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INVESTMENT INSIGHTS
First Quarter 2025

EM equities: 2024 review and 2025 outlook

In 2024, emerging market (EM) equities posted solid gains for the second consecutive year and fourth of the last six. A particularly strong third quarter saw the MSCI Emerging Markets Index outperform both U.S. and non-U.S. developed market indexes, lifting the EM benchmark's year-to-date return to +16.8%. Nearly half of this robust performance was erased in the fourth quarter, however, reflecting concerns about tariffs, a surging U.S. dollar and higher-for-longer interest rates, among other headwinds. While 2025 generally got off to a promising start, sustained improvement for the EM equity asset class is far from assured. Both cyclical and secular factors inform our cautiously optimistic outlook, but thorny issues remain. The following analysis explores these issues and offers our best investment insights into this important but still underappreciated asset class.

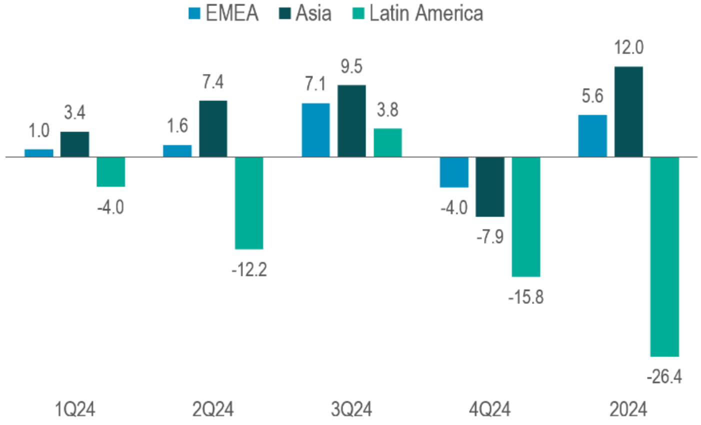
Emerging Market Equities Team
Nuveen

2024: YEAR IN REVIEW

With a +7.5% return in U.S. dollar terms, EM equities delivered another year of good performance in 2024, effectively doubling the +3.8% advance of their non-U.S. developed market counterparts but trailing U.S. stocks, which surged +25%.[1] EM results were boosted by Taiwan (+34.4%) and China (+19.4%), the two-largest country constituents in the MSCI Emerging Markets Index.[2] Overall, 16 of the index's 24 countries rose in 2024.

From an EM regional perspective, Asia (+12%) was the year's top performer, led by Taiwan, China and India (Figure 1). The European, Middle East and Africa (EMEA) region, made up of smaller markets, also posted a positive return (+5.6%). In contrast, Latin America (-26.4%) fell sharply, hindered by Brazil (-29.8%) and Mexico (-27.1%).

Figure 1. Asia advances, Latin America lags
Total return (%) of MSCI EM Index regions[3] in $U.S.



Source: FactSet as of 31 Dec 2024. **Performance data shown represents past performance and does not predict or guarantee future results**. It is not possible to invest directly in an index.

The weakness of EM currencies relative to the U.S. dollar in 2024 weighed heavily on EM equity returns when translated into dollar terms. The JPMorgan EM Currency Index fell -11.1% for the year, with the Egyptian pound (-39.2%), the Brazilian real (-21.4%) and the Mexican peso (-18.5%) the worst performers.

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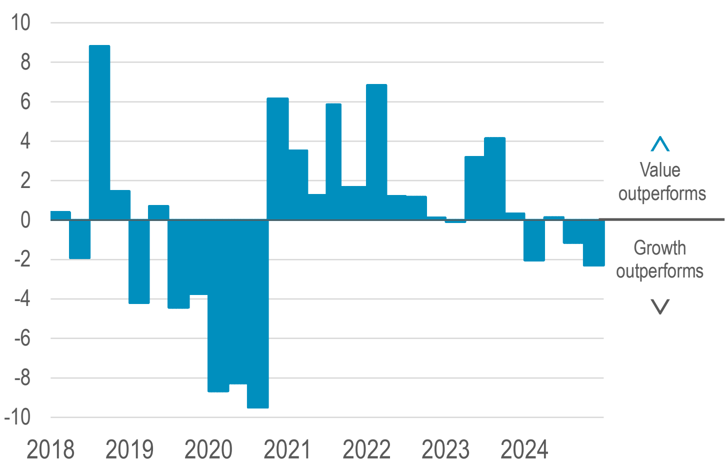
Regarding investment style, EM growth stocks (+10.3%) topped their value counterparts (+4.5%) for the first time in four years (Figure 2), fueled by central bank rate cuts and a broad rally among technology stocks, particularly those with a focus on artificial intelligence (AI).

Figure 2. Growth regains the lead in EM

Total returns (%), quarterly, EM value minus EM growth



Source: FactSet as of 31 December 2024. Based on MSCI Emerging Markets Value and MSCI Emerging Markets Growth indexes. **Performance data shown represents past performance and does not predict or guarantee future results**. It is not possible to invest directly in an index.

SPANNING THE GLOBE: MAJOR EM COUNTRIES OF INTEREST

EM equities are not a monolithic asset class, as market dynamics vary across countries. More broadly, the long-standing trend toward globalization has begun to reverse, and the spectrum of potential outcomes has widened. To better navigate and take advantage of this evolving environment, we believe investors are best served by active management in the asset class. We've identified key macroeconomic, geopolitical, and idiosyncratic opportunities and risks in the following EM nations.

China

The MSCI China Index handily outpaced the overall MSCI EM Index in 2024, +19.4% to +7.5%. This strong performance came despite deeply skeptical sentiment and other headwinds, including headlines claiming that China had become "uninvestable," a significant increase in EM ex-China investment mandates and few signs of a reacceleration in Chinese economic growth.

China's 2024 gains were accompanied by significant volatility. The MSCI China Index surged in mid-September following announcements of government stimulus designed to spur domestic demand, lift investor sentiment and revitalize the ailing Chinese property sector.

But the rally was short-lived, as markets were underwhelmed by Beijing's subsequent policy announcements intended to boost the economy. Investors were also rattled by the Trump administration's plans to impose tariffs on Chinese exports to the U.S.

Despite these market headwinds, we believe there's an upside for Chinese equities. Policymakers haven't exhausted their arsenal of stimulus measures, and regarding tariffs, President Trump may be willing to negotiate a lasting, wide-ranging trade deal rather than implement a punitive one. Meanwhile, China could prosper in an environment in which tariffs on certain sectors are unlikely to be raised and Chinese companies are able to make long-term investment decisions in the context of a more enduring framework.

India

Thanks to massive fund flows from retail investors, the Indian equity market has posted an average annual return of +12.5% from 2020-2024. From an economic standpoint, India has generated 5%+ annual GDP growth for seven straight quarters,[4] driven by a growing middle class, favorable demographics and rising exports.

Those positives aside, we're cautious about investing in this market. The MSCI India Index looks expensive compared to both the S&P 500 and its own 10-year average. Additionally, outperformance by riskier segments of the Indian stock market has led to rampant speculation — an environment that could trigger a major correction if market conditions deteriorate.

Moreover, Indian businesses face government bureaucracy and cumbersome labor laws. And though India has long been one of the few politically stable EM countries, that stability may be in question after Prime Minister Modi's party failed to win another parliamentary majority in June.

> *EM equities are not a monolithic asset class, as market dynamics vary across countries.*

Mexico

Claudia Scheinbaum's landslide presidential win last June fueled fears that her party and its allies would pass constitutional changes designed to dismantle checks on presidential authority. Equity markets tumbled as a result, contributing to Mexico's dismal 2024 stock market performance. Interestingly, Donald Trump's victory and threatened tariffs had little impact on Mexican equities, likely because investors had already priced in a Trump win.

Looking ahead, we're focused on three factors that could support a rebound: (1) The Mexican central bank has proven to be independent and credible, underpinning the country's stability and, in our view, largely removing the prospect of an economic spiral; (2) Four of the five largest stocks in the MSCI Mexico Index have little to no exposure to the export sector; and (3) Mexico's GDP growth is closely tied to the U.S. economy, which remains resilient.

Brazil

After rallying in 2023 (+33%), Brazilian equities stumbled last year. President Luiz Inácio Lula da Silva (Lula) failed to rein in government spending, fueling concerns about the country's deteriorating fiscal outlook, causing Brazil's currency to plunge and driving up inflation.

The country's October 2026 presidential election could provide a spark for Brazilian stocks. Lula has hinted at stepping down after his term ends, and with his public approval rating only in the mid-30s, he will likely face challenges from candidates promising reforms and fiscal discipline. Markets might begin pricing in a Lula defeat sooner rather than later, possibly jumpstarting this market.

South Korea

President Yoon Suk Yeol's sudden declaration of martial law in December triggered a rapid fall in the country's stock market, which returned -23.4% in 2024.

How can South Korean equities bounce back? One potential market positive would be the continued implementation of Korea's "Value Up" program. Launched in February 2024, it aims to enhance corporate governance and market practices to increase shareholder value — a plan similar to measures successfully adopted by Japanese regulators beginning a decade ago.

Taiwan

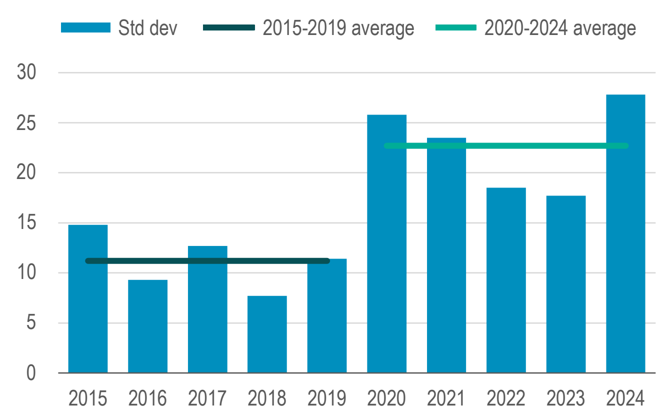
Taiwan is closely tied to the global technology sector, especially semiconductors. (Taiwan Semiconductor Manufacturing Company Limited alone accounts for 53% of the MSCI Taiwan Index's market cap.) The fate of the Taiwanese stock market in 2025 will therefore depend once again on the performance of chip makers, and, in particular, their ability to benefit from booming AI demand. Geopolitics will play a lesser role, in our view, although we'll continue to monitor U.S./China relations and any attempts by Beijing to compel unification with Taiwan.

A MORE CONCENTRATED EM INDEX, WITH GREATER DISPARITY OF RETURNS

Over the five-year period from 2020 to 2024, the average annual standard deviation of equity returns among the five largest countries in the MSCI Emerging Markets Index more than doubled (from 11.2 to 22.7, Figure 3) compared to the previous five years (2015-2019). At the same time, the index has become more concentrated, with the five largest countries making up 80% of the index in 2024, versus 70% in 2015.

Figure 3. Choosing the "wrong" EM country has become more costly

Standard deviation of returns for 5-largest EM countries



Source: FactSet. Based on MSCI Emerging Markets Index. **Performance data shown represents past performance and does not predict or guarantee future results**.

The ramifications of these shifts are clear: During the earlier five-year period, EM portfolio managers who allocated assets to underperforming countries weren't significantly punished, since returns among countries were relatively comparable. But more recently, making the wrong country call has had a far greater impact on performance given the wider disparity of results.

In 2018, for example, a down year for EM equities overall, the disparity in returns among the five-largest index countries was 20.2 percentage points (South Korea, at -20.4% and Brazil, at -0.2%). But in 2024, that spread widened to 57.8 percentage points (Taiwan, at +34.4% and South Korea, at -23.4%).

In terms of individual stock selection, performance data demonstrates the difficulty of generating excess returns, or alpha, in lagging countries. Figure 4 shows the percentage of stocks that since 2015 (1) made up at least 2 basis points (bps) of their respective country's MSCI benchmark index weighting and (2) outperformed the overall MSCI EM Index.

In 2024, only two of the largest 11 countries (China and India) in the MSCI EM Index saw more than 50% of their larger stocks (> 2 bps weighting) outperform. At the same time, three countries had exceptionally low percentages of outperforming larger stocks: Mexico (0%), Brazil (4%) and Indonesia (17%). The only year to produce worse results than 2024 using this metric was 2020, when no country had more than 47% of its larger stocks beating the MSCI EM Index, and seven countries had fewer than 17% topping the index.

Figure 4. Percentage of individual EM stocks outperforming the MSCI EM Index

Based on stocks > 2 bps of country benchmark weight

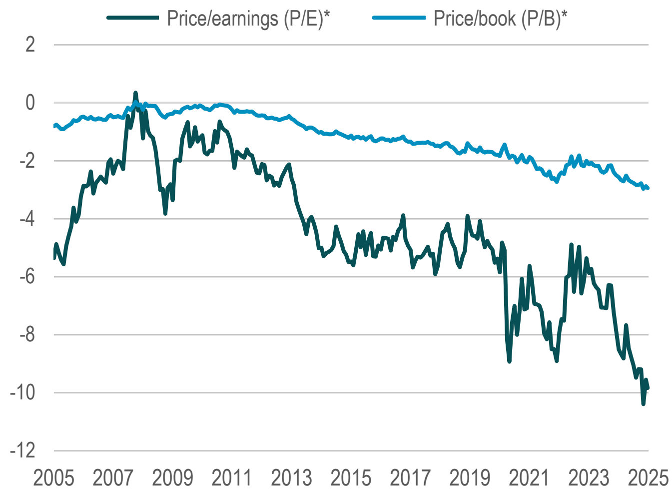
	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
China	60	21	44	44	47	37	38	48	20	55
India	62	32	52	47	21	38	84	73	77	52
Taiwan	43	45	14	60	63	38	87	45	64	34
South Korea	62	25	43	40	14	47	39	40	55	28
Brazil	14	88	27	66	67	7	14	73	76	4
Indonesia	32	44	29	64	14	10	47	94	32	17
Malaysia	24	3	15	74	14	9	47	79	4	48
Mexico	60	11	8	58	23	17	76	85	86	0
Saudi Arabia						10	85	79	39	37
South Africa	26	65	30	26	23	16	67	81	42	35
Thailand	42	57	45	67	26	0	50	93	8	31

< 25%
25%-50%
>50%

Source: FactSet. **Performance data shown represents past performance and does not predict or guarantee future results.** It is not possible to invest directly in an index.

Figure 5. EM equities: from cheap to cheaper

Valuations: MSCI EM Index vs. S&P 500 Index since 2005



*Next 12 months. Source: FactSet. **Performance data shown represents past performance and does not predict or guarantee future results.** It is not possible to invest directly in an index.

MAKING THE CASE FOR EM

While the MSCI EM Index has trailed the S&P 500 Index for seven straight years and 11 of the last 12, this "lost decade" was preceded by another 12-year period (2001 to 2012) in which the MSCI EM Index bested the S&P 500 10 times.

Still, given the challenges facing EM in the current environment, we're not ready to forecast that EM equities will outperform their U.S. market counterparts. We do believe, however, that the asset class can begin to deliver more competitive absolute and relative returns, supported by the following:

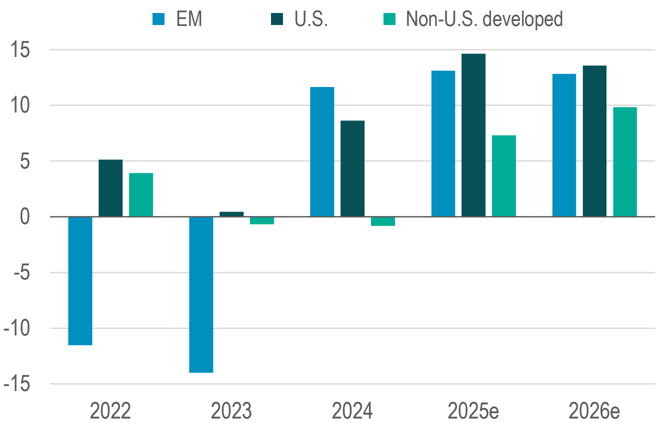
Attractive valuations

Valuations of EM stocks, as measured by their price-to-earnings (P/E) ratios, have been cheap relative to those of U.S. stocks since the 2008 global financial crisis — and they've become even less expensive (Figure 5 above).

> *We believe EM equities can begin to deliver more competitive absolute and relative returns, supported by a number of cyclical and secular factors.*

Figure 6. EM has closed the earnings growth gap

1-year EPS growth (%), EM vs. developed markets



Source: FactSet as of 21 Jan 2025. Data for 2025 and 2026 is estimated. **Representative indexes: EM: MSCI Emerging Markets; U.S.: S&P 500; non-U.S. developed: MSCI EAFE.** It is not possible to invest directly in an index.

A disappearing gap in earnings growth

The most reliable way for EM stocks to catch up is by exhibiting solid company fundamentals and delivering strong earnings growth. And in 2024, EM erased its earnings growth gap relative to both the U.S. and non-U.S. developed markets (Figure 6). Analyst estimates for 2025 and 2026 show EPS (earnings per share) growth that's on par with the U.S., but at lower valuations.

The potential for a weaker U.S. dollar

Influenced by highly anticipated interest rate cuts by the Federal Reserve, the dollar started to weaken in the third quarter of 2024 before strengthening again on the back of Donald Trump's perceived "pro-growth" platform and expectations that the Fed would take its time lowering interest rates amid solid U.S. economic data and still-sticky inflation. Looking ahead, signs of cooling inflation or potentially less stringent U.S. tariffs if they occur, should weaken the dollar — typically a tailwind for non-U.S. stocks.

And although the dollar has been on a long-term upward trajectory since the financial crisis ended in 2009, there have been five shorter periods within the longer time frame during which it fell by at least 10%. The cumulative returns for EM equities in those shorter periods ranged from +17.9% to +100.5%, beating the S&P 500 four times out of five.

A refocus on diversification

Accepted wisdom is that diversifying assets is crucial for long-term investment success. Global allocations to EM equities have not benefited from this accepted tenet, as they represent only 5.3% of global assets under management (AUM) compared to a 20-year average of 8.4% and a current weight within the MSCI ACWI Index of 9.7%. Narrowing this EM underallocation to historical averages would help lift the asset class.

Compelling long-term drivers

EM economies should benefit over time from:

- **Strong demographic trends**. Many EM countries have young, growing populations. The median age in India, for example, is just 28.4 years.[5]
- **An expanding middle class.** The middle class in EM is set to nearly double over the next decade, from 354 million households to 687 million by 2034.[6] As the middle class broadens, economic growth at both the consumer and country level should increase, enabling EM consumers to boost discretionary spending.
- **Ties to "nearshoring."** Moving manufacturing supply chains closer to the home markets in which multinational companies are domiciled should benefit EM broadly, and countries like Mexico, India, Indonesia and Vietnam specifically.

CONCLUSION

There's no foolproof way to know precisely when or to what extent positive drivers like favorable valuations and a shrinking earnings gap may drive the next leg up for EM stocks — especially in an environment where global trade disputes and escalating geopolitical tensions are fueling uncertainty about inflation, U.S. dollar strength and economic growth.

These challenging dynamics can affect different countries in different ways, reinforcing our belief that investing in EM equities is best-suited to active management. Such an approach makes it possible to identify and take advantage of compelling opportunities while seeking to reduce exposure to idiosyncratic risks.

For more information, please visit us at nuveen.com.

Endnotes

1 Based on the respective total returns of the MSCI Emerging Markets Index, MSCI EAFE Index and S&P 500 Index.

2 In terms of market capitalization.

3 EM regions: Asia (80.8% of the MSCI EM Index by market capitalization) consists of China, India, Indonesia, Korea, Malaysia, the Philippines, Taiwan and Thailand; EMEA (12.4% of the index) consists of Egypt, Saudi Arabia, South Africa, United Arab Emirates, Qatar, Kuwait, Poland, Turkey, Greece, Hungary and the Czech Republic; Latin America (6.6% of the index) consists of Brazil, Mexico, Chile, Peru and Colombia.

4 Source: Trading Economics.

5 Source: Worldometer, 15 Feb 2025.

6 Source: Oxford Economics, "The future of the middle class in emerging markets," 16 Oct 2024.

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