Sparinvest

DOMINATING RISK AVERSION

Inflation fears replaced by growth fears

Markets. June ended with a negative return for Emerging Markets (EM) government bonds of 6.52%. 10Y American interest rates increased by 16 bps and the credit spread increased by 61 bps, which combined resulted in the negative total return for the month.

The financial market shifted focus during June. At the beginning of the month, the fear of inflation dominated, but towards the end of month, growth fears took over. The fear of lower growth put significant pressure on risky assets and the High Yield market was no exception, as lower growth (perhaps even a recession) will likely lead to higher bankruptcy rates. Growth fears also resulted in declining commodity prices in June, where for example, the price of iron ore fell by 13% and the price of oil fell by 6%.

Key indicators point to a significant loss of growth momentum in the OECD area during June. This can be seen in the order components of the recently published business confidence indicators. For the U.S., the EU and Japan, the order index fell to a low level in June. This development was subsequently confirmed by ISM data from the U.S., where the order component also de-creased. The widespread vacuum in the order intake coincides with signs of stock build-up. The balance between the order index and the stock index is at the lowest since November 2001 - disregarding the extraordinary major shocks associated with the financial crisis and the corona crisis. Overall, the development has brought the CLI indicator for the OECD area into a downturn phase.

However, it should be emphasized that China is currently experiencing a renewed growth momentum. The development is mainly due to less restrictive Corona restrictions in China, where partial shutdowns in Shanghai, Shenzhen and Beijing are being phased out. In country specific news, we have seen the fall-out from increasing food prices in the prior months, as riots emerged causing governments to resign. Both countries are establishing temporary governments working on reactivating their IMF program for Pakistan and Sri Lanka to enter into a program and restructuring their debt making it sustainable again.

Weak relative return

The Portfolio had a negative return of 7.34% in June, which was 0.82% worse than the benchmark before costs. The continued declining growth momentum hit the high yield segment the most, which caused the fund to underperform.

The largest positive contributions to the absolute fund return came from our positions in Ukraine, Colombia and Egypt. At the opposite end, Ghana, Kazakhstan and Nigeria made the largest negative contributions. The relative return was positively affected by underweights in Turkey, Pakistan and Kazakhstan. Overweight in Colombia, Egypt and Mexico pulled in a negative direction. Colombia elected their first left wing president in their democratic history, which disappointed the market and sent their bonds lower.

In June, we adjusted our exposure in Argentina, participated in a new issue from Hungary and added a bit of Tunisia and South Africa. During the month, we sold our bonds in Costa Rica and reduced our Barbados and Brazil exposure.

See performance and fund data Click here >

Strategy

Value Bonds - Emerging Market Corporates primarily invests in Emerging Markets corporate bonds, cf. the fund's prospectus. Bond selection is based on the value approach, meaning that the team focuses on bonds issued by companies with healthy long-term earnings power and strong balance sheets as well as an expected ability to service outstanding debt. The portfolio is diversified across sectors, regions and credit ratings. The investment universe includes Investment Grade bonds, High Yield bonds and to a limited extend non-rated corporate bonds.