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Market mispricing persists amid rising resilience

What was your key takeaway from 2025?

2025 was a pivotal year for the asset class. Conversations with asset allocators, news headlines and flows all pointed to the same thing: perceptions have shifted and emerging market (EM) fixed income is firmly on investors' radars. Drivers of this included growing recognition that the lines between emerging and developed markets (EM/DM) have blurred. The 'EM'ification' phenomenon we first alerted our clients to in 2022 was laid bare in 2025, with mounting credibility concerns jostling DM yield curves while the EM debt market cemented its status as a maturing and increasingly resilient asset class.

In addition, EM debt rose in relevance for many asset allocators thanks to its increasingly powerful portfolio diversification benefits. Ongoing credit-rating upgrades and credible policymaking across many EM economies further boosted its appeal. For many, the debate shifted from "why should I consider the asset class?" to "how can I get the asset class to work for me?". EM fixed income's many regional, currency and credit-quality variations have helped answer this question.

Can investors ditch concerns around the dollar?

Much ink has been spilt over the direction and future of the US economy, yet what really matters for EM debt investors is the relative strength of the US dollar and its impact on the asset class. In both cases, the outlook is encouraging. After a decade of dominance, the US dollar's bull run appears to be ending. In tandem, the dollar's relevance for the EM debt asset class has faded. The traditional relationship of strong dollar = poor EM debt performance has weakened thanks to EM economies maturing – stronger domestic policy frameworks, deeper local markets, and reduced reliance on the dollar have improved EM resilience to currency moves. We saw clear evidence of this last year, with EM local assets performing well even during periods of US dollar strength. As we noted in August, EM debt performance is increasingly a reflection of policymaking and growth dynamics within EM economies, rather than the direction of the dollar.

Has the inflation problem retreated?

Inflation dynamics in EM are broadly supportive, thanks to credible EM monetary policy and the disinflationary forces of US trade policy. In short, while significant uncertainty remains around the path of DM inflation, EM economies are at a significant advantage: with real (inflation-adjusted) yields near 20-year highs by our estimates, EM central banks are better placed than their DM counterparts to cut interest rates when the right macroeconomic conditions are in place. Of course, EM is an expansive universe of countries, and there are always exceptions to the broad trend; investors who do their country-by-country inflation homework will continue to find interesting exceptions both on and off benchmark.

What happens if the AI risk-rally reverses?

The sustainability of the rally in risk assets is a key 'known unknown' as we enter 2026. Aside from the odd speed bump, for many months, optimism over the potential of AI-related technologies has overshadowed mixed data on the real economy and uncertainty around the eventual impact of AI on growth and productivity. While a correction in AI-related asset valuations could weigh on global sentiment, EM debt is now a more resilient asset class thanks to stronger fundamentals and improved policy frameworks. As noted above, it is better equipped to absorb global shocks. Furthermore, the impact of any AI-driven market correction would likely vary; for active investors with a long-term horizon, a broad-based sell-off could present attractive valuations amid market dislocation. We've seen this before, notably in the 2022 high-yield market sell-off.

How do you view geopolitical risks for the year ahead?

Heightened geopolitical risk remains a defining theme, compounded by another busy election calendar in EM. As active managers, this is the new normal to navigate. As we enter 2026, our base case expectation is that tensions and tariffs will remain, however they will be targeted and ultimately contained. After all, the one clear investment lesson from 2025 is that, despite a long list of unsettling events, markets generally recovered and performed well.

In light of this, we will remain open-minded and continue to run rigorous scenario analysis, recognising that periods of change and market stress often create the most compelling investment opportunities.

Where are you focusing your attention this year?

Three broad themes present the best opportunities across the asset class in 2026:

1. Hard currency markets where fundamental strength and credit-rating upgrade potential are currently overlooked by many market participants.
2. High-yielding local currency markets with improving macroeconomic trends and supportive market technicals (supply/demand dynamics).
3. Idiosyncratic turnaround stories.

The following roundup from colleagues across our EM debt platform shows that these opportunities can be found across the global EM universe.

Africa - Thys Louw

Significant diversification within Africa's fixed income markets means that opportunities continue to span a wide range of economies – from energy exporters such as Nigeria and Angola to reform-focused markets like Egypt, Kenya and Morocco. The Egyptian pound appears well placed to benefit from the country's improving fiscal position and continued economic support from the Gulf. The Nigerian naira remains an attractive carry market, while on the hard-currency side, Senegal is on a positive trajectory thanks to ongoing economic reforms and resilient regional market access. By contrast, we see limited upside potential for Kenya's currency and local rates following several strong years. On the hard-currency side, slow progress on Kenya's fiscal consolidation makes an IMF deal unlikely in the near term.

Asia – Wai Kiat Soh and Mark Ledger-Evans

Subdued inflation and lacklustre growth are likely to put pressure on the region's central banks to continue cutting rates, particularly given ongoing fiscal consolidation plans. That should support local rates markets. On the growth front, Malaysia stands out as a likely beneficiary of sustained foreign investments – coupled with resilient domestic consumption, that suggests the ringgit could continue to outperform. In the north of the region, attention will turn to Thailand's general elections scheduled for 8 February; the risk of no single party securing a simple majority keeps us cautious on the baht as the formation of fragile coalitions could lead to renewed inter-party disagreements. Finally, China's export strength will likely remain a prominent theme in 2026, with several countries already expressing concern about its sizeable trade surplus and its role as a key engine of economic growth.

CEEMEA – Roger Mark and Aurelie Martin

South Africa stands out in this highly diverse region: ongoing fiscal discipline, reform momentum and an anchoring of inflation expectations suggest potential for further outperformance. Elsewhere, Turkey's macro stabilisation programme looks set to continue; that should underpin the lira carry trade and support local yields, despite political risks remaining. In Central and Eastern Europe, relatively strong growth and a positive German fiscal impulse create uncertainty around the extent of interest rate cuts, with Hungary's outlook further complicated by a hotly contested election. More broadly, the outlook for the Russia-Ukraine war remains a key unknown, with any move towards a lasting peace deal positive for the wider region's fundamentals and risk premia. Regardless, growth in the Caucasus and Central Asia should remain strong, helped by continued structural reforms and prudent macro policy; Kazakhstan and Uzbekistan are particularly interesting markets. In the Gulf region, while broader (non-oil related) growth should remain firm, the oil price will remain important for economies and their bond-issuance needs; we will monitor closely regional geopolitics, notably around Lebanon, which finds itself caught between competing interests.

Latin America - Nicolas Jaquier and Christine Reed

Politics will be front and centre in this region, with elections taking place in Brazil, Colombia, Peru and Costa Rica; investors should watch carefully for signs of fiscal loosening/premature monetary policy easing. For Mexican assets, the United State-Mexico-Canada (USMCA) trade agreement review will be the defining catalyst, influencing trade expectations, investment flows, and investor confidence. Within EM FX, we like markets with strong terms-of-trade such as Chile and Peru. On the hard currency side, Ecuador is a structurally improving economy, with record current-account surpluses and FX reserves; it is anchored by an on-track IMF programme, yet its debt offers a generous risk premium.

Turning to events unfolding in Venezuela at the time of writing, regime change in the absence of a major military escalation is among the more optimistic scenarios market participants had anticipated during the recent build-up of forces in the region. Investors should monitor closely political developments in the country as a successful restructuring ultimately requires a legitimate government able to credibly commit to reforms, typically anchored by an IMF support programme. In terms of the broader regional impact, Cuba's economy stands to lose access to heavily discounted Venezuelan oil; at the other end of the spectrum, if stability is maintained and Venezuela eventually reopens its economy, Colombia stands to benefit most in terms of bilateral trade.

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