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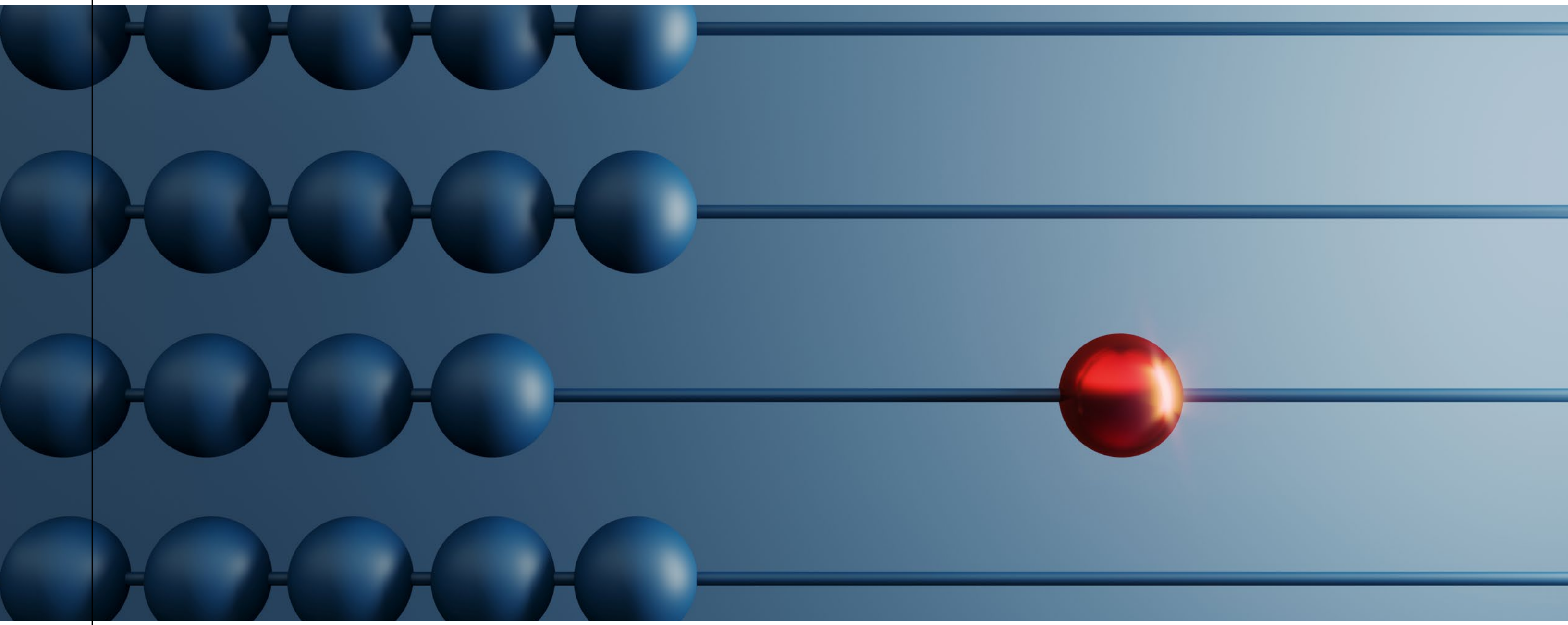
Emerging Markets 2026:
The Next Phase of Global Rebalancing



Emerging markets (EMs) are entering 2026 as a central force in the reordering of global growth. The combination of a softer U.S. dollar, moderating inflation, and stronger domestic fundamentals has created conditions for a more sustainable expansion across asset classes. Capital is rotating toward higher-quality companies and higher-yielding sovereigns, while policy realignment in China and other key economies is shifting the balance of global manufacturing, technology, and trade. Against this backdrop, we believe EMs are poised to play a defining role in the next phase of global rebalancing—where growth leadership broadens, diversification deepens, and structural change becomes the primary driver of returns.

December 2025

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Macro | Protectionism, Policy Shifts, and the New Economic Reality

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Renewed focus on domestic economies spells better growth support in the United States and the European Union (EU). China's domestic consumption will likely continue to struggle under the weight of the ongoing housing market correction. All in all, we believe a stable U.S. dollar, ample global liquidity, and strong demand for industrial commodities are likely to prove fertile ground for EM assets in 2026.

EM Growth Depends on Three Developed Demand Centers

The vast majority of EMs are small, open economies whose fortunes depend on what happens in the world's three principal demand centers: the United States, Europe, and China. Put another way, EMs are a high-beta play on developed market growth. Interest rates, exchange rates, and commodity prices are largely set by the economic and liquidity conditions in the three global demand centers. At the same time, these prices—interest rates, exchange rates, and commodity prices—set binding constraints on economic outcomes in most EMs.

United States: Tariff Challenges Spur Policy Shifts

The U.S. economy is entering 2026 with narrow gross domestic product (GDP) growth, challenged consumer spending, and weaker corporate profits. And because of the recent government shutdown, economic data for the second half of the year is scant.

However, AI-related infrastructure investment—think data centers, software, chips, and related equipment—explained as much as three-fourths of the overall GDP growth in the first six months of 2025, based on official data.[1]

Considering the announced acceleration of capital expenditure (capex) spending by all major hyperscalers, there is little reason to expect AI-related infrastructure to feature less prominently in U.S. GDP growth in the second half of 2025.

Meanwhile, the U.S. consumer faces ongoing challenges as tariff-induced inflation eats into consumers' purchasing power. Seven months after the current U.S. administration raised tariffs on "Liberation Day," the overall consumer price inflation is up modestly: annual inflation accelerated from a low of 2.3% in April to just over 3% in September, thanks largely to continued (and belated) housing disinflation.

Just below the headline level, things look less rosy. Goods prices are moving up sequentially at an accelerating rate. This is in sharp contrast to two decades of persistent declines. According to the Harvard Business School Pricing Lab, imported goods prices are up approximately 6% from pre-tariff trends, while domestic goods prices are up some 4.3%.

U.S. consumer spending has not remained unscathed: retail sales adjusted for inflation are barely growing and consumer discretionary stocks within the S&P 500 Index have lagged the overall index by about 12% through the end of November 2025.

Tariff-related disruption is also eating into corporate profits more broadly. According to aggregate corporate profits data tracked by the U.S. Bureau of Economic Analysis, manufacturing, wholesale trade, and transport profits are down sequentially by 10% to 20% in the first half of 2025 from 2024. Outside of AI-related investment and financials, U.S. companies are feeling squeezed.

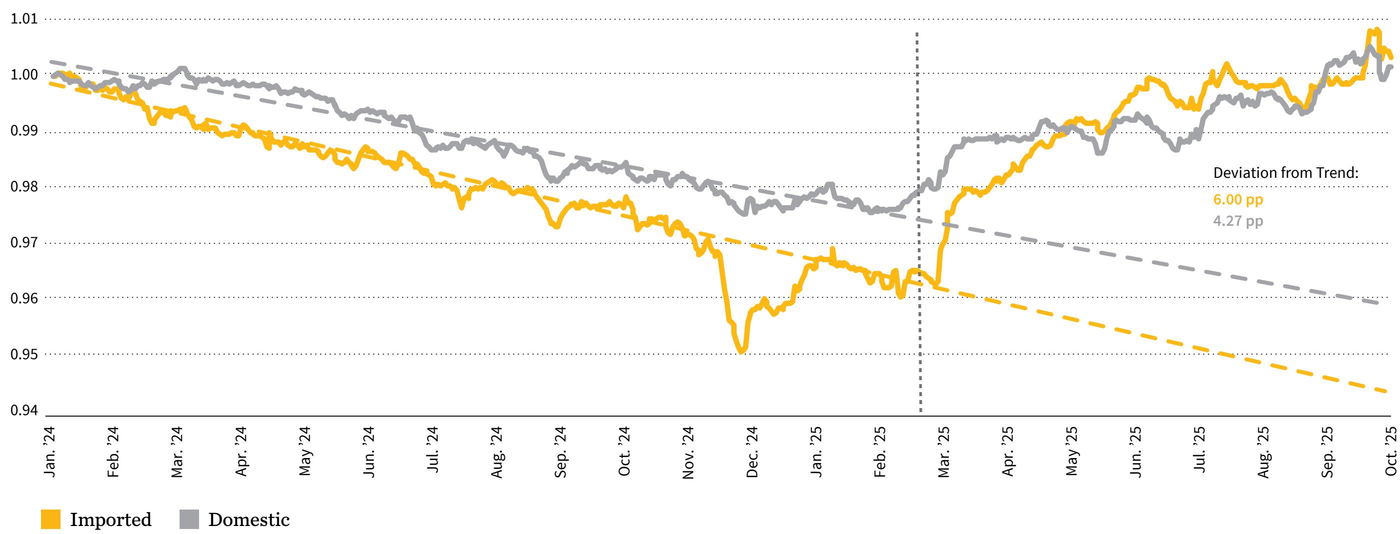
Facing midterm elections in November 2026, the current U.S. administration is likely to focus on supporting the domestic economy. The One Big Beautiful Bill Act aims to catalyze greater investment into domestic production by reducing or eliminating tax on structures, research and development, and other activities. The Tax Foundation

1 Source: *Bloomberg*.

EXHIBIT 1

Goods Prices Break From Trend Following New Tariffs

After years of gradual price declines, both domestic and imported goods have seen abrupt increases once new tariff measures took effect. Imported goods prices have climbed the most, rising around 6 percentage points relative to trend, while domestic goods are up more than 4 points.

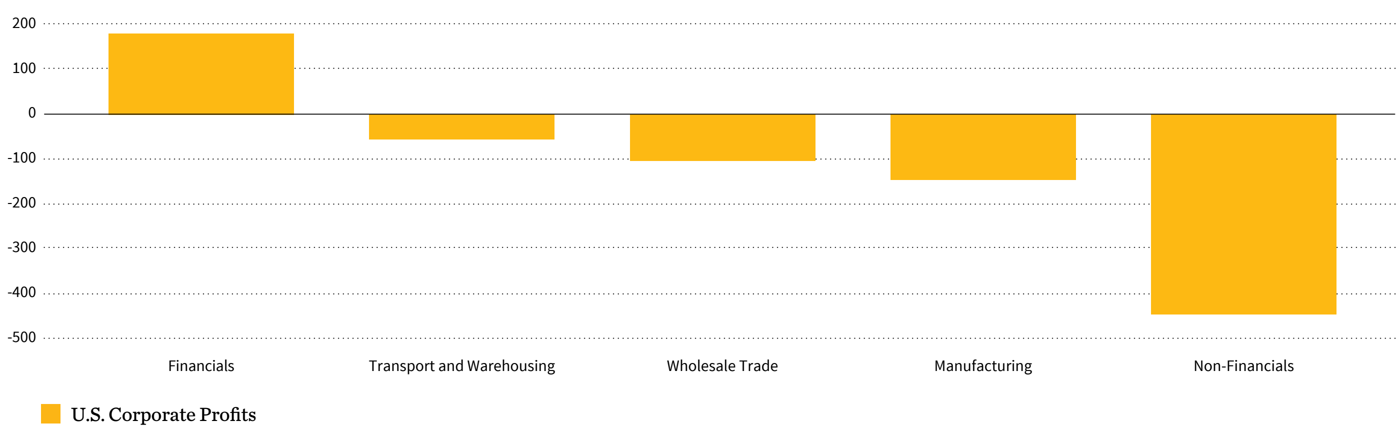


Sources: Harvard Business School Pricing Lab and William Blair, as of October 11, 2025.

EXHIBIT 2

Year-Over-Year Change in U.S. Corporate Profits (In Billions)

Tariff-related disruptions have weighed on corporate profitability, and most industries outside AI investment and financials have experienced noticeable strain.



Sources: U.S. Bureau of Economic Analysis (BEA) and William Blair, as of June 30, 2025.

estimates that the new rules will reduce 2026 tax liabilities for manufacturers by over 2% and other industries by half that amount.

In mid-November, the U.S. administration reversed its stance on tariffing agricultural products after domestic consumers recoiled from rapid increases of food prices. And allowing banks to hold smaller capital buffers, together with a 30% reduction in supervisory and regulatory units of the U.S. Federal Reserve (Fed), is estimated to free several trillion dollars' worth in lending capacity.[2]

Lower corporate taxes and more lending, not to mention a possible "housing emergency" to lower mortgage rates in a bid to revive the moribund housing market, all suggest stronger, broader GDP growth in 2026.

But inflation is likely to prove sticky, especially since much of the tariff impact is still working its way through the economy, and new tariffs—on kitchen cabinets and bathroom vanities, for example—have yet to take effect.

Europe and China: Shifting Toward Domestic Revival

All these tariffs and "America First" policies have produced a broad focus on reviving domestic market dynamism in Europe and China.

Europe's New Growth Era

European exporters are facing major headwinds from U.S. tariffs and Chinese competition. German exports to the United States fell by 7.4% in the first nine months of 2025. And although the European Union (EU) negotiated a trade deal that taxes steel and aluminum as final products, U.S. authorities have been applying the negotiated tariff rate of 50% on 407 steel and aluminum "derivative" products (which are capital and consumer goods produced in Europe) as well, further crimping European exporters. And in the latest negotiations twist, U.S. Secretary of Commerce Howard Lutnick and U.S. Trade Representative Jamieson Greer used their late-November trip to Brussels to make tariff relief contingent on the EU scrapping its digital regulations.

> "'Made in Europe' is now an explicit policy aim across the continent."
>
> **Olga Bitel, Partner**

In response, Germany, the single largest economy within the euro area, abandoned its decades-old self-imposed fiscal austerity in favor of investing in national infrastructure and defense. Although the size of the investment is enormous—€500 billion relative to Germany's €4.5 trillion-sized economy—the infrastructure upgrade is urgently needed. Hence, the fiscal multiplier from this spending is likely to be significantly more than one, meaning that for every €1 spent, the returns to the economy will be several times higher. Once the funds disbursement gains steam, it is likely to help Germany register economic growth in 2026 after four years of stagnation.

In addition, much of the government funds in Germany and elsewhere in Europe are increasingly likely to be spent purchasing from domestic producers; "Made in Europe" is now an explicit policy aim across the continent.

The rest of the EU is not standing still. According to the Centre for European Policy Studies, the EU has been generating more start-ups than the United States in each of the last five years, and many acknowledge the continent's highly skilled and increasingly entrepreneurial labor force.

What is needed is domestically generated financial capital, which the European Commission already identified earlier in 2025. Change in Europe tends to be slow, but the continent is undeniably moving toward incentivizing more growth after years of focus on fiscal austerity.

2 Source: *Financial Times*.

China's Path to Market Efficiency
In China, rather than supporting start-ups, winding down companies is identified as a key impediment to building a truly single, domestic market. Local governments tend to support local firms via tax breaks, preferential access to bank lending, and other schemes; they prop up local champions and resist industry consolidation, often leading to overcapacity and meager profits for all.

This is a complex challenge involving revenue sharing among central and regional fiscal authorities. For the past 18 months, local authorities have been issuing bonds as a means of debt swap, and local government financing vehicles are supposed to be wound down by June 2027. For now, aggregate government deficit is running in double digits of the country's GDP, but domestic consumption is likely to remain depressed in 2026, as housing prices continue to adjust.

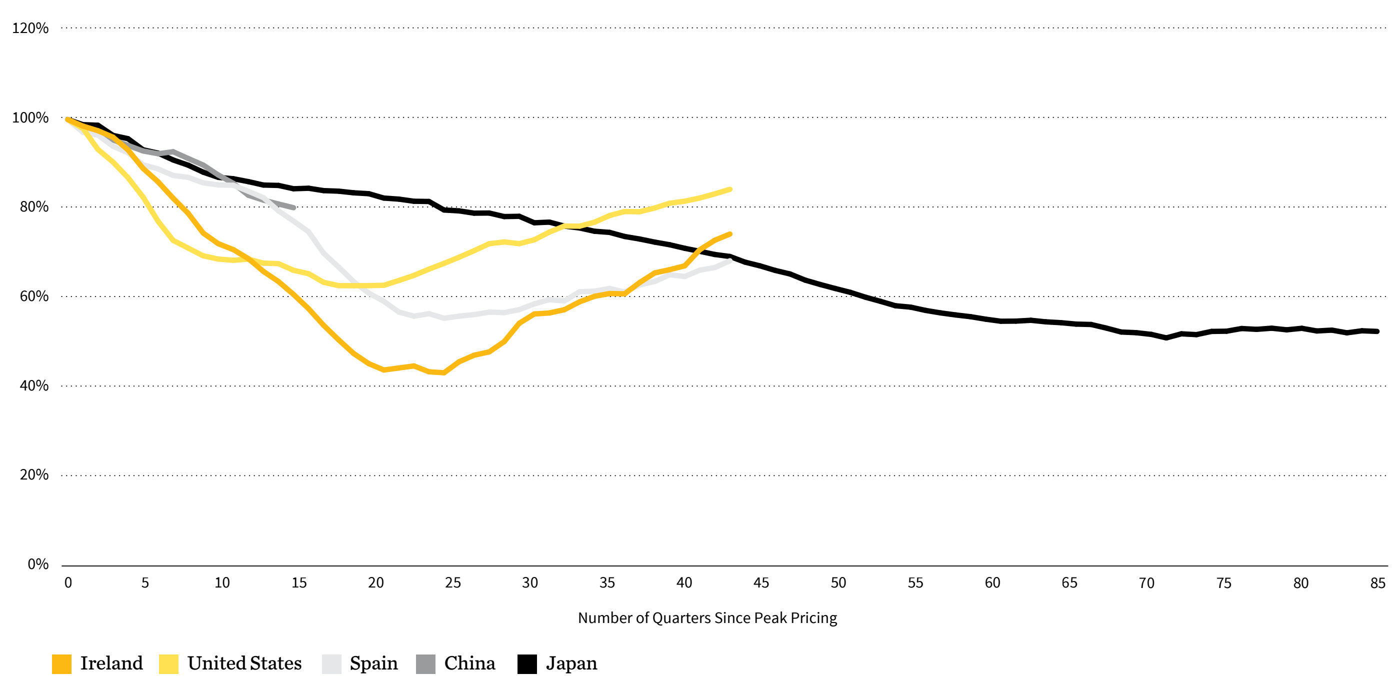
Chinese authorities have also made periodic efforts to support residential real estate activity and household incomes, and we are likely to see renewed efforts in 2026. However, China's residential real-estate sector must continue to downsize, and housing prices are not yet done decelerating. International experience suggests that a housing market correction typically lasts about five years and results in cumulative price declines of 40% to 60%.

China's prices are down approximately 20% from their peak, but are likely to decline further, as affordability is still an issue. A modestly sized apartment in Shanghai still retails for about $3 million. For as long as the housing slump will continue, China's domestic consumption will likely remain challenged.

EXHIBIT 3

Chinese Housing Prices Are Still Decelerating

China's housing sector has continued its multiyear price adjustment. Lessons from the United States, Japan, and other countries indicate that similar corrections can last five years or more, signaling that domestic housing prices in China may still have room to fall.



Sources: Federal Reserve Economic Data (FRED) database and William Blair, as of November 2025. FRED housing index data (y axis) measures the cumulate decrease in housing prices from peak (set to 100 in each case).

Conclusion

In summary, growth is likely to broaden and accelerate in two of the world's three principal demand centers in 2026. EM exporters of industrial commodities are also likely to continue experiencing material improvement in fortunes in 2026.

Although the U.S. dollar may not depreciate much further from current levels unless growth in Europe and in Japan surprises materially to the upside, broad-based economic growth and ample liquidity are likely to provide a fertile ground for EM assets.

> "China's residential real-estate sector must continue to downsize, and housing prices are not yet done decelerating."
>
> **Olga Bitel, Partner**

EM Equity | From Rebound to Rotation

Todd McClone, CFA, Partner
PORTFOLIO MANAGER, EM EQUITIES

Ian Smith, Partner
PORTFOLIO MANAGER, EM EQUITIES

EMs are entering 2026 from a position of renewed strength. A weakening U.S. dollar, improving fundamentals, and broadening country and sector leadership have created a favorable backdrop for investors—and we believe EM equities continue to offer an efficient gateway to global secular themes such as AI, power infrastructure investment, healthcare innovation, changing consumer patterns, and manufacturing upgrades.

Performance Highlights From 2025

After more than a decade of underperformance, EM equities outpaced developed market (DM) equities in 2025. The MSCI Emerging Markets Index rose 30% year to date as of November 30, compared with 17% for the MSCI USA Investable Market Index (IMI), marking EM's strongest relative year since 2009.

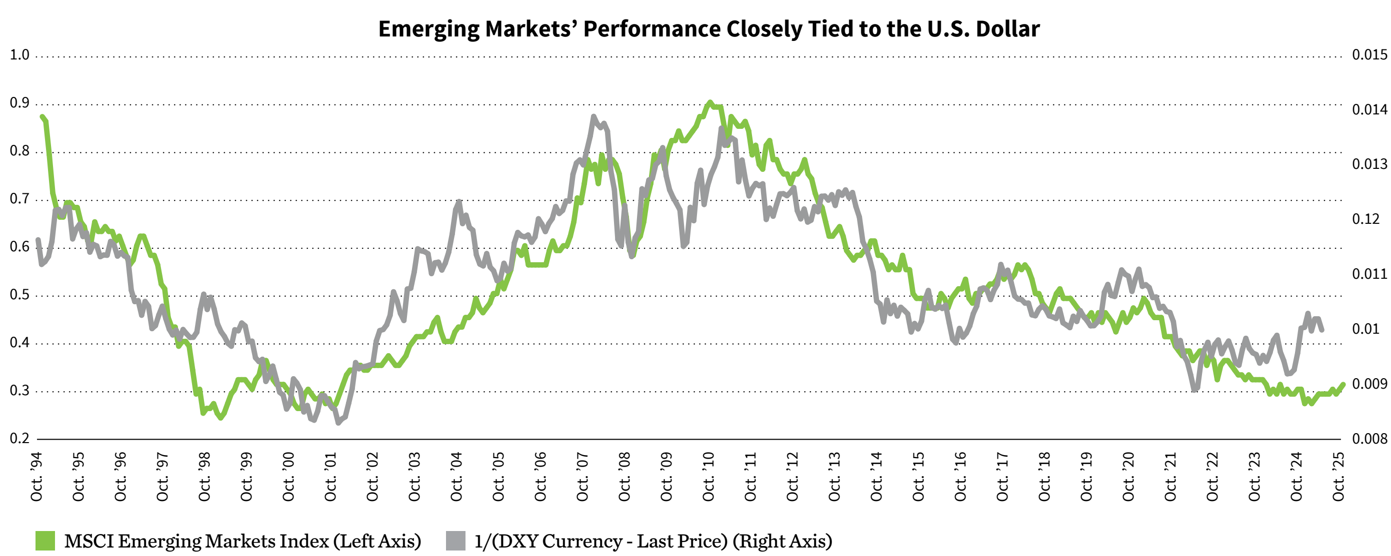
Gains were widespread across regions: North Asia led, with Korea and Taiwan benefiting from AI-related semiconductor demand, and China's robust exports and renewed focus on innovation driving its performance. Elsewhere, Latin America and South Africa rebounded amid policy easing, a weaker dollar, and stronger commodity prices.

Sector performance also broadened beyond information technology to include materials, industrials, and healthcare, underscoring that the opportunity set in EMs now extends beyond technology.

EXHIBIT 4

EM Relative Performance Strengthened When the U.S. Dollar Weakened

An inverted U.S. Dollar Index shows that periods of dollar weakness typically coincide with EM equities outperforming those of developed markets.



Sources: Bloomberg and William Blair, as of October 2025. left axis shows relative performance of the MSCI Emerging Markets Index to the MSCI World Index. The right axis shows the inverse of the U.S. Dollar Index. **Past performance is historical and not indicative of future returns.** A direct investment in an unmanaged index is not possible.

A key driver of renewed EM performance has been a sustained shift in global macro conditions. EM markets historically exhibit a strong inverse relationship with the U.S. dollar, and 2025's weakening U.S. dollar trend provided a significant tailwind. The strong negative correlation between EM relative returns and dollar strength highlights the importance of currency cycles to EM valuations.

The rerating of EM equities stands on a firm foundation. After U.S. President Trump's April "Liberation Day" announcement of sweeping tariffs triggered a brief bout of volatility, investor flows into EM equities turned positive and have remained steady since. Institutional positioning, however, is still relatively light despite the performance recovery, suggesting continued room for capital reallocation. At the same time, heightened concentration risk in U.S. markets has likely strengthened investors' motivation to diversify globally. The United States now represents roughly two-thirds of the MSCI All Country World Index by market capitalization, or nearly three times its share of global GDP.

Broadening Drivers: AI, Power, and Defense

The AI investment cycle is redefining the global landscape, and EMs are deeply embedded in the AI growth story. Markets such as Taiwan and Korea remain integral to the global semiconductor and server-component supply chains, providing much of the hardware required for AI applications. More than 20% of total EM revenue is expected to be AI-related in 2029, according to Goldman Sachs, and we believe the ongoing AI capex cycle should remain a durable source of growth across North Asia.

While U.S. firms have captured a disproportionate share of the AI-related market-cap expansion, EMs play a central role in the infrastructure buildout. This is most pronounced in semiconductors, memory, and data-center power systems. China's domestic AI initiatives, including the emergence of locally developed models, have also accelerated technology investment, placing the country roughly two years behind the United States in the AI investment cycle, in our view.

Rising AI-driven energy demand has created parallel opportunities in EM power infrastructure. Korean firms such as Hyundai Electric and Hyosung Heavy are key suppliers of transformers and grid components, while Indian manufacturers are expanding renewable-energy and transmission capacity to meet industrial demand.

> "The AI investment cycle is redefining the global landscape, and EMs are deeply embedded in the AI growth story."
>
> **Todd McClone, CFA, Partner**

Defense spending has also emerged as a durable global theme. Korea's Hanwha Aerospace and Hyundai Rotem, along with Turkey's Aselsan Elektronik, have become major exporters of defense systems to Western Europe and the Middle East, while Indian defense companies such as Bharat Electronics and Hindustan Aeronautics are benefiting from increased domestic defense budgets and import substitution. The Korean shipbuilding sector, through HD Hyundai Heavy Industries and related firms, is participating in both liquefied natural gas (LNG) infrastructure and potentially the U.S. naval upgrade program, reinforcing its industrial relevance.

Healthcare is another source of structural growth. After several years of weakness, Chinese and Indian contract research and contract development and manufacturing (CRO/CDMO) firms are seeing renewed demand linked to biotechnology investment and GLP-1 production. As domestic research-and-development (R&D) ecosystems mature, healthcare innovation is becoming a more enduring contributor to EM earnings quality.

Outlook for 2026: Quality Growth in a Broader EM Cycle

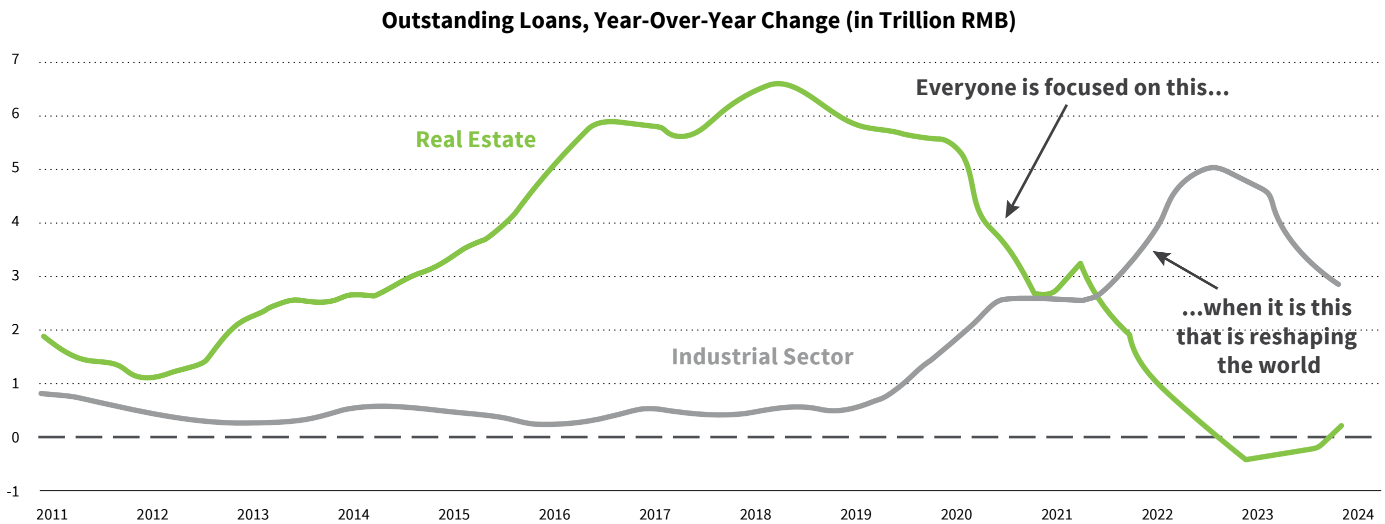
After several years of relative underperformance, the valuation gap between quality and value within EM has begun to narrow as investors refocus on sustainable earnings and resilient business models. Historically, periods in which quality-oriented EM equities have lagged the index have been short-lived.

As inflation moderates and monetary policy across several EM economies shifts toward easing, market leadership is likely to broaden beyond early-cycle beneficiaries. A U.S. Federal Reserve pivot to rate cuts and a softer dollar

EXHIBIT 5

China's Credit Allocation Shifts From Real Estate to Industry

Year-over-year loan growth shows a clear pivot away from property lending and toward industrial sectors, underscoring Beijing's push to support advanced manufacturing and productive investment.



Sources: Gavekal and William Blair, as of 12/31/24.

would create room for many EM central banks to lower rates without undermining currency stability, reinforcing domestic growth prospects and supporting asset valuations. Investor sentiment has improved meaningfully, with renewed inflows into EM equities and bonds reflecting rising confidence in the durability of this cycle.

The macro backdrop remains constructive. EM economic growth is expected to continue outpacing that of developed markets, supported by improving fiscal balances, moderating inflation, and an increasingly stable global policy environment. As fundamentals regain influence, we believe corporate earnings momentum should strengthen, particularly in markets in which high real yields previously constrained growth.

From a portfolio perspective, we believe investors could benefit from maintaining core exposure to high-quality manufacturing companies in North Asia and India, two markets positioned to capture the next wave of AI and industrial spending. In Latin America, opportunities are emerging in quality growth names with attractive valuations in Brazil and Mexico as monetary and fiscal conditions improve. Meanwhile, exposure to defensive quality companies, particularly in healthcare and select areas of the consumption-related sector, can serve as portfolio ballasts and provide resilience against market volatility.

China: From Property Drag to Industrial Upgrade

China's economy continues its transition from property-driven growth to advanced manufacturing. The government's massive fiscal support program has prioritized industrial upgrading and technological self-reliance. Bank lending has shifted accordingly, with financing to the property sector declining sharply, while credit to manufacturing, semiconductors, robotics, and biotech has surged.

Although domestic consumption remains subdued, rising exports to EMs are helping offset trade frictions with the West. China's dominance in electric vehicles (EVs), batteries, and solar power continues to anchor its manufacturing edge, while infrastructure investment and targeted fiscal programs provide a steady policy backstop.

Despite lingering structural headwinds and geopolitical risks, we believe current valuations are attractive, and point to potential reengagement from Western investors, which could have an outsized impact on performance.

India: A Strong Engine Amid Consolidation

India's market lagged in 2025 as high valuations, modest earnings growth, trade tensions with the United States, and limited AI exposure weighed on performance. Yet India's structural story remains compelling. The country's ongoing infrastructure buildout continues to drive growth, supported by sustained public investment and pro-manufacturing initiatives, such as the Make in India and Production Linked Incentive programs.

Consumption and the deepening of the financial system continue to serve as key growth engines. Low household leverage and a young, expanding workforce underpin steady demand for credit and durable goods, while rising incomes support the shift from staples to discretionary spending. India's economy is forecast by Morgan Stanley and World Bank to grow at roughly twice the pace of global GDP over the medium term.

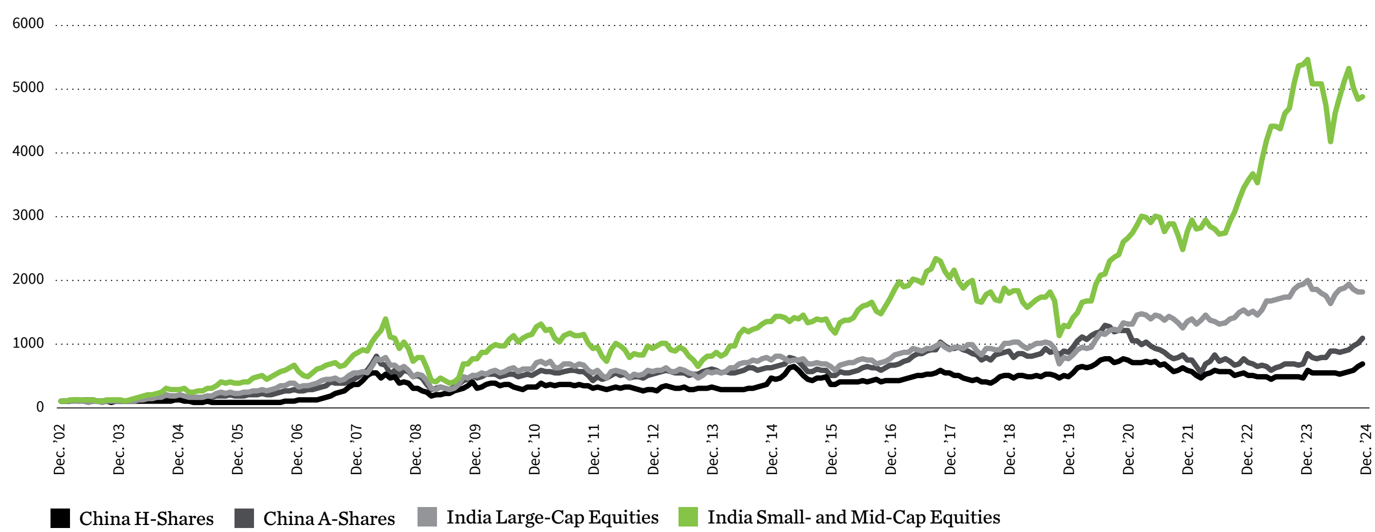
> "In India, consumption and the deepening of the financial system continue to serve as key growth engines."
>
> **Ian Smith, Partner**

Despite near-term consolidation, we believe India's encouraging long-term equity story remains intact. Over the past decade, Indian small- and midcap equities have far outperformed both the NIFTY and Chinese benchmarks, illustrating the country's depth of entrepreneurial opportunity. Corporate earnings are expected to strengthen in 2026, supported by policy continuity, fiscal stimulus,

EXHIBIT 6

India's Small- and Mid-Cap Stocks Have Outperformed Major Asian Equity Markets

Since the early 2000s, India's small- and mid-cap segment has delivered substantially higher cumulative returns than China A-shares, China H-shares, and the NIFTY.



Sources: Bloomberg and William Blair, as of September 2025. Chart shows total returns rebased to 0 on 1/31/2002. China A-shares are represented by the CSI 300 Index; China H-shares by the MSCI China Index; India large-cap equities by the NIFTY; India small- and mid-cap equities by the NIFTY Midcap 100. **Past performance is historical and is not indicative of future returns.** A direct investment in an unmanaged index is not possible.

and an improving macro backdrop. Although valuations are still somewhat elevated, we believe the combination of reform momentum, expanding manufacturing capacity, and resilient consumer demand continues to reinforce India's position as one of the most durable growth stories in EMs.

Latin America: Turning a Corner on Rates and Reform

Brazil and Mexico headline a Latin American recovery story centered on improving monetary conditions and fiscal pragmatism. Brazil's benchmark interest rate was 15% as of November 2025, its highest level in nearly two decades. However, its disinflation trend has strengthened, and analysts expect a gradual easing cycle to commence in early 2026. Despite the drag from high borrowing costs, Brazil's macroeconomic backdrop remains stable, and lower rates should help revive credit growth and corporate investment.

Mexico continues to benefit from nearshoring: roughly 85% of its exports enter the U.S. tariff-free under existing trade agreements. Foreign direct investment reached a record high in the first half of 2025 as manufacturers continued to relocate supply chains closer to the U.S. market. Elsewhere, Argentina's market remains small and illiquid, though scope for renewed policy reforms under President Javier Milei's administration have drawn cautious optimism.

UAE and South Africa: Standouts in EMEA

In Europe, the Middle East, and Africa (EMEA), we believe United Arab Emirates (UAE) equities offer a compelling case supported by strong macro fundamentals, geopolitical stability, and positive investor sentiment. The economy is projected to grow at 4% to 5% annually, driven by diversification into non-oil sectors, such as technology, renewable energy, and tourism. Real estate continues to benefit from robust demand and rising prices, while financial institutions enjoy healthy credit growth and digital transformation. Infrastructure spending on transport, logistics, and energy projects underpins long-term growth, reinforcing the UAE's position as a resilient and diversified market in the region.

Meanwhile, South Africa's market rebounded in 2025, supported by improved political sentiment, a steadier macro backdrop, and stronger commodity prices. With valuations still below historical averages and sectors like mining, financials, and consumer staples positioned to benefit from cyclical recovery, we believe South Africa offers selective opportunities for long-term investors seeking exposure to EMs with commodity leverage.

Conclusion: The Case for Sustained EM Leadership

EMs now account for 60% of global population and 40% of global GDP (driving 70% of real growth), but represent only 11% of the MSCI All Country World Index (ACWI) weight. They also remain underweighted in global portfolios, underscoring the long-term potential for reallocation.

With the U.S. dollar in retreat, fundamentals improving, and new growth engines emerging across regions, we believe the case for sustained EM leadership is gaining traction. EMs are home to many of the world's most competitive companies, many of which are global leaders in semiconductors, energy infrastructure, and healthcare innovation.

As capital redistributes, we expect investors reward proven profitability and quality, and we believe EM equities are poised to continue their shift from potential to performance.

> "EMs are home to many of the world's most competitive companies, many of which are global leaders in semiconductors, energy infrastructure, and healthcare innovation."
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> **Todd McClone, CFA, Partner**

Marcelo Assalin, CFA, Partner
HEAD OF EM DEBT

Momentum continues in EM debt, and we believe the forces behind it haven't faded. Solid growth, improving balance sheets, attractive real yields, and renewed inflows have carried strength from 2025 into the year ahead. But first let's look back at 2025.

Strong Performance in 2025

EM debt had a strong year in 2025. The asset class delivered robust returns across the board, with credit spreads in hard currency corporates and sovereigns tightening and yields moving lower. In the local currency space, EM currencies appreciated while local interest rates declined. And throughout the year, EM debt benefited from a combination of resilient fundamentals, strong technical conditions, and supportive valuations. All this resulted in strong performance across sub-asset classes.

> "Although risks related to U.S. tariff policy and global trade are ongoing, EMs have become increasingly insulated."
>
> **Marcelo Assalin, CFA, Partner**

A Stable Macroeconomic Backdrop

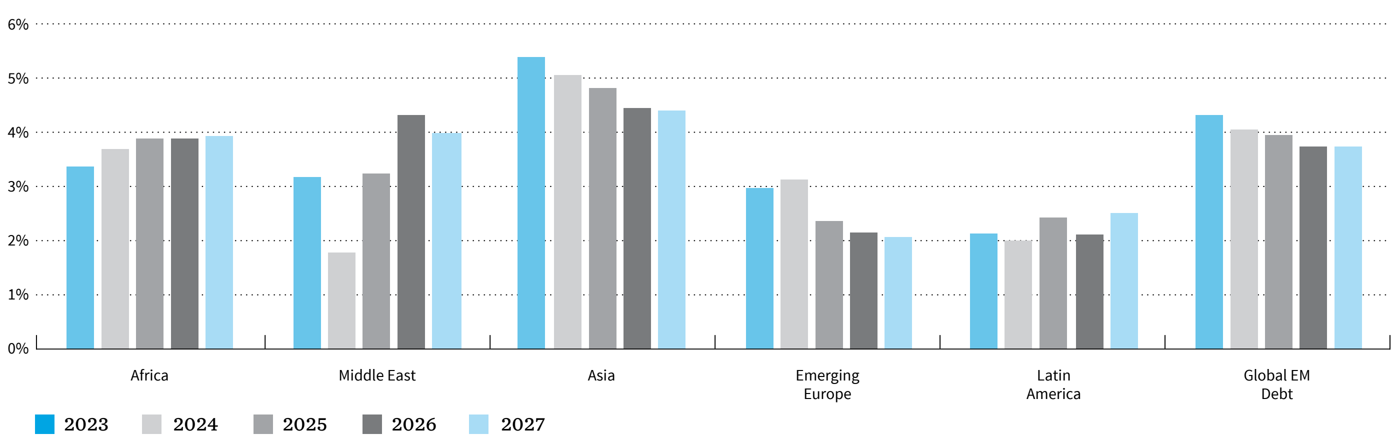
Despite rising concerns about potential impacts from global trade tensions driven by U.S. policies and ongoing geopolitical conflicts, the overall fundamental backdrop remains resilient, and we believe this resilience should persist into 2026.

We expect EM economies to grow at approximately 3.7% on a GDP-weighted basis next year, as shown in exhibit 7, broadly in line with 2025's estimated 3.9%, which exceeded expectations following concerns raised by the April 2025 U.S. tariff announcements.

EXHIBIT 7

Resilient GDP Growth in EM Economics

We expect EM GDP growth to remain steady across regions, holding near 4% through the forecast period. Asia and Africa continue to lead. While growth moderates slightly from 2025 onward, the trajectory remains stable, reinforcing the resilience of EM economies.



Sources: Oxford Economics, J.P. Morgan, and William Blair, as of October 31, 2025. Years 2025, 2026, and 2027 are forecasts.

This solid economic growth should continue to anchor fiscal and debt dynamics across most EMs, where we anticipate stable fiscal positions and debt-to-GDP ratios. Furthermore, AI-related productivity gains should further support growth dynamics in many EMs.

External accounts are a particularly bright spot, where we believe persistent capital flows, strong direct foreign investment, and healthy current account surpluses will lead to robust balance-of-payments positions. The inflationary backdrop is benign, which should allow EM central banks to continue cutting rates, providing additional support going forward.

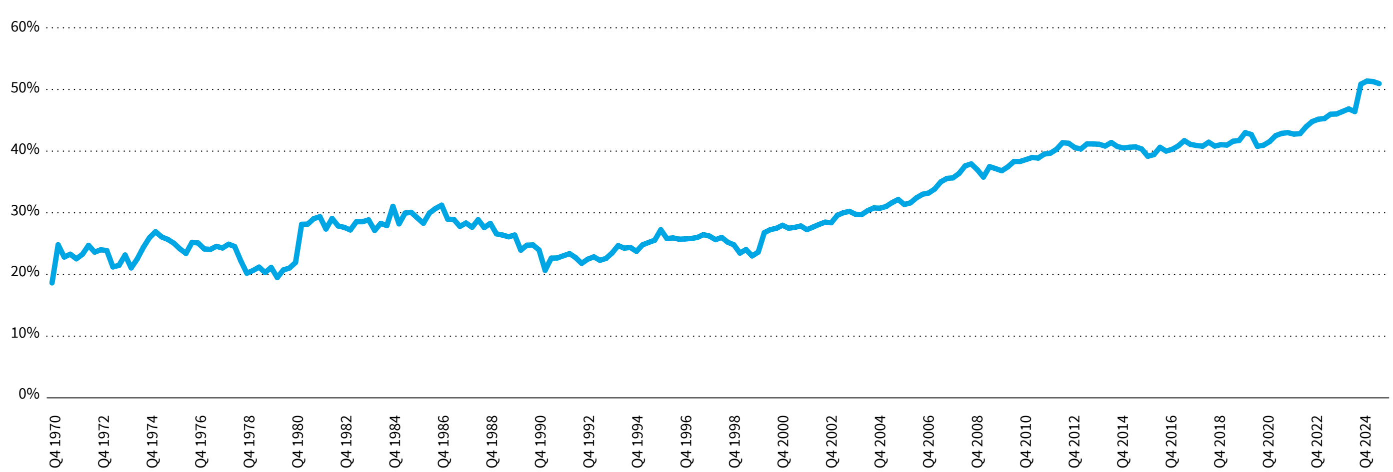
In 2025, the effective U.S. tariff rate on imported goods saw one of its largest increases in more than a century. However, by the end of 2025 the impact was less severe than many had forecast in April, and reciprocal tariffs announced were softened by exemptions for critical goods and subsequent adjustments. Although risks related to U.S. tariff policy and global trade are ongoing, EMs have become increasingly insulated, with intra-EM trade now accounting for more than 50% of total EM trade, up from roughly 25% in the early 2000s, as shown in exhibit 8. This significantly reduces EM reliance on advanced economies, particularly the United States.

While global growth may decelerate due to softer conditions in developed markets, we believe EM fundamentals are resilient enough to withstand this gradual deceleration and credit default risk is expected to remain well contained. Overall, we view EM fundamentals as constructive for continued strong performance.

EXHIBIT 8

Intra-EM Trade Rising

Intra-EM trade now accounts for more than 50% of total EM trade, up from roughly 25% in the early 2000s. This significantly reduces EM reliance on advanced economies, particularly the United States.



Sources: Direction of Trade Statistics (DOTS) and William Blair. Data is from March 31, 1970, through June 30, 2025, quarterly. DOTS presents the value of merchandise exports and imports disaggregated according to a country's primary trading partners. Area and world aggregates are included in the display of trade flows between major areas of the world. Reported data is supplemented by estimates whenever such data is not available or current. Imports are reported on a cost, insurance and freight (CIF) basis and exports are reported on a free on board (FOB) basis, with the exception of a few countries for which imports are also available FOB. Time series data includes estimates derived from reports of partner countries for non-reporting and slow-reporting countries.

The Oil Outlook

In 2025 oil markets were pressured by constant oversupply expectations and global trade concerns, with bouts of geopolitics providing price spikes. Prices are closing the year at about $65 per barrel, the lower end of the yearly range.

Demand for crude is expected to grow by approximately 1 million barrels per day in 2025, a bit lower than historical levels, but still decent, although some of this demand went into strategic inventories in China. Supply created an imbalance, with additional barrels coming from U.S. shale, Brazil, Guyana, Canada, Norway, and the Organization of the Petroleum Exporting Countries (OPEC).

Visible inventories have been built, and floating storage seems to be absorbing sanctioned barrels, which eventually will need to hit the market. So, in 2026, fundamentals point to an oversupplied market. With expectations of more than 2 million barrels per day of oversupply, prices should remain under pressure even as demand remains steady.

Given this, we remain cautious on oil-related investments, but also note that low-visibility events such as geopolitics or OPEC's (and others') reactions to much lower prices could offset the visible imbalance and provide some price support. Moreover, a resolution or escalation of geopolitical conflicts—such as those in Ukraine, Iran, or Venezuela—would likely impact global oil markets.

Notably, recent updates to longstanding forecasts propose steadier crude demand growth into the foreseeable future, with some even suggesting a supply crunch stemming from decline rates (the natural rate at which production declines from an existing oil or gas field) and the investment cycle later this decade.

Supportive Technical Conditions

We expect technical conditions to remain supportive. Net new debt issuance should stay contained, below historical averages, and bilateral and multilateral institutions should continue to provide ample and affordable funding to EMs, reducing the need for issuance of new debt. At the same time, 2025 marked a shift in flows, with EM debt posting its first year of inflows since 2021. Global fixed-income investors remain underinvested in the asset class, creating room for increased allocations. Looking ahead, we anticipate a favorable backdrop for continued allocations into dedicated EM debt strategies in 2026.

Compelling Valuations

Valuations across EM debt remain supportive as we head into 2026.

In hard currency, credit spreads are tight but yields remain above long-term averages. We expect overall index-level spreads to tighten toward the 250-basis-point mark, driven primarily by further narrowing in high-yield credits. We believe this backdrop, combined with an expected decline in U.S. Treasury yields (we expect the 10-year to reach 3.5% over the next 12 months), should support compelling returns for the J.P. Morgan Emerging Markets Bond Index (EMBI) Global Diversified.

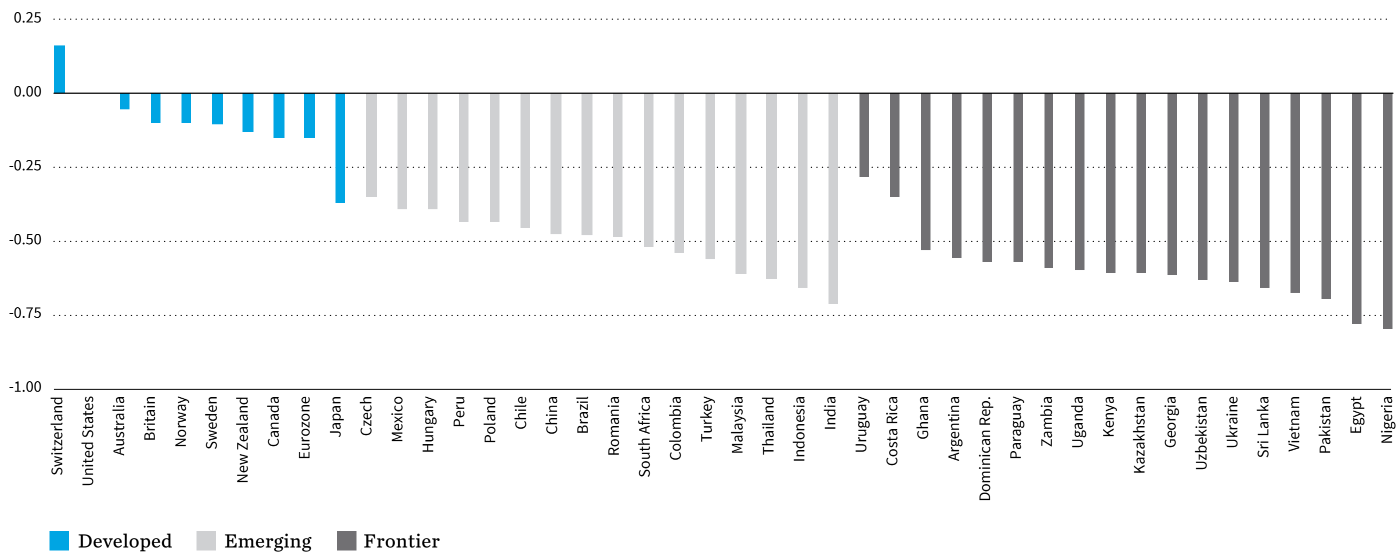
In local currency, we believe investors are underestimating the potential for further monetary easing and see significant value in local rates. Attractive valuations suggest room for currency appreciation, as the U.S. dollar remains in overvalued territory. We expect EM currencies to perform well against the dollar and currencies of other developed markets. Spot rates versus purchasing power parity (PPP, as shown in exhibit 9) and real yields (as shown in exhibit 10) continue to highlight opportunities.

EM Debt | Momentum Continues (continued)

EXHIBIT 9

Spot Currency Deviations From PPP Conversion Rate Per Dollar

EM currencies appear undervalued relative to the U.S. dollar based on PPP deviations, while most developed market currencies hover near fair value or slightly overvalued. We expect EM currencies to perform well against the dollar and those of other developed markets.

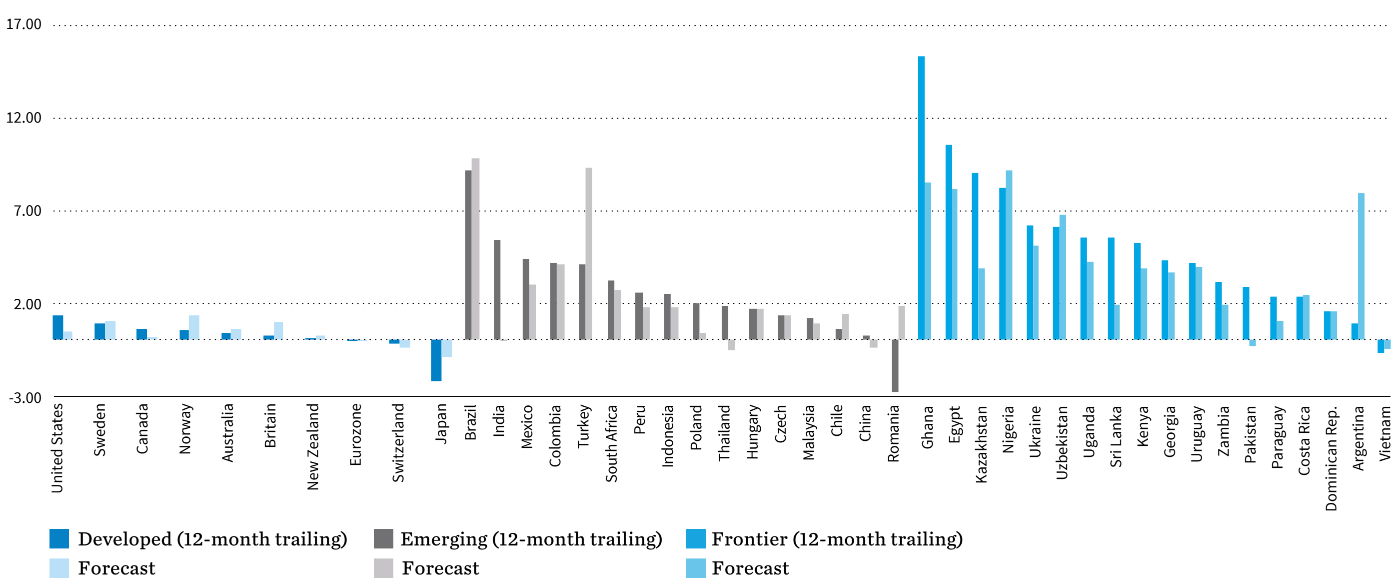


Sources: Bloomberg, Oxford Economics, and William Blair, as of October 31, 2025.

EXHIBIT 10

Developed, Emerging, and Frontier Market Real Policy Rates

Emerging and frontier markets generally exhibit substantially higher trailing and forecast real yields compared to developed markets, where real yields remain near zero or negative. This disparity highlights a potential advantage for investors seeking positive real returns, as EM and frontier economies may offer more attractive income opportunities relative to developed markets.



Sources: Bloomberg, Oxford Economics, and William Blair, as of October 31, 2025.

A Strong Case for Frontier Markets

We also believe frontier markets remain attractive, supported by resilient fundamentals, high real yields, and ongoing foreign exchange adjustments.

While the potential for further rate cuts is generally limited after aggressive easing in 2025, select countries—including Egypt, Ghana, Zambia, and Kenya—have room for additional monetary easing as inflation moderates and external balances improve. In Nigeria, we believe further cuts are likely to be gradual and data-dependent rather than substantial. While the potential for further rate cuts elsewhere is more limited, strong carry, improving fiscal dynamics, and robust external accounts—especially among commodity exporters—should sustain investor interest.

Despite tighter spreads and concentrated positioning in a few markets, we believe the risk/reward profile is still positive, with most frontier debt offering a meaningful spread pickup over sovereign and developed market peers, and systemic risks contained by resilient fundamentals.

Diverse Opportunities in Corporate Credit

We also believe EM corporate credit continues to offer myriad investment opportunities at incremental spreads to sovereign credit at specific durations.

Issuance in 2025 rebounded to its highest level since 2021, still driven by supply outside of China. Expectations are for issuance to increase modestly into 2026, with net financing still marginally negative. Default expectations of 3% rise modestly for next year but are still below historical norms. With top-level credit metrics only marginally weaker, but still stronger than those of developed markets, we believe it is unlikely systemic risks will occur as fundamentals remain resilient.

Lastly, while the index-level valuation conundrum continues, with historically low spreads but still attractive all-in yield, corporate credit continues to offer a spread pickup when compared to its country of risk.

The Metals Outlook

We experienced an exceptional year for metals in 2025, with precious metals leading the charge. Gold and silver reached all-time highs driven by investor flows amid geopolitical uncertainty and Fed rate cuts. Gold was also supported by central bank purchases and silver by liquidity squeezes resulting from tariff concerns and inventory builds in the United States. Platinum benefited from gold's gravitational pull, illiquidity in non-U.S. markets, and supply tightness.

Meanwhile, 2025 industrial metal performance was more diverse as copper outperformed on strong energy transition demand and supply downturns while aluminum gains were more modest given the metal's ample supply. Nickel's oversupply woes continued throughout the year.

For 2026 we believe that precious metals will remain supportive, driven by the Fed rate-cut cycle, geopolitical uncertainty, and fiscal deficits. In our opinion, gold should continue to benefit from ongoing central-bank buying, which we view as a more structural source of demand. Meanwhile, silver's liquidity concerns could ease if tariff risks subside for the metal.

Industrial metals, meanwhile, could see continued momentum from major themes such as electrification and the expansion of AI and data centers, and cyclical demand might return. We remain cautious on Chinese demand growth in 2026 due to policy changes and economic uncertainty. However, nickel's supply-demand balance could improve if the Indonesian government follows through on scaling back supply incentives and energy allocation shifts toward other metals, such as aluminum.

Conclusion: A Bright Outlook

All in all, we anticipate another strong year for EM debt in 2026. While risks remain—stemming from U.S. policy uncertainty, trade tensions, and ongoing geopolitical conflicts—we believe these risks should stay relatively well contained.

A constructive backdrop for performance stems from resilient fundamentals anchored by solid GDP growth, stable fiscal positions, and benign inflation; valuations supported by attractive real yields and currency upside; and technical conditions reinforced by contained net new debt issuance and asset class inflows.

Pragmatism from U.S. policymakers and steady global engagement reinforce our view that the opportunities outweigh the risks, and we are positioned accordingly to capture upside potential across both hard and local currency markets.

"Pragmatism from U.S. policymakers and steady global engagement reinforce our view that the opportunities outweigh the risks."

Marcelo Assalin, CFA, Partner

China | Repositioning for the Next Phase of Global Industrialization

Vivian Lin Thurston, CFA, Partner
PORTFOLIO MANAGER,
EM AND CHINESE EQUITIES

Clifford Chi-wai Lau, CFA
PORTFOLIO MANAGER, EM DEBT

"China also understands that as its economy gets bigger, growth will slow structurally, and the country needs new growth engines."

Vivian Lin Thurston, CFA, Partner

In 2025, China's economic policy reached an inflection point, actively encouraging technology and manufacturing companies to move up the value chain while taking a more hands-off approach to the property market and domestic consumption.

As a result, China's exports of these industries surged in 2025, helping Chinese equity markets outperform other major markets.

What are the main policy developments in China over the past 12 months that investors should be aware of?

Vivian: The biggest change is that the Chinese government has begun to decisively support innovation and technological advancement in areas such as AI, electric vehicles (EVs), and automation. The era of restrictions on China's major internet and technology companies appears to be over.

This is a strategic move to upgrade China's position in the economic value chain from labor-intensive to innovation- and technology-led industries. This will likely be an ongoing, longer-term initiative, and U.S. trade pressure on China has further catalyzed these efforts as China realizes it needs to become more technologically self-reliant. China also understands that as its economy gets bigger, growth will slow structurally, and the country needs new growth engines.

By contrast, government support for other parts of the economy has been rather muted. The country's broad-based economy continues to struggle, whether you look at consumption, the property market, or domestic infrastructure and manufacturing investments. The government has taken relatively minor steps to support these areas but not nearly enough to make a major impact.

Despite a resumption of the U.S.-China trade war, Chinese exports on a global basis have continued to rise as China broadens its exports to other regions. U.S. export volume is still large in absolute terms, but the growth has been coming from exports to the rest of the world. Strong exports have helped alleviate pressure on the domestic side of the economy.

Clifford: Reading between the lines of the new five-year plan the Chinese government issued in October 2025, the government seems set on reallocating resources from low-value manufacturing to high-value technology and services. I expect more capital expenditure to be directed towards building out advanced chip technology, for example. This could be the leading driver of Chinese economic activity in the next few years.

With consumer confidence depressed, the government has undertaken some short-term initiatives to encourage spending—subsidizing upgrades to electrical appliances and smart phones, for example. These types of measures are not very sustainable, whereas a longer-term policy to transition to a higher-value-added position in the value chain could be.

A year ago, China was struggling with macroeconomic weakness on several fronts including the property sector, local authority finance, and consumer confidence. What are the latest developments in these areas?

Vivian: In China's property market, we've seen some stabilization in tier 1[3] cities and certain outlying regions. However, overall demand for property remains weak. Youth unemployment also remains a problem, and consumer confidence is still low.

Given the weakness in the broader economy, you could ask why the government has not been more aggressive with stimulus. Again, I think they are encouraging a structural rebalancing of the economy, pushing it higher up the value chain and trying to find new pillars of growth such as innovation and technology. If the property market can't support China's economy as it did in the past, why stimulate it?

At the same time, the broad-based China economy continues to face deflationary pressures; producer prices have experienced their longest streak of monthly declines since China's market reforms of the late 1970s and early 1980s.

How do you expect the Chinese economy to perform in 2026?

Clifford: As China pursues its goal of rebalancing the economy to higher-value manufacturing, it's doubtful that policy makers will look to push for aggressive growth.

The government's unofficial GDP growth target is 5%, and we've reduced our own expectations and set a lower bound of 4.5%. It's more realistic and gives the government more space to operate while executing this rebalancing act.

Vivian: It's possible real GDP growth could hit 5% in 2025 as exports have accelerated, with some trade being pulled forward because of the trade war. Exports may decelerate a bit in 2026, but they should remain a strong growth driver.

3 In China, a tier 1 city refers to the country's most economically developed, internationally connected, and influential urban centers such as Beijing, Shanghai, Guangzhou, and Shenzhen.

We're less sure about the strength of China's domestic economy, but base effect should start getting better. Over the next 5 to 10 years, China's annual GDP growth will likely decline to 3.5% to 4.0%, which is a natural development as absolute GDP gets bigger.

How has the U.S.–China trade war affected China's export activity?

Vivian: The United States is still one of China's largest trading partners, with gross trades reaching approximately $650 billion in 2024, but Chinese exports to the United States have been in decline since the first U.S.-China trade war in 2018. However, China's gross exports to the rest of the world have increased over 40% during the same period.

EVs provide a prime example of how China is globalizing its high-value industrialization. Chinese manufacturers have come up with technologically advanced, user friendly, and aesthetically appealing EVs at affordable prices and are now leading global EV development. These EVs are an especially good solution for emerging countries. And we're seeing similar trends in Europe, with Chinese EVs accounting for approximately 13% of the EV market in Western Europe.

Given the weakness of the domestic economy, Chinese companies have had to seek growth outside China. The government is encouraging them to go abroad to support exports and take up the slack in the domestic economy.

How have Chinese equity markets performed in 2025?

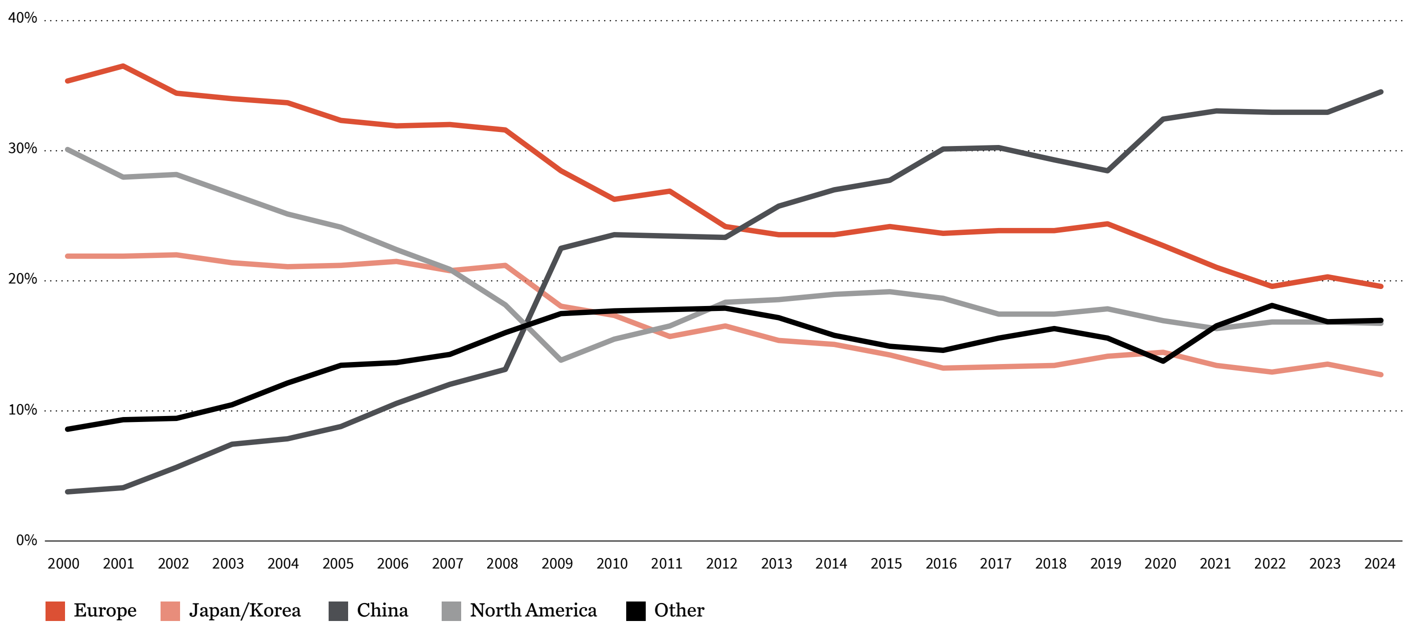
Vivian: Chinese equity markets have outperformed other major markets. The MSCI China Index—mainly Hong Kong-listed ADRs and some China A shares—was up around 37% year-to-date as of mid-November 2025. This compares to about 15.7% for the S&P 500 Index, 19% for the MSCI World Index, and 32% for the MSCI Emerging Markets Index.

We're seeing a long-overdue rerating of Chinese equities. You can point to several catalysts—inflows sparked by distressed valuations and a weak U.S. dollar, benign monetary and fiscal policy, government support for innovation, and the headlines from DeepSeek in January

EXHIBIT 11

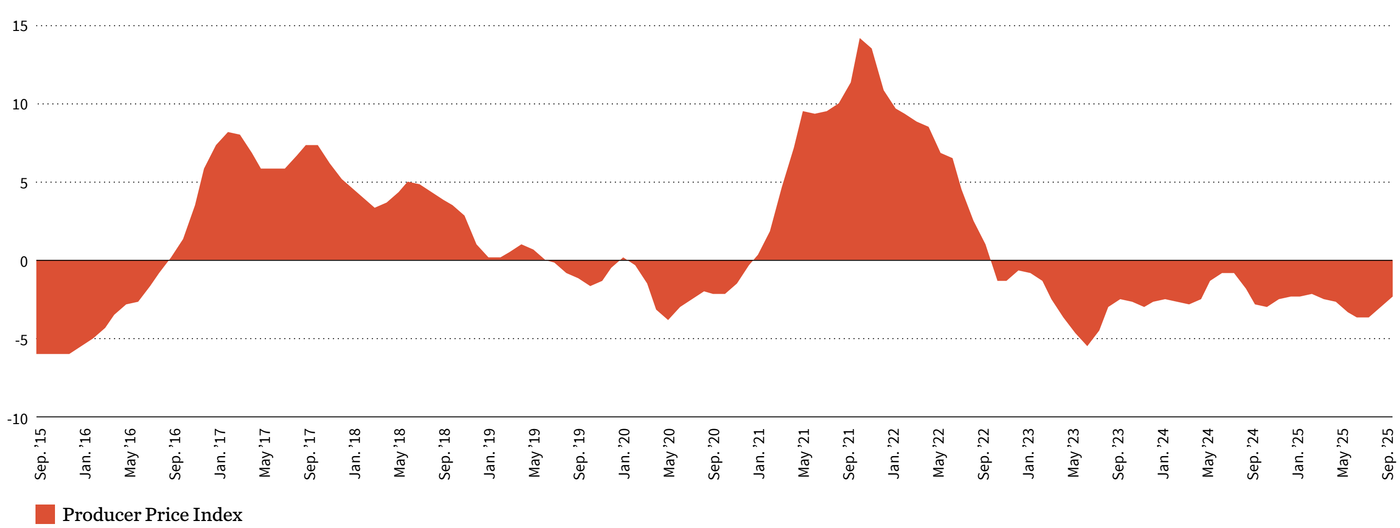
China's Economy: A Tale of Two Cities

China's growing dominance in the global EV market is just one example of the country's momentum in innovation- and technology-led manufacturing.



Sources: BofA Global Research and William Blair, as of December 2024.

At the same time, the broad-based China economy continues to face deflationary pressures; producer prices have experienced their longest streak of monthly declines since China's market reforms of the late 1970s and early 1980s.



Sources: National Bureau of Statistics of China, Bloomberg, and William Blair, as of December 2024.

2025, which is when global investors started to recognize China's AI progress. We've also seen an improvement in tech and internet company fundamentals and earnings.

The U.S.–China trade war is another factor. Chinese equities sold off sharply after the so-called "Liberation Day" at the beginning of April but have outperformed since. This is most likely a reflection that investors are betting that President Trump's harsh anti-China rhetoric is mainly a negotiating position. The October 30, 2025, meeting between President Trump and President Xi, the first in six years, seemed amicable, and it looks as if there was agreement in several key areas.

As a quality growth investor, where do you currently see the most compelling opportunities in the Chinese equity market?

Vivian: Our focus is on innovation and technology. AI will likely continue to be the key global investment theme. In our view, we're still in the early innings in China, but recently, we've seen companies such as Alibaba, ByteDance, and Tencent—which are becoming Chinese hyperscalers—step up AI spending. We expect their stock prices to benefit, first through sentiment and momentum and then through earnings traction.

E-commerce continues to be very competitive, so it's important to pick winners and losers carefully. Alibaba, for example, is starting to turn around its e-commerce business, helped by improved regulatory backdrop, its AI capabilities, and a new CEO who is implementing some encouraging initiatives.

We're also looking at AI-related tech hardware on two fronts: companies servicing the global AI supply chain, supplying Nvidia or global hyperscalers such as Google and Meta, and domestic AI development. China is likely to decouple from the rest of the world in AI systems, partly because of restrictions placed on companies such as Huawei, and thus has had to develop its own domestic supply chain.

The EV supply chain is another focus area for us. There are interesting developments in autonomous driving, and although EV growth remains a compelling top-down story, intense competition continues to pressure margins, especially for the EV original equipment manufacturers (OEMs). Bottom-up, it's harder to find strength, but we believe there could be some winners along the value chain, such as EV battery maker Contemporary Amperex Technology Co. Limited (CATL). It is the largest global EV battery producer with world-leading technology and agnostic to any EV manufacturer, which puts it in a strong position.

> "We believe there may be opportunities to trade the range if the yield curve steepens or the market consolidates or corrects."
>
> **Clifford Chi-wai Lau, CFA**

We also like biotech, specialty pharma, and contract research development and manufacturing organizations (CRDMOs). Chinese companies in this space have been out of favor for the last few years, but as policy and geopolitical risk has declined and demand picked up in the global industry, they are starting to show tremendous earnings recovery. They have showcased to the world how much progress China has made on cutting-edge cancer drugs.

How have Chinese bond markets performed this year, and what do you expect in 2026?

Clifford: It has not been an especially exciting year for the Chinese government bond (CGB) market. The 10-year CGB is now yielding 1.5%, which is not particularly attractive, especially when there is no reason to expect a sharp increase in economic activity.

I don't believe the government is concerned about inflation, so we do not expect interest rates to go much higher, and yields are likely to be range-bound. There may be some steepening in the yield curve, both from natural pressure to normalize and selling activity from local investors reducing fixed-income allocations to catch the rally in Chinese equities.

In this environment, we believe there may be opportunities to trade the range if the yield curve steepens or the market consolidates or corrects, but these shifts would likely be minor. In general, we believe investors should consider limiting CGB holdings and turn those allocations to higher-beta or higher-yielding Asian or EMs.

What is your outlook for the renminbi over the next year or so?

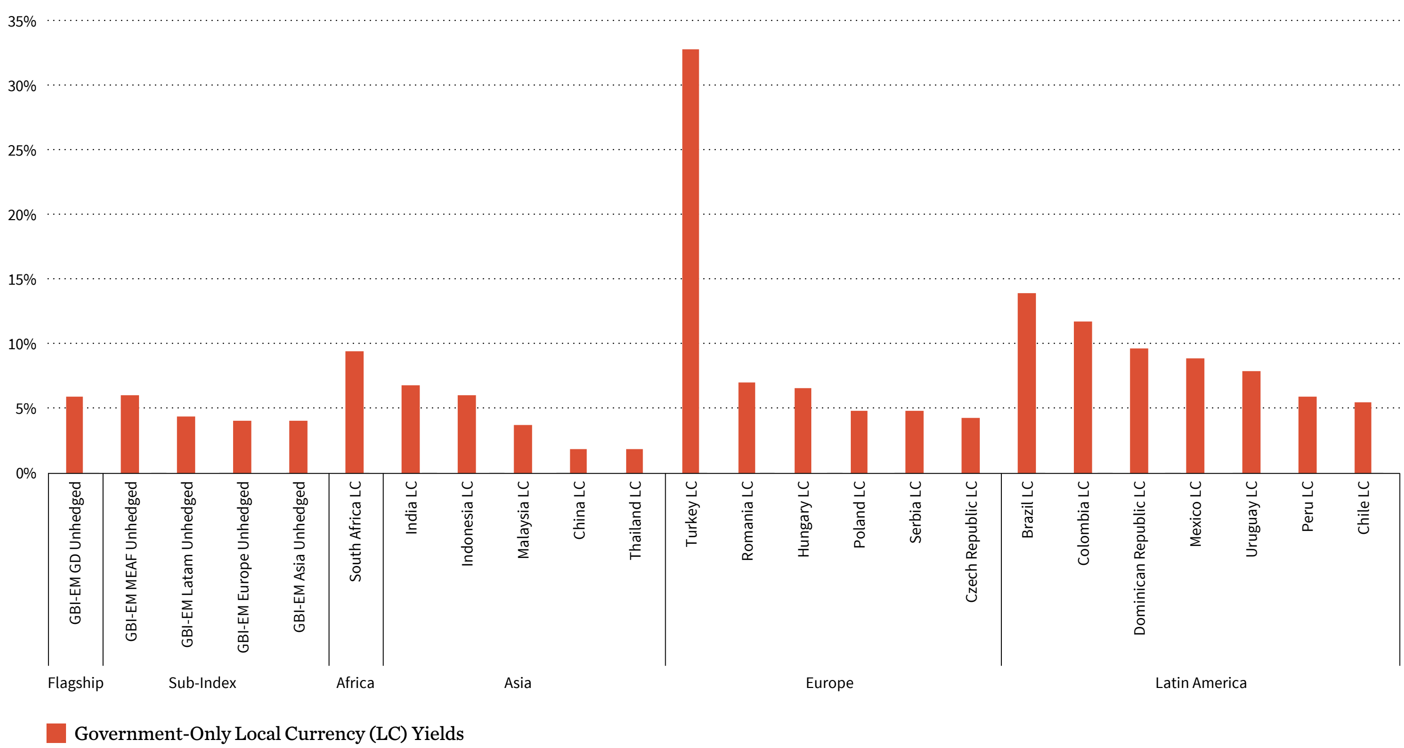
Clifford: We expect the renminbi to remain fairly stable versus other currencies. There is no pressure on the government to devalue because exports have been doing fine without this intervention.

There may be modest technical upside as China continues its efforts to build a currency bloc with EM countries and promote the renminbi as an alternative reserve currency. The share of global trade settled in renminbi has been rising, but it is a very long way from the scale of a reserve currency such as the U.S. dollar, which is incredibly liquid, highly transparent, and without capital controls. China cannot match that, certainly not now.

EXHIBIT 12

China Local Yields Stay Unattractive Compared to Other EM Benchmarks

Chinese government bond yields are among the lowest of all major EMs. Low yields are likely to remain as long as China's domestic economy remains soft and deflationary pressures prevail.



Sources: J.P. Morgan and William Blair, as of October 2025. Local currency yields are represented by the J.P. Morgan Government Bond Index—Emerging Markets (GBI-EM) suite of indices.

Final Takes

Marcelo Assalin, CFA, Partner
HEAD OF EM DEBT

Despite ongoing trade tensions and geopolitical conflicts, EM debt is supported by resilient fundamentals, constructive policy paths, compelling valuations, and a technical backdrop that we believe favors further participation. With potential for further spread compression, currencies still undervalued, and local real rates offering room to move, the environment appears set up for another year of opportunity.

Olga Bitel, Partner
GLOBAL STRATEGIST

With the United States and Europe turning toward domestic renewal and China still weighed down by a housing correction, global growth in 2026 is likely to broaden in uneven but supportive ways. A stable U.S. dollar, ample liquidity, and industrial commodity demand has the potential to create a constructive backdrop for EMs.

Clifford Chi-wai Lau, CFA
PORTFOLIO MANAGER, EM DEBT

It is unusual for Chinese interest rates to have stayed so low for so long and for the market to be so disconnected from the rest of the world. Any excitement in China's bond market will likely come only when there is a case to be made that low-yielding CGBs are about to normalize.

Todd McClone, CFA, Partner
PORTFOLIO MANAGER, EM EQUITIES

As the dollar softens, geopolitical risks remain contained, and structural growth themes such as AI, defense, and electrification gain momentum, we believe EMs stand to benefit. These conditions offer a compelling backdrop for EM equities to realize their long-term potential.

Ian Smith, Partner
PORTFOLIO MANAGER, EM EQUITIES

While we appreciate the arguments for U.S. exceptionalism, there are many phenomenal companies in EMs led by world-class management teams. These companies don't just dominate their local markets; they are major forces globally as well.

Vivian Lin Thurston, CFA, Partner
PORTFOLIO MANAGER, EM EQUITIES

China has reached an inflection point for innovation and technological advancement, driven by capital investment and policy support. At some point, we should start to see the monetization impact show up in improved fundamentals and higher earnings.

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The **CSI 300 Index** is a market-capitalization-weighted index that consists of 300 A-share stocks traded on the Shanghai and Shenzhen exchanges. The **J.P. Morgan Emerging Markets Bond Index (EMBI) Global Diversified** tracks total returns for U.S. dollar–denominated sovereign and quasi-sovereign EM debt while capping individual country weights to enhance diversification. The **J.P. Morgan Government Bond Index—Emerging Markets (GBI-EM)** suite of indices track local-currency sovereign bonds issued by EM countries. (Index information has been obtained from sources believed to be reliable but J.P. Morgan does not warrant its completeness or accuracy. The indices are used with permission. The indices may not be copied, used, or distributed without J.P. Morgan's prior written approval. Copyright 2024, JPMorgan Chase & Co. All rights reserved.) The **MSCI All Country World Index (ACWI)** captures large- and mid-cap representation across developed and emerging markets. The **MSCI China Index** captures large- and mid-cap representation across China A shares, H shares, B shares, Red chips, P chips, and foreign listings (such as ADRs). The **MSCI Emerging Markets (EM) Index** captures large- and mid-cap representation across 27 EMs. The **MSCI World Index** measures the performance of large- and mid-cap stocks across 23 developed markets, representing about 85% of their total market capitalization. The **MSCI USA Investable Market Index (IMI)** captures large-, mid-, and small-cap companies across the U.S. equity market. The **NIFTY** (formally **NIFTY 50**) is India's main stock market benchmark. It tracks the 50 largest and most liquid companies listed on the National Stock Exchange of India (NSE). The **NIFTY Midcap 100 Index** tracks the performance of the 100 mid-sized companies listed on the National Stock Exchange of India. The **Standard & Poor's (S&P) 500 Index** tracks the performance of 500 large companies listed on stock exchanges in the United States. The **U.S. Dollar Index** measures the value of the U.S. dollar against a basket of major foreign currencies to assess its relative strength. Index performance is provided for illustrative purposes only. Indices are unmanaged and do not incur fees or expenses. A direct investment in an unmanaged index is not possible.

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