March 2022

Stone Harbor
INVESTMENT PARTNERS

Investment Policy Statement

A monthly review of the markets

Investment Implications of the Russia-Ukraine War

"There never was a good war or a bad peace."

– Benjamin Franklin, American politician

More than a month after the launch of the Russian invasion of Ukraine, economic and geopolitical uncertainties remain high. A quick Russian military victory did not materialize in light of the fierce Ukrainian resistance and growing arms supplies from Western countries. On the other hand, a full Russian withdrawal also seems unlikely given Vladimir Putin's defiant reaction to sanctions, military escalation, including shelling and bombing of civilians, and lack of serious negotiations. Although talks of a ceasefire are underway, as of this writing, a near-term definitive resolution of the tensions appears unlikely.

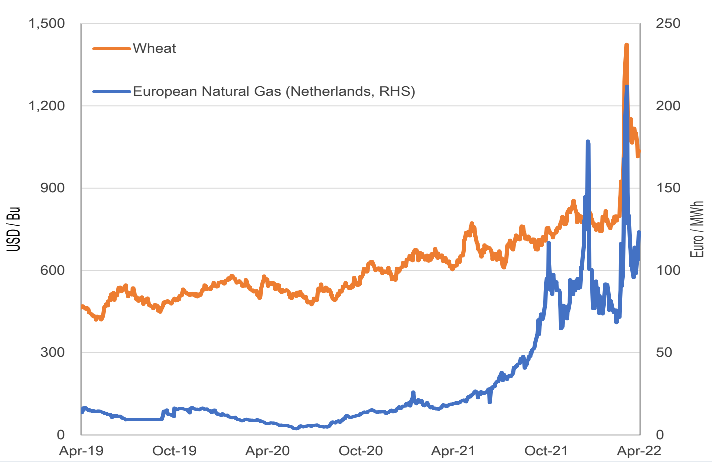
In this context, Western sanctions imposed on Russia carry profound implications for the global investment outlook – both in the near term as well as in the long run. The most acute and immediate economic impact from the sanctions has been evident in rising commodity prices that stand to further weaken the global growth outlook, with some exceptions including select commodity exporters in emerging markets (EM) and with varying degree of impact in developed markets. But beyond the near-term, we see longer-term efforts to realign supply chains to guard against geopolitical shocks that could potentially benefit select EM countries.

The immediate impact reverberating globally is surging commodity prices across products (e.g., energy, agricultural, metals), further exacerbating the already substantial global inflationary impulse. The global growth outlook has weakened due to higher commodity prices, tighter monetary policy, and existing and potentially more supply chain disruptions. From an investment standpoint, Russian assets — both local debt and equities — have either become uninvestable/untradable for international investors, or trade at deeply distressed prices, in the case of hard currency debt. Major EM indices have already eliminated Russian assets. A reversal is highly unlikely in the foreseeable future.

Extending beyond the near-term impact, we see longer-term implications from efforts to reduce economic vulnerabilities. This is clearly evident in European energy policy that is moving away from Russian energy, but we also expect to see a broader move to make supply chains more resilient and less exposed to potential future

Select Commodities

3/31/2019 = 100



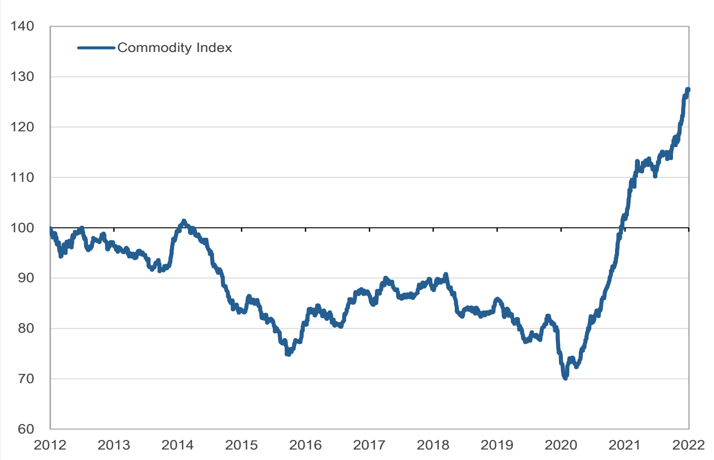
As of As of 31 March 2022

Sources: Bloomberg, CRB, Stone Harbor Investment Partners

Past performance is not a guarantee of future results. For illustrative purposes only

CRB Commodity Index

3/31/2012 = 100



As of As of 31 March 2022

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geopolitical conflicts. We do not believe this will result in a broad de-globalization of the global economy; the economic gains from trade are (and will remain) too large. However, the focus is shifting to reducing exposure to potentially unreliable partners and to diversifying supply chains.

For EMs, the immediate impact has been manifested through higher commodity prices, higher inflation, and in some cases, higher core rates. Importantly, there are select countries that benefit from this environment — namely, commodity exporters such as South Africa, Angola, Brazil, Peru, Ecuador, and Indonesia. In contrast, commodity importers, including Turkey, Tunisia, Sri Lanka, Lebanon, or Egypt are negatively impacted. Many EMs had already been very pro-active regarding rate hikes to deal with the global inflation spike. Now, some vulnerable EM countries, such as Egypt, have already approached the International Monetary Fund for support and have allowed their currency to adjust.

Over the long term, we believe various EMs have the potential to benefit from efforts of Western democracies to diversify supply chains. In the energy sector, this means increasing use of liquefied natural gas (LNG) and efforts to source it outside of the Middle East. Beneficiaries could be countries like Mozambique with large LNG projects currently in development, but also potential smaller producers, such as Papua New Guinea. In the tech sector, the key vulnerability is high reliance on a few Asia producers, such as China and Taiwan. The vulnerability of semiconductor supply chains has already been exposed during the pandemic. As a result, we expect to see increased efforts to diversify production. Potential beneficiaries in this area include Mexico, some European economies, as well as countries in South-East Asia. On the flip side, countries that we believe could be negatively impacted by the process of diversifying supply chains include China, Taiwan, and the Middle East.

The impact of higher commodity prices across developed markets (DM) varies considerably, with Europe highly exposed, DM Asia moderately exposed, and the US/Canada least exposed, in our view. Europe's exposure is twofold: both through non-trivial direct trade linkages, and energy and non-energy prices. Europe imports a significant share of both oil and natural gas from Russia and has limited domestic production, which could increase in response to the higher prices. Oil is a global market and prices have increased everywhere, and will drag on European growth, but natural gas markets are more segmented and European natural gas prices have jumped sharply—currently about five times the price in the US — differentially weighing on growth. Along with the downbeat central scenario, there remains downside risk of an actual cutoff of natural gas supplies and the consequent curtailment of economic activity. That said, we note that European natural gas consumption drops sharply by approximately 50% in May relative to highs in January, so the worst of this risk fades some over the next several months. We expect Europe's response will include a substantial, long-lasting reorientation of energy policy away from Russia and toward essentially all other energy producers.

In contrast, North American growth should feel a smaller impact. Both the US and Canada have limited direct trade linkages with either Russia or Ukraine. Markets for natural gas are mostly segmented due to limited LNG terminals and shipping, so price increases within North America have been relatively restrained. That leaves elevated oil prices the main transmission mechanism to the US and we do expect some drag from the elevated levels. Still, we think the overall impact on growth to be limited for several reasons. First, the current US$100-120 range for Brent oil isn't unprecedented as oil was around this range from 2011-2014 and growth held up. Second, unlike 20 years ago, the US is a significant oil producer, so a portion of the higher consumer energy spending gets recycled domestically — a partial offset when it comes go overall growth, though there are regional and distributional impacts.

Lastly, DM Asia should fall somewhere in between Europe and North America. On the lesser effect side of the ledger, direct trade links are generally smaller than for Europe and some have longer-term natural gas supply contracts that will attenuate that channel. But the oil price effect will be significant and, like Europe, domestic production of energy goods is generally small.

Our base case scenario assumes the Russia-Ukraine war continues without a firm resolution, keeping global sanctions against Russia broadly in place and commodity prices elevated. As a result, we currently anticipate materially slower global growth, but not a derailment of the ongoing recovery from COVID. Against this backdrop, we see central banks in both EM and DM generally moving in the same direction, with the US Federal Reserve hiking seven times over the next 12 months; many EMs continuing rate hikes, with the notable exception of China; and the European Central Bank winding down asset purchases by the middle of this year and initiating rate hikes early next year. We assign a 40% probability to this base case scenario, a notably lower weighting than usual reflecting the inherent uncertainty in the current environment. We assign a 20% probability to each of the remaining scenarios: easing international tensions; commodity price spike accelerates further; and a global recession.

MACRO RISK SCENARIO ASSUMPTIONS AND MARKET OUTLOOK[1]

Elevated Commodity Prices—Fallout of Russia-Ukraine War—Materially Slow, But Don't Derail, Global Growth (40%)

- Russia-Ukraine continues without definitive resolution. Global sanctions against Russia mostly remain in place.
- Disruption, and reduction of supply from Russia, keeps commodity prices elevated.
- Covid drag continues to fade as global economies broadly move further toward operating along pre-pandemic norms.
- But higher energy and commodity prices prove a modest drag on US growth and a meaningful drag on European growth. Interest rate sensitive sectors, e.g. housing, start to lag with the move higher in rates.
- Policy of local lockdowns remains in place for China, and continues to impact economic behavior. China growth somewhat softer than consensus.
- US/China tensions remain cooler, but do not return to pre-Trump status quo.
- Core PCE remains through H1-2022. Some of the increase comes from still-snarled supply chains, which start to normalize in the summer combined with rotation of demand back to services. But the underlying inflation run-rate has moved higher.
- Fed hikes rates 7 times over next 12m, starting in March. Balance sheet runoff commences early-H2.
- ECB winds down asset purchases by middle of 2022; rate hikes priced for early 2023.
- Rate hikes continue across EM, with the exception of China.
- Oil continues to price at a premium, though a smaller one than currently ~$90/barrel WTI, Brent ~$95.

Easing International Tensions (20%)

- Some form of resolution to Russia-Ukraine War leads to cessation of active hostilities and partial rollback of US/EU restrictions and sanctions put into place.
- Russian oil and gas find their way back into global markets and much of the risk premium unwinds.
- Post-covid rebound continues. Higher energy prices only a temporary drag; DM growth rebounds from H1 weakness over H2. For year as a whole, US growth is meaningfully above potential.
- Supply chain issues improve and unwind of energy and commodity price increases helps put some downward pressure on core.
- Fed proceeds along a very similar policy normalization route over 2022.
- Oil prices: ~$70/barrel for WTI; Brent ~$75.

Commodity Price Spike Accelerates Further (20%)

- Western economies broadly prove resilient to the higher commodity prices and growth remains strong. Output moves clearly above the pre-pandemic trend.
- Europe cuts off Russian oil and gas exports. Diversion to China and other countries ongoing, but is a messy process.
- Firm growth bumps up against ongoing sanctions and removal of substantial amount of Russian supply to elevate commodity prices even further.
- Supply chain issues do not resolve and price increases remain elevated. Facing tight labor supply, firms continue to bid up wages attempting to pull workers off the sidelines. Higher energy prices spill into core.
- With US inflation continuing to run well above target the Fed starts increasing rates at the March meeting and continues to do so over 2022. At least one FOMC meeting sees a 50bp rate hike.
- Rates move sharply higher along the curve.
- Oil prices rise further with growth and inflation: WTI to $145/barrel, Brent $155/barrel.

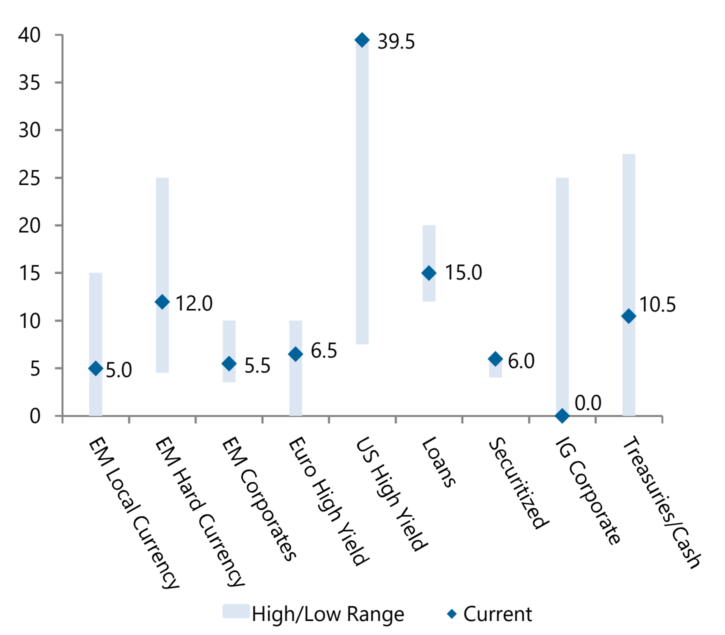
Global Recession (20%)

- Combination of tighter fiscal and monetary policies, sharply elevated energy prices, hit to sentiment from Russia-Ukraine War and associated trade disruption tips global economies into recession.
- Growth fades rapidly into H2 and contracts in at least one quarter for the US; Eurozone is even weaker.
- With slower activity and sluggish consumer demand inflation moderates rapidly, dipping toward target by early-23.
- European growth even slower than US growth. The recession spills over into other DM and EM economies, though they perform relatively better than the US/EZ.
- Broadly, sanctions against Russia remain in place.
- Fed, having hiked rates, reverses course and cuts them back to the lower bound. Balance sheet shrinkage pauses, and then restarts after rates hit the lower bound.
- ECB never manages to get off the lower bound; asset purchases ramp back up.
- EM economies reverse some of the recent rate hikes.
- Oil: WTI at ~$55/barrel; Brent ~$60/barrel.

	Elevated Commodity Prices—Fallout of Russia-Ukraine War—Materially Slow, But Don't Derail, Global Growth (40%)	Easing International Tensions (20%)	Commodity Price Spike Accelerates Further (20%)	Global Recession (20%)
US Real 4Q GDP (%)	2.25	2.75	3.50	0.00
Fed Funds (%)	1.88	1.88	2.63	0.13
US Core PCE (%)	2.70	2.50	3.75	2.00
2yr Treasury (%)	2.30	2.25	2.70	0.35
10yr Treasury (%)	2.35	2.15	3.25	1.25
10yr Bund (%)	0.50	0.70	1.20	-0.50
China 4Q GDP (%)	5.00	5.50	5.50	3.50
EM 4Q GDP (%)	2.70	3.50	3.00	1.00

[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	Jan-Feb 2022	-2.5
EM Hard Currency	Jan-Feb 2022	-5.0
EM Corporates	May-June 2018	+1.5
Euro High Yield	Dec-Jan 2022	+2.5
US High Yield	Jan-Feb 2022	+8.5
Loans	Jan-Feb 2021	+1.5
Securitized	Mar-April 2019	+1.0
IG Corporate	June-July 2021	-2.0
Treasuries/Cash	Jan-Feb 2022	-1.0

[2]Since Inception: September 2013. Stone Harbor Multi-Asset Credit Representative Target Allocation as of 28 February 2022. 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	-0.90	-6.55	-0.51	-5.00	-4.84	-3.03	-2.12
Duration (Returns from Interest Rates %)	-0.48	-0.73	-0.02	-0.48	-0.51	-0.38	-0.76
Credit Beta (Returns from Spreads %)	-0.42	-5.82	-0.49	-4.52	-4.33	-2.65	-1.36

Month Ended 28 February 2022. 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, London, and Singapore.
- Effective January 1, 2022, Stone Harbor Investment Partners is an affiliate of Virtus Investment Partners

Stone Harbor Investment Partners, LLC 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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