

CIO View

CIO View Quarterly | Quarterly Market Outlook – Q1 2026



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Cruising altitude reached despite turbulence

Solid economic growth, supported by neutral monetary policy and supportive fiscal policy, has underpinned the capital markets. A vast array of risks makes diversification a top priority in our view.



Vincenzo Vedda
Chief Investment Officer

“ Despite all the risks, most asset classes should continue to be strong this year, provided the economic cycle remains intact. ”

There are many risks at present in the global picture and yet we remain optimistic and expect solid returns in the vast majority of asset classes in the coming twelve months. We assume that the strikes against Iran do not escalate into a broader conflagration that could drive oil prices to levels of \$90 per barrel or more over the longer term. We also have a constructive view of the AI boom though AI's ability to surprise, negatively or positively, was once again demonstrated at the start of the year, when concerns about the new technology's potential became the driver of the largest sector rotations in equities since the Great Financial Crisis of 2007/08.¹ Indeed, because of the uncertainty that is attached to AI, we are favoring the less technology-heavy European and Japanese equity markets over the U.S. market. Their valuation discount relative to the U.S. should narrow from current levels, not least given that we expect more institutional investors seeking greater geographic diversification.²

We do not expect a classical global upswing in 2026 and 2027 but we believe economic growth should provide a sufficiently solid foundation for the capital markets. We are also calm about inflation. In Europe, the inflation rate should fall to an annual average of 2% in 2026; we expect the U.S. to come down to that level only in 2027. U.S. policy interest rates are therefore higher in the U.S. than in Europe at present and we expect the U.S. Federal Reserve (the Fed) to deliver two further rate cuts by March 2027, while the European Central Bank (ECB) is likely to remain on hold. The Bank of Japan is on a quite different course: Its attempts at monetary policy “normalization” may imply two further rate hikes.

This ‘not too hot, not too cold’ environment for growth, inflation and policy rates, known as the Goldilocks scenario, is one in which stocks and bonds can perform well, as price losses from interest rate hikes appear unlikely. In most bond categories we expect sideways movement. Corporate bonds remain attractive in our view, despite very low credit spreads, thanks to the supportive macro environment and high demand, though we favor a selective approach in the high-yield segment, where

we see greater idiosyncratic risks.

Meanwhile, equity markets appear to be benefiting not only from economic growth and moderate interest rates – we see only a very low risk that 10-year U.S. Treasury yields could become entrenched above 4.5% and instead expect a rate of about 4.0% over a 12-month horizon – but above all from earnings. We expect vigorous earnings growth: 6 to 12% in developed markets and up to 20% in emerging markets. The strength of equity markets has recently broadened and is no longer predominantly dependent on the technology sector alone. So long as the economic cycle remains intact, the positive momentum in equity markets should, in our view, continue. Setbacks triggered by nervousness about AI or by the consequences of military conflicts nevertheless remain very likely.

While geopolitics could weigh on equity markets, it should boost gold and oil. For oil, however, we currently continue to anticipate structural oversupply, into which rising demand will only gradually make a dent over the course of the year. However, keeping open the Strait of Hormuz, through which one fifth of daily oil demand flows, is the assumption underpinning our oil price forecast of \$66 per barrel in March 2027. Still, there is certainly a danger that Iran will block the Strait for a longer period – or that vessels voluntarily avoid it given the risks to crew and cargo. In our view, the U.S. dollar has partially lost its status as a safe haven³ and is likely to weaken over time.

We see three major risks: AI, sovereign debt sustainability and geopolitics. With regard to AI, we see risks both to the upside and the downside. Sovereign debt sustainability, for its part, could become an issue at any time, but just when is impossible to predict. Where geopolitics is concerned, the rule is that politics usually only has a lasting impact on markets when its consequences are reflected in companies' bottom line. Our core scenario remains positive on the coming twelve months, as rising corporate earnings and accommodative monetary policy should be helping the markets along.

¹ “Markets Brief: The Big 2026 Sector Rotation as AI Disrupts the Disruptors,” Morningstar as of 2/9/26

² “Global Investor Insights Survey 2025,” Schroders as of July 2025

³ Financial safe havens are investments or assets that are expected to retain or increase in value during times of market turbulence.

Glossary

The **Bank of Japan (BoJ)** is the central bank of Japan.

Diversification refers to the dispersal of investments across asset types, geographies and so on with the aim of reducing risk or boosting risk-adjusted returns.

Emerging markets (EM) are economies not yet fully developed in terms of, amongst others, market efficiency and liquidity.

The **European Central Bank (ECB)** is the central bank for the Eurozone.

The term **Goldilocks economy** refers to a state of the economy, where there is neither a threat of inflation due to an overheating economy, nor a threat of a recession.

Inflation is the rate at which the general level of prices for goods and

services is rising and, subsequently, purchasing power is falling.

Monetary policy focuses on controlling the supply of money with the ulterior motive of price stability, reducing unemployment, boosting growth, etc. (depending on the central bank's mandate).

The **spread** is the difference between the quoted rates of return on two different investments, usually of different credit quality.

Treasuries are fixed-interest U.S. government debt securities with different maturities: Treasury bills (1 year maximum), Treasury notes (2 to 10 years), Treasury bonds (20 to 30 years) and Treasury Inflation Protected Securities (TIPS) (5, 10 and 30 years).

The **U.S. Federal Reserve**, often referred to as "the Fed," is the central bank of the United States.

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