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Riding the EM Debt Bull

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> EM debt is thriving despite risks, with stronger currencies and U.S. rate rallies boosting returns. High carry, priced-in tariff concerns, and high real rates support its outperformance.

The **VanEck Emerging Markets Bond Fund** was up 1.47% in February, compared to 1.11% for its benchmark. YTD, the fund is up 3.59%, compared to 2.88% for its benchmark, 50% J.P. Morgan GBI-EM Global Diversified Index/50% J.P. Morgan EMBI Global Diversified Index. The Global Agg and 10-year treasuries were up YTD by 2.29% and 3.8%, respectively.[1] During February, China (corporates), Chile (local currency), and Tunisia led outperformers. Ecuador led underperformance. Country-specific views will remain more important than top-down *anything*. We increased duration yet again, as telegraphed, and remain happy with an overweight relative to our benchmark. HY sovereigns remain our hunting ground in USD, but IG Sovereigns in the Gulf have allowed the fund to capture U.S. rate rallies. The fund had around 50% in curated local currency, with a noteworthy underweight to Brazil in local currency. Carry is 7.7%, YTW is 9.0%, and duration is 6.6.

Average Annual Total Returns* (%) (In USD)

As of February 28, 2025	1 Month	3 Month	YTD	1 Year	3 Year	5 Year	10 Year
Class A: NAV (Inception 07/09/12)	1.43	1.82	3.72	7.36	4.03	2.99	2.20
Class A: Maximum 5.75% load	-4.40	-4.04	-2.25	1.19	2.00	1.78	1.60
Class I: NAV (Inception 07/09/12)	1.47	1.91	3.59	7.63	4.34	3.29	2.50
Class Y: NAV (Inception 07/09/12)	1.45	1.87	3.75	7.53	4.21	3.22	2.43
50% GBI-EM/50% EMBI	1.11	1.17	2.88	6.09	2.56	0.16	2.09

As of December 31, 2024	1 Month	3 Month	YTD	1 Year	3 Year	5 Year	10 Year
Class A: NAV (Inception 07/09/12)	-1.83	-5.05	2.52	2.52	1.61	2.21	1.87
Class A: Maximum 5.75% load	-7.48	-10.51	-3.38	-3.38	-0.37	1.00	1.27
Class I: NAV (Inception 07/09/12)	-1.62	-4.93	3.09	3.09	2.01	2.54	2.20
Class Y: NAV (Inception 07/09/12)	-1.81	-5.14	2.84	2.84	1.86	2.44	2.11
50% GBI-EM/50% EMBI	-1.66	-4.48	2.01	2.01	-0.88	-0.83	1.84

* Returns less than one year are not annualized.

Expenses: Class A: Gross 2.08%, Net 1.21%; Class I: Gross 1.34%, Net 0.86%; Class Y: Gross 1.35%, Net 0.96%. Expenses are capped contractually until 05/01/25 at 1.20% for Class A, 0.85% for Class I, 0.95% for Class Y. Caps excluding acquired fund fees and expenses, interest, trading, dividends, and interest payments of securities sold short, taxes, and extraordinary expenses.

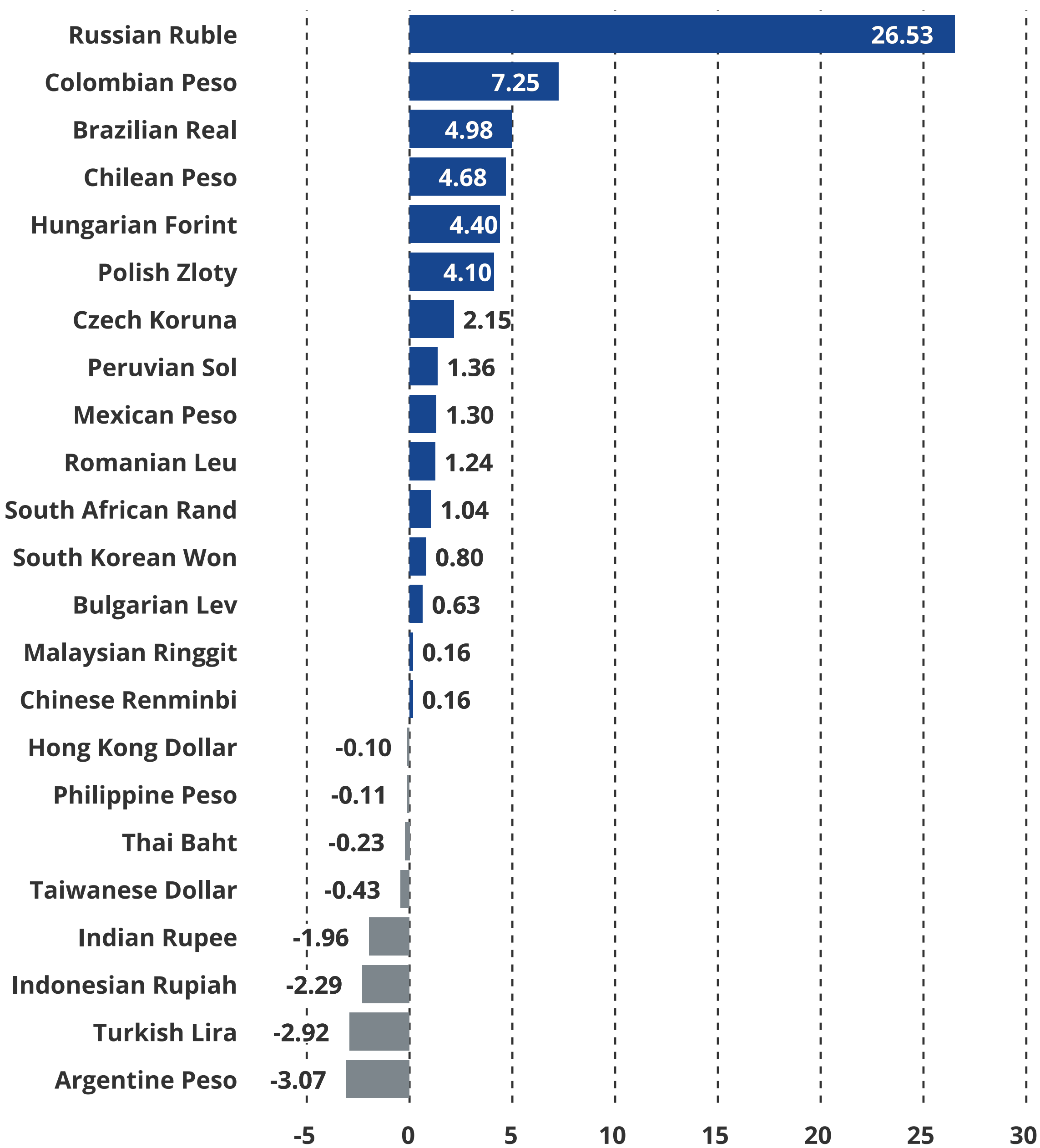
The performance data quoted represents past performance. Past performance is not a guarantee of future results. Investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Performance may be lower or higher than performance data quoted. Please call 800.826.2333 or visit vaneck.com for performance current to the most recent month ended.

The "Net Asset Value" (NAV) of a Fund is determined at the close of each business day, and represents the dollar value of one share of the fund; it is calculated by taking the total assets of the fund, subtracting total liabilities, and dividing by the total number of shares outstanding. The NAV is not necessarily the same as the ETF's intraday trading value. Investors should not expect to buy or sell shares at NAV.

[1] Global Agg represented by the ICE Global Broad Market Index; 10 Year Treasury represented by the ICE BofA Current 10-Year U.S. Treasury Index.

It's all bullish for EM debt! Despite tariff fears, U.S. policy uncertainty, geopolitical risk, and weak equity markets, EM debt is doing great. Our benchmark is up over 3% YTD, better than the Global Agg (once again). If you like themes, there have been three boosting EM bonds – a) the U.S. rates rally, b) tariff fatigue, and c) "Ukraine". The U.S. rates rally speaks for itself and seems sustainable. Our rationale for liking duration appears intact, with our original rationale (now actual causes, at this stage) including a big short rates "hedge", progress from DOGE despite persistent skepticism, growth risks from migration and tariff policy, and an independent Fed. Let's add to that last point – we find it striking and noteworthy that the new Trump administration has left the Fed out of its rhetorical targeting. In fact, the administration's focus on the 10y yield and *lack* of Fed criticism are boosting Fed independence and thus anchoring the 30-year, in our opinion. The U.S. rates rally obviously boosted all bonds. USD bonds thus led outperformance in EM in February. The second theme is that tariffs may be priced - interestingly, high beta EMFX is the winner *within* local currency, with the Colombian peso, Brazilian real, and Chilean peso as the leaders. It's hardly a sign of turmoil that bonds are rallying *and* currencies are rallying, led by the riskiest! The final theme is "Ukraine", with the Russian rouble, Polish zloty, and Hungarian forint as other YTD FX winners. These three themes are consistent with the following in our existing outlook – they show that EM can be uncorrelated, even when directly subject to risks such as tariffs. The "blob" called EM has many winners, but the country components must be curated by a consistent investment process.

Exhibit 1 – EMFX Strong YTD



Source: Bloomberg as of 3/3/25.

Exhibit 2 – Treasuries Strong YTD

Source: Bloomberg as of 3/3/25.

EM outperformance makes sense to us. Generally, in EM, carry is higher, tariff concerns are priced, and real rates are high (cushioning growth concerns). Specifically in EM, call us when China adjusts its currency, and until then, we see it as an anchor for EMFX stability. Is there any better example of our "fiscal dominance" thesis in DM than in the past few weeks? Political and policy uncertainty emanating from a highly indebted U.S. is challenging EMs. EMs are responding from positions of low indebtedness, high real rates, independent central banks, and political authorities are doing their best. No important EMs need major structural reforms (maybe India is an exception), they just need to absorb the impact with their existing structures. The most important EM, China, continues to fix its currency (at the daily fix) unchanged and better than predicted, as we've been harping on. This is an anchor for *all* EMFX. We will also reiterate that the Trump administration continues to hint at the need for a currency accord that keeps the dollar from strengthening and thus offsetting any perceived gains from tariffs. Support for this thesis (or attitude) is in the strong performance of EMFX so far in 2025.

Tariff risks remain. Tariffs are a risk to most conventional economists, as they are a tax that normally leads to less-optimal trade. Moreover, with open capital accounts, currencies can simply adjust weaker, so nothing is accomplished other than uncertainty, plus higher costs/lower margins. This is behind our prediction that the U.S. will attempt to reach an accord with key trading partners to keep currencies stable despite tariffs – China, for sure, but Japan also gets mentioned. Treasury Secretary Bessent has alluded to this. A precedent would obviously be the 1987 Plaza Accord. This held for only under two years, if that (a subsequent Louvre Accord was required) -- but it was a development one *absolutely had* to anticipate. There are more prosaic risks from tariffs, too. It's possible the market is simply not pricing tariffs until tariffs are actually in place, meaning risks lie ahead and the recent rally is to be faded. We've all heard the popular interpretation that tariff announcements have had a tactical negotiation objective (bluster, not reality). It's further possible that tariffs take on an anti-China flavor (i.e., some version of being off the hook if you duplicate U.S. tariffs with China), which could transmit costs and risks through global supply chains. But, gauging the market reactions to tariff headlines (we are writing this on March 4, following Chinese, Mexican, Canadian reciprocal tariffs on the U.S.), it appears a lot of this is priced. Exhibit 1 above should be acknowledged. In fact, our strategy in 2024 was largely to get here – the post-tariff world (whatever it is). For example, the fund was overweight local currency in 2024, and even though local currency did poorly overall, curation (in particular, our severe underweight in Mexico) allowed us to maintain our strategy and outperform. We remain bullish, though open-minded and nimble.

Exposure Types And Significant Changes

The changes to our top positions are summarized below. Our largest positions in February were Mexico, Colombia, Indonesia, Brazil, and Turkey.

- We increased our local currency exposure in Poland. The country is expected to benefit from a potential ceasefire in Ukraine, like the rest of the region. One thing that sets Poland apart though – especially with regards to local debt – is that this is the only European economy where higher defense spending is already the reality, and it is fully reflected in the country's credit metric. The latest data also point to the improving growth outlook, which should reduce pressure on the central bank to lower interest rates. In terms of our investment process, this improves the economic and policy test scores for Poland.
- We also increased our local currency exposure in Mexico and Kazakhstan. Mexico was motivated by the respite in the tariff war with the U.S., which improved the policy test score for the country. Our decision in Kazakhstan was in part due to better prospects of resolving the Russia-Ukraine conflict, which strengthens the country's policy test score. Another important development on the structural front is tax reform/fiscal consolidation, which is now in the works and which is expected to boost revenue collection by a significant amount.
- Finally, we increased our hard currency sovereign exposure in the United Arab Emirates. We were driven mostly by duration considerations here, which improved the technical test scores for the country. Negative market positioning provided additional technical support, and the economy can also benefit if additional tariffs lift oil prices higher.
- We reduced our local currency exposure in South Africa and Brazil. South Africa is affected by (somewhat surprising) negative spillovers from President Trump's comments linking the land expropriation law with tariffs. And it is not entirely clear what South Africa can do to reduce this pressure. In terms of our investment process, this worsened the country's policy test score. Brazil is also affected by the trade war uncertainty, as well as by the accumulation of longs in January. However, Brazil's drivers are mostly domestic – specifically, the ongoing increase in inflation expectations (which requires continuing policy tightening) and the government's inability to clarify its fiscal consolidation plans for 2025 and beyond. The latter worsened Brazil's policy test score.
- We also reduced our hard currency corporate exposure in Ecuador. The decision was driven by the incumbent's (President Noboa) surprisingly weak performance in the first round of the presidential elections and stronger than expected results of the leftist candidate, whose second-round chances were boosted by potential support from other political parties. This worsened the political test score for Ecuador.
- Finally, we reduced our hard currency exposure in Kuwait and Saudi Arabia. Even though we think that duration can benefit from concerns about the U.S. global outlook, there are better ways (in terms of valuations) to express this view. This factor worsened the technical test score for both countries.

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