Emerging Market Debt Market Commentary

October 2021

Emerging market debt (in USD terms) recorded modest negative returns as rising inflation trends across the world have prompted markets to price in an earlier-than-expected hiking cycle in the US and several other major economies. In addition to rising inflation (driven by high energy prices and supply chain disruptions), global and EM growth coming slightly off their peaks and lingering fiscal and political risks – particularly in Latin America (LatAm) – contributed to weakness over the month. Local and hard currency funds registered outflows in October of -$1.6bn and -$1.4bn, respectively.

Figure 1 - Emerging Market Debt Index Returns – As of 29 October, 2021

	1m	3m	6m	YTD	12m	3yrs	5yrs
In USD							
GBI-EM GD (EM Local Currency)	-1.33%	-3.98%	-3.19%	-7.62%	0.84%	3.89%	1.96%
EMBI GD (EM Hard Currency)	0.02%	-1.09%	1.11%	-1.34%	4.41%	6.43%	4.15%
CEMBI BD (EM Corporates)	-0.46%	-0.43%	1.27%	1.06%	5.27%	7.18%	5.11%
In EUR							
GBI-EM GD (EM Local Currency)	-1.18%	-1.61%	0.70%	-2.33%	1.50%	3.16%	0.86%
EMBI GD (EM Hard Currency)	0.17%	1.35%	5.18%	4.32%	5.10%	5.69%	3.03%
CEMBI BD (EM Corporates)	-0.32%	2.03%	5.34%	6.85%	5.97%	6.43%	3.98%
In GBP							
GBI-EM GD (EM Local Currency)	-2.94%	-2.61%	-2.22%	-7.87%	-4.88%	1.48%	-0.38%
EMBI GD (EM Hard Currency)	-1.61%	0.33%	2.13%	-1.61%	-1.51%	3.97%	1.77%
CEMBI BD (EM Corporates)	-2.09%	0.99%	2.29%	0.78%	-0.70%	4.70%	2.71%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 29 October, 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 29 October, 2021

Item	Δ 1 Month	Δ 3 Months	Δ YTD	Current Level
GBI-EM GD Yield	35 bps	73 bps	143 bps	5.65%
EMBI GD Yield	2 bps	27 bps	59 bps	5.14%
EMBI GD Spread	2 bps	3 bps	7 bps	358 bps
CEMBI BD Yield	8 bps	22 bps	45 bps	4.49%
CEMBI BD Spread	4 bps	-7 bps	-11 bps	310 bps
CDX.EM 5y	4 bps	21 bps	34 bps	186 bps
10y UST	6 bps	33 bps	64 bps	1.55%
Dollar Index (DXY)	-0.11%	2.11%	4.65%	
DOW 30	5.84%	2.53%	17.03%	35,820
Oil (WTI)	11.38%	13.01%	72.24%	$ 83.57

Source: JP Morgan, Bloomberg as of 29 October, 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 $)	**-1.33%**	**-3.98%**	**-7.62%**
FX Return (vs $)	0.08%	-1.63%	-4.41%
Price Return (Local currency)	-1.82%	-3.62%	-7.46%
Interest Return (Local currency)	0.42%	1.28%	4.26%
In EUR			
Total Return (in €)	**-1.18%**	**-1.61%**	**-2.33%**
FX Return (vs €)	0.22%	0.74%	0.88%
In GBP			
Total Return (in €)	**-2.94%**	**-2.61%**	**-7.87%**
FX Return (vs €)	-1.54%	-0.26%	-4.67%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 29 October, 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 -1.33% in US dollar terms in October, as measured by the JP Morgan GBI-EM Global Diversified Index, with almost all of that attributable to currency weakness. The underlying drivers of returns were quite diverse, ranging from policy uncertainty and geopolitical risks in Turkey, the accelerating pace of monetary policy normalization (most of LatAm and Central and Eastern Europe (CEE)), and a relief rally in Peru where investors reacted to positive political news.

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

October 2021	Country	Total Return USD (%)	Bond Return (%)	FX Return (%)	Index Weight	Index Impact (bps)**
GBI-EM GD		**-1.33**	**-1.39**	**0.06**		
Top 5 Performers	Peru	8.1	4.2	3.9	2.1%	17
	Indonesia	1.9	0.9	1.0	10.0%	19
	China	0.6	-0.4	1.0	10.0%	6
	Philippines	0.6	-0.6	1.2	0.1%	0
	Malaysia	0.1	-1.0	1.1	8.2%	1
Bottom 5 Performers	Poland	-3.8	-3.4	-0.4	7.5%	-29
	Uruguay	-4.6	-1.8	-2.8	0.1%	-1
	Czech Republic	-5.0	-3.6	-1.4	4.5%	-22
	Brazil	-6.7	-3.5	-3.2	8.2%	-55
	Turkey	-8.3	-0.7	-7.5	1.7%	-14

Source: State Street Global Advisors, JP Morgan as at 29 October, 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.

Turkey was the worst performer in the month as the lira tumbled on a surprise central bank rate cut of 200 basis points (bps) on 21 October, and the bank's indication there is scope to cut rates further. This was considered by the markets to be a quite unconventional move, given the central bank had revised its year-end inflation forecast higher by 4.3 percentage points to 18.4% year-on-year (y/y).

Brazil performed relatively poorly, returning -6.7% to be the biggest detractor from index returns (-55 bps). The bonds and the currency sold off as the country's fiscal situation continues to deteriorate and its spending cap comes under threat. The central bank hiked the Selic rate 150bps to 7.75% due to persistent broad-based price pressures. Markets are expecting that the current hiking cycle will significantly increase debt service costs, and that the weakening fiscal anchor implies a higher premium to Brazilian assets.

CEE countries **Czech Republic** and **Poland** underperformed, with markets pricing in steeper tightening cycles on the back of expectations for inflation to overshoot targets amid tight labour markets, strong wage growth and expectations of above-trend growth in the near term due to EU-funded capital expenditure.

Peru was the best performing country in the month (+8.1%) as President Pedro Castillo accepted the resignation of Prime Minister Guido Bellido, a leftist who has called for the nationalization of the nation's largest gas field, following a cabinet reshuffle. Investors seemed to be optimistic on what appears to be a shift to the political centre for the recently-incepted government and the removal of a radical section of Castillo's party.

Indonesia performed well and was the top contributor (+19 bps) to index returns, with both rates and FX components contributing equally. Bank Indonesia (BI) left its policy rate unchanged at 3.50% and reiterated that it would continue its "pro-growth" stance, while downplaying the potential impact of tapering by the US Federal Reserve. Furthermore, Indonesia's headline CPI inflation rate has been benign, printing at 1.65% y/y in October and 1.60% in September to remain below BI's 2-4% target range.

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	**0.02%**	**-1.09%**	**-1.34%**
Spread Return	-0.08%	0.51%	1.89%
Treasury Return	0.11%	-1.59%	-3.17%
IG Sub-Index	0.32%	-0.67%	-2.64%
HY Sub-Index	-0.27%	-1.51%	0.24%

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 29 October, 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 sovereign debt generated flat returns of 0.02% in October, as measured by the JP Morgan EMBI Global Diversified Index. Spreads and yields were relatively resilient despite the recent moves in US rates markets, as long-end rates have remained relatively well anchored and are below the March peaks, and the UST curve has flattened. This is in contrast to EM local yields, where inflationary dynamics continue to push the market to re-evaluate terminal rates.

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

October 2021	Country	Total Return (%)	Spread Return (%)	Treasury Return (%)	Index Weight	Index Impact (bps)**
EMBI Global Diversified		**0.02**	**-0.08**	**0.11**		
Top 5 Performers	Suriname	9.5	10.1	-0.5	0.1%	0
	Sri Lanka	5.0	5.4	-0.4	1.1%	5
	El Salvador	3.5	3.7	-0.2	0.7%	3
	Papua New Guinea	2.5	3.2	-0.6	0.1%	0
	Zambia	2.0	2.3	-0.3	0.3%	1
Bottom 5 Performers	Tunisia	-4.6	-4.1	-0.5	0.1%	0
	Ghana	-4.9	-4.9	0.0	1.5%	-7
	Ethiopia	-5.1	-4.6	-0.5	0.1%	-1
	Argentina	-5.4	-5.1	-0.3	1.1%	-6
	Lebanon	-10.9	-10.9	0.0	0.3%	-3

Source: State Street Global Advisors, JP Morgan as at 29 October, 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.

Suriname spreads rallied after the government announced that it has implemented all prior actions for a $690m three-year extended fund facility program from the International Monetary Fund (IMF) to be approved. Approval of the program by the IMF executive board would unlock $57.5m immediately.

Sri Lanka was a good performer over the month. Spreads rallied even though Moody's downgraded Sri Lanka's foreign currency debt rating to Caa2 from Caa1 on an increased risk of default due to the lack of a comprehensive debt repayment plan and the country's low FX reserves. Sri Lanka's official FX reserves dropped to just $2.5 billion by the end of September. The country's central bank, in response, said the government was committed to meeting its debt obligations and that it was expecting investments of around $1.1bn from deals being made in the real estate, ports and energy sectors to help the country's flagging FX reserves.

El Salvador bonds bounced back from the recent selloff, as the president of the Central Reserve Bank dismissed fears that the country's adoption of Bitcoin (BTC) as legal tender will hamper plans for a $1.3bn loan facility from the IMF. Uncertainty over IMF talks, as well as the recent BTC adoption, has contributed to significant volatility in the country's bonds.

Among the poorer performers in October were: **Ghana**, where slow growth led to revenues of $5.66bn in the first seven months of the year falling 12% short of targets, and may continue to do so, making debt servicing even more difficult; **Argentina**, whose external liquidity position remains critical as low central bank reserves continue to erode, while a deal with the IMF to reschedule large upcoming payments in 2022 totaling $17.6bn due to begin in March has yet to be reached; and **Lebanon**, where the recent civil war has diverted attention away from addressing economic reforms required in a country already suffering from hyperinflation, medicine shortages and significant power blackouts.

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Expiry date 30 November 2022