



A richer blend

Why frontier markets offer real diversification beyond the US technology mega-caps.

Update
09 December 2025

Emerging markets are back in the spotlight as developed counterparts grapple with economic headwinds and shifting global dynamics. While they offer growth at compelling valuations, diversification arguably remains the main draw. Scratch beneath the surface, though, and that diversification may well not be doing what it says on the tin.

The MSCI Emerging Markets Index is dominated by just four powerhouses, with China, Taiwan, India and South Korea accounting for three-quarters of the index. As a result, much of Latin America, Eastern Europe, Africa and the Middle East have been left largely untapped.

There's similar concentration on the corporate front, where a handful of mega-caps such as TSMC, Tencent and Samsung drive returns and earnings are heavily dependent on global demand. TSMC is a case in point: as NVIDIA's primary manufacturer and a key supplier to Apple, AMD and Broadcom, its performance is tied more to the US tech sector than the Taiwanese economy.

And this interdependence extends in both directions, as economist Jim O'Neill put it: "What is GE other than a BRIC stock? Look at Apple: 20% of its revenues are from China."

Frontier markets and smaller emerging markets, however, offer a unique proposition for investors seeking genuine diversification: exposure to growth opportunities beyond the largest economies, together with returns driven by domestic rather than global drivers.

Keeping it local

Falling inflation and interest rates, together with an improving fiscal and political backdrop, are creating positive domestic dynamics in a number of countries across the frontier universe.

In Pakistan, sweeping reforms have brought inflation down from 38% to 6%, paving the way for interest rate cuts. Meanwhile, IMF support and rising foreign direct investment are underpinning the government's target of achieving GDP growth of 6% by 2028. Turkey, Egypt and Bangladesh are also pursuing reforms aimed at restoring stability and rebuilding investor confidence.

Success in these markets depends on deep knowledge of their diverse political and macroeconomic environments. Sam Vecht and Emily Fletcher, managers of **BlackRock Frontiers (BRFI)**,

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bring over four decades of combined experience in emerging and frontier markets, supported by the extensive resources of BlackRock's Global Emerging Markets team.

The team spends considerable time on the ground, meeting not just company management but also customers, suppliers, journalists and policymakers, to build a 360-degree picture of both country and company-specific dynamics.

Moves toward orthodox monetary policy and fiscal discipline are creating macro tailwinds in a number of frontier countries: inflation is trending lower, central banks are preparing to cut rates and momentum is building for cyclical recoveries in domestically-oriented economies. As a result, Sam and Emily have seen opportunities re-emerging in smaller frontier countries such as Egypt, Kenya, Nigeria, Pakistan and Sri Lanka.

The managers combine this top-down view with bottom-up stock selection. A positive contributor to performance has been BRAC Bank, a leading SME lender in Bangladesh, whose shares are up more



than 50% year-to-date as credit penetration deepens and financial inclusion improves.

Another standout performer has been Emaar Properties in the UAE, owner of the Burj Khalifa and Dubai Mall, which has rallied more than 40% in the past year on the back of rising demand for residential, hospitality and leisure assets.

The benefit of an active approach

Frontier markets are often perceived as more volatile than their emerging counterparts, but the numbers tell a different story. Over the past five years, the MSCI Frontier Markets Index has posted volatility of 12.6%, comfortably below the 15.7% and 15.4% for the MSCI Emerging Markets and USA indices respectively (as at 28/11/2025).

This resilience has been evident this year when global equities sold off sharply post Trump's 'Liberation Day'. In the following week, the MSCI Frontier Markets Index fell just 8% - less than emerging markets, the US, UK and Europe.

In addition to their reliance on local dynamics, frontier and smaller emerging markets also exhibit relatively low correlations with one other. Saudi Arabia's equity market has little in common with Indonesia's, while developments in Vietnam may have little bearing on Pakistan.

For BRFI, this dispersion allows dynamic allocation across a range of countries and sectors, offsetting risk and reducing portfolio volatility. In April, for example, Vietnam's export-led challenges dragged the market lower but were offset by gains in Hungary, Thailand and the U.A.E.

Active management also helps manage liquidity risk. BRFI focuses on larger companies and markets with high daily trading volumes, reducing the chance of being trapped in illiquid positions.

After years of limited investor interest, valuations across many frontier and smaller emerging markets also remain compelling. Companies often trade at substantial discounts to both larger emerging and developed market peers despite strong fundamentals. Limited sell-side coverage also creates further scope for active managers to identify mispricing opportunities.

BRFI's track record demonstrates the power of this approach: the trust has delivered a share price return of 124% over the past five years, compared with just 52% for its benchmark (as at 31/09/2025). While the trust has traded at a premium on occasions, it currently sits at a discount of around 2%.

Emerging markets may have become concentrated bets on a handful of economies and mega-caps but frontier and smaller emerging markets still offer an untapped source of genuine diversification. With returns driven by domestic demand, low correlations and attractive valuations, they offer a rich blend of growth and diversification for long-term portfolios.

All data as at 04/12/2025 unless specified otherwise.

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