GRAMERCY: EM WEEKLY

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FEATURING:

TURKEY | VENEZUELA | MEXICO | SOUTH AFRICA

Potential steps on sanctioning Turkey by U.S. Congress and/or the White House

Market Relevance: In December 2019, the Foreign Relations Committee of the U.S. Senate backed proposed legislation to sanction Turkey over its military offensive in Syria and urged President Trump to impose additional sanctions over Turkey's purchase of the S-400 Russian air defense system. The key question at the moment is if the Senate majority leader, Mitch McConnnell, will bring the Foreign Relations Committee's sanctions bill to the floor for a full Senate vote that will likely further exacerbate the simmering geopolitical tensions between the U.S. and Turkey, thus impacting Turkish assets. President Erdogan has threatened the closure of two strategic U.S. air bases in Turkey in the event of hostile U.S. behavior. Significant sanctions by Congress will certainly be seen in such light by the Turkish authorities.

Gramercy View: We remain of the view that material U.S. sanctions that will have a tangible impact on the fragile Turkish economy are unlikely to materialize under current conditions especially given President Trump's revealed preference to do everything in his power to preserve his good personal relationship with President Erdogan. As such, if President Trump is forced by Congress to finally enact sanctions over the S-400 issue, we believe he will pick the mildest five measures from a list of twelve options. However, we are concerned about possible market volatility caused by renewed geopolitical noise around the already very strained U.S.-Turkey diplomatic relationship and the potential reaction by President Erdogan in the event of any U.S. sanctions. Such measures will be seen as another sign of the ongoing rift in the relationship between Turkey, its western NATO allies and trading partners and should keep the geopolitical risk premium embedded in Turkish assets high for the foreseeable future.

Venezuela to elect new National Assembly managing board on January 5th

Market Relevance: The internal vote will determine whether National Assembly President, Juan Guaidó, will remain in his post and maintain control of the opposition led-National Assembly. While President Nicolás Maduro's formation of the Constituent Assembly in 2017 has essentially stripped the National Assembly of its power, Guaidó's ability to sustain support and unity among the opposition is key to maintain the international pressure on Maduro. Over 50 countries, including the U.S., currently recognize Guaidó as Venezuela's interim President until free and fair elections are held.

Gramercy View: We expect Guaidó to be re-elected as leader of the National Assembly as there are limited alternatives. However, Guaidó's inability to catalyze change has resulted in increased divisions among the opposition and a decline in his support from over 60% a year ago to just under 40% in November, according to local pollster, Datanalisis. Additionally, Maduro continues to bribe and detain opposition lawmakers. The more significant challenge will be the National Assembly election that is due to be held anytime between now and year-end with the specific date at the discretion of Maduro. There will likely be disagreement among the opposition over participation amid current conditions, further splintering the coalition. Meanwhile, Maduro's ability to manipulate the vote will likely cause the opposition to ultimately lose control over the National Assembly in 2020.

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Mexico inflation, consumer confidence, and vehicle sales for December

Market Relevance: The economy was weak for much of 2019 amid policy uncertainty and contracting investment. Inflation has declined steadily allowing the Central Bank to begin to loosen monetary conditions. However, sticky core inflation and persistent policy uncertainty, which poses risks to the peso, have kept the Central Bank from cutting rates faster.

Gramercy View: We expect inflation to continue to soften this month, although the 20% increase in minimum wages may pose some upside risk to future prints. Consumer confidence is likely to remain muted in the near-term but higher wages should provide some modest boost as 2020 progresses. Lastly, vehicle sales and broader economic activity should benefit on the margin from finalization of USMCA this month. However, broader questions regarding policy under President Andrés Manuel López Obrador will still likely weigh on investment.

South Africa high frequency economic data

Market Relevance: Growth has underperformed amid electricity shortages, waning confidence, and external headwinds. Fiscal and rating pressures continue to mount as low growth, state owned enterprise costs, and limited spending flexibility challenge any adjustment.

Gramercy View: We anticipate near-term activity data to remain bleak albeit with some possibility for modest cyclical pick-up in the event of global growth and external demand recovery. However, any improvement is unlikely to be enough to resolve the country's fiscal problem. Structural reform is needed, but political dynamics are unlikely to allow for much progress on this front. The ruling African National Congress remains divided, despite Ramaphosa's more business friendly mindset, and it is unclear at best if the strategy in place to resolve Eskom's issues will be successful in permanently reducing costs to the sovereign. Lastly, while there may be some political willingness to eventually address the overly cumbersome public sector wage bill, the government's ability to do so ahead of the next round of wage negotiations in 2021 is limited.

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