

EMERGING MARKETS DEBT TOTAL RETURN STRATEGY

The Opportunity

Emerging markets debt represents an approximately \$25 trillion opportunity set, yet only \$6.7 trillion¹ is covered by conventional hard and local currency benchmarks. This tradable universe offers a rich variety of exposures, such as sovereign/quasi, corporates, currencies, and rates, to a diverse set of countries that span AA to default credit quality. These opportunities also extend across both easily accessible and less accessible formats, including private and frontier markets. The latter can be defined as countries with less developed institutions and local financial markets that are harder to access and require specialized custody, tax, and trading infrastructure. Further, as EM local markets develop, their share of global currency and interest-rate derivatives notional amounts and turnovers continue to climb, giving investors excellent tools with which to take and hedge risks.

We believe an investment strategy with a return objective rather than a benchmark-relative objective (either a single benchmark or a blended benchmark²) can serve a variety of investors keen to take advantage of the full breadth of the opportunity while focusing on the higher-return potential sub-segments, generally those that are of low investment grade or sub-investment grade.

The GMO Solution

The GMO Emerging Markets Debt Total Return Strategy seeks annualized returns of 3% (net of fees) above the Secured Overnight Financing Rate (SOFR) over a complete market cycle. The Strategy pursues this objective by combining a funded asset portfolio selected from a subset of the emerging market debt universe that satisfies the SOFR +3% hurdle (typically expected to be BB-rated or below), with two derivatives-based overlays — one in FX and one in local rates.

FUNDED ASSET PORTFOLIO

- Hard currency credit instruments are expected to satisfy the SOFR+3% hurdle while offering a solid risk/return profile in terms of spread versus fundamental risk. For non-distressed hard currency instruments, we would expect them to be held long. For distressed, we may add short positions in bonds or derivatives to limit jump-to-default risk. Our typical process seeks to trade complexity for return, focusing on unique opportunities in sovereign, quasi-sovereign, and project finance issues in either public or private markets.
- Frontier local market instruments are expected to offer more return potential than their hard currency counterparts, with return potential advantages stemming from expertise that requires specialized custody, tax, and trading infrastructure.

DERIVATIVE-BASED OVERLAYS

- Our core EMFX systematic program has an information ratio (IR) close to 1.0, taking risk-controlled positions in ~20 major EM currencies. The program takes very limited USD net positions, ranging from -4% to +6%.
- Our core EM rates systematic program has an IR close to 1.0, taking risk-controlled positions in ~16 major EM rates markets. The program takes limited net EM duration positions, ranging from -0.75 to +0.75 contribution to duration (CTD).

Both programs have had stable factor betas over time. For USD-based investors, they may offer a more stable return profile than that of allocating to local debt benchmarked portfolios.

TEAM EXPERTISE

- eVestment data shows GMO has delivered top-decile alpha in both hard and local currency EM debt over 3-, 5-, and 10-year horizons. Favorable upside/downside capture ratios³ across our benchmark-relative track records reflect a disciplined, repeatable investment process that has created value across market environments. The GMO Emerging Markets Debt Total Return Strategy builds on this approach with greater flexibility and less benchmark constraint.

¹ As of June 2024, Sources: J.P. Morgan, Bank of America, GMO calculations

² For instance, a blended benchmark such as 50% JPM EMBI Global Diversified/ 50% JPM GBI EM Global Diversified implies no hurdle for considering unhedged local currency exposures

³ eVestment data as of 3/31/2026

Client Fit

We believe the GMO Emerging Markets Debt Total Return Strategy can be a good fit for investors seeking explicit outcome-based exposure to emerging market debt without inheriting the duration, credit quality, or currency composition of a benchmark. Our unique approach can be used in the following ways:

- **As a benchmark-agnostic, EM debt allocation** within a broader credit or opportunistic income bucket.
- **As an alpha emphasis sleeve** alongside more benchmark-aware emerging debt exposures, where the investor wants to separate return-seeking implementation from benchmark construction.
- **As a beta diversification** to core USD fixed income (e.g., Aggregate-benchmarked) and U.S. corporate high yield portfolios, which are expected to have minimal holdings or exposure overlap.
- **For investors with the governance flexibility** to tolerate higher tracking error to peers, and a less conventional reporting construct than familiar benchmark-relative mandates, in exchange for greater control over duration, currency, credit quality, and hedging tools.

Who We Are

Founded in 1977, GMO is a private partnership whose sole business is investment management. The firm manages global portfolios with offices and clients worldwide. Investment offerings include equities, fixed income, multi-asset class, and alternative strategies. GMO is known for blending fundamental and quantitative investment research expertise and a long-term orientation toward value opportunities.

The Team

The GMO Emerging Markets Debt team has been managing emerging debt portfolios – both benchmark relative and absolute return – since 1994, consistently employing an investment approach emphasizing bottom-up, valuation-based instrument selection.

RISK | Risks associated with investing in the Strategy may include: Credit Risk, Market Risk - Fixed Income Investments, Market Disruption and Geopolitical Risk.