News release

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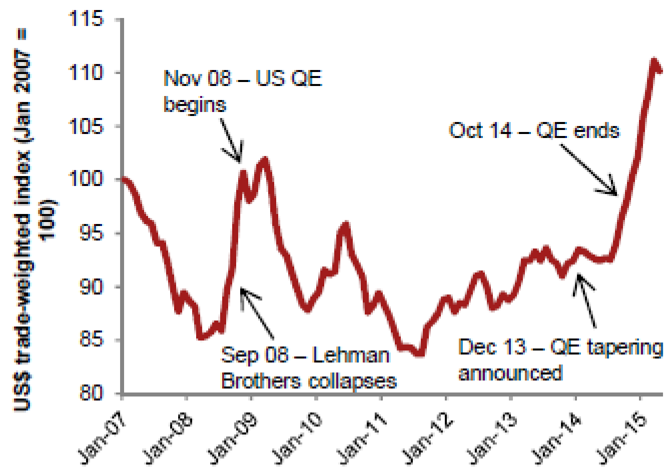
Payback time! Emerging markets and the rising dollar

Rising cost of US$ credit impacts many emerging economies, says PwC report

Dollar denominated debt issued outside the US increased from around $6 trillion before the first round of quantitative easing (QE) was introduced in November 2008 to around $9 trillion in 2014. Currently, the value of outstanding dollar denominated debt in emerging economies is around $3.3 trillion, which equates, for example, to more than double the annual economic output of Spain.

As the US economy has picked up and QE has come to an end, however, the dollar has appreciated by around 20% on a trade-weighted basis over the past 12 months (see Figure 4).

Fig 4: In the past year, the US dollar has appreciated by around 20% in trade-weighted terms



Sources: PwC analysis, Federal Reserve

"A strong dollar, like oil prices, is a rare thing in economics: its impact can be felt throughout the global economy, but it's the impact outside the US which I think is of particular interest," says PwC senior economist Richard Boxshall.

PwC's economists have assessed the vulnerability of 14 emerging markets which have issued significant amounts of dollar denominated debt. Most seem reasonably well placed to deal with the risks associated with a stronger dollar.

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Table 1: Turkey, Peru, Colombia and South Africa are the most vulnerable economies to the strong dollar

Countries	Vulnerability	Foreign currency external debt (% of GDP)	12-month currency movement (%)	Current account balance (% of GDP)
Turkey	High	46%	-19.4%	-5.7%
Peru	High	30%	-10.3%	-4.1%
Colombia	High	25%	-23.2%	-5.0%
South Africa	High	19%	-12.1%	-5.4%
Malaysia	Medium	65%*	-11.0%	4.6%
Chile	Medium	51%	-9.9%	-1.2%
Russia	Medium	37%*	-33.3%	3.1%
Indonesia	Medium	33%*	-11.7%	-3.0%
Brazil	Medium	24%*	-27.9%	-3.9%
Mexico	Medium	22%	-13.8%	-2.1%
Argentina	Medium	27%	-9.6%	-0.9%
Thailand	Medium	27%	-0.5%	3.8%
India	Medium	17%	-3.3%	-1.4%
Philippines	Low	20%	0.3%	4.4%

*Number shows total external debt as a % of GDP
Sources: PwC analysis, World Bank, IMF, Datastream

Focusing on the larger emerging markets, the three main findings are that:

- **'Fragile 5' now the 'Tender 2':** Of the so called 'Fragile 5' from 2013 (Brazil, South Africa, Indonesia, India and Turkey), PwC economists think that only South Africa and Turkey remain particularly vulnerable (see Table 1). Both economies have suffered relatively large capital outflows in the past 12 months and continue to run high current account deficits.

- **India in better shape but keep an eye on Brazil and Indonesia:** India, one of the original 'Fragile 5' economies, has improved its position over the past two years. While Brazil and Indonesia are not included amongst PwC's high vulnerability countries, they are worth keeping an eye on. Both are running sizeable current account deficits which indicate reliance on foreign lending. Also, both currencies have depreciated in double digit terms in the past 12 months.

- **Governments insulated from the rising dollar:** PwC analysis shows that most of the governments in the sample have a relatively modest ratio of external public debt to GDP. This suggests that emerging market governments have largely resisted the temptation to take advantage of cheap foreign credit (compared to the private sector) and are therefore less exposed to the effects of a strengthening dollar.

Finally, Richard Boxshall says: "The main takeaway for our clients is that US dollar credit is becoming more expensive and is likely to have consequential and sometimes amplified impacts on financing in many emerging economies."

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Notes:
The May edition of PwC's *Global Economy Watch* can be found at www.pwc.com/gew

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