GAM Multibond - Local Emerging Bond

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Market environment

Local emerging market (EM) bonds began 2025 on a firm footing. While concern over the impact of likely US trade tariffs had overshadowed the asset class ahead of Donald Trump's inauguration, investors adopted a more sanguine approach in late January on signs that tariff threats could be – at least in part – a negotiating tactic from the new administration to secure improved terms with some nations. The suspension of 25% tariffs on neighbouring allies, Mexico and Canada, after border security concerns were addressed raised hopes that threats of new barriers to trade, with tariffs of up to 25% on imports from the EU and China, could yet be overstated, albeit that considerable uncertainties remain.

The JP Morgan Government Bond Index Emerging Market (GBI-EM) Global Diversified Index ended the month +2.05% higher, more than reversing December's dip.

In regional terms, Latin American bonds led January's gains, with Brazilian debt in favour as the central bank's latest interest rate hike reassured investors over its determination to tackle inflation. Elsewhere, Turkish bonds also enjoyed a firm start to 2025, reflecting investors' confidence that the central bank's battle to contain sky-high inflation was finally being won as interest rates were cut for the second successive month. However, Asian bonds generally lagged behind the wider rally, with yields on Philippines bonds ending January largely unchanged, partly reflecting unease over firmer-than-expected inflation data.

Performance

The strategy had positive start to the year, with a January return of 217 basis points (bps), outperforming the benchmark by 12 bps.

In gross terms and from a top-down angle, January's performance primarily reflected contributions from both Rates, FX, and to a lesser extent, Carry. In a benchmark-relative context, Rates positioning more than offset a modest detraction from our FX exposure.

From a bottom-up perspective, the strategy benefited from aggregate allocations to Brazil, Colombia, Mexico, and to a lesser degree, the Czech Republic and South Africa.

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. In the aggregate, we remain modestly underweight both EM duration and EM FX, at least in nominal terms.

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

Notwithstanding January's positive returns, we maintain our view that our asset class is facing a number of challenges in 2025, with the main issue 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

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which has lifted the economy in the past, although we await developments with keen interest. Meanwhile, the Trump administration in the US is set on derailing the decades-long drive to globalise that has been a driver of EM progress, although it remains to be seen to what extent rhetoric will be matched with damaging action. 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.

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, albeit with less conviction than only a few months ago.

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

For more information, please visit GAM.com

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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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