EM in trade finance: unmet demand and alpha potential

Chris McGinley,
Head of Trade Finance

Maarten Offeringa,
Portfolio Manager

Kazaur Rahman,
Portfolio Manager

Q3 2025

Federated Hermes
Limited

www.hermes-investment.com
For professional investors only

Emerging markets provide an ideal investment environment for trade finance, connecting underserved areas with a vital source of alternative capital, while potentially offering investors a compelling mix of risk and return.

- Federated Hermes' Trade Finance Strategy has a global investment mandate. We seek to maximise the benefits of portfolio diversification and generate higher potential risk-adjusted returns for investors – wherever in the world those opportunities may be.
- While the Strategy also invests in developed markets (DM), our portfolio of alternative credit assets typically has significant exposure to emerging markets (EM). EM boasts unique attributes, including the potential for higher returns, faster economic growth and access to commodities – yet they are fundamentally underserved in terms of access to credit.
- The case for EM credit investing typically focuses on growth and returns relative to economic fundamentals. However, EM also introduces jurisdictional, geopolitical and country-specific risks. By focusing on trade finance as a unique subset of the wider EM private credit universe, Federated Hermes' Trade Finance Strategy aims to avoid (or mitigate against) many of those risk factors, without compromising the EM risk premium.

Federated Hermes' Trade Finance Strategy invests in short-term loans that play a key role in facilitating global trade flows and their related infrastructure.

In contrast to strategies that invest in public credit markets, trade finance is not beholden to a fixed universe of issuers – instead it independently selects where and when to deploy capital, and which companies and projects to back.

While our Trade Finance Strategy is able to invest across both emerging markets (EM) and developed markets (DM), the sizable unmet demand for alternative credit in EM creates many more compelling investment opportunities compared to DM.

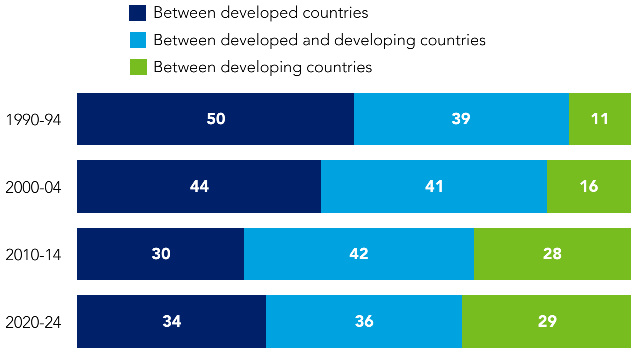
Incorporating EM into trade finance has numerous benefits

Over the last couple of decades, globalisation has led to a significant amount of industrial activity – and its related supply chains – moving from DM to EM. As a result, EM has significantly increased its share of global trade.

Between 2000 and 2019, the share of emerging markets in global trade increased from 32% to 46%, and its share of global foreign direct investment (FDI) rose from 15% to 46%. At present, the majority of the world's GDP growth occurs in EM.[1]

Figure 1: Trade between emerging economies on the rise

Share of the value of global goods trade between developed and developing countries (%)



Source: International Trade Centre (ITC) – a joint agency of the United Nations and the World Trade Organization (WTO).

Many EM countries boast robust economic growth, supported by young populations and a fast-growing middle class, and these factors have transformed production and consumption patterns: EM has increasingly become a destination for – as well as an originator of – global trade flows.

Emerging markets enjoy unique attributes:

- **Primary goods/commodities:** Many EM countries are rich in natural resources and are leading producers of primary goods. EM economies play outsized roles across the value chain of key commodities such as oil and gas, metals and agricultural products.
- **Solid fundamentals:** EM economies have matured and are now more resilient to external shocks than has been the case in the past. The Strategy focuses investment on EM 'national champions' – borrowers that play an outsized role in an economy, with well-established businesses with strong balance sheets and operating track records. Many of these national champions enjoy unique competitive advantages and have become increasingly integrated into global supply chains.
- **Underserved markets:** The breadth of sources of finance available in DM are not usually available in EM. Since EM public markets are not as developed, availability of credit overall remains comparatively scarce. Bank-led financing is usually the primary source of credit and in the case of trade finance – a market subset – there is a significant shortage.[2]
- **Potential for higher returns and lower default rates:** On a relative basis, EM debt has historically offered higher yields and spreads in comparison with DM. Emerging market issuers have also reported corporate default rates typically below those in global high yield.[3]

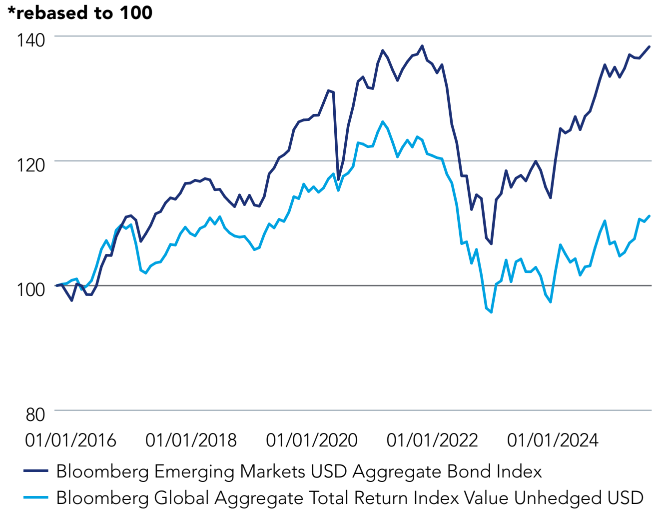
EM economies play outsized roles across the value chain of key commodities such as oil and gas, metals and agricultural products.

[1] Emerging Markets Network | OECD

[2] The gap for global trade finance opportunities was valued at US$2.5tn by the Asian Development Bank in 2022, up from US$1.7tn two years previously, and is forecast to continue widening, according to the Asian Development Bank.

[3] S&P Global Ratings: 2024 Annual Global Corporate Default and Rating Transition Study; 2024 EM and Frontier Markets Corporate Default and Rating Transition Study

Figure 2: EM debt has historically offered higher yields vs. DM



Source: Bloomberg as at 18 June. **Past performance is not a reliable indicator of future performance.**

Trade finance supports the primary production of goods, and facilitates their movement along the value chain – both domestic and cross-border.

Trade finance has traditionally fallen under the remit of global commercial banks – with loan origination achieved through their extensive domestic and international relationship networks.

The Strategy's approach is to operate alongside these banks, working together to deploy capital productively, rather than competing with them.

Our close links with leading banks allows us to benefit from their expansive loan origination networks. It's a quid pro quo relationship, where we help facilitate solutions to regulatory pressures on capital and other constraints on banks' balance sheets.

Where banks step back, our Trade Finance Strategy finds opportunity

Despite its obvious attractions, EM investing can also introduce exposure to jurisdictional and country-specific risks – such as geopolitical instability, less-developed regulatory systems and greater macroeconomic volatility.

Federated Hermes' Trade Finance Strategy is designed to either seek to avoid (or mitigate against) many of those risk factors, without compromising the EM risk premium.

- **Currencies:** The potential risk to portfolio credit quality from fluctuations in the US dollar is effectively mitigated against by investing in hard-currency transactions.
- **Documentation:** The use of market-standard English and New York law-governed legal documentation helps mitigate against potential idiosyncrasies in EM local law. The incorporation of features such as the offshore routing of cash flows and advance waivers of immunity can help protect against non-payment risk and convertibility and transferability risks.
- **Contractual risk mitigants:** Traditional credit protections such as maintenance covenants, the use of offshore collateral, and placing restrictions on borrowers' operational and financial flexibility, remain a key feature of EM trade finance loans (even with higher-quality borrowers).
- **Selective and adaptable investment mandate:** The Strategy navigates potential concentration risk by applying rigorous diversification across its investment portfolio. Investments are not exclusively tied to any country or region, or any specific industry or originator. All transactions are selected for investment following careful analysis of their standalone merits. The Strategy is highly selective and focuses on established leaders in their respective industries – businesses that have a distinct and compelling competitive advantage (regardless of where they operate). For such businesses, we provide senior capital linked to specific trade activity or to capital projects of significant strategic importance (as opposed to providing generic blank cheque corporate funding).

Federated Hermes' Trade Finance Strategy provides alternative credit globally, on a highly selective basis, utilising robust financing structures that are of strategic importance to the parties involved.

In underserved EM capital markets, the Strategy is able to pick and choose where to provide flexible solutions, which can result in attractive risk-adjusted returns for investors.

The value of an investment can go down as well as up and return on your investment will therefore be variable. Past performance may not be a reliable guide to future performance. Yield may fluctuate in accordance with market conditions and taxation arrangements. Fixed-income securities are sensitive to changes in interest rates, and a rise in interest rates can cause a decline in their prices. The Strategy will make investments in emerging markets which tend to be more volatile than those in mature markets hence the value of an investment can move sharply down or up. Where the Strategy invests in debt instruments there is a risk that the entity who issues the contract will not be able to repay the debt or to pay the interest on the debt. If this happens then the value of the Strategy may vary sharply and may result in loss. Trade finance investments are not listed on any stock exchange. Due to their nature, being typically private and bespoke, these investments will not be as easily sold in the market as publicly traded securities therefore ability to redeem is limited and may be significantly deferred.

For professional investors only. This is a marketing communication. It does not constitute a solicitation or offer to any person to buy or sell any related securities, financial instruments or financial products. No action should be taken or omitted to be taken based on this document. Tax treatment depends on personal circumstances and may change. This document is not advice on legal, taxation or investment matters so investors must rely on their own examination of such matters or seek advice. Before making any investment (new or continuous), please consult a professional and/or investment adviser as to its suitability. Any opinions expressed may change. All figures, unless otherwise indicated, are sourced from Federated Hermes. Whilst Federated Hermes has attempted to ensure the accuracy of the data it is reporting, it makes no representations or warranties, expressed or implied, as to the accuracy or completeness of the information reported. The data contained in this document is for informational purposes only, and should not be relied upon to make investment decisions. Federated Hermes shall not be liable for any loss or damage resulting from the use of any information contained on these pages. All performance includes reinvestment of dividends and other earnings. Please consider all strategy characteristics when investing and not just ESG characteristics. Federated Hermes refers to Federated Hermes Limited ("Federated Hermes"). The main entities operating under Federated Hermes are: Hermes Investment Management Limited ("HIML"); Hermes Fund Managers Ireland Limited ("HFMIL"); Hermes Alternative Investment Management Limited ("HAIML"); Hermes Real Estate Investment Management Limited ("HREIML"); Hermes Equity Ownership Services Limited ("EOS"); Hermes Stewardship North America Inc. ("HSNA"); Hermes GPE LLP ("Hermes GPE"); Hermes GPE (USA) Inc. ("Hermes GPE USA"), Hermes GPE (Singapore) Pte. Ltd ("HGPE Singapore"), Federated Investors Australia Services Pty Ltd. ("FIAS"), Federated Hermes Japan Ltd ("FHJL") and Federated Hermes (UK) LLP ("FHUK"). FHUK, HIML, HAIML and Hermes GPE are each authorised and regulated by the Financial Conduct Authority. HAIML and HIML carry out regulated activities associated with HREIML. FHUK, HIML, Hermes GPE and Hermes GPE USA are each a registered investment adviser with the United States Securities and Exchange Commission ("SEC") and HAIML and HFMIL are each an exempt reporting adviser. HGPE Singapore is regulated by the Monetary Authority of Singapore. FHJL is regulated by Japan Financial Services Agency. FIAS holds an Australian Financial Services Licence. HFMIL is authorised and regulated by the Central Bank of Ireland. HREIML, EOS and HSNA are unregulated and do not engage in regulated activity. In the European Economic Area ("EAA") this document is distributed by HFMIL. Contracts with potential investors based in the EEA for a segregated account will be contracted with HFMIL. Issued and approved by Hermes Investment Management Limited, as distributor, which is authorised and regulated by the Financial Conduct Authority. Telephone calls may be recorded for training and monitoring purposes. Potential investors in the United Kingdom are advised that compensation may not be available under the United Kingdom Financial Services Compensation Scheme.

In Australia: This Strategy Document relates to potential offer of financial products or investment opportunities in Australia (Investment opportunities). Both Hermes Investment Management Ltd (HIML) and Federated Investors Australia Services Ltd. ACN 161 230 637 (FIAS) are the distributors of the Investment opportunities. HIML does not hold an Australian financial services licence (AFS licence) under the Corporations Act 2001 (Cth) ("Corporations Act"). HIML operates under the relevant class order relief from the Australian Securities and Investments Commission (ASIC) while FIAS holds an AFS licence (Licence Number - 433831). The offer of Investment opportunities only made in circumstances under which no disclosure is required under Chapter 6D and Part 7.9 of the Corporations Act. Nothing in this Strategy Document is, or purports to be, an offer to a person to whom disclosure would be required under Chapter 6D or Part 7.9 of the Corporations Act. This Strategy Document is not a disclosure document under Chapter 6D of the Corporations Act or a product disclosure statement for the purposes of Part 7.9 of the Corporations Act. This Strategy Document has not been and will not be lodged with ASIC and does not contain all the information that a disclosure document or a product disclosure statement is required to contain. The distribution of this Strategy Document in Australia has not been authorised by ASIC or any other regulatory authority in Australia. In addition, the Fund is not a registered managed investment scheme, as defined in the Corporations Act. This Strategy Document is provided for general information purposes only and is not intended to constitute, and does not constitute, the provision of any financial product advice or recommendation and must not be relied upon as such. This Strategy Document is not intended to influence a person in making a decision in relation to a particular financial product or class of financial products, or an interest in a particular financial product or class of financial products. This Strategy Document has been prepared without taking account of your objectives, financial situation or needs and you should obtain independent professional financial advice that considers your circumstances before making any financial or investment decisions.

In Hong Kong: The contents of this document have not been reviewed by any regulatory authority in Hong Kong. You are advised to exercise caution in relation to the offer. If you are in any doubt about any of the contents of this document, you should obtain independent professional advice. The strategies are not authorised under Section 104 of the Securities and Futures Ordinance of Hong Kong by the Securities and Futures Commission of Hong Kong. Accordingly, the distribution of this document, and the placement of interests in Hong Kong, is restricted. This document may only be distributed, circulated or issued to persons who are professional investors under the Securities and Futures Ordinance and any rules made under that Ordinance or as otherwise permitted by the Securities and Futures Ordinance.

In Japan: Federated Hermes Japan Ltd is registered as a Financial Instruments Business Operator in Japan (Registration Number: Director General of the Kanto Local Finance Bureau (Kinsho) No. 3327), and conducting the Investment Advisory and Agency Business as defined in Article 28 (3) of the Financial Instruments and Exchange Act (FIEA). Federated Hermes Japan Ltd is acting as agent or intermediary for the conclusion of investment advisory contracts or discretionary investment contracts between affiliated companies within the Federated Hermes group and Japanese licensed discretionary investment managers, trust banks and other Japanese financial institutions. Federated Hermes Japan Ltd is a member of Japan Investment Advisers Association (JIAA). Reference to Federated Hermes in this material is not limited to Federated Hermes Japan Ltd, but includes group affiliates.

In Spain: This document is issued by Hermes Fund Managers Ireland Limited, Branch in Spain, with Fiscal Identity Number W0074815B, registered in the Mercantile Registry of Madrid, - Volume 40448, Book 0, Sheet 16, Section 8, Page M-718259, first registration, with domicile at Paseo de la Castellana 18, 7° planta, 28046 Madrid - Spain, and registered in the Comisión Nacional del Mercado de Valores with official registration number 36.

BD016149 0019078 07/25

Federated Hermes

Limited

Federated Hermes

Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns and, where possible, to contribute to positive outcomes that benefit the wider world.

Our investment and stewardship capabilities:

- **Active equities:** global and regional
- **Fixed income:** across regions, sectors and the yield curve
- **Liquidity:** solutions driven by five decades of experience
- **Private markets:** private equity, private credit, real estate and infrastructure
- **Stewardship:** corporate engagement, proxy voting and policy advocacy

For more information, visit **www.hermes-investment.com** or connect with us on social media:

SAI GLOBAL
ISO 14001
Environmental