



# BlueBay Global Sovereign Opportunities Debt Weekly Update

February 15, 2018

## Big Picture

- It has been a difficult week of performance for the strategy. Extreme volatility generated within US equity markets has driven weakness in European peripheral assets, especially Greece, and in emerging market (EM) hard currency government bonds. Yields in core rates markets have retreated from their highs as it has become obvious that risk assets can no longer ignore the repricing of future Federal Reserve rates hikes and longer-dated maturities moving above 3% in yield. The strategy has benefitted modestly from downside S&P and Hang Seng puts.
- Oil markets have also been hard hit, which has been negative for the EM sovereign book where we have exposure to Ecuador, Nigeria and the Mexico national oil company.
- In Europe, Greece brought a new seven year deal right into the teeth of escalating volatility causing a significant re-pricing of the entire curve and hurting performance.
- The FX book has been negative for returns, long positions in the Scandinavian currencies (Norwegian krone and Swedish krona) were negative, as were longs in the Russian rouble, the Kazakh tenge, and the Brazilian real. The short position in the Mexican peso was a boost for performance, and we re-entered a short in the UK pound vs the euro which has also been positive.

## Opportunity Bites

- We stick to the view that unless we get a strong macro fundamental impulse coming from economic data or major central banks, then global risk conditions should settle down in the coming weeks. To this end, we are watching the evolution of inflation, particularly in the US. The biggest sustainable risk to the goldilocks environment is rapidly rising core inflation in the US, which would lead to an acceleration of rate hikes out of the US. Our base case is that it is too early to see this move, and on this basis, we are cautiously adding risk where valuations have improved and the underlying fundamental stories are still constructive.
- In terms of the short rates exposure, we continue to like the risk reward at the front end of the US curve, and maintain short positioning in the December 2019 Eurodollar contract. However, we are also positioned long duration in Europe. This trade works for the balance of the strategy from two angles. A recent research trip to Frankfurt to meet with officials from the European central Bank (ECB) confirmed our perception that the market has become more bearish on the outlook for rates than is the reality from within the core governing council of the ECB. Secondly, if volatility in equity markets persists, and there is more of a risk transfer that needs to take place in EM assets, then Bund's will benefit from flight to quality and the strategy will be somewhat protected.
- In EM local markets, we maintain long duration positions in South Africa, Mexico, Brazil and Russia. In sovereign credit, we have reduced risk by cutting out of the long Spain maturity, but remain long in Greece and Italy. In EM, we maintain a modest long through Argentina, Ecuador, Nigeria and Kazakhstan.
- The FX book has edged longer EM beta versus the US dollar, primarily through a new position in the Indonesian rupiah. We like the fundamental backdrop in Indo, and also are playing for the technical, flow driven boost that should come when Indonesia is included in the Barclays Global Agg index. We have modest longs in South African rand, Argentine peso, Nigerian naira and the Egyptian pound, against a short in the Mexican peso. In Europe, we maintain long positions in the Scandinavian currencies including the Norwegian krone, the Swedish Krona and the Icelandic Krona against the euro.

## Contributors and detractors (02/02-09/02)

Alpha Family	Contributors	Detractors	P&L
G10 Rates	Short: US duration, Japan duration Long: EUR duration		-
Other Rates	Long: South Africa, Iceland	Long: Mexico	-
Sovereigns		Long: Argentina, Ecuador, Nigeria, Mexico, Greece	-
Currency	Short: MXN vs USD, GBP vs EUR	Long: RUB, BRL, ARS, KZT vs USD, NOK, SEK vs EUR	-
Non Sov	Short: S&P put, Hang Seng put	Long: Mexican sovereign oil company	+

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