

## Investment Insight

### EMERGING MARKET CORPORATE DEBT: FOUR KEY QUESTIONS FOR 2026

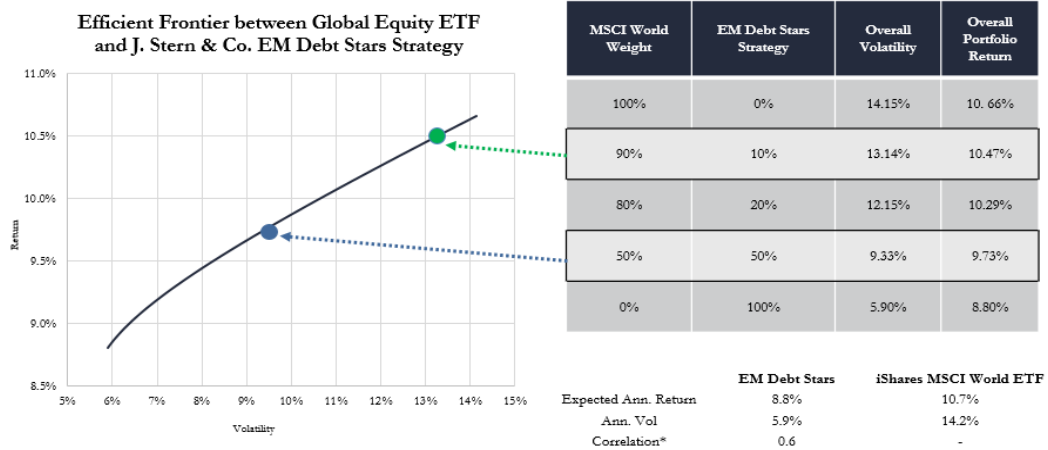
Emerging market ('EM') hard-currency corporate bonds, overlooked by many investors despite being almost twice as big as the US high-yield market (\$2.5trn v \$1.3trn), have held up remarkably well in a year of economic and political uncertainty. The asset class offers a compelling investment case today, with all-in yields, low volatility, and diversification benefits. It is an asset class that has matured over the past two decades. It now boasts over 1,000 companies in a broad range of sectors in over 60 countries, which supports this diversification. We examine the four key questions that investors are asking about this EMD sector for 2026.

Risk asset class returns	2025 YTD (USD)	2024 (USD)	2023 (USD)	2022 (USD)	2021 (USD)
<b>Global Equities</b>					
US equities (S&P 500)	17.8%	25.0%	26.3%	-18.1%	28.7%
Developed Market Equities (MSCI World NTR)	20.1%	18.7%	23.8%	-18.1%	21.8%
Emerging Market Equities (MSCI Emerging Markets NTR)	15.7%	14.7%	6.1%	-14.9%	4.9%
<b>Developed Market Fixed income</b>					
US Treasuries	6.7%	0.6%	4.1%	-12.5%	-2.3%
US Investment Grade	8.1%	2.8%	8.4%	-15.4%	-1.0%
US High Yield	7.8%	8.2%	13.5%	-11.2%	5.4%
<b>Emerging Market Fixed income</b>					
EM Hard Currency Sovereign	13.0%	6.5%	11.1%	-17.8%	-1.8%
EM Hard Currency Corporate	8.0%	7.6%	9.1%	-12.3%	0.9%

#### 1. DO YOU BELIEVE MULTI-ASSET PORTFOLIOS SHOULD HAVE A STRATEGIC ALLOCATION TO EMERGING MARKET CORPORATE DEBT IN 2026?

We have long recommended to our clients that they allocate strategically to emerging-market corporate debt (hard currency) because of the attractive returns and lower volatility this sub-asset class offers. As the chart below shows, a portfolio with 50% in EMD and 50% in equities reduces volatility while still generating returns that are only slightly lower than those of a 100% equity portfolio, but with a substantially lower volatility.

#### EM corporate debt reduces volatility without sacrificing returns



Source: Bloomberg, J. Stern & Co. and J.P. Morgan. As at 31st July 2025

\*Correlation has been calculated between iShares EM corporate ETF and iShares MSCI World ETF since 2012

The significant expansion of the EMD asset class over the past decade has provided active managers with a much larger pool of opportunities to apply their research and asset management skills. There has been a 50% increase in the number of bonds available and a 34% increase in the number of issuers. This is especially true for our investment style, which is focused on quality corporates and fundamental analysis, even if they are in challenging jurisdictions. Such bonds tend to yield more than they would in developed markets, despite the relative strength of their business models, balance sheets and cash flows. Our emerging market strategy has an income yield of 7.5% and a yield-to-maturity of 8.6% for a very short duration of 2.5 years. Volatility over the last five years has been 5.8%, lower than a developed market investment-grade bond portfolio.

## 2. HOW HAVE TARIFFS IMPACTED EM CORPORATE CREDIT?

Liberation Day on 2<sup>nd</sup> of April 2025 created significant uncertainty worldwide when President Donald Trump announced sweeping tariffs aimed at balancing trade deficits, promoting domestic manufacturing and protecting national security.

Emerging market corporate credit spreads (a proxy for credit risk) reacted sharply to the news. They widened by c. 25%, reflecting uncertainty about the new trade policy's impact on corporate performance. However, as the dust settled, with exemptions granted and various trade deals struck, credit spreads tightened back to pre-Liberation Day levels over the following four months and have continued to tighten. The spread compression has been a positive contributor to total returns of the asset class year to date, which stand at 8.0%.

The direct impact from tariffs has been modest so far, with most regions/sectors affected more indirectly through slower growth and currency volatility. From a regional perspective, Asia has been the most vulnerable, with China in the crosshairs of President Trump. Latin America is more complex with Mexico being the obvious target for tariffs. However, many companies are better placed than previously with share of non-US revenues having increased and established operations in the US which mitigates tariff risk. Central & Eastern Europe, Middle East and Africa have been the least vulnerable. There should be limited direct impact related to trade policy with Turkey being the only significant non-commodity exporter.

From a sector perspective, the key sectors to be impacted directly were industrials and metals & mining. The energy sector was also impacted by lower oil prices which are sensitive to growth and trade concerns.

### ***Industrials***

Industrials is the only sector where credit spreads have widened year to date, implying a deterioration in credit quality. Asian manufacturing companies that have direct exports to the US were most affected and the key contributor the spread widening.

From a portfolio perspective, our exposure to the sector is via companies such as *CEMEX*, a leading buildings material group. They have assets in the US which mitigate tariff risk. This has been confirmed by recent results which have highlighted the first quarterly sales growth since the first quarter of 2024. Management expects volumes to improve in Mexico and the US as governments accelerate infrastructure spend.

## Metals & Mining

There have been headline tariffs on steel, aluminium and other critical minerals. However the sector has been buoyed by strong gains across most base and precious metals. Gold prices have been strong, with investors seeking a flight to safety amid an uncertain macroeconomic environment. Meanwhile, copper and platinum-group metals (PGMs) benefited from favourable supply and demand dynamics. This strong commodity performance has benefited corporates in our portfolio, such as *Sibanye-Stillwater* (a PGM and gold miner in South Africa) and *First Quantum Minerals* (a copper miner in Zambia).

## Oil & Gas

Brent Crude oil dropped from c.USD 75 to USD 62 per barrel over the year as tariffs put up trade barriers, and oil demand decreased. This was compounded by increased global production. Despite the price pressure, oil and gas has been the top-performing sector in the asset class. There are a number of the high-quality companies with attractive yields and short duration, which have provided good income. In our portfolio, *Azule Energy*, an oil producer in Angola, is a good example. They have a strong balance sheet with leverage less than 1.0x and very low breakeven prices (operating cost to extract oil per barrel). This means they are still generating cashflow in the current environment and reducing risk on debt serviceability.

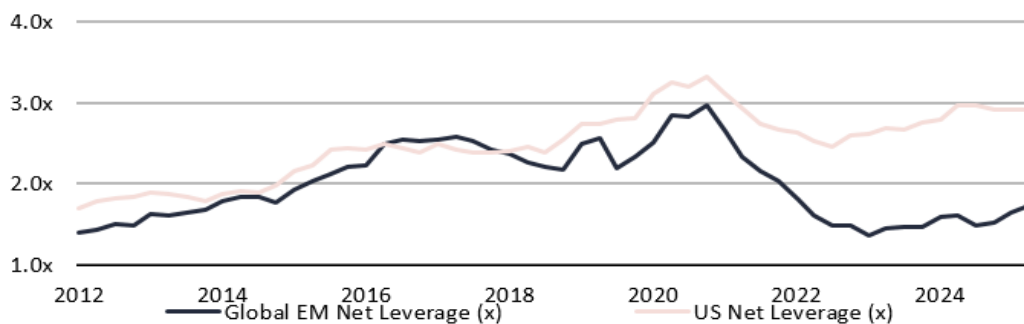
### 3. IS DEFAULT RISK PICKING UP ACROSS THE CORPORATE UNIVERSE?

With interest rates persisting at higher levels for longer than expected, markets have been surprised by unexpected defaults in the global corporate sector. This has made the headlines, particularly in US private credit, such as the bankruptcies of US companies *Tricolor* and *First Brand*. The question that has continued to haunt investors is whether we are at a late stage of the credit cycle and about to experience a pickup in default risk across the spectrum.

We generally tend to compare EM corporate default rates against US peers. However, in this insight we have also brought in some comparative analysis against developed market private debt sector to complete the picture.

Looking at the leverage metrics, both EM and US corporates have seen a marginal weakening in their debt-to-EBITDA ratio, albeit starting from a strong base. On a relative basis, EM corporates are less levered than their US counterparts.

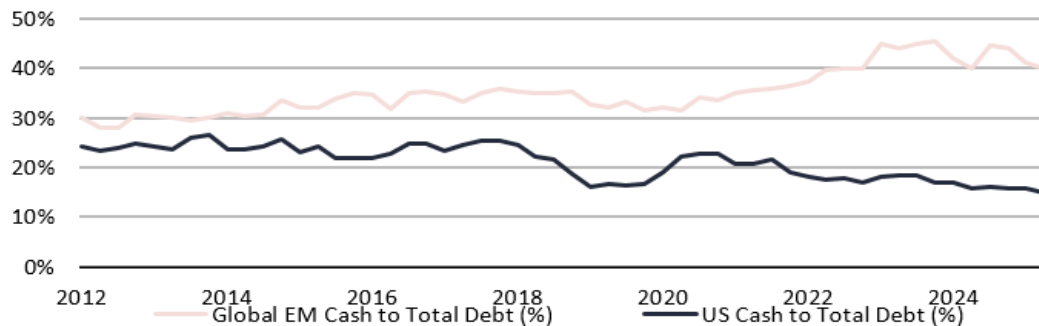
Net leverage of US and EM corporates



Source: J. Stern & Co; Bank of America; data as at 30th June 2025

Cash on the balance sheet has also slightly deteriorated in both US and EM corporates. However EM corporates are against in a much better position to defend their businesses and continue servicing debt, with more than double the liquidity of US corporates.

### Liquidity of US and EM corporates



Source: J. Stern & Co; Bank of America; data as at 30th June 2025

These relative strengths of EM corporates are reflected in the achieved and forecast default rates. EM corporate high yield defaults peaked in 2022-2023, owing to localised exogenous factors in Russia and China real estate, which have now started to subside, allowing the default rates to fall to the long-term average of around 3%.

### Default rates of US and EM high yield corporates

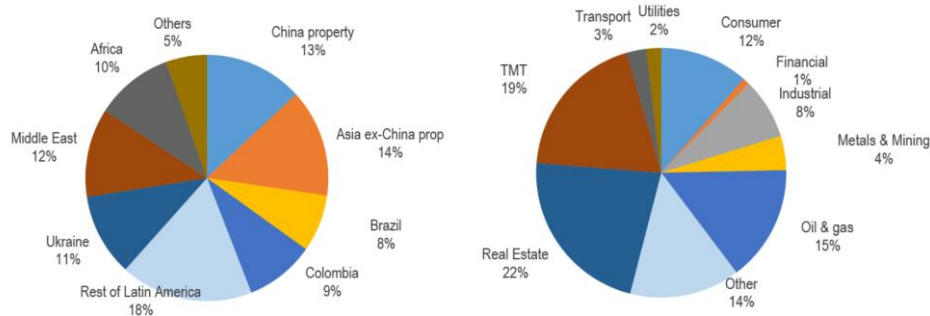
Default rates	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025 YTD	2026 Forecast	2022 (ex-Russia and China property)	2023 (ex-Russia and China property)
EM Corporate HY	3.7%	2.5%	4.0%	1.4%	1.2%	0.8%	2.5%	4.5%	6.0%	6.8%	2.9%	2.4%	3.0%	1.8%	2.3%
US Corporate HY	3.0%	2.6%	4.3%	1.5%	1.9%	2.9%	6.8%	0.4%	1.7%	2.8%	1.5%	0.8%	2.7%	-	-

Source: J. Stern & Co; JP Morgan; Default data as at 31st October 2025

### Forward-looking expectations

According to J.P.Morgan, default rates are expected to be around 3.0% in 2026, in line with historical averages. The expected default distribution within the EM corporates is relatively evenly distributed (by market-value-weighted basis) across countries and sectors. Looking at this distribution, we note that our portfolio does not have exposure to China or the real estate segment in Asia, thereby avoiding two key areas of expected defaults in 2026.

## Balanced distribution of defaults

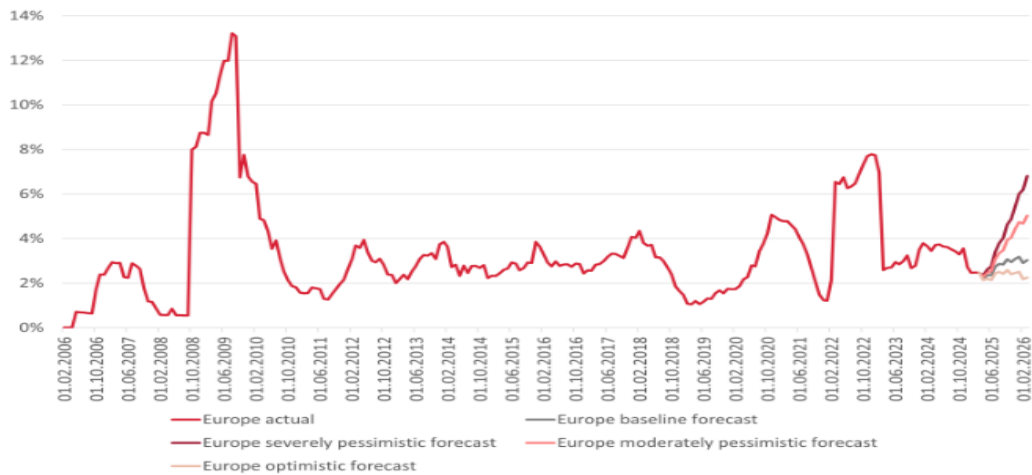


Source: JP Morgan, November 2025

## Comparison with other developed market sectors

The question is how this default rates trend compares with the two other sectors in which investors often have exposure, namely European high yield and private credit. Looking first at European high yield, ex-Eastern European region, default rates have tended to be very similar to EM corporate, with a baseline forecast being around 3%. Arguably, a materially more benign interest rate environment in Europe would further alleviate refinancing pressures.

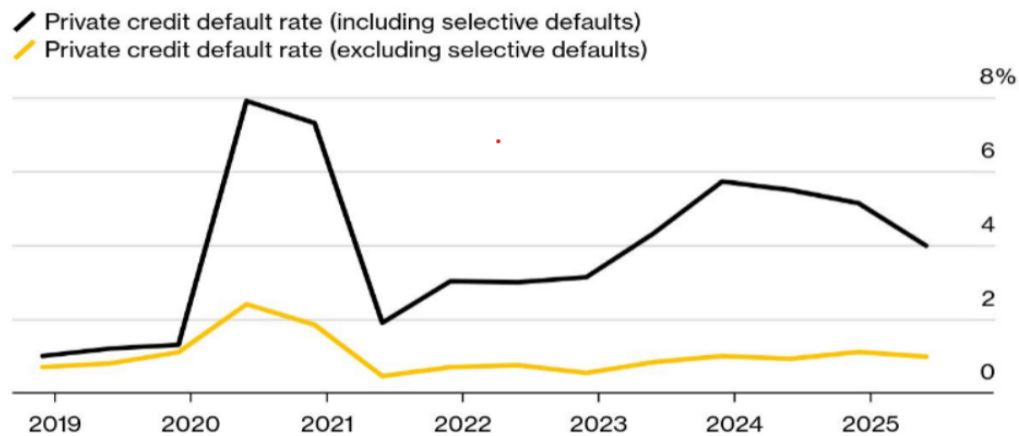
## European corporate default rates in line with EM



Source: Moody's Global default rate. April 2025, Nordea Asset Management

Comparing private debt default rates is more difficult, primarily because of the opacity of this illiquid asset class and the widespread use of Payment in Kind (PIK) arrangements, which can delay potential defaults. Historically, the private credit defaults have been assumed to be very low (<1%), but recent data and analysis by S&P highlight that when “selective defaults” (including but not limited to security changes such as PIK and Amend & Extend) are incorporated, the overall default rate is about a third higher than EM corporate.

## Selective defaults push overall rate higher in private credit



Source: S&P, Bloomberg, October 2025

## 4. AFTER THE PERONISTS' ELECTORAL DEFEAT IS IT TIME TO INVEST IN ARGENTINA?

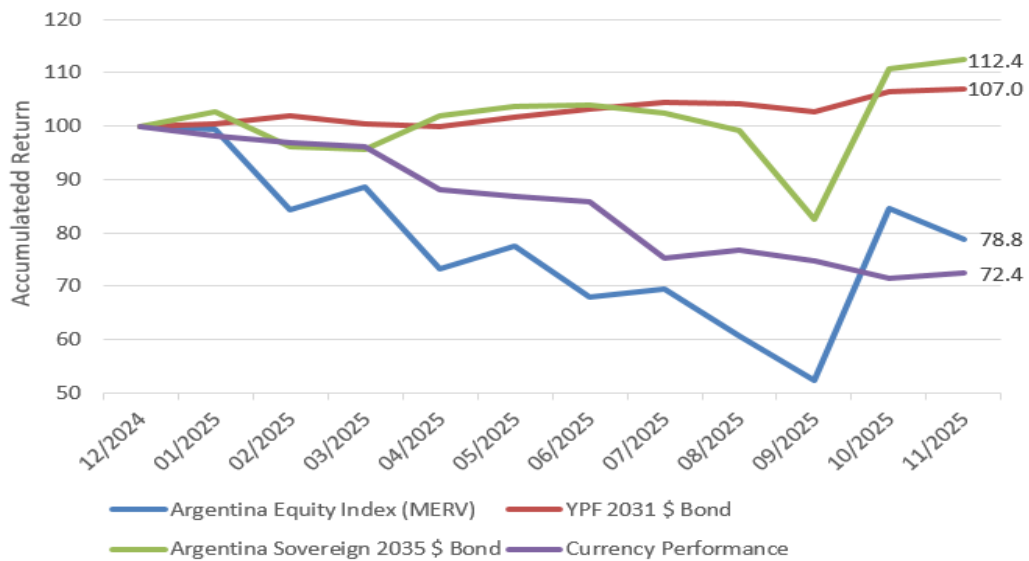
Investing in Argentina has long been synonymous with pronounced market volatility, and 2025 was no different. There has been political uncertainty, corruption scandals, slowing economic growth, depleting FX reserves and concerns about government debt refinancing. Investors are periodically reminded that the country has defaulted on its sovereign debt nine times.

After a largely successful first year in power, President Milei's libertarian party suffered a shock landslide defeat at September's local elections in the bellwether province of Buenos Aires. In part due to social fatigue around the government's fiscal adjustments. The result raised doubts about the political backing for his free-market agenda, which is pursuing structural reforms in labour, pensions and tax.

Stocks, sovereign bonds and currency tumbled, marking some of the steepest intraday losses since 2020. Assets then whipsawed from September to October as Milei surprised the market with a decisive victory in the mid-term elections and the US looked to support its political ally, promising a USD 40 billion credit line to prop up the currency and help with bond payments.

Needless to say, predicting and timing political and geopolitical developments in Argentina (and emerging markets more generally) is difficult.

## Cumulative return of Argentine risk assets



Source: Bloomberg, J. Stern & Co. as of October 2025

There are opportunities to invest in the country which provide very attractive returns with significantly lower volatility. Select Argentine hard-currency corporate bonds have shown resilience, driven by strong underlying fundamentals. YPF is a good example. It is the largest energy company in the country and has access to Vaca Muerta, among the world's largest undeveloped shale formations. The company is strategically important for the country and future economic recovery. It is a critical component to the country's desire to reach energy self-sufficiency or, better still, become a net exporter, which will provide a source of US dollars. To get there, it will need foreign direct investment to fund capex and needs to foster an attractive investment landscape.



Source: Seeking Alpha; Perfil. YPF presenting their strategy to Wall Street in April 2025

Despite ongoing macro challenges, YPF has shown strong operational growth, with increased production and improved financial metrics driven by efficiency gains. The company can now operate profitably with oil at USD 45 per barrel. Its strategic plans forecast production more than doubling in the next five years. Progress is also already being made on their export capabilities, with the company having exported approximately USD 3 billion over the past 12 months. We particularly like the US dollar bonds secured by these exports, which more than cover the face value of the debt. The exports are collected in a Citibank account in New York, reducing FX and transfer risk and ultimately providing downside protection. At the same time, they still offer relatively attractive income yields and total return potential.

### ***The year ahead***

The asset class deserves attention given the attractive yields, low volatility and diversification benefits. Our emerging-market corporate debt strategy is one way to gain exposure. It aims to deliver attractive risk adjusted returns. The high-income generation provides visibility on returns and helps serve as a volatility buffer.

As shown in the table below, the strategy has generated equity like returns with significantly lower volatility. The 3-year annualised gross return (11.0% to October 2025) is basically in line with the yields on the strategy three years prior (11.5% YTM in October 2023). The returns were achieved with an annualised volatility of 4.6%, approximately one third the volatility of the US equities.

<b>Strategy Characteristics</b>	<b>31/10/2023</b>	<b>Strategy return and volatility</b>	<b>3 year annualised</b>
Income yield	7.6%	Income generated	7.7%
Yield to Maturity	11.5%	Total return	11.0%
Duration	2.5	Volatility	4.6

*Source:*

Today the strategy has an income yield of 7.5% and yield to maturity of 8.6%, with a duration of 2.6 year. This provides a good indicator for the expected returns over the coming years.

*J. Stern & Co. Credit Team  
Jean Yves, Charles, Jack and Som*

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