

<https://blog.en.erste-am.com/do-eastern-european-bonds-offer-opportunities/>

## Do Eastern European bonds offer opportunities?

Anton Hauser



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The war in Ukraine is taxing for the nerves of bond investors. A particular focus is currently on government bonds from Central and Eastern Europe. After all, Russia has been punished with grave sanctions that brought trading to a standstill. But there is a silver lining, as Anton Hauser, fund manager of [ERSTE BOND DANUBIA](#) – a fund that focuses on East European government bonds – explains in an interview with OUR VIEW.

***Bonds from states in and around the crisis region have seen better days. What effects have the sanctions had?***

Of course, these bonds incurred losses, and Russian bonds suffered the most. Hard currency bonds had a default priced in, and the rouble depreciated dramatically. Trading in local currency bonds was suspended. When trading is resumed this week, we should get a clearer picture about the price development in these segments. Currencies and bonds in the other CEE countries have recovered some of the original, in some cases drastic losses.

***Russia has defied expectations by honouring its coupon payment on 16 March, not without a lot of issues though. What can we expect for the upcoming payments?***

Yes, it has been a bit messy over the past few days. At first, Russia said it wanted to honour its debt, but only in rouble if it deemed a country hostile. Then it decided to pay in US dollar after all. But it was not clear whether the payments would be successful. In the end, the investors received their payments with a slight delay. Not too bad, then.

***Does Russia still play a role in the portfolio of [ERSTE BOND DANUBIA](#)?***

We envisage a default, which is why the bonds in the portfolio are valued in single digit percentages. As of the end of February, Russian bonds accounted for only 9% of fund assets. We also have to accept that due to the EU capital market sanctions, trading is currently in some cases not possible.

The interesting question is whether Russia will continue to service its debt in US dollar. Numerous coupon payments are scheduled until the end of March, and on 2 April, a USD 2bn bond falls due. In some of these cases, the Russian state has the legally stipulated right to pay in rouble, which should at the very least push back a possible default.

***What alternatives do you have in your allocation? After all, Eastern Europe is the “growth region at our doorstep”?***

After the reduction of Russian bonds, the focus of the fund is now increasingly on Eastern and South-Eastern Europe. Bonds and currencies from those regions came under pressure as well. Given the economic perspectives of these countries and the weak economic ties with Russia, the losses are only partially justified. The catch-up potential of Eastern and South-Eastern Europe is still enormous. The people are industrious and want to create something for themselves. You only have to look at the development of countries like Slovenia, Hungary, the Czech Republic, or Slovakia in the past three decades. They have caught up enormously in terms of economic output and standard of living.

„After the reduction of Russian bonds, the focus of the fund is now increasingly on Eastern and South-Eastern Europe.“

Anton Hauser, Senior Fund Manager, Erste AM

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***What are the arguments in favour of East European government bonds?***

The average creditworthiness of the countries is solid, the government debt is low in comparison with the Eurozone or USA. At about 5Y, the maturities of bonds in local currency are on average shorter than for Euroland government bonds. This is a good card to hold in times of rising interest rates. In the Czech republic, for example, the average yield is 3.5%; in Poland, 4.5%; in Romania, about 6% (Bloomberg, as of 18 March 2022). These yield levels should be able to compensate for the prevalent level of inflation.

## **▲ Risk notes according to 2011 Austrian Investment Fund Act**

In accordance with the fund provisions approved by the Austrian Financial Market Authority (FMA), ERSTE BOND DANUBIA intends to invest more than 35% of its assets in securities and/or money market instruments of public issuers. A detailed list of these issuers can be found in the prospectus, para. II, point 12.

The fund employs an active investment policy and is not oriented towards a benchmark. The assets are selected on a discretionary basis and the scope of discretion of the management company is not limited.

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### **Anton Hauser**

Anton Hauser is senior fund manager for government bonds and foreign exchange markets at Erste Asset Management with more than 20 years of expertise. He specializes in local currency bonds from emerging markets with a focus on Central and Eastern Europe and manages, among others, ERSTE BOND DANUBIA.