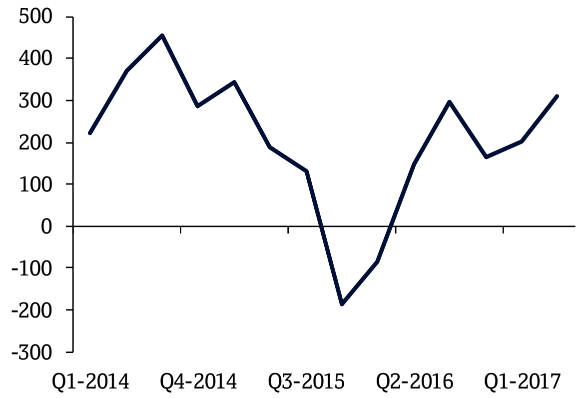
QNB Economics
economics@qnb.com
26 November 2017

Sources of global portfolio outflows

The world is awash with liquidity. After two years of subdued global capital flows, investors have flocked to both advanced economy (AE) and emerging market (EM) risk assets in 2017 with most of the foreign investment coming in the form of portfolio flows (including equity, debt and other investment which is mainly banking transactions). Driving this bullish risk appetite is a supportive macroeconomic backdrop. A broad-based acceleration in global growth, low policy rates and a weak USD. The question is, where is this liquidity coming from and have there been major changes in the sources of liquidity? We analyse the major trends in global portfolio outflows witnessed thus far in 2017 and discuss the outlook for 2018.

US & Euro Area portfolio outflows
(bn USD; three quarter moving average)



Sources: International Monetary Fund; individual country sources and QNB Economics

Euro Area and US investors accounted for the overwhelming majority of global foreign portfolio outflows in 2017, as they have historically. Combined outflows surged to over USD2.2tn in H1 2017 on an annualised basis compared to USD0.7tn for the full year in 2016. In the Euro Area, monetary policy is expected to remain accommodative until next year, keeping real interest rates negative and pushing investors overseas in the search for yield. As a result, the Euro Area will be a net exporter of capital to the world this year as it was in 2016.

Meanwhile in the US, outflows have also been strong despite the fact that the Fed has gradually tightened policy. Higher growth and appreciating currencies outside of the US have incentivised investors to put capital abroad. The US, like the Euro Area, is on pace to increase net portfolio outflows in 2017.

An important change in the global liquidity has been the lower outflows from Asia, particularly China. Portfolio outflows from Hong Kong, Singapore, South Korea and China were high in 2016 at USD700bn. This mainly reflected slower growth in China, prompting investors to move capital overseas. Portfolio outflows slowed to USD549bn on an annualised basis in H1 2017 as concerns eased about faltering Chinese growth and its negative impact on the region and as capital controls in China were tightened.

Looking ahead, we believe these patterns could change in 2018 as the global macroeconomic landscape shifts. In China, credit policy is tightening and growth is expected to slow in 2018. At the same time, the US Federal Reserve plans to hike its policy rate and reduce the size of its balance sheet and the European Central Bank plans to begin tapering its quantitative easing programme. These developments are likely lead to an increase in portfolio outflows from Asia while portfolio outflows from the US and Euro Area level off. Nonetheless, the US and Euro Area are likely to remain the largest providers of global liquidity in 2018.

QNB Economics Team:

Rory Fyfe
Acting Head of Economics
+974-4453-4643
* Corresponding author

Ali Jaffery*
Economist
+974-4453-4423

Nancy Fahim
Economist
+974-4453-4648

Abdulrahman Al-Jehani
Research Analyst - Trainee
+974-4453-4436