Emerging Markets—The New Engine of Global Growth

Investment Management

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We believe the case for emerging markets (EMs) has become increasingly compelling. Between a weakening U.S. dollar, strengthening fundamentals, and attractive valuations, the asset class appears well positioned for renewed investor interest, with recent outperformance suggesting EM equities may be at the start of a long-awaited recovery. But because EM investments generally involve greater volatility and risk than developed market (DM) investments, active management is key.

Five key themes help make the investment case for EMs:

1. Structural Dollar Decline
2. Earnings-Led Rally
3. Underowned and Undervalued
4. The Global AI Buildout
5. Multiple Structural Growth Pillars Beyond AI

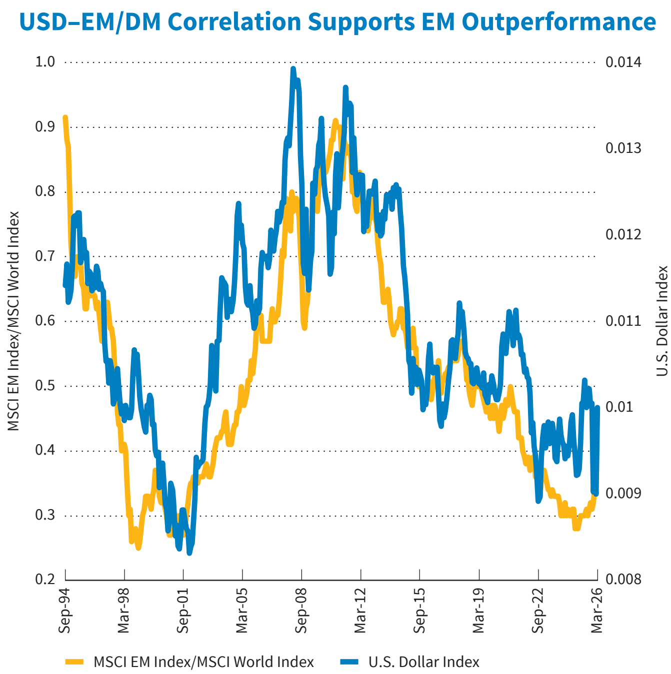
Theme 1: Structural Dollar Decline

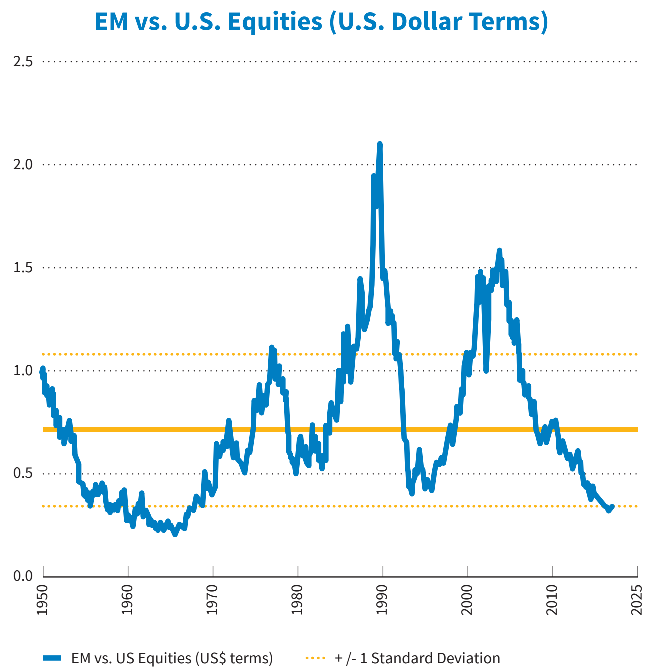
- The U.S. dollar's 2025 decline was the worst calendar-year performance in over 20 years, and the conditions behind it are still in place.
- The cause is structural: the United States is simultaneously running a large fiscal deficit and a large current account deficit, which together accounts for approximately 6% to 7% of gross domestic product (GDP). That means the government is spending well beyond its tax revenues while the economy imports significantly more than it exports. These imbalances don't resolve in a quarter or two.
- Real rate differentials, which is the key driver of dollar strength during the Fed tightening cycle, have now peaked and are moving against the U.S. dollar as well.
- It's important to note that historically, periods of sustained EM outperformance relative to DMs have coincided with a weakening dollar. That relationship has held true across various global economic environments.
- In other words, a softer dollar eases EM financial conditions, reduces dollar-denominated debt burdens, supports commodity exporters, and pulls capital back into higher-growth markets.
- But in our view, EMs don't need a dollar collapse to outperform; the asset class just needs the trend to continue.
- We believe that short-term spikes driven by geopolitical safe-haven demand (including around Iran) have not reversed the structural picture, though geopolitical events can contribute to periods of heightened volatility across EMs.
- We believe the current dollar setup provides macro support in favor of adding EM exposure right now.

EXHIBIT 1

As the Dollar Weakens, the Case for EMs Strengthen

The historically inverse relationship between the U.S. dollar (USD) and EM relative performance suggests that dollar weakness is a powerful tailwind for EMs.





Sources: BofA, CLSA, Bloomberg, and William Blair, as of May 2026. **Past performance is not indicative of future returns.** A direct investment in an unmanaged index is not possible. See back page for index information.

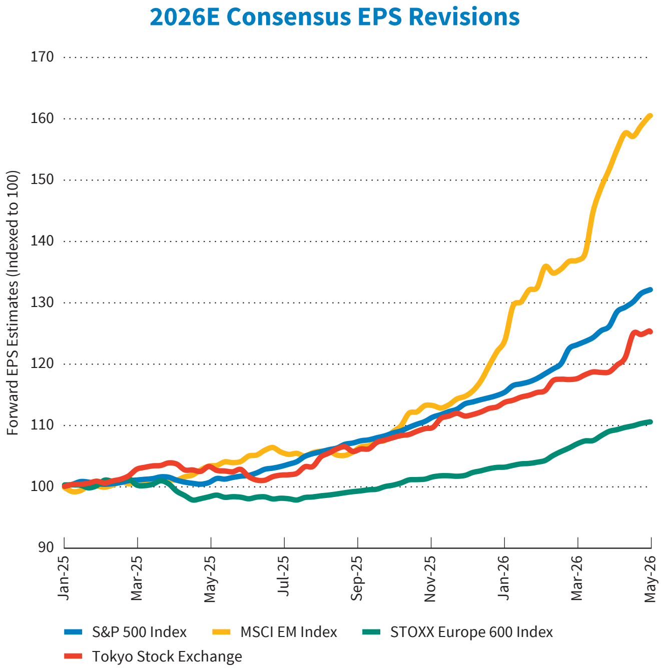
Theme 2: Earnings-Led Rally

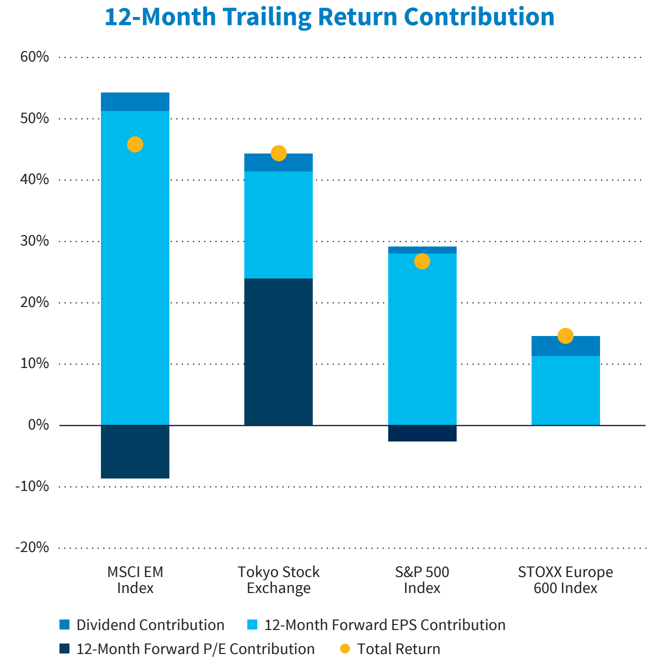
- EMs' 2025 rally was built on strong earnings, not hope or cheap money. We believe that's a meaningful distinction.
- EM EPS growth outpaced DM EP growth in 2025. The growth gap between EMs and DMs is real and it has widened, driven in part by North Asia's leadership in the AI supply chain. While this contribution is concentrated, it reflects participation in a multi-year structural capital expenditure (capex) cycle rather than a temporary demand surge.
- Crucially, total shareholder returns in EMs have been predominantly driven by earnings growth, with limited reliance on multiple re-ratings. As a result, EM performance has been more directly linked to underlying corporate profitability rather than changes in investor sentiment.
- Importantly, periods where EM earnings growth exceed that of DMs have historically been associated with sustained relative outperformance. The current widening earnings differential is, therefore, supporting the case for continued leadership, in our view.
- In contrast to the past decade, where EM rallies were often narrow and episodic, we are seeing a more balanced contribution to earnings growth. We believe this combination of earnings leadership, improving quality, and structural support provides a more durable foundation for potential continued EM outperformance, although EMs remain exposed to political, regulatory, and macroeconomic risks that can affect individual countries and sectors differently.

EXHIBIT 2

Quality of Returns Favor EMs: Earnings-Driven Gains vs. Multiple-Dependent DMs

EM consensus EPS estimates have surged ahead of DM peers in 2026, and the decomposition of total shareholder returns show EM gains are being driven by fundamental earnings growth rather than multiple expansion.





Sources: Goldman Sachs, Bloomberg, I/B/E/S, and William Blair, as of May 2026. For left chart, forward 12-month EPS estimates are shown for each index, rebased to 100 as of January 1, 2025. **Past performance is not indicative of future returns.** A direct investment in an unmanaged index is not possible. See back page for index information.

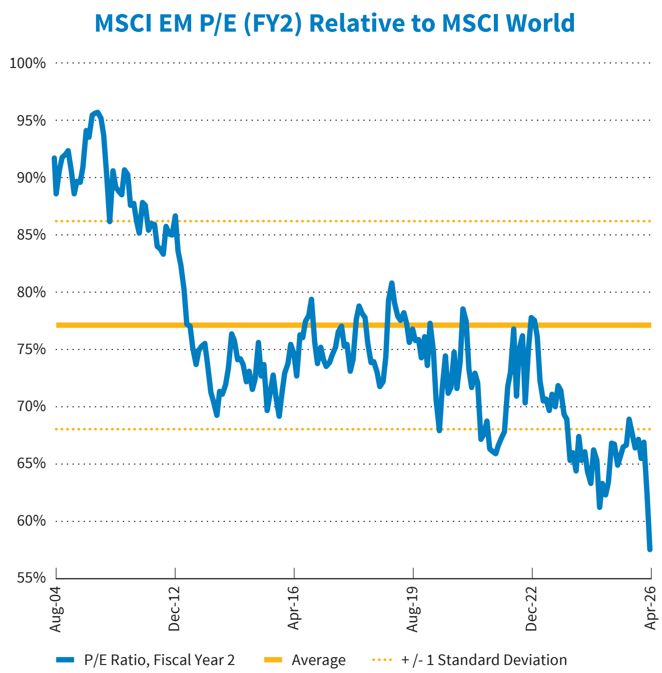
Theme 3: Underowned and Undervalued

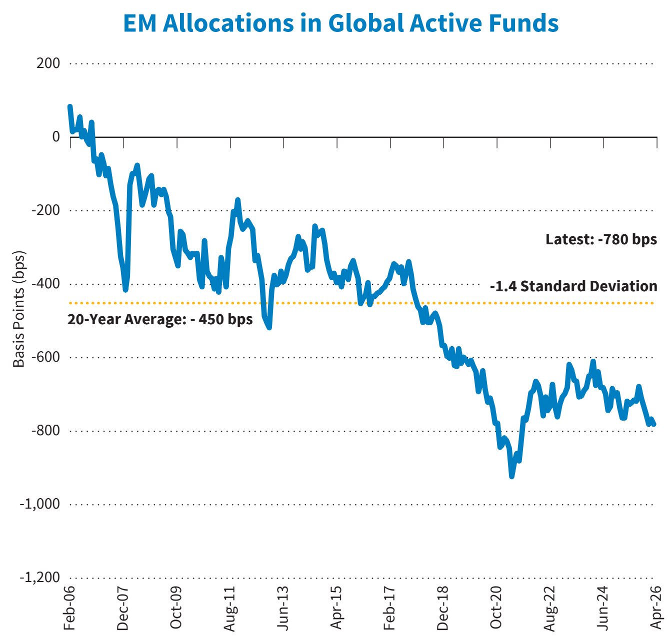
- Even after a strong 2025, EMs still trade at a meaningful discount to DMs based on forward price-to-earnings.
- We believe that discount appears increasingly compelling, as the composition of EMs have materially changed in favor of high growth sectors. Today, the index carries significantly more technology exposure and far less balance sheet leverage than it did in previous cycles, so investors are getting a better asset class at a cheaper price.
- In addition, active global funds are still meaningfully underweight EMs relative to benchmark, and that underweight has been building for a long time.
- Cumulative outflows from EM equities ran into the hundreds of billions of dollars over the past decade, and the reversal that began in 2025 appears measured and in its early stages. We do not view this as the kind of euphoric inflow that could signal a peak.
- We believe this is re-engagement, not capitulation buying, as the rotation back into EMs has room to run simply because many allocators haven't made it yet.
- It is also important to view this in a historical context. Relative EM vs. DM performance has tended to move in long cycles. Following approximately eight years of underperformance, we believe EMs may now be in the early innings of a new period of relative outperformance. Of course, there can be no assurance that historical market cycles will repeat or that relative performance trends will persist.
- We believe the combination of discounted valuations, improving earnings dynamics, low positioning, and cyclical timing creates a compelling technical and fundamental backdrop to support the asset class.

EXHIBIT 3

EM Equities Remain Cheap Relative to DMs: Low Valuations Meet Sizable Underweights

The MSCI EM Index's two-year forward P/E has traded at a sustained discount to the MSCI World Index, reflecting a persistent valuation gap between EM and DM equities. Meanwhile, global fund managers remain significantly underweight the asset class.





Sources: MSCI, FactSet, EPFR, Goldman Sachs, and William Blair, as of April 2026. For right chart: global funds include both global and global ex-USA mandates; total AUM = $1.1 trillion. **Past performance is not indicative of future returns.** A direct investment in an unmanaged index is not possible. See back page for index information.

Theme 4: The Global AI Buildout

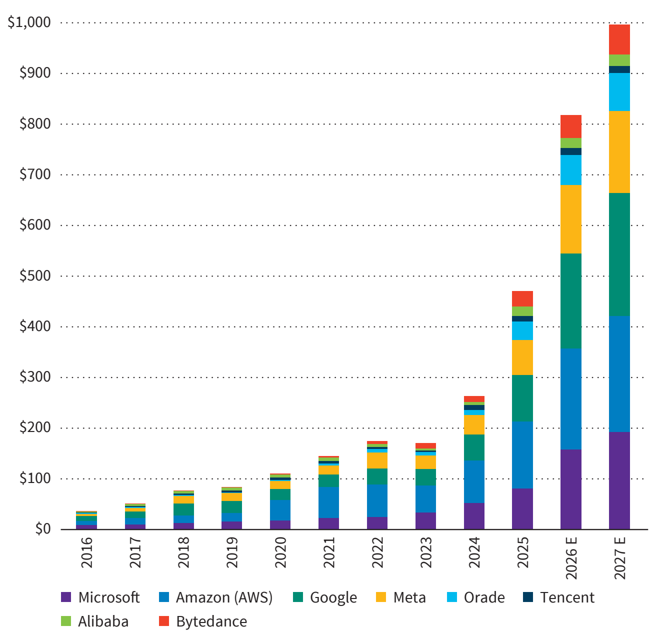
- We believe the global AI buildout could end up being the largest infrastructure investment cycle in the history of technology. Hyperscalers are expected to spend more than $800 billion in capex in 2026 alone, up roughly 75% year-over-year.
- The vast majority of that spend requires hardware that can only be produced in a handful of places, and most of those places are in EMs.
- For instance, Taiwan dominates advanced logic and chip packaging, and Korea dominates high bandwidth memory.
- So, in our view, EMs provide more than just exposure to AI; many aspects of the AI buildout are dependent on EM companies. The global AI buildout likely cannot proceed without EM semiconductors and supply chain, and we believe that gives certain EM companies genuine pricing power rather than the passive exposure of a supplier that can be swapped out.
- Reshoring efforts and geopolitical pressure to diversify supply chains are real—but current industry data suggests limited near-term alternatives exist at scale.
- For investors who think of EMs as a macro trade, we believe the AI supply chain reframes the conversation entirely. EMs provide direct, systemic exposure to what we view to be one of the defining capex cycles of the decade.
- Of course, changes in technology spending, competitive dynamics, trade policy, and geopolitical developments could affect the pace and magnitude of AI-related growth, potentially creating periods of volatility for EM companies tied to the theme.

EXHIBIT 4

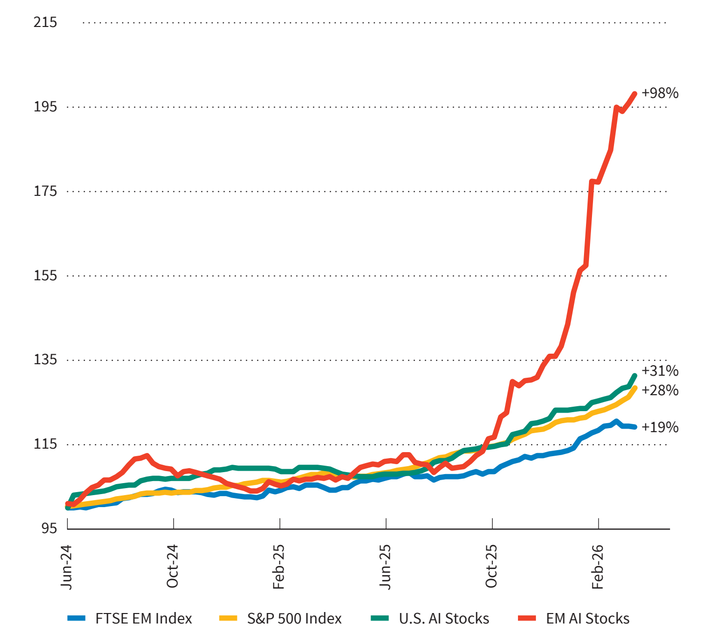
From Capex to Earnings: The Broadening Impact of AI Investment

Global hyperscaler capex is approaching $1 trillion, while consensus earnings revisions for EM AI stocks reflect the potential opportunity of this investment cycle.

Global Hyperscaler Capex



Consensus Revisions to 2026 EPS Estimates (Indexed to 100)



Sources: HSBC, FactSet, FTSE Russell, Bloomberg, and William Blair. Left chart is as of May 2026. Right chart is as of March 2026. Past performance is not indicative of future returns. A direct investment in an unmanaged index is not possible. References to specific companies are provided for illustrative purposes only and should not be interpreted as investment advice or recommendations to buy or sell any security. See back page for index information.

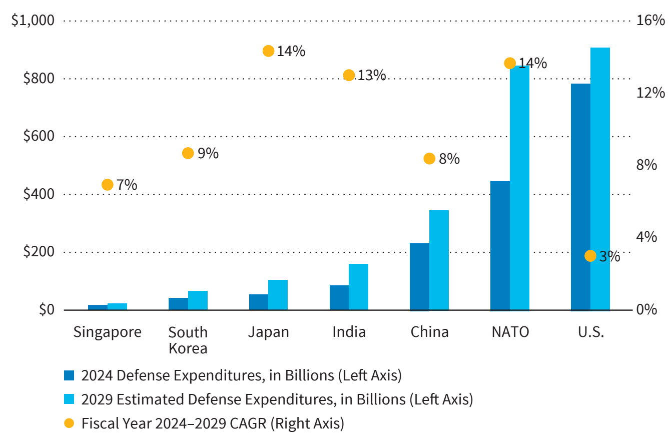
Theme 5: Multiple Structural Growth Pillars Beyond AI

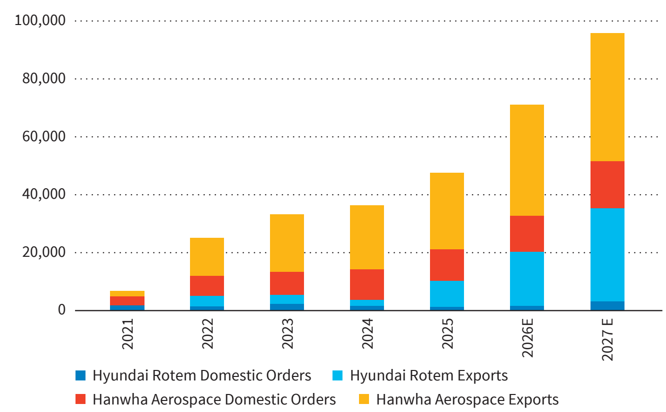
- While the AI supply chain theme dominates in EMs, we believe it's critical to focus on other key growth pillars.
- **Defense** spending is undergoing a global structural reset, not a temporary surge. The post-Ukraine, post-Middle East geopolitical order has changed procurement priorities across NATO, Asia, and the Middle East. Several EM countries have moved from defense importers to export-capable manufacturers. That could potentially mean multi-year production pipelines, long-dated government contracts, and cash flows that may be largely insulated from consumer demand or global growth slowdowns.
- Furthermore, **the energy transition** in EMs is being primarily driven by energy security and cost competitiveness. Electrification, renewable buildout, and grid investment are structural necessities in fast-growing economies, but the trend has been further accelerated by AI datacenter power needs.
- EM companies are also critical suppliers of power equipment, grid infrastructure, and the materials and components that underpin power generation, transmission, and storage. While boosted by the AI cycle, we believe the energy transition and electrification theme has a steady, long-term compounding growth trajectory.
- Then there is **India**, which we believe is one of the most compelling long-duration growth stories in the world, driven by demographics, urbanization, infrastructure investment, and expanding manufacturing and services.
- And **China**, which continues to play a critical role in global innovation, particularly across areas such as AI and automation, advanced manufacturing and robotics, and drug development and biomanufacturing. While the growth model is evolving, we believe innovation-led segments provide differentiated opportunities within the broader EM universe.
- While not guaranteed—we've discussed how volatile growth in EMs can be—these growth themes may provide diversification benefits as they tend to be imperfectly correlated with each other. When one slows, others can help carry returns. In our view, this is what shifts EMs into a genuine multi-pillar structural allocation.

EXHIBIT 5

Korean Defense Exports Surge as Global Military Spending Accelerates

Heightened geopolitical tensions are driving defense spending higher across major economies, while EM manufacturers such as Korean defense companies are emerging as key beneficiaries, with export order books growing sharply alongside domestic demand.





Sources: Company data and William Blair, as of March 2026. E refers to estimated. Right chart displayed in KRW billions. References to specific companies are provided for illustrative purposes only and should not be interpreted as investment advice or recommendations to buy or sell any security.

The Iran Conflict Has Tempered, But Not Derailed, 2026 Outlook

In the first quarter of 2026, the Iran-related escalation triggered a textbook risk-off response: oil prices spiked $15 to $20 per barrel at peak stress, volatility rose sharply, and EM assets sold off alongside other higher-risk allocations. However, supply chain disruption has remained far more contained than during COVID or the 2022 Ukraine invasion, and this time, global growth downgrades have been measured in tenths of a percentage point, not whole numbers.

One of the main risks we are monitoring is not the geopolitical headline itself, but whether a prolonged escalation tips oil prices high enough, and for long enough, to push the global economy toward recession. As has happened in the past, geopolitical shocks tend to move markets quickly and visibly, and every major EM cycle has had its geopolitical disruptions. We believe such periods can offer opportunities for long-term investors.

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