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Hasenstab: Focus on Fundamentals in US, Emerging Markets

October 12, 2018

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In this video, Templeton Global Macro CIO Michael Hasenstab shares his thoughts on why he thinks US Treasury yields have moved higher. He also gives his take on recent weakness in emerging markets.

The full transcript of the video follows.

US Economic Data Supports Higher US Treasury Yields

Michael Hasenstab: We have an acknowledgement that the US economy is actually pretty strong. Whether you look at the [Institute for Supply Management] numbers, the labour data, even the [US Federal Reserve's] conversation tone is changing, to acknowledge that, yeah, we're at full employment, you know, the economy is growing quite strong. You look at [gross domestic product] numbers—you name it—things are strong, and as a result, Treasuries have now started to gap higher, and we've had a pretty big move.

Michael Hasenstab: We have seen US [Treasury] yields rise, the US dollar strengthen against G-10 currencies, but the US dollar weaken against those emerging markets with decent fundamentals. We've seen some stability in places like Brazil. So we think it is very possible with a moderate rise in US yields—not so much that you trigger a recession, but a moderate rise in yields—that the US dollar will strengthen against the euro or the yen or the Australian dollar, which have very accommodative policies. But that positive economic backdrop will be good for emerging-market aggregate demand and the demand for their exports. And since the interest rate differential is still significant, they will still attract capital.

Taking the Long View on Emerging Markets

Michael Hasenstab: In India and in Indonesia, I think the market's overreacting. I think their vulnerabilities both to oil, both to slightly higher US Treasury yields, are overstated vis-a-vis what the exchange rate has done. The current accounts are funded. The fiscal policy has been quite prudent in Indonesia's case, for close to a decade. They do not have high levels of indebtedness, and again, they have dealt with this exchange rate depreciation without any debt sustainability problems, corporate defaults, etcetera. So we think that the market has overreacted.

Michael Hasenstab: In Argentina, we think they are doing every policy decision correctly, and it's not just us saying it from the private sector. The IMF's package of close to US$57 billion provides, I think, a huge endorsement that these are the right policies. The IMF does not sign up for a US$50+ billion project without being very confident that all the right policies are being pursued for debt sustainability.

Michael Hasenstab: If you have a three-month time horizon, EM investing is very difficult. If you have a couple-year horizon, you can exploit these panic sell-offs that are not fundamental in nature. So, I think we've seen, since "Taper Tantrum" [2013], about half a dozen of these, and we've seen a snapback almost each time. The sell-off in August hasn't completely snapped back yet, but we don't see any reason why it shouldn't, because the fundamentals are lined up.

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