Swiss Life Asset Managers

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"Emerging corporate debt is becoming an inescapable asset class"

As part of its corporate event entitled "Tendances & Perspectives", which was attended by investors and partners alike, Swiss Life Asset Managers presented a full perspective of the investment opportunities in the emerging corporate debt market.

In order to take advantage of this mature investment universe, which is nonetheless sensitive to exogenous factors (policies of the central banks, commodity price trends), an increase in the "country risk" and the selectivity of the issuers are the most important criteria.

Despite the slowdown in the past few years, the emerging economies continue to develop at a fast pace. In the opinion of Claudia Bernasconi, an economist who specialises in emerging markets at Swiss Life, "*the average growth rate in the emerging countries is anticipated to stabilise at between 4.4% and 5% per annum in the years to come, a rate significantly higher than that of the developed economies*."

This positive outlook is underpinned by the national monetary and budget policies which are far more stable than in the past. The exchange rate regime in the emerging countries is far better adapted to their most important foreign exchange reserves than a few years ago. *"In a large number of emerging countries, the governments have also introduced an effective budgetary policy by implementing fiscal reforms that have allowed the public deficit to be rigorously contained. As a result, the situation for the emerging markets is far healthier globally than in the 1990s*," states Claudia Bernasconi.

Measuring the "country risk" and the sensitivity to exogenous shocks

However, it is important to consider the heterogeneity of the various situations at the heart of the emerging markets. The short-term perspectives, taking into account any possible impact from exogenous factors, are quite different from one country to the next. Rishabh Tiwari, fund manager with Swiss Life Funds (LUX) - Bond Emerging Markets Corporates, insists that it is essential not to underestimate the "country risk". *"Our investment approach is purely bottom-up, we focus above all on the fundamentals of the company's credit. If the issuer, however robust it might be, is over-sensitive to the risk of the economic, political or judicial instability of its country, we refrain from investing in its debt."*

Claudia Bernasconi highlights the countries that have been penalised by the recent collapse in the price of commodities, "*as the main exporters of commodities amongst the emerging countries, Peru, Chile and Russia have been affected by the fall in the price of commodities. On the other hand, however, China, Turkey and Thailand have all benefited from this trend as they are major consumers of commodities."*
As for the impact of the tighter monetary policy in the USA, it could have particularly severe implications for Turkey and South Africa. "*The increase in rates by the Fed in next June or September could put pressure on these countries as they are financing their deficits through international capital*," she explains.

As well as the margin for manoeuvre in economic policy matters, it is also important to take into account the structural specifics for each country. Brazil, South Africa and Russia for example are confronted by a severe shortage of investments, whilst in India and Mexico the structural reforms initiated by their governments are sufficient to sustain growth.

Blue chip issuers

Emerging corporate debt forms an asset class that has gained in maturity and its expansion is supported by the investment flows from the institutional players in the United States, Asia and the Middle East. "*This asset class fulfils the aims of investors for diversification, whilst still maintaining an attractive risk/return profile. Whilst it is becoming increasingly difficult to find satisfactory returns on the debt securities markets in the developed countries, the issuers for the emerging markets benefit from comparative advantages*," says Rishabh Tiwari.

In effect, the majority of companies in the emerging markets are classified as "High Grade" and have a better quality debt ratio compared with that of companies in the developed markets. In terms of potential yields, emerging market credit enjoys an attractive premium: the spread between the investment grade bonds issued on the emerging markets and of their counterparts in the developed markets is around 150 basis points.

"Within the scope of our investment strategy, we favour investment grade securities exclusively and only those that are issued in a hard currency. We aim to identify bonds where the credit spread seems unjustified, with regard to the quality of the issuer's underlying," Rishabh Tiwari explains. *"For example, we recently subscribed to the bond Coca-Cola Icecek 2018 (Turkey), which stood out due to a return at maturity of 3.01% and a rating BBB whilst the company posted earnings growth of 5.7%. In contrast, the German issuer Metro AG 2019, is offering a derisory return at maturity of 0.6%, even though the company's underlying is less (earnings of 0.3%, rating BBB-)*," the manager says in conclusion.

About Swiss Life Asset Managers - www.swisslife-am.com

Swiss Life Asset Managers has more than 150 years of experience in managing the assets of the Swiss Life Group and has developed from this a complete range of products and services. This insurance background has exerted a key influence on their investment philosophy, which is governed by such principles as the generation of consistent and sustainable performance as well as a responsible approach to risks. As at 31.12.2014 Swiss Life Asset Managers managed a total volume of EUR 152.2 billion assets for the Swiss Life Group, of which EUR 28.0 billion was for external clients in France, Switzerland and Germany as well as for international clients.

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