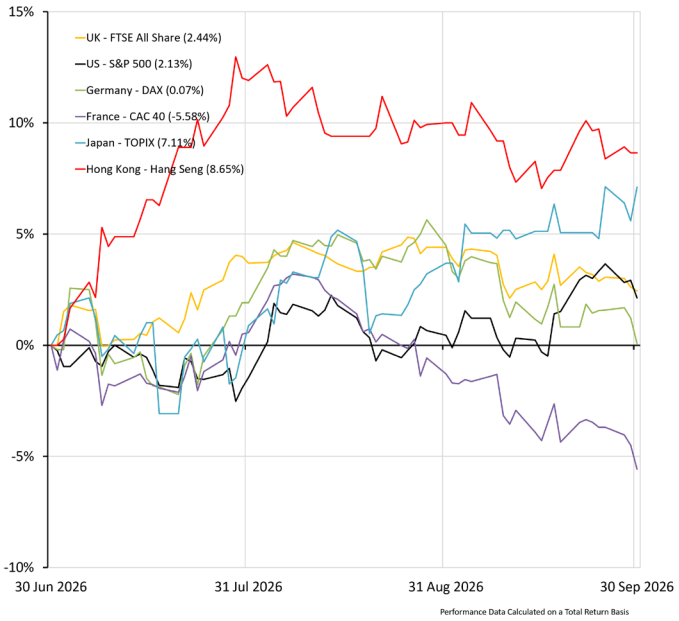
AUTUMN OUTLOOK

REVIEW OF THE PAST QUARTER:

High oil prices and the AI-driven tech rally shaped markets this quarter. The tech rally continued but regional equities diverged and there was considerable volatility – particularly in South Korea where tech companies dominate the market. Oil climbed back above $100 a barrel as the Persian Gulf remained largely closed to shipping. Fighting intensified in September further restricting exports from the region. The price of fuels such as diesel and jet fuel climbed faster than crude oil.

High oil prices meant energy was the best-performing equity sector in the US, UK, Europe and Japan. The global AI race continued but concerns over valuations saw Japanese tech stocks drag the broader market to a loss. Emerging markets also declined as Indian equities were hindered by high energy costs and Korean tech companies tumbled from very high valuations. Other developed markets fared better as solid second-quarter earnings in the US and Europe offset geopolitical worries. Value stocks beat growth stocks around the world as investors rotated to safety, a shift that helped the UK outperform.

High energy prices and rising food and transport costs have pushed up inflation expectations, and the world's major central banks have started to increase interest rates. This pushed government bond yields to multi-decade highs as government bonds fell with European government debt hit hardest. High-yield bonds held up better but still fell as corporate and government bonds struggled with difficult conditions for fixed income assets.



ASSET CLASS RETURNS

Cash	Government Bonds	Index Linked Bonds	Corporate Bonds	UK Equities	Overseas Equities	Emerging Markets	Property
+0.95%	-0.75%	-1.71%	+0.01%	+5.13%	+1.67%	-1.79%	+1.02%

THE ANALYSTS' VIEW:

Continued fighting in the Middle East means traffic through the Strait of Hormuz is likely to remain below pre-conflict norms for a sustained period and oil prices are expected to remain high this year, before falling back in 2027. Inflation is expected to peak in this year (although far below the level of 2022) and this is unlikely to trigger broader second-round inflation impacts. Central banks will be reluctant to allow another extended period of above-target inflation, but most will keep interest rates on hold for now. As inflation peaks major central banks such as the Fed and ECB will pivot towards cutting gently.

We expect geopolitical uncertainty to persist, adding to volatility and downside risks. There will be no meaningful thawing in US/China relations and that the US will continue to impose larger tariffs on China. The rest of the world will continue to be subject to smaller, but still substantial tariffs and global trade will decline as a share of GDP as President Trump continues to use tariffs to drive policy goals.

WHAT TO LOOK FOR IN THE NEXT QUARTER:

- **UK:** Bank of England interest rate meetings on 5 November and 17 December. Monthly consumer inflation figures due on 21 October, 18 November and 16 December. GDP growth for the third quarter is due on 12 November. The Autumn Budget is on 28 October.
- **US:** Federal Reserve interest rate decisions on 28 October and 9 December. September CPI inflation reading is due on 14 October. The first estimate of third-quarter growth is due on 29 October. The monthly non-farm payrolls report is due on 2 October, 6 November and 4 December. The midterm elections are on 3 November.
- **Eurozone:** Eurozone: European Central Bank interest rate decisions on 29 October and 17 December. GDP for the third quarter is due on 30 October. Monthly inflation readings due on 2 October and 4 November.
- **Other Data:** Bank of Japan interest rate decisions on 30 October and 18 December. Chinese third-quarter GDP growth figures along with industrial output and retail sales on 19 October. Chinese monthly inflation readings due on 14 October, 9 November and 9 December.

ASSET CLASS SCENARIOS:



UK EQUITY

Most likely: High energy costs add to inflation as the Bank of England leans towards rate hikes. Large companies with global earnings, including energy and defence stocks, are best suited to this backdrop. Domestic cyclicals, consumer-facing and smaller companies stay under pressure until inflation and gilt yields show clearer signs of peaking, though low valuations should limit the downside.

Worst Case: The energy shock drives up inflation and forces the Bank of England to hike again. The budget fails to convince the bond market and pushes borrowing and mortgage costs higher. This adds to the risk of recession. UK equities fall, with cyclicals, housebuilders, consumer-facing sectors and smaller companies most effected. Energy, defence and companies with overseas earnings offer only partial protection.

Best Case: Inflation concerns ease as energy prices fall due to the reopening of the Strait of Hormuz. UK equities gains broaden out from energy and defensives into domestic cyclicals, rate-sensitive stocks, and mid and small caps, which should respond quickly to lower energy prices and falling rate expectations, supported by low starting valuations and improving confidence.



GLOBAL EQUITY

Most likely: Equities make modest but uneven progress as growth holds up, despite central bank rate hikes. US gains are mainly in mega-cap technology and semiconductors, as AI infrastructure spending supports earnings. European equities are supported by resilient activity and strong earnings. Japan stands apart as a stronger yen caps exporter earnings, though corporate reform and buybacks lift domestic shares.

Worst case: The Iran conflict keeps oil above $110, pushing inflation higher and forcing central banks to increase rates. US equities fall sharply on concerns about high company valuations. European equities tumble due to high inflation and low growth, and political uncertainty. In Japan, a stronger yen hits exporters and inflation outpaces wages.

Best case: Peace in the Middle East eases inflation. US equities gains broaden into small caps, cyclicals, and rate-sensitive sectors. No more rate hikes in Europe extends an equity rally to small and mid-caps, and into consumer-facing sectors and industrials. Japanese equities outperform on earnings momentum, corporate reform, and renewed foreign inflows.



EMERGING MARKET EQUITY

Most Likely: Emerging markets remain resilient despite tighter financial conditions as the Federal Reserve hikes interest rates. The US-Iran conflict remains unresolved so high energy prices support exporters while weighing on importers. Gains are concentrated in technology, especially semiconductors and AI hardware, while China stabilises on targeted government support.

Worst Case: US strikes on Iran escalate after the November midterms and oil surges higher, driving a global inflation spike and forcing an extended Fed hiking cycle. The dollar appreciates sharply, triggering EM equity outflows and a broad fall in valuations. China weakens and Taiwan and Korean stocks fall as companies cut AI-related spending.

Best Case: A formal US-Iran peace agreement drives a sharp fall in oil as the Fed to pivot towards cuts in 2027, weakening the dollar and boosting equity inflows into EM. China recovers on targeted government stimulus and resilient exports, while Taiwan and South Korea continue their AI-driven semiconductor boom. Lower energy costs, improved liquidity and dollar weakness support broad EM outperformance.



CASH

Most likely: Returns stay firm as the Bank of England holds rates around current levels. Inflation is above the Bank's target and is expected to rise further into next year. A growing minority of the Bank's policymakers have voted for higher rates and markets lean towards a rise, but the Bank has cautioned against assuming an increase is inevitable. Cash and money market funds continue to offer steady, low-risk returns at attractive levels.

Worst case: The energy shock fades faster than expected and inflation falls back towards target. A resolution to global tensions and easing energy prices would turn attention back to rate cuts. Falling rates would gradually reduce the return on cash, supporting a rotation towards shorter-dated bonds and other assets. Investors may still hold some cash for safety while the outlook settles.

Best case: Persistent inflation pushes the BoE to raise rates. High energy costs feed inflation concerns and more of the Bank's policymakers begin to favour a rise. Higher rates would lift money market returns, reinforcing the appeal of holding cash, though longer-dated bond funds would come under pressure.



FIXED INCOME

Most Likely: Energy disruption keeps inflation elevated and bond yields remain unsettled. Government bonds earn returns mainly through income, while concerns over public borrowing limit price gains. Investment-grade corporate bonds hold up better than high yield bonds. Emerging market government bonds diverge as energy exporters importers face higher costs and borrowing pressures.

Worst Case: Peace talks fail as energy prices push higher, forcing interest rate increases. Government bonds fall as investors demand higher yields to offset inflation and the risks of more public borrowing. Corporate bonds weaken as growth slows and profits fall. Emerging market bonds struggle due to stronger dollar and high energy bills.

Best Case: A peace deal lowers energy prices and inflation expectations. Investors anticipate fewer rate increases, allowing government bonds to recover. Gilts benefit from a reassuring Budget. Corporate bonds strengthen as borrowing costs fall and confidence improves. Emerging market bonds benefit from a cheaper energy and weaker dollar.



ALTERNATIVES

Most Likely: Oil and gas prices are high and volatile, while higher interest rates hold back demand. Industrial metals benefit from AI-related infrastructure spending. Gold benefits from uncertainty, but higher interest rates reduce its appeal. Infrastructure income remains steady, even as borrowing costs weigh on valuations.

Worst Case: War in the Middle East further disrupts energy supplies as winter demand rises, pushing up inflation and forcing more rate increases despite weaker growth. Oil and gas prices rise while industrial metals suffer from falling demand. Gold offers some safety, although prices remain volatile. Infrastructure and real estate values fall sharply as higher borrowing costs delay projects and squeeze returns.

Best Case: Peace restores energy supplies, easing inflation expectations while growth holds up. Oil and gas prices retreat, while industrial metals benefit from steady demand and investment in AI, electrification, and power networks. Gold loses some appeal as a safe haven but benefits from lower interest rates. Infrastructure values recover as borrowing becomes more affordable and project confidence improves.

Data Sourced from FE Analytics, and MCSI Barra

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