Like much of the investing universe, emerging market debt (EMD) experienced significant drawdowns in March 2020 as social distancing measures taken in response to the COVID-19 pandemic halted economic activity. However, as detailed in Exhibit 1, the asset class has historically been resilient, recovering more rapidly than most other markets following selloffs. EMD has taken on average only 0.8 years to recover in to the wake of selloffs (defined as drawdowns exceeding 10%) compared with 1.8 years for the global equity market, and over the past 20 years it has produced a positive return 97% of the time with an average annualized return of 9%.1

It is difficult to time markets under normal conditions, let alone in the current context, with so much uncertainty surrounding the virus and economic activity. While further downside risk undoubtedly still exists, volatility and dislocations present opportunities for active managers, and those with the ability to differentiate between resilient and fragile credits will potentially be able to buy oversold assets at cheaper prices.

Exhibit 1: Emerging market debt drawdowns and recovery periods

Source: Bloomberg as of 29 May 2020. Figures are in USD, unhedged.

Key takeaways

- **Resilience:** EMD has historically been a resilient investment in spite of periods of volatility and drawdowns. Over the past 20 years, it has produced an average annualized return of 9%, and there have been only three years in which it has produced a negative annual return.1

- **Strategic allocation:** In addition to the current favorable valuation, there are good reasons for investors to maintain a strategic allocation to EMD. These include the increased quality of the asset class, higher yields, diversification benefits and the attractive risk-adjusted returns of the asset class.

- **Active management:** The present environment will create opportunities in EMD for long-term investors and managers who are able to navigate the current turmoil and successfully differentiate between winners and losers.

To learn more about the EMD asset class, please see our white paper on the subject. (For reference – Resilience in Emerging Markets Debt)
Investment Insights

The Resilience of Emerging Market Debt

End notes

1 Source: Factset. Based on annualized monthly returns from December 31, 1998 to December 31, 2019.

2 Drawdown defined as peak-to-trough decline of 10% or greater. Recovery time calculated as the number of months from the month after a trough until the month in which the index returns to its prior peak. Indices are MSCI World = MSCI World Net Total Return USD Index, EMBI Global = JPMorgan EMBI Global Index.

3 Based on annualized total return data from 31 December 1998 through 31 December 2019, for the J.P. Morgan EMBI Global Index. Past performance is no guarantee of future results. It is not possible to invest directly in an index.

Emerging Markets: Emerging markets can have less market structure, depth, and regulatory, custodial or operational oversight and greater political, social, geopolitical and economic instability than developed markets.

J.P. Morgan EMBI Global Index measures dollar-denominated sovereign bonds issued by a selection of emerging market countries.

The MSCI World Index is a broad global equity index that represents large and mid-cap equity performance across all 23 developed markets countries.

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