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# Mosaic theory: from fragments to conviction

**No single indicator tells investors everything they need to know. Mosaic theory builds a fuller picture by bringing together the signals that drive markets. Applied to emerging market equities today, the framework supports a constructive view on the asset class.**



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Durable investment views rarely rest on a single datapoint. Markets are too complex, noisy and interconnected for that. Much like a mosaic assembled from individual fragments, mosaic theory combines a range of signals – from macroeconomic data to investor behaviour – to develop a more comprehensive investment view.

As multi asset investors, mosaic theory can form a valuable part of the investment process for some of our strategies where it can provide balance, challenge and discipline. Mosaic theory does not eliminate uncertainty, but it helps show where the weight of evidence is strongest, where confidence should be capped, and where our view needs to evolve.

## Key takeaways

- Successful investment decisions rarely depend on getting one factor right, but on drawing on a broader number of inputs that can allow investors to be more certain in their convictions.
- Mosaic theory turns fragmented data into robust investment conviction by combining independent signals rather than allowing any single indicator to drive asset allocation.
- Emerging market equities show mosaic theory in practice: favourable signals from earnings, cyclical growth and technicals outweigh concerns around valuation, liquidity and risk, supporting a measured overweight.

## Seeing the bigger picture: why mosaic theory matters

The value of mosaic theory is that it can lead to more robust investment decisions, not more precise forecasts. It allows investors to cross-check indicators, incorporate uncertainty and build conviction probabilistically rather than treat one scenario as truth. This matters when markets send mixed messages: growth can improve even as valuations become

stretched, and sentiment can improve even as risks increase. Mosaic theory integrates those tensions into investment decision-making rather than allowing one narrative to dominate.

Mosaic theory also provides a behavioural discipline: it reduces the risk of overreacting to headlines,

chasing crowded trades or anchoring on a single datapoint. In practice, the weight assigned to each factor changes over time: cyclical growth and monetary conditions often matter more for shorter-term positioning, while valuation matters most at extremes. Conviction comes from judging which signal matters most.

## Mosaic theory in practice: assessing emerging market equities

Emerging market equities offer a useful case study in the application of mosaic theory. We begin with valuation, an important signal that

currently offers neither a compelling reason to invest nor a significant cause for concern. From there, we assess the other factors shaping

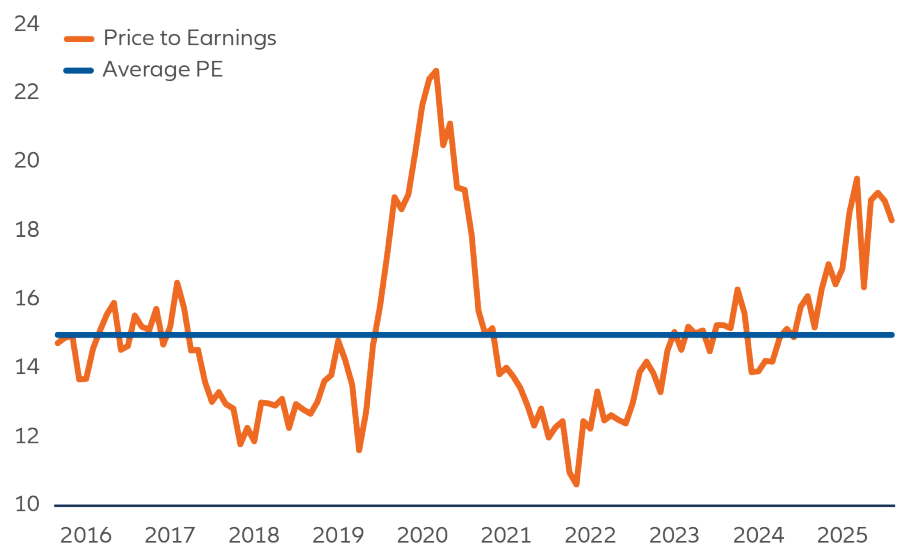
the outlook, before bringing the individual signals together to form an overall view of the asset class.

### 1. Valuation – neutral

Valuation remains an important starting point – but in this case, it is not decisive. Emerging markets (EM) continue to trade at a discount to developed markets, but this discount is no longer compelling enough to anchor a strong standalone investment case. The valuation gap has narrowed, and EM is now broadly fairly valued relative to its own history (see Exhibit 1). More importantly, the composition of the index has changed. EM is no longer simply an old-economy, commodity-sensitive exposure; it is increasingly shaped by technology and AI-linked supply chains. That makes headline valuation comparisons less straightforward than they once were.

Within the mosaic for EM equities, valuation therefore plays a neutral role: it does not argue against EM, but it also does not justify aggressive positioning.

**Exhibit 1: Emerging market equities are now broadly fairly valued relative to historical trends**



Source: Bloomberg. Data as at 31 August 2026

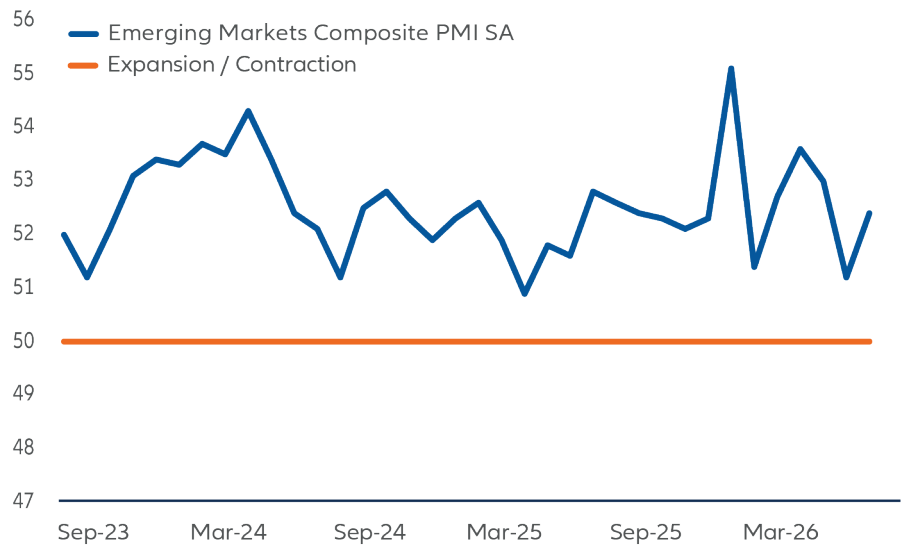
## 2. Cyclical growth – clearly positive

The growth backdrop is where the case becomes more compelling. Emerging markets continue to benefit from a structural growth premium over developed markets, supported by demographics, urbanisation and productivity catch-up.

At the same time, cyclical tailwinds are strengthening. Global investment cycles – including infrastructure spending and AI-related capex – are disproportionately supportive for EM economies with industrial and technology exposure. This is demonstrated by the expansionary Emerging Market Composite Purchasing Managers' Index (PMI) that tracks private sector output across emerging economies.

The result (see Exhibit 2) is a clear growth advantage, both structurally and cyclically. This is a key pillar of the overweight case.

**Exhibit 2: Private sector activity in emerging markets is growing**

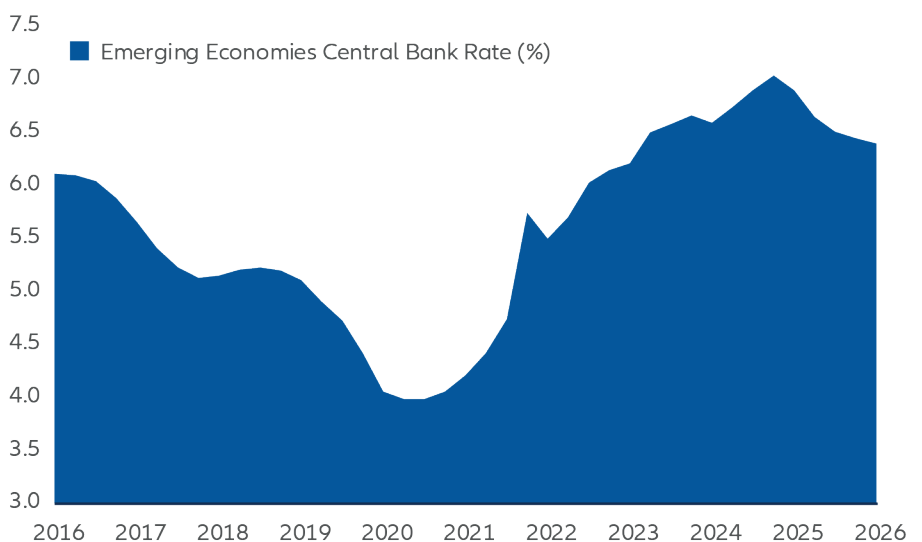


Source: Bloomberg. Data as at 31 August 2026

## 3. Monetary conditions – neutral rather than supportive

Monetary conditions are no longer the clear tailwind they appeared to be earlier in the year. A firmer US dollar and a less benign global liquidity backdrop have reduced the support for EM assets. At the same time, many EM central banks still retain policy flexibility, having moved earlier in the inflation cycle than their developed market counterparts (see Exhibit 3). The result is a mixed signal: not a reason to abandon the EM case, but no longer a major source of conviction. This combination creates a neutral liquidity environment.

**Exhibit 3: Many emerging market central banks have monetary policy flexibility**

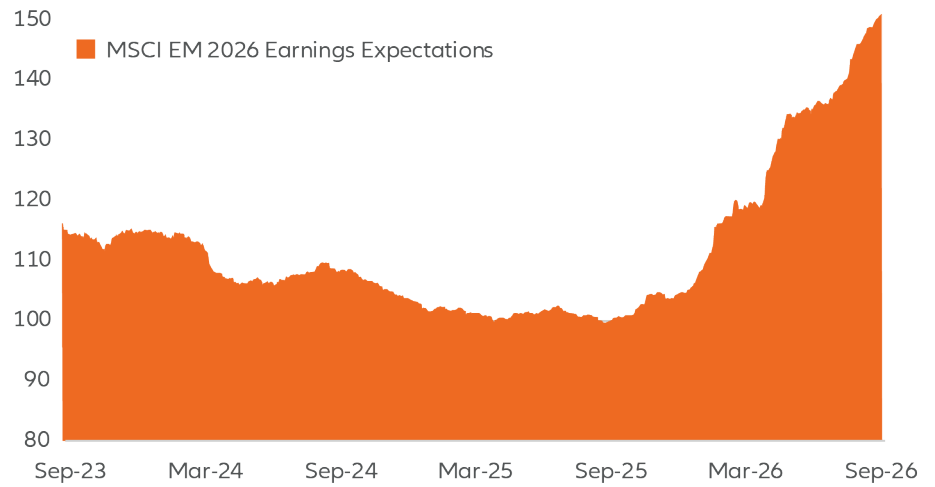


Source: Bloomberg. Data as at 30 June 2026

#### 4. Earnings – sharply improving

Earnings are the most powerful signal in the current mosaic. Earnings revisions have moved sharply higher (see Exhibit 4), initially driven by AI-related supply chains, but with early signs that the improvement is broadening beyond a narrow group of winners. That distinction matters: a concentrated earnings recovery can support performance, but a broadening one can sustain it.

**Exhibit 4: Earnings expectations have moved sharply higher**

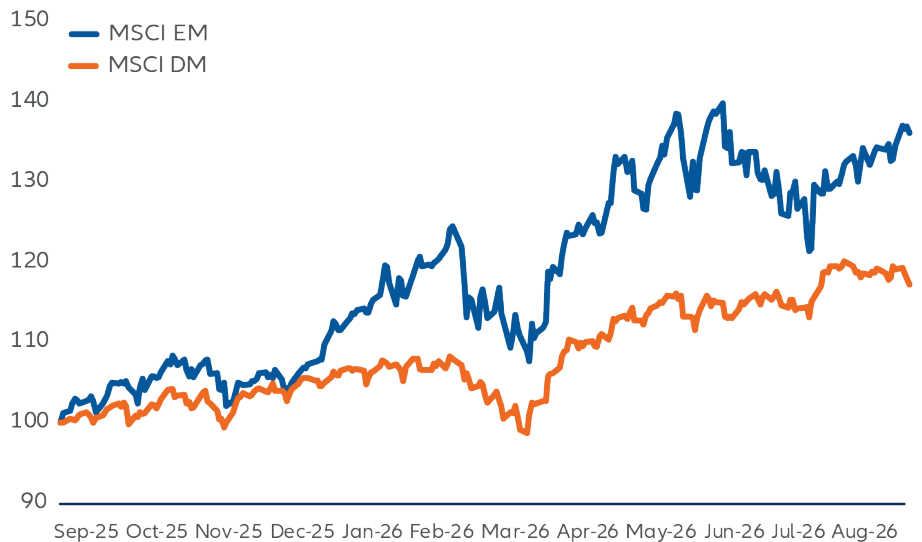


Source: Bloomberg. Data as at 10 September 2026

#### 5. Technicals – turning decisively positive

Technical signals have become increasingly supportive, suggesting that investors are beginning to recognise the improving fundamental backdrop. After years of underperformance, emerging market equities have started to generate stronger relative returns (see Exhibit 5), consistent with improving growth and earnings expectations. This matters because technicals can provide an important test of an investment thesis. Fundamentals may tell investors what should happen; price action reveals whether the market agrees. Today, market behaviour appears increasingly consistent with the positive signals emerging elsewhere in the mosaic. While periods of consolidation would not be surprising following the recent rally, the broader trend remains constructive.

**Exhibit 5: Emerging market equities have started to produce better returns than developed markets**



Source: Bloomberg. Data as at 10 September 2026

6. Positioning and flows – supportive

Positioning remains one of the most compelling aspects of the EM case. Despite recent performance, allocations to EM equities remain below long-term averages. This reflects years of underperformance and persistent investor caution.

From a mosaic perspective, this is powerful. When positioning is light, downside risk from positioning-led selling may be lower, while upside potential from renewed inflows is significant. That has been the case recently, with USD 6 billion of inflows in August pushing full-year totals to a

new annual record of USD 50 billion, more than the USD 37 billion from 2017.<sup>1</sup>

As sentiment improves, flows can become a key driver of returns. This creates a favourable asymmetry in the risk-reward profile.

7. Risks and opportunities – real and meaningful

The case for EM is not without risks. Key vulnerabilities include geopolitical tensions, commodity exposure and sensitivity to global growth and liquidity conditions. In addition, the market-capitalisation-based MSCI index is now highly concentrated by stock, sector and country (see Exhibit 6). The same force that strengthens the EM earnings story also increases its vulnerability: the growing influence of AI-linked supply chains.

These risks do not invalidate the investment case – but they do limit the extent of conviction and ignoring them would weaken the mosaic.

**Exhibit 6: The market-capitalisation-based MSCI index is now highly concentrated by stock**

| MSCI EM Index Weight       | %    |
|----------------------------|------|
| TSMC                       | 15.3 |
| Samsung                    | 8.4  |
| SK hynix                   | 6.1  |
| Tencent                    | 2.7  |
| Alibaba                    | 1.9  |
| MediaTek                   | 1.7  |
| Delta Electronics          | 0.9  |
| China Construction Bank    | 0.8  |
| Hon Hai Precision Industry | 0.8  |
| HDFC Bank                  | 0.7  |

Source: Amundi. Data as at 9 September 2026.

Monitoring AI-related capital expenditure (capex) remains critical. Any slowdown in spending could have an outsized impact on parts of the EM universe, as recent market moves have demonstrated. Even modest shifts in investor sentiment have led to substantial share price volatility, particularly where speculative positioning had become elevated. While the sector undoubtedly carries risks, a continuation or extension of the AI capex cycle could support both earnings growth and valuation re-rating, providing meaningful upside potential for investors.

From signals to conviction: a disciplined EM overweight

Together, these signals create a positive mosaic. Growth, earnings, technicals and positioning support a constructive stance; valuation and monetary conditions argue for discipline; and identifiable risks cap the level of conviction. The result is not a blanket endorsement of EM

equities, but a reasoned case for a measured overweight, primarily 3-6 months in nature, contingent on a still resilient global growth cycle and exceptional earnings strength. In complex markets, that disciplined conviction can be a

meaningful edge. Mosaic theory’s value is that it turns multiple, sometimes conflicting signals into a disciplined basis for action, helping investors build conviction without mistaking it for certainty.

1 Source: State Street Investment Management, 31 August 2026.

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