM FMIL). The business of Eaton Vance Global Advisors Limited was transferred to MSIM FMIL on 1 October 2021. MSIM Fund Management (Ireland) Limited has been appointed as management company of the Eaton Vance International (Ireland) Funds plc and is responsible for the distribution of the funds together with the distribution of Eaton Vance strategies and strategies of Eaton Vance affiliates. For any queries in respect of the products and strategies referred to on this website, please contact MSIM FMIL at 7-11 Sir John Rogerson's Quay, Dublin 2, D02 VC42, Ireland. MSIM FMIL is regulated by the Central Bank of Ireland with Company Number: 616661.

The value of your investment can go up or down so you may get back less than your initial investment. Past performance is not a guide to future returns.

The information on this webpage is not intended for U.S. residents. To visit our U.S. website [please click here](#).

Eaton Vance Management (Registration No. 1121368) and Parametric Portfolio Associates (Registration No. 1217626) are the registered trade marks of Eaton Vance.