The COVID-19 shock has resulted in a pronounced sudden stop in capital flows to EM. Our daily tracking of non-resident portfolio flows points to the largest EM outflow ever in Q1 2020, including at the worst points of the global financial crisis. This Global Macro Views feeds these outflows into our EM positioning database, which we introduced last year. That database folds in data on the value of foreign real money holdings of stocks and bonds in EM, which allow us to estimate valuation changes on underlying positions. What emerges is that, on top of record outflows, substantial valuation losses are also likely in Q1 2020, so that the overall reduction in foreign investor exposure to EM is very substantial. That decline, coupled with the many Fed easing measures announced in recent weeks, is a stabilizing force for EM. At the same time, it is possible markets are re-focusing on potential fall-out of the COVID-19 shock for emerging and frontier markets, which – even after big outflows in Q1 – carries the risk of a second wave of outflows.

Our high-frequency tracking of non-resident portfolio flows to and from EM points to record outflows in Q1 2020 (Exhibit 1), with the bulk of these outflows coming from non-China EM (Exhibit 2). Our daily data are noisy and so we often look at them on a quarterly basis, which also allows us to compare them to official BoP data (for the same 20 emerging markets) that are typically released with a substantial lag. Our tracking of Q1 outflows around - $62 bn is roughly twice the size of outflows recorded at the peak of the global financial crisis (Exhibit 3) and is historically near official BoP data that are released subsequently (red). When we merge these outflows with our EM positioning database, adjusting for additional countries where we don’t have daily tracking data, the picture points to record outflows and substantial valuation losses in Q1 (Exhibit 4).
The position reduction foreign investors are experiencing in stocks and bonds is a stabilizing force for EM. Two arguments weigh against that, however. First, a decade of extraordinarily easy monetary policy in the G10 pushed large real money flows into EM – the hunt for yield – with foreign holdings up substantially over the last decade (Exhibit 5), especially where inflows have been heavy like in South Africa and Chile (Exhibit 6). Second, markets have so far been preoccupied with the economic fall-out from COVID-19 on advanced economies. This focus may now be shifting to EM, which could set in motion a second wave of capital outflows, even after the unprecedented pace of outflows in Q1.