UBS House View

CIO Americas, WM

Weekly

15 October 2018

Week Ahead

- **Will US data unsettle markets?** Treasury yields have risen over the past month on the back of strong US economic data releases, and the increase contributed to last week's equity sell-off. This week, investors will need to digest the US JOLTS and industrial production reports, which could give further indications of whether the US economy is overheating.
- **Is easier monetary policy in China feeding through to growth?** The People's Bank of China (PBoC) has cut the reserve requirement ratio for banks by around 250bps year-to-date, yet worries of a Chinese slowdown have weighed on markets. This week's GDP, retail sales and fixed asset investment data should provide an indication of whether the PBoC's measures are having an impact yet.
- **Is a Brexit deal finally on the table?** Sterling continues to be buffeted by the twists and turns in the Brexit negotiations. With Prime Minister Theresa May refusing to agree to the EU's proposal, this week's EU summit could be a critical point in the attempt to reach a deal. We think the coming weeks are critical for the pound, as EU government heads have increased the pressure on the UK to improve the deal in their favor.

Investor spotlight

Leaving growth. Investors pulled USD 1.2bn from US tech stocks in the week to 10 October, the largest outflow since February, according to EPFR data.

Preferential treatment. Last week, investors poured USD 1.1bn into US equity funds, USD 0.9bn into Japanese equities, but withdrew USD 0.8bn from emerging markets.

For your information

- **For more key messages on the week ahead from Justin Waring, Investment Strategist Americas, click here.**
- We welcome your feedback: wmrfeedback@ubs.com

Key Messages

A bull market resetting, not ending.

All major US equity market indexes suffered a two-day slide of over 5% to 11 October, before recovering somewhat, with global stocks ending the week down 4.1%. A few factors contributed to the sell-off. First, the 10-year Treasury yield has risen as much as 40bps in the past six weeks, making stocks look relatively less attractive. Second, rising rates have fueled concerns that the US economy could slow down. Third, in the past few days companies exposed to trade with China have discussed the adverse impact of tariffs on their business. But what hasn't changed over the past week are solid US economic and earnings fundamentals. We expect 23–24% earnings growth in 3Q, while strong growth momentum should help the economy absorb higher rates. And for most sectors, the tariffs announced aren't that impactful yet.

Takeaway: Given the fundamental outlook, we remain overweight global equities. Periods of rising volatility and market pullbacks are likely to be more common as the cycle matures.

Treasuries still a portfolio stabilizer.

One bright spot in last week's sell-off was that 10-year US Treasury yields fell, too, by as much as 9bps on 10 October. That has helped alleviate some of the concerns about higher yields and demonstrates that Treasuries can still act as a portfolio stabilizer in times of market volatility. We maintain our overweight stance on 10-year US Treasuries, given our view that they have already largely priced in the Federal Reserve's current tightening cycle. Extreme speculative short positioning in 10-year Treasuries means there are fewer sellers remaining in the market. And in our view, US inflation is unlikely to materially overshoot the Fed's 2% target, providing no incentive for the Fed to accelerate the pace of monetary tightening, which reduces the chances of a significant further spike in yields.

Takeaway: We expect US Treasuries to perform well as the cycle matures. Investors worried about rising correlations between stocks and bond yields should look to alternatives such as hedge funds.

Climate change demands portfolio change.

With volatility increasing, filtering out the noise to focus on longer-term themes could be an attractive strategy. A UN report published last week sounded the alarm on climate change and added a new goal of a carbon-neutral global economy by 2050. While this won't be easy to achieve, we see several ways investors can contribute toward progress. Efforts to stem carbon emissions should accelerate the growth of companies involved in renewable energy output. The market share of renewables in global power generation needs to expand from about 20% today to more than 60% to meet the UN goal. Automobile electrification should increase, too, with a 35–65% target by 2050 for low-emission energy share in the broader transport sector (versus less than 5% now). And sustainable investing (SI) options such as green bonds can help contribute to the reduction of carbon emissions along with other positive goals, without sacrificing economic returns.

Takeaway: Through our multi-asset sustainable investing offering and our longer-term investment themes including Renewables and Smart mobility, investors can put their capital to work in ways that benefit both their finances and the environment.

UBS

Deeper Dive

Where we stand on the sell-off

Mark Haefele

President Donald Trump put the blame for last week's equity market slide firmly on the Federal Reserve, claiming the central bank was "going loco" by raising rates too far, too fast. The S&P 500 dropped 4.1% over the week, the Nasdaq fell 3.7% and the MSCI All Country World index by 4.1%.

Rising rates are just one of several reasons for the sell-off, but we think it's too early to suggest they mean the bull market is over:

- **Rising rates had made stocks relatively less attractive.** The 10-year Treasury yield had risen to 3.25%. But, in a similar fashion to February's equity correction, last week's stock market decline halted, and partly reversed, the rise in yields that helped precipitate it. Importantly, while we have seen US Treasury yields move higher in recent months, we think they can continue to act as a portfolio stabilizer during times of equity market volatility. Furthermore, weaker-than-expected inflation data should help calm concerns about US economic overheating.

- **The US administration's trade dispute with China is also a contributory factor.** US equity markets had been resilient to rising trade tensions compared to other markets. A few companies exposed to China have highlighted pockets of sluggish demand. In addition, some companies have warned that the latest round of US/China tariffs will have an impact on their operations. That said, with the 3Q earnings season getting underway, we still expect corporate America to indicate that the earnings growth outlook remains favorable – we expect 23-24% earnings growth, on 7-8% revenue growth, for the S&P 500.

- **The CFTC's Treasury market positioning data suggest China may have sold US Treasuries** ahead of the Trump administration's decision on whether to label the country a currency manipulator. This could have contributed to higher rate volatility and, in turn, higher equity volatility, prompting systematic accounts to reduce their exposure to stocks. However, CFTC data is noisy, so it is difficult to prove either way. And we see it as unlikely that China would resort to a policy of actively selling Treasuries to pressure the US administration, given the side-effects on its currency and domestic yields at a time when it is trying to add stimulus to the economy.

- **Technical selling appears to have amplified the move.** Thursday's sell-off, in the absence of any clear catalyst, suggests forced selling by funds that target specific levels of portfolio risk, reminiscent of market moves in February. While short-term fund flows are highly unpredictable, technical selling can often present opportunities for longer-term fundamental investors.

In a higher volatility environment, further downside can't be excluded. As we argued in our series of reports asking Are you prepared?, periods of rising volatility and market pullbacks are likely to become more common as the cycle matures, and this current bout may not yet have run its course.

But putting the decline into context, the S&P 500 has returned 5% this year, while earnings have grown by around 20%. Valuations have improved. The S&P 500 forward P/E multiple based on our 2019 earnings forecast is now 16.25x, down about a full point since the sell-off started. This is only slightly above the long-term average of 16.0x for the 12-month forward

Bottom line

President Donald Trump blamed the Fed for last week's equity slide. But rising yields were just one of several reasons behind the sell-off, which also included concerns about growth and the impact of tariffs, as well as technical selling. Further downside can't be excluded, but, against a backdrop of solid corporate earnings and better valuations, we don't think the bull market is over.

Deeper Dive

Where we stand on the sell-off

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P/E. Against this backdrop the extent of the sell-off appears unjustified by the fundamentals. We remain overweight global equities and recommend that investors consider using the move to rebalance allocations.

Bottom line

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Regional view - United States

The best lines of the night

Jeremy Zirin
CFA, Head of Equities Americas

Last week we hosted a discussion with members of the UBS Research Advisory Board (RAB) consisting of top thought leaders from around the financial services industry. We asked our RAB members three questions: what are the biggest risks today; what are the best investment opportunities; and what single piece of investment advice would you give.

It's difficult to overstate the power of great one liners. Go see a movie, a comedy act, or a Broadway show, and I'll bet the thing that will stick with you long after the event is that memorable quip, punchline, or metaphor. Much to the chagrin of my wife and kids, I'm still quoting lines from the movie Airplane! ("Surely, you can't be serious?...")

But my family should be grateful I'm quoting movies, when I could just as easily quote the famous one liners of great financial thinkers. One of the most impressive traits of Warren Buffet is his ability to take complex finance topics and boil them down into easily accessible allegories. How do you explain the risk of overleveraged companies in a booming expansion? Buffet responds, "You only find out who is swimming naked when the tide goes out." How do you think about finding stocks that are truly underpriced? "Price is what you pay; value is what you get."

Along these lines, I was fortunate enough to moderate a discussion with members of the UBS Research Advisory Board (RAB) this past week. The RAB is a group of thought leaders from firms across the industry that provides guidance into our CIO investment process and insights for UBS advisors and clients.

At the event, we were joined by several RAB members, including: Kristina Hooper (Invesco); Lyle Fitterer (Wells Capital Management); Joe Harvey (Cohen & Steers); Colin Moore (Columbia Threadneedle Investments); David Kelly (JP Morgan Asset Management); Kearney Posner (Lord Abbett); and John Tousley (Goldman Sachs Asset Management).

We asked three questions: (1) what are the biggest risks today; (2) what are the best investment opportunities; and (3) what single piece of investment advice would you give.

So let me share some of the "best lines of night."

Regarding risks, Kristina noted that "tariffs are like bacteria in a petri dish." A great framing of one of the biggest market risks, protectionism. Within fixed income, Lyle suggested that investors should upgrade credit quality in portfolios, because "when it turns (the credit cycle), it turns quickly." Finally, Joe also expressed concern about late cycle dynamics in the bond market, noting that "tightening cycles historically have created accidents." And he's right. It's no coincidence that both the late 1990s tech bubble and the financial crisis last decade occurred after an extended period of rate hikes the Fed.

Turning to opportunities, Colin sagely suggested that "it's worthwhile looking for secular trends." We often think of markets in terms of regions, size and sector, but secular growth opportunities in cloud computing, automation and robotics and e-commerce cut across traditional categories.

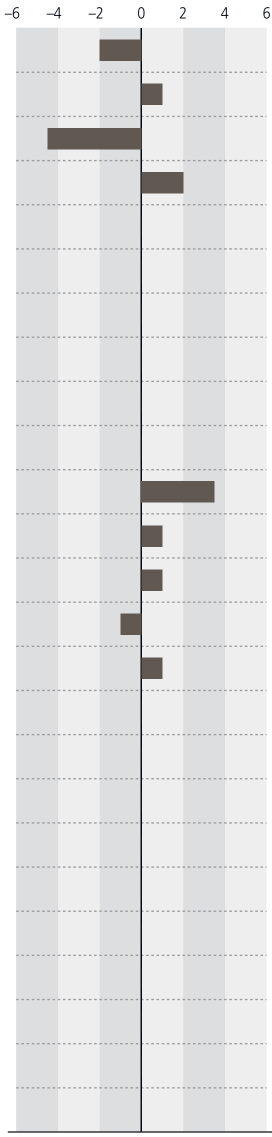
As for parting advice, David warmed up the evening with solar references by noting that investors should "make hay and fix the roof while the sun is shining." Interpretation? That investors should stay invested in stocks as the expansion continues (make hay), but consider preparing for the next downturn (fix the roof) by ensuring portfolios are properly diversified.

Kearney and John are new members to the RAB this year. Kearney reflected that "liquidity and yield are not costless" — a good reminder to always understand the risks of any investment. And with the midterm elections less than a month away, John told the audience that there is not any statistically significant relationship between the makeup of Congress and equity markets. Or, in other words, "express your political views with a vote, not a trade."

Those will be lines that I remember…"and don't call me Shirley."

Strategy and performance

TAA and market returns



Asset class	Tactical Deviation in %*	Total return in % 1–week	1–month	YTD	Annualized total return in % 1–Year	5–Year	10–Year**	Benchmark
Cash	**–2.0**	**0.04**	**0.17**	**1.38**	**1.61**	**0.59**	**0.45**	Barclays Capital US Treasury – Bills [1–3 M]
Fixed Income	**+1.0**							
US Gov't	–4.5	0.51	–0.74	–1.99	–1.98	1.29	2.65	BarCap US Agg Government
US Gov't 10 year	+2.0	0.80	–1.25	–4.32	–4.66	1.34	3.30	Bloomberg Barclays US Treasury Bellwethers 10 Year
US Municipal	0.0	–0.19	–1.03	–1.16	–0.72	3.43	4.65	BarCap Municipal Bond
US IG Corp	0.0	0.36	–0.66	–2.79	–2.00	3.20	5.84	BarCap US Agg Credit
US HY Corp	0.0	–0.46	–0.48	1.65	1.93	5.18	9.22	BarCap US Agg Corp HY
Int'l Developed Markets	0.0	0.75	–1.26	–3.43	–1.95	–0.41	1.96	BarCap Global Agg xUS
Emerging Markets	0.0	0.40	1.11	–4.76	–3.57	1.88	5.09	50% BarCap EM Gov and 50% BarCap Global EM (USD)
Emerging Markets Local Currency	0.0	0.70	1.48	–6.47	–4.42	–0.45	2.96	BarCap EM Gov
Emerging Markets Hard Currency	+3.5	0.09	0.74	–3.04	–2.72	4.20	7.22	BarCap Global EM (USD)
Equity	**+1.0**							
Global Equity	+1.0	–3.84	–3.80	–1.97	2.13	7.15	7.59	MSCI ACWI
US Large cap Growth	–1.0	–3.96	–5.05	9.80	16.32	14.89	13.83	Russell 1000 Growth
US Large cap Value	+1.0	–4.32	–3.90	–0.46	3.96	9.37	9.35	Russell 1000 Value
US Mid cap	0.0	–4.69	–7.06	0.27	4.99	9.88	11.80	Russell Mid Cap
US Small cap	0.0	–5.22	–9.72	1.69	4.06	8.82	10.70	Russell 2000
Int'l Developed Markets	0.0	–3.93	–3.45	–7.52	–4.70	2.98	4.60	MSCI EAFE
EM Equity	0.0	–2.03	–2.26	–13.61	–10.51	1.51	4.92	MSCI EMF
Commodities	**0.0**	**–0.72**	**3.50**	**–0.75**	**3.06**	**–7.03**	**N/A**	Blooomberg Commodity Index
Yield Assets	**0.0**							
Senior Loans	0.0	0.00	0.56	4.19	5.02	4.12	6.14	S&P/LSTA U.S. Leveraged Loan 100 Index
Preferreds	0.0	–0.38	–2.68	–1.92	–1.37	6.66	8.55	BofA Merrill Lynch Fixed Rate Preferred Securities Index
MLPs	0.0	–3.17	–4.21	4.41	2.74	–2.85	8.73	Alerian MLP Total Return
US Real Estate	0.0	–2.82	–7.38	–4.04	–4.28	7.29	7.28	FTSE NAREIT Equity REIT Index

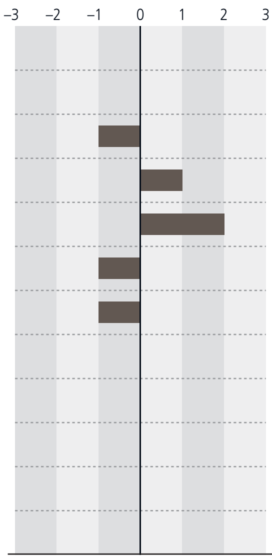
*The tactical deviation is for a moderate, non-taxable investor without alternative investments. See the latest *UBS House View: Investment Strategy Guide* for an interpretation of the tactical deviations and an explanation of the corresponding benchmark allocation.
**As of last month end
Source: UBS, as of 12 October 2018

S&P 500 forecast	**CIO GWM**
6-month rolling price target	USD 2950
2017 earnings per share actual	USD 133.0
2018 earnings per share estimate	USD 161.0
2019 earnings per share estimate	USD 168.0

Source: UBS, as of 12 October 2018

Strategy and performance

TAA and market returns: US equity sectors



Sector	Tactical Deviation	Total return in % 1–week	1–month	YTD	Annualized total return in % 1–Year	5–Year	10–Year**	Benchmark
Communication Services	0.0	–2.84	–3.90	–4.26	3.24	5.08	8.29	SPX Index
Consumer Discretionary	0.0	–3.52	–6.97	11.29	21.32	14.12	16.91	S5COND Index
Consumer Staples	–1.0	–1.92	–4.01	–6.04	–1.04	8.17	9.84	S5CONS Index
Energy	+1.0	–5.38	–0.39	3.58	10.22	0.27	3.29	S5ENRS Index
Financials	+2.0	–5.56	–5.32	–3.97	3.10	12.00	6.84	S5FINL Index
Health Care	–1.0	–3.45	–1.35	11.71	12.13	14.07	13.94	S5HLTH Index
Industrials	–1.0	–6.40	–5.04	–1.12	3.25	11.30	11.46	S5INDU Index
Information Technology	0.0	–3.82	–4.07	13.46	20.84	20.61	16.56	S5INFT Index
Materials	0.0	–6.58	–8.81	–9.60	–5.44	6.92	7.82	S5MATR Index
Real Estate	0.0	–2.88	–7.46	–3.93	–2.90	5.93	4.53	S5RLST Index
S&P 500		–4.07	–4.07	5.06	10.57	12.46	11.51	S5TELS Index
Utilities	0.0	–1.26	–1.32	3.30	0.66	10.72	8.62	S5UTIL Index

Note: Tactical deviations are intended to be applicable to the US equity portion of a portfolio across investor risk profiles.
**As of last month end
Source: UBS, as of 12 October 2018

Market moves

	Level	*1–w chg*	*YTD chg*
S&P 500	2,767	–4.07%	5.06%
DJIA	25,340	–4.17%	4.29%
Nasdaq	7,497	–3.74%	9.50%
Nikkei 225	22,695	–4.58%	1.32%
Eurostoxx 50	3,194	–4.46%	–5.93%
MSCI EM*	980	–2.02%	–13.43%
MSCI World*	2,063	–4.05%	0.11%
MSCI EAFE*	1,851	–3.93%	–7.10%
DXY	95	–0.42%	3.36%
Gold	$ 1217/oz	1.11%	–6.58%
Brent crude oil	$ 80.4/bbl	–4.43%	20.28%
US 10–year yield	3.16%	–7 bps	+76 bps
VIX	21.3	+6.5 pts	+10.3 pts

Source: Bloomberg, as of 12 October 2018
Note: All returns are in local currency
* As of intraday 11 October 2018

Tactical time horizon is approximately six months.
Total return market performance is from Bloomberg as of close of business on source date, using representative indices, and is provided for information only. Past performance is no indication of future performance.

+ – Indicates +/– change

Terms and abbreviations
YTD = year-to-date.
TAA = tactical asset allocation.

Earnings calendar

The Earnings Calendar provides publicly announced reporting dates and times of companies covered by Chief Investment Office GWM. Reporting dates and times are subject to change by the reporting companies.

Date	Company	Ticker	Company	Ticker	Company	Ticker
15-Oct-2018	The Charles Schwab Corp.	SCHW	Bank of America Corp.	BAC		
16-Oct-2018	Lam Research Corp.	LRCX	Prologis, Inc.	PLD	Comerica, Inc.	CMA
16-Oct-2018	BlackRock, Inc.	BLK	Morgan Stanley	MS	The Goldman Sachs Group, Inc.	GS
16-Oct-2018	CSX Corp.	CSX	International Business Machines Corp.	IBM		
17-Oct-2018	Kinder Morgan, Inc.	KMI	Northern Trust Corp.	NTRS	Steel Dynamics, Inc.	STLD
17-Oct-2018	Alcoa Corp.	AA				
18-Oct-2018	The Bank of New York Mellon Corp.	BK	KeyCorp	KEY	Philip Morris International, Inc.	PM
18-Oct-2018	American Express Co.	AXP	Celanese Corp.	CE	Citizens Financial Group, Inc. (Rhode Island)	CFG
19-Oct-2018	SunTrust Banks, Inc.	STI	Honeywell International, Inc.	HON	Synchrony Financial	SYF
19-Oct-2018	VF Corp.	VFC	Procter & Gamble Co.	PG	Schlumberger NV	SLB
19-Oct-2018	State Street Corp.	STT				

Source: FactSet, UBS, as of 12 October 2018

Key economic indicators

Date	Indicator	Period	Time (ET)	Unit	Consensus	Previous
15-Oct-18	Empire State Manufacturing Survey	Oct	08:30 AM	level	20.5	19.0
15-Oct-18	Retail Sales	Sep	08:30 AM	m/m	0.7%	0.1%
15-Oct-18	Retail Sales less autos and gas	Sep	08:30 AM	m/m	0.4%	0.2%
15-Oct-18	Retail Sales Control Group	Sep	08:30 AM	m/m	0.4%	0.1%
15-Oct-18	Business Inventories	Aug	10:00 AM	m/m	0.5%	0.6%
16-Oct-18	Industrial Production	Sep	09:15 AM	m/m	0.3%	0.4%
16-Oct-18	Capacity Utilization Rate	Sep	09:15 AM	level	78.2%	78.1%
16-Oct-18	Manufacturing Production	Sep	09:15 AM	m/m	0.3%	0.2%
17-Oct-18	Housing Starts	Sep	08:30 AM	level	–5.0%	9.2%
17-Oct-18	Housing Permits	Sep	08:30 AM	level	2.5%	–5.7%
18-Oct-18	Philadelphia Fed Business Outlook	Oct	08:30 AM	level	21.0	22.9
18-Oct-18	Leading Indicators	Sep	10:00 AM	m/m	0.5%	0.4%
19-Oct-18	Existing Home Sales	Sep	10:00 AM	m/m	–0.6%	0.0%

Source: Bloomberg, UBS, as of 12 October 2018
UBS forecast estimates are published on Friday evenings in *Economic Perspectives* by economists employed by UBS Investment Research, a part of UBS Investment Bank.
m/m = month–over–month. q/q = quarter–over–quarter. y/y = year–over–year. k = thousand. mn = million. bn = billion.

ESG/Sustainable Investing Considerations: Sustainable investing strategies aim to consider and in some instances integrate the analysis of environmental, social and governance (ESG) factors into the investment process and portfolio. Strategies across geographies and styles approach ESG analysis and incorporate the findings in a variety of ways. Incorporating ESG factors or Sustainable Investing considerations may inhibit the portfolio manager's ability to participate in certain investment opportunities that otherwise would be consistent with its investment objective and other principal investment strategies. The returns on a portfolio consisting primarily of ESG or sustainable investments may be lower or higher than a portfolio where such factors are not considered by the portfolio manager. Because sustainability criteria can exclude some investments, investors may not be able to take advantage of the same opportunities or market trends as investors that do not use such criteria. Companies may not necessarily meet high performance standards on all aspects of ESG or sustainable investing issues; there is also no guarantee that any company will meet expectations in connection with corporate responsibility, sustainability, and/or impact performance.

Non-Traditional Assets

Non-traditional asset classes are alternative investments that include hedge funds, private equity, real estate, and managed futures (collectively, alternative investments). Interests of alternative investment funds are sold only to qualified investors, and only by means of offering documents that include information about the risks, performance and expenses of alternative investment funds, and which clients are urged to read carefully before subscribing and retain. An investment in an alternative investment fund is speculative and involves significant risks. Specifically, these investments (1) are not mutual funds and are not subject to the same regulatory requirements as mutual funds; (2) may have performance that is volatile, and investors may lose all or a substantial amount of their investment; (3) may engage in leverage and other speculative investment practices that may increase the risk of investment loss; (4) are long-term, illiquid investments, there is generally no secondary market for the interests of a fund, and none is expected to develop; (5) interests of alternative investment funds typically will be illiquid and subject to restrictions on transfer; (6) may not be required to provide periodic pricing or valuation information to investors; (7) generally involve complex tax strategies and there may be delays in distributing tax information to investors; (8) are subject to high fees, including management fees and other fees and expenses, all of which will reduce profits.

Interests in alternative investment funds are not deposits or obligations of, or guaranteed or endorsed by, any bank or other insured depository institution, and are not federally insured by the Federal Deposit Insurance Corporation, the Federal Reserve Board, or any other governmental agency. Prospective investors should understand these risks and have the financial ability and willingness to accept them for an extended period of time before making an investment in an alternative investment fund and should consider an alternative investment fund as a supplement to an overall investment program.

In addition to the risks that apply to alternative investments generally, the following are additional risks related to an investment in these strategies:

- Hedge Fund Risk: There are risks specifically associated with investing in hedge funds, which may include risks associated with investing in short sales, options, small-cap stocks, “junk bonds,” derivatives, distressed securities, non-U.S. securities and illiquid investments.
- Managed Futures: There are risks specifically associated with investing in managed futures programs. For example, not all managers focus on all strategies at all times, and managed futures strategies may have material directional elements.
- Real Estate: There are risks specifically associated with investing in real estate products and real estate investment trusts. They involve risks associated with debt, adverse changes in general economic or local market conditions, changes in governmental, tax, real estate and zoning laws or regulations, risks associated with capital calls and, for some real estate products, the risks associated with the ability to qualify for favorable treatment under the federal tax laws.
- Private Equity: There are risks specifically associated with investing in private equity. Capital calls can be made on short notice, and the failure to meet capital calls can result in significant adverse consequences including, but not limited to, a total loss of investment.
- Foreign Exchange/Currency Risk: Investors in securities of issuers located outside of the United States should be aware that even for securities denominated in U.S. dollars, changes in the exchange rate between the U.S. dollar and the issuer’s “home” currency can have unexpected effects on the market value and liquidity of those securities. Those securities may also be affected by other risks (such as political, economic or regulatory changes) that may not be readily known to a U.S. investor.

Emerging Market Investments

Investors should be aware that Emerging Market assets are subject to, amongst others, potential risks linked to currency volatility, abrupt changes in the cost of capital and the economic growth outlook, as well as regulatory and socio-political risk, interest rate risk and higher credit risk. Assets can sometimes be very illiquid and liquidity conditions can abruptly worsen. CIO GWM generally recommends only those securities it believes have been registered under Federal U.S. registration rules (Section 12 of the Securities Exchange Act of 1934) and individual State registration rules (commonly known as "Blue Sky" laws). Prospective investors should be aware that to the extent permitted under US law, CIO GWM may from time to time recommend bonds that are not registered under US or State securities laws. These bonds may be issued in jurisdictions where the level of required disclosures to be made by issuers is not as frequent or complete as that required by US laws.

For more background on emerging markets generally, see the CIO GWM Education Notes, *Emerging Market Bonds: Understanding Emerging Market Bonds*, 12 August 2009 and *Emerging Markets Bonds: Understanding Sovereign Risk*, 17 December 2009.

Investors interested in holding bonds for a longer period are advised to select the bonds of those sovereigns with the highest credit ratings (in the investment grade band). Such an approach should decrease the risk that an investor could end up holding bonds on which the sovereign has defaulted. Sub-investment grade bonds are recommended only for clients with a higher risk tolerance and who seek to hold higher yielding bonds for shorter periods only.

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