

Investment Outlook – December 2017

One of our prominent global macro themes for 2018 is emerging market political risk. Over the next 12 months, approximately half of the Bloomberg Barclays Emerging Markets Index will hold important elections.

Here is a list of some of the potential impactful, upcoming elections (in chronological order): South Africa, Russia, Colombia, Indonesia, Mexico, Malaysia, Brazil, Thailand. Brazil and Mexico for example, two of the largest weights in the index, face general elections where the current leader is not standing for re-election. New regimes and the uncertainty they bring have the potential to introduce wild swings in volatility in local markets.

2017 has been quite an event-filled year in emerging markets.

2017 EM Hot Spots

Biggest news-generating countries



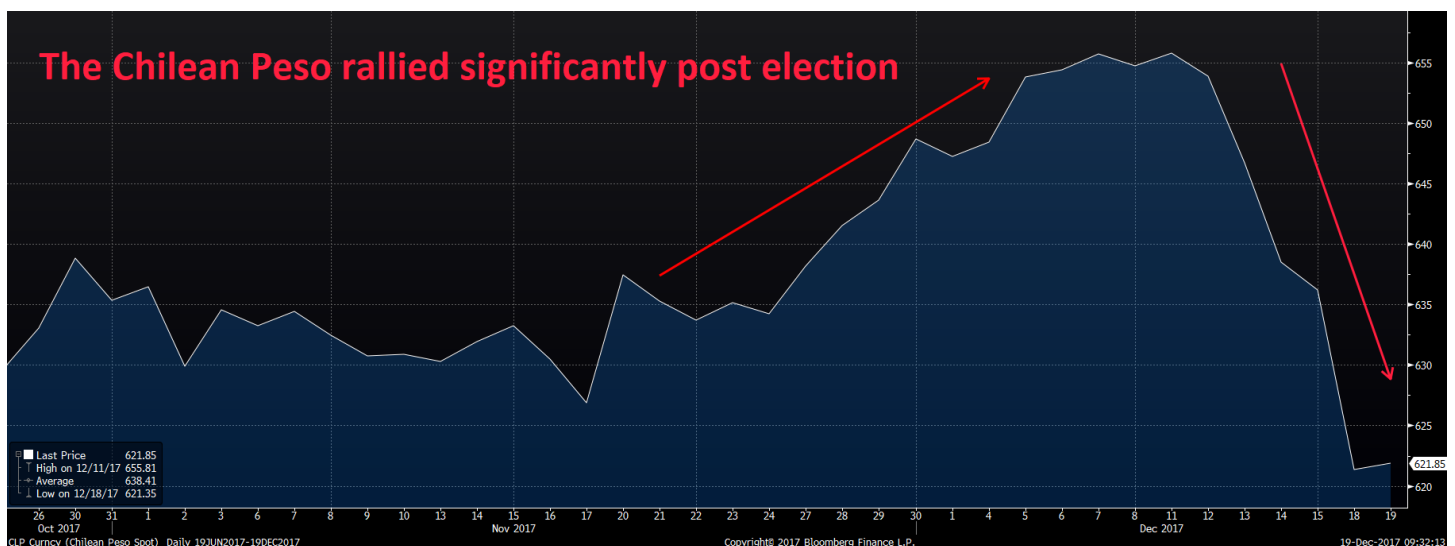
Source: Bloomberg

Bloomberg

Not every forthcoming election, however, is unpredictable. Outcomes in countries like Malaysia and Russia are relatively certain. An additional term for current regimes such as President Putin’s in Russia may embolden them to force through their agendas. It’s the close contests in large index constituents like Brazil and Mexico that require greater focus by investors. These events may potentially introduce larger periods of volatility into the markets.

Analysis has shown that elections in emerging market countries have been a significant catalyst for subsequent “issues”. Argentinian elections in 2001 were followed by the country’s default. President Lula da Silva’s 2002 victory (after 3 failed attempts) in Brazil caused bond yields to spike to 28%. Financial crises in Mexico in the ’70s, ’80s and ’90s were also preceded by elections.

Not all elections have negative consequences. In late November, the first round of Chile’s presidential elections sparked a selloff in the Chilean peso after center-right leader Sebastian Pinera’s lead shrunk. Since then, Chilean assets soared in the wake of Sebastian Pinera's election as president, with the country's currency rallying significantly. The benchmark stock index hit a record high.



Source: Bloomberg

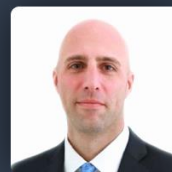
Not every political uncertainty is election related. One of Latin America's shining stars, Peru, faces a corruption scandal with their market-friendly President Pedro Pablo Kuczynski. He now faces impeachment.



Source: Reuters

Conclusion: Investors should be prepared for the impact elections and political uncertainty can cause to emerging market assets. Historical analysis has shown that political outcomes may introduce significant bouts of volatility with material movements in local markets and currencies.

At OceanSquare, our global strategies seek to navigate through these periods of volatility by undertaking extensive research and due diligence on a country by country basis. With our tactical, benchmark-agnostic approach to investing, we may potentially avoid large benchmark constituents facing political uncertainty and position ourselves in opportunities with bullish outlooks.



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