

Your AMs/PMs want to buy new Saudi Aramco bonds? Have them consider the alternatives

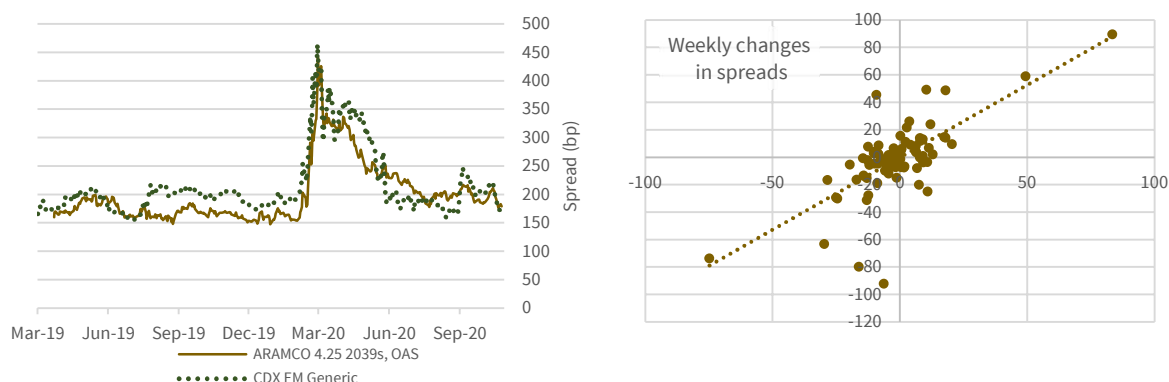
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Apparently Saudi Aramco is looking to tap the bond market again, after their initial bond issuance in April, 2019, see “[Aramco Turns to Bonds to Help Fund \\$75 Billion Dividend](#)”, Bloomberg, 16 Nov 2020. We rarely like bond investments with the sole purpose to fund payments of large dividends, and we are of the view the E, S, and G credentials of Aramco are not advantageous. However, we realize that there will be discussions across more than a few teams if the risk-return potential in buying Aramco bonds should outweigh potential reputational downsides and negative ESG impact.

We opine that one can construct risk-return profiles similar to buying Aramco bonds but without actually putting money in the account of the company or its shareholder(s).

In Figure 1, we illustrate how the Aramco 4.45 2039 bonds have been trading almost exactly in line with the CDX.EM index (here depicted in its generic version). The correlation once we switch out to weekly sampling frequency is quite strong, right hand of Figure 1. Considering that CDX.EM is considerably more liquid than cash bonds and has little need for duration hedging (for investors who trade on a spread basis), this suggests that the index could be a good replacement. Indeed, when going through a more technical analysis, we find few compelling arguments to own the bonds rather than the index.¹

Figure 1. (Left) Saudi Aramco bond spread vs CDX.EM CDS index spreads. (Right) Weekly changes of spreads, correlation.



¹ Please contact the AFII team for details around CDX.EM constituents and ESG, defaults/total returns, carry and roll-down dynamics, collateral requirements and other technical factors. For a fuller discussion around replacing low ESG assets with highly correlated/lower volatility assets in an MPT setting, see “[The Green Bond Risk Premium](#)” paper in the Reference section.

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“Credit alpha and CO2 reduction: A portfolio manager approach”, SSRN working paper, May 2017. [Link](#)

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