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The Often Overlooked and Misunderstood Bond Buy

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> Rising rates and emerging risks in developed markets could spell trouble for bond portfolios. As such, we believe investors need to take another look at this often-overlooked bond buy.

Many U.S. investors, in general, tend to shrug off global markets, particularly when it comes to bonds. After nearly a decade and a half of declining yields and low volatility for developed markets, the past few years have been characterized by rising rates and emerging risks in global bond markets. As such, we believe investors may hold a number of misconceptions and need to take another look at an often overlooked asset class, emerging markets bonds, as we believe they may add resilience to an overall bond portfolio.

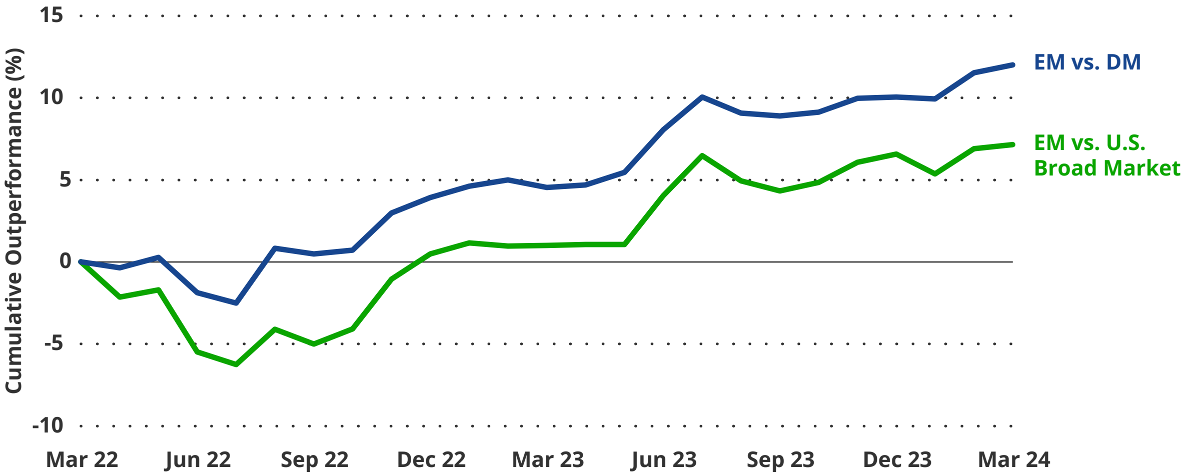
Below we explore three reasons investors should consider allocating to emerging market bonds in the current market environment.

1. EM Bonds May Help Insulate a Bond Portfolio from DM Risks

Developed markets rates have risen sharply since pandemic-era lows, and bond investors in these markets are on track for a third straight year of losses. Central banks have been aggressively hiking rates, after falling behind the curve on inflation. More recently, long term yields have begun to rise to levels not seen in over 15 years, as the market begins to price in a "higher for longer" environment amid persistent inflation, still hot economic data and rising fiscal problems. An eventual Fed rate cut would likely occur when recessionary risks are high, which would likely be adverse for developed markets corporate bonds, which are still very tight. In other words, a turn in rates is not the turn in risk. In contrast, emerging market central banks generally got ahead of inflation in the early days following the pandemic. Inflation has been declining, and real rates in many markets remain attractive, which has provided support to local currencies along with rising commodity prices. The lack of irresponsible fiscal policy in EM stands in stark contrast to what is playing out in developed markets.

Given these diverging backdrops, it is not surprising that emerging markets bonds have been more resilient compared to both U.S. and global investment grade aggregate bonds given the volatility in those markets since the Fed began its latest rate hiking cycle. Given the long-term nature of the risks that continue to emanate from developed markets, we believe there is a strong case to allocate to EM bonds to make a bond portfolio more resilient.

The Market Has Rewarded Responsible Policies



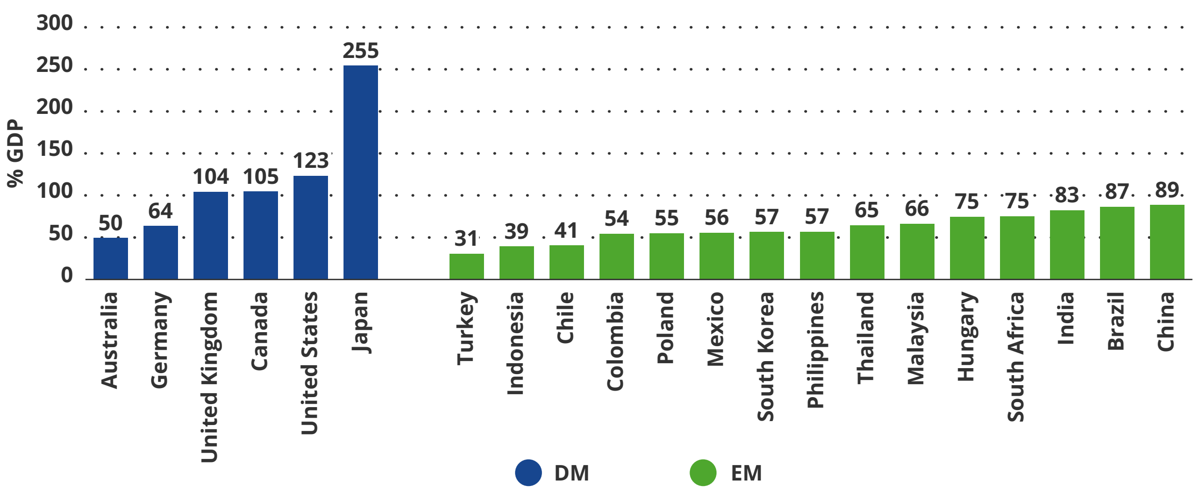
Source: VanEck as of 03/31/2022 - 03/31/2024. The performance data quoted represents past performance. Past performance is not a guarantee of future results. EM represents 50% J.P. Morgan GBI-EM Global Diversified Index/50% J.P. Morgan EMBI Global Diversified Index. DM is represented by the ICE BofA Global Broad Market Index. U.S Broad Market is represented by the ICE BofA U.S. Broad Market Index.

2. Emerging Markets Have Lower Debt

Notwithstanding China's more recent policy direction, **emerging markets, in general, have moved much more quickly to increase interest rates compared to the U.S.** and other developed markets in order to stay ahead of inflation. For investors, this fundamental backdrop means less issuance and rolling over of debt, a favorable supply/demand dynamic that should help support EM bonds. In addition, if needed, EM central banks can hike interest rates without bankrupting the government (unlike the challenges we saw in the United Kingdom or even the U.S. during its budget showdowns).

Debt Levels of EM Countries Are Relatively Attractive

General Government Gross Debt, % GDP



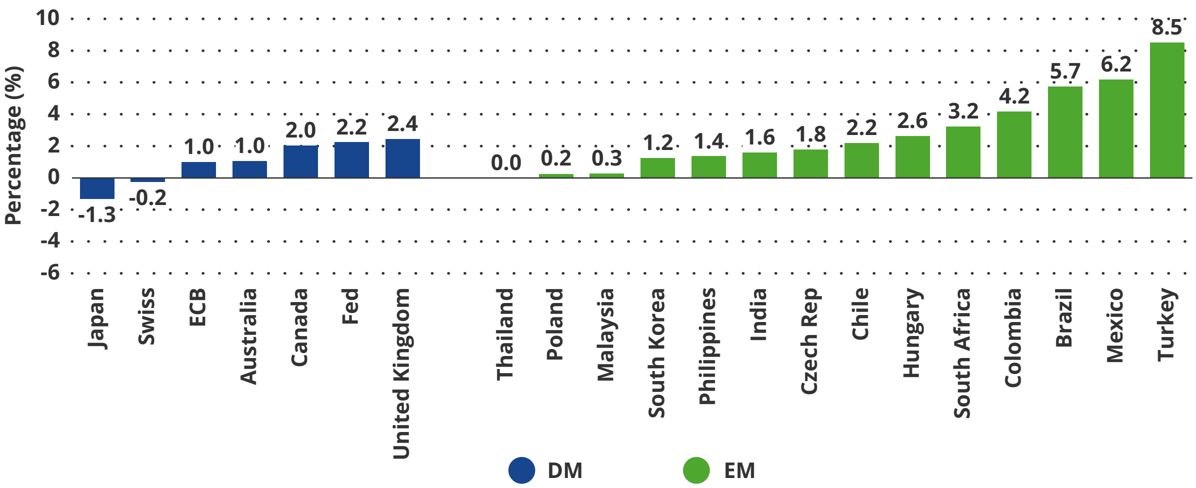
Source: VanEck Research; Bloomberg LP. Data as of April 2024.
Past performance is not indicative of future results. Please see important disclosures and definitions at the end of the blog.

3. EM Has Independent Central Banks

The primary focus of EM central banks is to focus on controlling inflation, and they do this by maintaining high real interest rates. For investors, the result has been not only higher nominal yields but higher real yields. The benefits to EM local currency investors are a more substantial level of income that is not eroded by the loss of purchasing power (through a potentially weaker currency). Additionally, if the central bank's actions are successful in controlling inflation, it can lead to a stronger and more stable economy.

EM Central Banks' Focus on Inflation Means Higher Income for Investors

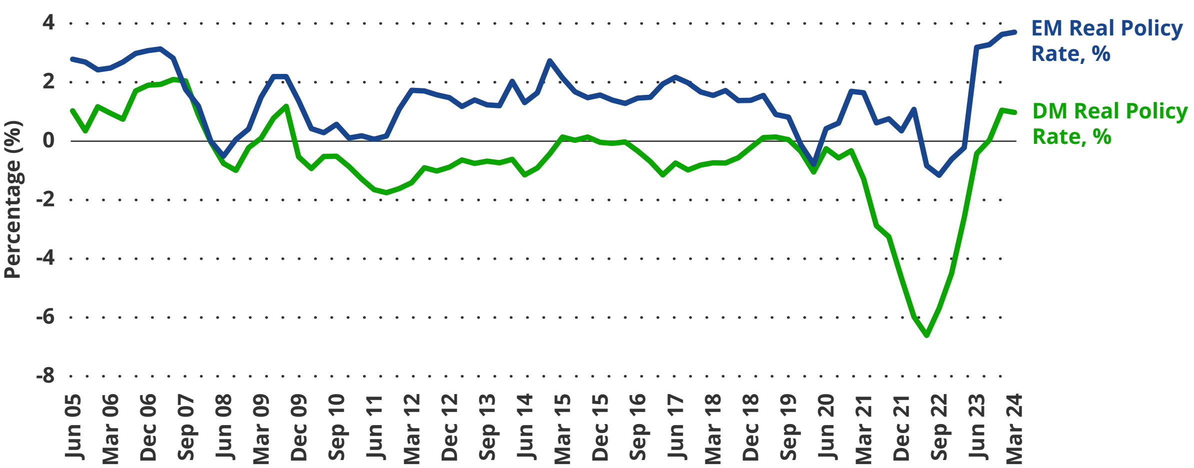
Real Policy Rates in EM and DM (%), 12m from now if current expectations for rates and inflation materialize



Source: VanEck Research; Bloomberg LP. Data as of April 2024.

Ex-Post Real Policy Rates (Trailing) in EM and DM (%)

Ex-Post Real Policy Rates in EM and DM, %



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The **VanEck Emerging Markets Bond Fund** was one of the first blended emerging markets bond strategies in the market. The Fund is actively managed with the flexibility to invest in sovereign and corporate debt in hard and local-currency. The Fund's broad universe and bottom-up, high active share approach drives the opportunity to potentially outperform the benchmark over a market cycle.

IMPORTANT DISCLOSURES

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Duration measures a bond's sensitivity to interest rate changes that reflects the change in a bond's price given a change in yield. This duration measure is appropriate for bonds with embedded options. Quantitative Easing by a central bank increases the money supply engaging in open market operations in an effort to promote increased lending and liquidity.

The Fund's benchmark index (50% GBI-EM/50% EMBI) is a blended index consisting of 50% J.P. Morgan Government Bond Index-Emerging Markets (GBI-EM) Global Diversified and 50% J.P. Morgan Emerging Markets Bond Index (EMBI). The J.P. Morgan GBI-EM Global Diversified tracks local currency bonds issued by Emerging Markets governments. The J.P. Morgan EMBI Global Diversified tracks returns for actively traded external debt instruments in emerging markets, and is also J.P. Morgan's most liquid U.S dollar emerging markets debt benchmark.

ICE BofA U.S. Broad Market Index tracks the performance of U.S. dollar denominated investment grade debt publicly issued in the U.S. domestic market, including U.S. Treasury, quasi-government, corporate, securitized and collateralized securities.

ICE BofA Global Broad Market Index tracks the performance of investment grade debt publicly issued in the major domestic and eurobond markets, including sovereign, quasi-government, corporate, securitized and collateralized securities.

Emerging Market securities are subject to greater risks than U.S. domestic investments. These additional risks may include exchange rate fluctuations and exchange controls; less publicly available information; more volatile or less liquid securities markets; and the possibility of arbitrary action by foreign governments, or political, economic, or social instability.

Investments in emerging markets bonds may be substantially more volatile, and substantially less liquid, than the bonds of governments, government agencies, and government-owned corporations located in more developed foreign markets. Emerging markets bonds can have greater custodial and operational risks, and less developed legal and accounting systems than developed markets. ***When interest rates rise, bond prices fall.*** This risk is heightened with investments in longer duration fixed-income securities and during periods when prevailing interest rates are low or negative.

All investing is subject to risk, including the possible loss of the money you invest. As with any investment strategy, there is no guarantee that investment objectives will be met and investors may lose money. Diversification does not ensure a profit or protect against a loss in a declining market. Past performance is no guarantee of future performance.

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