Vanguard

Q1 2022

EMERGING MARKETS BOND FUND

Quarterly update

LOW-COST ACTIVE FIXED INCOME

The Vanguard Emerging Markets Bond Fund is an actively managed fixed income solution investing primarily in emerging market sovereigns. The fund is managed by Vanguard's Fixed Income Group and aims to generate a diversified, consistent level of return over the long term.

Highlights

- Emerging market bonds delivered a negative return over the quarter.
- Russia's invasion of Ukraine weighed on the asset class.
- The Vanguard Emerging Markets Bond Fund outperformed its benchmark.
- An underweight allocation to Russian debt contributed to performance.
- We see select pockets of value remain in emerging market bonds.

Market overview

Emerging market (EM) bonds continued to experience a challenging environment in the first quarter of the year. The year began with low global yields and historically tight credit spreads while investors continued to focus on inflation and quantitative easing. By the end of February, Russia's invasion of Ukraine and the subsequent sanctions placed on Russia by governments around the world dominated financial markets and hurt EM bonds.

The dramatic decline in the value of bonds issued by both Russia and Ukraine and the broader drag from higher US Treasury rates sparked the large negative performance of the sector so far this year. Given the circumstances, EM debt still managed to be fairly resilient in the face of such a substantial shift in geopolitics. Contagion to other EM assets has been relatively muted outside of Eastern Europe, and many of those bonds managed strong recoveries over recent weeks as fears of a more broad-based military escalation have eased.

The first half of March continued with the theme of EM asset price weakness, in part off the back of developments in Russia and Ukraine. However, the second half saw a meaningful rally in sovereign credit as fears of broader EM contagion were alleviated. Russia alone was responsible for around one-third of the spread widening in the early part of the month; as a result, combined with the more recent overall rally and Russia's month-end exclusion from the index, EM sovereign credit spreads retraced to more normal levels by the end of the quarter. The longer-term implications of this conflict will continue to be felt across EM countries and in the broader macroeconomic environment.

Strategy, performance and positioning

The Vanguard Emerging Markets Bond Fund recorded a negative absolute return; however, it outperformed its benchmark over the quarter, returning -8.28% compared with a return of -10.07% for its benchmark, the JPM EMBI Global Diversified Index[1].

The fund's outperformance relative to its benchmark was driven largely by an underweight allocation to Russian bonds. Country and security selection, primarily within the bonds of Latin American countries, also contributed to returns.

1 Source: Vanguard and J.P. Morgan as at 31 March 2022.

Meanwhile, country selection, specifically underweight allocations to Turkey and Egypt, detracted from performance, as did the fund's overweight position in Ukraine. The beta of the market also caused broad-based (EM) bonds to sell off.

In terms of the portfolio's positioning, (EM) bonds have become cheaper overall, driven by Russia and Ukraine. However, even after adjusting for this, EM sovereign credit spreads had retraced to more normal levels by the end of the quarter. While we saw some retracement in the second half of March, spreads were still cheap relative to recent history. We continue to see opportunities but also remain cautious on the challenges to EM growth as well as from more potential stimulus from China. As such, we have been more constructive on the market and have raised the fund's beta.

The US Federal Reserve (Fed) interest rate policy normalisation remains a challenge, especially if interest rates move faster and in higher increments than expected. This is especially challenging for the investment grade part of EM credit, given its sensitivity to interest rates.

Outlook

Our ongoing caution around EM is based partly on the impact that the gradual but definitive removal of monetary stimulus by the Fed and other developed market central banks will have on risky assets, including (EM) bonds. Also of concern is that EM growth did not catch up with that of developed markets during the second half of 2021.

Some EM central banks had already pre-emptively begun tapering before the Fed embarked on its interest rate hikes—a risky move given that EM growth remains fragile. Despite fragile economies, market participants expect many EM sovereigns to reduce, or at best consolidate, their fiscal funding needs this year, and countries that fail to do so may face lower returns from the market.

In terms of Russia and Ukraine, we continue to monitor developments. That said, there are reasons for cheer around EM. We believe EM high yield is more attractive in this environment as higher spreads provide some more insulation relative to investment grade. Technical factors in terms of low new issuance from EM remain in place for now – this has helped mitigate some degree of outflows from the asset class.

In terms of EM rates, we believe this will be a good source of opportunities and await more clarity on the terminal interest rates of certain EM central banks, as well as the Fed. In EM currencies, while we remain cautious, we are starting to see more opportunities, especially for carry trades.

Fixed income overall continues to go through a very challenging period. Underlying risk free 10-year US Treasuries produced a negative total return exceeding -6.60% in Q1, while 30-year US Treasuries delivered a negative return of -9%[2]. It's important to note that a large portion of EM negative total returns derive from this US Treasury move. While we see value in EM, we're mindful of the risk of further shocks and are maintaining high levels of liquidity as insurance against further market deterioration.

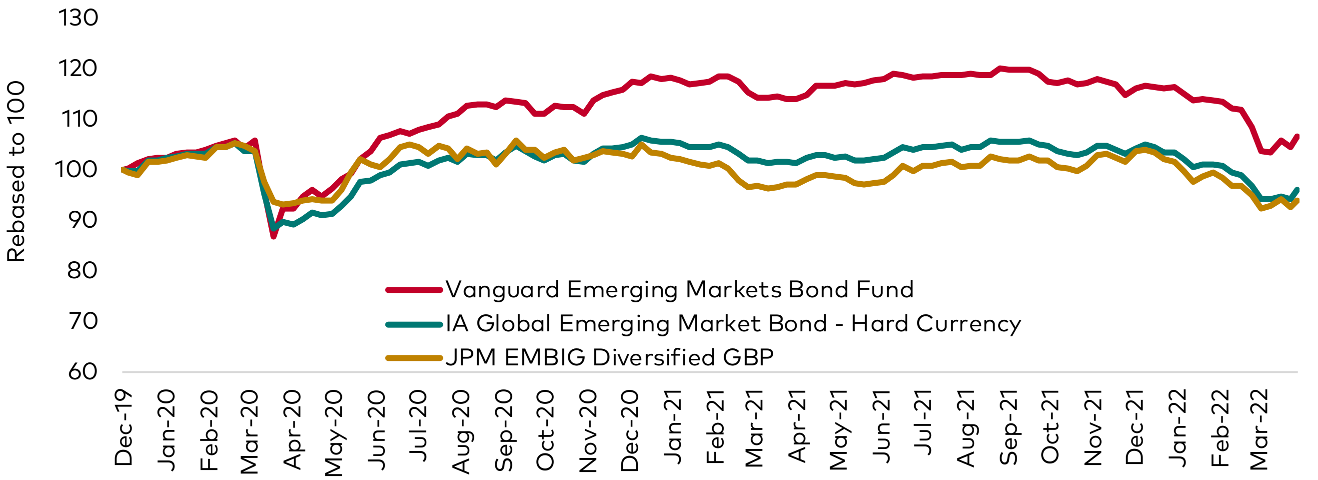
2 Source: Bloomberg as at 31 March 2022.

Key fund facts (as at 31 March 2022)

Investment manager: Vanguard Fixed Income Group
Inception date: 03 December 2019
Domicile: Ireland
Benchmark: JPM EMBI Global Diversified Index
Ongoing charges figure[1]: 0.60%
Fund AUM: GBP 341m
Number of holdings: 227

Average coupon: 4.4%
Average maturity: 12.7 years
Average quality: BB+
Average duration: 6.7 years
Turnover rate: 430.5%
ISIN: IE00BKLWXP06

Fund performance since inception (as at 31 March 2022)



Cumulative (%)	YTD	3m	1 year	3 yr (ann.)	5 yr (ann.)	Since inception
Fund	-8.28	-8.28	-6.14	--	--	2.82
Peer Group	-7.11	-7.11	-5.61	-0.73	-0.30	-5.27
Benchmark	-10.07	-10.07	-7.76	-0.99	0.43	-2.90

Year on year (%)	1 Apr 2017 - 31 Mar 2018	1 Apr 2018 - 31 Mar 2019	1 Apr 2019 - 31 Mar 2020	1 Apr 2020 - 31 Mar 2021	1 Apr 2021 - 31 Mar 2022
Fund	--	--	--	22.96	-6.14
Peer Group	-2.26	3.68	-7.15	11.80	-5.61
Benchmark	3.01	2.17	-8.76	15.34	-7.76

Past performance is not a reliable indicator of future results.
Source: Vanguard and Morningstar, as at 31 March 2022. Peer group is IA Global Emerging Market Bond - Hard Currency. Performance figures include the reinvestment of all dividends and any capital gains distributions. The performance data does not take account of the commissions and costs incurred in the issue and redemption of shares. Basis of fund performance NAV to NAV. Basis of index performance is total return. All performance is calculated in GBP, net of fees, and the return may increase or decrease as a result of currency fluctuations.

[1]The Ongoing Charges Figure (OCF) covers the fund manager's costs of managing the fund. It does not include dealing costs or additional costs such as audit fees.

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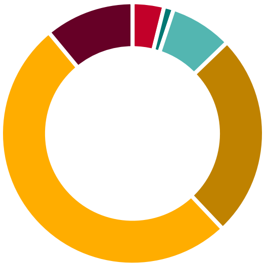
Fund breakdown (as at 31 March 2022)

Distribution by issuer (% of bonds)

Characteristics	Fund %
Sovereign	55.4
Agencies	23.8
Cash	10.9
Treasury/federal	5.2
Industrials	4.0
Financial institutions	0.7
Other	0.0
Utilities	0.0

The allocations are subject to circumstances such as timing differences between trade and settlement dates of underlying securities, that may result in negative weightings. The fund may also employ certain derivative instruments for cash management or risk management purposes that may also result in negative weightings. Allocations are subject to change. Cash includes physical cash on the account, cash like instruments (such as ultra-short term treasury bonds) and derivative instruments.

Distribution by credit quality (% of bonds)



AAA	3.9
AA	1.2
A	7.7
BBB	25.2
Less than BBB	51.1
NR	11.0

Credit quality ratings for each issue are obtained from Bloomberg using ratings derived from Moody's Investors Service, Fitch Ratings, and Standard & Poor's. When ratings from all three agencies are available, the median rating is used. When ratings are available from two of the agencies, the lower rating is used. When one rating is available, that rating is used.

Investment risk information

The value of investments, and the income from them, may fall or rise and investors may get back less than they invested.

Past performance is not a reliable indicator of future results.

Some funds invest in emerging markets which can be more volatile than more established markets. As a result the value of your investment may rise or fall.

Funds investing in fixed interest securities carry the risk of default on repayment and erosion of the capital value of your investment and the level of income may fluctuate. Movements in interest rates are likely to affect the capital value of fixed interest securities. Corporate bonds may provide higher yields but as such may carry greater credit risk increasing the risk of default on repayment and erosion of the capital value of your investment. The level of income may fluctuate and movements in interest rates are likely to affect the capital value of bonds.

The Vanguard Emerging Markets Bond Fund may use derivatives, including for investment purposes, in order to reduce risk or cost and/or generate extra income or growth. For all other funds they will be used to reduce risk or cost and/or generate extra income or growth. The use of derivatives could increase or reduce exposure to underlying assets and result in greater fluctuations of the Funds net asset value. A derivative is a financial contract whose value is based on the value of a financial asset (such as a share, bond, or currency) or a market index.

Some funds invest in securities which are denominated in different currencies. Movements in currency exchange rates can affect the return of investments.

For further information on risks please see the "Risk Factors" section of the prospectus on our website at https://global.vanguard.com.

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