

EMERGING ATTRACTIONS

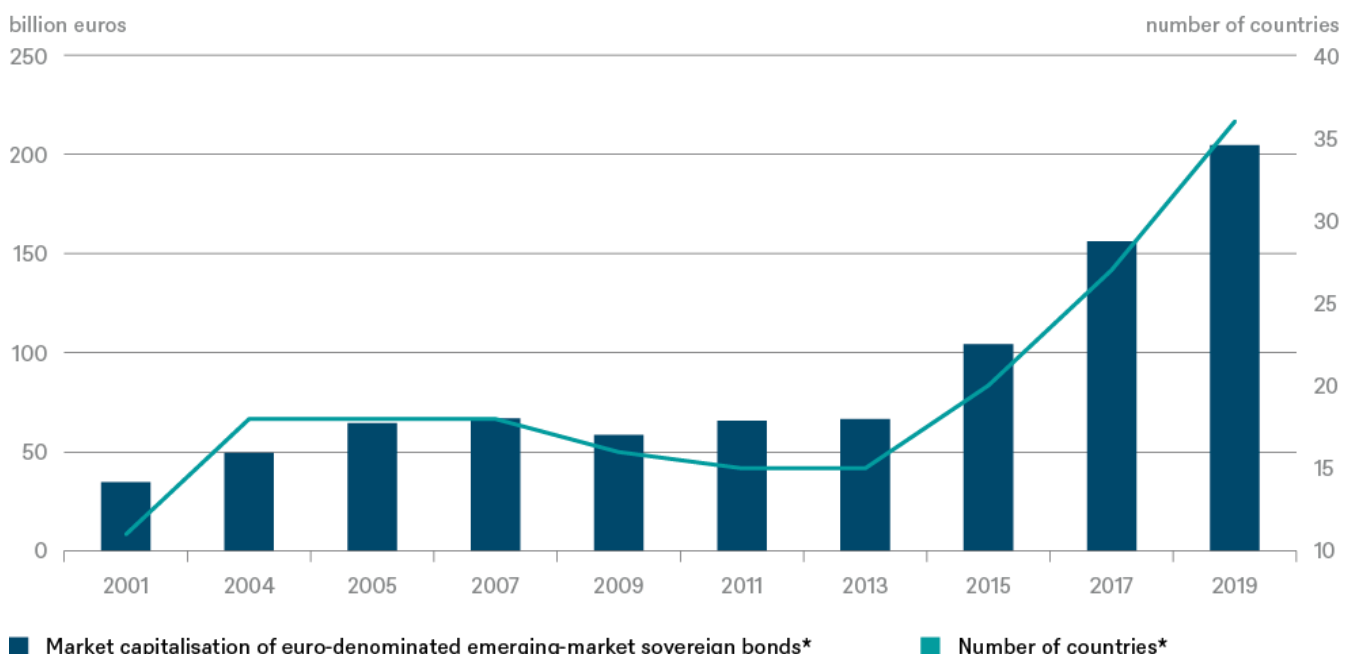
Emerging-market sovereign bonds denominated in euros offer ever more opportunities for diversifying credit risk.

Nowadays, if investors acquire a German government bond with 10 years to maturity, their investment of 100 euros will shrink to less than 95 euros by the time it is repaid in 2029. This calculation does not yet take into account the loss of purchasing power. If inflation rates were on average 1% per year, the investment would only buy goods and services worth 85 euros in 10 years' time. German sovereign bonds (sovereigns) are generally recognized as one of the safest investments in Europe. Yet, when it comes to preserving purchasing power, or even nominal value, they are far from perfect. Although techniques exist that may help to facilitate better capital preservation (see [Chart of the Week: How one might beat negative government-bond yields](#)), the search for alternatives is certainly worthwhile.

One example, Roland Gabert, fund manager at DWS, suggests considering, are emerging-market (EM) government bonds denominated in euros. The choices for investors have expanded significantly in recent years. Most EM bonds are still denominated in U.S. dollars. But the market for euro

-denominated bonds has seen strong growth since 2015. As Gabert points out, the composition of the J.P. Morgan Euro Emerging Markets Bond Index has grown by seven new countries in 2019 alone. Overall, the market capitalization has more than tripled since 2013, as our "Chart of the Week" shows. Of course, a larger universe has the potential to offer more opportunities for diversifying credit risk.

In terms of risk, EM sovereigns do not enjoy the same AAA credit rating as German government bonds. Their credit quality tends to be roughly equivalent to the European corporate-bond sector. Interestingly, bonds issued by a number of EM countries continue to have a yield premium over these issuers with comparable ratings. This implies that yields for core European sovereign bond yields can be considered a key driver for euro-denominated EM sovereigns as well. Unsurprisingly, almost one-third of euro EM bonds now also yield a negative return. However, we believe this still leaves a sufficiently large universe that deserves a closer look.



Sources: J.P. Morgan Chase & Co., DWS Investment GmbH as of 9/10/19

* Based on the J.P. Morgan Euro Emerging Markets Bond Index Global (Euro Embig)

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GLOSSARY

Emerging markets (EM)

Emerging markets (EM) are economies not yet fully developed in terms of, amongst others, market efficiency and liquidity.

Face value

Face value is the nominal value of a security stated by the issuer. For stocks, it is the original cost of the stock shown on the certificate, for bonds, it is the amount paid to the holder at maturity.

Inflation

Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.

J.P. Morgan Corporate Emerging Markets Bond Index (CEMBI)

The **J. P. Morgan Corporate Emerging Markets Bond Index (CEMBI)** is an index tracking dollar-denominated bonds issued by emerging-market corporates.

Rating

A **rating** is a standardized assessment of the creditworthiness of the issuer and its debt instruments by specialized agencies. The main three rating agencies are the Moody's (Aaa over Baa1 to C, best to worst), S&P (AAA over BBB+ to D, best to worst) and Fitch (AAA over BBB+ to D, best to worst).

Sovereign bonds

Sovereign bonds are bonds issued by governments.

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