

# Emerging Markets Bond

## Monthly Review and Outlook

October 2016

### Key highlights:

- US Treasuries sold-off as economic data in the US improved, strengthening expectations of a US rate hike in December.
- We reduced duration risk in October, taking profit particularly in some long-dated bonds which had performed very well.
- Trump is also expected to undertake fiscal stimulus, through tax cuts, and infrastructure spending, likely leading to higher US rates, Treasury yields have moved higher following the election.

### Market review

US Treasuries sold-off as economic data in the US improved, strengthening expectations of a US rate hike in December. Investors also re-assessed the likelihood of further policy action in the EU and Japan. In the US election campaign, the likelihood of a Hillary Clinton victory increased mid-month before falling back, keeping uncertainty elevated. In emerging market (EM), October saw significant issuance and Saudi Arabia's inaugural sovereign bond issue raised \$17.5bn, surpassing Argentina's \$16.5bn issue in April.

EM debt (in US dollar terms) was down on the month (-1.24%) as US 10-year yields rose 23 basis points (bps) to 1.84%. EM spreads widened marginally to 340bps with the yield increasing to 5.24%. Long-dated investment grade (IG) EM bonds sold-off as the US Treasury curve steepened, while high yield (-0.9%) held up better than IG (-1.5%).

The worst performing bonds were those of Mozambique (-28.1%), as the government announced a potential restructuring as debt had risen to unsustainable levels. Venezuelan bonds also fell (-8%) amid the national oil company PDVSA offering a voluntary swap to holders of short-dated bonds in a bid to preserve cash. The investor participation rate fell some way short of the 50% targeted amount. Colombia declined (-3.4%) in the wake of the referendum result rejecting the peace agreement in September, which may delay fiscal reform and possibly result in less comprehensive reforms.

Positive performers comprised mainly a mix of high yield credits including Ecuador (+4.4%), which reversed the decline seen in the wake of its \$1bn 2022 bond issue in late-September, Ghana (+3.1%), Pakistan (+2.5%) and Ukraine (+1.7%).

### Portfolio positioning

We reduced duration risk in October, taking profit particularly in some long-dated bonds which had performed very well. Given event risks in November and December (US election, OPEC meeting, potential US interest rate hike), we wanted to reduce portfolio risk. We also reduced higher-risk African credits where we believed that a lot of potential positives were already priced in. We added some shorter-dated bonds in Bahrain and Russia.

### Performance

In USD terms, the First State Emerging Markets Bond Fund declined by 1.1% in October.

### Outlook

The election of Donald Trump as president in the US introduces significant uncertainty over the future course of the global economy, geopolitics and financial markets. While the precise implications of a Trump presidency are as yet difficult to fully predict, in view of the president elect's rhetoric during the campaign there is a risk of significant disruption to the current global environment, especially if the US introduces protectionist policies as expected, which would be negative for EM. We now see greater risks to EM countries where a high share of exports go to the US and where remittances from the US are high. Trump is also expected to undertake fiscal stimulus, through tax cuts, and infrastructure spending, likely leading to higher US rates, Treasury yields have moved higher following the election, impacting countries with high external financing needs.

**Disclaimer**

The information contained within this document has been obtained from sources that First State Investments ("FSI") believes to be reliable and accurate at the time of issue but no representation or warranty, expressed or implied, is made as to the fairness, accuracy, completeness or correctness of the information. Neither FSI, nor any of its associates, nor any director, officer or employee accepts any liability whatsoever for any loss arising directly or indirectly from any use of this. This document is intended solely for distribution to professional/institutional investors as may be defined in the relevant jurisdiction and is not intended for distribution to the public. The information herein is for information purposes only; it does not constitute investment advice and/or recommendation, and should not be used as the basis of any investment decision. Some of the funds mentioned herein are not authorised for offer/sale to the public in certain jurisdiction.

The value of investments and the income from them may go down as well as up and you may not get back your original investment. Past performance is not necessarily a guide to future performance. Please refer to the offering documents for details, including the risk factors.

This document/the information may not be reproduced in whole or in part without the prior consent of FSI. This document shall only be used and/or received in accordance with the applicable laws in the relevant jurisdiction.

Reference to specific securities (if any) is included for the purpose of illustration only and should not be construed as a recommendation to buy or sell the same. All securities mentioned herein may or may not form part of the holdings of First State Investments' portfolios at a certain point in time, and the holdings may change over time.

In Singapore, this document is issued by First State Investments (Singapore) whose company registration number is 196900420D. First State Investments (registration number 53236800B) is a business division of First State Investments (Singapore).