



UBAM – EM RESPONSIBLE CORPORATE BOND

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

- The Federal Reserve (Fed) raised interest rates by 25 bps in May. However, it did not hike rates in June, adopting a hawkish pause. The rate predictions indicated two further rate rises in 2023. There were some concerns around US debt ceiling at the beginning of the second quarter. However, US Congress approved a legislation that suspended the debt ceiling in the first days of June, in a deal that included concessions on spending expected to have little effect on economic growth.
- The European Central Bank (ECB) raised interest rates twice in the quarter, taking the main refinancing rate to 4.0%. Headline inflation declined during the period, with annual inflation estimated at 5.5% in June, down from 6.1% in May. However, the core inflation rate went up to 5.4% in June. The eurozone composite purchasing managers' index (PMI) fell to 50.3 in June from 52.8 in May.
- Enthusiasm around AI and the potential for a boom in related technology drove chipmakers, in particular, higher, as well some expectations of how the productivity might increase in certain sectors of the economies.
- Tension between the US and China was a contributing factor behind EM underperformance, as were concerns about China's anaemic economic recovery. Hungary, Poland and Greece were the top-performing index markets despite rising recessionary fears in Europe. Brazil was also a top performer amid easing fiscal policy concerns, optimism about potentially imminent rate cuts and a better print in the Q1 GDP data.
- Colombia was up too, as were the UAE, Peru, Saudi Arabia and Mexico. Korea and Taiwan outperformed on the back of the optimism around AI growth.
- China underperformed amid concerns over a weaker than expected economic recovery. South Africa was among the worst performers as the country's power situation continued to deteriorate, with severe consequences for economic growth. Turkey posted the largest loss in US dollar terms. This came with the news of Erdogan re-election in May.
- According to data and JP Morgan research forecast, Emerging Markets bond flows have seen an decrease of \$2.2bn since the beginning of the year, with the exception of local currency bonds. High yielding rated and a weaker dollar keep being supportive to the sub-asset class.

Sources: UBP, Bloomberg Finance LP, JP Morgan

Performance Review

- Over the quarter, the fund returned 1.58% net of fees compared to +1.29% for the JP Morgan CEMBI Diversified index.
- Duration management was active and moved to 0.7yrs long to position in a market with higher risk appetite. Outperformance mainly came for credit issuer allocation (+48bps).
- An UW in Asia / Pacific (China, Hong Kong, Taiwan and Singapore) continued the main performance contributor.
- An OW in Latin America, alongside with the allocation in Thailand and S. Korea, specially in HY issuers, added to the overall performance.
- In terms of sectors, industrials and financials contributed the most to positive results.

Portfolio Activity

- Over the quarter, we increased our exposure EM Europe and Middle East. On the other hand, reduced in Asia.
- In EM Europe, we initiated exposure to Czech Rep. Hungary, Romania and Slovakia, mainly in the Financial sector.
- In Middle East, we closed our position in Qatar (Oil & Gas) and added to Israel (Financials).
- In Asia ex Japan, we closed our position in Malaysia (TMT and Transport), reduced India and S. Korea (various sectors).
- In Latin America, overall exposure remained the same, but with changed in country and sector allocation, reducing Colombia (TMT) and increasing Mexico (Utilities and Consumer)

Outlook

- As experienced in May, US base rates continued increasing in June on the back of US strong activity indicators especially in the services sector. We continue being of the view that we are at the end of FED's hiking cycle, and the main part of US base rates adjustment is behind us. Consequently, US base rates should be supportive of hard currency fixed income returns during the rest of the year.
- Besides with the US debt ceiling agreement reached recently, a big source of volatility is behind us and investors' risk appetite has returned leading to a very good performance of DM and EM equities, EM FX, EM sovereign and corporate debt.
- It is worth highlighting that we are seeing a decoupling in DM vs EM inflation dynamics and central banks' actions and guidance. In EM countries there are clear signs of inflation subsiding with central banks pausing and heading into the start of an easing cycle in the short term, while in DM central banks continue with a hawkish stance as inflation dynamics are still not that positive and above targets. As inflation falls, high real rates and FX appreciation should give EM central banks space to cautiously ease policy starting in 2H23, despite DM CBs continuing to tighten to tame core inflation. Some CBs, especially in Latam, could take advantage of this mix and stronger external accounts to start accumulating reserves anticipating rockier seas ahead. Others, such as in CEE, might opt to tolerate stronger currencies to aid in the short-term disinflation process (considering large FX buffers already and EU money to support them). EM Asia may intervene to smooth FX volatility.
- The start of a near term easing cycle in EM countries and inflation subsiding is obviously good news for EM corporates, although this comes as a consequence of a deceleration in activity that has already been translated into more negative companies' outlook for the current year compared to 2022. Having said this, it is worth reiterating that EM IG companies on an aggregate level are in a very healthy credit position in general, having deleveraged in past years and having extended their debt maturities at lower interest rates taking advantage of the low interest cycle prior to the quantitative tightening cycle, so they stand on solid foot to weather a challenging period.
- Besides, recently we have seen some positive developments in various Latin American countries leading to a decrease in political headwinds. For instance, in Colombia and Chile, the popularity of the left wing presidents has been trending down turning the probability of radical non-market friendly reforms low.
- Finally, in this context of renewed appetite for risk, we have seen a pick-up in primary market new issuances met by solid demand from investors with books highly oversubscribed and leading to solid performance of the new issues in the secondary market as investors are underweight EM fixed income asset class.
- In terms of strategy, we continue with our high conviction positioning, underweighting Asia, including China, on the back of relatively weak issuers' credit metrics, poor governance, and tight valuations for the risks implied and compared to issuers from other regions such as Latin America. On the other hand, we continue overweighting Latin America as these issuers offer attractive spreads and yields for the risks implied on a relative basis vs other regions. We believe this positioning will continue bearing its fruits during the rest of the year.



ESG Metrics

- At the end of Q2, the overall **ESG Quality Score** of the portfolio was 23% higher than the index, standing at 6.5 (equivalent to an MSCI ESG Rating of AA) vs. 5.3 for the index (equivalent to an MSCI ESG Rating of BBB)

Source: @2023 MSCI ESG Research LLC - coverage: 93% for the fund and 88% for the index.

KEY INDICATORS

- The **weighted average carbon intensity**¹ of the fund is 55% below its index, at 273 tons CO₂e/\$M sales revenues v. 603 tons CO₂e/\$M sales revenues for the index.

Source: @2023 MSCI ESG Research – coverage by number of issuers: 92% for the fund and 91% for the index.

- **International norms:**

- Violation of UN Global Compact: 0% (vs. 0.7% in the index)
- Violation of Human Rights norms: 0% (vs. 0.7% in the index)
- Violation of Labour norms: 0% (vs. 0.3% in the index)

Source: @2023 MSCI ESG Research - coverage level: 90% for the fund and 89% for the index

- **Board Independence:** 84.7% of the portfolio is invested in companies that have a majority of independent board members, vs 74.3% for the index.

Source: @2023 MSCI ESG Research - coverage level: 90% for the fund and 86% for the index

- **Board Diversity:** 89.2% of the portfolio is invested in companies that have at least one female Director, vs 87.5% for the index.

Source: @2023 MSCI ESG Research - coverage level: 90% for the fund and 86% for the index

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