

Emerging Markets Debt Team Market Reaction Update

April 2020

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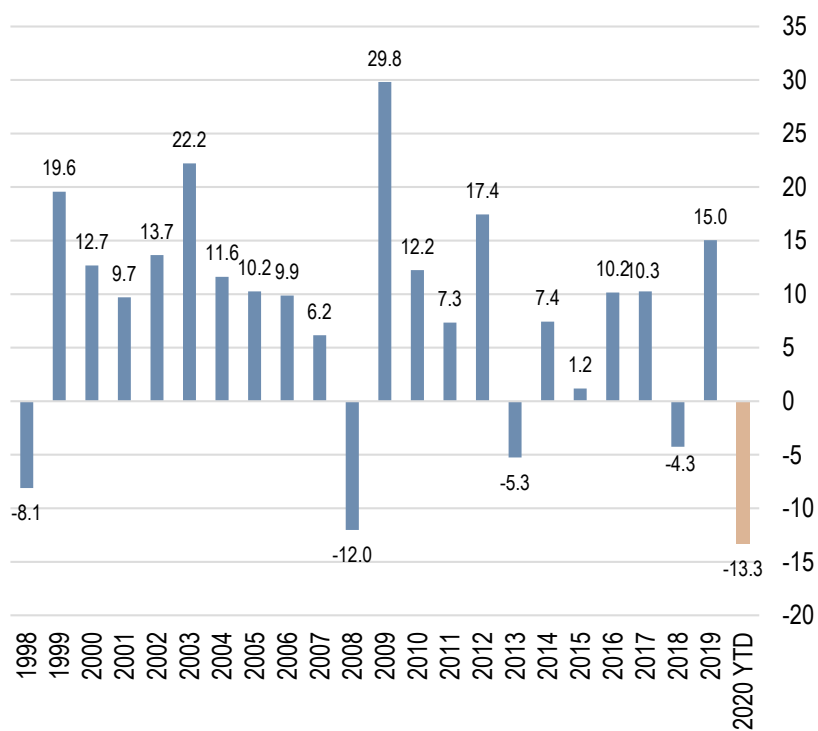
Global Co-Head of Emerging Markets Debt

Market Update And Outlook

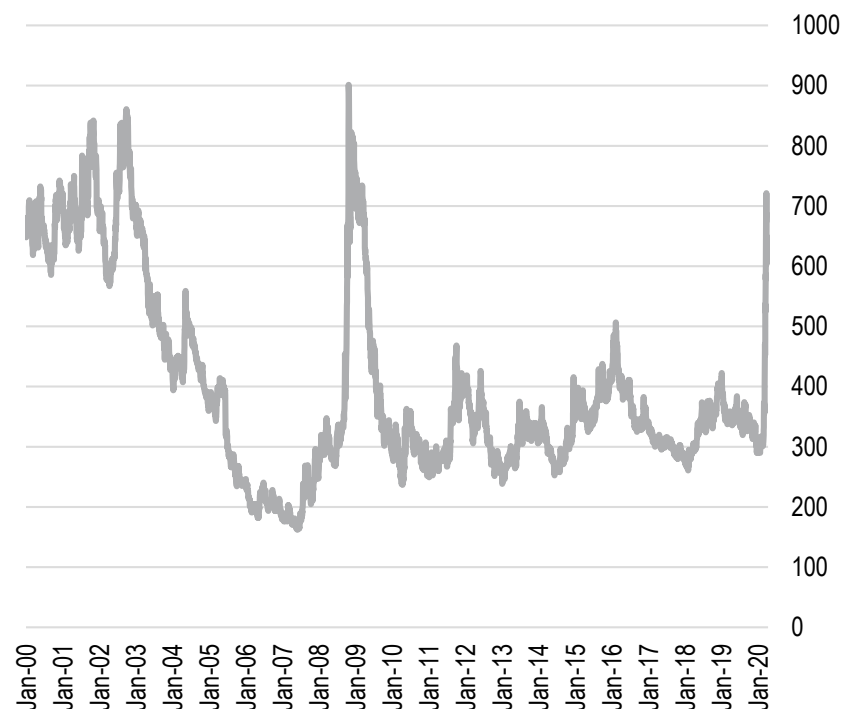


Markets: EM HC Spreads Highest Since 2008 GFC

EMD HC Index – Calendar Year Total Returns in USD (%)



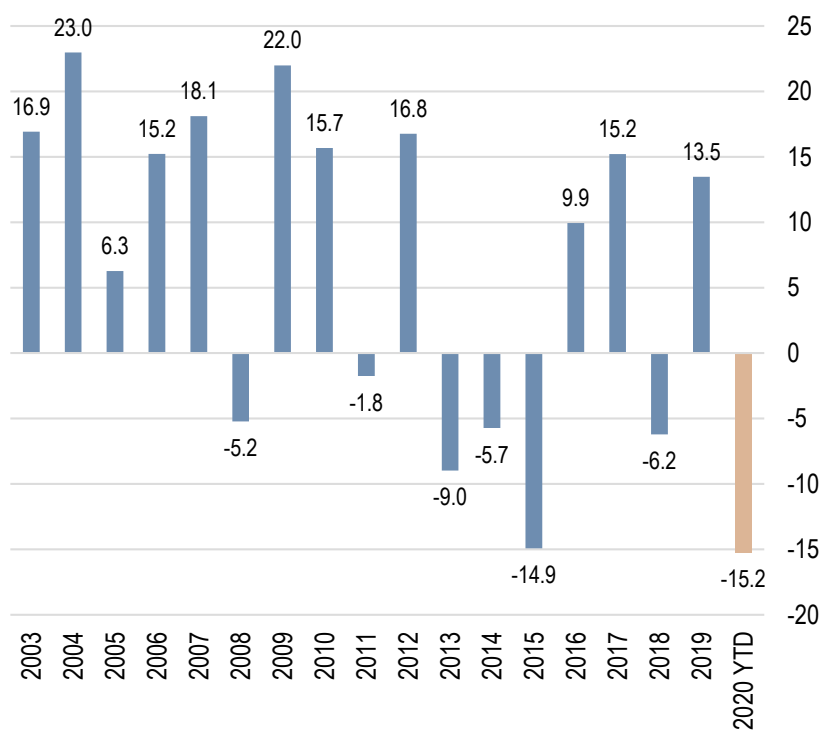
EMBI GD Spread (bps over US Treasuries)



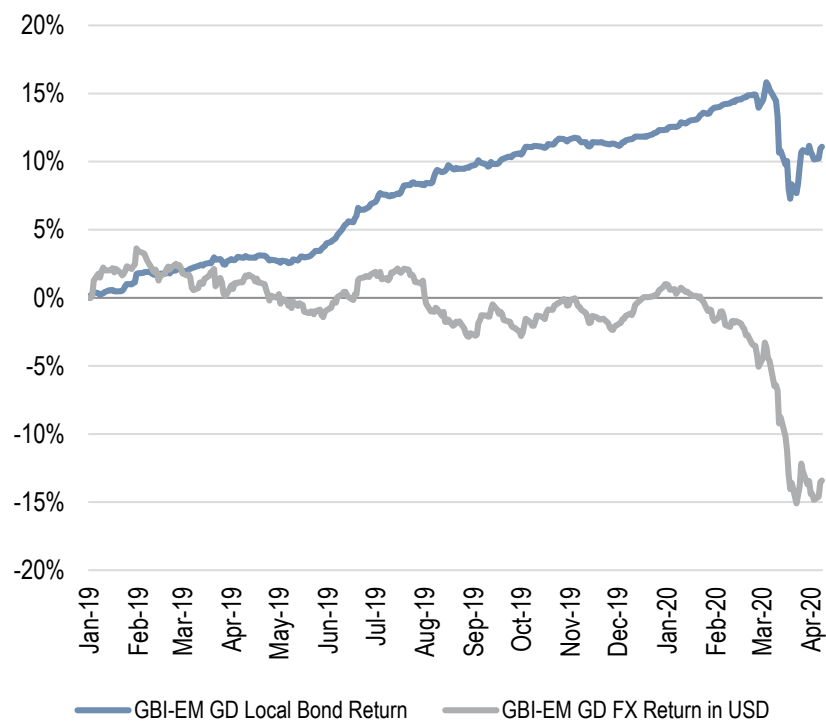
Source: Bloomberg as of April 8, 2020. EMD HC Index = JPMorgan EMBI Global Diversified Index. For illustrative and discussion purposes only. Nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. This material is not intended as a formal research report and should not be relied upon as a basis for making an investment decision. Investing entails risks, including possible loss of principal. Past performance is no guarantee of future results. Historical trends do not imply, forecast or guarantee future results. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed.

Markets: Sharp Weakening in EM Local Currencies and Higher Local Rates

EMD LC Index – Calendar Year Total Returns in USD



EMD LC Bond and EM FX Return Components



Source: Bloomberg as of April 8, 2020. EMD LC Index = JPMorgan GBI-EM Global Diversified Index. For illustrative and discussion purposes only. Nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. This material is not intended as a formal research report and should not be relied upon as a basis for making an investment decision. Investing entails risks, including possible loss of principal. Past performance is no guarantee of future results. Historical trends do not imply, forecast or guarantee future results. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed.

EM Fixed Income Markets Witnessed Three Interrelated Shocks in March

Initially triggered by the COVID-19 outbreak, the sell-off in EM Fixed Income intensified on the back of the oil price drop post the Russia/Saudi supply headlines and then morphed into a liquidity freeze amidst a broad rush to dump risk assets

COVID-19 Crisis

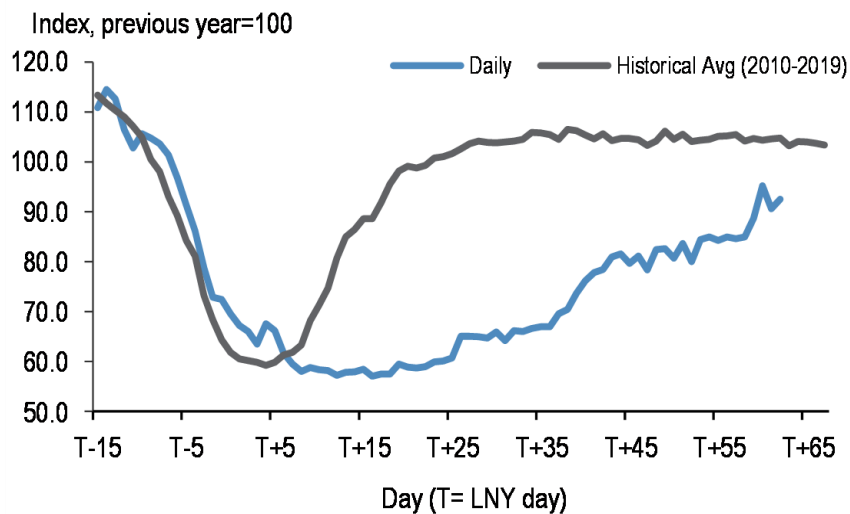
Oil Price Shock

Market Illiquidity

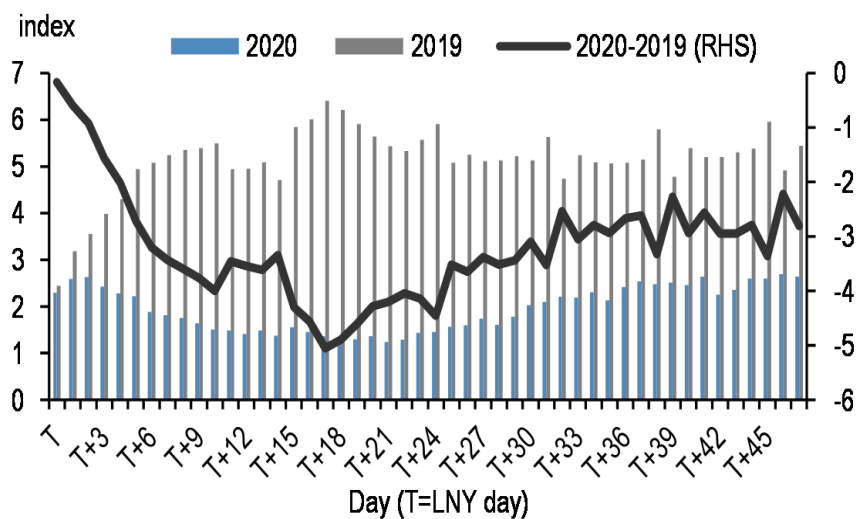
China: Tracking The Recovery in Economic Activity

High frequency data suggests that industrial production and domestic demand are recovering in China, though the COVID-19 outbreak in the rest of the world is posing a renewed headwind to growth

Daily coal consumption during LNY¹



Transportation Hub Passenger Flow Index²



We see activity in China having recovered to around 80-85% of 'normal'

1. Source: Wind, JPMorgan; As of March 27, 2020. Showing daily coal consumption at six major power generators.

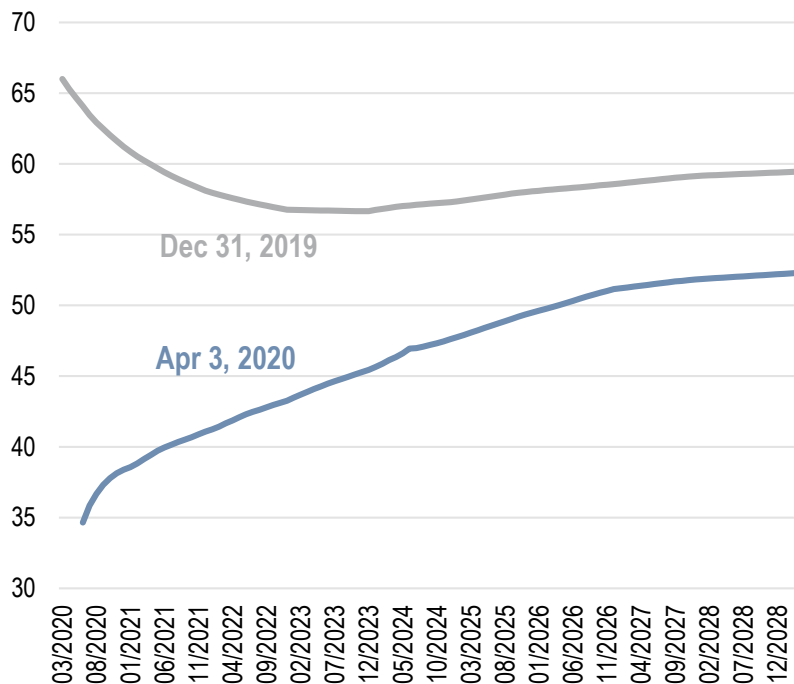
2. Source: Wind, Baidu, JPMorgan; As of March 27, 2020. Transportation hub include airports and major train stations.

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Oil Price Shock: Hard Currency Markets Typically Most Affected Given Country Composition

We expect a medium/long-term recovery to a \$40-50 range for oil, though near term risks for oil are still biased to the downside given the degree of short-term demand/supply imbalances; we remain selective in our oil related exposures

Brent Futures Curve – From Backwardation to Extreme Contango¹



1. Source: Bloomberg; As of April 3, 2020

2. Source: Neuberger Berman; As of February 28, 2020.

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Main Exposures in Oil Producing EM Countries – NB EMD HC Strategy²

Overweight

- Azerbaijan, Kazakhstan, Russia, Mexico, Angola

Neutral

- Nigeria, Ghana

Underweight

- Ecuador, Bahrain, Oman, Iraq, Saudi Arabia, Qatar, UAE

Rating Downgrades Across EM Countries

MTD change in foreign currency long-term rating as of 30 March 2020

Investment Grade	Agency	Rating Change
Kuwait	S&P	AA → AA-
Mexico	S&P	BBB+ → BBB
Trinidad & Tobago	S&P	BBB → BBB-
South Africa	Moody's	Baa3 → Ba1

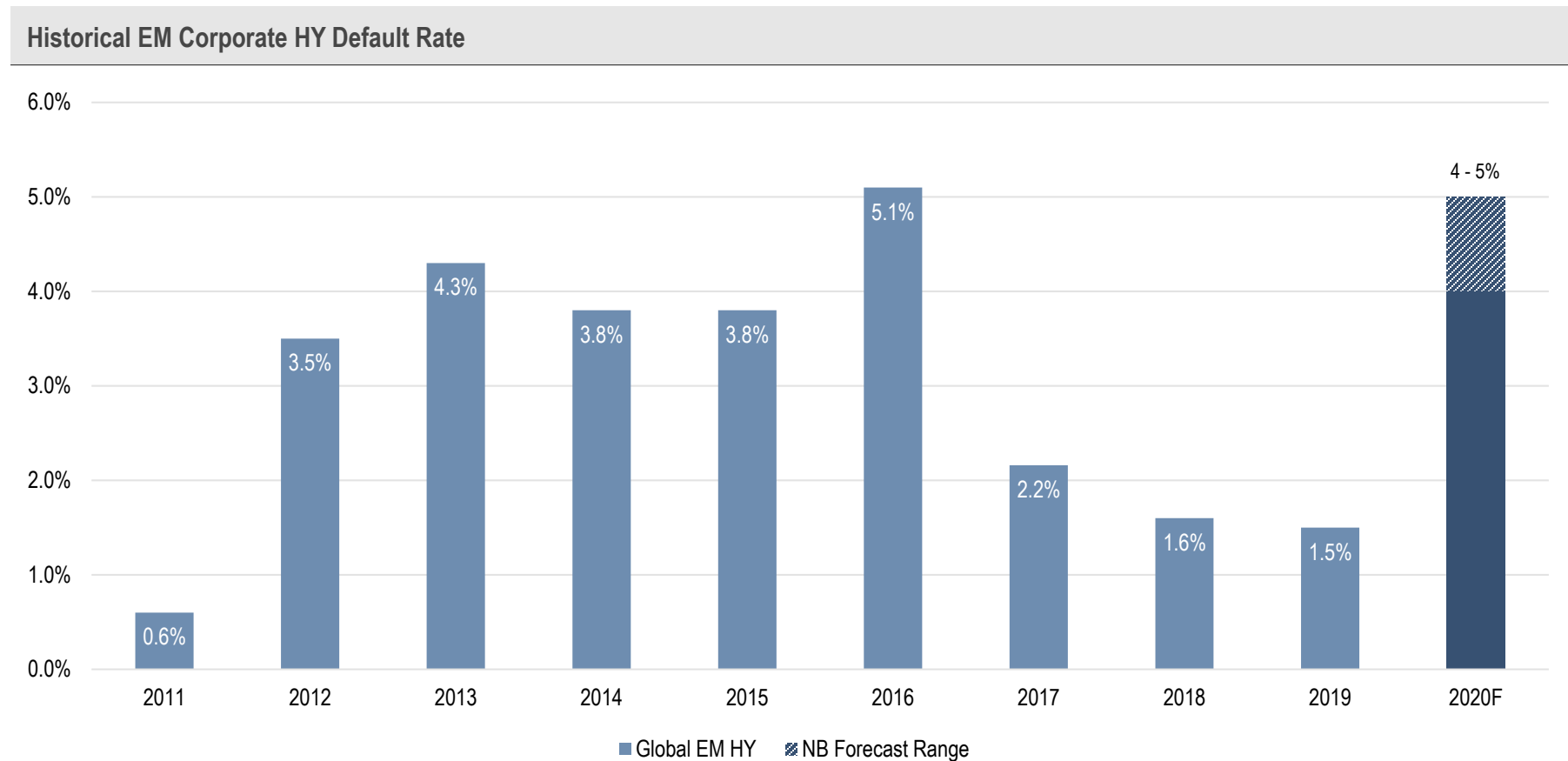
High Yield	Agency	Rating Change
Bolivia	Moody's	Ba3 → B1
Lebanon	S&P / Fitch	CC → SD / C → RD
Ecuador	S&P / Fitch	B- → CCC- / B- → CC
Angola	S&P / Fitch	B- → CCC- / B → B-
Oman	Moody's / S&P / Fitch	Ba1 → Ba2 / BB → BB- / BB+ → BB-
Nigeria	S&P	B → B-

- Sovereign Rating downgrades have been concentrated in **oil exporting countries**.
- **South Africa** has been the only country so far to migrate from Investment Grade to High Yield.
- On the **EM Corporate** side, we expect the default rate in the high yield part of the universe to pick up to 4-5%, up from 1.5% in 2019.

Source: Moody's, S&P, Fitch, Bloomberg. As of March 30, 2020.

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We Expect the Default Rate in the EM High Yield Universe to Pick Up in 2020 Towards 4-5%



Source: JP Morgan, Neuberger Berman expectations. As of March 31, 2020. EM Corporate HY represented by JPM CEMBI HY index.

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IMF / World Bank Stepped Up Support for Lower Income Countries Affected by the Pandemic

While FED dollar liquidity swap lines of \$60Bn each for a number of Central Banks including those of Mexico, Brazil, South Korea, Singapore have eased USD funding pressures

Key IMF & World Bank Initiatives/Programs Include:

- **\$50Bn** made available by the IMF via its **rapid-disbursing emergency financing**, including \$10 billion on highly concessional terms for low-income countries.
- IMF **Catastrophe Containment and Relief Trust** - \$200m available to support international debt relief efforts when poor countries are hit by severe natural disasters or battling public health crises. The IMF has expanded the qualification criteria to obtain debt service relief and is looking to increase the size of the Trust to around \$1Bn.
- The World Bank Group and the IMF **called on all official bilateral creditors to suspend debt payments from IDA countries¹ that request forbearance**. This will help with IDA countries' immediate liquidity needs to tackle challenges posed by the coronavirus outbreak and allow time for an assessment of the crisis impact and financing needs for each country.
- As of March 27, 2020, **World Bank teams are finalizing COVID-19-related projects in 60 countries** for up to \$2.8 billion under the \$14 billion Fast Track Facility.

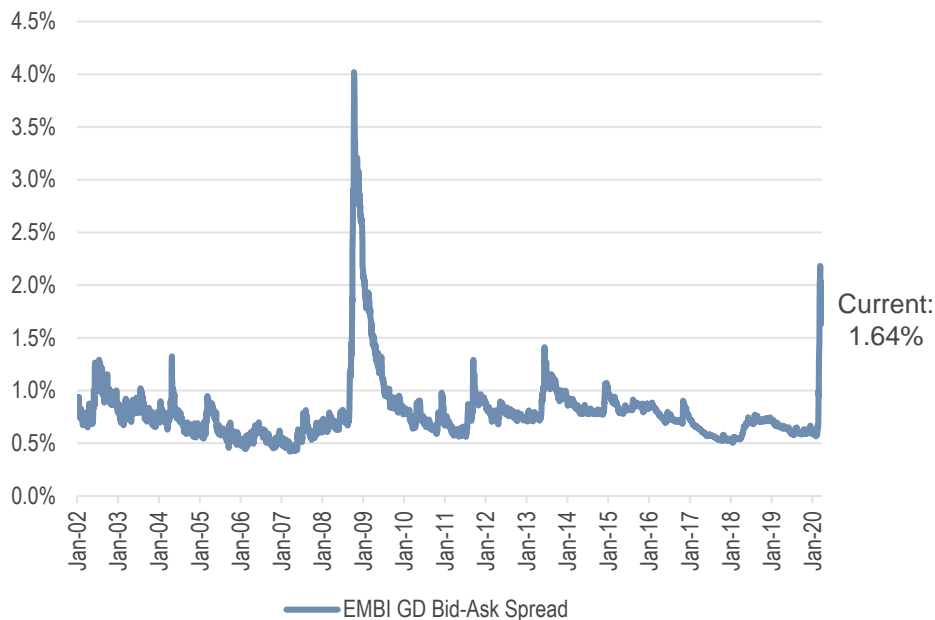
Source: IMF, World Bank, IFC. As of 30 March 2020

1. 'IDA countries' refers to countries which are eligible for support from the International Development Association. Eligibility for IDA support depends first and foremost on a country's relative poverty, defined as GNI per capita below an established threshold and updated annually (\$1,175 in fiscal year 2020).

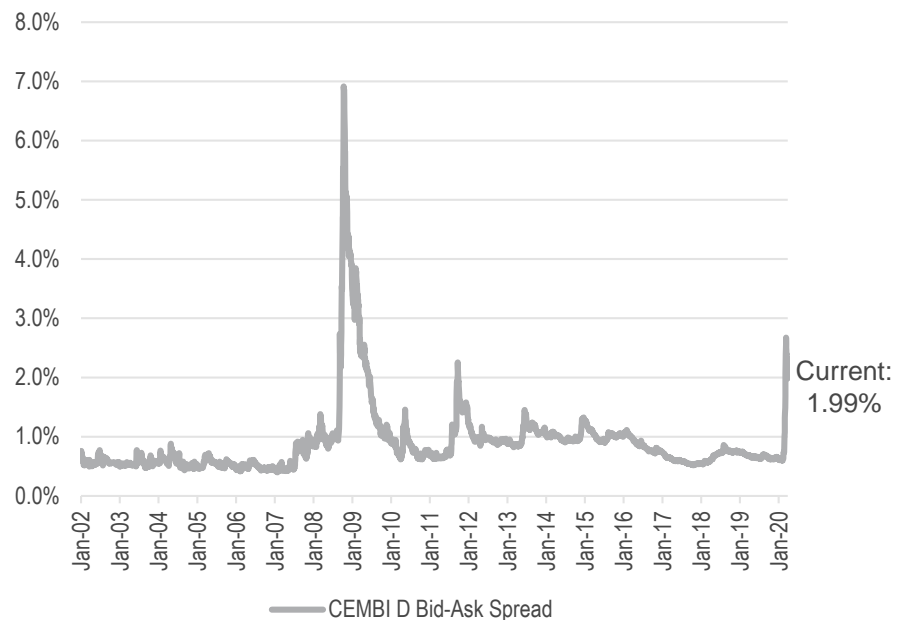
EM Fixed Income Market Liquidity

Liquidity began to deteriorate sharply in the 2nd week of March, and only started to improve more recently following the massive stimulus packages by the FED and the US Government

EMD HC Sovereigns: Average Bid-Ask Spread (EMBIGD Index)



EMD HC Corporates: Average Bid-Ask Spread (CEMBID Index)



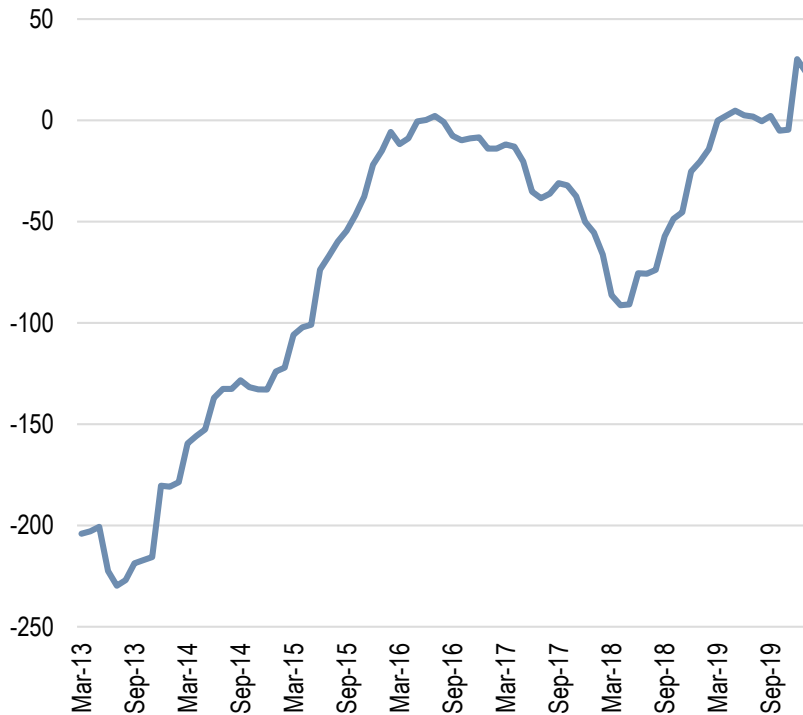
Liquidity is actually worse than shown above, given low volumes getting through at any price plus the lack of any pricing available is not captured.

Source: JPMorgan. As of April 8, 2020.

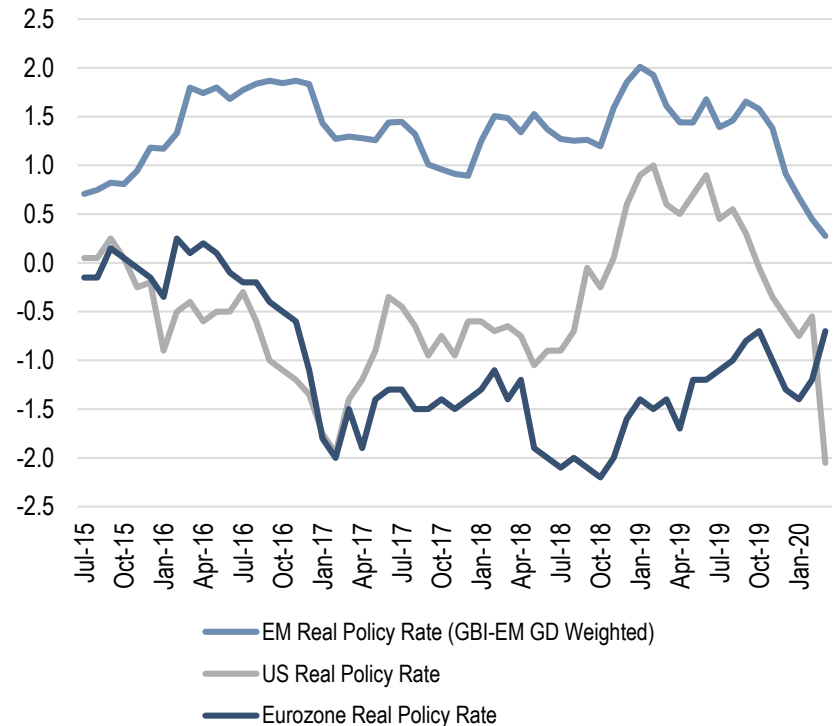
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EM External Balance and Policy Mix Still Favorable in Aggregate

EM-10 Aggregate Current Account (\$Bn)



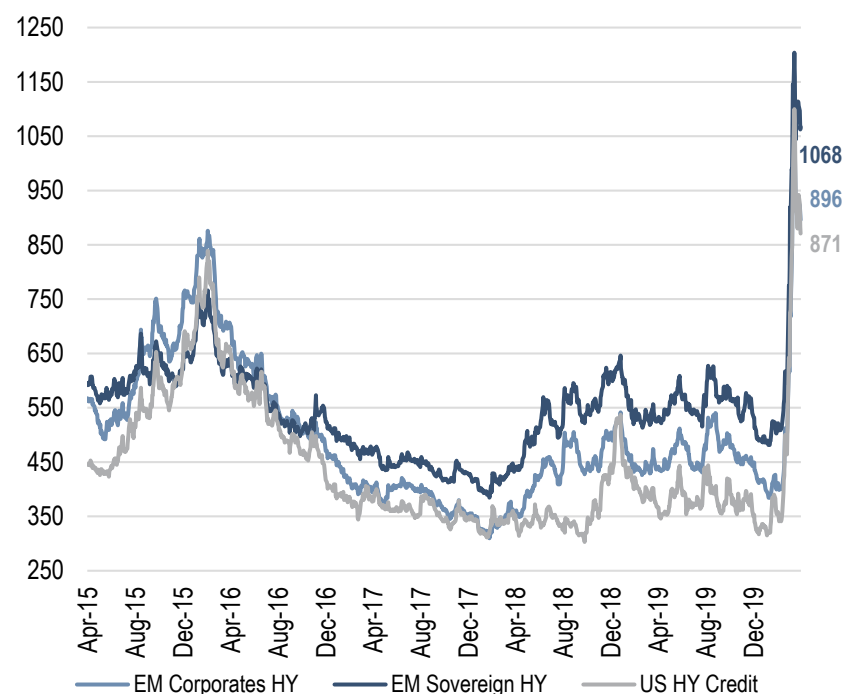
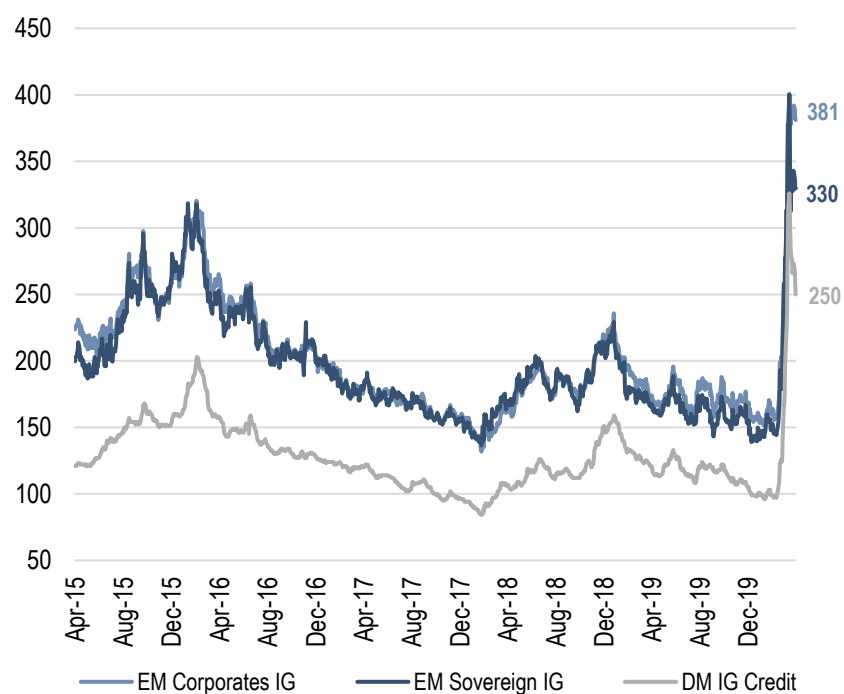
Real Policy Rates: EM vs DM



Source: LHS: Bloomberg, as of January 31, 2020. EM-10: Brazil, Colombia, India, Indonesia, Korea, Mexico, Poland, Russia, South Africa, Turkey; RHS: Bloomberg, as of March 31, 2020. Real Policy Rate data series are calculated as the policy rate for each country minus the headline inflation rate. The countries included in the EM Real Policy Rate series are all the countries in the GBI-EM GD Index as of January 31, 2019 with the exception of Argentina, Dominican Republic and Uruguay; The countries included in the EM Real Policy Rate series are weighted based on their weights in the JPMorgan GBI-EM Global Diversified Index as of January 31, 2019. For illustrative and discussion purposes only. Nothing herein constitutes investment, legal, accounting or tax advice, or a recommendation to buy, sell or hold a security. This material is not intended as a formal research report and should not be relied upon as a basis for making an investment decision. Investing entails risks, including possible loss of principal. Past performance is no guarantee of future results. Historical trends do not imply, forecast or guarantee future results. Nothing herein constitutes a prediction or projection of future events or future market behavior. Due to a variety of factors, actual events or market behavior may differ significantly from any views expressed.

EM Hard Currency Spreads Widened to Extreme Levels, Especially in the High Yield Segment

Spread Over Treasuries

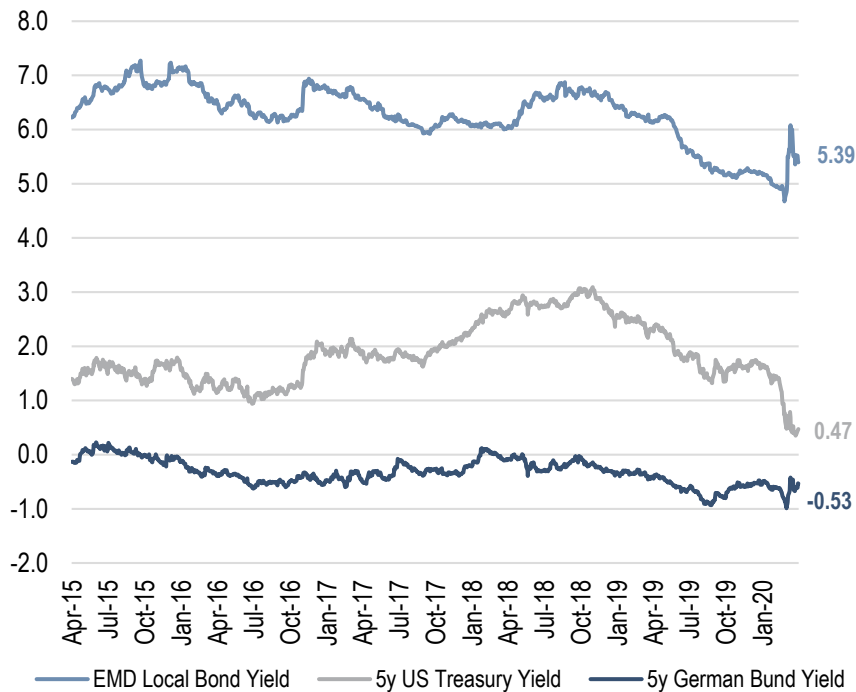


Source: JPMorgan, Barclays; As of April 8, 2020.

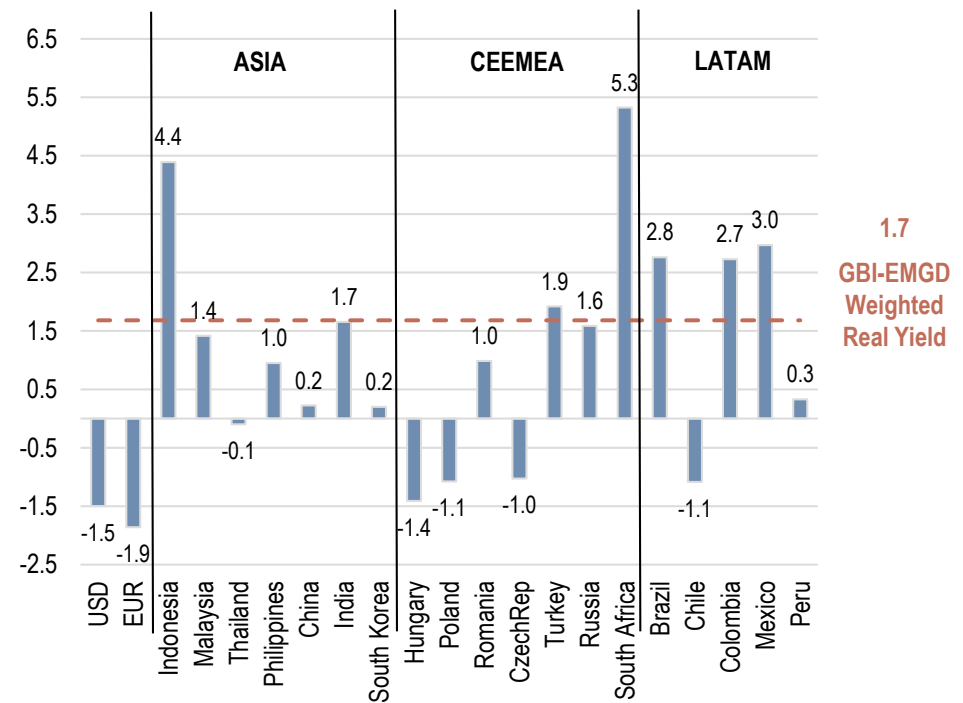
Indices used: JPM EMBI Global Diversified HY and IG subindices, JPM CEMBI Diversified HY and IG subindices, Barclays US High Yield Index, Barclays Global Aggregate Corporate Index. This material is intended as a broad overview of the portfolio managers' current style, philosophy and process, is as of the date hereof and is subject to change without notice. Information on this page represents historical observations about the sub-asset classes and is not intended to represent or predict future events. Historical trends do not imply, forecast or guarantee future results.

EM Local Yields Have Widened Sharply, Particularly For High Yielders

GBI EM VS. US 5Y and 5Y Bund Nominal Yields (%) as of April 8, 2020

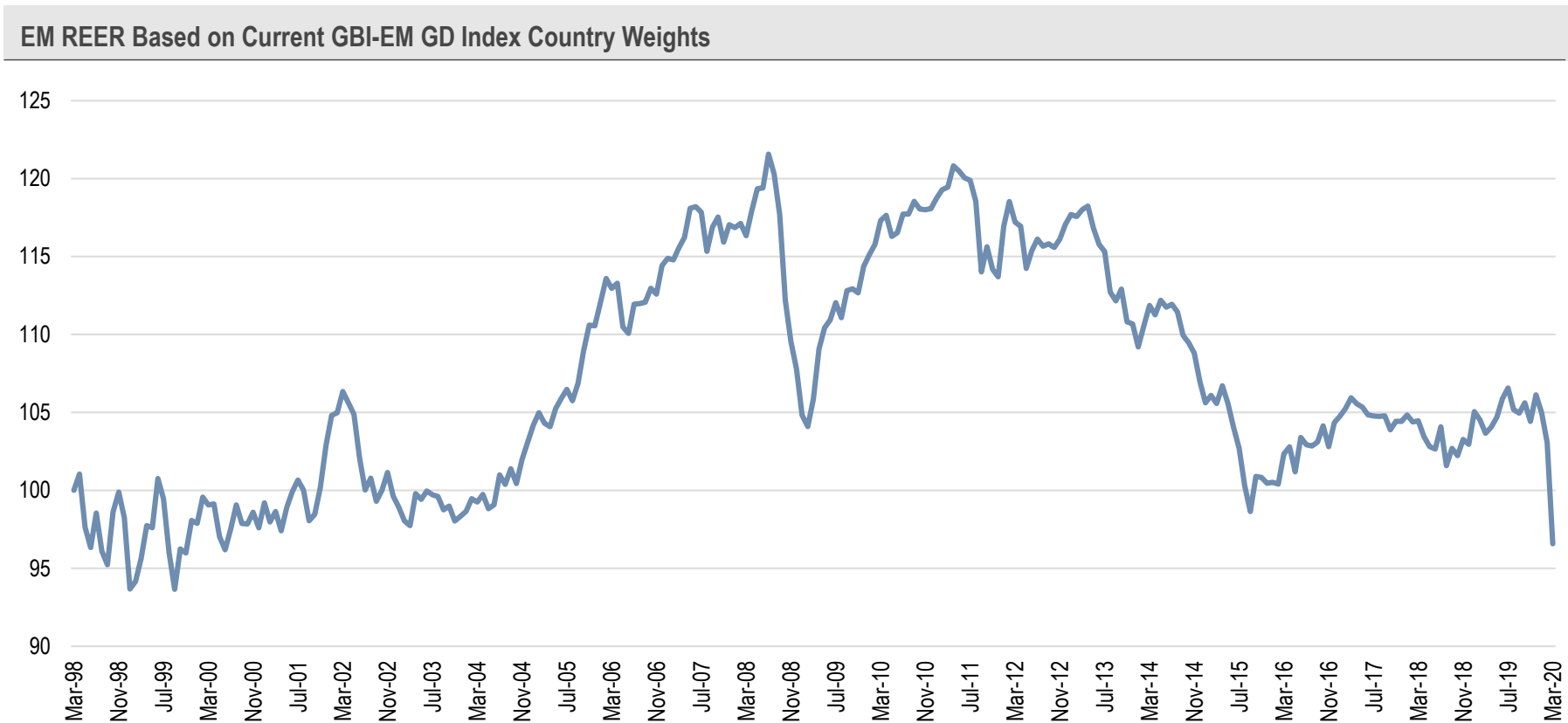


EM VS DM Real Yield as of April 8, 2020, Based On Current 5y Nominal Yield VS 12m Fwd CPI



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Real Effective Exchange Rates in Emerging Markets Have Reached Extreme Levels



Source: JPMorgan, Bloomberg; as of March 31, 2020.

Historical JPMorgan EM REERs for individual EM currencies are weighted using current GBI-EM GD Index country weights.

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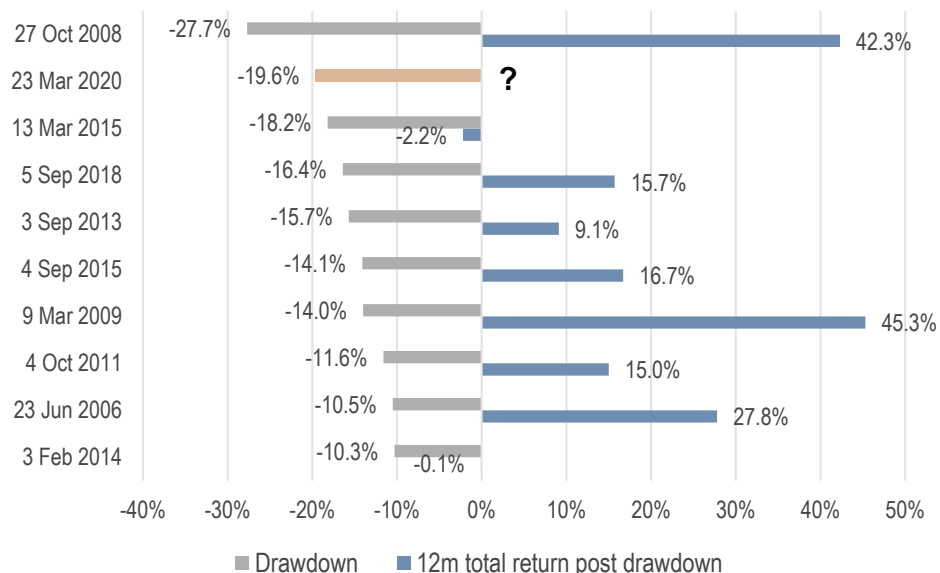
Historically, Periods EMD Hard Currency Spreads Were in Excess of 500bps Have Been Followed by Strong 12m Total Returns

And in EMD Local Currency, drawdowns of >10% have historically been followed by strong rebounds in the following 12 months in most occasions

EM Sovereign
Historical 1 year Performance
After Spreads Widened
to 500+ basis points...
 (3/27 OAS: +624 bps)

1 Yr. Total Returns	JPM EMBI Global Diversified Index
Average	20.8%
Median	21.3%
High	41.6%
Low	3.3%
Positive	31
Negative	0

**EMD Local Currency – 12m total returns in USD after drawdowns >-10%
 Based on JPM GBI-EM GD Index**



LHS: Sources: Bloomberg, JPMorgan. Returns expressed in USD based on period 1/1/2002 – 2/29/2020

RHS: Sources: Bloomberg, JPMorgan. Returns expressed in USD based on period 1/1/2003 – 3/31/2020

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Total Asset Class Return Views – 12 Month Horizon

Total return analysis combines the outcomes of the TAA scorecard into a forecast per asset class

April 8, 2020	12 M Expected Returns	Scenario 1: Recession & U-Shaped Recovery	Scenario 2: V-Shaped Recovery Post Q2	Scenario 3: Extended Recession
Probability		50%	30%	20%
EMD Hard Currency Sovereign	16.3%	18.9%	19.7%	4.7%
EMD Hard Currency Corporate	14.1%	15.3%	19.4%	3.0%
EMD Local Currency	7.8%	10.0%	14.6%	-8.0%
EMD Blended Benchmark (25/25/50)	11.5%	13.5%	17.1%	-2.1%

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EMD Outlook – Our Views

- **The Coronavirus spreading will likely result in a material drop in Q1 & Q2 global GDP growth.** However, our base case is for a recovery later in the year assuming that the virus will be contained in the coming months, supported by aggressive policy stimulus efforts globally.
- **Other potential risks in 2020 remain mostly geopolitical,** with the primary focus being the US elections in November.
- **Valuations for EM hard currency bonds have become very attractive** following the recent spike in spreads, especially in the high yield space. Local bond yields widened less dramatically but dislocations occur in higher yielding markets. Currencies are now very cheap on REER.
- We have **reduced the our EM FX overweight towards neutral** starting from January given the near term headwinds to EM growth from the Coronavirus impact and added local duration exposure. We continue to have a balanced position in hard currency, with the **long bias in sovereign debt** funded with an underweight in corporate credit.

As of March 30, 2020.

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