The Case for Emerging Market Local Currency Supranational Bonds

EMERGING MARKET DEBT INSIGHTS – JUNE 2025

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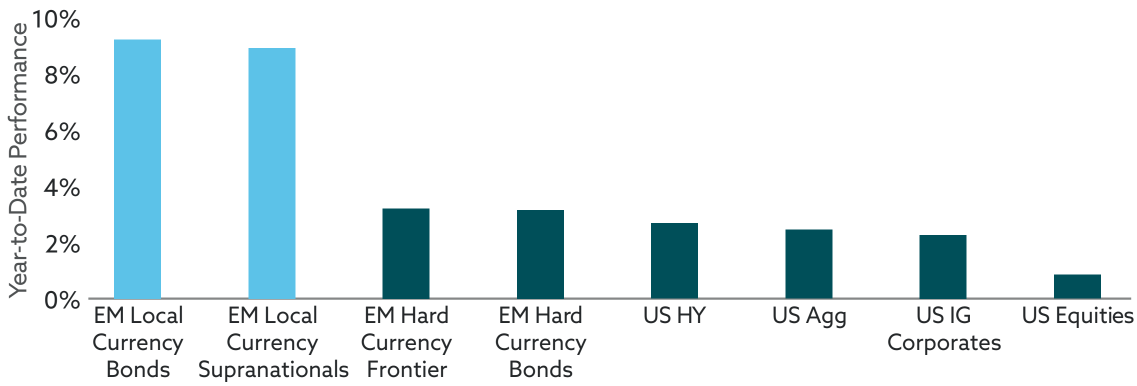
Emerging market (EM) currencies have broadly appreciated against the US dollar to begin 2025, moving in line with other major currency pairs, such as the euro and yen. Given this backdrop, EM local currency assets (i.e., unhedged exposure to EM currencies and interest rates) have outpaced other major fixed income and equity opportunities so far this year. In our opinion, fundamental and asset allocation trends are in place that should benefit EM local currency assets over the medium term. At PPM, we expressed this view by recently increasing exposure to supranational bonds denominated in EM currencies in our EM client portfolios. We believe these types of bonds can offer investors the ability to blend attractive return opportunities with risk-mitigating contractual features that can be applied across a broad and highly-diversified set of currency pairs.

POLICY UNCERTAINTY AS A CATALYST FOR EM LOCAL CURRENCY INVESTING

Policy uncertainty in the United States has generated significant volatility across global markets. Slowing global growth, stagflationary economic dynamics in the United States and material headwinds for global trade have historically presented challenges for emerging markets, from both an economic and a markets perspective. While we are always cautious to argue "this time is different," we think the current environment warrants a more nuanced assessment of likely market returns.

After a remarkable period of "US exceptionalism," a combination of factors points toward some level of fragility in US assets in relation to economic growth. Valuations for US equities and the US dollar opened the year at objectively elevated levels, having benefited from record-setting inflows from offshore portfolio investors over the past two years. As growth begins to weaken, the risk of a potential pullback in capital flows increases, with little room in valuations to cushion against potential disappointment. In our view, local currency EM assets are likely one of the top beneficiaries of this unwinding US exceptionalism.

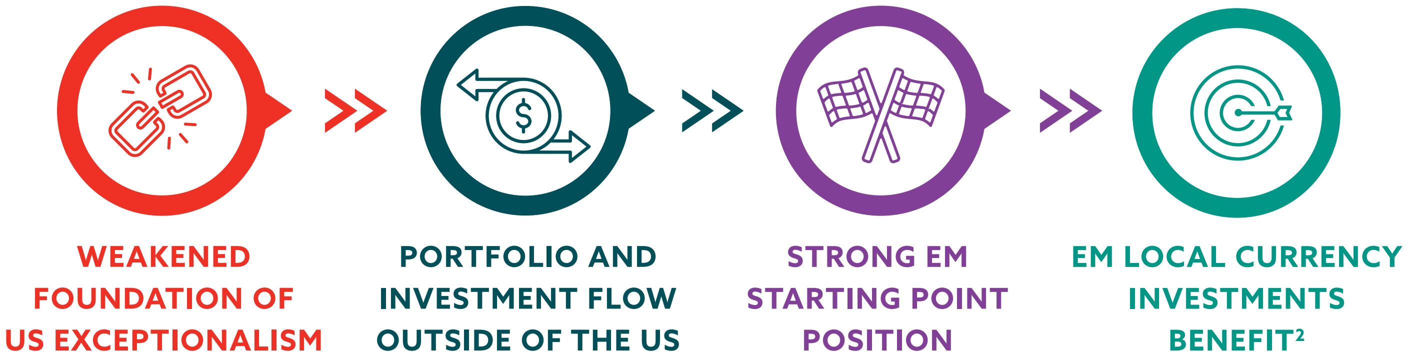
EM LOCAL CURRENCY ASSETS HAVE OUTPERFORMED IN 2025[1]



As of 12 June 2025. Unless otherwise stated, the information presented has been prepared from market observations and other sources believed in good faith to be reliable. Information and opinions expressed by PPM are current as of the date indicated and are subject to change without notice. Past performance is no guarantee of future results. Forward-looking statements are subject to uncertainties that could cause actual developments and results to differ materially from the expectations expressed.

(1) Bloomberg. EM Local Currency Bonds, EM Local Currency Supranationals, EM Hard Currency Frontier, EM Hard Currency Bonds, US HY, US Agg, US IG Corporates and US Equities as represented by the J.P. Morgan GBI EM Global Diversified Index, the ICE Broad Local Currency EM Supranational Index, the J.P. Morgan Next Generation Markets Index, the J.P. Morgan EMBI Global Diversified Index, the Bloomberg US Corporate High Yield Index, the Bloomberg US Aggregate Index, the Bloomberg US Corporate Index and the S&P 500 Index, respectively. Year-to-date performance as of 31 May 2025.

EM economies have had to commit to policy orthodoxy in the face of stiff global headwinds, given the combined effect of a commodity price shock, a Fed hiking cycle, and weakness in both the European and Chinese economies since 2022. As a result, a diverse core of EM countries is favorably positioned to sustain growth levels despite the macroeconomic uncertainty. While we would be cautious to frame this as a direct parallel to the post-GFC euphoria for EM growth prospects (and EM assets), we still believe EM will net-benefit from the weakened foundations underpinning US (market) exceptionalism. That should imply portfolio flows begin to look for a home outside the US, translating into a weaker US dollar and stronger EM currencies.



Choosing the most efficient way to access EM foreign exchange (FX) markets will likely prove crucial to getting this cyclical local markets trade "right." EM local currency supranational bonds have a number of features that help underpin an attractive risk-reward proposition. These include a greater potential to diversify FX exposures (including into more idiosyncratic, less-correlated stories), AAA ratings and a similar carry/total return profile to EM local currency sovereign bonds. Supranational issuances also have a few key features that can help mitigate risks and further optimize portfolios.

UNIQUE BENEFITS OF SUPRANATIONAL ISSUANCE

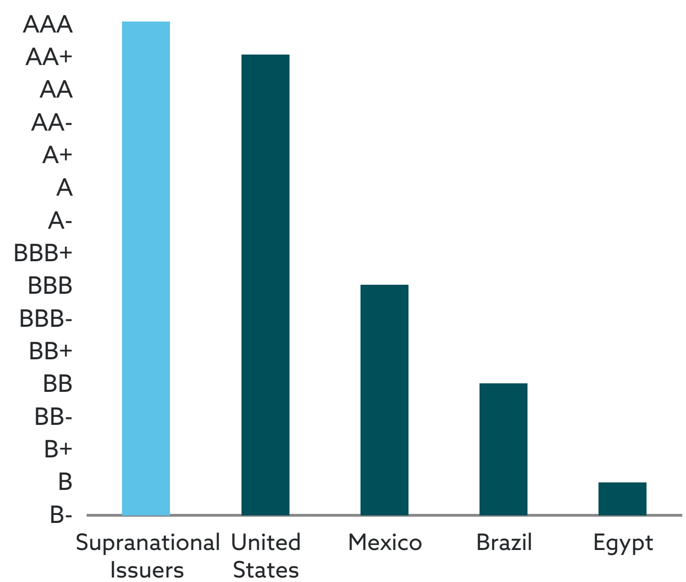
Credit Quality: Superior credit quality is one of the major benefits of EM currency supranational issuance. The vast majority of issuance from this segment is via AAA rated issuers such as the World Bank, Asia Development Bank and The European Bank for Reconstruction & Development. High-quality member countries, robust capitalization ratios and preferred creditor status (i.e., issuers get paid back first before other senior creditors) are key drivers behind the strong credit ratings. For those supranational issuers where the US is a participant, we expect these important credit dynamics to support the overall credit quality and ratings of these issuers despite the recent downgrade of US debt by Moody's.

Convertibility: History has shown that some EM countries have shut down their capital accounts during periods of volatility, essentially trapping offshore investors. However, supranational issuance is unique in the fact that there is a framework embedded in the bond documentation where investors have access to their money/investments in the event that a sovereign places capital controls on onshore investors.

Settlements: Supranational issuance is settled offshore in major clearing houses such as Euroclear. The securities can be structured in a fashion where coupons and amortizations are paid in US dollars at the prevailing reference exchange rate. As a result, there is no need for local cash and custody accounts.

Tax Efficiency: Since supranational issuance is traded offshore, settled offshore and coupons/amortizations are paid offshore, no local withholding or transaction taxes are associated with the investments.

SUPRANATIONAL ISSUERS ARE AMONGST THE HIGHEST-RATED ISSUERS GLOBALLY[3]



(2) The information presented is for illustrative purposes only and is not intended to be relied upon as a prediction or forecast of actual future events or performance, guarantee of future results, recommendation or advice. Opinions expressed herein are current as of the date indicated and are subject to change without notice. (3) J.P. Morgan. 30 April 2025.

Governing Law: Supranational issuance is typically governed under the auspices of New York or English law. The legal framework governing this issuance is well understood and time-tested. On the contrary, there are examples of local law issuance having maturity dates and coupons unilaterally changed at the discretion of the issuing country upon a simple vote in Congress. Investors in these securities had little recourse but to accept the new, inferior terms.

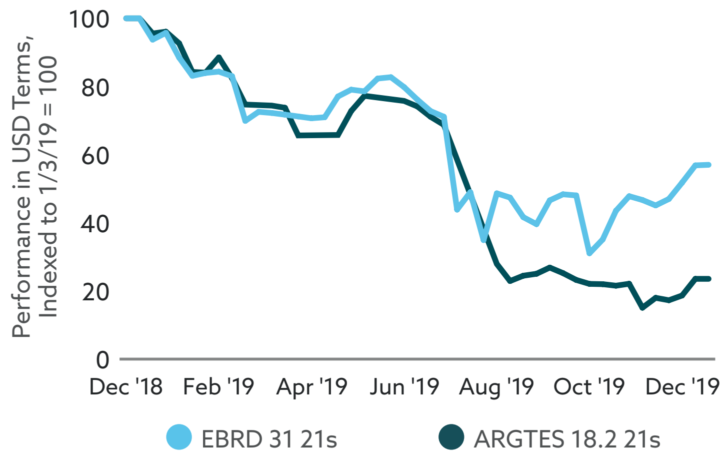
Governance and Sustainability: Supranational issuers are amongst the most highly-regulated issuers globally. Use of proceeds are clearly defined and are often used to maximize development goals while having positive impacts on the broader population via growth and environmental improvements. Many supranational bonds are issued in sustainable or other ESG-friendly formats. Sovereign issuance, on the other hand, often funds broader budget needs which have little transparency on the use of proceeds.

Customization: Supranational issuance is highly customizable by currency, maturity, coupons (zeros available), fixed/floating rates and callability. These features allow for targeted portfolio solutions to match investment views.

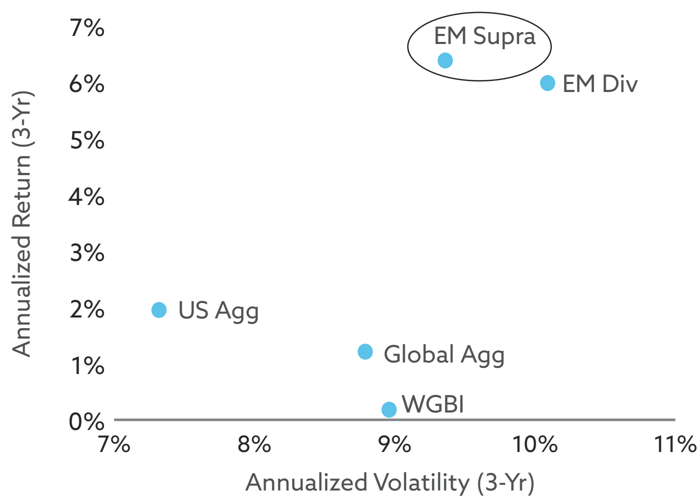
RISK, RETURNS AND CORRELATION COMPARISON

Despite headwinds from a strong US dollar in recent years, a basket of EM local currency bonds (as represented by the ICE Broad Local Currency EM Supranational Index) has outperformed traditional local currency and global strategies. The shorter duration profile of these securities enables investors to take advantage of carry without adding interest rate duration embedded in common indices. With a low correlation relative to other asset classes, EM currency supranational strategies have the potential to be a diversification element which mitigates portfolio risk while adding to potential returns.

SUPRANATIONAL ARS INVESTORS FARED BETTER THAN LOCAL BOND INVESTORS[4]



EM CURRENY RISK/RETURN METRICS COMPARE FAVORABLY[5]



LOW CORRELATIONS ALLOW FOR BROADER PORTFOLIO OPTIMIZATIONS[6]

	US Equities	US Agg	US Credit	US HY	EM HC Sov	EM LC Sov	EM LC Supra	WGBI
US Equities	1.00							
US Agg	0.68	1.00						
US Credit	0.73	0.99	1.00					
US HY	0.88	0.76	0.81	1.00				
EM HC Sov	0.80	0.86	0.90	0.86	1.00			
EM LC Sov	0.57	0.81	0.83	0.65	0.85	1.00		
EM LC Supra	0.63	0.78	0.82	0.69	0.85	0.96	1.00	
WGBI	0.65	0.95	0.94	0.75	0.84	0.89	0.87	1.00

(4) Bloomberg. As of 27 December 2019. (5) Bloomberg. US Agg, Global Agg, EM Supra and EM Div as represented by the Bloomberg US Aggregate Index, the Bloomberg Global Aggregate Index, the ICE Broad Local Currency EM Supranational Index and the J.P. Morgan GBI EM Global Diversified Index, respectively. WGBI is the FTSE World Government Bond Index. As of 30 April 2025. (6) Bloomberg and PPM. Three-year correlations through 30 April 2025. US Equities, US Agg, US Credit, US HY, EM HC Sov, EM LC Sov, EM LC Supra as represented by the S&P 500 Index, the Bloomberg US Aggregate Index, the Bloomberg US Credit Index, the Bloomberg US Corporate High Yield Index, the J.P. Morgan EMBI Global Diversified Index, the J.P. Morgan GBI EM Global Diversified Index and the ICE Broad Local Currency EM Supranational Index, respectively. WGBI is the FTSE World Government Bond Index.

CHARACTERISTICS OF AN EM LOCAL CURRENCY SUPRANATIONAL PORTFOLIO

Yields: Yields are competitive with high yield-rated asset classes around the world including US HY and EM Frontier sovereigns. Pending market conditions, supranational yields can be higher than those of domestic bonds despite the aforementioned more attractive characteristics.

Duration: A portfolio of EM currency supranational bonds is typically shorter duration than other fixed income indices. The shorter duration portfolio helps reduce volatility emanating from the rates component relative to other local market indices.

Currencies: EM currency supranational portfolios typically have more currency exposures than traditional EM indices as capital account restrictions are not a hurdle for this type of investment.

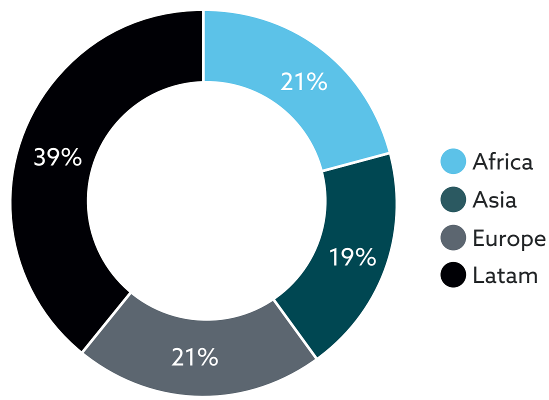
HIGH YIELDS, SHORTER DURATIONS AND HIGH CREDIT QUALITY ARE ATTRACTIVE MODEL PORTFOLIO ATTRIBUTES[7]

MODEL PORTFOLIO FOR EM LOCAL CURRENCY SUPRANATIONALS

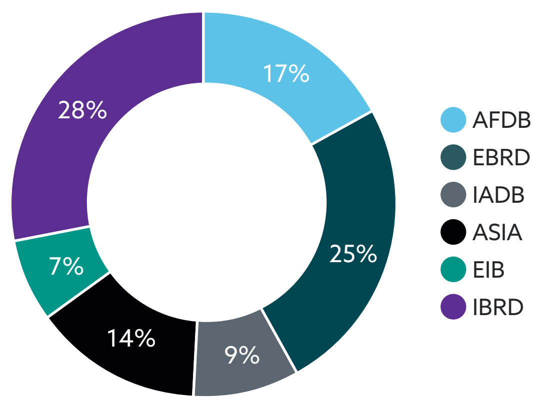
Portfolio Summary	
Currencies (#)	22
Yield (%)	10.13
Duration (yrs)	3.14
Average Rating	AAA

Currency Breakdown	Market Value (%)
INR	10.00
IDR	9.00
BRL	8.00
MXN	8.00
ZAR	8.00
COP	7.00
UYU	6.00
CLP	5.00
HUF	5.00
PLN	5.00
Other	29.00
Total	100.00

REGIONAL BREAKDOWN



ISSUER BREAKDOWN



(7) As of 13 May 2025. Information is representative of a specific account and may vary. The portfolio characteristics are provided solely for informational purposes and could vary substantially from that of a particular separately managed account or other mandate.

BACKGROUND INFORMATION ON SUPRANATIONAL ISSUERS

Supranational issuers are multilateral institutions which promote economic growth, development and regional integration amongst member countries. These issuers raise capital in both developed world currencies (e.g., the US dollar and euro) and EM currencies (e.g., the Egyptian pound, Brazilian real and Indian rupee) to fund their borrowing programs. EM currency borrowings may be used to fund local projects or, alternatively, swap back into hard-currency to fund broader lending needs. Supranational issuers view funding in EM currencies as an attractive avenue to further diversify their funding base. EM currency supranational investing has become increasingly popular in recent years due to the advantages described above.

EXAMPLES OF SUPRANATIONAL ISSUERS

Issuer	Ticker	Composite Ratings[8]
International Finance Corp	**IFC**	AAA
International Bank for Reconstruction & Development	**IBRD**	AAA
European Bank for Reconstruction & Development	**EBRD**	AAA
Asian Development Bank	**ASIA**	AAA
European Investment Bank	**EIB**	AAA

UNITED STATES PARTICIPATION IN SUPRANATIONAL ISSUERS

The US is a key shareholder in the world's largest multilateral development banks (MDBs), which are generally the most meaningful issuers of supranational debt. Given the current US administration's reticence toward multilateralism, the durability of these institutions' AAA ratings in a world in which the US withdraws its membership from MDBs has been a frequent focus for the market. During April's International Monetary Fund (IMF)/World Bank spring meetings, the US position was clarified, to some extent, via comments from Treasury Secretary Scott Bessent. He acknowledged the important roles that the IMF and MDBs play in the global financial architecture, while indicating the need to "reform" certain practices to better align with shareholder interests.

While we would expect the benefits noted by Secretary Bessent to anchor US support for these institutions over time, it is important to point out that the creditworthiness of these institutions does not depend entirely (or, in some cases, even materially) on the US's participation, given a multitude of other shareholders, strong capitalization ratios, preferred creditor status, and growing access to differentiated forms of private capital (including hybrid capital). The case study provided by the UK post-Brexit, in which it left the European Investment Bank, is instructive in this regard, with other members increasing capital positions to offset the UK's withdrawal. Moody's also observed recently that the process of US withdrawal would be quite protracted, given ongoing financial liability for loans extended prior to a (theoretical) withdrawal date. All of this supports a generally constructive outlook on the likely trajectory of supranational ratings, with or without the US.

(8) Moody's, Standard & Poor's and Fitch.

ABOUT PPM AMERICA

Our mission is to be seen by clients and their advisors as a consistently reliable partner to help them achieve their long-term value goals.

PPM is a US-based institutional asset manager with $80.22 billion in assets under management as of 31 March 2025.[9] Established in Chicago in 1990, PPM exists to consistently support institutional clients in achieving their long-term value goals. We offer our Midwestern mentality of hard work, straight talk, full transparency and humility. Our success is supported by a team-based culture that encourages debate, collaboration and consistency. At the center of our belief is the fact that our best ideas to date have and can come from any team member anywhere in our firm. We believe the success of our investment culture is best demonstrated by the strong retention of our clients and investment professionals.

(9) AUM includes committed but unfunded capital for PPM's private equity and commercial real estate businesses. AUM includes both securities issued by PPM CLO vehicles held by PPM separately managed account clients and the underlying collateral assets of the CLO vehicles managed by PPM.

The **Bloomberg Global Aggregate Index** provides a broad measure of global investment grade, fixed rate bonds. The three major components of this index are the US Aggregate, Pan-European Aggregate and the Asian-Pacific Aggregate indices. It also includes Eurodollar and Euro-Yen corporate bonds, Canadian government, agency and corporate securities, and USD 144A securities.

The **Bloomberg US Aggregate Index** provides a broad measure of fixed- and floating-rate USD-denominated debt issued from sovereign, quasi-sovereign and corporate EM issuers.

The **Bloomberg US Corporate Bond Index** measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD-denominated securities publicly issued by US and non-US industrial, utility and financial issuers.

The **Bloomberg US Corporate High Yield Index** covers the universe of fixed rate, non-investment grade debt. Eurobonds and debt issues from countries designated as emerging markets (sovereign rating of Baa1/BBB+/BBB+ and below using the middle of Moody's, S&P and Fitch) are excluded, but Canadian and global bonds (SEC registered) of issuers in non-EMG countries are included.

The **Bloomberg US Credit Index** measures the investment grade, US dollar-denominated, fixed-rate, taxable corporate and government related bond markets. It is composed of a corporate component and a non-corporate component that includes foreign agencies, sovereigns, supranationals and local authorities.

The **FTSE World Government Bond Index** provides a measure of the performance of fixed-rate, local currency, investment-grade sovereign bonds from over 20 countries, denominated in a variety of currencies.

The **ICE Broad Local Currency EM Supranational Index** tracks the performance of local currency emerging markets debt from supranational issuers issued in the international markets.

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The **J.P. Morgan EMBI Global Diversified Investment Grade Index** tracks liquid, US dollar, investment grade emerging market fixed and floating-rate debt instruments issued by sovereign and quasi-sovereign entities.

The **J.P. Morgan GBI EM Global Diversified Index** tracks the performance of local currency debt issued by emerging market governments, whose debt is accessible by most of the international investor base.

The **J.P. Morgan Next Generation Markets Index** tracks the performance of smaller emerging countries of lesser credit quality that are not a European Union member or engaged in the process of seeking EU membership.

The **S&P 500 Index** provides a broad, market capitalization-weighted measure of US large cap stocks. It includes approximately 500 publicly-traded stocks of the largest US companies.

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Unless otherwise indicated, the portfolio(s) ratings calculations presented herein have been calculated using the same rating methodology as the portfolio(s) respective benchmark(s). Additional information is available upon request.

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