

# A month of Athens and Beijing

The developments in Greece and China should give confidence to market participants. **Stefan Hofer** says emerging markets will benefit from the recent developments in the two countries.

**F**or investors following the emerging markets, March 2010 witnessed two unrelated but important events. The first was the successful issue of EUR5 billion 10-year bonds by Greece and the second was China's National People's Congress. The former was critical, as it signalled that the market was still open to finance the Greek government's borrowing needs. This uncertainty had weighed heavily on the market's risk appetite. The second reiterated China's stance vis-à-vis growth, inflation and the policymakers' overall priorities. Both outcomes were supportive for emerging markets overall, but for different reasons.

First, with regards to the Greek bond issue, market participants breathed a sigh of relief as strong demand helped lower the cost of borrowing. That said, at a yield of 6.2 per cent, this still represented a 300-basis-point yield pick-up over benchmark German bonds. While Greek bonds have rallied, the still-high spread illustrates that the government has a long road ahead in terms of consistently implementing its fiscal consolidation plans. In terms of market perception, however, this process is off to a good start. The national parliament

passed austerity measures in early March, in line with what had been agreed to with the European Union. And, despite mounting social pressures and ongoing strikes, the government has pressed ahead with its goal of bringing the 2010 budget deficit to under nine per cent of GDP.

Greece is expected to issue more bonds. Successfully implementing fiscal consolidation measures should mean again lower borrowing costs for the new debt. This, in turn, could set off a virtuous circle whereby increased confidence in Greece's fiscal institutions boost economic growth. Given that investors' concerns for much of 2010 have arguably centred on fiscal vulnerability and debt sustainability in developed economies, alleviated concerns in Greece would have a marked effect on risk premia in general. While emerging markets were never the focus on that front, risky assets should benefit all else being equal, from diminished worries over developed markets' finances.

In terms of the National People's Congress, the main messages coming from China's policymakers largely reiterated their growth and job creation priorities. The government's growth

target for 2010 is 10 per cent, while loan growth expectations remain accommodative. With a new loans target of RMB7.5 trillion for 2010, this helps assuage some concerns that China was moving quickly towards a tightening stance, given the array of policy adjustments undertaken so far this year (e.g. bank's reserve requirement hikes). Separately, the authorities explicitly highlighted steps to reign in property prices in China, which marks a departure from previous practice. While it remains to be seen how the market will interpret the implementation of these steps, they could well be a source of volatility in the months ahead.

Given China's immensely important role in supporting global growth, the largely status quo signals from Beijing in March are supportive for emerging markets. Emerging Asia in general is likely to maintain its growth lead and thereby continue to attract investor flows. At the same time, the softening (but not fully resolved) fiscal woes in Europe should boost market confidence and the tolerance for risk.

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