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FRONTIER BONDS: An enterprise worth exploring



GlobalEvolution

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Their high yields attract attention, but the diversification potential of frontier bonds deserves equal billing. Under-researched economies, domestic investor bases and reform momentum create opportunities for investors prepared to look beyond familiar markets, explains Witold Bahrke, Senior Macro and Allocation Strategist at Global Evolution.

What if some of the bond markets investors find most uncomfortable could help them navigate the risks keeping them awake at night?

Frontier markets are often associated with political uncertainty, volatile currencies and limited liquidity. Yet their relatively low exposure to global capital flows can offer valuable diversification when inflation shocks and geopolitical tensions unsettle mainstream assets.

At Global Evolution, we believe the frontier label itself is widely misunderstood. All too often, frontier bonds are seen purely as a way to increase risk and return, serving mainly as a satellite allocation outside conventional benchmarks. **Their diversification potential is largely underappreciated.**

A SHORTER QUEUE AT THE EXIT

Frontier markets are more heavily dominated by domestic investors and less influenced by foreign capital flows. There are still relatively few foreign "tourists" in this segment. When risk aversion rises, the queue at the emergency exit is therefore shorter, typically resulting in smaller drawdowns and faster subsequent recoveries.

Local currency bonds stand out. Put simply, these are the "true" frontier bonds: default risk is very low – currency depreciation tends to occur instead – and they often offer unexpected diversification benefits. Unlike local currency bonds in more established emerging markets, frontier local currency bonds do not primarily reflect movements in the EUR/USD exchange rate and global risk appetite.

Many frontier economies are also less integrated into global supply chains, setting aside heavily commodity-dependent countries and exceptions such as Vietnam. This means they are less affected by current geopolitical risks such as protectionism.

INCOME WITH LESS DURATION

The income opportunity is substantial, with yields to maturity in the frontier segment currently exceeding 12%.[1] The very low duration of less than three years in the local currency segment reduces vulnerability to the structurally greater uncertainty surrounding global inflation since the pandemic.

The appeal of frontier markets is structural rather than cyclical, a point that much of the investment community continues to underestimate. Limited analyst coverage and scarce data create genuine market inefficiencies, and long-term return opportunities that remain far from fully exploited.

Currency depreciation can erode long-term total returns. High carry can provide a substantial cushion, although outcomes depend on the country, entry point and subsequent policy decisions.

REFORMS CAN CHANGE THE TRAJECTORY

We are primarily discussing countries at a very early stage of economic development. In a sense, investors have a second chance if they missed the opportunity to invest in countries such as Mexico or South Africa decades ago. Countries with young populations and low labour costs generally have substantial growth potential.

Their institutions typically have considerable room for improvement, creating significant scope for reform. Countries that realise this potential offer the best long-term prospects, in our view. The growth-enhancing potential of such reforms is often underestimated because many investors view it through the lens of industrialised economies.

We favour countries demonstrating fiscal or monetary discipline, including Kazakhstan, Egypt and Uganda, alongside economies pursuing meaningful reform.

Nigeria stands out in the latter group. Following a change of government, Nigeria has cut subsidies and liberalised its exchange rate regime, setting economic policy on a sustainable course.

We see strong return potential alongside declining

*Full Legal name: Generali Investments Holding S.p.A.
[1]Measured by Global Evolution's Frontier Markets Composite as of Sep. 30th 2026.

macroeconomic risks, supported by a rapid pace of reform. Nigeria's role as an oil exporter also provides a cushion against global geopolitical risks.

Looking ahead, Paraguay and Uruguay are candidates to move from frontier to emerging market status, with Georgia a possibility over a somewhat longer horizon. There are also larger "rising star" candidates, such as Argentina, where reform momentum is gathering pace. Some investors are already referring to the country as "the new Brazil".

RESEARCH TURNS UNFAMILIARITY INTO INSIGHT

Frontier countries receive far less analyst coverage than other emerging markets. Political risks are also higher, partly because institutions operate with less independence. This knowledge gap must be bridged through proprietary research and country visits. The considerable resources this requires deter many investors.

At Global Evolution, we combine analysis of global macroeconomic conditions with detailed country research and relative-value assessment.

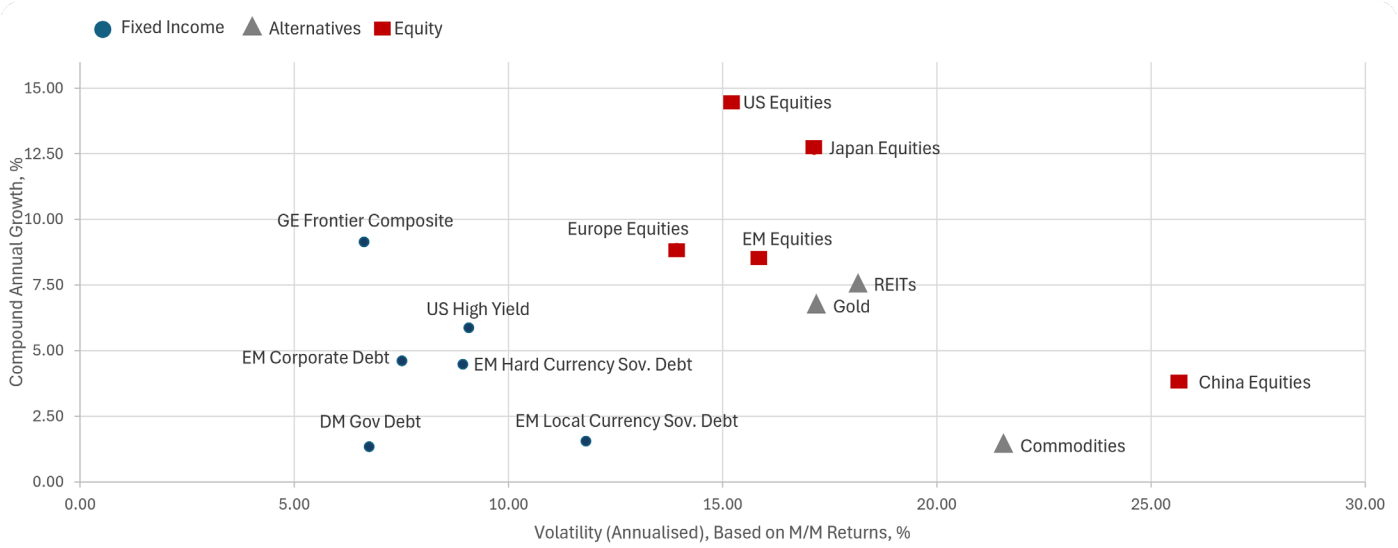
Our experience suggests that liquidity concerns tend to be overstated. Even during the pandemic, we maintained daily liquidity in our funds at all times. Liquidity nevertheless requires careful assessment at investment and portfolio levels.

If we had to give just one reason to look more closely at frontier bonds, it would be the Sharpe ratio. It captures the relationship between return and risk that is ultimately decisive for investors. With a Sharpe ratio of 2.2,[2] frontier bonds are highly attractive compared with other liquid bond segments.

Thanks to high carry and a low correlation with global risk factors, frontier bonds may offer an exceptional balance of return and risk. Since 2010, they have delivered a higher total return than US high-yield bonds, with volatility comparable to that of G7 government bonds (see Figure 1).[3]

Figure 1: Frontier bonds may offer an exceptional balance of risk and return[3]

15Y HORIZON (INCEPTION DATE FOR GE FRONTIER COMP.), MONTHLY DATA



[1]Measured by Global Evolution's Frontier Markets Composite as of Sep. 30th 2026.
[3]Source: Global Evolution, Macrobond, Bloomberg, Data as of Sep. 30th 2026.

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