



Portfolio Manager Perspectives

BlueBay Emerging Market Debt Update

Weekly Update May 27, 2021

Equity markets were mixed this week, with the S&P 500 and Russell 2000 both posting small losses, while European indices made small gains. Emerging-market (EM) equities were the outperformers, with gains of around 1.7%, as they recovered from sharp losses the week before. Core rates were little changed over the week, with a small flattening bias to the US Treasury curve, although 10-year real rates did move higher by around 9 basis points (bps) as inflation breakevens fell.

The main event this week was the release of the Federal Open Market Committee minutes, where the statement hinted at upcoming discussions around when to end tapering. This raises the focus on upcoming Federal Reserve (Fed) meetings as markets try to gauge the Fed's thinking on the timing and pace of any tapering of asset purchases.

Commodities continued to take a breather this week, as oil and metals both ended the week down more than 2%. After these moves, the Bloomberg commodity index is up around 50bps over the month, having been up more than 3.5% at its peak.

In EM fixed income, returns were muted but positive across the board. In credit, sovereign high-yield markets were the outperformers as a couple of idiosyncratic stories began to play out. In local markets, local rates outperformed foreign exchange (FX), which finished flat over the week.

Market review

- In China, industrial output and fixed-asset investment continued to make solid gains as export demand remained positive and the property market buoyant. Retail sales numbers disappointed however, as consumer demand was more tepid than expected.
- Colombia's credit rating was downgraded by S&P, which ran out of patience after the failed tax reform. This moves Colombia to a split-rated credit, with two investment-grade ratings and now one high-yield (BB+) rating. The initial moves in Colombian assets were muted, as the market had largely priced this event, despite the earlier-than-expected timing. A more meaningful move may come with a second downgrade into high yield, which is likely to bring with it some forced selling.

Market outlook

In our view, markets remain calm at the moment as a high degree of uncertainty over the future path of both inflation and the employment outlook ties the Fed to a dovish path for now and keeps the world awash with liquidity. There was not much to glean from the Fed minutes last week and so we simply need to focus on the incoming data from here, as well as the virus prognosis. It seems fair to assume that the Fed will err on the side of caution and perhaps that is the market's read, with real rates oscillating between -80bps and -90bps, broadly supporting risk assets in general. It is, however, an uneasy calm, as the Fed is in uncharted waters and has a difficult balancing act ahead as it seeks to pare back stimulus without undoing much of the hard work it has done to date.

For EM fixed income, the US dollar weakness has been notable, with increasing twin deficits, higher inflation and easy Fed policy all creating the perfect storm in the near term. This has supported EM assets across the board, particularly given the improved valuations given the first-quarter sell-off. Over the year to date, returns have retraced more than half of their losses from the first quarter. We believe the path from here will be dictated by certain external factors, mainly the pace of stimulus withdrawal from the Fed, but also many EM specific factors including the pace of vaccine rollouts along with the related impact on fiscal consolidation. It is this last point, on fiscal consolidation, that we think will prove to be perhaps the key differentiator among the performance of EM sovereigns for the remainder of the year.

Index Review – Weekly Market Snapshot as of 05/21/2021

	Total return			Spread / yield change (bps)			Spread (bps)	Yield (%)
	Weekly	MTD	YTD	Weekly	MTD	YTD		
Hard Currency Sovereign	0.20%	2.84%	-1.83%	0	-20	-17	335	5.01
Hard Currency Corporate	0.11%	1.10%	0.10%	0	3	-31	286	4.31
Local Currency Corporate	0.08%	2.86%	-0.29%	1	-5	-61	135	5.43
Local Currency Sovereign	0.05%	3.84%	-3.09%	1	-3	75		4.96

Source: Bloomberg, JP Morgan

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