EMERGING MARKETS SERIES | PART 1

EMERGING MARKETS, REFRAMED

How stronger fundamentals and shifting global dynamics are reshaping EM's portfolio role

- The defining characteristics of Emerging Markets are changing.
- A more fragmented world calls for a new investor playbook.
- Old assumptions may no longer explain new realities.

Within a few years, the U.S. could be spending as much of its budget servicing debt as a median high-yield emerging market country. It is a stunning role reversal, and a useful starting point for rethinking the case for EM.

For most of this century, emerging markets have been treated as a cyclical allocation tied to commodities, China's industrialisation and global risk appetite. That framing now looks increasingly dated. Many EM economies are now more self-sustaining, supported by deeper local capital markets, stronger policy frameworks, rising domestic demand and higher value-add manufacturing. Rather than a leveraged play on global liquidity, EM now represents a broader and more differentiated investment universe.

Emerging Markets - Then vs. Now

Driver	Old EM	New EM
Growth catalysts	Externally driven by commodities, China's industrialisation and exports to the U.S. and Europe.	More diversified, led by domestic demand, regional trade, services and higher value-add manufacturing.
Financing and markets	Reliant on foreign capital, hard-currency debt and shallow local markets.	Deeper local capital markets and greater ability to fund in domestic currencies.
Policy frameworks	Weaker institutions, uneven reforms and recurring vulnerabilities to policy slippage.	More credible monetary frameworks, better banking supervision and improved fiscal discipline.
External environment	Supported by globalisation, China's WTO entry and healthier developed-market balance sheets.	Shaped by DM fiscal pressure, geopolitical fragmentation, friendshoring and South-South trade.
Portfolio role	Largely treated as a high-beta, risk-on allocation.	A more differentiated source of growth, income, diversification and inflation-sensitive exposure.

EM'S ROLE IN A REWIRED WORLD

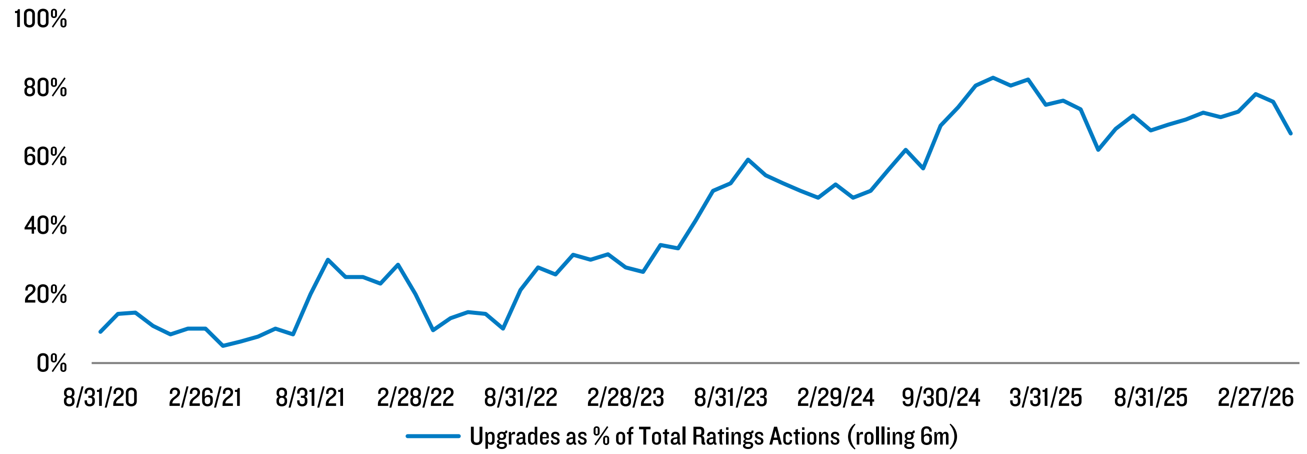
The case for EM is also being strengthened by the changing developed-market backdrop. Many DM economies face rising debt-servicing burdens, ageing populations, political strains and a more constrained policy environment. The IMF's April 2026 Fiscal Monitor notes that global interest spending has climbed from around 2% to nearly 3% of GDP in just four years, with advanced-economy debt trajectories driving global public debt towards 100% of GDP by 2029, a level last seen in the aftermath of World War II.[1]

At the same time, several EM economies have entered this period with healthier public finances, improving fiscal balances and credible monetary frameworks. While these strengths are not universal, they challenge some long-held assumptions about the relative economic positions of developed and emerging markets. For investors heavily concentrated in U.S. or developed-market assets, EM exposure can help diversify fiscal, demographic and valuation risks without requiring a wholesale retreat from developed-market innovation or market depth.

This shift is changing EM's portfolio behaviour. Correlations with DM equities and bonds have weakened as the old "risk-on/risk-off" pattern has become less dominant in a more multipolar global economy. Dispersion within EM has also widened, with markets increasingly shaped by domestic policy choices, sector composition, currency dynamics and local capital-market depth. EM assets remain volatile and can still underperform when global risk appetite deteriorates, but stronger fundamentals have helped many markets recover more quickly than in past cycles. For asset allocators, the implication is that EM may still carry volatility, but its behaviour in stress periods is becoming less one-dimensional.

On an Upswing

Sovereign Rating Upgrades as a % of Rating Actions



Source: Moody's Investors Service, S&P, and Fitch Ratings

Common EM Misconceptions:

1. **EM = high-risk, high-beta play:** Today's EM offers a range of outcomes. Some EM assets can provide lower volatility or defensive characteristics (e.g. local bonds supported by domestic institutions, or infrastructure assets with stable cashflows), and correlations are falling (so EM won't always crash when U.S. markets wobble).
2. **EM = one big homogeneous bloc:** EM is not monolithic; it spans more than 20 major countries with vastly different economies, policies, and cycles. Dispersion within EM is high, creating opportunities for active management.
3. **EM success = commodity boom or China growth:** The modern EM story is far broader. Commodities and China are important, but the real novelty is in other EM economies where internal engines and reforms are paying off. Indeed, China's growth is now slower, and not every EM has reformed but others (India, Southeast Asia, Latin America's smaller economies, Gulf states, etc.) are stepping up to drive the next phase.
4. **There is always time to rotate into EMs later:** The regime shift is already underway, making early strategic positioning important. Valuations in several EM assets remain reasonable historically (e.g. EM equities still trade at over a standard deviation P/E discount to DM) and growth differentials are widening now.

[1] IMF, April 2026, Fiscal Policy Under Pressure: High Debt, Rising Risks

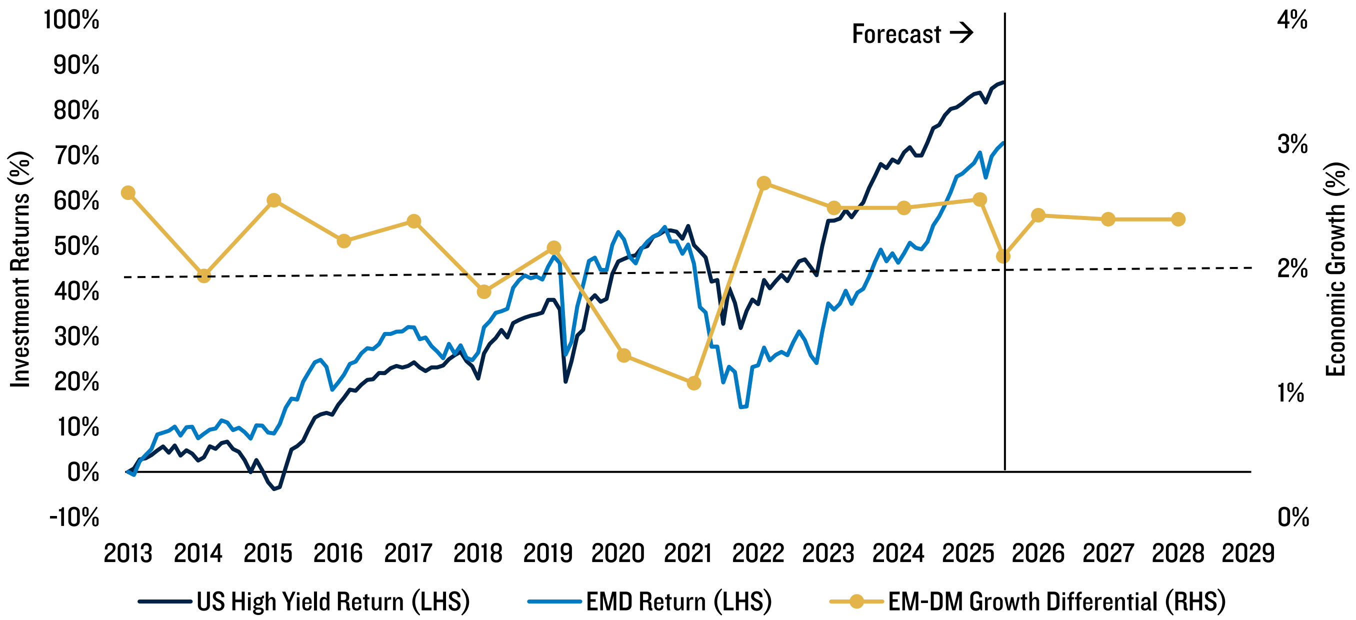
While the internal transformation of EM is underway, a growing secondary theme is playing out, i.e. EMs are becoming essential players in global mega-trends. Some of them are:

The "Great Power Competition" Backdrop: The geopolitical rivalry between major powers is reshaping trade and capital flows, often to the advantage of select EM economies. "Friendshoring" and China+1 strategies are prompting multinational firms to invest in manufacturing capacity across Southeast Asia, India, Mexico and others. The more durable point for investors is not any single geopolitical forecast, but the broader reconfiguration of supply chains, which is helping EM countries move up the value chain in manufacturing and services rather than remain low-cost exporters of basic inputs.

Resources & the Next Commodity Upswing: The world is entering a new commodities cycle shaped by years of underinvestment in supply and rising demand for critical minerals, energy and compute capacity. Unlike the 2000s, EM economies benefit not only by exporting raw materials, but also by capturing more value along the chain. Indonesia's shift from exporting raw nickel to processing it domestically is one example of how EM economies are upgrading their role in global production chains. AI's infrastructure build-out will still demand far more copper, uranium, rare earths, semiconductors and reliable electricity, linking the digital transition directly to the physical resources and production capacity concentrated across EM.

AI infrastructure and technology supply chains: The more investable AI story in EM is less about consumer applications and more about the physical build-out required to support them. Taiwan and Korea sit at the heart of this shift through companies such as TSMC, Samsung and SK Hynix, which supply the semiconductors, high-bandwidth memory and advanced manufacturing capacity needed by global hyperscalers. The opportunity also extends beyond chips: data centres require networking equipment, industrial components and vast, reliable power. That links AI infrastructure to energy, uranium and other critical-resource exposures, including EM producers that sit upstream of the digital economy. From a forward earnings perspective, MSCI EM trades at a nearly 50% discount to its U.S. counterpart.[2]

The Great Divergence



Sources: Growth data IMF as of June 2026. Returns data Bloomberg as of June 30, 2026. **The forecasts begins June 30, 2026. The forecasts presented herein are for informational purposes. There can be no assurance that these forecasts will be achieved.**

PORTFOLIO IMPLICATIONS

The following represents a simple framework that can be applied to EM asset investing, focused on durable portfolio-construction themes rather than short-lived geopolitical calls.

Structural growth advantage: EM's improved fundamentals now support opportunities across equities, debt and real assets. Stronger domestic demand, deeper intra-EM trade, better governance and

[2] MSCI USA Factsheet; MSCI EM Factsheet

critical roles in AI infrastructure supply chains support earnings growth in equities. In debt, credible policies and lower inflation are improving sovereign credit trends. In real assets, urbanisation, power demand and data-centre investment create long-term infrastructure opportunities.

Resilience: EM can help diversify portfolios concentrated in richly valued or macro-challenged DM markets. Selected EM equities, local bonds, commodity-linked currencies and real assets may provide differentiated sources of return and potential ballast if U.S. markets face higher-for-longer rates, fiscal pressure or a reversal in AI-led concentration.

Multiple Ways to Win: EM offers different exposures for different objectives: high real yields in local bonds, secular earnings growth in companies exposed to semiconductors, high-bandwidth memory, industrial automation and data-centre supply chains, and inflation-sensitive exposure through commodities, currencies and real assets linked to copper, uranium, rare earths and power demand.

Active Management Matters: Greater dispersion across countries, sectors, currencies and issuers raises the burden of proof for passive EM exposure. Benchmark investors gain automatic exposure to dominant AI hardware names such as TSMC, Samsung and SK Hynix, but also inherit greater concentration risk. The top three companies in the MSCI EM equity index account for nearly a third of the index.[3]

In this environment, the question is less whether a manager has the right macro call on China, India, Brazil or Korea and more whether the process can exploit inefficiencies consistently across a large, heterogeneous universe. Diversified, stock-oriented approaches may be better placed to capture idiosyncratic opportunities while managing concentration risks and tracking error.

EM as an asset class has entered a new regime of performance, just as the global macro regime is shifting. The next article in this series will examine how shifting supply chains, expanding manufacturing capacity, re-globalisation and friendshoring are reshaping the opportunity set across emerging markets.

[3] MSCI EM Index Factsheet

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The MSCI Emerging Markets Index captures large and mid-cap representation across 24 Emerging Markets (EM) countries. Investors cannot invest directly in an index.

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