Stone Harbor
INVESTMENT PARTNERS

Investment Policy Statement

A monthly review of the markets

The Looming Transition to Vaccine Abundance for the Developed World

"Of all cooperative enterprises, public health is the most important and gives the greatest returns."

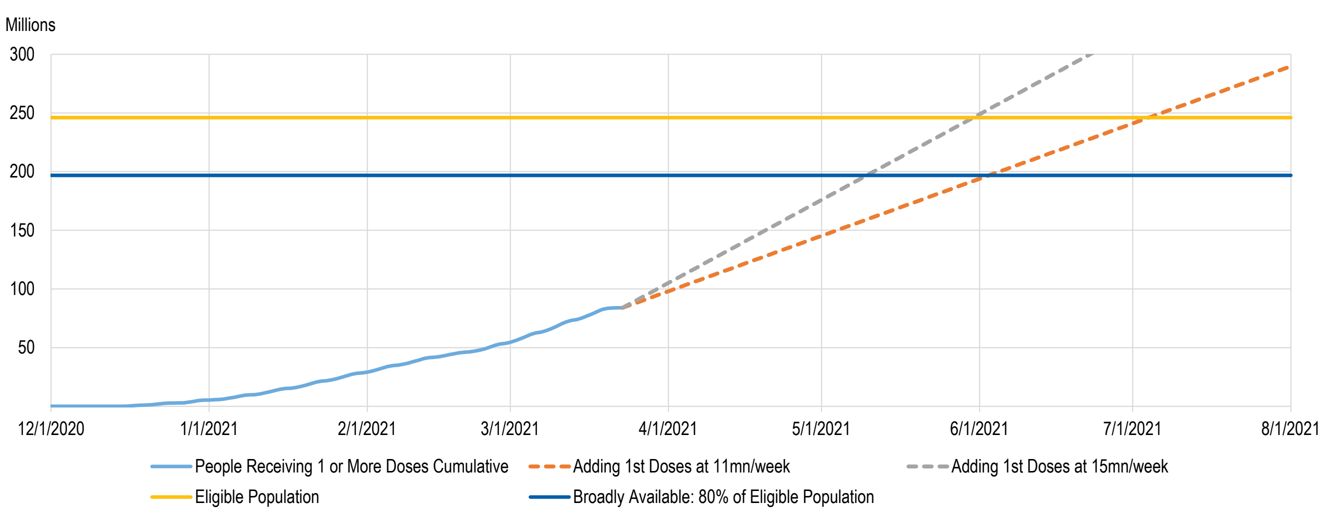
– William J. Mayo, physician, surgeon, and a founder of the Mayo Clinic

The developed world is undergoing a rapid transition from vaccine scarcity to vaccine abundance. After over a year of pandemic-related restrictions seriously constraining economic activity, vaccine supply increases look poised to rapidly transition us to a world where people can quickly and easily get vaccinated. Once that happens, we think that economic activity will resume rapidly. The timing will vary across countries and regions, but we expect much better outturns by the fall, at least for developed markets. Emerging markets (EM) will lag, but the younger age distributions of their population will likely allow substantial activity to resume before full vaccination.

By the late spring, we expect vaccines to be abundant in the US. What do we mean by abundant? That anyone can, without meaningful advance planning, walk in and get a vaccine dose—a marked contrast to the last several months. Currently there are about 250 million US residents over age 16 and presumably vaccine eligible. With vaccine hesitancy, and some at very low risk who will not prioritize getting vaccinated, our rough estimate is that vaccines will hit that "walk in and get it" point when 80% of the population has been vaccinated. Why late spring then? As is detailed in Figure 1, our expectation stems from the rapid ramp up in vaccine capacity we have seen over the last several months. The most recently announced schedule from the CDC had about 11 million first doses scheduled for delivery the week of 29 March. If vaccine deliveries proceeded at that pace we'd get to the 80% by early June. We think it likely that the US achieves an even faster pace with (1) continued manufacturing progress, (2) the potential for additional approvals, and (3) fewer second doses are needed with people already vaccinated. With a 15 million per week pace we would get to 80% by early May.

At that point, regardless of guidance, we think it likely that many people will move toward resuming more economic activity. Moreover, in the last several weeks state and local governments have started to reduce restrictions. Without taking a stance on whether or not that is too early, we only expect the process to accelerate as more widespread vaccinations drives down case growth, hospitalizations, and deaths further.

Figure 1: Toward A Vaccine Abundant World



As of March 2021
Source: Centers for Disease Control and Prevention (CDC), United States Census Bureau (USCB), and Stone Harbor Investment Partners Calculations

Vaccination abundance for the US implies positive developments for most other developed markets. The UK will, like the US, likely be vaccine abundant by then as they continue to rollout vaccines at a pace broadly similar to the US. After vaccines saturate these markets, the production capacity, likely still expanding, will remain in place and be available to be directed elsewhere.

At this point, it appears that the next destinations for vaccines are other developed markets, most specifically Europe and Canada. Europe has certainly lagged substantially in securing vaccines and using those they have while Canada appears to be more challenged simply by scarcity. In Europe, we think procuring vaccines is the more pressing issue and that becomes much less pressing with the increased supply being turned toward them. The US rollout was underwhelming back in January and February, and it was only through "learning by doing" that we saw the pace accelerate - we expect a similar process in Europe. Though issues of vaccine hesitancy remain, we think the lure of much more normal life, with the US, UK and Israel as examples, will push the populace toward inoculations. So by mid to late summer we think they follow the US toward abundance.

In Japan, vaccinations are progressing but remain well behind other developed countries as only 0.55% of the population have been inoculated with at least one dose of vaccine. Similar to Japan, Australian vaccinations have lagged other developed countries with only 1.3% of the population having received at least one dose. The slow rollout had been partially attributed to production setbacks in AstraZeneca's European facilities; however, the approval of 800,000 locally manufactured doses should assist with Australia's vaccination efforts.

In EMs, vaccination activity is clearly lagging the US and will take more time to reach a comparable vaccine abundant state. That said, the situation is improving in EMs, and we expect this to continue with greater vaccine ability and as some capacity is directed toward them. Some EM countries are already doing quite well and have achieved high vaccination rates including the United Arab Emirates, Bahrain, Chile, Serbia, and Hungary, while others are catching up fast including Uruguay, Qatar, and Singapore. Vaccine diplomacy is being instituted as China, and to a lesser extent, Russia, are supplying vaccines to various other EM countries. We expect such good will to proliferate when vaccine abundant countries (including the US) may share supply with countries that are lacking, but we don't see this happening until the 2nd half of 2021.

Several EM countries are currently experiencing another wave of infections, driven by faster spreading variants, including the CEE countries, Brazil, Uruguay, and Turkey. We do, however, expect substantial improvements by late spring and into summer as a growing share of the vulnerable population will have been vaccinated and COVID waves have so far tended to abate after 2-3 months.

In our view, the vaccination abundance in the developed world has started flowing through to the economic data. Regional services PMIs in the US have picked up significantly in March and the most recent claims data showed a notable move down. In our scenarios, the move toward vaccine abundance shows up by us placing significantly more weight on our "Medical & Stimulus Led Acceleration" scenario. We marked our probability up from 10% to 35%, and it's currently only marginally less likely than our base case.

US MACRO RISK SCENARIO ASSUMPTIONS AND MARKET OUTLOOK[1]

Base Case: Slow Grind Transitions to Sharp Vaccine-Led Rebound (45%)

- Vaccine distribution acceleration continues; vaccines provide at least partial protection against variants.
- Travel, restaurants, sports, conventions and large gatherings improve with wider vaccination.
- European countries keep containment measures in place over short-term hurting activity. Near-term shortfalls made up for by more rapid future growth.
- Substantial stimulus passes through reconciliation, which meaningfully boosts growth. Other countries continue to provide further fiscal support.
- US/China tensions cool with Biden administration, but do not return to pre-Trump status quo.
- Core inflation picks up sharply—to over 2½%—in Q2-2021 as year-over-year measures lap the declines from 2020. The Fed and other DM central banks look through and core inflation drops back below 2% by mid-summer.
- Central banks maintain extremely stimulatory policies.
- Oil remains roughly stable: ~$60/barrel WTI, Brent ~$65.
- Dollar broadly weakens, partly due to closing of interest rate differentials and partly from lower US real rates associated with Fed policy shift.

Medical & Stimulus Led Acceleration (35%)

- Pharmaceutical progress exceeds expectations. Additional vaccines approved and get to the populace quickly. At the same time, the use of monoclonal antibodies increases which helps push death rates down.
- US and European economies prove resilient to containment measures. Asia remains in relatively good shape.
- With better-than-expected outturns on containment, treatment and vaccination, activity improves substantially by the spring.
- The Democratic Senate passes a substantial stimulus package and moves on to infrastructure. The combination further accelerates the recovery.
- Supportive monetary policies gain traction.
- Improvement is global as better treatments spread.
- Fed maintains accommodative policy, but doesn't feel need to push further. Similarly ECB only maintains PEPP.
- Oil: WTI at ~$70/barrel; Brent ~$75/barrel.

Variants Derail Vaccine-Led Recovery (10%)

- Coronavirus variants prove resistant to current vaccines; the new strains spread rapidly. As a result the recovery lags as social distancing and government restrictions remain in place. The 2021 recovery disappoints meaningfully and economic scars turn lasting.
- The scars come from a variety of lingering effects: 1/ business bankruptcies increase; 2/ risk taking sentiment is depressed leading to less investment and fewer new business formations; 3/ layoffs turn permanent and unemployment rates elevated in many countries and 4/ elevated sovereign balance sheets lead to payment stress in some countries.
- Malaise not limited to the US: other DMs and most EMs underperform expectations through 2021.
- Fed institutes yield curve control (YCC) and pegs 10y at 0.25%. Additional financing facilities put in place; Fed pushes further out risk spectrum.
- Trade tensions persist, as in the base case.
- Dollar sees renewed flight to safety support.
- Oil prices hit by lower growth: ~$35-30/barrel for WTI; Brent ~$30-35.

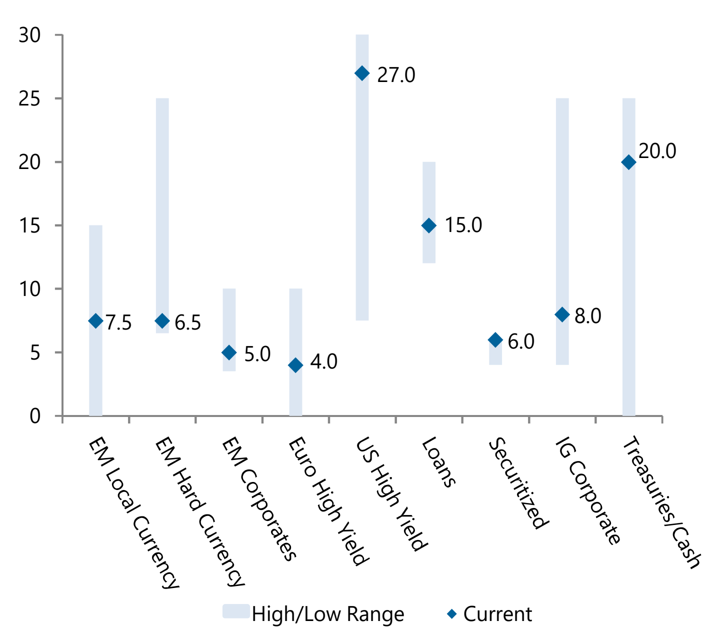
Inflation Accelerates (10%)

- Next several months proceed as in the base case, but inflation does not come back down in the summer.
- Stimulus induced demand crashes into still constrained supply, and firms respond by raising prices. Firms start to materially bid up wages attempting to pull workers in.
- Core inflation remains well over 2%, and is around 2½% heading into the end of 2021 for the US, and similarly higher in other DMs.
- Despite the rise in inflation, central banks initially maintain accommodative policies. Toward the end of the year they being to react pulling back on asset purchases and indicating that rates are likely to rise much sooner than anticipated.
- Rates move sharply higher along the curve.
- Interest rate sensitive sectors start to drag, but that is offset in the broader economy by growth elsewhere.
- Oil prices rise notably with growth and inflation fears: WTI to $70/barrel, Brent $75/barrel.

	Base Case: Slow Grind Transitions to Sharp Vaccine-Led Rebound (45%)	Medical & Stimulus Led Acceleration (35%)	Variants Derail Vaccine-Led Recovery (10%)	Inflation Accelerates (10%)
US Real 4Q GDP (%)	6.50	8.00	3.00	6.50
Fed Funds (%)	0.13	0.13	0.13	0.13
US Core PCE (%)	1.70	1.90	1.10	2.60
2yr Treasury (%)	0.40	0.60	0.13	1.00
10yr Treasury (%)	1.75	2.25	0.25	2.50
10yr Bund (%)	-0.35	0.10	-0.75	0.75
China 4Q GDP (%)	5.25	5.50	4.50	5.25
EM 4Q GDP (%)	5.50	6.50	3.50	5.00

[1]Forecast Period: Next 12 months. Source: Stone Harbor.

MULTI-ASSET CREDIT TARGET ALLOCATIONS (%) SINCE INCEPTION & RECENT ALLOCATION CHANGES[2]



Latest Allocation Changes		
	Month	Change (%)
EM Local Currency	Dec-Jan 2021	+2.5
EM Hard Currency	Jan-Feb 2021	+1.0
EM Corporates	May-June 2018	+1.5
Euro High Yield	May-June 2020	-2.5
US High Yield	Jan-Feb 2021	-0.5
Loans	Jan-Feb 2021	+1.5
Securitized	Mar-April 2019	+1.0
IG Corporate	Jan-Feb 2021	+2.5
Treasuries/Cash	Jan-Feb 2021	-4.5

[2]Since Inception: September 2013. Stone Harbor Multi-Asset Credit Representative Target Allocation as of 28 February 2021. Actual allocations within any account may be significantly different from the target allocations shown here. For illustrative purposes only.

FEBRUARY CREDIT MARKET TOTAL RETURNS & ATTRIBUTION

	US High Yield	EM Hard	Loans	EM Local	EM Corp	Euro High Yield	IG Corporate
Total Return	0.34	-2.55	0.59	-2.68	-0.10	0.54	-1.45
Duration (Returns from Interest Rates %)	-1.03	-2.58	-0.14	-1.62	-1.29	-0.64	-2.25
Credit Beta (Returns from Spreads %)	1.37	0.03	0.73	-1.06	1.19	1.18	0.80

Month Ended 28 February 2021. Performance reflects representative asset class benchmarks.HY: ICE BofAML US High Yield Constrained Index; EMD: J.P. Morgan EMBI Global Diversified; EMDLC: J.P. Morgan GBI-EM Global Diversified; EMDCR: J.P. Morgan Corporate Emerging Markets Bond Index Broad Diversified; EUR HY: ICE BofAML European Currency High Yield 2% Constrained Ex Financial; IG Corp: Bloomberg Barclays Global Agg Corporate Index; Loans: S&P/LSTA Leveraged Loan Index; Past performance is not a guarantee of future results. Returns are shown gross of fees. For illustrative purposes only.

STONE HARBOR INVESTMENT PARTNERS

- Institutional fixed income investment firm focused on credit risk strategies and asset allocation.
- 100% employee-owned
- Over 30-year performance history
- Offices in New York, Chicago, London, and Singapore.

Stone Harbor Investment Partners LP manages institutional clients' assets across a range of investment products including multi-sector credit, emerging markets debt, core fixed income, securitized, high yield, and bank loan strategies. Across all strategies, we seek to generate attractive risk-adjusted returns through a disciplined process of fundamental credit analysis complemented by solid portfolio management skills and sound risk management. Experience, teamwork and dedicated client service - the cornerstones of our success - help us achieve sustainable results.

Indices referred to herein are broad-based securities market indices. Broad-based securities indices are unmanaged and are not subject to fees and expenses typically associated with managed accounts or investment funds. Investments cannot be made directly in an index.

Index Definitions

The J.P. Morgan CEMBI Broad Diversified (CEMBI Broad Diversified) tracks total returns of U.S. dollar-denominated debt instruments issued by corporate entities in emerging market countries and consists of an investable universe of corporate bonds. The minimum amount outstanding required is $350 mm for the CEMBI Broad Diversified. The CEMBI Broad Diversified limits the weights of those index countries with larger corporate debt stocks by only including a specified portion of these countries' eligible current face amounts of debt outstanding.

The J.P. Morgan EMBI Global Diversified (EMBI Global Diversified) limits the weights of those index countries with larger debt stocks by only including specified portions of these countries' eligible current face amounts outstanding. The countries covered in the EMBI Global Diversified are identical to those covered by the EMBI Global.

The J.P. Morgan GBI-EM Global Diversified (GBI EM Global Diversified) consists of regularly traded, liquid fixed-rate, domestic currency government bonds to which international investors can gain exposure. The weightings among the countries are more evenly distributed within this index.

The ICE BofAML European Currency Non-Financial High Yield 2% Constrained Index contains all non-Financial securities in The ICE BofAML European Currency High Yield Index but caps issuer exposure at 2%. Index constituents are capitalization-weighted, based on their current amount outstanding, provided the total allocation to an individual issuer does not exceed 2%. Issuers that exceed the limit are reduced to 2% and the face value of each of their bonds is adjusted on a pro-rata basis. Similarly, the face values of bonds of all other issuers that fall below the 2% cap are increased on a pro-rata basis.

The ICE BofAML U.S. High Yield Constrained Index (HUC0) contains all securities in ICE BofAML U.S. High Yield Index but caps issuer exposure at 2%. Index constituents are capitalization-weighted, based on their current amount outstanding, provided the total allocation to an individual issuer does not exceed 2%. Issuers that exceed the limit are reduced to 2% and the face value of each of their bonds is adjusted on a pro-rata basis. Similarly, the face values of bonds of all other issuers that fall below the 2% cap are increased on a pro-rata basis. In the event there are fewer than 50 issues in the Index, each is equally weighted and the face values of their respective bonds are increased or decreased on a pro-rata basis.

The S&P/LSTA Leveraged Loan Index is a partnership between Standard & Poor's and the Loan Syndications and Trading Association, tracking returns in the leveraged loan market and capturing a broad cross-section of the U.S. leveraged loan market - including dollar-denominated, U.S.-syndicated loans to overseas issuers.

The Bloomberg Barclays US Aggregate Index is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States

The Bloomberg Barclays Global Aggregate Bond Index provides a broad-based measure of the global investment grade fixed-rate debt markets. It is comprised of the U.S. Aggregate, PanEuropean Aggregate, and the Asian-Pacific Aggregate Indexes. It also includes a wide range of standard and customized subindices by liquidity constraint, sector, quality and maturity.

Important Disclosures

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