EMERGING MARKETS

EQUITIES

India and EM are winners of the rerouting shift

We maintain a positive outlook on emerging market (EM) equities for H2 2025, driven by recovering macro momentum, stabilising inflation, and central banks on an easing path. While growth remains positive and earnings decelerate to low single digits, the key narrative is the fading US exceptionalism, highlighted by a weakening dollar and declining trust in US policy, which enhances the attractiveness of EM through repatriation and diversification flows.

The pending sectoral tariffs present risks, but they also fuel localised supply chain initiatives that benefit EM.

We favour selective positioning in domestically-orientated sectors across regions: Turkey and South Africa offer compelling domestic consumption plays in retail and automotive, while undervalued Asian markets like South Korea, Indonesia, and the Philippines present opportunities, with the latter two backed by young demographics and expanding middle classes. Commodity price stabilisation limits support for LatAm exporters, reinforcing our preference for **domestic industries that benefit from reduced foreign competition.**

The rerouting of global supply chains continues to shape EM dynamics, where India and ASEAN emerge as key beneficiaries. India's manufacturing push through initiatives like 'Make in India' attracts multinational corporations, particularly in defence, IT services, and consumer goods. ASEAN economies benefit from their strategic ties with the US and expanding middle-class consumption. Meanwhile, Turkey and Mexico's strategic locations have kept them as re-routing hotspots.

The rerouting trend underscores the importance of EMs not just as manufacturing hubs but as dynamic markets with growing consumer bases. Against this backdrop, EM equities are well-positioned to benefit from structural shifts, provided investors focus on resilient sectors and countries adapting to global economic realignments.

India: the steadfast winner in global supply chain shifts

While near-term market valuations remain stretched relative to the broader EM universe following the Indian equity market's sharp recovery in recent months, we view certain segments of the market—including large-cap equities—as offering better relative value at the present juncture.

We are positive on industrials, consumer discretionary, and financials, where we see an underlying recovery in consumption and public investment trends as well as an easing in domestic liquidity conditions within the broader economy.

Recovery in consumption is supported by supportive policies (e.g pay increases for civil servants) and a noticeable decline in inflationary pressures, while Capex intentions are on the rise.

While preferring domestic stories, it's notable to see India's effort towards a multi-tranche trade agreement with the US, leveraging on the advantages of being a first mover.

China: balancing domestic challenges with global aspirations

Corporate China faces challenging dual pressures: persistent domestic deflationary forces dragging on profitability while increased US rivalry limits access to high-income markets.

In this environment, we favour defensive positioning in domestic demand-driven names, as policymakers continue efforts to shore up confidence and stimulate internal consumption. In the long term, Corporate China is compelled to diversify markets to reduce 'Japanification' risks domestically and rebrand as global players to mitigate geopolitical risks from sanctions.

Companies successfully exploring and exploiting global markets will emerge as winners, while domestically-focused sectors like healthcare (benefiting from an ageing population), renewable energy, and consumer services
offer defensive positioning against external pressures.

EMERGING MARKETS

BONDS

EM bonds to benefit from the EM – DM growth differential and dollar weakness

The **outlook for Emerging Market (EM) bonds, encompassing both hard currency and local currency, is cautiously optimistic for the next six months**. Several factors, including moderating inflation, improving economic momentum and easing monetary policy, are expected to maintain a favourable environment for these assets. A weaker US dollar is also expected to benefit EM, facilitating the servicing of dollar-denominated debt and enhancing potential returns. However, challenges such as geopolitical tensions and trade tariffs continue to pose significant concerns, potentially through a reacceleration of inflation.

Hard currency bonds are likely to benefit from the growth gap between EM and Developed Markets (DM), which is projected to stabilise slightly above historical averages in the coming months. **Emerging market bonds still offer yields that exceed those of DM, providing a buffer against the volatility of US Treasury yields**, which are on the rise. Although the spread between EM yields and US Treasuries is tight, the high **carry environment offers some protection against potential losses**. Additionally, **low volatility enhances the risk-adjusted expected returns of this asset class. Default rates are expected to remain contained.**

Particularly favoured are countries with **strong fiscal discipline, stable political conditions, and improving credit profiles**. Average inflation in EM is expected to stabilise in the second half of 2025, with a potential peak in the first quarter of 2026 due to base effects. This scenario could support bonds issued by **Brazil, Mexico, Colombia, and South Africa**, where real interest rates are attractive.

EM local currency bond views

In Brazil, the central bank has likely finished with rate hikes and may begin to reverse the high rate of 14.75% in early 2026, contingent on clear improvements in the economy and inflation. We expect a relatively conservative fiscal stance in 2025, although the fiscal approach in 2026 will be influenced by the elections in October 2026.

In Mexico, Banxico is responding to a soft economic outlook—growth is nearing a technical recession—while inflation remains mostly within target ranges, aided by pronounced fiscal consolidation despite a wait-and-see approach from the Federal Reserve.

In Colombia, inflation has been gradually decreasing, allowing the central bank to implement rate cuts. However, concerns over a loose fiscal stance have led to caution, with authorities awaiting the right signals before making further moves. We anticipate some spending cuts soon, though these may not fully mitigate fiscal risks, allowing monetary authorities to continue cutting rates with occasional pauses.

In South Africa, after three attempts, the budget has finally been adopted, easing tensions surrounding South African assets. Additionally, negotiations on tariffs with the Trump administration appear to be progressing positively. On the monetary front, authorities are communicating a new inflation target centred around 3%, replacing the current target of 3%-6%. The SARB has successfully navigated various domestic and external shocks that have impacted the economy, and its credibility remains strong. If the new target is adopted, markets are likely to respond positively.

In Turkey, nominal yields are quite high, but real yields remain negative. As happened in the April meeting, the central bank is proving more orthodox, mindful of inflation expectations that pose risks to the disinflation process, FX depreciation and pass-through effects, rising core goods prices driven by resilient domestic demand, depletion of FX reserves, and risks stemming from global trade tensions. We continue to expect the central bank to maintain a cautious stance and resume easing only in the summer, contingent on lower inflation.

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DEFINITION ABBREVIATIONS

Currency abbreviations: USD – US dollar, BRL – Brazilian real, JPY – Japanese yen, GBP – British pound sterling, EUR – Euro, CAD – Canadian dollar, SEK – Swedish krona, NOK – Norwegian krone, CHF – Swiss Franc, NZD – New Zealand dollar, AUD – Australian dollar, CNY – Chinese Renminbi, CLP – Chilean Peso, MXN – Mexican Peso, IDR – Indonesian Rupiah, RUB – Russian Ruble, ZAR – South African Rand, TRY – Turkish lira, KRW – South Korean Won, THB – Thai Baht, HUF – Hungarian Forint, COP – Columbian Peso.

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