MetLife Investment Management



FIXED INCOME

Emerging Markets Debt Review and Outlook

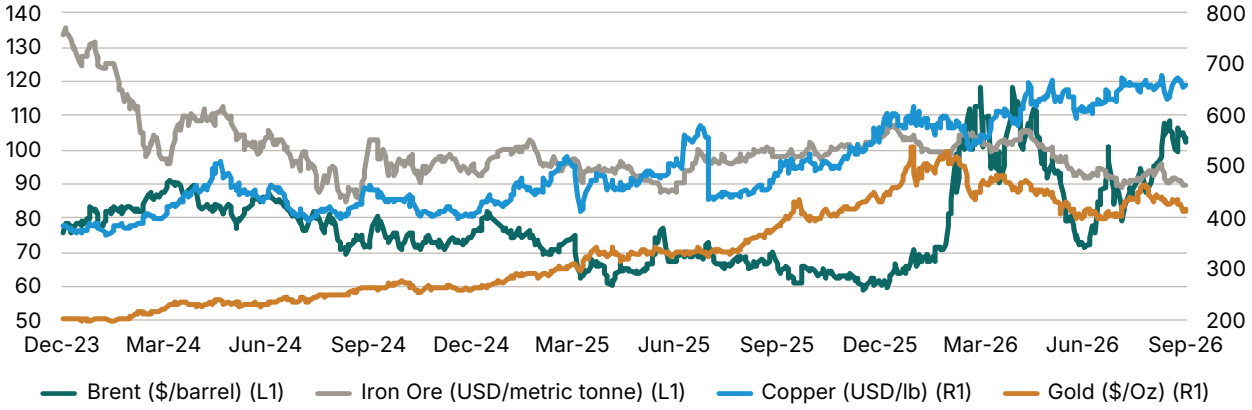
Q3 2026

Emerging markets debt (EMD) entered the third quarter with generally resilient fundamentals, which helped weather the external environment that became progressively more challenging as the quarter progressed. A sharp rise in U.S. Treasury yields, persistent inflation, renewed Federal Reserve tightening, and elevated geopolitical risk ultimately outweighed those supports. The Treasury curve bear steepened, with the 10-year yield rising 82 basis points (bps) to 5.28%, its highest level since 20071. Although the U.S. dollar finished the quarter essentially flat, that result masked an important reversal: Early in the quarter, dollar weakness gave way to a sharp September rebound as U.S. rate differentials moved in the dollar's favor, tightening financial conditions and weighing on EM currencies.

The shift in the U.S. rates backdrop was reinforced by an uncomfortable mix of moderating growth, persistent inflation, and a still-resilient labor market. Above-consensus core inflation readings and strong consumer spending suggested that price pressures had broadened beyond energy. Against this backdrop, the Fed raised the federal funds rate by 25 bps in September, bringing the upper bound to 4.00%, and maintained a hawkish tone that left open the possibility of additional tightening.

Commodity markets added another layer of pressure. Brent crude rose 42% to $103.5 per barrel as disruptions around the Strait of Hormuz and attacks on regional energy infrastructure intensified supply concerns. The oil rally amplified inflation risks, complicated the policy outlook, and contributed to a more defensive tone across global fixed income. Other commodities were firmer for different reasons: Gold gained 3.7% on episodic safe-haven demand, while copper rose 7.7% as expectations for infrastructure and artificial intelligence (AI)-related demand met ongoing supply constraints.[1]

Figure 1 | Commodities



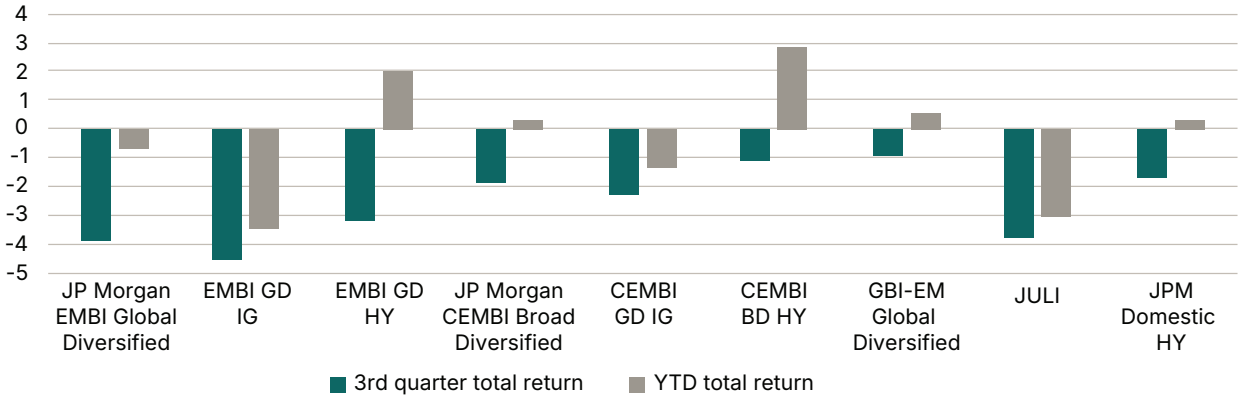
Sources: Bloomberg L.P., MIM as of Sept. 30, 2026.
Gold values are adjusted by a factor of 10 for scaling purposes.

Higher risk-free rates, renewed dollar strength, and geopolitical uncertainty weighed on the asset class, with duration driving much of the dispersion. The J.P. Morgan EMBI Global Diversified Index returned –3.86% for the quarter, as investment-grade sovereigns returned –4.55%, underperforming the –3.80% return for U.S. investment grade, while high-yield sovereigns returned –3.24% versus –1.73% for U.S. high yield. Longer-duration Latin America was the weakest region at –4.86%, while Africa was the strongest at –2.55%. Positive returns in Lebanon and Senegal showed that reform momentum, policy credibility, commodity exposure, and political catalysts could still offset broader market headwinds.[2]

Shorter duration and healthy corporate balance sheets helped EM corporate credit outperform both EMBI and U.S. credit during the quarter. The J.P. Morgan CEMBI Broad Diversified Index returned –1.83%, as high yield returned –1.11% versus –2.32% for investment grade. Financials and infrastructure held up relatively well, while transport, metals and mining, TMT, and utilities were among the weaker sectors.ii The pattern reinforced, during a quarter dominated by the rates shock, that carry and lower duration provided a meaningful cushion.

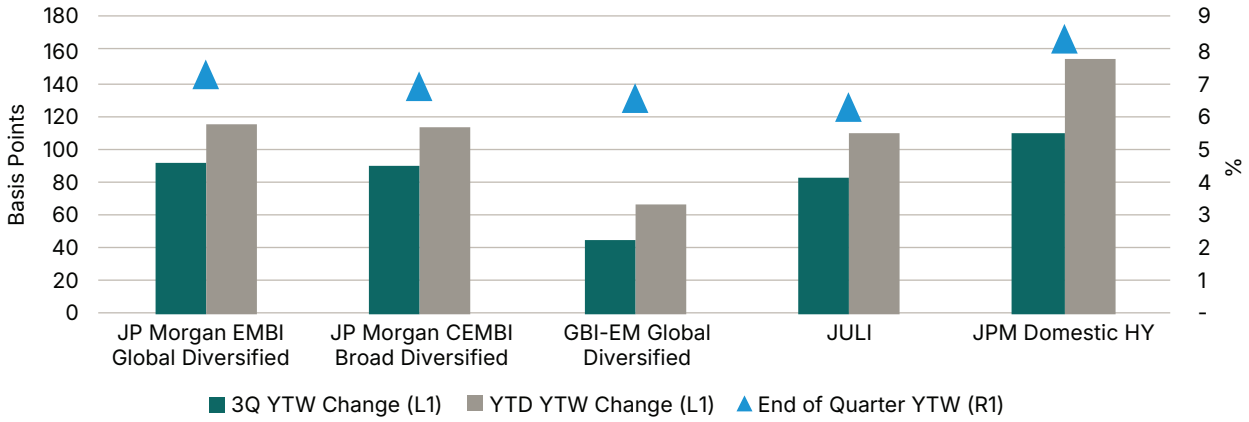
Local currency debt followed a similar pattern of broad pressure but significant country-level dispersion. The J.P. Morgan GBI-EM Global Diversified Index returned –0.94% in unhedged U.S. dollar terms, as modestly positive local bond returns were offset by late-quarter currency weakness. Brazil returned 4.21% and Colombia gained 2.99%, demonstrating that attractive carry and domestic catalysts could still support returns even as higher U.S. yields and a firmer dollar challenged the broader market.[2]

Figure 2 | Indexes total returns (%)



Sources: Bloomberg L.P., JP Morgan, MIM as of Sept. 30, 2026.

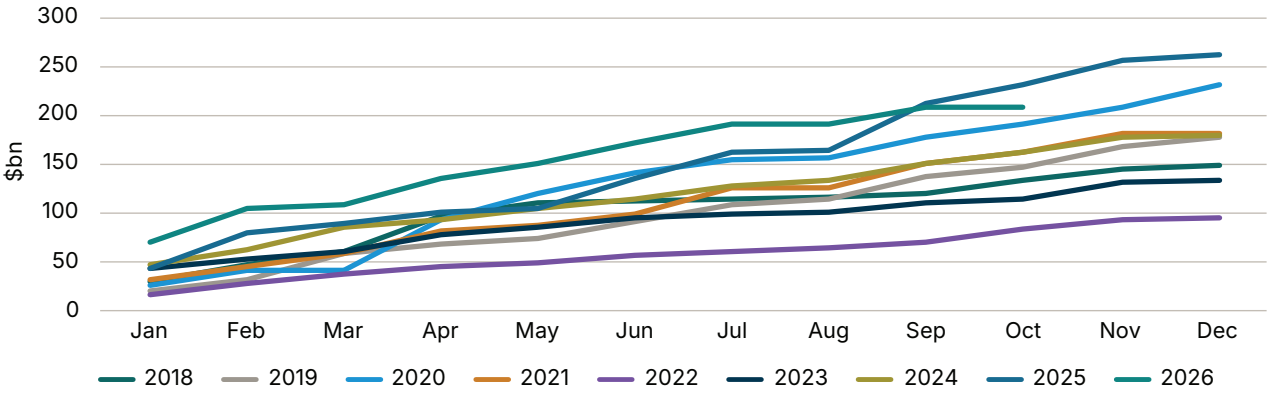
Figure 3 | Indexes yield-to-worst



Sources: Bloomberg L.P., JP Morgan, MIM as of Sept. 30, 2026

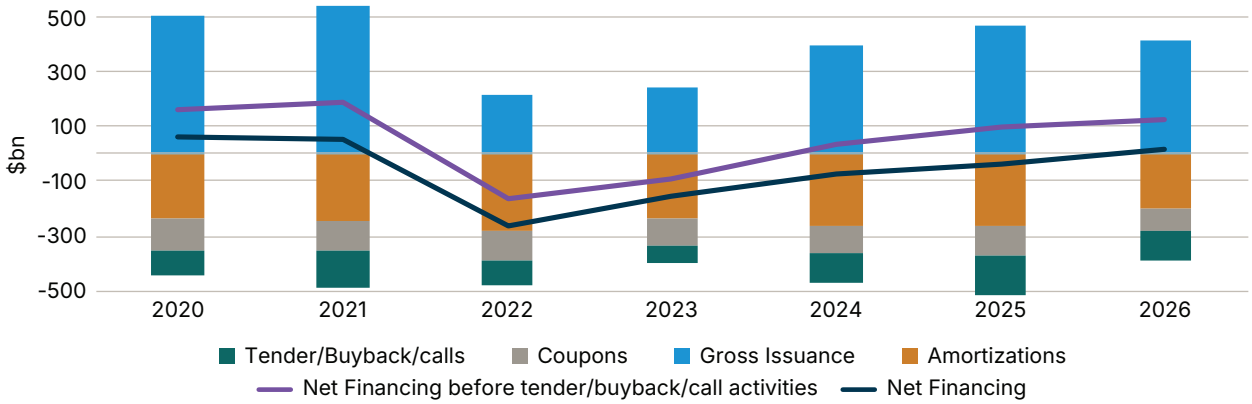
Importantly, the quarter's volatility did not significantly slow the primary market. EM sovereign gross issuance totaled approximately $36.4 billion, bringing year-to-date supply to $208.1 billion. EM corporate issuance reached $102 billion, above the five-year quarterly average of $90 billion, with investment-grade borrowers accounting for $81 billion. Since redemptions more than offset corporate gross issuance, approximately $28 billion of negative net financing supported secondary-market technicals. Investor flows were less consistent: EM ex-China portfolio flows stabilized after significant outflows in May and June, while modest September inflows into hard currency debt contrasted with subdued broader EM debt fund flows.[3]

Figure 4 | Cumulative gross sovereign issuance



Sources: JP Morgan, MIM as of Sept. 30, 2026.

Figure 5 | Corporate net issuance



Sources: JP Morgan, MIM as of Sept. 30, 2026.

Country-specific developments remained an important driver of investor sentiment during the quarter. In Brazil, investors increasingly positioned for a more market-friendly political outcome ahead of the presidential election, contributing to lower political and fiscal risk premia. Those expectations were reinforced shortly after quarter-end, when first-round election results showed stronger-than-expected support for the political right, boosting confidence in the prospects for fiscal reform, policy continuity, and a more orthodox economic policy framework. In Argentina, assets faced pressure as investors reassessed the government's ability to sustain fiscal adjustment and advance its broader reform agenda, although approval of a new central bank charter aimed at strengthening institutional independence and establishing a single mandate focused on currency stability was viewed as a constructive longer-term development. Elsewhere in Latin America, investors monitored the economic implications of a major earthquake in Colombia shortly after the new administration took office, while sentiment toward Bolivia improved following congressional approval of an IMF-supported program and reforms to diesel subsidies. El Salvador also remained in focus as progress on IMF reviews reinforced confidence in the country's reform trajectory. Within Africa, Senegal's announcement of a new IMF program was viewed positively despite limited details, while improving inflation dynamics, currency stability, and expectations for monetary easing supported Nigeria. In Emerging Europe and Central Asia, Romania remained in political limbo as competing fiscal proposals failed to gain traction, while investors also monitored governance concerns stemming from a Turkish fund scandal and sanctions-related scrutiny involving one of Kyrgyzstan's largest banks.

Investment strategy (outlook):

The same forces that shaped third-quarter returns are likely to remain central to the near-term outlook: U.S. rates, inflation, labor market data, oil prices, and developments in the Middle East. September's sharp repricing in Treasury yields raised the hurdle for risk assets, and volatility may persist as investors assess whether restrictive U.S. monetary policy can contain inflation without causing a sharper slowdown. At the same time, the quarter's wide dispersion showed that resilient EM balance sheets, differentiated domestic policy cycles, and issuer-specific catalysts continue to create opportunities beneath the challenging global backdrop.

From a sovereign perspective, EM appear better positioned than in many previous periods of elevated global rates. Balance sheets are generally stronger; external financing needs are more manageable; and many countries have made meaningful progress strengthening policy frameworks. While higher oil prices continue to create winners and losers across the asset class, they also reinforce the importance of country differentiation. We favor sovereigns where reform momentum, improving fiscal dynamics, and potential ratings migration can support further spread compression, while remaining more cautious in countries facing deteriorating fiscal trajectories, political uncertainty, or refinancing pressures.

In local markets, attractive real yields, easing inflation pressures, and increasingly flexible monetary policy settings continue to create a compelling opportunity set. Although persistent U.S. economic resilience and elevated Treasury yields may contribute to periods of currency volatility, many EM have entered this environment with stronger fundamentals and greater policy flexibility than in previous cycles. We remain constructive on idiosyncratic opportunities such as Egypt, Uzbekistan, and Turkey, while also finding value in the carry available across Brazil, Colombia, and South Africa.

For corporates, the third quarter reinforced the attractiveness of income generation and issuer selection. Corporate fundamentals remain healthy, with generally manageable leverage, solid liquidity profiles, and limited near-term refinancing requirements following several years of proactive balance sheet management. We continue to favor companies with resilient business models, conservative financial policies, and clearly identifiable catalysts, where spread tightening potential can complement carry. While high-yield corporate credit remains attractive, we believe selective exposure offers a more compelling risk-reward profile than broad market beta.

Technical conditions provide an additional source of support. Primary markets remain open; corporate net supply is negative; and demand continues to favor fundamentally stronger issuers. The asset class is also underowned by many global investors, while yields compare favorably with developed-market alternatives. Even so, wider risk premiums and greater dispersion across quality, duration, regions, and sectors call for disciplined new-issue participation and bottom-up credit analysis rather than a broad increase in market exposure.

Overall, we retain a constructive medium-term view while recognizing that elevated global yields and geopolitical uncertainty warrant disciplined risk taking. The quarter demonstrated that outcomes are likely to depend less on broad EM beta and more on how portfolios balance duration, income, currency risk, and country- and issuer-specific catalysts. High yield offers attractive income and less duration sensitivity, while a balanced duration posture limits reliance on large directional rate positions. A credible path toward de-escalation in the Middle East would reduce the geopolitical premium in oil, ease inflation concerns, and support lower global yields, although the timing remains uncertain. Against this backdrop, resilient fundamentals, supportive technicals, and widening cross-country dispersion create a strong opportunity set for active investors.

Endnotes

[1] Data sourced from Bloomberg LP as of September 30, 2026.

[2] Data sourced from JP Morgan as of September 30, 2026.

[3] Data sourced from JP Morgan as of September 30, 2026.

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