Emerging Market Debt Market Commentary

January 2020

Figure 1 - Emerging Market Debt Performance – As of 31 January 2020[1]

	1m	3m	6m	12m	3yrs	5yrs
In USD						
GBI-EM GD (EM Local Currency)	-1.29%	0.93%	2.08%	-1.29%	6.22%	5.78%
EMBI GD (EM Hard Currency)	1.52%	3.07%	3.66%	1.52%	11.85%	6.71%
CEMBI BD (EM Corporates)	1.54%	2.91%	4.57%	1.54%	11.79%	6.39%
In EUR						
GBI-EM GD (EM Local Currency)	-0.01%	1.60%	2.56%	-0.01%	9.98%	4.90%
EMBI GD (EM Hard Currency)	2.83%	3.77%	4.15%	2.83%	15.81%	5.82%
CEMBI BD (EM Corporates)	2.85%	3.61%	5.06%	2.85%	15.75%	5.51%

Past performance is not a guarantee of future results. Index returns reflect capital gains and losses, income, and the reinvestment of dividends. Performance returns for periods of less than one year are not annualized.

Emerging Market (EM) asset performance was mixed in the opening month of 2020 amid increased geopolitical and coronavirus-related risks. The early part of the month saw raised geopolitical tensions following the US killing of Iran's General Soleimani. Iran retaliated by firing missiles at Iraqi air bases housing US troops, but the situation did not escalate any further. The latter part of the month was dominated by investor concerns around the potential impact of the Chinese coronavirus outbreak on manufacturing, transportation, tourism and retail sales, as a result of an outbreak of coronavirus in China. The rapid spread of the virus turned investor risk sentiment slightly negative and stoked a rally in safe-haven assets.

[1] Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 31 December 2019.

Local Currency Market Highlights[2]

Figure 2 - Key return drivers of EM local government bond markets in USD[1]

GBI-EM GD (EM Local Currency)	Monthly Return	3 Month Return	YTD Return
In EUR			
Total Return (in €)	**-1.29%**	**0.93%**	**-1.29%**
FX Return (vs €)	-2.67%	-1.16%	-2.67%
Price Return (Local currency)	0.96%	0.69%	0.96%
Interest Return (Local currency)	0.49%	1.43%	0.49%
In USD			
Total Return (in $)	**-0.01%**	**1.60%**	**-0.01%**
FX Return	-1.46%	-0.51%	-1.46%
Price Return	0.96%	0.69%	0.96%
Interest Return	0.49%	1.43%	0.49%

EM Local Currency debt generated a negative return of -1.3% in US dollar terms in January, as measured by the JP Morgan GBI-EM Global Diversified Index; the foreign exchange (FX) component drove the decline, detracting -2.7%. On the inflation front, EM forecasts have been moving higher. These have been largely driven by supply-side food price pressures, but investors are concerned that this trend might result in some central banks bringing their easy monetary policies to an end. Recent EM economic activity indicators haven't pointed to any significant downtrends, although market focus is on upcoming data releases that would reflect the initial impact from the virus outbreak.

Details of key performance drivers are highlighted in Figure 3 below.

Figure 3 - Best and worst performers across EM local government bond markets in USD*

January 2020	Country	Total Return USD (%)	Bond Return (%)	FX Return (%)	Index Weight	Index Impact (BP)**
GBI-EM GD		**-1.29**	**1.43**	**-2.67**		
Top 5 Performers	Turkey	5.84	6.44	-0.55	3.7%	21
	Indonesia	3.62	1.93	1.66	10.0%	36
	Uruguay	2.30	2.71	-0.40	0.2%	0
	Mexico	1.74	1.92	-0.19	10.0%	17
	Malaysia	1.28	1.46	-0.18	6.4%	8
Bottom 5 Performers	Hungary	-3.56	-0.26	-3.31	3.7%	-13
	Thailand	-3.63	1.15	-4.72	9.5%	-34
	Brazil	-4.70	1.24	-5.87	10.0%	-47
	South Africa	-5.73	1.12	-6.78	9.1%	-52
	Chile	-6.84	-0.80	-6.09	2.6%	-18

Source: State Street Global Advisors, JP Morgan as at 31 January 2020. Past performance is not a guarantee of future results. Index returns reflect capital gains and losses, income, and the reinvestment of dividends.
* Country and currency performance of JP Morgan GBI-EM Global Diversified Index
**Index impact is calculated by multiplying the period end weight by total return.

[2]The returns stated in this section are based on the local currency returns as per JP Morgan GBI-EM Global Diversified. Returns calculated in USD.

Chile was the worst performer in January returning -6.8% and detracting -18 bps from the overall index return. Chilean assets continued to sell off amid ongoing social unrest, the worst that it has experienced for decades, and amid the potential for new demands from protestors. Investors believe that the implementation of progressive tax reform is unlikely to fulfill the demands of the new pension reform, and, consequently, gross public debt is expected to increase to ~40% of GDP, which would hurt growth potential. Chile, a leading copper producer, is also affected by the sharp fall in copper prices and a tumult in global commodity trade in the wake of the coronavirus outbreak; Chinese buyers are asking Chilean miners to delay shipments due to port shutdowns.

South Africa was the second-worst performer (-5.7%) and the biggest detractor from index returns (-52 bps), with almost all of it from the FX component. The increasing regularity of power outages by state-owned electricity company Eskom due to system constraints, and the concomitant decline in the country's manufacturing PMI down to 46.5 in January hurt investor confidence.

Brazil was among the worst performers returning -4.7% and detracting -47 bps from index returns. Market expectations of a 25 bps cut in the Selic rate, and a delay in expected policy normalization from the central bank has weighed in on the Brazilian currency through further erosion of carry. Furthermore, a weak domestic growth environment and some US-China deal implications may lead to a diversion of trade (such as soybean exports) away from Brazil.

Thailand was a laggard, returning -3.6% in the month, while also detracting -34 bps from overall index returns. Thailand's weak economy has experienced a marked slowdown in GDP growth, and the country also stands out as one of the more vulnerable economies to the coronavirus outbreak due to its reliance on tourism. This has all weighed on the currency.

Turkey was the best performer (+5.9%) and a significant contributor to index returns (+21 bps), with almost all contribution coming from the bond component. The Central Bank of the Republic of Turkey cut its policy rate by 75 bps to 11.25% in the month. Even though the rate cut was in line with expectations, market participants believe that the bank's easing cycle is not over yet and an additional 150 bps of cuts are anticipated in the first half of 2020 – the potential impact on FX stability will be a factor for future meetings. It remains to be seen whether Turkey would get continued investor support, given it might lose its current real yield advantage, against the backdrop of continued easing and a pick-up in inflation.

Indonesia was the second-best performer (+3.6%) and the largest contributor to index returns (+36 bps). Bank Indonesia mentioned that the country's economic cycle has bottomed out and is picking up again, with both external and domestic conditions improving. The central bank reiterated that it expects GDP growth to improve to 5.1-5.5% in 2020 from 5.1% in 2019, while emphasizing that it still has room to cut the policy rate further to support economic growth. Indonesia's exports, which have been a cause of concern since 2018, showed signs of improvement, growing by +1.3% in December (on a year-on-year basis) after 13 months of decline. Inflation has remained benign, easing to 2.68% y/y in January from 2.7% in December.

Mexico was among the best performers (+1.7%) and a significant contributor to index returns (+17 bps). Preliminary reports showed GDP growth to be flat in the final quarter of 2019, which was better than expectations. Contraction in industrial output (-1.0%) and primary activities (-0.9%) offset an expansion of 0.3% in services. Market participants expect a 25 bps rate cut from Banxico at its February meeting to provide ongoing support to the economy; inflation at 3.5% y/y remains within Banxico's target range of 3% (+/-1%).

Hard Currency Market Highlights[3]

Figure 4 - Key return drivers of EM hard currency government bond markets in USD[1]

EMBI GD (EM Hard Currency)	Monthly Return	3 Month Return	YTD Return
Total Return	**1.52%**	**3.07%**	**1.52%**
Spread Return	-1.54%	1.24%	-1.54%
Treasury Return	3.11%	1.81%	3.11%
IG Sub-Index	2.29%	3.16%	2.29%
HY Sub-Index	0.64%	2.99%	0.64%

EM Hard currency sovereign debt returned 1.52% in January, as measured by the JP Morgan EMBI Global Diversified Index. Investor concerns about the potential economic implications of the coronavirus outbreak and EM valuations at tight levels have challenged the benign risk-environment entering into 2020. In addition to a deterioration in the global risk backdrop, discouraging news events around idiosyncratic high yield (HY) EM such as Argentina, Lebanon and Ecuador led to an overall widening of EM HC sovereign spreads. However, the potent rally in the underlying treasury component more than offset the spread-widening, leading to a positive total return overall.

Figure 5 - Best and worst performers across EM hard currency government bond markets*

January 2020	Country	Total Return (%)	Spread Return (%)	TSY Return (%)	Index Weight	Index Impact (BP)**
EMBI Global Diversified		-0.48	-0.09	-0.39		
Top 5 Performers	Suriname	10.74	8.64	1.94	0.1%	1
	Tajikistan	8.13	6.02	1.99	0.1%	1
	Venezuela	6.16	5.83	0.32	0.0%	0
	Turkey	5.22	2.63	2.52	3.5%	18
	Uruguay	4.18	-1.05	5.28	2.4%	10
Bottom 5 Performers	Iraq	-1.28	-2.52	1.28	0.5%	-1
	Bolivia	-1.59	-3.30	1.77	0.3%	0
	Ecuador	-5.49	-7.13	1.76	2.1%	-11
	Argentina	-8.09	-9.80	1.91	1.4%	-11
	Lebanon	-16.47	-17.57	1.34	0.9%	-14

Source: State Street Global Advisors, JP Morgan as at 31 January 2020. Past performance is not a guarantee of future results. Index returns reflect capital gains and losses, income, and the reinvestment of dividends. * Country and currency performance of JPM EMBI Global Diversified Index **Index impact is calculated by multiplying the period end weight by total return.

Suriname, **Tajikistan** and **Venezuela** had strong total return numbers of +10.7%, +8.1% and +6.2%, but with negligible impact on index returns, given their respective weights.

Turkey performed well, returning +5.2%, and contributing 18 bps to the index return. Turkey spreads continue to benefit from the ceasefire in northern Syria, reduced tail risks, and as high-frequency indicators point to early signs of an economic rebound due to the central bank's extensive policy stimulus in 2019.

[3] The returns stated in this section are based on the hard currency returns according to JP Morgan EMBIG Diversified. Returns calculated in USD.

Uruguay was among the best performers, returning +4.2% and contributing 10 bps to index returns. Higher probability of a much-needed fiscal consolidation from the Lacalle Pou administration and an improved growth outlook, preventing a sovereign rating downgrade in the near-term, have supported spreads.

Lebanon was the worst performer, returning -16.5% in the month. This was also the largest detractor from index returns (-14 bps). As one of the world's most indebted countries with debt at ~150% of GDP, Lebanese credit spreads have continued to soar after months of economic slowdown and a dollar liquidity squeeze that has pressured the government's capacity to service its debt. Market participants believe that the new government's reform plans will be constrained by the terms of the budget prepared before the October protests, which could slow down reform momentum in the near term.

Argentina was also a poor performer, returning -8.1% and detracting -11 bps from index returns. Spreads widened as the likelihood of a sovereign default increased after the provincial authorities were not able to garner enough support for a four-month emergency maturity extension.

Ecuador also featured as a weak performer in returning -5.5% and detracting from index returns (-11 bps). The government was struggling to narrow its fiscal deficit after violent protests in early October forced it to backtrack on a plan to scrap fuel subsidies and implement spending cuts. Uncertainty over the next disbursement from the International Monetary Fund (IMF) has increased, as the country failed to meet the organization's international reserves target for 2019.

Hard Currency Corporate Bond Markets[4]

Figure 6 - Key return drivers of EM hard currency corporate bond markets[1]

CEMBI BD (EM Corporates)	Monthly Return	3 Month Return	YTD Return
Total Return	**1.54%**	**2.91%**	**1.54%**
Spread Return	-0.35%	1.61%	-0.35%
Treasury Return	1.90%	1.29%	1.90%
IG Sub-Index	1.59%	2.24%	1.59%
HY Sub-Index	1.48%	3.84%	1.48%

[4] The returns stated in this section are based on the hard currency returns according to JP Morgan CEMBIB Diversified. Returns calculated in USD

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