

**Emerging market debt: sustainable financial and ESG performance**

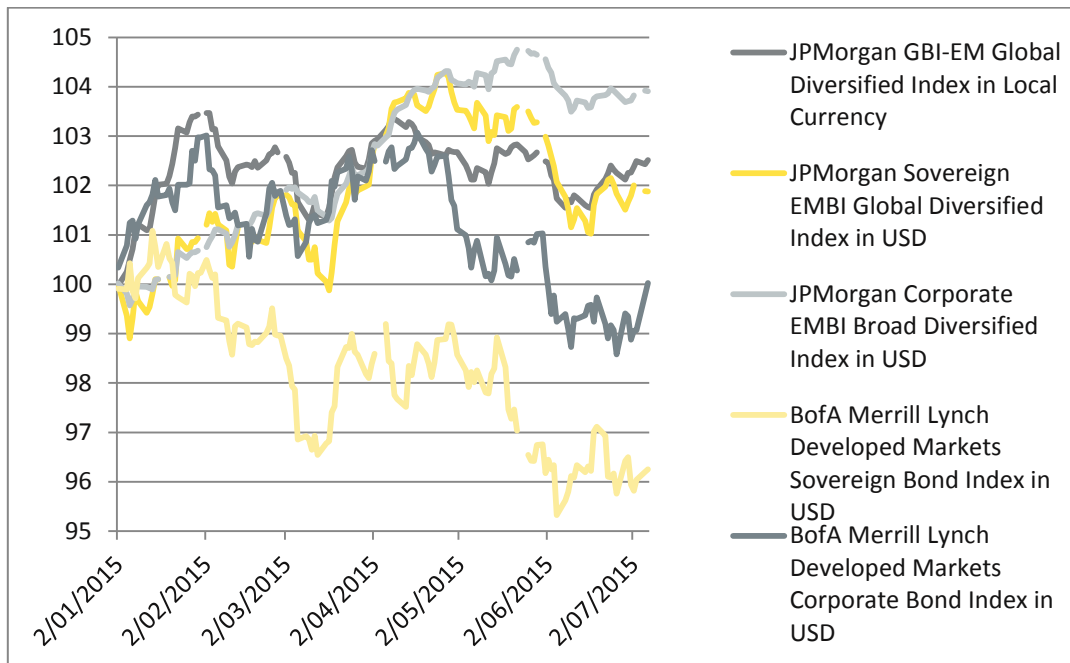
*Emerging market debt should be considered as a fully-fledged asset class within a diversified portfolio, argues Thierry Larose. In the light of the current volatility on fixed income markets, the attractive risk premium and sound fundamentals plead for emerging market debt. Our strategy offers additional added value through the ESG filter, avoiding undemocratic countries with high risk profiles.*

**Over the last two months we have seen rising yields in Europe. Has this also impacted EMD yields?**

Yes, it has, albeit not very significantly. US rates (Treasuries) and European core rates (Bunds) have been quite volatile over this period. Maybe surprisingly so, EMD yields have not suffered more than these core rates.

Barring the FX component, EM bonds are doing a lot better than their developed market equivalents. Moreover, EMD corporates have outperformed corporates in developed markets.

It seems that all the liquidity that has been created over the past few months is flowing more easily to this asset class than to core rates in Europe and the US.

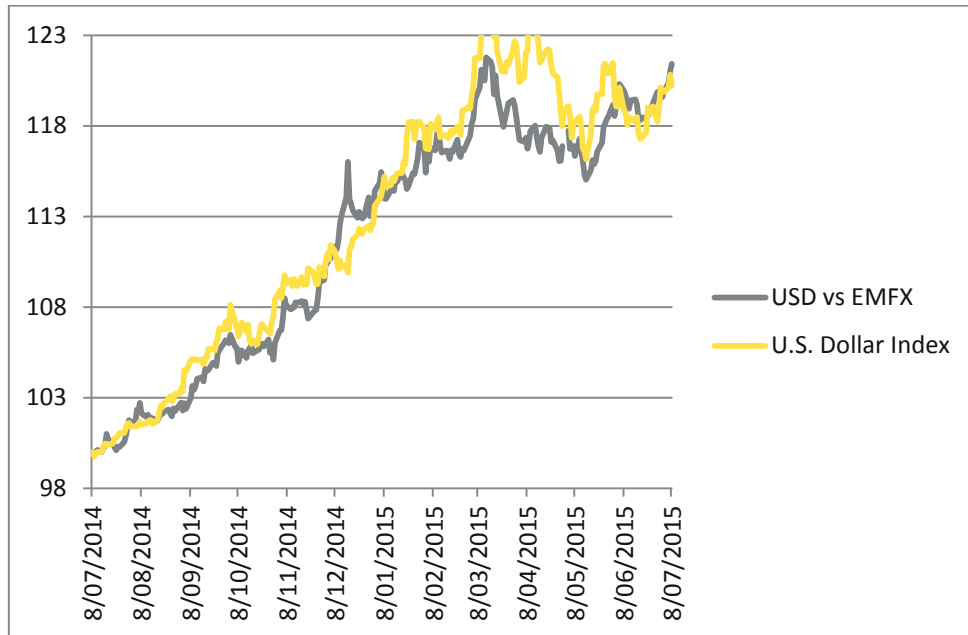


Source: Petercam IAM

**What are the current drivers of the EMD markets?**

The drivers for these markets are real rates, which are much more attractive than in developed markets. Indeed, core rates are not only lower in developed markets, they have also proven to be more volatile than in emerging markets. This supports our stance that in the long run, a progressive rotation can be expected from developed markets sovereign bonds into emerging market bonds.

It is also worthwhile mentioning that in recent years, EM currencies have depreciated versus the USD and EUR. This makes the entry point even more interesting for EMD in local currency. In that regard, dollar strength is not hurting EM FX more than other so-called hard currencies. This can be seen from the graph on the next page.



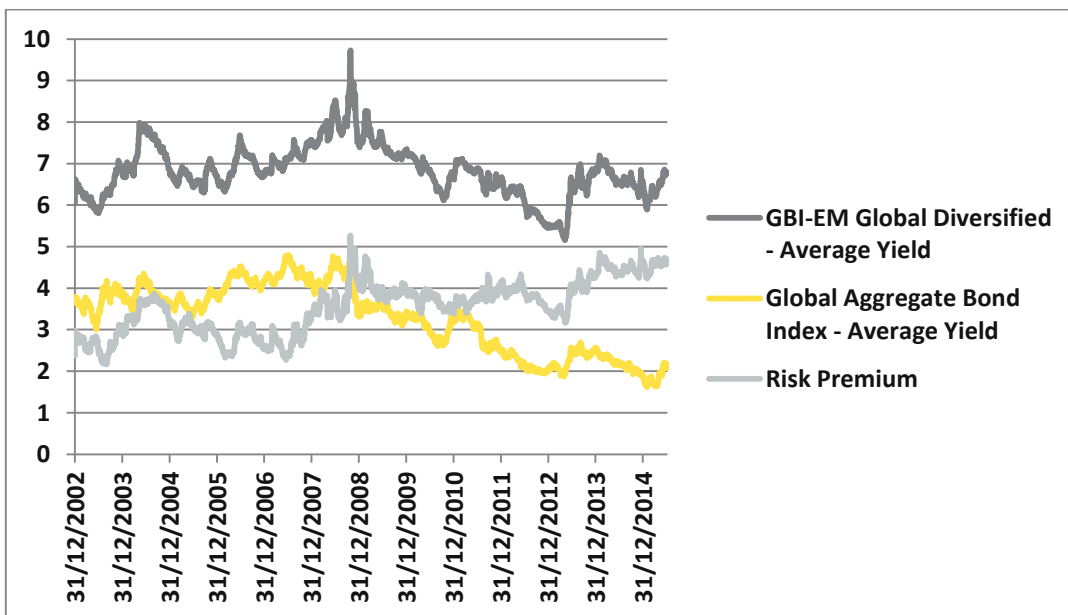
Note: "USD vs EMFX" refers to the inverse of the "JPMorgan Emerging Market Currency Index (EMCI) Live Spot Index". This tradable benchmark comprises of ten currencies: BRL, CLP, CNH, HUF, INR, MXN, RUB, SGD, TRY and ZAR.

The U.S. Dollar Index (ticker: USDX or DXY) is an index of the value of the USD relative to a basket of other hard currencies.

Source: Petercam IAM

**What about the yield spread of local EMD compared to hard currency EMD bonds?**

This spread is quite attractive at the present time. We argue that if the pickup in yield between EM local bonds and global bonds is a valid measure of risk premium, EM local bonds are relatively cheap. Our stance is supported by the graph below:



Source: Petercam IAM

In our investment process, FX is a long-term performance source in the portfolio. It should nonetheless be stressed that we are very selective in our currency allocation, looking at the underlying fundamentals. These are also discussed with our Senior Economist, who closely follows emerging markets and the dynamics of these upcoming countries.

**In the Petercam L Bonds Emerging Markets Sustainable fund you also invest in Frontier Markets. Has this been a good contributor to the performance recently and in general?**

Yes, frontier markets have handsomely contributed to overall returns. These countries often find themselves in the fourth quartile of the ESG universe, which is capped at 10% for investment. I am thinking of countries such as Ivory Coast, Tanzania, Kenya and Zambia, which are going through a transformation process and currently present attractive risk/return dynamics.

**What are currently your expectations for the EMD markets?**

We strongly believe the investment case is still intact. It is comforting to see that the dollar strength is not impacting these markets to a large extent. Also, EMD rates have suffered less than core rates in developed markets.

The very sharp correction we saw in 2013 has not repeated itself. This is also thanks to the prudent communication of the Fed, which has prepared markets for a rate hike for a while now.

In terms of risks, we have identified three major ones:

- A Grexit hampering investors' risk appetite;
- A Fed hike which comes sooner than expected;
- A more marked China slowdown. In that respect, we do believe the PBOC has erred on the side of caution, and that it is doing a good job in making sure the economy does not enter a hard landing.

### Petercam L Emerging Markets Sustainable: Share Classes

Fund Name	Share Class	ISIN	Currency	Management Fee	Typ	
Petercam L Emerging Markets Sustainable	A	LU0907927171	EUR	1,00%	Distribution	Retail
Petercam L Emerging Markets Sustainable	B	LU0907927338	EUR	1,00%	Accumulation	Retail
Petercam L Emerging Markets Sustainable	E	LU0907927841	EUR	0,50%	Distribution	Institutional
Petercam L Emerging Markets Sustainable	F	LU0907928062	EUR	0,50%	Accumulation	Institutional
Petercam L Emerging Markets Sustainable	K	LU0907928229	EUR	1,50%	Distribution	Retail
Petercam L Emerging Markets Sustainable	L	LU0907928575	EUR	1,50%	Accumulation	Retail

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