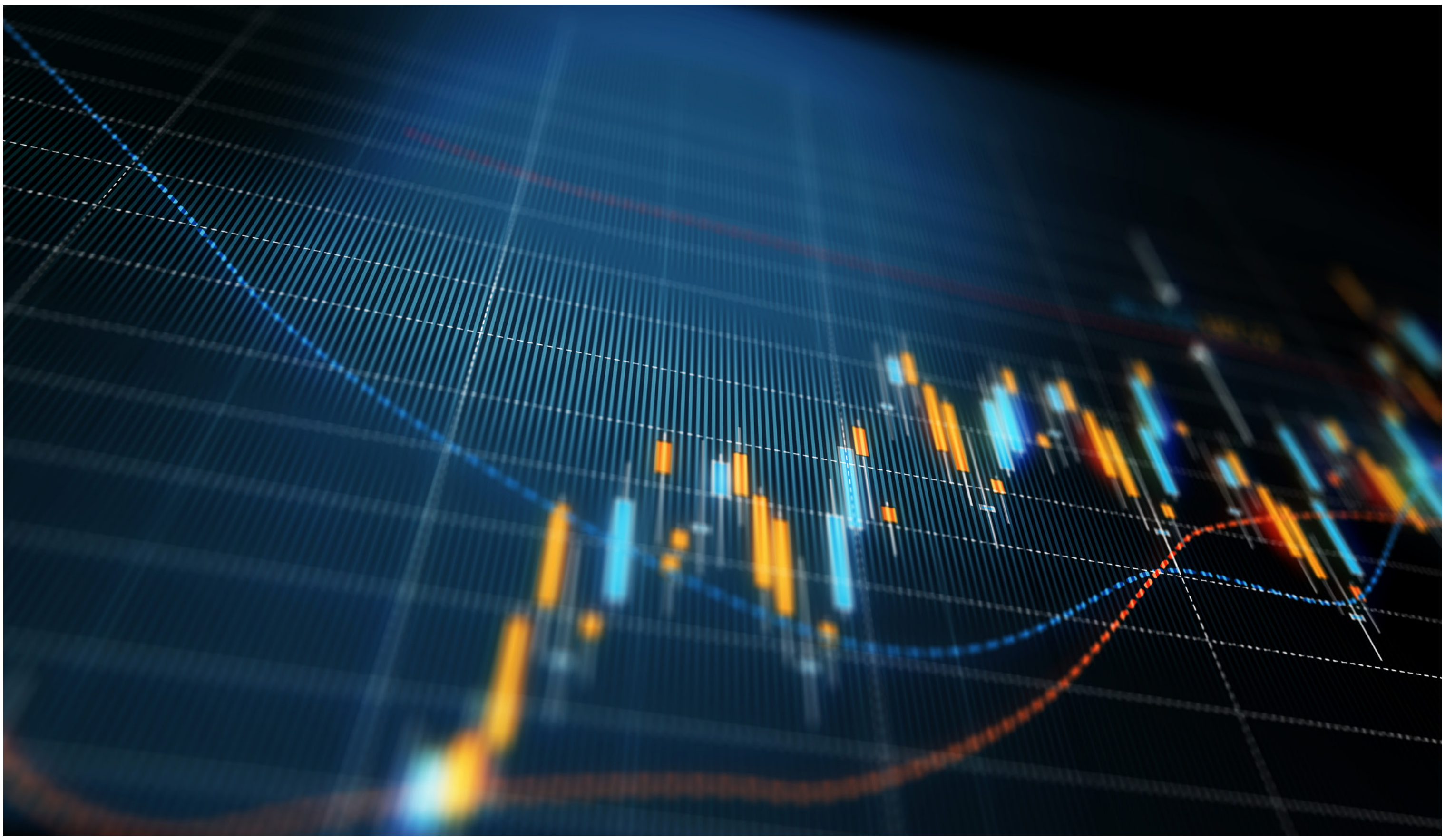
# Portfolio Manager Perspectives
# BlueBay Emerging Market Debt Update
## Weekly Update

March 12, 2020



## Volatility Endures

Markets continued to struggle with the effects of coronavirus: Wall Street was an exception, posting slight gains for the week, while European and EM equities were down. Oil prices plunged after OPEC+ talks collapsed, while a US rate cut helped EM FX performance.


**Summary**

Volatility continued across risk markets this week as investors struggled to price the impact of covid-19. US equities finished the week up 0.6%, while European and emerging-market (EM) equities ended down 1.8% and 3%, respectively.

In commodities, oil prices dropped dramatically following the breakdown of OPEC+ talks, with Russia taking an aggressive stance and scuppering a deal that would have slashed oil production in a bid to balance oil markets. This sent crude down more than 30% on the week and almost 50% over the month. To compound the pain, over the weekend, Saudi Arabia decided to explicitly increase oil production as a direct result of the breakdown in talks. Their likely strategy is now to grab market share with the hope that this forces everyone back to the negotiating table, but there is also the distinct possibility of a sustained price war with Russia.

In the US, the Federal Reserve cut interest rates by 50 basis points (bps) in an inter-meeting cut. The market was also buoyed by a positive showing from Joe Biden in the Democratic primaries.

In EM fixed income, local markets outperformed hard-currency markets as US rate cuts helped boost foreign-exchange (FX) performance, but it was rates markets that were the main driver of returns. In hard-currency markets, investment grade (IG)

outperformed materially versus high yield (HY), as the rally in core rates helped to boost total return (IG up 2% versus HY down 30bps). However, spread widening was material across both as prices could not keep up with the rampant price action in US Treasuries.

**Market review**

- Lebanon announced plans to miss a USD1.2 billion eurobond payment that was due on Monday (9 March). The government announced its intentions to restructure its debts in negotiations with creditors. At this stage, the government lacks any detailed plan as to the path forward and we feel that advisers will not have had enough to time to review the situation, leaving bondholders in 'wait-and-see' mode for now.
- Asian manufacturing indices continued to show a sharp deterioration as a result of the coronavirus. Governments have responded with a mix of targeted fiscal measures, including tax breaks, mortgage holidays and cash handouts. We also expect that central banks will continue to ease policy rates to help loosen financial conditions.

**Market outlook**

The double hit from an escalation in the coronavirus spread and much weaker oil prices has made for a toxic mix in EMs, in our opinion. The lower oil price, if sustained, may have a meaningful impact on the fiscal balance of many EM sovereigns and we believe raises the default rate for the EM sovereign and corporate asset classes.

Over the near term, we continue to expect elevated volatility in equity, credit and commodity markets. We believe that the volatility in current markets will mean investors have a need to de-risk their portfolios, collapsing risk as value-at-risk levels have increased.

For local markets, FX has already taken the brunt of the damage, but we feel it will remain volatile as US rate cuts help reduce the strength of the US dollar. However, growth is likely to be more important and, at this point, global growth expectations are falling. In our opinion, EM rates will suffer from position unwinds but, ultimately, will be interesting from the long side.

All of this sounds quite challenging, but what will help is a coordinated global response. We expect further interest-rate cuts across most central banks, and we should also see a robust fiscal response. We expect that targeted support will also be provided to individual sectors, such as airlines, and micro-level support to individuals who have been impacted – examples would be mortgage relief for people affected by the virus, tax payment holidays and direct cash transfers. We feel that this will be the first step towards building a policy cushion to, at least, partially offset the economic damage that has been inflicted over the last few weeks.

Index Review – Weekly Market Snapshot as of 03/06/2020

| | Total return | | | Spread / yield change (bps) | | | | |
|---|---|---|---|---|---|---|---|---|
| | Weekly | MTD | YTD | Weekly | MTD | YTD | Spread (bps) | Yield (%) |
| Hard Currency Sovereign | 1.14% | 1.14% | 1.68% | 29 | 29 | 111 | 402 | 4.84 |
| Hard Currency Corporate | 0.74% | 0.74% | 2.17% | 22 | 22 | 72 | 362 | 4.29 |
| Local Currency Corporate | 0.11% | 0.11% | -2.55% | 6 | 6 | 10 | 148 | 5.65 |
| Local Currency Sovereign | 1.62% | 1.62% | -3.11% | -19 | -19 | -46 | | 4.76 |

Source: Bloomberg, JPMorgan

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