

EBND

VanEck Emerging Income Opportunities Active ETF (Managed Fund)

Emerging markets bonds

Emerging markets (EM) bonds are, as the name suggests, bonds issued in and by emerging markets. Despite emerging markets representing over 50% of global GDP, the level of EM bond issuance and investment is nowhere near what would be implied by their contribution to global growth. Additionally, many emerging markets boast strong economic performance based on good economic policy decision making in the last 15 years which has made them stronger than many of their developed market counterparts. There is a new world order and EM bonds are at the forefront of this change.

There are a number of reasons many investors do not have EM bonds in their portfolio, including awareness, understanding and difficulty of access. All of this means investors are potentially missing out on the diversification and yield benefits associated with EM bond investing. With Australian and global developed markets (DM) bond yields extremely low, the higher yields available on EM bonds provide investors with the potential for higher income with commensurate risk.

An 'unconstrained' approach considers the entire opportunity set within emerging markets. This means being able to take advantage of the best opportunities without being inhibited by benchmark constraints, and allows for flexibility to navigate the idiosyncrasies between countries, currencies, credit, duration, maturities and regions.

The universe of EM bonds consists of four main segments, each with its own unique characteristics.

Hard currency sovereign bonds

Issued by governments in hard currencies, usually US dollars. The yield is typically higher than US treasuries to compensate for the additional risk of investing in EM.

Local currency sovereign bonds

Issued by governments in their own currency. This is the largest segment of the EM bonds universe so it is the most liquid. Investors can also take advantage of the returns from currency movements.

Hard currency corporate bonds

Issued by companies in hard currencies, usually US dollars. There are many issuers which allows for diversification by sector, country and security.

Local currency corporate bonds

Issued by companies in their own currency. This is the least liquid segment of the EM bonds universe.

There is a new world order and EM bonds are at the forefront of this change.

The “new world” of emerging markets bonds

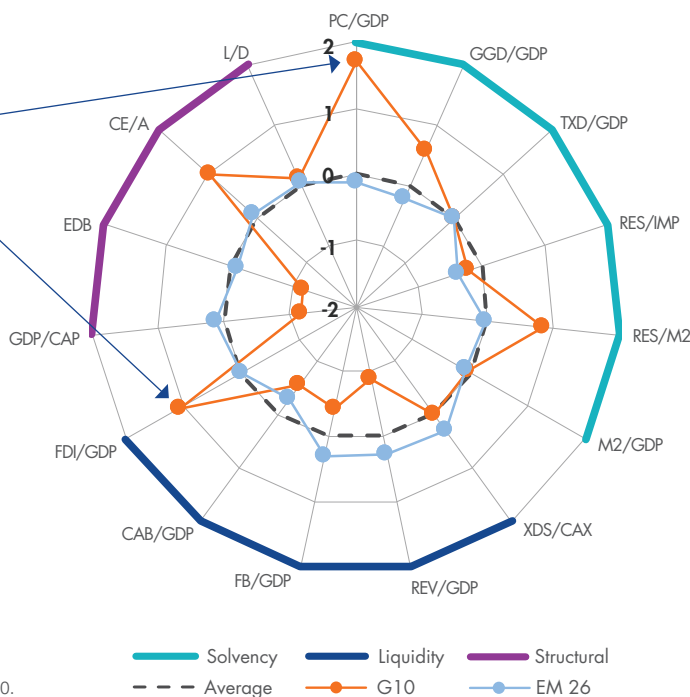
Today, global comparisons show that emerging market economies are as liquid and structurally sound as developed markets. Emerging markets generally have stronger balance sheets. On the radar chart, the red line is the global mean. The circles represent standard deviations above and below the mean. The further you are away from the centre, the worse it is.

Macroeconomic radar: EM and DM

You can see developed markets have worse:

- Private credit to GDP
- Foreign direct investment to GDP, which can negatively impact demand and growth

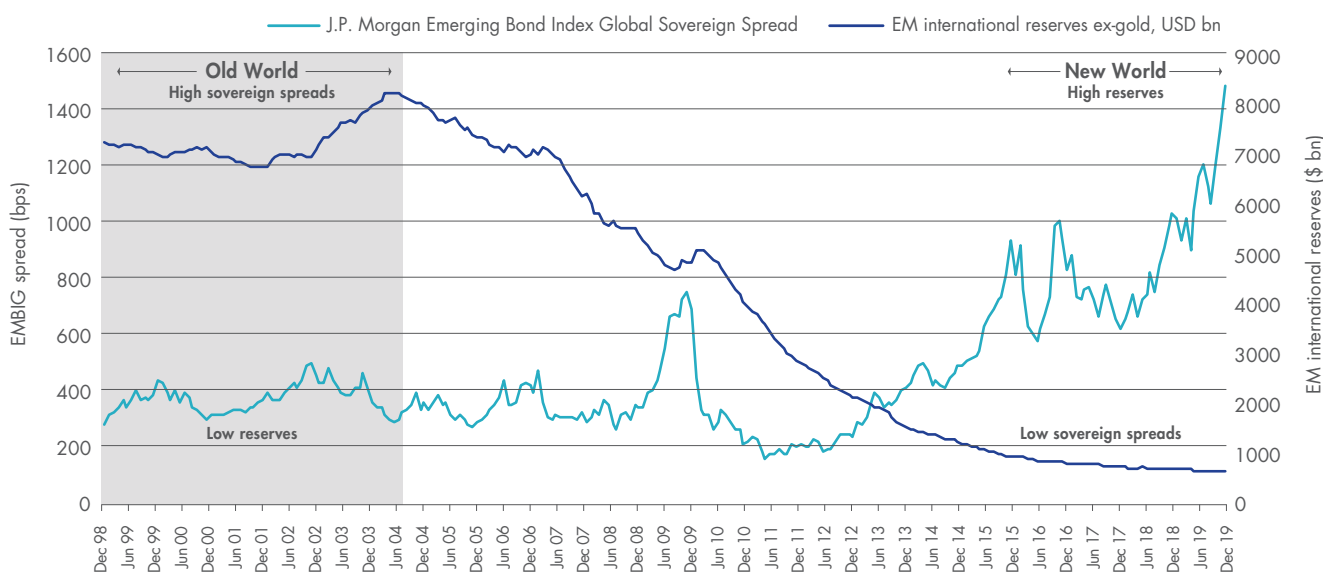
- Key:
- PC/GDP: Private credit/GDP
 - GGD/GDP: General government debt/GDP
 - TXD/GDP: Total external debt/GDP
 - RES/IMP: International reserves/months of imports
 - RES/M2: International reserves/M2
 - M2/GDP: M2/GDP
 - REV/GDP: Government revenue/% GDP
 - FB/GDP: Headline fiscal balance/% GDP
 - CAB/GDP: Current account balance/% GDP
 - FDI/GDP: Net foreign direct investment/% GDP
 - GDP/CAP: US\$ GDP per capita/PPP
 - EDB: Ease of doing business
 - CE/A: Common equity/% assets
 - L/D: Loans to deposit ratio
 - XDS/CAX: External debt service (public and private)/% CA receipts



Source: VanEck, IMF, World Bank, Moody's, Bloomberg. Data as of January 2020.

Despite their stronger fundamentals, emerging market governments and corporations generally pay more than their developed market counterparts when they issue bonds. This is an opportunity for investors to look beyond the past.

How EM bonds have changed



Source: Bloomberg. Data as of December 2019. EMBIG spread is the difference between EM hard currency sovereign bonds and US treasuries, and is captured by the J.P. Morgan Emerging Bond Index Global Sovereign Spread.

Two decades ago, in the “old world”, EM bonds were risky and volatile due to low reserves and the limited ability to absorb losses. This was typified by the 1997 “Asian financial crisis” and the 1998 Russian financial crisis. The Asian financial crisis began in 1997. Thailand’s currency devalued as foreign investors withdrew, concerned the country was bankrupt. With no reserves, Thailand’s government could do little. The crisis spread throughout the region and those hardest hit were the ones with low domestic reserves. Finally the IMF stepped in to stabilise the Korean, Thai and Indonesian economies. This crisis was closely followed by the similar Russian currency crisis and Argentina’s much publicised default in 2001.

These crises set the scene for significant economic reforms through the early part of the new millennium in many emerging markets. Governments were forced, often for the first time, to be fully transparent with foreign investors and global monetary funds. As a result many came out of the GFC structurally stronger than their developed market counterparts. Many emerging market governments were able to better implement counter-cyclical fiscal expansion to reignite growth because of their growing foreign exchange reserves, strong budgets and robust balance of payments.

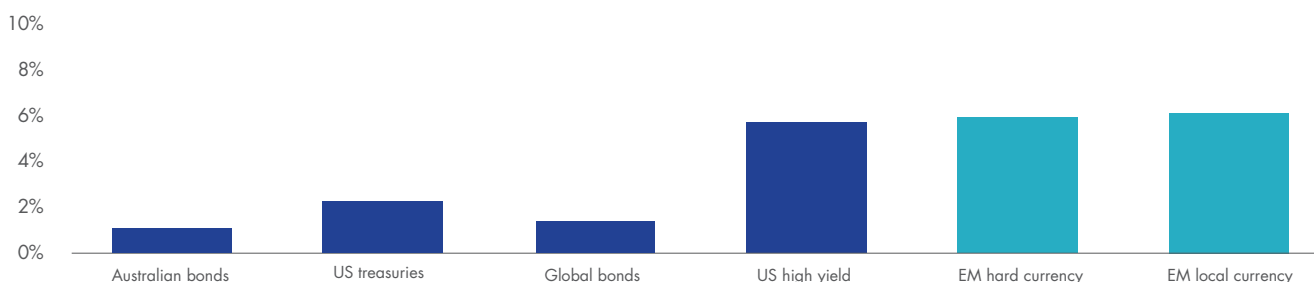
The “new world” in emerging markets is characterised by higher reserves and lower spreads on bonds. Current accounts and government budgets are largely in check. Policy makers, appealing to an ever growing and better educated middle class encourage savings and pension reforms driving capital investment. Some of the best managed economies are in emerging markets.

It’s little wonder more and more investors are embracing EM bonds, especially when they consider the yields being offered.

Yield and performance

EM bonds offer access to debt with attractive yields relative to DM bonds.

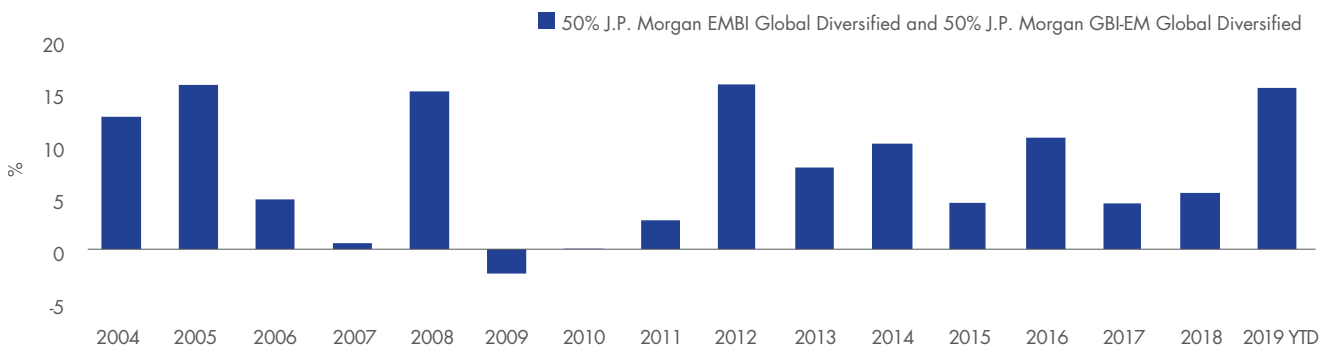
Yield to maturity – 2019



Source: Bloomberg. Data as at 31 December 2019. Data is in Australian dollars. You cannot invest in an index. Past performance is not a reliable indicator of future performance. Indices used: Australian Bonds - Bloomberg AusBond Composite 0+ Yr Index; US Bonds - Bloomberg Barclays U.S. Aggregate Total Return Index Unhedged AUD; Global Bonds - Bloomberg Barclays Global-Aggregate Total Return Index Value Unhedged AUD; US High Yield - ICE BofAML US High Yield Index; EM Hard Currency - J.P. Morgan Emerging Market Bond Index Global Diversified (EMBIGD). EMBIGD is unhedged. EBND will hedge its hard currency; EM Local Currency - J.P. Morgan Government Bond Index-Emerging Markets Global Diversified (GBIEM).

EM bonds have produced positive returns in 14 of the last 15 calendar years.

Calendar performance



Source: Morningstar Direct. Data as at 31 December 2019. Data is in Australian dollars. EM Bonds is 50% J.P. Morgan EMBI Global Diversified and 50% J.P. Morgan GBI-EM Global Diversified. This index is used to illustrate historical performance of the EM Bond market only. It is not the benchmark for EBND. You cannot invest in an index. Past performance of the market is not a reliable indicator of future performance of the fund.

Taking advantage of EM bonds

With Australian and global DM bond yields extremely low, the higher yields available on EM bonds provide investors with the potential for higher income with a commensurate increase in risk. However to take full advantage of the opportunities within EM bonds, it is necessary to take an unconstrained approach.

VanEck Emerging Income Opportunities Active ETF (Managed Fund) (ASX: EBND) takes an unconstrained approach and is available on ASX.

The benefits of an unconstrained approach

EBND has the flexibility to invest in all types of EM bonds: sovereigns and corporates in hard and local currencies.

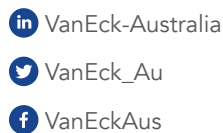
- ▶ **Greater ability to diversify:** EBND's investment team attempts to exploit the different risk and return characteristics of different EM bonds and currencies to optimise country and portfolio risk-adjusted returns. With its unconstrained approach, the team has a greater ability to maintain exposure to attractive yields while diversifying by currency, region, maturity, duration and credit.
- ▶ **Conviction:** EBND will often be composed of high-conviction investments, with a maximum weighting of 15%.
- ▶ **Contrarian views:** The investment team avoids crowded investments and often strives to find the next best investment ahead of other investors.

The VanEck advantage

- ▶ The depth and breadth of VanEck's experienced and stable emerging markets bond team is unparalleled. The team has an average of over 20 years* of investing experience across a variety of market conditions and stages of the economic cycle.
- ▶ VanEck manages in excess of US\$5.4 billion* in emerging markets fixed income.
- ▶ VanEck has been investing in emerging markets since 1993.

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EBND invests in emerging markets. An investment in EBND has specific and heightened risks that are in addition to the typical risks associated with investing in the Australian market. These include: currency risks from foreign exchange fluctuations; foreign laws and regulations including application of foreign tax legislation including confiscatory taxation and withholding taxes; changes in government policy; expropriation; economic conditions including international trade barriers; securities trading restrictions; changed circumstances in dealings between nations; lack of uniform accounting and auditing standards; potential difficulties in enforcing contractual obligations and extended settlement periods. See the PDS for more details of the key risks.

No member of the VanEck group guarantees the repayment of capital, the payment of income, performance, or any particular rate of return from EBND.

*As at 31 December 2019.

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