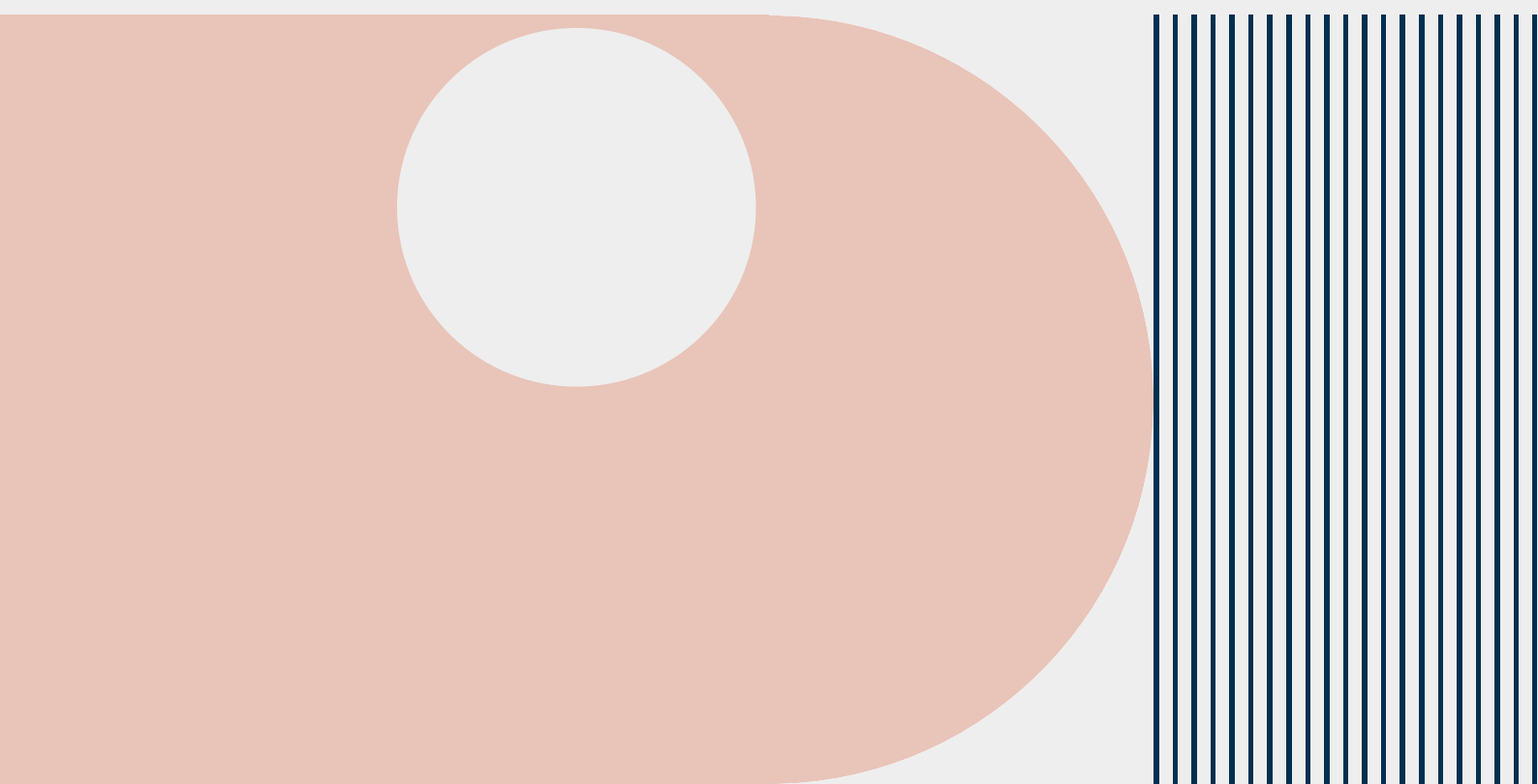




INVESTMENT OUTLOOK

OCTOBER 2026



THE END OF CHEAP CAPITAL

Considering the complicated stagflationary backdrop, the third quarter turned out to be surprisingly benign for markets and economic activity. Business sentiment across the western hemisphere broadly recovered from its Iran-related dip in spring, and global equities continued to advance, albeit with flagging momentum.

Yet, with no end in sight for the conflict in Iran, nor for the resulting global energy crisis, downside risks are mounting. Energy prices surged again in September, with Brent crude rising above USD 100 per barrel and staying firmly above that threshold throughout the month. Meanwhile, energy inventories have come under considerable strain. EU gas storage levels are about 16 percent below their seasonal average, and the US Strategic Petroleum Reserve is near historic lows. China, which had acted as an important stabilising force during the crisis by curbing crude oil imports and drawing on domestic reserves, resumed higher import volumes over the summer.

This drove a fresh surge in inflation and a sharp global repricing of the interest rate outlook. Treasury yields surged broadly across yield curves and currency areas, ultimately forcing the Federal Reserve to pivot to a tightening stance and hike rates for the first time since 2023, following the ECB's hikes in June and September. As a result, interest rate levels across advanced economies have reached heights not seen in around two decades — or longer, in Japan's case — with the yield on a globally diversified investment-grade bond benchmark now at 4.4 percent, up 0.6 percentage points over the quarter.

Together with the ongoing AI capex boom, which increasingly affects debt markets and keeps absorbing enormous amounts of capital, this monetary turnaround has tightened funding conditions globally. As we see it, the era of cheap money, near-zero interest rates and abundant capital has clearly come to an end, giving way to a world in which capital is scarcer, costlier, and can no longer be taken for granted.

At first glance, this shift is not yet reflected in investment demand, which would normally be expected to weaken under such tight conditions. In the US, at least, demand has remained remarkably resilient. But a closer look reveals that recent US investment growth has been driven entirely by AI-related capex. Total private fixed investment outside the AI orbit has stagnated

since 2018 and has actually declined since 2024. The same concentration can be seen in equity markets. Strip out the large chipmakers and hyperscalers and the S&P 500's outperformance over European markets over the past four years largely vanishes.

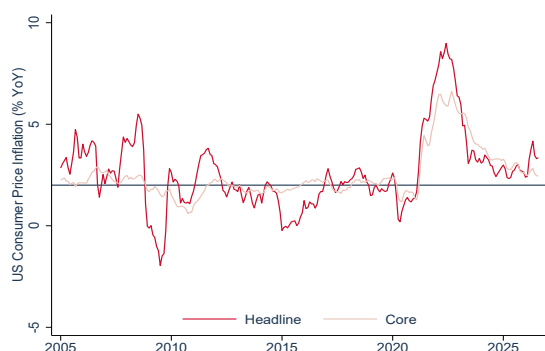
Taken together, broadly rising capital costs, mounting AI-bubble risk, and the lingering energy shock present considerable downside risk – not to mention the heightened geopolitical uncertainty and increasing global fragmentation. This includes, among other risks, a potential reversal of the yen carry trade, which could trigger broad-based pressure on risk assets worldwide. Nevertheless, the broad-based stabilisation in business sentiment observed through the summer points to expanding activity over the coming two to three months. While business prospects in the US profit from the ongoing AI capex boom, Europe's economies are benefiting from a recovery in foreign trade and a positive fiscal impulse, with Germany's large fiscal package now fully feeding through into economic activity. Germany's defence expansion alone is expected to boost GDP by almost 0.8 percentage points in 2026, by about half a point in 2027 and a quarter of a point in 2028.

In light of positive if fading momentum, we kept our cautious positioning and a neutral stance on equities for now. We already de-risked from the overly concentrated US market in May and again in September by selective profit-taking and by introducing slight overweights in Asian and European equities and in defensive sectors. We have also maintained our neutral fixed-income position, noting that while the asset class has suffered from the surge in real yields, current yield levels exceed equity dividend yields by a comfortable margin, leaving duration risk more attractively priced than it has been in a long time.

1.1 NORTH AMERICA

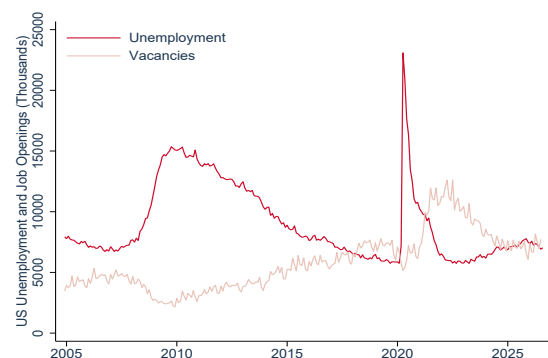
- The US economy expanded by 0.6 percent quarter-on-quarter in Q2, supported by a rebound in personal consumption. Growth was driven primarily by consumption and investment. Government spending remained broadly flat, as higher defence and state and local government expenditures offset declining federal spending, while net exports acted as a drag on overall growth.
- Optimistic capex plans tied to the AI-infrastructure buildout should remain a key driver of US investment demand in the coming quarters – provided AI sentiment doesn't cool suddenly. Business sentiment, as measured by the *S&P Global US Composite PMI*, improved markedly in Q3 after an Iran-related dip earlier in the year, jumping from 51.9 at the end of Q2 to 58.4 in September, signalling a dynamic expansion in activity.
- Following the renewed sharp surge in energy prices in September, price pressures remain a key concern for businesses and consumers alike and should push headline producer and consumer price inflation rates — 5.4 and 3.4 percent year-over-year in August, respectively — higher still in the coming weeks. Underlying price pressures have also stayed above the Fed's 2-percent target, with core CPI at 2.4 percent in August and core PCE, the Fed's preferred gauge, at 3.0 percent year-over-year in July.
- High energy prices and inflation concerns have also weighed on consumer sentiment, with both the *Conference Board Consumer Confidence Index* and the *University of Michigan Consumer Sentiment Index* edging lower over Q3, while elevated mortgage rates kept housing activity and residential investment subdued.
- The US labour market looked resilient: the unemployment rate fell to 4.1 percent in August, job openings grew 4.3 percent, and jobless claims remained low. Some caution is warranted, though, as shrinking labour market participation likely contributed to this benign picture, not demand strength alone. Thus, the Fed's feared stagflationary scenario proved less severe than expected, with inflation the dominant concern without being accompanied by an economic slowdown and rising unemployment.
- Against this backdrop, the Federal Reserve, under new Chair Kevin Warsh, abandoned its easing path, raising the key rate by 25 basis points in September for the first time since 2023 to a new target range of 3.75 to 4 percent. Warsh's overhauled, less forward-guidance-driven communications have markets pricing one further hike by year-end.

Persistent price pressures



Source: LSEG, MFO

...and a robust labour market

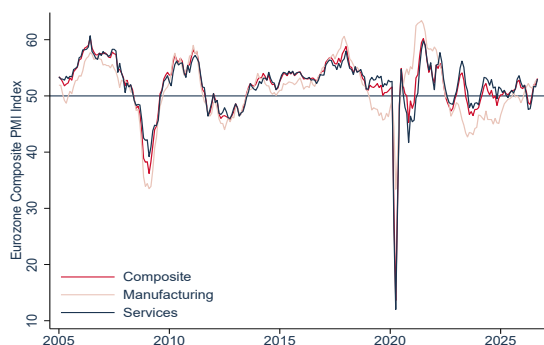


Source: LSEG, MFO

1.2 EUROPE

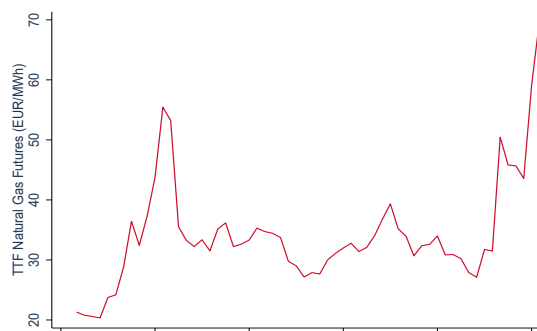
- The Eurozone economy exceeded expectations in Q2, after a contraction in Q1 and deteriorating sentiment data through much of the second quarter had raised the spectre of a technical recession. The upside surprise came from a rebound in exports, which more than offset weaker domestic demand as capital expenditure declined. As a result, Eurozone GDP expanded by 0.6 percent quarter-over-quarter and 1.2 percent year-over-year in Q2.
- The outlook, however, remains challenging. While Germany's fiscal package provides a substantial, positive fiscal impulse, the energy price shock continues to weigh on business margins and household budgets. Producer and consumer price inflation both rose further, to 5.8 and 3.2 percent year-over-year, respectively. The picture is likely to worsen in the coming months. Fossil fuel prices surged anew in September, just as the bloc enters the heating season with unusually low gas reserves, which stood at just under 70 percent, roughly 16 percentage points below the five-year average.
- Refinancing costs are also rising, as the ECB moved before the Fed and raised its key rate by 50 basis points in two steps, one in June and one in September, with futures markets pricing in one further hike by year-end. At its September meeting, the ECB revised its inflation forecast higher, noting upside risks to inflation along with downside risks to growth.
- Even so, business and consumer prospects have firmed since the spring slump. Consumer sentiment has recovered steadily since bottoming out in April, while purchasing managers indexes, supported by a pick-up in new orders, rose to 53 in services and 52.9 in manufacturing in September — pointing to sustained expansion ahead. For the first time this year, the PMIs also signalled rising employment.
- The UK economy also surprised to the upside in Q2, expanding 0.5 percent quarter-over-quarter, with momentum firming into Q3 as the composite PMI rose from 49.3 at the end of Q2 to 51.7 in September. The Bank of England held rates steady in September despite headline CPI climbing to 3.1 percent year-over-year in August.
- The Swiss economy also recovered in Q2, with GDP up 1.9 percent quarter-over-quarter on accelerating consumption and investment, even as exports continued to decline. That export weakness likely reversed in Q3, aided by improving business sentiment and the franc's sustained depreciation.

Firming business activity



Source: LSEG, MFO

...amid an escalating energy crisis

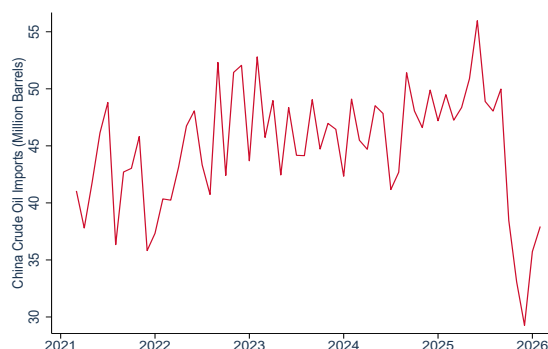


Source: Bloomberg, MFO

1.3 ASIA AND EMERGING ECONOMIES

- Emerging markets faced diverging economic currents in Q3. The *JPMorgan EM Composite PMI* held above the 50-point expansion threshold, while the renewed surge in commodity prices from the ongoing energy price shock weighed disproportionately on energy-importing EMs. China has acted as a crucial global shock absorber by curbing its oil imports, cutting refinery throughputs and drawing down domestic inventories. However, rising Chinese crude imports in July and August suggest this buffering role may be weakening, adding to the risk of a worsening energy crisis.
- China itself remained in a deflationary adjustment. The property sector continued its multi-year slump, while GDP growth decelerated more than expected in Q2, slowing to 4.3 percent year-over-year from 5.0 percent in Q1 as soft consumer sentiment and the ongoing property downturn weighed on domestic demand, albeit partly offset by resilient exports.
- Q3 data painted a similarly uneven picture. The official *NBS Manufacturing PMI* remained near stagnation at 50.1 in September, while the private *Caixin* gauge, more tilted toward smaller, export-oriented firms, climbed to 52.1 – a multi-year high – boosted by the strongest foreign orders in seven months. Policymakers have so far refrained from fresh monetary stimulus, keeping policy accommodative while relying on sizable bond issuances and fiscal support to keep growth within the 4.5 to 5.0 percent official target.
- Thus, China's growth model remains unbalanced, reliant on debt-powered manufacturing and export-based growth while the necessary shift toward domestic private consumption still remains out of reach. While national account breakdowns in consumption and other expenditures aren't available, retail sales figures offer a proxy. In August retail sales grew just 0.4 percent year-over-year, versus exports, which grew by 25 percent and imports up by 28.2 percent.
- Japan's economy extended its recovery for a third consecutive quarter in Q2, with GDP up 0.4 percent quarter-over-quarter, driven by resilient net exports and government spending, even as private consumption stagnated and capital expenditures fell for a second straight quarter amid elevated energy costs.
- Momentum firmed into Q3, with manufacturing orders and services activity expanding robustly throughout the quarter. Against freshly rising inflation, the Bank of Japan delivered its sixth hike since exiting its negative rate regime in 2024, lifting its policy rate to 1.25 percent in September, its highest level in 31 years.

Chinese oil imports revive



Source: Bloomberg, MFO

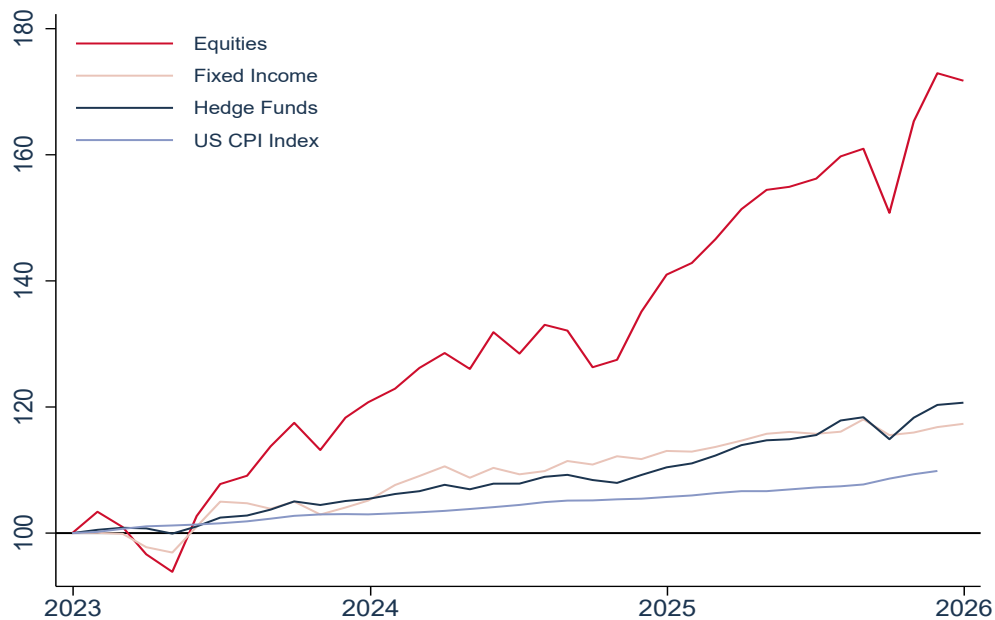
Trade as the sole growth driver



Source: Bloomberg, MFO

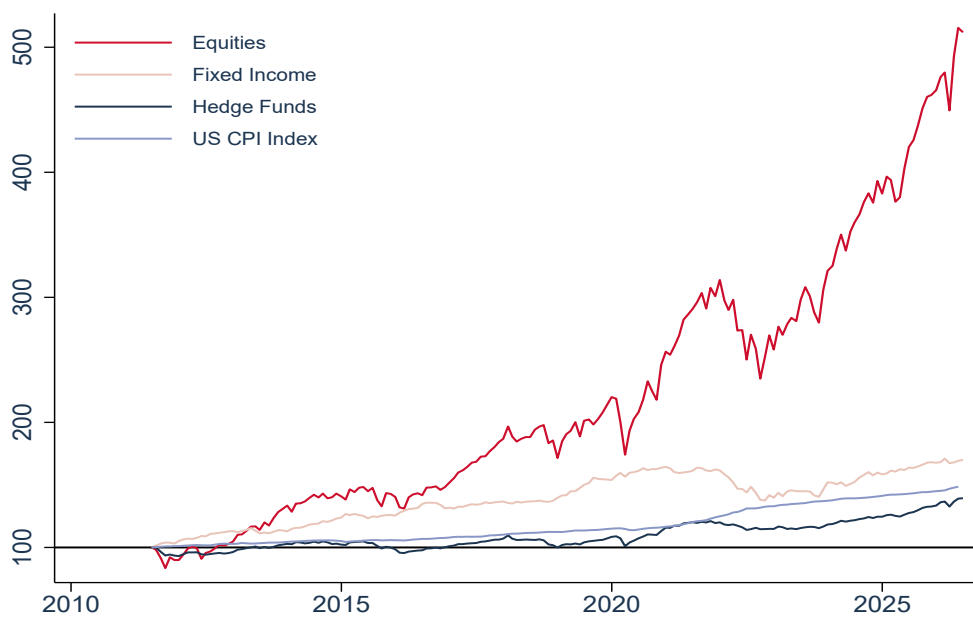
2. FINANCIAL MARKETS

Medium-term market developments



Source: LSEG, MFO

Long-term market developments



Source: LSEG, MFO

2.1 EQUITIES

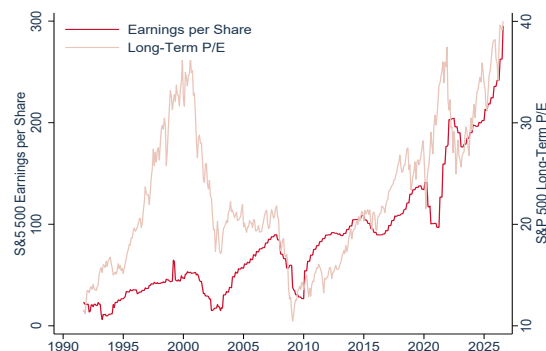
- The third quarter of 2026 unfolded against persistent geopolitical tensions and a pivotal US monetary policy shift. The US-Iran conflict continued to weigh on energy markets, with the Strait of Hormuz effectively closed and oil prices remaining volatile — falling to around 70 dollars in early July, rebounding above 100 dollars by late July, and surging again in September as renewed hostilities reversed earlier relief. The Federal Reserve raised rates in September for the first time since 2023, citing persistently elevated inflation. Sovereign bond yields reached multi-year highs, yet resilient economic activity and corporate earnings kept equity markets broadly supported.
- According to *FactSet*, the Q2 2026 earnings season closed with 87 percent of *S&P 500* companies beating expectations and year-on-year earnings growth of 52.3 percent. For Q3, analysts project growth of 28.9 percent — a third consecutive quarter above 25 percent. Unusually, estimates were revised upward since June, against a historical pattern of cuts averaging 2.5 percent over the same period.
- During the third quarter of 2026, momentum weakened and global equity markets delivered mixed, more modest results than in the prior quarter. The *Nikkei 225* fell 4.2 percent in JPY, while *MSCI Asia ex Japan* lost 0.4 percent in USD. The *Nasdaq 100* delivered 0.6 percent in USD, while the *S&P 500* gained 2.3 percent in USD. In Europe, the *MSCI Europe Index* fell 0.9 percent in EUR and Switzerland's *SPI* declined 2.0 percent in CHF.
- Two themes defined the quarter for equities: a rotation within AI and the return of monetary tightening. Capital shifted from infrastructure and semiconductor names towards software and enterprise adopters, as investors demanded monetisation over continued buildout. Semiconductors remained the biggest contributor to technology earnings, but the market grew more selective. This selectivity was compounded by a concentration dynamic, with AI-driven gains in the US increasingly limited to a handful of names, which flattered index returns while masking wider dispersion. The Fed's September hike was read as a credibility signal rather than a growth threat; with markets little changed on the day.
- We continue to hold a neutral view on global equities, with a preference for non-US markets where valuations remain more attractive and earnings estimates are being revised upward. The quarter's outcome — with the US the sole positive market — reflects how elevated bond yields and the Fed's pivot weighed on markets globally. Monetary policy, oil prices and AI earnings are likely to remain the key variables for Q4, in our view.

US market stays concentrated



Source: LSEG, MFO

Record earnings, rich valuations

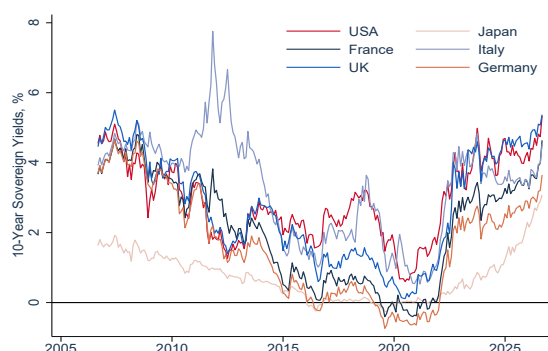


Source: Bloomberg, MFO

2.2 FIXED INCOME

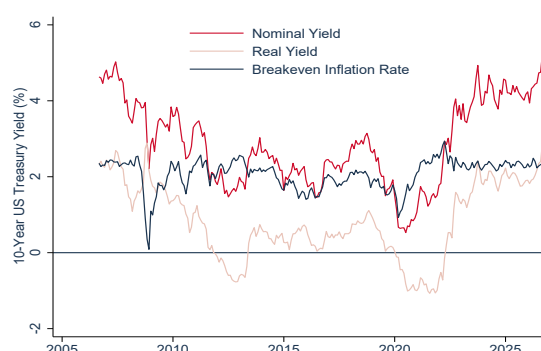
- Global bond markets saw another turbulent quarter in Q3, as the US-Iran conflict entered its seventh month, the US Federal Reserve and the European Central Bank resumed hiking, and Brent crude remained firmly above pre-conflict levels. Benchmark yields pushed to multi-decade highs — the 10-year Treasury climbing above 5.2 percent in September, its highest level since 2002 — leaving global investment grade bonds with a negative 2.5 percent return, as measured by the *Bloomberg Global Aggregate Index* (USD hedged).
- The ECB moved first, hiking 0.25 percent to a 2.50 percent deposit rate in September, its second increase of 2026, as August Eurozone inflation reached 3.2 percent, driven mainly by a 14.3 percent jump in energy costs. The Fed followed with its own 0.25 percent hike, citing persistent inflation worsened by the oil shock. The futures market currently prices one more hike by both the Fed and ECB until year-end, confirming that the “higher for longer” narrative is firmly back in investors’ focus.
- Notably, the yield rise was driven almost entirely by real rates rather than inflation expectations or term premiums. The 10-year TIPS real yield — the inflation-adjusted return demanded on Treasury Inflation-Protected Securities — climbed to roughly 2.9 percent, its highest level in nearly two decades, while the derived expected inflation rate stayed range-bound near 2.4 percent, actually falling on the September CPI release despite it coming in higher than expected. This suggests markets see the Fed’s and ECB’s hawkish pivots as credible and the oil shock as a relative-price shift rather than a de-anchoring of long-term inflation expectations.
- Credit markets remained resilient. US investment-grade spreads held near 0.8 percent, close to 20-year lows, while high-yield spreads widened modestly to around 3.1 percent from 2.8 percent at the end of Q2, according to the *ICE BofA* option-adjusted spreads, supported by solid fundamentals and robust risk appetite.
- Overall, Q3 was defined by an amplified oil-driven inflation shock that pushed key central banks into hiking mode and drove yields to multi-year highs. With real yields at their highest in nearly 20 years, the all-in valuation case for fixed income is the strongest it has been in years. But with the US-Iran conflict unresolved, spreads tight, and further rate hikes anticipated, we favour capturing this carry through income and credit selection over aggressive duration extension, maintaining a neutral duration stance.

10-year yields at multi-decade high...



Source: LSEG, MFO

...while inflation premiums remain anchored



Source: Bloomberg, MFO

2.3 ALTERNATIVES

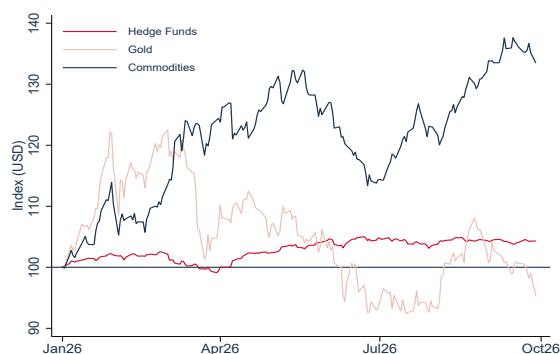
HEDGE FUNDS, PRIVATE MARKETS AND COMMODITIES

- Q3 began with negative performance, driven primarily by weakness in technology and AI-related equities, alongside a deteriorating outlook for a near-term resolution to the Iran conflict, which triggered a sharp rise in oil and energy prices and led to high volatility in risk assets. August marked a recovery in hedge fund performance, led by global macro strategies. Managers benefited from volatility as persistent inflation and fiscal concerns kept long-term borrowing costs elevated, while hawkish Federal Reserve signals pressured global bonds. In September, quantitative strategies performed particularly well, supported by accelerating trends across several areas of financial markets.
- Gold delivered a positive, but volatile performance in Q3 2026. Prices remained high, supported by persistent geopolitical uncertainty, resilient central bank demand and continued investor interest in diversifying away from the US dollar. Gold rallied sharply during July and August, benefiting from fluctuations in US interest rate expectations and concerns about inflation. However, gains largely reversed in September as tighter monetary policy and rising real yields dimmed the yellow metal's appeal.

CURRENCIES

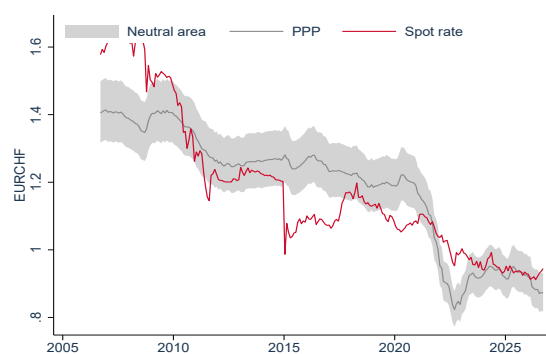
- After an initial depreciation trend, the trade-weighted US dollar strengthened toward the end of the quarter, underpinned by the Fed's reasserted inflation-fighting credibility under Chair Kevin Warsh, ending the quarter near fair value.
- The yen remains the weak link. Despite the Bank of Japan's sixth hike since exiting negative rates, it stayed near multi-decade lows versus the dollar, as wide rate differentials keep the yen carry trade intact. A more decisive monetary policy path, or a sharper US slowdown, could trigger a disorderly unwinding — worth monitoring given the scale of yen-funded positions globally.
- The Swiss franc continued its weakening trend during Q3 and now screens as undervalued against the euro — a rare reversal of its structural appreciation trend, as widening rate differentials and the SNB's signalled willingness to intervene in currency markets have dulled its safe-haven appeal.

Gold with headwinds



Source: LSEG, MFO

For once the franc looks cheap



Source: LSEG, MFO

3. INVESTMENT VIEWS

- **Equities:** We maintain a neutral allocation, reflecting positive, albeit fading, market momentum and positive earnings surprises against a backdrop of a tightening monetary policy stance, an intensification of the ongoing energy price shock, and extreme US market concentration in the dominant AI theme. We retain a slight overweight in non-US and defensive markets, given their more attractive valuations and improved earnings outlook, and in order to de-risk from the concentrated AI bet inherent in the US market without foregoing participation altogether.
- **Fixed Income:** We maintain a neutral fixed-income allocation. Given the ongoing tightening bias, we continue to refrain from increasing duration exposure, even though duration is more attractively priced than it has been in years, supported by multi-decade highs in real yields. Instead, we remain focused on disciplined credit selection.
- **Hedge Funds:** We keep a neutral allocation across our diversified hedge fund book, spanning equity long/short, uncorrelated macro, convex and unconstrained fixed-income strategies. With volatility and dispersion both elevated, we see this mix continuing to earn its keep as a genuine diversifier and stabiliser for the broader portfolio.
- **Gold:** Restored credibility at the Federal

Reserve under newly installed Chair Kevin Warsh, real bond yields at multi-decade highs, and weak price momentum collectively produce headwinds for the yellow metal's performance. We therefore keep the gold position in line with our target allocation, at the middle of the defined range.

Overview

	Equities				Fixed income		Alternatives			Liquidity
	North-America	Europe	Asia-Pacific	Emerging Markets	Duration	Credit	Hedge Funds	Commodities	Precious Metals	
Macro	→	→	→	→	↓	↓	→	↑	↓	→
Market	↑	→	↑	↑	↓	→	↑	↑	↓	→
Valuation	↓	↓	↓	↓	↑	→			↓	→
Sentiment	→	→	↑	↑	→	↓	→	→	→	→
Aggregate	→	→	↑	↑	→	↓	→	→	↓	→

Source: MFO

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Published by	Marcuard Family Office Ltd.
Editors	Nadja Bleuler, n.bleuler@mfo.ch Mauro Eichin, m.eichin@mfo.ch Christoph Orschel, c.orschel@mfo.ch Philipp Stokinger, p.stokinger@mfo.ch
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Bellerivestrasse 36 8008 Zurich Switzerland	Phone +41-(0)43-344 6000 info@mfo.ch https://www.marcuardfamilyoffice.com/

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