VanEck® FUNDS

Under Pressure

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VanEck Unconstrained Emerging Markets Bond Fund

EMBAX / EMBCX / EMBUX / EMBYX

Market Review

What a month November was. Two key market drivers of 2018 – the Fed, and "China trade" – whipped all asset classes back and forth. In addition, two key asset prices – U.S. stocks and U.S. Treasuries – dominated sentiment. Emerging markets (EM) debt had been buffeted earlier in 2018 by these two market drivers, when an initial rise in U.S. yields was viewed as positive for EM debt (EMD), with only U.S. dollar bonds selling off in the first quarter of the year, while local currency bonds continued to rally. As 2018 wore on and U.S. growth started clearly diverging from weakening developed markets (DM) growth, all EM bonds (local currency and U.S. dollar-denominated) suffered. November followed what was a similarly volatile October. Since this is the setup going into 2019, this is what we think.

We see three scenarios going forward: goldilocks (bullish for EM risk), U.S./global recession (bearish for EM risk), and continued economic divergence (bearish for EM risk). Let us examine each one, starting with goldilocks. In this scenario, the market is in the midst of a somewhat typical post-QE (quantitative easing) selloff. The cause – Fed tightening – will be reversed as global uncertainty feeds back to policymakers, and they "blink." This was the case (to varying degrees) with: the European debt crisis in 2011, the "taper tantrum" in 2013, and the commodities-related selloff of 2015. In the goldilocks scenario, global growth will re-couple with U.S. growth, as U.S. policymakers ease (relatively) monetary policy and get the U.S dollar (USD) down, boosting EM debt. Under this scenario, we will be back to the "synchronized global growth" theme that existed up until the first quarter of 2018.

The continued economic divergence scenario is bearish for EM debt, in our view. In this scenario, we get more of what we saw in 2018 (excepting the first quarter). That is, a U.S. economy that continues to outperform the rest of the world. We would note that U.S. purchasing managers' indices (PMIs) have been in the high-50s throughout 2018 and that that remains the case in recent months. This is in comparison to European and Asian PMIs that have clearly declined. In our thinking, such a scenario keeps the Fed in tightening mode and wary of inflation pressures. With higher relative growth and interest rates, the USD remains under upward pressure. As a result, we would expect hard currency EM debt to be pressured by rising yields, and local currency EM debt to be pressured by a rising USD.

The volatility and asset price weakness of October and November introduce a third scenario: U.S./global recession, which would be even more bearish for EM debt, in our view. In this scenario, it is just a matter of time for relative global weakness to catch up with a U.S. economy that is in the late stages of its economic cycle. As a result, the U.S. economy will turn, hitting global demand. Policymakers might not have the usual flexibility and tools to react to this scenario. Global leverage has increased following the global financial crisis, so fiscal policy might not be as usable. Similarly, given that the Fed's tightening of policy has been very shallow compared to that of previous recoveries, the usual monetary forbearance might not be that strong. This, and the deeper problem that all of these policies have already been tried, makes any recession a potentially more troublesome one for markets. In any case, (our prior) is that the USD is boosted in the event of a U.S./global recession, as "risk-off" and position closing translates fairly directly into U.S. dollar buying.

These scenarios strike us as generally bearish for EM debt. Even though we see a chance of a goldilocks scenario, it would be short-lived and is substantially already priced in, in our opinion. The reason we believe such a goldilocks scenario would be short-lived is that it depends on Fed forbearance. As we have argued before, what has been unique about the current Fed tightening cycle is that financial conditions largely eased when the Fed intended the opposite, mostly because the U.S. dollar didn't weaken significantly against the major DM currencies (EUR and JPY). So, let us say goldilocks happens. We see a Fed moving quickly to concern that financial conditions are easing excessively. Moreover, such a scenario is arguably already priced into bond markets. As of this writing (December 10, 2018, 11:00am), the market-implied policy rate sees 35 bps of Fed hikes over the next 12 months, with only a 71% chance of a 25 bps hike in December. Put differently, economic conditions would need to worsen substantially for the Fed to truly be on hold. So much so that we might be in the U.S./global recession scenario for such implied policy rates to hold. There is a fine line between the goldilocks scenario and the US/global recession scenario.

Our stance remains largely intact, as a result, although we have brought the portfolio a little closer to benchmark, given market volatility as it entertains these scenarios and as the goldilocks scenario plays out. This has involved some increase in our local currency exposures, as we had limited local currency exposure this year following the first quarter. Our increases here (details below) were to countries that are cheap in our investment process and which, we believe, are responding properly to tougher global conditions (Indonesia, which recently surprised by hiking interest rates, and Peru). We are not, for example, investing in Turkey or Mexico, as, in each, we see big turns to the worse in economic policy (so technically, they get a "fail" on the Policy/Politics test in our investment process). We emphasize this because our calculations indicate that problematic (in our view) markets such as Turkey's local market have generated 3% of the 3.8% return in the GBI-EM from September 1 to the close of December 6, 2018. We do not intend to chase rallies in fundamentally flawed countries simply because they rally. We also increased exposure to some smaller U.S. dollar-denominated sovereigns that had sold off excessively (in our opinion), and in which we had underweights (Guatemala and El Salvador).

Exposure Types and Significant Changes

The changes to our top positions are summarized below. Our largest positions are currently: Brazil, Argentina, Indonesia, South Korea, and Mongolia.

- We increased local currency exposure in Indonesia and Peru. Indonesia's pre-emptive monetary policy moves created good anchors, while the macro flow remains mostly benign. In terms of our investment process, this improved the economic and policy scores for the country. In Peru, the post-August price correction created a better entry point against the backdrop of contained political risks, strong external buffers, robust growth, and low inflation. In terms of our investment process, this translates into the improved technical score for the country.

- We also increased our hard currency sovereign exposures in Guatemala and El Salvador. The bond of our choice in Guatemala continues to look attractive valuation wise, while the country's low debt makes it an attractive investment option if global rates' volatility increases further. In addition, the congressional approval of the 2019 budget improved the policy score for the country. In El Salvador, an agreement on the fiscal bill opened the door for talks on the 2019 budget and the rollover authorization for the 2019 sovereign bond, improving the policy and fundamental scores for the country.

- We increased our hard currency sovereign exposure in Costa Rica, following the approval of fiscal reform by the country's congress. In terms of our investment process, this improved the policy score for the country.

- We reduced local currency exposures in Poland and Brazil. In Poland, concerns about the bank scandal implications for the central bank (which can potentially affect the monetary policy stance) were the main reason for the reduction, as they worsened the country's policy score. In Brazil, the market participants are waiting for more visibility on the reform front (social security reform, in particular), which is unlikely to materialize until early 2019, capping the near-term improvement in the policy score.

- We reduced hard currency sovereign exposure in Dominican Republic. Even though macroeconomic fundamentals are solid, we decided to bring out exposure closer to neutral in order to focus on other opportunities. In terms of our investment process, this lowered the technical score for the country.

- We also reduced hard currency corporate exposures in South Africa and Colombia. In Colombia, changes to the corporate bond's covenants made it a weaker credit. In South Africa, the corporate's outlook got affected by uncertainty about the sovereign, worsening the technical score for the credit.

Fund Performance

The VanEck Unconstrained Emerging Markets Bond Fund (Class A shares excluding sales charge) lost 1.28% in November compared to a gain of a 1.19% for the 50/50 J.P. Morgan Government Bond Index-Emerging Markets Global Diversified (GBI-EM) local currency and the J.P. Morgan Emerging Markets Bond Index (EMBI) hard-currency index.

The Fund's biggest winners were Indonesia, Poland, and Costa Rica. The Fund's least contributors were Brazil, Ukraine, and Venezuela. Turning to the market's performance, the GBI-EM's biggest winners were Indonesia, South Africa, and Turkey. The biggest losers were Argentina, Brazil, and Mexico. The EMBI's biggest winners were Mozambique, Zambia, and Costa Rica. The biggest losers were Venezuela, Nigeria, and Ghana.

Average Annual Total Returns (%) as of November 30, 2018

	1 Mo†	3 Mo†	YTD	1 Yr	5 Yr	Life
Class A: NAV (Inception 7/9/12)	-1.28	-0.87	-6.73	-5.65	-0.46	0.44
Class A: Maximum 5.75% Load	-6.91	-6.64	-12.13	-11.12	-1.63	-0.48
50 GBI-EM GD / 50% EMBI GD	1.19	1.14	-6.39	-5.10	1.68	1.44

Average Annual Total Returns (%) as of September 30, 2018

	1 Mo†	3 Mo†	YTD	1 Yr	5 Yr	Life
Class A: NAV (Inception 7/9/12)	1.51	1.66	-4.49	-4.72	0.29	0.84
Class A: Maximum 5.75% Load	-4.39	-4.19	-10.02	-10.21	-0.89	-0.11
50 GBI-EM GD / 50% EMBI GD	2.05	0.25	-5.55	-4.60	1.86	1.70

†Monthly returns are not annualized.

Expenses: Class A: Gross 1.71%; Net 1.26%. Expenses are capped contractually until 05/01/19 at 1.25% for Class A. Caps exclude acquired fund fees and expenses, interest expense, trading expenses, dividends and interest payments on securities sold short, taxes and extraordinary expenses. Please note that, generally, unconstrained bond funds may have higher fees than core bond funds due to the specialized nature of their strategies.

The tables above present past performance which is no guarantee of future results and which may be lower or higher than current performance. Returns reflect temporary contractual fee waivers and/or expense reimbursements. Had the Fund incurred all expenses and fees, investment returns would have been reduced. Investment returns and Fund share values will fluctuate so that investors' shares, when redeemed, may be worth more or less than their original cost. Fund returns assume that dividends and capital gains distributions have been reinvested in the Fund at Net Asset Value (NAV). An index's performance is not illustrative of the Fund's performance. Certain indices may take into account withholding taxes. Index returns assume that dividends of the index constituents in the index have been reinvested. Investing involves risk, including loss of principal; please see disclaimers on next page. Please call 800.826.2333 or visit vaneck.com for performance current to the most recent month ended.

International Monetary Fund (IMF) is an international U.S.-based organization of 189 countries focused on international trade, financial stability, and economic growth.

The World Government Bond Index (WGBI) measures the performance of fixed-rate, local currency, investment-grade sovereign bonds. The WGBI is a widely used benchmark that currently comprises sovereign debt from over 20 countries, denominated in a variety of currencies, and has more than 30 years of history available. The WGBI is a broad benchmark providing exposure to the global sovereign fixed income market. The Blended 50/50 Emerging Markets Debt Index is an appropriate benchmark because it represents the various components of the emerging markets fixed income universe.

Duration measures a bond's sensitivity to interest rate changes that reflects the change in a bond's price given a change in yield. This duration measure is appropriate for bonds with embedded options. Quantitative Easing by a central bank increases the money supply engaging in open market operations in an effort to promote increased lending and liquidity. Monetary Easing is an economic tool employed by a central bank to reduce interest rates and increase money supply in an effort to stimulate economic activity. Correlation is a statistical measure of how two variables move in relation to one other. Liquidity Illusion refers to the effect that an independent variable might have in the liquidity of a security as such variable fluctuates overtime. A Holdouts Issue in the fixed income asset class occurs when a bond issuing country or entity is in default or at the brink of default, and launches an exchange offer in an attempt to restructure its debt held by existing bond holding investors. Carry is the benefit or cost for owning an asset.

All indices are unmanaged and include the reinvestment of all dividends, but do not reflect the payment of transaction costs, advisory fees or expenses that are associated with an investment in the Fund. Certain indices may take into account withholding taxes. An index's performance is not illustrative of the Fund's performance. Indices are not securities in which investments can be made. The Fund's benchmark index (50% GBI-EM/50% EMBI) is a blended index consisting of 50% J.P. Morgan Government Bond Index-Emerging Markets (GBI-EM) Global Diversified and 50% J.P. Morgan Emerging Markets Bond Index (EMBI). The J.P. Morgan GBI-EM Global Diversified tracks local currency bonds issued by Emerging Markets governments. The J.P. Morgan EMBI Global Diversified tracks returns for actively traded external debt instruments in emerging markets, and is also J.P. Morgan's most liquid U.S. dollar emerging markets debt benchmark.

Please note that the information herein represents the opinion of the portfolio manager and these opinions may change at any time and from time to time and portfolio managers of other investment strategies may take an opposite opinion than those stated herein. Not intended to be a forecast of future events, a guarantee of future results or investment advice. Current market conditions may not continue. Non-VanEck proprietary information contained herein has been obtained from sources believed to be reliable, but not guaranteed.

Investing involves risk, including loss of principal. You can lose money by investing in the Fund. Any investment in the Fund should be part of an overall investment program, not a complete program. The Fund is subject to risks associated with its investments in below investment grade securities, credit, currency management strategies, debt securities, derivatives, emerging market securities, foreign currency transactions, foreign securities, hedging, other investment companies, Latin American issuers, management, market, non-diversification, operational, portfolio turnover, sectors and sovereign bond risks. Investing in foreign denominated and/or domiciled securities may involve heightened risk due to currency fluctuations, and economic and political risks, which may be enhanced in emerging markets. As the Fund may invest in securities denominated in foreign currencies and some of the income received by the Fund will be in foreign currencies, changes in currency exchange rates may negatively impact the Fund's return. Derivatives may involve certain costs and risks such as liquidity, interest rate, and the risk that a position could not be closed when most advantageous. The Fund may also be subject to risks associated with non-investment grade securities.

Investors should consider the Fund's investment objective, risks, charges, and expenses of the investment company carefully before investing. Bond and bond funds will decrease in value as interest rates rise. The prospectus and summary prospectus contain this and other information. Please read them carefully before investing. Please call 800.826.2333 or visit vaneck.com for performance information current to the most recent month end and for a free prospectus and summary prospectus.