Commentary
Fixed Income

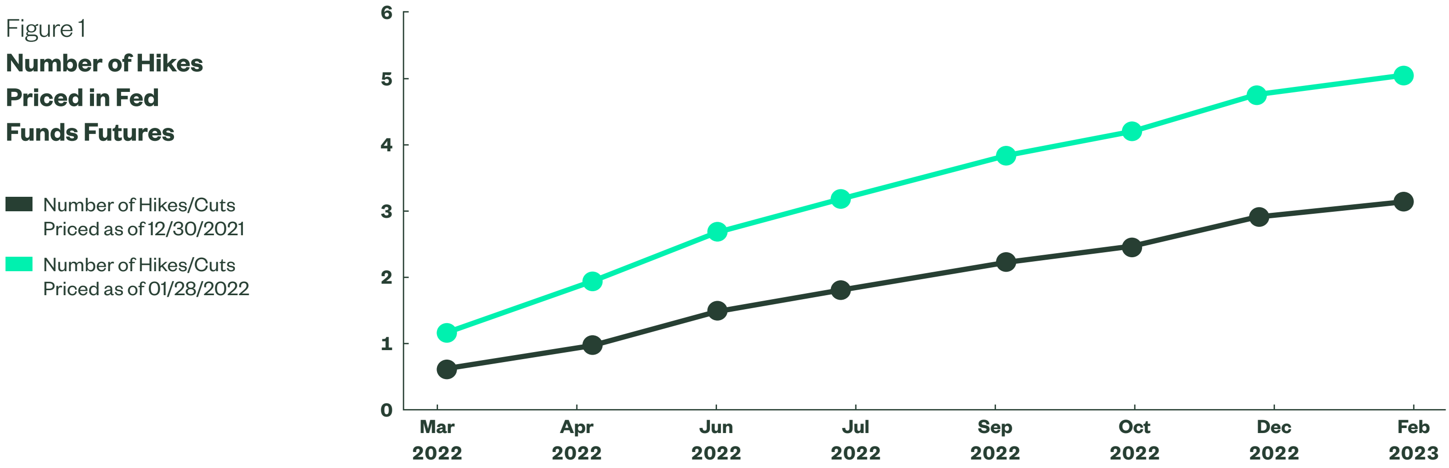
January 2022

Emerging Market Debt Market Commentary

Chart of the Month: Markets Raise US Rate Hike Expectations

The opening month of 2022 witnessed a notable uplift in how many rate hikes the market is expecting the US Federal Reserve to implement in 2022. At the end of January, market participants were anticipating five rate hikes in the year.

Figure 1
Number of Hikes Priced in Fed Funds Futures



Source: Bloomberg Finance L.P., as of 31 January 2022.

EMD Commentary — January 2022

Emerging market debt (in USD terms) experienced a tepid start to 2022 as a sell-off in US Treasuries put pressure on a range of risk assets. This included EM local rates, depressing both local and hard currency returns. Concerns around the severity of the Omicron variant eased as the hospitalisation rates are comparatively low relative to previous variants. Mobility restrictions due to surging Omicron cases were still a feature though as India, Thailand and Philippines imposed some constraints. Idiosyncratic geopolitical risks — especially around the Russia/Ukraine situation — remain elevated and contributed to a widening of spreads; the local yields for Russian and some eastern European countries' government debt moved higher.

The US Federal Reserve doubled its planned tapering of Treasury and Agency MBS purchases to $30bn at its January meeting and asset purchases are expected to end in early March. US rates sold off amid high US inflation (7% December CPI, year-on-year) and expectations of a more aggressive rate hike schedule than initially expected. Spreads of hard currency EM debt increased amid discouraging news flow around Russia/Ukraine and concerns about debt servicing capabilities of frontier EM countries. But with higher real rates and hawkish EM central banks, many EM countries seem reasonably well positioned to overcome domestic inflation and FX instability amid higher US rates. During January, hard currency outflows amounted to -$3.9bn, while local currency inflows were $1.3bn. (source: JP Morgan).

Figure 2
Emerging Market Debt Index Returns — As of 31 January, 2022

	1m (%)	3m (%)	6m (%)	YTD (%)	12m (%)	3yrs (%)	5yrs (%)
In USD							
GBI-EM GD (EM Local Currency)	-0.01	-1.23	-5.16	-0.01	-7.76	0.28	2.36
EMBI GD (EM Hard Currency)	-2.84	-3.30	-4.35	-2.84	-3.54	3.43	3.75
CEMBI BD (EM Corporates)	-1.67	-1.82	-2.24	-1.67	-0.71	5.38	4.74
In EUR							
GBI-EM GD (EM Local Currency)	1.44	1.97	0.32	1.44	-0.04	1.06	1.61
EMBI GD (EM Hard Currency)	-1.44	-0.17	1.18	-1.44	4.54	4.24	2.99
CEMBI BD (EM Corporates)	-0.25	1.35	3.41	-0.25	7.60	6.20	3.98
In GBP							
GBI-EM GD (EM Local Currency)	0.95	0.92	-1.72	0.95	-5.59	-0.38	1.05
EMBI GD (EM Hard Currency)	-1.92	-1.20	-0.88	-1.92	-1.27	2.75	2.43
CEMBI BD (EM Corporates)	-0.74	0.31	1.31	-0.74	1.62	4.69	3.41

Sources: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 January, 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 annualised.

Figure 3
Key EM and Macro Levels as of 31 January, 2022

Item	∆ 1 Month	∆ 3 Months	∆∆ YTD	Current Level
GBI-EM GD Yield	23 bps	29 bps	23 bps	5.94%
EMBI GD Yield	43 bps	58 bps	43 bps	5.72%
EMBI GD Spread	16 bps	26 bps	16 bps	385 bps
CEMBI BD Yield	37 bps	46 bps	37 bps	4.95%
CEMBI BD Spread	9 bps	10 bps	9 bps	321 bps
CDX.EM 5y	25 bps	26 bps	25 bps	212 bps
10y UST	27 bps	22 bps	27 bps	1.78%
Dollar Index (DXY)	0.91%	2.57%	0.91%	—
DOW 30	-3.32%	-1.92%	-3.32%	35132
Oil (WTI)	17.21%	5.48%	17.21%	$88.15

Source: JP Morgan, Bloomberg, as of 31 January, 2022.

Local Currency Market Highlights

EM local currency debt returned -0.01% in US dollar terms in January, as measured by the JP Morgan GBI-EM Global Diversified Index. Gains in EM FX and income returns were completely offset by the increase in local yields. Unfavourable performance has been drivenby a range of factors including: geopolitical risks in Russia-Ukraine, uncertainties around inflation and the Fed's hawkish policy path. The sustained rise in inflation led to surprise policy rate hikes from a number of EM central banks, notably in Chile and South Africa, which contributed to EM FX gains.

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 $)	**-0.01**	**-1.23**	**-0.01**
FX Return (vs $)	0.54	-1.20	0.54
Price Return (Local currency)	-0.98	-1.35	-0.98
Interest Return (Local currency)	0.43	1.32	0.43
In EUR			
Total Return (in €)	**1.44**	**1.97**	**1.44**
FX Return (vs €)	1.99	1.99	1.99
In GBP			
Total Return (in €)	**0.95**	**0.92**	**0.95**
FX Return (vs €)	1.50	0.94	1.50

Sources: State Street Global Advisors, Bloomberg, JP Morgan as of 31 January, 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 annualised.

Figure 5
Best and Worst Performers Across EM Local Government Bond Markets in USD*

January 2022	Country	Total Return USD (%)	Bond Return (%)	FX Return (%)	Index Weight (%)	Index Impact (bps)**
GBI-EM GD	—	**-0.01**	**-0.55**	**0.54**	—	—
Top 5 Performers	Chile	7.0	0.3	6.7	2.1	15
	Brazil	4.5	-0.4	4.9	8.3	37
	South Africa	4.1	0.9	3.2	8.4	34
	Turkey	3.7	4.8	-1.1	1.1	4
	Peru	3.2	-0.7	4.0	2.2	7
Bottom 5 Performers	Czech Republic	-1.3	-2.0	0.8	4.7	-6
	Romania	-1.7	-0.3	-1.4	3.1	-5
	Poland	-2.0	-0.4	-1.5	7.0	-14
	Dominican Republic	-3.5	-2.7	-0.8	0.1	0
	Russia	-6.9	-3.9	-3.0	6.8	-47

Source: State Street Global Advisors, JP Morgan, as at 31 January, 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 end weight by total return.

Russia was the worst performer in January, returning -6.9% in USD terms and detracting 47 bps from the index return. Geopolitical pressures escalated as Russia decried NATO's influence in Ukraine and Eastern Europe, with the deployment of around 100,000 Russian troops and tanks along the Russia-Ukraine border raising tensions to a new high. The United States and European Union have threatened heavier sanctions on Russia should they invade. Although economic fundamentals have been solid with soaring commodity prices and lower debt burdens, inflation touched an annual rate of 8.6%, which is way above the central bank's target. Along with the geopolitical risks, both Russian bonds and RUB sold off.

Poland was also a relatively poor performer, depreciating -2.0% in USD terms and detracting 14 bps from the index return. The Polish zloty was one of the worst performing EM currencies even as the central bank signaled an aggressive rate hike plan. This weakness was mostly due to fallout from tensions between Russia and Ukraine — Poland relies on Russia for energy imports.

Czech Republic underperformed in the month, returning -1.3% in USD terms and detracting from the index return. Government bond yields climbed after central bank indications of aggressive monetary policy tightening as the core annual inflation rate hit a 13-year high of 6.6% in December.

Chile was the best performer in January, returning 7.0% in USD terms and contributing 15 bps to the index return. The outperformance was almost entirely driven by a rally in the CLP currency, which appreciated by 6.35% against USD in the month. The currency gained as the central bank announced a larger-than-expected interest rate hike of 150 bps, taking the policy rate up to 5.50%.

Brazil was among the best performing countries, returning 4.5% in USD terms and contributing 37 bps to the index return. Leftist ex-President Luiz Inacio Lula da Silva, the front-runner in this year's presidential race, leaned towards the center and expressed interest in having former Sao Paulo Governor Geraldo Alckmin as his running mate. This boosted sentiment, as did buoyant commodity prices.

South Africa also performed strongly, returning 4.1% in USD terms and contributing 34 bps to the index return. The central bank delivered a 25 bps hike at its January meeting, taking the repurchase rate up to 4.0%. South African local debt attracted foreign investors — who were net buyers of 8.1bn rand worth of the country's bonds as of 19 January — as the market doesn't expect the central bank to hike rates aggressively, given the December inflation print of 5.9% is within the central bank's target range of 3–6%.

Hard Currency Market Highlights

EM hard currency sovereign debt returned -2.85% in January, as measured by the JP Morgan EMBI Global Diversified Index. The 10-year US Treasury yield climbed 27 bps to end the month at 1.78% and spreads widened in a poor start to the year for risk assets against the backdrop of a worsening geopolitical situation in Russia-Ukraine. Concerns around the debt refinancing capabilities of some frontier EM countries also mounted amid higher yields. The Fed doubled its pace of tapering at its January meeting, reaffirming market expectations that it will end asset purchases in early March and that rate hikes will begin the same month. Hard currency spreads widened by 16 bps in January amid broad risk-off sentiment.

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	**-2.85**	**-3.30**	**-2.84**
Spread Return	-0.89	-1.18	-0.89
Treasury Return	-1.97	-2.15	-1.97
IG Sub-Index	-3.74	-3.04	-3.74
HY Sub-Index	-1.90	-3.54	-1.90

Sources: State Street Global Advisors, Bloomberg, JP Morgan, as of 31 January, 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 annualised.

Figure 7
Best and Worst Performers Across EM Hard Currency Government Bond Markets*

January 2022	Country	Total Return (%)	Spread Return (%)	Treasury Return (%)	Index Weight (%)	Index Impact (bps)**
EMBI Global Diversified	—	-2.85	-0.89	-1.97	—	—
Top 5 Performers	Ethiopia	13.1	14.1	-0.9	0.1	1
	Ecuador	6.6	8.8	-2.0	1.6	10
	Lebanon	3.4	3.7	-0.3	0.2	1
	Tunisia	2.5	3.4	-0.9	0.1	0
	Angola	1.2	3.0	-1.7	1.1	1
Bottom 5 Performers	Ghana	-4.8	-3.4	-1.4	1.4	-7
	Belarus	-5.5	-4.4	-1.1	0.4	-2
	Honduras	-5.8	-4.6	-1.2	0.2	-1
	Ukraine	-6.0	-4.9	-1.2	2.2	-13
	Russia	-9.3	-7.6	-1.8	3.1	-29

Source: State Street Global Advisors, JP Morgan, as at 31 January, 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 end weight by total return.

Russia was the worst performer in January, returning -9.3% in USD terms and detracting 29 bps from the index return. Escalating tensions on the Russia-Ukraine border and the threat of sanctions should Russia invade weighed on sentiment. This led to a widening of the spreads in Russian dollar-denominated bonds. Although economic fundamentals have been solid amid soaring commodity prices and lower debt burdens, concern around high inflation still persists.

Not surprisingly, **Ukraine** was also one of the underperformers in the month, returning -6.0% in USD terms and detracting 13 bps from the index return. The sell-off in its debt securities was triggered by increasing risk of Russian military aggression. The yield on the September 2032 bond shot up to 10.91% on 25 January, before stabilising to end the month at 9.68%.

Among the poorer performers in January was **Ghana**, returning -4.8% in USD terms and detracting from the index return. Investors were concerned about the debt servicing capability of the West African country as the government debt level climbed to 81.5% of GDP and the fiscal deficit widened. This was reflected in a higher risk premium being demanded by investors as the spreads widened in Ghana bonds for much of January. Yields stabilised by the end of January as the government reassured investors of its commitment to fiscal targets set out in the budget.

Ethiopia was the best performer in January, returning 13.1% in USD terms and contributing 1 bp to the index return. The rally was largely driven by the government's decision to end a state of emergency amid subsiding tensions around its 15-month conflict with rebels.

Ecuador was among the best outperformers, returning 6.6% in USD terms and contributing 10 bps to the index return in the month. Ecuador lifted force majeure on its oil sector and resumed deliveries of oil with two 360,000-barrel shipments of crude and the refineries returned to full capacity. Buoyant oil prices also boosted investor sentiment.

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* Pensions & Investments Research Center, as of December 31, 2020.
† This figure is presented as of December 31, 2021 and includes approximately $61.43 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.

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