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MONTHLY COMMENTARY JUNE 2020

VanEck Emerging Income Opportunities Active ETF (Managed Fund)

ASX Code: EBND

Investment objective

EBND aims to provide investors with a globally diversified portfolio of bonds and currencies in emerging markets. The fund aims to provide total investment returns, measured over the medium to long term in excess of the Benchmark.

Benchmark

A blended index consisting of 50% J.P. Morgan Emerging Market Bond Index Global Diversified Hedged AUD and 50% J.P. Morgan Government Bond-Emerging Market Index Global Diversified.

Performance as at 30 June 2020

	1 month	3 months	6 months	1 year	3 years (p.a.)	5 years (p.a.)	Since EBND inception (p.a.)
Price Return	3.51%	11.25%	-	-	-	-	-7.88%
Income Return	0.47%	1.61%	-	-	-	-	2.00%
Total Return	**3.98%**	**12.86%**	**-**	**-**	**-**	**-**	**-5.88%**
Benchmark	0.14%	4.61%	-4.33%	-1.04%	3.86%	-	-6.81%
Value Add	**+3.84%**	**+8.25%**	**-**	**-**	**-**	**-**	**+0.93%**

Benchmark is 50% J.P. Morgan Emerging Market Bond Index Global Diversified Hedged AUD and 50% J.P. Morgan Government Bond Emerging Market Index Global Diversified. The table above shows past performance of the Fund from its Inception Date and of the Benchmark from 31 December 2015. Results are calculated to the last business day of the month and assume immediate reinvestment of distributions. Fund results are net of management fees and costs, but before brokerage fees or bid/ask spreads incurred when investors buy/sell on the ASX. Returns for periods longer than one year are annualised. Past performance is not a reliable indicator of current or future performance which may be lower or higher.

Key benefits

Emerging market income opportunities: Emerging markets bonds generally pay higher interest than developed markets bonds offering investors an opportunity to broaden their income horizon with elevated risk.

Active management: An actively managed benchmark-unaware approach that makes high conviction investments.

Target yield of 5% per annum: Income from investing in emerging markets government, semi-government and corporate bonds that provides an attractive addition for investors' growing income needs.

Key risks

An investment in the Fund carries risks associated with: emerging markets bonds and currencies, bond markets generally, interest rate movements, issuer default, currency hedging, credit ratings, country and issuer concentration, liquidity and fund manager and fund operations. See the PDS for details.

Fundamentals[1]

Number of constituents	60
Number of issuers	33
Modified Duration (yrs)	6.46
Yield to Maturity	7.69%
Running Yield	7.92%
Weight of top 10 issuers	64.0%
Credit Rating Profile	B+
Time to Maturity (yrs)	12.78
Top Holding Weight (%)	4.89%
Investment Grade (%)	24.64%

1. As at 30 June 2020

Summary

- VanEck Emerging Income Opportunities Active ETF (Managed Fund) (EBND) outperformed the benchmark in June by 384bps.
- Strong contributors to the outperformance was a result of country exposure, specifically Angola, Indonesia and El Salvador.
- Top five current Portfolio country exposures are currently in Indonesia, Argentina, Angola, Mexico and Uruguay.
- We remain optimistic still seeing opportunities created by the COVID-19 crisis.
- Rebounding growth data out of China and Emerging Markets point to a sharper economic recovery than the market had been pricing. Nonetheless, bearish commentators will point to still weak levels of growth and employment, while the bulls will point to strong changes in growth and employment. This is why we like the re-raters rather than top-down global 'themes', where any story can make sense.

Market and portfolio commentary

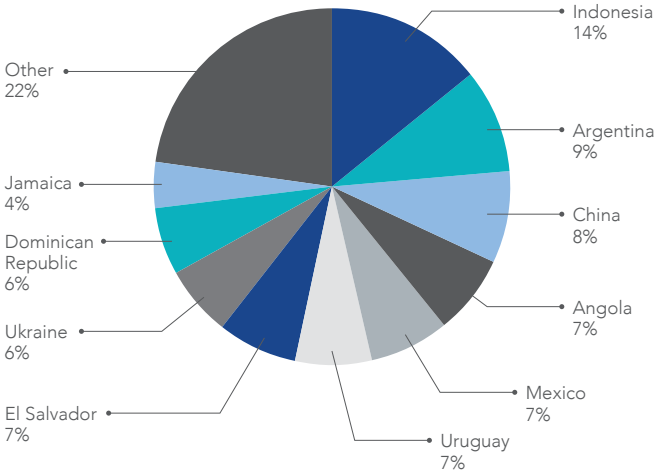
VanEck Emerging Income Opportunities Active ETF (Managed Fund) (EBND) outperformed in June aided by our exposure to Angola, Indonesia, El Salvador and Jamaica.

The success of our selectivity is highlighted by the fact that the local currency index, the JP Morgan Government Bond Emerging Market Index Global Diversified barely rose in June compared to the hard currency benchmark. Yet despite EBND having had around 40% in this poorer performing part of EM debt, it still significantly outperformed. Our local currency exposure to Indonesia, in particular, turned out well for country specific reasons. We think this underpins the view that this is a country and company pickers market, not a global macro view market.

We remain optimistic, still seeing opportunities created by March's liquidity crisis. As was the case in May, we still see exciting investment opportunities in "catch-up" situations. These opportunities can be characterised as being oversold/poorly sponsored, and have improving fundamentals, they are arguably re-rating candidates. The key ones include Argentina, Angola, Ukraine, El Salvador, Uruguay, and Jamaica.

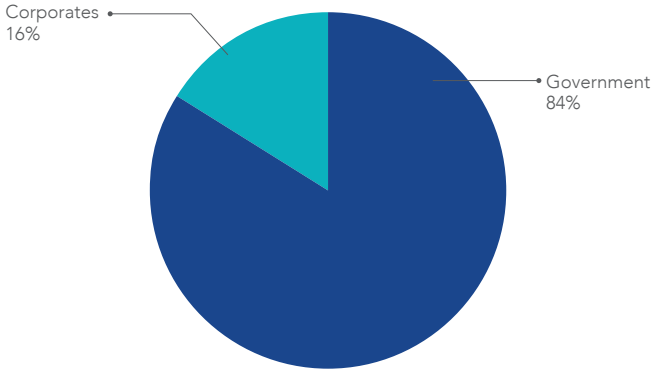
- **Argentina** is negotiating with creditors, not fighting with them; that has now been priced in. The government's latest offer is worth substantially more than the market is pricing.
- **Angola** is adhering to a credible IMF program and benefitting from bilateral sovereign creditors' (quasi) debt forgiveness, without requiring bondholders to haircut debt. All of this arose amid the COVID-19 liquidity crisis, which in our view represents a potential re-rating process.
- **Ukraine** remains a juggernaut, and the pandemic crisis is just overstated. It is adhering to its IMF program, has market access, and is subject to significant upside growth risks as well as being cheap in our investment process. While the central bank governor's resignation has thrown up some uncertainty, we think this is in line with the noise surrounding a deeply reformist impulse.
- **El Salvador** has a new reformist president, whose new party is set to gain new seats in the legislature next year. The long-term policy prospective is positive, and there are indications of an IMF program. The problem is that newly elected President Bukele has increased spending due to COVID-19, and the balance between the need to stimulate and the need to moderate is unclear. He wants a good setup in the lead-up to the elections, and we are supposed to believe he will do all the right things when he has full power. We believe it, but 2021 is far away. Practically, our view could be at risk from bond issuance in the coming 12 months, correlation risk and other factors including being wrong in our judgment on the long-term policy trajectory.
- As for **Uruguay** and **Jamaica**, events of the past month seem consistent with their re-rating stories.

Country breakdown



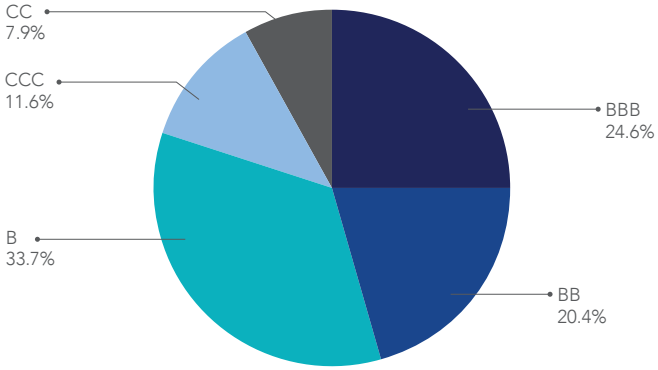
Source: VanEck, as at 30 June 2020.

Portfolio Allocation



Source: VanEck, as at 30 June 2020.

Credit rating breakdown



Source: VanEck, as at 30 June 2020.

Our outlook has not changed, we still see incredible buying opportunities in emerging market bonds similar to those during the GFC.

- EMs have the same fundamentals that made it perform and attract inflows post-GFC when lower leverage and higher real interest rates characterised emerging markets relative to developed markets.
- There's more stimulus from developed markets in response to the current crisis than there was to the GFC. Some of this money will flow to emerging markets bonds, in our view, as happened post-GFC. Also, a lot of the developed stimulus for this current crisis is specifically aimed at stabilising emerging markets.
- There is a lot of emerging market bonds being sold at prices reflecting a liquidity crisis. As economies stabilise, and as COVID-19 eventually abates, we see upside in a number of situations.

Portfolio changes

The changes to our top positions are summarised below.

- Our largest overweight country positions are currently: Indonesia, Argentina, Angola, Mexico and Uruguay.
- We increased our hard currency sovereign exposure in Jamaica and Honduras. Jamaica's sovereign valuations improved after the latest iteration of our valuation model, which was great news given that the country has good macroeconomic policies that should support a relatively speedy exit from the current crisis. In Honduras, the government gave an update to investors, during which it identified about US$1 billion from multilateral creditors (concessional credits) which should cover the country's financing needs for 2020. Honduras also expanded its program with the IMF, which runs through 2021 and should serve as a powerful policy anchor.
- We also increased our hard currency sovereign exposure in Angola and Tajikistan. Our position in Angola increased as its price appreciated, investors finally caught on to the fact that the country has good relations with the IMF and that it cleared a lot of debt issues with China. In regards to Tajikistan, the sovereign had a high valuation in our model (the highest initial allocation bucket), and it does not look like it will be having near-term problems with debt payments. It applied to participate in G20 debt relief program, and the IMF thinks that the country's debt will be sustainable on current policy commitments.
- Against these, we reduced our hard currency sovereign exposure in Azerbaijan and Mongolia. We used the proceeds to fund better opportunities, because bonds' spread-to-yield ratios in both countries were among the lowest in the portfolio.
- We also reduced our local currency exposure in South Africa and Mexico. South Africa's surging fiscal deficit and debt ratios, and the slump in real GDP growth pushed down the economic test score for the country. These factors are behind growing concerns about issuance and financing needs – there is no clear policy on how to address these challenges. Mexico also generated negative headlines during June, but the reason we sold a longer-dated local bond is that the valuation became stretched after a rally.

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