

MONTHLY INVESTMENT REPORT – 30 JUNE 2023

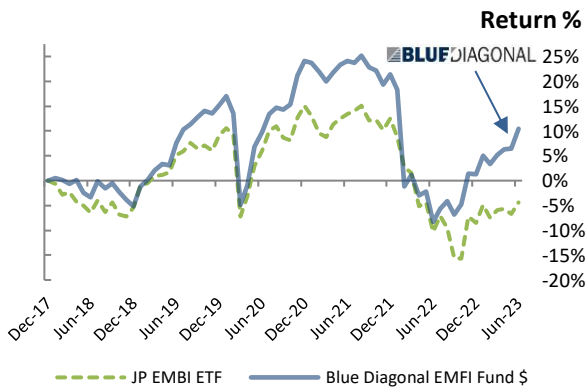
BLUE DIAGONAL EM FIXED INCOME FUND

Class A (EUR) NAV per share: 0.966224 (0.933239)
 Class B (USD) NAV per share: 1.195652 (1.151872)

Class A (EUR) Monthly Ret: +3.53% (1y Ret: +19.2%)
 Class B (USD) Monthly Ret: +3.80% (1y Ret: +20.4%)

Fund Performance

The Fund had a strong performance with a return of +3.8% in June, outperforming the benchmark JP EMBI Global Index by ~200bp for the month, and by 5.1% Year to Date.



Source: Blue Diagonal Capital, Bloomberg

Macro Environment

Recent US economic data continue to come out better than expected, with US Q2 GDP growth now expected to come in above 2%. The strength in employment data in combination with core inflation persisting above 4.50% points to a hawkish FED, and a US policy rate that will likely stay elevated for a considerable period of time.

In Europe, where inflation is also elevated, economic growth has stagnated. The manufacturing sector has remained weak, while service sector strength has started to soften. Lower/middle income households with variable rate mortgages will suffer a double hit from the higher cost of living and considerably higher mortgage interest payments. The transmission mechanism of higher rates will vary from country to country depending on each country's ratio of fixed-rate v floating mortgages.

Saudi Arabia and Russia are working in conjunction to stabilize the oil price above \$75pb (Brent crude) by reducing the supply of oil against a background of disappointing demand.

EM sovereign bond yield ended the month slightly above 8.00%. EM credit spread came down to ~365bp (from 400bp), with the 10y US Tr. yield higher at 3.85% from ~3.65% a month ago.

Investment Outlook

The recent flood of Artificial Intelligence (AI) news coverage has generated a euphoric wave in a narrow section of US stocks driving equity index returns higher. It has raised market confidence, and together with the better-than-expected US economic data, the predictions of a near-certain US recession has receded somewhat. US Treasury yields rose – especially in maturities up to 5 years, while long-term rates have proved more resilient. The risk-on environment has contributed to a rally in EM high yielding bonds that tend to perform best when the world economy is set to grow/avoid a recession.

The persistent weakness in manufacturing across the developed world and in China - where the reopening of the economy (post Covid) has mostly benefited the service sector – has impacted the prices of some commodities such as industrial metals, while lower demand for oil has been met by reduced supply. Precious metals have been the least affected and prices remain elevated.

Geopolitical tensions are adding complexity to the macro analysis. Ukraine has launched its long-awaited counter offensive, while the recent internal political challenges in Russia could lead to unforeseen events. The technological cold war between US/EU vs China is escalating – China will now limit the export of materials critical to chip production as of August 1st. The move to a multi-polar world will present complex challenges for many EM countries.

High US/EU interest rates, tighter financial conditions, and complex geopolitics add to uncertainty. We aim to maintain a portfolio that will provide positive returns against the uncertain backdrop. We remain cautious, with an underweight in weak credits (B rating), and overweight in selected BB credits with superior risk-reward characteristics. We are running an interest rate duration considerably shorter than the benchmark (4.7y vs 7.2y) but are evaluating the appropriate time to increase duration when value emerges.

BLUE DIAGONAL EM FIXED INCOME FUND (the “Fund”), an investment compartment of Blue Diagonal AIF V.C.I.C. Plc
 Blue Diagonal AIF V.C.I.C. Plc is authorised by CySEC (AIF17/2014)
The Fund is externally managed by Blue Diagonal Capital Limited, Cyprus

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