Marketing communication - For professional investors

THE INVESTMENT OUTLOOK FOR 2027

Testing Resilience



BNP PARIBAS
ASSET MANAGEMENT

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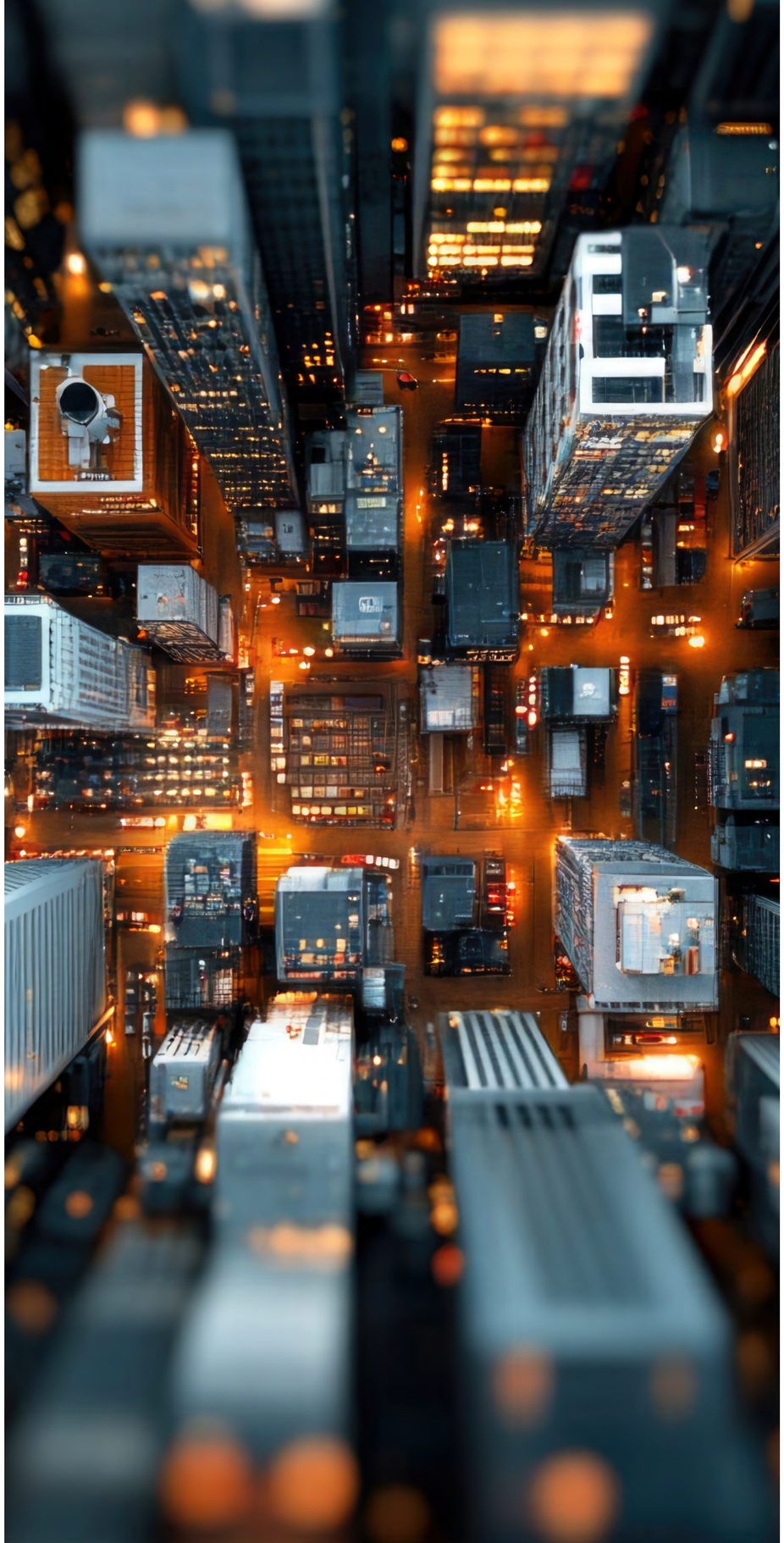
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LETTER TO INVESTORS



By Rob Gambi
Global Head of Investments, BNP Paribas Asset Management

This is an exciting time for BNP Paribas Asset Management. Our ambition is to become the pre-eminent asset manager in Europe, and we are grateful to you for putting your faith in us on that journey.

We are acutely aware that we will only reach our target by consistently delivering strong performance to you.

The merger of BNP Paribas Asset Management and AXA Investment Managers, two strong institutions with complementary capabilities, has created a scalable business which is well-placed to build on what are already strong foundations.

Within the European space, we are one of the largest fixed income, thematics and active fund managers – and number one in European long-term savings.[1]

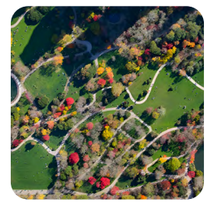
But we are not resting on our laurels. We have used the merger to develop a more powerful investment franchise – one which we believe can generate the returns we demand, and that you expect. We have strengthened our investment culture by prioritising a strategic approach to risk and a commitment to collaboration.

We have enhanced our research capability across a range of disciplines – macro, quant and sustainability – to contribute to idea generation, help sharpen conviction and target market-beating returns. And we plan to exploit the opportunity that new technology brings, to not only increase efficiency, but to drive performance and customisation for you.

We have ambitious plans for how to grow the business. We are focused on scaling our best-performing strategies so they can reach their full potential. We are strengthening our active management expertise, accelerating the growth of our exchange-traded fund franchise, and enhancing our solutions business.

Our aim is to become the partner of choice for investors, from individuals to institutions, cultivating the strategic partnerships we already have and leveraging our expertise to win new business.

But we know none of that happens without delivering performance to you, which brings us back to today and answering familiar questions: Where is the economy heading? What is currently priced in? And ultimately how can we best position portfolios to make the most of the opportunities the market presents us with? Our 2027 Investment Outlook will give you an insight into how we are thinking about those issues testing macroeconomic and market resilience today.



1 #1 in European long-term savings. Source: ranking based on assets under management (AuM) as of 31 December 2024 for internal and external insurers and external pension funds (global AuM for European asset managers; European AuM for non-European asset managers).

EXECUTIVE SUMMARY

Resilience remains but may be increasingly tested

As 2027 approaches, investors face a world showing considerable resilience to ongoing transformation and persistent uncertainty. Our 2027 Investment Outlook explores the key macroeconomic, technological, sustainability, and market trends likely to shape investment opportunities and risks in the year ahead.

Globally, economic growth remains more robust than many anticipated. Europe enters 2027 with renewed industrial momentum, the US continues to benefit from strong productivity and investment, while the global economy generally remains broadly resilient despite increasing divergence across regions. In China, economic growth is likely to ease as low consumption and property investment persist. But while export growth looks set to moderate, policy stimulus could provide some support.

Across emerging markets, we expect growth to remain resilient albeit uneven in 2027. Artificial intelligence-driven demand should support both Taiwan and South Korea but developing countries face headwinds from high debt servicing costs, defence and climate-related spending.

In markets, we expect the technology sector to remain a key driver of equity prices, though the other sectors have seen steady gains, particularly in the US. In fixed income, government bond outlooks are weighed down by fiscal and inflation concerns but we view corporate bond returns in the US and Europe as currently attractive.

Key themes

A central theme throughout our report is the transition from ambition to execution. In sustainability, the focus is moving beyond purely 'green' investments toward financing credible transition pathways, climate adaptation, and nature-positive strategies. Investors are increasingly challenged to distinguish genuine long-term value creation from compelling narratives.

Technology remains a powerful driver of change. AI is expected to progress from experimentation to measurable economic impact, with growing adoption across consumer applications, enterprise operations, cloud infrastructure, and physical automation. As the cycle continues and exuberance gives way to scrutiny, attention will shift toward

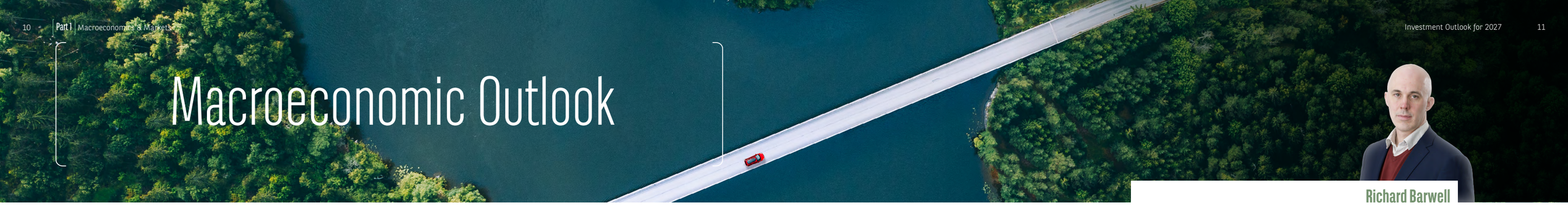


monetisation, productivity gains, governance, and valuation discipline.

In our Investment Outlook 2027, we examine how investors can navigate today's more volatile environment. For fixed income investors, inflation-linked bonds provide a potential source of diversification and protection in a world where inflationary shocks may become more frequent and unpredictable. Meanwhile, Europe's strategic autonomy agenda is creating substantial investment opportunities across defence, infrastructure, energy, technology, and critical supply chains, although successful outcomes will increasingly depend on execution rather than policy intent alone.

And despite elevated volatility, we see European investment-grade credit continuing to demonstrate strength, supported by healthy corporate fundamentals and attractive yield levels.

Across all asset classes, the message is clear: sustainable returns in 2027 will depend on active selection, disciplined risk management, and the ability to identify those investments most capable of converting structural change into sustainable value creation.



Macroeconomic Outlook

Richard Barwell
Head of Macroeconomic Research and Investment Strategy,
BNP Paribas Asset Management

2027 Macroeconomic outlook: Resilience to be tested by geopolitical risks

- European economy enters 2027 with renewed industrial momentum, but elections loom on the horizon
- US growth has been robust this year and is on course to exceed 2% for the fifth year in a row in 2027
- China's near-term recovery looks set to fade in 2027, prompting additional stimulus but no meaningful rebalancing

"Europe to regain momentum, the US to face uncertainty, and China to focus on medium-term growth"

In Europe, we end the year with a greater appreciation of the economy's resilience than we began 2026.

If we look through the volatility induced by Ireland's economic numbers, growth has been robust in Europe in the first half of 2026, and survey data is pointing in the direction of stronger, not weaker, numbers in the second half.

Indeed, the growth outlook is more positive now than it has been for quite some time. The performance of Europe's industrial sector has been underwhelming in recent years, but we enter 2027 with real momentum.

The turnaround is particularly stark in Germany, where industrial production had been in outright decline since the tail end of the last decade but now growth is back, powered by fiscal stimulus and a turn in the investment cycle.

Political uncertainty persists

Inflation remains a cause for concern. The ongoing Iran conflict coupled with the stretched level of global oil and gas reserves on the one hand, and the extreme weather conditions that are likely to accompany El Niño on the other, point to a highly uncertain outlook for commodity prices.

However, unlike the 2022/2023 episode, there is not the same level of concern around a possible wage-price spiral – the risk that a significant increase in the level of commodity prices triggers a persistent increase in the rate of inflation.

Politics will be front of mind in Europe in 2027. The focus is on France, with a presidential election and, most likely, a legislative election soon after. National Rally leader Marine Le Pen looks set to reach the second round of the presidential election, but whether she faces a candidate from the centre-right, centre-left or far-left is unclear, and hence so too is the probable victor.

There is political uncertainty beyond France too; there will be elections in Italy and Germany's coalition remains weak.

US robustness

In the US, productivity growth's resilience in the face of repeated supply shocks, caused by President Donald Trump's actions on tariffs, immigration and the war on Iran, is testament to the underlying strength of the American economy.

With support from both consumer spending and domestic capital investment, growth is on course to exceed 2% for the fifth year in a row in 2027, even as some of the tailwind from the artificial intelligence boom is expected to fade.

Growth is not the only variable that has been above 2% for several years. Inflation is still an issue. Next year we expect underlying inflation to slow, dragged down by a further deceleration in goods price inflation, such that by the end of the year inflation as measured by the Fed's preferred core Personal Consumption Expenditures index will be around 2.5%.

The eventual easing of inflation pressures in 2027 should then enable the Federal Reserve to leave policy on hold throughout the year. The wildcard will be any additional supply shocks that result from the White House's policy choices. The Fed will meet any nasty supply side surprises with additional policy tightening.

China's challenges

In China, we think the recovery in activity is likely to lose momentum as we move through 2027. Policy stimulus should provide some support to activity early in the year, with infrastructure spending and to a lesser extent manufacturing investment doing the heavy lifting. But consumption is likely to stay subdued, property investment will remain a drag, and export growth looks set to moderate.

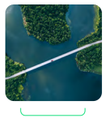
So, we do not share the confidence of the consensus that this narrow policy-driven rebound in activity can be sustained throughout 2027. Yes, official GDP numbers will probably still show growth of a touch under 4.5% in 2027. However, our in-house estimate – which has consistently told a different and weaker story about the underlying path of activity – is likely to suggest growth barely above 3% next year.

As has been the case for several years now, expectations are high within markets and the public policy realm that we are on the cusp of a meaningful policy pivot towards consumption-led growth in China. And as has been the case now for several years, we think those expectations will prove wide of the mark. Policy in 2027 will reinforce the investment-driven growth model, not transform it.

Emerging market divergence

In the rest of the emerging markets, growth will remain resilient yet uneven in 2027, supported by domestic demand with AI-related gains still concentrated in Taiwan and South Korea. Meanwhile, inflationary pressure will subside only gradually, as energy relief fades and El Niño poses upside risks to food prices.

The scope for a broad synchronised monetary easing is therefore limited. The path for rates in each country will depend on the currency, external buffers and domestic inflation dynamics. Fiscal credibility is likely to become an increasingly important source of differentiation, as high debt-servicing costs and infrastructure, defence and climate-related spending collide with domestic politics.





Market Outlook - Fixed Income

Daniel Morris
Chief Market Strategist
Head of Investment Insights Centre

Fixed income outlook 2027: Navigating volatility and inflationary pressures

- Inflation and fiscal concerns are weighing on the outlook for government bonds
- Inflation-linked bonds can potentially offer a hedge against a renewed escalation in the Middle East
- Corporate credit spreads are currently attractive in both the US and Europe, but fixed income investors should remain selective

Bond markets are entering 2027 from a very different position than a year ago. Expectations at the beginning of 2026 were for two cuts in the US fed funds rate over the year, while markets now forecast two hikes by the middle of next year. The European Central Bank may do the same.

There are many reasons for the change in perspective. Inflationary pressures have risen due to the Iran war, even if second-order effects have yet to materialise. If the conflict continues and oil and petrol prices remain elevated, higher transportation costs are likely to increasingly pass through to other goods and services.

At the same time, US growth has been strong, thanks primarily to artificial intelligence-linked investments but also to deregulation. Consumer demand, which economists had feared would weaken in the face of more expensive petrol, has proved to be resilient.

Meanwhile labour market supply has fallen, due to restrictive immigration policies. One of the risks for the coming year is that growth continues above trend when inflation is already above target. This could lead the Federal Reserve to raise interest rates even more than is already forecast.

> *"Above-trend growth and above-target inflation could lead the Fed to raise rates by more than forecast"*

We are cautious on the outlook for US government bonds given sustained inflationary pressures. Though Fed Chair Kevin Warsh has raised the question of how to measure inflation, it is likely too high regardless of the measure used and will require further tightening from the central bank.

In addition, one wonders for how much longer markets will indulge the US government running such a large budget deficit when economic growth is robust. The war in Iran is only adding to budgetary pressures. While nominal GDP is currently high, lowering the near-term risk, a decline in real growth and/or inflation would soon lead to an uncomfortably high debt-to-GDP ratio. The Democratic takeover of Congress, however, means it is less likely that spending will materially increase or that taxes will be reduced.

Higher range for sovereign yields

While growth has been resilient in the Eurozone, it is still running at a lower rate than in the US, meaning inflation pressures are less. The ECB reacted first to the increase in energy prices, which should help contain those pressures from spreading as much to other sectors. Markets, though, are pricing in more hikes from the ECB than we believe will materialise.

Rising policy rates have contributed to the increase in government bond yields this year for major fixed income markets, but they were not the only factor. Political uncertainty in France and worries about the country's fiscal trajectory saw a divergence of bond yields within the Eurozone.

France, though, is not the only country facing a challenging debt-growth dynamic. It was simply precipitated sooner thanks to the upcoming elections, but the outlook for many other countries is also problematic. The risk is that bond investors start becoming more demanding of other countries they believe are not on a sustainable fiscal path.

As the French elections are not until April, there is the possibility of renewed volatility in domestic yields, with potential contagion to Spain, Italy and Belgium. While yields may swing, we see fundamentals as sufficiently strong to avoid a sustained rise in spreads. As a result, there may be potential opportunities in these markets as the yields on offer are high and adequately compensate, in our view, for the volatility.

UK government bonds arguably look the most attractive as yields are comparatively high while inflation may start to fade and economic growth has possibly peaked.

Japan's government bonds' outlook in the near term is more challenging. We see 10-year yields rising back above 3% in the year ahead as the central bank seeks to control inflation while fiscal stimulus remains strongly positive.

Taken together, we expect developed market government bond yields to move in a higher range in 2027 than in 2026; US 10-year Treasuries will likely remain above 5%. Depending on how the situation in the Middle East and the US economy evolves, the income from yields at these levels looks appealing.

Inflation and credit dynamics

Inflation, either from high energy prices or rapid AI growth, should remain a worry for investors. The market expectation for future US inflation is close to its pre-Iran war level and consequently inflation-linked bonds are attractive. In the Eurozone, the asset class can potentially offer a hedge against a renewed escalation of Middle East tensions.

The sharp sell-off in corporate credit, both investment grade and high yield, was partly precipitated by concerns about weaker AI-linked borrowers. Not only is AI pushing up economic growth rates and inflation, it is also increasing volatility due to uncertainty about how exactly the industry will evolve and who the winners and losers will be.

Hyperscalers are expected to continue tapping the corporate credit market to finance their capital expenditures, maintaining pressure on corporate bond yields. Given that economic fundamentals and corporate profits remain solid, however, we do not anticipate further, sustained increases in spreads. At current levels, spreads are attractive in both the US and Europe in both investment grade and high yield. In the high yield space, however, selectivity is more important.

Looking ahead to 2027, the combination of higher yields and attractive spreads offers an attractive potential opportunity for disciplined investors. Despite ongoing headwinds from inflation and political volatility, a diversified strategy focusing on high-quality credit and inflation-linked bonds could prove a potentially attractive combination.

> *"Spreads are currently attractive in the US and Europe in both investment grade and high yield"*



Market Outlook - Equity



Daniel Morris
Chief Market Strategist
Head of Investment Insights Centre

Equity investment outlook: The great divides

- We expect the current divergence between technology and non-tech stocks, as well as between hardware and software companies, to continue into 2027
- While there is uncertainty over the long-term winners of AI development, earnings growth expectations are positive, offering potential opportunities for investors who can tolerate volatility
- We believe equity markets can generate a positive return in 2027, driven by a supportive economic environment and the impact of AI, despite likely short-term fluctuations

The great divides that characterised equity markets in 2026 – first, between tech and non-tech stocks, and second within the technology sector between semiconductor/hardware and software stocks (including hyperscalers) – is likely to persist into 2027.

Returns for technology stocks fell into two phases in 2026: in the first half of the year, we saw a big rally in global semiconductor and hardware stocks, when they rose by 58% (local currency terms).[1]

This gain was partly mirrored by declines in software companies' stocks including the hyperscalers, who were the principal customers of the semiconductor/hardware companies, or in those whose business models were themselves at risk from artificial intelligence technologies.

In the second half of the year, waning confidence in the capital expenditure outlook led to a reversal of performance, with semiconductor and hardware stocks declining 23%, while software stocks recovered their losses, rising 9%.[2]

Through all of this, non-tech stocks marched steadily higher (see Exhibit 1).

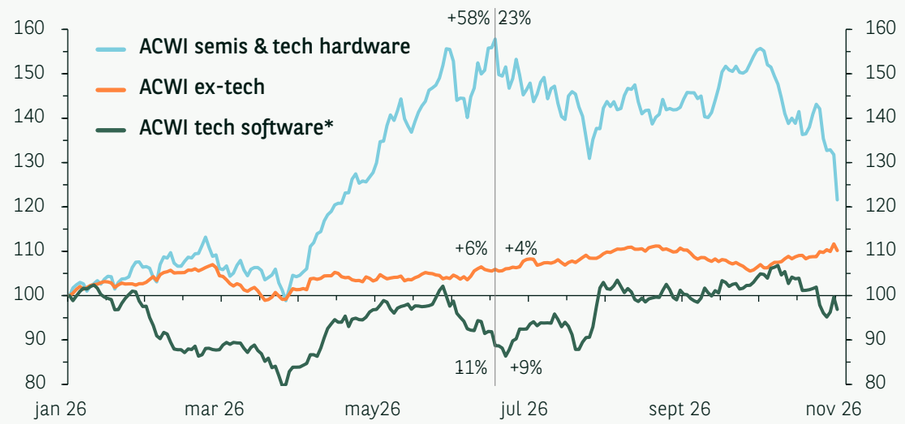
Growth despite earnings uncertainty

We expect these divides to persist, but the key question is, which pattern we will see?

Part of the high levels of volatility witnessed recently in tech stocks stems from the extreme uncertainty around how AI will develop, its impact on society, the economy and corporate profits. Views on who the winners and losers will be change almost daily with periodic 'out of the blue' surprises (like the launch of Chinese start-up DeepSeek's AI model in January 2025) to shake things up even more.

This uncertainty can be seen in the big increase in the standard deviation of earnings estimates for tech stocks – showing how much analysts' forecasts differ from one another. It has increased more than five times over the last two years, while for non-tech stocks it has been steady (see Exhibit 2).

Exhibit 1: Tech equities had two phases over the year while non-tech rose steadily



Data as at 5 November 2026. *Includes Broadline Retail (online retailers) and Interactive Media & Services (search engines, social media and networking platforms). Sources: FactSet, BNP Paribas Asset Management.

Given the wide range of forecasted profits, any marginal news can have a big impact on stock prices. This dynamic is likely to remain part of the AI investment universe.

As for the pattern we may see next year, we anticipate semiconductor and hardware stocks posting good returns given the still very high levels of planned capital expenditures.

The performance of software stocks, including the hyperscalers, is harder to predict. There is intense competition between them, and it is unlikely all the investments being made today will generate a sufficient and timely return on investment.

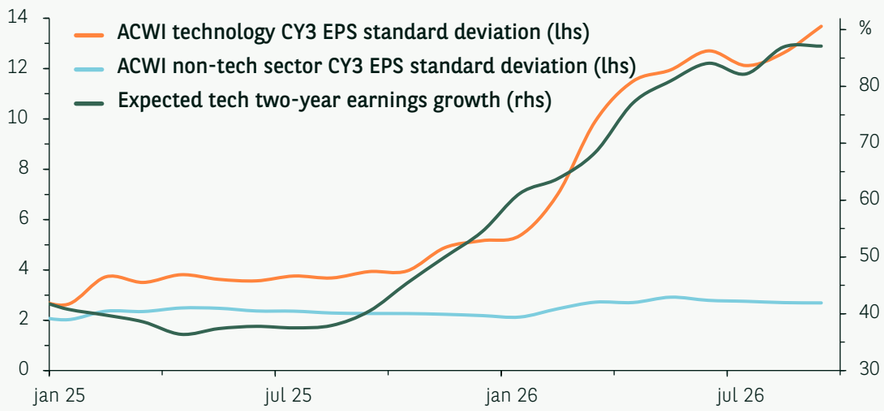
Revenue generation, however, is increasing as companies learn how to incorporate AI into their operations and see meaningful productivity gains. Consumers, too, may be willing to pay more in the future for the benefits AI tools can provide.

Looking beyond volatility

Investors should not lose sight of the medium-term opportunity. It is essentially a question of how fast technology sector earnings will grow. Consensus estimates are for nearly 90% earnings growth over the next two years.

Even if it turns out to be 'only' 70%, that would still imply strong stock appreciation, particularly as valuations are currently below average. The z-score of the forward price-to-earnings ratio – which indicates how far valuations sit below their historical average – is around -0.2 for the Nasdaq 100 index and -1.4 for emerging market technology stocks.

Exhibit 2: Earnings uncertainty has increased, but growth rates forecasted to be high



Data as at 4 November 2026. Sources: FactSet, BNP Paribas Asset Management.

For all the volatility over the last few months, the earnings trajectory remains positive.

This dynamic, though, of high potential returns alongside high volatility, presents a challenge to investors who want to participate in the gains but are concerned by the wide swings in stock prices.

The slices of the AI 'pie' will continue to expand and shrink (and in some cases disappear). Some of the challenges ahead include higher financing costs, increasing competition (notably from China), and energy supply constraints. Nonetheless, we believe the pie will continue to grow over time. An investor who can accept the volatility may find there is potential for returns above those of the broad market over the medium term.

At the same time, the high volatility offers significant potential opportunities to portfolio managers who are able to identify the winners and avoid the losers.

The wider market

Of course, few investors would dedicate their entire portfolio to AI; the technology sector still only represents about 40% of the MSCI All Country World Index by market capitalisation.

Returns for the other sectors have been steadily positive, as Exhibit 1 illustrates. This has been driven by strong growth in the US and lower, but still steady, growth in Europe. The most recent earnings season saw double digit gains across many of the major equity indices and forecasts for next year are also good (18% for MSCI ACWI). We foresee this supportive economic environment continuing, even with interest rates likely to be higher on average in 2027 than in 2026, in our view.

The opportunity, however, may be in identifying those companies which are able to incorporate AI into their operations and accelerate profit growth. This is where the US may have an advantage.

To the degree that AI allows companies to reduce labour costs, US companies are among the quickest to adjust the size of their workforce, in contrast to those in Europe and Japan. This dynamic has its own implications for consumer demand depending on how quickly displaced workers move into new roles, but currently the US adult unemployment rate remains low and steady.

From a market perspective, the superior returns of the Russell Value index compared to other indices with a similar sector composition is perhaps evidence already of this phenomenon.

The potential for European companies may be best among those that can monetise the significant amount of funds behind the European strategic autonomy initiative in sectors such as defence and infrastructure.

The positive global macroeconomic outlook bodes well for equity returns in 2027. AI is likely to continue to play an outsized role in equity returns, with different dynamics between software companies and hyperscalers relative to semiconductor and hardware manufacturers.

The medium-term outlook is positive, but it is unlikely to be a smooth path. Meanwhile, we expect non-tech sectors to see steady growth, with upside potential in those companies best able to leverage the AI revolution.



1 Source: FactSet, BNP Asset Management
2 As of 5 November 2026

Sustainability



Jane Ambachtsheer
Chief Sustainability Officer

2027 Sustainability outlook: Navigating transition, opportunity and risk

- The focus is shifting from purely 'green' investments toward financing the transition of high-emission businesses, with an emphasis on the credibility of corporate governance and technical capacity
- There is an urgent need to balance emissions mitigation with climate adaptation and nature-positive strategies, using new frameworks to assess corporate dependencies on ecosystems and physical climate risks
- While AI offers productivity gains, investors must consider its absolute environmental impact and social consequences, while leveraging stewardship to help address systemic risks

Looking ahead to 2027, sustainability remains central to understanding the multiplicity of changes unfolding in the world and their potential implications for investment.

As highlighted by FTSE Russell, sustainability adoption has rebounded to the near-record levels of 2022, with 84% of asset owners integrating sustainability considerations into their investment processes in 2026.[1]

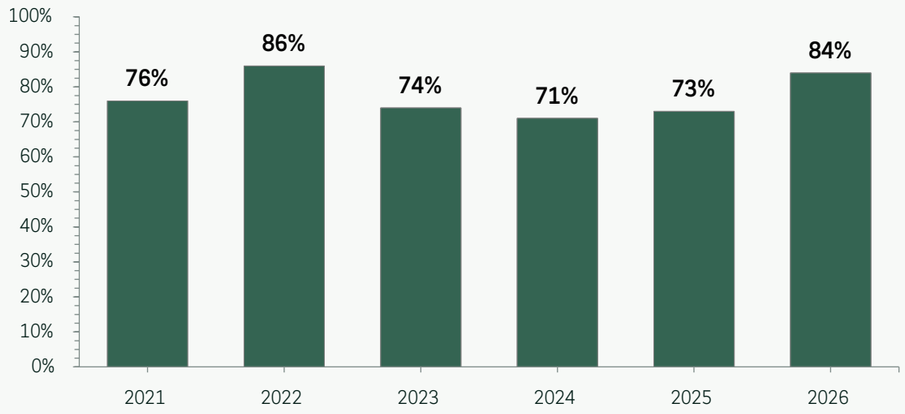
Environmental pressures, geopolitical fragmentation, demographic shifts and technological innovation are reshaping business models and economies. These interconnected forces create opportunities but also risks that traditional financial analysis may not fully capture.

For instance, a growing emphasis on sovereignty is putting pressure on food, energy and critical mineral supply chains, with the results often aligning sustainability priorities with political considerations.

For investors, the challenge is to distinguish durable opportunities from compelling narratives and understand where risks may not yet be adequately reflected to make better-informed investment decisions and achieve resilient long-term outcomes.

We brought these considerations together in our recent 2026 - 2030 Global Sustainability Strategy.

Exhibit 1: Percentage of asset owners implementing sustainability considerations in their investment strategy



Data as at September 2026. Sources: Ninth Annual Sustainable Investment Asset Owner Survey, FTSE Russell, BNP Paribas Asset Management.

From green to transition

The transition opportunity set is becoming broader than merely investing in clean-energy generation. A growing emphasis globally on energy security, affordability and reliability is bringing greater attention to necessary investments in grids, storage, electrification and novel energy production technologies.

In 2027, we expect greater emphasis on financing the transition of higher-emission businesses, alongside investing in activities that are already green. Extractive or carbon-intensive sectors need capital to transform their operations, particularly where technological and economic barriers remain significant.

The differentiator in transition finance will be credibility. Investors need to look beyond targets set by companies to the governance and technical/financial capacities in place to support their achievement.

Forward-looking analysis and frameworks should help distinguish companies making substantive progress from those whose ambitions remain disconnected from their business decisions.

Climate action: Broadening the focus on mitigation to include adaptation

With 2030 fast approaching, less time remains to deliver near-term emissions reductions. But even as the urgency of mitigation increases, so too does the urgency of adapting to physical climate risks reinforced by increasingly visible climate impacts.

Understanding physical climate risk requires attention to asset locations, macro weather shifts and institutional preparedness. But the need for adaptation creates opportunities for a different set of climate solutions such as resilient infrastructure, precision agriculture or alternative risk financing. Identifying these risks and opportunities will become increasingly important.

Beyond real assets where the opportunity for greater investment in adaptation and resilience is gradually unlocking with ever more enhanced risk analytics and growing awareness, investing in adaptation in listed markets could also present opportunities. Environmental infrastructure, for instance, is a focused and forward-looking sub-set of this growth. It can help scale adaptation solutions by financing companies developing and deploying new adaptation solutions.

Nature: Making transition progress more assessable

Nature belongs in this same discussion alongside resilience. Dependencies on water, land and ecosystem services can affect operating capacity and supply-chain continuity. Investment analysis needs to consider not only businesses providing nature-related solutions, but also how existing companies reduce their dependencies and pressures on ecosystems.

A development to watch in 2027 is Finance for Biodiversity Foundation's Nature Transition Framework, which we are helping to develop. It aims to translate existing guidance, including the Taskforce on Nature-related Financial Disclosures work on transition planning, into a more consistent and decision-useful assessment of corporate progress towards a nature positive economy.

The current timetable envisages consultation and publication in 2027, subject to completion. Its potential contribution is practical: helping investors assess issuers, set engagement priorities and monitor progress. The objective should be stronger investment and stewardship decisions, rather than another layer of disclosure.

AI: Look beyond the efficiency promise

Technological innovation will remain part of the sustainability opportunity set. Artificial intelligence can definitely improve natural resource productivity, but efficiency gains should not be confused with a reduction in absolute environmental pressures.

Lower resource use per activity may be offset by expanding demand, the rebound effect often referred to as Jevons' paradox. Investors therefore need to assess absolute energy, water and resource requirements alongside the benefits of individual applications.

Additionally, AI holds promise to increase human resource productivity which could yield dividends for shareholders in the short term but have many potential adverse social impacts later as jobs are lost and/or transformed.

In 2027, the challenge will be to distinguish applications that deliver durable economic and environmental value from those whose benefits are outweighed by negative consequences. Governance and accountability matter, too.

Investor collaboration can help develop shared expectations where standards remain incomplete, while keeping the focus on how technologies are deployed and scaled.

Regulation and disclosures

Addressing these opportunities and challenges often requires conditions beyond the control of individual companies and investors. For 2027, the focus should be on how regulation and disclosure frameworks can support informed investment decisions globally.

Clearer sustainability-related information can help investors assess corporate progress and distinguish investment approaches, including transition strategies. The review of the European Union's Sustainable Finance Disclosures Regulation (SFDR) is one example of this broader discussion, with final requirements and application dates remaining subject to the legislative process.

Across jurisdictions, simplification should preserve the information investors need. Clear product descriptions, credible claims and useful corporate data support trust and informed allocation decisions.

Greater coherence across disclosure and transition frameworks would help investors navigate regional differences, while keeping the emphasis on decision-useful information rather than additional reporting alone.

Systemic risk requires system-level stewardship

Climate change, nature loss, and social pressures can affect the wider systems on which diversified portfolios depend. However, security selection alone cannot address every risk to long-term returns.

This is why stewardship needs to connect issuer engagement with public-policy advocacy. Dialogue with issuers can identify barriers to investment; engagement with policymakers can help explain the conditions needed to overcome them. Collaboration should focus on material, strategic issues, while recognising the limits of any individual investor's influence.

In 2027, we should see public policy advocacy increasingly address the underlying drivers of systemic risk. The aim would be to support conditions that enable issuers and investors to act and strengthen the resilience of the wider economy.

The continuing transition

Looking ahead to 2027, the themes explored in this outlook are only part of a broader landscape of opportunities and challenges. Geopolitics and demographic shifts will also require close attention.

Keeping these interconnected themes in view will be essential to understanding emerging risks and opportunities and informing our approach in the year ahead.



1 FTSE Russell's 9th Annual Sustainable Investment Asset Owner Survey 2026 | LSEG

Artificial Intelligence



Pamela Hegarty
Co-Portfolio Manager
of the Disruptive Technology Fund

Derek Glynn
Co-Portfolio Manager
of the Disruptive Technology Fund

Technology investment outlook 2027: AI moves from promise to proof

- AI shifts from promise to measurable return on investment: 2027 should see AI move further from experimentation toward monetisation, productivity gains, and demonstrable returns, particularly across cloud and enterprise applications
- AI infrastructure spending remains strong: Demand for GPUs, custom silicon, optical networking, data centre power, and other infrastructure should remain robust, with supply constraints persisting in several areas
- A constructive outlook balanced by rising risks: Technology valuations remain broadly supportive, but higher interest rates, debt-financed AI capex, geopolitics, and AI safety concerns could create periods of volatility

After several years of rapid innovation, the year ahead could mark the point at which artificial intelligence's economic impact becomes increasingly visible.

The conversation is likely to shift from technological possibility to real-world adoption, monetisation, and return on investment.

Personal AI agents, enterprise automation, physical AI, and cloud infrastructure are all moving from experimentation toward broader deployment at scale.

The companies best positioned to monetise new products and distribute this innovation should be the primary beneficiaries of the AI cycle's next phase.

Personal AI agents go mainstream

2027 could be the year that agentic AI transitions from an emerging technology to a mainstream consumer product.

Rather than simply answering questions, personal AI agents will increasingly perform tasks on a user's behalf. Common use cases could include prioritising email messages, booking travel, scheduling appointments, managing subscriptions, and coordinating household services.

Improvements in reasoning, memory, and tool use should allow these agents to operate across applications and websites with minimal user input.

Adoption will likely be driven less by model breakthroughs and more by convenience, reliability, and integration into products consumers already use. Over time, personal AI agents could become a new interface layer for the internet.

AI moves into core enterprise workflows

Enterprise AI use cases will expand beyond coding assistants and customer service into agentic capabilities that augment core business workflows.

Organisations will increasingly deploy AI across functions such as finance, sales, human resources, and supply chain management. The next stage of the AI cycle will be defined not only by model capabilities, but also by the ability to deliver useful intelligence at an attractive cost.

Smaller models are likely to handle routine tasks, while larger models are reserved for more complex reasoning. Increasingly sophisticated orchestration software will manage these interactions behind the scenes, making AI more seamless for end users.

As adoption broadens, the focus should shift from experimentation to measurable productivity gains.

AI safety and cybersecurity remain top of mind

The AI safety debate will continue in 2027. Many industry experts fear a major cybersecurity breach or biohazard attack by bad actors using AI models. It is increasingly clear that cybersecurity, governance, and observability software will play a critical role going forward.

Microsoft co-founder Bill Gates and others have advocated for deterministic supervisory software monitoring each AI model to build in policy guardrails for governance, compliance, and security.[1]

Other suggestions by industry experts include third-party auditing of training workloads and independent testing of models before public release. There is a growing consensus that governments need to regulate the industry, but also significant disagreement over how such regulations should be formulated.

Physical AI and edge computing build momentum

Next year could be a pivotal period for physical AI and edge computing – where data processing and storage is physically closer to the data source – as advances in AI begin translating into real-world automation.

Adoption is likely to accelerate first in structured environments such as factories, warehouses, and logistics networks, where intelligent robots can improve productivity and help address labour shortages.

Likewise, AI-enabled wearables, such as smart glasses, could emerge as an important new computing category by bringing contextual intelligence into everyday activities.

Humanoid robots may also make meaningful technical progress, but large-scale adoption likely remains several years away. Taken together, 2027 may represent the beginning of a new phase in which AI expands beyond software and digital workflows into the physical world.

Sector outlook

Semiconductors and hardware: Demand continues to exceed supply

We expect AI infrastructure demand to continue to outpace supply through 2027. Demand remains strong with hyperscalers and other customers providing suppliers with orders stretching through 2027 and beyond.

Optical components, semiconductors, and power for data centres will continue to be key constraints on the supply side. Leadership will continue to diversify as investors look for the next area of investment to support training and inferencing applications, especially as model innovations open new opportunities.

One key risk to monitor is access to capital at an economic cost, especially in a rising interest rate environment. It is unreasonable to expect the buildout to proceed in a linear fashion, but it is hard to know the timing of any digestion period or interruption in the AI infrastructure race.

Given the magnitude of outperformance of technology infrastructure names particularly during the first half of 2026, it would not be surprising to see continued volatility through 2027 as investors debate the relative merits of software versus semiconductors.

Cloud service providers: Return on investment comes into focus

2027 could be the year that cloud service providers prove the return on investment for their unprecedented AI infrastructure spending.

Cloud service providers are uniquely positioned to monetise AI given their unmatched data centre footprints, access to graphics processing units, rapidly expanding custom silicon programmes, and highly profitable core businesses which support funding needs.

Investors should become more constructive as cloud revenue growth accelerates, capex growth moderates, and cloud margins remain healthy. Together, these factors could provide compelling evidence that AI infrastructure can generate attractive long-term returns rather than simply support an arms race.

Software: Careful navigation required

The software sector will require increasingly careful navigation as investors distinguish between AI beneficiaries and companies vulnerable to AI disruption.

Broad-based scepticism toward application software should give way to a more nuanced assessment of which companies can leverage AI to expand their total addressable markets and strengthen their competitive positions.

While AI monetisation is likely to accelerate across the industry, it will still represent a relatively small portion of revenue for most software companies in 2027.

We remain constructive on cybersecurity and infrastructure software, where AI is driving both increased demand and new product opportunities, though we are mindful of premium valuations given strong performance in 2026.

The first wave of frontier AI IPOs arrives

The potential public listings of leading frontier AI labs in the year ahead would mark a significant milestone. The initial public offerings would likely represent some of the most notable technology debuts since the emergence of the cloud service providers.

Beyond expanding the investable universe, these listings could provide investors with direct *pure play* exposure to the development and monetisation of frontier AI models, potentially attracting significant capital flows and reshaping technology indices.

More broadly, due to public market scrutiny, these companies will be under pressure to demonstrate sustainable revenue growth, scalability, margins, and returns on capital.

Valuations bolster environment

Valuations across much of the technology sector remain supportive, providing a constructive backdrop for investors.

While select AI beneficiaries continue to command premium multiples, many software, semiconductor, and hardware names trade at levels that appear reasonable relative to their growth and earnings outlooks.

The average forward price-to-earnings ratio for the semiconductor industry has declined to below 19 times (as of mid-October 2026) compared to the five-year average closer to 25, and the software sector's enterprise value-to-sales ratio is moderately below its long-term average.[2]

- **Semiconductor stock valuations look reasonable given earnings momentum.** In the semiconductor industry group, valuations are compelling, but for companies in commodity markets for standardised components like memory chips, investors are hesitant to put high multiples on what could prove to be peak earnings expectations

- **Valuations remain compelling for select application software companies that can monetise AI and defend their competitive positions against disruption.** Outside of application software, widely perceived AI beneficiaries including certain data management and cybersecurity companies now command premium valuation multiples. Meanwhile, the cloud service providers appear undervalued, particularly if further evidence emerges that AI investments are generating attractive returns

- **Select hardware stocks are undervalued.** Optical and other data centre infrastructure stocks have pulled back on concerns about the sustainability of supply shortages and of demand, and perhaps in relation to the prospects of a Democratic sweep in the US (which we believe would not in and of itself have a major impact on data centre approvals); select stocks look compelling

The long-term opportunity created by AI remains significant, but investors should remain mindful of several risks that could slow adoption or pressure valuations. While these risks are worth monitoring, the balance of evidence continues to support a constructive outlook for the sector. Key risks include, but are not limited to:

- **High interest rates** could result in valuation pressure for long duration assets and could raise the cost of capital for financing AI infrastructure

- **The geopolitical environment is uncertain** and makes it more likely that there will be competing AI ecosystems, inefficient supply chains, and physical risks to AI infrastructure

- **AI safety concerns could slow development,** particularly if there is a cyber or biological attack by a bad actor, and/ or if there are more breaches by AI agents going rogue

- **Financing challenges could slow AI investment**, especially as a higher portion of capex is being debt financed

- **Trends could give rise to the formation of an AI bubble,** including circular relationships, increasing use of debt financing and off-balance sheet vehicles, lax regulation, private market valuations moving into the public markets with IPOs, and rising interest rates (which could pop a bubble)

> *"The long-term opportunity created by AI remains significant, but investors should remain mindful of several risks"*

However, mitigating factors include investor scepticism, encouraging AI adoption trends in consumer and enterprise applications which demonstrate paths to positive return on investment, and reasonable valuations that are not yet at dotcom bubble levels.

The next stage

The next phase of the AI cycle is likely to be defined less by technological breakthroughs and more by execution, adoption, and monetisation.

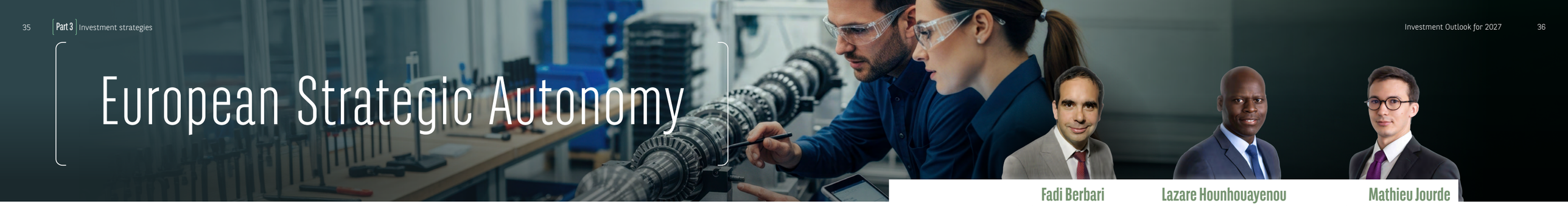
Companies that can translate AI investment into sustainable revenue growth and attractive returns on capital should emerge as the long-term winners.

While periodic volatility is inevitable, we remain constructive on the technology sector and the opportunities created by the ongoing AI transformation.



1 The choices we make about AI now are critical | Bill Gates / Dario Amodei — We Must Pace the Frontier / https://mustafa-suleyman.ai/a-warning-about-model-welfare
2 Source: BNP Paribas Asset Management, FactSet

European Strategic Autonomy



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European Strategic Autonomy in 2027: Where are we? Where are we going?

- Two years after Mario Draghi's 2024 competitiveness report, implementation of recommendations is uneven; while security and defence have seen significant progress other sectors have advanced more slowly
- There is substantial investment growth across several strategic areas, including a rising defence budget and €21.1 billion earmarked for critical raw materials projects
- The focus is transitioning from policy announcements to execution, where the primary challenge for investors is identifying which companies and issuers can successfully convert increased EU spending into sustainable earnings and durable economic returns

In September 2024, former European Central Bank President, Mario Draghi presented a landmark report on the future of European competitiveness.

The report diagnosed structural weaknesses in productivity, investment and industrial capacity relative to the US and China and set out 383 recommendations spanning several sectors.

Its central thesis is that Europe must mobilise substantially higher public and private investment – originally estimated at between €750 billion and €800 billion annually – and streamline decision-making if it is to safeguard strategic autonomy.

The agenda has since become a reference point for European Union industrial and security policy.

Two years on, the so-called Draghi Implementation Index shows that 15.7% of the recommendations have been fully implemented, with the combined strict-plus-partial rate – a measure of how much of Draghi's competitiveness report has been turned into binding law – at 41.3%.[1]

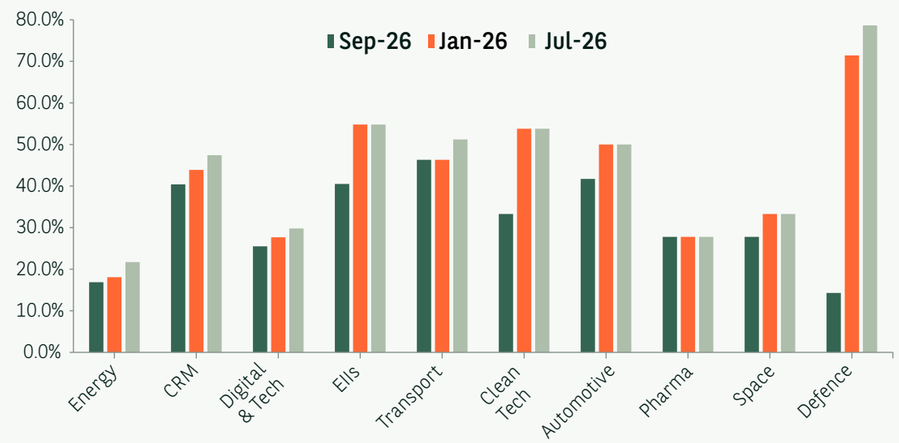
Progress is uneven but tangible in security-linked areas. Defence has reached 78.6% (strict-plus-partial), but digitalisation and advanced technologies (29.8%), pharmaceuticals (27.8%) and energy (21.7%) have advanced more slowly. These results indicate that delivery has been strongest where competitiveness overlaps with security imperatives.

Addressable markets are expanding

In defence, EU member states spent €418 billion in 2025 and are projected to reach €454 billion in 2026, with trends indicating further growth toward as much as €547 billion by 2029.[2]

A substantial share of equipment and investment spending flows to European industry, generating multi-year opportunities measured in the high hundreds of billions of euros.

Exhibit 1: Strict + Partial Index by Sector



Data as at July 2026. Sources: Draghi Observatory & Implementation Index, BNP Paribas Asset Management.
CRM: Critical raw materials. EIIs: Energy-intensive industries

Additional demand for non-traditional defence suppliers could reach up to €500 billion over 2026–29.[3]

Major joint programmes can be tricky to agree on as Germany and France have showed recently: the next-generation fighter Future Combat Air System and the Main Ground Combat System initial plan have been cancelled, which will reduce economies of scale.[4]

In space, the Infrastructure for Resilience, Interconnectivity and Security by Satellite – IRIS constellation – with a total cost of €15.6 billion, has moved into the implementation phase.

Major manufacturing contracts awarded in August–September 2026 cover the bulk of the 348-satellite programme, with first launches scheduled for 2029.[5]

Furthermore, space sovereignty has moved higher up in Europe's strategic agenda: The disruption to Starshield connectivity in Ukraine on 14 October 2026 has highlighted Europe's dependence on US space infrastructure.

While Eutelsat OneWeb satellite and IRIS provide European-controlled alternatives, Europe still lacks Starlink's scale and a sovereign space-based missile-warning capability. Limited launch capacity remains another vulnerability.

This urgency is strengthening political support for Project Bromo (proposed consolidation of the satellite-manufacturing activities of Airbus, Thales and Leonardo).

Further spending on secure communications, missile warning and Earth observation should support the order pipeline. However, without greater launch capacity, Europe risks developing sovereign satellite capabilities while remaining reliant on US infrastructure to deploy them.

Raw materials and clean tech bolster backdrop

Critical raw materials offer a growing project pipeline: the 46 new strategic projects selected in October 2026 under the Critical Raw Materials Act are expected to mobilise around €21.1 billion in public and private investment, advancing capacity in lithium, nickel, cobalt, rare earths and related materials for batteries, defence and permanent magnets.[6]

Clean technologies and the energy transition continue to present large-scale opportunities, in our view. Draghi's original framework of roughly €750 billion to €800 billion in annual additional investment needs remains a useful reference, while McKinsey analysis highlights multi-trillion-euro global cleantech capital expenditure by the mid-2030s, with substantial accessible value for European players in e-mobility, grids and related technologies.[7]

Digitalisation and advanced technologies offer long-term markets linked to AI and industrial connectivity.

Industrial policy measures are reinforcing these dynamics. The EU steel measure, effective from 1 July 2026, establishes a duty-free quota of 18.3 million tonnes with a 50% out-of-quota duty, supporting domestic capacity utilisation.[8] Strategic designations for critical materials and refinements to battery local-content rules further strengthen the operating environment for European producers.

Equity valuations in exposed sectors have adjusted from earlier peaks, creating interesting entry points alongside still-elevated earnings growth expectations in defence.

Fixed-income markets continue to see increased issuance linked to defence and infrastructure, new issuers mainly in euro are paving the way, the market is broadening and new eastern European and Nordic companies are now using the euro bond market to fund their needs. The EU money injections are driving a whole ecosystem all over Europe.

Table: European autonomy - Equity valuations in exposed sectors

Index valuation	PE NTM* ~one year ago	PE NTM now (approx.)	EPS CAGR** now (approx.)	PEG*** one year ago	PEG now	FCF**** yield one year ago	FCF yield now	Market cap variation in one year
MSCI World	20.1	17.6	19.0	1.2	1.0	3.1	3.4	12.6%
MSCI Europe	14.9	14.0	13.5	1.3	1.1	4.0	4.8	5.2%
MSCI Europe Aerospace & Defense	29.4	23.6	18.3	1.9	1.5	2.8	3.5	-5.0%
MSCI Europe Industrials	21.3	19.3	16.7	1.6	1.3	3.8	4.4	-1.3%
MSCI Europe Energy	10.1	9.1	10.0	1.3	0.8	8.1	13.3	48.2%
MSCI Europe IT	27.9	24.9	26.7	1.3	1.1	2.8	2.1	27.7%
MSCI Europe Materials	16.9	15.9	15.9	1.5	1.1	3.0	4.1	6.7%
MSCI Europe Utilities	14.2	14.8	9.9	1.9	1.6	-1.8	-2.0	15.7%

*PE: Price to earnings ratio, NTM: Next twelve months. **EPS: Earnings per share, CAGR: Compound annual growth rate. ***PEG: Price/earnings to growth ratio. **** FCF: Free cash flow
Source consensus Factset as of 19 October 2026, past performance is not indicative of future results

2027: From policy ambition to investment execution

Europe's strategic-autonomy agenda is increasingly translating into tangible investment across defence, energy infrastructure, space and critical supply chains. For investors, however, the opportunity is becoming more selective.

In equities, the focus is shifting from policy announcements and order intake towards companies able to convert larger backlogs and capacity investment into sustainable earnings and cash flow.

In fixed income, higher investment creates additional issuance opportunities but also requires greater differentiation. Sector selection is key and rating agencies are really segregating between companies that are benefiting from the EU umbrella (upgrades such as in the defence sector) and those losing momentum in the face of fierce global competition.

The key investment question for 2027 is therefore no longer simply whether Europe will spend more, but which companies and issuers can translate strategic autonomy into durable economic returns?

> *"The main challenge is identifying which companies can convert increased EU spending into sustainable earnings anddurable returns."*



1 Draghi Observatory & Implementation Index - EPIC
2 European Defence Agency
3 A €500 Billion Opportunity for Nondefense Firms | BCG
4 Defense Magazine
5 European Commission / SpaceRISE
6 European Commission
7 McKinsey
8 European Commission

Protection From Inflation





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Navigating volatility in 2027 with inflation-linked bonds

- Geopolitical and economic shocks have made inflation less predictable, strengthening the case for inflation-linked bonds
- Higher real yields can provide a stronger buffer and more attractive entry points for inflation-linked bonds than in previous years
- A diversified, active approach is essential to navigate changing inflation dynamics and managing interest-rate sensitivity across different markets

A series of inflationary shocks have buffeted the global economy in recent years – from pandemic-related shutdowns, followed by massive fiscal stimulus intended to protect firms and households, to wars in Ukraine and Iran, to tariffs, and most recently the artificial intelligence capex boom. Central banks have had the unenviable task of responding to these supply and demand shocks, having to judge their magnitude and persistence to calibrate policy rates.

Despite inflation having remained well above central bank targets for several years, investors have not seemed overly concerned about central banks' willingness or ability to tackle inflation.

But geopolitical tensions, trade wars, energy insecurity, supply chain disruptions and rising investment in infrastructure and AI are reshaping the inflation outlook.

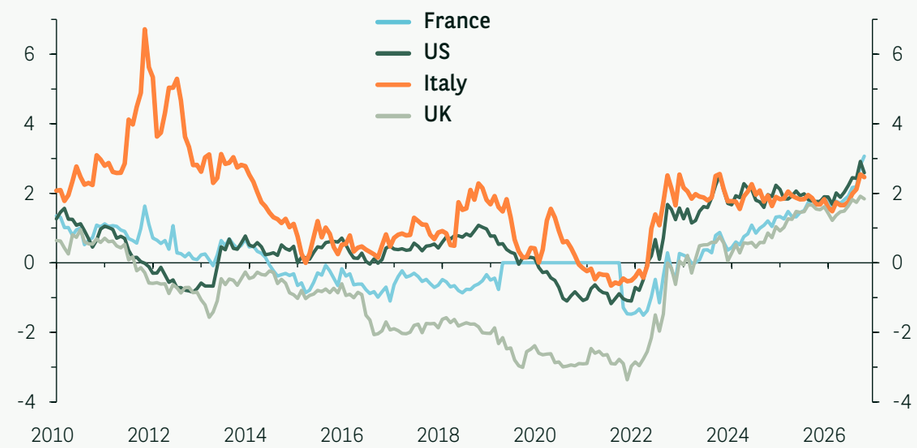
As we look to 2027, we believe that rather than assuming there will be a return to the relative price stability of the pre-pandemic decade, investors may need to prepare for a world in which inflation might be more elevated, but will also almost certainly be more volatile, less predictable, with a broader range of possible outcomes.

Inflation volatility: A structural shift?

For investors, a more volatile inflationary backdrop changes the way inflation protection should be considered. We believe it strengthens the case for inflation-linked bonds, especially now that real yields (returns adjusted for inflation) have normalised from pre-pandemic levels. Rather than a tactical response to the next inflation release, inflation-linked bonds can serve as a structural component of a fixed income or multi-asset portfolio.

Importantly, valuations of inflation-linked bonds have also become more attractive. Real yields derived from inflation-linked bonds are now significantly higher than during much of the past two decades, providing a significant buffer in case central banks need to tighten policy further than is currently priced. Exhibit 1 shows developments in generic 10-year real yields for the key US, UK, French and Italian inflation-linked bond markets.

Exhibit 1: Generic 10-year Inflation-linked bond yields



Source: Bloomberg, as of 31 October 2026.

How do inflation-linked bonds work?

Unlike conventional bonds, inflation-linked bonds have cash flows that are adjusted in line with realised inflation, in order to protect the investor's purchasing power. Their principal and coupon payments are linked to an inflation index, providing compensation for changes in prices over the life of the bond.

However, investors should be aware that inflation-linked bonds do not always rise in value whenever inflation increases. Their mark-to-market performance depends on three main drivers:

- Real coupon income: Like conventional bonds, inflation-linked bonds generate income through the periodic payout of (inflation-adjusted) coupons

- Inflation accretion: An inflation-linked bond's principal payout moves in line with the underlying Consumer Price Index, and in most cases with a floor at the bond's original face value. As a bond ages, it accrues inflation via a formulaic uprating of the principal paid out at maturity (but which increases the bond's market value immediately)

- Duration impact: Like conventional bonds, inflation-linked bond prices are sensitive to fluctuations in yields. The magnitude of these movements depends on the bond's duration, or sensitivity to yield changes. They tend to outperform conventional bonds when investors perceive inflation risk is rising, reflected in a widening of the spread between nominal and real yields on bonds of comparable maturity (the so-called breakeven inflation spread)

A common critique of inflation-linked bonds is that an investor who holds a 10-year bond through a period of elevated inflation may end up gaining less from inflation accretion than they lose on duration when the central bank tightens policy to combat the rise in inflation. This explains why investors looking for inflation protection have in recent years focused on short-dated inflation-linked bond funds.

Real yields and relative returns

However, the analysis is incomplete for a couple of reasons. First, starting yields matter. Today's higher yields provide a much larger buffer against rising yields, especially if some monetary policy tightening is already priced in.

Second, most investors already own duration elsewhere in their fixed income allocations, but holding real yields could potentially be the better choice when faced with an inflation scare that initially pushes breakevens wider and then allows the investor to collect that inflation.

For some investors then, relative return, not absolute return, is the focus. By way of example, the Bloomberg one-to-30-year Treasury Inflation-Protected Securities (TIPS) index outperformed its maturity-matched comparator Treasury index by 12.6% in total return terms between 1 January 2020 and 12 December 2024, a period that covered the pandemic inflation, Ukraine war and a full Federal Reserve hiking cycle.[1]

This outperformance was achieved despite the rise in breakevens being temporary, and the central bank moving policy into restrictive territory, with inflation-linked bonds accreting the unanticipated rise in the CPI index.

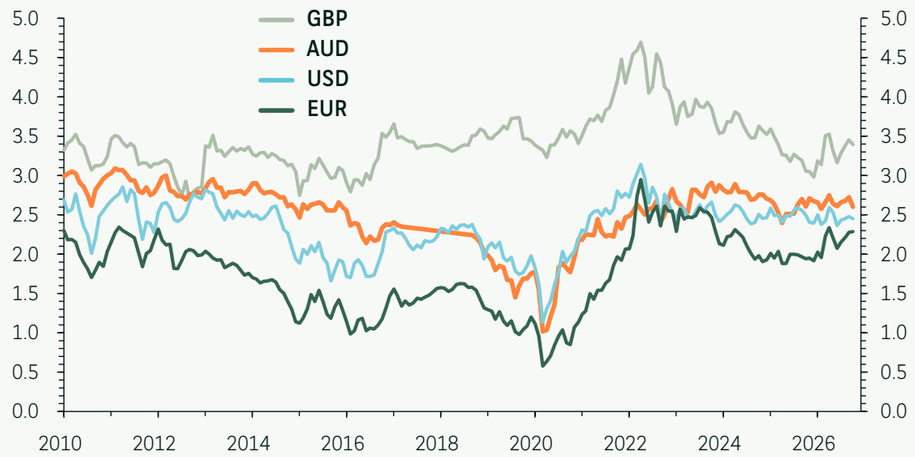
So, for investors with a fixed duration allocation, the role of inflation-linked bonds in a portfolio is really to aim to provide diversification in the near term (when real yields diverge from nominal yields), and long-term insurance against inflation shocks (via the gradual process of inflation accretion).

Aiming for this insurance is most valuable when inflation episodes are likely to be more frequent than has been the case in the last three decades, and when the cost of the insurance (reflected in breakeven inflation rates) remains low.

With breakeven inflation rates at around 2.0 to 2.4% in the Eurozone and US, the hurdle will not be hard to clear if the global economy continues to be subjected to supply shocks.

Investors looking to gain protection against inflation surprises therefore need to ask themselves two questions: which markets should they focus on and how much interest rate sensitivity should they take on?

Exhibit 2: 10-year breakeven inflation rates derived from CPI swaps



Source: Bloomberg, as of 31 October 2026.

Taking a global approach

Inflation may be a global phenomenon, but it does not evolve uniformly across countries.

The US, Eurozone and UK can experience different inflation dynamics and monetary policy cycles. As a result, opportunities in inflation-linked bonds can shift between markets over time.

For example, US TIPS were attractive during 2025's 'Liberation Day' tariff announcements, while 2026's Iran-related energy shock shifted attention towards Europe and UK inflation-linked bonds. A global investment universe therefore offers access to a broader range of opportunities and allows investors to diversify their sources of inflation exposure rather than relying on a single market.

Navigating inflation and interest-rate risks

Choosing the right market is only part of the challenge. Investors must also consider maturity, duration and the inflation expectations already reflected in bond prices.

Passive inflation-linked bond indices are typically weighted according to outstanding issuance or market capitalisation. This does not necessarily provide the most attractive investment exposure and can result in significant interest-rate sensitivity. UK inflation linked bonds, for example, make an outsized contribution, both in terms of weight and duration, to global inflation-linked indices.

The soaring inflation and sharp increase in interest rates witnessed in 2022 illustrates why duration matters. Investors seeking inflation protection may not want to assume substantial exposure to the interest rate risks associated with longer-maturity bonds during periods when central banks are aggressively tightening policy.

In these circumstances, investors may favour the shorter end of the yield curve, seeking to capture inflation exposure while limiting some of the volatility associated with longer-duration bonds.

An actively managed approach allows portfolio managers to adjust exposure across countries and maturities, manage real-yield sensitivity and assess whether market inflation expectations offer attractive value.

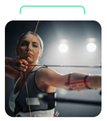
The objective is to identify where investors are being best compensated for the risks they assume, rather than simply replicating the composition of the inflation-linked bond market.

What does this mean for investors?

The case for inflation-linked bonds rests on three considerations:

- Inflation protection beyond short-term market movements: A more unpredictable inflation environment supports considering inflation-linked bonds as a structural portfolio allocation rather than a tactical trade
- More attractive real yields: Investors can now combine seeking inflation protection with positive real yields, unlike during much of the previous decade
- Greater scope for selective positioning: A global, actively managed approach can help investors navigate differences in inflation expectations, real yields and duration across markets

With inflation outcomes becoming less predictable, the question for investors is no longer simply when to seek inflation protection, but how best to incorporate it into their long-term allocation.



1 Bloomberg

Euro Credit Total Return



Boutaïna Deixonne
Head of Euro Investment Grade and High-Yield Credit

European investment grade credit: Leveraging fundamentals and attractive yields

- Despite significant challenges in 2026 the European investment-grade credit market has remained remarkably resilient
- While volatility is expected to persist, the outlook remains constructive, supported by positive economic growth and healthy corporate fundamentals
- We believe current all-in yield levels provide an attractive entry point for investors, helping to offset pressures from higher rates and supporting long-term demand

2026 has been marked by significant challenges – heightened interest-rate volatility, elevated energy prices, persistent inflation concerns and frequent shifts in monetary policy expectations.

These factors have largely overshadowed the risks that dominated discussions at the beginning of the year, particularly those related to the impact of artificial intelligence on corporate business models and concerns surrounding private credit markets.

Despite persistent geopolitical uncertainties, the European investment-grade credit market has demonstrated remarkable resilience. That said, market dispersion has increased since the summer, with cyclical sectors and high-yield spreads underperforming.

In Europe, the sharp rise in government bond yields pushed total returns into negative territory, weighing somewhat on investor flows. Nevertheless, investment-grade spreads have remained resilient and have outperformed other fixed-income segments, notably euro high yield.

New year expectations

Looking ahead to 2027, we expect volatility to remain elevated against a backdrop of fiscal concerns, increased sovereign funding needs, elections in several major economies and uncertainty surrounding future central banks' actions.

Even so, we remain constructive on the credit asset class. Economic growth remains positive, corporate fundamentals are healthy, and all-in yields continue to offer an attractive entry point for investors. These factors should ultimately support demand for credit despite periodic bouts of volatility.

Investors generally raise three key concerns regarding the European credit outlook: namely the impact of higher rates on corporate fundamentals; the outlook for flows into the asset class; and the potential consequences of elevated primary market supply. In our view, each of these concerns is valid but ultimately overstated.

The yield factor

The first concern is whether the sharp increase in yields could eventually weaken corporate balance sheets and lead to rating pressure. While this risk is more relevant for highly leveraged issuers in the high-yield universe, European investment-grade corporates enter this period of higher rates from a position of strength.

Although some sectors and issuers face structural and cyclical challenges and rising funding costs, the broader picture remains favourable. Cash-flow generation is solid, profitability remains healthy and leverage is generally contained.

Recent earnings seasons have confirmed these trends, with revenue growth remaining resilient and credit metrics continuing to improve. Robust earnings should continue to offset part of the pressure from a prolonged period of elevated rates.

Consequently, we expect investment-grade fundamentals to remain broadly stable. However, we remain more selective in the lower-rated high-yield segment, where refinancing needs are more front-loaded and financial flexibility is more limited.

Policy influence

The second question is related to the impact of a higher interest rate environment on demand for credit. Historically, negative total returns have tended to weigh on investor flows, and the recent increase in rate volatility has indeed triggered periods of outflows from credit markets.

However, these outflows have remained relatively modest compared with previous market stress episodes. We believe this resilience is largely explained by the significantly higher income available in fixed income today.

Current yield levels are increasingly attractive for a broad range of investors, including pension funds, insurance companies and fixed-to-maturity products.

Exhibit 1: Euro investment-grade yield (%)



Data as at September 2026. Sources: Bloomberg, BNP Paribas Asset Management.

While we believe the structural backdrop for flows remains supportive, a sustained recovery in inflows will likely require greater stability in both underlying rates and rate volatility.

Once this adjustment phase is complete, the combination of attractive income and solid fundamentals should encourage investors to increase allocations to the asset class.

Issuance issues

The final concern is supply absorption, particularly financing needs from hyperscalers and AI-related investments. This has been one of the most frequently cited risks among investment-grade investors over the past 12 months.

While issuance has been particularly dynamic in the US market, totalling approximately $180 billion, it has so far been much more moderate in Europe, with only around €25 billion year-to-date.[1]

Although additional issuance remains possible before year-end, market volatility could encourage issuers to adopt a more measured approach in the near term. For 2027, issuance from hyperscalers could accelerate further.

Nevertheless, we believe that if issuance is spread over different maturities and if it becomes more programmatic over time, this could allow investors to better anticipate funding needs as long as issuers continue to show strong earnings and business models.

Opportunities ahead

Overall, we remain constructive on European credit, supported by strong corporate fundamentals, resilient economic activity and attractive all-in yield levels. While volatility is likely to remain elevated and spread dispersion may increase further, these conditions should also create opportunities for active investors to generate alpha.

We continue to see attractive opportunities across selected areas of the market, including higher-quality, high-yield, subordinated financial debt and parts of the real estate sector.

In an environment characterised by greater differentiation between issuers, security selection will become increasingly important to capture the opportunities ahead.



1 Source: Bloomberg, as at 30 October 2026

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