

Editorial

When Interest Rates Wake Up...

We have just experienced a particularly turbulent third quarter in bond markets, with an almost uninterrupted rise in long-term yields over the past three months, both in the United States and, by extension, in Europe. This took place against a backdrop of persistent tensions around the Strait of Hormuz, but also positive growth surprises, especially in the United States. The yield on the 10-year US Treasury note rose from 4.40% at the end of June to 5.28% on September 30. A similar move occurred in Europe, where the German 10-year yield climbed from 2.86% at the end of June to 3.59% at the end of September. Equity markets, meanwhile, proved fairly resilient, supported by the technology sector and the AI theme. The S&P 500 gained 2.30% over the quarter (versus -0.62% for the Euro Stoxx 50), a remarkable performance given the recent surge in long-term yields.

In this editorial, we will try to take a closer look at what happened over the summer and outline some prospects for the remainder of the year.

The fragile agreement reached in Islamabad in June collapsed in early July. Following attacks on vessels in the Strait of Hormuz, Donald Trump declared the truce over and resumed targeted strikes. The summer was subsequently marked by a naval blockade and a battle over pipelines, as the US Navy reimposed a strict blockade on Iranian ports and diverted more than one hundred commercial vessels. In retaliation, the Houthis, who are allied with Iran, imposed a blockade on Saudi shipping in the Red Sea (Bab el-Mandeb), forcing Saudi Arabia to reroute its flows through the East-West Pipeline. During the night of September 8–9, intense exchanges of fire took place between Washington and Tehran, and on September 10 a drone attack attributed to pro-Iranian militias temporarily disabled the major Saudi pipeline leading to Yanbu. A few weeks later, the United Nations General Assembly failed to secure a peace agreement, and the US president firmly denied any intention of easing sanctions on Iran. With the risk of a renewed offensive around the US midterm elections in November, the Pentagon deployed a third aircraft carrier strike group, led by the USS Theodore Roosevelt.

Against this backdrop, developments in the oil market over the past three months have revolved around a paradox: physical flows have been substantially reorganized, yet the geopolitical risk premium has kept prices at very high levels.

The announcement of the short-lived agreement between Iran and the United States in mid-June had initially pushed WTI down to around \$70. However, when the ceasefire broke down in early July, prices immediately rebounded. In August, crude prices approached \$90 a barrel, reacting day by day to rumors of unsuccessful bilateral negotiations mediated by Qatar. The military escalation in September then drove oil above \$100 a barrel, meaning that between June 30 and the September 15 peak, the price of a barrel surged by 52%. Another major development was the complete collapse of Iranian exports. The US blockade has indeed proved highly effective. In September 2026, for the first time since the conflict began, Iran loaded no crude oil onto tankers (compared with 250,000 barrels per day in August), drying up its direct revenues. At the same time, Gulf countries and the shipping industry managed to adapt and bypass the Strait of Hormuz (using pipelines and ship-to-ship transfers), bringing the region's total exports back to nearly 80% of their pre-war level. Yet even as crude oil is flowing again, the cost of shipping it to Asia has soared.

Moreover, shipments of refined products such as diesel remain severely constrained, triggering a historic surge in prices at the pump in Europe and the United States. This has weighed on inflation figures, despite core inflation remaining relatively contained, which is rather encouraging (see our macro section on page 3).

Despite this uncertain geopolitical environment and inflation running above target, growth has remained resilient. The United States appears poised to reaccelerate from a solid base, while China could rebound in the fourth quarter.

This stronger growth backdrop—another positive surprise—has prompted central banks to remain focused on inflation, adopting a more hawkish tone than expected a few months ago, even as markets and economies adjust to higher long-term interest rates. Kevin Warsh, the new head of the Fed, implemented the first increase in US policy rates in three years on September 16, one week after the ECB raised rates, bringing the federal funds target range to 3.75%–4.00%. Following these hikes, it is possible that the US Federal Reserve, the European Central Bank and the Bank of Japan will each raise rates by a further 25 basis points before year-end.

Strong corporate earnings, supported by investment and spending on artificial intelligence, should sustain momentum and continue to underpin equity markets.

	Q3 2026	YTD 2026	Close 30/09/26
DOW JONES	-2.70%	5.91%	50 906.05
S&P 500	2.03%	11.77%	7 651.54
FTSE	1.04%	6.79%	10 606.12
EUROST .50	-0.93%	8.25%	6 269.02
CAC 40	-5.23%	-2.27%	7 964.57
FTSE MIB	-0.60%	14.30%	51 371.98
MSCI EM	-1.05%	21.40%	1 704.87
CRUDE OIL	41.92%	70.14%	90.42
GOLD	13.67%	5.51%	4 157.41
EUR/USD			1.1330
EUR/CHF			0.9469
EUR/GBP			0.8541
EURIBOR 1M			2.617%

Bond yields are also rising, but given the scale of the increase in energy prices, the adjustment remains consistent with the broader backdrop (see our Special Topic on page 4). August macroeconomic data showed signs of a recovery (particularly in manufacturing), overall sentiment remained firm, and business confidence improved for the fourth consecutive month.

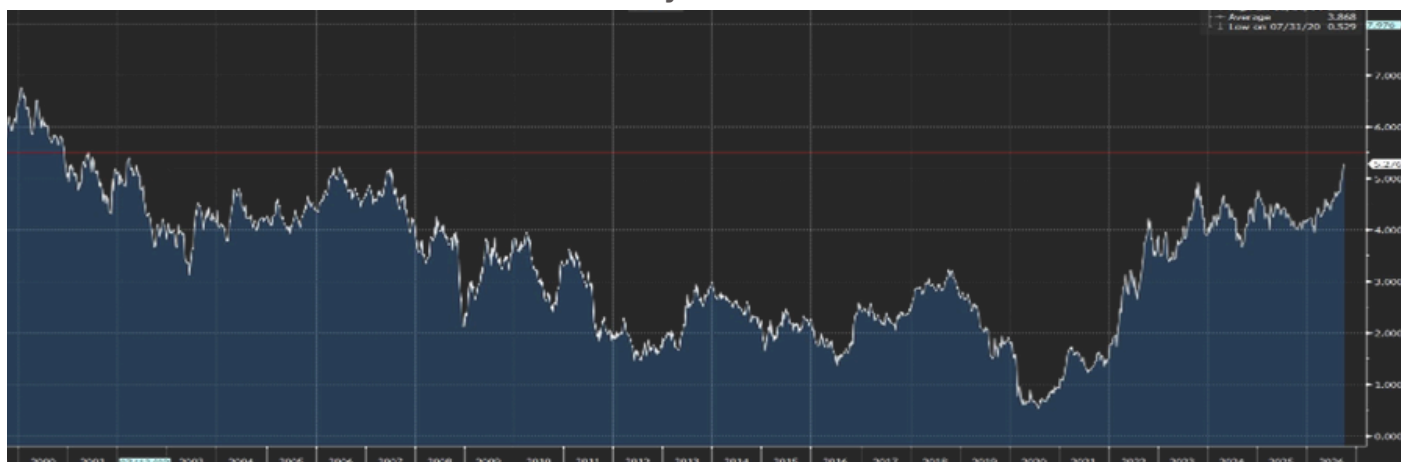
One development to watch in the United States is the approach of November's midterm elections. Polls suggest that Democrats could regain control of the House of Representatives and potentially even the Senate, limiting the Trump administration's legislative room for maneuver. It is, however, very difficult to anticipate how markets would react to such an outcome.

In Europe, fiscal measures—particularly in Germany—are increasingly supporting the European economy and cushioning the impact of external shocks. Friedrich Merz's government is now incorporating a major €126.7 billion investment plan covering the renovation of transport infrastructure, digitalization, education and housing, not to mention off-budget allocations that continue to fund orders for weapons and equipment to modernize the armed forces. France, by contrast, remains a source of concern: stagnant growth, high debt levels, social unrest, major political uncertainty and a country that seems unable to reform peacefully.

In Asia, an acceleration in fiscal stimulus and project spending should provide a boost, at least temporarily, to the Chinese economy during the final quarter of the year.



US 10-Year Treasury Yield Evolution Since 1999



Outside China, growth remains resilient, while Japan's recovery continues, supported by Prime Minister Sanae Takaichi's pro-growth economic policies and corporate governance reforms.

Around the world, the range of AI-related opportunities continues to broaden beyond graphics processing units alone, as the deployment and applications of AI agents reshape the physical infrastructure of computing. Electrification also continues to benefit from the rollout of data centers, improving industrial orders and infrastructure spending (see our In Focus feature on this topic on page 4).

Against this backdrop, we remain constructive on the equity component of our portfolios, despite the rise in long-term yields, which mechanically weighs on valuations. This view is particularly relevant if the third-quarter earnings season, due to begin in a few days, confirms the trends observed in the first and second quarters: robust earnings growth, positive revisions and continued capital expenditure (capex) related to AI. Robotics, defense and gold mining should continue to offer attractive thematic opportunities.

Other sectors have been neglected by equity investors for several quarters, including luxury goods and quality-growth stocks such as EssilorLuxottica, L'Oréal and Saint-Gobain. At this stage, it is very difficult to know whether their time in the wilderness is nearing an end. The same applies to Europe's automotive sector, which has been battered both industrially and on the stock market by the seemingly unstoppable rise of Chinese manufacturers.

On the fixed-income front, we believe the recent increase in long-term yields offers a good opportunity to add to our positions, especially with managers running somewhat longer duration, at a time when our short-maturity target-date funds have held up remarkably well.

We also see value in emerging-market bonds, particularly where real yields are high and fiscal conditions are favorable. In Europe, like many of our managers, we remain cautious on France because of the surge in debt, the near-insurrectionary social climate and electoral uncertainty.

Investor demand, fiscal concerns and questions about central bank independence encourage us to remain constructive on gold. The same applies to commodities more broadly, supported by supply constraints, refinery disruptions and persistently tight energy markets.

What Are the Risks to This Scenario?

A prolonged closure of the Strait of Hormuz would clearly not be good news for Western economies. Oil remaining above \$100 a barrel for an extended period would place significant pressure on consumers' wallets and confidence.

It is in everyone's interest for this conflict to reach a favorable resolution quickly, but for now the Iranians do not appear willing to make concessions on the nuclear issue. Another geopolitical concern to monitor is the escalation in tensions between Russia and Europe. Hardly a week goes by without Moscow testing Europe's patience and resilience (a train attack in Poland, unauthorized drone flights near European borders or critical infrastructure, GPS jamming in the Baltic region and electronic warfare, large-scale cyberattacks on government institutions, and so on).

For the moment, these actions remain below the threshold of Article 5, but what happens if an incident goes too far? Furthermore, this hybrid war comes at a cost: covert physical attacks (sabotage of energy or transport infrastructure) and large-scale cyberattacks are forcing European governments to ramp up defense and security spending. Financed through borrowing, this unproductive investment widens national budget deficits.

Another risk, as mentioned earlier, is political. First in the United States, where the president is not polling particularly well. Rising interest rates, higher gasoline prices and a prolonged conflict in Iran that is costing US taxpayers money are hardly helping. Has the market already priced in the loss of one of the two chambers of Congress? We will, of course, monitor this closely next month. In Europe, France will be the focus of attention in the coming months, with polls consistently pointing to a Le Pen-Mélenchon second-round runoff, a prospect that is unsettling for markets, to say the least. France is also suffering from stagnant growth, heavy indebtedness and near-ungovernability. This contrasts with the strong results seen in Southern Europe, particularly Spain and Italy.

Finally, disappointment in the expected returns on artificial intelligence could be one last risk to monitor closely. Indeed, much of the current economic resilience (and the strength of equity markets) rests on the enormous technology boom and AI-related capital spending (data centers and the entire associated ecosystem, semiconductors, and so on).

If companies' actual productivity gains fail to justify the hundreds of billions of dollars invested by technology giants, a stock market correction and a freeze in investment could quickly dampen macroeconomic momentum.

In the face of these risks, our best defense remains our methodology: diversification (across geographies, sectors and investment styles), combined with continued rigorous manager selection, with a particular focus on quality and liquidity.

Christophe Carrafang



Macro Q3 2026 : The economy accelerates despite inflationary pressure

Inflation: The decline in prices comes to a halt

- In the Euro Area, inflation rose from 2.8% in June to 3.8% in September. This increase was driven in particular by a rebound in energy prices. Core inflation, however, remains contained and stable at 2.5%.
- In the US, annual inflation rose to 3.4% in August, from 3.0% in June. Inflation excluding food and energy remains more moderate at 2.4%. Nevertheless, the rebound in gasoline and energy prices, combined with pressure on production costs, continues to fuel persistent inflationary pressures.
- In China, inflation remains low but is gradually picking up. Consumer prices rose by 0.8% year-on-year in August. Domestic demand nevertheless remains relatively subdued, notably due to continued weakness in the property sector.

Manufacturing activity: AI-driven acceleration

- Global manufacturing activity continues to improve. The global manufacturing PMI reached 53 in August, its highest level in more than two years. AI-related investment remains one of the main drivers of industrial demand.
- In the United States, the ISM Manufacturing Index continues to rise in expansionary territory, reaching 54.5 in September. Cost pressures nevertheless remain significant, with the ISM Prices Index rising to 77.9.
- In the Euro Area, the industrial recovery is clearly gaining traction. The manufacturing PMI reached 52.9 in September, its highest level in more than four years, up from 52.7 in August.
- In China, the official manufacturing PMI moved back above the 50 threshold in September, to 50.1. The private RatingDog index reached 52.1. The quarter ended with an improvement in industrial activity.

Services activity: The rebound takes hold

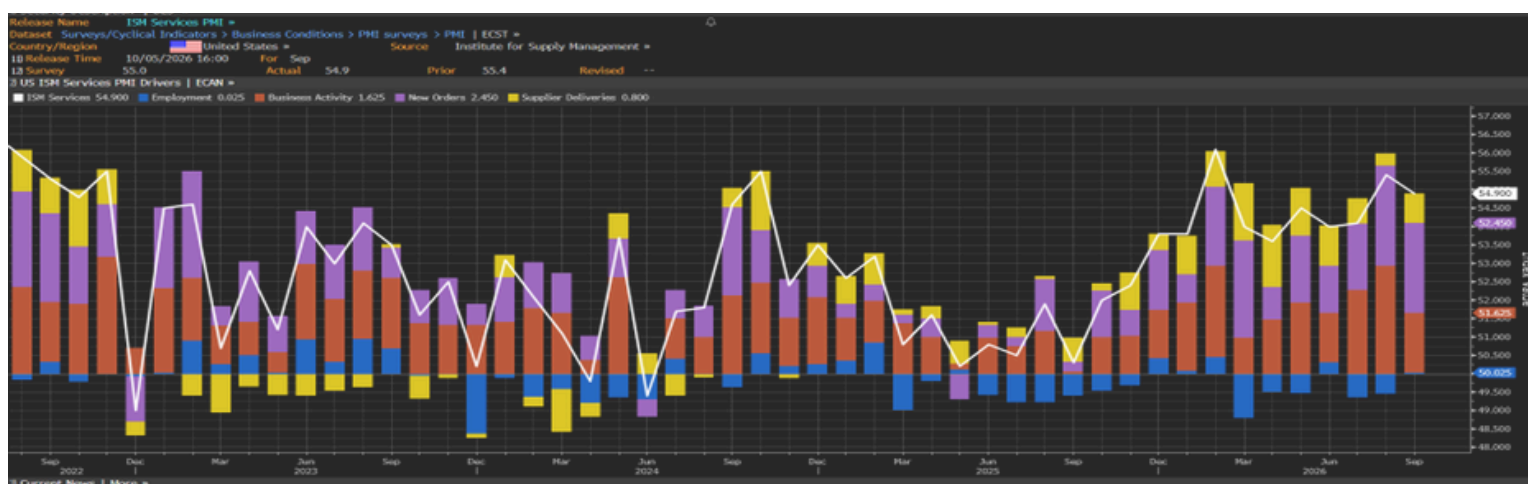
- The services sector is becoming the main driver of the acceleration in the global economy. The global services PMI rose sharply during the third quarter, gaining 2.8 points to reach 54.5.
- In the US, the ISM Services Index stood at 54.9 in September. The Prices Index was at 74, New Orders at 59.8, and the Employment Index moved back slightly above 50.
- In the Euro Area, the rebound is particularly pronounced. The services PMI increased to 53 in September. France, which had been particularly weak in the second quarter, also benefited from an improvement in demand for services, with its index rising from 48 to 51.2 in one month.
- In China, services indicators also improved toward the end of the quarter. The official non-manufacturing index returned to 50.2 in September, while the private RatingDog PMI rose to 51.6.

Labour market: Resilient, but losing momentum

- The US labour market remains resilient but is showing signs of losing steam toward the end of the quarter. In September, the US economy created just 29,000 jobs.
- The Euro Area also continues to enjoy a robust labour market. The unemployment rate stood at 6.4% in August, compared with 6.2% in May, indicating a slight deterioration but remaining historically low. Employment thus remains an important support for European consumption.
- In China, the labour market remains more fragile. The urban unemployment rate stood at 5.3% in August, compared with an average of 5.2% over the first eight months of the year. The improvement in manufacturing and services activity toward the end of the quarter is a positive signal for the remainder of the year.

Trends in the Key Drivers of the US ISM Index

Damien Liegeois





The Big Picture

AI: How Far Can the Investment Cycle Go?

After serving as the main driver of equity markets in recent years, artificial intelligence is entering a new phase: financing. Investment in data centres, semiconductors and power infrastructure is reaching unprecedented levels, while technology giants are beginning to rely more heavily on debt. This acceleration comes as long-term interest rates have returned to historically high levels, raising the cost of capital just as investment is reaching new peaks. This has fuelled questions about a potential 'AI bubble'. But perhaps the real issue lies elsewhere: are we facing a bubble, or the beginning of an investment cycle whose scale is still being underestimated?

A bubble is not defined by high valuations or investor enthusiasm. It emerges when supply capacity exceeds the demand that can absorb it. Yet the available indicators do not appear to support this scenario so far. Order books remain strong, delivery lead times are lengthening, power capacity is constrained and prices for certain components, particularly memory, are rising sharply. The strains affecting infrastructure and inputs look more like shortages than an industry that has already built too much capacity.

This does not mean that current valuations are immune to a correction. The risk is more one of timing. Capital expenditure can rise sharply before the productivity gains and revenues associated with AI materialise. The history of major technological transitions shows that infrastructure can be built out over a few years, while its adoption across the economy and its translation into productivity gains take much longer. Electrification in the United States offers a precedent: several decades separated the deployment of the technology from its full economic impact, notably because companies had to adapt their organisations and production processes.

Against this backdrop, debt and interest rates are becoming the true test of the cycle. The AI boom is now being financed at a time when the cost of capital can no longer be ignored. Rising bond issuance by hyperscalers is therefore not, in itself, a sign of a bubble. It does, however, become a concern if increasing leverage is accompanied by inadequate returns on capital or slowing demand. For markets, the question is thus no longer simply how much growth AI will generate, but how quickly that growth will produce sufficient returns on the hundreds of billions of dollars invested.

The debate over an 'AI bubble' is probably premature if it focuses solely on equity valuation multiples or the amounts being invested. The real warning signs to watch will be both physical and financial: the emergence of unused capacity, a reversal in order books, easing input prices, shorter lead times and, above all, a sustained decline in return on invested capital. As long as these signals do not appear together, the situation looks more like a structural investment phase than an overcapacity bubble. But with interest rates high and debt rising, the market now has a more demanding mechanism for testing that hypothesis: the cost of capital.

Damien Beasse

Special Topic

Reflections on Interest Rates

Looking back to the end of last year, interest rates were not expected to be a major concern in the 2026 outlook, except for those who were already warning that a pickup in economic activity could lead to renewed wage pressures and inflation.

In early March 2026, those forecasts were upended, although not immediately, as the prevailing assumption quickly became that the war would be short-lived and have no medium-term consequences. Instead, the prolonged crisis and its knock-on effects—higher energy prices, inflation, long-term bond yields and central bank policy rates—have, as always, affected the credit spreads of financially vulnerable sovereigns, starting with France, as well as those of already heavily indebted companies. The crisis has also dealt another blow to the real estate sector, which was already struggling to recover from the 2022 shock and from regulatory and tax pressures, particularly in Europe.

What is surprising in this challenging environment, after six months of conflict, is that the energy crisis has not triggered an economic slowdown. Instead, we are seeing an acceleration—although for how long?—in global activity, both in manufacturing and in services, which is hardly likely to halt the rise in interest rates.

Beyond the developments described above, current long-term interest rates are not necessarily another example of market excess in absolute terms. Under Fisher's theory, the equilibrium 10-year "risk-free" rate corresponds to the level of inflation (actual or expected) plus the long-term growth rate. This broadly matches current levels of 5.3% for the US 10-year Treasury yield (3% long-term growth and 2.5% inflation) and 3.5% for the German 10-year Bund, reflecting Europe's lower potential growth. The same is less true of French government bonds, whose yields are affected by country-specific risks arising from high indebtedness and a lack of political visibility over the past two years.

Indeed, over the past 30 years, the average US 10-year Treasury yield has been around 5%, compared with 3% for the Bund. Current yields therefore simply bring us back towards the upper end of a long-term range. The problem is that many market commentators remain anchored to the average rates prevailing between 2008 and 2020, a period when the overriding fear was stagflation. Two developments ushered in this borrower-friendly era: the quantitative easing policies introduced in the wake of the 2008 and 2011 crises, and the expansion of global trade (including price and demographic shocks), which exerted a powerful disinflationary effect. That period came to an end—at least as far as unfettered free trade is concerned—with Covid, which triggered protectionist responses subsequently intensified by geopolitical tensions and wars. As for quantitative easing, it has not been entirely consigned to history: it could even return in Europe if the credit-spread crisis were to worsen.

Therefore, although the near-term direction of interest rates remains uncertain, as it depends on political decisions that can be taken at short notice, there is a strong possibility that the era of low interest rates is behind us for a long time and that we will have to get used to different trading ranges. Borrowers will quickly come under pressure, while lenders (including our clients) will welcome the change. For an asset manager, building a fixed-income portfolio in this environment becomes a particularly attractive opportunity.

Damien Liegeois

DISCLAIMER

Document completed on September, 6th, 2026. The information contained in this document is for informational purposes only and may contain errors. The information contained in the text and illustrations may not be copied or used without the prior agreement of 2PM. All rights reserved