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Emerging Markets Equities Handbook

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Foreword

Emerging markets (EM) have historically carried a reputation that no longer reflects reality. Many investors still picture EM as just being a handful of volatile frontier economies, when in fact the bulk of EM equity exposure today lies in large, advanced, markets such as China, Korea, Taiwan and India. At the same time, long held beliefs about the safety and diversification of developed markets have been increasingly challenged by the extreme concentration of mega-cap stocks in the US, declining institutional and fiscal credibility, and increasing geopolitical risk.

This handbook seeks to debunk the outdated EM myths we hear – presenting a clear picture of what EM equity investing truly looks like today. We aim to make EM more accessible by showing how the asset class has evolved, why its perceived risks have changed, and where real long term opportunities lie.

The goal of the handbook is simple – to give you the clarity and confidence to view EM not as an exotic and optional corner of the equities market but instead as a vital, and often misunderstood, source of global growth potential and diversification in a well-balanced portfolio.

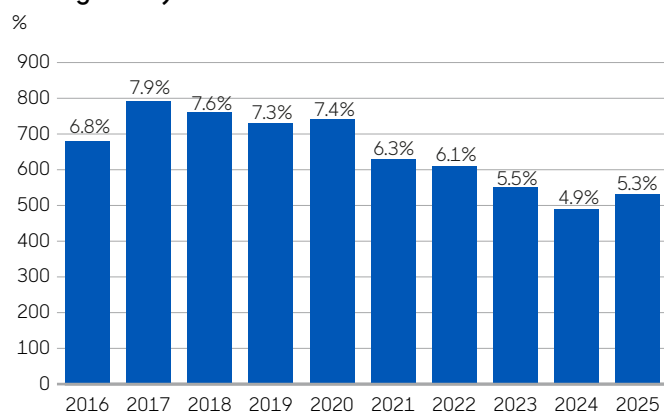


Introduction

EMs are no longer a peripheral story – we believe they’re central to the next cycle of global innovation and diversification. After a decade of underperformance, EMs regained momentum in 2025, outperforming developed markets (DM) by more than 10 percentage points.

Perceptions are now shifting. Volatility between EM and DM has converged, and policy developments last year helped redirect capital back towards EM after a decade of declining allocations.

Figure 1: Declining EM global AUM (assets under management) share



Source: EPFR Global, MSCI, September 2025.

We believe this trend can continue. Several structural forces that have been building for years are now aligned in EM’s favour. We summarise them as the **Three Cs**:

| | |
|----|---|
| 01 | Carry (weaker dollar): EM economies typically benefit from a softer US dollar through improved purchasing power, stronger capital inflows and healthier domestic financial conditions. |
| 02 | Capex: EM earnings tend to correlate with global investment growth. Given their leading resource and manufacturing bases, an EPS growth premium is developing as we invest in AI, supply chain security and energy transition. |
| 03 | Cheap: Valuations across EM remain well below long term averages and continue to trade at a substantial discount to developed markets. |



The Three Myths of EM



With these tailwinds in place, now is an ideal moment to reassess the role EM can play in a globally diversified portfolio.

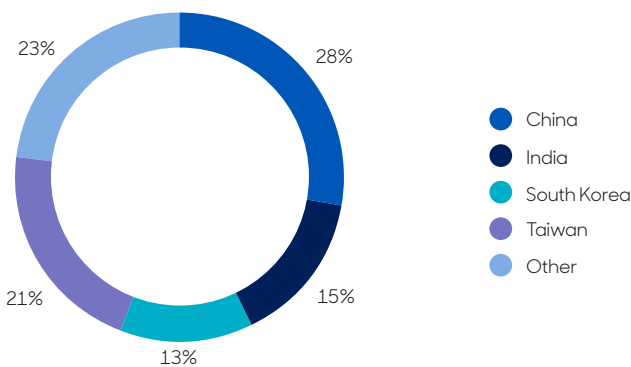
1. EMs are too risky

EMs have long-carried a reputation for instability, shaped by memories of past crises in Latin America and Asia. These events still influence investor perceptions today. Yet the fundamentals of EM have changed materially over the past two decades.

Following extensive policy reforms, stronger institutions and more disciplined balance sheets, EMs have moved well beyond the era of excessive borrowing, boom bust cycles and extreme currency volatility. Today, the bulk of MSCI EM Index exposure is in large, export driven economies such as China, Korea, Taiwan and India. Together they represent around 77% of the index and share characteristics more commonly associated with DMs: stable currencies, deepening capital markets and an ongoing programme of market reforms.

Figure 2: EMs are led by larger, more sophisticated economies

MSCI EM Index Country Exposure (%)



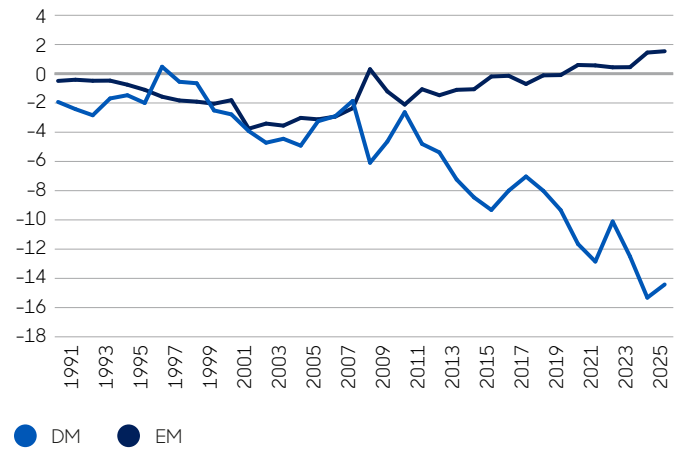
Source: Aberdeen, MSCI, December 2025.

At the same time, the risk gap between EM and DM has narrowed significantly. Three year rolling volatility across the two groups has converged, reflecting improved macro stability across EM.

A key driver of this stability is balance sheet strength. EM corporate leverage remains far lower than in DM – around 23% compared with 72% in the US – while many EM sovereigns maintain strong current account positions and robust foreign-exchange (FX) reserves. Over the past decade, this has led to meaningful improvement in net international investment positions (NIIP), supporting currency stability and reducing reliance on foreign funding.

Figure 3: Relatively strong NIIP across EM

Net International Investment Position (% of world GDP)



Source: FactSet, IMF, Aberdeen, 31 December 2025.

Large sovereign wealth funds across the Middle East are further underpinning EM's resilience. Persistent surpluses have allowed these investors to channel capital into domestic development and strategic partnerships across Asia. This, combined with structurally stronger EM balance sheets and reduced dependence on the US dollar, has created a more self sustaining financial ecosystem.

In short, EMs today are fundamentally more stable, better capitalised and less externally vulnerable than many investors assume. The nature of risk has evolved – yet perceptions have not.

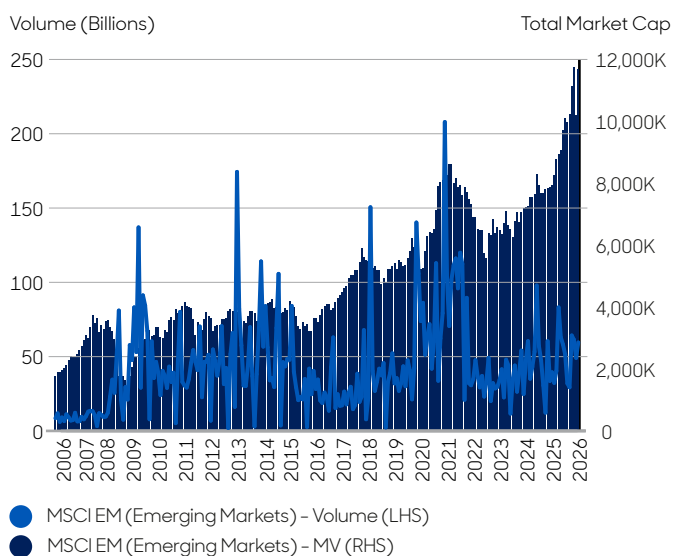


2. EMs don't have enough liquidity

Concerns about liquidity in EMs are often based on memories of past volatility rather than the reality of today's market structure. EM equity index market capitalisation has more than doubled since 2017, and overall market liquidity has increased as the asset class has matured. Ironically, this improvement in market breadth and depth has occurred as international allocations have hit record lows.

Figure 4: EM market cap continues to set new records

EM Market Cap and Volume

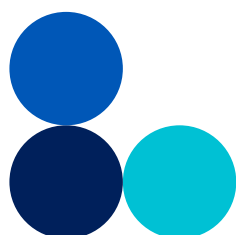


Source: FactSet, IMF, Aberdeen, 31 December 2025.

A key driver of this improvement is the rise of domestic participation. In China, for example, retail investors account for around 28% of the market, while foreign institutional ownership remains low. This growing local investor base provides a stable source of liquidity and reduces reliance on short term global flows.

Importantly, despite this progress, global allocations to EM remain near multi decade lows. If investors simply moved back toward long term average weights, it would unlock significant capital inflows into the asset class.

In reality, EMs are far more liquid, deeper, and more resilient than many investors appreciate – creating both improved trading conditions and a meaningful opportunity for reallocation.

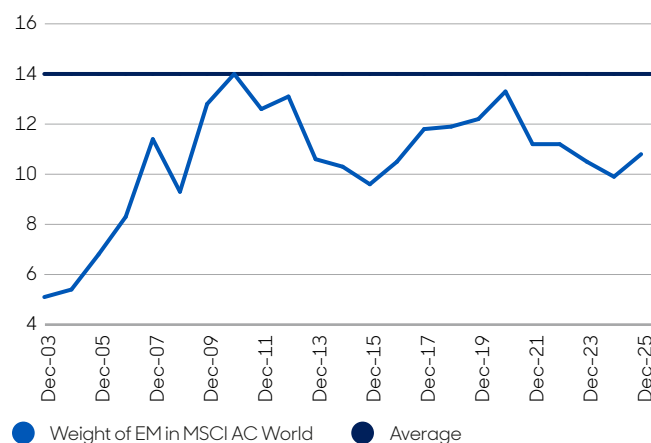


3. EMs are too small to matter

A common misconception is that EMs are a peripheral part of the global economy. In reality, they are central to global growth and production. If equity portfolios were weighted by economic size, EMs would represent more than 61% of global GDP (PPP) and have contributed roughly 70% of global economic growth in recent years. Despite this, most global investors remain materially underexposed.

Figure 5: EMs are underrepresented in global indices

EM as a % of ACWI (MSCI Weight)

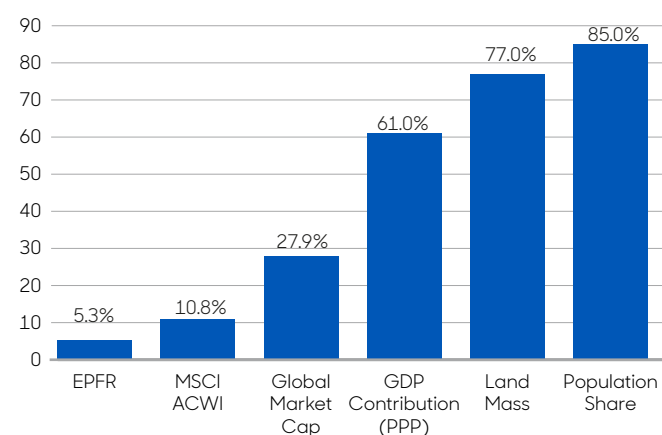


Source: Jefferies, FactSet, MSCI, 2025.

EMs are equally significant from a market capitalisation perspective. They account for around 24% of global equity market cap, supported by a free float market of approximately US\$34 trillion. Yet due to index methodology and accessibility adjustments, EM's weight in MSCI ACWI Index is less than half that level. China alone represents around 12% of global free float, but only 3% of ACWI.

Figure 6: Low allocations despite strong EM positioning

EM allocation and current positioning (%)



Source: Bloomberg October 2021, EPFR Global October 2021, IMF 2026, World Bank.

The gap between EM's economic importance and its representation in global indices – and in investor portfolios – remains substantial. Far from being too small to matter, EMs are too large and too influential to ignore.

The Three Realities of EM



EMs can offer the potential for more alpha

EM equities remain one of the most attractive areas for active management. They are broad, diverse and relatively under researched compared with DMs. This creates meaningful dispersion in company performance and frequent mispricing – conditions where selective, research driven approaches can add significant value.

Three structural features make EM particularly supportive for active investors:

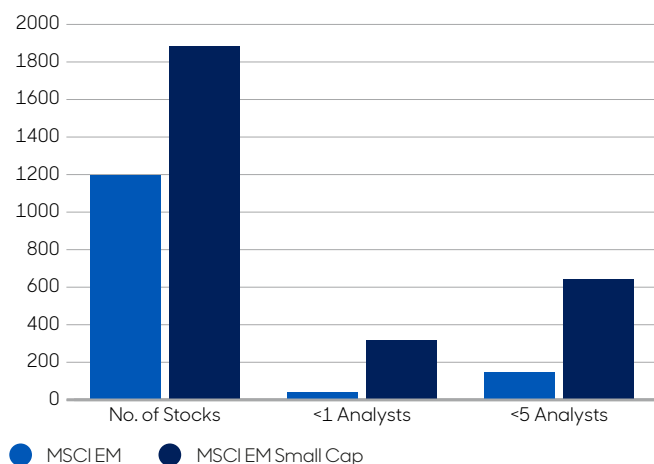
1. Risks that need to be managed

Macro, policy and currency cycles differ widely across EMs. Passive strategies simply absorb these risks, while active managers can avoid weaker markets and focus on improving ones.

2. Information gaps create opportunity

Analyst coverage remains shallow in many countries, and company disclosures are inconsistent. This creates genuine information asymmetry, which can reward investors who do deeper fundamental research.

Figure 7: EM are significantly under-researched



Source: MSCI, 2025.

3. Pitfalls for passive investors

EM indices contain many companies that are not run in the interests of shareholders. There are some well-known offenders that can reach significant index weights. For example, SOEs (state-owned enterprises) are around 12% and Korean Chaebols are roughly 7% of the EM index. These are not all bad companies, but corruption and political interference are much more likely in these areas.

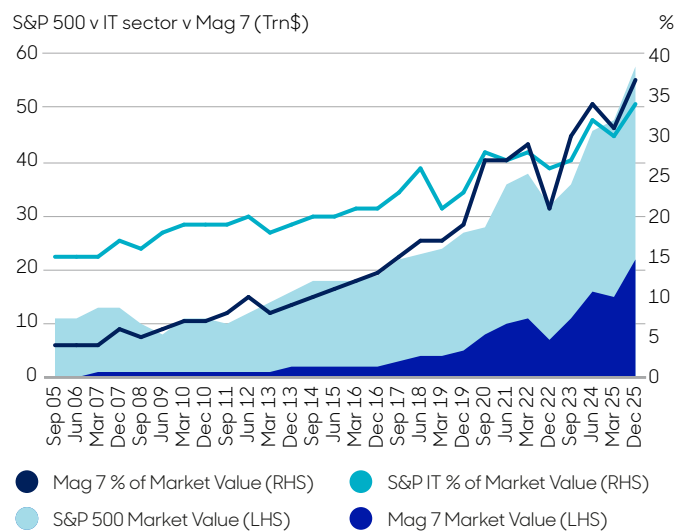
In this environment, on-the-ground insight is essential. We meet around 1,500 companies each year and review nearly 3,000 investable EM names. This helps us identify quality businesses early and avoid structural risks that passive strategies cannot screen for.

With more dispersion, more inefficiency and more change than DMs, EMs can offer a consistent and repeatable source of alpha for active investors.

EMs offer greater diversification

Despite the 'global' label, many portfolios today are heavily concentrated in DMs – particularly the US. A small group of mega cap technology stocks now dominates global equity indices, leaving portfolios exposed to a single growth driver and a narrow set of risks.

Figure 8: US equities are increasingly more concentrated in the Magnificent 7



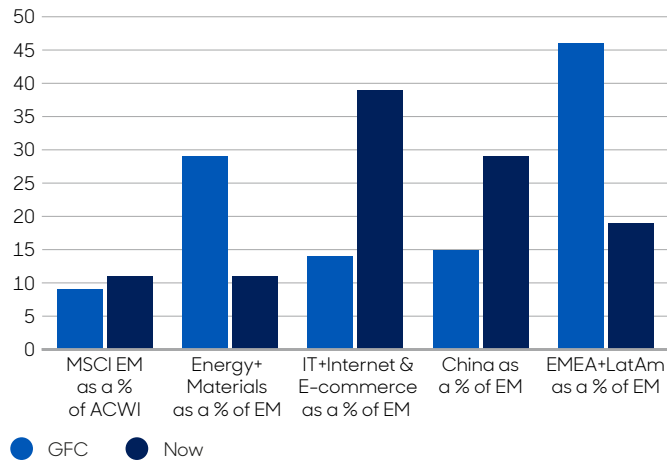
Source: FactSet, S&P500 and Magnificent 7 stocks, December 2025.

EMs provide genuine diversification. Their growth is driven by different forces – demographics, domestic demand, the energy transition, and structural reforms – rather than reliance on the same technology giants that dominate DMs. EMs also remain highly diverse within the asset class. The Middle East is reducing its dependence on oil, Latin America continues to benefit from commodity linked earnings, and North Asia offers world class technology and industrial leadership. This variety reduces macroeconomic concentration and broadens the opportunity set.

Sector evolution

Figure 9: EM today is more developed and diverse

The new economy and China dominated the last cycle (%)



Source: MSCI, DataStream, UBS 2025.

Sector composition has evolved significantly. Since the Global Financial Crisis, EM exposure has shifted toward technology and services, while traditional sectors like energy and materials have become less dominant. Yet this evolution remains dynamic. In 2025, renewed demand for metals such as copper, aluminium and rare earths – alongside higher gold and silver prices – highlighted how EMs continue to span both the old and new economies.

Economic diversification is also accelerating. Countries such as Saudi Arabia and the United Arab Emirates are expanding non oil sectors including tourism, entertainment and infrastructure. At the same time, Latin America continues to benefit from global infrastructure spending and the energy transition. EM earnings are far less sensitive to commodity cycles than investors often assume, with growth drivers varying markedly across regions.

This diversity means EM equity returns frequently diverge from those of DMs, particularly during periods of heightened volatility. EM doesn't need to replace DM exposure, but it can complement it by offering a different set of growth engines and structural trends. The message is symbiosis: pairing EM and DM can enhance risk adjusted returns by tapping into sources of growth that are underrepresented in most global portfolios.



¹ Source: Bloomberg consensus data, April 2026.

EMs are at the forefront of global structural change

A powerful set of structural forces is reshaping global capital flows, supply chains and investment cycles. The idea that EMs simply follow the lead of developed economies is increasingly outdated. MSCI EM delivered 10.4% earnings-per-share growth, with consensus expecting a further ~32%¹ in 2026. We believe annualised EPS growth of 12-15% is achievable over the coming cycle. The earnings growth premium is tied to a global revival in real economy investment – what we see as a new capex supercycle. EM earnings have historically shown a strong correlation with capex.

Today's investment wave is fuelled by several long-term trends: decarbonisation, supply chain reconfiguration, digital infrastructure, re-industrialisation and increased defence spending. EM economies offer the industrial depth, technical capability and resource base needed to support this transformation.

Beyond capex, we see three structural drivers where EM is uniquely positioned to lead:

Technological developments – EMs are increasingly central to the world's technological buildout. North Asia provides the hardware backbone of the AI cycle, while China continues to build a full domestic AI stack and broaden innovation across multiple industries. EM is no longer simply a destination for outsourced manufacturing – many EM economies have moved up the value chain and now play a critical role in enabling global technological progress.

Electrification – according to the International Energy Agency, global electricity demand is expected to grow 3.6% annually through 2030 – 50% faster than in the previous decade. Digital infrastructure, industrial electrification and rising consumer usage are driving this acceleration. EM is well-positioned to supply both the infrastructure and the raw materials required. From solar and electric-vehicle leadership to the world's most important deposits of copper, aluminium and critical minerals, EM countries sit at the centre of the global electrification.

Consumption – consumer demand remains one of the most powerful engines of global growth. Emerging economies account for the majority of the world's population, and rising incomes are transforming spending patterns. Domestic brands in EM are flourishing. Demand is expanding across goods – from apparel to autos – and increasingly across services such as housing, healthcare and entertainment. This creates a long-duration growth tailwind supported by demographics and urbanisation.

Figure 10: More people live inside the circle than outside



Source: Aberdeen, February 2026.

Taken together, these forces place EM at the forefront of global structural change – not behind it. The asset class offers opportunities in a wide range of investments shaping the next decade of growth, providing access to a diverse set of changes that are hard to replicate in most global portfolios.



Conclusion

Today's EM equities bear little resemblance to the asset class many investors still imagine. The outdated view of them as immature, volatile or peripheral sits at odds with the reality of an asset class that is now central to global growth, technological progress and long term capital formation.

Over recent decades, EM economies have strengthened their institutions, deepened their financial systems and reduced external vulnerabilities. At the same time, global dynamics have shifted. DMs have become increasingly concentrated, while EM has evolved into a broader, more liquid and more structurally important opportunity set.

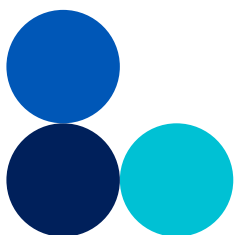
Yet allocations have not kept pace with this change. EM remains significantly underrepresented in global portfolios, despite its scale, resilience and contribution to global GDP and earnings. This gap between perception and reality represents one of the most compelling opportunities for long term investors.

Active management is well-suited to navigate this landscape. EM's breadth, dispersion and structural change create a rich environment for bottom up stock selection – enabling investors to manage risk while capturing the diverse drivers of growth across regions and sectors.

With the ongoing evolution and sophistication of the asset class, now is an opportune moment to reassess the role of EM in a well balanced portfolio. Rebalancing towards EM can improve diversification, enhance return potential and position investors to benefit from the structural trends shaping the next decade.

The opportunity is clear. The fundamentals are in place. For investors willing to look beyond outdated perceptions, EM offers a powerful source of growth potential, diversification and long term value.

Now is the time to take a fresh look – and ensure EM is working for your portfolio.



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