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DECEMBER 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 31 December 2020

	1 month	3 months	6 months	1 year	3 years (p.a.)	5 years (p.a.)	Since EBND inception (p.a.)
Price Return	0.38%	2.51%	4.42%	-	-	-	-3.81%
Income Return	0.00%	0.90%	2.32%	-	-	-	4.27%
Total Return	**0.38%**	**3.41%**	**6.74%**	**-**	**-**	**-**	**0.46%**
Benchmark	0.30%	3.67%	3.03%	-1.44%	3.80%	-	-3.99%
Value Add	**+0.08%**	**-0.26%**	**+3.71%**	**-**	**-**	**-**	**+4.45%**

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

Fundamentals[1]

Number of constituents	77
Number of issuers	47
Modified Duration (yrs)	5.90
Yield to Maturity	4.67%
Running Yield	5.47%
Weight of top 10 issuers	45.0%
Credit Rating Profile	BB+
Time to Maturity (yrs)	8.42
Top Holding Weight (%)	3.06%
Investment Grade (%)	46.65%

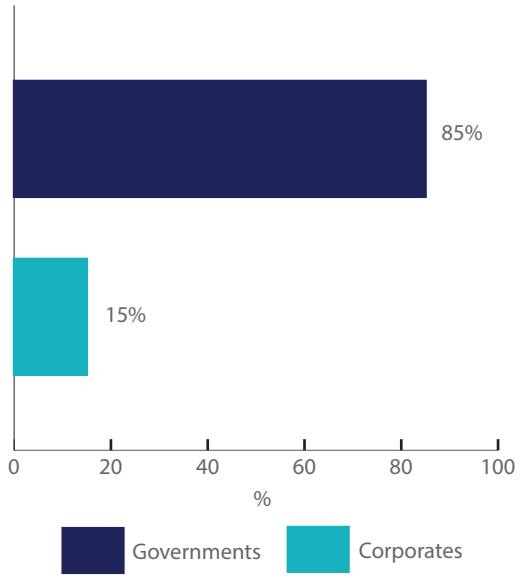
1. As at 31 December 2020

Monthly Dividends History (CPU)

Financial Year	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	YTD
2021	5	5	5	5	5	5	-	-	-	-	-	-	30
2020	-	-	-	-	-	-	-	2.5	5	5	5	5	22.5

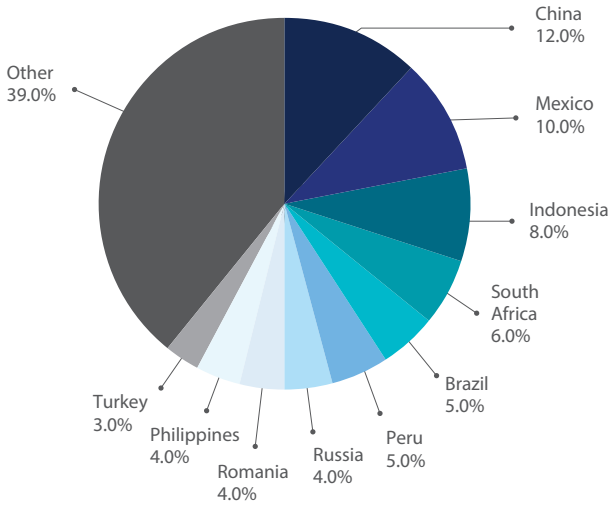
Source: VanEck. Past dividends are no indicators of future dividends. CPU is Cents per Unit. Since EBND inception, 11th February 2020.

Portfolio Allocation



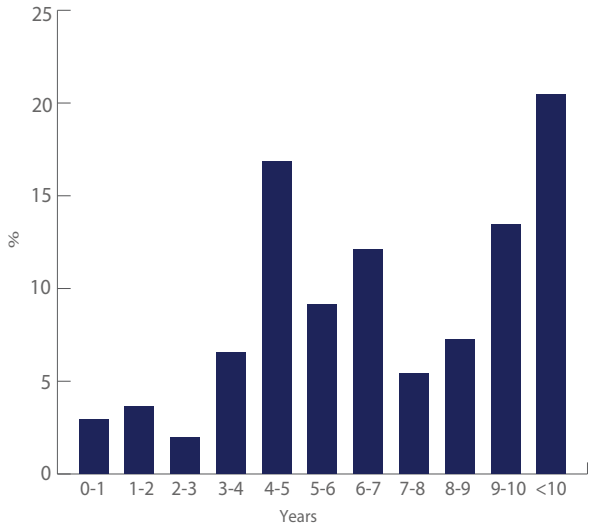
Source: VanEck, as at 31 December 2020.

Top 10 Country Breakdown



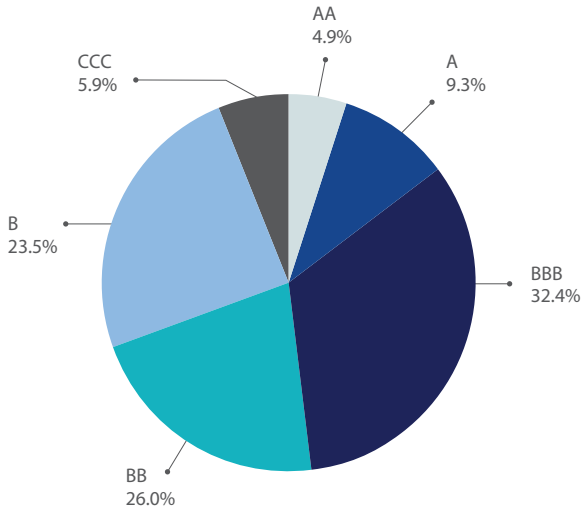
Source: VanEck, as at 31 December 2020.

Time to Maturity Profile



Source: VanEck, as at 31 December 2020.

Credit rating breakdown



Source: VanEck, as at 31 December 2020.

Summary

- The VanEck Emerging Income Opportunities Active ETF (Managed Fund) (EBND) returned 0.38% in December outperforming the 50% J.P. Morgan Emerging Market Bond Index Global Diversified Hedged AUD and 50% J.P. Morgan Government Bond-Emerging Market Index Global Diversified Index by 0.08%

- Top five country exposures are currently in China, Mexico, Indonesia, South Africa and Brazil.

- With 2020 now behind us it is worthwhile reflecting on the year. What worked for the fund was our view that the March/April selloff was a buying opportunity. Later in the year, the portfolio benefited from taking profits on the bonds we bought in April, and shifted the portfolio to have a greater allocation to local currency bonds. This remains key to our current view and we currently have 60% of the fund in local currency.

- Looking ahead, US rates look set to rise, making duration a big risk, especially for "safe" investment-grade bonds. EMFX seems likely to benefit from global reflation, as rising yields are being generated by risk-on economic conditions, not taper-tantrum conditions. Commodity prices, too, appear set to continue to rise, supporting our positioning.

Market and portfolio commentary

EBND outperformed its benchmark in December, aided by our holdings in Mexico, Suriname, China, and Russia. Holdings in Brazil, Sri Lanka and Indonesia detracted from performance as these markets rose less than for the benchmark.

The fund currently has about a 60% allocation in local currency bonds, which is about as high as we get. These positions include a combination of safer Asian stalwarts, such as China and Indonesia, as well as those bonds referred to as 'high-beta' EMFX such as South Africa, Russia, Mexico, and Turkey. These currencies tend to move quickly.

We continue to like China for reasons explained in previous monthly commentaries. Moreover, if the authorities challenge currency weakness, the bonds themselves should rally – they offer among the highest real yields in emerging markets.

Indonesia is a reform stalwart with high real yields and we increased our position during December. Russia has never had better fundamentals and we see sanctions risks as being priced into current values. While South Africa is not being supported by the market, it does have an improving current account and the prospect of near-term growth. In Latin America, Brazil benefits from strong external accounts, no real inflation pressures and leverage to global reflation.

Elsewhere we're closely watching considering Turkish in local currency bonds. We recently added its US dollar-denominated bonds. Turkey's real policy rate is the highest in the emerging markets world and it seems as if policy has been made orthodox.

There are numerous fundamental drivers underlying our views and positioning. First, hopes of more US fiscal stimulus are growing now that the Democrats have control of the Senate. On that note, stimulus should continue to generate even bigger current account deficits, which generally help emerging markets economies. Second, Chinese currency strength translates into global inflation. Third, higher oil and other commodity prices should further boost inflation and emerging markets fundamentals. It doesn't look like US rate rises will be viewed as a challenge to the Fed, which seems willing to accept them for now. If we do get to the point of yield curve control, that will be when the Fed will realise it is an organ of the government and cannot bankrupt it with high interest payments. That could be negative for the dollar and positive for risk assets.

G-10 rates have been highly correlated, and the rise in US rates should be mirrored in other "risk-free" bond markets.

It is difficult to find serious inflation pressures in emerging markets, and we tend to hold bonds with high real interest rates. Also, emerging markets tends to export the things that create inflation (food and energy), which means their external accounts (and currencies) should be supported. Inflation should ultimately be the result of policy, not these one-off price rises in emerging market economies, as emerging market's central banks tend to be orthodox.

So far since the start of the year, we've seen US rates, commodity prices and equities all rising, but not EMFX. EMFX is simply taking a breather, owing to overdone concerns about an early Fed taper. The trifecta of higher rates, higher commodity prices, and a lower US dollar should maintain in the first quarter of 2021. Moreover, EMFX remains below its pre-COVID highs. Fed Vice-Chair Richard Clarida recently clarified that there is no change to the central bank's bond buying program, pushing that discussion into late 2022.

Portfolio changes

The changes to our top positions are summarised below.

- We increased our local currency exposure in Indonesia, Colombia and Chile. Indonesia's valuations still look attractive. There were no negative changes in the macro story either, so the country's technical test score keeps improving and we felt comfortable getting closer to our sovereign limit. Colombia continues to benefit from the oil price dynamics and falling inflation. These factors improved the country's technical and economic test scores. Chilean assets should get a boost from strong correlations with China's economic rebound and the ensuing support to copper prices. In terms of our investment process, this improves the technical test score for the country.

- We also increased our hard currency exposure in Turkey. The Turkish central bank made its traditional orthodox policy U-turn after being cornered by the market, which was getting nervous about numerous policy slippages. President Erdogan replaced top economic officials (including the central bank governor and the finance minister), who were previously given "carte blanche" to fix things. The central bank immediately delivered two sizable and above-consensus rate hikes, and pledged to maintain tight policies, while the new minister of finance presented a decent to-do list. These changes led to a big improvement in technical and policy test scores for the country.

- Conversely, we reduced our local currency exposure in South Africa and Peru. We took partial profits in South Africa after the currency and rates rallied to incorporate a more realistic 2021 budget and a stronger global risk-on sentiment. In terms of our investment process, this worsened the technical test score for the country. The reason for taking partial profits in Peru was similar: local rates and the currency rallied on the back of lower political risks and the expectation of FX inflows after the second round of pension fund withdrawals, weakening the technical test score for the country.

- We also reduced local currency exposure in Thailand and Romania. We had good runs in both countries, benefitting from Thailand's incredibly strong current account position and the dissipation of Romania's domestic political risks. We think that both narratives have legs, but we felt it would be prudent to take partial profits and re-deploy the money to fund more attractive opportunities.

- Finally, we reduced our local currency exposure in Russia. We continue to like Russia's macroeconomic and policy stories – the latter one has been the best in years. But with recent news of a major US government agencies' hack strengthening the sanctions drumbeat, it is unclear if the post-election geopolitical thaw will last. In terms of our investment process, this worsened the policy test score for the country.

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