

Developed and emerging markets converge, creating long-term opportunities

One of our four 2026 global fixed income themes explores the blurring between developed and emerging markets. Political, fiscal and institutional risks once reserved for emerging economies increasingly apply to developed markets, while many emerging nations have strengthened their fundamentals — expanding opportunities for fixed income investors.

Key takeaways:

- Although geopolitical turmoil has weighed on markets, emerging markets debt remains an attractive longer-term opportunity due to ongoing structural dynamics.
- Blurring market distinctions, expanding EM corporate opportunities and a declining U.S. dollar all support EM going forward.
- Emerging markets debt can provide attractive additional yield over similarly rated developed market securities.
- Consider judiciously adding exposure through more diversified approaches like multi-sector or core plus bond strategies or a dedicated EM strategy.

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Middle East conflict affects recent bond market returns

Rising interest rates and increased risk premiums due to the ongoing war in the Middle East subdued first quarter fixed income returns (Figure 1). Not surprisingly, sectors with longer duration profiles or more credit risk fared the worst. However, higher yields are creating a more attractive entry point for investors.

High oil prices fuel inflation and slow growth

Oil price disruption has long been the primary market risk tied to Middle East instability. Oil is now more than \$90 per barrel, up from a prior three-month average near \$60. The spike in oil will pressure inflation higher. If prices remain near current levels, we estimate headline inflation will run 1.0% higher in 2026. Core inflation — which removes the effects of energy prices — will likely also face upward pressure, since oil is an essential input across the economy — adding roughly 0.3% this year.

Higher oil prices also compress real incomes and will likely weigh on consumption. The good news is that U.S. consumers now allocate less than 4% of spending to energy, down 2% from 2014 and 5.5% from the 1982 peak. And as a major energy producer, the U.S. should see higher oil prices spur investment, partially offsetting the drag on growth. On net, we expect the oil shock to reduce real GDP growth

to 1.8% this year, a fairly modest reduction of 0.2% from our prior forecast. Even if oil were to reach \$120 a barrel, we estimate it would bring growth to 1.5%, keeping it well above recession territory.

With near-term inflation persisting and growth decelerating only mildly, the Fed is likely on hold until later in the year. Outside the U.S., we expect one rate hike from the European Central Bank (ECB) and two from the Bank of Japan. These central bank policies may sustain elevated yields and enhance the income potential of fixed income investments.

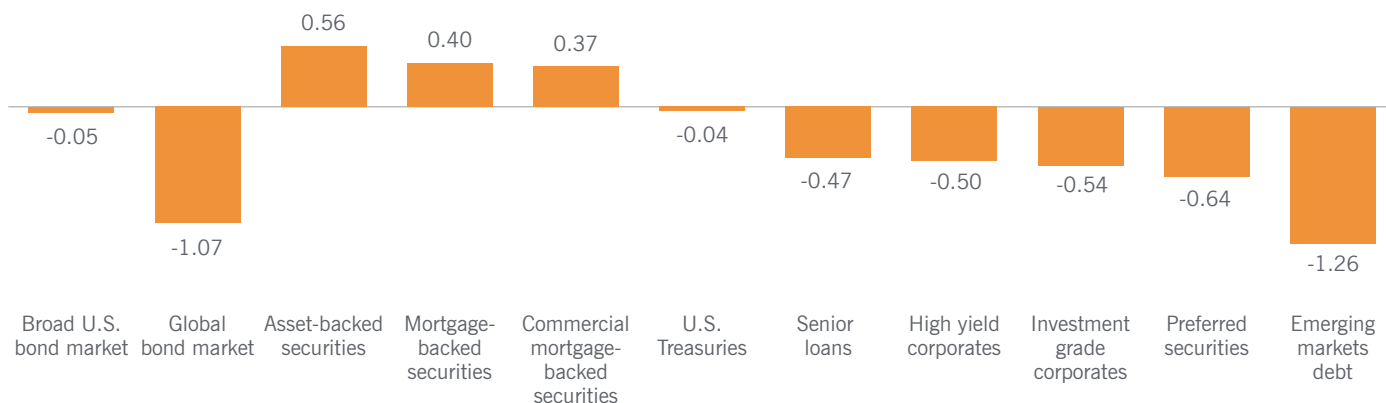
The strategic case for emerging markets debt

While uncertainty around the conflict and its impact on oil prices persists, we remain focused on opportunities driven by more enduring economic trends. We see three structural factors continuing to support the emerging markets debt asset class: converging developed and emerging markets dynamics, growth in emerging markets corporate debt and the gradual decline of the U.S. dollar. We do not believe the conflict meaningfully alters these longer-term trends.

At the same time, elevated oil prices may create opportunities for active managers in energy-producing regions. We believe a strategic allocation to emerging markets debt remains a compelling consideration for many portfolios.

Figure 1: Global tensions dampen fixed income returns

Total return, 2026 year-to-date (%)



Data source: Morningstar Direct, 31 Mar 2026. Performance data shown represents past performance and does not predict or guarantee future results. Representative indexes: broad U.S. bond market: Bloomberg U.S. Aggregate Index; global bond market: Bloomberg Global Aggregate Index; emerging markets debt: JPM EMBI Global Diversified Index; high yield corporates: Bloomberg U.S. Corporate High Yield of 2% Issuer Capped Index; mortgage-backed securities: Bloomberg U.S. Mortgage-Backed Securities Index; investment grade corporates: Bloomberg U.S. Corporate Index; commercial mortgage-backed securities (CMBS): Bloomberg CMBS ERISA Eligible Index; preferred securities: ICE BofA U.S. All Capital Securities Index; U.S. Treasuries: Bloomberg U.S. Treasury Index; senior loans: S&P UBS Leveraged Loan Index; asset-backed securities: Bloomberg Asset-Backed Securities Index.

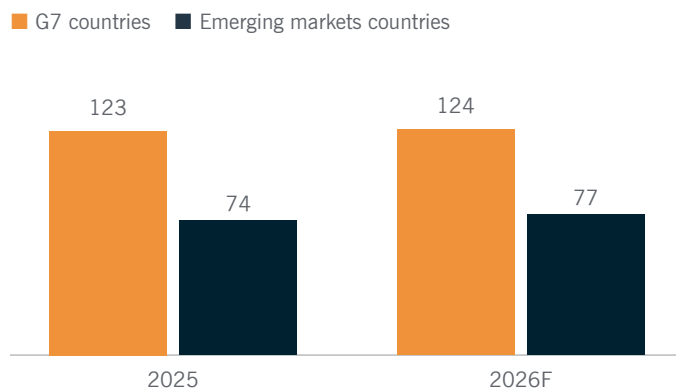
Developed and emerging boundaries are blurring

For decades, global fixed income portfolios followed a simple framework: developed markets offered stability and institutional credibility while emerging markets offered yield premiums alongside higher political, fiscal and currency risks. That framework is increasingly being challenged.

Today, fiscal trajectories, institutional credibility and policy stability vary as much within developed and emerging markets as between them. Political risk, fiscal deficits and policy uncertainty — once viewed as predominantly EM characteristics — now appear across major developed economies. Meanwhile, many emerging markets have strengthened balance sheets, improved policy frameworks and demonstrated greater market discipline (Figure 2).

Figure 2: Fundamentals remain meaningfully stronger for emerging markets than developed markets

Debt-to-GDP ratio (% of GDP)



Data source: International Monetary Fund, April 2026.

Corporate debt has become globally significant

What began predominantly as a sovereign market has evolved into a broad, deep and increasingly corporate-led opportunity set. The EM corporate hard currency market has grown to approximately \$2.6 trillion, exceeding the EM sovereign universe and rivaling — in some measures surpassing — the U.S. high yield market.¹

“Political risk, fiscal deficits and policy uncertainty — once viewed as predominantly EM characteristics — now appear across major developed economies.”

This evolution materially changes emerging markets’ role in global portfolios.

First, EM risk is no longer solely sovereign. Corporate issuers now dominate, allowing investors to express country, sector and thematic views with greater precision and less reliance on sovereign balance sheets.

Second, scale matters. At its current size and depth, EM corporate debt is no longer a peripheral allocation. It increasingly competes with developed market credit on both yield and quality, particularly when adjusted for fundamentals.

Dollar weakness provides sustained support

Global investors are navigating a changing currency regime. While the U.S. dollar remains the world’s dominant reserve currency, its status is gradually declining. Central banks and institutional investors are increasingly diversifying away from dollar-based exposures, driven by geopolitical fragmentation, fiscal uncertainty and risk management considerations.

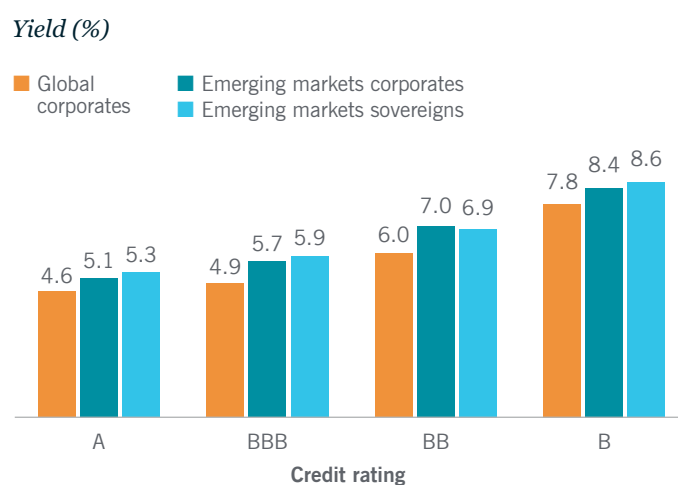
Importantly, diversification is occurring through market participants hedging U.S. dollar exposure. That dynamic creates persistent downward pressure on the dollar — a material tailwind for emerging markets.

Dollar weakness directly improves EM debt sustainability by reducing the real burden of servicing external obligations. It also enhances competitiveness and supports growth, particularly for export-oriented economies. While EM local currency debt may benefit most directly, EM hard currency debt may also gain as improving balance sheet dynamics reduce default risk and compress spreads.

Yield advantages remain compelling across ratings

Beyond the broader structural shifts, emerging markets debt provides a yield advantage versus global peers on a ratings-adjusted basis. Across the credit quality spectrum, both EM corporates and sovereigns offer higher yields than the broader universe (Figure 3). This additional yield can boost portfolio income and returns over time. While credit spreads are relatively tight, they remain favorable compared to other fixed income sectors, and attractive opportunities exist within the asset class itself.

Figure 3: Emerging markets debt offers higher yields than developed market credit



Data source: Bloomberg L.P.; JPMorgan, 31 Mar 2026. Performance data shown represents past performance and does not predict or guarantee future results. Representative indexes: global corporates: Bloomberg Global Corporate Index; emerging markets corporates: JPM EMBI Global Diversified Index; emerging markets sovereigns: JPM CEMBI Diversified Index.

Active management can capture opportunity across complexities

Given the wide variety of emerging market countries — from those with strong fundamentals to more vulnerable, oil-linked economies — and the diverse range of instruments spanning sovereign, quasi-sovereign and corporate bonds, we believe active management is particularly well-suited to this asset class. Success requires diligent research across multiple dimensions.

For sovereign analysis, this means examining macroeconomic factors including inflation trends and

monetary policy, economic growth and fiscal positioning, political stability, and currency dynamics. Corporate analysis requires additional considerations: competitive dynamics within specific industries, broader sectoral trends and peer benchmarking, plus issuer-specific factors like credit quality, capital structure and management capabilities. A well-resourced and experienced research team is essential to navigate this complexity effectively.

Two approaches provide flexible portfolio integration

Diversified multisector and core plus bond strategies suit investors seeking active asset allocation across the broader fixed income markets with emerging markets debt as one component.

These strategies offer diversification across the entire global fixed income universe. An active manager can strategically position the portfolio to capture opportunities within emerging markets debt while adjusting both the size and composition of this allocation as economic and geopolitical conditions change.

- **Multisector bond strategies** tend to be more aggressive and typically permit higher allocations to emerging markets debt. These strategies offer maximum flexibility to invest across both investment-grade and below-investment-grade sectors, encompassing emerging markets debt alongside securitized products, senior loans, collateralized loan obligations and preferred securities.
- **Core plus bond strategies** generally allocate up to 30% in higher-yielding plus sectors like high yield corporates or emerging markets debt. This structure can deliver diversification and return enhancement while maintaining a moderate overall risk profile.

Dedicated emerging markets strategies suit investors who want direct control over their emerging markets allocation.

Within this approach, we favor strategies with broad mandates encompassing sovereign, quasi-sovereign and corporate segments, along with flexibility to invest in local currency debt. This breadth provides a comprehensive opportunity set and enables meaningful exposure across the full spectrum of emerging markets debt.

Outlook

Higher oil prices cloud the outlook, but credit opportunities remain

We have updated our macroeconomic and market forecasts to reflect the likely effects of the war in the Middle East, though the situation remains highly uncertain. We now expect U.S. real GDP growth of 1.8%, down 0.2% from our prior forecast, driven primarily by a drag on consumption from higher fuel prices, partially offset by a modest lift to business fixed investment from the oil-extraction sector. We have also raised our core inflation forecast by 0.3% to 2.8%, reflecting oil price pass-through as tariff-related disinflationary effects fade. The labor market is expected to remain broadly stable.

These revisions push our Fed rate cut expectations later into the year. We now anticipate the first cut in the second half of 2026, rather than around mid-year, with the second cut likely shifting into 2027. Outside the

U.S., we continue to expect at least one ECB rate hike and two Bank of Japan hikes this year.

In asset allocation, we maintain a modest preference for spread sectors and credit risk, with an up-in-quality bias within asset classes. Spread volatility in the coming months may create more attractive entry points for adding risk. We currently see select opportunities in preferred securities, senior loans and collateralized loan obligations (CLOs), as well as in emerging market economies with strong fundamentals or direct exposure to higher oil prices. We expect Treasury yields to rally modestly and the yield curve to steepen over the course of 2026, with the 10-year Treasury yield likely ending the year near the low end of our 4.00% – 4.25% forecast range.

Four themes are shaping our approach in 2026

	What's happening?	Market implications	Actions to consider
Time for a takeover: Fiscal policy outweighs monetary policy	Government spending dominates as central bank rate-cutting cycles end	Longer-term rates likely remain elevated despite policy easing	Favor positioning for a steeper yield curve over aggressive duration extension
Economic resilience: Tight spreads, but room for credit risk	Technology investment, productivity gains and strong corporate fundamentals underpin 2026 growth rebound	Spreads can remain compressed for extended periods during steady growth; premature de-risking sacrifices income	Focus on higher-quality segments within below-investment-grade sectors, like high yield corporates, preferreds and senior loans
Digging deeper for diversification: Look beyond traditional credit	Historically tight credit spreads have reduced income potential of traditional bond investments	Less-traded credit sectors provide wider spreads and different risk exposures than traditional corporates	Capture incremental yield by moving into emerging markets debt, CMBS, preferreds, senior loans, CLOs and municipals
New playbook: Developed and emerging markets converge	Political and institutional risks now affect developed markets while emerging markets have strengthened fundamentals	Traditional analytical boundaries between developed and emerging markets are dissolving	Emphasize sectors insulated from sovereign risk (securitized credit, municipals); raise strategic allocation to high-quality emerging markets debt

For more information, please visit us at nuveen.com.

¹ Data source: J.P. Morgan, 31 Oct 2025.

Endnotes

Inflation: U.S. Bureau of Labor Statistics Consumer Price Index for All Consumers. **Global debt and yields:** Bloomberg, L.P.

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