UBAM – EM SUSTAINABLE CORPORATE BOND

Quarterly Comment

For Professional Investors in Switzerland or Professional Investors as defined by the relevant laws.

Market Comment

- The third quarter was split in two, with the continuation of the market optimism seen in Q2 in July and August and renewed concerns in September amid signs a resurgent virus could lead to more lockdowns and a deeper global recession.
- Over the quarter, US treasury bonds appear fairly stable, masking a rally in July, a sell-off in August when expectations that the worst had been avoided were predominant, and a new rally in September when the pandemic accelerated again. Overall, the curve steepened slightly, with 2-year US Treasury rates down -2 bps to 0.13% and 10-year rates up +3 bps to 0.68%.
- Commodities were also weak in September, on concerns of lower demand but overall stronger over the quarter. The CRB index was up by 7.6%, thanks notably to the rally in metal prices (silver +28%, iron ore +18%, copper +11%, gold +5.9%). Oil prices underperformed, however, up only 2.4%. The OPEC cut demand estimates for its oil by 1.1 million barrels a day, while surplus stockpiles of crude and refined products continue to build up.
- Contrary to many countries around the world, there are already signs that economic activity is picking up in China. Industrial production was up in August by 5.6% yoy. Manufacturing PMI came at 51.5 in September, while non-manufacturing PMI stood at 55.9.
- Overall, EM corporate bonds returned 2,63% over the quarter, with spread tightening by 29 bps to 386 bps.
- Investment grade and High Yield bonds posted very similar performance of 2.6%.
- At a regional level, the best performance came from Latin America (+4.4%) and the Middle East(+2.8%). In contrast, Europe (+0.7%) and Asia (+2.1%) underperformed.
- At a country level, the best performance came from Brazil (+6.0%), followed by Egypt (5,9%) and Bahrain (5.8%).
- In contrast, the worst performance came from Ghana (-16.5%),.Kazakhstan (-8.4%) and Argentina (-0.8%) also posted negative performance.
- At a sector level, the best performance came from Pulp & Paper (+7.3%), Transport (+5.5%) and Infrastructure (+5.3%). In contrast, Oil & Gas underperformed (1.5%) reflecting the sell-off in crude prices in September. TMT (+2.1%) and Consumer companies (+2.2%) also underperformed.
- Over the quarter, the performance of EM Sustainable corporate bonds (+2.7%), as measured by JP Morgan ESG CEMBI Broad index was broadly in line with the overall EM corporate bond universe.

Sources: UBP, Bloomberg Finance LP, JP Morgan

On April 1, 2020, UBAM – EM Sustainable High Grade Corporate Bond was renamed UBAM – EM Sustainable Corporate Bond. On June 8, 2020, the fund widened its investment guidelines to include HY issuers.

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 2.63% net of fees, in line with the JP Morgan CEMBI Diversified index*.
- Performance attribution shows that the fund outperformed, gross of fees, thanks to its credit selection (carry and spread effect). Our interest rate duration positioning was neutral, but our curve positioning detracted proved costly.
- Country-wise, the best performance came from our underweight in Kuwait, overweight in Chile as well as from our zero holdings in Ghana and our underweight and selection in Israel.
- In contrast, our underweight in Brazil, selection in Mexico, and underweight in the UAE proved costly.
- Sector-wise, the fund benefited from its overweight and selection in Industrials, selection in Utilities and underweight in Oil & Gas and Financials. In contrast, overweight in TMT proved costly.

**Index provided for comparison and information purposes only. The fund has no official benchmark.*

Portfolio Activity

- We added exposure to Sino Ocean, a Chinese real estate company, which is which has close to 50% of its portfolio is in green-certified buildings. The company also puts high emphasis on health and safety. It is ESG-rated BBB and is not involved in any controversy.
- We increased holdings in Colbun, a Chilean utilities company. The company targets to add around 4,000 MW of renewable capacity by 2030 and announced its plan to retire its coal power plants by 2040. It also increased efforts to protect biodiversity and ecosystems.
- We sold exposure to REC Limited, an Indian government-owned financial company, following the downgrade of its ESG rating to B from BBB. This was triggered by the departure of two independent directors, leaving the company with an undersized board and a weak governance structure.
- Two of our holdings in India TMT were called over the period.
- Due to new inflows late September, the fund held a fairly large cash position at the end of the quarter. This cash was gradually invested early October

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Outlook

- We expect the pick-up in volatility seen in September to remain in the short-term, given the increased risk of new lockdowns and the upcoming US elections. Still, we remain constructive on emerging debt for the medium-term.
- Indeed, the pandemic-triggered recession is likely to be less severe in emerging markets than it will be in Developed Markets (DM), and the rebound next year is expected stronger. In its World Economic Outlook, published early October, IMF forecasts emerging economies to slow by 3.3% this year and bounce back by 6.0% in 2021, vs -5.8% and +3.9% respectively for DM.
- Also, investors' appetite for yield remains high and valuations of EM bonds appear attractive especially compared to US and Euro credit, where the combined actions of G3 central banks have pushed Developed Market yields to extremely low levels.
- Importantly, if considering corporate issuers, fundamentals appear more solid than in DM, as leverage for both IG and HY issuers remains lower in EM than in DM. As it is, year-to-date, the default ratio in EM corporate remains lower than in US High Yield credits.
- Still, we recognize that the economic slowdown will have a negative impact on issuers' creditworthiness. Hence, thorough issuer selection remains of paramount importance. We thus rely on our sovereign and credit analysts to avoid negative credit events, with special focus on:
    - Issuers' capacity to generate operating cashflows and maintain a good level of activity, and keep adequate liquidity
    - Their capacity to refinance
    - Their ability to support the leverage accumulated during the crisis
    - Valuations to identify attractive opportunities (overly penalised issuers)
- At a country level, our largest overweight positions are in South Africa, Chile, Hong Kong, Russia and Singapore.
- Our largest underweights are in China, Brazil, Israel, Saudi Arabia and Turkey.
- At a sector level, our largest underweight is in Financials while our largest overweight is in TMT.

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ESG Metrics

- At the end of the quarter, the overall ESG Quality Score of the portfolio was 70% higher than the index, standing at 6.57 (equivalent to an MSCI ESG Rating of A) vs. 3.86 for the index (equivalent to an MSCI ESG Rating of BB) (@2020 MSCI ESG Research LLC).
- The weighted average carbon intensity[1] of the fund was 29% below its index, at 477.6 tons CO2e/$M sales revenues v. 672.9 tons CO2e/$M sales revenues for the index. (@2020 MSCI ESG Research LLC).
- According to ISS, scope 1,2, and 3 greenhouse gas emissions stood 19% below those of the index.
- 59% of the electricity generated from our holdings in the utilities sector came from green power. In comparison, in the index, 72% of the electricity generated came from brown, fossil-fuel related, sources.

- International norms (source: @2020 MSCI ESG Research):
  - Violation of UN Global Compact: 0% (v. 3.3% in the index)
  - Violation of Human Rights norms: 0% (vs. 2.1% in the index)
  - Violation of Labour norms: 0% (vs. 1,3% in the index)

[1] taking into account subsidiary mapping

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