No room for complacency

We sense the decisive battles around duration and the US dollar are yet to commence

News Analysis

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Global markets continue to experience very low volatility. Over the past week there was no decisive indication from the Fed minutes that a March rate hike was more likely than the 30% chance priced in by the market. There was also no material detail about the fiscal plans of the new US administration. As a result, markets remain becalmed, with a sense that the decisive battles around duration and the dollar are yet to commence.

We continue to like local interest rates particularly the short end of the Mexican bond market as well as in India and Turkey. Continued low volatility is likely to increase the carry attractiveness of these markets. In India, we believe the central bank will respond to recent lower-than-expected inflation prints. In Mexico, we still retain caution on the direction of sovereign creditworthiness, but acknowledge that recent currency strength has taken pressure off the central bank to increase interest rates further. Last week's announcement to provide forward currency hedges to the market should also promote short-term stability. We have also been more active in the Asian hard currency corporate new issuance market, particularly China, where liquidity trends remain strong.

In the other main EM stories we have had no material developments. The South African budget delivered a tax increase for high earners, but no resolution in the Jacob Zuma/Pravin Gordhan power struggle. We still sense Zuma is biding his time, but aims to weaken Gordhan's hold on the Finance Ministry. In Venezuela, the government has met immediate coupon obligations, providing some short-term relief to bond prices. Mongolia has also been a focus of investor attention this past week, with the authorities aiming to launch new sovereign issuance at yields above 8.75% to fund forthcoming quasi-sovereign obligations.

We expect more volatility in March. We still do not believe that a March rate hike is off the table. We continue to invest in idiosyncratic stories within the asset class and keep a tight grip on overall directional exposure. We do not share any complacency that today's low volatility environment may be engendering.