

Emerging markets outlook

Are we expecting further outperformance?



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Key takeaways

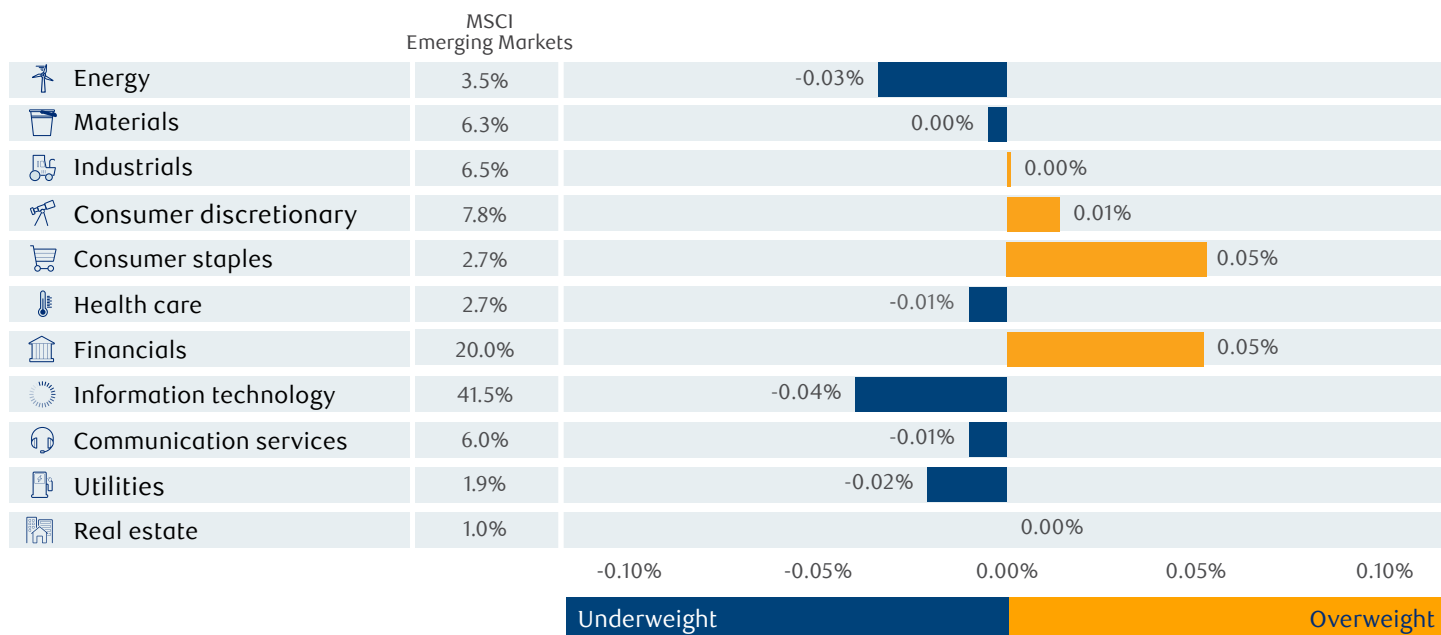
- So far in 2026 emerging market equities have outperformed developed markets, continuing a trend that began at the end of 2024. The MSCI Emerging Markets Index has added 62% (USD) since December 2024 to the end of July 2026 – roughly double the U.S. market.
- Liberation Day in April 2025 was a turning point for the asset class as President Trump involuntarily put the spotlight back on emerging countries. After more than a decade of underperformance, a new positive cycle appears to be underway.
- The drivers behind this shift are both structural and cyclical – accelerating earnings growth, the Artificial Intelligence (AI) investment supercycle, strengthening macroeconomic fundamentals, and the increasing economic independence of the developing world.

The AI value chain: a structural tailwind for emerging markets

Taiwan and South Korea have become critical to the global AI value chain. Companies such as TSMC, Samsung Electronics, and SK Hynix exhibit genuine technological leadership with unparalleled capabilities in foundry and memory semiconductors. Their revenues, margins, and market values have grown dramatically over the past five years as the beneficiaries of hyperscaler AI capital expenditure have proven to be largely domiciled in emerging markets.

However, and this is crucial for sustained long-term performance beyond these top names, an estimated 100-150 companies across emerging markets are exposed to AI through semiconductor design, ASIC development, power infrastructure, cooling technology, testing equipment, networking, and industrial automation. This represents a multi-decade investment theme with significant beneficiaries located in emerging markets, and the opportunity set continues to broaden as AI applications mature and new segments of the value chain develop.

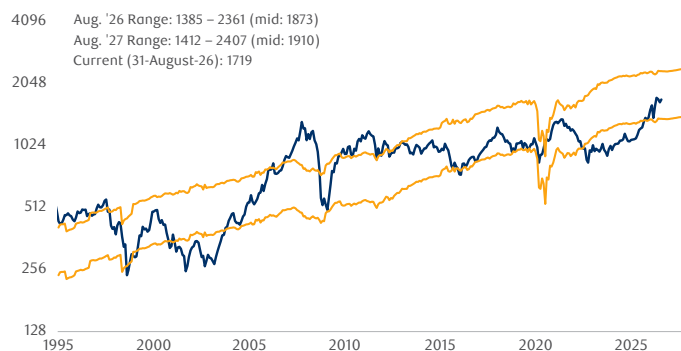
Emerging markets – Recommended sector weights



Note: As of August 31, 2026. Source: RBC GAM

“Index concentration is unprecedented: the top five stocks now represent approximately 35% of the MSCI EM benchmark, and until recently less than 25% of stocks had outperformed the index over the past 12 months.”

MSCI Emerging Markets Index Equilibrium Normalized earnings and valuations



Note: The fair value estimates are for illustrative purposes only. Corrections are always a possibility and valuations will not limit the risk of damage from systemic shocks. It is not possible to invest directly in an unmanaged index. Source: RBC GAM

China's parallel AI ecosystem

Despite the Chinese equity market being deeply out of favour, it is currently interesting to note that China is building an entire parallel AI ecosystem from scratch. The domestic AI supply chain is expected to approach US\$580 billion by 2030 – a roughly 9x increase from 2020. Escalating U.S. export controls have made self-sufficiency an existential objective, and it is difficult to see these restrictions being relaxed, given each round since 2022 has been progressively tighter. The result is that China and the U.S. are likely to operate as the two leading AI powers globally, each with a separate, complete technology stack.

Opportunities exist across semiconductor equipment makers, AI chip designers, and packaging and testing companies – segments where China is making genuine progress toward global competitiveness. Many of those names have seen their share price and valuation rise strongly, however this hasn't been the case for the Chinese internet platforms. Current lower earnings growth in their core businesses has led to derating; however they are proven, high-return businesses now investing tens of billions into AI infrastructure. We believe this will pay off in the coming years. The focus for investors should be on high-quality companies with strong management teams, genuine competitive moats, and robust corporate governance.

Beyond AI: compelling opportunities across emerging markets

Non-AI sectors such as Consumer and Financials are trading at historically wide valuation discounts to Technology. Consumer Staples, which has always traded at a premium, has seen that premium completely erode. Financials are at the widest-ever discount to Tech. Yet their fundamentals and returns remain strong.

Meanwhile, earnings upgrades are broadening beyond Taiwan and South Korea across emerging markets as governments implement various versions of Value-up programs targeting better shareholder returns and giving confidence that the outperformance story extends well beyond AI alone.

Despite near-term headwinds, India offers several compelling structural themes: the financialisation of savings as

households shift from physical assets to financial markets; rising discretionary spend driven by attractive demographics and growing GDP per capita; a manufacturing inflection point underpinned by Production-Linked Incentive schemes and "Make in India" policy frameworks; and energy transition opportunities as India targets majority renewables within a decade. New AI services in IT are projected to grow from 3-5% to 30-50% of total industry revenues within five years, expanding the sector's addressable market from US\$1 trillion to US\$5-6 trillion. The transition may be painful but the future is bright for the industry.

Latin America is well-positioned for rate normalisation and reflation, with commodity exports providing natural hedges. Furthermore, a move towards business-friendly leadership is underway in the region, which should lead to much needed reforms.

Structural pillars supporting long-term outperformance

The global economic landscape is undergoing a historic transformation. Emerging markets account for over 50% of global GDP and are expected to generate approximately 65% of global growth by 2035. Five critical pillars underpin this shift:

- **Domestic demand replacing export dependency:** Rising middle classes, urbanisation, and fintech-driven financial inclusion are creating indigenous demand drivers independent of developed market cycles.
- **De-dollarisation:** The dollar's share of global reserves has declined from 70% to 58% over two decades, reducing currency vulnerability. The current fiscal situation in the U.S. could accelerate a shift away from the dollar, benefiting EM countries.
- **Stronger macroeconomic fundamentals:** Healthier fiscal positions, lower government debt, and higher real policy rates relative to developed markets.
- **Inter-EM integration:** Intra-EM trade has surged from roughly 25% in 1990 to approaching 50% today, creating self-reinforcing growth ecosystems.
- **Technological independence:** Select markets are establishing global leadership positions in semiconductors, electric vehicles, and software.

Challenges and risks to monitor

Despite the constructive outlook, meaningful risks demand attention. Index concentration is unprecedented: the top five stocks now represent approximately 35% of the MSCI EM benchmark, and until recently less than 25% of stocks had outperformed the index over the past 12 months. Performance has been extremely narrow, with only IT outperforming at the sector level.

Retail speculation and leverage – particularly in South Korea – are creating short-term risks, with regulators expressing concern around leveraged single-stock ETFs. Much of the AI capex is being fuelled by debt, raising questions around monetisation timelines and sustainability.

China faces structural bottlenecks: the absence of EUV lithography constrains leading-edge production, potential further U.S. export controls could set back timelines, and governance risks around capital misallocation persist as government directs billions into strategic sectors. India, meanwhile, lacks domestic AI infrastructure and semiconductor manufacturing capacity, remaining reliant on imported GPUs and foreign hyperscalers.

Additional risks include a potential resumption of U.S. exceptionalism redirecting capital flows, geopolitical instability, and commodity price vulnerability for energy-dependent emerging markets.

Conclusion

The medium-term outlook for emerging markets remains constructive, but near-term volatility is likely to persist given extreme index concentration and speculative excess. However, the AI sell-off in July has reduced volatility somewhat, and the rally has recently broadened to other sectors such as Materials and Health Care. Selectivity and a focus on quality companies with genuine competitive moats will be essential. The trajectory, however, is clear: EM economies are increasingly independent, powered by rising domestic demand, deepening integration, and growing financial autonomy. The next era of global growth increasingly belongs to the emerging world.

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