Emerging Market Debt Market Commentary

August 2021

Emerging market debt (in USD terms) posted a modestly positive overall return in August as worries related to the possibility of early monetary policy tightening by the US Federal Reserve eased following the Fed chairman's dovish speech at the central bank's annual Jackson Hole symposium. Concerns related to the Delta variant have also abated somewhat, with hospitalization and case rates in many countries starting to slow. With global growth remaining strong, even as it has shown signs of peaking, and commodity prices stabilising at reasonably high levels, markets saw the return of a cyclical recovery trade in EM – this was especially evident in the final week of August, with relative outperformance of high-beta, and commodity-linked currencies.

Figure 1 - Emerging Market Debt Index Returns – As of 31 August, 2021

	1m	3m	6m	YTD	12m	3yrs	5yrs
In USD							
GBI-EM GD (EM Local Currency)	0.77%	-0.88%	0.70%	-3.05%	4.14%	5.78%	3.18%
EMBI GD (EM Hard Currency)	0.98%	2.15%	4.50%	0.73%	4.59%	6.93%	4.41%
CEMBI BD (EM Corporates)	0.71%	1.77%	2.38%	2.21%	6.24%	7.71%	5.38%
In EUR							
GBI-EM GD (EM Local Currency)	1.23%	2.66%	3.55%	0.49%	5.51%	5.27%	1.99%
EMBI GD (EM Hard Currency)	1.44%	5.41%	7.45%	4.41%	5.97%	6.41%	3.20%
CEMBI BD (EM Corporates)	1.16%	5.02%	5.28%	5.95%	7.63%	7.19%	4.16%
In GBP							
GBI-EM GD (EM Local Currency)	1.80%	2.38%	2.30%	-3.70%	1.32%	3.78%	2.17%
EMBI GD (EM Hard Currency)	2.02%	5.23%	6.16%	0.05%	1.76%	4.91%	3.38%
CEMBI BD (EM Corporates)	1.74%	4.85%	4.01%	1.52%	3.36%	5.67%	4.34%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 31 August, 2021. 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.

Figure 2: Key EM and Macro levels as of 31 August, 2021

Item	Δ 1 Month	Δ 3 Months	Δ YTD	Current Level
GBI-EM GD Yield	7 bps	4 bps	77 bps	4.99%
EMBI GD Yield	-7 bps	-14 bps	26 bps	4.81%
EMBI GD Spread	-12 bps	11 bps	-8 bps	343 bps
CEMBI BD Yield	-7 bps	-14 bps	17 bps	4.21%
CEMBI BD Spread	-11 bps	2 bps	-16 bps	306 bps
CDX.EM 5y	-12 bps	-8 bps	1 bps	152 bps
10y UST	9 bps	-29 bps	40 bps	1.31%
Dollar Index (DXY)	0.49%	3.11%	2.99%	
DOW 30	1.22%	2.41%	15.53%	35,361
Oil (WTI)	-7.37%	3.29%	41.18%	$68.5

Source: JP Morgan, Bloomberg as of 31 August, 2021

Local Currency Market Highlights

Figure 3 - Key return drivers of EM local government bond markets

GBI-EM GD (EM Local Currency)	Monthly Return	3 Month Return	YTD Return
In USD			
Total Return (in $)	**0.77%**	**-0.88%**	**-3.05%**
FX Return (vs $)	0.64%	-1.85%	-2.16%
Price Return (Local currency)	-0.28%	-0.30%	-4.25%
Interest Return (Local currency)	0.41%	1.27%	3.37%
In EUR			
Total Return (in €)	**1.23%**	**2.66%**	**0.49%**
FX Return (vs €)	1.09%	1.69%	1.38%
In GBP			
Total Return (in €)	**1.80%**	**2.38%**	**-3.70%**
FX Return (vs €)	1.67%	1.41%	-2.82%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 31 August, 2021. 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.

EM local currency debt returned 0.77% in USD terms in August, as measured by the JP Morgan GBI-EM Global Diversified Index. Differentials in performance between countries generally related to fiscal and institutional deterioration risks (Peru, Chile) with political uncertainties also playing a part (particularly in Latin America). Recent growth and inflation prints and how much investors perceive their central banks to be behind/ahead of the tightening curve, were also factors in the month.

Figure 4 - Best and worst performers across EM local government bond markets in USD*

August 2021	Country	Total Return USD (%)	Bond Return (%)	FX Return (%)	Index Weight	Index Impact (bps)**
GBI-EM GD		**0.77**	**0.14**	**0.63**		
Top 5 Performers	Uruguay	3.7	0.7	2.9	0.1%	0
	Dominican Republic	3.4	3.3	0.1	0.1%	0
	Colombia	3.4	0.6	2.7	4.6%	15
	South Africa	2.9	1.7	1.2	8.0%	23
	Indonesia	2.9	1.4	1.4	9.9%	28
Bottom 5 Performers	Peru	-0.5	0.3	-0.8	1.9%	-1
	Brazil	-0.6	-1.1	0.5	8.2%	-5
	Czech Republic	-1.0	-0.8	-0.2	4.5%	-4
	Romania	-1.6	-0.8	-0.9	3.0%	-5
	Chile	-3.6	-1.6	-2.0	2.1%	-8

Source: State Street Global Advisors, JP Morgan as at 31 August, 2021. 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.

Uruguay (which leads vaccination rates in LatAm, while improving economic indicators have underpinned currency outperformance) and **Dominican republic** (with a decline in both headline and core inflation since May bolstering its bond rally) performed well, but had minimal impact on index returns due to their low weights.

Colombia performed well, most of it from the strengthening peso, amid expectations for a recovery in oil output and exports; a reacceleration in economic activity was evident following widespread strikes in the second quarter. Domestic demand has shown signs of recovery as well, led by industrial goods and consumption.

South Africa was a good performer, contributing 23 basis points (bps) to index returns. The rally in the rand was fueled by a bounce in commodity prices and a data revision showing South Africa's debt burden to be less than previously thought. Bond gains were also supported by recent soft inflation prints that have reduced expectations of near-term tightening pressures.

Indonesia performed well and was the top contributor (+28 bps) to index returns, with both rates and FX components contributing equally. Second quarter GDP returned to expansion in year-on-year terms (+7.1%), reflecting easing social distancing measures and improving domestic demand, as well as a favorable base effect. Bank Indonesia left the 7-day reverse repo rate unchanged at 3.50% at its August meeting, in line with consensus expectations. The central bank downplayed the impact of potential tapering by the US Fed and reiterated its focus on keeping the exchange rate stable amid low CPI inflation to support the economic recovery.

Chile underperformed in returning -3.6% over the month. Bonds sold off on expectations that the central bank could accelerate the pace of interest rate hikes against the backdrop of economic activity data continuing to surprise to the upside, expansion of the fiscal stimulus and the country's CPI inflation print coming in higher than expected in July, at 0.8% month-on-month versus the consensus expectation of 0.4%. Political and institutional risks, as well as low carry, have weighed on the Chile peso.

Central and Eastern European (CEE) countries **Romania** and **Czech Republic** experienced modest underperformance on the back of higher inflation prints, with markets pricing in risks skewed towards more rate hikes.

Brazil and **Peru** also modestly underperformed, with political tensions and concerns around fiscal credibility weighing on Brazil. Worries about a strong leftist bias in the new administration increasing political tensions and weakening the institutional framework potentially leading to rating downgrades weighed on Peru's performance.

Hard Currency Market Highlights

Figure 5 - Key return drivers of EM hard currency government bond markets in USD

EMBI GD (EM Hard Currency)	Monthly Return	3 Month Return	YTD Return
Total Return	**0.98%**	**2.15%**	**0.73%**
Spread Return	1.34%	-0.18%	2.74%
Treasury Return	-0.36%	2.33%	-1.96%
IG Sub-Index	0.78%	2.70%	-1.22%
HY Sub-Index	1.18%	1.52%	2.97%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 31 August, 2021. 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.

EM hard currency (HC) sovereign debt delivered a return of 0.98% in August, as measured by the JP Morgan EMBI Global Diversified Index. Spreads tightened by 12 bps over the month, offsetting the previous month's widening, but a sell-off in underlying rates eroded part of the total return. Even as re-opening and vaccination progresses, along with a historic SDR (special drawing rights) allocation announcement provides a positive backdrop for EM, supply is likely to pick up again soon – September is an active month for primary market issuance of sovereign HC bonds.

Figure 6 - Best and worst performers across EM hard currency government bond markets*

August 2021	Country	Total Return (%)	Spread Return (%)	Treasury Return (%)	Index Weight	Index Impact (bps)**
EMBI Global Diversified		**0.98**	**1.35**	**-0.36**		
Top 5 Performers	Zambia	20.4	20.5	-0.1	0.3%	6
	Argentina	6.3	6.7	-0.4	1.2%	8
	Tunisia	4.5	4.6	-0.1	0.1%	1
	Lebanon	4.5	4.5	0.0	0.2%	1
	Ecuador	3.3	3.7	-0.4	1.5%	5
Bottom 5 Performers	Slovakia	-0.2	-0.2	0.0	0.2%	0
	Brazil	-0.2	0.0	-0.3	3.0%	-1
	El Salvador	-0.3	-0.1	-0.2	0.8%	0
	Tajikistan	-1.0	-0.9	-0.2	0.1%	0
	Belize	-1.6	-1.3	-0.3	0.0%	0

Source: State Street Global Advisors, JP Morgan as at 31 August, 2021. 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.

The International Monetary Fund (IMF) on August 23 announced the largest allocation of Special Drawing Rights (SDRs) ever, of $650 billion, with $275 billion going to emerging and developing countries – with some low income countries receiving as much as 6% of GDP. This has led frontier and high yielding EM countries' bonds to rally. **Zambia** further benefited from investor optimism that opposition leader Hakainde Hichilema would bring a resolution to the country's debt troubles after a landslide election win. Markets view Hichilema's plans to put Zambia on a more sustainable fiscal footing and engage with investors as being more market-friendly than those of the incumbent.

Belize, **Tajikistan** and **El Salvador** recorded modest relative underperformance – mostly on idiosyncratic news flow. Belize's prime minister dismissed the central bank governor over integrity and operational autonomy concerns, while some institutional investors reduced their holdings of Tajikistan bonds around concerns that the likely exodus of refugees from Afghanistan could strain the finances of neighbouring countries. Meanwhile, El Salvador was downgraded by Moody's to Caa1 from B3 over fears of weakened governance and as investors exhibited nervousness on the country's plan to adopt cryptocurrency as legal tender.

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