

# GAM Multibond - Local Emerging Bond

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## Market environment

Local emerging market (EM) debt faced headwinds during December as the Federal Reserve's (Fed) 'hawkish' 25 basis point (bps) interest rate cut pegged back expectations for further reductions this year. In line with policymakers' projections, markets soon priced in only circa 50 bps in cuts for the year, triggering renewed strength in the US dollar, to the detriment of local currency bonds. The JP Morgan Government Bond Index Emerging Market (GBI-EM) Global Diversified Index ended the month -1.93% lower.

At the country level, South African bonds struggled on disappointment at the lack of new economic stimulus from China, a key buyer from South Africa's mining sector. Meanwhile, the strong US dollar also acted as a headwind for export-orientated Brazil and Mexico. However, Asian debt held up relatively well, notably China, Taiwan and Malaysia.

## Performance

The strategy had a soft end to the year, underperforming the benchmark by 80 basis points (bps), with a return of -273 bps (USD, Institutional) in December.

In gross terms and from a top-down angle, December's performance primarily reflected the negative effect of FX exposure, while Rates positioning also far outweighed the contribution from Carry.

From a bottom-up perspective, negative relative contributions were led by our aggregate overweights in South Africa and Brazil. Overweight exposure to India detracted to a smaller extent. These detractors were offset to a small extent by holdings in USD cash and cash equivalents, as well as an underweight position in Mexican FX.

## Positioning

In allocation terms, we again engaged in only a limited number of select adjustments to our positioning – both from a top-down and bottom-up angle. We are now short EM duration, albeit slightly long duration in beta-adjusted terms, while slightly underweight in EM FX.

Our allocations remain structured around the following unchanged cyclical top-down themes:

- Overweight EM Rates in countries with steeper yield curves, positive real yields and a sustainable fiscal outlook
- Underweight EM Rates in countries with low/negative real yields
- Overweight EM FX where balance of payments fundamentals appear most solid and/or in countries that are best positioned to outperform the global economic and/or commodity price cycle
- Underweight EM FX where balance of payments fundamentals or fiscal/monetary policy are most challenged
- Underweight or avoiding markets exposed to adverse political or economic event risk

## Outlook

We maintain our view that 2025 looks like being a challenging year for our asset class, and the main issue is identifying which challenge is biggest. China's economy has been the motor for the commodity exports that drive many EMs, and it seems clear that 2024's stagnation has not been enough to trigger the sort of aggressive policy response which has lifted the economy in the past. The Trump administration in the US is set on derailing the decades-long drive to globalise that has been a driver of EM progress. The European economy remains moribund, and Europe is the only credible driver for global growth that does not produce a stronger US dollar – an environment in which EM currencies invariably struggle.



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On the positive side, cyclical drivers are, if not positive, at least not obviously negative. Growth in the US remains robust and reasonably balanced, though has been dependent on loose fiscal policy without recent precedent. The post-Covid inflationary surge does look to have been transitory and, despite some recent scaling back of expectations, bond markets are still pricing in further rate cuts.

At the single country level, Czech, Mexican and South African rates markets rank as principal marginal duration overweights, while China, Malaysia and Thailand make up our main underweights.

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JPMorgan GBI-EM (Government Bond Index-Emerging Markets) Global Diversified Composite Index is a comprehensive global local emerging markets index that consists of regularly traded, liquid fixed-rate, domestic currency government bonds and includes only the countries that give access to their capital market to foreign investors (excludes China, India and Thailand). This index is unhedged USD.

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