Q1 2024

# 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 U.S. economy continued to demonstrate robustness into the first quarter of 2024, defying the widespread anticipation of economic slowdowns. Despite market expectations leaning heavily towards rapid central bank rate cuts at the beginning of the year, U.S. economic data revealed persistent high inflation and a strong labour market, with over 300,000 jobs created in March alone. This sustained economic vitality led to a revision of growth forecasts upwards. However, the Federal Reserve, noting the economic strength, delayed any rate cuts, with the first reduction now postponed to the second quarter. Consumer spending showed resilience, though it did not match the growth rates of previous quarters.
- In contrast, Europe's economy lagged significantly behind the U.S., with the first quarter showing continued fragility. The Eurozone fluctuated between recession and stagnation, with significant disparities between its member countries. By the end of March 2024, inflation in the region had slightly decreased to 2.4%, with core inflation at 2.9%. The European Central Bank (ECB) responded by cutting its inflation forecast for 2024 to 2.3% and growth forecast to 0.6%, adopting a wait-and-see approach to further rate cuts.
- Japan faced continued challenges from a slowdown at the end of the previous year, with early 2024 remaining weak. However, there was a noticeable rebound in manufacturing confidence and exports by quarter's end. The Bank of Japan ended its negative interest rate policy and introduced a target rate range of 0-0.1%, marking a significant shift in its monetary stance.
- Emerging markets displayed a diverse performance but generally underperformed compared to developed markets, with overall gains of 2.0% in dollar terms. This was particularly marked by underperformance in China and Brazil, which saw declines in their local markets.
- China showed slight economic improvements by the end of the quarter, buoyed by the Chinese New Year and governmental measures. The growth target for 2024 was set at 5% during the National People's Congress in March, with a strategic focus on curbing inflation to 3%.
- Commodity markets saw significant activity, with oil prices rising by 16% in the first quarter, driven by OPEC+ production cuts and geopolitical tensions. Gold prices surged to a record high of over USD 2,200 per ounce by March 2024, largely as investors sought safe-haven assets amidst economic uncertainties.
- Equity markets were buoyant, with the S&P 500 and other major indices reaching all-time highs, driven by optimism for a steady recovery and potential central bank rate cuts later in the year. Despite the upbeat performance in equities, sovereign debt markets faced headwinds, with rising yields contributing to negative returns across various regions, including a -0.9% return in the U.S. and -1.9% in the UK for the first quarter.
- EM investment grade corporate bonds index was up by 1% (JPM CEMBI BD IG), led mainly by the tightening in spreads (spreads tightened by 24bp to 130bp). By region, Asia IG spreads tightened by 29bp, Latam IG by 22bp, EM Europe by 19bp and Middle East by 20bp.
- At a country level, the best performing countries over the quarter were Panama (+4.1%), Israel (2.6%) and Egypt (+2.2%). The worst performing countries were Saudi Arabia (-0.3%), Taiwan (0.3bps) and Czech Republic (0.4%).


- At a sector level the best performing sectors over the period were Infrastructure (+2.2%), followed Financial (+1.4%). The worst performing sectors were Oil & Gas (+0.3%) and Industrial (+0.6%).

  *Sources: UBP, Bloomberg Finance LP, JP Morgan*

## *Performance Review*

- Over the period, the fund returned 0.21% net of fees (share:IC USD) compared to 2.34% for the JP Morgan ESG CEMBI Broad Diversified index.
- Duration was actively manage being 4.17 years compared to the index to 4.33 years. This duration alignment contributed a positive 0.04% due to parallel shift effect.
- Underweight positions in Africa / Middle East, specifically in Nigeria and Ghana, continued as key performance detractors. Latin American countries such as Mexico and Colombia, and in Asia, notably Hong Kong and India, added positively to the performance.
- Within sector performance, finance and utilities sectors were the top performers, while industrials dragged down performance due to a significant negative spread effect of -0.47%

## *Portfolio Activity*

- This quarter, we made strategic adjustments to our portfolio to align with the current economic conditions across various regions.
- Africa: Decreased exposure to South Africa.
- Asia: Increased exposure to Macau in Consumer, South Korea in Industrial and Financial, and Thailand in Utilities and TMT. Expanded in India's TMT sector. Decreased in Hong Kong and China's Financials and Industrials.
- Europe: Increased investments in Turkey's Consumer and Industrial sectors. Decreased exposure in Hungary, Poland, Romania, and the Czech Republic's Financials.
- Latin America: Boosted exposure in Brazil across multiple sectors and in Mexico's Real Estate, Transport, and Financials. Reduced exposure in Colombia and Costa Rica. Made positive adjustments in Peru and Argentina, focusing on Utilities in Peru.
- Middle East: Increased exposure in Kuwait's Financials and the UAE's Real Estate.

## *Outlook*

- The U.S. economy continues to display resilience with growth projections remaining robust at over 2% for 2024. Despite global economic uncertainties, the U.S. stands out for its strong economic fundamentals, supported by a firm labour market and sustained consumer spending. However, inflation challenges persist, with rates expected to remain above 3% into the second quarter before gradually declining towards 2.5% by year-end. This inflationary pressure keeps the Federal Reserve cautious, delaying any significant rate cuts until inflation is firmly under control.


- In contrast to the U.S., the Eurozone's economic recovery remains tepid, with overall growth rates not expected to exceed 1%. The region shows signs of disparate recovery trajectories among its member countries, with Spain exhibiting stronger growth while others lag. Inflation in the region is slowly abating, allowing for potential monetary easing later in the year if the trend continues. Fiscal deficits remain a concern, with most countries projected to run deficits well above the 3% GDP mark, challenging the adherence to Maastricht fiscal rules.
- Emerging markets are set to experience varied growth in 2024. China's growth is forecasted at 4.5%, dampened by ongoing real estate sector issues. Conversely, India and other countries in Asia and Latin America are expected to achieve stronger growth, buoyed by robust domestic demand and favourable macroeconomic conditions. The investment climate in these regions is supported by significant structural shifts such as nearshoring and diversification away from traditional economic dependencies like Russian commodities.
- Countries reliant on commodities are expected to benefit from the global economic restructuring, including those in Africa, Latin America, and parts of Asia. The geopolitical landscape, particularly tensions in the Middle East, poses risks that could influence global oil prices and economic stability. These factors necessitate a vigilant investment approach, balancing the potential for high returns against geopolitical and economic uncertainties.
- Central banks globally are signalling a more accommodative monetary stance as inflation pressures begin to ease. While the U.S. Federal Reserve may be slower to cut rates, other central banks are preparing for potential rate reductions as early as June 2024, contingent on sustained decreases in inflation. This global shift towards monetary easing could support further economic recovery across both developed and emerging markets.

## *ESG Metrics*

- At the end of Q1, the overall **ESG Quality Score** of the portfolio was 11% higher than the index, standing at 5.9 (equivalent to an MSCI ESG Rating of A) vs. 5.3 for the index (equivalent to an MSCI ESG Rating of BBB)

  *Source: @2024 MSCI ESG Research LLC - coverage: 88% for the fund and 86% for the index.*

**KEY INDICATORS**

- The **weighted average carbon intensity**[1] of the fund is 48% below its index, at 294 tons CO2e/$M sales revenues v. 566 tons CO2e/$M sales revenues for the index.

  *Source: @2024 MSCI ESG Research – coverage by number of issuers: 86% for the fund and 84% for the index.*
- **International norms**:
  - Violation of UN Global Compact: 0% (vs. 0.8% in the index)
  - Violation of Human Rights norms: 0% (vs. 0.8% in the index)
  - Violation of Labour norms: 0% (vs. 0.0% in the index)

  *Source: @2024 MSCI ESG Research - coverage level: 86% for the fund and 84% for the index*
- **Board Independence**: 70.4% of the portfolio is invested in companies that have a majority of independent board members, vs 73.4% for the index.

*Source: @2024 MSCI ESG Research - coverage level: 88% for the fund and 86% for the index*

- **Board Diversity:** 91.5% of the portfolio is invested in companies that have at least one female Director, vs 88.5% for the index.

  *Source: @2024 MSCI ESG Research - coverage level: 86% for the fund and 84% for the index*

- **Accident Prevention Policy:** 73.8% of the portfolio is invested in companies that have at least one female Director, vs 79.2% for the index.

  *Source: @2024 MSCI ESG Research - coverage level: 86% for the fund and 84% for the index*

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