

# Virtus Stone Harbor Emerging Markets Bond Fund

A: VSHAX (92828Y615) | I: SHCDX (92828Y599)

## MARKET REVIEW

### Sector Review “Broad Market”

Following strong gains in the fourth quarter of last year, the global backdrop was more challenging for fixed income investors in the first quarter of 2024. Upside surprises to U.S. economic growth and inflation readings led to upwards pressure on core bond yields, as market participants scaled back expectations for Federal Reserve (Fed) easing over the balance of 2024. However, despite higher core bond yields, external debt returns in emerging markets remained positive, largely due to a continued compression in risk premia for high yield emerging markets (EM) sovereign and corporate issuers. EM fundamentals have been supported by continued disinflation, together with on-going policy easing, which have in turn supported an improvement in growth prospects. Local currency EM debt returns were hurt by renewed strength in the U.S. dollar, although local yields were broadly unchanged during the quarter, notwithstanding the increase in U.S. Treasury yields.

For more on our quarterly market review and outlook, [click here](#).

### Benchmark Performance

The J.P. Morgan CEMBI Broad Diversified posted a total return 2.3%, consisting of positive returns from high yield bonds (+4.2%) and positive returns from investment grade bonds (+1.0%). High yield bond spreads declined by 87 bps, and investment grade bond spreads declined by 24 bps, on average.

At the industry level, all industries had positive total return with the real estate and transport sectors the largest outperformers. Within the real estate sector, Chinese homebuilders were a top contributor with an average total return of 6.5%. The pulp & paper and oil & gas sectors were the largest underperformers with total returns of 1.1% and 1.6%, respectively.

At the regional level, Africa and Europe were the top performers posting total returns of 4.1% and 3.2%. In Europe, Ukrainian bonds were the largest contributor to total return as Metinvest released positive operational results. Corporate bonds from the Middle East underperformed the benchmark with a total return of 1.1% for the quarter.

## FUND PERFORMANCE REVIEW

The Fund (Class I) returned 2.84% (net of fees) and 3.10% (gross of fees) in the first quarter versus the J.P. Morgan CEMBI Broad Diversified Index return of 2.32%.

### Positive Contributors

- > **Mexico:** Issue selection
- > **Brazil:** Overweight exposure and issue selection
- > **India:** Overweight exposure and issue selection

### Performance Detractors

- > **Philippines:** Underweight exposure and issue selection
- > **Hong Kong:** Underweight exposure and issue selection
- > **South Africa:** Overweight exposure

## OUTLOOK & STRATEGY

Our base Case (40% probability) assumes a soft-enough landing that will enable the U.S. Fed to cut interest rates as the economy and inflation slow in response to higher interest rates. We currently expect between two to three reductions in the Fed funds rate over the balance of the year. The ECB is also likely to cut rates in response to a sluggish domestic economy and lower inflation rates. China is likely to continue its gradual easing policy to sustain growth, although largescale bailouts are unlikely due to moral hazard issues. The three main risks that we have identified include a sharper-than-expected fall in inflation, a sharper-than-expected fall in global growth, and also a more resilient U.S. economy leaving the Fed on hold for an extended period of time.

For external markets, in our base case, we see spreads as being more or less fairly priced at current levels, but lower core interest rates supporting overall total return gains. The major downside for EM risk premia is posed by the global recession scenario—when core rates would likely fall significantly. Total return expectations would also be lower than the Base Case in a scenario where the Fed remains on-hold, as core rates would likely continue their recent move higher.

Within the local currency space, we continue to see scope for local interest rates to fall as easing cycles are maintained. There may also be scope for some weakening of the U.S. dollar once the Fed starts to ease interest rates. Again, the global recession scenario and the Fed on-hold scenario would likely see renewed dollar strength, potentially damaging returns.

**PERFORMANCE ATTRIBUTION BREAKDOWN** as of 03/31/2024

Portfolio (gross basis - USD)	3.10
JPM CEMBI Broad Div	2.32
<b>Difference</b>	<b>0.78</b>
<b>Breakdown</b>	
Country Attribution	0.21
Issue Attribution	0.63
Miscellaneous Difference	-0.06

**REGIONAL ALLOCATION** % Fund Benchmark

Africa	9.06	7.42
Asia	39.99	41.94
Europe	5.45	7.14
Latin America	29.73	24.81
Middle East	12.91	18.69
Net Cash	2.86	0.00

Weightings are subject to change. Weightings may not add up to 100% as a result of the use of certain financial instruments, including derivatives, which may be used to gain or reduce market exposure and/or for risk management purposes.

**SECTOR DISTRIBUTION** % Fund Benchmark

Sovereign Hard Currency	4.06	0.00
Corporate Hard Currency	93.08	100.00
Sovereign Local Currency	0.00	0.00
Corporate Local Currency	0.00	0.00
Net Cash	2.86	0.00

Sector weights are subject to change.

**TOP 5 COUNTRIES (%)**

	Sovereign-Hard		Sovereign-Local		Corporate-Hard		Total	
	Fund	Index	Fund	Index	Fund	Index	Fund	Index
Brazil	0.00	0.00	0.00	0.00	8.02	5.18	8.02	5.18
Mexico	0.93	0.00	0.00	0.00	6.94	4.51	7.87	4.51
India	0.00	0.00	0.00	0.00	6.74	4.27	6.74	4.27
Macau	0.00	0.00	0.00	0.00	5.48	3.71	5.48	3.71
Indonesia	0.36	0.00	0.00	0.00	5.10	3.20	5.46	3.20

**CURRENT FUND STRATEGY**

**Positioning**

- > Underweight U.S. Treasury duration
- > Regional overweight in Latin America
- > Underweights in Banking, Technology, and Food & Beverage. Overweights in Exploration & Production, Electric, and Gaming.
- > BB-rated credits are favored

Strategy	YIELD (%)		RATING**		NOTABLE DEVIATIONS	
	Portfolio	Relative*	Portfolio	Benchmark	O/W	U/W
Corporate Hard Currency	7.39	0.46	BB+	BBB-	Brazil, India, Mexico	Qatar, Taiwan, China
Quasi-Sovereign Hard Currency	7.40	N/A	BBB-	N/A	UAE, South Africa, Mexico	N/A <sup>†</sup>

\*Relative to JPMorgan CEMBI Broad Diversified Index.

\*\*Credit ratings issued by Nationally Recognized Statistical Rating Organizations assess the credit worthiness of the issuers of the underlying securities and not to the Fund or its shares. Ratings are measured using a scale that ranges from AAA (highest) to NR (not rated). Not rated securities do not necessarily indicate low quality. The security's credit rating does not eliminate risk and credit ratings are subject to change. Credit Quality reflects a weighted average composite of the ratings of Standard & Poor's Corporation, Fitch, Moody's Investors Service, Inc and DBRS. Ratings are then adjusted to the Standard & Poor's rating tiers shown. In the case where the composite is in between two ratings the rating will be rounded down. A composite will not be generated if the bond is only rated by one of the four rating agencies. Expected ratings and unsolicited ratings, designated by 'e' and 'u', are not included in calculating the composite.

<sup>†</sup>Not in the index.

Benchmark: JPMorgan CEMBI Broad Diversified Index.

**AVERAGE ANNUAL TOTAL RETURNS (%)** as of 03/31/24

	QTD	YTD	1 Year	3 Year	5 Year	10 Year	Since Inception 06/01/11
<b>Class I</b>	2.84	2.84	10.55	0.86	3.34	3.85	3.41
<b>J.P. Morgan CEMBI Broad Diversified Index</b>	2.32	2.32	9.17	-0.13	2.63	3.73	4.08

Performance data quoted represents past performance. Past performance does not guarantee future results. Investment return and principal value will fluctuate so that shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please visit [virtus.com](http://virtus.com) for performance data current to the most recent month end. This share class has no sales charges and is not available to all investors. Other share classes have sales charges. See [virtus.com](http://virtus.com) for details.

The fund class gross expense ratio is 2.21%. The net expense ratio is 1.00%, which reflects a contractual expense reimbursement in effect through 9/30/2024.

Average annual total return is the annual compound return for the indicated period and reflects the change in share price and the reinvestment of all dividends and capital gains. Returns for periods of one year or less are cumulative returns.

Index: The **J.P. Morgan CEMBI Broad Diversified Index** tracks total returns for U.S. dollar denominated debt instruments issued by corporate entities in emerging markets countries. The benchmark limits the current face amount allocations of the bonds in the CEMBI Broad by constraining the total face amount outstanding for countries with larger debt stocks. Qualifying corporate bonds have a face amount greater than USD 300 million, maturity greater than 5 years, verifiable prices and cash flows, and from countries within Asia ex Japan, Latin America, Eastern Europe, Middle East, and Africa. The index is calculated on a total return basis. The index is unmanaged, its returns do not reflect any fees, expenses, or sales charges, and is not available for direct investment.

**INVESTMENT ADVISER**

Virtus Investment Advisers, Inc.

**INVESTMENT SUBADVISER**

Stone Harbor Investment Partners

**PORTFOLIO MANAGERS**

**Peter J. Wilby, CFA**

Industry start date: 1980

Start date as Fund Portfolio Manager: 2011

**James E. Craige, CFA**

Industry start date: 1988

Start date as Fund Portfolio Manager: 2011

**Stuart Sclater-Booth**

Industry start date: 1992

Start date as Fund Portfolio Manager: 2017

**Kumaran Damodaran, Ph.D.**

Industry start date: 2000

Start date as Fund Portfolio Manager: 2015

**David A. Oliver, CFA**

Industry start date: 1986

Start date as Fund Portfolio Manager: 2011

**Notes on Risk: Emerging Markets Investing:** Emerging markets securities may be more volatile, or more greatly affected by negative conditions, than those of their counterparts in more established foreign markets. **Foreign Investing:** Investing in foreign securities subjects the portfolio to additional risks such as increased volatility; currency fluctuations; less liquidity; less publicly available information about the foreign investment; and political, regulatory, economic, and market risk. **Credit & Interest:** Debt instruments are subject to various risks, including credit and interest rate risk. The issuer of a debt security may fail to make interest and/or principal payments. Values of debt instruments may rise or fall in response to changes in interest rates, and this risk may be enhanced with longer-term maturities. **Counterparties:** There is risk that a party upon whom the portfolio relies to complete a transaction will default. **Currency Rate:** Fluctuations in the exchange rates between the U.S. dollar and foreign currencies may negatively affect the value of the portfolio's shares. **Derivatives:** Derivatives may include, among other things, futures, options, forwards and swap agreements and may be used in order to hedge portfolio risks, create leverage, or attempt to increase returns. Investments in derivatives may result in increased volatility and the portfolio may incur a loss greater than its principal investment. **High Yield Fixed Income Securities:** There is a greater risk of issuer default, less liquidity, and increased price volatility related to high yield securities than investment grade securities. **Liquidity:** Certain instruments may be difficult or impossible to sell at a time and price beneficial to the portfolio. **Income:** Income received from the portfolio may vary widely over the short- and long-term and/or be less than anticipated if the proceeds from maturing securities in the portfolio are reinvested in lower-yielding securities. **Market Volatility:** The value of the securities in the portfolio may go up or down in response to the prospects of individual companies and/or general economic conditions. Local, regional, or global events such as war or military conflict, terrorism, pandemic, or recession could impact the portfolio, including hampering the ability of the portfolio's manager(s) to invest its assets as intended. **Prospectus:** For additional information on risks, please see the fund's prospectus.

**Please consider a Fund's investment objectives, risks, charges, and expenses carefully before investing. For this and other information about any Virtus Fund, contact your financial professional, call 800-243-4361, or visit [virtus.com](http://virtus.com) for a prospectus or summary prospectus. Read it carefully before investing.**

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