

Investment Outlook

EYES ON THE BALL

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RATES

USTs

We remain tactically NEUTRAL and continue to recommend increasing exposure at 4.50%-4.60%.

We stick to the view that the bias for UST yields is upward amid solid growth, expansionary fiscal policy, and a building term premium. That said, in the short-term, yields above 4.50-4.60% remain a low-probability event, for the following reasons:

- 1) We believe that Trump and the US Treasury rhetoric on lower rates are slowing any rise in yields driven by macro fundamentals.
- 2) Investors continue to be more sensitive to downside surprises in growth and the labour market data rather than upside surprises.

Meanwhile, we raise our bar to turn outright SHORT to 3.95% (vs. 3.80% before). A sudden deterioration in economic growth and/or in the labor market is needed for yields to fall sizeably below 4.0%.

We keep our strategic NEUTRAL stance UNDER REVIEW, with a NEGATIVE OUTLOOK. We continue to think that UST performance in the medium-term will be driven by macro fundamentals (overheating risks), concerns over further fiscal deterioration ahead of midterm elections, as well as political risk premium. All these factors point to higher UST yields over the forecast horizon.

Bund

As Bunds hit our recommended accumulation bar (2.90%), **we turned LONG** (vs. NEUTRAL before) **and set the bar for further accumulation at 3.0-3.10%. We suggest turning NEUTRAL at 2.55%.**

Although incoming news regarding the macro and fiscal outlook in Germany has been constructive lately, we believe that 10Y Bund yields will not rise above 2.90% in the short-term for two reasons:

- 1) EA core inflation slowed in January led by services inflation reaching the lowest level since September 2025 while wage-sensitive services items decelerated markedly, confirming that the underlying trend in disinflation is well supported.
- 2) We do not expect monetary policy expectations for the ECB to turn more hawkish in the short-term, especially considering downside risks to inflation and growth (e.g. the recent EUR-USD rise, the rise in geopolitical uncertainty). In fact, since the beginning of December when the market priced in a 50% probability of a rate hike in H2 2026, expectations have turned much more dovish now expecting 6-7bp of rate cut by year-end.

Strategically, we remain NEUTRAL. While the full and effective implementation of the German fiscal package could trigger a further increase in Bund yields above 3.0% in the medium-term, as investors price in expectations of higher growth potential in

Germany and the EA, we expect solid demand to prevent yields from increasing much more than that.

BTP

As BTPs approached our accumulation target (3.55%) and on the heels of our updated Bund view, we have turned LONG on BTPs (vs. NEUTRAL before).

While the growth-data core-periphery gap is narrowing, we expect BTP carry to continue attracting foreign investor inflows. For instance, Japanese investors are becoming more active buyers of BTPs.

We set the bar for further accumulation at 3.65-3.75%, while we suggest turning NEUTRAL at 3.20%.

Strategically, we remain NEUTRAL:

- 1) The strong and positive correlation with Bunds suggests an upward bias for BTP yields in the medium term.
- 2) In the absence of a decisive improvement in European infrastructure investment, we do not expect a further sharp tightening of periphery spreads vs. the core (perhaps with the exception of spreads vs. France), as progress in macroeconomic convergence between the periphery and the core is likely to slow this year.
- 3) We expect solid demand for BTPs (driven by appealing yields and a steeper curve compared with Bunds), and an improved in the fiscal outlook to help offset at least some of the upward pressure on yields.

EQUITY

We turn NEUTRAL (previously LONG). **We expect global equities to keep moving sideways over the next few weeks within a narrow trading range.** The floor is underpinned by robust macroeconomic conditions, subdued inflationary pressures/monetary easing expectations, and continued fiscal support across regions. The ceiling is set by valuations in a context of diminishing near-term catalysts, which are likely to keep driving rotations and associated performance dispersion.

That said, we tactically continue to buy on dips, anticipating that the upward trend will persist, albeit with more volatility.

The main risks to our constructive outlook stem from any dramatic shift in expectations about the Fed's stance and/or a significant reduction in liquidity.

We view any rise in geopolitical tensions as a potential buying opportunity, provided China is not directly involved. Escalations in Latin America or the Middle East are seen as marginally supportive.

From a regional perspective, we turn more selective (previously a NEUTRAL stance on the main regions). We cut the US to SHORT expecting the current underperformance to continue, while we promote the Rest of the Developed World - Japan, Continental Europe, and the UK - to LONG. We stay NEUTRAL on EM.

From a sector standpoint, we maintain a cyclical tilt with a bias towards traditional cyclical Value names. Within the main sectors, we still like Banks, Diversified Financials, and Materials; while we cut Capital Goods to NEUTRAL (previously LONG) favouring Transportation, now promoted to LONG (previously SHORT), owing to its strong EPS momentum. Within the AI theme, we continue to

prefer semiconductors over software. We tactically downgrade Media & Entertainment and Retail to SHORT (previously NEUTRAL). Within Defensives, Telecoms and Food, Beverages, and Tobacco are now the top picks (previously NEUTRAL and SHORT, respectively), while we downgrade Pharma to NEUTRAL (from LONG) due to its poor earnings momentum.

Strategically, we reiterate our OVERWEIGHT stance on equities and view any market weakness as a buying opportunity. We expect the global benchmark to accelerate in 2026, driven mostly by earnings growth. Our GDP forecasts for the US suggest global EPS will rise by around 12% in 2026. Already rich valuations will limit gains from multiple expansion, whose impact has been progressively decreasing since 2023.

Regionally, we continue to see equity performance becoming more aligned across regions over the next 12 months. That said, we neutralise our previous US and EM tilt in favour of a more agnostic approach. We believe this is the most effective approach for navigating a year marked by synchronized global economic growth and latent geopolitical risks, including the US midterm elections. **Sector-wise, we favour Cyclical over Defensives**, remaining neutral on style.

FX

EUR/USD – Tactically, we remain NEUTRAL on EUR/USD and DXY.

After depreciating sharply on geopolitical and political uncertainty and expectations of a US-Japan joint intervention to prop up the yen, the USD recovered some ground as Trump nominated Warsh as next Fed Chair (markets consider Warsh as a “safer” option compared to the other candidates when it comes to the Fed’s independence).

NEUTRAL positioning remains the best option for these reasons:

- 1) Over the last month, the USD performance has been mainly driven by political and geopolitical developments rather than cyclical factors, confirming that the USD is the asset class that bears the brunt of US political and institutional uncertainty.
- 2) While news on growth out of the euro area is constructive, the underlying trend in disinflation remains well supported, leaving the ECB firmly on hold and markets expecting no action by the ECB in 2026. We do not expect this balance to change in the near-term.

Strategically, we remain LONG on EUR/USD and SHORT on DXY, but we signal that, compared to last month, the balance of risks has shifted further towards a more NEUTRAL stance.

We expect the dollar to remain under pressure in the medium-term due to:

- 1) Geopolitical and domestic political risk in the US. The Supreme Court ruling on the legality of IEEPA tariffs and mid-term elections will be crucial for USD performance.
- 2) Gradually slowing portfolio inflows into US assets, particularly from central banks.
- 3) Continued hedging flows by foreign investors.

However, compared to last month, **we see less downside pressure coming from concerns about the Fed’s independence.** While the outcome of the Supreme Court decision on Lisa Cook, as well as the outcome of the criminal investigation into Chair Powell, remain uncertain, Trump’s nomination of Kevin Warsh as his candidate for the Fed Chair has been met with relief by markets and should clear at least one hurdle for the dollar.

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