FAQ:
Russia/Ukraine debt outlook

March 15, 2022

This FAQ is designed to help provide perspective on the current Russia/Ukraine crisis.

Q. How likely is it that Russia will default on its sovereign debt?

A. The Russian government's willingness to pay on its debt obligations is now explicitly in question following comments by the Putin regime, despite economic buffers put in place before the events of recent weeks.

Russia sits with a large current account surplus (meaning that the country is a net lender to the rest of the world) and deep international reserves suggested to be as large as $650 billion prior to the start of the invasion at the end of February. Approximately 50% of these reserves are based in U.S. dollars, euros, or sterling, and are held with western institutions. With recently imposed sanctions, these reserves are now inaccessible.

Approximately 12% of the country's reserves are in gold which, while accessible, are not liquid. The remaining assets are either in rubles (which have devalued significantly) or Asian currencies (Chinese yuan is the largest holding). This accessibility problem changes the fundamental picture for "Fortress Russia" (the notion that Russia's reserves would allow it to withstand Western sanctions) considerably.

As of March 9, market expectations (based on the pricing of credit default swaps) suggested a high probability of sovereign default of both Russia's local (denoted in rubles) and hard-currency (generally U.S. dollar, euro, sterling, Japanese yen, and Swiss franc) obligations.

A coupon on a key Russian corporate (Gazprom) delivered a hard-currency coupon payment March 7. At the sovereign level, the next significant event is March 16, when a hard-currency coupon is due.

Q. What happened the last time that Russia defaulted? Should we expect the same to happen this time?

A. Russia's previous debt default in 1998 followed the Asian crises in 1997, which contributed to lower energy consumption, a decline in oil prices, and a decrease in the region's trade with Russia. At the time, the ruble was a floating-peg currency (managed within an artificial range). In quick succession and unable to prop up its currency and meet debt obligations, Russia defaulted on its domestic debt and moved to a free-floating ruble.

A $20 billion financial package approved by the International Monetary Fund helped stabilize the Russian market at the time. Additionally, improving relations with the Paris Club (a group of officials from major creditor countries whose role is to find solutions to payment difficulties experienced by debtor countries) helped negotiate a rescheduling of old Soviet debt.

The interest payments remained burdensome, although they arguably would have been manageable were it not for externalities such as the Asia crises and decline in oil prices. It is unlikely the country will see similar support for its debt this time around.

Q. Would a Russian sovereign-debt default impact Russian corporate debt the way it did in the U.S. when the country's rating was cut?

A. Rating agencies often use a corporation's country of primary residence as a floor for rating corporate debt. This is particularly true when firm revenues are intertwined with the trade of that country for either domestic demand or its composition of exports.

© 2022 SEI

Several Russian state-owned and corporate entities have been sanctioned due to the nature of their business or ownership structure. These entities are the most at risk of receiving rating downgrades.

At the sovereign-debt level, Fitch Ratings has already cut the rating on Russian sovereign debt to below-investment grade status (aka “junk”).

Q. What would a default mean for investor portfolios (how big is the index exposure), and does it appear to be accounted for by the current trading halt?

In general, exposure to Russian debt in most major emerging-market bond indexes was minimal before the invasion of Ukraine. With valuations falling, they are smaller post-invasion. For example, at the end of February, index exposure in the 50% JP Morgan Emerging Markets Bond Index-Global Diversified 50% and JP Morgan Government Bond Index-Emerging Markets Global Diversified blended benchmark (a common benchmark for some of SEI’s emerging-market debt portfolios) was 1.40%. As of March 9, EMD blended benchmark exposure was less than 0.11%.

Accordingly, a default is unlikely to have a significant direct impact on most portfolios, particularly of they are well diversified.

Q. What are the spillover effects to the global economy?

A. Net importers of energy will face higher input costs. This event is inflationary in nature, but it may have also second-order growth effects and create risks to the global economy. There is also the potential to tip from a reflationary path to a stagflationary path if growth is tepid and inflation soars.

While Russia is known for its energy exports, it also contributes significantly to other world commodities, including 13% of fertilizer, 17% of nickel, and 8% of cereals. The first could directly impact crop yields, which would create food inflation, while the last is disproportionally sent to sub-Saharan Africa to meet consumption demands. Exporters more generally may benefit from the increase in commodity prices, albeit absent meaningful growth, this may be short-lived.

© 2022 SEI

Glossary

Credit default swaps: Credit default swaps are contracts that transfer third-party credit risk from one party to another. For example, if an investor believes a bond issued by a company may default, they can enter into an agreement with a bank, insurance company or other entity by which they agree to cover the cost of the possible default in exchange for periodic payments. An investor does not need to own the bond issued by the company in order to purchase a credit default swaps related to it.

International Monetary Fund: The International Monetary Fund (IMF) is an international organization of 189 member countries that promotes global economic growth and financial stability, encourages international trade, and reduces poverty. Monetary policy: Monetary policy relates to decisions by central banks to influence the amount of money and credit iJunk bonds: Junk bonds or high-yield debt is rated below investment grade and is considered to be riskier. Junk bonds carry a higher risk of default than most bonds issued by corporations and governments.

Reflation: Reflation refers to a fiscal or monetary policy designed to expand output, stimulate spending, and curb the effects of deflation, which occurs after a period of economic uncertainty or a recession.

Sovereign: A sovereign refers to government-issued debt.

Stagflation: Stagflation refers to slow economic growth and high unemployment, or economic stagnation, which is also accompanied by rising prices and inflation.

Treasury Inflation-Protected Securities (TIPS): TIPS are sovereign securities issued by the U.S. Treasury that are indexed to an inflationary gauge to protect investors from the decline in the purchasing power of their money. The principal value of TIPS rise as inflation rises, while the interest payment varies with the adjusted principal value of the bond. The principal amount is protected so that investors do not risk receiving less than the originally invested principal. Yield: Yield is a general term for the expected return, in percent/

Index definitions

JP Morgan Emerging Markets Bond Index-Global Diversified: The JP Morgan Emerging Markets Bond Index-Global Diversified tracks total returns for traded external debt instruments in the emerging markets, and is an expanded version of the JPMorgan EMBI+. As with the EMBI+, the JP Morgan Emerging Markets Bond Index-Global Diversified includes U.S. dollar-denominated Brady bonds, loans, and Eurobonds with an outstanding face value of at least $500 million.

JP Morgan Government Bond Index-Emerging Markets Global Diversified: The JP Morgan Government Bond Index-Emerging Markets Global Diversified is a market capitalization weighted total return index of U.S. dollar and other external currency denominated Brady bonds, loans, Eurobonds, and local market government debt instruments traded in emerging markets.

Important information

This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events or a guarantee of future results. Positioning and holdings are subject to change. All information as of the date indicated. There are risks involved with investing, including possible loss of principal. This information should not be relied upon by the reader as research or investment advice, (unless you have otherwise separately entered into a written agreement with SEI for the provision of investment advice) nor should it be construed as a recommendation to purchase or sell a security. The reader should consult with their financial professional for more information.

Statements that are not factual in nature, including opinions, projections and estimates, assume certain economic conditions and industry developments and constitute only current opinions that are subject to change without notice. Nothing herein is intended to be a forecast of future events, or a guarantee of future results.

Certain economic and market information contained herein has been obtained from published sources prepared by other parties, which in certain cases have not been updated through the date hereof. While such sources

are believed to be reliable, neither SEI nor its affiliates assumes any responsibility for the accuracy or completeness of such information and such information has not been independently verified by SEI.

There are risks involved with investing, including loss of principal. The value of an investment and any income from it can go down as well as up. Investors may get back less than the original amount invested. Returns may increase or decrease as a result of currency fluctuations. Past performance is not a reliable indicator of future results. Diversification may not protect against market risk.

Bonds and bond funds will decrease in value as interest rates rise. High-yield bonds involve greater risks of default or downgrade and are more volatile than investment-grade securities, due to the speculative nature of their investments. Treasury Inflation Protected Securities can provide investors a hedge against inflation, as the inflation adjustment feature helps preserve the purchasing power of the investment. Because of this inflation adjustment feature, inflation protected bonds typically have lower yields than conventional fixed rate bonds. Commodity investments and derivatives may be more volatile and less liquid than direct investments in the underlying commodities themselves. Commodity-related equity returns can also be affected by the issuer's financial structure or the performance of unrelated businesses.

This material is not directed to any persons where (by reason of that person's nationality, residence or otherwise) the publication or availability of this material is prohibited. Persons in respect of whom such prohibitions apply must not rely on this information in any respect whatsoever.

The information contained herein is for general and educational information purposes only and is not intended to constitute legal, tax, accounting, securities, research or investment advice regarding the strategies or any security in particular, nor an opinion regarding the appropriateness of any investment. This information should not be construed as a recommendation to purchase or sell a security, derivative or futures contract. You should not act or rely on the information contained herein without obtaining specific legal, tax, accounting and investment advice from an investment professional.

Information in the U.S. is provided by SEI Investments Management Corporation (SIMC), a wholly owned subsidiary of SEI Investments Company (SEI).

Information provided in Canada by SEI Investments Canada Company, the Manager of the SEI Funds in Canada.

Information issued in the UK by SEI Investments (Europe) Limited, 1st Floor, Alphabeta, 14-18 Finsbury Square, London EC2A 1BR which is authorised and regulated by the Financial Conduct Authority. Investments in SEI Funds are generally medium- to long-term investments.

The offer or invitation to subscribe for or purchase shares of the Sub-Funds (the "Shares), which is the subject of this Information Memorandum, is an exempt offer made only: (i) to "institutional investors" pursuant to Section 304 of the Securities and Futures Act, Chapter 289 of Singapore (the "Act"), (ii) to "relevant persons" pursuant to Section 305(1) of the Act, (iii) to persons who meet the requirements of an offer made pursuant to Section 305(2) of the Act, or (iv) pursuant to, and in accordance with the conditions of, other applicable exemption provisions of the Act.

SIEL has appointed SEI Investments (Asia) Limited (SEIAL) of Suite 904, The Hong Kong Club Building, 3 Jackson Road, Central, Hong Kong as the sub-distributor of the SEI UCITS funds. SEIAL is licensed for Type 4 and 9 regulated activities under the Securities and Futures Commission ("SFC")

This information is being made available in Hong Kong by SEIAL. The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to the offer. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice.

This information is made available in Latin America FOR PROFESSIONAL (non-retail) USE ONLY by SIEL.

Any questions you may have in relation to its contents should solely be directed to your Distributor. If you do not know who your Distributor is, then you cannot rely on any part of this document in any respect whatsoever.

© 2022 SEI

SIEL is not licensed under Israel's Regulation of Investment Advising, Investment Marketing and Portfolio Management Law, 5755-1995 (the "Advice Law") and does not carry insurance pursuant to the Advice Law. No action has been or will be taken in Israel that would permit a public offering or distribution of the SEI Funds mentioned in this email to the public in Israel. This commentary and any of the SEI Funds mentioned herein have not been approved by the Israeli Securities Authority (the "ISA").

Issued in South Africa by SEI Investments (South Africa) (Pty) Limited FSP No. 13186 which is a financial services provider authorised and regulated by the Financial Sector Conduct Authority (FSCA). Registered office: 3 Melrose Boulevard, 1st Floor, Melrose Arch 2196, Johannesburg, South Africa.

© 2022 SEI