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 United States 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 emerging markets.

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. EM now represents a broader and more differentiated investment universe — one that offers growth, income, diversification and inflation-sensitive exposure in a single opportunity set.

Growth catalysts that were once externally driven — commodities, exports to the U.S. and Europe, and China's expansion — are increasingly domestic, regional and services-led. Financing that once relied on foreign capital and hard-currency debt is now underpinned by deeper local markets and the ability to fund in domestic currencies. Policy frameworks that were historically vulnerable to slippage are, in many cases, more credible, with better banking supervision and improved fiscal discipline. For allocators still working from the old playbook, the risk is misreading a structural change.

EM'S ROLE IN A REWIRED WORLD

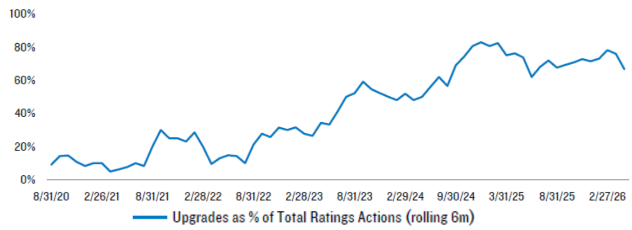
The case for EM is also being strengthened by the changing developed-market backdrop. Many DM economies face rising debt-servicing burdens, ageing populations, political strains and a more constrained policy environment. The IMF's April 2026 Fiscal Monitor notes that global interest spending has climbed 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 the Second World War.

At the same time, several EM economies have entered this period with healthier public finances, improving fiscal balances and credible monetary frameworks. These strengths are not universal, but they challenge some long-held assumptions about the relative 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.

This 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. Asset price dispersion within EM has widened, with markets increasingly shaped by domestic factors. 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 making 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

GLOBAL MEGA-TRENDS

EM economies are becoming essential players in the global mega-trends that will define the coming decade.

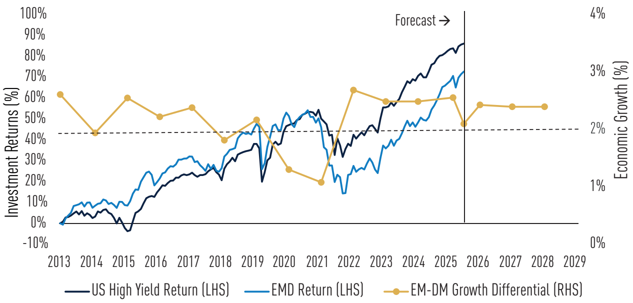
Great power competition. Geopolitical rivalry between major powers is reshaping trade and capital flows, often to the advantage of select EM economies. "Friendshoring" and China+1 strategies are prompting multinationals to build manufacturing capacity across Southeast Asia, India and Mexico. The broader reconfiguration of supply chains that is helping EM countries move up the value chain rather than remain low-cost exporters of basic inputs.

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 a case in point. The AI build-out will demand far more copper, uranium, rare earths, semiconductors and reliable electricity, linking the digital transition directly to resources concentrated across EM.

AI infrastructure and technology supply chains. The more investable AI story in EM is 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 that global hyperscalers depend on. The opportunity extends beyond chips to networking equipment, industrial components and vast, reliable power — connecting AI infrastructure to energy and critical-resource exposures upstream of the digital economy. On a forward-earnings basis, MSCI EM trades at close to a 50% discount to its U.S. counterpart.

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

A simple framework can be applied to EM investing — simple but durable.

Structural growth advantage. Improved fundamentals now support opportunities across equities, debt and real assets. Stronger domestic demand, deeper intra-EM trade, better governance and critical roles in AI supply chains support earnings growth in equities; credible policies and lower inflation are improving sovereign credit trends in debt; and urbanisation, power demand and data-centre investment create long-term opportunities in real assets.

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 returns and potential ballast if US markets face higher-for-longer rates, fiscal pressure or a reversal in AI-led concentration.

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, but also inherit concentration risk — the top three companies in the MSCI EM index account for nearly a third of it. The question 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 risk and tracking error.

EM has entered a new performance regime as the global macro order shifts. Its defining characteristics are changing, a more fragmented world demands a new investor playbook and old assumptions no longer explain new realities.

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