



KEY HIGHLIGHTS

Portfolio flows to emerging markets have been volatile in recent months, and on balance, they are negative so far in Q3. Monthly flow estimates in fact show July to be one of the weakest months (Chart 3). Overall, there is considerable country variation, with Mexico and South Africa having prolonged local currency debt outflows (Chart 1). South Africa also has significant equity outflows (Chart 2). Equity flows to China remain notably stronger than the flows to the rest of EMs, mirroring the trend in the local currency debt flows ([link](#)). This highlights China's relative resilience to the COVID shock, and its faster growth. Continued concerns about the domestic fundamentals of other emerging markets continue to weigh on equity and local currency debt flows. Overall, Mexico, Poland and South Africa portfolio flows have been consistently less than their historical 40th percentile (Chart 3). Longer term analysis shows that volatility has risen across all capital flow components since Q1 2020 except for other investment flows (Chart 22)

Breakdown of portfolio flows: Local currency debt flows remain weak driven by mutual funds, while ETFs have seen a sharp pick-up – primarily due to flows to China-related funds (Chart 4). Hard currency bond fund flows have remained strong on net but have come under pressure in the last few weeks weighed down, in particular, by higher advanced economy rates (US 10yr yields are up 20 bps since end July). Hard currency ETFs have underperformed mutual funds, reflecting their higher sensitivity to external risk sentiment. The overall muted trend in 2021 is driven by a decline in both retail and institutional investors as compared to the strong rally in Q4 2020 (Chart 5). Active fund flows have also underperformed passive flows in last few months (Chart 21) reflecting concerns around the elevated market volatility.

Non-Resident Capital Flows: Quarterly balance-of-payments data as of Q2'21 suggest that non-resident flows have remained stable in the last few quarters, albeit with a changing composition (Chart 6). Portfolio flows, at 1.7% of GDP in Q2, have declined from the record high 2.3% in Q4'20. However, FDI flows (Chart 7) have picked up to 1.9% of GDP in Q2 (vs a historical low of 1.4% in Q4'20) along with a slight rise in other investment flows as well. Portfolio debt flows are at 77th percentile historically – reflecting the strong hard currency issuance in Q2 ([issuance monitor](#)). Equity flows and other investment flows are broadly in line with their historical average (Chart 8). Aggregating across categories, Chile, Peru and Malaysia have led total non-resident flows, while South Africa and Philippines have been the laggards (Chart 9). Remittance flows, on an average, have normalized now after the very strong post COVID recovery (Chart 17). Asian economies have seen a sharp decline in the growth in remittances (notably Bangladesh) while Latam economies continue to see a strong remittance growth driven by Colombia, Guatemala and Mexico (Chart 18).

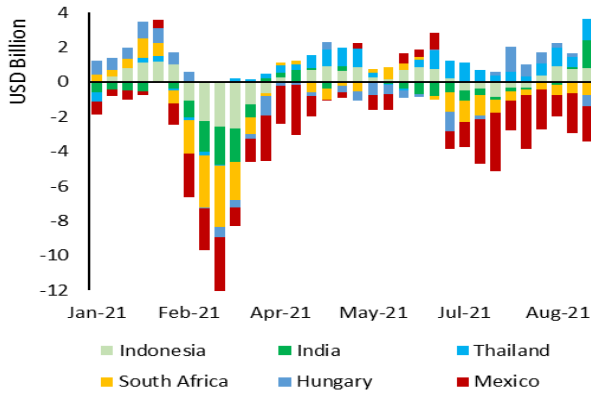
Resident Capital Flows: The retrenchment in resident outflows during the COVID sell-off which supported the balance of payments ([link](#)), has now dissipated. Net flows have become weaker (Charts 10 and 12) as resident outflows have accelerated in many EMs (Chart 13) reflecting potential domestic investor concerns around the currency outlook. Brazil, Colombia, Peru and Mexico are seeing historically highest resident outflows which is adding to pressures on the current account dynamics. On the other hand, Romania, Russia, Malaysia and Indonesia continue to benefit from a retrenchment in the resident outflows (Chart 14). The composition of resident flows differ significantly across countries as there are still pockets of retrenchment in resident portfolio and other investment flows (Chart 16). China has also seen a steady rise in the resident outflows (and errors and omissions), which is partially offset by the strong pick-up in the non-resident flows (Chart 11).

Other EM BoP Components: Accumulation of EM reserves has continued this year, driven in particular by the Asian economies (Chart 19). China, India, Poland and Indonesia are only economies to see a reserve accumulation in both 2020 and 2021 (Chart 20). The current account balances for EMs at 0.7% of GDP remained strong in Q2, (driven by Russia, Brazil and Malaysia) though less than the historically best quarters of 1.8% of GDP in Q3 and 0.8% of GDP in Q4 (Chart 12). This could reflect improving growth dynamics and a potential normalization of imports.

EM Portfolio Flows – Using High Frequency Indicators

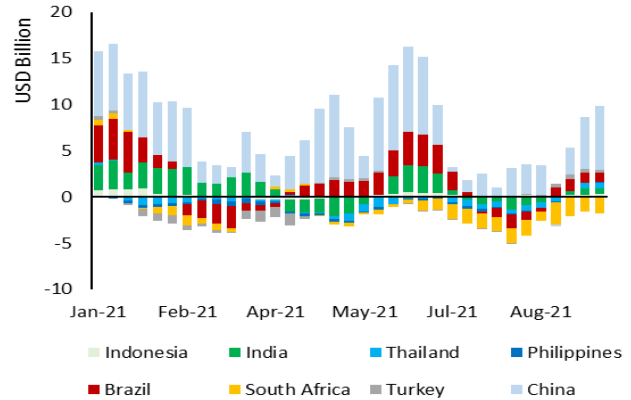
Local currency debt flows came under pressure again in the last few months, after a stabilization in May/June. Mexico is the most notable underperformer

Chart 1. Weekly Debt Flows to Major EMs ex China (USD Billions)



Equity flows have improved in the last few weeks after the sell-off in July and early Aug. Equity flows to China have outperformed EMs like the debt flows

Chart 2. Weekly Equity Flows to Major EMs (USD Billions)



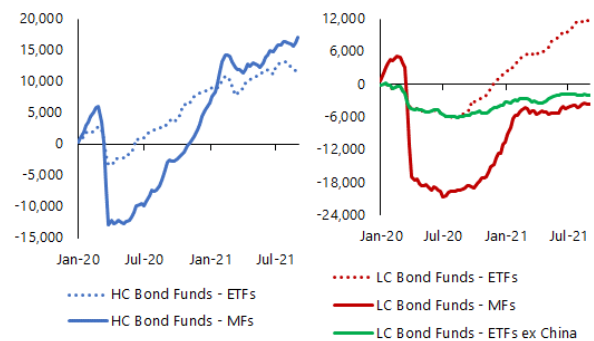
Flows have remained weak through 2021 with a very weak July following a robust June. Mexico, South Africa and Poland have seen flows consistently in the bottom 40%

Chart 3. Non-Resident Portfolio Flows to EMs: Percentile Rank* Relative to Their Own History (since 2010; totals are ex China)

	Q1 21	Apr	May	Jun	Jul	Aug
Total ex CHN	15%	15%	38%	56%	19%	45%
Equity ex CHN	43%	18%	40%	68%	10%	51%
Debt ex CHN	11%	15%	37%	45%	30%	35%
Countries						
China	97%	76%	51%	75%	30%	65%
India	57%	10%	37%	45%	12%	71%
Indonesia	20%	47%	41%	76%	20%	68%
Malaysia	85%	73%	47%	37%	23%	
Philippines	0%	18%	21%	38%	26%	49%
Russia	3%	3%	55%	69%	90%	30%
Thailand	26%	62%	14%	64%	35%	75%
Brazil	54%	50%	78%	78%	63%	59%
Chile	78%	96%	94%			
Mexico	9%	40%	9%	23%	4%	2%
Colombia	4%	95%	88%	68%	20%	79%
Bulgaria	58%	82%	88%			
Hungary	57%	62%	25%	4%	100%	41%
Poland	16%	11%	10%			
Turkey	26%	31%	47%	40%	45%	53%
Ukraine	63%	12%	53%	79%	23%	6%
South Africa	17%	31%	60%	6%	9%	4%
*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 exceeded 70% of all observations since Jan 2010.						
Legend (%)	80-100	60-80	40-60	20-40	0-20	

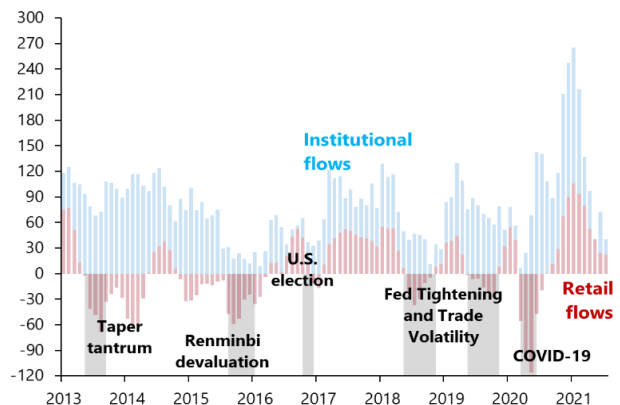
Local currency bond fund flows remain weak driven by the mutual funds and ETFs (ex China) while hard currency funds have been relatively strong

Chart 4. Hard Currency vs Local Currency Bond Fund Flows (USD Billions; Cumulative since 2020 beginning)



The decline in the last six months was driven by both retail and institutional investors

Chart 5. Estimates of Retail and Institutional Portfolio Flows (USD Billions, 3-month rolling sum; incl China)



Non-Resident Capital Flows – based on Balance of Payment Releases

Non-resident flows have remained stable in the last few quarters. Debt flows have been strong in 2021, while equity flows have remained weak

FDI flows have recovered in 2021 with very few countries in the worst quartile anymore

Chart 6. EMs ex China: Non-Resident Capital Inflows (% of GDP, “other investment” includes bank-related flows)

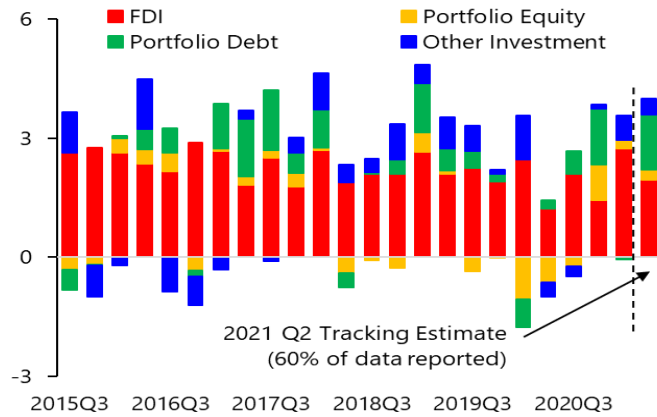
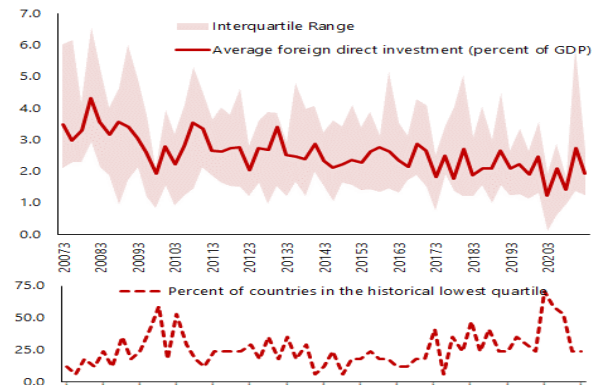


Chart 7: FDI Flows: Average for EMs ex China, and the proportion of countries in sharp reversals



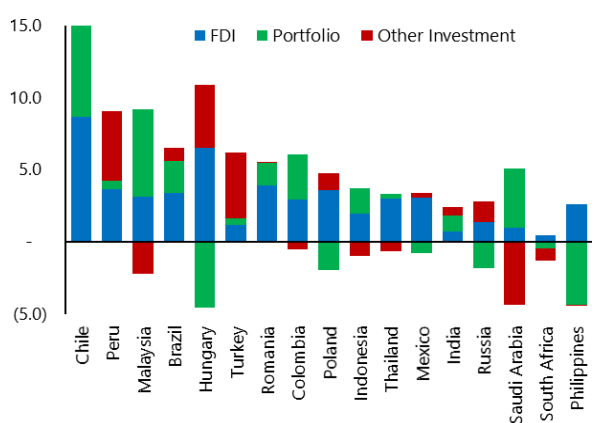
FDI flows on an aggregate are at just 11th percentile, while portfolio debt at 77th percentile. Equity and other investment flows are around average

Chile, Peru and Malaysia have led total non-resident flows, while South Africa and PHP have lagged

Chart 8. Major EMs ex. China: Key Parameters of the Non-Resident Flows (Percent)

Non Resident Flows	EMs ex China average (% of GDP)	Percentile Rank	% of countries in their historical lowest quartile	% of countries in their historical highest quartile
Portfolio Equity	Q3	-0.2	19	60
	Q4	0.9	86	44
	Q1	0.2	51	56
	Q2	0.3	56	22
Portfolio Debt	Q3	0.6	40	20
	Q4	1.4	79	11
	Q1	-0.1	11	89
	Q2	1.4	77	33
FDI	Q3	2.1	19	59
	Q4	1.4	2	53
	Q1	2.7	65	24
	Q2	1.9	11	24
Other Investment	Q3	-0.3	18	35
	Q4	0.1	26	35
	Q1	0.6	49	29
	Q2	0.4	40	18

Chart 9: EMs ex China: Composition of the Non-Resident Flow (Percent of GDP; 2021 flows)



Overall, the net capital flows have diverged significantly between China and EMs ex China

The strong rise in resident outflows in China, is partially offset by the continued ramp-up in non-resident flows

Chart 10. Net Capital Flows (USD Billions; Monthly)

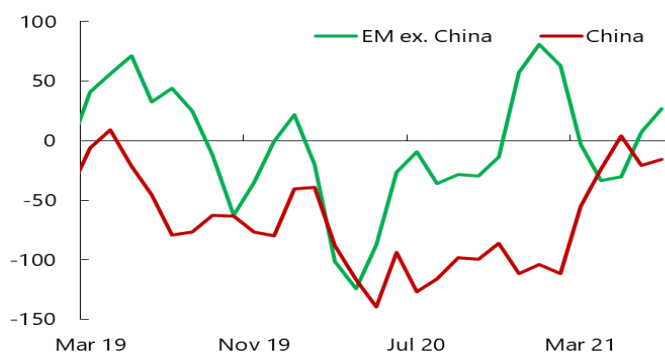
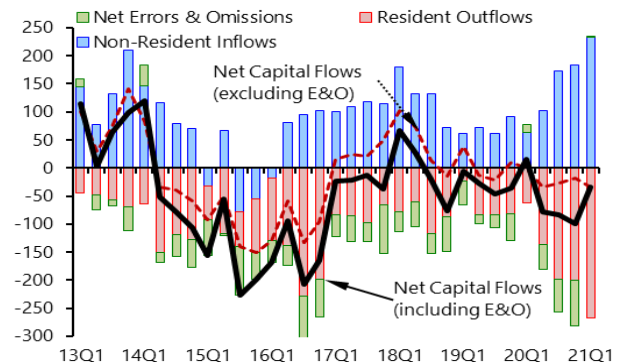


Chart 11. China: Capital Flows (USD Billions)



Resident Capital Flows – based on Balance of Payment Releases

Current account and non-resident flows are helping BoP; The drag from reserve accumulation and resident outflows has increased recently

Resident outflows have resumed now, normalizing from the decline during the COVID-19 sell-off

Chart 12: EMs ex China: Major Balance of Payments Components (Percent of GDP)

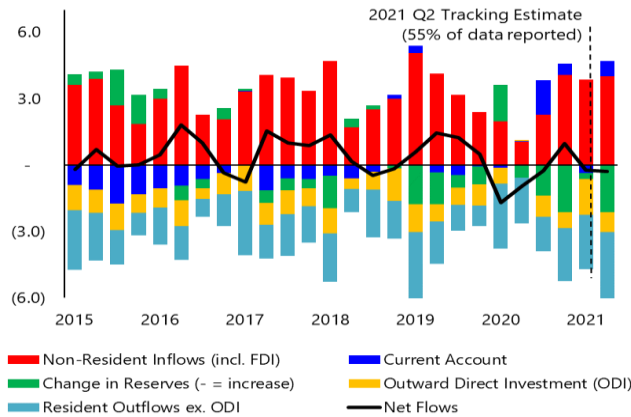
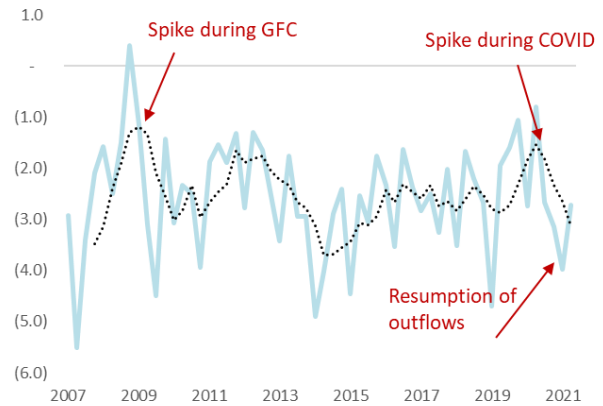


Chart 13: EMs ex China: Total Resident Flows (Percent of GDP; EM Median and 4q moving average)



Brazil, Colombia, Peru and Mexico are seeing historically highest resident outflows; while Romania, Russia, Malaysia and Indonesia are seeing less outflows

Chart 14. Total Resident Flows to EMs: Percentile Rank Relative to Their Own History (since 2007; Percent)

	Brazil	Chile	Colombia	Mexico	Peru	Saudi Arabia	India	Indonesia	Malaysia	Philippines	Thailand	Hungary	Poland	Romania	Russia	Turkey	South Africa
2019 Q1	47%	68%	98%	54%	21%	13%	18%	21%	63%	63%	48%	27%	44%	7%	25%	2%	2%
2019 Q2	65%	70%	58%	58%	91%	16%	46%	61%	70%	23%	64%	70%	77%	68%	61%	56%	50%
2019 Q3	56%	61%	91%	67%	98%	0%	68%	63%	47%	13%	89%	84%	46%	82%	95%	19%	98%
2019 Q4	75%	67%	75%	70%	44%	41%	34%	86%	60%	82%	39%	80%	82%	16%	81%	68%	84%
2020 Q1	77%	7%	46%	32%	53%	5%	36%	49%	65%	25%	61%	45%	14%	19%	68%	47%	46%
2020 Q2	100%	28%	30%	47%	89%	9%	7%	81%	84%	18%	96%	95%	93%	86%	51%	100%	96%
2020 Q3	58%	100%	53%	16%	39%	95%	43%	75%	44%	7%	80%	41%	37%	0%	89%	9%	38%
2020 Q4	4%	91%	0%	28%	51%	46%	64%	16%	53%	43%	43%	77%	32%	63%	79%	44%	13%
2021 Q1	28%	12%	100%	56%	56%	39%	21%	60%	56%	29%	23%	20%	12%	25%	32%	5%	14%
2020 Q2	0%	82%	16%	37%	2%			67%	61%				42%	95%	74%	46%	

Very strong Resident Outflows (Red) Less Strong Resident Outflows (Green)

Composition of resident flows differ significantly across the countries – with other investment flows still retrenching in some cases

The correlation b/w resident and non-resident flows remain near historical highs – showing the potentially buffering role provided by residents during sell-offs

Chart 15: EMs ex China: Composition of the Resident Flows (Percent of GDP; in 2021)

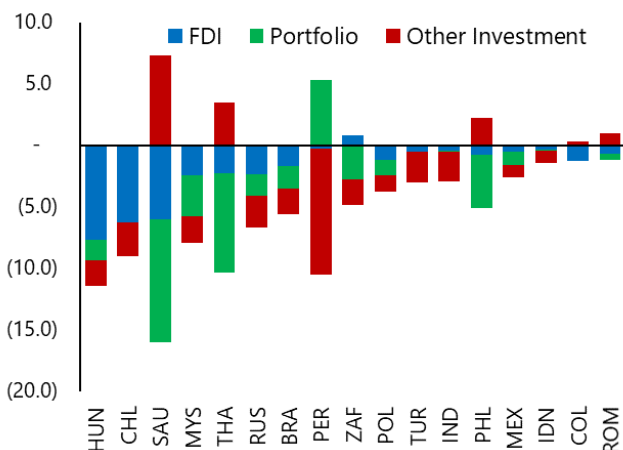
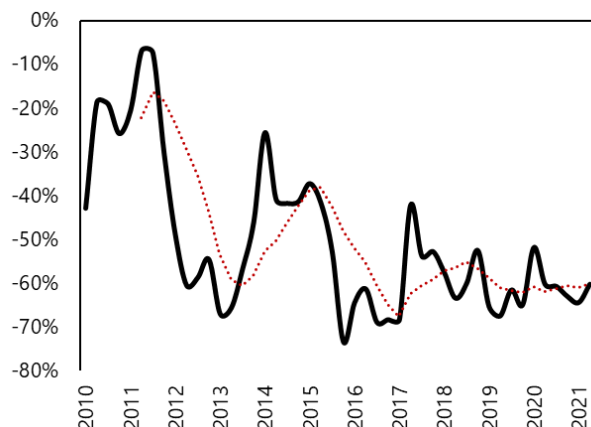


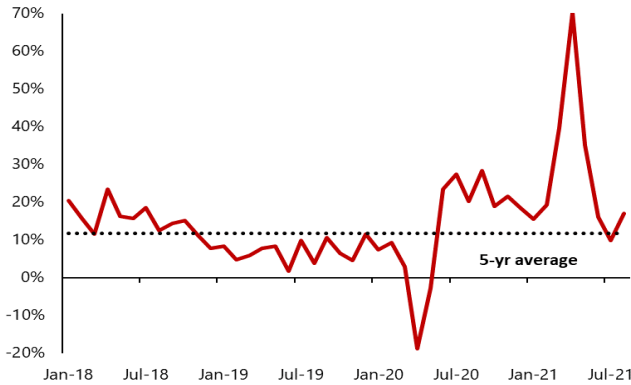
Chart 16: Correlation between Resident and Non-Resident Flows (Percent; 12 quarter moving correlation)



Other Dimensions of EM Balance of Payments

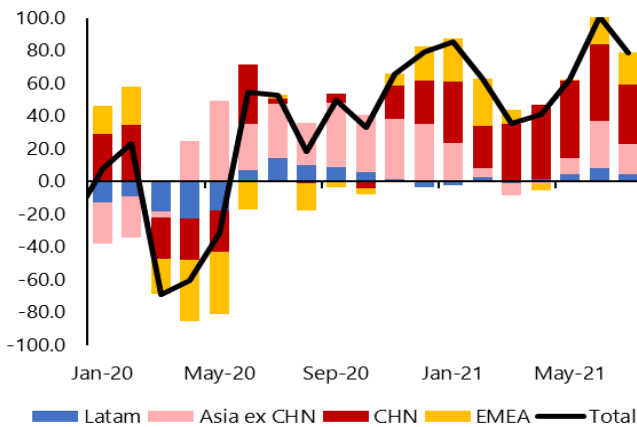
Remittance flows have normalized now after the very strong post COVID recovery

Chart 17. Remittance Flows to Select EMs
(YoY Growth; Percent; Equal Weighted Average)



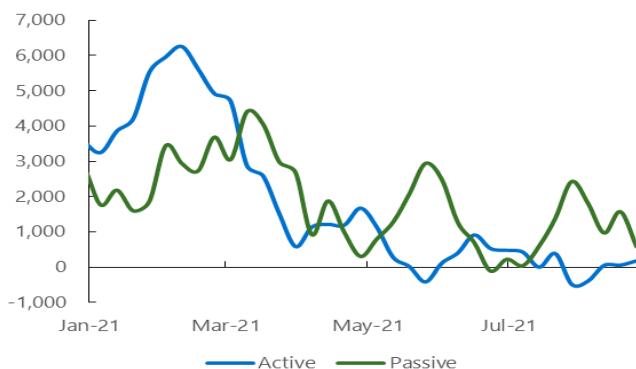
There is a strong accumulation of reserves in the last few months driven by Asian economies

Chart 19. EM Reserve Operations (USD Billions, three month moving sum)



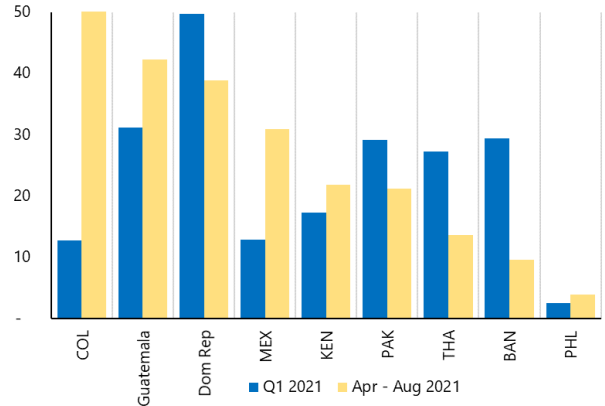
Active fund flows have especially underperformed the passive flows in the last few months

Chart 21. Active vs Passive EM Fund Flows (USD Billions; 4 week moving average)



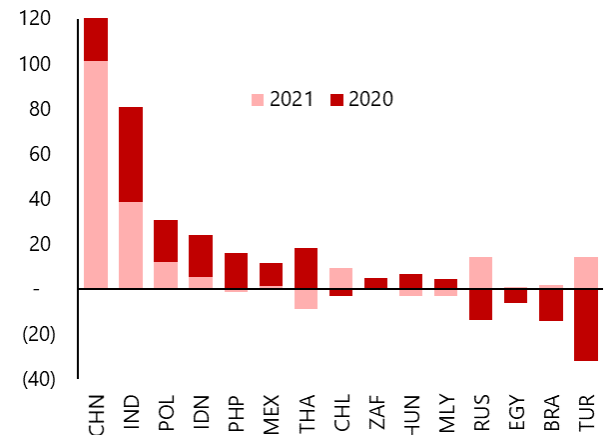
Asian economies have seen a sharp decline in the growth while Latam economies continue to see a strong remittance growth

Chart 18. Country level Remittance Flows to Select EMs (Percent; YoY Growth)



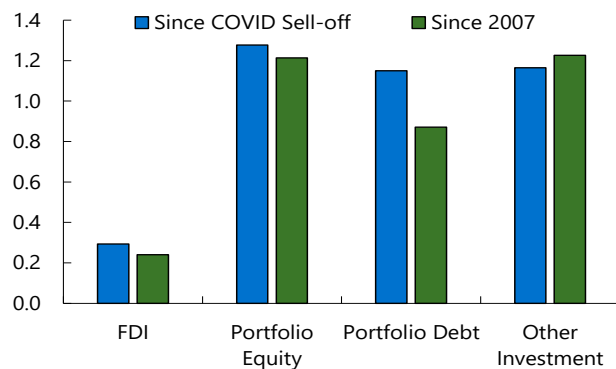
China, India, Poland and Indonesia are only economies to see a reserve accumulation in both 2020 and 2021

Chart 20. Country level EM Reserve Operations (USD Billions)



Capital flow volatility has risen since covid for all categories, except the other investment flows

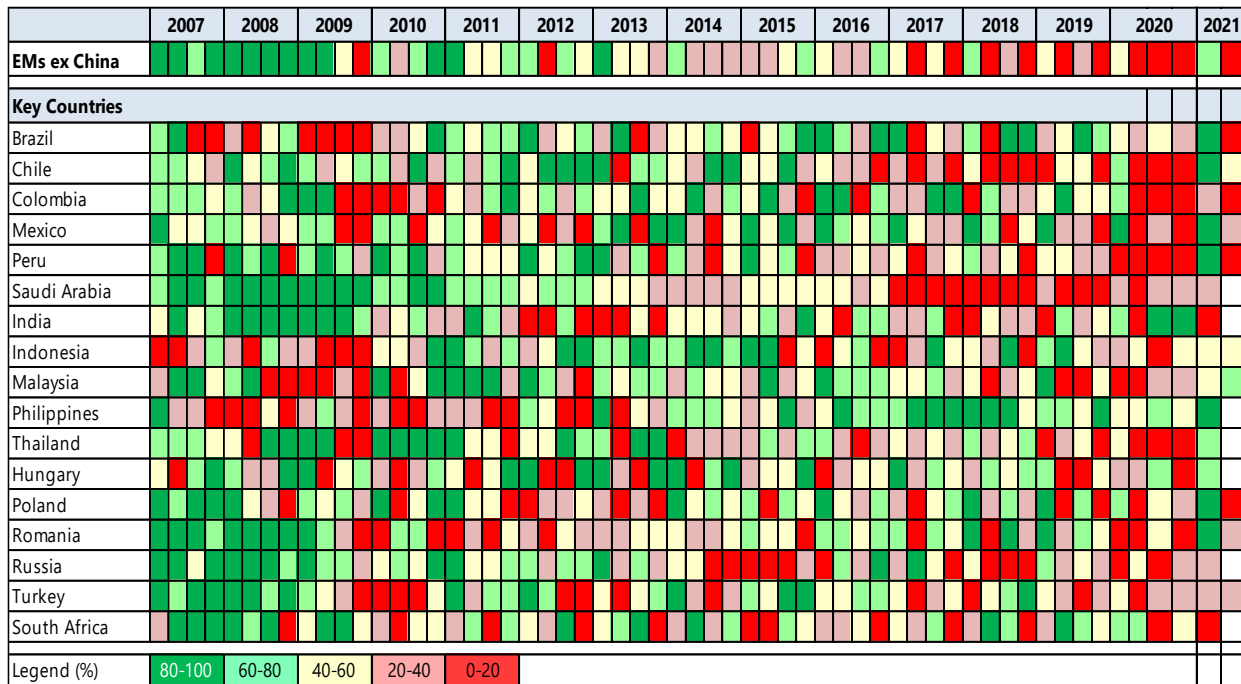
Chart 22. Capital Flow Volatility (Coefficient of Variation, Percent)



Appendix: Long Term Heat Maps on Non-Resident Capital Flows

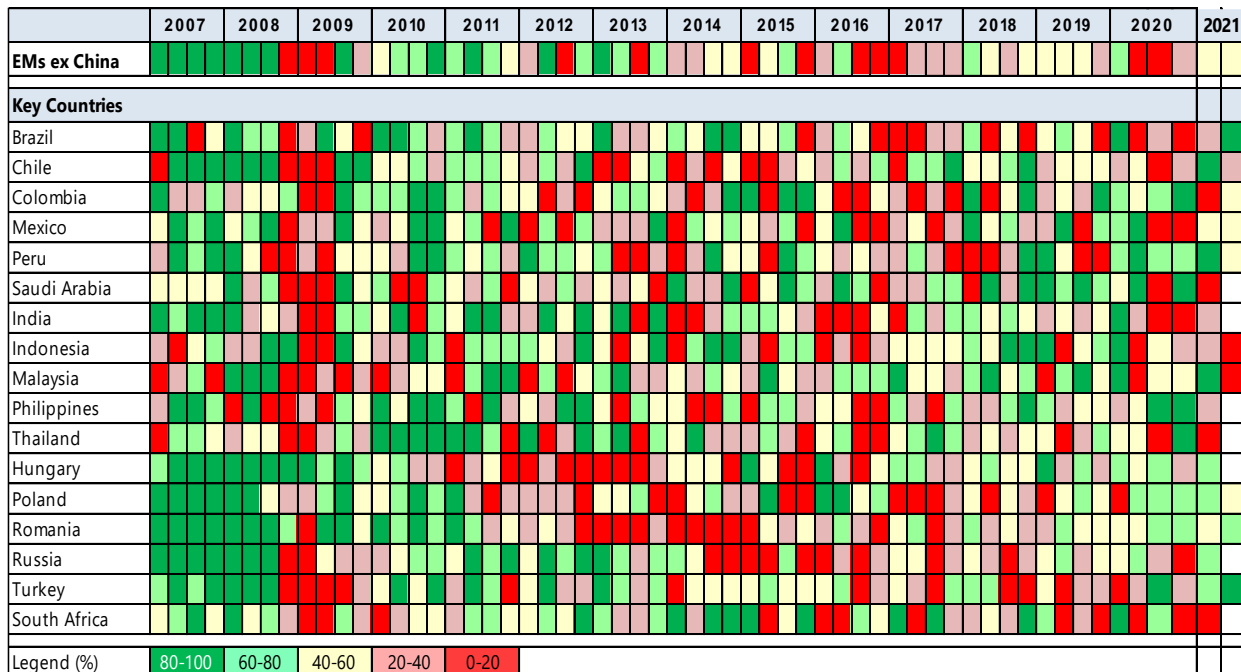
FDI flows to EMs ex China continue to remain weak (despite the recovery in 2021 Q1). Country level trend vary

Chart 23. Non-Resident FDI Flows to EMs: Percentile Rank relative to their Own History (since 2007)



Other Investment Flows have improved recently after the sharp drawdown in 2020

Chart 24. Non-Resident Other Investment Flows to EMs: Percentile Rank relative to their Own History (since 2007)



Portfolio flows to EMs in perspective: crisis in 2008-09, surge in 2010-14, retrenchment in 2015-16; increased volatility in 2018-19; the sharp sell-off in 2020 with a late recovery; and a sell-off in 2021 again.

Chart 25. Non-Resident Portfolio Flows to EMs: Percentile Rank relative to their Own History (since 2007)

