UBAM - EM RESPONSIBLE SOVEREIGN 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 year began with positive sentiment on the growth outlook as energy costs fell and China's economy reopened. However, February and March saw US-China tensions re-escalate and a widespread loss of confidence in US and European banks. The Fed hiked rates to new highs and further reduced liquidity. EM has benefited from the shift of relative growth momentum with a rebounding mainland China and surprisingly resilient Europe. EM central banks generally were not constrained by financial stability concerns and remained focus on inflation. The collapse of Silicon Valley Bank in mid-March and the later Credit Suisse bought by UBS in a deal brokered by the Swiss authorities, reduced concerns over re-accelerating inflation. It caused a sharp rally in government bond markets due to fears of a possible banking crisis, where government bond markets went from pricing in rate hikes to discounting sizeable rate cuts. Following the strains on the US and European banking sector, EM Financials conversely did well during the first quarter.
- Emerging Markets bond flows have seen an increase of +$2.1bn since the beginning or the year, where a widening EM-DM growth differential and a more benign dollar supported EM capital flows, according to data and research forecast from JP Morgan.
- At a country level, the best performance came from Malaysia (+4.4%), Thailand (4.2%) and Taiwan (+3.7%). The worst performance was delivered by Egypt (-2.2%), Nigeria (-1.6%), and Panama (-1.4%).

Sources: UBP, Bloomberg Finance LP, JP Morgan

Performance Review

- Over the quarter, the fund returned +0.21% net of fees, compared to +1.86% for the JP Morgan EMBI Global Diversified Index. Gross of fees, UBAM - EM Responsible Sovereign Bond returned +0.50%, underperforming its index by -1.36%.
- The quarter saw higher rates and widening spreads. In relative terms, the fund suffered from its duration positioning with -1.29%, but compensated by its curve positioning with +0.13%. Its issuer selection also brough relative negative results with -0.36%.
- Main contributors to relative performance were:
  - On the positive side, the selection and underweight in Ecuador and the underweight in Hungary, Romania, Mexico and Costa Rica.
  - On the negative side, the selection in the Gabon, Kenya, Egypt and Ivory Coast.

Portfolio Activity

- In Africa, we increased our exposure Cote D'Ivoire, Gabon and Kenya. On the other hand, reduced South Africa and fully sold our exposure to Egypt.
- In Asia, we reduced our exposure to the Philippines.
- In Latin America, we reduced the exposure to the region as a whole. We initiated exposure to Colombia. We also increased our exposure to some countries such as Costa Rica and Dominican Republic. Conversely, we sold our exposure to Ecuador, El Salvador, Paraguay and Peru and decreased our exposure to some countries such as Chile, Mexico and Uruguay.
- In the Middle East, we increased the exposure to Oman.
- In Emerging Europe, we increased our exposure to Romania. We sold our exposure to Czech Rep and decreased our exposure to Hungary.
- Our investments in Supranational issuers in local currency bonds denominated in KZT and INR remained – such securities typically finance development projects in those countries.
- The fund achieved an MSCI ESG Quality Score of 4.4, outperforming the standard market index (JP Morgan EMBI Global Diversified), which returned an ESG Quality Score of 3.5. (Source: MSCI ESG Research. Data as of 31.03.2023).

Outlook

- Although the high volatility in US base rates has been seen a the sharp decrease in yields on the back of financial stability concerns during the first quarter, we think we are close to the end of Fed’s hiking cycle and the main part of US base rates adjustment is behind us. The significant market repricing of monetary policy trends for core CB has also led to a reassessment of the next steps for EM CB. Expectations for cutting rates on several EM CB (in LatAm and CEEMEA) in the next year are now higher. For the few countries where further tightening is expected (Thailand, Mexico, and South Africa), markets are pricing a more accommodative stance.
- With regards to EM corporates, as in previous months, the outlook for 2023 is more challenging compared to 2022, on the back of the tighter financial conditions and increased inflation that will exert their full impact on corporates’ financials figures during this year. However, on an aggregate level EM IG corporate credit fundamentals remain healthy 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.
- Additionally, EM IG corporate valuations (spreads) look very attractive for the risks implied compared to other regions such as US IG, with almost 100 bps spread pick-up in the case of LATAM IG, for instance. It is worth highlighting that we maintain our OW in LATAM as we continue seeing solid fundamentals and very attractive valuations on a relatively basis vs other EM regions.
- On the other hand, recent movements in local currency debt could open up opportunities and we focus on LatAm, South Africa and India. Overall, EM growth and a stable policy backdrop are positive for EM assets, including hard currency debt. We are monitoring the political environment in Turkey, but do not see insolvency risks. Country selection is essential amid the geopolitical tensions over China and the United States.

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