

Emerging Markets Debt

KEY TAKEAWAY

> While history would suggest that recent macroeconomic developments bode poorly for emerging markets debt, the asset class has been resilient and offers diversification away from concentrated risks in US credit markets

The past 18 months have presented a challenging environment for global fixed income investors, with a range of inflationary shocks resulting in the market rapidly pricing in a new Fed hiking cycle. The ongoing increase in global yields has been somewhat mitigated by comparatively stable and tight credit spreads.

However, Fed hikes have historically been accompanied by tightening financial conditions and availability of capital, to which emerging markets (EM) are uniquely vulnerable. In the case of recent faster-than-expected Fed tightening cycles in 2018 and 2022, EM spreads widened and local currency bonds lost value as EM central banks were forced to hike, despite the unintended consequence of slower economic growth.

In contrast to this historical precedent, EM debt has held up well in the face of the unexpected developments of "Liberation Day" in April 2025 and the start of the Iran conflict in February 2026. As the chart below indicates, hard currency EM bonds have outperformed US investment grade and high yield bonds since the beginning of 2025.¹ In fact, many countries we perceive as more sensitive to financial conditions, including Argentina, Ecuador and Nigeria, have outperformed over this time frame.

Why is this time potentially different for EM debt? We would suggest that previous crises have prepared policymakers for current challenges. As an example, the intermittent 'closure' of capital markets for lower-rated EM issuers from 2022-24 pushed policymakers toward International Monetary Fund programs and a series of market-friendly stabilization reforms. Higher starting overnight rates at EM central banks also may require less of an adjustment in response to the current Fed hiking cycle.

While comparatively tight spreads across both EM and US credit markets can give buyers today pause, we believe core EM issuers offering robust yields in the 6-9% range still represent an attractive opportunity both in terms of income and total return. EM



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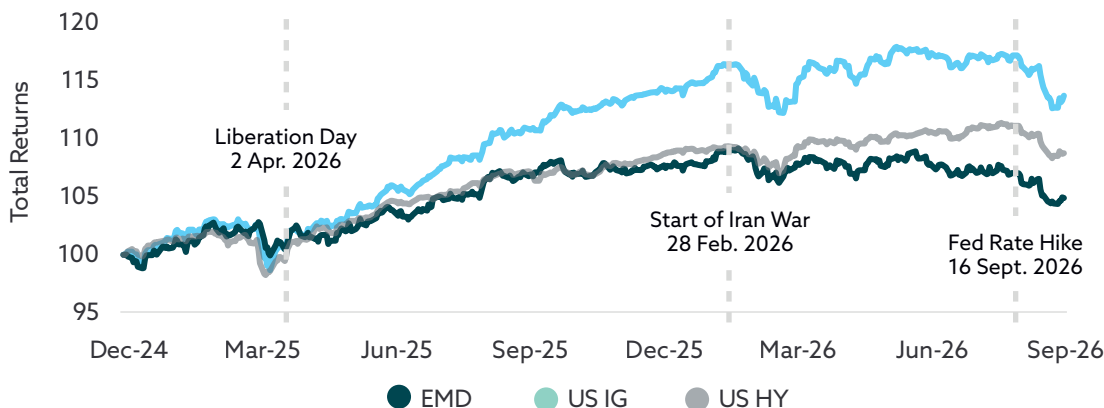


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EM DEBT HAS OUTPERFORMED US COUNTERPARTS DESPITE HEADWINDS¹



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debt also benefits from diversification away from the debt-funded AI capex cycle in the US, with nearly zero exposure to proliferating hyperscaler, data center or neocloud credits.

On the topic of investing in EM local currencies, we recommend taking a more nuanced approach given the pressure that US rate hikes and AI-fueled growth may continue to put on dollar appreciation. Here, we focus on idiosyncratic currencies with catalysts, such as the Nigerian naira and Kazakh tenge, likely to keep up with USD-based EM returns.

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The **J.P. Morgan EMBI Global Diversified Index** tracks liquid, USD-denominated emerging market fixed- and floating-rate debt instruments issued by sovereign and quasi-sovereign entities.

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