Asian Credit Strategies

Wavering rally to test investment convictions

- Some encouraging signs of macro recovery benefitting from strong central bank support as well as fiscal policies; concerns remain over virus containment and impact
- HY valuations still look attractive despite the rally with IG closer to fair value; considerable dispersion at the sector level
- Technicals are mixed, supported by abundant liquidity and demand for yield, offset by robust supply pipeline; sentiment is positive on balance

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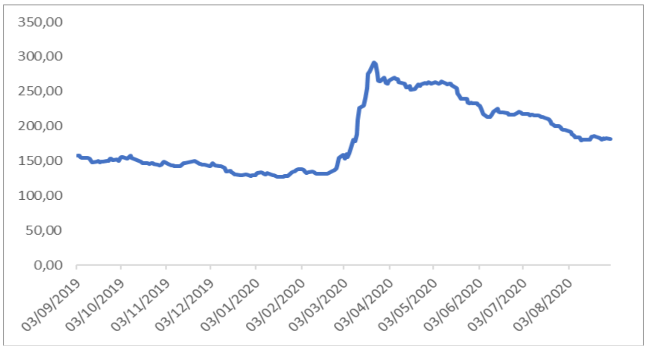
What's happening?

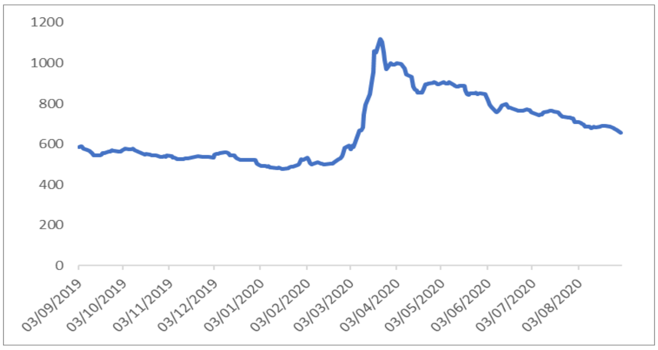
The J.P. Morgan Asia Credit Index (JACI) ended the month 0.4% higher in total return terms, marking a slowdown in the post-Q1 rally period. YTD returns at +4.94%. As of 31st August, the index is represented by 605 issuers, with a market capitalization amounting to US$ 1.16 trillion. JACI's positive performance has been underpinned by the strong contribution of High Yield sovereigns (+7,7%), with Sri Lanka (+11,5%) emerging once again as the best performing country on the month. Spread returns (+1,6%) sustained the positive performance, outweighing the drag in Treasury returns (-0,9%). The JACI High Yield (+2,2%) continued to outperform the Investment Grade segment (-0,1%), as single-B credit spreads gapped further in August. Economic data released in 2Q were overall positive, particularly in China and India, with some sectors showing signs of V-shape recovery. That said, the global outlook remains fragile, with the resurgence of the Covid-19 in India and Indonesia, and persisting US-China tensions, as a backdrop. The market sentiment was positive on balance, comforted by the ample liquidity provided by global central banks, and significant fiscal stimulus measures.

Asian Credit Market* Valuation

JACI IG Z Spread to Worst



JACI HY Z Spread to Worst



*Refers to the J.P. Morgan Asian Credit Index
Source: J.P. Morgan, as of 31/8/2020

Monthly Returns:

J.P. Morgan Asia Credit Index (JACI) +0.40%					
Investment Grade -0.10%			High Yield +2.15%		
Corporates +0.14%	Sovereign - 0,73%	Quasi-Sov -0,27%	Corporates +1.76%	Sovereign +7.66%	Quasi-Sov +1.07%

Portfolio positioning and performance:

Key Strategies		Performance
Country /Sector:	Maintained UW positioning to HY frontier sovereigns, which dragged on relative HY performance while structural UW to IG sovereigns helped in crossover strategies. OW to Indonesian HY corps and China HY where value and carry remain was broadly beneficial. Caution on IG Indian Corp and financials due to rating migration concerns was not a factor.	**=**
DTS:	DTS exposure close to neutral for HY strategy, with a preference for converting spread duration for carry. OW DTS positioning was beneficial for crossover SD strategy given continued HY spread compression.	**+**
Bottom-up:	Participation in new issues remains selective with mixed performance. Illiquid and distressed names have generally been marked down, having a negative impact across strategies; offset somewhat in HY by OW to recovering Indian M&M bellwether.	**-**

Outlook

Some volatility has recently returned to the Asian credit markets interrupting what has been a strong and steady rally and recovery from March's steep selloff. This is likely a sign of more to come as valuations in many sectors have returned to or even surpassed pre-Covid levels despite a fair amount of remaining uncertainty over the virus trends and impact. The news is far from all bad as recent economic data, particularly from China, suggests the economic recovery is gathering momentum. The market also seems calm in the face of US-China disagreements on a growing range of topics. Despite an abundance of heated rhetoric there have yet to be any actions of materially negative consequence for the market. While early November's US presidential election will not have an immediate impact on Asian bond issuers, anticipation of who will win and what they will do in their new administration will very likely make an impact across risk markets globally with ripples of various amplitudes finding their way into Asian credit portfolios. This alone should not deter conviction based bottom-up investing. While macro uncertainties may suggest a bias for duration neutrality and caution on a broad extent of credit exposure, opportunities exist to generate returns from spread compression and high yield carry. In this context, we currently favor high yield Indonesian corporates and short duration China property issuers while remaining cautious on investment grade Indian corporates and financials as a result of potential negative rating migration. Outside of China, India and Indonesia, valuations are extremely tight with exposure limited to issuers for diversification and defensive portfolio needs.

No assurance can be given that the Asian Credit Strategy will be successful. Investors can lose some or all of their capital invested.
The Asian Credit Strategy is subject to risks including Credit risk, Liquidity risk, Derivatives and leverage, Investments in specific countries or geographical zones, Sovereign debt, Emerging markets, High yield debt securities, Contingent convertible bonds.