Investment Outlook 2026

Fuel in the engine

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In brief

- Global markets remain resilient despite geopolitical noise, with fiscal and monetary stimulus fuelling growth across the US, Europe, and Asia. We expect the expansion to continue in 2026, with activity broadening across regions.
- However, this abundance of liquidity is not without risks. History suggests that excessive stimulus typically shows up in one of two forms: inflation, and/or asset bubbles.
- In this environment, we see several strategies that investors can deploy. Our 2026 Investment Outlook includes four calls to action:
  - Navigate tech concentration carefully
  - Diversify selectively across global equities
  - Don't be fearful of private markets
  - Protect against derailment

Monetary and fiscal fuel is powering expansion

With President Trump returning to the White House and trade hostilities back on the agenda, one might have thought markets would be challenged in 2025. Instead, global equities look set to close out the year with yet another double-digit gain.

Markets have understood that while geopolitical hostilities dominate the headlines, other forces are also at play. The bigger story is the ever-increasing monetary and fiscal fuel being delivered to an already healthy economic engine.

Indeed, never before have we seen fiscal deficits, or rate cuts of this magnitude, delivered outside of recessions (see **Exhibits 1** and **2**).

US citizens will start to feel the personal benefits of fiscal stimulus when the One Big Beautiful Bill results in significant tax rebates early in 2026. This cash flow boost adds to the wealth effects being generated by double-digit stock and house price gains. Under intense political pressure, the Federal Reserve (Fed) now seems likely to bring interest rates back to 'neutral' – a level which it believes to be around 3%.

It is important to note that not all US citizens are feeling the benefits of fiscal stimulus and lower interest rates, with spending increasingly driven by middle- and higher-income households rather than those on lower incomes. **Exhibit 3** depicts why the US has recently been termed the K-shaped economy.

Alongside middle- and higher-income households, businesses are also spending at pace, particularly technology companies. The hundreds of billions of dollars of capex we hear about during US earnings calls are tangibly adding to US growth.

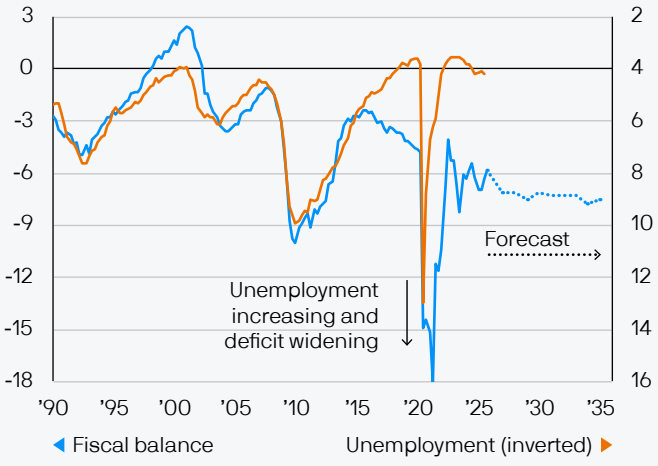
Activity should also meaningfully accelerate in continental Europe in 2026. The enormous fiscal stimulus announced in Germany in 2025 will start to feed through into economic data. This spending covers a very wide range of potential projects, from defence to transport infrastructure and industrial support measures. The investment-focused nature of Germany's plans should aid manufacturing activity and broader growth.

The rest of Europe is also looking to spend more on defence, having pledged to increase military expenditure to 3.5% of GDP (5% including other associated infrastructure spending) by 2035. In 2024, European Union (EU) defence spending reached €343 billion, up 19% year on year, and by the end of 2027 it is set to hit €400 billion. The EU has announced plans to help member states achieve this, including the €150 billion 'Security Action for Europe' (SAFE) programme that provides loans for defence procurement, as well as tweaks to its fiscal rules.

Exhibit 1: Unprecedented fiscal stimulus given low unemployment in the US...

US fiscal balance and unemployment rate

% of nominal GDP (LHS); % (RHS)

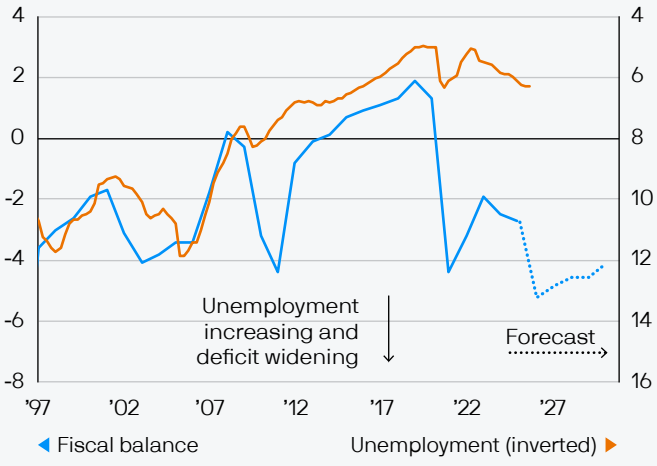


Source: Bloomberg, CBO, J.P. Morgan Asset Management. The fiscal balance forecast is based on the CBO's latest budget and economic outlook. Data as of 31 October 2025.

Exhibit 2: ... and now in Germany

Germany fiscal balance and unemployment rate

% of nominal GDP (LHS); % (RHS)



Source: Bloomberg, Destatis, J.P. Morgan Asset Management. The fiscal balance forecast is from Destatis. Data as of 31 October 2025.

As European Central Bank (ECB) President Lagarde has noted, defence spending can be productivity-enhancing if research and development spills over to innovation. Historically, European defence spending has tilted towards personnel, but future plans look likely to focus on procurement from European-domiciled firms, supporting activity.

Investors shouldn't underestimate the potency of fiscal policy. In our view, the lack of fiscal stimulus in Europe relative to the US goes a long way towards explaining the growth differential between the two regions over the past 15 years (see **Exhibit 4**). Fiscal stimulus also helps explain why southern Europe, which received most of the EU's Recovery Fund, has been performing so well in recent years. The fact that Germany is joining the fiscal party – with growth in government investment forecast to hit 20% year on year in 2026 – is therefore big news.

Europe is also benefiting from monetary stimulus. The ECB was quick to lower interest rates as inflation risks receded. The eurozone is still an economy sensitive to short-term interest rates, and past rate cuts continue to support credit growth in the region – both household and corporate loan growth have marched higher this year. In Germany, increased activity in the housing market is likely to be followed by more spending on furniture and home improvement, which should further support domestic demand.

Trade is also likely to be less of a drag on European growth in 2026. The 'front-loading' of European exports ahead of the introduction of US tariffs in spring 2025 led to depressed exports over the remainder of the year but as this effect fades, trade is likely to normalise.

Germany – having been termed the sick man of Europe in recent years – therefore looks set to finally start growing.

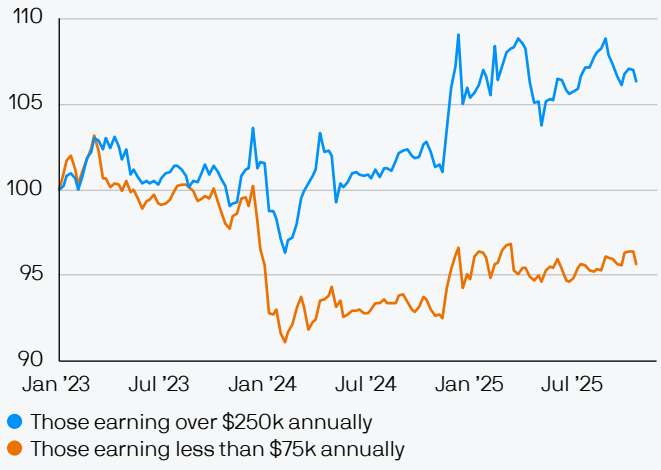
The French political situation remains a blight on the European landscape, but tough decisions – and fiscal consolidation – have now largely been postponed until the 2027 presidential election. France is, therefore, unlikely to derail the European recovery in 2026. With France fundamentally 'too big to fail', we suspect EU solutions may be found to ease this pressure, such as the SAFE programme to support defence spending using the EU balance sheet.

The outlook looks slightly less perky in the UK, with both monetary and fiscal options more limited. As in France, there are political constraints to restraining government spending, so further tax rises will likely weigh on near-term growth. However, slow activity may finally start to bring down inflation, which would at least allow the Bank of England to ease its foot off the brake.

Exhibit 3: Higher income groups account for the majority of US spending

Average weekly spend by annual income bracket

Four-week moving average, indexed to 100 at the start of 2023

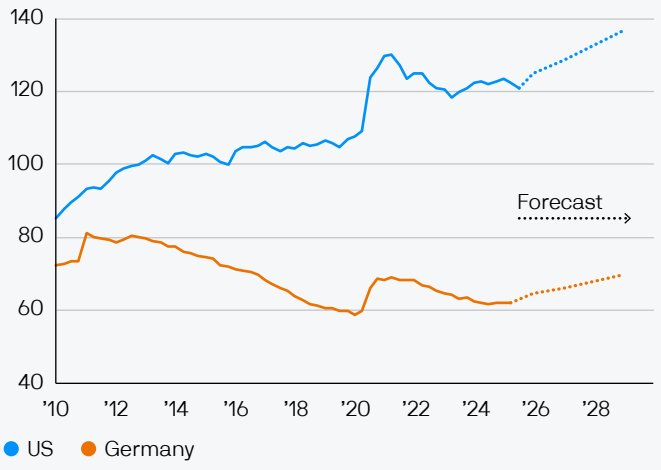


Source: J.P. Morgan Asset Management. The chart is based on select internal Chase data. Data as of 31 October 2025.

Exhibit 4: Germany's former fiscal restraint likely played a key role in its underperformance

Government debt

% of nominal GDP



Source: Bank for International Settlements, BEA, Eurostat, IMF, LSEG Datastream, J.P. Morgan Asset Management. Debt refers to gross debt at face value. Dotted lines represent IMF forecasts. Data as of 31 October 2025.

Asia is also providing monetary and fiscal fuel. The election of a new pro-growth prime minister in Japan with strong views on the need for ongoing loose monetary and fiscal policy has reduced the prospect of meaningfully higher Japanese interest rates, securing the country's place as the ongoing provider of cheap capital to the world.

China has been trying to combine monetary stimulus with targeted fiscal support, but with little success until recent months. Both corporate and household confidence has been subdued since the Covid pandemic, and the government's regulatory interventions during its shift towards a 'common prosperity' narrative appear to have structurally dented Chinese corporates' appetite to take risk.

However, China's outlook appears to be at a turning point. The emergence of the artificial intelligence (AI) company DeepSeek was a reminder to the world of China's entrepreneurial spirit. The recovery in Chinese growth stocks sparked by DeepSeek's progress has lifted the overall Chinese market, and alongside a stabilisation in home prices this should help lift consumer sentiment. China's trade has also not really suffered, despite the headlines, as Chinese goods are either redirected to other markets or rerouted via other regions to US consumers (see **Exhibit 5**).

Overall, with more and more fuel being added to the economic engine, global activity should regain momentum and broaden out regionally in 2026.

Potential derailments: Inflation

Such unprecedented 'peacetime' stimulus is not without risks, however. These risks will be important for investors to monitor to ensure that while they enjoy the ride, they are not blinded by potential issues coming down the track that could derail returns.

History suggests that excessive stimulus can prove problematic if it feeds either rising consumer prices (particularly challenging in the 1970s and early 2020s), or asset bubbles (the 1920s and 1990s).

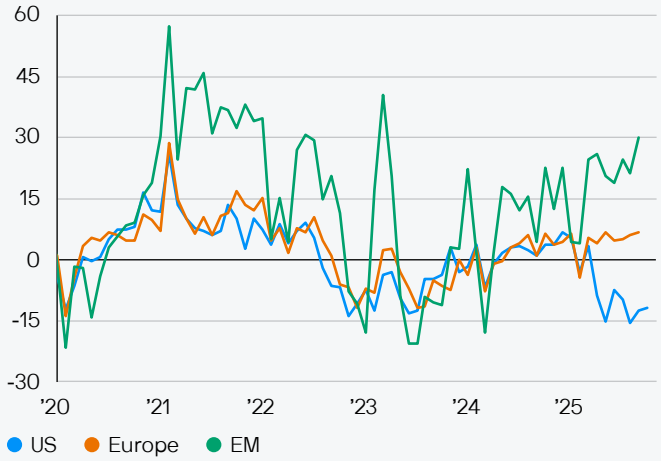
We have been worried about inflation proving problematic, and remain so over the medium term. At present, however, a sufficiently subdued labour market and moderating pay requests are providing central banks comfort that any further uptick in headline inflation will not become embedded via higher inflation expectations and wage growth.

The risk, therefore, for 2026 is that as activity gains momentum, workers start to feel more confident asking for higher pay and inflation does become a bigger issue. We are mindful that economists generally have a poor track record of forecasting inflation spikes. The magnitude and persistence of the inflation rise that occurred in 2022, which proved so traumatic for both stocks and bonds, was not predicted by consensus forecasts (see **Exhibit 6**).

Exhibit 5: China's exports to the US have suffered but trade elsewhere has compensated

China exports by destination

USD billions, actual change year on year

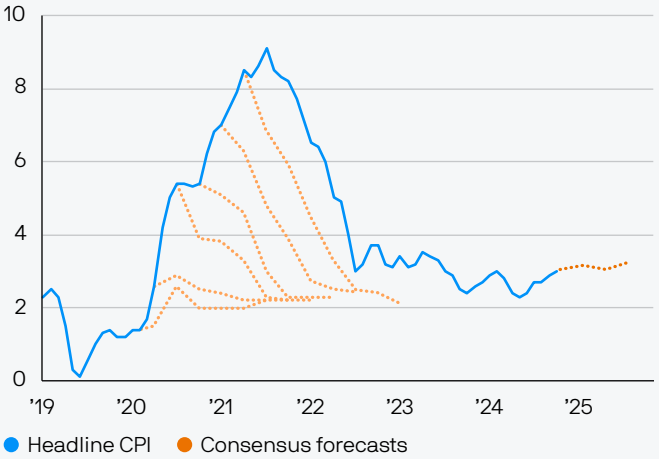


Source: China Customs, LSEG Datastream, National Bureau of Statistics of China, J.P. Morgan Asset Management. Data as of 31 October 2025.

Exhibit 6: Consensus expects US inflation to remain subdued, but didn't forecast the last spike

US headline CPI and consensus forecasts

% change year on year



Source: Bloomberg, BLS, LSEG Datastream, J.P. Morgan Asset Management. Data as of 31 October 2025.

If inflation does firm further, Western central banks would surely have to postpone the idea of further rate cuts. Some might argue that political pressures would lead central banks to push on with easing regardless. However, bond markets may then get jittery about the monetary authorities' commitment to price stability, leading to higher long-run yields.

The Fed will be under particular scrutiny in 2026. A combination of the review of the regional Reserve Bank presidents in February, and the replacement of Jerome Powell as Chairman in May, offers the Trump administration opportunities to exert significant influence over monetary policy. If the administration is successful in removing Governor Cook, and the current Trump appointees play ball, there exists a possibility that it could find itself being able to appoint all 12 Reserve Bank presidents and three out of seven governors including the chair.

This is not our core scenario, but if US central bank independence really comes into question, the asset that might suffer most acutely is the dollar. We remind investors again to think carefully about their currency exposure since, as in 2025, dollar moves have the potential to be a major contributor to final returns.

Potential derailments: Asset bubbles

Excess liquidity does not always show up in consumer prices. Sometimes, it finds its way into asset prices. With equity markets sitting on high valuations and house prices soaring in countries like the US and Germany, this is a risk worth scrutinising.

The trouble is that identifying the point when rational excitement becomes irrational exuberance is hard. Gauging the timing of a turn from euphoria to despair is even harder. For this reason, we have devoted an entire chapter of this outlook to the loftiest part of today's stock market – see Navigate tech concentration carefully. We continue to be nervous about the high degree of concentration towards tech in equity benchmarks, given questions about the return on investment of the enormous amount of capex these companies are undertaking, as well as the gradual rise in leverage now appearing to support this spending. We have also dedicated a chapter to where we see more compelling risk/reward opportunities outside of the US market – see Diversify selectively across global equities.

> **History suggests that excessive stimulus can prove problematic if it feeds either rising consumer prices or asset bubbles.**

Our next chapter addresses private credit and private equity, two markets that have also faced questions recently as the potential recipients of excess liquidity that could lead to problems ahead. We find the narrative here less troubling than recent headlines might suggest – see Don't be fearful of private markets.

Better destinations may yet be ahead

It is not a given that abundant liquidity will lead to either rampant inflation or an asset price bubble. A benign scenario of further sustainable economic expansion is possible, if all this stimulus serves to expand the supply side of the global economy.

This will be the case if AI and other new technologies enhance the productivity of a wide range of companies. The earnings of the tech giants today could eventually be shared with the global corporate universe. These benefits might also then be shared with a more productive labour force. To complete this happy outlook, finance ministers would also find themselves awash with tax receipts from a thriving corporate and household sector, enabling them to repay their earlier spending.

This outlook is possible. We conclude, therefore, with the guidance to remain on the risk train while fuel is still being added to its engine. But we also suggest that investors remain very mindful of how things could go wrong, and to select their carriage carefully – see Protect against derailment. If inflation causes a derailment, both stocks and bonds will likely struggle. A safer onward journey that mitigates against inflation shocks must include the suite of alternatives that provide genuine inflation protection, in our view. If tech falters, those investing passively in US or global equities will find themselves in the front carriage on impact. Investors should therefore think carefully about how they are allocating to ensure they enjoy the ride but also have sufficient protection should the train derail.

Navigate tech concentration carefully

Artificial intelligence (AI) bubble talk is back. Megacap tech stocks have had another strong year, but with focus intensifying on the circular nature of recent high-profile deals and unprecedented concentration in US equity benchmarks, investors are once again concerned around the potential for a major correction in AI stocks.

The AI ecosystem

To address these concerns, first we must get a grip of the increasingly sprawling AI ecosystem (see **Exhibit 7**).

The hardware manufacturers sit at the bottom of the tech stack. This group includes companies such as Nvidia (which designs highly sophisticated chips), TSMC (which manufactures chips for Nvidia, among others) and ASML (which creates precision tools that are used in chip manufacturing).

Next come the 'hyperscalers'. This group includes industry titans such as Alphabet, Amazon, Meta, Microsoft and Oracle.[1] These companies build and operate data centres that are the backbone of AI and cloud computing more broadly. With an estimated half of AI-related capex typically being spent on chips, the hyperscalers are critical customers for the hardware manufacturers.

We'll call our third group the AI architects. These companies develop large language models (LLMs) and other AI applications that can be used for everything from video creation, to chatbots, to complex medical research. OpenAI's ChatGPT is arguably the most famous LLM to date, but there are many other popular examples, such as Anthropic's Claude, Google's Gemini, xAI's Grok, and Mistral's Le Chat.

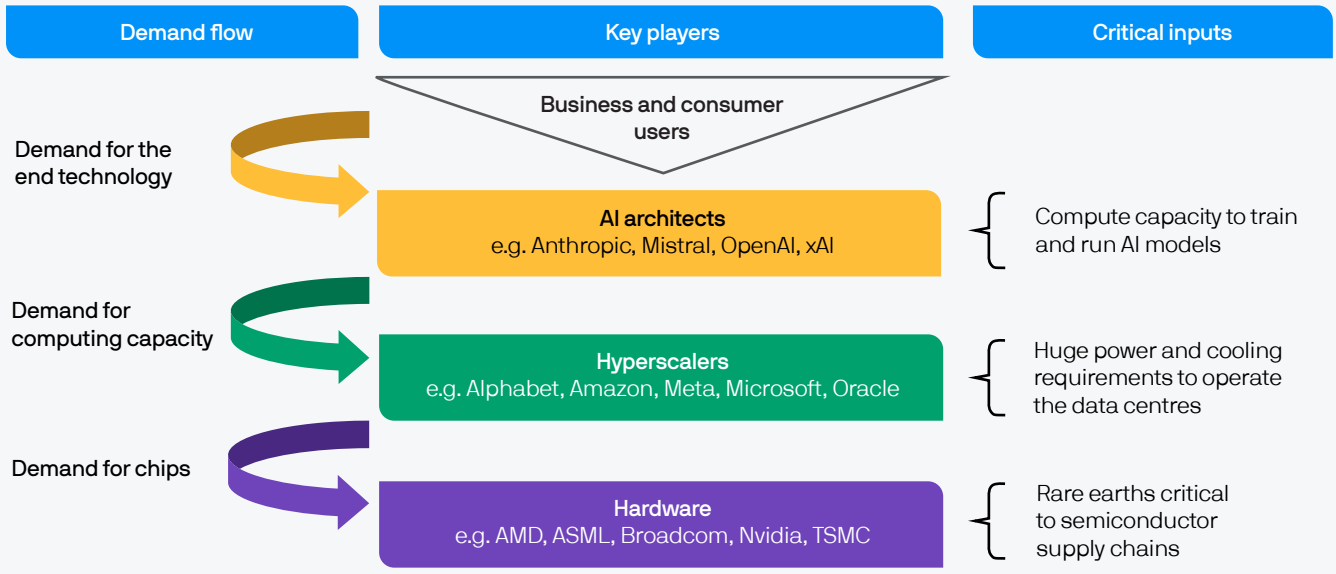
While these buckets neatly encompass the supply side of AI infrastructure, it is far harder to apply a blanket definition to the demand side. Users range from individuals (e.g., using ChatGPT), to enterprises (e.g., a call centre using AI chatbots), to companies that place AI at the heart of their service offering, such as software companies who sell AI-driven tools.

In a well-functioning, mature ecosystem, the money spent by end users must be sufficient to generate profits throughout the system. Take the example of a weekly supermarket shop. The money you spend at the till should be enough for the supermarket, the real estate operator, the food manufacturers and the farmers to all take their cut.

[1] While the link to data centres often receives most emphasis, the picture is muddied by these companies also featuring in many other parts of the ecosystem. Take Microsoft: Azure is Microsoft's cloud computing platform, Microsoft 365 Copilot is an AI-driven productivity assistant and the company has also invested in OpenAI since 2019.

Exhibit 7: There are many dependencies across the AI ecosystem

The AI ecosystem



Source: J.P. Morgan Asset Management, as of November 2025.

> Investment booms do have an unfortunate habit of leading to overcapacity, which in turn damages margins.

In today's AI ecosystem, the demand from end users, both individuals and enterprises, is currently insufficient for all the other players to turn a profit. For several years, the hyperscalers have been largely footing the bill, using revenues from other parts of their businesses to fund the build out of AI capacity, which in turn has created profits for the hardware players. Whether end demand can accelerate fast enough to generate a reasonable return on investment right across the value chain is the million/billion/trillion-dollar question.

Bubble watch

Given the incredible run-up in tech share prices since the pandemic, it is no surprise that comparisons are being made to prior investment bubbles.

Valuations: High, but not prohibitively so if earnings deliver

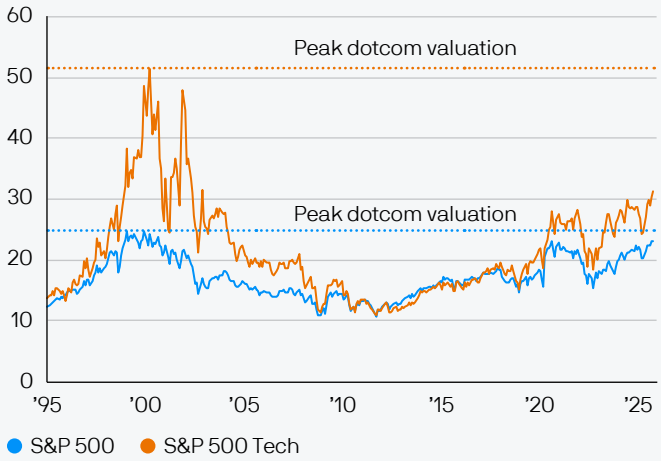
While today's valuations are not as extreme as the dotcom bubble, the S&P 500's 12-month forward P/E ratio of 23x is not far off the peak valuation in 2000, while the tech sector trades on 31x forward earnings (see **Exhibit 8**).

Hardware names currently sit on higher valuations (35x 12-month forward earnings) than the hyperscalers (30x). For the AI architects, however, valuations are harder to compare given that major players such as Anthropic, Mistral and OpenAI are still private today. This lack of visibility makes accurately assessing the fundamentals of a group integral to the entire ecosystem much more challenging.

Exhibit 8: Valuations are high, but still below the dotcom peak

US equity valuations

x, multiple



Source: LSEG Datastream, S&P Global, J.P. Morgan Asset Management. Data as of 31 October 2025.

Exhibit 9: Getting to the top is tough, staying there is even harder

How the most popular tech stocks fared post 2000

Company	Status	P/E at dotcom peak	Return since dotcom peak
Microsoft	Survived	50.9x	1412%
Cisco	Survived	105.4x	42%
Intel	Survived	39.6x	1%
Oracle	Survived	103.9x	653%
IBM	Survived	23.9x	409%
Lucent Technologies	Merged	43.9x	2%
Nortel Networks	Bankrupt	87.6x	-
S&P 500	-	22.6x	620%

Source: LSEG Datastream, S&P Global, J.P. Morgan Asset Management. The dotcom peak is 24 March 2000. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Two key lessons can be drawn from prior run-ups in tech valuations. The first is that high valuations do not automatically prohibit future returns. An investor who purchased Microsoft at a peak valuation of 68x in December 1999 would be up over 1,000% over the following 25 years (provided that they held the stock through a 65% drawdown in 2000). The second lesson, however, is that stock markets generally do a very poor job of predicting future winners during technology revolutions. Looking at the most popular tech companies in the S&P 500 at the dotcom peak in 2000, only Microsoft retained its place in the largest 10 companies a decade later (see **Exhibit 9**). Identifying long-term winners in real time is an incredibly complex task.

Financial health: Much improved versus 2000, but with cracks beginning to emerge

The financial strength of the AI megacaps is arguably the biggest reason to downplay comparisons with the dotcom bubble. Unlike the flimsy nature of corporate balance sheets 25 years ago, Amazon, Apple, Alphabet, Meta, Microsoft and Nvidia are today sat on a cash pile to the tune of $450 billion. Given that tightening credit conditions have often been a major trigger for prior bubbles to burst, this suggests that today's tech titans are in much better shape.

> **Whether end demand can accelerate fast enough to generate a reasonable return on investment right across the value chain is ultimately the million/billion/trillion-dollar question.**

Critically, this financial strength has so far allowed many of the hyperscalers to fund their AI-related capex from free cash flow. We note, however, that capex commitments planned for the coming years will eat further into available cash piles (see **Exhibit 10**). Recent high profile moves from Meta, Oracle and xAI to tap both public and private debt markets bear watching in this regard.

The increasingly circular nature of AI deals over recent months does, however, have some echoes of the late 90s. September's announcement that Nvidia plans to invest up to $100 billion in OpenAI was arguably the highest profile of these investment deals. OpenAI in turn will funnel much of this investment into securing new compute capacity, which will then drive demand for Nvidia's chips.

Exhibit 10: Capex commitments are eating into cash piles
Capital spending from the five major US AI hyperscalers
USD billions (LHS); % (RHS)

Source: Bloomberg, J.P. Morgan Asset Management. The chart shows the total company capex for Alphabet, Meta, Microsoft and Oracle, as well as an estimate of Amazon's AWS spend. Operating cash flow represents cash flow before capital expenditures. Data as of 31 October 2025.

Optimists would argue that Nvidia is using the cash on its balance sheet to simply bring forward future demand. Yet the more that the fate of individual companies becomes intertwined, the greater the risk that a single failure could lead the broader system to unravel.

Market structure: A greater skew towards private markets requires a different approach

Initial public offering (IPO) activity is another major point of difference today. Exuberant IPO activity was a key feature of the dotcom bubble: in 1999, the median first-day return for the 476 US companies that went public was a whopping 57%, compared to just 7% on average between 1980-2024. These bumper returns enticed companies to rush into the market far quicker than normal (see **Exhibit 11**).

While IPO activity has picked up in the second half of 2025, the situation remains far more muted. In part, this reflects a growing preference from companies to stay private, given the combination of a lower regulatory burden and ample availability of private capital, as we discuss in Don't be fearful of private markets.

The good news from companies waiting much longer to IPO is that this has strengthened the overall fundamental picture of the listed tech sector. The bad news is that for investors accessing the AI theme only via public markets, they may well miss out on exposure to some of the long-term AI winners that are only accessible via private equity strategies currently.

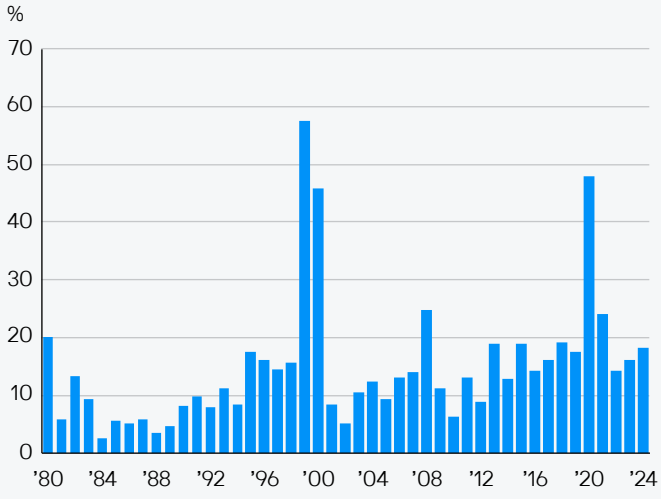
Earnings: Supernormal profit delivery has become the norm, but could be tough to maintain

Unlike in the late 1990s, when valuations surged while earnings lagged, today's run-up in share prices has been driven far more by expanding earnings. This is not only a revenue story, but also a margin one: US tech sector margins are currently more than double that of the broad S&P 500. Investors now assume that tech companies will deliver supernormal profits compared to the rest of the index.

Admittedly, the profitability of the AI names in the private markets is generally far weaker, but their revenue growth has still been impressive. OpenAI is reported to now be generating annual revenues north of $13 billion, although given the company's huge R&D spend, it is not expected to reach profitability until much closer to 2030.

Exhibit 11: IPO activity is less exuberant today

Median first-day return for US IPOs

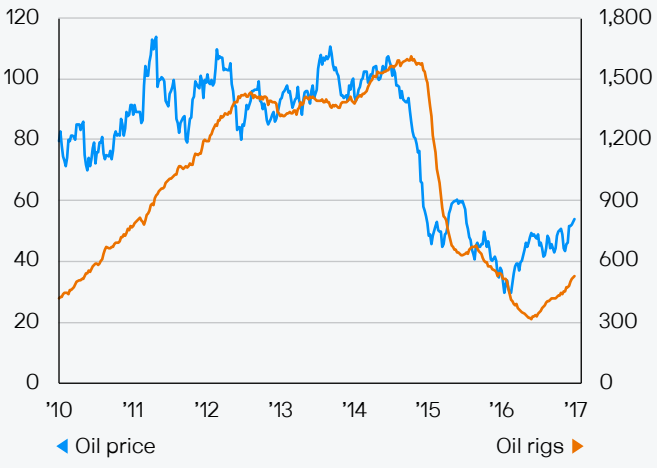


Source: Jay Ritter – University of Florida, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Exhibit 12: The US shale investment boom was followed by a bust

WTI crude oil price and oil rig count

USD per barrel (LHS); number of rigs (RHS)



Source: Baker Hughes, Bloomberg, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Whether this earnings growth can continue depends on both end demand, as well as whether the tech firms can maintain their supernormal margins. Investment booms do have an unfortunate habit of leading to overcapacity, which in turn damages margins. The shale boom of the 2010s is a prime example: breakthroughs in drilling techniques led to a surge in oil supply, before a sharp collapse in oil prices led to a wave of bankruptcies (see **Exhibit 12**).

The biggest challenge for the hyperscalers in accurately estimating future demand is the many variables involved. By 2030, will the resource intensity of current AI have reduced materially? Will we have made major breakthroughs in artificial general intelligence (AGI)? And how quickly will AI hardware be made obsolete by new technological developments? None of these questions have concrete answers today, leading to wide error bars around estimates for both future capex needs and earnings overall.

End demand: The most important question, and the most difficult

If AI ultimately allows companies to create major new revenue streams and significantly cut back on their labour costs, the tech giants will continue to generate impressive earnings growth. Yet if consumers and corporates prove more resistant to spending big sums on new AI tech, achieving a return on today's surging investment will be far more challenging.

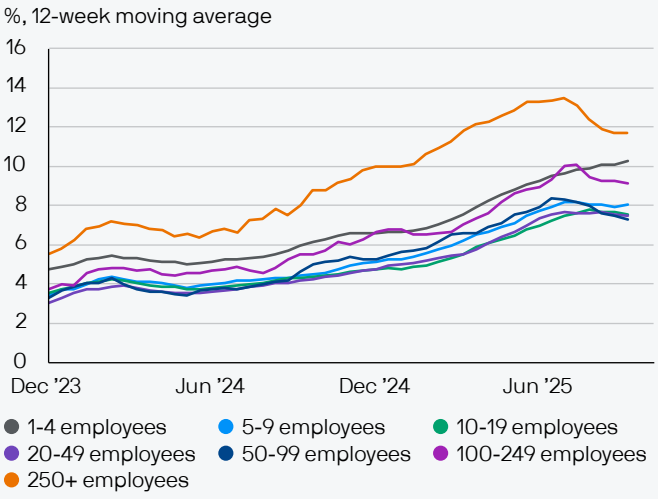
The AI architects have been keen to stress the astronomical growth in their user base, although paid users have been much harder to come by. In OpenAI's case, ChatGPT has eclipsed all records for the pace of technology adoption, yet only 5% of the 800m users of ChatGPT are currently paying customers, according to the Financial Times.

Survey data presents a similarly mixed picture. The US Census Bureau's AI survey suggests that only 9% of US businesses are using AI to produce goods and services, with large variation across sectors. Somewhat concerningly, when breaking out this survey by business size, recent responses suggest that demand from the largest companies may be starting to slow (see **Exhibit 13**).

Other surveys point to a much more positive outlook, such as the Ramp AI Index that shows 44% of surveyed businesses pay for an AI subscription (see **Exhibit 14**), or KPMG's Quarterly Pulse Survey that evidences a steady increase in the deployment of AI agents designed to boost employee productivity.

Exhibit 13: Large businesses are showing signs of pulling back on AI

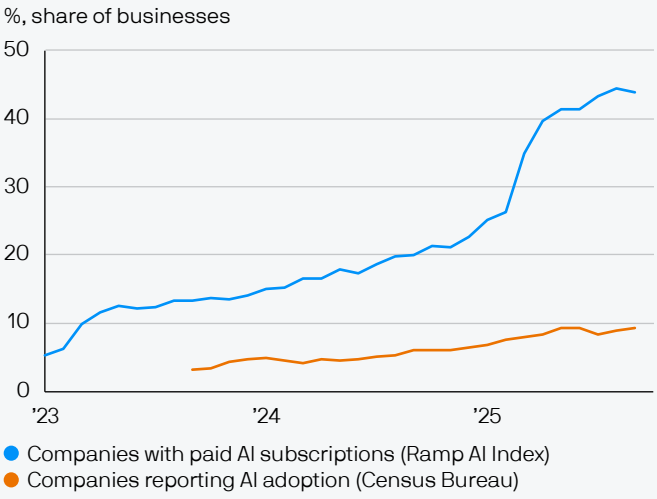
US businesses using AI to produce goods and services by size



Source: Census Bureau, J.P. Morgan Asset Management. Data as of 31 October 2025.

Exhibit 14: Invoicing data paints a prettier picture of AI adoption

Measures of AI adoption



Source: Census Bureau, Ramp AI Index, J.P. Morgan Asset Management. Data as of 31 October 2025.

Triggers for a turn in sentiment

We now focus our attention on identifying potential triggers that could lead market positivity around the AI theme to reverse.

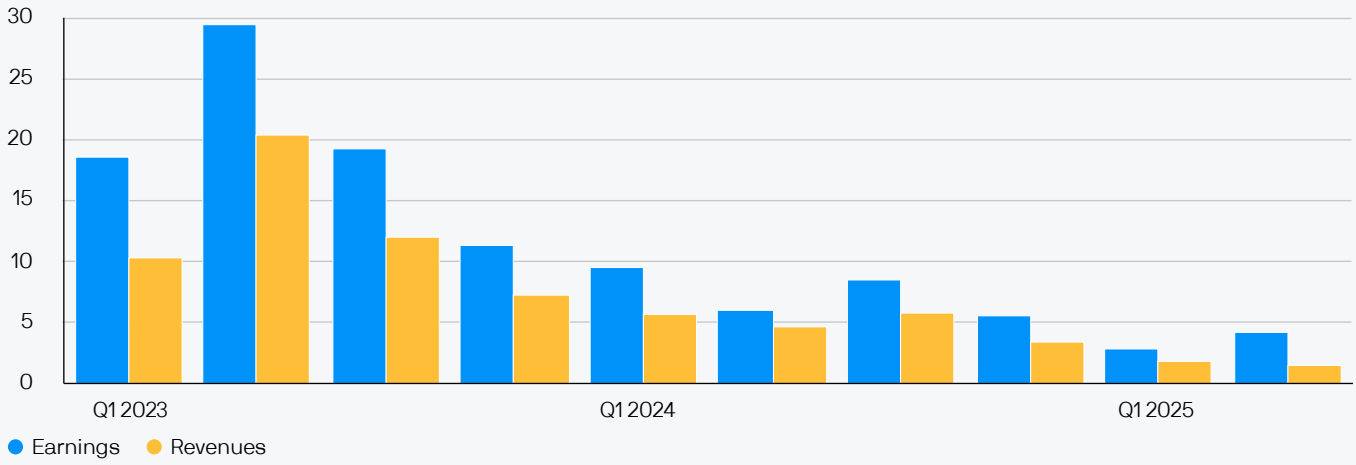
A high-profile misstep

Given the increasing number of interlinkages within the AI ecosystem, one high-profile 'flop' could be very damaging for the broader universe. Earnings reports are the most obvious place to look. Nvidia, for example, beat both earnings and revenue expectations in every quarter from Q1 2023 to Q2 2025. The size of the beats has been diminishing as expectations ramp up, and we should also consider that the pace of capex growth from the hyperscalers is set to slow (see **Exhibits 15** and **16**). A big miss from any of the AI megacaps would likely create significant concern about firms across the industry. Another example would be if OpenAI pressed ahead with IPO plans in 2026 and subsequently faced difficulties in achieving its desired valuation.

Exhibit 15: Big beats are becoming harder to come by as expectations rise

Nvidia quarterly revenue and earnings growth beats

% point difference vs. consensus

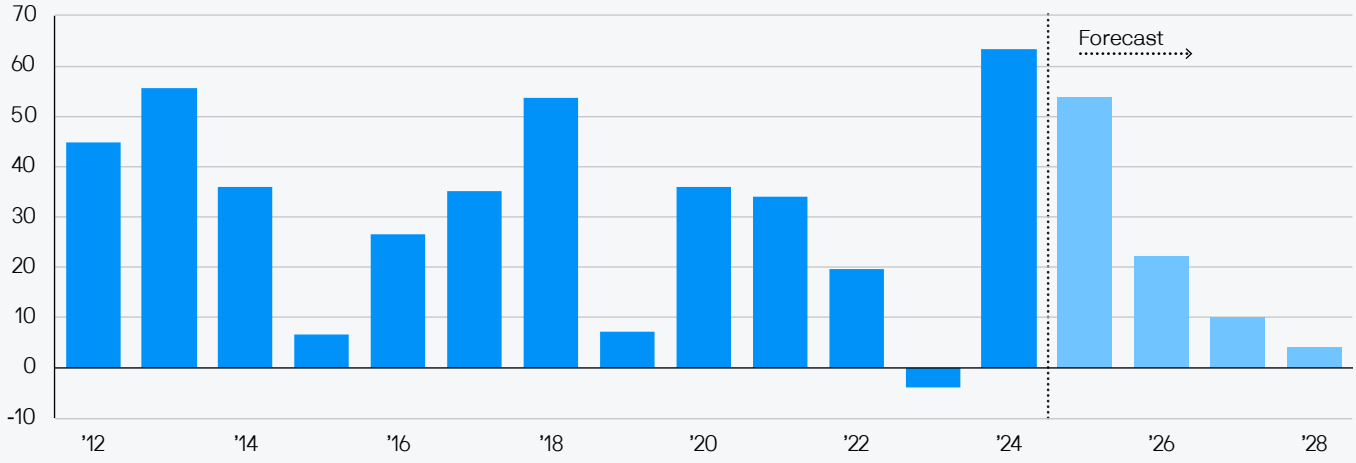


Source: LSEG Datastream, J.P. Morgan Asset Management. Data as of 31 October 2025.

Exhibit 16: Hyperscaler capex growth is set to slow

Capex growth from the five major US AI hyperscalers

% change year on year



Source: Bloomberg, J.P. Morgan Asset Management. The chart shows the annual growth in total company capex for Alphabet, Meta, Microsoft and Oracle, as well as an estimate of Amazon's AWS spend. Data as of 31 October 2025.

Capacity constraints

Whether the provision of energy and raw materials can keep up with the demand for future compute capacity is a question that has so far received far less market attention, but is another crucial one. News reports of electricity blackouts linked to data centre expansion, or a shortage of critical minerals that are essential to chip manufacturing, are both examples of issues that could potentially shift sentiment.

A liquidity event

We must also consider that an external shock, independent of technology, could be the catalyst for a correction. With valuations elevated, technology is increasingly trading as a 'high beta' theme, outperforming in rising markets and underperforming when markets fall. If our tail risk scenario of an inflation shock that triggers higher bond yields plays out, we would expect AI-related stocks to be hit particularly hard.

How to position

With AI sentiment such a dominant driver of markets today, clearly investors do not have the luxury of waiting to see how demand develops before taking a view. Typically, when faced with unpredictable outcomes, diversification is a shrewd approach. For AI unpredictability, we see three specific ways to boost diversification.

1. **Diversify across the ecosystem**: The risks and opportunities facing AI-related companies can vary substantially. If, for example, hyperscalers overestimate the future demand for compute, this overinvestment could lead to downward pressure on prices, hurting hyperscaler margins while benefitting the consumers of this compute capacity. We may also find that there are winners and losers within each AI bucket. In the hardware bucket, for example, time will tell whether the AI ecosystem can sustain multiple chip manufacturers, or whether Nvidia, Broadcom and AMD (among others) are ultimately facing a 'winner takes all' scenario.
2. **Diversify regionally**: The particular exposure of US indices to the AI theme makes a strong case for regional diversification, as we lay out in Diversify selectively across global equities. First, we may find that the ultimate winners of the AI race are situated in other parts of the world, most notably Asia. Second, if the market's attention shifts from AI producers to AI users, Europe's sector mix could benefit. Alternatively, if AI sentiment turns altogether, the low exposure to technology of markets like the UK and Switzerland suddenly looks more appealing.
3. **Diversify across public and private markets**: History provides many examples of those responsible for the build out of a new technology later being ousted by more dynamic, younger start-ups. If value creation is ultimately more focused in the developers of the tools that can harness AI, rather than the infrastructure providers, the long-term winners could well still be lurking in the private markets today. This is one of the reasons we are structurally positive on private equity – see Don't be fearful of private markets.

Conclusion

The earnings of the tech giants have been incredibly impressive, but the outlook for future AI demand remains highly uncertain and, in turn, it is highly uncertain whether high expectations will be fulfilled. Moreover, navigating the timing of when we could encounter such disappointments is even harder. For these reasons we would warn against positioning portfolios strongly in either direction. Diversification across the AI ecosystem, across regions, and across public and private markets should provide the best risk/reward, helping investors manage whichever twists and turns this latest technology revolution throws at us.

Diversify selectively across global equities

With policymakers globally adding fuel to the economic engine, we are positive about a broadening of global growth. This economic outlook should support equity markets outside the US. Investors should therefore ensure their portfolios are not overly concentrated in US tech (see Navigate tech concentration carefully), even if the US rally could successfully extend into 2026.

Importantly, regional diversification does not just mitigate risk; it can also be return enhancing. Of course, diversification will help hedge portfolios against the risk of a retrenchment in sentiment towards artificial intelligence (AI) and subsequent market correction. But diversification can also boost returns in a world where the AI rally continues, as we've seen in 2025 (see **Exhibit 17**).

In 2026, the focus should be on markets with improving fundamentals, and to some degree those less correlated with AI sentiment. Returns will likely be increasingly driven by earnings rather than by multiple expansion, given equity valuations are elevated in many regions (see **Exhibit 18**). Investors must also weigh the impact that currency moves might have on returns.

European equities: Earnings improvement

European equities had a strong start to 2025, fuelled by a large valuation gap with the US, under-positioning in Europe, and a sharp shift in Germany's fiscal policy. But disappointing earnings have caused performance to stall since June.

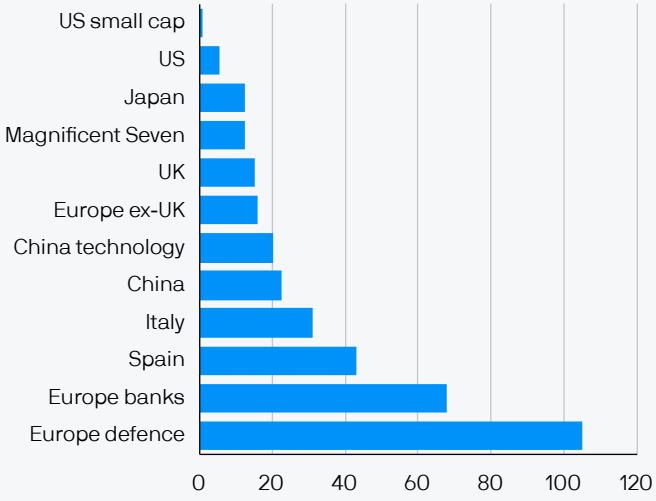
After seven months of negative revisions to earnings per share (EPS) forecasts, Europe's 2026 EPS estimate is now being revised up and bottom-up forecasts point to growth of 12% year on year. Mid-single digit growth seems more realistic to us, consistent with the typical pace of downgrades to consensus EPS expectations.

The first driver of positive profit growth is a likely slowing or stalling of euro appreciation in 2026, which should offer relief to European companies given they generate about half their revenues internationally. The euro has appreciated meaningfully versus the US dollar in 2025, driven more by dollar weakness than by stronger European growth prospects. This has contributed to the 17% downward revision in 2025 EPS estimates for European exporting sectors, versus a 1% upward revision for domestic sectors (see **Exhibit 19**).

Exhibit 17: Regional diversification has paid off in 2025

Total returns year to date

% total return in EUR

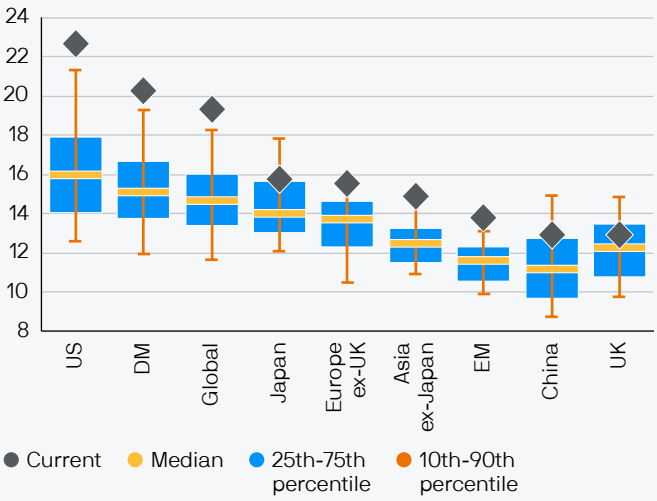


Source: BME, FTSE, LSEG Datastream, MSCI, Russell, S&P Global, STOXX, Tokyo Stock Exchange, J.P. Morgan Asset Management. China, China technology and Europe ex-UK are MSCI. Europe banks: STOXX 600 Banks; Europe defence: basket of selected European defence stocks; Italy: FTSE MIB; Japan: TOPIX; Spain: IBEX; UK: FTSE 100; US: S&P 500; US small cap: Russell 2000. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Exhibit 18: Equity valuations are elevated across most markets

12-month forward P/E ratios

x, multiple



Source: FTSE, IBES, LSEG Datastream, MSCI, S&P Global, Tokyo Stock Exchange, J.P. Morgan Asset Management. Asia ex-Japan, China, DM, EM, Europe ex-UK and Global are MSCI. Japan: TOPIX; UK: FTSE 100; US: S&P 500. Valuation is price to 12-month forward earnings, as published by IBES. Range and median calculated over last 20 years. Data as of 31 October 2025.

Second, more stable energy prices should also support European profits, given the weight of commodity-related sectors in index earnings. European commodity sectors have seen their 2025 EPS estimates revised down 27% this year as oil prices have fallen. In 2026, EPS growth for the energy and materials sectors is forecast to rebound to 7% and 31% respectively, and revisions have recently turned positive.

It is not just the removal of headwinds that should return European earnings to growth. The European economy could also surprise to the upside. Eurozone GDP growth expectations are already on an upward trajectory, and fiscal policy should provide a further boost, especially in Germany where we expect growth to pick up from zero to well above potential (see Monetary and fiscal fuel is powering expansion).

Still 'less expensive', if not outright cheap

European valuations remain attractive relative to US equities and other assets. The MSCI Europe ex-UK Index is the only major equity index with a 12-month forward P/E ratio currently below its start-2022 level (see **Exhibit 20**). European multiples are currently 35% lower than in the US, close to all-time wides. Yet the earnings growth gap between the two regions is narrowing. After the global financial crisis, US earnings have grown on average 8 percentage points faster than European earnings (annualised), but this gap is expected to shrink to 2 percentage points from 2025 to 2027. Thus, on current consensus forecasts, investors can pay a multiple of 16x forward earnings in Europe (ex-UK), or 23x in the US, for relatively similar future earnings streams.

Stay selective

While we are broadly positive on Europe, we nonetheless recommend investors are selective, focusing on three main areas: banks, fiscal beneficiaries, and the GRANOLAS.[1]

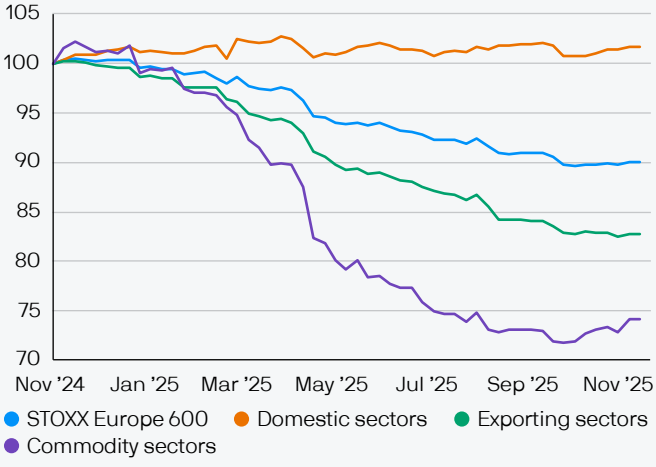
First, **European banks** are attractive. Despite returning nearly 200% including dividends since the start of 2022, we believe the sector still has tailwinds. European banks trade at a reasonable price-to-book ratio of 1.1x, well below their pre-global financial crisis average, and offer a robust shareholder yield (buybacks plus dividends) of 8%. Profit growth has been more than double that of the broad index since 2019, and revisions to consensus 2026 EPS forecasts show continued strength. Stronger nominal growth and steeper yield curves than in the 2010s should further support bank earnings.

[1] GSK, Roche, ASML, Nestle, Novartis, Novo Nordisk, L'Oréal, LVMH, AstraZeneca, SAP and Sanofi.

Exhibit 19: Exporters and commodities were a major drag on 2025 earnings

2025 earnings estimates

Index level, rebased to 100 on 31 October 2024

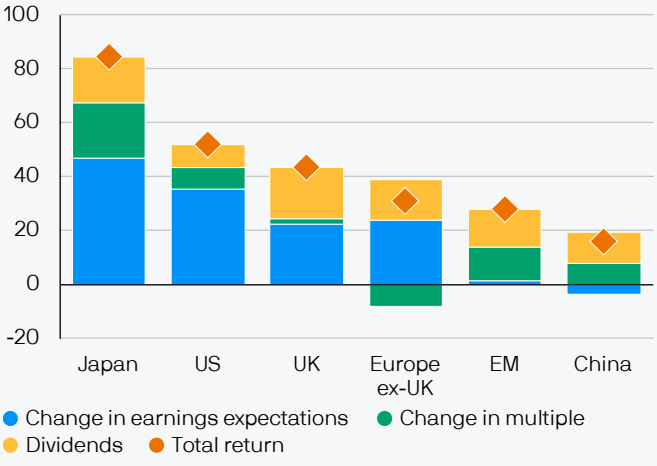


Source: IBES, LSEG Datastream, STOXX, J.P. Morgan Asset Management. Domestic sectors are those with more than 50% of revenues generated within Europe. Exporting sectors are those with less than 50% of revenues generated within Europe. Data as of 31 October 2025.

Exhibit 20: Europe is rare in seeing no valuation expansion since 2022

Return decomposition since start-2022

%, sources of total return in local currency



Source: FTSE, IBES, LSEG Datastream, MSCI, S&P Global, Tokyo Stock Exchange, J.P. Morgan Asset Management. China, EM and Europe ex-UK are MSCI. Japan: TOPIX; UK: FTSE 100; US: S&P 500. Returns are shown in local currency (Europe ex-UK in EUR), with the exception of EM which is in US dollars. Multiple is price to 12-month forward earnings and earnings expectations are 12-month forward, as published by IBES. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

> Europe's defence firms are expected to grow their earnings much faster than their US peers over the next few years. When compared to the recent growth in military spending, recent valuation expansion appears more reasonable.

Second, **fiscal beneficiaries** look set to do well. The European Union plans to release significant funds over the coming years for defence, power security and infrastructure. Companies in these sectors have surged: a basket of European defence names is up over 100% year to date, and capital goods firms involved in AI infrastructure and utilities have also gained strongly. We believe this rally has further to run, as in our view investors are still sceptical about the delivery of European spending. Europe's defence firms are expected to grow their earnings much faster than their US peers over the next few years. When compared to the growth in military spending, recent valuation expansion appears more reasonable.

Third, the **GRANOLAS** are attractive laggards. These firms, which represent Europe's 11 largest stocks across the healthcare, staples, tech and luxury sectors, have underperformed since early 2022 as yields rose sharply, the euro strengthened, and growth in China slowed. Now on a 19x forward P/E ratio, the GRANOLAS trade at a discount to the S&P 500 and at a smaller premium to the rest of Europe than in recent years. They offer a hedge against shifts in AI sentiment, as their correlation with the Magnificent Seven is low. Some sector-specific factors may also improve. European luxury companies, which have underperformed by c.25% since the start of 2023, could benefit from a pickup in Chinese demand as an equity rally and housing market recovery help stabilise household wealth.

China: The AI investment case at a more reasonable price

We are modestly positive on China. While the Chinese market has rallied nearly 80% since its low in early 2024, we believe that the bull market can continue, albeit at a more moderate pace, driven by both earnings and valuations.

Focus on tech and exporters

The fundamental backdrop is improving for Chinese equities, powered by the tech sector. Consensus forecasts expect MSCI China EPS growth to pick up from 2% in 2025 to 15% in 2026, and maintain this strength in 2027, well above last decade's average of 10%. **Technology firms** are key drivers of this profit growth: consensus 2026 EPS forecasts for China's tech sector have been revised up 4% this year, and annualised earnings growth over the next two years is expected to be over 30%. Chinese tech stocks trade on lower multiples than their US counterparts (25x vs. 31x forward earnings) yet are expected to deliver stronger earnings growth.

Chinese tech firms are also well positioned to take advantage of future AI development. In a recent survey, 93% of Chinese participants reported using AI intentionally at work in 2024, compared to 67% in the US.[2] Data centre capacity is expected to grow faster in China than in the US over the next few years (see **Exhibit 21**). We suspect there will be fewer regulatory frictions slowing broad AI integration in China than in other countries, which may take a more considered but therefore slower approach.

Chinese tech firms also benefit from state support, with the government's latest five-year plan highlighting technology as an area of focus. State support has previously helped Chinese industries such as electric vehicles (EVs) develop astonishing economies of scale which international competitors have been unable to match. Chinese EVs now make up nearly two-thirds of global sales (see **Exhibit 22**), and China's share of European EV sales sits six times higher than in 2020.

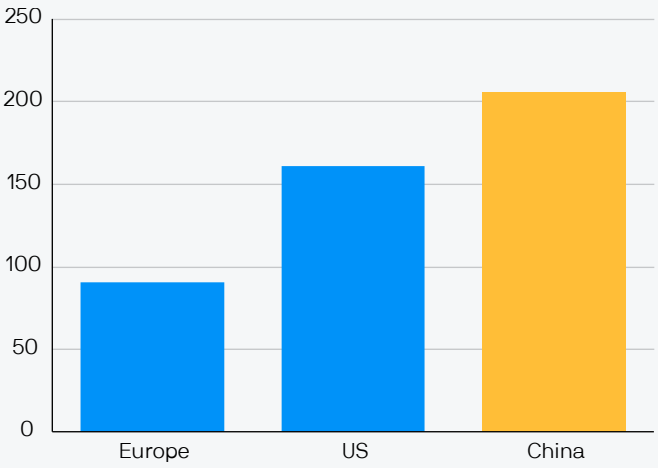
Beyond tech, we are positive on **Chinese exporters** more broadly. The Chinese government continues to provide stimulus to its favoured industries, many of which are export-oriented such as solar module manufacturing. Efforts to reduce excessive competition ('anti-involution') may lead to consolidation in high-competition sectors such as EVs, supporting larger companies' net income margins.

[2] Gillespie, N., Lockey, S., Ward, T., Macdade, A., & Hassed, G. (2025). *Trust, Attitudes and Use of Artificial Intelligence: A Global Study 2025*. The University of Melbourne and KPMG.

Exhibit 21: China is expected to build data centres at pace

Forecast growth in tech data centre installed capacity

%, 2024 to 2030e

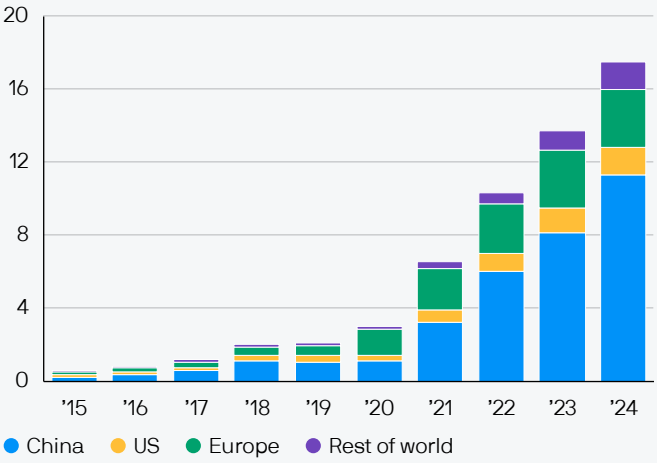


Source: IEA, J.P. Morgan Asset Management. Data as of 31 October 2025.

Exhibit 22: Beijing's industrial policy often has global implications

Global EV sales

Millions



Source: IEA, J.P. Morgan Asset Management. Data as of 31 October 2025.

Chinese exporters have also demonstrated their ability to reroute their goods despite global trade headwinds. China's exports have grown strongly in 2025, with losses in the US more than offset by gains elsewhere, particularly to emerging markets (see **Exhibit 5** in Monetary and fiscal fuel is powering expansion). China also holds a dominant position in global supply chains for rare earth metals, solar modules, lithium batteries and EVs. Thus, export sectors are expected to drive MSCI China's profit growth in 2026, with consensus EPS growth for the technology and autos sectors sitting at near 40% and over 80% respectively.

Two key risks to our view on Chinese equities are AI sentiment and Chinese regulation. If sentiment towards AI weakens, Chinese tech firms could suffer due to their correlation with US tech stocks. And any regulatory shift from Chinese policymakers, similar to late 2021, could derail the China rally, though this is not our base case.

> Importantly, regional diversification does not just mitigate risk; it can also be return enhancing.

Other emerging markets: Export rerouting a headwind

Chinese resilience could come at the expense of other emerging markets (EM): a sustained rise in Chinese exports to other nations would weigh on EM ex-China profits. To become more positive, we would need to see stronger earnings growth in the financial and commodities sectors. However, with EM central banks generally easing policy rates, banks are unlikely to drive profits, and commodity prices are expected to remain stable but low.

One exception to this view is North Asia – South Korea, Taiwan and Hong Kong. These markets tend to perform well when the Federal Reserve is cutting rates, due to their cyclical nature and concentration in long-duration sectors, such as technology, capital goods and healthcare.

Japan equities: Ride reflation, be aware of currency risk

We also see opportunities in Japanese equities. An improving domestic political environment, continued corporate reform, strong earnings momentum (see **Exhibit 23**), and room for valuation expansion should support the Japanese market. However, investors should remain alert to how yen moves could affect returns.

Policy and fundamentals supportive

The election of Sanae Takaichi as prime minister on 21 October extends the relatively supportive political backdrop in Japan. The new prime minister's pro-growth stance, plus her focus on US-Japan cooperation and national security, was taken positively by markets. Since her election, expectations of hikes from the Bank of Japan (BoJ) have been pushed out.

As in Europe, in our view Japanese equity valuations still have room to expand. While current valuations may seem high compared to the past 20 years, this period includes the aftermath of the asset price bubble, which depressed multiples. Looking at a broader timeframe, the TOPIX's forward P/E ratio of 15.8x is well below its average since 1990 (24x), and still below its Abenomics peak of 16.3x. Rising bond yields are also benefiting earnings in the financial sector, which makes up about 15% of the TOPIX.

Favour defence and banks, watch the yen

Within Japanese equities, we favour **defence-related stocks**, which are set to benefit from increased global military spending and the new prime minister's hawkish foreign policy stance. Japanese defence-related stocks trade on 20x 12-month forward earnings, compared to 22x for a US defence basket.

We also see strong potential for **Japanese banks**. Japanese banks have outperformed the TOPIX since 2021, aided by reflation, but still trade at a price-to-book ratio of just 1x. Although Takaichi is encouraging the BoJ to keep interest rates low, the bank's next move is still likely a hike, which would support financial sector margins. Earnings revisions for Japanese financials have been very positive, surpassing those of their US peers.

The key risk for Japanese equities remains the yen. Given 40% of TOPIX revenues come from overseas, Japanese equity performance is typically negatively correlated with the yen (see **Exhibit 24**). For European investors, what is lost via yen moves is often gained on the equity market, and vice versa.

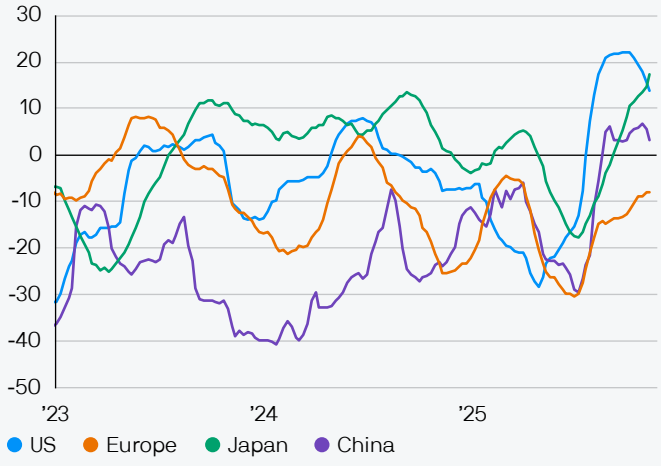
Conclusion

We believe diversifying equity portfolios regionally can both enhance returns and protect against concentration risks, particularly if AI sentiment turns less positive. Outside the US, we see the strongest opportunities in select areas of the European, Japanese and Chinese markets with fundamental tailwinds, including European and Japanese banks, Chinese tech and exporters, defence names, and fiscal beneficiaries.

Exhibit 23: Earnings revisions have been strong in Japan

Earnings revision ratios

%, 13-week ratio of earnings estimate upgrades to downgrades

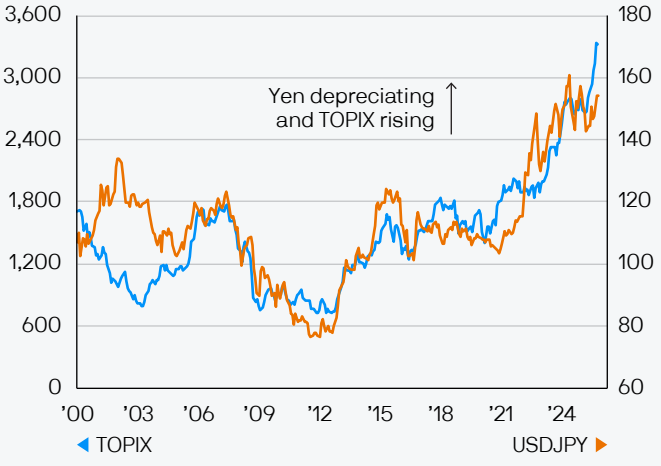


Source: LSEG Datastream, MSCI, S&P Global, STOXX, Tokyo Stock Exchange, J.P. Morgan Asset Management. China: MSCI China; Europe: STOXX 600; Japan: TOPIX; US: S&P 500. Earnings revision ratios are based on 12-month forward earnings expectations, as published by IBES. Data as of 31 October 2025.

Exhibit 24: Japanese equity performance has typically been negatively correlated with the yen

TOPIX and the yen vs. US dollar

Index level (LHS); JPY per USD (RHS)



Source: LSEG Datastream, Tokyo Stock Exchange, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Don't be fearful of private markets

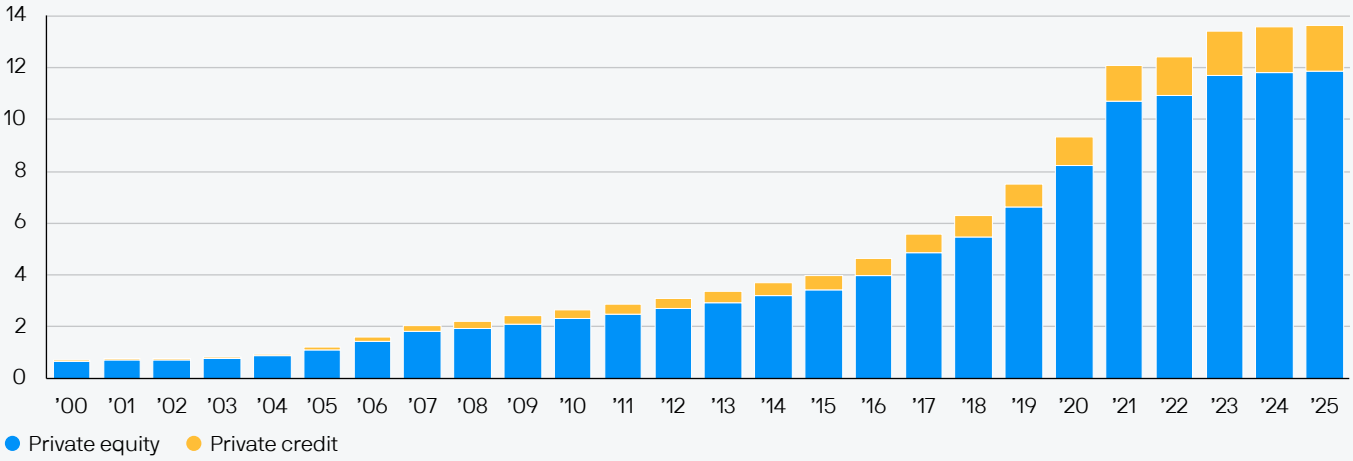
Private markets have grown rapidly over the past decade. Private market assets under management have grown five-fold since 2010, reaching over $13 trillion globally (see **Exhibit 25**). This expansion of private capital, which is more opaque than public market capital, has prompted concern that problems may be lingering in the shadows of the financial system.

Rapid growth in a financial asset class should attract scrutiny. But interpreting these developments purely through the lens of 'excess' misses a key part of the private market story, which is that over the past two decades, the nature of corporate financing has changed profoundly.

> **Put simply, where growth once happened after initial public offering, it now happens beforehand.**

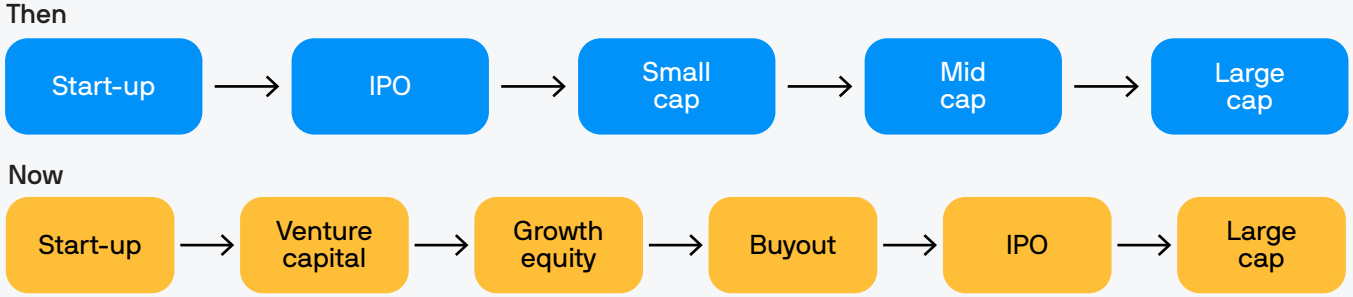
Where companies once depended on public markets for capital to grow, they can now access vast pools of private money through venture capital and private equity. As a result, a larger part of the pathway to maturity for businesses has shifted from the public to the private domain (see **Exhibit 26**). What looks like exuberance is, in many respects, the reflection of a new normal in corporate finance.

Exhibit 25: Private markets have grown rapidly
Global private markets assets under management
USD trillions



Source: Preqin, J.P. Morgan Asset Management. Assets under management are the sum of unrealised value and dry powder. 2025 data is as of Q1 2025. Data as of 31 October 2025.

Exhibit 26: From public to private: How the capital raising model evolved
Stylised journey from start-up to large cap public company



Source: J.P. Morgan Asset Management, as of November 2025.

The rise of private markets

To understand the rise of private markets, it helps to remember how companies used to grow. Two decades ago, a business would typically raise early-stage funds from private investors, go public relatively quickly, and then continue to scale through the public markets. Amazon, Apple and Google – three of the Magnificent Seven – all listed within five years of being founded, creating trillions of dollars in value for public market investors over the decades that followed.

Today, that growth sequence has migrated to the private markets. Companies now stay private for longer and reach far larger scale before listing – if they list at all. In the late 1990s, the median age of a company at its initial public offering (IPO) in the US was around five and a half years. In 2024, that had risen to 14 years. In 1996, there were over 8,000 publicly listed companies in the US; today, there are fewer than 6,000. Over the last decade alone, the number of private 'unicorns' – venture capital-backed start-ups valued at over $1 billion – has increased eight-fold.

This trend towards listing publicly much later has been made possible by the growth of capital available in private markets. The venture capital and growth equity markets have grown as technology, healthcare and consumer innovations have created new investable opportunities. 'Buyout' funds have expanded, to allow companies in venture capital or growth equity portfolios to be sold multiple times while remaining private. Together, these areas of the private markets now provide the financing that small- and mid-cap public markets once supplied. Put simply, where growth once happened after a firm's IPO, it now happens beforehand.

Why companies choose to stay private

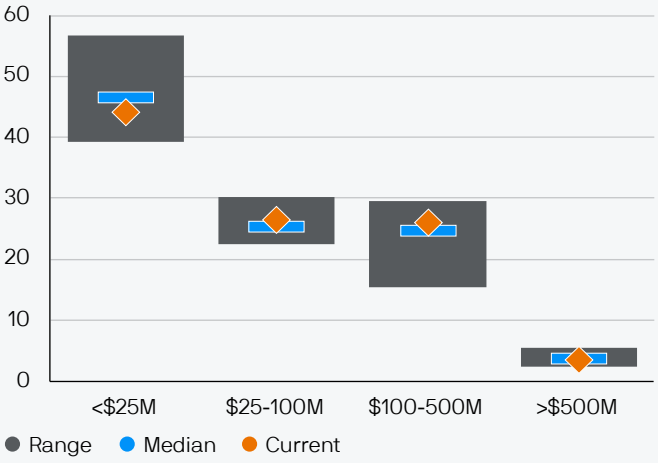
The shift to private markets is not primarily about companies being unable to go public. It is more about firms choosing not to. Listing on a public exchange can offer liquidity and visibility, but it also brings a higher regulatory burden, greater scrutiny via quarterly reports, and the share price volatility that comes with public markets. For fast-growing companies, staying private can provide more flexibility and allow longer-term decision making without the pressure of the quarterly reporting cycle.

Meanwhile, institutional investors – pension funds, insurers, endowments and sovereign wealth funds – have actively sought out private assets to enhance their returns. That influx of capital has created a self-reinforcing ecosystem. More capital leads to larger private market deals; larger deals enable companies to remain private for longer; and the resulting private market expansion attracts yet more capital. It is this structural migration of capital that explains much of the growth in private markets.

Exhibit 27: The majority of private equity activity is still in small to medium-sized companies

US private equity investments by size

%, annual share of total investments, 2008-2025



Source: LCD, Pitchbook, J.P. Morgan Asset Management. 2025 data is as of Q2 2025. Data as of 31 October 2025.

> Private equity valuations are high, competition for deals remains intense, and the growing links between private equity and private credit mean that stress in one corner of the market can affect another. But these are risks to monitor, not evidence of excess.

Where the growth really happens: Small and mid-market activity

A common misconception is that private equity is primarily about very large buyouts – the kind of multi-billion-dollar transactions that make headlines. The reality is very different, with most of the deal activity taking place in the small and mid-market areas, where enterprise values (a company's market cap plus its outstanding debt) are typically below $500 million (see **Exhibit 27**).

In this part of the private equity market, creating value is less about financial engineering and more about improving company operations. Firms benefit from access to well-established and experienced private equity managers that help improve and expand their product offerings, reduce costs, and reach greater scale by entering new geographies.

Private credit: The other half of the story

The expansion of private credit[1] is due to many of the same forces that have reshaped private equity. Greater regulation after the global financial crisis led banks to retrench from lending markets. This opened the door for non-bank lenders to fill the gap in corporate financing, particularly in the small and mid-market where banks once dominated. Over time, such direct lenders have become an essential source of capital across company's lifecycles.

Much of the capital raised in private credit markets today is lent to private equity-backed companies, effectively providing the private debt counterpart to private equity capital. Private credit allows companies to refinance loans, change the mix of their financing, and expand without turning to public markets. For investors, private credit offers an attractive yield pickup over public credit in exchange for providing patient, long-term capital.

Private credit serves two different purposes within private markets. First, it provides growth financing – loans to companies looking to expand, invest or refinance. Second, private credit can help finance buyouts – that is, it can supply loans to finance private equity groups acquiring a company. Today, around 90% of US mid-market buyouts are financed by private credit, up from around 50% in 2017. It's this latter trend – the financing of private equity buyouts through private credit – that has drawn recent scrutiny.

Where the risks lie

Our view is that the growth of both private equity and private credit has occurred thanks to structural changes in the nature of corporate financing. This is not to suggest that private markets are without risk. Private equity valuations are high, competition for deals remains intense, and the growing links between private equity and private credit mean that stress in one corner of the market may spread into another. However, in our view these remain risks to monitor, rather than evidence of excess.

Starting with valuations, global buyout multiples (EV/EBITDA)[2] for mid-market companies are below their 2021 peak but still above long-term averages (see **Exhibit 28**), at around 13x. That implies less room for multiple expansion to drive private equity returns, making returns more dependent on rising earnings growth and operational improvements. Yet relative to public markets, private market valuations are not out of line: the median EV/EBITDA multiple for the S&P 500 last year was approximately 14x. In other words, private equity valuations are high, but nonetheless in line with public market comparators.

The rise of private equity 'continuation vehicles' has also been cited as a cause for concern about private markets, given their rising share of global private equity exits (see **Exhibit 29**). A continuation vehicle is a new fund set up by a private equity manager to hold on to one or more portfolio companies beyond the life of the original fund. Sceptics argue that the increasing use of continuation vehicles reflects managers trying to hide problems with portfolio companies, problems preventing those companies being sold on at the private equity manager's desired valuation.

Again, we think this scepticism about continuation vehicles misses the point. While continuation vehicles do allow private equity managers to hold assets for longer, to avoid selling in a depressed market, they do not simply represent managers 'selling assets to themselves'. In almost all cases, a continuation vehicle transaction requires an independent secondary buyer to validate the valuation and commit new capital. These secondary buyers are typically sophisticated institutional investors or dedicated secondary funds, who will conduct full due diligence on a portfolio company before agreeing to get involved.

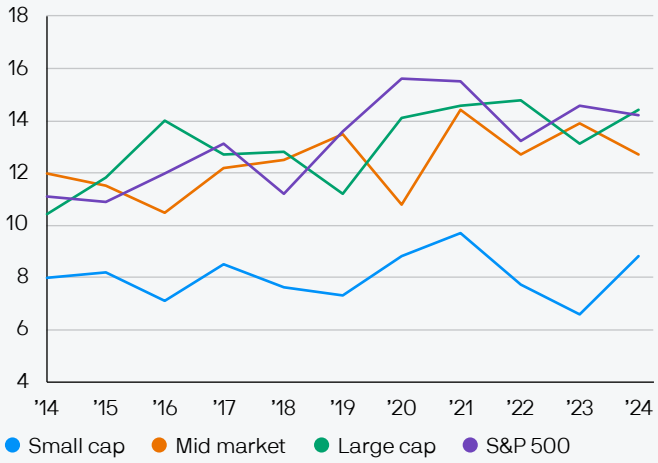
[1] Private credit is a broad asset class that can encompass several types of non-bank lending. Here, unless otherwise specified 'private credit' refers to direct lending, where lenders other than banks make loans to companies without intermediaries – the largest component of the broader 'private credit' asset class.

[2] The ratio of a firm's enterprise value (EV, a company's market cap plus its outstanding debt) to its EBITDA (earnings before interest, tax, depreciation and amortisation).

Exhibit 28: Valuations in private markets don't look out of kilter with public markets

Private company buyout multiples vs. S&P 500

x, median EV/EBITDA ratio, trailing 12-month multiple

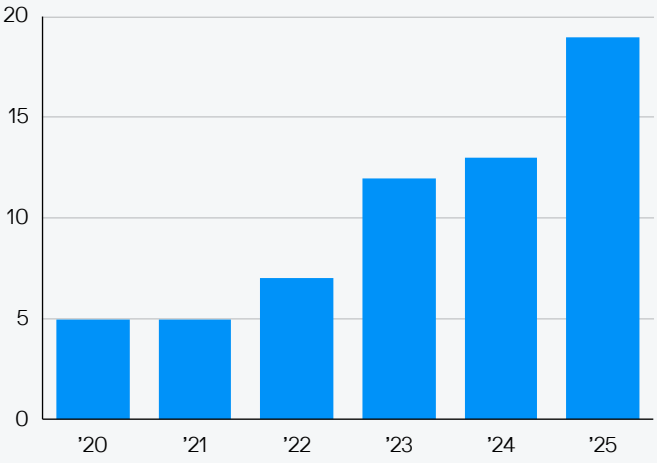


Source: LCD, Pitchbook, S&P Global, J.P. Morgan Asset Management. EV/EBITDA is the ratio of enterprise value to earnings before interest, taxes, depreciation and amortisation. Data as of 31 October 2025.

Exhibit 29: PE companies using continuation vehicles isn't necessarily cause for concern

Continuation vehicles as a share of global PE exit activity

%



Source: Dealogic, Jefferies, J.P. Morgan Asset Management. 2025 is as of H1 2025. Sponsor-backed exit deal volume estimates are from Dealogic and include M&A and IPO proceeds. Percentage represents continuation vehicle transaction volume divided by sponsor-backed exit deal volume. Data as of 31 October 2025.

Most recent secondary (continuation) deals have been priced at small, single-digit discounts to the company's net asset value, well within typical valuation ranges. During a period when IPO and merger and acquisition activity in public markets has been slow, continuation vehicles have offered liquidity and price discovery in the private markets, giving private investors options. Again, we think the rise of private equity continuation vehicles simply represents another example of how the system of corporate financing is developing.

The growing interconnectedness of private equity and private credit is another area of debate. It is true that private equity and private credit are increasingly intertwined, with private credit often financing private equity buyouts, or supporting private equity portfolio companies with refinancing.

However, private credit investors are receiving a good fee for these services. There are high starting yields on offer in private credit markets, often in the low double digits for senior (highest priority for repayment) direct lending. This provides a meaningful buffer against potential losses. Even if default rates were to rise modestly, historically strong recovery rates would help offset much of the downside. It would take a severe and prolonged deterioration in private equity portfolio companies to generate material losses within private credit.

Conclusion

All told, we remain constructive on private equity and private credit.

In private equity, falling US interest rates will make borrowing cheaper, helping boost returns and supporting current valuations. The small and mid-market segments of the private equity market, along with secondaries (continuation vehicles), still offer investors attractive ways to access the artificial intelligence theme at more reasonable valuations, potentially at discounts to net asset value. In Europe, more fragmented financing markets and less strident competition to lend make private markets a compelling source of potential alpha. European private markets' relatively higher weight to technology than public equity indices is also attractive.

In private credit, declining US interest rates will ease debt servicing costs, helping mitigate some default risk even as this gradually compresses headline yields. As always, investors should diversify across managers and vintages (the year a loan or fund was originated) to help reduce concentration and idiosyncratic risk. Within private credit, combining direct lending with exposure to infrastructure and real estate debt can broaden investors' sources of return, while allocations to opportunistic or distressed debt funds may prove valuable if a material economic slowdown results in market stress.

Protect against derailment

As we lay out in Monetary and fiscal fuel is powering expansion, unprecedented 'peacetime' stimulus is supporting both the economy and risk assets. Investors face two key risks should all this excess create problems: a major shift in artificial intelligence (AI) sentiment, and the resurgence of inflation. In this chapter, we examine the strategies available to investors who wish to mitigate against these risks.

What if it is a bubble?

As discussed in Navigate tech concentration carefully, we simply don't know at this stage what the end demand for AI will be and whether the large-cap tech companies will be able to sustain the supernormal profits that the market expects. Investors who are concerned that these highly valued companies may not meet long-term growth expectations have two main hedging options.

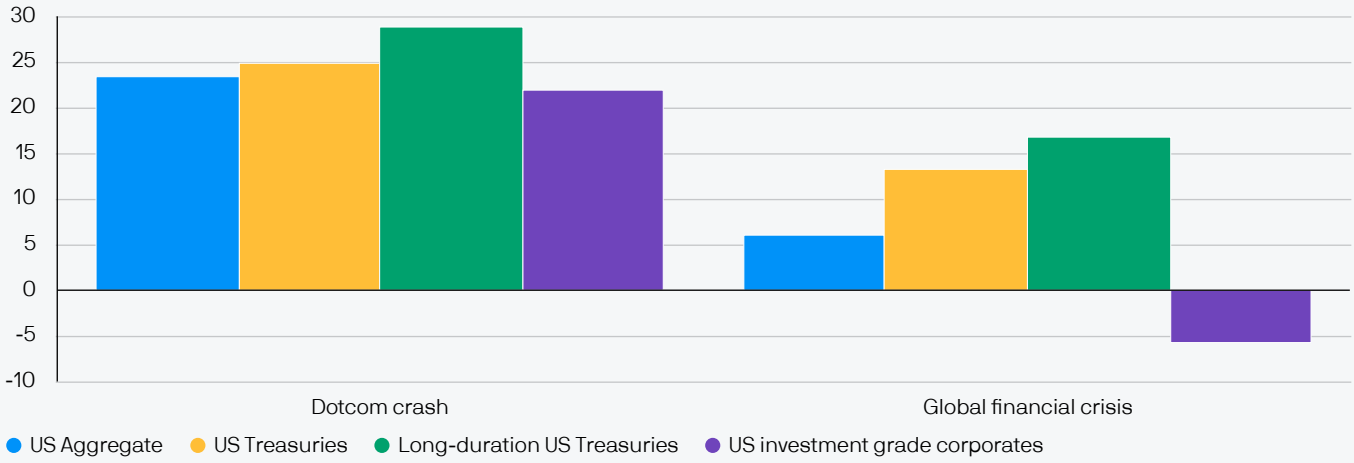
High-quality, long-duration bonds should provide a substantial buffer in the event of a tech and AI-driven crisis, which would be deeply disinflationary. If demand for AI infrastructure is overestimated and the return on this investment disappoints, we could see overcapacity, falling prices, shrinking margins, and lower investment, echoing the early 2000s. Stock prices would fall, driving negative wealth effects, and consumer spending would contract. Private markets would also be affected, as 36% of private equity and 25% of private credit are exposed to tech.

Such a scenario could push the US economy towards recession, prompting the Federal Reserve (Fed) to cut rates sharply. During the dotcom bubble and the global financial crisis, long-dated US Treasuries delivered returns of 29% and 17% respectively (see **Exhibit 30**). In the bursting of the tech bubble, high-quality, long-duration corporate bonds also offered protection.

Non-US investors should also consider currency movements. The US dollar typically strengthens during market stress but given the leading role of US firms in the AI story, its safe-haven status is not assured in this scenario. Depending on hedging costs, long-duration local government bonds could be an alternative to US Treasuries, though the return potential from falling yields in the eurozone and the UK is likely lower than in the US.

> **High-quality, long-duration bonds should provide a substantial buffer in the event of a tech and AI-driven crisis.**

Exhibit 30: Bond prices should rise meaningfully in the event of a tech crash
US fixed income returns during equity market sell-offs
%, total return during the period when the S&P 500 was falling



Source: Bloomberg, LSEG Datastream, S&P Global, J.P. Morgan Asset Management. Dotcom crash: Aug '00 to Sep '02; global financial crisis: Oct '07 to Feb '09. US Treasuries: Bloomberg US Aggregate - Treasuries; Long-duration US Treasuries: Bloomberg US Treasury: Long (10+ years); US investment grade corporates: Bloomberg US Aggregate - Corporate. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Investors should also think about the concentration risks within global equities. The tech and communication services sectors now account for 37% of the MSCI All Country World Index.

Simply diversifying outside of tech and tech-related sectors is insufficient. An AI slowdown would have broad economic implications, and valuation risks are widespread. Cyclical sectors offered protection during the dotcom era. However, since 2022, cyclical sector valuations (excluding technology sectors) have expanded from 13x to 22x 12-month forward earnings, leaving these sectors vulnerable if an oversupply of AI infrastructure slows growth.

Defensive sectors, after a period of underperformance, now sit on undemanding valuations. Their earnings are also less tied to tech infrastructure build out and economic activity more generally, making these sectors better insulated from any tech downturn (see **Exhibit 31**). Portfolios with a high share of defensive stocks should therefore prove relatively resilient if AI exuberance fades.

Largesse induced inflation

The second key risk is inflation. Loose fiscal policy is pressuring bond markets with rising supply and deteriorating sovereign creditworthiness. Government consumption can fuel inflation if it coincides with strong private demand or supply shortages. Such inflation could take the form of an acute shock or instead a chronic creep, with different assets best positioned in each scenario.

Acute inflation: Lessons from 2022

As previously discussed, we are wary of the potential for fiscal largesse to trigger a resurgence of inflation. Tax rebates from the One Big Beautiful Bill, and possible further stimulus ahead of the midterms, could stimulate demand-driven price pressures in the US economy. Also, while the current trajectory for trade policy appears more benign, the full inflationary impact of tariffs is yet to be felt, and there remains the risk of further supply-side disruptions from new US tariffs or partner retaliation.

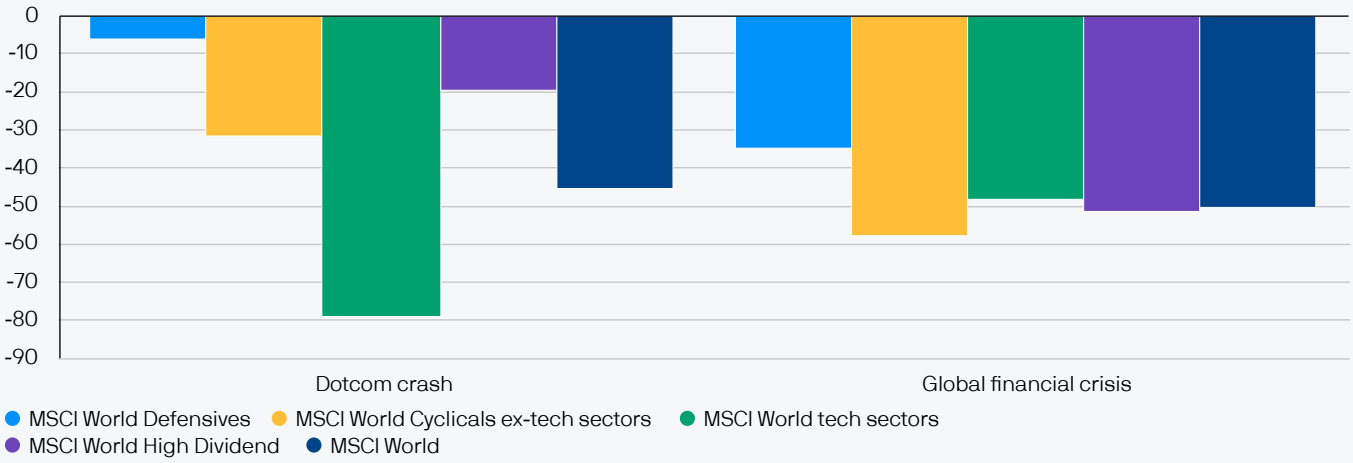
In this scenario, the Fed could be forced to halt its cutting cycle and potentially hike rates to maintain credibility. Rising bond yields would force broad asset repricing, hurting public markets.

Real assets such as timber and core infrastructure would offer the best protection during an acute inflation shock (see **Exhibit 32**). Traditional inflation diversifiers, such as real estate and inflation-linked bonds, struggle as income adjustments lag behind capital losses, while the commodity-heavy FTSE 100 would likely outperform other equity markets.

Exhibit 31: Defensive stocks should also protect in the event of a tech bust

Global sector performance during equity market sell-offs

%, total return in USD during the period when the S&P 500 was falling



Source: LSEG Datastream, MSCI, S&P Global, J.P. Morgan Asset Management. Dotcom crash: Aug '00 to Sep '02; global financial crisis: Oct '07 to Feb'09. Defensives: consumer staples, healthcare and utilities; Cyclicals ex-tech sectors: energy, materials, industrials, consumer discretionary, financials and real estate; tech sectors: information technology and communication services. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Chronic inflation: Erosion of real returns

Inflation could prove less of a short, sharp shock and more of a creeping problem, as each year closes out with yet another modest target miss. Governments were very successful in the 1950s and 1960s at inflating away their debt via a series of small inflation surprises: nominal interest rates below nominal GDP growth slowly shifted the burden of debt away from taxpayers and towards bondholders, whose returns were eaten away by inflation.

With chronic inflation, the risk is therefore a gradual erosion of real returns rather than rapid repricing. Historically, in periods of chronic, creeping inflation real estate outperformed stocks, while inflation-linked bonds outperformed their nominal counterparts (see **Exhibit 33**). Without sharp upfront capital losses, the inflation adjustments inherent in these two assets' income streams can help protect real returns.

Gold is another asset to consider. In chronic inflation scenarios, its store-of-value properties make it an important portfolio diversifier. It also serves as a hedge against concerns around US institutional credibility, or fiat currency risks. If US institutional credibility was called into question, this would likely support demand for gold as international reserve managers diversified away from the dollar.

However, gold's performance as a diversifier against acute inflation shocks is mixed. Average returns are boosted by strong performance in the late 1970s when investors were already hyper-focused on inflation, but returns were negative when inflation spiked in 1990 and 2022 as inflation surprised markets. This mixed performance raises the risk that investors looking to gold for protection against an inflation shock could be disappointed.

Conclusion

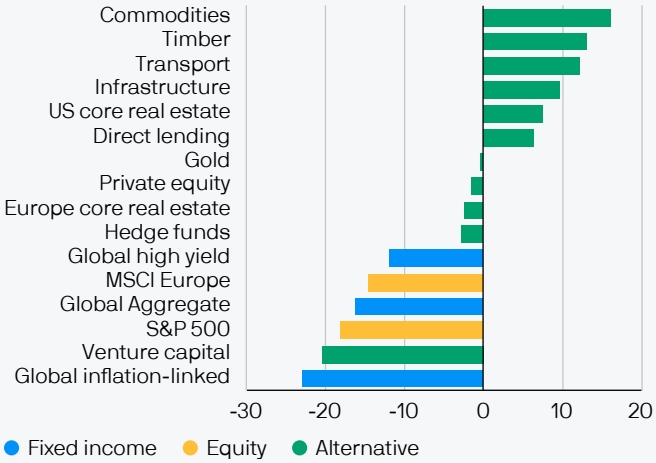
Our base case is that monetary and fiscal fuel continues to power an economic expansion. But there is a risk that policy 'excess' leads to either an asset bubble, or inflation. Investors should think carefully about building up protection against these outcomes.

To protect against a fall in tech stocks, investors should consider high-quality, long-duration bonds and defensive equity sectors. To protect against inflation risk, investors should allocate adequately towards alternative assets, which should support a portfolio whether inflation is acute or chronic.

Exhibit 32: 2022 showed us that protection against inflation shocks is best found in alternatives

Selected public and private market returns in 2022

%, total return in USD

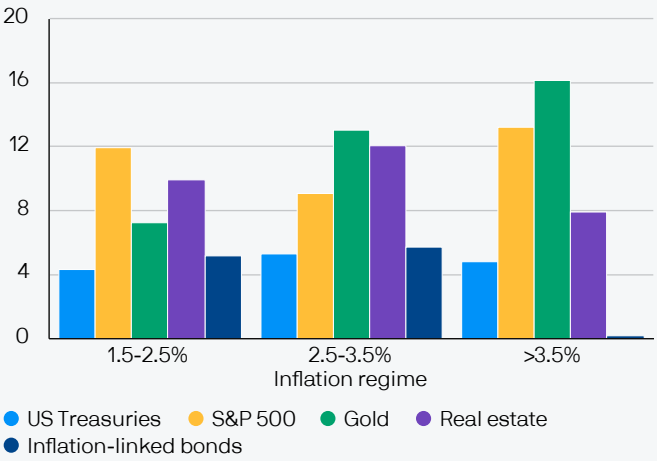


Source: Bloomberg, Burgiss, Cliffwater, FactSet, HRFI, LSEG Datastream, MSCI, NCREIF, S&P Global, J.P. Morgan Asset Management. Bond and commodity indices are Bloomberg except high yield, which is ICE BofA Global High Yield. Hedge funds: HRFI Fund Weighted Composite; US core real estate: NCREIF Property – Open End Diversified Core Equity; Europe core real estate: MSCI Global Property Fund – Continental Europe; Direct lending: Cliffwater; Infrastructure: MSCI Global Quarterly Infrastructure Asset (equal-weighted); Timber: NCREIF Timberland Total Return. Private equity and venture capital are time-weighted returns from Burgiss. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Exhibit 33: Traditional diversifiers work better for chronic inflation

Selected asset class returns by inflation regime

%, average three-year annualised total returns



Source: Bloomberg, BLS, LSEG Datastream, NCREIF, S&P Global, J.P. Morgan Asset Management. Inflation: headline CPI; US Treasuries: Bloomberg US Aggregate - Treasury; Real estate: NCREIF National Property Index; Inflation-linked bonds: Bloomberg US TIPS. Inflation regimes are defined using the three-year annualised growth in CPI, and exclude periods of disinflation. Returns data starts in 1976, except for inflation-linked bonds which start in 1997. Past performance is not a reliable indicator of current and future results. Data as of 31 October 2025.

Scenarios and risks

With more fuel being added to the economic engine, global activity should broaden out across regions in 2026. We expect the US economy to be supported by positive wealth effects, rate cuts and ongoing artificial intelligence (AI) capital expenditure. European growth should accelerate against a backdrop of monetary and fiscal support.

There are, however, downside market risks to be aware of. If technology stocks falter, this could lead to major market and economic ramifications. Inflationary pressures could also prove frustratingly sticky. Well-diversified portfolios are essential to protect against both the risk that growth weakens if tech sentiment sours, as well as the risk that inflation picks up by more than expected.

Base case: Global growth broadens

Macro: Economic activity broadens across geographies. European growth surprises to the upside and narrows the gap with US growth in 2026 amid considerable fiscal stimulus and ongoing support from prior rate cuts. The US expansion continues, supported by further easing from the Federal Reserve (Fed). China's economy is boosted by a stabilisation in the property market, while policymakers support growth in domestic AI technology.

Markets: Equity diversification is essential across the AI ecosystem and across regions, as well as across public and private markets. With the US dollar falling further against a broad basket of currencies, albeit in an orderly fashion, non-US investors should weigh the impact that currency moves might have on returns. Lower US rates support private equity and private credit.

Downside risk: Inflation resurges

Macro: Inflation accelerates, either acutely or slowly as prints creep upward. Acute inflation could occur if tariffs' effects on US inflation turn out to be larger than feared, as companies pass on higher costs to a resilient consumer. Income tax refunds in early 2026, alongside any further tax cuts in the run-up to the midterm elections, would worsen the inflation problem. Chronic, creeping inflation could result from persistent fiscal deficits and questions about Fed independence.

Markets: A negative environment for stocks, with interest rate-sensitive sectors hit hardest. Rising yields in core fixed income lead to losses as stock-bond correlations remain positive. In an acute inflation scenario, real assets, such as timber and core infrastructure, would offer the best protection. In a chronic inflation scenario, gold is an important portfolio diversifier.

Downside risk: Tech stocks falter

Macro: AI sentiment sours, as it becomes clear that the demand for AI infrastructure was overestimated. This leads to overcapacity, falling prices and shrinking margins, as the return on investment of AI capex disappoints. US economic growth slows as AI-related spending stalls and a sell-off in stocks leads to negative wealth effects for US households.

Markets: A very negative environment for equities, particularly for the US. Defensive stocks outperform cyclicals and the negative stock-bond correlation returns. By contrast, this is a positive environment for high-quality, long-duration fixed income. However, private equity and private credit struggle given their tech exposure.

Upside risk: Productivity boom

Macro: Growth accelerates meaningfully, driven by an AI-induced productivity boom. Inflation is kept in check by rising productivity and, potentially, lower energy prices on the back of a Russia-Ukraine resolution. This allows central banks to cut interest rates more aggressively than currently priced by markets.

Markets: A very positive environment for stocks globally. Fixed income also sees strong returns, as policy rates move lower and credit spreads tighten to new record levels.

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