



# EM Capital Flows Monitor

MONETARY AND CAPITAL MARKETS DEPARTMENT

October 1, 2018

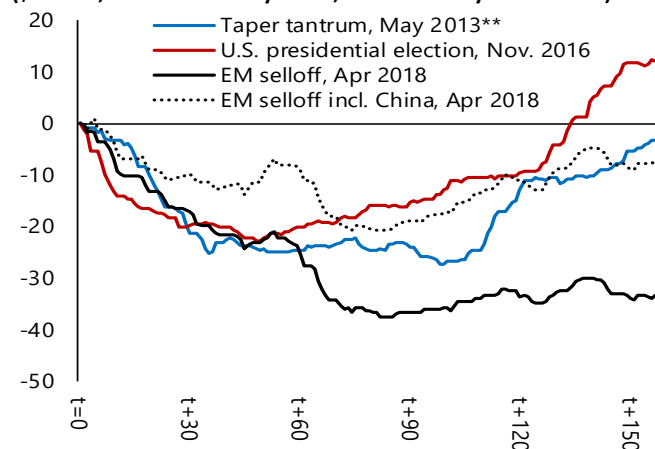
## Highlights:

- **Capital flows to EMs have remained under pressure in recent months.** The reversal of equity and bond flows was most acute and broad-based from April to June, followed by some stabilization in July/August and some renewed outflows in early September (Charts 1 to 6). Outflow pressures are evident in both cross-border flows data (from the IIF) and fund flows data (from EPFR). While outflows from investment funds – mostly used by retail investors – led the charge, they were less pronounced than in previous episodes of reversals. Buy-side contacts see risks of additional outflows if retail investors were to shift out of EMs more decisively, for instance, if US rates were to rise.
- **Portfolio flows to China have remained strong in recent quarters,** likely driven by [China's inclusion in the MSCI EM index](#), which led investors to allocate additional funds to China since MSCI's decision in June 2017 (Chart 7). Contacts note that China's inclusion may also have diverted funds away from other EMs. On September 25, 2018, MSCI [announced](#) that it may raise the weight of Chinese stocks in its indices starting next year, which is likely to support inflows in the coming months.<sup>1</sup>
- **Foreign direct investment to EMs ex. China weakened to 1.7% of GDP in Q2 from an average of 2.1% in the four preceding quarters (Chart 8).** Outward direct investment from EMs also declined markedly in Q2, potentially pointing to caution by businesses to expand internationally amid trade tensions (Chart 9).

## EMs ex. China suffered a period of portfolio outflows starting in April, but flows have stabilized recently

Chart 1. EM Portfolio Equity and Debt Flows\*

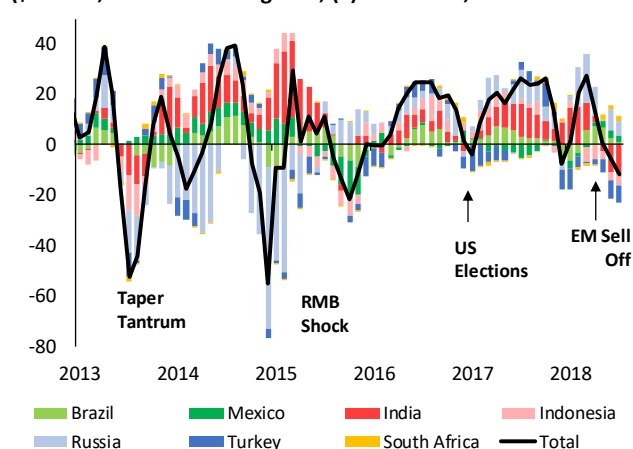
(\$ billion, cumulative daily flows, t=1 is first day of outflows)



## A number of EMs have intervened to support their currencies in recent months

Chart 2. Major EMs ex. China: Estimated Change in Reserves

(\$ billion; 3 months rolling sum, (+) = increase, last obs = Jul 2018)



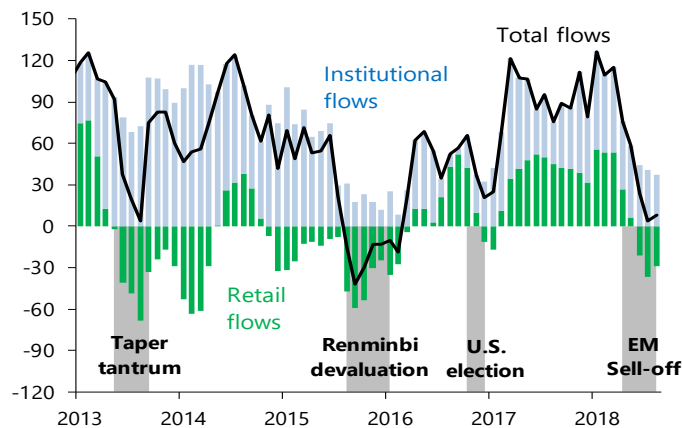
Source: IIF, IMF staff calculations

\*Countries include: India, Indonesia, Thailand, South Africa and Hungary (for debt flows); India, Indonesia, Korea, Thailand, South Africa, Brazil, Philippines, Vietnam, Taiwan, China (for equity flows) \*\*Outflows for the taper tantrum would appear relatively larger if shown as a share of EM GDP or portfolio liabilities. Source: IIF, IMF staff calculations

<sup>1</sup> Note that IIF daily and monthly flow aggregates were changed to include China since our last Monitor, reflected in charts 1, 3, and 6.

**Retail flows have reversed and inflows from institutional investors have slowed sharply**

**Chart 3. Estimates of Retail and Institutional Portfolio Flows (\$ billion, 3-month rolling sum; last obs: Aug 2018; includes China)**



Source: EPFR, IIF, IMF staff calculations

**Outflow pressures were most intense in April, May and June, followed by some stabilization**

**Chart 5. Non Resident Portfolio Flows to EMs: Percentile Rank\* relative to their Own History (since 2010; totals exclude China)**

	Q1 18	Apr	May	Jun	Jul	Aug	Sep
<b>Total</b>	47%	9%	2%	8%	76%	26%	20%
<b>All Equity</b>	29%	16%	6%	7%	53%	48%	33%
<b>All Debt</b>	62%	9%	3%	14%	82%	15%	19%
<b>Countries</b>							
China	89%	88%	86%	100%	93%	73%	43%
India	41%	5%	2%	11%	33%	35%	7%
Indonesia	21%	6%	8%	13%	46%	43%	18%
Korea	82%	47%	67%	79%	39%	61%	32%
Malaysia	44%	21%	7%	16%	61%		
Philippines	31%	33%	30%	18%	46%	40%	24%
Thailand	38%	7%	8%	10%	27%	71%	56%
Brazil	44%	78%	3%	9%	97%	46%	36%
Chile	36%	18%	47%	12%			
Mexico	15%	61%	46%	14%	49%	1%	41%
Bulgaria	61%	1%	87%	94%			
Hungary	61%	61%	53%	1%			
Poland	42%	12%	16%	6%			
Turkey	35%	13%	18%	24%	28%	30%	29%
Ukraine	61%	50%	35%	38%			
South Africa	94%	59%	0%	6%	29%	7%	16%

\*The percentile rank shows how strong recent flows have been relative to the flows observed since Jan 2010. For example, a percentile rank of 70 indicates that recent flows exceed 70% of all observations since Jan 2010.

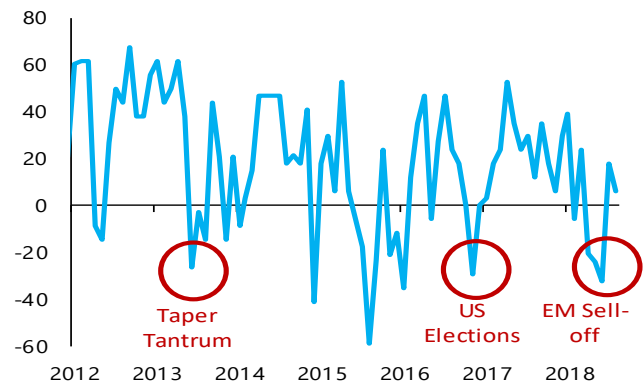
Legend (%)	80-100	60-80	40-60	20-40	0-20
------------	--------	-------	-------	-------	------

Source: IIF, IMF staff calculations

Note: An extended heatmap is provided on page 4.

**Recent outflows seem to have been broad-based across countries**

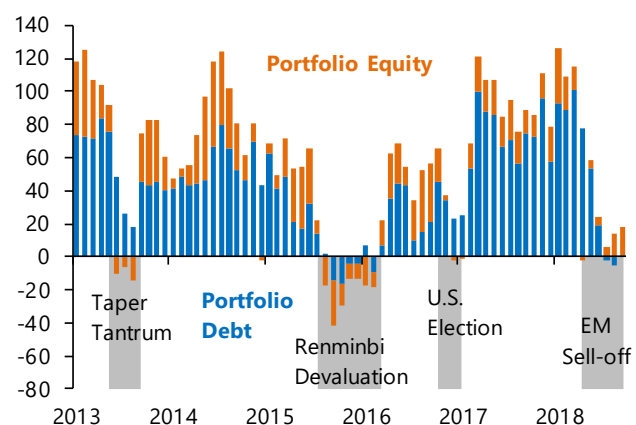
**Chart 4. Percentage of Monthly EM Portfolio Flows Series with Positive/Negative Observations (Example: -100% means all 18 EM monthly flows series show net outflows)**



Source: IIF, IMF staff calculations. The 34 time series include data include 17 equity flows series and 17 debt flows series for a total of 18 countries.

**The recent slowdown was most pronounced in bond flows and occurred after strong inflows in 2017**

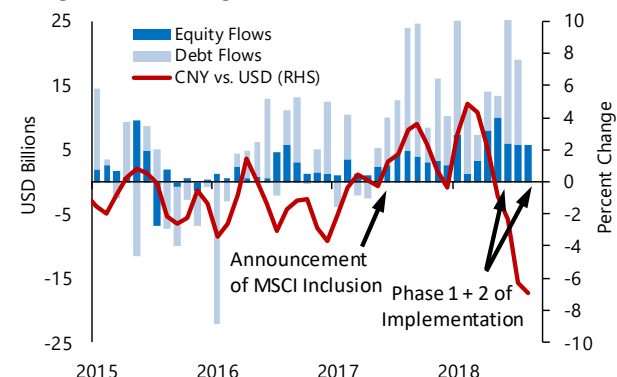
**Chart 6. Non-Resident Portfolio Flows to EMs (incl. China) (\$ billion, 3-month rolling sum; last observation: September 2018)**



Source: IIF, IMF staff calculations

**China has received strong portfolio inflows thanks to its inclusion in the MSCI EM, and despite RMB depreciation**

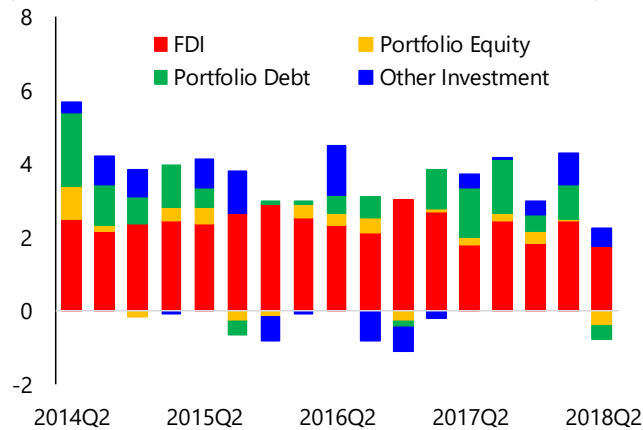
**Chart 7. China: Non-resident portfolio flows vs. 3-month percent change in the exchange rate**



Source: Bloomberg, IIF, IMF staff calculations

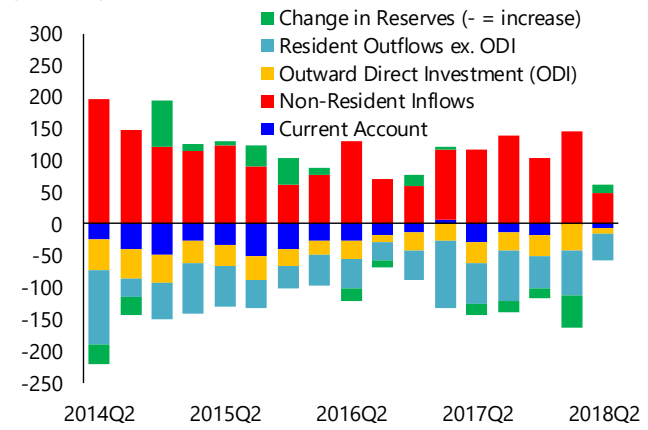
**FDI inflows declined to 1.7% of GDP in Q2, while other investment inflows remained robust**

**Chart 8. EM ex China: Non-Resident Capital Inflows**  
(% of GDP, "other investment" includes bank-related flows)



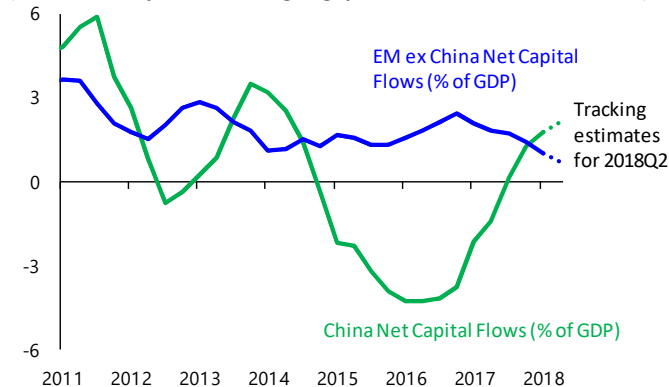
**EM ex. China: reduced inflows are reflected in sharply lower outward investment by EM residents**

**Chart 9. Breakdown of Major Balance of Payments Components**  
(\$ billion)



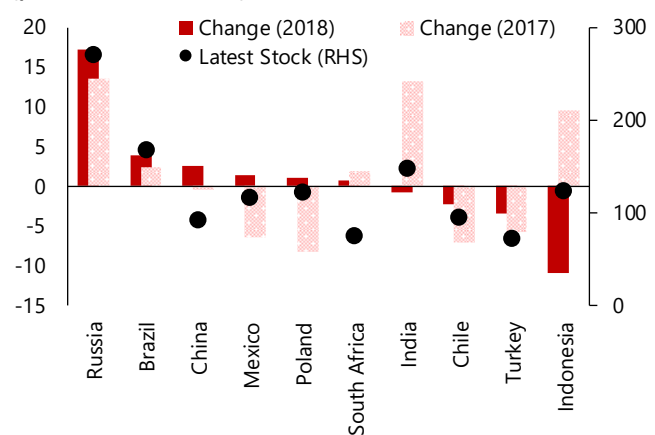
**Net capital flows to EMs ex. China are estimated to have slowed further in Q2**

**Chart 10. Net Capital Flows to Emerging Markets**  
(% of GDP, 4-quarter moving avg, positive number = net inflows)



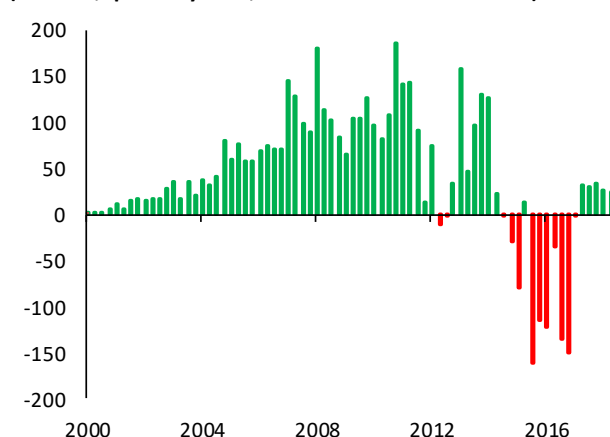
**Countries with lower reserve coverage have tended to intervene more this year**

**Chart 11. Major EMs: Reserves**  
(percent of ARA metric)



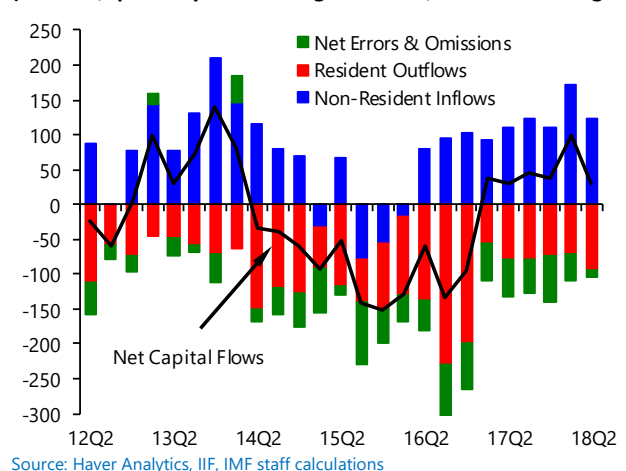
**China continued to rebuild reserves in Q2...**

**Chart 12. China: Change in Reserves**  
(\$ billion, quarterly data; last observation is 2018 Q2)



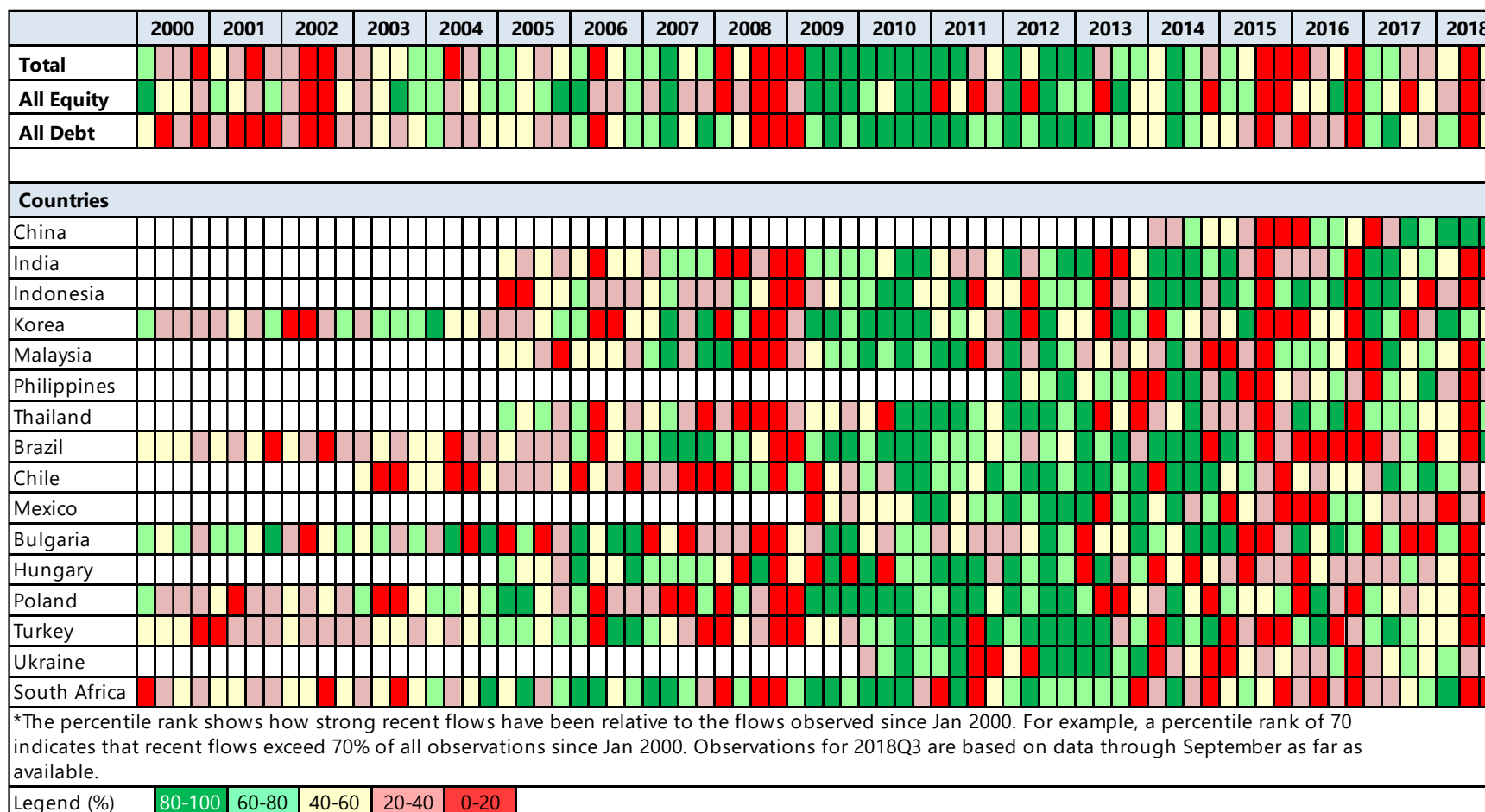
**...while net capital flows to China slowed**

**Chart 13. China: Capital Flows**  
(\$ billion, quarterly data through 2018 Q1; net flows through Q2)



*Portfolio flows to emerging markets in perspective: crisis in 2008-09, surge in 2010-14, retrenchment in 2015-16; a challenging 2018*

Chart 14. Non Resident Portfolio Flows to EMs: Percentile Rank\* relative to their Own History (since 2000; totals exclude China)

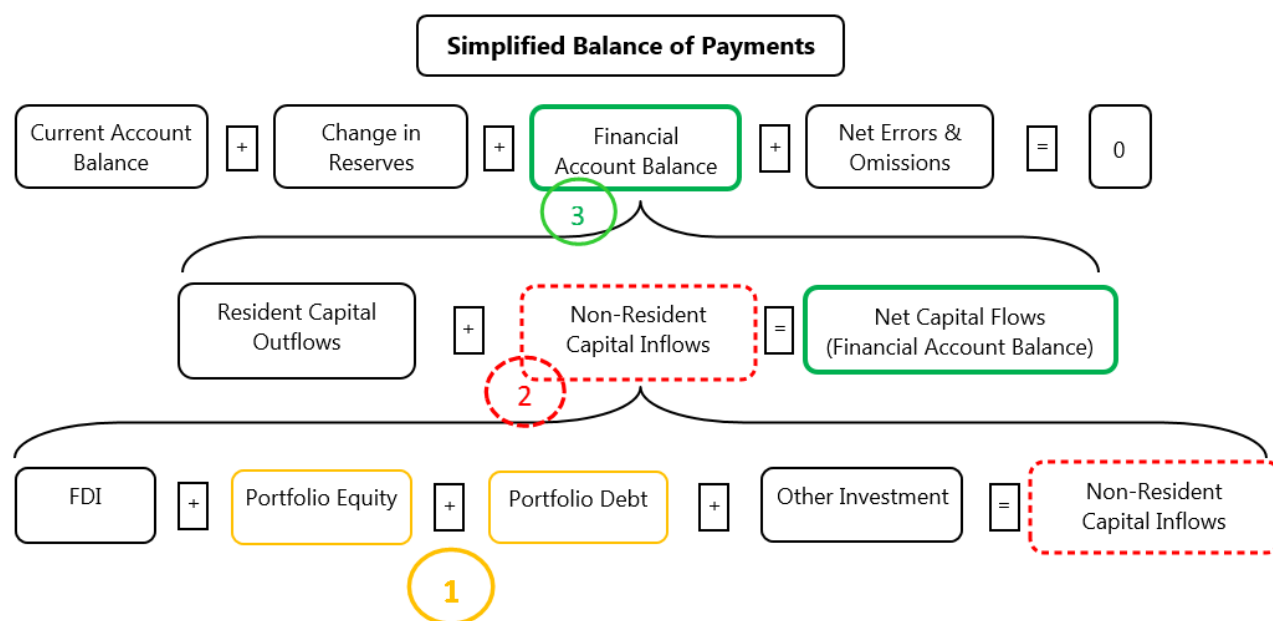


Source: IIF, IMF staff calculations

## Tracking Framework for the EM Capital Flows Monitor

The monitor discusses trends in capital flows as measured in the balance of payments (BoP). A simplified BoP breakdown is provided in the figure below. Consistent with this illustration, flows are discussed in the following order:

- First, we look at **non-resident portfolio flows**. This is only one (small) component of the financial account, but it is generally the most volatile component and the one that matters most for asset prices fluctuations. Moreover, available data sources on portfolio flows are timelier and more comprehensive than for other capital flows components.
- Second, we show estimates of **total non-resident capital flows**. Aside from portfolio flows, this encompasses FDI and “other” investment (which includes bank lending and deposits, among others). We also provide estimates of EM resident outward investments.
- Third, we provide an estimate of **net capital flows** (i.e. the financial account balance) and look at reserve dynamics. Net capital flows can be estimated in a timely manner using available data for the other BoP components, including the trade balance and the valuation-adjusted change in the stock of reserves, among others.



Note: For ease of illustration, the sign conventions used in this figure correspond to BPM5.