Emerging Markets

International Equity Strategies

Second Quarter 2026

Confluence Emerging Markets invests primarily in large cap, growth-oriented companies in the emerging, frontier, and standalone markets around the world, as well as limited exposure to developed markets and ETFs. The strategy's management team employs both top-down and bottom-up fundamental analysis to identify attractive countries and economic sectors as well as high-quality companies worthy of a long-term investment allocation. The portfolio's primary objective is long-term capital appreciation.

Market Commentary

The MSCI Emerging Markets (EM) Index gained 24.1% in the second quarter of 2026, making it the strongest quarterly performance since Q2 2009. The rally was overwhelmingly driven by the artificial intelligence (AI) technology cycle, especially semiconductor stocks in Taiwan and South Korea, alongside improving geopolitics, falling oil prices, and stronger earnings expectations.

The primary driver of the strong emerging market performance was the continued AI infrastructure boom. Emerging markets have significant exposure to semiconductor and technology hardware companies, particularly in Taiwan and South Korea. Investors rotated aggressively into companies supplying chips, memory, networking equipment, and data-center infrastructure. Taiwan's market surged on strong AI-related earnings expectations and South Korea was one of the best-performing markets, led by semiconductor giants such as Samsung Electronics and SK Hynix. The outsized weighting of semiconductors and IT hardware within the MSCI EM Index was the major reason for the index's strong gain. McKinsey projects that worldwide AI-driven expenditures will exceed $5 trillion by 2030 with an accelerated scenario reaching $7.9 trillion. This includes data center infrastructure, IT equipment, and power generation/transmission costs.

Furthermore, higher corporate earnings expectations have driven emerging market equity prices higher. Investors became increasingly confident that the global AI investment cycle would remain intact despite geopolitical tensions. Major hyperscale technology companies continued increasing capital-expenditure budgets for data centers and AI infrastructure, supporting earnings forecasts throughout the semiconductor supply chain.

Market sentiment has also improved as tensions eased in the Middle East during the quarter. Falling geopolitical risk encouraged investors to move back into risk assets, including emerging market equities.

Declining oil prices relaxed inflationary pressures in emerging market economies. Brent crude retreated sharply after peaking during the quarter. Lower energy prices helped reduce concerns about inflation and economic disruption, supporting equity valuations across many emerging market countries. The issues surrounding the Strait of Hormuz have not yet been fully resolved. Whether this becomes a full-blown oil shock depends on how long the strait remains closed and the extent of damage to the Middle East energy infrastructure. If higher oil prices materialize, the macro backdrop is far more favorable than in prior energy spikes. Real rates are positive, inflation expectations are anchored, growth is stable, and the labor market is soft enough to limit pass-through to wages. If the initial inflation spike turns into a growth shock, the Federal Reserve will have room to cut rates. Emerging market central banks, having front-loaded their tightening, would have even more room to ease.

The emerging market rally highlights the resilience of the emerging economies, flexibility of global supply chains, and continued reform efforts that improved the macro stability across the emerging market universe. Since the April 2025 market selloff, emerging market investors have been encouraged by signs of stabilization in China, easing inflation in key countries, and the massive AI buildout.

Due to proactive emerging market central banks, inflation dynamics in these markets are likely to remain better anchored than in the US and other developed markets. Nevertheless, we expect emerging market central banks will be cautious and pause their easing cycles, with others proceeding to cut policy rates only gradually. Higher real policy rates and more firmly anchored inflation expectations suggest that emerging market rates present an asymmetric policy dynamic relative to the US. Should an oil shock tip the global economy into a recession, emerging market central banks retain significantly more room to cut than their developed market counterparts, a macro stabilizer that was absent in prior cycles.

See GIPS Report on pages 5-6.

As we've written extensively, the trajectory of the US dollar (USD) remains an important driver of emerging market equity returns. The MSCI EM Index tends to move inversely with the USD, hence a weakening USD is historically consistent with higher emerging market equity prices. During the second quarter, the USD rose slightly (+1.5%) and had limited impact on emerging market returns; however, the USD appreciated by 4.4% in the past year through June 30, 2026, with no material impact on non-US equity returns. Despite ongoing global conflicts, the Confluence macroeconomic team still feels that the USD will be under pressure for the longer term. The weaker USD provides additional tailwinds to emerging market firms that issue debt denominated in USD since their debt-servicing costs decrease as the greenback weakens.

Emerging market equities remain one of the most underpriced asset classes, in our opinion, with valuations reaching historically attractive levels. As of June 30, 2026, the MSCI EM Index was trading at a forward P/E of 11.7x compared to 15.5x for the MSCI EAFE Index and 21.0x for the MSCI USA Index. Emerging markets continue to trade with stronger earnings growth forecasts (20%+ vs. mid-single digit to low double-digit for developed market earnings), high and improving return on equity, high free cash flow yield, and a dividend yield nearly double that of the US (1.9% for MSCI EM vs. 1.1% for MSCI USA). Furthermore, the emerging/developed market GDP growth gap is set to remain robust at two percentage points in 2026. This recovery can be attributed to global monetary easing, with many emerging market monetary authorities already reducing interest rates in response to lower-inflation expectations, as discussed above.

Quarterly Trading Summary

Several changes were made during the quarter in the Emerging Markets strategy.

In mid-April, we sold HDFC Bank Ltd. (HDB; India, Financials), one of two Indian financials in the portfolio. HDB had significantly weaker performance than current holding ICICI Bank Ltd. (IBN), which we feel offers better growth potential and profitability. The HDB position was replaced with Nu Holdings Ltd. (NU; Brazil, Financials), a Brazil-based holding company that engages in the provision of digital banking services and is the fastest growing, most profitable digital bank in the world. The company offers products across the five financial areas: spending, saving, investing, borrowing, and protecting, with 100 million customers across Brazil, Mexico, and Colombia. Profitability is exploding and market penetration is deepening as NU appears to be disrupting a broken banking system in Latin America. Credit expansion is the company's next growth initiative, and NU offers attractive upside as financial services increasingly shift toward digital banking.

Later in April, we purchased ERO Copper (ERO; Brazil, Materials), a copper producer with operations exclusively in Brazil. The company's primary asset is a 99.6% interest in the Brazilian copper mining company, Mineração Caraíba S.A. (MCSA), which is the 100% owner of its Caraiba Operations — located in the Curaçá Valley in Brazil's Bahia State — and the Tucumã Operation, an open-pit copper mine located in Pará State, Brazil. ERO sits on long-life, expandable assets in a mining-friendly jurisdiction. Due to the global AI infrastructure buildout, copper demand should outstrip copper supply and keep copper prices elevated. ERO is virtually a "pure play" on copper, with high-grade assets, low operating costs (all-in sustaining costs), and long mine lives that should provide a massive growth opportunity in a world of constrained copper supply.

Performance Review

During the second quarter of 2026, the MSCI Emerging Markets (EM) Index was up an astonishing 24.1% in USD terms, outperforming the quarterly returns of developed international markets (MSCI EAFE, +10.8%) and the US market (S&P 500, +15 .2%). By comparison, the Confluence Emerging Markets strategy was up 7.2% in the second quarter, for a one-year gain of 30.8% (both gross of fees) versus 43.5% for the benchmark over the same one-year period. [*The strategy's net-of-fees returns for the same periods were 6.4% QTD and 27.0% one-year trailing. See disclosures on last page for fee description; actual investment advisory fees may vary.*]

The top three stocks represent 29% of the benchmark and the top sector, Information Technology, is 43% of the benchmark. These stocks and sectors were the top performers in the index, but their concentration levels are well above what we believe are prudent for a properly diversified portfolio. This difference in concentration was the primary factor in our Emerging Markets strategy's underperformance relative to the benchmark this quarter. Moreover, two of those top three stocks lacked an ADR in which we could invest. We do own the largest stock in the index, Taiwan Semiconductor Manufacturing, although our position size is nowhere near the 15% weighting that stock has in the index. Our investment discipline emphasizes diversification at much smaller position sizes to prevent any single stock from dominating the portfolio's return or risk profile.

Performance by region showed a wide divergence between the strongest and weakest performers. MSCI EM Asia delivered the best performance, rising by 30.2%, led by South Korea (+87.6%) and Taiwan (+48.9%), as semiconductors (especially memory chips), IT hardware, and AI infrastructure components raced higher. MSCI EM EMEA was the second-best performing region (+2.4%), supported by gains in Hungary (+33.7%), Greece (+20.5%), and Egypt (+25.1%) but offset by weakness in the Middle East. MSCI EM LatAm was the laggard since it lacked exposure to the sectors that surged. LatAm has minimal exposure to AI and meaningful exposure to Energy, Commodities, Financials, and Utilities which did not perform as well as the IT complex.

During the quarter, the two best-performing countries in our portfolio, on an absolute basis, were the Netherlands (former Russian position) and Taiwan, while Indonesia and South Africa recorded the worst returns. From a sector standpoint, Information Technology and Industrials were the strongest sectors, while Materials and Energy were the weakest.

From a relative standpoint, the most accretive country allocations were the overweights and strong security selection to the Netherlands and Panama, while an underweight allocation and security selection in South Korea and an underweight position in Taiwan detracted the most from performance. From a sector perspective, our security selection in Health Care and overweight position in Industrials added the most alpha during the quarter, whereas our large underweight to Information Technology and overweight to Materials contributed negatively to returns.

The performance of Taiwan (+62.4%) and South Korea (+118.6%) on a YTD basis has been breathtaking. Much of the AI capex spending has been directed to these Asian economies, where many of the AI infrastructure components and equipment are manufactured. As AI capex spending continues to ramp higher, these economies will continue to benefit. By the end of the second quarter, both Taiwan and South Korea have displaced China as the largest constituent in the MSCI EM Index, having held the position for the last 17 years. The top three country weights in the index are now Taiwan (27.4%), South Korea (23.7%), and China (19.0%).

Ticker	Security	Avg Weight (%)	Contribution (%)
	Top 5		
ASX	ASE Technology Holding Co. Ltd.	5.45	6.15
NBIS	Nebius Group N.V.	3.35	4.59
TSM	Taiwan Semiconductor Manufacturing Co.	4.34	2.13
VIST	Vista Energy S.A.B. de C.V.	5.15	1.31
BAP	Credicorp Ltd.	2.69	1.02
	Bottom 5		
MMYT	MakeMyTrip Ltd.	1.49	(0.90)
BABA	Alibaba Group Holding Ltd.	2.46	(0.93)
INFY	Infosys Ltd.	1.94	(1.00)
TCEHY	Tencent Holdings Ltd.	3.35	(1.09)
GFI	Gold Fields Ltd.	7.33	(1.43)

(Contribution data shown from a sample account, based on individual stock performance and portfolio weighting)

The portfolio's top contributors and detractors thus far in 2026 are shown in the accompanying table.[1]

What We Are Watching

Macro and micro factors are moving in a positive direction for emerging market equities, in our opinion, indicating to us that they are poised for a period of outperformance in the coming years. In general, we expect countries that are more exposed to the US to outperform relative to those with more exposure to the eurozone or China.

The most significant driver of recent emerging market performance has been semiconductor and IT hardware spending. Valuations are still reasonable provided that the massive AI buildout spending continues. We will be watching hyperscalers' announcements for indicators that the AI investment cycle remains intact and is accelerating. Especially important for emerging markets are Taiwan Semiconductor Manufacturing capex cycles, high bandwidth memory pricing dynamics, and foundry utilization rates.

While our Emerging Markets strategy is significantly underweight Chinese holdings, the health, or lack thereof, of the Chinese economy has international ramifications. Economic recovery is underway, but we are monitoring property sector stress, local government debt, weak consumer demand, and regulatory unpredictability. While "greenshoots" are starting to emerge in the Chinese economy, we are looking for low-risk, high-reward opportunities to add value to our strategy. Chinese IT securities have not yet participated to a meaningful extent in the most recent AI rally, creating interesting investment opportunities. Further, as China continues to export deflation to the rest of the world, global central banks can consider looser monetary policies to stimulate economic growth.

We have previously discussed the potential for China to take military action against Taiwan, and pressure also continues to build in the territorial dispute between China and the Philippines. Both situations carry a real risk of immediate escalation, which could impact investors around the globe. The US response to a potential Chinese attack on Taiwan remains one of "strategic ambiguity," but the position may become a bargaining chip during further China trade negotiations.

2026 is shaping up to be a year of significant transformation for Latin America. The US is already putting into practice its renewed prioritization of the Western Hemisphere. The "Donroe Doctrine," an adaptation of the historical Monroe Doctrine, refers to principles of President Donald Trump's foreign policy and describes a perceived desire by the second Trump administration to reassert American predominance in the region. Supporters see the doctrine as restoring American primacy and combating the influence of China, Russia, and possibly Iran in our hemisphere. The communist regime in Cuba is reeling from the US embargo on goods into Cuba, especially energy as these resources are in extremely short supply. The island nation has suffered several recent grid failures leaving the entire island without power for significant periods of time. The fall of the Cuban government would reduce the chances that China, Russia, or any other "adversary" could establish a presence 100 miles from US shores.

We are closely monitoring the situation in the Middle East to assess whether the fragile ceasefire holds, as well as US attempts to control the Strait of Hormuz through a blockade restricting Iranian ships entering or leaving the country. Negotiations have yet to produce solutions acceptable to all parties. The US and Israel are likely to continue pressuring the Iranian government to abandon its nuclear ambitions, ensure the Strait of Hormuz remains open, and stop supporting terror groups in the region until an agreement amenable to all interested parties can be reached.

Against the backdrop of growing US assertiveness, a crowded electoral calendar will also play a decisive role in the emerging market outlook. Disappointing economic results under left-leaning incumbents are creating momentum for right-wing candidates following a long period of left-of-center dominance. This ideological shift is likely to bring more market-friendly policies, including lighter regulations and business-friendly reforms. The Brazilian election in early October will provide important indicators as to the country's expected fiscal policy direction and other critical data points.

The Confluence International Equities Investment Committee continues to diligently monitor the various geopolitical theaters in order to manage our strategies accordingly.

Portfolio Characteristics[2] (as of 6/30/2026)

10 Largest Holdings	Weight
ASE Technology Holding Co. Ltd.	7.8%
Nebius Group N.V.	5.3%
Taiwan Semiconductor Manufacturing	5.0%
Vista Energy S.A.B. de C.V.	4.5%
Gold Fields Ltd.	4.5%
KB Financial Group Inc.	4.2%
Shinhan Financial Group Co. Ltd.	3.2%
Techtronic Industries Co. Ltd.	2.8%
Credicorp Ltd.	2.7%
Copa Holdings SA	2.7%

Sector Allocation	Weight
Consumer Discretionary	12.8%
Consumer Staples	9.7%
Energy	6.2%
Financials	22.2%
Health Care	2.0%
Industrials	10.9%
Information Technology	19.6%
Materials	9.4%
Communication Services	4.0%
Cash	3.2%

10 Largest Countries	Weight
Mexico	17.4%
China	13.6%
Taiwan	12.8%
Brazil	8.8%
South Korea	8.3%
India	7.6%
Hong Kong	6.0%
Netherlands	5.3%
South Africa	4.5%
Peru	2.7%

Performance Composite Returns[3] (For Periods Ending June 30, 2026)

	Since Inception**	15-Year*	10-year*	5-year*	3-year*	1-year	YTD	QTD
Emerging Markets *Pure Gross-of-Fees[4]*	6.6%	6.0%	8.4%	5.8%	18.9%	30.8%	13.1%	7.2%
Max Net-of-Fees[5]	3.5%	2.8%	5.2%	2.6%	15.4%	27.0%	11.4%	6.4%
MSCI Emerging Markets (Net)	6.3%	5.2%	10.1%	7.2%	23.0%	43.5%	23.8%	24.1%

Calendar Year	Pure Gross-of-Fees[4]	Max Net-of-Fees[5]	MSCI EM (Net)	Difference (Gross-MSCI EM)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	MSCI EM 3yr Std Dev	Composite Dispersion
2009**	10.3%	9.5%	8.5%	1.8%	5	$1,030	-	N/A	N/A	N/A
2010	13.1%	9.8%	18.9%	(5.7%)	5	$1,462	-	N/A	N/A	0.1%
2011	(15.7%)	(18.2%)	(18.4%)	2.7%	7	$2,430	-	N/A	N/A	0.0%
2012	11.4%	8.1%	18.2%	(6.8%)	4	$2,346	-	18.3%	21.5%	0.8%
2013	13.5%	10.2%	(2.6%)	16.1%	1	$220	-	16.0%	19.0%	N/A
2014	(3.6%)	(6.4%)	(2.2%)	(1.4%)	4	$1,636	-	13.9%	15.0%	N/A
2015	(2.7%)	(5.6%)	(14.9%)	12.2%	6	$3,218	-	14.7%	14.1%	0.5%
2016	0.7%	(2.3%)	11.2%	(10.5%)	17	$6,265	-	15.5%	16.1%	0.2%
2017	42.7%	38.5%	37.3%	5.4%	16	$9,288	-	15.0%	15.4%	0.8%
2018	(19.7%)	(22.1%)	(14.6%)	(5.1%)	15	$8,643	$5,486,737	14.8%	14.6%	0.6%
2019	17.3%	13.9%	18.4%	(1.1%)	13	$9,604	$7,044,708	16.0%	14.2%	0.7%
2020	22.9%	19.2%	18.3%	4.6%	14	$11,350	$6,889,798	21.3%	19.6%	2.0%
2021	(11.4%)	(14.1%)	(2.5%)	(8.9%)	9	$8,357	$7,761,687	20.7%	18.3%	0.4%
2022	(13.7%)	(16.2%)	(20.1%)	6.4%	7	$6,068	$6,931,635	21.3%	20.3%	0.6%
2023	15.7%	12.2%	9.8%	5.8%	6	$5,807	$7,200,019	18.5%	17.1%	2.0%
2024	5.6%	2.5%	7.5%	(1.9%)	7	$6,051	$7,280,773	17.4%	17.5%	0.9%
2025	33.9%	29.9%	33.6%	0.3%	3	$7,075	$6,769,052	13.8%	13.4%	0.7%

*Average annualized returns   **Inception is 10/1/2009   *See performance disclosures on last page.*

Portfolio Benchmark

MSCI Emerging Markets (Net) Index – Free float-adjusted market capitalization index designed to measure the equity market performance of emerging markets. Performance results are presented net of estimated foreign withholding taxes on dividends, interest, and capital gains. *(Source: Bloomberg)*

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Indexes: The MSCI Emerging Markets Index is shown as additional information. This index is unmanaged. An investor cannot invest directly in an index. It is shown for illustrative purposes only & does not represent the performance of any specific investment. Index performance figures are reported as net returns.

[1] **Contribution—**Table showing the top 5 contributors/detractors reflects the strategy's best and worst performers (net), based on each holding's contribution to the sample account for the period stated. Individual client portfolios in the strategy may differ, sometimes significantly, from these listings.

[2] **Portfolio Characteristics—**Listings of countries and holdings do not represent all of the countries/stocks currently or previously owned in the portfolio or which Confluence may be currently recommending. Sector/country weightings and holdings of individual client portfolios in the program may differ, sometimes significantly, from these listings.

[3] **Performance Composite Returns—Confluence Investment Management LLC claims compliance with the Global investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Confluence Investment Management LLC has been independently verified for the periods August 1, 2008, through December 31, 2024. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards.**

Verification provides assurance on whether the firm's policies and procedures related to composite maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report.

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The Emerging Markets Strategy was incepted on October 1, 2009, and the current Emerging Markets Composite was created on May 1, 2018. Performance presented prior to May 1, 2018, occurred while the Portfolio Management Team was affiliated with a prior firm and was independently verified for the periods of 10/1/1999 through 12/31/2017. The Portfolio Management Team members were the primary individuals responsible for selecting securities to buy and sell. Composite performance is typically net of foreign withholding taxes on dividends, interest income and capital gains with some exceptions based on custodian treatment. Confluence Investment Management LLC is an independent registered investment adviser. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. The US Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

[4] Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

[5] Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite: 1.00% on the first $500,000; 0.90% on the next $500,000; and 0.75% over $1,000,000.There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Subsequent to February 1, 2013, bundled fee accounts make up 100% of the composite for all periods. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Performance prior to February 1, 2013, is based on the Emerging Markets–Direct Composite which was initially created on October 1, 2009. The Emerging Markets–Direct Composite includes accounts that pursue the Emerging Markets strategy, but do not have bundled fees. Gross returns from the Emerging Markets–Direct Composite include transaction costs and net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly.

A complete list of composite descriptions is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. The annual composite dispersion is an equal-weighted standard deviation, using gross-of-fee returns, calculated for the accounts in the composite for the entire year. Prior to year-end 2018, the annual composite dispersion was an asset-weighted standard deviation calculated for accounts in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Emerging Markets Composite contains fully discretionary Emerging Markets wrap accounts. The Emerging Markets portfolio invests in US-listed shares of companies from emerging markets.

**Results shown for the year 2009 represent partial period performance from October 1, 2009, through December 31, 2009. N/A-Composite Dispersion: Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. N/A-3yr Std Dev: Composite does not have 3 years of monthly performance history.