



On May 22, 2020, Argentina defaulted on \$65 billion in debt owed to foreign bondholders.¹ Ecuador quickly followed Argentina.² Two more emerging-market countries, Suriname and Zambia, did so in November.³ As the pandemic raged across the world, causing the worst global economic crisis since 2008, investors braced for further sovereign defaults and more financial wreckage.

To put it mildly, the COVID-19 pandemic has walloped the world's emerging-market (EM) economies. Lacking the means for massive liquidity infusions, many EM countries had to stand by and watch as their economies came to a halt. Making matters worse, slow or nonexistent vaccine rollouts this year have been the norm across the EM world, prolonging the crisis there. The Emerging Market Bond Index has, not surprisingly, shown negative total returns since the beginning of the pandemic. Nearly 50% of the sovereign bonds issued by emerging-market nations carry a negative outlook from one or more of the three major credit-rating agencies, up from about a third as of December 2019.⁴ Only 5%, or 20 countries, have a positive outlook, according to the agencies.⁵

And yet, Scott Moses, portfolio manager for emerging market debt at MetLife Investment Management, says this is precisely the moment for optimism. "Despite the stress we've gone through, we feel there are significant opportunities within the EM landscape, especially as we work through the pandemic fiscal crunch toward a better global growth environment," he says. For one thing, the International Monetary Fund and other official

Finding Resilience

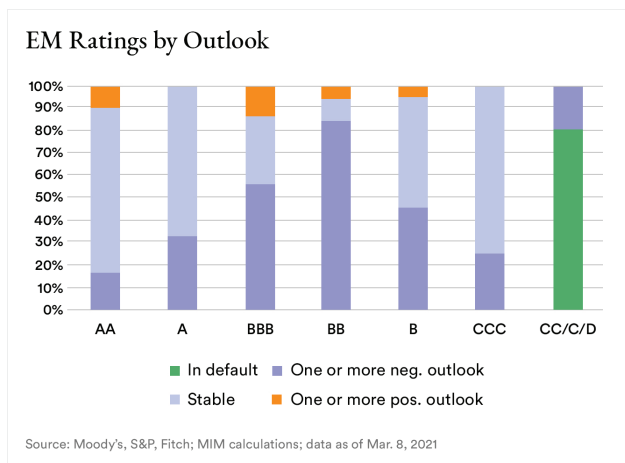
Emerging-market economies have experienced enormous challenges during the pandemic, and so have their bond issues. But the diversity of the asset class is its strength.

creditors have poured more than \$30 billion into 74 countries,⁶ helping to stave off multiple defaults and quieting fears of more on the horizon. More important, robust recoveries, led by China and the U.S., have boosted commodity prices, a boon to a sector in which more than half the countries are commodity exporters.

"Despite the stress we've gone through, we feel there are significant opportunities within the emerging-market landscape." — Scott Moses, Portfolio Manager for Emerging Market Debt, MetLife Investment Management

The commodity angle helps explain why investor inflows into emerging-market bond funds have been so healthy, with \$17 billion moving into such funds in the first quarter alone.⁷ Inflows aside, Moses says, "You have to be a little bit more careful how you attack the asset class, and what opportunities you'll see."

The key, says Moses' colleague Thomas Smith, who focuses on EM government bonds for MetLife Investment Management, is delving into the details. "Virtually every sovereign in the world was negatively affected by the pandemic, and early on we focused on trying to identify which countries would be most resilient through the pandemic," he says. "What we're looking for now, in 2021 and beyond, is who's stabilizing and at what pace."



One potential tell is reform: Which governments are willing to reevaluate their economic policies to try to achieve greater stability? One example is Costa Rica, currently pursuing a \$1.7 billion IMF fund program to help shore up its pandemic-shaken balance sheet.⁸ Or take Angola, in sub-Saharan Africa. Though the country has large oil reserves, and is thus a commodity play, Smith says the nation has also made notable improvements on the policy side, after putting an end to a civil war two decades ago and actively seeking to enhance its non-oil economy, especially in sectors such as agriculture and manufacturing.

Emerging-market corporate bonds are another potential bright spot, as the asset class continues to outperform the sovereign universe. Year to date (through March), EM corporates have outperformed sovereigns by approximately 3.7% after outperforming by close to 1.8% last year.⁹ The combination of balance sheet flexibility and shorter duration profile has benefited the asset class. Company-specific fundamentals, therefore, play a greater role in bond performance than global macroeconomic trends. Moses says he looks for companies that have been able to “de-lever” since the pandemic and to keep generating cash. “One of the biggest changes I’ve seen as an EM investor over the past 20 years,” Moses says, “has been improved skill and talent levels of corporate management teams. A lot of operators have gotten better at managing the volatility of their domestic markets and handling liquidity needs in times of stress.”

Acquiring this kind of deep knowledge—of coun-

tries as well as companies— can help mitigate all sorts of risk, including those associated with environmental, social and governance (ESG) factors. Social instability, for example, is highly correlated with income inequality and poverty levels, Smith says. If you find quality management teams and good governments, you have a greater chance of also finding resilience.

“I think investors often paint emerging markets with this broad brush,” Moses says. But, he adds, if you can dissect the asset class and differentiate between individual issues and companies, the opportunities become clearer. “There are definitely countries that are going to continue to struggle to come out of this. And we feel there are other countries that are going to come out of this in relatively good shape. And we believe those assets offer a lot of value.”

Sources:

1. Dube, Ryan and Santiago Perez, “Argentina Defaults on Sovereign Debt Amid Coronavirus Crisis,” The Wall Street Journal, May 22, 2020.
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3. Steinhäuser, Gabriele and Joe Wallace, “Africa’s First Pandemic Default Tests New Effort to Ease Debt From China,” The Wall Street Journal, November 18, 2020.
4. Howard, Todd and Thomas Smith, et al, “Emerging Markets 2021” MetLife Investments, March 26, 2021.
5. Ibid
6. Ibid
7. J.P. Morgan, EMTA.
8. “IMF Reaches Staff-Level Agreement with Costa Rica on a Three-Year Extended Fund Facility and Completes 2021 Article IV Discussions,” IMF, January 22, 2021.
9. J.P. Morgan, Cembis vs. EMBIGD, through 3/30 for YTD and for 2020.

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Appendix

This appendix contains details for the preceding charts and provides additional information for greater accessibility.

EM Ratings by Outlook

Note:

- All values are approximate
- Source: Moody's, S&P, Fitch; MIM Calculations: data as of Mar. 8, 2021

Rating	In default	One or more neg. outlook	Stable	One or more pos. outlook
AA	0%	16%	73%	11%
A	0%	33%	67%	0%
BBB	0%	57%	30%	13%
BB	0%	84%	10%	6%
B	0%	45%	50%	5%
CCC	0%	25%	75%	0%
CC/C/D	80%	20%	0%	0%