Global Asset Management

BlueBay Asset Management

Portfolio Manager Perspectives
BlueBay Emerging Market Debt Update
Weekly Update

November 29, 2018

All Eyes on Buenos Aires

Risk assets came under pressure again this week as sharply lower oil prices, combined with weaker global PMI data, fuelled concerns of a more widespread economic slowdown. US high yield credit spreads widened aggressively on the week as default risk was priced back into some of the more leveraged oil names.

In equity markets, the US technology sector continued to suffer under the weight of lofty investor expectations.

In Europe, the focus remains on Brexit and the Italian budget. Although we expect more volatility to come, there were initially positive signs on both with the EU ratifying the Brexit agreement and the Italians taking a more conciliatory stance on the budget.

In emerging markets (EM), equities fell but outperformed developed markets, while EM local had another week of outperformance as the market continued to downwardly reprice its Fed rate-hiking expectations.

In EM News:

- The South African rand rallied after the central bank struck a hawkish tone and raised rates in response to what it sees as elevated inflation risks. The IMF signalled concerns over South Africa's public debt, which is reaching 'uncomfortable levels', according to the fund.
- In Mexico, incoming President AMLO held public consultations over the weekend to determine the fate of various infrastructure projects in a further sign of his unconventional approach, which is unnerving investors. The Mexican peso came under pressure yet again.
- The Indian rupee was again a strong performer as the central bank and the government resolved a dispute over the bank's capital, while in China bond yields rallied as rates are expected to head lower as the Chinese economy slows.
- Barbados disclosed indicative restructuring scenarios to the market after its default earlier this year. Initial thoughts involve extensions out to 15-25 years in new amortising bonds, although this is just indicative for now.

Weekly Market Performance as of 11/23/2018

	Total return 1 week	Total return MTD	Total return QTD	Total return YTD	Spread change 1 week	Spread change MTD	Spread change QTD	Spread change YTD	Current spread	Current YTM
Hard currency corp	-0.27%	-0.22%	-0.87%	-2.52%	10	24	40	74	334	6.16%
Hard currency corp - IG	-0.15%	-0.14%	-0.84%	-1.90%	7	20	34	49	227	5.08%
Hard currency corp - HY	-0.42%	-0.34%	-0.92%	-3.29%	16	30	55	117	494	7.87%
Hard currency sov	-0.70%	-0.92%	-3.06%	-6.01%	16	32	63	114	399	7.04%
Local currency corp	0.08%	1.21%	-1.14%	-2.91%	2	15	12	(21)	144	7.11%
Local currency sov	0.03%	2.60%	0.59%	-7.61%	n/a	n/a	n/a	n/a	n/a	6.58%
Local currency sov - rates	0.37%	1.44%	1.37%	1.61%	n/a	n/a	n/a	n/a	n/a	n/a
Local currency sov - FX	-0.33%	1.14%	-0.77%	-9.07%	n/a	n/a	n/a	n/a	n/a	n/a

Movers and shakers on the week

Sovereign credit		Corporate credit		EM FX		Local rates	
India	0.31%	Transport	-0.04%	South Africa	1.46%	Philippines	1.53%
Serbia	0.25%	Consumer	-0.16%	Turkey	1.02%	Dominican Rep	1.51%
Philippines	0.22%	TMT	-0.18%	Philippines	0.50%	South Africa	1.19%
Venezuela	-2.74%	Diversified	-0.42%	Brazil	-1.74%	Mexico	-0.21%
Nigeria	-3.09%	Infrastructure	-0.48%	Colombia	-1.88%	Russia	-0.26%
Ghana	-3.56%	Metals & Mining	-0.60%	Argentina	-1.98%	Turkey	-0.49%

Source: Bloomberg, JPMorgan. Past results are not indicative of future results.

In EM corporates news:

- The Mexican mining industry came under pressure as a senator in AMLO's Morena party called for tougher regulations on the sector. Mining stocks tumbled as a result.
- A Brazilian conglomerate defaulted on its 2025 bonds and hired advisors to help with a debt restructuring; bonds moved down around five points and began to trade flat of accrued interest.

Outlook:

November has been a difficult month as liquidity becomes more challenging into year-end, particularly in the context of generally weak returns among the investor community. Sharp moves in many risk assets are becoming the norm, with oil the latest domino to fall and the knock-on effects to other assets significant as we have seen in the case of the US high yield energy sector. It is therefore crucial to determine whether these price moves are the result of a regime shift or whether they are transitory and based on short-term factors, including technicals. In the case of oil, we see supply-side moves as the primary driver of weakness but also look ahead to the OPEC meeting on 6 December as a possible source of support for the market. Most fundamental analysis suggests oil prices should end 2019 higher than where spot prices are right now. We are willing to subscribe to this view for now. Therefore, looking through the noise, we do see some interesting valuations within the EM high yield credit space, given the sharp repricing over the last few weeks.

In the very near term the G20 meeting in Buenos Aires looms large with expectations growing that presidents Trump and Xi will be able to agree on a framework for further discussions around trade.

Looking further ahead, the market pricing of the Fed has been the most material move of late, with only two hikes now priced by the market for the rest of the cycle, whereas the Fed dots currently project five hikes. Ending up at either extreme will have meaningful implications for risk assets, although it is reasonable to assume that the reality may lie somewhere in the middle. For emerging markets, visibility into when the Fed will pause is, in our view, the key to being able to monetise more attractive valuation levels across both local and hard currency assets.