

# Investment Grade Emerging Market Debt for General Account Clients

EMERGING MARKET DEBT INSIGHTS – MARCH 2025



**MARK HUGHES, CFA**  
Co-Head of Emerging Market Debt, Portfolio Manager

At PPM, we see an elegant solution to General Account (GA) portfolios seeking capital-efficient yield enhancement without giving up liquidity or transparency – Investment Grade (IG) rated Emerging Market (EM) public debt. This segment of the EM universe allows an opportunity for a significant pick-up over comparable US corporate credit allocations with all-in yield and spread levels similar to those attainable in the IG Private Credit space. Counterintuitively, this income pick-up is generated with a risk, volatility, impairment and capital charge profile similar to, if not better than, US corporate credit opportunities.



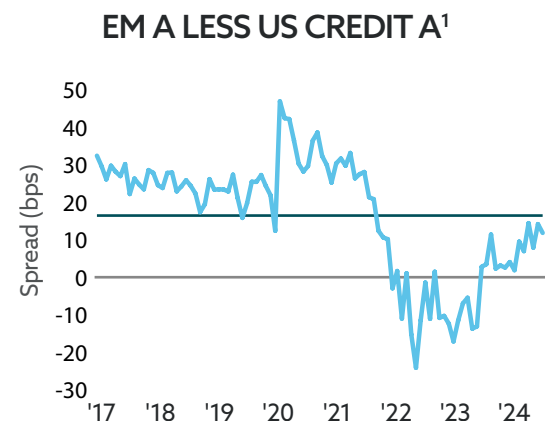
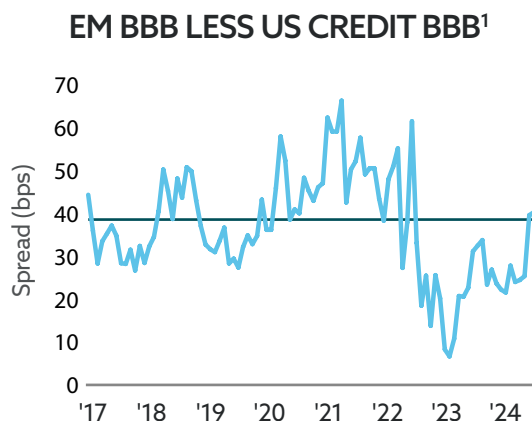
**KEVIN RITTER, CFA**  
Co-Head of Emerging Market Debt, Portfolio Manager

We think that is primarily due to home bias within large pools of assets in the developed world. While we understand concerns regarding EM vulnerabilities to geopolitical and global trade policies, those concerns generally do not distinguish between the IG and lower-rated segments of the EM universe, where the buffers available to shield against macro shocks are vastly different. The track record in recent years bears this out: many IG EM sovereign and corporate issuers have navigated successive external shocks in the form of COVID, regional wars, commodity price volatility, inflation spikes and a sustained tightening of global financial conditions without the incidence of a textbook 1990's style "EM crisis."

We believe this disconnect has created an attractive risk-return opportunity in the IG EM space. Furthermore, PPM's deep fundamentals-based credit teams work to identify vulnerable issuers and further insulate portfolios from potential volatility. In our view, we find the risk-return opportunities in the IG EM opportunity set compelling and are currently adding exposures to client portfolios.

## INCOME PICK-UP: THINK BEYOND THE INDEX TO DOUBLE THE US SPREAD

As the charts below demonstrate, there is a structural premium in EM when comparing like-for-like credit buckets relative to US corporate credit. We believe this premium alone is attractive and withstands scrutiny when normalizing for risk/volatility and impairments (more below). Perhaps not as straightforward has been the evolution of the EM indices, which skew headline index valuations tighter versus US corporate credit and obfuscate some of the best value in the sector. For example, prolific issuance from highly-rated issuers in China and the GCC (Gulf Cooperation Council) has caused material regional and country re-weightings of the indices. These issuers typically trade much tighter within the EM landscape due to the deep pockets of domestic investors. As a result, some of the best values in the EM sector may be passed over by investors simply looking at index levels.



As of 3 March 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. Monthly data through December 2024. Spreads of the A and BBB segments of the Bloomberg Emerging Markets USD Aggregate Bond Index and the Bloomberg US Credit Index. Teal lines are averages.

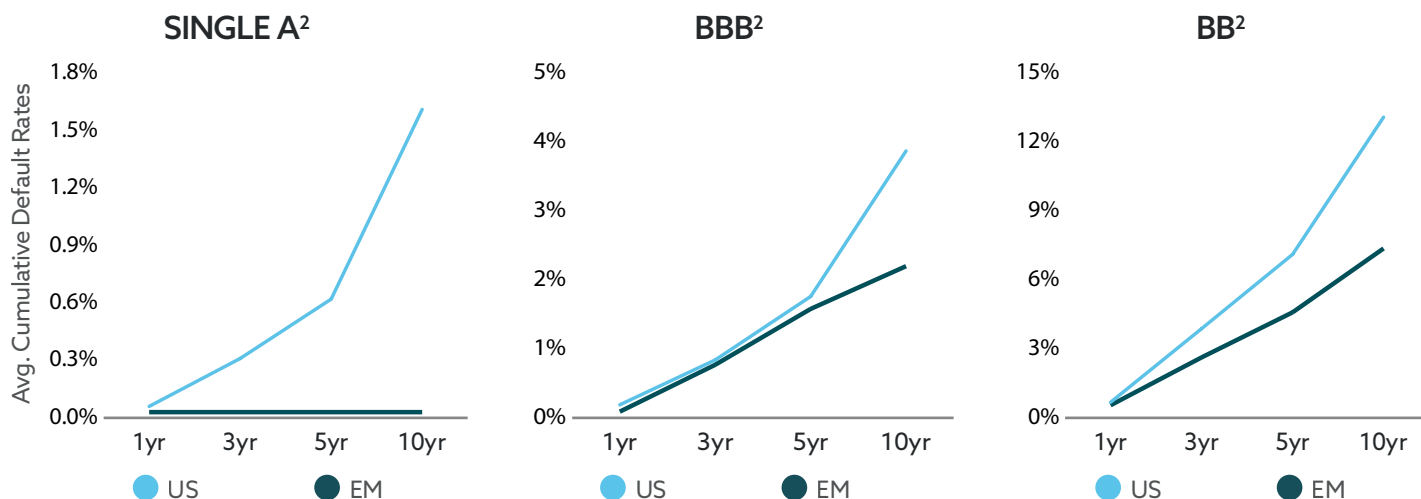
At PPM, we are taking advantage of these EM index idiosyncrasies. We have constructed a capital-optimized portfolio with geographic, sector and issuer diversification, which we believe can materially increase spreads/yields relative to popular index measures of valuation. As seen in the appendix, PPM's EM GA model portfolio essentially doubles the US index spread and is comparable to US IG Private Credit yields and spreads.

### COUNTERINTUITIVELY, HISTORICAL RISK METRICS SUGGEST EM COMPARES SIMILARLY TO US CORPORATE CREDIT

If the EM yield pick-up is straightforward and generally required by investors, many market participants may be surprised to learn the EM risk profile compares similarly to, if not favorably to, US credit. When discussing risk,

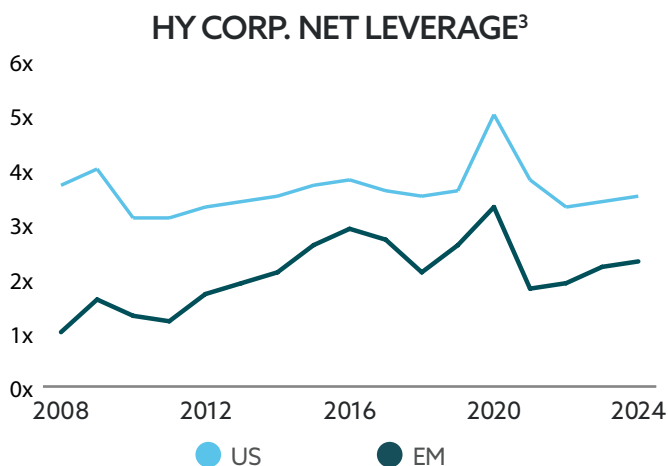
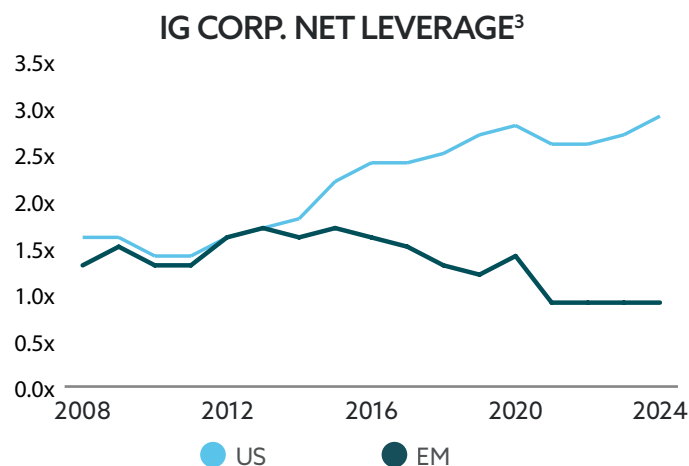
we note that GA clients typically focus on impairments (defaults), rating migrations and drawdown/volatility. We discuss each of these metrics in detail below:

**Impairments:** Periodically, the rating agencies release ex-post analyses detailing default metrics across their coverage universe, which allow for cross-sector comparison of trends. The charts below show S&P's cumulative default rates from 1981 to 2023 for EM and US by credit buckets. For example, S&P adds up and averages all of the defaults by issuers previously rated BBB and buckets the defaults according to the year of the credit event (1yr, 3yr, 5yr or 10yr). As the chart shows, cumulative 10yr default rates were higher for US issuers initially rated BBB at 3.87% relative to EM issuers at 2.20%.



As you can see from the charts above, there is a clear trend where EM default rates have been lower than that of US corporate credit comparables. We believe within the single A space the EM outperformance is likely due to the fact there are fewer EM issuers for which to compare relative to the US. However, the outperformance in the BBB and BB buckets is notable and we believe there are EM-specific factors which contribute to this dynamic. One, EM issuers tend to run more conservative balance sheets

than US peers with outsized cash positions (charts below). The cash positions mitigate liquidity crunches for these issuers which can be brought on during times of sovereign stress. Two, and unlike the US, there is likely less industry competition for many of these issuers. Industry dynamics in EM tend to be oligopolistic and allow for further balance sheet flexibility as a result. These dynamics have likely led to slightly better EM performance as measured by cumulative default rates comparing EM and US buckets.



(2) Standard & Poor's. "Default, Transition and Recovery: 2023 Annual Global Corporate Default and Rating Transition Study." 28 March 2024.

(3) J.P. Morgan. As of 30 September 2024.

**Rating Migrations:** The table below shows Moody's average 1yr rating transitions in EM and Advanced Economies from 1995 to 2023. Although there is some variation in the data, the 1yr rating changes in EM and Advanced Economies were very similar. Take for example the Baa bucket. From a historical perspective, EM Baa issuers retained the same ratings 88.21% of the time over a 1yr time horizon, which is within 0.9% of the Advanced Economies metric. A move to the Ba bucket

happened just over 1% more often than in the Advanced Economies at 3.82% vs 2.64%. Although EM rating migrations have been slightly elevated in the Baa bucket, there has been EM outperformance in A and Ba buckets relative to Advanced Economies. Regardless, and as the differences are small, we conclude the historical 1yr ratings evolution between EM and Advanced Economies to be relatively similar without a distinct advantage for one asset class over the other.

#### EM VS. ADVANCED ECONOMY RATING PROGRESSIONS<sup>4</sup>

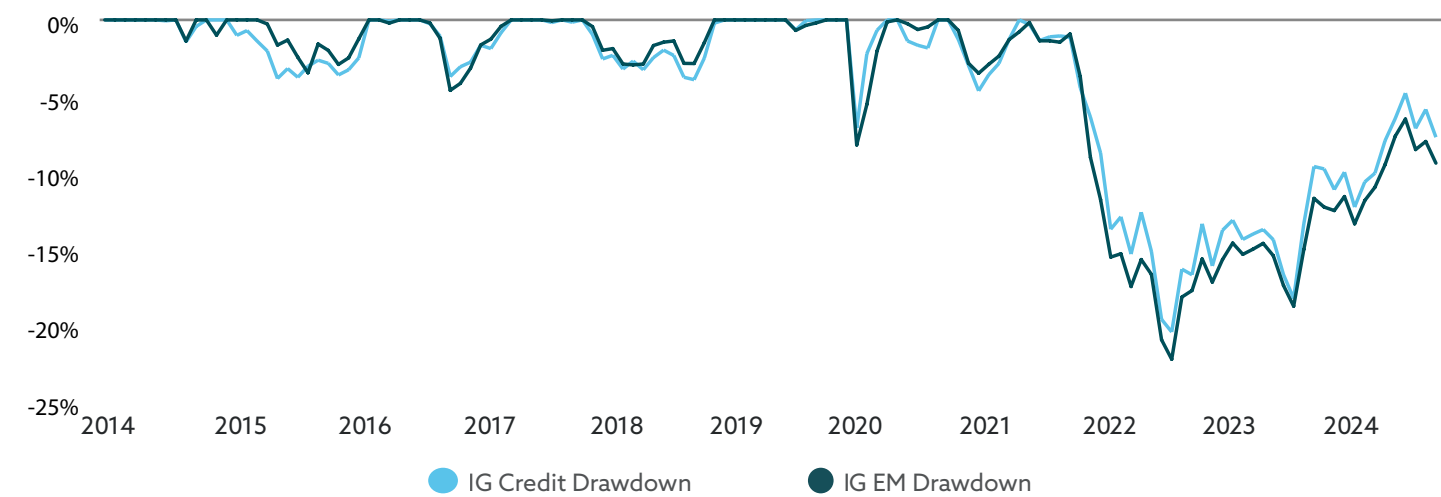
Emerging Markets									
From/To	Aaa	Aa	A	Baa	Ba	B	Ccc-C	WR	Default
Aaa	84.21%							15.79%	
Aa		79.35%	16.56%					4.10%	
A		0.51%	89.95%	4.83%	0.21%	0.42%	0.02%	4.06%	
Baa			1.42%	88.21%	3.82%	0.23%	0.05%	5.88%	0.39%
Ba			0.18%	3.69%	77.14%	6.72%	0.94%	10.34%	0.99%
B			0.08%	0.22%	5.44%	69.97%	9.24%	11.15%	3.91%
Ccc-C				0.02%	0.39%	5.92%	59.65%	16.94%	17.09%

Advanced Economies									
From/To	Aaa	Aa	A	Baa	Ba	B	Ccc-C	WR	Default
Aaa	86.75%	6.77%	0.46%	0.11%	0.13%	0.02%		5.77%	
Aa	0.58%	86.49%	8.04%	0.50%	0.07%	0.02%		4.30%	
A	0.02%	0.91%	88.73%	5.69%	0.28%	0.06%	0.04%	4.23%	0.03%
Baa	0.01%	0.03%	2.41%	89.10%	2.64%	0.56%	0.16%	5.02%	0.07%
Ba		0.02%	0.13%	6.07%	76.21%	7.13%	0.86%	9.18%	0.40%
B		0.01%	0.07%	0.30%	4.33%	73.58%	8.22%	11.30%	2.18%
Ccc-C		0.01%	0.00%	0.03%	0.14%	4.83%	73.22%	13.95%	7.81%

**Drawdown:** Furthering the risk discussion, we examined drawdowns between IG EM and US IG credit and reached similar comparative risk conclusions. From our observations, there are periods of IG EM outperformance

and there are periods of US IG credit outperformance. However, in aggregate the drawdowns are of similar scale and do not suggest a benefit of one asset class over the other.

IG EM AND US IG HISTORICAL DRAWDOWNS<sup>5</sup>

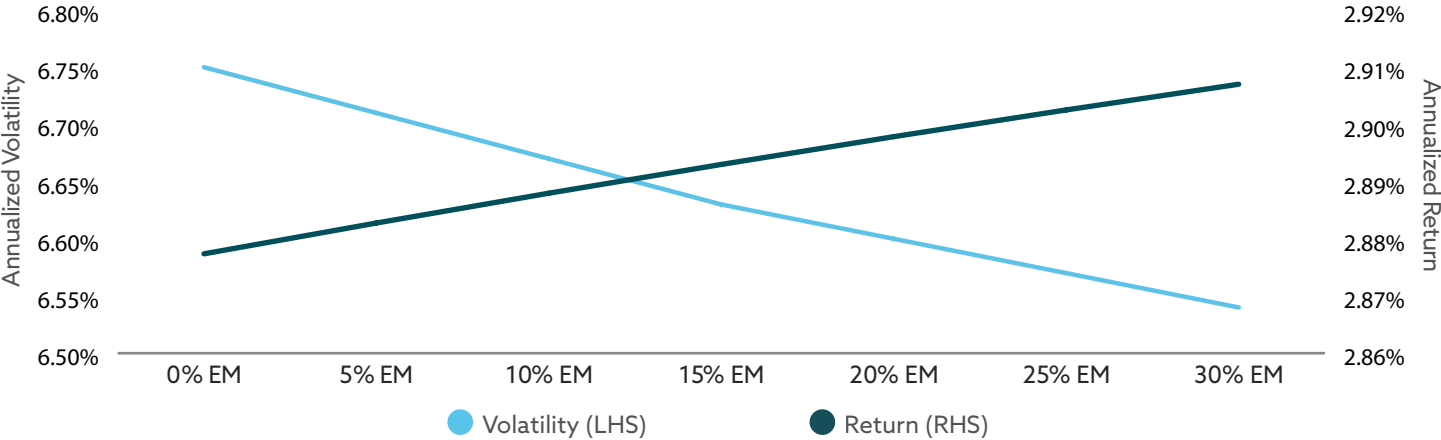


In conclusion, our broad assessment of risk metrics suggests that there does not appear to be a discernible difference between EM and US credit buckets. Said differently, the rating agencies appear to be “doing their job” as a rating is merely a combination of probability and time to default. The analysis above suggests the rating agencies are consistent and accurate in their treatment of these two credit sectors. As portfolio managers, analysts, traders and risk managers, it is our job to navigate market cycles in the sector, optimizing opportunities and avoiding defaults (the key to EM investing).

**WHERE DOES EM FIT IN A BROADER GA ALLOCATION?**

At PPM, we view IG EM as an extension of the US corporate credit allocation with the added benefits of yield enhancement, increased issuer diversification and broader portfolio optimization. Adding IG EM to a GA allows for additional diversification without sacrificing income. Separately, there is a broader portfolio construction argument for combining an EM allocation with US credit. EM’s higher yields and similar risk profile can increase returns and yields while lowering overall portfolio volatility. The chart below demonstrates this efficient frontier approach via combining EM and IG allocations over the past 10yrs. In our view, this 10yr period shows ample market cycles in both EM and the US and clearly demonstrates the broader portfolio fit for EM.

IG EM ALLOCATION COMBINED WITH US CREDIT<sup>6</sup>

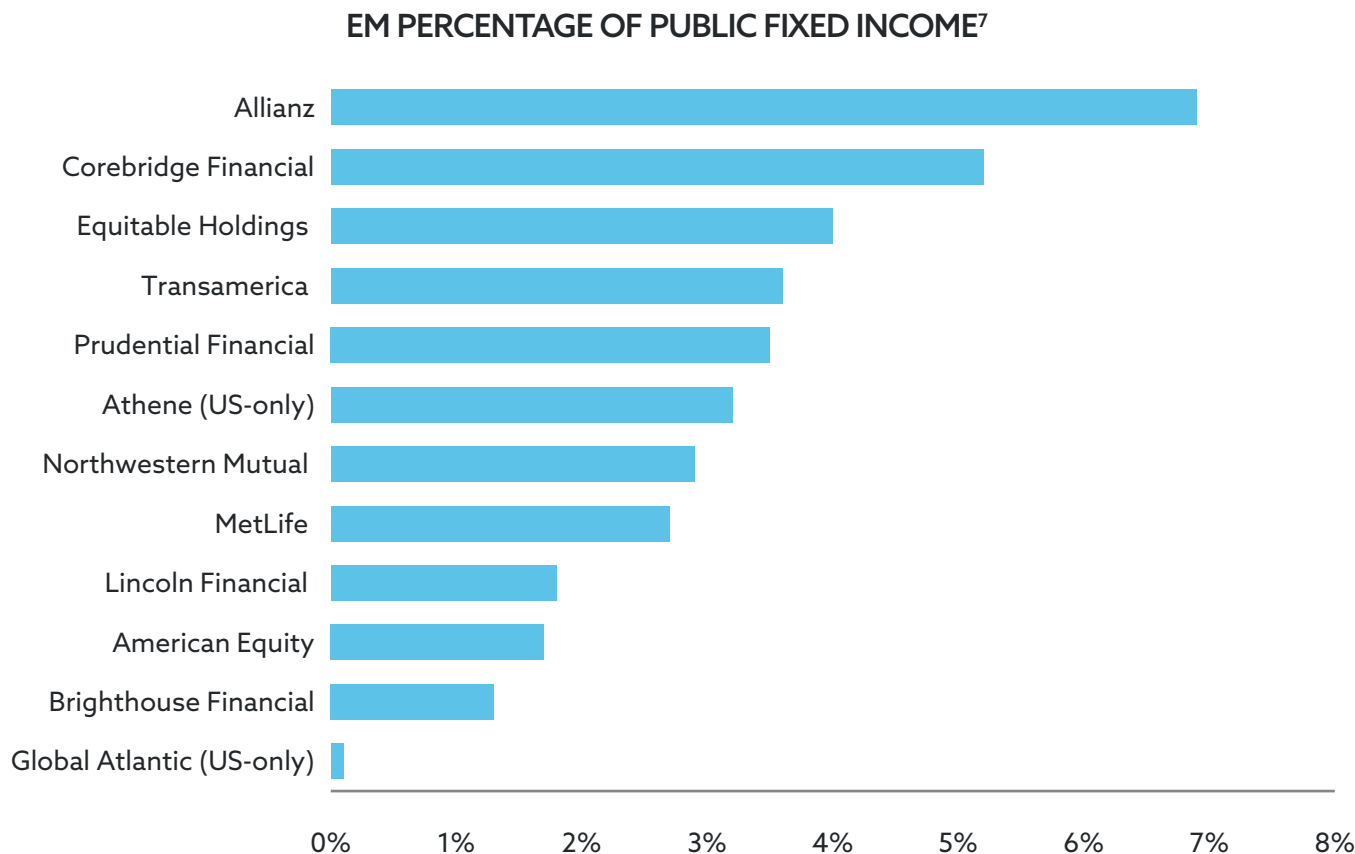


(5) Bloomberg, J.P. Morgan. Historical drawdowns calculated by PPM. Monthly data through 31 December 2024. The EM component constitutes 50% of the J.P. Morgan EMBI Global Diversified Investment Grade Index and 50% of the J.P. Morgan CEMBI Broad Diversified Investment Grade Index. The US component is the Bloomberg US Corporate Bond Index. (6) Bloomberg, J.P. Morgan. Annualized volatility and returns calculated by PPM. As of 31 December 2024. The EM allocation constitutes 50% of the J.P. Morgan EMBI Global Diversified Investment Grade Index and 50% of the J.P. Morgan CEMBI Broad Diversified Investment Grade Index. The US allocation is the Bloomberg US Corporate Bond Index. The information presented is for illustrative purposes only.

## WHAT ARE PEERS DOING?

Our analysis of the peer set suggests a bifurcation of EM exposures. Larger peers with broad investment teams have been enjoying EM allocations for 10+ years. Meanwhile, there is a significant portion of the peer set that has yet to take advantage of the attractive IG EM risk-reward proposition. PPM made the strategic decision

to develop an EM platform to not only benefit the GA of our parent company, Jackson Financial, Inc. (JFI), but also because we suspect other peers will follow either by hiring external managers or, if feasible, increasing in-house EM capabilities. Regardless, we expect EM GA allocations to increase in the coming periods.



## WHY PPM?

PPM is owned by JFI who is committed to helping clarify the complexity of retirement planning—for financial professionals and their clients. Through its range of annuity products, financial know-how, history of award-winning service<sup>(8)</sup> and streamlined experiences, JFI strives to reduce the confusion that complicates retirement planning. The EM team and broader PPM investment platform gain significant perspective and insight managing GA assets on behalf of Jackson National Life Insurance Company (Jackson), a wholly-owned subsidiary of JFI.

In addition, capital from the Jackson GA allows the team to further optimize insurance solutions which can be offered and applied to third-party relationships. For example, the EM team is able to offer EM private debt solutions for clients made possible via the in-house private debt expertise at PPM. Furthermore, the EM team at PPM has 15+ years of experience managing dedicated EM GA assignments and specializes in customization with direct interaction with GA investment personnel. We believe this “extension of staff” service fosters communication and understanding, which in turn further optimizes outcomes.

(7) SNL. As of 31 December 2023, the latest available. The source used J.P. Morgan country list to tag emerging markets. (8) SQM (Service Quality Measurement Group) Call Center Awards Program for 2004 and 2006-2023. (Criteria used for Call Center World Class FCR Certification is 80% or higher of customers getting their contact resolved on the first call to the call center (FCR) for 3 consecutive months or more.)

## APPENDIX<sup>9</sup>

### MODEL PORTFOLIO

Portfolio Level		Industry Breakdown	Weight
Yield to Worst (%)	6.19	Energy	21.79%
OAS (bps)	169	Government	21.19%
Duration (years)	7.73	Utilities	17.01%
Avg. Ratings	BBB	Basic Materials	16.12%
IG %	81.20%	Industrial	7.76%
Below IG %	18.80%	Financial	6.57%
Avg. Price	92.59	Consumer Non-Cyclical	5.37%
		Communications	3.58%

NAIC Buckets	Weight	Yield (%)	OAS (bps)	Duration (years)	ICE US Index OAS (bps)
NAIC 1	19.70%	5.88	129	11.06	68
NAIC 2	61.49%	6.12	162	7.57	101
NAIC 3	18.81%	6.76	236	4.78	166

**EM Sovereigns versus EM Corporates:** Our preferred GA allocations typically have a 70% to 80% skew toward EM Corporate exposures over EM Sovereign (Industry Breakdown above shows the EM government allocation). EM Corporates tend to have higher spreads than EM

Sovereign. In addition, corporate issuers, particularly exporters or multi-national companies, are better positioned to withstand sovereign-related shocks and can be rated higher than the sovereign ratings.

(9) As of 3 March 2025. Model portfolio was constructed at a point in time by PPM with data sourced from Bloomberg as of 31 January 2025. OAS shown are from the ICE BofA US Corporate Index. The information presented has been prepared for illustrative purposes only and is not representative of any client account. The portfolio characteristics are provided solely for informational purposes and could vary substantially from that of a particular separately managed account or other mandate.

## 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 \$74.42 billion in assets under management as of 31 December 2024.<sup>10</sup> Established in Chicago in 1990, PPM exists to consistently support institutional clients in achieving their

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The **Bloomberg Emerging Markets USD 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.

(10) 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.

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.

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 **ICE BofA US Corporate Index** provides a broad measure of the USD-denominated investment grade corporate debt securities publicly issued in the US domestic market.

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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.

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