

Quarterly Equities and Multi Asset Outlook Is anyone swimming naked?

Navigating frothy markets

Q4 2025

Contents

CIO foreword	4
Multi asset	8
Global	10
Global technology	12
UK	14
Japan	16
Asia Pacific ex Japan	18
Emerging markets	20
Impact	22
Global research	24
Convertibles	26

The value of investments will fluctuate, which will cause prices to fall as well as rise and you may not get back the original amount you invested. Wherever mentioned, past performance is not a guide to future performance.

The views expressed in this document should not be taken as a recommendation, advice or forecast and they should not be considered as a recommendation to purchase or sell any particular security.



Is anyone swimming naked?

The recent flurry in AI deals is fuelling speculation of an AI bubble and prompting investors to ask if we've reached a peak in equity markets.

For now, there are no clear challenges to companies' earnings, which are the real drivers of risk markets, but we need to stay watchful. Tariffs may not be the prevailing narrative, but that doesn't mean their impact will disappear. Localised credit episodes are contained but need to be monitored.

Undoubtedly, there are pockets of excessive exuberance and inflated expectations, but the rerating in markets has often been driven by a handful of stocks as index concentration remains high. There are plenty of stocks that still have meaningful upside potential.

Importantly, when conclusions appear to become almost obvious (Do we have a bubble? Of course!!!), that is the time for investors to seek dissent, to find those around them who think differently and listen to the logic behind their opinions.

There is always someone swimming naked but, when the tide goes out, there will still be more than a few who have their costumes firmly on.

Dive deep to surface the winners

Warren Buffett famously remarked **“you don’t find out who’s been swimming naked until the tide goes out”**.

The recent flurry of AI deals, creating increasing interdependencies among some of the world’s largest AI players, is bringing back memories of the dot.com bubble. The key question in investors’ minds is whether we are now facing an AI bubble. The second derivative of the same question is whether we have reached a peak in equity markets overall, after a remarkable run. In our opinion, as is often the case, the answer’s not straightforward.

Amid ongoing macroeconomic and geopolitical uncertainty, we continue to witness an element of ‘crises fatigue’ from investors. In the face of global conflict, political shocks and policy swings, sentiment on risk markets has remained sanguine. Until now, such resilience has been justified, as macroeconomic datapoints and geopolitical events have a durable impact on risk assets only when company earnings are impacted. However, we recognise that it’s only a short leap from ‘fatigue’ to ‘complacency’.

For now, there are no clear challenges to companies’ earnings. But, we still have not seen the full impact of tariffs. The fact that the market narrative is less focused on tariffs, doesn’t mean that their concrete effects will disappear. Also, while some recent localised credit events in the United States appear, for now, to have had limited impact and contagion, that doesn’t mean that we should let our guard down.

A restless political landscape, increased scrutiny of central banks, high sovereign debt levels (particularly in the US), a challenge to the availability and veracity of macroeconomic data, and index concentrations, are other potential sources of instability to monitor.

As investors, we know that dismissing the whole market with a broad brush has historically been the worst recipe for long-term returns. Let’s not forget that missing just 30 of the best days in the 20 calendar years to the end of 2024 would have reduced the annualised total returns of the MSCI AC World (8.2%) and S&P 500 (10.4%) indices to 1.2% and 1.3% respectively¹. Crucially, many

of those best performing days have followed some of the worst performing days, making trading amid such market gyrations difficult to time.

AI capital expenditure (capex), market concentration, and the likelihood of certain elevated earnings expectations being met, are all topics that are being debated across the M&G Equities and Multi Asset team.

Undoubtedly, there are pockets of excessive exuberance and inflated expectations out there. As our Asia investment team reminds us, a number of Chinese semiconductor names are still at the nascent growth stage of their evolution and yet the market is ascribing large amounts of value to businesses that have yet to prove they can successfully perform on a commercial scale. In addition, there are also a number of second tier AI names in Korea and Taiwan that are benefiting from near-term strong demand but, ultimately, have little in the way of long-term ‘moats’ to their businesses.

However, there are still companies that offer share price upside. Some of them are linked to AI, such as service providers and companies across different sectors that benefit from the use of AI. Our Technology investment team reminds us that, for investors, discerning the winners from the losers requires rigorous due diligence, asking questions such as ‘who is actually buying?’, ‘who is using the technology at scale?’, and ‘what workflows are changing?’.

There are also companies that are not directly driven by the AI theme and are simply good companies that have been left behind in the chase for ‘everything AI’.

Seek dissent

Our experience tells us it is at times like these that we have to dig deeper. Two elements become crucial for asset managers: first, having the right research capabilities and knowledge in place to distinguish materiality from hype; and second, being equipped with sufficient diversity of age, gender, cultural and social background in a team to have different points of view. When conclusions appear to become almost obvious (Do we have a bubble? Of course!!!), that is the

¹Source: M&G Investments, Bloomberg. Data is total returns in USD over a 20-year period through 31 December 2024.

time for investors to seek dissent, to find those around them who think differently and listen to the logic behind their opinions.

The next few pages will offer some colour on the investment decisions that the M&G Equities and Multi Asset investment team has been making across markets and asset classes, and where we believe we can still find upside returns.

“ When conclusions appear to become almost obvious, that is the time for investors to seek dissent, to find those around them who think differently ”

At an asset allocation level, in our Multi Asset portfolios we maintain a broadly neutral equity exposure, having reduced some areas that we felt had performed particularly strongly.

Such ‘cuts’, however, are very localised. Many clients have been asking us if equity market valuations have reached a peak. It is true that many of the largest global markets’ valuations are higher than where they were 10 years ago, as this year’s strong run has only, in part, been supported by earnings upside. However, such rerating has often been driven by a handful of stocks. Index concentration remains high. In the S&P 500 Index, 23 stocks constitute half of the index weight, while the same figure is 16 for the FTSE All-Share Index and 35 for the MSCI Asia Pacific ex Japan Index, respectively².

The good news is that there are plenty of stocks that have not seen the same rerating and have meaningful upside potential. We are not the only ones looking

beyond the small number of index behemoths, and we are seeing an improvement in dispersion of returns: since 2020 the price dispersion among stocks in the MSCI AC World Index has been fairly consistently above its ten-year median, with only some short-lived instances of price compression. Even the S&P 500 Index – where market news flow has been dominated by the Magnificent 7 (Mag 7) – has seen 113 stocks outperform the median return of the Mag 7-year to date³.

Such dispersion of returns cements opportunities for active investors. Hence, we remain very focused on underlying companies rather than sector or country choices and continue to find significant opportunities in markets outside of the US, including Europe and Asia. That said, the strong rally in Korea and China has led us to reduce some of our positions more recently.

Europe has had a pause in its strong run, given the political turmoil in France, a disappointing earnings season, and the fact that infrastructure investment is yet to materialise. After the strong run in cyclical stocks, we have seen opportunities among a number of higher-quality companies that have been left behind. European markets could find a renewed tailwind ahead as we get closer to the disbursement of infrastructure spending in Germany.

We have also seen a number of quality consumer-related businesses being materially de-rated in valuation terms in Asia. In recent weeks, we have trimmed some of our technology ‘winners’ and added to a selected number of consumer stocks.

Globally, including in the US, we continue to like technology, particularly linked to AI, and we are also finding opportunities in healthcare after a long period of underperformance. In AI, not all stocks are created equal, and fundamentals need to warrant the increased valuations. We are currently finding interesting pockets of value in AI-related service providers.

²Source: M&G Investments, LSEG DataStream, 30 September 2025

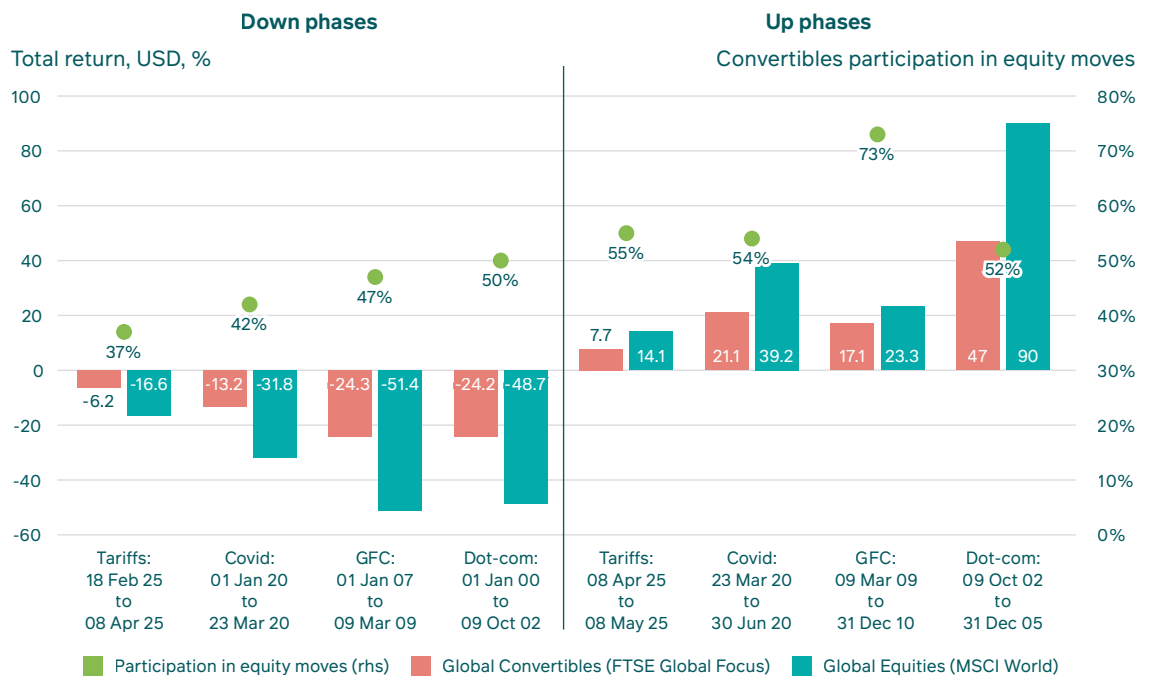
³Source: M&G Investments, Bloomberg, 30 September 2025

Within fixed income, we maintain a broad diversification across geographies and we particularly like Emerging Markets (EM) local currency bonds. Our allocations combine both nominal and inflation-linked bonds, reflecting elevated real yields in some regions.

We believe diversification, both across and within asset classes, is the best recipe for generating differentiated returns while building in portfolio resiliency in the face of an uncertain macroeconomic environment.

Perhaps this is a good time to bring up one asset class that has proven resilient during market downturns: Convertible Bonds. During market downturns – either because of bubbles bursting (such as in 2000-2001), or due to geopolitical or macroeconomic concerns (such as during the Global Financial Crisis or on Liberation Day), or when suddenly one of those ‘unknown unknowns’ occurs (such as COVID-19) – Convertibles have outperformed broad equity markets; by capturing more of the upside than the downside – shielded by the inbuilt protection of the bond floor and supported by the upside of their equity component.

Convertibles: Greater participation in equities' upside than downside during downturns



Source: M&G Investments, Bloomberg, September 2025

In the high seas of markets, there is always someone swimming naked. When the tide goes out, however, there will still be more than a few who have their swimming costumes firmly on.

We wish you an enjoyable and – hopefully – interesting read.



Fabiana Fedeli
Chief Investment Officer, Equities,
Multi Asset and Sustainability





Multi asset

Christophe Machu
Deputy Fund Manager



Misplaced faith can leave investors exposed

The past quarter has delivered another strong performance across global equity markets. However, gains were driven less by earnings growth and more by re-ratings, as optimism outweighed hard fundamentals. Emerging markets such as Brazil and Korea enjoyed sharp rallies, while US equities also delivered robust returns. Europe, by contrast, lagged with relative gains from earlier in the year fading. Against this backdrop, it is tempting to celebrate the resilience of risk assets – but it is equally important to ask: what assumptions are carrying us forward, and which may prove frothy?

Metaphorically, froth is the foam on the surface: it looks abundant, it feels buoyant, but it is insubstantial. Underneath, the real currents matter far more. As investors, the challenge is to distinguish between surface froth – momentum, narratives, short-term optimism – and the deeper currents of sustainable growth, valuation discipline, and structural shifts in policy.

Warren Buffett famously remarked that **“you don’t find who is swimming naked until the tide goes out”**.

In markets, that moment of exposure often comes when widely-held beliefs prove unstable. A good example is the role of government bonds in portfolios. For decades, bonds and treasuries were seen as unquestioned sources of diversification, expected to provide protection when equities sold off. But 2022 revealed that this assumption was not as stable as many thought. Bonds and equities fell together, leaving investors exposed. The properties of an asset are not permanent – they depend on starting valuations and on the collective faith that sustains them. When that faith is misplaced, the tide goes out and reveals who has been swimming naked.

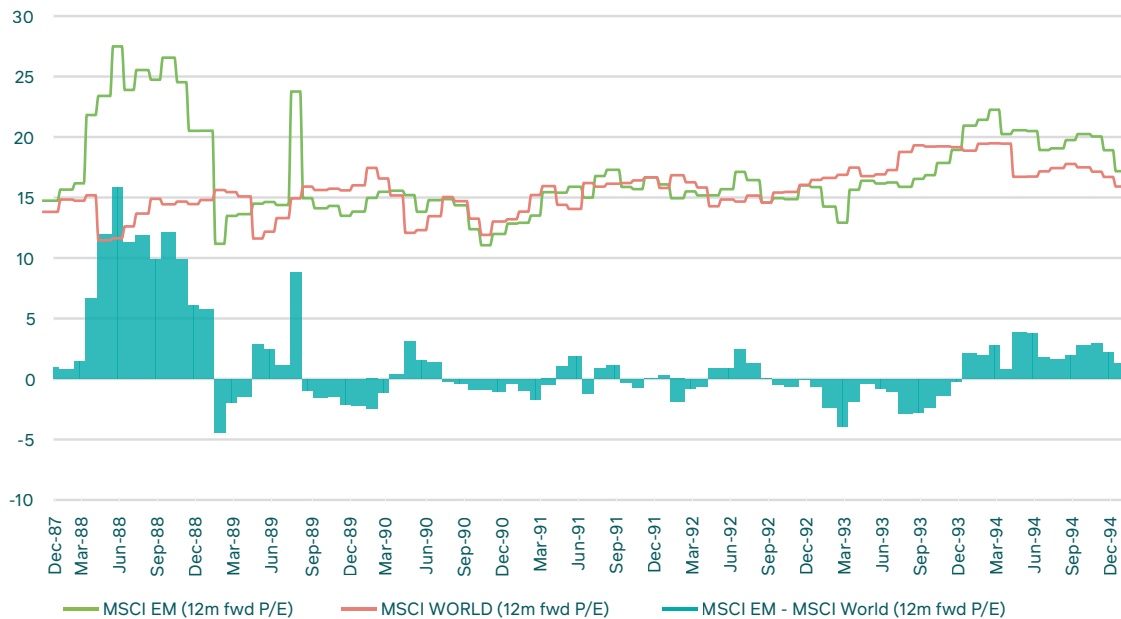
Challenging the EM narrative

This lens is especially relevant when comparing emerging markets (EM) and developed markets (DM). The prevailing narrative assumes that EM assets are inherently riskier and should always trade at a discount. Yet fundamentals do not always confirm this, and history shows exceptions: EM equities even traded at higher valuations than DM equities for part of the 1980s and 1990s.

“In markets, that moment of exposure often comes when widely-held beliefs prove unstable”

EM equities have not always traded at a discount to DM equities

Price-to-earnings ratio, MSCI World and MSCI EM Indices (1988-1994)



Source: LSEG DataStream, October 2025. MSCI Indices in USD. IBES 12m forward price-to-earnings ratios.

If we look below the surface today, many EM countries boast lower debt-to-GDP ratios than their DM counterparts, healthier demographic trends, converging inflation dynamics and, for many, higher real yields alongside solid earnings growth. Meanwhile, developed economies face slowing growth, aging populations, and the overhang of debt-financed stimulus. If inflation in the West proves sticky, the valuation gap between EM and DM could compress in unexpected ways for both equities and bonds.

In other words, the very notion of a permanent EM risk premium – beyond the specific case of hard-currency debt – may itself be froth. The tide could yet reveal that it is not EM markets that are swimming naked, as many assumed only months ago, but rather DM ones: more exposed to fiscal constraints, persistent inflation, and structural headwinds than common beliefs may admit. The surprise for investors may come not from EM weakness, but from EM resilience.

Against this backdrop, our portfolios tilt toward emerging markets, where we see strategic opportunities across equities, bonds, and currencies. This stronger EM exposure often comes at the expense of a default allocation to developed markets, where concentration risk, stretched valuations and an uncertain fundamental backdrop prompt caution. While we have tactically reduced some of our North Asian equity exposure in recent weeks, we retain a meaningful allocation to EM more broadly. At the moment, we are also particularly attentive to idiosyncratic opportunities in markets such as South East Asia or Turkey, where potential entry points are emerging.

Looking ahead, the key question for the quarters ahead is not just who is swimming, but who is truly clothed in fundamentals, and who is relying on froth to stay afloat.



Global

Daniel White
Head of Global Equities



The high water mark?

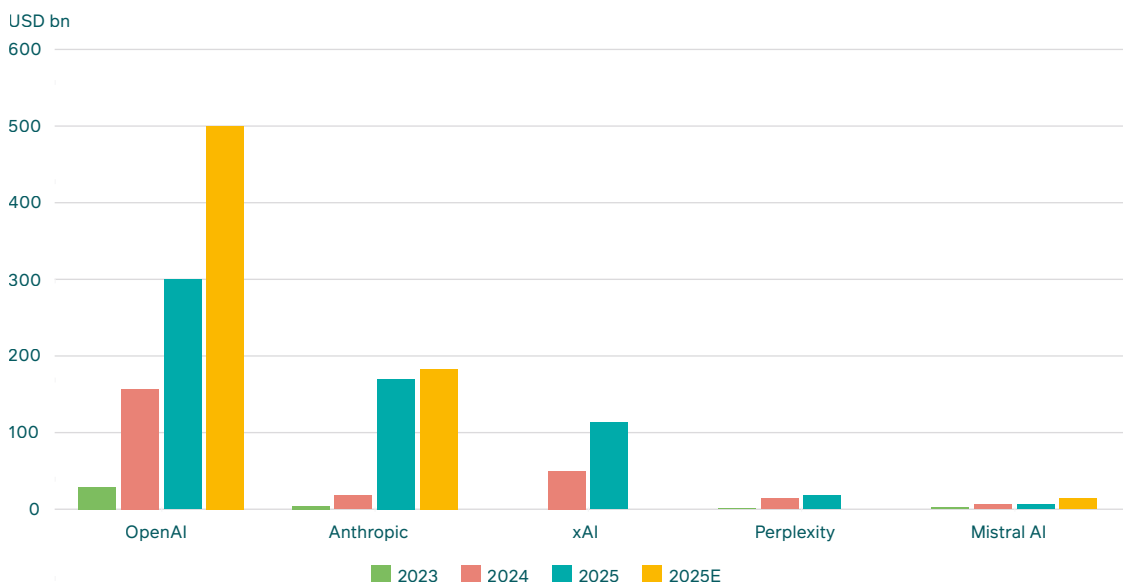
As we enter the final stretch of 2025, almost all global and regional equity indices are in positive territory year to date. The market gyrations of DeepSeek and Liberation Day – just a few months prior – feels like a lifetime ago. Many companies, sectors and regions have been swept up in the warm waters of market enthusiasm.

Artificial Intelligence (AI) continues to dominate the headlines. The so-called ‘hyper-scalers’ capital expenditure plans are enormous and ever-increasing. Sell side analysts and industry consultants estimate cumulative AI and data centre related spend to be in the region of US\$4 to US\$5 trillion for the remainder of this decade.

It’s not hyperbole to state that these numbers are absolutely mind-blowing.

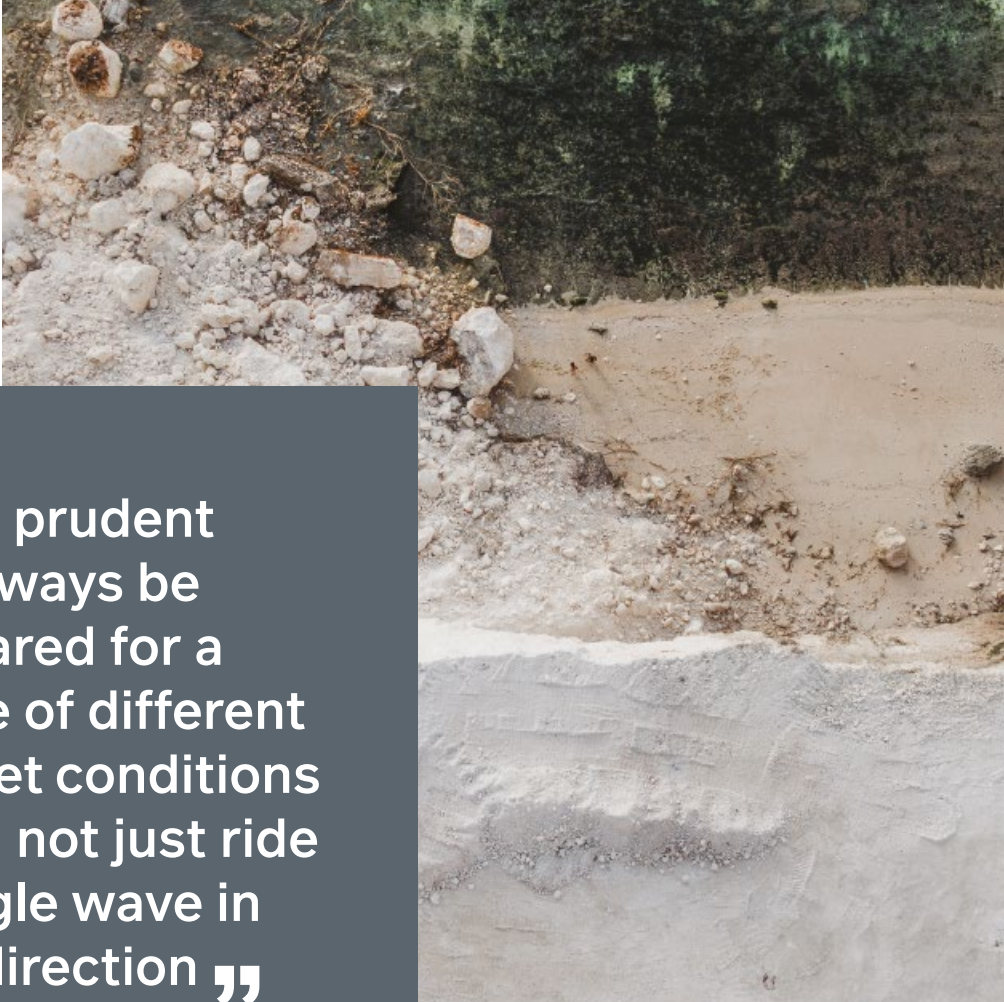
Given the increasingly intertwined nature of the AI protagonists, it’s not surprising that we’ve witnessed a (mixed-metaphor) merry-go-round of rising-tide valuations. This is not limited to public equity markets – privately-held AI companies’ valuations are rising, and (predominantly US Investment Grade) tech credit spreads are evermore excitable.

Is the real ‘bubble’ in private tech companies?



Source: Notice.co, Deutsche Bank Research. October 2025

Some investors are beginning to ask – what happens if the water level begins to drop? And in case anyone needs reminding, high valuations without supportive fundamentals are the equivalent of swimming with no trunks!



“...[it’s prudent to] always be prepared for a range of different market conditions – and not just ride a single wave in one direction”

Bathing suits on

But rather than try to predict the direction of the tide, we’re focused on identifying the companies wearing the bathing suits. These are the ones with robust business models, backed by healthy balance sheets, generating durable free cash flow on attractive valuations.

On this basis, we still find global listed equity markets to be a rich and attractive hunting ground. But it does often mean looking left when most other market participants are looking right.

Recent new purchases across the global fund range have included Allied Irish Bank (an Irish bank), Henkel (a German consumer conglomerate) and Aalberts (a Dutch plumbing supplies company) in Europe. And, in the US, Mosaic (an agricultural fertilizer company), Abbot Labs (a healthcare company) and Salesforce (a CRM software company).

So whilst we do still find some new opportunities within US technology and European banks (the other stock market sector darling of 2025), we’ve generally been allocating incremental capital elsewhere. Not because we’re trying to ‘time the market’ or due to a particular ‘top-down’ view. But because our disciplined focus on the bottom-up fundamentals, combined with attractive valuations, is guiding our decisions.

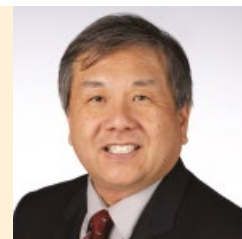
Maybe this means, for a time, we end up swimming against the tide. But we believe it’s prudent for investors to always be prepared for a range of different market conditions – and not just ride a single wave in one direction.



Global technology

Jeffrey Lin

Head of Global Technology Equities



Don't miss the boat, but avoid the sharks

In the third quarter, the broader markets expressed optimism, particularly as it relates to technology, as evidenced by all-time highs in the NASDAQ Index and a very healthy environment for IPOs. We expect this enthusiasm to last through year end, and the remainder of the decade. Indeed, IPO activity is likely to accelerate given the optimism. The primary driver for this has been continued strong growth in AI-related companies, and we see the AI investment case broadening into sectors outside of technology. Looking forward, we believe AI technology remains a long-term tailwind for global economic growth.

Catching the tide

The acceleration in AI adoption represents a paradigm shift unlike anything we've seen before. Companies across markets are operating with a heightened sense of urgency, and this urgency is fuelling a frenzy of acquisitions and hiring – predominantly among the AI leaders.

Distinguishing companies engaged in 'real AI' versus those with more superficial efforts remains a challenge. This is why mega caps such as Google and Meta have led the development of AI foundational models, leveraging their vast troves of consumer data. Still, while data remains the most critical asset, usability and accessibility are prerequisites for meaningful enterprise AI adoption.

Traditionally, incumbents that rapidly adopt new technologies often thrive and create immense value, while start-ups that disrupt slow-moving incumbents can also capture enormous upside. Both dynamics are likely to play out with AI.

Importantly, for the successors, adoption has moved beyond experimentation – companies of all sizes have been deploying AI, with benefits already proving sizable.

For investors, discerning the winners from the losers requires rigorous due diligence; asking questions such as 'who is actually buying?', 'who is using the technology at scale?', and 'what workflows are changing?'.

And to understand who will win out between the incumbents and the disruptors, requires identifying how prepared incumbents are to shift pricing models and operating approaches to lead in the next cycle and combat the pressure from a growing number of disruptors.

“ We expect that as AI solutions mature, there will be a step function increase in the use of AI in corporate settings ”



Structural advantage in riding the wave

The investments in AI infrastructure have the potential to create new AI products and AI services that provide a step function increase in productivity levels. The Generative AI era, which began in late 2022, is rapidly evolving into Agentic AI where the computers can think and reason like humans. Agentic AI is expected to evolve into Robotic AI, where autonomous vehicles and humanoid robots become mainstream.

Demand for AI data centres is coming from corporate users, start-ups, and sovereign nations. There is currently an arms race to accelerate AI's capabilities and there is a global investment cycle. In September, Microsoft announced a US\$30billion investment in data centre infrastructure in the UK, indicating the broad opportunity for AI geographically. In our opinion, countries with access to AI will have structural competitive advantages and higher GDP growth versus nations that do not.

While there have been some concerns that the promises of AI productivity gains in enterprise have not materialised yet, we believe there remains huge potential for AI in enterprise settings.

Wade into companies able to deliver productivity gains, growth acceleration and margin improvements

There have already been AI productivity enhancements in call centres, software coding, predictive analytics, and advertising. We expect that as AI solutions mature, there will be a step function increase in the use of AI in corporate settings that will unleash growth acceleration and margin improvements.



UK

Michael Stiasny
Head of UK Equities



UK Equities: can swim and trunks are firmly on

The third quarter of 2025 provided another reminder that the UK equity market often moves to a different beat than its global peers. While US indices were led higher by a narrow group of mega-cap tech stocks, the FTSE All-Share Index delivered more balanced gains, supported by its global earnings base, with financials, industrials, basic materials and healthcare all contributing meaningfully to the Index's progress. This is in comparison to the S&P500 Index, where 70% of returns were driven by the technology sector alone. Sterling's stability and resilient commodity prices further added to the FTSE All-Share Index's relative outperformance⁴.

Multiple compression has left valuations less stretched

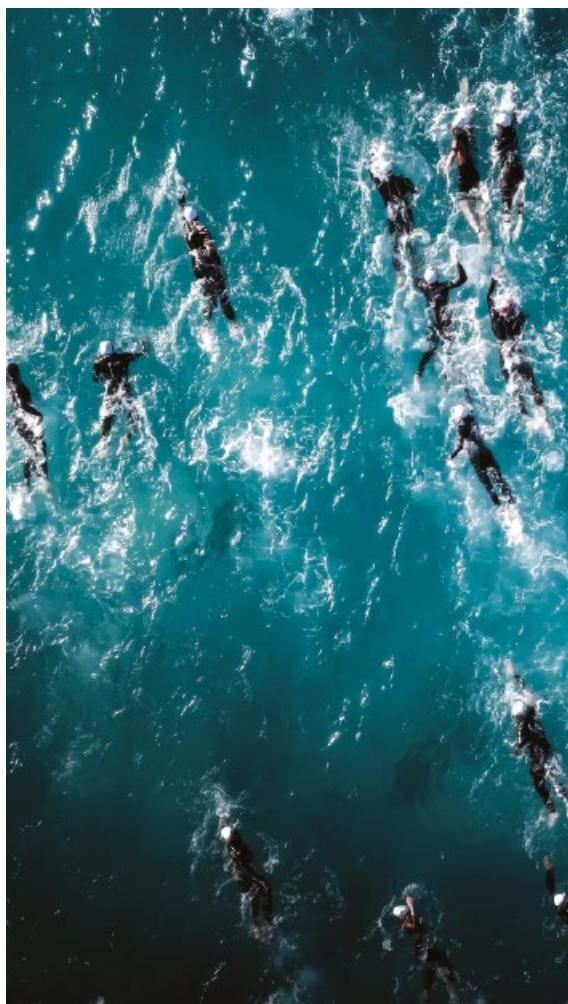
We can find richly-valued growth stocks and speculative corners of the market in some places around the world but these are much harder to find in the UK. This market started from a deeply discounted position, and despite this year's recovery, valuations remain modest relative both to history and to global peers. While the UK market as a whole now trades at higher levels than at the start of the year, several of the most expensive FTSE 100 Index names, such as Relx and London Stock Exchange, have seen meaningful multiple compression, leaving the top end of the market less stretched than it has been for some time.

At a sector level, the appeal of defensive yield plays remained intact. Utilities and tobacco continued to attract capital as investors prioritised income visibility, possibly because there is a concern that we live in a world where rates are likely to stay higher for longer, but more likely because these are both sectors where tariffs and geopolitical risk seem to have less of a role to

play. Equally, a number of global-facing industrials and consumer staples are demonstrating pricing power and margin resilience, attributes that will prove critical if the UK's domestic economy remains sluggish. However, the domestic backdrop does bear watching. The run-up to the Autumn Budget in November will likely be accompanied by heightened political noise and negative sentiment, especially around sectors tied closely to policy, from housebuilders to banks and transport.



⁴Source: Refinitiv Workspace, total returns in local currency, quarter through 30 September 2025.



“we’d argue that...
many [UK-listed]
companies are
still wearing their
trunks: undervalued,
resilient and
quietly executing”

The market is not the economy

Yet, we should remember that the UK equity market is not the UK economy. With over two-thirds of the revenues from companies in the FTSE All-Share Index being derived from overseas, global exposure offers an important buffer. Simultaneously, management teams of domestically-oriented companies have shown admirable agility in navigating a difficult policy and demand environment.

Looking ahead to the fourth quarter, the opportunity lies in separating the genuinely undervalued from those exposed to structural headwinds. In today’s global market, froth might exist in some corners. But in the UK market, we’d argue that beneath the surface, many companies are still wearing their trunks, undervalued, resilient and quietly executing. This leaves us in a position where company valuation often bears no resemblance to the underlying fundamentals – so our opportunity set is strong. If the tide goes out, many companies in both international and domestically-focused parts of the UK market are prepared for it – they have trunks on and they can swim.



Japan

Carl Vine

Co-Head of Asia Pacific Equities

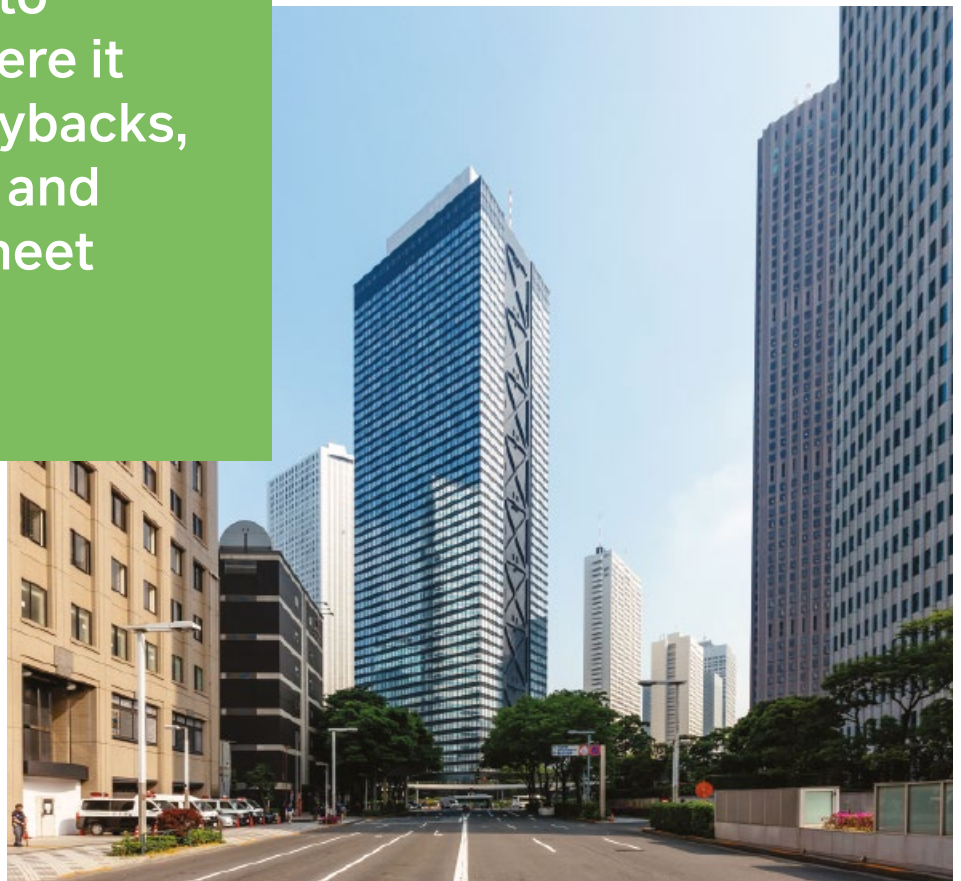


Animal spirits return – but not excess

Japanese equities surged c.12% in the third quarter, an 85th percentile move by historical standards⁵. The rebound was broad, and unlike the relief rally of the second quarter, this one was driven by renewed animal spirits. Yet, despite the punchy returns, the tone was not one of mania. Froth was visible mainly at the periphery, in a handful of AI-related semiconductor and optical switching names, rather than across the market.

Outside these pockets, strength was grounded in improving earnings visibility and rising shareholder returns. Corporate Japan continues to deliver where it counts: buybacks, dividends, and balance-sheet repair. Guidance into the second half of the fiscal year remains conservative, but underlying fundamentals are holding up far better than many companies assumed. The result is an equity market that feels primed for upgrades heading into year-end.

“Corporate Japan continues to deliver where it counts: buybacks, dividends, and balance-sheet repair”



⁵Source: Refinitiv Workspace, MSCI Japan Index total returns in local currency terms; quarter through 30 September 2025.

Dividends, discipline, and dormant assets

Japan's dividend story is no longer a reform narrative – it's an earnings reality. For companies in the benchmark MSCI Japan Index, dividends per share have grown at an average compound rate of 11–12% over the past decade and nearly 20% over the past year. Payout ratios still hover around 40%, leaving scope for continued acceleration, especially as buybacks reach record levels⁶.

Meanwhile, the quiet unlocking of listed Japan's potential US\$2 trillion real estate treasure trove is gathering momentum. Disposals are becoming more frequent, activists more vocal, and developers better positioned to recycle dormant land into productive assets. It is not hyperbole to call this one of the largest latent value opportunities anywhere in global equities.

An unexpected surge

Markets initially embraced the victory of Sanae Takaichi as the leader of the Liberal Democratic Party (LDP) – and potentially Japan's first female prime minister – viewing her as a pro-market and pro-growth continuity figure, who would likely sustain reform momentum while sharpening Japan's strategic and industrial agenda. The 'Takaichi trade' – a rally led by financials, capital goods and exporters – reflected relief that policy direction appeared stable. But that sense of stability was upended following Komeito's withdrawal (only days later) from its 25-year coalition with the LDP.

The split is sharper than past disputes and leaves the government without a working majority. Whether this proves to be another episode of brinkmanship or a genuine breakup will determine the degree of policy drift ahead. For now, markets have treated it as a headline shock rather than a structural shift. Japan has weathered similar political turbulence before, and investors still expect either a renewed coalition or a pragmatic new alignment to emerge.

Looking ahead: constructive, not complacent

The set up for the fourth quarter of 2025 feels balanced and constructive. Corporate guidance remains cautious, but operating data suggests resilience. Reform momentum persists, and the earnings-power narrative continues to broaden beyond exporters and financials. Dividend growth and balance-sheet optimisation remain underappreciated compounding engines.

Yes, a few swimmers are still splashing about in the AI-themed shallows. But the tide in Japan is rising for deeper reasons – cash generation, capital discipline, and the rediscovery of self-help. For investors, that's the kind of current worth riding.

“...the tide in Japan is rising for deeper reasons – cash generation, capital discipline, and the rediscovery of self-help”

⁶Source: Morgan Stanley, MUFG, Japan Equity Strategy, 5 September 2025.



Asia Pacific ex Japan

David Perrett

Co-Head of Asia Pacific Equities



Some froth in the whitewash

Asia Pacific equities posted robust gains in the third quarter of 2025, bolstered by easing trade tensions, expectations for lower US interest rates and a renewed focus on AI-related stocks, both in terms of companies that are involved in manufacturing AI chips and those expected to benefit from their application. The region outperformed global peers, with the MSCI Asia Pacific ex-Japan Index rising c.9%⁷, led by Chinese, Taiwanese and certain Korean technology-related stocks. Of the major regional indices, India was a laggard, weighed down by valuation concerns and also heightened trade tensions with the US.

Standouts in terms of strong performing stocks included Samsung Electronics which benefited from a broad recovery in terms of demand and therefore pricing for semiconductors, and Alibaba which reported positive earnings results, raised capital expenditure on AI initiatives and unveiled a core AI strategy. Other large-cap winners were Delta Electronics and TSMC, with the former more than doubling – again in response to strong demand for its products and a subsequent material increase in earnings expectations. Such a stock move is quite remarkable for a company like Delta, which added more than US\$40bn in market capitalisation in the quarter. Delta's move paled though compared to a number of Chinese domestic 'AI plays' that, in some cases, almost tripled during the period.

Have valuations gone too far for a number of stocks?

Given such a strong move in share prices, it is worth asking this question. There are causes for concern. A number of Korean and Taiwanese technology companies have seen their earnings expectations revised higher, but at the same time have also seen the valuation multiples attached to those future earnings rise – in some cases, on what may prove to be peak earnings. That said, for some of the larger tech companies in the region – the likes of Tencent, Alibaba and TSMC – they trade on 20x 2026 earnings – not cheap given where earnings expectations are, but

nowhere near 'silly' levels. Cyclical DRAM makers like SK Hynix and Samsung trade on low double-digit earnings multiples – although, again, on what looks like near peak earnings.

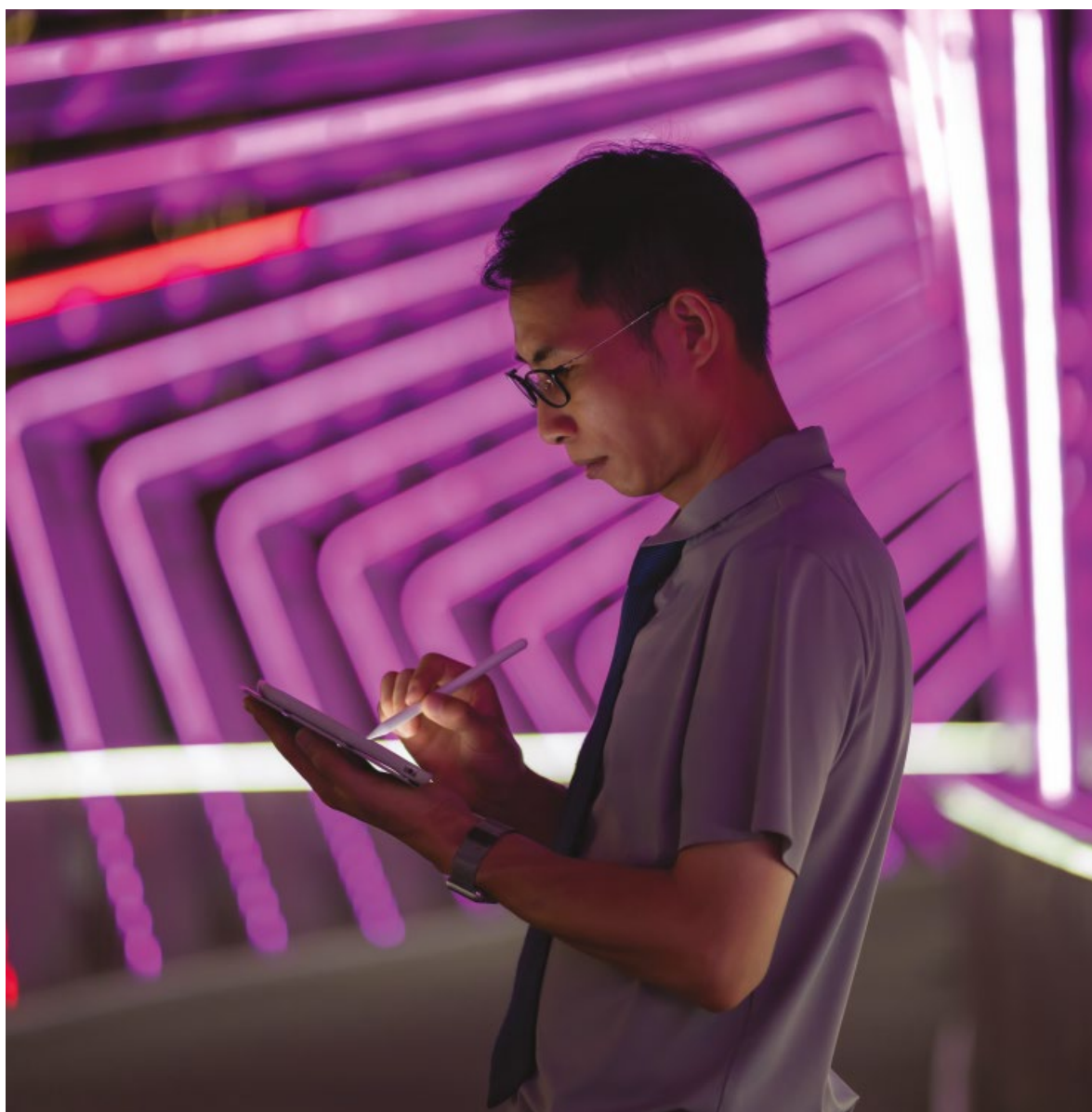
There are potential pockets of excess. A number of Chinese semi-conductor names are still at the nascent growth stage of their evolution, yet the market is ascribing large amounts of value to businesses that have yet to prove they can successfully perform on a commercial scale. In addition, there are also a number of second tier AI names in Korea and Taiwan that are benefiting from near-term strong demand, but ultimately have little in the way of long-term 'moats' to their businesses.

“There are potential pockets of excess [where] the market is ascribing large amounts of value to businesses that have yet to prove they can successfully perform on a commercial scale”

⁷Source: Refinitiv Workspace, MSCI Asia ex Japan Index, total return in USD through 30 September 2025.

Submerged but able to stand

In all markets there are opportunities. As investors have chased after AI winners (or laggards), driven by a collective sense of FOMO (fear of missing out), we are seeing a number of quality consumer-related businesses being materially de-rated in valuation terms. In recent weeks, we have trimmed some of our technology 'winners' and added to certain consumer stocks. Indeed, two of our largest positions today are in consumer-facing companies with 6%+ dividend yields and pathways to steady earnings and dividend growth over the next 12 to 24 months. Given the state of current market pricing and sentiment, this feels a sensible course of action as one peers into 2026.





Emerging markets

Michael Bourke

Head of Emerging Market Equities



Stay at the helm and gauge the conditions

The rally in Emerging Markets (EM) intensified over the third quarter, with the benchmark MSCI EM Index rising c.10% – amounting to year-to-date total returns of c.28% in US dollar terms⁸. For context, this is the strongest EM performance since 2017; a year when Chinese technology names burst onto the scene with the addition of Alibaba and Tencent into the index. We haven't seen such a consistent period of EM performance since the heyday of the last EM bull market in 2003-2007. Markets have been buoyed by a combination of AI fervour, USD weakness, asset class inflows and attractive relative valuations.

Upward swell

While technology names have also driven much of this rally, dominated by the tech-heavy markets of Korea and Taiwan, and the concentrated performance among Chinese tech names, Korea has had the added self-help tailwind with domestic reforms promising to boost shareholder returns and improve corporate governance. So, where does this all leave us as we look into the fourth quarter and beyond in 2026?

Earnings sensitivity ahead

Judging by historical patterns, the mean reversion in multiple re-rating is over. Most of the rally year to date, in the largest EM markets, is down to multiple expansion rather than earnings delivery. Many markets in EM have now retraced to historical average multiples, if not above. The market will face a moment of truth at some point when earnings delivery will be tested. That's not to say multiples cannot expand further – it's in the nature of the asset class that we swing from one extreme to another as sentiment combines with flows to propel the market higher. There is no 'right'

number as regards the multiple for any market.

But we believe returns from here will likely become more sensitive to earnings and one should expect over/under reactions as a result.

Too soon to determine what lies beneath the froth

Nowhere is this more true than the AI space, as one bullish corporate announcement of AI capital expenditure (capex) begets another – consider the recent announcement (in February) from Alibaba's CEO, for capex spend to be higher than \$50 billion. We are witnessing an 'I'm investing because you are' mentality. As students of capital cycles, this reminds us of previous bouts of exuberance whereby the original demand driver (AI) is met with a wall of investment, inevitably leading to 'tears' in some areas as aggregate returns either fail to materialise or disappoint.

“...our decisions as investors cannot be calibrated on the basis of fundamentals alone but by gauging what's in current market pricing”

⁸Source: Refinitiv Workspace, MSCI Emerging Markets Index total returns in US dollar through 30 September 2025.

It is too soon to say whether the current situation is ‘frothy’, albeit we know that the market will always run far ahead of fundamentals and our decisions as investors cannot be calibrated on the basis of fundamentals alone but by gauging what’s in current market pricing. Investor psychology in this area is optimistic right now. However, there are some material bottlenecks to the delivery of AI ambitions – namely the adequate supply of semiconductors and energy capacity. AI may yet prove transformational to our way of life and economies but the economic benefits may accrue to different actors as the capex cycle rolls forward. For example, in China, the AI models are going ‘open source’, so the benefits may accrue more to the application developers rather than the model builders.

Return dispersion providing ample opportunities for ‘active’ managers

The good news is that the inherent strength of the asset class is the (active) investor’s best friend – correlations between and across countries and sectors diverge, offering opportunities to diversify risk exposures and optimise the risk premium of our exposures. Year to date, ASEAN countries such as Thailand and Indonesia have been clear laggards – we have even seen some mean reversion in elevated Indian valuations.

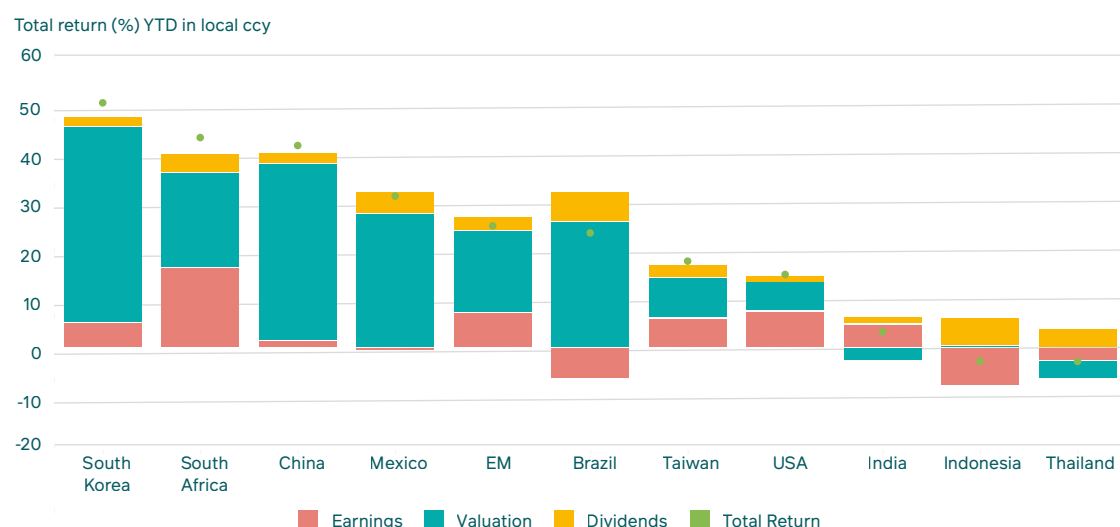
From a sector perspective, utilities, consumer staples and energy have materially underperformed. Utilities and consumer staples are historically defensive sectors, offering opportunities for investors to rotate into such areas with different valuation drivers.

Latin America offers a divergent risk premium and should benefit from the monetary freedom to cut rates as the Federal Reserve begins to cut in the US. The Middle East, especially Saudi Arabia has been hampered by the weak oil price, which has tempered economic transformation ambitions but led to a convergence of valuations with the wider asset class.

Further out, on the risk spectrum, Argentina and Turkey offer idiosyncratic opportunities for the brave-hearted; if we see President Milei’s economic reform momentum continue in Argentina or inflation begin to normalise in Turkey.

Two years ago, China was deemed ‘uninvestable’ by many commentators. We didn’t buy into such bearish rhetoric then and we’re not getting carried away with the current bullish sentiment either. Such is the life of an EM active manager; looking to the long-term opportunity, sticking to process and always calibrating when to step up risk and when to dial it back, and indeed rotate exposures.

Breaking down the drivers of EM returns in 2025



Source: LSEG DataStream, MSCI, 30 September 2025. Past performance is not a guide to future performance.



Impact

John William Olsen
Head of Impact Equities



To avoid the froth, anchor in calmer waters

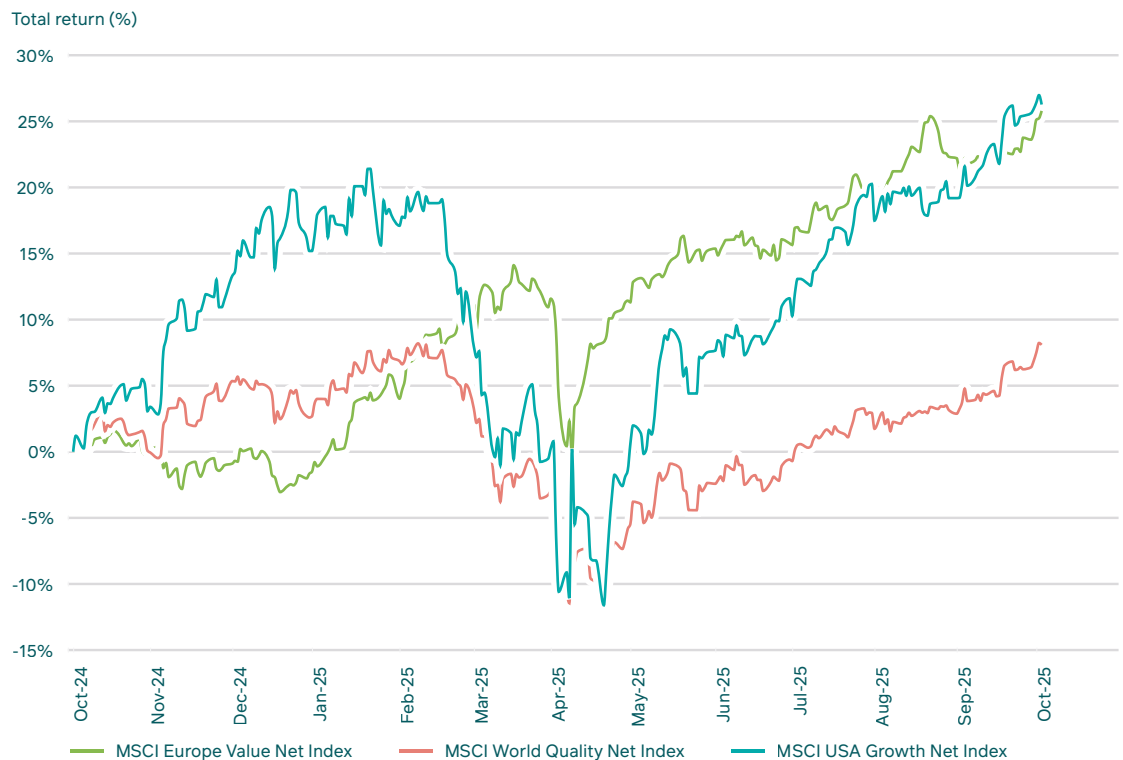
Global equity markets are experiencing heightened dispersion, with momentum emerging as a key driver of performance. However, momentum can be unpredictable – especially in an environment shaped by rapid technological advancement, unprecedented political uncertainty in the country that represents the majority of our investment universe, and abundant liquidity. Investor behaviour driven by FOMO (fear of missing out) or just plain FOM, tends to exaggerate price movements, making short-term positioning more difficult. Yet, this volatility also presents meaningful long-term opportunities, in our view.

The Sustain and Impact core philosophy is to invest in high-quality businesses with a long-term view, maintaining balanced portfolios to manage risk, and responding thoughtfully to market extremes rather than making bold market calls.

Regional style divergence

Currently, we're seeing renewed optimism around cyclical value stocks, particularly in Europe. At the same time, enthusiasm for AI-related technology has driven strong performance in US growth stocks. In contrast, the quality segment, especially defensive quality, has been notably overlooked.

European Value and US Growth have overshadowed Quality stocks



Source: Bloomberg, 3 October 2025. MSCI Net Total Return Indices in GBP. Past performance is not a guide to future performance.

We believe this momentum is vulnerable. Investors have become used to brushing off headline noise, but the macroeconomic outlook remains highly uncertain, and while AI is a genuine driver of innovation and structural change, billions are now being invested in projects that may not deliver meaningful returns. Lofty promises of future technology spend propels stock prices of both spenders and receivers. Big tech profit pools face increasing competitive pressures and, while aggressive AI capital expenditure seems the best option, it is partly defensive. Big new winners will emerge, as we have seen in previous innovation and capital cycles, but risks are high, and we believe these risks will become more obvious.

Look beyond the shoreline

While it's natural to seek future winners, stretched valuations and speculative behaviour prompt us to look beyond the obvious. We're currently identifying attractive risk/reward opportunities in areas such as healthcare, medical devices, and specialty chemicals – amongst others. These opportunities offer solid fundamentals, relatively defensive characteristics, and good contrarian value potential. We've recently increased exposure through both existing holdings and new additions.

We always believe it makes sense to focus on quality, resilience and long-term value creation, but especially in times of heightened market uncertainty and speculative tendencies.

An aerial photograph showing a sandy beach on the left and the ocean on the right. The ocean has several parallel wave lines moving towards the shore, with white foam visible in the surf. The colors range from light tan for the sand to various shades of blue and green for the water.

“ While it’s natural to seek future winners, stretched valuations and speculative behaviour prompt us to look beyond the obvious ”



Global research

Ed Booth

Head of Global Research, Global Banks Analyst



European banks: not in the shallows yet

European banks have led the European market's re-rating this year, with the sector posting a total return of over 60% year to date⁹, in return for a high single-digit revision to 2026 earnings estimates. Can this sustain or is the European banks story now over?

Have banks caught their last wave?

This earnings revision has been driven mainly by current year earnings. Capital markets revenue growth has driven this, helped by 'good volatility' in fixed income markets in response to macroeconomic uncertainty. Traditional bank revenues have been less exciting. Upgrades have been driven by benign depositor behaviour in response to lower interest rates and expectations of German economic stimulus, which have generated a healthy yield curve from which banks can profit. Loan growth is running at around 4% on both sides of the Atlantic.

A bear would argue that European banks are now as expensive as they've been since the financial crisis: 1.4x P/B (price-to-book ratio) versus a trough of 0.5x during COVID-19, and a 2-year forward (FY2) P/E (price-to-earnings ratio) of c. 8.7x versus a trough of 5.5x in 2011 during the sovereign debt crisis. As ever, banks remain a reflection of the health of the economies in which they operate – that is uncertain today.

The biggest change that has driven this re-rating is, of course, higher interest rates. Somewhere below 2% interest rates, deposit margins at our biggest banks start to get squeezed, hurting profitability. Since the end of zero interest rate policy (ZIRP), European banks' RoEs

(return on equity) have doubled, to a healthy 14%. This 14% is the highest since before the Global Financial Crisis (GFC) – and on a much healthier capital base. Today's 8.7x FY2 P/E compares to a 30-year average of just below 10x, driven by periods of higher RoE like today.

Several macroeconomic risks are double edged. Loan growth is likely to remain limited but alongside higher RoEs, this allows banks to return substantial capital to shareholders. Mild concern about fiscal sustainability and inflation helps to sustain both a steeper yield curve and cautious depositor behaviour (which supports profit for the best-funded banks). German stimulus could still help growth; some macroeconomic uncertainty supports capital markets volumes (and M&A is weak today). AI is being harnessed across the sector to boost productivity, taming labour cost inflation.



⁹Source: Refinitiv Workspace, Euro Stoxx – Banks total return year to date to 30 September 2025

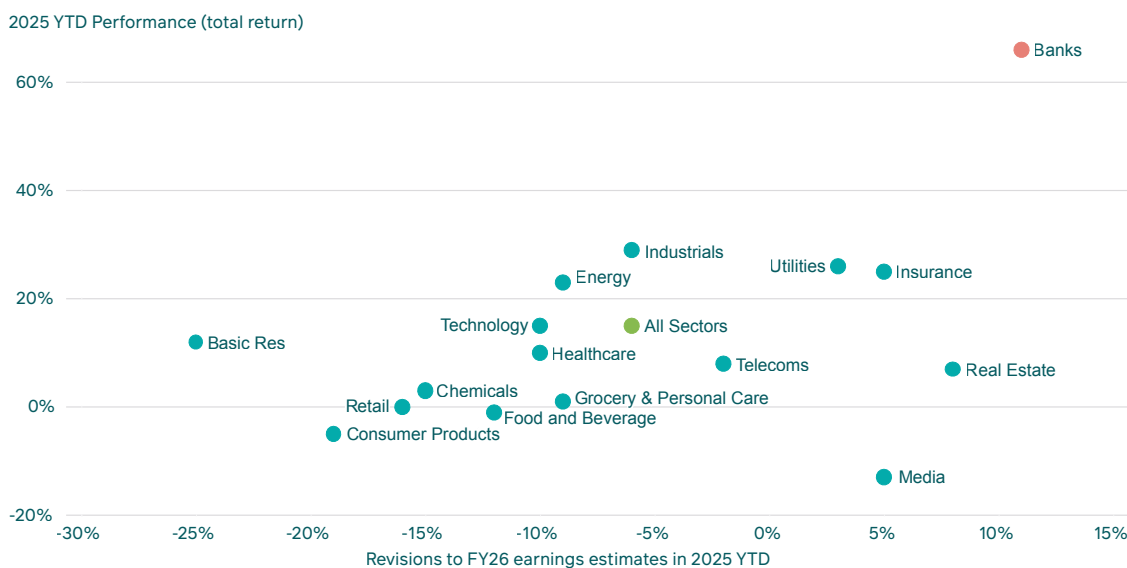
“ While the big sector tailwinds may have eased, the right banks can still deliver meaningful performance for investors from here ”

What can drive earnings from here?

The sector is in good health today and there are stocks and themes that remain well positioned. Banks in the UK and Belgium carry longer duration exposure to interest rates that is still benefiting earnings. Some, notably those in Central and Eastern Europe, can reinvest their superior RoEs persistently into higher loan growth (and at higher interest rates). Spain and Ireland have seen customer loans-to-GDP decline hugely since the GFC, which has inflected recently. The big changes in interest rates and markets are supporting client activity in wealth and capital markets – and this growth is also higher RoE, where it exists.

While the big sector tailwinds may have eased, the right banks can still deliver meaningful performance for investors from here.

2025 YTD returns vs consensus 2026 earnings revisions

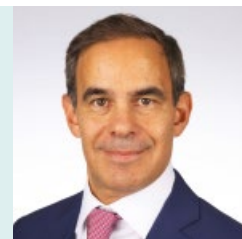


Source: Bloomberg, 7 October 2025.



Convertibles

Leonard Vinville
Head of Convertibles



Amid signs of frothiness, seek protection rather than relying on hope

The convertible bond universe, like global equities, is dancing to strong thematic beats. For instance, recently and notably during September, there has been a high level of opportunistic new issuance by AI-related firms such as Alibaba, Nebius, Cipher and Terawulf, to name a few, raising capital to fund AI infrastructure projects. We can make the same observations about the strong AI-fuelled momentum in equity markets, driven by insatiable investor demand. We estimate that about 15% of our benchmark FTSE Global Focus Index is involved in AI-related activities. A similar thematic vein we have discussed in the past is crypto-related firms. They now comprise almost 10% of our benchmark, with bitcoin miners turning AI providers overlapping in approximately 1-2% with the AI theme¹⁰.

We believe there are signs of excess in these themes, and that investors are increasingly driven by hype, momentum and beta, rather than just reacting to favourable fundamentals.

Often, stock valuations imply years and even decades of high growth ahead. While we do not know how long it may last, we are concerned that momentum may experience a sharp and sudden reversal.

We do not believe the solution is to avoid these themes entirely. After all, their promise and structural transformations are real. But we do wish to be protected against the risk of disappointments.

“We believe there are signs of excess [with] investors increasingly driven by hype, momentum and beta, rather than...fundamentals”

Protection against (downside) exposure

For us, we can achieve downside mitigation in two ways. One is using the inbuilt protection of the bond floor (which would amount to buying out of the money puts if one was holding straight equities). For this, we seek strong bond floors substantiated by robust credit quality that gives us the safety brake needed should accidents (downward equity movements) happen.

The other way is to actively construct a portfolio that does not shun the AI theme, but that proactively invests and places larger weights in securities with the combination of solid business models, sensible valuations, and attractive risk-reward characteristics, with sufficient delta and equity sensitivity to capture improving fundamentals. For instance, rather than betting on specific data centre developers, we prefer players along the AI supply chain, such as memory chipmakers and cable manufacturers.

¹⁰Source: M&G, Aladdin, 3 October 2025.

An aerial photograph of a white sailboat with a tall mast and complex rigging, sailing on vibrant turquoise water. The boat is angled towards the bottom right of the frame. The water's surface is covered in small, shimmering whitecaps. The image is partially obscured by a white rectangular box containing text on the left side.

**“ Risk mitigation
is not about
avoiding AI
stocks entirely,
it is about picking
our investments
carefully ”**

In crypto, rather than taking a directional view on the price of crypto currencies, we favour brokers that benefit from greater trading activity and institutional adoption.

To us, undifferentiated business models with high valuations, weak credits and inflated expectations, trading on hope and hype, are the most vulnerable to a sudden momentum reversal and, longer term, are likely to see increased competition, diminished returns and value creation leaking out to other parts of the value chain – ultimately to users and consumers of their products. Risk mitigation is not about avoiding AI stocks entirely, it is about picking our investments carefully.

In addition to this, the importance of portfolio diversification is paramount. We do not run, nor wish to run AI portfolios. Rather, we manage broadly diversified portfolios with exposures to a full range of stocks, sectors and geographies. Just because strong themes pervade the current market narrative, we do not have to limit ourselves to them. Instead, we have investments in multiple areas such as mobility, e-commerce, healthcare and biotech, emerging markets consumption, software applications and defence.

In short, a focus on downside protection, active management and portfolio construction are essential ingredients in navigating the market currents, in our view.

Marketing Communication for Professional Investors only. Not for onward distribution. No other persons should rely on any information contained within.

This information does not constitute an offer or a solicitation to buy shares in any of M&G's funds.

This document reflects M&G's present opinions reflecting current market conditions. They are subject to change without notice and involve a number of assumptions which may not prove valid. It has been written for informational purposes only and should not be considered as investment advice, a forecast or guarantee of future results, or as a recommendation of any security, strategy or investment product. Where relevant, any reference to individual companies is for illustrative purposes only and should not be considered a recommendation to buy or sell securities of those companies.

Information is derived from proprietary and non-proprietary sources which have not been independently verified for accuracy or completeness. While M&G Investments believes the information to be accurate and reliable, we do not claim or have responsibility for its completeness, accuracy, or reliability. Statements of future expectations, estimates, projections, and other forward-looking statements are based on available information and management's view as of the time of these statements. Accordingly, such statements are inherently speculative as they are based on assumptions which may involve known and unknown risks and uncertainties. Actual results, performance or events may differ materially from those expressed or implied in such statements. All forms of investments carry risks. Such investments may not be suitable for everyone.

This document has not been reviewed by any regulatory authority.

For Australia only: This document is intended for wholesale clients as defined under the Corporations Act 2001.

For Hong Kong only: This document is for professional investors only.

For Singapore only: This document is for institutional investors as defined under the Securities and Futures Act (Cap. 289) of Singapore only.

For Taiwan only: This document is for institutional investors only.

For Japan only: This document is for Institutional Investors only. This document is provided to you for the purpose of providing information with respect to investment management business capabilities of M&G Investments Japan Co., Ltd (the 'Company') and its offshore group affiliates.

For the Republic of Korea only: This document is for Qualified Professional Investors only.

For Malaysia only: This document is for accredited investors and high-net worth entity under the Guidelines on categorises of sophisticated investors.

For China only: For Eligible Investors only (eg qualified domestic institutional investors). The materials contained herein are introductory and are not intended to solicit or induce the audience to enter into commercial arrangement with M&G.

For the United States only: M&G Investment Management Limited is registered as an investment adviser with the Securities and Exchange Commission of the United States of America under US laws, which differ from UK and FCA laws.

For Canada only: Upon receipt of these materials, each Canadian recipient will be deemed to have represented to M&G Investment Management Limited, that the investor is a 'permitted client' as such term is defined in National Instrument 31-103 Registration Requirements, Exemptions and Ongoing Registrant Obligations.

In the UK, the United States, Canada and Australia, this Financial Promotion is issued by M&G Investment Management Limited, registered in England and Wales under number 936683, registered office 10 Fenchurch Avenue, London EC3M 5AG. M&G Investment Management Limited is authorised and regulated by the Financial Conduct Authority. In Hong Kong and Korea, this financial promotion is issued by M&G Investments (Hong Kong) Limited. Office: Unit 1002, LHT Tower, 31 Queen's Road Central, Hong Kong; in Singapore by M&G Investments (Singapore) Pte. Ltd. (UEN 201131425R), regulated by the Monetary Authority of Singapore; In Taiwan, independently operated by M&G Investments (Taiwan) Limited, regulated by Financial Supervisory Commission of Taiwan, R.O.C. (113-gingwantougu-009). Address: Rm B1, 33F., Taipei 101 Tower, No. 7, Sec. 5, Xinyi Rd., Xinyi Dist., Taipei, 110, Taiwan. Tel: +886-02-81010600; in Japan by M&G Investments Japan Co., Ltd. Investment Management Business Operator, Investment Advisory and Agency Business Operator, Type II Financial Instruments Business Operator Director-General of the Kanto Local Finance Bureau (Kinsho) No. 2942. Membership to Associations: Japan Investment Advisers Association, Type II Financial Instruments Firms Association; elsewhere by M&G Luxembourg S.A. Registered Office: 16, boulevard Royal, L-2449, Luxembourg. **OCT 25 / W1575605**