

Emerging Market Debt Market Commentary

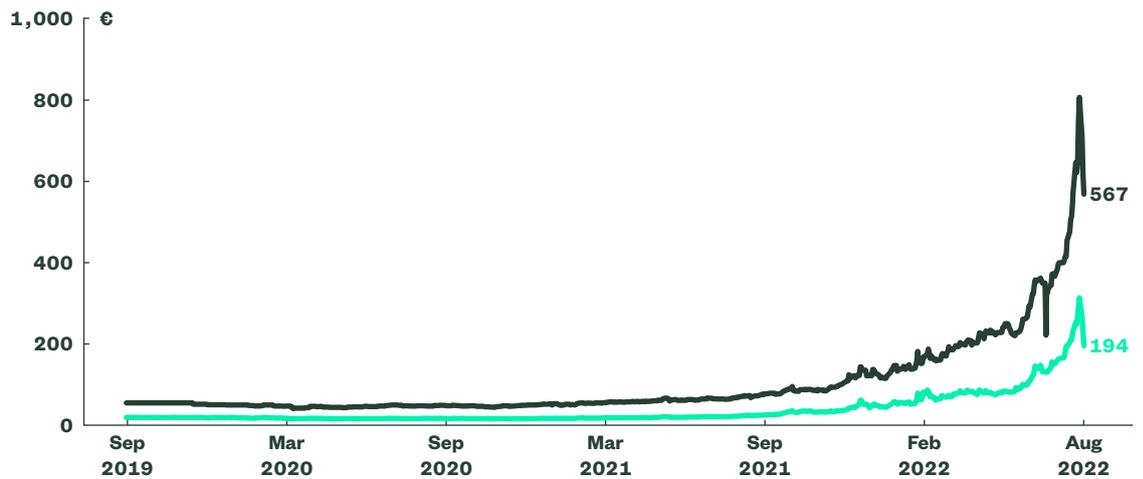
Chart of the Month: European Power and Gas Prices Surge

There was a significant increase in European power and gas prices in August as Russia again reduced gas supplies. Notwithstanding some easing in prices near month-end, this has further heightened uncertainty around the economic outlook as central banks continue to raise interest rates to tackle sustained high inflation.

Figure 1
Markets Reflect
Spike in Energy
Prices

Germany Year Ahead
Electricity Price (€/Mwh)

Dutch Natural Gas
Jan-23 Futures
Contract Price (€/Mwh)



Source: Bloomberg Finance L.P., as of 31 August 2022. Past performance is not a reliable indicator of future performance.

EMD Commentary — August 2022

Emerging market debt (in USD terms) recorded a modestly negative move overall in August. Worries related to slowing global activity, hawkish central bank policies amid continued elevated headline inflation, and a significant surge in European power prices outweighed the positive sentiment seen early in the month. We see some technical anchors, particularly in EM hard currency (HC) given depressed valuations, generous risk premia and a tentative turn in flows — there were positive flows of +\$1.4 billion in HC in August compared to -\$2.7 billion in local currency (LC) flows, according to JP Morgan. However, near-term uncertainty remains high and the outlook has become more fragile due to a number of external shocks and idiosyncratic factors.

Figure 2
**Emerging Market
Debt Index Returns —
As of 31 August 2022**

	1m (%)	3m (%)	6m (%)	YTD (%)	12m (%)	3yrs (%)	5yrs (%)
In USD							
GBI-EM GD (EM Local Currency)	-0.14	-4.31	-9.89	-14.40	-19.43	-5.20	-3.02
EMBI GD (EM Hard Currency)	-0.94	-4.41	-10.55	-18.78	-20.82	-5.24	-1.33
CEMBI BD (EM Corporates)	0.18	-1.87	-6.89	-12.88	-13.99	-1.05	1.14
In EUR							
GBI-EM GD (EM Local Currency)	1.26	1.94	0.65	-3.19	-5.42	-2.28	0.28
EMBI GD (EM Hard Currency)	0.44	1.83	-0.08	-8.15	-7.04	-2.33	2.04
CEMBI BD (EM Corporates)	1.59	4.55	4.00	-1.47	0.97	1.99	4.59
In GBP							
GBI-EM GD (EM Local Currency)	4.43	3.64	3.91	-0.36	-4.71	-3.75	-1.02
EMBI GD (EM Hard Currency)	3.59	3.53	3.15	-5.46	-6.34	-3.79	0.71
CEMBI BD (EM Corporates)	4.77	6.29	7.37	1.41	1.73	0.46	3.23

Source: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 August 2022. 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 3
**Key EM and Macro Levels
As of 31 August 2022**

Item	Δ 1 Month	Δ 3 Months	Δ YTD	Current Level
GBI-EM GD Yield	5 bps	13 bps	117 bps	6.89%
EMBI GD Yield	18 bps	92 bps	308 bps	8.37%
EMBI GD Spread	-31 bps	53 bps	133 bps	502 bps
CEMBI BD Yield	12 bps	61 bps	241 bps	6.99%
CEMBI BD Spread	-43 bps	19 bps	59 bps	371 bps
CDX.EM 5y	0 bps	55 bps	138 bps	327 bps
10y UST	54 bps	35 bps	168 bps	3.19%
Dollar Index (DXY)	2.64%	6.83%	13.62%	—
DOW 30	-4.06%	-4.49%	-13.29%	31,510
Oil (WTI)	-9.20%	-21.91%	19.07%	\$ 89.55

Source: JP Morgan, Bloomberg Finance L.P., as of 31 August 2022. Past performance is not a guarantee of future results. Index returns reflect capital gains and losses, income, and the reinvestment of dividends.

Local Currency Market Highlights

EM local currency debt returned -0.14% in USD terms in August, as measured by the JP Morgan GBI-EM Global Diversified Index. Differentials in performance between countries have generally been related to commodity exposures, inflation expectations, and vulnerability to geopolitical risks. Latin American (LatAm) countries have held up comparatively well as growth has proved resilient in the region amid robust domestic demand and positive terms of trade — a notable contrast with the experience of much of the rest of the world. Meanwhile, in the Central and Eastern Europe region (ex-Turkey), energy dependence on Russia has weighed heavily on performance.

Figure 4
**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 \$)	-0.14	-4.31	-14.40
FX Return (vs \$)	-0.62	-5.61	-6.32
Price Return (Local Currency)	0.02	-0.07	-11.35
Interest Return (Local Currency)	0.46	1.38	3.27
In EUR			
Total Return (in €)	1.26	1.94	-3.19
FX Return (vs €)	0.78	0.64	4.88
In GBP			
Total Return (in £)	4.43	3.64	-0.36
FX Return (vs £)	3.95	2.34	7.72

Source: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 August 2022. 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 5
**Best and Worst
Performers Across
EM Local Government
Bond Markets in USD***

August 2022	Country	Total Return USD (%)	Bond Return (%)	FX Return (%)	Index Weight (%)	Index Impact (bps)**
GBI-EM GD		-0.14	0.48	-0.62	—	—
Top 5 Performers	Turkey	14.9	16.6	-1.8	1.0	15
	Dominican Republic	4.7	1.8	2.9	0.1	1
	Peru	4.2	1.9	2.4	2.4	10
	Brazil	2.8	2.4	0.3	10.0	28
	Romania	2.3	2.0	0.4	3.6	8
Bottom 5 Performers	China	-1.4	0.9	-2.3	10.0	-14
	South Africa	-1.9	0.4	-2.3	10.0	-19
	Hungary	-2.5	-1.5	-1.0	2.9	-7
	Poland	-3.1	-1.9	-1.2	6.8	-21
	Czech Republic	-3.2	-2.2	-0.9	4.9	-16

Source: State Street Global Advisors, Bloomberg, JP Morgan, as at 31 August 2022. 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 average weight by total return.

Turkey was the best performer, driven by local rates returns following an unexpected policy rate cut of 100 basis points (bps) to 13.0% at the central bank's August policy meeting. On the economic front, second quarter GDP growth came in at 7.6% year-on-year (y/y), driven largely by private consumption. This was slightly better than Bloomberg consensus expectations of 7.4% and makes it one of the fastest growing economies in the G-20. Significant risks of a policy misstep remain though, with inflation soaring to a 24-year high of close to 80%, and with the Turkish lira trading near a record low.

Peruvian assets performed well despite political noise around a third attempt to impeach President Castillo. The country registered some moderation in capital outflows from Q2 2022 and recorded solid GDP growth of 3.54% in the first half of the year; this was driven by trade and manufacturing and improved fiscal metrics due to lack of spending execution, while inflation seems to have stabilized at high levels.

While **Brazil's** monetary policy committee raised its benchmark Selic rate by 50bps to 13.75% in line with consensus, its statement was more dovish than anticipated. This led to a modest bond rally as market participants began to price in an end to the country's most aggressive tightening cycle since 1999. Inflation slowed in July and August as well, with the annual IPCA benchmark inflation rate falling from 11.9% y/y in June to 8.9% by August.

The Central and Eastern European (CEE) countries of **Czech Republic, Poland, and Hungary** underperformed against the backdrop of the ongoing energy crisis that is expected to markedly slow economic growth in the region. Even though these countries delivered reasonably strong growth in Q2, recent purchasing managers' index (PMI) reports have reflected a notable slowdown, with index readings indicating contracting activity in the Czech Republic and Poland for a third and fourth month in a row, respectively. Hungary said it would amend some laws criticized by the European Commission if agreement on the disbursement of EU funds can be reached, and are awaiting a response from the EC on whether this meets Brussels' demands on respecting the rule of law.

South Africa was also among the underperformers amid ongoing power outages that are expected to slow mining, manufacturing and construction activity. While local fuel prices are moderating, food price inflation is considered likely to remain persistent over 10% y/y, and broader price pressures in services and other goods components also remain.

Hard Currency Market Highlights

EM hard currency (HC) sovereign debt delivered a return of -0.94% in August, as measured by the JP Morgan EMBI Global Diversified Index. Spreads tightened by 31bps over the month, but a sell-off in underlying rates eroded all spread returns. A volatile month saw markets moving away from expectations of a more dovish US Federal Reserve to repricing for a more hawkish stance emerging from the central bank's annual Jackson Hole Economic Symposium. Weaker global activity data, increasing energy risks in Europe, and seasonally-low liquidity levels contributed to spreads hardening from the middle of the month, despite supportive commodity prices.

Figure 6
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	-0.94	-4.41	-18.78
Spread Return	2.27	-2.35	-8.77
Treasury Return	-3.14	-2.11	-10.97
IG Sub-Index	-1.89	-1.89	-18.54
HY Sub-Index	0.08	-6.99	-19.04

Source: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 August 2022. 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 7
Best and Worst
Performers Across
EM Hard Currency
Government
Bond Markets*

August 2022	Country	Total Return (%)	Spread Return (%)	Treasury Return (%)	Index Weight (%)	Index Impact (bps)**
EMBI Global Diversified		-0.94	2.27	-3.14	—	—
Top 5 Performers	Pakistan	17.1	19.6	-2.1	0.9	15
	Tunisia	12.3	13.4	-1.0	0.1	1
	Egypt	10.3	13.0	-2.4	2.5	25
	Lebanon	10.0	10.0	0.0	0.2	2
	Sri Lanka	9.9	11.2	-1.1	0.6	6
Bottom 5 Performers	Hungary	-5.3	-2.4	-2.9	1.7	-9
	Ukraine	-12.9	-11.5	-1.6	0.6	-8
	Venezuela	-13.0	-13.0	0.0	0.0	0
	Ghana	-13.9	-12.1	-2.0	1.0	-13
	Ecuador	-14.3	-11.6	-3.0	1.1	-16

Source: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 August 2022. 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 average weight by total return.

Pakistan bonds rallied after the International Monetary Fund (IMF) approved the immediate disbursement of a \$1.1bn bailout package near the end of the month, ensuring the country avoided a default on its foreign debt. Market reaction was positive as the IMF also agreed to extend the program by a year and increase the total funding by \$940 million at current exchange rates.

Egypt spreads recovered by 250bps from extreme distressed levels as the prime minister said on 22 August that the government is nearing an agreement with the IMF on a new loan. The country, which has a debt-to-GDP ratio of 95% and is a major food importer, has been impacted by the sharp increase in grain prices fueled by Russia's invasion of Ukraine.

Ecuador's bonds continued to sell off on risks that liabilities due to ongoing arbitration cases between the country and foreign oil and gas firms could add to financing needs. The sovereign's accounts in Luxembourg were frozen recently for non-payment of a \$374m settlement to French oil firm Perenco. Ongoing social and political instabilities remain, hindering the incumbent administration's ability to carry out its liberal economic agenda.

Ghana bonds performed poorly on concerns about the impact of the global growth slowdown on its cocoa exports. Fitch downgraded Ghana's long-term foreign currency ratings by two notches to CCC on 10 August, and the other two main rating agencies already have it at CCC+ and Caa1. Annual inflation in Ghana rose in July to 31.7%, its highest level since November 2003, and the country's central bank increased its benchmark interest rate by the biggest margin on record to 22% in an effort to combat price pressures.

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* Pensions & Investments Research Center, as of December 31, 2021.

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