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The Navigator

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Bubblicious

By Edward Lim, CFA

If you spent your childhood in the late 70s and early 80s like this writer did, you will likely remember this brand of bubble-gum, Bubblicious. It was marketed on one big difference from the competitors; it can be blown to a bigger bubble than the rest. For a few glorious minutes, the expansion seemed limitless, defying the laws of physics until the inevitable: a sticky mess that leaves you picking residue off your nose. But like all fad, Bubblicious, and the rest of the gum industry peaked by the 90s as it went from as symbol of youth and rebellion to thrashy and unhealthy junk at the turn of the century. Investors are currently blowing an AI bubble. It is ubiquitous in everyday lingua franca, enthusiastically hyped, and yet capable of producing something genuinely impressive. But will it have lasting substance beneath the initial rush, or whether we are once again watching a very large bubble being blown?

There are three important developments we will be watching for in 2026. Will a jobless growth lead to an economic recession? Will the AI bubble finally burst? Will Fed lose its independence? Each on its own will have important ramifications to asset allocation; all of them happening together will have serious negative consequences to returns.

Topic 1: The curious case of a jobless growth

It is remarkable how well the US and global economies have endured the tumultuous and brouhaha of US tariff in 2025. At the start of the year, we argued that consensus forecasts of 2.1% growth for the US and 3.1% globally were overly optimistic, given the rhetoric surrounding tariffs and immigration. Our own expectation was for trend-like outcomes: 1.8–2.0% for the US and 2.8–3.0% globally.

That assessment was tested in April, when ‘Liberation Day’ tariff announcements raised the spectre of stagflation should the proposed measures persist for two quarters or longer. In the end, pragmatism prevailed. A combination of negotiated retreats, asymmetric concessions from trading partners, and selective enforcement diluted the worst outcomes. When coupled with an accelerating AI-led capital expenditure cycle, expansionary fiscal policies, easing financial conditions, and resilient corporate profitability, both the US and global economies are now on track to end the year growing at approximately 2.0% and 2.7% respectively remarkably close to our initial expectations.

For 2026, we continue to rely on our three-pronged framework to assess the global growth outlook. First, near-term momentum, as captured by our Nowcaster, points to annualised growth of 1.7% in the US and 2.6% globally. Second, forward-looking indicators remain constructive: the November Global PMI of 52.7 and US Composite PMI of 53.0 imply medium-term growth of roughly 2.9% and 2.5% annualised. Third, consensus forecasts for full-year 2026 anticipate growth of 2.0% in the US and 3.0% globally. Taken together, **the evidence points to another year of trend-like global expansion, no recession.**

Nowcast, PMI and Forecast have +ve momentum and point to trend-like growth for 2026

	Nowcaster GDP Growth (Annualised)	Change from 4Q25 publication
Global	2.6	0.1
Developed Markets	1.5	0.0
Emerging Markets	4.3	0.6
US	1.7	-0.4
Euro Area	1.2	0.3
Germany	0.1	0.4
France	1.0	0.4
Japan	1.1	1.4
UK	0.0	-0.6
China	5.1	0.2
India	7.6	0.9
Brazil	0.6	0.1

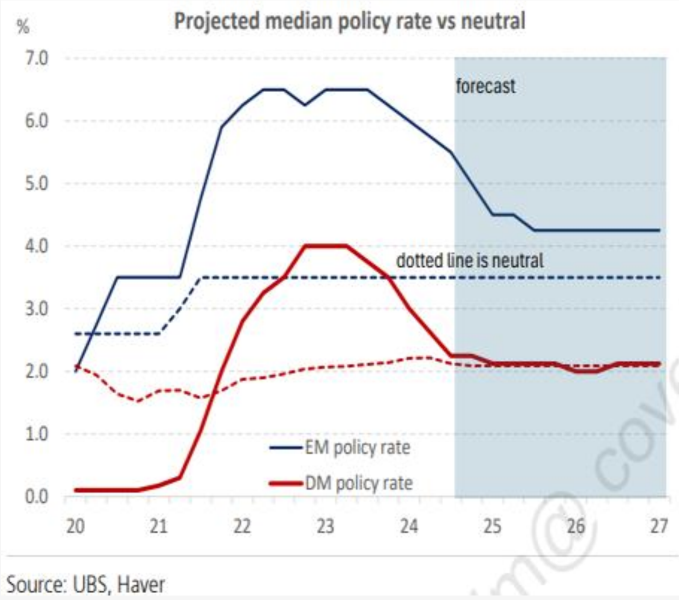
Source: Goldman Sachs

	GDP Forecast by Economists			Change from 4Q25	
	2025('E)	2026(F)	2026(F)	2025('E)	Change 2026(F)
Global	3.0	3.0	3.0	0.1	0.1
Developed Markets	1.7	1.7	1.8	0.2	0.1
Emerging Markets	4.2	4.2	4.1	0.1	0.2
US	2.0	2.0	2.0	0.2	0.2
Euro Area	1.4	1.2	1.4	0.1	-0.2
Germany	0.3	1.0	1.5	0.0	-0.1
France	0.8	0.9	1.1	0.2	0.0
Japan	1.2	0.7	0.8	0.2	0.0
UK	1.4	1.1	1.4	0.1	-0.1
China	4.9	4.5	4.3	0.1	0.3
India	7.5	7.2	6.5	1.0	0.7
Brazil	2.3	1.7	1.9	0.1	0.1

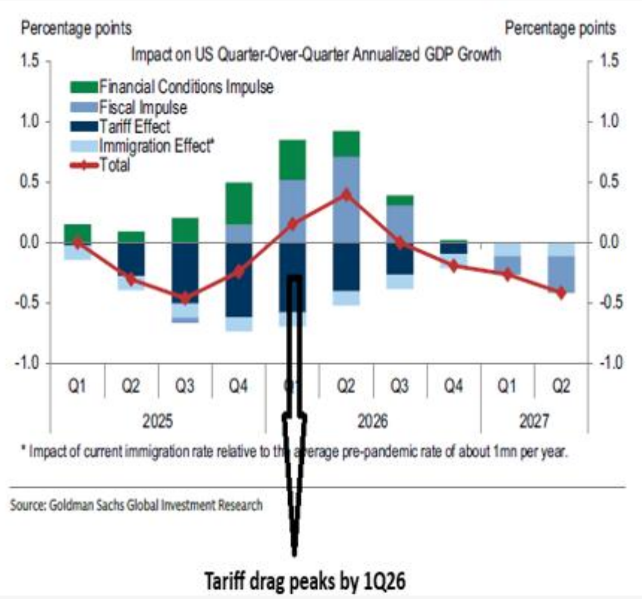
Source: Bloomberg

The drivers of growth in 2026 are expected to resemble those of 2025. AI-related capital expenditure remains the dominant force. Spending by hyperscalers alone is projected to rise 33% year-on-year to approximately US$660bn in 2026. Globally fiscal policy will also remain moderately expansionary, supported by higher defence spending across developed markets, the implementation of the One Big Beautiful Bill Act in the US, and a wider augmented fiscal deficit spending in China. Financial conditions are likely to ease further, although the rate-cutting cycle in most developed economies is approaching its end. More importantly, credit impulses are poised to turn meaningfully positive across the US, Europe and China. This reflects a combination of looser bank capital requirements, rising corporate loan demand, and continual government pump-priming. Meanwhile, the drag from US tariffs is expected to peak in the first quarter of 2026 at roughly -0.5%ar before fading sequentially thereafter.

DM policy rates to ease just a little more



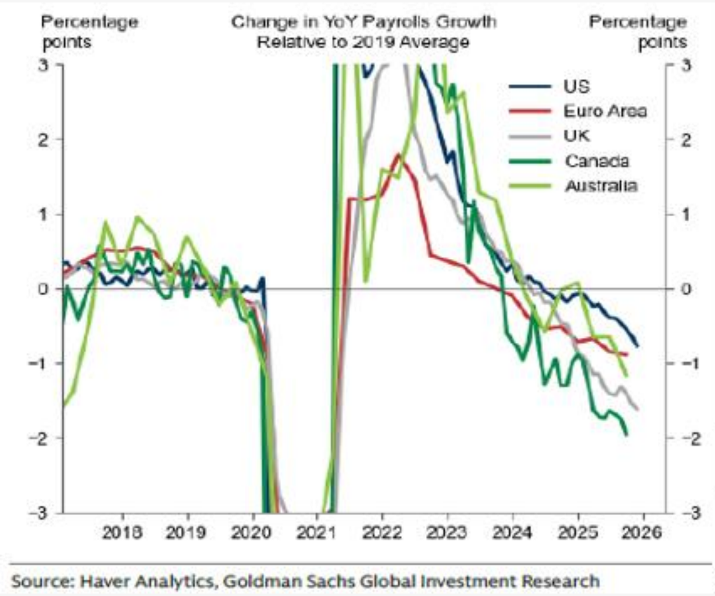
Tariff drags in the US fades after 1Q26



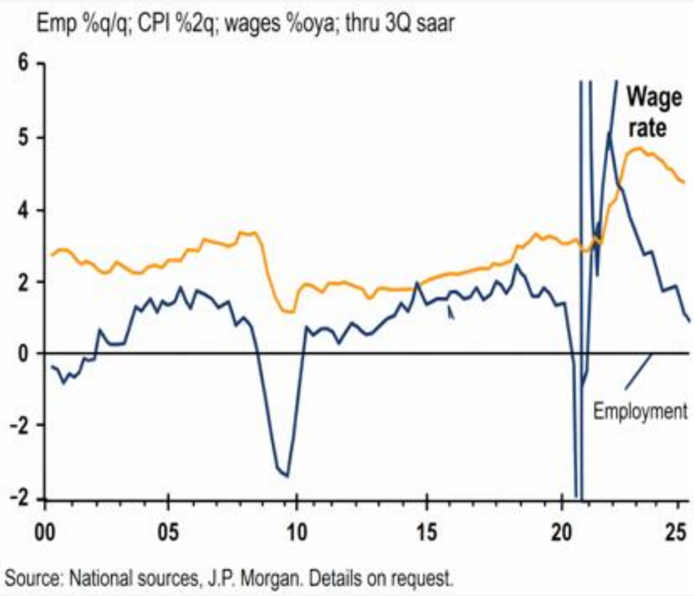
Yet beneath this constructive growth backdrop, labour market conditions have deteriorated noticeably. US non-farm payroll growth has been effectively flat year-to-date and has turned negative since June. The unemployment rate has risen to 4.6%, edging close to triggering Sahm's Rule — historically a reliable recession signal. Wage growth has slowed to 3.5% from 4% at the start of the year, while hours worked have stagnated, leaving aggregate labour income growth near zero.

This dynamic is not unique to the US. Employment growth across much of the developed world has rolled over relative to pre-pandemic levels, and unemployment rates have risen steadily since bottoming out two years ago. With wage growth stalling, job opportunities diminishing, and food inflation remaining elevated, risk of consumption slowing mounts.

DM employment growth rolled over



It is especially pronounced in the US



Markets have increasingly focused on the apparent contradiction: a weakening labour market alongside resilient growth. **The prevailing concern is that joblessness must inevitably lead to recession. We believe this conclusion is premature.**

A historical parallel can be found in the period between 1991 and 1993. During those years, non-farm payrolls contracted by 0.8%, unemployment rose from 6.4% to 7.8%, and wage growth slowed to below 3%. Despite this, real GDP expanded by 3.5% in 1992 and 2.8% in 1993. Non-residential fixed investment grew at a robust 7% pace, while productivity accelerated above trend to more than 3%. The Federal Reserve also provided substantial policy support, cutting rates by over 200 basis points. Equity markets responded accordingly, with the S&P 500 delivering a cumulative return of approximately 55% over the period.

That episode coincided with the large-scale deployment of personal computers and enterprise software. Rapid declines in hardware costs, the dominance of Windows 3.0, and the adoption of ERP and just-in-time business practices drove a surge in productivity — a textbook illustration of Jevons' Paradox.

We've seen it before: A jobless recovery growth in 1991-1993

	NFP Growth	Unemployment Rate	Real GDP	Non-res. Investment	Productivity	Fed Funds	S&P 500 Returns
1991	-0.90%	6.90%	-0.10%	-4.70%	1.00%	5.7%	30.5%
1992	0.50%	7.50%	3.50%	7.00%	3.00%	3.5%	7.6%
1993	1.30%	6.90%	2.80%	8.50%	0.30%	3.0%	10.1%

Source: BEA, BLS and Fed

The parallels with the current environment are striking. **From 2026 onwards, AI deployment is set to move decisively into the mainstream.** Just as the PC revolution reshaped productivity in the early 1990s, widespread adoption of AI is likely to lift output even as labour intensity declines. Estimates of the potential productivity dividend vary widely, but the direction of travel is clear. Across academic and sell-side research, estimates of incremental GDP gains range from US$1.2 trillion at the low end to as much as US$7 trillion by 2030. While the dispersion reflects differing assumptions, the implication is the same: productivity gains from AI could offset labour market softness for longer than markets currently assume.

Various research points to productivity improvement potentially lifting US GDP

	Productivity lift adding to US GDP by 2030
Morgan Stanley	$940 bn
MIT - Acemoglu	$1.5 trn
JP Morgan Private Bank	$2.5 trn
Stanford - Brynjolfsson	$7.0 trn

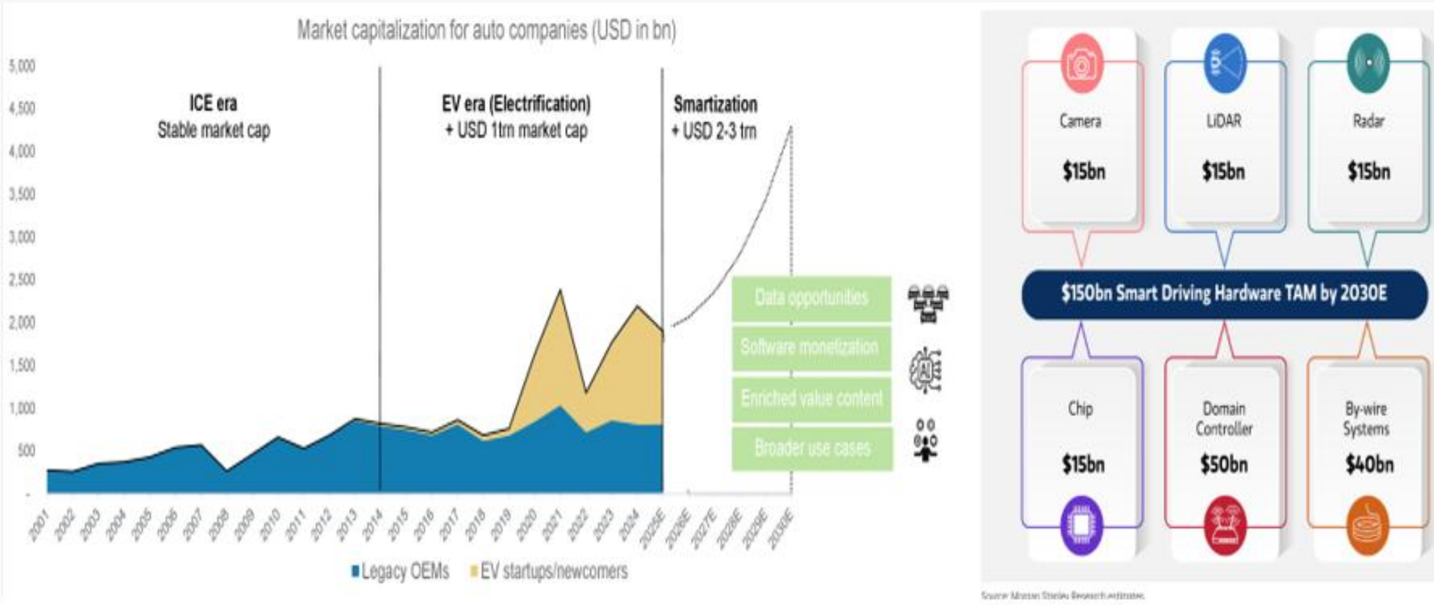
Topic 2: AI bubble?

Every speculative episode shares a familiar anatomy. Over-estimation of its usefulness, Over-leveraged, Over-owned, and Over-valued. Even when all four exist, the precise catalyst that ends a boom is rarely obvious. Still, this 'four Os' framework provides a disciplined way to assess where the risks are accumulating.

Over-estimating its usefulness? As we have shared in our outlook event a year ago, we believe the first use case of AI will come from productivity improvements rather than a killer app. We believe 2026 will mark the year of wide-spread enterprise adoption. The case of coding, customer services, and content creation as the early adopters are simple to comprehend, but this is the year, the more consequential shift is underway where the physical world interacts with generative AI.

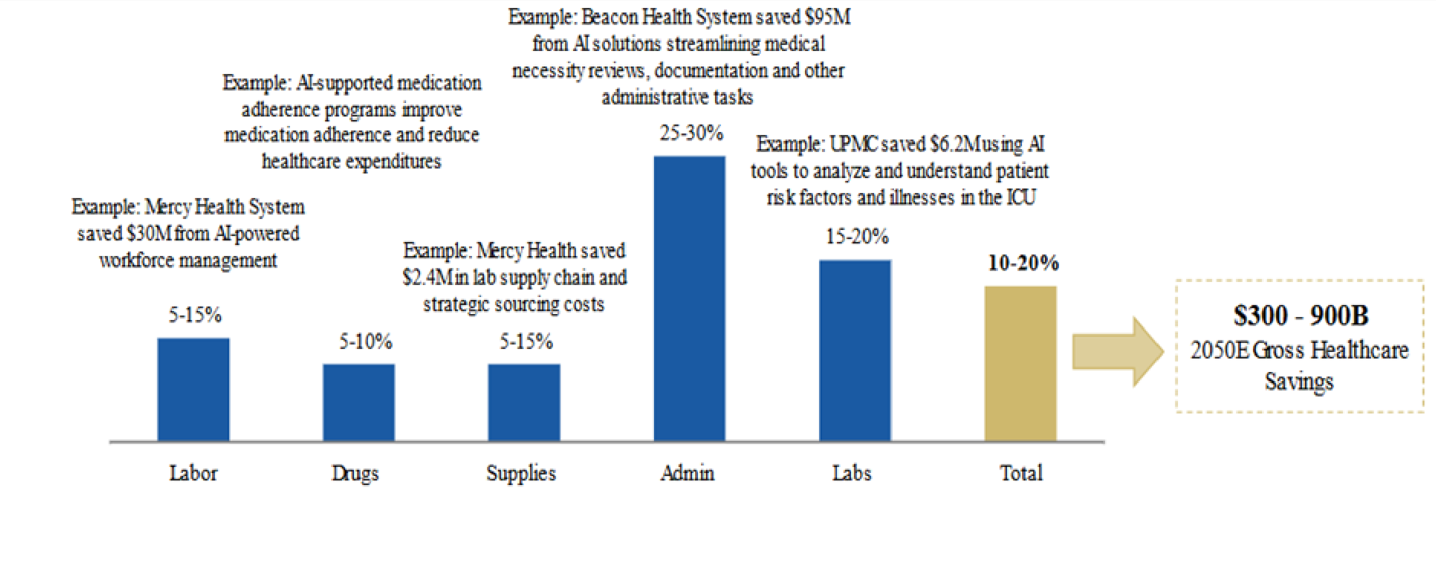
In manufacturing, we are moving from repetitive rules-based, to training based, and eventually to context-based robotics. 2026 will also mark the deployment of autonomous vehicles across many countries. The adaption of vision-language-action AI models will compress L4 driving technology curve. The advent of EV car has already added an extra of $1trn in market capitalization for the automobile market in the last 5 years. According to Morgan Stanely, the "smartization" of cars in the next 5 years could potentially add another $2-3 trn in potential market opportunities. Humanoid robotics will attract increasing attention as well, though we view large-scale deployment as a post-2030 story.

The evolution of automobile from transportation to smart vehicles



In the healthcare, the deployment of AI will come managing workforce and patient loads, improvement in workflows, and predictive analysis on inventory and patient care. Morgan Stanley estimates that 10-20% of cost savings can be accrued to cost of healthcare amounting to $300-900bn gross saving till 2050.

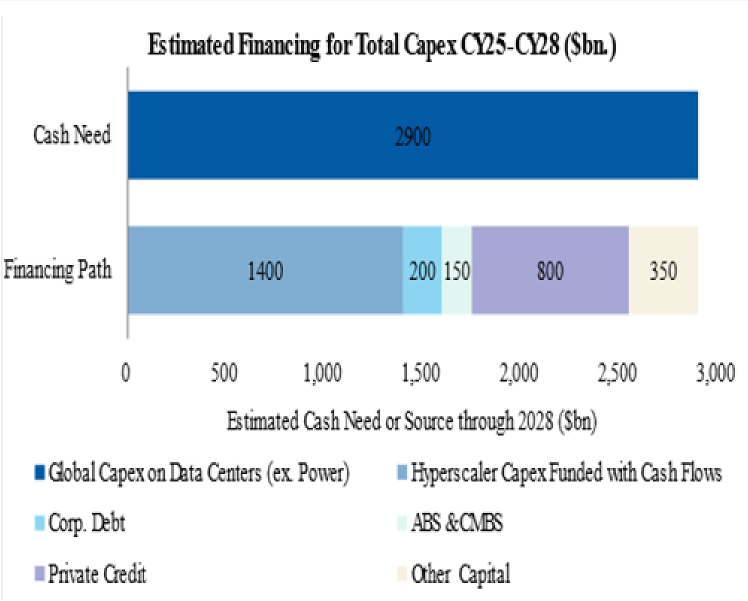
Potential cost saving of 10-20% in healthcare expenditure from AI



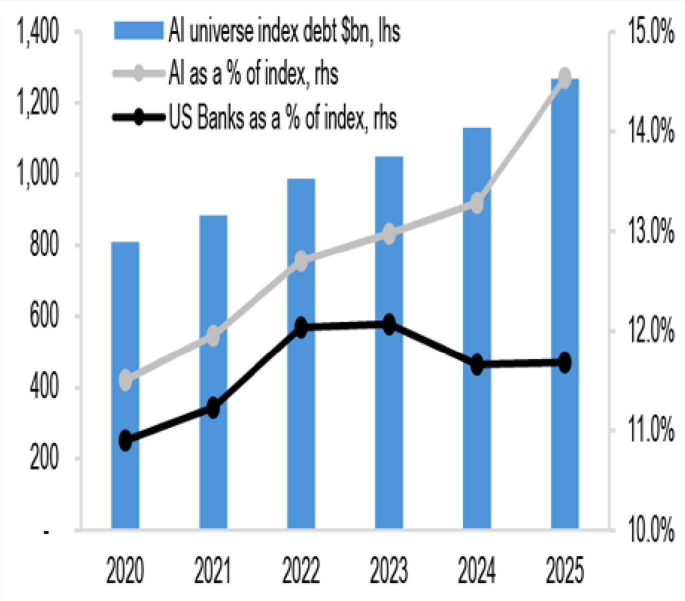
Source: Morgan Stanley Research.

Higher leverage but manageable: It is estimated that the total AI related capex will top $2.9trn by end of 2028. Half of that will be financed by the internal cashflow of these companies but the rest will be via the debt market through a combination of private credit and public debt markets. In fact, AI related debt issuances in 2025 dominates the investment-grade debt market and is now 15% of the market, larger than the second largest sector which is banks at 12%. It is appropriate for investors to gauge the vulnerability of these companies.

Half of capex will be funded by debt



Already has increased significantly



Source: Morgan Stanley and JP Morgan

Our analysis suggest gross gearing of this cohort of AI companies will increase from less than 30% in Jun 2025 to 37% by end of this year and peak at 50% in 2027 as their debt financing needs increase. But 50% gross gearing is not a significantly precarious level and if you factor that they collectively held $421bn in cash, their net gearing would have fallen below 40%. The interest coverage ratio will also decline from a high of 52x to 19x but at 19 times cover, that is also a significant buffer. Yes, leverage will increase but as a cohort they are not overly leveraged but some companies are more vulnerable than others, e.g. Oracle and Coreweave.

AI companies leverage will increase but not till threshold levels

Leverage Analysis	As of 3Q25	FY2025 (F)	FY2026 (F)	FY2027 (F)
Total Debt	536,109	524,773	674,773	1,124,773
New Total Debt	**536,109**	**674,773**	**1,124,773**	**1,574,773**
% Change		*26%*	*67%*	*40%*
Debt/Equity	**32%**	**37%**	**46%**	**50%**
Operating FCF Interest Cover	**51**	**27**	**22**	**19**

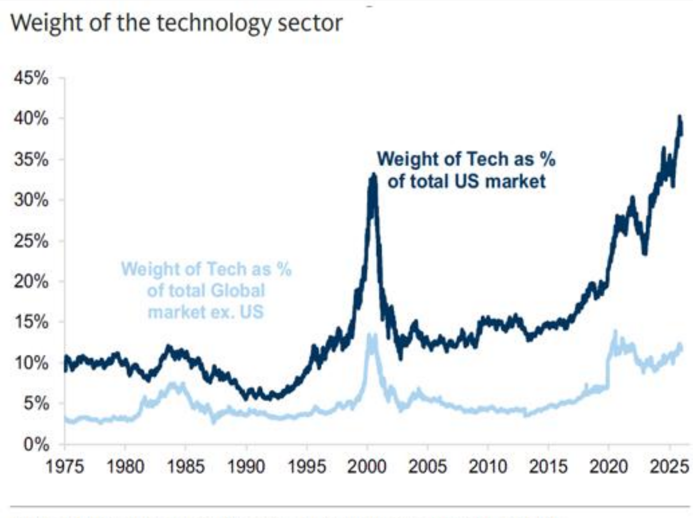
Source: Company reports and Bloomberg estimate

Cohort: Amazon, Google, Microsoft, Meta, Nvidia, AMD, Intel, Broadcom, Oracle, Coreweave

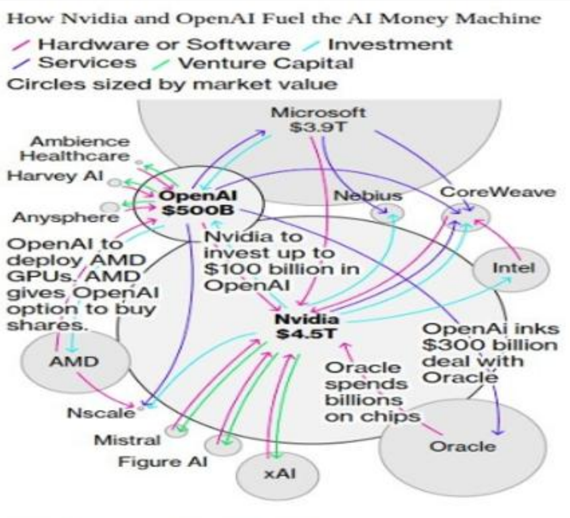
Over-owned for sure: Performance of the so-called 'Magnificent Seven' over the past three years, combined with their weight in major equity indices, has left investors heavily positioned. The same is true in VC/PE and private credit markets, where AI has become the dominant issuer.

More concerning is the web of circular financing arrangements emerging around OpenAI, echoing elements of vendor financing seen during the dotcom era. Nvidia, Oracle, AMD and CoreWeave are simultaneous suppliers, financiers, and stakeholders. While this creates concentration risk, it is also highly visible. By definition, black swan events are rare, impactful, and unpredictable. AI is clearly impactful, but given the intense scrutiny, it will not be easy for the vulnerability of OpenAI or others to be concealed within the hype and become unpredictable and an unknown risk.

Definitely over-owned by investor in both private, debt and equity markets



Source: Datastream, Goldman Sachs Global Investment Research



Source: Bloomberg News reporting

We do not agree that the AI-related names are over-valued. AI-related equities are not cheap, but nor are they obviously overvalued. As a cohort, they trade at 24x 2-years forward PE however their median net income margin is 33% and generates ROE in excess of 25% (except Telsa) and most are net cash companies (except Broadcom). In the last 3 years, their 264% rise share price was supported more by EPS growing 135% in the same period than valuation expansions.

AI cohort isn't cheap but they have strong performance metrics:
High ROE and margin, Net Cash, Share price driven more by EPS growth

	24M fPE	ROE	Net Income Margin	Net Debt/Equity	3Y Price Change (%)	3Y EPS Change (%)	3Y PE Change (%)
NVIDIA CORP	20.0	105%	54%	-65%	1185%	1569%	-23.0%
APPLE INC	29.0	164%	27%	-11%	113%	35%	58.5%
MICROSOFT CORP	23.8	32%	37%	-22%	108%	65%	26.1%
ALPHABET INC-A	24.5	37%	34%	-17%	258%	100%	79%
AMAZON.COM INC	23.7	26%	12%	-12%	177%	235%	-17.4%
META PLATFORMS INC	19.9	32%	31%	-5%	457%	190%	92.1%
BROADCOM	25.5	33%	37%	62%	555%	169%	143.0%
TESLA INC	159.0	7%	6%	-21%	269%	-59%	800%
Median AI cohort	**24.1**	**33%**	**33%**	**-15%**	**264%**	**135%**	**69%**

Source: Covenant Capital

Dot-com cohort traded double the forward PE of AI, earns half the margin
and was driven more by PE revaluation

	24M fPE	ROE	Net Income Margin	Net Debt/Equity	3Y Price Change (%)	3Y EPS Change (%)	3Y PE Change (%)
MICROSOFT CORP	53.2	35%	39%	-63%	364%	191%	59%
CISCO SYSTEMS	101.7	22%	17%	-17%	1346%	118%	562%
INTEL CORP	42.1	26%	25%	-33%	281%	34%	184%
ORACLE CORP	84.6	39%	15%	-61%	811%	123%	308%
IBM	23.5	39%	9%	111%	252%	40%	152%
Lucent	37.9	36%	9%	38%	376%	111%	126%
Nortel Networks	86.4	-1%	-1%	-3%	682%	172%	187%
Median Dot-Com	**53.2**	**35%**	**15%**	**-17%**	**376%**	**118%**	**184%**

Source: Covenant Capital

When we contrast the dot-com era cohort, they traded at even more expensive level of 54x forward PE, earned half the net income margin than the AI group, and their share price appreciation of 376% were driven more by multiple revaluation (184% jump) than EPS growth.

Topic 3: By far the most pressing topic: will the Fed independence be challenged and how will the markets react?

The most important lesson I learned as investor of 30 years' experience is that no housing and financial institutions collapses, frequent boom-bust of oil, and not even a once-in-lifetime global pandemic and can reverse a bull market except that of a hawkish Fed and a commiserating rise in yields.

We do not claim expertise in US constitutional law. **Our task, as investors, is more prosaic: to identify, quantify and price risk. The focal point is the pending Supreme Court case, Trump v Slaughter, with a ruling expected in the second half of 2026.** A judgement in favour of a broader interpretation of 'for-cause' termination would materially expand presidential authority over independent agencies, including the Federal Reserve. Such an outcome would also set precedent for the related Trump v Cook case, potentially allowing the President to remove sitting Federal Reserve governors. While these scenarios remain uncertain, they are no longer theoretical and warrant close monitoring.

The Federal Open Market Committee comprises seven governors. Four of whom were nominated by President Trump and alongside a rotating cast of regional Federal Reserve presidents that does not need to be nominated or approved by Trump. Chair Jerome Powell, himself a Trump nominee, is expected to step down upon the completion of his term. Governor Miran is departing, while Governor Cook faces the risk of removal pending legal outcomes.

Therefore, the composition of voting regional presidents in 2026 should introduces a counterweight to heavy handed political influence. Traditionally dovish voters will rotate out, replaced by more hawkish figures such as Kashkari, Logan, and Hammack. Williams of New York and Paulson of Philadelphia are regarded as centrists. The net effect is a committee in which pro-easing influences may increase but are unlikely to dominate.

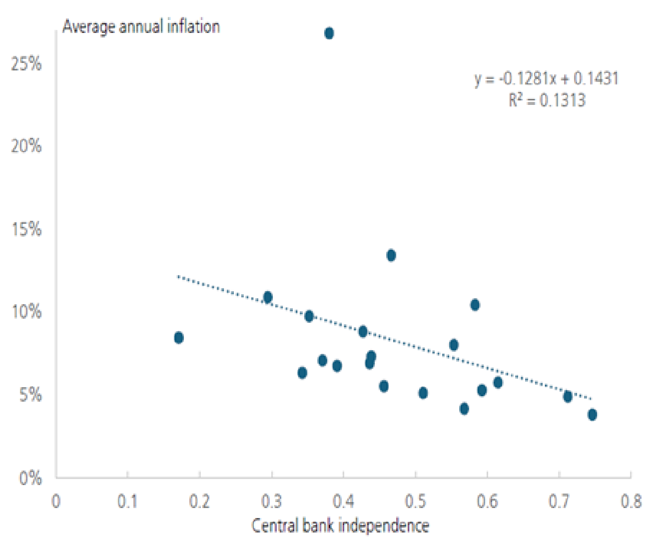
The state of play in FOMC voting in 2026

	Doves	Centrist	Hawks
Governors	**Miran** (Leaving, Trump Nominee) **Cook** (Trump threatening to fire) **Bowman** (Trump nominee) **Waller** (Trump nominee)	**Powell** (Term ends 2026, rumoured to be leaving) **Jefferson** (Biden nominee) **Barr** (Biden nominee)	
Regional Presidents		**William** (NY President is permanent member)	**Hammack** (Incoming) **Logan** (Incoming) **Kashkari** (Incoming)

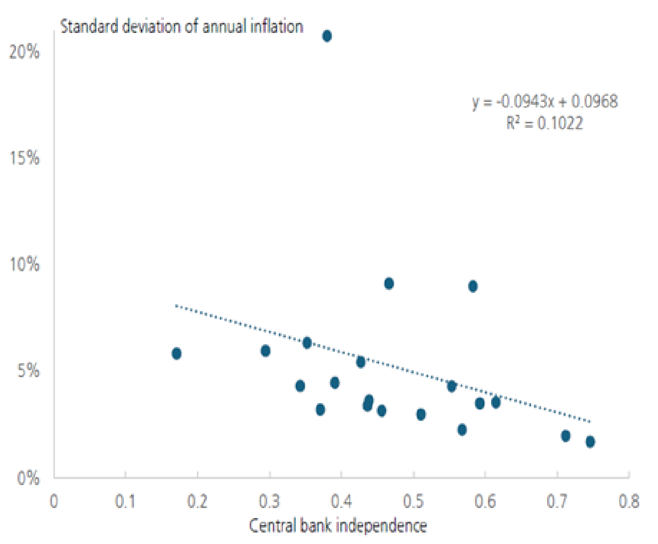
Source: Federal Reserve Board

What does it mean if Fed does losses its independence? Empirical evidence suggests that greater central bank independence is associated with lower and less volatile inflation. Freed from short-term political pressures, central banks are better able to execute their mandates credibly. Conversely, political interference has historically been linked to higher inflation volatility and, paradoxically, higher long-end bond yields. While short-term rates may be temporarily suppressed, investors demand compensation for diminished policy credibility.

Greater independence of central banks lower inflation and the volatility of it



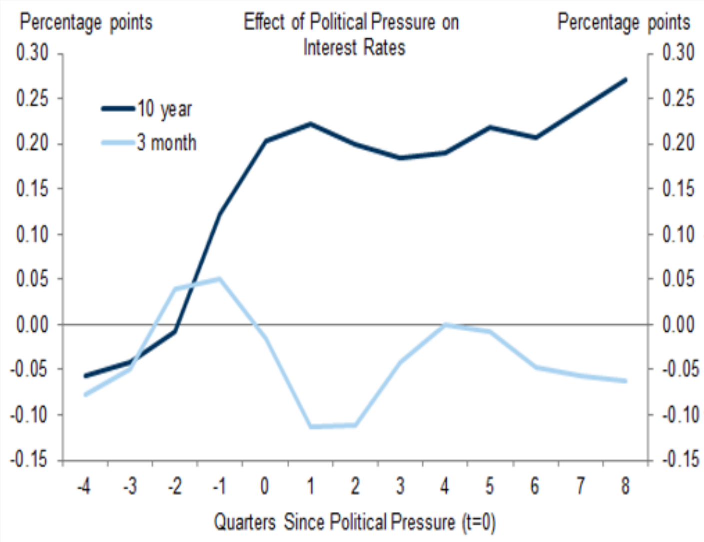
Source: Romelli (2025), OECD, Haver, UBS



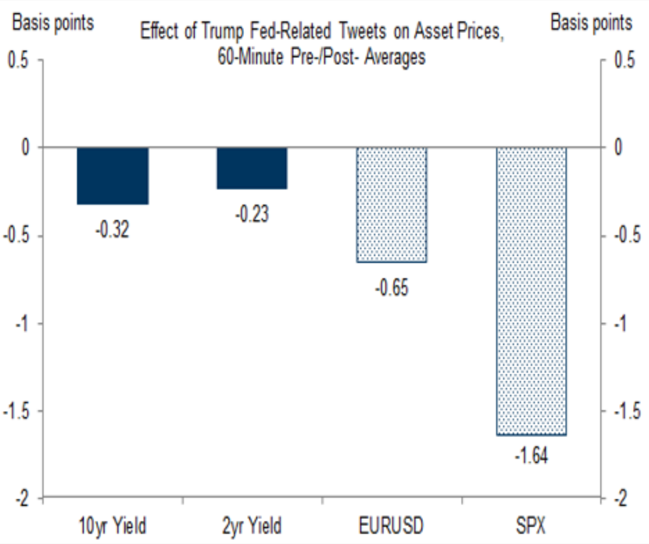
Source: Romelli (2025), OECD, Haver, UBS

However, it must be noted both studies have limitations as central banks have in general become more independent in the past decades and the central banks that have been perceived to have lost their independence were mostly emerging economies, not a developed country like the US.

Higher long-end rates when CBs are pressured



-ve reactions when Trump tweets rates



Source: Goldman Sachs

But perhaps, the impact could be far worse for the US? We are already experiencing this in the recent Fed easing cycle. Historically, when a Fed eases. 10-year yield typically falls, [The Rare Ones](). However, the 10-year and 30-year yields have risen by 10bps since Fed resumed its easing in September. If political pressure intensifies alongside a widening fiscal deficit, the risk is a steeper curve driven by rising term premia even as policy rates are pushed lower. **There is the risk that Trump's meddling of Fed's dual mandate could eventually stoke higher and more volatile inflation pathways.** It is not our base case, but it is a risk investor must monitor.

Asset Allocation Strategy

The macro set-up remains conducive for risk assets with growth expected to be trend like. We expect inflation to trend lower albeit still above central bankers above 2% target rate, but the path of policy rate will diverge in 2026. ECB has signalled the end of their easing cycle as inflation is re-anchored to target and growth risk has eased. BOJ needs to hike further as inflation is entrenched. BOE has reverse course from hiking to cutting rates recently citing growth risk outweighs inflation. PBOC will use more off-balance sheet tools than cutting rates outright. Critically, we are out of consensus in our belief that the Fed is near the end of this easing cycle.

This put most economies in the recovery part of the investment clock favouring equities, commodities and hedge funds over bonds and cash.

Macro regime matters and determines asset allocation mix

Regime Returns	Cash (%)	Equities (%)	Bonds (%)	Commodities (%)	Hedge Funds (%)
Reflation	4.4	10.7	9.8	-6.7	10.6
Recovery	4.9	17.2	5.9	16.2	13.9
Overheating	1.8	9.2	7.1	20.0	7.6
Recession (Stagflation)	6.5	- 9.5	7.4	- 10.8	4.4

Source: NDR, Bloomberg 1972 -2025; Hedge Fund proxy Managed Futures 1987-1996, CTA Dec 1979- 2025

Overweight Equities: The broadening of the bull. The common pushback for equities has always been valuation is steep. We have argued in various publications of the Navigator, I'll be back, a starting point of high valuation does not mean negative returns in the year ahead. There are 2 key preconditions to overcome the vulnerability of expensive markets. First, EPS growth needs to be positive and second, arguably more important, earnings revision momentum needs to be positive. Case in point, at the start of 2025, S&P was expensive at 22x forward PE or +1.5sd to its ten-year average but it still returned 19% last year. Consensus forecasted EPS to grow 9% at the start of the year, and aside from the momentary post Liberation Day revision downgrade, EPS was consistently upgraded throughout the year and is likely to end the year at 11-12% yoy. If you have been a miser, eschewing returns on the ground of steep valuation, you would have missed out 48% returns in the last two years.

SPX been trading above +1sd PE bands but ROE is 35% higher now

Source: Bloomberg

EPS growth across all regions are forecast to be strong with the US markets leading in both growth and earnings revision momentum. However, the growth differential between S&P and MSCI World is set to narrow this year at +2% compared to previous years of 4 to 5% ppt higher. EM markets look particularly attractive from growth, PEG and ERM but overall, we will be taking lesser regional bets preferring to diversify and let bottom-up selection dictate regional compositions.

Strong EPS growth across and ERM profiles but S&P growth lead narrows

	EPS Growth 2026	EPS Growth 2027	2yrs EPS CAGR	PE 2026	PE 2027	PEG 2026	3mth EPS Revision (2026)
MSCI World Equities	13%	12%	12.7%	19.1	17.0	1.45	1.3%
S&P 500	15%	14%	14.5%	22.3	20.9	1.49	2.7%
NASDAQ	21%	15%	18.0%	28.4	23.7	1.35	4.4%
MSCI Europe	10%	10%	9.9%	15.3	13.9	1.61	0.3%
FTSE 100	9%	13%	10.7%	13.3	11.8	1.56	2.2%
TOPIX	10%	9%	9.5%	16.3	14.9	1.61	3.5%
MSCI China	12%	15%	13.6%	12.2	10.6	0.99	-1.3%
MSCI Emerging Markets	18%	14%	15.7%	13.2	11.7	0.74	4.3%

Source: Bloomberg

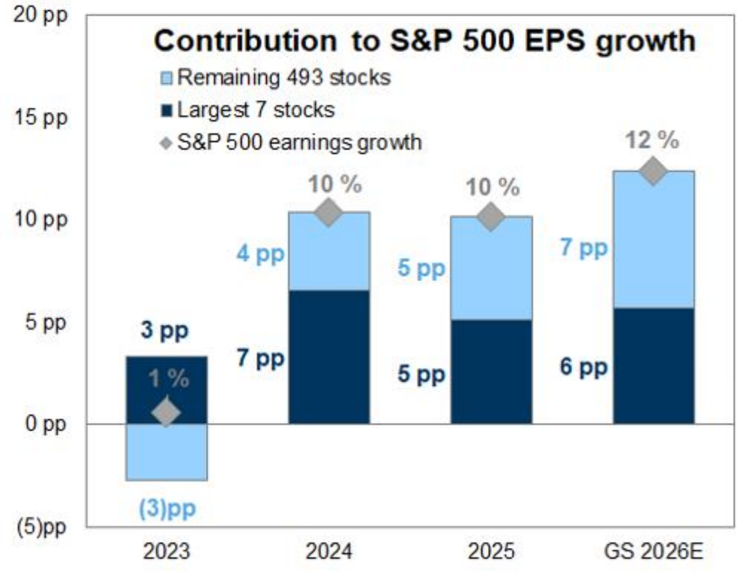
At the US sector levels, we are also seeing a broadening of growth drivers. While still dominated by tech sector, 9 out of 11 GIC sectors will post 2 years EPS CAGR of more than 10% with cyclical sectors like materials, consumer discretionary, and industrials posting growth above 13% in the next two years. If we narrow down to the Mag 7 versus rest of S&P 493, their dominance will also recede in the coming two years. The broadening of growth across regions and sectors provides a larger pool of investment picks beyond the confined narrative of everything AI. All good characteristics of a sustained bull.

Broadening growth profile = richer stock picking pool

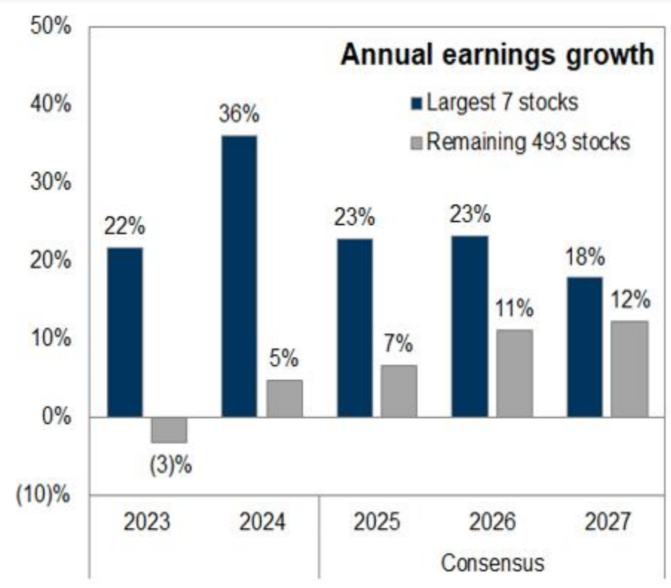
	EPS Growth 2026	EPS Growth 2027	2yrs EPS CAGR	PE 2026	PE2027	PEG 2026	3mth EPS Revision (2026)
Healthcare	9%	11%	10.0%	18.7	16.8	2.08	0.0%
Utilities	11%	11%	10.7%	17.8	16.0	1.62	0.1%
Consumer Staples	6%	8%	6.9%	21.0	19.4	3.49	-0.3%
Consumer Discretionary	11%	16%	13.1%	29.2	25.3	2.75	-0.5%
Technology	27%	19%	23.1%	26.8	22.6	0.99	9.7%
Communication Services	9%	13%	11.1%	22.4	19.8	2.49	0.9%
Financials	8%	8%	8.0%	16.9	15.6	2.11	2.1%
Industrials	14%	14%	14.0%	24.2	21.2	1.73	-0.6%
Energy	9%	15%	12.0%	15.8	13.6	1.76	-4.8%
Real Estate	15%	7%	11.1%	18.6	17.3	1.24	-1.1%
Materials	18%	14%	15.8%	19.5	17.2	1.08	1.7%
S&P 500	**15%**	**14%**	14.5%	**22.3**	**20.9**	1.49	**2.7%**

Source: Bloomberg

Mag 7 growth contribution narrows and decelerates



While rest of 493 growth accelerates

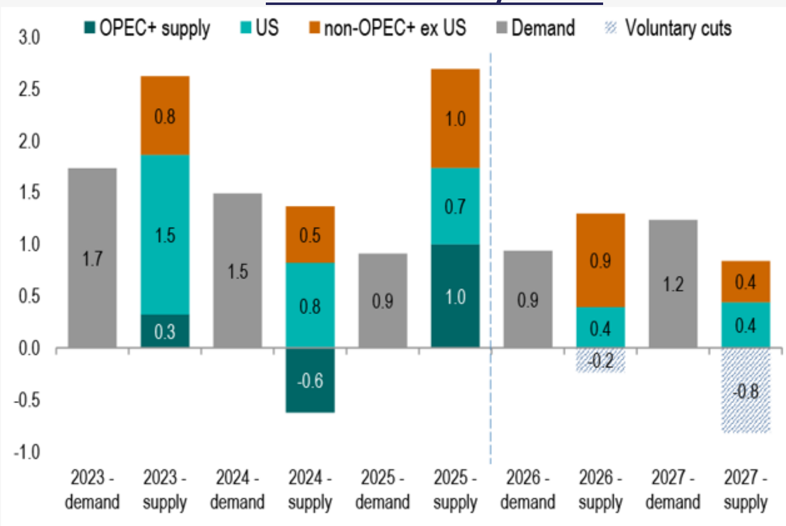


Source: Goldman Sachs

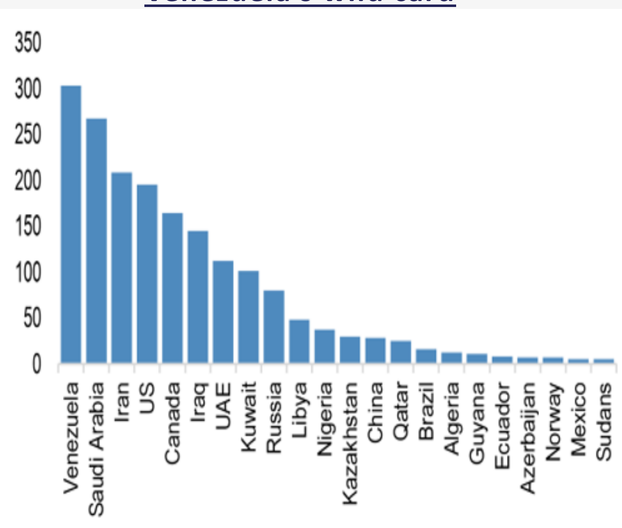
We prefer sectors with both value and growth, coupled with endogenous upside catalysts such as financials (greater regulatory forbearance, higher loan growth, and margin expansion), healthcare (under-valued, under-performed but with streams of clinical wins, drug launches, AI-innovation, and end of managed care and drugs repricing risk). In the tech space, we will be more discerning; think inferencing over training, TPUs over GPUs, SRAM over HBM memory, underperforming software over semiconductors. Industrials will be another area we will be looking into as Trump has delivered reshoring initiatives many past Presidents have pledged but failed to do so.

We have held utilities, Who really knows? as a 2nd derivative play on AI for a while now when it was an anti-consensus trade but we believe political headwinds will increase as cost of electricity has become a mid-term election issue. The sector's valuation is no longer attractive, consensus EPS estimates could be too high, and with Fed at the end of its easing cycle, the added impetus of lower rates for a highly geared sector will fade too. Instead, we are looking into another contrarian trade in energy names on the back of earnings inflecting higher to 12% CAGR in the coming two years versus morbid low growth seen in the past two years. The supply glut that has pervaded the industry in last few years could start normalising by 2H27. Trump's recent audacious kidnapping of Venezuela's President should be view through the prism of both risk and rewards. There is risk is that in the medium term, Venezuela supply could flood the market up-ending current forecast of supply balance by 2027, but it could also be viewed as larger production therefore higher revenues for US oil majors.

Oil in balance by 2027?



Venezuela's wild card

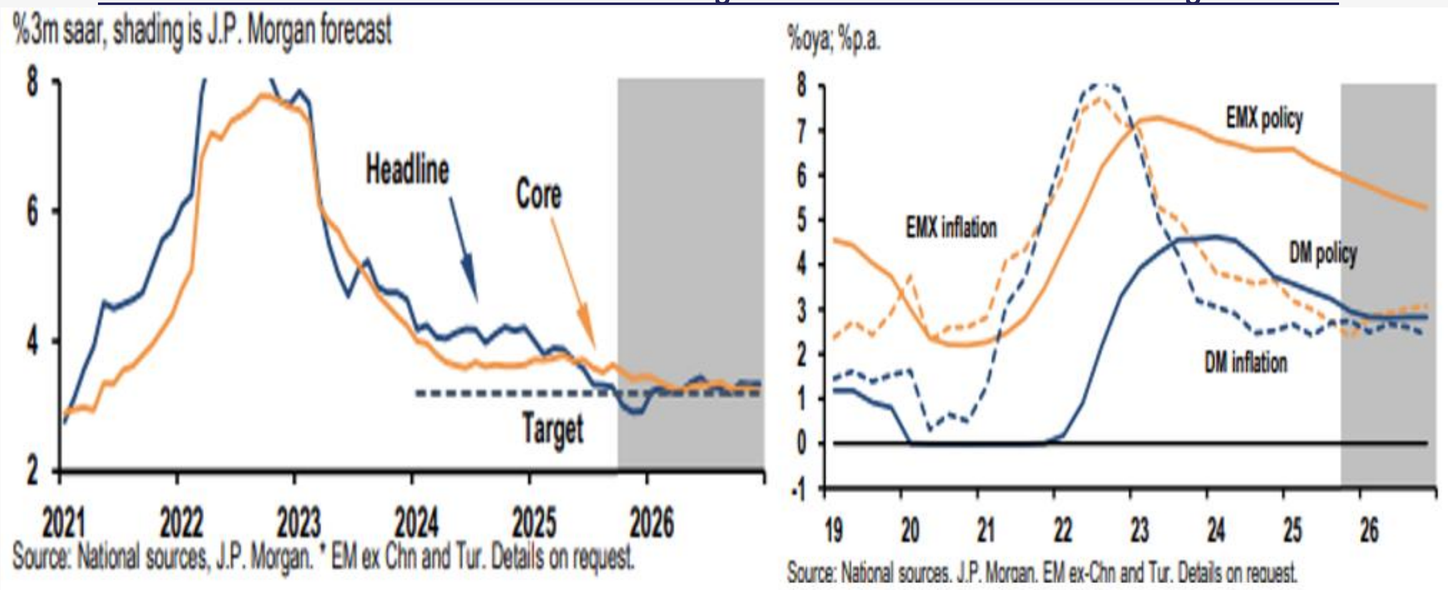


Source: JP Morgan, Goldman Sachs

Fixed Income: Underweight but still an adequate carry to be earned. We believe we are in a shallow Fed easing cycle and do not agree with market expectation of 3 cuts in 2026. The economy is unlikely to head into a recession even as the labour market weakens. The K-shape consumer market means a cautious lower-income consumers, but with middle to high-income consumer experiencing positive real wage growth, higher equity and property values, a large-scale consumption contraction is unlikely. We believe productivity improvement will be evident in the coming 2 years as physical AI takes root across many industries counterbalancing negative immigration flows. Animal spirits evident in the IPO market, higher loan demand, and industries reshoring has put US capex growth at one of its highest levels in a decade.

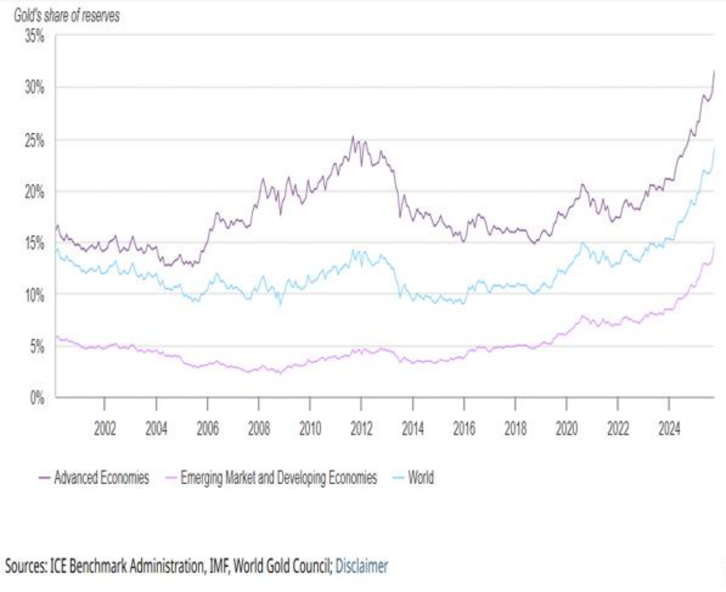
Taking cue from our empirical research, in a **shallow cut scenario, 10-year yields is broadly unchanged, curves flatten marginally, and credit spreads narrow modestly. Our range for US10 yield for 2026 is from 3.80% to 4.20% if a recession is avoided, therefore keeping our duration neutral. We continue to favour emerging markets debt over developed markets.** Emerging market economies have demonstrated resilience through a period of pronounced trade policy uncertainty and external shocks. Growth in 2025 has exceeded trend, supported by stronger than expected exports, AI related demand for manufactured goods, and a more gradual implementation of US tariff measures. At the same time, subdued domestic demand and contained wage growth have kept inflation pressures manageable, leaving real interest rates elevated and creating a supportive environment for bondholders as central banks have been able to ease policy without undermining price stability. Looking into 2026, emerging market growth is expected to remain close to trend, with inflation broadly anchored near targets and monetary policy still accommodative.

Prefer EM debt as EM inflation close to target and has more room for easing than DM

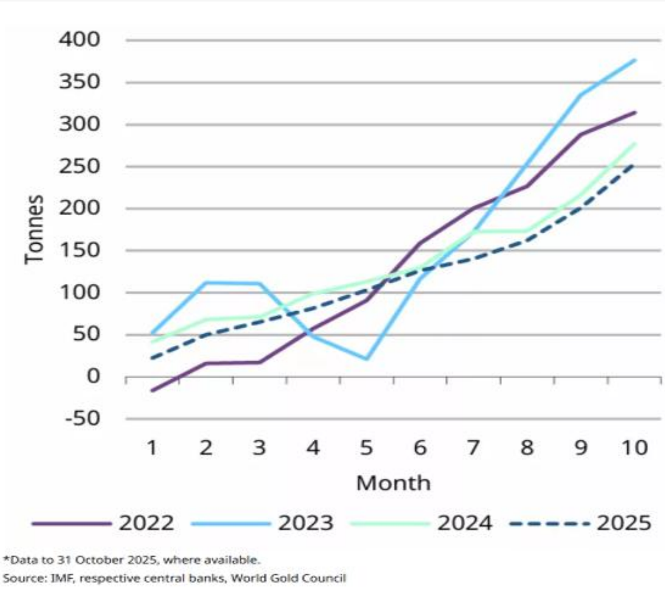


Commodities: Our preference for Bitcoin versus Gold in 3Q25 was premature with the latter powering to all time high but Bitcoin return negative -6% for the year. With Fed and several developed economies nearing the end of their easing cycle, the appeal for fiat alternatives such as gold and bitcoin should wane. There are 2 headwinds for both asset classes and we have reduced exposures in both. We have advocated owning gold as hedge against inflation, dollar hegemony and especially after the world sanctioned and froze all Russian assets in the 2nd invasion of Ukraine spurring many countries to reconsider the dollar holdings in their reserves. We believe this switch has largely occurred with many economies now holding the largest percentage of gold in their reserves in more than 30 years. This is evident when we look at their purchases in the last 6 months where they have slowed down and are more price sensitive. The entire push past our target of $4000 in the last 4 months is driven by easy and speculative money flows into ETFs which could easily reverse if there is a peace dividend in Europe.

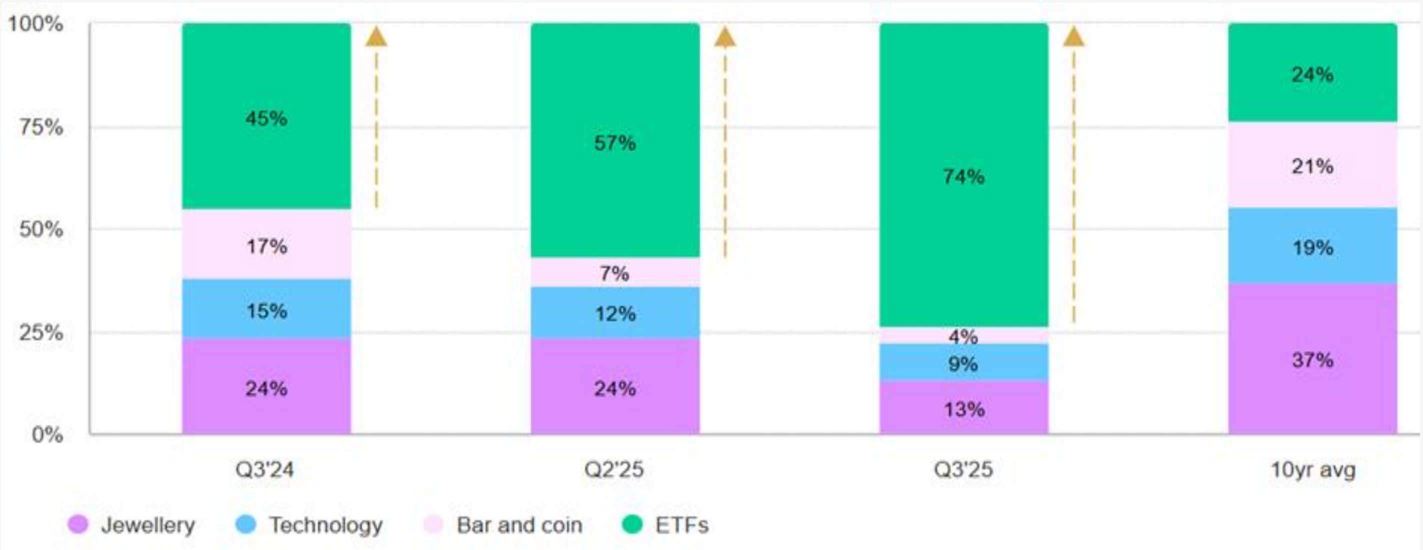
CB's gold reserves highest in 30 years



Still buying, but lesser



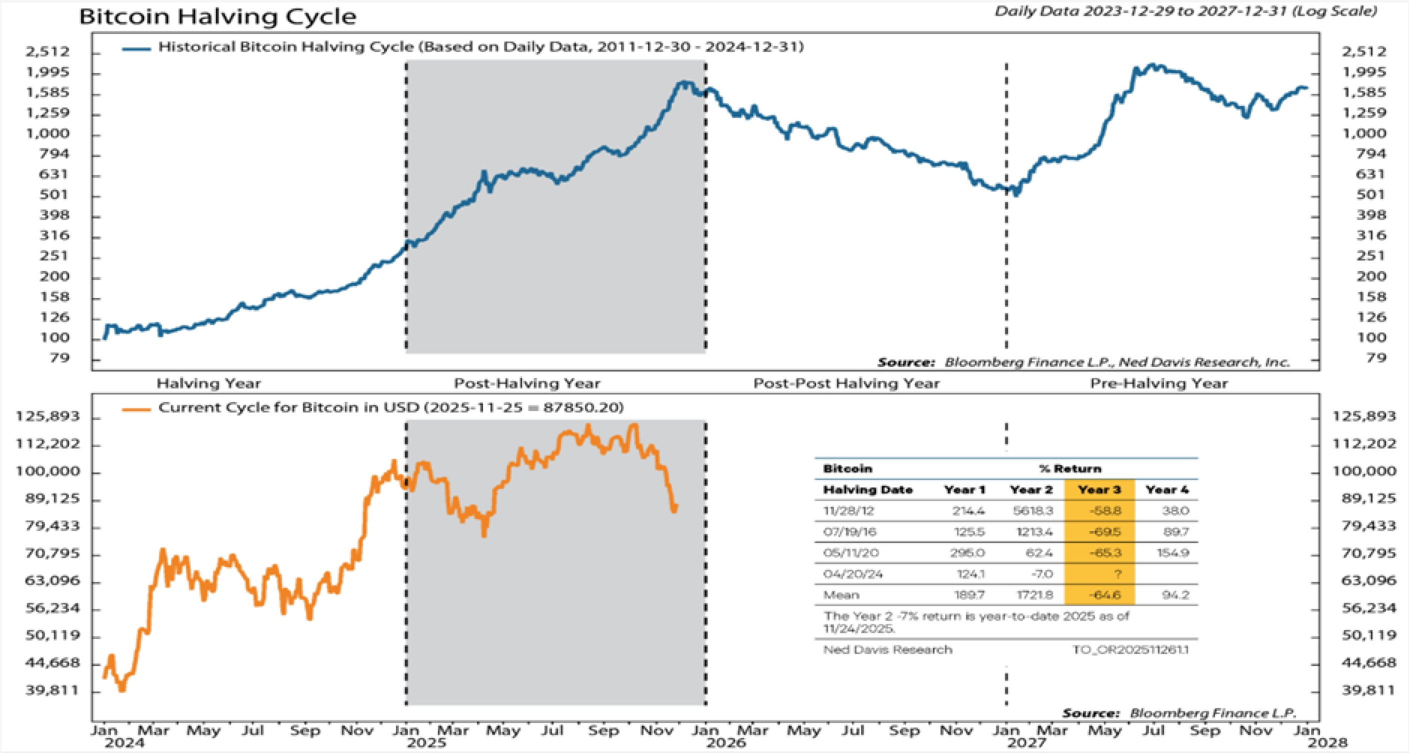
ETF purchases in 3Q is 74% of demand: Be careful of fast money



Source: World Gold Council

Typically, year 3 post bit-coin halving event, the price of bitcoin fell more than 60%. We have previously contended Bitcoin can escape the scourge of post halving Year 3 blues given widespread institutional interests and bouts of hedging characteristic it as exhibited. But looks like history is repeating itself with bitcoin correcting 31% since it peaked in Oct and is at risk of another -40% correction if history serves as a guide.

Bitcoin: Can't escape the curse of the Year 3 halving cycle



Source: NDR

Alternatives: No change with 30% allocation to hedge funds. We continue to advocate for hedge funds over all sub-classes of alternatives from the angles that returns are comparable when one adjusted for leverage in PE funds, better liquidity terms, and more transparent mark to market. The holding in our one-stop fund of hedge funds solution have provided an alternative stream of returns that has quintessentially been low beta to equities and almost no correlation to bonds.

Cash/FX: Will be nimble with cash holding even as we espouse a constructive view because history can humble us. Three historical cues to keep in mind. There have been few bear markets (more than 20% drop peak to trough) outside of a recession, but for the few times it did, it occurred between 37 to 49 months of an ongoing bull market. This bull market is 36 months long now. Second, since 1949, 4 out of the 7 cyclical bull market, the Year 4 returns were negative from -0.4% to -15% in that year. Third, **in every of the year 4 bull market, drawdowns are expected and can be large.**

Not unusual to expect large drawdown and negative return in Year 4 of bull market

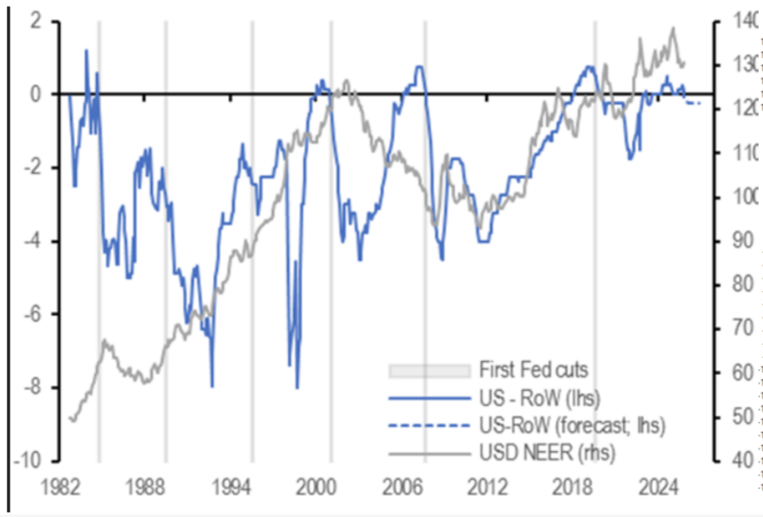
Bull start	Positive Returns in year 4	Full Year, Year 4 Return (%)	Max Drawdown in Year 4	Prior 3 years Cumulative Return
6/6/1949	No	-2.1	-15	81
26/6/1962	No	5.5	-21	56
24/7/1984	No	-14.8	-31	126
11/10/1990	Yes	-0.4	-9	56
9/10/2002	Yes	14	-8	53
3/10/2011	No	-1	-7	79
11/2/2016 *	Yes	23.9	-33	48
Current Bull market (Jan '23)	?		86	86

% of Positive Year 4 Returns	43%
Median Year 4 Returns	-0.4
Median Negative Year 4 Returns	-2.1
Median Max DD in Year 4	-15
Median Positive Year 4 Returns	14.00

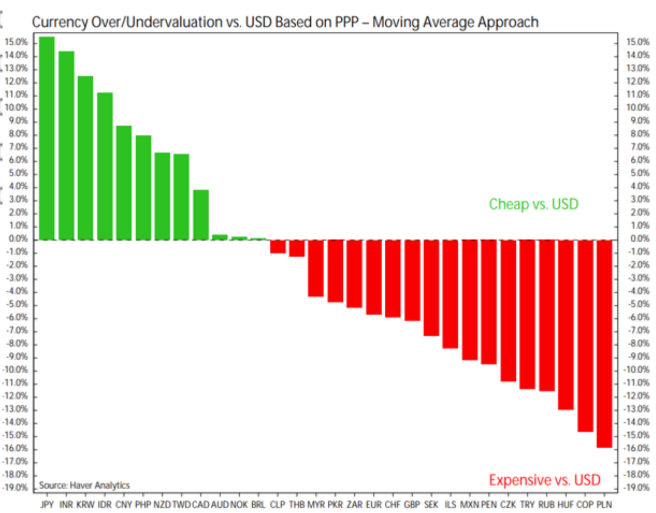
Source: NDR * 2016 bull market: year 4 was covid

We capitulate on bullish Yen trade. Even as USD-Yen yield spread is now at the narrowest since 2022 and should precipitate to a stronger Yen. The spectre of rising fiscal deficit spending aggravating Japan already the highest debt/GDP ratio amongst developed economies and a reluctant hawk in BOJ has truncated this relationship. On the other hand, we believe the bout of dollar weakness, the worst decline since 2003, is near the end and would be cautious to embrace the widely held consensus call for more dollar weakness. Dollar carry is now the near its four-decades high and on a purchasing-power parity basis, the list of currencies that are more expensive than the USD has increased from our last update. The Pound, Euro, Swiss Franc are 5 to 7% more expensive than the USD.

USD Yield spread at 4 decades high



USD is cheap relative to its majors



Source: JP Morgan and NDR

Featured Picture/Quote:

AI slop is the second-best thing that's happened to the Internet in a long time.

Edward Lim, CFA

Chief Investment Officer

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Risk Disclosure