UBAM – EMERGING MARKET CORPORATE BOND SHORT DURATION

Quarterly Comment

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws.
The classification of the fund(s) as per the Sustainable Finance Disclosure Regulation (SFDR) is available on ubp.com or in the latest prospectus

Market Comment

- US interest rates increased significantly over the quarter; 2-year US Treasuries were up 160bps to 2.33%, while 10-year US Treasuries rose by 83bps to 2.34% as the Fed delivered its first hike and the market priced more than 200bps of hikes until the end of the year.
- In terms of the risk environment, we downgraded our short-term expectations in Q1 2022, given Russia's invasion in Ukraine affecting the global supply chain, which was slowly recovering from the pandemic.
- Fears of rising interest rates kept investors away from fixed income in general over last quarter. The asset class saw outflows at -$14.1bn, according to data from JP Morgan. This follows up from weak flows of +$0.3bn in Q4 2021. In 2021, EM Fixed Income funds saw an inflow of $52.5bn.
- Rising US Treasury yields paired with the geopolitical crisis impacted returns across most of fixed income in Q1 2022. EM Corporate bonds delivered returns of -9.3% over the quarter according to the JP Morgan CEMBI Div index.
- Over the quarter, EM Investment Grade corporate bonds underperformed the broader EM Corporate universe, returning -9.9%, while their High Yield counterparties returned -8.5%, outperforming the broader index. Spreads over US Treasuries widened by 17bps to 318bps in Q1 2022.

- At a regional level, Africa (-3.61%) fared better than others, while Emerging Europe (-47.9%) was the worst performer due to Russia's exclusion from the JP Morgan indices with the exit price of 0.
- At a country level, the best performance came from Turkey (+0.4%), Paraguay (-0.5%) and Zambia (-1.2%). The worst performance by country were in Emerging Europe with Russia (-66.3%)* and Ukraine (-53.5%), while Moldova (-15.4%) and Kazakhstan (-14.8%) also suffered.
- At a sector level, the worst performance came from Metals & Mining (-20.7%) and Oil & Gas (-15.8%) and Industrial (-10.7%).
- The shorter end of the credit curve suffered the most over Q1 2022 as short-term US Treasury yields rose: 1-3-year EM corporate bonds returned -11.9%, while 3-5-year bonds were at -6.2%, ahead of longer maturity buckets.

**As of February 2022, before its exclusion from the index*
Sources: UBP, Bloomberg Finance LP, JP Morgan

All performance figures are given net of fees. Past performance is not a guide to current or future returns. See full disclaimer at the end of the document.

Performance Review

- Over the quarter, the fund returned -8.18 % net of fees. The fund marginally benefited from its high carry but widening spreads and duration outweighed negatively as yields rose at the short part of the yield curve.
- At a country level, the worst performance came from our holdings in China, Russia, Belarus, and Ukraine. In contrast, our allocation to Ghana proved beneficial over the course of the quarter.
- At a sector level, the worst performance came from Financials and Industrials, followed by Consumer and our holdings in Sovereign bonds.
- Our allocation to HY CDX indices contributed negatively at -19bps.

Portfolio Activity

- Over the quarter, our scorecard fell into in the "conservative" territory, with March marking the lowest score in the last twelve months in the view of deteriorating risk environment, although EM fundamentals moved into positive territory.
- In Africa, we reduced our exposure to Cameroon (sovereign) and Nigeria (TMT).
- In Asia, we reduced our holdings in China across a number of sectors. We also sold holdings in India and Indonesia over Q1 2022. We marginally added exposure to Macau gaming sector.
- In Emerging Europe, we decreased our holdings in Russia and Ukraine.
- In Latin America, we sold our holdings in Brazil across multiple sectors, predominantly in the Industrial sector. We sold our TMT holdings regionwide. We reduced our exposure to Guatemala sovereign bonds over the quarter.
- In the Middle East, we reduced our exposure to UAE's Financial and Infrastructure sector.

Outlook

- Inflation has risen to elevated levels globally and has impacted interest rates world-wide. Many EM Central banks have hiked early, starting a tightening cycle in early 2021 already for some of them. DM Central banks first read this inflation as transitory and have been reassessing their outlook and seem now set for a quicker tightening of their interest rates.
- US rates have sold off significantly in Q1 2022 and remain a risk to be watched carefully going forward. The curve is now pricing a significant amount of tightening by end of 2022 (about 2.5% in rate hikes according to Fed Fund futures).
- The front end of US curve (up to 2years) is now very steep, and yields start to be compelling on the asset class. We wouldn't expect in the short term a strong rally back in rates or spreads, but the increased carry should start to do its work in helping the asset class performance.
- In Q1 2022, about USD 15bln exited the asset class (mainly retail). Despite the negative Q1 performance, but on the back of higher yields, we would expect investors to get attracted back in the asset class.
- Front end yield has become appealing (6.47% at the end of March for the fund). This high level of carry should provide a good cushion to dampen any potential further move in spreads or rates, for a product that has a reduced level of sensitivity via its lower duration.

- At a regional level, our main exposure are in Latin America and Asia.
- At a country level, our largest weights are on China, Colombia and Brazil
- At a sector level, our largest positions are in TMT and Consumer.

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