IIF RESEARCH NOTE

Capital Flows to Emerging Market Economies

January 30, 2014

- Emerging market conditions have continued to be quite choppy, including a significant market correction in early 2014. We do not anticipate a sustained pull-back from emerging markets, but investors have become increasingly sensitive to country risks, which will test countries that experience heightened political uncertainties or do not take timely and decisive measures to address policy weaknesses.
- As anticipated, the retrenchment of flows in the summer of 2013 proved temporary (and was less severe than previously estimated) as the global economy gained pace and markets absorbed the December decision on Fed tapering.
- As our baseline scenario, we continue to expect a gradual rebound in capital flows in 2014 and 2015, in line with a projected sustained pick-up in world growth and a gradual Fed exit (Chart 1). However, flows will remain at a much lower level relative to GDP than over 2010-2012 (Chart 2, next page).
- Downside risks for aggregate flows mainly relate to risks surrounding market expectations for the Fed's eventual policy rate hiking path. At the country-level, economies with large external financing requirements, macroeconomic policy gaps and political uncertainties remain most vulnerable. The recent market volatility has highlighted this risk.

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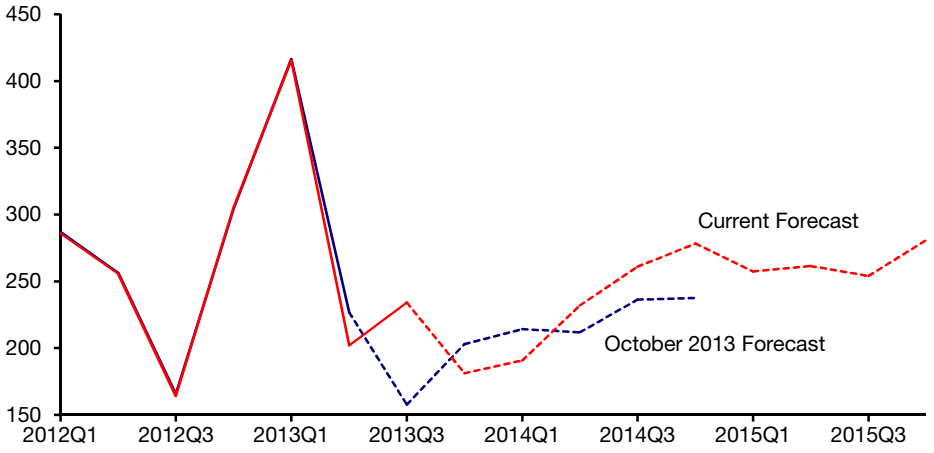
CHOPPY CONDITIONS IN EMERGING MARKETS, BUT GRADUAL REBOUND IN CAPITAL INFLOWS SHOULD CONTINUE

Emerging market conditions have continued to be quite choppy in recent months. Following the significant retrenchment over the summer of 2013 after Chairman Bernanke signaled the start of Fed tapering of asset purchases by end-year, markets

Chart 1
Total Capital Inflows to Emerging Markets
$ billion; net non-resident capital flows to the 30 EM economies covered by the IIF



Source: IIF, IMF, National Sources.

Table of Contents

Global Overview 2
Flows by Region 19
Annexes and Tables 28

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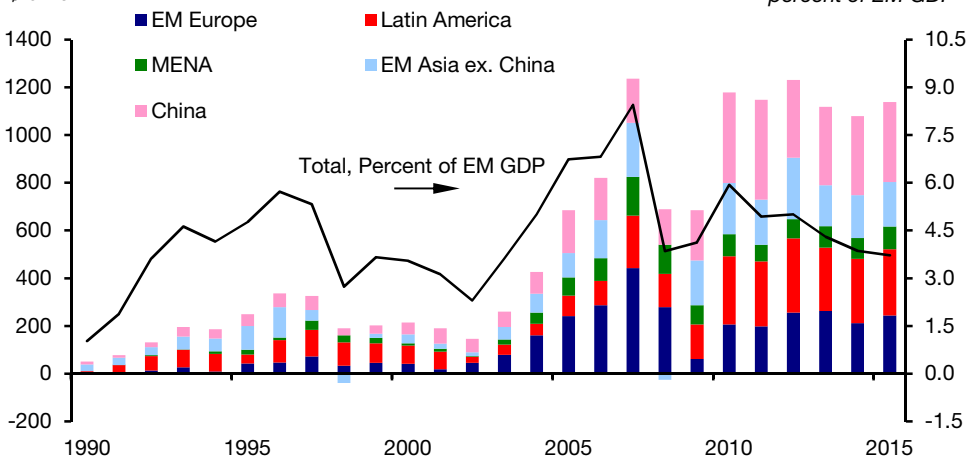
Chart 2
Emerging Market Private Capital Inflows, Net
$ billion *percent of EM GDP*



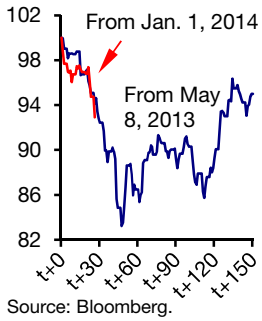
Source: IIF, National Sources.

stabilized in the fall as the global economy gathered momentum and as investors were convinced that the start of Fed tapering did not imply a quick move to raise policy interest rates. The Fed's announcement in mid-December of its decision to start tapering from January 2014 was absorbed without major difficulties. However, market conditions have taken a turn for the worse in early 2014, as investors became more risk-averse, in response to a rising sense that advanced economy central banks were adopting a more hawkish tone and to some less positive economic news (particularly from China) and increasing concerns about political developments in a number of countries with large external financing needs and relatively fragile policy frameworks, including Argentina, Turkey and Ukraine.

MARKET CONDITIONS HAVE TAKEN A TURN FOR THE WORSE IN EARLY 2014, AS INVESTORS BECAME MORE RISK-AVERSE

To date, this recent correction is significantly smaller than occurred in the summer of 2013 (Chart 3; see Box 3, page 8), but provides a healthy reminder that as liquidity becomes less abundant in the global financial system, investors will become more risk-sensitive and alert to weaknesses in policy frameworks particularly where amplified by political uncertainties.

Chart 3
EM Equities
index, rebased t=100



Source: Bloomberg.

Notwithstanding recent market volatility, we continue to project that capital inflows to emerging markets will have bottomed out in late 2013/early 2014 and will rise gradually in 2014 and 2015, consistent with our Capital Flows Report in October 2013. An important factor behind this assessment is that, based on recent data, capital inflows in the second half of 2013 tracked quite well with our projections. Indeed, flows were a little stronger than anticipated as the retrenchment of flows in the summer proved temporary and less severe than expected, especially in debt flows, as institutional investors continued purchases even as retail investors continued to sell.

Going forward, we envisage overall flows to increase gradually this year and rise further in 2015, helped by a stabilization of the EM growth outlook and assuming that the Fed's

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Table 1
Emerging Market Economies: Capital Flows
$ billion

	2012	2013e	2014f	2015f
Capital Inflows				
Total Inflows, Net:	*1268*	*1146*	*1133*	*1176*
Private Inflows, Net	**1231**	**1119**	**1079**	**1138**
Equity Investment, Net	670	639	664	696
Direct Investment, Net	546	554	560	585
Portfolio Investment, Net	124	84	104	112
Private Creditors, Net	561	480	415	442
Commercial Banks, Net	118	135	135	154
Nonbanks, Net	443	345	280	288
Official Inflows, Net	37	27	53	38
International Financial Institutions	2	-3	12	17
Bilateral Creditors	34	31	41	21
Capital Outflows				
Total Outflows, Net	*-1296*	*-1374*	*-1360*	*-1354*
Private Outflows, Net	-947	-972	-1054	-1049
Equity Investment Abroad, Net	-324	-393	-379	-394
Resident Lending/Other, Net	-623	-579	-675	-655
Reserves (- = Increase)	-349	-402	-306	-305
Memo:				
Net Errors and Omissions	*-249*	*-4*	*0*	*0*
Current Account Balance	*277*	*232*	*227*	*178*

scaling back of monetary stimulus goes broadly as currently priced in by markets (with a first hike in the policy rate around mid-2015). Equity flows are projected to benefit in particular under this environment, while debt inflows may be less buoyant.

On an annual basis, our forecast is for non-resident private inflows into EMs to decline to $1,079 billion in 2014 from $1,119 in 2013 (Table 1). Both figures are around $50-60 billion higher than projected in our October report, mainly reflecting upward revisions for Asia (see Box 1, next page). While we expect a recovery in quarterly terms starting in 2014Q1, the projected rise of flows during 2014 will only be gradual, leaving annual inflows below the 2013 level. However, with flows continuing to rise in quarterly terms, we envisage that 2015 will see the first increase in nominal flows since 2012, with overall private inflows reaching $1,138 billion. This level is close to the historical highs reached in 2007 in nominal terms. However, as a share of GDP flows have fallen since 2010 and are projected to stabilize only in 2015 at a much lower level (Chart 2, previous page).

WE EXPECT A RECOVERY IN QUARTERLY TERMS STARTING IN 2014Q1

Notwithstanding the constructive baseline view for aggregate flows, uncertainty remains high and dispersion across countries remains wide. Downside risks relate particularly to countries facing external financing challenges with questionable policy frameworks, especially in countries facing political uncertainty. Recent developments in Argentina, Turkey and Ukraine exemplify these concerns.

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BOX 1: REVISIONS TO IIF FORECASTS

Since our October 2013 report we have made net upward revisions to our capital flows projections. On a quarterly basis, EM capital inflows turned out stronger in 2013Q3, but appear to have slowed in 2013Q4. We project flows to pick up gradually in coming quarters before stabilizing in 2015. The new quarterly trajectory implies considerable upward revisions to our annual capital flows projections for 2013 and 2014 (Table 2). On a regional basis, EM Asia accounts for the biggest share of the revisions, followed by EM Europe. Shorter term capital flows (e.g. portfolio investment and bank lending) were generally revised up, while 2013 FDI flows turned out weaker than projected.

Table 2
Revisions to IIF Private Capital Inflow Projections
$ billion

	2012	2013e	2014f	2015f
IIF Private Capital Inflows				
January 2014 Forecast	1,231	1,119	1,079	1,138
October 2013 Forecast	1,215	1,062	1,029	
Revision	16	57	50	
Revisions by Region				
Latin America	3	-3	-10	
Emerging Europe	9	12	20	
Africa/Middle East	7	6	3	
Emerging Asia	-3	41	38	
Revisions by Component				
Direct Equity Investment	10	-20	31	
Portfolio Equity	0	33	11	
Commercial Banks	13	8	-5	
Nonbanks	-7	35	13	

e=IIF estimate, f=IIF forecast

THE SUMMER RETRENCHMENT WAS LESS BAD THAN THOUGHT

Based on a broad set of data, flows to EMs in the second half of 2013 took less of a hit than is widely thought, primarily due to greater resilience of portfolio flows to EMs in the summer of 2013. Specifically, we estimate that actual portfolio equity and debt inflows in 2013 were around $70 billion higher compared to our October assessment (see Box 2, page 6).

FLOWS TO EMS IN 2013H2 TOOK LESS OF A HIT THAN IS WIDELY THOUGHT

Much of the discussion during 2013 was focused on available data on inflows to EM-dedicated funds from Emerging Portfolio Fund Research (EPFR). Those showed large

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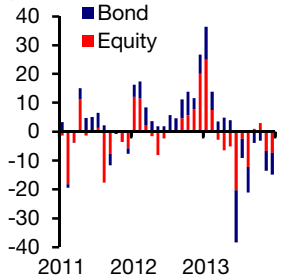
outflows in the summer (with June 2013 marking the largest decline in portfolio inflows on record) and continued net outflows during the remainder of the year and into 2014 (Chart 4). By contrast, a broader range of data that have become available since then, most importantly monthly balance of payments data in a number of key EMs, indicate that inflows – especially into debt instruments – developed much more favorably than indicated by the fund flows. We estimate that from May to October 2013, emerging markets received net portfolio equity inflows of $10 billion and net portfolio debt inflows of $71 billion, rather than net outflows of $36 billion and $37 billion, as suggested by EPFR[1]. Other financial market data support this more positive view. Foreign ownership of domestic EM government bonds held up relatively well at high levels (Chart 5). Moreover, EM external bond issuance rose to a record level in 2013, with solid issuance continuing in H2 after a brief mid-summer lull (Chart 6), and EM dollar Eurobond issuance has surged in January 2014, reaching twice the monthly average since 2008. For example, Indonesia sold a record $4 billion sovereign bond, Romania issued a debut 30yr bond ($2 billion) and Mexico, Philippines and Poland raised between $1.5 billion to $4 billion each. Even Turkey was able to issue a $2.5 billion 10yr bond, despite recent market tensions.

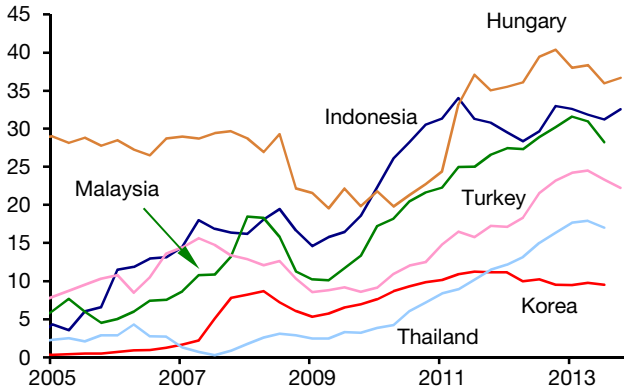
Chart 4
EM Funds: Debt and Equity Net Flows
$ billion



Source: EPFR.

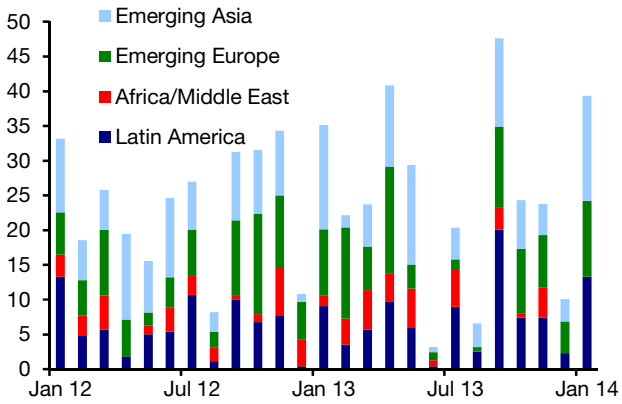
The divergence between fund and aggregate inflows to EMs partly reflects the dynamics of the EM investor base. Retail investors are heavily represented in the volatile inflows into EM-dedicated funds that are reported by EPFR. Institutional investors, however, such as pension funds in mature economies or sovereign wealth funds in EMs, appear to have maintained their exposure to EMs, responding to strategic mandates to gradually raise their underweight allocations to EMs in overall portfolios, and presumably are behind sustained strong demand for EM new bond issues.

Chart 5
Foreign Holdings of Government Debt
percent of total government debt securities



Source: ADB, National Sources.

Chart 6
Emerging Market External Bond Issuance*
$ billion



Source: Thomson Financial; IIF calculations. * Includes bonds issued in an external market, for the 30 major EM countries covered in the IIF's Capital Flows to EM report.

1. This estimate is based on 12 EM economies that publish monthly portfolio equity flows and 11 EM economies that publish debt flows data.

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BOX 2: REVERSAL REVISITED - TRACKING PORTFOLIO FLOWS DURING THE SUMMER OF 2013

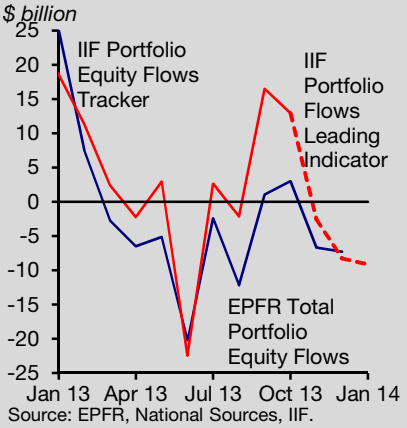
During the summer months of 2013, emerging market asset prices depreciated sharply, a development that seems to have been prompted primarily by a shift in market expectations towards an earlier Fed exit. The sharp adjustment in prices seemed to coincide with a sharp reversal in non-resident capital flows. Data on monthly flows to EM dedicated funds as published by EPFR show a sharp retrenchment from June to August 2013, followed by continued weakness through the end of the year (Chart 4, previous page).

While this apparent reversal in portfolio flows has received substantial public attention, more recent data releases on country-level balance of payments statistics show a much less adverse trajectory in portfolio flows over the summer.

In order to obtain a more accurate estimate of the overall trajectory of portfolio flows over the past year, we have developed a monthly measure of portfolio flows based on data from 12 EMs that report monthly BoP data on a timely basis. Our monthly portfolio flows tracker follows total quarterly portfolio inflows into our IIF EM-30 economies very closely (the correlation coefficient is 0.91 for equity flows and 0.88 for debt flows over the last 10 quarters). According to the tracker, total portfolio equity flows to our group of 30 EM economies declined sharply in June, but held up quite well in subsequent months (Chart 7). Further, portfolio equity flows seem to have recovered during the fall, in contrast to data from EPFR that show a decline in November. A similar picture is painted by our estimates of portfolio debt flows, which appear to have reached a low-point in June 2013 (albeit in positive territory), followed by an increase in flows in the following months (Chart 8). The portfolio flows tracker has a relatively short lag of 2-3 months, which is a significant improvement over the 4-6 month lag for total quarterly EM BoP data from the IMF.

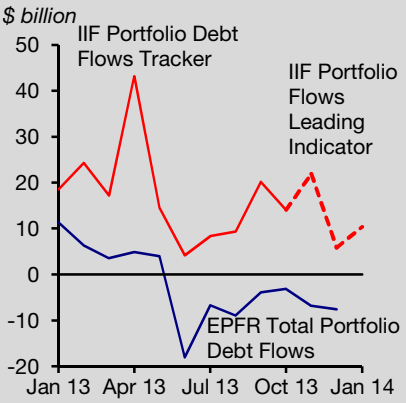
WE HAVE DEVELOPED A MONTHLY TRACKER OF PORTFOLIO FLOWS

Chart 7
Portfolio Equity Inflows to Emerging Markets



Source: EPFR, National Sources, IIF.

Chart 8
Portfolio Debt Inflows to Emerging Markets



Source: EPFR, National Sources, IIF.

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WE HAVE ALSO DEVELOPED A PORTFOLIO FLOWS LEADING INDICATOR

In addition, we have developed a portfolio flows leading indicator (PFLI) that provides real-time estimates of overall portfolio flows to emerging markets. The PFLI is available for the current month and the two prior months, covering the same group of countries as the above portfolio flows tracker. It is estimated mainly based on asset price movements, bond issuance trends, and lagged portfolio flows. According to our estimations as of late January 2014, portfolio equity flows declined by $9 billion this month and by a cumulative $20 billion since November 2013. By contrast, portfolio debt flows seem to have held up relatively well through January, posting net inflows of $10 billion this month and a cumulative $38 billion since November. This benign trajectory is consistent with a healthy pace of emerging market bond issuance in the last few months up to January.

The methodology behind our estimations is summarized briefly in Annex 1 on page 28. We aim to release a detailed methodology note in late February. If you are interested in our latest portfolio flows estimates, please send an email to rkoepke@iif.com.

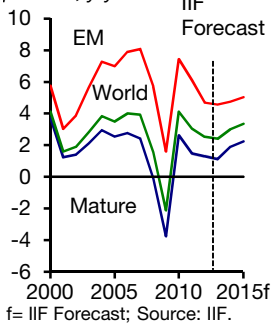
RECOVERY ON TRACK — WHAT WILL DRIVE CAPITAL FLOWS OVER THE NEXT YEARS?

Going forward, we are projecting a continued gradual increase in capital inflows, but with marked downside risks. Three factors are likely to shape the macro environment for EM inflows:

1. Better global growth helping equity flows

The evidence has mounted in recent months that global economic activity is picking up, in line with our forecast for world growth rising by around ½ percentage point to 3 percent in 2014 (see Global Economic Monitor December 2013, Chart 9). This growth acceleration is led by mature economies, notably the U.S. and the Euro Area. Stronger growth in mature economies also benefits EMs via stronger export demand – a development that has become more visible since we published our last Capital Flows Report in October. For China, we expect growth to continue around 7½ percent in 2014, as the authorities aim to gradually bring down credit growth in the economy, while sustaining overall growth in activity. Overall, notwithstanding the fact that a number of EMs are being affected by somewhat tighter external financial conditions since last summer, we expect EM growth to rise moderately to 4¾% in 2014 and to 5% in 2015.

Chart 9
Global Real GDP
percent, y/y



f= IIF Forecast; Source: IIF.

In this environment, capital flows benefit from the stabilization of growth in EMs as the relative growth advantage of emerging countries over mature economies remains high (though lower than it was for most of the past decade). In addition, stronger growth in mature economies also has collateral benefits for capital flows, for example as firms from mature markets increase vertical FDI flows into EMs in order to keep up with rising global and domestic demand. Equity inflows over the period 2014-15 are projected to

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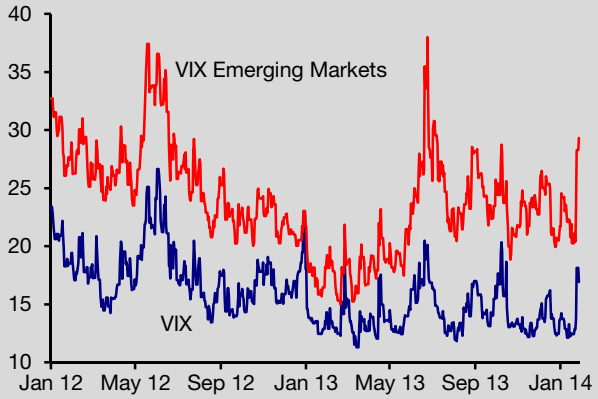
BOX 3: ANOTHER FAST-MOVING STORM: THE JANUARY 2014 EMERGING MARKET CORRECTION IN PERSPECTIVE

The striking thing about the early 2014 selloff in emerging market assets was how quickly it materialized, from seemingly blue skies—and how many factors played a role in making it happen. The January decline has to date followed a similar pattern to the selloff that began in May 2013 as Fed Chairman Bernanke put tapering on the table, although price declines would have to continue much further to match the hit that occurred in May-June 2013. Volatility has risen abruptly across asset classes, reaching its highest level for equities since July of last year (Chart 10). The selloff has hit emerging market bonds as well, particularly sovereign issues (EMBIG +40bp year-to-date, Chart 11).

January's correction came at a time when the risk rally was arguably overextended and vulnerable to correction. Despite the generally positive economic news in late 2013, anticipation of higher U.S. interest rates kept EM assets underperforming. January's positive economic surprise index reached its highest level since early 2012—pushing market expectations of the Fed funds rate at end-2015 higher (Chart 12, next page). Combined with perceptions of a rather more hawkish tone from some other central banks (notably the BoE, but also the RBNZ and the SNB via its macroprudential efforts to curb housing prices), this played into renewed concerns about a reduction in global liquidity—and unwinding of carry trades. Against this backdrop, a cluster of country-specific negatives (including weaker growth in China, political strains in Turkey, strikes in South Africa and devaluation in Argentina) hit at just the wrong time, triggering a sharp rise in risk aversion and pullback from emerging markets.

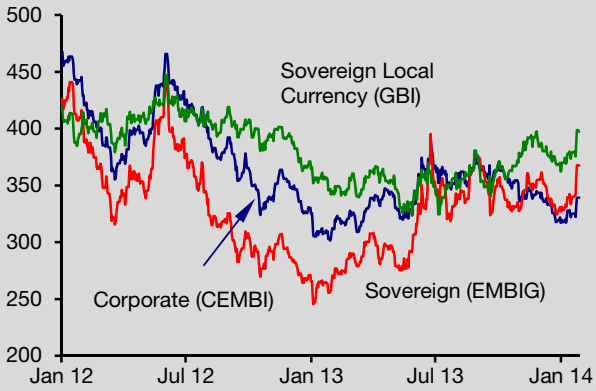
Calmer for now: Reactive policy responses (e.g. rate hikes in India, aggressive tightening in Turkey and hawkish language from Brazil) have helped stabilize EM currencies and markets, but concerns about underlying vulnerabilities are likely to persist. Investors are likely to remain concerned that shifts in view about the Fed's tightening path could trigger further rounds of pressure on emerging markets. The key question is how far such pressures would discriminate across countries. January's correction was fairly broad—correlation among price movements of key EM equity markets was near 0.65, slightly higher than the 0.6 seen in May-June 2013. However, over time, as the Fed moves closer to higher rates, investor discrimination is likely to become much more evident. Bracketing of emerging market countries on key vulnerability metrics –reliance on more-volatile portfolio capital, levels of external debt, twin deficits, credit growth, level of foreign ownership in domestic markets, domestic policy credibility— should thus be increasingly reflected in both market pricing and valuation.

Chart 10
VIX Index and Emerging Markets VIX Index
index



Source: Bloomberg.

Chart 11
EM Sovereign and Corporate Bond Spreads
bps



Source: Bloomberg.

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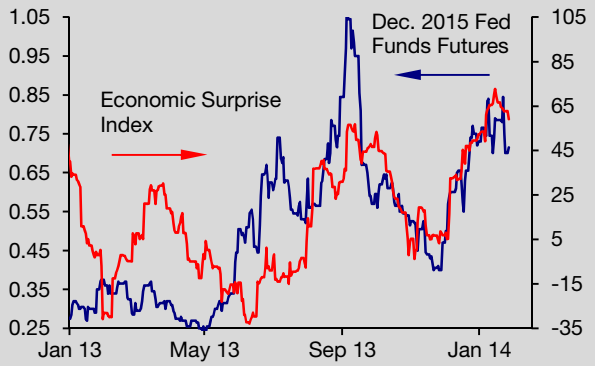
Not out of the woods—more investor discrimination seen: Overall EM equity market valuation has now fallen to very low levels (forward price-earnings ratio of about 9, below the long-run average near 11 and well below developed markets at 15, Chart 13). However, this masks a significant level of divergence among countries (e.g. Russia at 4.6, Mexico at 21). Is this divergence in line with perceptions of country risk?

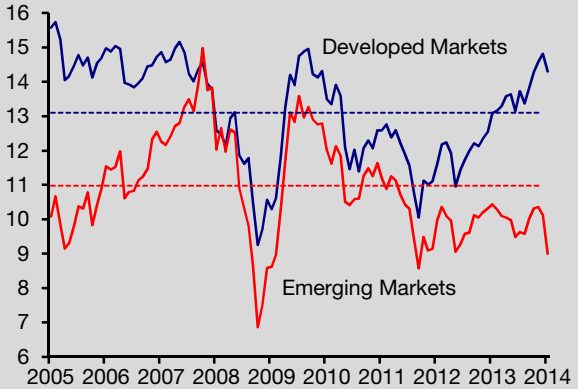
Price movements since last May have generally been in line with well-established country risk metrics (Table 3). However, valuation levels such as price-earnings and price-book ratios appear less aligned with perceived country risk levels. Some of this reflects country-specific market structure (e.g. market depth, market governance and transparency, and level of foreign participation). However, higher valuation levels for more vulnerable countries in some instances suggests more room for correction, particularly given the challenges many emerging market countries face in implementing structural reforms and finding sources of growth. The broad weakness in expected earnings over the next 12 months (with only China expected to see much pickup) is another warning that "cheap" may not translate to "rally" any time soon.

Chart 12
Fed Funds December 2015 Futures Expected Rate and the U.S. Economic Surprise Index
percent, 24th rate, 30-day *index*



Source: Bloomberg, Citi.

Chart 13
Forward P/E ratios: Developed and Emerging Markets
MSCI indices, price to 12M forward earnings estimates



Source: MSCI, Bloomberg, IIF Calculations.

Table 3
EM Price Movements and Valuation Metrics

Since May 22, 2013

	Change in EMBIG Spreads, bps	Equities % Change	FX % Change vs. USD	P/E Current Levels	Price/Forward Earnings Current Levels	Price/Book Current Levels	12M Forward Earnings Growth,%
Turkey	170.0	-31.1	-18.1	7.9	8.7	1.4	-11.7
Indonesia	134.0	-17.9	-19.9	15.0	12.7	3.2	-17.8
India	93.0	1.7	-11.5	17.0	14.6	2.5	-5.8
South Africa	91.0	8.9	-13.4	17.1	14.3	2.6	-21.2
Emerging Markets	88.7	-11.1	-9.1	10.9	10.1	1.4	-3.2
Brazil	88.0	-26.8	-15.5	12.2	10.0	1.2	-14.7
Russia	56.0	-8.9	-9.6	4.6	4.3	0.7	-0.7
Mexico	44.0	-6.1	-6.4	21.0	18.2	2.7	-14.8
China	27.0	-5.7	1.3	9.2	9.0	1.4	12.1
South Korea	--	-2.9	3.8	16.7	8.5	1.2	2.2
Poland	14.0	-1.2	6.0	12.9	12.9	1.3	-8.8

Source: MSCI, JP Morgan, Bloomberg, Datastream, IIF Calculations.

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be around 3¾% higher than over the preceding two-year period, equally driven by higher FDI and portfolio equity inflows (Chart 14).

2. Focus on Fed exit to weigh on debt inflows

Related to the growth pick-up in mature economies, and notably in the U.S., a key issue will likely remain the path for phasing out of monetary stimulus and thus increasing interest rates. In our baseline, we are assuming that the first increase in the policy interest rate will occur in mid-2015, and that subsequent rate rises will be gradual, broadly consistent with market expectations (Chart 15). Accordingly, the 10yr U.S. bond rate should rise gradually to 3.5-4% by the end of 2015. In this environment, debt inflows are likely to evolve less favorably than equity inflows. While still increasing on a sequential basis throughout the projection horizon, 2014/15 debt flows are envisaged to remain around 16% below their 2012/13 level, driven by non-bank flows.

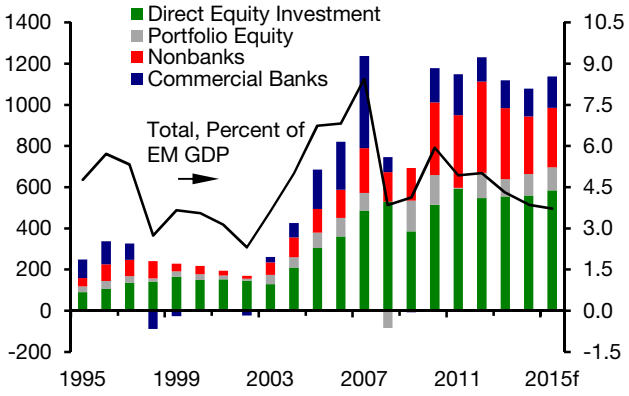
A KEY ISSUE WILL LIKELY REMAIN THE PATH FOR PHASING OUT OF MONETARY STIMULUS IN THE U.S.

As recent market turbulence has illustrated, the gradual tightening in global liquidity conditions raises the potential for more volatile market conditions. In particular, there remain downside risks of renewed EM retrenchment as the market focus shifts increasingly from the path of Fed tapering of asset purchases towards the prospective trajectory of Fed policy rate hikes post-2015. Currently, market expectations are for a rate hike path that is less steep than in previous Fed tightening cycles (Chart 15). However, a re-pricing of these expectations upwards would raise Treasury yields and further weigh on debt inflows. If this repricing were driven by a more robust U.S. recovery, there would be offsetting benefits from the positive spillovers of greater U.S. demand for EM exports. Of greater concern would be an upside surprise in U.S. wage pressures on the back of a tighter than assumed labor market which could lead to a sense that the Fed had fallen behind the curve even without upward revisions to projections for activity (See Box 4, next page)

Chart 14

Emerging Market Private Capital Inflows, Net

$ billion *percent of GDP*

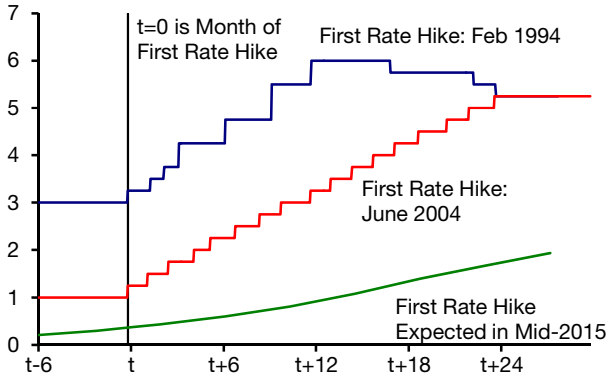


Source: IIF, National Sources.

Chart 15

Federal Funds Target Rates During Fed Tightening Cycles

percent, t in months, market expectations estimated from fed funds futures and Eurodollar contracts



Source: Bloomberg, Datastream, IIF.

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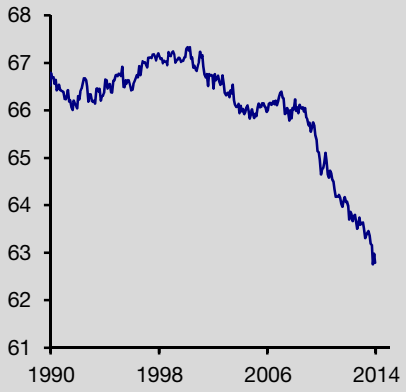
BOX 4: HOW TIGHT IS THE U.S. LABOR MARKET?

U.S. WAGE PRESSURES COULD INCREASE IF LABOR FORCE PARTICIPATION DROPS FURTHER

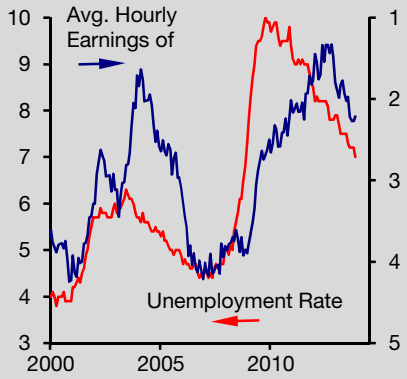
What could trigger a renewed re-pricing of Fed policy rate expectations, potentially leading to another EM sell-off? Clearly, stronger growth than expected by the Fed and an associated decline in the unemployment rate would be one possibility, although the impact of the repricing on EM flows would be muted by improved export prospects. A more damaging risk for EMs would be a sustained increase in inflation expectations, even under the Fed's current growth and employment forecasts. Such a scenario could arise if the labor market turns out to be tighter than assumed. It is difficult to assess the damage to labor market structures from the financial crisis, which makes it difficult to forecast how quickly wage pressures will build in coming quarters. Specifically, labor force participation has fallen sharply since the crisis, in part for underlying demographic reasons (largely related to an aging population) and in part for cyclical reasons as workers facing long-time unemployment have become discouraged (Chart 16). What is not clear is to what extent discouraged workers will return to the labor force as the economy improves, after long periods of unemployment that may have eroded labor skills. If significant numbers of discouraged workers do not return, participation could continue to fall, implying that fewer people are looking for work and tighter labor market conditions, and rising pressure on wages, eventually leading to higher core inflation (Chart 17). Simulations that assume a continued fall in labor force participation suggest that inflation could be markedly higher in 2015 and beyond, likely forcing an earlier and/or steeper than anticipated increase in policy rate hikes (see Global Economic Monitor, December 2013). Amidst a continued fall in labor force participation in the December employment report, wage inflation thus bears watching in the months ahead

Chart 16
U.S. Labor Force Participation Rate
percent



Source: BLS.

Chart 17
U.S.: Unemployment Rate and Wage Inflation
% of labor force *% change over a year*



Source: BLS, IIF.

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3. Country differentiation to remain high

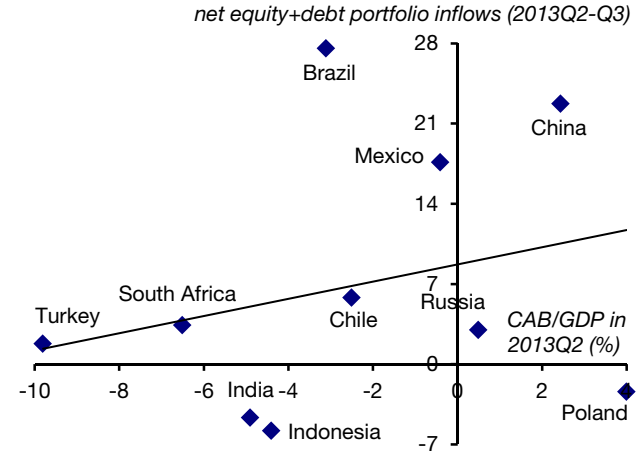
While aggregate capital flows to EMs are expected to rise gradually, cross-country dispersion is likely to remain substantial. Countries that are expected to perform less well going forward are those with large external financing requirements (which already received relatively lower inflows during last summer's episode, Chart 18), especially when financing needs are met predominantly by portfolio flows and where the debt maturity structure is more weighted to the short-term. Also, evidence of rapid past credit growth and substantial real exchange rate appreciation increases perceptions of imbalances and hence countries' vulnerability (Chart 19). Moreover, political risk will likely play an increasingly important role with the number of elections in EMs being particularly high in 2014 (see Annex table Y for an overview of vulnerability indicators across countries). Based on a selection of measures, the "Fragile 5" countries (Brazil, India, Indonesia, South Africa and Turkey) stand out – though to varying extent. Turkey is a particular example of a vulnerable country suffering from political tensions, although recent action by the central bank to sharply increase policy interest rates will help to bolster confidence in the policy framework.

POLITICAL RISK WILL LIKELY PLAY AN INCREASINGLY IMPORTANT ROLE

WILL CAPITAL CONTINUE TO FLOW UPHILL?

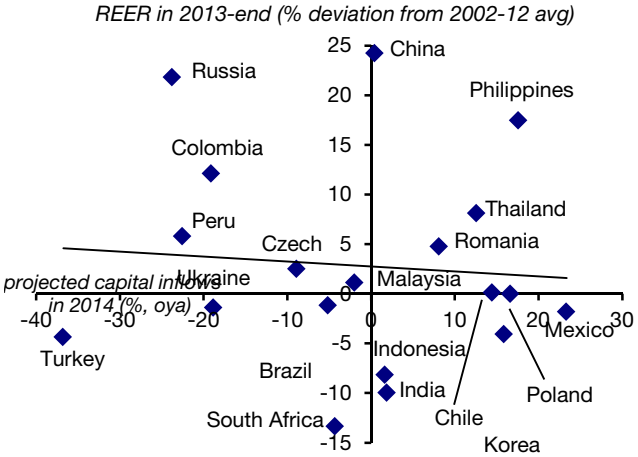
A remarkable feature of the past 10-15 years was the enormous amount of capital that flowed out of emerging economies, both in gross and in net terms. On a gross basis, EM residents have invested around $13.4 trillion abroad (including in other EMs) in the years 2000-2013, while net flows from EMs to mature economies amounted to roughly $4 trillion during that period (Chart 20, next page). The tendency of EM economies to be net capital exporters is against the predictions of standard economic theory, which posits

Chart 18
Current Account Vulnerability



Source: National Sources, IIF.

Chart 19
Real Exchange Rate Developments & 2014 Flow Forecasts



Source: National Sources, IIF.

1. Lucas (1990): Why Doesn't Capital Flow from Rich to Poor Countries? American Economic Review 80, 92-96.

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that low-income countries with a small capital stock have high marginal returns to capital that should attract foreign investment. The fact that capital has tended to flow "uphill" from poor to rich countries is a paradox that was first identified by Robert Lucas in 1990[2]. It is noteworthy that a large chunk of the EM resident capital outflows relate to reserve accumulation by the official sector – partly related to a desire for self-insurance after the Asia crisis of the late 1990 and partly to resist exchange rate appreciation.

A more mundane paradox is that despite their large volumes, private capital outflows by EM residents generally receive much less attention than investments by non-residents into those economies (which our headline capital flows estimates on the front page of this report refer to). This may be partly explained by the fact that non-resident inflows to EMs tend to be more volatile than resident outflows and that EM economies tend to be more vulnerable to swings in foreign inflows than mature economies.

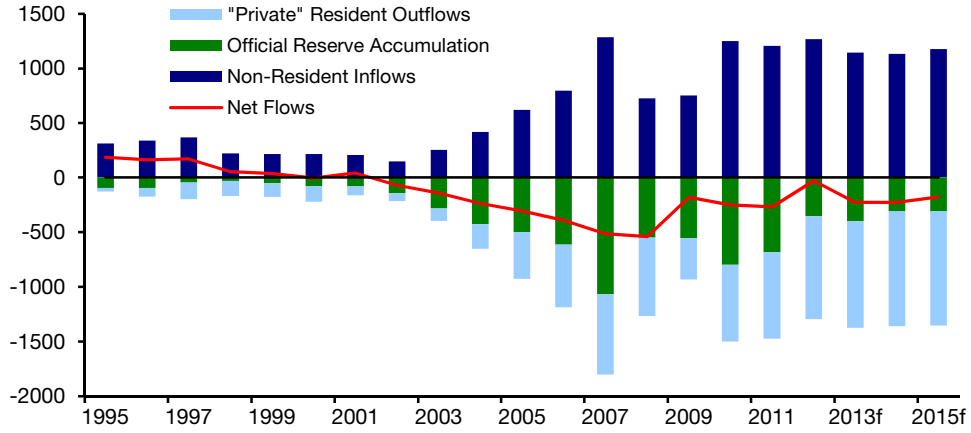
In recent years, two developments stand out about EM capital outflows:

- In net terms, the Lucas paradox is reduced. The overall net surplus is down since the crisis, and the number of surplus countries has also fallen (Charts 21 and 22, next page). EMs still have an overall CA surplus, but this is concentrated in a small group of countries.
- At the same time, while official reserve accumulation has slowed, private resident outflows have risen, largely reflecting increasing openness and portfolio diversification in EMs, although in some countries such flows may also have reflected concerns about domestic financial and political stability.

PRIVATE RESIDENT OUTFLOWS HAVE RISEN

Taking a closer look at aggregate developments in the EM world, the countries that kept the Lucas Paradox alive were a small number of export-oriented economies that either had large oil reserves (Saudi Arabia, UAE, and Russia) or leaned heavily against market

Chart 20
EM Capital Flows by Residency of Investors
$ billion, "private" resident outflows include state-owned enterprises and SWFs



f= IIF Forecast; Source: IIF.

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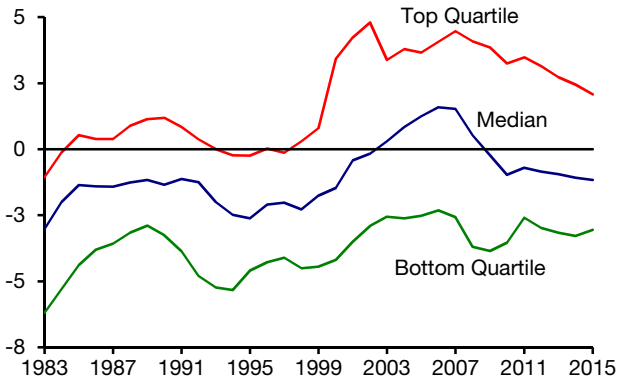
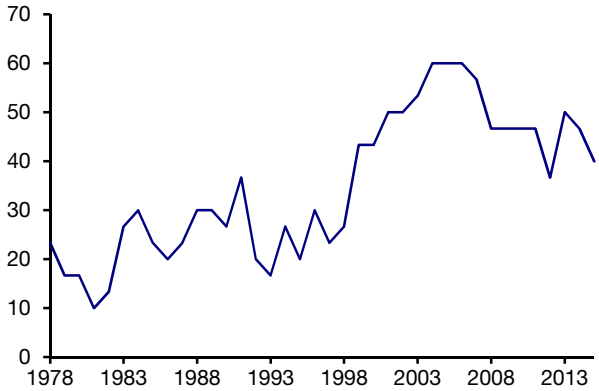
Chart 21
IIF Sample of 30 EMs : Current Account Balance
percent of GDP, 3-year moving average



Source: IIF.

Chart 22
Share of EMs that are Capital Exporters
percent



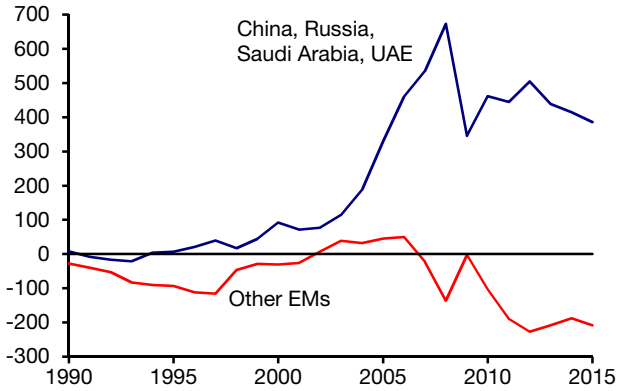
Source: IIF, National Sources.

forces to prevent an appreciation of their exchange rate (China). Together, these four countries account for roughly $4.8 trillion of net external asset accumulation from 2000-2013 (Chart 23). Excluding these four countries from our sample of 30 major EMs, emerging markets were net recipients of foreign capital to the tune of $776 billion during the same period.

EM OUTWARD FLOWS SHIFTING FROM RESERVES TO PRIVATE INVESTMENT

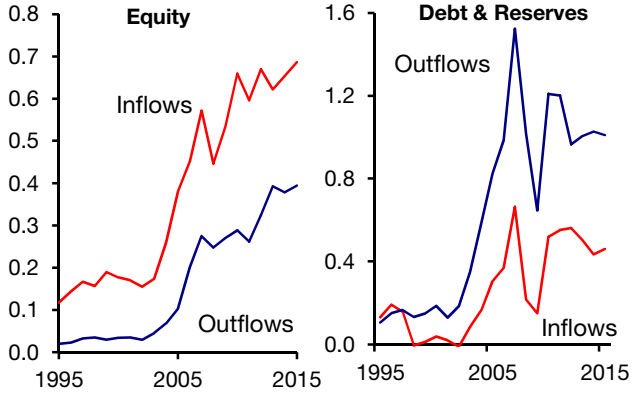
The pattern of EM capital outflows reflects the motivation behind them. EM external asset accumulation has been dominated by the investment of official reserves into very liquid, low-yielding debt, mainly U.S. Treasury securities (Chart 24). By contrast, emerging markets have long been large net recipients of equity investment, which tends to be less liquid (especially FDI) and has a higher risk-return profile (Chart 24). In recent years, however, there has been an important rotation away from reserve

Chart 23
EM: Cumulative Current Account Balance
$ billion



Source: IIF, National Sources.

Chart 24
EM Non-Resident Inflows and Resident Outflows
$ trillion



Source: IIF.

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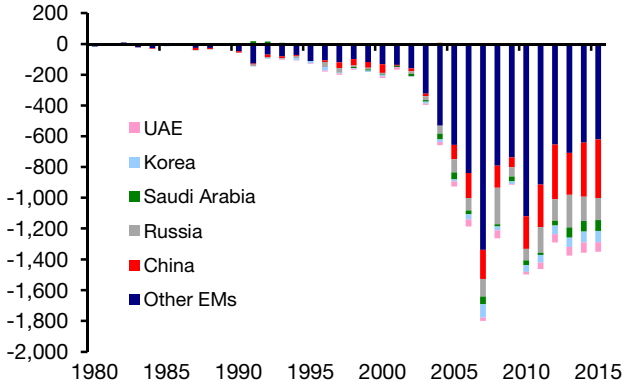
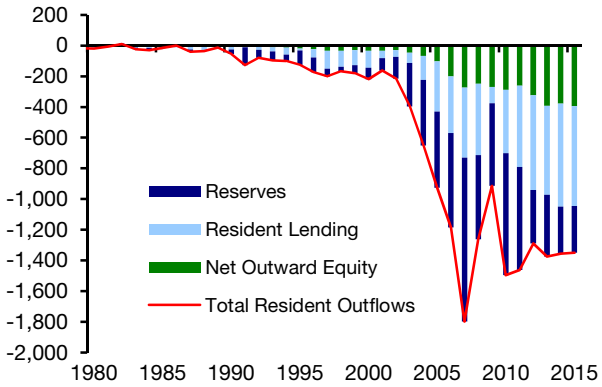
Chart 25
Private Resident Outflows
$ billion



Source: IIF.

Chart 26
Total Resident Outflows
$ billion



Source: IIF.

accumulation towards greater private sector outflows. China is an important part of this shift, but the rotation is also driven by the other BRICS and smaller EM economies (Chart 25). Equity investment abroad increased 10-fold from an average $36 billion per year in 2000-2003 to an estimated $365 billion in 2012-2013 (Chart 26). Resident lending abroad, which includes all debt instruments other than those that form part of official reserves, staged a similar increase from an average $67 billion per year to $595 billion per year during those same periods.

A significant portion of these investments goes towards other emerging economies. These flows, sometimes referred to as south-south flows, have received growing interest in recent years (see also our recent note on EM outward FDI). However, south-south flows are notoriously difficult to track because most EM countries do not publish a detailed breakdown of either the destination or the source countries of their capital flows. Two valuable data sources on bilateral investment statistics are the IMF's Coordinated Direct Investment Survey (CDIS) and Coordinated Portfolio Investment Survey (CPIS).[3] According to CDIS data as of end-2012, Chile, Mexico and China are the largest source countries for south-south FDI flows (Chart 27, next page). Chile and Mexico invest a considerable share of their outward FDI in other markets in the region, especially in Brazil. By contrast, China's share of investment in other emerging economies relative to its total outward FDI is quite small (6%).

SOUTH-SOUTH FLOWS HAVE RECEIVED GROWING INTEREST IN RECENT YEARS

Reported holdings of portfolio investment in other emerging markets are generally much smaller, ranging from $1-$10 billion for the top ten source countries that provide data to the CPIS (Chart 28, next page). Data availability is more limited for portfolio

3. For portfolio investment, participating countries report their assets (outward investment), but not their liabilities (inward investment). For direct investment, all participating countries report liabilities and most countries provide data on their assets. Data for some source and destination countries is incomplete because it is up to individual country authorities to report the data to the IMF. Therefore, the dataset tends to underreport countries' total outward investment, meaning that the true volume of south-south investment (and south-north investment) is probably underestimated. China participates in the CDIS, but not in the CPIS.

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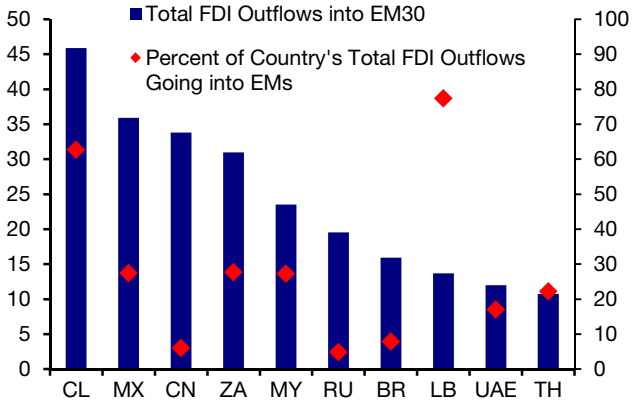
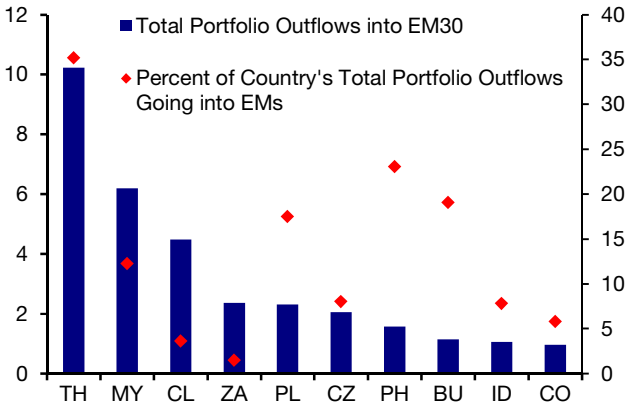
Chart 27
South-South Flows: Largest EM Sources of FDI to EMs
$ billion, stock data *percent, share of FDI to EM*



Source: IMF, IIF.

Chart 28
Largest EM Sources of Portfolio Investment to other EMs
$ billion, stock data *percent, share of PI to EMs*



Source: IMF, IIF.

investment, however, and China does not participate in the survey at all. Out of those countries that do report data, Thailand and Malaysia stand out as the largest source countries of portfolio investment in other EMs. Residents of both countries have been known to be active investors in other countries in the region, including Korea, Russia, and Indonesia.

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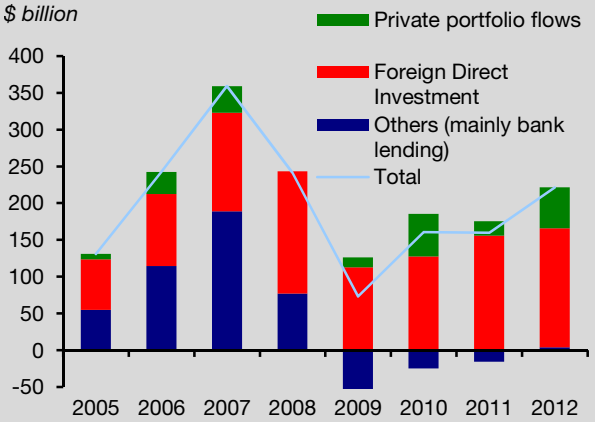
BOX 5: HOW WELL INSULATED ARE FRONTIER MARKETS?

Modest recovery in capital inflows since the financial crisis. With volatility in portfolio flows to emerging markets again on the rise as the Fed initiates tapering, it is instructive to take a closer look at capital inflows to less well-established frontier markets, which weathered the first wave of the Fed tapering shock relatively well compared to emerging markets. Frontier markets are by no means a homogenous group; rather, they comprise a number of distinct subgroups, including wealthy MENA countries, that have restructured their sovereign debt to private creditors and lost market access (e.g. Argentina),[4] much poorer Asian and African countries with little past bond market access, and small Central and Eastern European countries. That said, in the run-up to the 2008 financial crisis, capital flows to frontier markets grew at a remarkable pace—for the 31 countries in the group flows nearly tripled in size from $130bn (7.8% of GDP) in 2005 to $359bn (over 15% of GDP) in 2007.[5] A significant portion of this growth was in foreign direct investment (FDI) inflows (up by over 95%), and particularly, bank lending flows (up by 240%), with MENA and Emerging Europe accounting for the lion's share of the group (Charts 29 and 30). However, as with capital flows to both developed and EM economies, capital inflows to frontier markets were hit severely by the 2008 crisis and have only partially recovered since then. Although capital inflows to Sub-Saharan Africa have increased at a remarkable rate since 2009 (Chart 30), total private inflows to frontier markets are estimated to have been $191 billion (or 4.9% of GDP) in 2013, still almost 50% below pre-crisis levels.

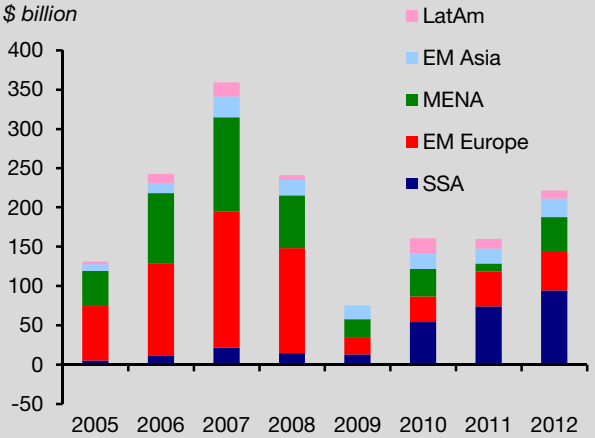
Banking inflows still subdued. The main factor behind this subdued recovery in private capital inflows has been the reversal of cross-border banking flows. With banks in developed countries adjusting to new regulatory frameworks in

Chart 29
Frontier Market Capital Inflows
$ billion



Source: IMF, IIF; A large share of "other private flows" accounts for banking flows.

Chart 30
Frontier Market Private Capital Inflows by Region
$ billion



Source: IMF.

4. The definition of frontier markets varies among different users of the term (e.g. official sector bodies, providers of market indices, etc.). For the purposes of this short note we have mainly used countries included in the MSCI Frontier Markets Index. Of note, this index includes Argentina—a G20 member with a large and diverse economy, but one which has a very thinly capitalized equity market. MSCI's index also includes a heavy weighting of wealthy or relatively well-off MENA countries, including Kuwait (27%), Qatar (14%) and UAE (10%), and a much smaller weighting of a number of European/Central Asian countries including Kazakhstan (3%), Croatia and Slovenia (each around 2%) and the Baltics (about 1% for all three). Poorer Asian and African countries are another subset—Pakistan (4%), Vietnam and Bangladesh (about 2.5% each), for example, with Kenya at 3% and Mauritius less than 1%. The MSCI index has little current Latin American/Caribbean weighting apart from Argentina, but other benchmarks (e.g. S&P Frontier Markets Broad, FTSE Frontier) give greater weight to some smaller countries like Ecuador, Jamaica and Trinidad and Tobago.
5. The sample has been selected to correspond with MSCI's definition of frontier markets and data availability at the required frequency. Our sample includes Argentina, Bahrain, Bangladesh, Bosnia and Herzegovina, Botswana, Bulgaria, Croatia, Estonia, Ghana, Jamaica, Jordan, Kazakhstan, Kenya, Kuwait, Lebanon, Lithuania, Mauritius, Morocco, Nigeria, Oman, Pakistan, Qatar, Romania, Saudi Arabia, Serbia, Slovenia, Sri Lanka, Trinidad and Tobago, Tunisia, Ukraine, and Vietnam.

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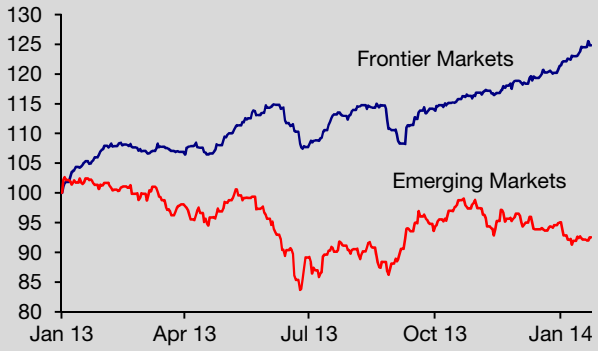
part by cutting back their cross-border lending activities, frontier markets recorded $90 billion of net banking outflows between 2009 and 2012—more than 2% of their GDP. The magnitude of these outflows has been largest for those countries with close ties to Euro Area banks. For example, frontier markets in MENA (-$54bn in total since 2008) and Eastern Europe (-$39bn) have been significantly affected by reversals of banking flows. In contrast, having slowed significantly in 2009/10, cross-border banking flows to frontier markets in Asia have recovered over time as regional emerging market and Japanese banks have stepped in to fill the gap.

FDI has been resilient: In the aftermath of the crisis, FDI has become the main component of total capital flows to frontier markets, accounting for more than 65% of total inflows since 2008. Solid growth momentum (an average 3.3% since 2008 compared to 0.4% in mature markets and about 5% in emerging markets more broadly) has attracted increasing global FDI flows over the past few years. The pick-up in FDI inflows to Mauritius has been particularly notable, reaching just over $60bn in 2012—reflecting factors including investment incentives, preferential access to the EU market in some cases, and, most importantly, the country's status as a conduit for FDI to India.

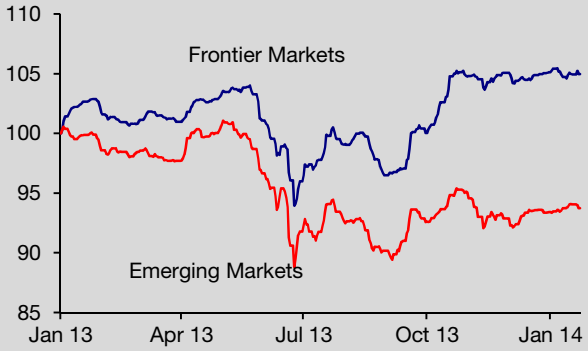
Portfolio flows more insulated from swings in EM sentiment: In recent years, many frontier markets have begun to receive more inflows of portfolio capital. While this trend in part reflects ongoing financial deepening (see for example our recent research note, "Financial Deepening in Sub-Saharan Africa"), many of these countries still have smaller and less liquid bond and equity markets than their emerging market peers—a factor that helped insulate frontier markets during last summer's reaction to the announcement of Fed tapering (Charts 31 and 32). Their relative lack of integration into the global economy and financial markets also serves to keep the correlation of financial asset prices with global markets relatively low. For frontier market equities, the correlation with the S&P500 has been below 0.5 on average since 2009, vs. around 0.7 for emerging markets more broadly—increasing their appeal as a source of portfolio diversification. However, while anticipation of Fed tapering has not put significant pressure on flows to frontier markets to date, those with high twin deficits, such as Ukraine, Lebanon, Ghana, Jordan, Tunisia and Serbia, remain more vulnerable to shifts in global financial conditions. Moreover, difficulties in larger frontier markets such as Argentina and Ukraine could add to stress on both frontier and emerging markets at times of heightened market tensions. At such times, other frontier markets may well remain quite insulated, supporting the performance of frontier market indices as a whole. However, previous experience suggests this may not always be the case—for example, between January 2008 and March 2009, the decline in frontier equity markets (-65%) was actually sharper than that in broader EM equity markets (-55%).

Chart 31
Market Performance: Equities
index, end-2012= 100



Source: MSCI Frontier Market index, JPMorgan Nexgem Bond index, Bloomberg. The country coverage may differ across series and time.

Chart 32
Market Performance: Bond Markets
index, end-2012= 100



Source: MSCI Frontier Market index, JPMorgan Nexgem Bond index, Bloomberg. The country coverage may differ across series and time.

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EMERGING ASIA: SIZEABLE INFLOWS WITH OCCASIONAL TURBULENCE

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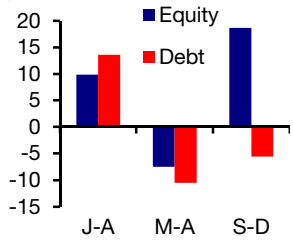
Last year proved to be a roller coaster ride for capital flows to the region, characterized by three phases. The first phase from January to late May witnessed easy global liquidity conditions and rising appetite for risk assets, which fueled foreign purchases of Asian equities and local currency bonds (Chart 33). Thereafter, the Fed announcement on May 22 that tapering was to begin by end-year surprised markets and precipitated a selloff of Asian stocks and bonds. The selloff persisted through August and was amplified by large foreign positions. In the third phase, from September, equity inflows revived and bond outflows diminished with the delay in Fed tapering calming markets. Improving prospects for economic growth in the region was also a supporting factor as were corrective policy measures in several countries aimed at preserving macroeconomic stability. The return of large equity purchases late last year reflected shifting global investor preference towards equities, before a correction in early 2014.

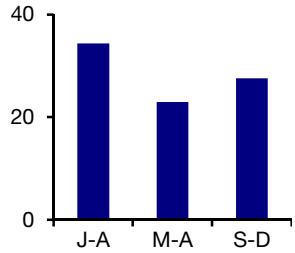
Chart 33
EM Asia: Net Portfolio Flows, 2013
$ billion



Source: National Sources, Bloomberg. Includes India, Indonesia, Korea, Thailand, Philippines.

Despite the fluctuations, there was only a small dip in external bond issuance in mid-2013 with offerings by sovereign as well as corporate borrowers continuing to be well-received through early 2014 (Chart 34). Spreads remained attractive enough for both issuers and investors. Moreover, purchasers of global bonds could avoid the currency risk inherent in domestic bonds. Foreign direct investment (FDI) to the region also held up over the course of the year. China dominated in this regard, with inward FDI sustained at around $60 billion per quarter.

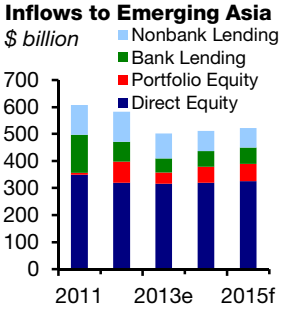
Chart 34
EM Asia: Global Bond Issuances, 2013
$ billion



Source: Thomson ONE. Includes China, India, Indonesia, Korea, Malaysia, Philippines, Thailand.

With Asia benefitting as the global expansion gathers pace, and assuming no major surprises in the path of Fed exit, we expect that capital inflows will remain sizeable this year and next, albeit not matching the pace of recent years and subject to periodic volatility as evident from the renewed portfolio equity selloff in early 2014. We project net private capital inflows for our seven countries constituting Emerging Asia to be around $510 billion in 2014 and $520 billion in 2015, after falling to $500 billion in 2013 from close to $600 billion in 2012 (Chart 35). Emerging Asia will continue to account for nearly half of capital flows to emerging markets. These will be underpinned by inward FDI both because of the importance of the region's export base and domestic markets. Being less affected by market gyrations, FDI's share in total inflows is set to rise from 55% in 2012 to 61% in 2015.

Chart 35
Net Private Capital Inflows to Emerging Asia
$ billion



Source: IIF. e = IIF estimate, f = IIF forecast.

Relatively attractive valuations and sizeable yield differentials should also be a draw for portfolio inflows along with commitment to macroeconomic stability and advancing of capital account liberalization. Dampening factors for flows are gradual monetary policy normalization in mature economies, unpredictable shifts in global sentiment and deleveraging by foreign banks.

Private capital inflows to China are set to remain around $330 billion a year, with FDI stabilizing around $250 billion (Chart 36, next page). Inflows should benefit from reforms, including the relaxation of restrictions on foreign investment, such as the shift to a 'negative investment list' in the Shanghai Free Trade Zone. Approval procedures to use RMB raised offshore to invest in China were also simplified in December, in line with the

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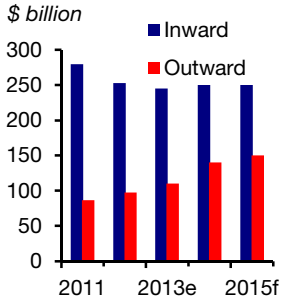
Third Plenum blueprint to gradually open the capital account. Meanwhile, we project outward FDI to rise from $100 billion in 2012 to $150 billion in 2015, or 46% of the total from emerging markets, spurred by the government's 'going global' strategy. Loans and investments abroad will continue to exceed $200 billion a year, fueled by the expansion of Chinese banks and the sovereign wealth fund, while reserve accumulation is also expected to remain around that level.

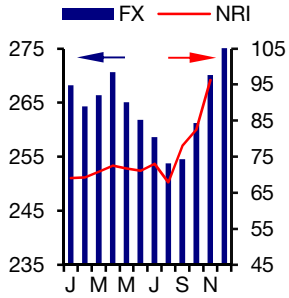
Chart 36
China: Foreign Direct Investment Flows
$ billion



Source: IMF, IIF. e = IIF estimate, f = IIF forecast.

Steps to attract capital inflows, curb gold imports and tighten monetary policy in the wake of the mid-2013 weakness along with a recovery in exports have bolstered India's balance of payments. In response to the policy measures, Nonresident Indian (NRI) deposits in the banking system and capital-raising by banks surged by $34 billion between August and November, prior to the closing of the central bank's special swap facility, allowing a rebuilding of reserves (Chart 37). Net private capital inflows are set to moderate to around $75 billion in the fiscal year ending March 2014, and then stabilize at that level in 2014/15 and 2015/16, well below the $100 billion inflows in 2012/13. While the increase in NRI deposits is likely to moderate, and administrative hurdles remain dampening factors, FDI is rising and Indian firms remain attractive to portfolio investors.

Chart 37
India: Foreign Reserves and NRI Deposits, 2013
$ billion

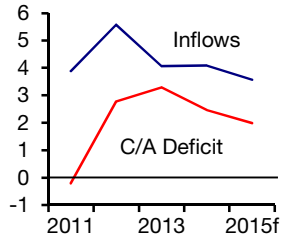


Source: Reserve Bank of India.

Indonesia also sought to counter the balance of payments weakness in mid-2013 by sharply tightening monetary policy, reducing the holding period for foreign investment in central bank certificates, easing curbs on short-term external borrowing by banks and resorting to greater sovereign bond issuance. The measures helped net private capital inflows revive to $36 billion in 2013, although falling well short of the $49 billion in 2012. With the government raising $4 billion in global bonds in early January 2014, net private capital inflows are set to remain around $37 billion this year and next, around 4% of GDP (Chart 38). This reflects in part lower inward FDI due to policy uncertainties in the oil and gas sectors along with mining.

There are several downside risks to our base case scenario. If market expectations about the course of Fed QE exit were to shift sharply as in mid-2013, the region, barring China and Korea which have large current account surpluses, would face financial market volatility because of the large foreign holdings of stocks and bonds. Indonesia could be most adversely affected because of its large external financial requirement, followed by India, although the latter's vulnerability has diminished considerably because of the recent correction in the current account deficit.

Chart 38
Indonesia: C/A Deficit and Private Capital Inflows
percent of GDP



Source: National Sources. f=IIF forecast.

With regard to domestic risks, capital inflows would be lower across the board if efforts to curb shadow banking, control local government debt and restrain real estate investment become more of a drag on activity in China than we anticipate. At the same time, high household debt in ASEAN and Korea and tighter credit conditions in India due to large nonperforming loans could have a greater adverse impact on growth and the capital account than we expect. Moreover, politics could play a spoiler if there is post-poll uncertainty following national elections in Indonesia and India mid-year, while prolonged political turmoil could undermine policy implementation and confidence in Thailand.

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EMERGING EUROPE: FOREIGN CAPITAL INFLOWS TO EASE SLIGHTLY IN 2014

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Weaker global risk appetite after Fed tapering was put on the agenda in late May led to a sharp drop in private capital inflows to Emerging Europe. Led by reversals of portfolio equity inflows and borrowing by domestic banks, and a shift to net sales by foreign holders of local currency government bonds, net inflows of foreign capital dropped to just $15 billion during the third quarter — less than one-third of the rate during the second quarter (Chart 39). Eurobond issues fell to their lowest level since mid-2012. The correction was the largest in Turkey and Russia, where net inflows fell to a fraction of those registered during the preceding quarter, and in Hungary, where net capital outflows more than doubled over the same period.

WEAKER GLOBAL RISK APPETITE AFTER FED TAPERING WAS PUT ON THE AGENDA IN LATE MAY LED TO A SHARP DROP IN PRIVATE CAPITAL INFLOWS TO EMERGING EUROPE

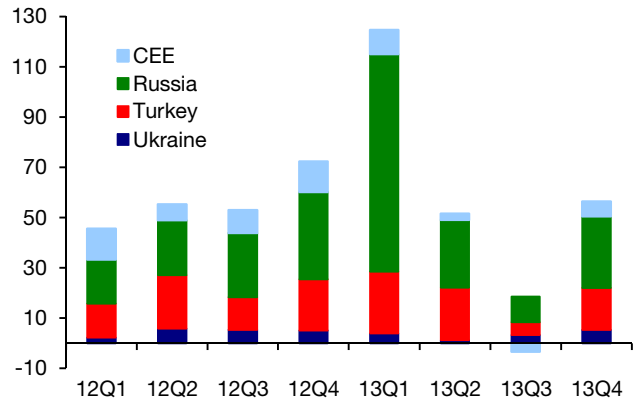
With concerns about Fed tapering easing in the second half of 2014, risk appetite firmed and inflows rebounded. Preliminary data suggest that net inflows of foreign private capital to Emerging Europe rose to $55 billion or so in the fourth quarter, returning to their second-quarter level. This rebound was driven by a near doubling in Eurobond issues to $26 billion, reflecting both issues postponed from the summer and advanced from 2014 (Chart 40). FDI inflows firmed, too, while portfolio inflows resumed thanks to a few large IPOs by Russian companies. Borrowing by banks recovered somewhat in Central Europe, but remained sluggish in Turkey and Russia at near third-quarter levels. On the other hand, nonresidents appear to have continued selling local currency-denominated bonds, with large outflows in Poland and Turkey more than offsetting small inflows in Hungary and the Czech Republic (Chart 41, next page).

WITH CONCERNS ABOUT FED TAPERING EASING RECENTLY, RISK APPETITE HAS FIRMED AND INFLOWS HAVE REBOUNDED

These developments are likely to have left net inflows of private foreign capital to the region at just over $250 billion last year as a whole, little changed from 2012. However, last year's inflows were boosted by transactions related to the acquisition by Rosneft, Russia's largest state-owned oil company, of the private oil company TNK-BP, which boosted foreign inflows by $44 billion and resident outflows by $55 billion (for details, see our June 2013 Capital Flows Report). Net of this transaction, private capital inflows would have amounted to just above $200 billion, a 20% decline from 2012.

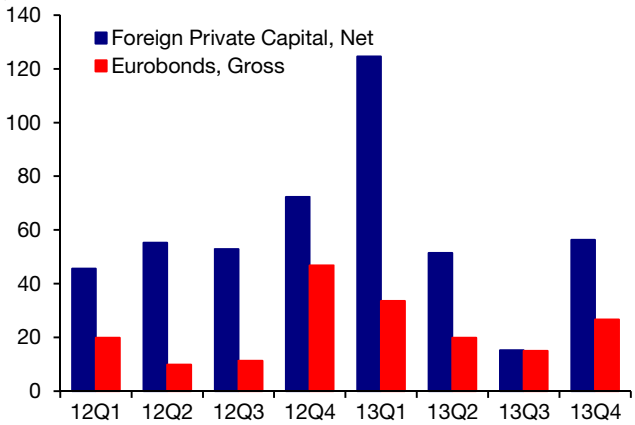
NET PRIVATE CAPITAL INFLOWS ARE LIKELY TO DECLINE BY ONE-FIFTH THIS YEAR (ADJUSTED FOR THE ROSNEFT TRANSACTION)

Chart 39
Emerging Europe: Foreign Private Capital Inflows, Net
$ billion



e = IIF Estimate; f = IIF Forecast.
Source: IIF.

Chart 40
Emerging Europe: Foreign Private Capital Inflows
$ billion



Source: IIF.

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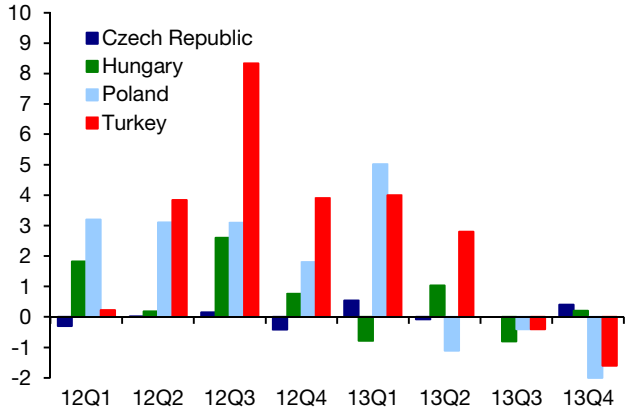
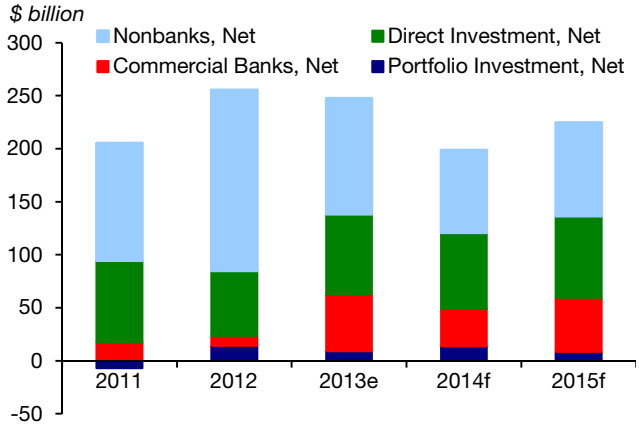
Chart 41
Emerging Europe: Nonresident Purchases of Bonds
$ billion, local-currency denominated bonds



Source: IIF.

Chart 42
Emerging Europe: Foreign Private Capital Inflows
$ billion



e = IIF Estimate; f = IIF Forecast.
Source: IIF.

Assuming the Fed exit proceeds in line with markets' expectations and does not trigger another round of volatility, net private foreign capital inflows to the region look likely to continue to recover on a sequential basis this year. Adjusted for the Rosneft transaction, inflows would remain little changed at just over $200 billion in 2014 before picking up again to $244 billion in 2015 (Chart 42). This projection assumes global risk appetite improves during the year as global growth firms, that Fed tapering proceeds smoothly, and that economic recovery stays on mark. It also assumes the current political tensions in Turkey are resolved without a full-blown political crisis and that the central bank will sustain the recent sharp increase in policy rates during most of 2014. While FDI inflows are likely to remain stable near $75 billion, portfolio equity inflows should firm and nonresident purchases of local currency bonds should resume, albeit at a slower pace than in early 2013. Banks in Central Europe are likely to continue repaying parent banks abroad this year but should return to modest net borrowing by 2015, assuming successful efforts to bolster confidence in European bank balance sheets ahead of introduction of the Single Supervisory Mechanism later this year.

NET PRIVATE FOREIGN CAPITAL INFLOWS TO THE REGION (ADJUSTED FOR THE ROSNEFT TRANSACTION) LOOK LIKELY TO REMAIN LITTLE CHANGED THIS YEAR

While Central Europe looks resilient to shifts in market sentiment given strong external positions and limited external financing needs, Russia, Turkey, and Ukraine will likely face a challenging 2014. Ukraine remains most at risk with an economy in deep recession and access to capital markets lost. The Russian bailout will help the authorities to muddle through for about a year. In the absence of reforms, access to capital markets appears unlikely to be restored soon, increasing rollover risks and eventually forcing the authorities to seek official financial support by early 2015 at the latest, from the IMF or elsewhere. In Turkey, the vulnerability due to a large current account deficit and heavy reliance on portfolio inflows for financing has been reinforced by heightened political tensions. The latter, if unresolved soon, may result in a further intensification of already significant financial market pressures. A reversal or even a sustained slowdown in portfolio inflows would make it difficult to sustain a current account deficit on the order of 6-7% of GDP. The central bank has sharply tightened its monetary stance in response

RUSSIA, TURKEY, AND UKRAINE WILL LIKELY FACE A CHALLENGING 2014

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to lira weakness. This will weigh on the growth outlook, especially if the depreciation pressure on the lira were to remain. In Russia the potential risks are related not to the sovereign, but rather to the heavy dependence of banks and corporations on foreign funding for investment. With the latter already suffering as a result of sharply lower profits, more expensive and less readily available foreign funding would further constrain investment and reinforce the economy's largely structural weakness.

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...PRIVATE CAPITAL INFLOWS TO THE REGION HAVE REBOUNDED, PARTICULARLY PORTFOLIO DEBT INFLOWS AS RESIDENTS FRONT-LOADED BORROWING IN ANTICIPATION OF HIGHER INTEREST RATES

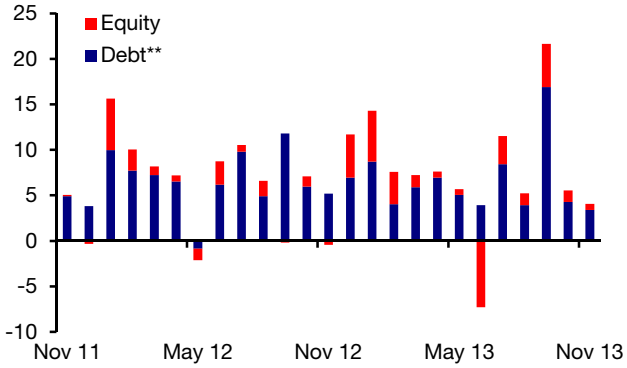
LATIN AMERICA: BACK TO FUNDAMENTALS

Following a decline in mid-2013 when talk of QE tapering began, private capital inflows to the region rebounded in the second half, particularly portfolio debt inflows as residents front-loaded borrowing in anticipation of higher interest rates (Charts 43 and 44). Looking forward we expect nonresident net private capital inflows to remain broadly unchanged at almost 5.0% of GDP over the next two years vis-à-vis 2013, but the outlook differs across countries. Prudent policies, sound fundamentals and improving export prospects are likely to make the nations of the Pacific Rim (Mexico, Chile, Colombia and Peru) the main recipients of foreign investment. On the other hand, Argentina and Venezuela are likely to face continuing external pressures in light of investor concerns about their unbalanced policy frameworks and weakening reserve positions.

Mexico, a country with one of the region's most liquid local debt markets, a robust macro policy framework and an impressive structural reform drive, has been an increasingly attractive destination for foreign investors. While they pulled out a net of $2.6 and $1.7 billion from the Mexican local sovereign debt market in June and October, respectively, they put back in more than $3.0 and $6.0 billion in November and December, thereby keeping the overall nonresident investment position broadly stable at 35-38% of the total market (Chart 45, next page). We project that capital inflows to Mexico will rise significantly in the years ahead as oil- and natural gas-related FDI inflows are set to jump

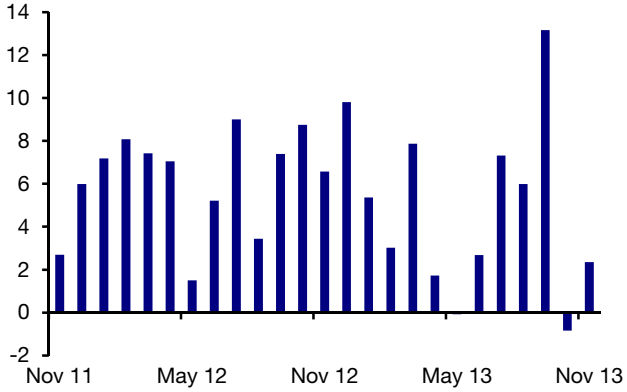
WE PROJECT THAT CAPITAL INFLOWS TO MEXICO WILL RISE SIGNIFICANTLY IN THE YEARS AHEAD AS OIL- AND NATURAL GAS-RELATED FDI INFLOWS ARE SET TO JUMP ON ENERGY REFORM IMPLEMENTATION

Chart 43
Latin America: Portfolio Inflows*
$ billion



Source: IIF From National Sources. *Inc. Brz, Chi, Col, Mex, Per; **Excludes flows into private debt securities for Mexico, Peru.

Chart 44
Latin America: Inflows into Local Sovereign Debt Markets
$ billion



Source: IIF; *Inc. Brazil, Chile, Colombia, Mexico, Peru, Uruguay

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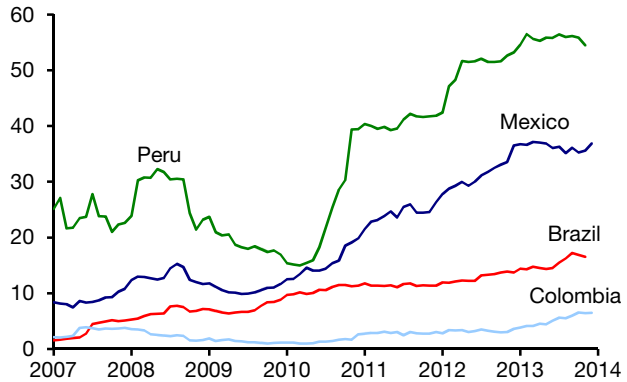
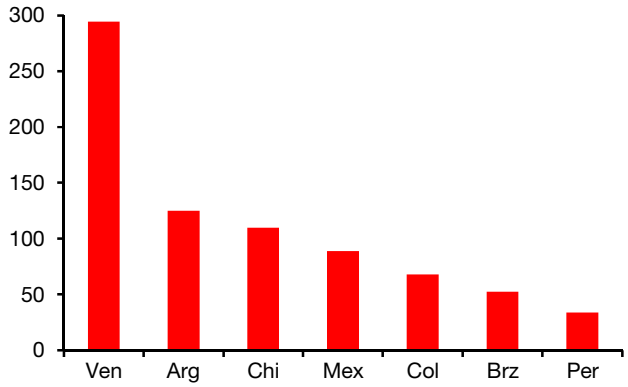
Chart 45
Latin America: Foreign Holdings in Local Sov. Debt Markets
percent of total



Source: IIF Based on National Sources.

Chart 46
External Vulnerability
*short-term financing needs as percent of reserves**



Source: IIF; *(2014f Current Account Deficit + 2013 ST Ext. Debt + 2014 LT Ext. Debt Amortizations) / Intl. Reserves (ex. gold)

on energy reform implementation. We forecast average FDI inflows to increase from 1.8% of GDP in 2010-2012 to 2.3% of GDP in 2014-2015, and to gain further momentum, approaching 2.5-3.0% of GDP, starting in 2016.

The Andean counties have also continued to attract private capital inflows. As in Mexico, foreign investor participation in Peru's local-currency sovereign debt market has remained stable at about 55% of the total amid approval of a fiscal rule in October (a 1%-of-GDP maximum cyclically-adjusted deficit). These inflows are also on the rise in Colombia due to lower taxation (the tax on nonresident income from domestic debt securities was cut to 14% from 33%) and in Chile, which in April 2013 launched a Global Depository Note (GDN) program allowing nonresidents to invest in the local treasury market via a U.S. custodian bank. Nonetheless, the ending of the mining investment cycle has begun to moderate FDI inflows to Chile and Peru.

Brazil has become increasingly reliant on portfolio debt inflows as foreign direct investment inflows to the country remain on a downward trend amid lack of progress on the structural front and unresolved policy inconsistencies. Despite large inflows linked to the auction of the offshore pre-salt Libra oilfield ($4.0 billion) in November, direct equity investment inflows fell to $42 billion in 2013, down from $53 billion in 2012. However, portfolio debt inflows have increased due to removal of the 6.0% financial operations tax (IOF) on nonresident fixed-income investment in mid-2013, depreciation of the real against the dollar, and monetary policy tightening (the Selic rate has increased 325 bp to 10.50% since April 2013). Net portfolio debt inflows totaled $23 billion in 2013, up from $11 billion in 2012.

Foreign capital inflows to Argentina and Venezuela are being deterred by deep macroeconomic imbalances, weak property rights, draconian controls on capital outflows, and in the case of Argentina, a history of bad relations with external creditors. While Venezuela is still able to access international debt markets through its state-owned oil

FOREIGN CAPITAL INFLOWS TO ARGENTINA AND VENEZUELA ARE BEING DETERRED BY DEEP MACROECONOMIC IMBALANCES, WEAK PROPERTY RIGHTS AND DRACONIAN CONTROLS ON CAPITAL OUTFLOWS

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company (PDVSA), the cost of doing so is rapidly rising. Venezuela's EMBIG spread widened 70% to almost 1300 bps in late January from a year ago. PDVSA raised $4.5 billion through a private bond offering in 2013. Two-thirds of dollars were used to pay PDVSA's suppliers and a third to beef up international reserves. Foreign-currency inflows, however, quickly turned into capital flight amid weak confidence. In the absence of pro-market policy shifts and assuming rollover of short-term debt, we forecast net private inflows to Argentina to be practically nonexistent in 2014 and 2015 and to be just 1.0% of GDP in Venezuela. Argentina and Venezuela are the region's economies most vulnerable to QE tapering by the Federal Reserve and softer commodity prices (Chart 46, previous page). In January, both countries were forced to devalue their currencies against the dollar in an effort to protect declining international reserves.

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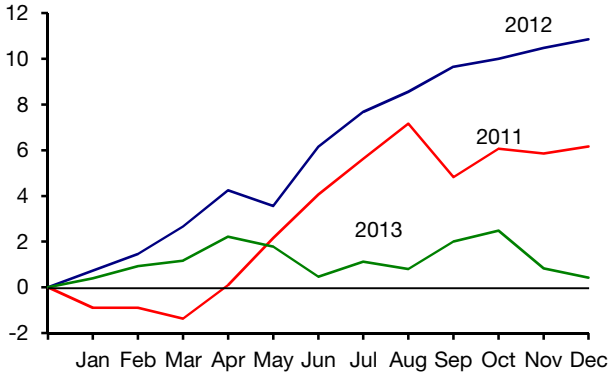
AFRICA/MIDDLE EAST: OPPORTUNITY TEMPERED BY POLITICAL UNCERTAINTY

Shifts in global financial market sentiment from risk-on to risk-off and back again did not have a major impact on capital flows to Africa/Middle East in 2013, with the notable exception of South Africa, the country in the region with the largest, most liquid domestic bond market. Up until last year, nonresidents' purchases of fixed income securities had been a mainstay of capital inflows into South Africa. Then, starting in May 2013, they slowed sharply amid speculation surrounding the start of Fed tapering. Initially there was a shift in investor preference from bonds to equities, but later in the year as concerns grew over the size of the current account deficit and South Africa's dependence on portfolio inflows, foreigners reduced their positions in both bonds (Chart 47) and equities (Chart 48).

SHIFTS IN GLOBAL FINANCIAL MARKET SENTIMENT FROM RISK-ON TO RISK-OFF AND BACK AGAIN DID NOT HAVE A MAJOR IMPACT ON CAPITAL FLOWS TO AFRICA/ MIDDLE EAST IN 2013, WITH THE NOTABLE EXCEPTION OF SOUTH AFRICA

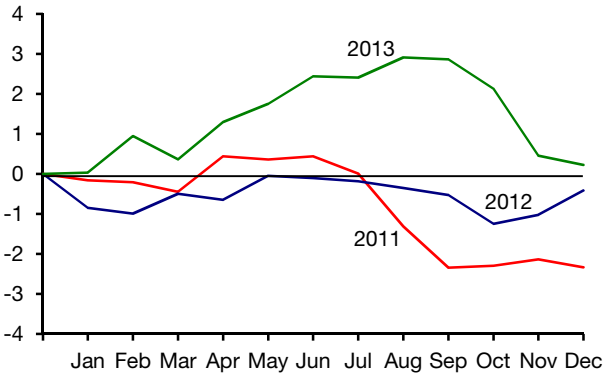
Despite developments in South Africa, which experienced a drop in inflows from nonbank private creditors last year, total net private flows to the seven countries covered in this report (South Africa, Nigeria, Egypt, Morocco, Lebanon, Saudi Arabia and U.A.E.) rose from $81 billion in 2012 to $89 billion in 2013. This reflected a steady increase in

Chart 47
South Africa: Nonresidents' Purchases/Sales of Bonds
$ billion, cumulative year-to-date



Source: South African Reserve Bank

Chart 48
South Africa: Nonresidents' Purchases/Sales of Equities
$ billion, cumulative year-to-date



Source: South African Reserve Bank

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FDI, but was mainly due to a jump in net portfolio equity inflows. This in turn reflected a swing from outflows in 2012 to inflows in 2013 in Egypt and a continued surge of investment in the Nigerian stock market.

Foreign appetite for sovereign bond issues in frontier markets in Sub-Saharan Africa (which are not included in our sample of countries in this report) also increased last year despite growing investor caution. In addition to South Africa and Nigeria, Ghana came back to the market and two others, Tanzania (a private placement) and Rwanda, issued maiden bonds. Kenya is planning to enter the market this year, issuing up to $1.5 billion worth of bonds, and Angola and Uganda are also weighing options. The appeal of African paper is partly its rarity (which helps foreign investors diversify their portfolios), but it also reflects the strong growth potential and natural resource wealth of these economies.

FOREIGN APPETITE FOR SOVEREIGN BOND ISSUES IN FRONTIER MARKETS IN SUB SAHARAN INCREASED LAST YEAR DESPITE GROWING INVESTOR CAUTION

We expect total net capital inflows to the group of countries covered to be broadly unchanged in 2014 and 2015, at just over $100 billion. Private flows are likely to slip a little in 2014 before rebounding to a record $93 billion next year, driven by a further increase in FDI and a pickup in nonbank private creditors. Domestic events, both political and economic, are likely to be the main determinant of flows going forward. Fed tapering, as long as it is steady and in line with market expectations may exert less of an influence.

DOMESTIC EVENTS, BOTH POLITICAL AND ECONOMIC, ARE LIKELY TO BE THE MAIN DETERMINANT OF FLOWS GOING FORWARD

In South Africa, politics and domestic economic prospects may be more of a determinant of capital inflows over the next couple of years than global capital market developments. Political uncertainty leading up to the general election in April/May and ongoing unrest in the mining sector, if not resolved satisfactorily, may keep foreign investors on the sidelines in the first half of the year. Although the ANC is expected to win the election, foreign investors will be waiting to see whether the outcome results in any policy shift. In particular, the speed at which reforms outlined in the NDP are implemented may determine foreign enthusiasm, or lack of, for South Africa. Concerns over the size of the current account deficit (forecast at 6.4% of GDP in 2014) will likely persist as Fed tapering progresses. As a result, we do not expect any early rebound in nonresidents' purchases of fixed income securities. Although elections are not due until 2015 in Nigeria, political infighting has already started, resulting in a split in the ruling PDP. While this may raise concerns and dampen portfolio inflows over the next year and a half, it is not likely to impact total inflows significantly as FDI is likely to continue to rise following the recent privatization of the power sector and reflecting increasing opportunities in the rapidly growing nonoil sector.

THE SPEED AT WHICH REFORMS OUTLINED IN THE NDP ARE IMPLEMENTED MAY DETERMINE FOREIGN ENTHUSIASM, OR LACK OF, FOR SOUTH AFRICA

In the MENA region, politics is likely to be a key influence in Egypt and Lebanon. Foreign investors will likely be watching developments closely in both countries, which are gearing up for presidential and/or parliamentary elections this year. Prospects for stronger economic growth and a rebound in FDI in Egypt hinge on the achievement of political stability and structural reforms. The current interim government received large official financial assistance from Saudi Arabia, the UAE, and Kuwait. Net private capital flows, notably from these same countries, could rise to about $7.5 billion by 2014/15, but

THE PROSPECTS FOR STRONGER ECONOMIC GROWTH AND A REBOUND IN FDI IN EGYPT HINGE ON THE ACHIEVEMENT OF POLITICAL STABILITY AND STRUCTURAL REFORMS

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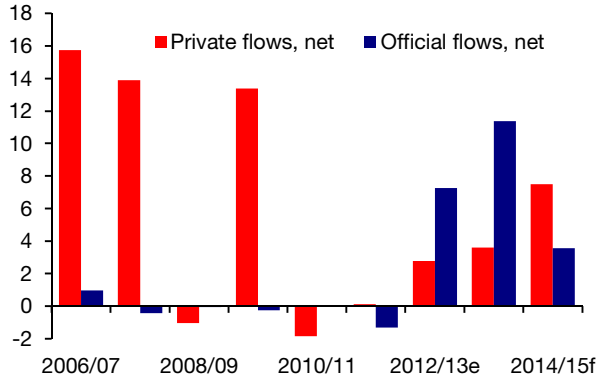
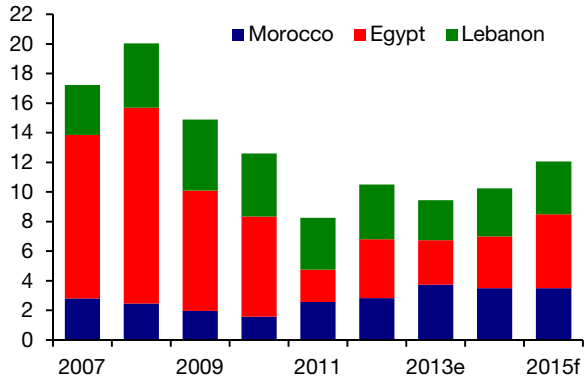
Chart 49
Egypt: Net Private and Official Flows
$ billion



Source: Central Bank of Egypt, IIF calculations.
e = estimate; f = IIF forecast. 2006/07 = year ending June

Chart 50
Consolidated FDI to Egypt, Lebanon, & Morocco
$ billion



Source: National Sources; IIF calculations.
e = estimate; f = IIF forecast. For Egypt 2007 = 2006/07

would remain far below the peak of $15.7 billion in 2006/07 (Chart 49). Net private capital inflows to Lebanon, the bulk into nonresident deposits, are expected to increase modestly from $2.9 billion in 2013 to $4.4 billion in 2014, despite prevailing political uncertainties (still well below the peak of $12 billion in 2009). In Morocco, we expect net private capital inflows to remain modest at around $4 billion (equivalent to 4% of GDP, close to the average for emerging economies) and mostly in the form of FDI (Chart 50).

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ANNEX 1: METHODOLOGY FOR IIF PORTFOLIO FLOWS TRACKER

The challenge with tracking portfolio flows in real time is that balance of payments (BoP) data are typically published on a quarterly basis, and are often released with a considerable lag. For those countries that publish high-frequency data on capital flows, the data are not always consistent with their quarterly BoP data.

In light of these data constraints, we have developed a monthly measure of portfolio flows that is based on both country-level BoP data (where available) and EPFR fund flows data. In terms of country-level BoP data, we use a sample of 12 EM economies that publish monthly portfolio equity flows data and 11 EM economies that publish debt flows data. This data is available with a relatively short lag of 2-3 months. We obtain our monthly estimate of portfolio equity flows based on the following two regressions:

$$\text{Total_Equity} = \underset{(0.0002)}{1.17} * \text{Country_Equity} + \underset{(0.007)}{0.5} * \text{EPFR_Equity} \qquad \text{adj. } R2 = 0.89$$

$$\text{Total_Debt} = \underset{(0.00012)}{2.34} * \text{Country_Debt} + \underset{(0.036)}{0.43} * \text{EPFR_Debt} \qquad \text{adj. } R2 = 0.72$$

Total_Equity (Total_Debt) are quarterly portfolio equity (debt) inflows to our sample of 30 EM economies, Country_Equity (Country_Debt) are quarterly portfolio equity inflows to the selection of countries that publish monthly portfolio flows data, and EPFR_Equity (EPFR_Debt) are quarterly EPFR equity flows to EM dedicated funds. P-values are in parentheses. The sample period is 2010Q1 to 2013Q2 for equity flows and 2011Q1 to 2013Q2 for debt flows (This is the period for which the EPFR debt flows data seem to be sufficiently representative, reflecting the growing coverage of fund flows over time). We use the coefficients from this regression for mapping monthly country-level flows and EPFR flows into a joint estimate of overall monthly portfolio flows.

The accuracy of our tracker can be assessed by comparing its forecast errors over the prediction period to the performance of a univariate regression based on EPFR data alone. A simple estimation of total quarterly BoP portfolio flows based on EPFR data (plus a constant term) has an average forecast error of $8.7 billion for equity flows and $11.6 billion for debt flows. Our monthly portfolio flows tracker reduces these forecast errors to $7.7 billion and $7.3 billion, respectively, over the period from 2011Q1 to 2013Q2. While these comparisons are based on in-sample predictions, the substantial differences in forecast accuracy suggest that our tracker is likely to outperform the univariate prediction out-of-sample as well.

Countries that publish monthly data on capital flows include Brazil, Poland, Romania, Philippines, South Korea, Czech Republic, Bulgaria, Turkey, Ukraine, Thailand, Indonesia and Chile.

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In addition, we have developed a portfolio flows leading indicator (PFLI) that provides real-time estimates of overall portfolio flows to emerging markets. The PFLI is available for the current month and the two prior months, covering the same group of countries as the above portfolio flows tracker. The estimations build on our recent empirical work on modelling the drivers behind portfolio flows to EM economies, which is described in the December 2013 IIF Research Note "Quantifying the Fed's Impact on Capital Flows to Emerging Markets."

The exact specification of the model used to predict portfolio flows depends on the type of flow (equity vs. debt) and the lag with which the variables used to predict portfolio flows are released (e.g. no lag for daily data vs. a 1-month lag for EPFR data). The predictors used for both types of flows include EM exchange rate data and changes in market expectations for U.S. monetary policy. Additional predictors for equity flows include an EM stock market index and equity fund flows as measured by EPFR. For bond flows, the additional predictors are EM bond issuance data, the EMBIG spread, and a risk indicator (the U.S. BBB-rated corporate bond spread over Treasuries).

We aim to release a more detailed methodology note in late February, and to provide the latest monthly estimates around the 20th of each month. If you would like to receive our latest portfolio flows estimates, please send an email to Robin Koepke at rkoepke@iif.com.

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ANNEX 2: HEAT MAP OF SELECTED VULNERABILITY INDICATORS ACROSS EMERGING ECONOMIES

	Argentina	*Brazil*	*Bulgaria*	*Chile*	*China*	*Colombia*	*Czech R.*	*Hungary*	*India*	*Indonesia*	*Korea*
External Financing Vulnerabilities:											
Current Account Balance/GDP (%)	-1.2	-3.7	2.5	-4.2	2.4	-3.4	0.4	5.3	-3.7	-3.4	5.8
Net FDI/Current Account Deficit (%)	79	38		25		104			41	37	
Reserve Coverage Ratio*	0.7	1.8	0.9	0.9	5.9	1.5	1.5	1.5	1.4	0.8	2.0
Short-Term External Debt/Total External Debt (%)	13	9	26	16	74	14	27	14	26	26	30
External Debt/GDP (%)	27	30	91	44	8	21	55	112	22	30	35
REER (% deviation at 2013-end from 2003-12 avg.)	26	-1	6	0	24	12	3	0	-10	-8	-4
Domestic Financial Vulnerabilities:											
Non-Financial Corporations Debt/GDP (%, change during 2011-2013Q1)		9.2	-3.2	8.4	19.4		3.6	12.2	2.4	3.9	7.6
Households Debt/GDP (%, change during 2011-2013Q1)		5.6	-3.2	2.4	4.1		2.4	-8.2	0.1	2.6	3.8
Credit Growth (% oya, 2010-12 avg.)	36	17	5	13	18	16	4	-2	17	18	5
Foreign Investor Share in Govt Debt Market (%, 2013-end)		17				6	13	37	2	33	10
Cross-Border Financial Claims/Domestic Credit (%, 2012)	24	21	89	60	4	31	150	95	20	31	16
Domestic Fiscal Vulnerablities:											
Fiscal Balance/GDP** (%)	-2.4	-3.6	-2.0	-1.0	-2.0	-1.0	-2.9	-2.9	-7.1	-2.4	1.7
Gross Government Debt/GDP (%)	48	68	16	13	23	32	48	80	67	26	36
Elections in 2014***		✓				✓	✓	✓	✓	✓	

	Malaysia	*Mexico*	*Peru*	*Philippines*	*Poland*	*Romania*	*Russia*	*South Africa*	*Thailand*	*Turkey*	*Ukraine*
External Financing Vulnerabilities:											
Current Account Balance/GDP (%)	2.7	-1.5	-4.5	2.6	0.8	1.5	1.5	-6.4	-0.8	-7.6	-8.3
Net FDI/Current Account Deficit (%)		67	98					7	133	12	37
Reserve Coverage Ratio*	1.6	1.1	3.2	3.6	0.9	1.1	2.5	0.8	2.1	0.5	0.2
Short-Term External Debt/Total External Debt (%)	61	24	14	21	18	20	18	20	45	28	25
External Debt/GDP (%)	38	30	31	30	76	69	36	40	37	52	83
REER (% deviation at 2013-end from 2003-12 avg.)	1	-2	6	17	0	5	22	-13	8	-4	-1
Domestic Financial Vulnerabilities:											
Non-Financial Corporations Debt/GDP (%, change during 2011-2013Q1)		0.8			4.4	-0.6	4.5	1.0	5.8	5.8	14.7
Households Debt/GDP (%, change during 2011-2013Q1)		1.1			0.3	-2.3	1.1	-0.5	12.0	3.8	-6.0
Credit Growth (% oya, 2010-12 avg.)	10	7	11	10	8	7	26	7	14	19	9
Foreign Investor Share in Govt Debt Market (%, 2013-end)	28	37	55		33	23	25		17	22	
Cross-Border Financial Claims/Domestic Credit (%, 2012)	40	90	134	28	87	111	26	40	19	39	22
Domestic Fiscal Vulnerablities:											
Fiscal Balance/GDP** (%)	-6.3	-2.4	0.8	-2.1	-4.0	-2.5	-0.5	-4.2	-3.4	-1.6	-7.0
Gross Government Debt/GDP (%)	57	44	19	41	58	38	14	43	47	36	43
Elections in 2014***					✓	✓		✓	✓	✓	

Note: Data refers to 2013 estimates unless otherwise specified

Color Code: Red - most vulnerable, Pink - vulnerable, Light Green - less vulnerable, Dark Green - least vulnerable

Vulnerability is shown relative to the countries in the sample and uses the following thresholds:

For CAB/GDP: Below -3% (most vulnerable), between -3% to 0 (vulnerable), between 0 to +3% (less vulnerable), above +3% (least vulnerable)

For reserve coverage ratio: Below 0.5 (most vulnerable), between 0.5-1.0 (vulnerable), between 1.0-2.0 (less vulnerable), above 2.0 (least vulnerable)
For other indicators, the four colors are assigned as follows: Above +1 standard deviation from the mean across countries, between mean and +1 standard deviation, between mean and -1 standard deviation, below -1 standard deviation from the mean

**FX reserves/(current account deficit + short-term external debt by residual maturity)*

***Applies to general or central government, where applicable*

****Includes local, parliamentary & presidential elections*

Source: IIF, IMF, BIS, National Sources.

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ANNEX 3: IIF CAPITAL FLOWS DATA – A LAYMAN'S GUIDE

Capital flows arise through the transfer of ownership of assets from one country to another. When analyzing capital flows, we care about who buys an asset and who sells it. If a foreign investor (a non-resident) buys an emerging market asset, we refer to this as a capital inflow in our terminology. We report capital inflows on a net basis. For example, if foreign investors buy $10 billion of assets in a particular country and sell $2 billion of that country's assets during the same period, we show this as a (net) capital inflow of $8 billion. Note that net capital inflows can be negative, namely if foreign investors sell more assets of a country than they buy in a given period. Our "net private capital inflows to emerging markets" measure is the sum of all net purchases of EM assets by private foreign investors.

Correspondingly, if an investor from an emerging market country (a resident) buys a foreign asset, we call this a capital outflow. Net capital outflows can also be positive or negative. Following standard balance of payments conventions, we show a net increase in the assets of EM residents (a capital outflow) with a negative sign.

For further details regarding terminology, concepts and compilation of our data, please consult our User Guide located on our website at www.iif.com/emr/global/capflows.

IIF CAPITAL FLOWS REPORT COUNTRY SAMPLE (30)

Emerging Europe (8)	Bulgaria	**Latin America (8)**	Argentina
	Czech Republic		Brazil
	Hungary		Chile
	Poland		Colombia
	Romania		Ecuador
	Russian Federation		Mexico
	Turkey		Peru
	Ukraine		Venezuela
Emerging Asia (7)	China	**Africa/Middle East (7)**	Egypt
	India		Lebanon
	Indonesia		Morocco
	Malaysia		Nigeria
	Philippines		Saudi Arabia
	South Korea		South Africa
	Thailand		UAE

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Table
Emerging Asia: Capital Flows
$ billion

	2012	2013e	2014f	2015f
Foreign Capital Inflows				
Total Inflows, Net:	*594*	*511*	*521*	*531*
Private Inflows, Net	583	501	511	521
Equity Investment, Net	398	357	379	389
Direct Investment, Net	319	316	320	325
Portfolio Investment, Net	79	41	59	64
Private Creditors, Net	185	144	132	132
Commercial Banks, Net	73	52	58	60
Nonbanks, Net	113	92	75	72
Official Inflows, Net	10	10	10	9
International Financial Institutions	3	3	3	3
Bilateral Creditors	8	7	7	6
Resident Capital Outflows				
Total Outflows, Net	*-623*	*-720*	*-752*	*-758*
Private Outflows, Net	-506	-428	-510	-542
Equity Investment Abroad, Net	-159	-166	-200	-216
Resident Lending/Other, Net	-347	-262	-310	-326
Reserves (- = Increase)	-117	-293	-242	-216
Memo:				
Net Errors and Omissions	-118	0	0	0
Current Account Balance	*148*	*209*	*231*	*228*

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Table
Emerging Europe: Capital Flows
$ billion

	2012	2013e	2014f	2015f
Foreign Capital Inflows				
Total Inflows, Net:	*256*	*251*	*217*	*245*
Private Inflows, Net	255	263	212	244
Equity Investment, Net	76	81	85	86
Direct Investment, Net	61	75	71	77
Portfolio Investment, Net	14	5	13	8
Private Creditors, Net	180	182	127	158
Commercial Banks, Net	9	54	36	51
Nonbanks, Net	171	128	91	107
Official Inflows, Net	0	-12	5	2
International Financial Institutions	-6	-10	0	3
Bilateral Creditors	7	-2	6	-1
Resident Capital Outflows				
Total Outflows, Net	*-223*	*-220*	*-177*	*-178*
Private Outflows, Net	-168	-225	-195	-189
Equity Investment Abroad, Net	-67	-126	-76	-79
Resident Lending/Other, Net	-101	-99	-118	-110
Reserves (- = Increase)	-55	5	17	11
Memo:				
Net Errors and Omissions	*-28*	*0*	*0*	*0*
Current Account Balance	*-4*	*-31*	*-40*	*-67*

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Table
Latin America: Capital Flows
$ billion

	2012	2013e	2014f	2015f
Foreign Capital Inflows				
Total Inflows, Net:	*335*	*282*	*291*	*296*
Private Inflows, Net	311	266	269	278
Equity Investment, Net	150	140	139	155
Direct Investment, Net	125	117	120	130
Portfolio Investment, Net	25	22	19	25
Private Creditors, Net	161	126	130	122
Commercial Banks, Net	29	17	30	31
Nonbanks, Net	132	108	100	91
Official Inflows, Net	23	16	21	19
International Financial Institutions	3	-1	5	7
Bilateral Creditors	20	17	16	12
Resident Capital Outflows				
Total Outflows, Net	*-218*	*-147*	*-167*	*-177*
Private Outflows, Net	-166	-151	-172	-148
Equity Investment Abroad, Net	-62	-56	-56	-53
Resident Lending/Other, Net	-105	-96	-116	-95
Reserves (- = Increase)	-52	4	6	-29
Memo:				
Net Errors and Omissions	-30	0	0	0
Current Account Balance	*-87*	*-135*	*-124*	*-120*

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Table
Africa and Middle East (AFME): Capital Flows
$ billion

	2012	2013e	2014f	2015f
Foreign Capital Inflows				
Total Inflows, Net:	*84*	*102*	*103*	*104*
Private Inflows, Net	81	89	87	96
Equity Investment, Net	47	61	61	66
Direct Investment, Net	41	46	49	52
Portfolio Investment, Net	5	15	12	14
Private Creditors, Net	34	28	26	30
Commercial Banks, Net	7	12	12	12
Nonbanks, Net	28	16	14	18
Official Inflows, Net	3	13	17	8
International Financial Institutions	3	4	4	4
Bilateral Creditors	0	9	12	4
Resident Capital Outflows				
Total Outflows, Net	*-231*	*-286*	*-264*	*-241*
Private Outflows, Net	-107	-167	-176	-170
Equity Investment Abroad, Net	-36	-45	-46	-46
Resident Lending/Other, Net	-71	-122	-130	-124
Reserves (- = Increase)	-124	-119	-87	-71
Memo:				
Net Errors and Omissions	*-73*	*-4*	*0*	*0*
Current Account Balance	*221*	*188*	*160*	*137*

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