CIO PERSPECTIVES

24 September 2026

Five Questions Shaping Our Outlook

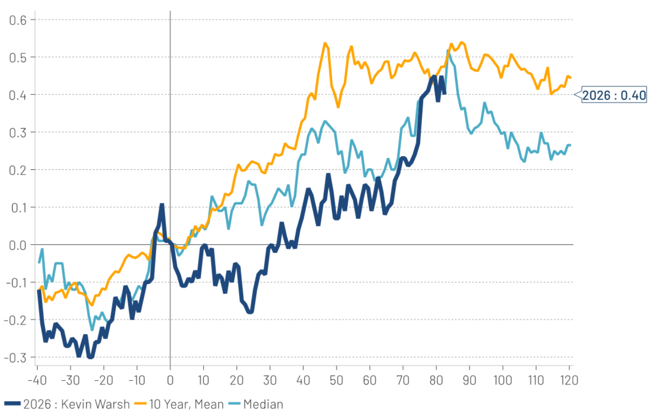
As we approach year-end, investors are navigating a market environment shaped by supply shocks, evolving central bank policies and a packed electoral calendar. Against this backdrop, our investment strategy is guided by a clear and disciplined assessment of opportunities and risks across asset classes. The following five questions and answers outline our current positioning on interest rates, the US dollar and equities, as well as the key convictions underpinning our outlook for the months ahead.

1. WHY HAVE LONG-TERM BOND-YIELDS RISEN, AND WHAT DOES THIS MEAN FOR INVESTORS?

The summer and the start of the autumn are marked by a sharp rise in US and global rates, reflecting several factors: the market revising up its growth expectations in an environment where inflation remains elevated; worsening fiscal positions in with governments borrowing capacity being increasingly challenged by the substantial financing needs of hyperscalers in the bond markets; rising energy prices amid continued uncertainty in the Middle East; and concerns about the Federal Reserve's (Fed) credibility following Kevin Warsh's mixed messages over the summer (Chart1).

Bond yields have returned to levels not seen since the Global Financial Crisis. This rise in interest rates has created an increasingly attractive environment for fixed income, which is now supported by a high carry[1]. Nevertheless, we remain somewhat cautious on duration, a positioning we have maintained throughout the year. The ongoing competition for capital between governments running persistently large deficits and the substantial financing needs associated with the artificial intelligence (AI) investment cycle continues to exert upward pressure on long-term yields. At the same time, geopolitical tensions in the Middle East leave the balance of risks skewed toward higher rates.

Chart 1: US 10-Year Yield at the Start of a New Fed Chair's[2] Term



Source: Macrobond, US Department of Treasury, 22.09.2026, Indosuez Wealth Management.

[1] Carry: the regular income earned from a bond, mainly from its coupon, excluding any price gains or losses.
[2] New Federal Reserve chairs tend to be tested by the markets in the early months of their tenure.

2. DOES THE FED'S LATEST RATE HIKE SIGNAL THE START OF A NEW TIGHTENING CYCLE?

Although we did not expect any Fed rate hike in our central scenario before the summer, the Fed raised rates by 25 basis points (bps) in September. This move appears aimed at strengthening Kevin Warsh's credibility and helping limit the unanchoring of long-term US rates, in coordination with the US Treasury, which made repeated efforts in this direction over the summer. Fed members have sounded increasingly impatient in recent weeks as inflation remains elevated, which supported the September hike. We now expect one further rate increase by year-end, taking the Fed Funds Rate to 4.25% by end-2026, versus 3.75% previously, before stabilising at 4.0% with a rate cut by end-2027, versus 3.5% previously.

In our view, this is more a monetary policy adjustment than the start of a full tightening cycle, even if markets have begun to price one in, with the Fed Funds rate still seen above 4.5% in 2028. We continue to see current inflation as driven by temporary supply shocks, notably tariffs and energy, while very specific components, particularly computer software and financial services, are keeping the Fed's preferred Core PCE measure elevated at 3.3%. At the same time, alternative indicators of underlying inflation do not suggest a broadening of price pressures, and the economy does not appear to be overheating, with labour market conditions remaining balanced and stable. As these temporary effects fade, inflation should slow in 2027 to below 3%, with or without further Fed hikes, which should reassure policymakers. In this context, we remain negative on the dollar, but a more restrictive and more credible Fed leads us to modestly revise our EUR/USD target to 1.18, from 1.20 previously.

3. HOW COULD MARKETS REACT IN CASE OF A "DEMOCRATIC SWEEP" AT US MIDTERM ELECTIONS?

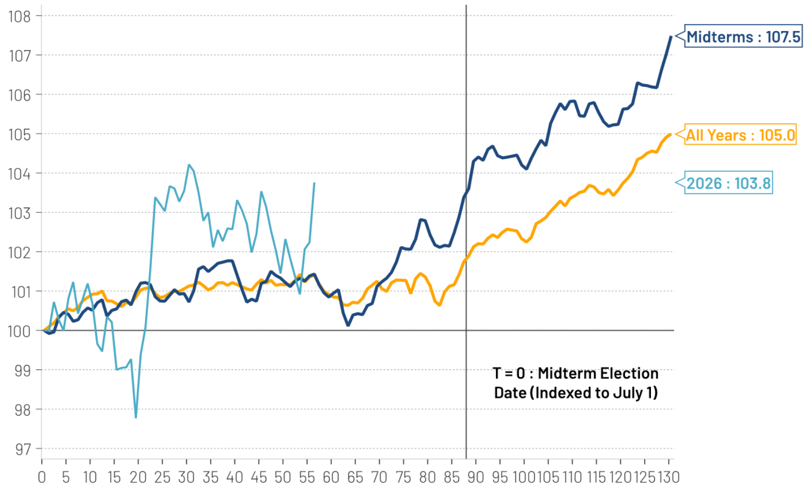
The US midterm elections will take place on 3 November 2026. Prediction markets now assign a 66% probability to Democrats winning unified control, up from less than 45% before the summer.

As noted in our July CIO Perspectives on the US midterms, markets have often seen higher volatility in the months leading up to the vote, as election uncertainty weighs on sentiment (Chart2). The post-election period is usually more supportive for equities, as uncertainty fades.

If Republicans lose the House, the administration will have less room to pursue policy changes, which should reduce uncertainty and help limit concerns about fiscal overreach. That said, it could also increase the risk of fiscal brinkmanship and debt-ceiling tensions. The president would still retain significant influence over trade and foreign policy, two areas that have already driven market volatility during his term. The same broad logic would apply in the event of a Democratic sweep, since the president's veto power would still constrain major legislative change. Even so, such an outcome would create additional pressure on the current administration's deregulation agenda and could be seen as a negative signal for investors ahead of the next presidential election, especially if it raises the prospect of tighter regulation, including around AI, and higher corporate taxes.

Overall, in what is usually a favourable post-midterm environment for equities, a Democratic sweep would likely be the least supportive short-term outcome for markets. It could trigger an initial risk-off move, leading investors to seek the relative safety of government bonds and easing pressure on the long end of the US yield curve, while also weighing on the dollar. Our medium-term constructive view on equities remains however unchanged. Corporate earnings remain the main driver of performance, and we expect earnings growth to continue supporting markets in the months ahead.

Chart 2: S&P 500 H2 Performance – Midterm Years



Source: Macrobond, S&P Global 22.09.2026, Indosuez Wealth Management.
Note: While uncertainty weights on risk assets ahead of the midterms, the post-election receding uncertainty is historically very supportive for equities.

4. HOW DO WE CURRENTLY ASSESS OUR OIL SCENARIO, GIVEN THE ONGOING TENSIONS IN IRAN?

We expect Brent crude prices to remain elevated through the end of the year, averaging around 90 dollars per barrel in Q4, broadly in line with Q3. China is adjusting demand and diplomacy appears to be moving in a more constructive direction, creating some downside risk to our near-term forecast. Of course, a credible breakthrough could bring Brent relatively quickly towards our 2027 assumption of 75-80 dollars per barrel. However, we do not expect a sustained move materially below that range in 2027, given the need to rebuild inventories, persistent supply uncertainty and continued geopolitical volatility. Risks around this outlook are broadly balanced. Additional supply, including the possibility of further fragmentation within the Organisation of the Petroleum Exporting Countries (OPEC), could push prices lower, while renewed geopolitical tensions could generate another upside shock.

5. WHAT DOES THIS IMPLY FOR OUR ECB VIEW?

For the Euro Area, persistently high Brent prices would keep headline inflation under pressure, with our forecast showing inflation peaking at above 4% in Q4. This creates a difficult environment for the European Central Bank (ECB). In principle, monetary policy does not respond aggressively to a temporary supply shock, particularly when core inflation (excluding food and energy prices) remains weak and was still easing in August. However, after eight months of elevated oil prices, the distinction between temporary and persistent is becoming less clear, while inflation expectations and wage dynamics warrant monitoring. We nevertheless see limited evidence of broad-based second-round effects, despite stronger activity and wage pressures in parts of southern Europe, notably Spain.

As a result, we continue to think markets are pricing too much monetary tightening into 2027. That said, if the Brent remains near 90 dollars per barrel through Q4, another ECB hike in December 2026 would be plausible. The ECB remains highly sensitive to energy-driven inflation following the 2022 experience and appears increasingly focused on protecting the credibility of its inflation mandate. Any additional tightening, however, is likely to be temporary and should be reversed once energy base effects begin to pull headline inflation lower in 2027.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