

# ADDING ALPHA IN EMERGING MARKETS

## Stock Selection or Country Selection?



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Emerging equity markets have traditionally been a high-volatility asset class, where differences among a country's social, political, and economic drivers lead to extremely different outcomes across the market. Over the last 10 years, these realized outcomes across emerging markets (EM) countries have diverged sharply, with leadership rotating quickly and unpredictably. Due to the heterogeneity of EM countries, it becomes challenging to consistently predict geopolitical outcomes in any country, and the consequences of being wrong can drastically affect one's strategy performance.

Quantitative EM strategies are structurally well-positioned for this type of environment. First, because of a large opportunity set along with inefficiencies, the potential for adding alpha is strong. Second, by diversifying across countries and sectors, focusing on stock-level opportunities while rebalancing systematically as leadership evolves, these strategies can offer upside without requiring timing on which specific countries will lead. The key takeaway? In EM, when country dispersion is high, *not* picking countries is a feature, not a bug, and can be a repeatable source of alpha.

### Setting the Stage: Emerging Markets Are Not a Single Market

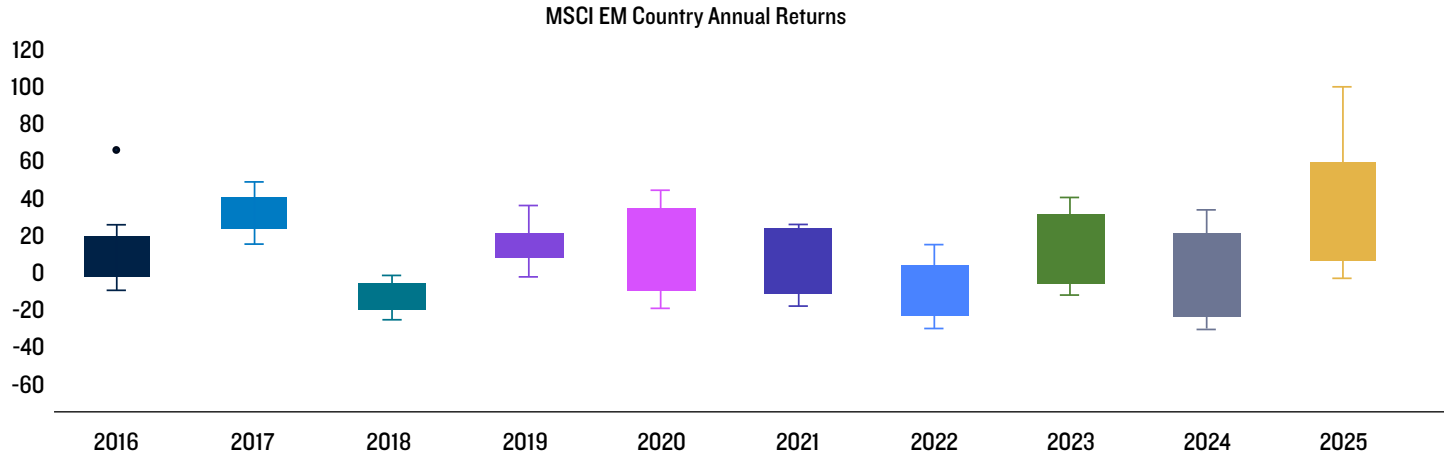
Emerging markets have always been heterogeneous, but recent experience has underscored just how misleading it is to think of EM as a single macro trade. Rather than moving together through a common cycle, EM increasingly resembles a collection of loosely related mini-markets, each driven by its own mix of policy choices, sector composition, currency dynamics, geopolitics, and domestic capital markets.

Country-level return dispersion has risen materially relative to history. Cross-sectional differences in annual country returns have widened and remained elevated for longer than in prior episodes (Exhibit 1).

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And it's not just a story of episodic stress, such as the 2013 taper tantrum, or synchronized recovery, like the immediate post-COVID rebound; instead, dispersion has been persistent, structural, and largely cross-sectional.

### Exhibit 1: Wide Dispersion In EM Country Returns

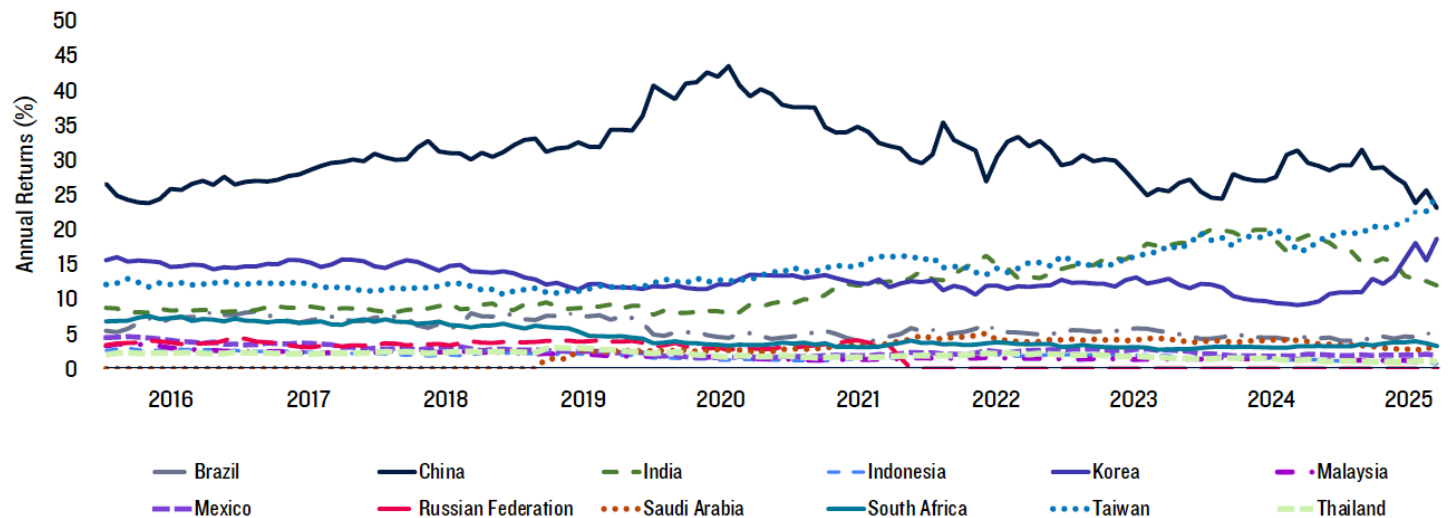


Source: Bloomberg, 22 EM Countries

This marks a sharp contrast with the historical intuition many investors still carry. For much of the 2000s and early 2010s, EM performance could be lumped together into the positive benefits of globalization and offshoring. Countries like China, India, and Korea either produced goods cheaply and shipped globally, or provided services at a better cost. This meant country correlation was higher, leadership narrower, and broad exposure often sufficient.

The first crack in the 30-year upward trend of globalization started in 2016, and since then we've seen major marketplace shifts. Russia has become uninvestable and fallen out of the index, China's stranglehold on export goods production continues a downward trajectory as it shifts its economy to more domestic consumption, and rich valuations of Indian stocks continues to scare away investors. Meanwhile, tech juggernauts such as Korea and Taiwan continue to benefit from the AI trade by producing key components into the ecosystem.

### Exhibit 2: Changing Influence Of Emerging Market Countries



Source: MSCI

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## Country Selection: Source of Alpha or Risk?

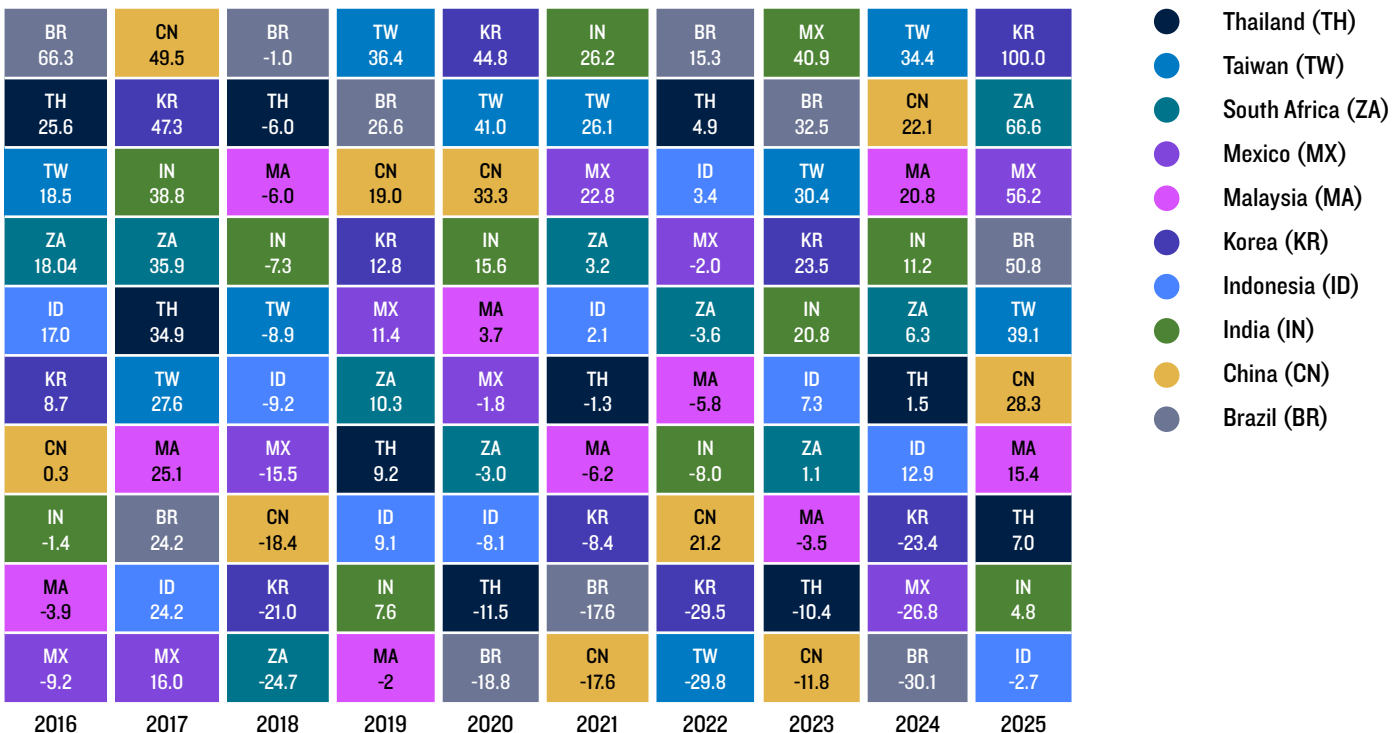
The intuitive response to high dispersion is often to double down on country selection. If outcomes are diverging, it would seem the solution is to identify the right markets to overweight and avoid the rest. In practice, country selection in EM is far more difficult — and riskier — than theory suggests.

First, market performance reflects not just fundamentals, but the sequence in which 1) policies are implemented, 2) reforms are perceived, and 3) capital flows respond. Two countries can arrive at similar macro conditions via different paths and generate entirely different equity outcomes.

Second, EM is unusually policy driven. Fiscal decisions, regulatory interventions, capital controls, and industrial policy can overwhelm traditional valuation or growth signals, often with little warning. Even well-reasoned macro theses can be invalidated, or delayed, by political cycles, social pressures, or administrative execution risk.

Third, country returns are often nonlinear. Long stretches of stagnation can be followed by sudden, violent repricing once conditions change and sentiment turns. What this leads to is highlighted in Exhibit 3, where we show the annual return of the top-10 countries in the MSCI Emerging Market index as of April 2026. The year-by-year fluctuations of the top and bottom performers are staggering. Take, for example, Korea, which was at the top in 2019-20, fell to the bottom in 2021-22, up again in '23, down in '24, and was the best in 2025. Or China, which essentially followed Korea closely up until 2022, but has diverged drastically since.

### Exhibit 3: Country Returns Can Often Be Non-Linear



Source: Bloomberg

For portfolio managers, this creates a dilemma. Structural underweights can persist just long enough to inflict material opportunity cost before reversals occur. Meanwhile, concentrated country overweights often dominate portfolio risk, through sector biases or flagship stocks. The payoff for being precisely right is large, but the cost of mistiming or missing nonlinear inflections can be greater.

## Leveraging Breadth: The Quant Advantage

High and persistent country dispersion fundamentally changes the relative attractiveness of investment processes. In such an environment, quant strategies gain a structural edge. This is further exacerbated in emerging markets, where inefficiencies create ample opportunities for stock selection.

### 1. Breadth Over Concentration

Quant EM strategies evaluate thousands of stocks across many countries simultaneously. This breadth allows them to express views in small, diversified increments rather than through a handful of large country exposures. When leadership rotates unpredictably, alpha is more likely to emerge from many small contributions than from a few large ones.

### 2. Countries as Outcomes, Not Decisions

Our portfolio construction process recognizes that it is possible for the model to gravitate toward liking or disliking stocks from a particular country. That is why we carefully build our strategy to manage this risk, recognizing dispersion among countries can swing sharply at any moment.

### 3. Systematic Rebalancing as Dispersion Evolves

High dispersion is not static. Leadership shifts, reversals occur, and correlations change. Quant strategies are built to adapt. Systematic rebalancing allows exposures to evolve as new information is reflected in prices and fundamentals, without anchoring to prior views or relying on discretionary regime calls.

## Process Over Prediction

The forces driving elevated country dispersion in emerging markets — geopolitical fragmentation, industrial policy, divergent development paths, and evolving capital markets — are unlikely to dissipate quickly. If anything, they suggest a regime in which dispersion remains a defining feature rather than a temporary anomaly.

In such an environment, success depends on managing these uncertain macro risks while simultaneously harvesting stock-level opportunities in inefficient parts of the market. Strategies utilizing a disciplined, diversified, and systematic approach are best suited to exploit these market dynamics.

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