

Global Asset Allocation: The View From Europe

October 2025

Outlook

- We maintain a balanced view on risk assets, buoyed by fiscal stimulus and accommodative central bank policies helping support economic growth, against a backdrop of elevated valuations and lingering inflation.
- US economic growth is supported by fiscal spending and the possibility of further Fed easing, as concerns have shifted to the labour market.
- Outside the US, growth is supported by fiscal and monetary stimulus helping offset potential weakness from tariffs. Despite the political uncertainty in France, increased fiscal spending in Germany should lead to stronger economic growth in Europe over the medium term. A de-escalation in trade tensions and pro-growth policy shift are improving sentiment towards China.
- Key risks to global markets include the lingering impacts of global trade tensions, sticky inflation, potential policy missteps by central banks, a weakening labour market and ongoing geopolitical tensions.

Themes driving positioning

Staying power?

Hopes for lower interest rates have sparked several small-cap rallies in recent years, seeing them finally outperform large-caps, but unfortunately the rallies have been short-lived. The latest Fed cut has reignited enthusiasm for small-caps, now seeing them ahead of large-caps by nearly 4% since April lows, with most of the gains coming since August. It may not just be the Fed reengaging on rates cuts this time that is driving outperformance, as other tailwinds may provide staying power. Among these is the recent passing of the One Big Beautiful Bill, a resurgence in M&A activity, the administration's push on deregulation and a de-escalation in trade tensions. And while valuations favour small-caps relative to large-caps and small-caps are seeing an uptick in earnings expectations, the risk of inflation keeping rates elevated and the recent weakness in the labour market possibly pointing to slower growth warrant a balanced view.

Small chance?

As of 30 September 2025

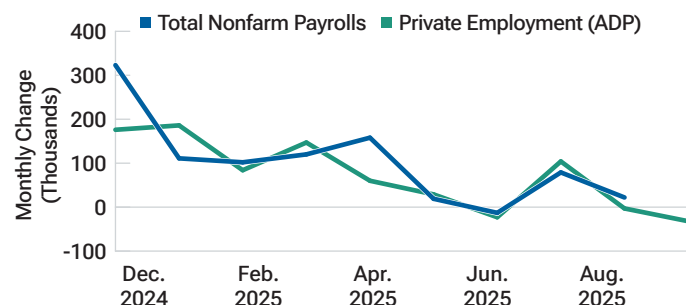


Private matters

Outside of the negative economic impacts of a prolonged government shutdown, the direct impact of no publicly available data could really challenge an already embattled and data-dependent Fed. Having just made their first rate cut since going on pause late last year has heightened the focus on the trajectory of the labour market. With the last read from August showing a steep decline in job growth and the unemployment rate jumping to a four-year high of 4.3%, investors were eager to see the—now delayed—September release. Last month's revisions showing 911,000 fewer jobs being added between April 2024 and March 2025 gave investors another reason to worry and question the reliability of the data. In the absence of public data, private market data are what matter, and ADP's September update showing a loss of 32,000 private sector jobs furthered concerns of a cooling labour market. With the Fed in the dark, the longer the absence, the bigger the chance of an unwelcome data dump.

Fortune-telling

As of 30 September 2025



Past performance is not a guarantee or a reliable indicator of future results.

Sources: Figure 1—Bloomberg Finance L.P. and S&P. Please see Additional Disclosures for more information about this sourcing information. Figure 2—ADP National Employment Report.

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Asset class positioning

Equities



- We maintain a neutral stance on equities, reflecting a balanced view between decent fundamentals and expensive valuations with risks for a broad range of outcomes both to the upside and the downside.
- Within regions, we continue to find more attractive opportunities outside the US, particularly in value, driven by more compelling valuations and improving sentiment, which are supported by fiscal spending tailwinds and accommodative central bank policies.

Fixed income



- We maintain an underweight to bonds as inflation and funding requirements associated with US fiscal stimulus could keep upward pressure on rates, particularly at the long end.
- We remain underweight on US Investment Grade Aggregate in particular as this asset class remains vulnerable to upward pressure stemming from the US government's fiscal funding needs.

Cash



- We continue to maintain an overweight position in cash due to its reasonable yields and limited duration risk.
- The sector offers liquidity to take advantage of market opportunities amidst market dislocations.

Equity market views

	Underweight Neutral Overweight					▼ or ▲ Month-Over-Month Change
Change	Underweight	Neutral	Overweight	Underweight	Overweight	
Regions						
US	U					US equity valuations are very elevated but are supported by strong and improving fundamentals. The earnings outlook is favorable, but any hiccups could be punished more harshly than normal.
Europe ex-UK		N				Increased fiscal spending should lead to stronger earnings growth over the medium term. We are also seeing a gradual move towards less regulation and more emphasis on innovation.
UK			O			Valuations are attractive, and the longer-term earnings growth outlook is healthy. However, budget concerns remain a significant headwind, and the inflation outlook remains volatile.
Japan		N				The economic outlook has improved considerably with Sanae Takaichi set to become prime minister and trade policy concerns waning. However, valuations now reflect considerable optimism.
Australia	U					Valuations are somewhat elevated despite signs that economic momentum is peaking and earnings growth will be modest.
Emerging Markets (EM)			O			EM stocks have benefitted from capital flight out of the US, whilst the global economy is benefitting from easing trade tensions and rising fiscal stimulus. A weaker US dollar offers a further tailwind.
China		N				While economic activity remains modest, sentiment has improved significantly. We expect further improvement in fiscal stimulus and the more market-friendly approach from Beijing to continue.
Style and Market Capitalisation						
Global Growth vs. Value ¹		N				US growth equity fundamentals continue to accelerate. Recently introduced tax incentives should also help. However, extended valuations make risk/reward less attractive. Regarding value, there is potential for deregulation. Fiscal policy, reshoring and Fed cuts to provide support. However, economic growth and housing market activity remain modest but improving.
Global Small-Cap vs. Large-Cap ¹ ▲			O			For large-caps, elevated valuations and concentration risks remain a concern. However, very strong and improving fundamentals have justified valuations thus far. Regarding small-caps, a muted economic growth outlook and sticky inflation pose challenges. However, Fed cuts, deregulation, fiscal stimulus and stronger mergers and acquisitions and IPO activity are supportive.

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These views are informed by a subjective assessment of the relative attractiveness of asset classes and subclasses over a 6- to 18-month horizon.

¹ For pairwise decisions in style and market capitalisation, positioning within boxes represents positioning in the first-mentioned asset class relative to the second asset class.

Fixed income market views

		Underweight Neutral Overweight			▼ or ▲ Month-Over-Month Change
Change		Underweight	Neutral	Overweight	
Euro Government Bonds	U				While large, ongoing issuance is a headwind for government bonds, geopolitical risks are a tailwind. We expect one more cut from the European Central Bank (ECB) based on greater downside risks to economic growth and inflation than what the market is pricing.
Euro Inflation Linked				O	Inflation is likely to fall below the ECB's 2% target in 2026 due to currency, oil and goods deflation, but this is all already priced in, and the ECB expects it to happen. We have modestly reduced the allocation to inflation-linked bonds, but we remain overweight due to risks of higher inflation because of the effects of tariffs.
Euro Investment-Grade (IG) Corporates			N		Credit fundamentals are supportive, with spreads expensive relative to history.
US IG Aggregate	U				Fed cuts and risks of sticky inflation give the curve a steepening bias. Credit fundamentals are still supportive, with spreads expensive relative to history.
Global High Yield				O	Spreads are approaching historically tight levels but are supported by strong fundamentals. The sector still offers a healthy yield, with measured expectations for increases in defaults.
EM Dollar Sovereigns				O	Yields are attractive and there is room to cut with lower inflation, though higher long-end US interest rates and the unclear impact from tariffs on economies are challenges.
EM Local Currency				O	US dollar weakness has been a tailwind and is expected to continue; however, longer-term fiscal challenges from tariffs remain unclear.
EM Corporates				O	The sector offers a shorter duration than that of EM dollar sovereigns. Spreads are tight, but total yields remain attractive relative to some other fixed income sectors.
Currency Market Views					
EUR vs. USD			N		Although the economic reaction to Trump tariffs remains resilient, the eventual effect of tariffs, French political uncertainty and EUR appreciation will push the ECB to cut once more reluctantly. This is a more dovish outcome than what the market prices. Only a slight improvement in the French political uncertainty or the geopolitical situation in the east of Europe is needed for the Euro to strengthen.
EUR vs. JPY			N		Takaichi's fiscal policies are likely to result in a Bank of Japan (BoJ) that is further behind the curve or that will need to start hiking more than the market expects. The yen is a safe-haven currency. Current valuations are attractive. However, given the recent volatility in the yen and uncertainty about BoJ policy, we remain neutral.

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