

Mid-Year Investment Outlook 2026

Enough fuel in the engine



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In brief

- The global economy is no longer being powered by all its growth engines as the Middle East conflict has dented consumer spending and reduced the amount of monetary fuel that is being added. However, AI capex continues to support activity and government spending looks set to accelerate.
- Despite the more complex geopolitical backdrop, we remain constructive on risk assets, with our base case seeing limited lasting economic damage from the conflict in the Middle East and all growth engines working again by 2027.
- Taking advantage of the opportunities while minimising the upcoming risks in AI remains a key challenge. It's one of the reasons we argue that, in equities, it is important to remain geographically diversified as tech opportunities broaden to EM and headwinds of the energy crisis on Europe fade. In fixed income we expect yield curves to steepen, with better value at the front end – especially in Europe.
- We also look ahead to the US midterm elections, and conclude that policy uncertainty is likely to persist but investors should remain focused on the bigger economic forces arising from geopolitical uncertainty.
- Finally, we assess the recent stress in private credit markets and conclude that the systemic risks are overstated and we do not expect the asset class to challenge our pro-risk stance.

A temporary pause in economic strength

We called our 2026 Investment Outlook *Fuel in the engine*, capturing our expectation that the combination of monetary and fiscal fuel would power a broadening in economic activity by sector and geography. We expected 2026 to be a good year for global growth, and in the early months all was looking good.

Short-term damage to one of the main growth drivers

The conflict in the Middle East has dented the ‘all engines’ nature of our growth outlook, particularly for consumer spending. Higher energy prices are in the process of pushing up headline inflation and will likely feed into a broader range of prices, such as food, as the year progresses (see [Exhibit 1](#)).

This situation is not like the cost shock of 2022, however. Back then, the world economy was only just re-opening after a global pandemic, with booming demand and a buoyant labour market. Inflation thus took off and required considerable interest rate hikes to get it back under control.

This time around the labour market is much weaker (see [Exhibit 2](#)). While some are already pointing to the impact of artificial intelligence (AI), the data isn’t conclusive. In the US, government cutbacks have played a significant role. And in Europe, labour market

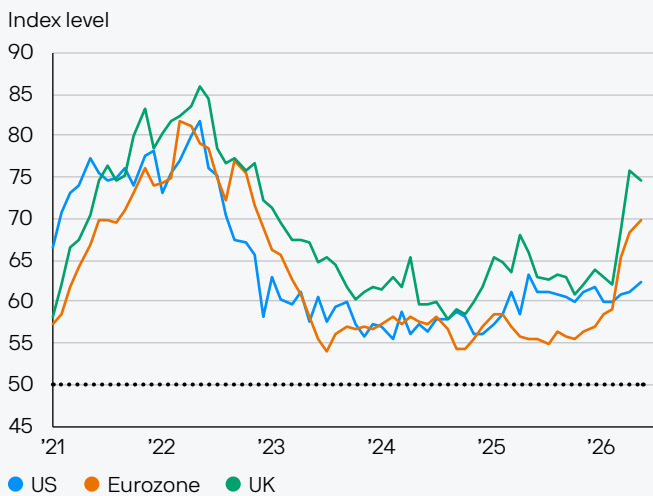
weakness represents corporate caution in a world where demand is only just recovering, although in the UK the rising minimum wage and employers’ national insurance contributions seem to have had a bigger effect.

Either way, workers are unlikely to get significant pay rises to compensate for the higher cost of living. Higher inflation will therefore squeeze disposable income, and in turn consumer spending, in the remaining months of the year.

This income squeeze hasn’t yet had much of an impact on US activity, which may be because workers have had their incomes supported by the tax rebates that were part of the One Big Beautiful Bill Act. Households will start to feel the pressure of higher gasoline prices more acutely in the remainder of the year, which may have implications for the upcoming midterm elections. One of our key risks in the second half of the year is that President Trump announces a new set of cheques in the post to buoy the electorate. With the US deficit already stuck at 6%, the bond market may not cheer. But it’s a risk, rather than our central expectation. You can read more about our expectations for policy before and after the midterms in the chapter: [Don’t be derailed by the US midterm elections](#).

Exhibit 1: The Middle East conflict is pressuring input costs...

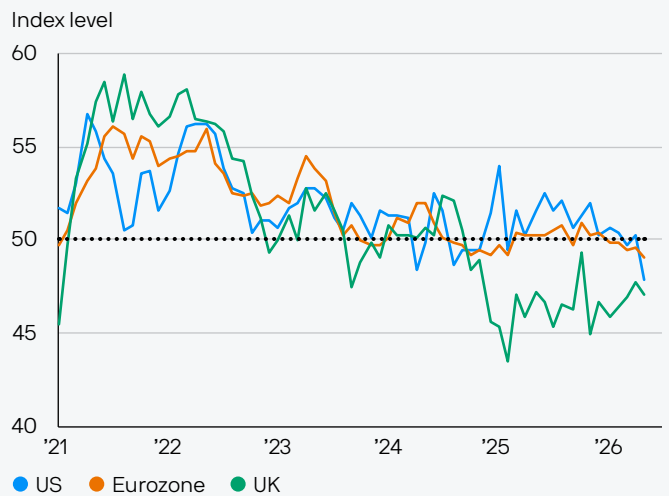
Composite PMIs: Input prices



Source: Bloomberg, S&P Global, J.P. Morgan Asset Management. A Purchasing Managers' Index (PMI) score of 50 indicates that prices are neither rising nor falling, above 50 indicates rising prices. Data as of 8 June 2026.

Exhibit 2: ...but unlike 2022, labour markets are relatively cool

Composite PMIs: Employment



Source: Bloomberg, S&P Global, J.P. Morgan Asset Management. A Purchasing Managers' Index (PMI) score of 50 indicates that employment is neither rising nor falling, above 50 indicates rising employment. Data as of 8 June 2026.

The impact of the income squeeze is more evident in Europe, where the service sector business surveys show that households are feeling the pinch. We are not, therefore, seeing the recovery in consumer spending that was a central tenet for our expectations of a more robust recovery this side of the Atlantic.

Consumer spending has been much weaker in all the major European countries than in the US since the pandemic. The reason appears to be a lack of confidence among European households, who tend to react more to uncertainty than their US counterparts (see **Exhibit 3**). Americans were quick to spend their pandemic savings and, more recently, have been willing to spend despite falling disposable income (see **Exhibit 4**). In Europe, by contrast, we have not only held on to our post-pandemic savings, but we also continue to save more than 'normal'. Until European households feel confident enough to go and spend, Europe will remain the laggard in the post-pandemic recovery.

The weakness of wage growth in the western economies at least means that the central banks will be less worried about inflation getting entrenched. As a result, we don't expect energy price woes to be compounded by higher interest rates. Back in 2022, households and firms had to face the double problem of rising costs and rising interest rates. This time around, most central banks have interest rates in neutral or restrictive territory. Therefore, while not much monetary fuel is being added to the fire we do not

believe there will be any concerted efforts to dampen growth. We expect all the major western central banks to hold rates steady through the remainder of the year.

How long higher energy prices remain a headwind to consumer spending depends on how quickly the Strait of Hormuz re-opens (even if all aspects of a 'deal' are yet to be resolved), and how long it takes the energy market to normalise. In both cases the timing is highly uncertain, as the outcomes depend on several relatively opaque factors.

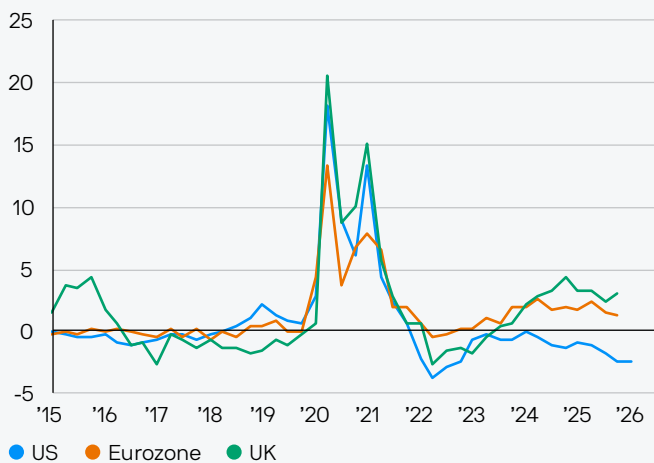
The Gulf states have done their best to keep the oil flowing from the ground, using alternative pipes and routes for exports, and putting any excess into available storage. But despite these efforts, and assuming that flows through the Strait gradually accelerate from June, the International Energy Agency forecasts that production will decline by 3.9 million barrels per day this year relative to 2025 (which equates to a loss of roughly 4% of total production). In addition, there is limited shipping capacity available to get the oil that is in storage out into the world when safe passage is secured.

Another issue is how much damage has been done to energy infrastructure, although we think this concern is overblown. Qatar, for example, has been in the news due to the damage that has been caused to two of its 14 liquefied natural gas (LNG) producing vessels, known as 'trains'. However, while the damage may take three-to-five years to restore, Qatar already has four more LNG trains in construction, which are still likely to be complete as early as next year.

Exhibit 3: European households have exhibited greater post-pandemic caution...

Excess savings rates

% points, savings rates relative to 2015-2019 average

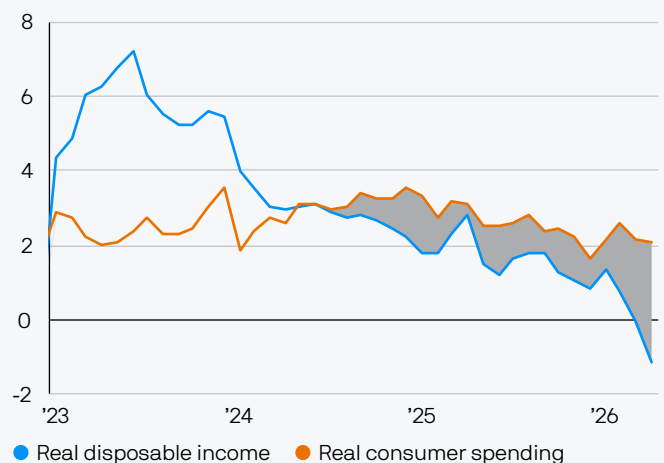


Source: BEA, Eurostat, LSEG Datastream, ONS, J.P. Morgan Asset Management. Data as of 8 June 2026.

Exhibit 4: ...while a slowdown in real income growth has not stopped Americans from spending

US real disposable income and consumer spending

% change year on year



Source: BEA, LSEG Datastream, J.P. Morgan Asset Management. Data as of 8 June 2026.

Higher oil prices also act as a strong incentive on the region to pump as much oil as it can, specifically given OPEC commitments have been structurally weakened with the departure of the UAE from the cartel. However, additional supply could get absorbed by governments around the world attempting to build strategic inventories in fear of new tensions. In this case, demand and prices would remain elevated.

The uncertainty in the outlook for oil prices can be seen in the different oil contracts (see **Exhibit 5**). Overall, we are working on an assumption that oil prices end the year between USD 80-90 per barrel before falling back below USD 80 per barrel in 2027. But there are two-sided risks around this scenario. At the start of the year, for example, one of the key points of discussion was the prospect of an energy glut due to new capacity.

The tech capex engine is still firing on all cylinders

While prospects for consumer spending have been dented by surging energy prices, the other key engine of growth, business capex, is still firing in certain regions. The US hyperscalers continue to ramp up their spending ambitions, which is powering not only US growth, but also growth in those markets that provide the chips and other inputs that the hyperscalers need.

China is embarking on its own AI boom, seeking to emulate US technology growth and win the AI race. How China's efforts interplay with US tech ambitions is yet to be seen and is therefore one of the key questions facing investors in US technology (see **The AI investment boom is reshaping stock market winners**).

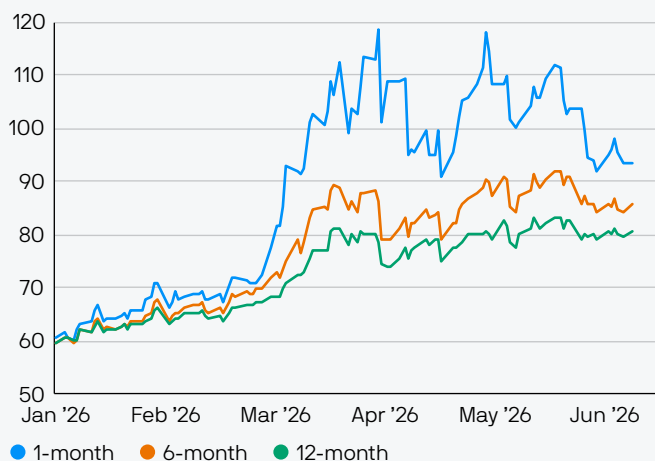
While AI capex looks likely to continue to fuel global growth, we will also start to learn more about the potential productivity gains that the broader corporate universe is managing to achieve by utilising AI. These potential gains are being seen as software's loss, creating pressure on software-heavy private credit funds. We don't see this pressure as substantial enough to derail our pro-risk view, however (see **Private credit will not upset risk sentiment**).

Broadly speaking, if the tech stocks deserve their valuations, AI should be a powerful source of productivity and profitability across the world, dispersing growth by sector and region. Europe has not been at the forefront of the production of new technologies, but is showing encouraging signs in terms of AI adoption (see **Exhibit 6**).

Exhibit 5: Oil price futures suggest markets are anticipating a resolution ahead

Brent crude oil price futures

USD per barrel

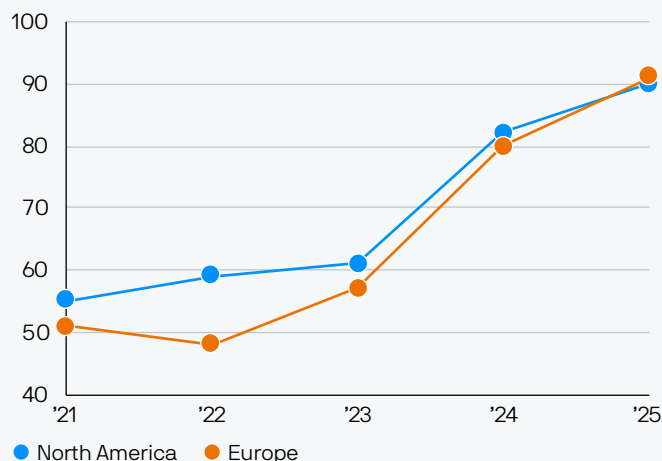


Source: LSEG Datastream, J.P. Morgan Asset Management. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

Exhibit 6: Europe has caught the US in terms of AI adoption

Share of companies using AI

%



Source: McKinsey & Company via AI Index Report with major processing by Our World In Data, J.P. Morgan Asset Management. Organisations are counted as using AI if they report using it in at least one business function. The definition of AI includes broader technologies, such as machine learning and natural language processing, as well as generative AI. Data as of 8 June 2026.

The government engine may get yet more fuel

Government spending was expected to be another major engine of growth this year. Geopolitical uncertainty and the fragmentation of previous relationships between regions is leading to a whole host of spending aimed at improving 'national resilience'. The more chaotic the political backdrop becomes, the more we are seeing governments spend, which is one of the central tenets driving a wedge between negative political headlines and positive market sentiment.

The German fiscal stimulus, one of the big stories of 2025, is now slowly being dispersed. While there is much debate (and scepticism) about the long-term productivity enhancements, in the near term we still expect this spending to be a major support to the biggest eurozone economy.

Back up and running in 2027

Overall, our assessment is that the positive story of growth accelerating and broadening has been damaged by the Middle East conflict, but not irreparably. Once the Strait re-opens and energy prices fall back, all engines should be up and running again in 2027.

Given markets are forward looking, they should anticipate the more buoyant backdrop, which keeps us generally positive about the outlook for risk assets (see [Staying risk on in our market outlook](#)). However, there are a wide range of risks to this benign scenario, so our chapter on key tail risks warrants careful scrutiny (see [The risks are clear and so is the protection](#)).



The more chaotic the political backdrop becomes, the more we are seeing governments spend...

The AI investment boom is reshaping stock market winners

“Is AI a bubble?” has been one of the most important, and most difficult, questions facing investors since the pandemic. In our 2026 Investment Outlook (published last November), we explained why we believed it was impossible to make a definitive call on whether the booming levels of capex related to artificial intelligence (AI) would deliver a sufficient return on investment. This was because it was simply too early to tell the extent to which AI would enhance corporate profitability and how much enterprises would be willing to pay for it. We therefore argued that tech exposure was still an important part of equity allocations but required careful risk management.

What we have learned over the past six months has generally been positive for the tech sector. Survey-based indicators highlight increasing corporate adoption, with the Ramp AI Index now suggesting that more than half of companies surveyed are paying for an AI subscription, up from 40% a year ago. Anthropic’s latest update to the Claude family of large language models (LLMs) helped to add to the excitement, with the new release more clearly targeted at augmenting professional tasks.

We also take reassurance from increased return dispersion in tech-related areas of the market. Dispersion has risen across subsectors (software vs. semiconductors), across stocks within subsectors

(US hyperscalers) and across regions. The implication is that investors are scrutinising individual company fundamentals rather than placing options on the overall market, which would be more common behaviour in the late-stage euphoria of a bubble forming. Increased dispersion also implies a stronger environment for active management to generate alpha.

It is clear, however, that questions remain: the effect that AI will have on the global economy and the profits that can be reaped from it, as well as who will take the largest share of the profit pie.

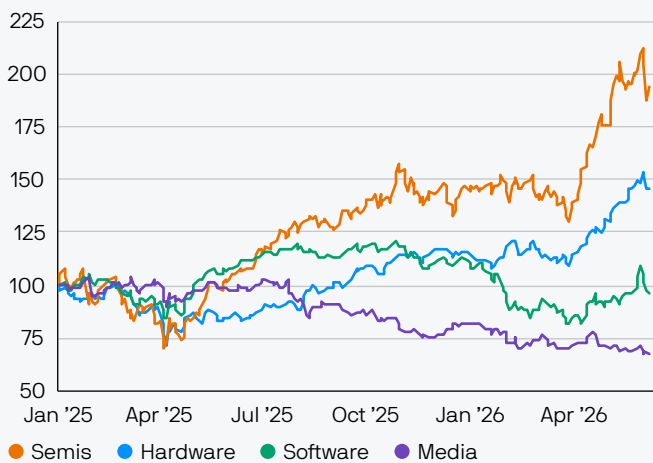
To avoid the brunt of these uncertainties, investors are demonstrating a preference for parts of the AI supply chain – such as high bandwidth memory – where bottlenecks are allowing companies to achieve strong pricing power and generate robust profits. Conversely, industries that are perceived to be most at risk of disruption have been punished hard: software and media companies are down 3% and 32% respectively since the start of 2025 (see Exhibit 7).

Below we outline three strategies to capitalise on the tech opportunities available while seeking to guard against areas of potential risk.

Exhibit 7: Dispersion has increased across AI-exposed industries

US subsector equity returns

Index level, total return rebased to 100 in January 2025



Source: LSEG Datastream, S&P Global, J.P. Morgan Asset Management. Subsectors are based on the S&P 500 Index. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.



Regardless of the return on investment that the hyperscalers will eventually achieve, the capex boom is having an extremely positive impact on the recipients of this spending today.

Prepare for hyperscaler volatility

US hyperscalers are going all-in to win the AI race. Sell-side analyst estimates for 2026 capex are now a remarkable USD 697 billion for just five US companies, up by USD 173 billion since the beginning of the year. At the same time, enormous financing requirements are pressuring balance sheets for some names. As a result, pairwise correlations – the extent to which stocks are moving in the same direction – among the US hyperscalers have reached new lows (see **Exhibit 8**). The spread of performance between the best (Alphabet) and worst (Meta) performing US hyperscaler over the past year to 8 June is a remarkable 125 percentage points.

Given the uncertainty about who the winners will be, investors are now conditioning the reward for additional capex spending on evidence of greater final demand, which is a trend we expect to continue. In the latest earnings season, higher capex plans only drove stronger performance when matched with higher revenue estimates. Balance sheet strength will also remain under scrutiny. With cash piles run down, AI capex has gone from 33% of the hyperscalers’ cash flow from operations in 2023 to an estimated 93% in 2026.

Ultimately, for the hyperscalers to win back investors’ favour, the equation is clear: demonstrate that demand is sufficient to deliver a positive return on investment, and do so quickly enough to avoid placing too great a strain on existing cashflow.

The AI supply chain should see less noise

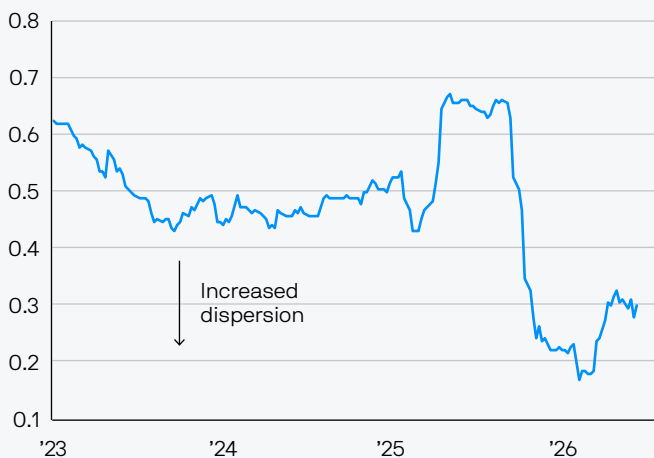
Regardless of the return on investment that the hyperscalers will eventually achieve, the capex boom is having an extremely positive impact on the recipients of this spending today. Companies that manufacture semiconductors, memory and electronic components are all seeing incredible earnings upgrades, as are companies linked to the build-out of data centres.

Consensus estimates see US semiconductor companies’ earnings growing by 98% in 2026, more than five times faster than those of the US hyperscalers (see **Exhibit 9**). While Nvidia remains the market leader in designing cutting-edge chips – with operating margins of 75% – the profitability of companies linked to semiconductor production has been soaring around the world. Since January, the 2026 earnings-per-share (EPS) estimates for Asian, US and European semiconductor names have been revised up by 89%, 22% and 17% respectively.

Exhibit 8: US hyperscalers are no longer moving in unison

Pairwise correlations of US hyperscalers

Average pairwise correlations based on rolling six-month daily returns

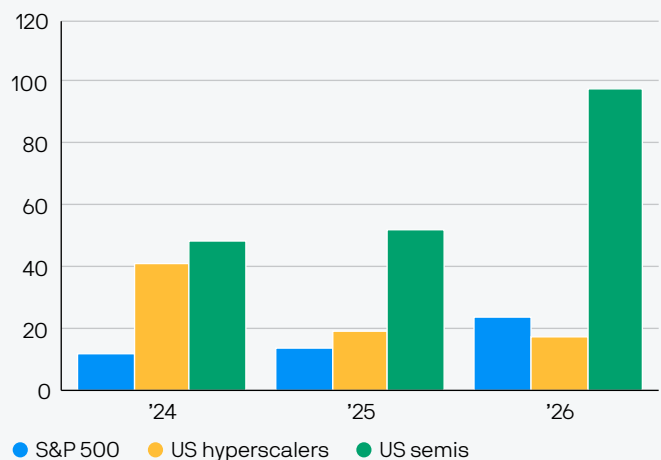


Source: LSEG Datastream, J.P. Morgan Asset Management. US hyperscalers include Alphabet, Amazon, Meta, Microsoft and Oracle. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

Exhibit 9: Semiconductor earnings are soaring while the hyperscalers are slowing

Annual earnings per share growth

%



Source: LSEG Datastream, S&P Global, J.P. Morgan Asset Management. US hyperscalers include Alphabet, Amazon, Meta, Microsoft and Oracle. 2026 earnings for Alphabet and Amazon are adjusted to remove the impact of the revaluation of Anthropic stakes. Data as of 8 June 2026.

In the long run, it is unsustainable for one subsector to capture such a large share of the total profit pie. Some degree of reconvergence is therefore likely, either through a “catch up” scenario, where AI demand validates the hyperscalers’ capex, who will require a bigger share of the overall gains. Or via a “catch down” scenario, where a pullback in AI capex would likely hit semiconductors harder than other subsectors, given their recent rise and the magnitude of earnings expectations already baked in.

While the extent of the recent semiconductor outperformance cannot continue indefinitely, valuations provide a reason to remain constructive. US semiconductor valuations have actually fallen over the past year, and at 22x 12-month forward earnings, their valuation is only one point higher than the valuation of the S&P 500. Given the expected earnings growth trajectory, this looks like a relatively small margin.

One might argue that unrealistic earnings growth assumptions are artificially lowering valuations. Measuring the trailing price-to-earnings growth (PEG) ratio is, therefore, useful in that it compares the P/E valuation with realised earnings growth rather than expected earnings growth. Surprisingly, the “backward looking PEG” for the US semiconductor sector is not only lower than that of other subsectors involved in the AI build-out, but has also fallen more than others over the past year (see **Exhibit 10**).

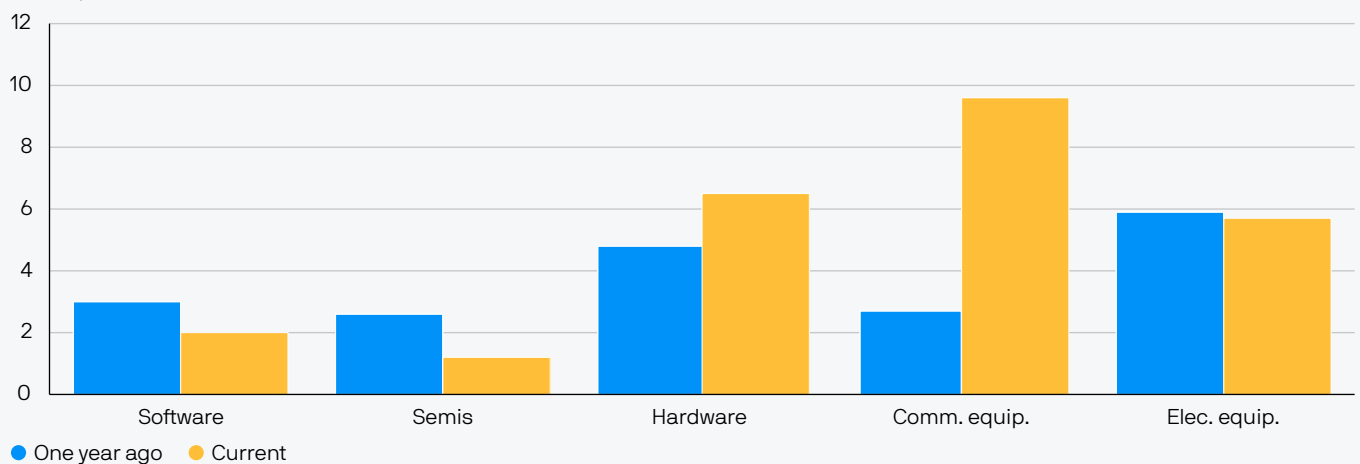


While the extent of the recent semiconductor outperformance cannot continue indefinitely, valuations provide a reason to remain constructive.

Exhibit 10: Robust earnings have helped to improve semiconductor valuations

US equity trailing PEG ratios

x, multiple



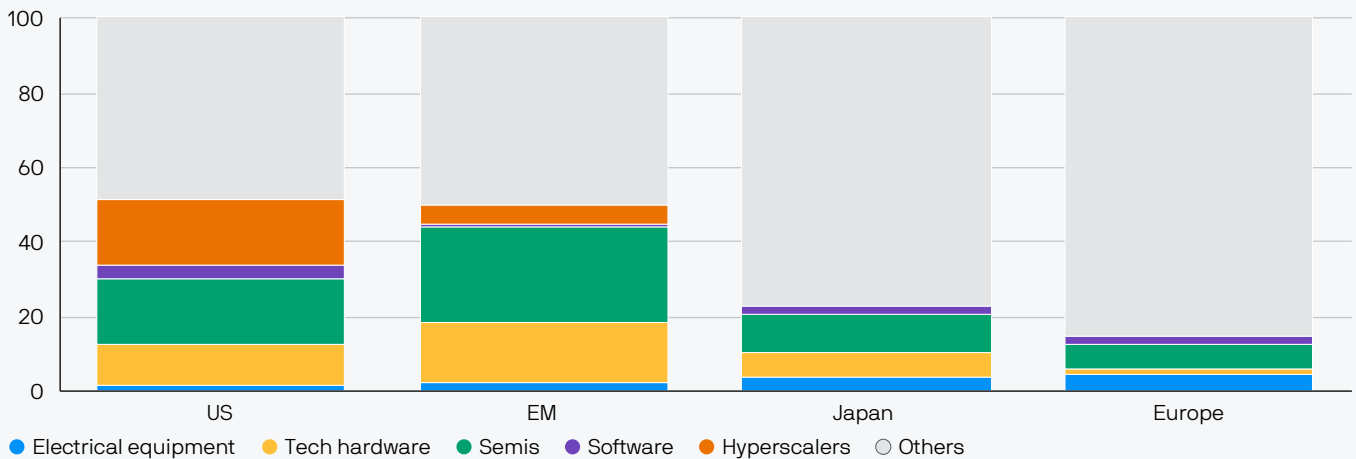
Source: LSEG Datastream, S&P Global, J.P. Morgan Asset Management. The trailing PEG ratio compares price to 12-month trailing earnings against three-year annualised trailing earnings growth, and therefore adjusts current valuations to reflect the strength of historical earnings growth. Subsectors are based on the S&P 500 Index. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

The opportunity is now global

The weight of tech exposure in regional benchmarks has once again been a key determinant of performance year to date (see **Exhibit 11**). While US and Chinese benchmarks have the largest exposure to hyperscalers, huge amounts of AI capex have flowed to suppliers in other countries, especially Korea and Taiwan. Earnings growth in emerging markets has been so strong that valuations have fallen in 2026 despite returns of 18%, with the tech sector having contributed more than 100% of this return (see **Exhibit 12**).

Exhibit 11: Tech sector weights have been a key driver of relative regional performance
Equity index exposure to AI-related industries

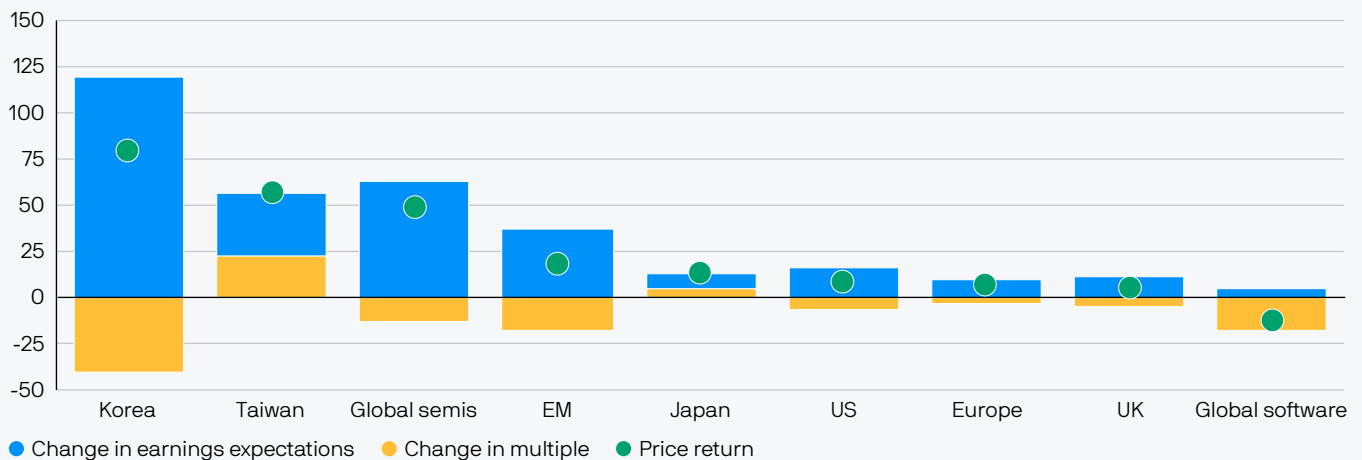
%, index weight



Source: LSEG Datastream, MSCI, S&P Global, J.P. Morgan Asset Management. MSCI indices are used for EM, Europe and Japan, US: S&P 500. US hyperscalers include Alphabet, Amazon, Meta, Microsoft and Oracle. Emerging market (EM) hyperscalers include Alibaba and Tencent. The US software weight is adjusted to exclude Microsoft and Oracle given they are counted as hyperscalers. Data as of 8 June 2026.

Exhibit 12: Earnings have driven the bulk of 2026 returns
2026 year-to-date equity return decomposition

%, price returns



Source: FTSE, IBES, Korea Stock Exchange, LSEG Datastream, MSCI, S&P Global, Stoxx, Tokyo Stock Exchange, J.P. Morgan Asset Management. Global semis, global software, emerging markets (EM) and Taiwan are based on MSCI indices. Europe: Stoxx 600, Japan: TOPIX, Korea: KOSPI, UK: FTSE All-Share, US: S&P 500. Returns are shown in local currency (Europe in euros), with the exception of EM and the sector indices which are in US dollars. Earnings and multiples are based on 12-month forward earnings metrics. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

With AI increasingly seen as a critical part of countries' national security, how the AI build-out evolves geographically bears watching. The US and China both appear determined to win the AI race, with the US leading in terms of frontier innovation "blueprints", although China's open-source/open-weight models offer much lower costs. (It remains to be seen whether other regions, including Europe, will be open to utilising AI capacity provided by others or whether they will become more determined to create their own domestic capabilities.)

China's strategy appears focused on achieving the broadest usage rather than the most powerful models, with AI agents and models aiming to become a commodity that every business can utilise. While the depth of adoption remains nascent, Chinese businesses seem eager to opt in: over 50% of small and medium-sized enterprises are already applying AI in operations and 27% plan to adopt it within the next two years.

China is also advanced in deploying robotics at scale, and seems more able and more willing to field real-world applications (for example, drones and uncrewed mobility), aided by a less restrictive domestic regulatory posture. Almost 40% of China's AI-related investment goes to robotics.

Finally, China has a "physical edge" thanks to its ample and rising power capacity, as well as its supply of critical minerals. This advantage allows the country to build data centres at a much faster pace than anywhere else in the world.

We see stronger investment opportunities today in Asian companies involved in the AI build-out (semiconductors, robotics, industrial equipment etc., both in China and broader emerging Asia) rather than in the Chinese hyperscalers. Because of Chinese government subsidies, the uncertainty over the ability of Chinese hyperscalers to monetise their current investments is higher relative to their US peers.

Capturing the pie, minimising volatility

AI-related developments since we published our 2026 outlook have generally been positive. Rising dispersion across the AI ecosystem suggests that investors are scrutinising company fundamentals. This process of discovery will continue to generate volatility, as we learn both how AI will influence the economic pie, as well as who will garner the largest slice. We suspect that the recipients of capex spend will enjoy a smoother ride.

Until there is much greater evidence to answer the return-on-investment question, a selective approach remains warranted. The next key test lies in several high-profile initial public offerings ahead, which will gauge investors' appetite for yet more AI exposure. We will tackle this subject in greater detail over the coming weeks, but ultimately don't expect these events to change the narrative. Signs of corporate demand for AI, whether good or bad, are likely to be the more important signal over the coming quarters.

Staying risk on in our market outlook

Investing in the global tech boom is an exercise in itself (see [The AI investment boom is reshaping stock market winners](#)). Turning to the rest of the investment universe, our base case remains supportive for risk assets: the world avoids an energy crisis, global growth slows gradually rather than falling into recession, earnings hold up, and the artificial intelligence (AI) investment cycle continues to support profits.

Looking through near-term weakness in activity

The Middle East conflict has lifted energy prices and revived volatility across rates, equities, and currencies.

In our base case, however, the conflict remains a manageable shock rather than the start of a broader macro break. Higher energy costs and tighter financial conditions should cool activity, and global growth should show signs of moderation in the coming months. But the slowdown looks more likely to be a temporary downshift than a stall: softer momentum, not an abrupt contraction.



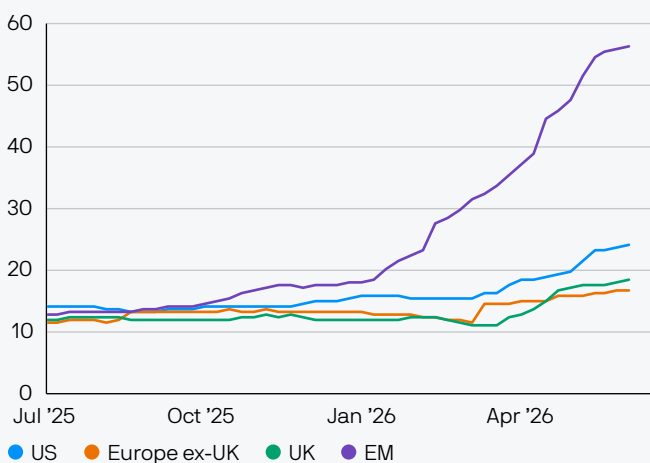
So far this year, earnings revisions have been so strong that index-level valuations have actually eased.

That distinction matters for portfolios. A gradual slowdown can remain compatible with decent returns on risk assets when earnings are resilient and liquidity conditions are not deteriorating sharply. This backdrop should support equities and credit even as cyclical momentum cools and headline inflation stays elevated.

So far this year, earnings revisions have been so strong that index-level valuations have actually eased in many regions despite robust returns (see [Exhibits 13 and 14](#)). This fact provides us with further comfort as we enter the second half of the year.

Exhibit 13: Earnings expectations have trended higher, especially in EM...

Consensus estimates for 2026 earnings per share growth % change year on year

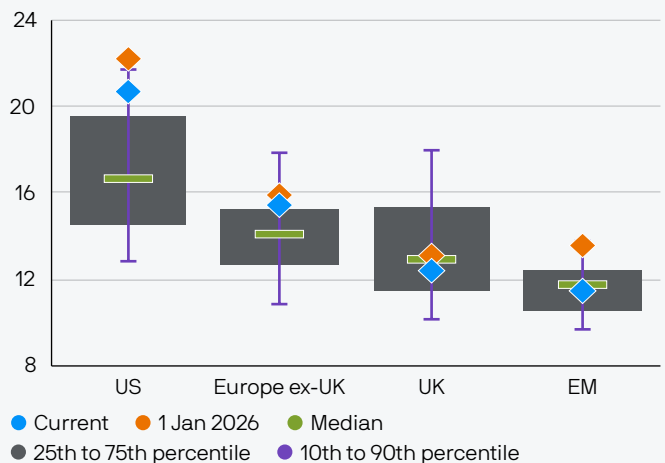


Source: FTSE, IBES, LSEG Datastream, MSCI, S&P Global, J.P. Morgan Asset Management. MSCI indices are used for Europe ex-UK and EM. UK: FTSE All-Share; US: S&P 500. Data as of 8 June 2026.

Exhibit 14: ...helping valuations to moderate

12-month forward P/E ratios

x, multiple, percentiles and median since 2000



Source: FTSE, IBES, LSEG Datastream, MSCI, S&P Global, J.P. Morgan Asset Management. Emerging markets (EM) and Europe ex-UK are MSCI. UK: FTSE All-Share; US: S&P 500. Valuation is price to 12-month forward earnings, as published by IBES. Percentiles and median calculated using monthly data since 2000. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

In equities, the tech super cycle and Middle East conflict dominate sentiment

The largest technology investment cycle of our lifetime is still underway, supporting demand, margins and pricing power across the AI and digital infrastructure ecosystem.

As long as tech momentum persists, we see US equities well supported, given AI-related stocks now account for more than 50% of the S&P 500. However, it's increasingly clear that a key feature of this cycle is that the technology investment boom is no longer US-only. It is broadening into Asia through hardware demand and the supply-chain build-out needed to deliver AI infrastructure at scale. Asian "picks-and-shovels" providers, especially semiconductor and memory producers, are well positioned.

What is interesting, and perhaps concerning, is that we are not yet seeing optimism about AI filter into the earnings expectations of the broader corporate universe. Positive revisions to analysts' earnings expectations remain concentrated in technology and in energy-related areas due to the oil price surge. Elsewhere, concerns about the economic impact of the Middle East conflict are dominating sentiment, particularly in areas of the market that act as bond-proxies, such as defensives and consumer-facing stocks (see **Exhibit 15**).

We see scope for this situation to change in the second half of the year. Not least, we expect a normalisation in energy markets to leave only limited scars on the global economy.

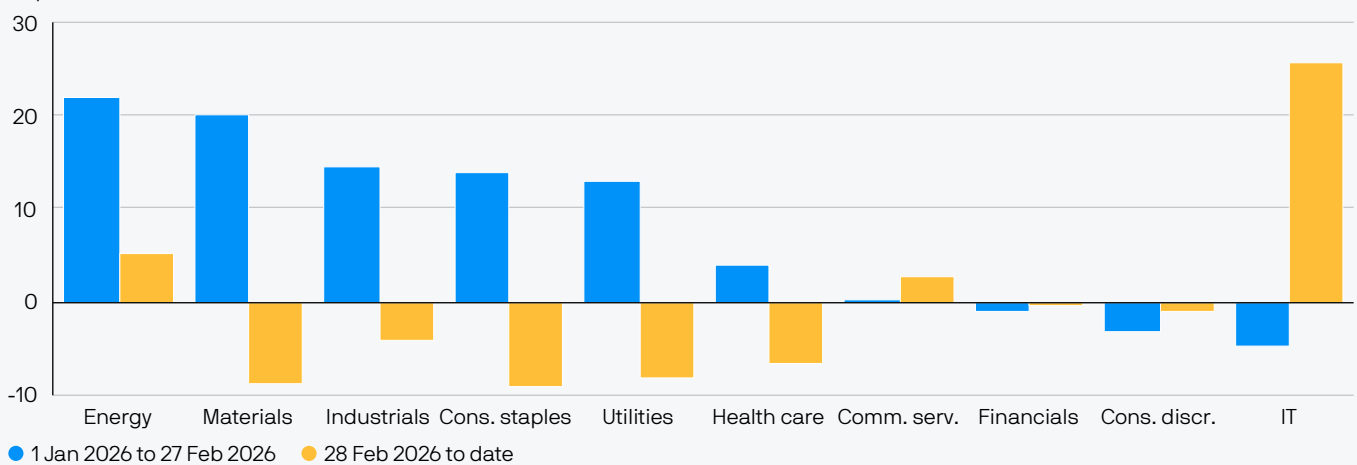
Emerging markets should benefit from two macro tailwinds in our base case. First, easing energy prices should reduce the probability of renewed policy tightening in the region. Second, assuming the Federal Reserve (Fed) does not increase interest rates, this reduces the pressure on emerging market central banks to defend currencies through restrictive rates, which improves the environment for duration, supports equity valuations, and allows domestic policy to become less defensive. While not a blanket buy signal across emerging markets, the macro backdrop creates a more constructive foundation for selective exposure where earnings and policy dynamics align.

Within emerging market equities, we remain cautious on the outlook for Chinese stocks. China's economy remains two-tier: exports and technology-related investment are firmer, while domestic demand remains weak. Private sector confidence has not recovered convincingly, reflecting the prolonged housing downturn and labour-market weakness. Despite the market's de-rating relative to Asian peers over the past 12 months, we do not see a clear catalyst for a broad re-rating into year-end.

Exhibit 15: The Middle East conflict has paused the broadening across sectors

Developed market equity sector returns

%, price returns



Source: LSEG Datastream, MSCI, J.P. Morgan Asset Management. Returns are in US dollars. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

Having outperformed the US in 2025, hopes that Europe could stage another year of outperformance were dented in the first half of the year as investors once again digested the region’s energy vulnerabilities, and tech enthusiasm returned to the fore. In our base case scenario of slowly normalising energy markets, the pressure should ease on sectors affected by fuel and input costs, especially consumer-oriented areas and parts of industrials. Lower energy and logistics costs would be expected to support discretionary spending and improve operating leverage for companies that have absorbed higher costs. Such a rotation would improve market breadth and reduce reliance on a narrow group of winners, which should be beneficial for European stocks.

Of course, whether Europe can keep pace with the US market depends in large part on the global technology story. Structurally, Europe’s sector mix is less exposed to the fastest-growing areas of technology and AI, limiting participation in current earnings momentum relative to markets with deeper tech representation. However, Europe can still perform well, particularly if financials remain strong on the back of a resilient credit cycle and an upward-sloping yield curve, and consumer names recover on the back of falling energy prices.

UK equities continue to offer a differentiated and relatively attractive profile. A weaker pound, on the back of political uncertainty and a less hawkish Bank of England than markets currently expect, supports internationally exposed revenues, while dividend yields, undemanding valuations, and stronger free cash flow generation provide a solid foundation for total returns.

A lot going on in bond land, but a lot is already in the price

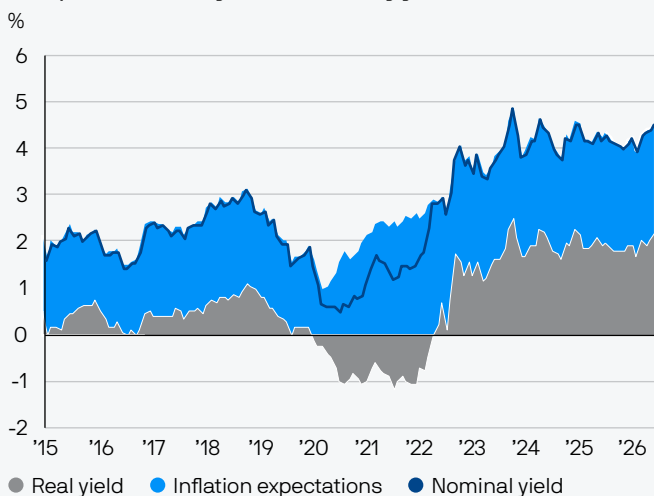
Government bond yields have whipped around in the last few months, as perceptions have shifted around both how large and persistent the inflation problem may be, as well as what governments might need to shell out to support their electorates.

More broadly, investors are wary about the structural shift facing the fixed income landscape – with inflation more prevalent and government commitments to fiscal prudence more questionable. Whether investors should still buy government bonds in a world in which government debt is continually rising is one of the most common questions we get asked.

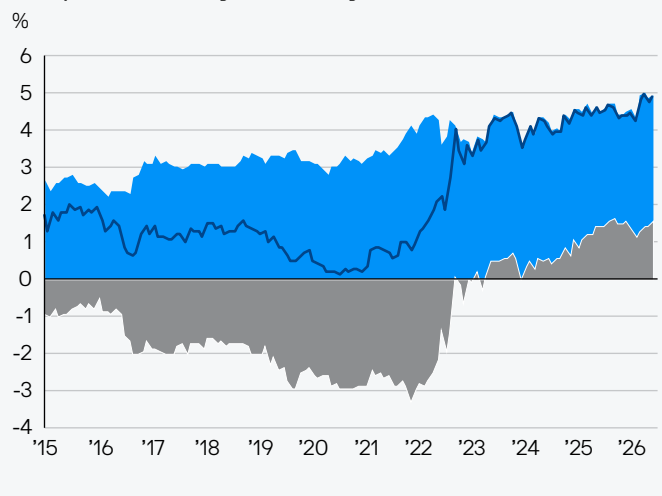
While these concerns are valid, we would argue that much of this ‘bad’ news is in the price. The post-Covid regime is defined by higher demand for capital. Governments are investing in “national resilience”, while corporates are also spending on AI capex and supply-chain resilience. This competition for capital raises the required return for investors, as demonstrated by the rise of nominal and real yields since 2020 (see **Exhibit 16**).

Exhibit 16: Higher demand for capital is driving yields upwards

Components of 10-year US Treasury yields



Components of 10-year UK Gilt yields



Source: (All charts) LSEG Datastream, J.P. Morgan Asset Management. Inflation expectations are calculated as the difference between nominal and real yields. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

The urgency to build resilience has intensified this year, but we do not expect bond markets to price materially higher inflation expectations. While we weren't convinced that the 2022 cost shock would be transitory, we are convinced this time. The risk of second-round wage effects is lower, and central banks can therefore be less hawkish than market pricing currently implies. This environment should support short-dated bonds and lead to steeper yield curves.

Even with a pro-risk stance, government bonds deserve a place in portfolios, with current yields offering downside protection if growth risks re-emerge. While not our base case, if global stock markets are hit by fading tech euphoria, government bonds would offer material portfolio protection (see [The risks are clear and so is the protection](#)).

Our strongest duration preference is UK Gilts. The next few months will remain politically challenging as the potential for a leadership challenge, and a shift in policy direction, becomes clearer. However, we suspect that any contender for the leadership will ultimately be fiscally prudent, having learned the lessons of former prime minister Liz Truss not so long ago. Again, we believe a lot of this political risk is now in the price. Moreover, a softer labour market should keep the Bank of England on hold through year-end.

In the eurozone, German Bunds look reasonably valued, with growth likely to soften as energy costs bite. Broad euro government bond spreads provide ample income, though we are more cautious on France, where September budget negotiations and the 2027 presidential election are likely to bring political risk back into focus.

We see more scope for yields to rise in the US and Japan. Market policy-rate expectations are closer to our view, fiscal policy is expansionary with upside risks, and the US growth outlook is stronger.

Corporate credit remains supported despite tight spreads across investment grade and high yield. All-in yields are attractive, and while issuance is picking up, particularly in US investment grade, demand remains resilient. We do not have a strong preference between investment grade, with higher quality and margins, and high yield, with higher carry and shorter duration. Adding risk through equities seems more appealing than credit since earnings growth offers more upside.

In our base case, the Fed doesn't hike rates. In which case, emerging market debt looks attractive. Emerging market policymakers showed discipline during the 2022 shock, preserving fundamentals

across fiscal balances, real policy rates and currency reserves. Local-currency debt appears particularly well positioned, with attractive real yields relative to developed markets. The asset class should therefore benefit from a weaker dollar once energy markets normalise.

Capital on the move

While we broadly expect risk assets to shrug off this latest bout of political concern, we see two lasting features that could have significant investment implications.

The first is the shifting nature of global capital flows and what this means for the US dollar. Despite benefiting recently from temporary 'energy-haven' support, we continue to believe that the dollar is on a new downward path, reversing the trend seen over the 15-year period to 2024. During this time, the US attracted substantial global excess savings, supported by favourable yield differentials and a growth advantage (see [**Exhibits 17**](#) and [**18**](#)). Looking ahead, narrowing growth and yield differentials would likely accelerate a marginal rotation away from US assets.

The role of official or public sector saving will be part of this global capital rotation. The more chaotic the world becomes politically, the more governments are spending. As mentioned, a less predictable global order increases the need for defence capability, supply-chain resilience, energy security, and commodity stockpiling. The implication is that global spending will be higher and there will be greater willingness to deploy surplus savings into domestic resilience investment and real assets, rather than purely into financial claims on future US income streams.

Concerns about institutional credibility also matter in dictating global capital flows. Lingered questions around Fed independence, for example, may raise the risk premium investors demand. In that environment, a softer dollar becomes an important tailwind for emerging market assets and, to a lesser extent, European equities.

Recent episodes show quite how sensitive markets are to incremental capital flow changes. On Liberation Day, the world did not dump US assets; it simply bought fewer of them. The impact was still meaningful: the dollar fell around 5% in April 2025, equities sold off, and Treasuries failed to provide their usual hedge, with the 10-year yield rising more than 30 basis points before stabilising.

The second key question for investors to consider is how the changing macro backdrop necessitates a different approach to diversification. Currently all this spending is pushing up real growth with only episodic bouts of inflation. If that balance shifts and inflationary concerns become more systemic, then investors will seek protection in assets that ‘can’t be printed’. Infrastructure, transportation assets, and real estate sit at the centre of resilience, supply-chain security, energy security, and domestic capacity building. They also offer a useful hedge in a more inflationary world, with tangible replacement value, long-duration cash flows, and potential inflation linkage through rents, contracts,

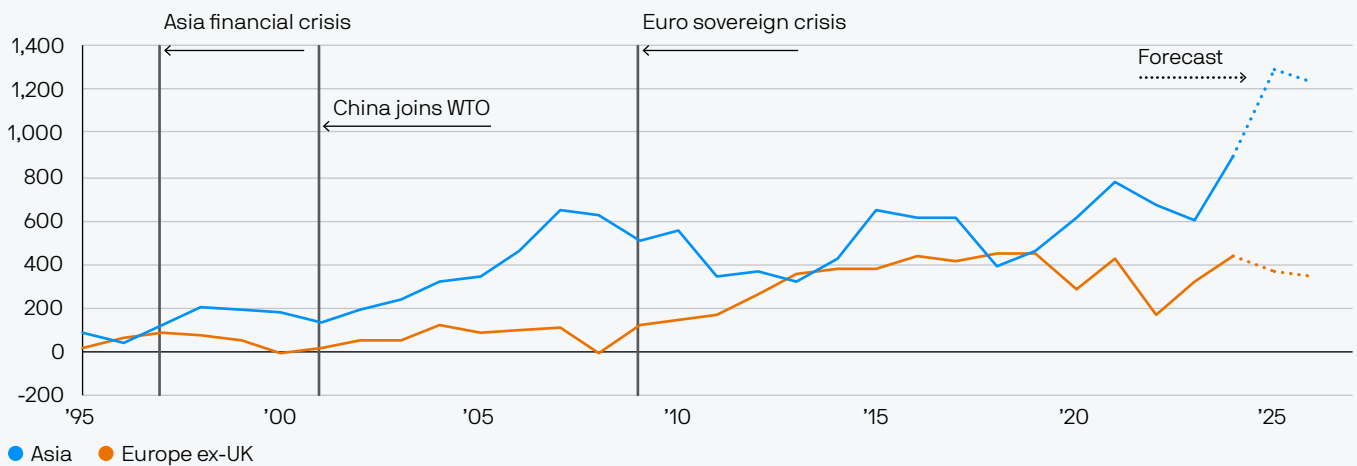
or regulated returns. For portfolios, real assets are an increasingly important complement to traditional financial assets.

In conclusion, we think markets are right to discount short-term political noise but should pay close attention to how this shifting geopolitical climate is creating structural changes that will have significant investment implications over the medium term.

Exhibit 17: Excess savings have left Europe and Asia...

Global current account balances

USD billions

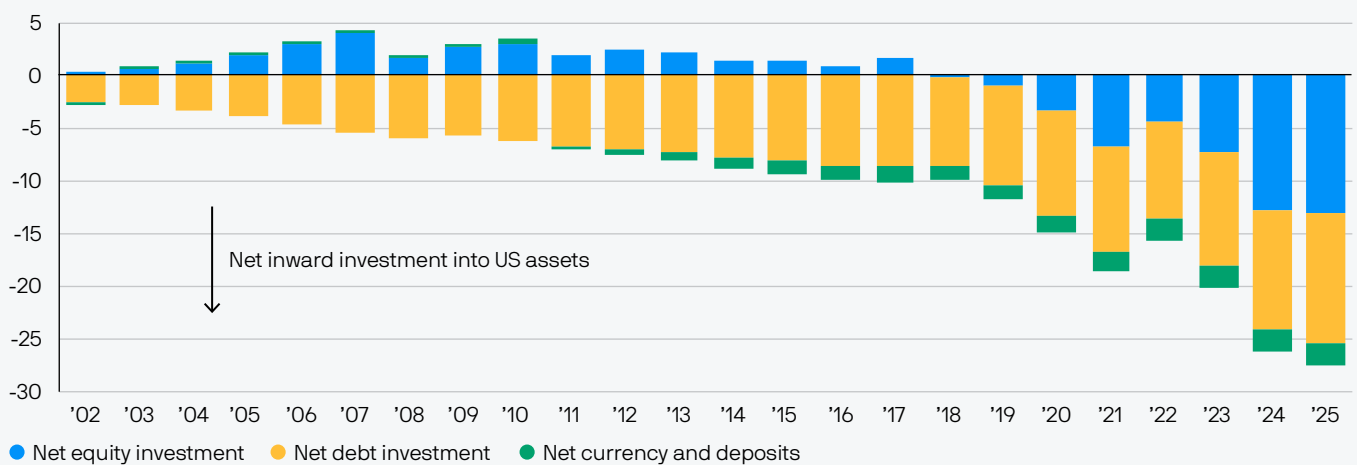


Source: IMF, LSEG Datastream, J.P. Morgan Asset Management. Europe ex-UK is represented by France, Germany, Italy, Spain and Switzerland. Asia is represented by China, Japan, Korea, Taiwan and Thailand. Data as of 8 June 2026.

Exhibit 18: ...and flowed into the US

US net international investment position

USD trillions



Source: BEA, LSEG Datastream, J.P. Morgan Asset Management. Equity and debt investments include funds. Data as of 8 June 2026.

Don't be derailed by the US midterm elections

The American electorate will head to the polls on 3 November 2026. While President Trump is not on the ballot, the elections are significant as they will determine control of Congress, which is currently held by the Republican Party. A divided government – the expected outcome based on current polls – would likely extend this period of political uncertainty.

What is needed to “win”

In the Senate, each US state appoints two senators. US senators serve six-year terms, meaning that roughly a third of the 100 Senate seats are up for grabs at every federal or midterm election. Currently the Republicans control the Senate, and of the 35 seats up for election this year (including special elections in Florida and Ohio), 22 are held by Republicans. To win control of the Senate, the Democrats would need a net gain of four seats.

In the House of Representatives, members represent individual districts within a state and serve two-year terms. Each of the 435 House seats is up for election in November. Currently the Republicans control the House. The Democrats have 212 seats and there are five vacancies, three of which were held by Democrats. If the Democrats keep those three seats for a total of 215, they only need an additional three to win a majority in the House.

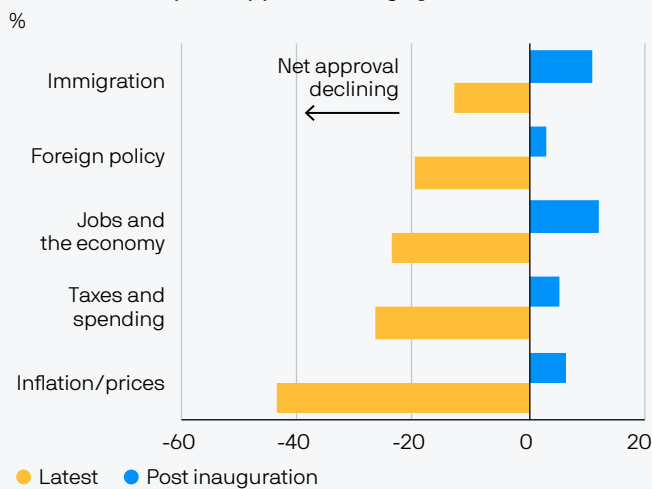
Divided government looks to be the most likely outcome

A post-2024 redistricting exercise should have played in favour of the Republicans at this year's midterms. However, current polling suggests that the Republicans face an uphill battle to retain control of the House. The President's approval ratings have deteriorated sharply (see **Exhibit 19**) with the Middle East conflict having pushed gasoline prices up to USD 4.50 per gallon.

While the elections are still some way off, cost of living pressures on US households are unlikely to ease quickly. Even once the conflict is resolved, headline and core inflation are likely to remain elevated for some time. At the same time, the administration may struggle to push through fiscal “sweeteners” to bolster support, given emerging fractures within the Republican Party. History shows that the president's party almost always loses ground in the House, as has been the case in 20 of the past 23 midterm elections. With only a narrow majority to begin with and low approval ratings, Republicans face a challenge to maintain control (see **Exhibit 20**).

Exhibit 19: The President's approval ratings have taken a hit

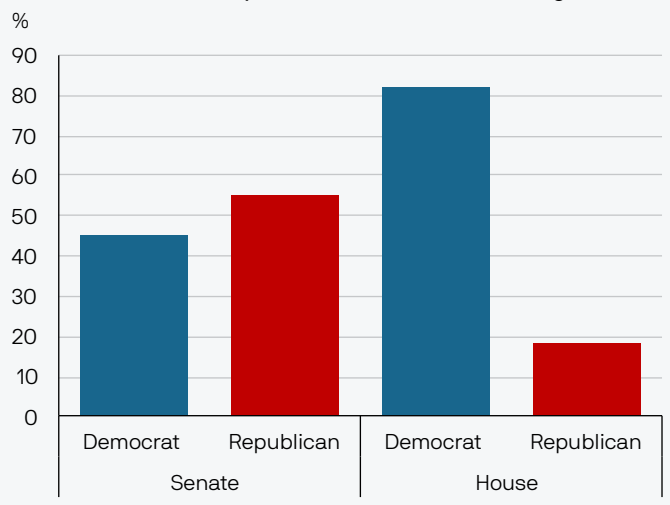
President Trump net approval rating by issue



Source: The Economist/YouGov, J.P. Morgan Asset Management. Data as of 8 June 2026.

Exhibit 20: The Republicans face an uphill battle to retain the House

Prediction market-implied odds for control of Congress



Source: Polymarket, J.P. Morgan Asset Management. Data as of 8 June 2026.

The battle for the Senate is a much closer race. Of the 35 seats up for election, the majority are considered safe for either party, meaning the outcome will hinge on a handful of competitive races. To take control of the Senate, the Democrats will need to hold onto their current seats in Georgia, Michigan, Minnesota and New Hampshire. They must also win four additional seats from those currently held by Republicans. These include North Carolina and Maine – where the Democrats are leading in the polls – as well as two seats from Ohio, Alaska, Texas, Florida, Nebraska and Iowa. The Senate is in play for the Democrats but it will be a challenge.

What this means for policy

Scenario one: Republicans lose the House but retain the Senate

If the Republicans lose the House, advancing their domestic policy agenda becomes materially more difficult, regardless of the Senate outcome. Fiscal policy is especially challenging: all revenue and spending bills must originate in the House. With the deficit already elevated (see **Exhibit 21**), a Democrat-controlled chamber would likely block any Republican attempt to deliver unfunded stimulus without concessions. There is also greater risk of political brinkmanship around the next debt limit deadline, leading to tougher budget standoffs and potential shutdown threats, though this likely won't occur until summer 2027 at the earliest.



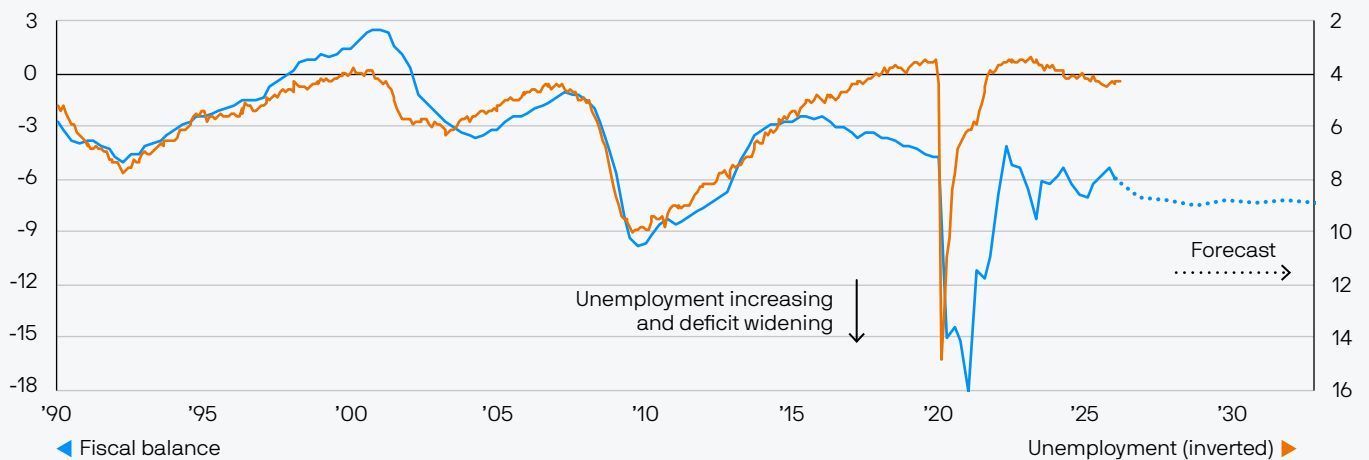
History shows that the president's party almost always loses ground in the House, as has been the case in 20 of the past 23 midterm elections.

With domestic policy options limited, the President may focus on areas where he has greater discretionary authority, such as foreign policy and trade. Post-midterms, attention could return to trade agreements that are yet to be finalised. The administration may also lean more heavily on tariff and trade authorities, such as Section 301 or Section 232, to fulfil its goal of reshoring manufacturing. How active the administration remains in foreign affairs more broadly is less certain, with the Middle East conflict having drawn criticism from the “America First”, isolationist faction of the Republican Party. On balance, however, reduced ability to shape domestic policy could increase the scope for unpredictable foreign policy.

Exhibit 21: The US budget deficit is far larger than the health of the economy would imply

US budget balance and unemployment rate

% of GDP (LHS); % (RHS)



Source: BEA, Bloomberg, BLS, CBO, LSEG Datastream, J.P. Morgan Asset Management. Forecasts are based on the CBO's latest budget and economic outlooks. Assumes tax cuts and incentive provisions in the One Big Beautiful Bill are made permanent and backdated spending cuts are not implemented. Data as of 8 June 2026.

A Democrat-controlled House would also be expected to substantially expand congressional oversight of the administration. Committee chairs would gain subpoena authority and control over investigative agendas, increasing scrutiny of the actions of the executive. While impeachment becomes procedurally more plausible under Democratic House control, the removal of a president from office would also require a two-thirds supermajority in the Senate, which is a highly unlikely scenario.

Scenario two: Republicans lose both the House and Senate

Even if the Democrats controlled both chambers, they would still find it hard to pass major legislation. 60 votes are required to overcome a Senate filibuster, while a two-thirds supermajority across both chambers is needed in a vote to overcome a presidential veto.

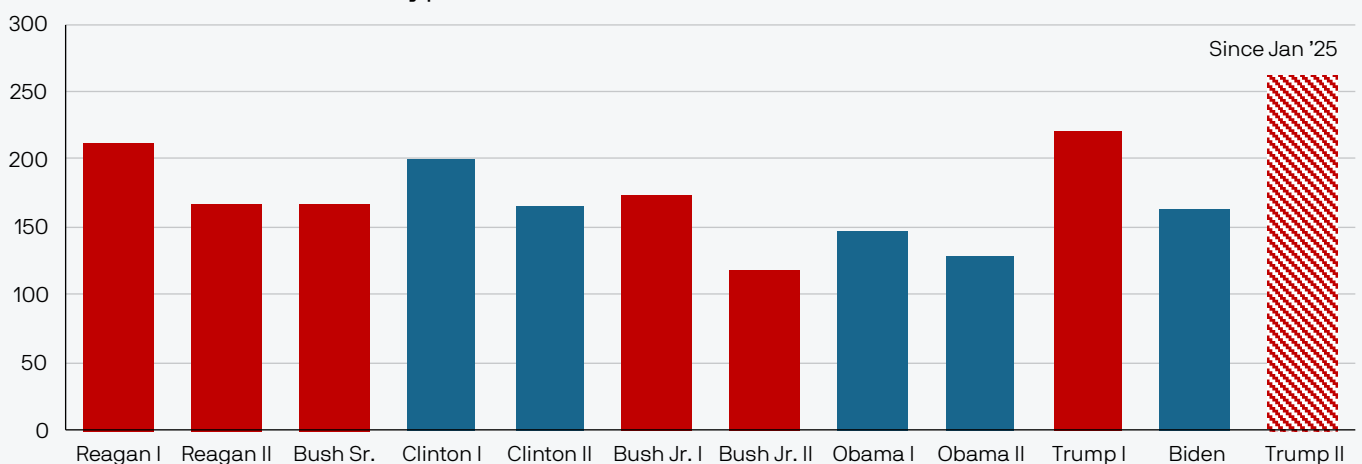
That said, Senate control would give the Democrats some additional powers. Most importantly, the Senate confirms presidential nominations by simple majority, so a Democratic majority could materially shape (or constrain) President Trump’s appointments. This, in turn, would reduce the risk of challenges to the independence of key institutions, most notably the Federal Reserve.

More of the same

Overall, in a divided government scenario – our base case – Washington would likely enter a period of policy gridlock, and the US administration would face greater oversight and scrutiny. Reduced ability to shape domestic policy increases the risk of a more unpredictable US administration on the global stage, as well as even greater reliance on executive orders (see **Exhibit 22**). That said, investors should not be derailed. As we have learned in the first 18 months of Trump 2.0, the more chaotic the political backdrop, the more likely governments globally are to administer fiscal stimulus, which explains why we expect markets to continue to shrug off political noise.

Exhibit 22: The US administration is already breaking records for the use of executive orders

Number of executive orders issued by presidential term



Source: The American Presidency Project, J.P. Morgan Asset Management. This chart does not include other forms of written presidential orders, such as memorandums, or discretionary executive actions not accompanied by a published presidential directive. Data as of 8 June 2026.

Private credit will not upset risk sentiment

Private credit’s rapid growth and some recent negative headlines about the asset class have led some investors to question whether private credit could become the source of a risk-off event. We see a number of factors that mitigate the risk of private credit posing a systemic threat to global risk markets.

Risk one: Private credit funding dries up

The first route by which private credit could become a systemic risk is if funding in the asset class dried up, making it difficult for businesses to roll over loans or achieve new credit. This situation could put pressure on public market alternatives, like high yield debt, and ultimately starve businesses of the funds needed to support economic activity, which would affect the broader economy. We see several factors that limit that risk.

First, the vast majority of private credit is invested through closed-end institutional vehicles, rather than semi-liquid retail structures. While retail funds have attracted attention because of redemption pressures, they account for only around 15% of global private credit assets. Institutional financing, which accounts for the lion’s share of the capital in the asset class, is largely invested in funds that do not offer periodic liquidity and is therefore invested long term (see Exhibit 23).

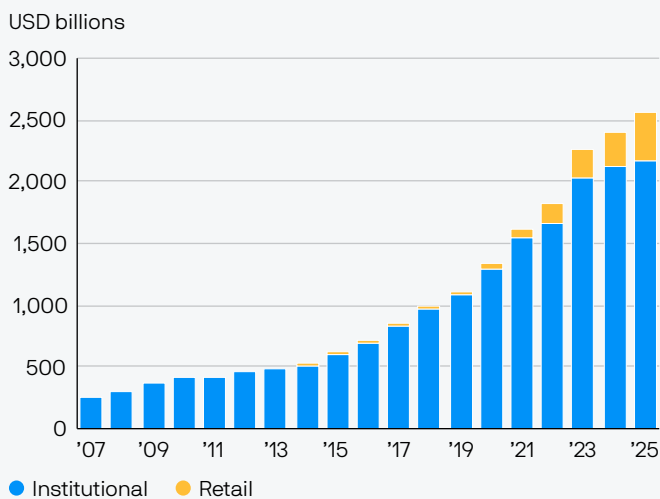


The asset class still represents a relatively small share of total corporate borrowing, credit fundamentals remain broadly resilient, dry powder remains abundant, redemption limits reduce liquidity risks and bank exposure remains modest.

Indeed, institutional investors continue to allocate capital to private credit strategies despite recent concerns around the asset class. While fundraising has moderated from its post-pandemic peak, demand from long-term investors remains positive (see Exhibit 24).

Exhibit 23: Institutional investors are the dominant investors in private credit funds

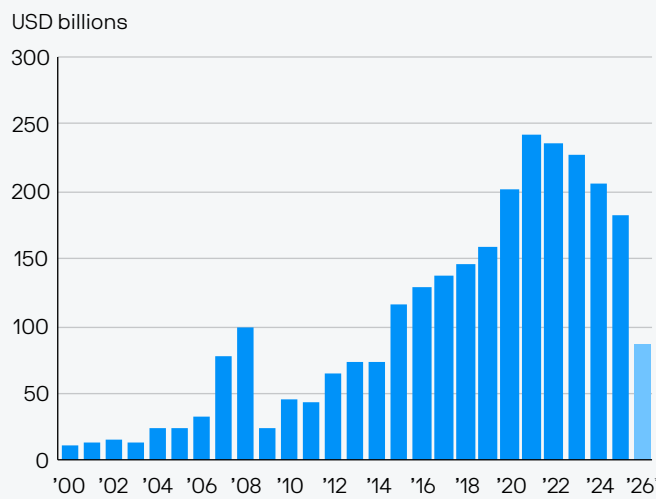
Global private credit assets under management by channel



Source: Pitchbook, J.P. Morgan Asset Management. Data as of 8 June 2026.

Exhibit 24: Capital raising has slowed over recent years, but demand still appears healthy

Global private credit capital raising



Source: Preqin, J.P. Morgan Asset Management. Private credit includes direct lending, mezzanine, special situations, distressed debt, fund of funds and venture debt. * 2026 is year to date. Data as of 8 June 2026.



While potential stress in the private credit market is one of the many risks worth monitoring, we do not currently see it as a sufficient reason to abandon a risk-on view for 2026.

Importantly, even if new fundraising slowed sharply, the industry has accumulated substantial dry powder in recent years (see **Exhibit 25**). This stock of uncalled capital provides a buffer for managers to continue deploying capital and support borrower refinancing activity for an extended period without relying on additional fundraising. This provides an important safeguard against any near-term slowdown in fundraising from retail investors.

It's important to also remember that despite its rapid growth, private credit remains a relatively small component of the broader financing ecosystem. Private credit accounts for roughly 9% of corporate borrowing, meaning the overwhelming majority of corporate financing continues to come from banks, public debt markets and other sources of capital.

Risk two: Private loan losses affect solvency and create problems elsewhere in the financial system

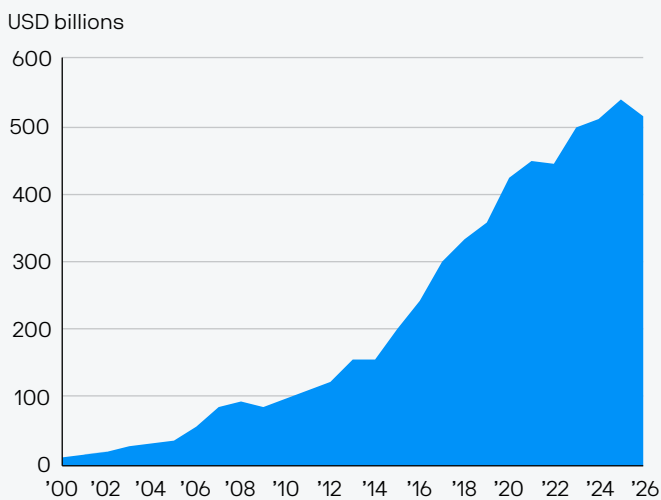
The second risk is that rising defaults across private credit portfolios result in losses that affect balance sheets elsewhere in the financial system, creating systemic problems. This risk has garnered attention because a high proportion of direct lending funds have built significant exposure to software and technology companies over the last decade (see **Exhibit 26**).

The behaviour of public equity prices highlights that rapid advances in artificial intelligence (AI) have introduced greater uncertainty around some of these companies' long-term earnings prospects and their ability to service future debt obligations. The concern is that defaults and losses could rise over the coming years, particularly in selected sectors.

However, there is little evidence of a broad deterioration in aggregate credit fundamentals today. Default rates have edged higher but remain low by historical standards. And while broader measures of distress such as payment-in-kind (PIK) interest, covenant amendments and borrower waivers rose meaningfully over the last few years, they have moderated over the last few quarters.

Exhibit 25: Private credit managers have vast amounts of dry powder to deploy

Global private credit dry powder

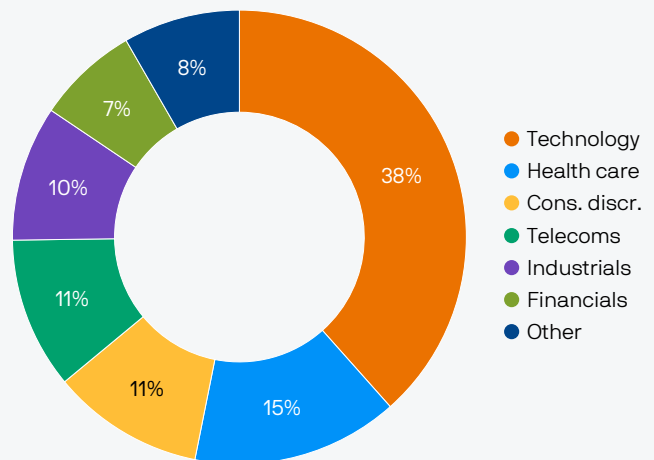


Source: Preqin, J.P. Morgan Asset Management. Dry powder refers to capital that has been committed to a private credit fund but not yet deployed. Private credit includes direct lending, mezzanine, special situations, distressed debt, fund of funds and venture debt. Data as of 8 June 2026.

Exhibit 26: Private credit deals have been concentrated in tech

Global private credit composition by industry

Share of total aggregate deal value over the last five years



Source: Preqin, J.P. Morgan Asset Management. Other includes energy, materials, utilities, real estate and non-classified categories. Data is latest available as of 8 June 2026.

In addition, for a solvency event to become systemic, losses must impair the institutions responsible for creating credit. Historically, these events have occurred when losses were concentrated within highly leveraged banks.

During the Global Financial Crisis (GFC), many banks operated with leverage ratios of around 10x and had substantial exposure to mortgages. In some cases, residential and commercial real estate lending accounted for close to half of total loan books. As losses mounted, bank capital was eroded, forcing institutions to deleverage, reduce lending and raise capital. The resulting contraction in credit availability amplified the economic downturn and transformed a housing correction into a broader financial crisis.

The structure of today's private credit market is materially different. Most credit risk is held by pension funds, insurers, sovereign wealth funds and other long-term institutional investors, rather than deposit-taking banks. While global banks remain involved through subscription lines, warehouse facilities and other financing arrangements, their exposure to private credit is estimated to be around 12.5%. In addition, private credit funds typically employ relatively modest leverage, often around one turn of debt, compared with the substantially higher leverage employed by banks prior to the GFC.

As a result, even if defaults were to rise meaningfully, losses would be less likely to impair the institutions responsible for creating credit across the broader economy than they were in 2008. The more likely outcome would be weaker investor returns, lower future commitments and, over time, less available credit within the asset class, rather than the type of balance-sheet shock required to trigger a systemic credit crunch.

A risk, but not the main event

Private credit will undoubtedly experience periods of stress, and it's likely that defaults will move modestly higher through 2026. However, for private credit to derail a constructive outlook for risk assets, those stresses would need to constrain the supply of credit to the broader economy or trigger a destabilising solvency event.

Current evidence suggests the risks are fairly low. The asset class still represents a relatively small share of total corporate borrowing, credit fundamentals remain broadly resilient, dry powder remains abundant, redemption limits reduce liquidity risks and bank exposure remains modest.

While potential stress in the private credit market is one of the many risks worth monitoring, we do not currently see it as a sufficient reason to abandon a risk-on view for 2026.

The risks are clear and so is the protection

The geopolitical crisis in the Middle East is the latest in a list of political events that investors have been bombarded with in recent years. This appears to be affecting household savings behaviour. European households are more reluctant to spend than before the pandemic and are therefore amassing vast war chests of savings (see **Exhibit 27**). And, perhaps due to the constant barrage of political headlines, households are keeping a large proportion of these additional savings in cash.

The opportunity cost of fear is, however, starting to prove sizeable. Higher rates of inflation are eroding the value of the cash on deposit, leaving a large loss relative to the purchasing power had the savings been invested (see **Exhibit 28**).

Nevertheless, the risks investors cite are understandable. We highlight two key risks and how investors can be invested, but with some protection against them.

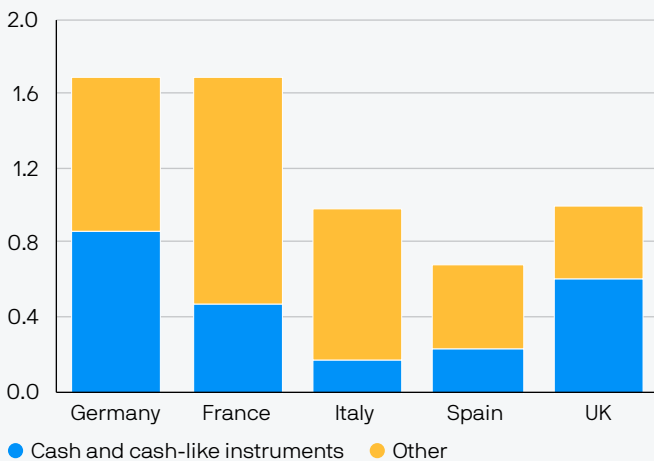


Any signs of more modest demand for AI than is currently baked into expectations would feed concerns about excess capacity, lower prices and margin compression.

Exhibit 27: Savers have been building vast cash piles since the pandemic

Household savings since the start of the pandemic

EUR trillions, UK is GBP trillions

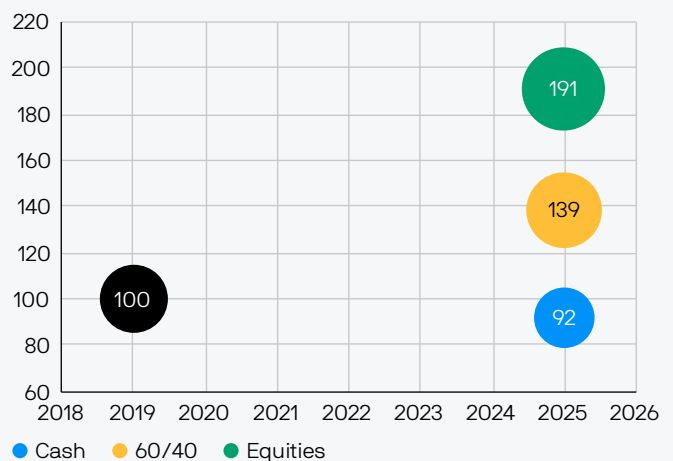


Source: Bundesbank, European Central Bank, IMF, INSEE, Istat, LSEG Datastream, OECD, ONS, J.P. Morgan Asset Management. Data as of 31 December 2025.

Exhibit 28: Cash is certainly not king in a higher inflation world

Total return of £100 in real terms

GBP



Source: Bloomberg, MSCI, J.P. Morgan Asset Management. Equities: MSCI World GBP Index; Bonds: Bloomberg Global Agg GBP Hedged Index; Cash: three-month GBP deposit. Past performance is not a reliable indicator of current and future results. Data as of 8 June 2026.

The Strait remains closed

The risk: The main risk to our base case scenario concerns the evolution of the geopolitical crisis between the US and Iran. In the recent past, negotiations have repeatedly come close to an agreement, only to collapse at the last moment. There are four particularly tricky aspects of the negotiation. Iran wants to have: some medium-term control over the Strait of Hormuz, potentially collecting tolls from passing vessels; sanctioned Iranian assets to be unfrozen; and reassurance of no further attacks from Israel on Lebanon. The US wants assurances that Iran will end its nuclear capability.

In our core scenario the Strait will open with many of these details left to be resolved at a later date, simply because it's too costly for either the US or Iran to be the cause of a global recession. However, it is plausible that political reasoning does not coincide with economic reasoning.

A prolonged crisis should, therefore, be treated as a key risk, including the possibility that the Strait remains closed for an extended period. This situation could lead to an oil supply shortage, potentially pushing oil prices above USD 150 per barrel. In this environment, both the consumer and business engines of growth would be affected, likely leading to an outright global recession.

With midterm elections approaching, the US government could introduce additional fiscal stimulus measures to mitigate the negative impact of higher gasoline prices. This action could limit the growth slowdown but with negative implications for the already high deficit-to-GDP ratio, which may unsettle government bond markets.

European activity could be more at risk given the region's energy vulnerability. The European Commission appears inclined to allow only limited flexibility for member states to implement support measures for consumers hit by higher energy costs, although this tone may soften in an extreme scenario. The energy and geopolitical crisis could increase pressure on European governments to step up investment in infrastructure, security and defence, though implementation timelines would likely be long. Asia could also be vulnerable, given many countries' high dependence on energy imports. This could translate into deteriorating trade balances, lower foreign currency reserves and weaker currencies.

While global growth would slow, inflation would rise, resulting in a stagflationary scenario. At that point, central banks would face a difficult trade-off: raise rates to fight inflation or stay on hold to avoid further damaging growth. With inflation already above target for some years now, central banks may lean towards tighter policy to prevent inflation expectations from de-anchoring and to avoid repeating the mistakes made in 2022, when delayed tightening contributed to an acute inflation episode.

The markets: A prolonged closure of the Strait is a challenging backdrop for both stock and bond markets. In equities, energy importers and rate-sensitive sectors are likely to be hit hardest. A more defensive, quality-focused strategy would be the most appropriate choice to help mitigate the impact of an equity market drawdown. It is unclear whether global technology would prove defensive in this environment. The ongoing scarcity of growth could lead global capital to crowd into this area of the equity market. However, rising inflation and fiscal support that leads to higher long-term bond yields could challenge growth stocks, particularly given that a likely fall in business investment would further hinder tech stocks' ability to demonstrate return on their investment.

In an acute inflation shock, commodities would perform well and real assets, such as timber and core infrastructure, would likely offer a strong hedge. In a chronic inflation scenario, gold could also play an important diversifying role, albeit with potentially elevated volatility.

Tech euphoria fades

The risk: A strong first quarter earnings season for tech has revived investor appetite, but positioning has been selective, favouring AI supply chain component makers and exposure to emerging markets, particularly South Korea and Taiwan. The key risk is that AI sentiment weakens if demand for AI infrastructure proves overstated; the main trigger could be signs of slowing demand from some of the highest-profile model providers, or perhaps more sceptical tones from the broader CEO universe. Any signs of more modest demand for AI than is currently baked into expectations would feed concerns about excess capacity, lower prices and margin compression. US growth would slow as AI capex stalls and a negative wealth effect for US households could be detrimental to US consumer spending.

Markets: This scenario would be negative for equities, particularly in the US and emerging Asia. Europe's relative lack of technology would turn from a perceived weakness to a perceived strength. Defensive stocks would likely outperform cyclicals. Concerns would intensify around private equity and private credit, given their technology exposure.

In this scenario we would expect core fixed income to provide valuable insurance as the correlation between equities and bonds would turn negative again. High-quality, long-duration fixed income could provide meaningful upside. If the 10-year US Treasury yield fell 200 bps, which would be likely in a recession scenario, this would represent a 20% return over 12 months.

It's not all downside, there is an upside risk that is not priced

The risk: There is a scenario whereby a rapid resolution to the conflict in the Middle East coincides with meaningfully lower energy prices next year as the structural damage to OPEC affects oil producers' behaviour. Each major producer would try to extract as much value as possible from their remaining oil assets, providing a major growth tailwind. It is also possible that as companies adapt to new technologies and realise the productivity gains, we will see a much greater uplift in corporate earnings across the broader universe. The combination of these two possibilities would create a "goldilocks" scenario with positive momentum into 2027.

Markets: We would expect this environment to be very constructive for global risk assets. Investors sitting on cash should be aware that markets aren't quite priced for perfection.

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