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MARKET OVERVIEW JANUARY 2026

By Jean-Philippe Vandenborght, Head of Fixed Income, and Dominique Marchese, Head of Equities

OUR VISION FOR THE YEAR 2026

We dedicate this note to the outlook for financial markets in 2026, after a brief recap of the main events and trends of last year.

2025 RETROSPECTIVE: THE WORST IS NEVER CERTAIN

Financial market performance and the 2025 economic outlook ultimately proved far better than expected, despite fears of further chaos following Donald Trump's return to the White House. Aside from "Liberation Day" (the announcement on April 2nd of reciprocal tariffs, the culmination of trade tensions) and the eventful weeks that followed, volatility in major asset classes remained relatively subdued, disproportionate to the high level of uncertainty that prevailed throughout the year. **The global economy remained on track for volume growth of around 3% per year, demonstrating its resilience in a more conflictual geopolitical context.** The United States benefited significantly from investment spending in artificial intelligence (AI) and the resilience of consumer spending (driven by high incomes), despite the slowdown in the job market and the significant contraction in migration flows. The spread of tariffs was rather slow (with importers absorbing most of the burden), while retaliatory measures from trading partners remained limited—or even nonexistent in the case of the European Union (EU)—with the notable exception of China, which leveraged its dominant position in rare earth production and refining to pressure Washington. The eurozone, whose economic growth was slightly better than expected, nevertheless suffered from rather sluggish consumer spending. The stronger activity in southern Europe, particularly in Spain, contrasts sharply with the gloom experienced in the north. However, the announcement of Germany's large-scale stimulus plan for infrastructure and defense, adopted by the new ruling CDU-SPD coalition, and the growing awareness among Brussels institutions and key EU member states of the declining competitiveness of European industries (omnibus directives on simplifying regulations) have given investors a glimmer of hope. Eurozone volume growth is hovering around 1%, close to its potential. China continued to suffer from deflationary pressures linked to its real estate crisis. Its mercantilist policies, of which Europe is the primary victim, and its undeniable progress in the global race for new technologies, particularly in AI, have allowed it to offset weak domestic demand and achieve its official target of around 5% growth.

On the central bank and interest rate market front, the US Federal Reserve (Fed) did not express undue concern about the potential impact of tariffs on inflation, deeming it temporary and limited, which allowed it to continue its monetary easing policy in the latter part of the year. The European Central Bank (ECB), for its part, prudently considers the monetary easing phase to be over, given that inflation has shown signs of resilience above the 2% target. We note that energy prices have generally declined, which has allowed inflation expectations to be anchored after the 2022-2023 crisis, and has consequently raised hopes for continued wage moderation. Nevertheless, **long-term interest rates** in the eurozone have risen due to the German stimulus package, announcements of increased military spending, and France's lack of fiscal consolidation efforts, while long-term dollar rates have fallen due to weak employment and the resumption of the Fed's easing cycle. On the currency front , eurozone investors will undoubtedly have noticed the sharp depreciation (-12%) of the USD/EUR exchange rate, which has had a significant impact on the performance of international asset portfolios. **The independence of the US Federal Reserve from the executive branch and the trajectory of the federal debt remained key issues throughout 2025.**

AI remained a major theme, but it doesn't fully explain the performance of the main stock market indices. Overall, for the third year in a row, the major markets posted more than respectable results, in line with the historically low risk premiums observed in corporate credit markets, reflecting their sound financial health. Global equities rose by approximately 20% in USD and 8% in EUR. European equities, up 16%, also performed well, driven by Southern European exchanges, financial stocks, industrial companies, defense firms, and small-cap stocks . The leading US technology companies (the "Magnificent Seven") contributed nearly half of Wall Street's performance, with the main index rising by more than 15% in local currency.

The year 2025 finally ended with some glimmers of hope on the geopolitical front (easing of tensions in the Middle East, peace negotiations in Ukraine). Fears of an AI bubble, widely publicized and debated by investment professionals, demonstrate that markets, while cautious, are far from behaving irrationally. This is evidenced by the significant disparity in sectoral and individual stock market performance, and the questioning of the strength of oligopolistic positions (for example, Amazon.com versus Alphabet and Meta Platforms in digital advertising, or Nvidia weakened by the success of

Pure Capital S.A., société de gestion régulée par la CSSF (Luxembourg)
www.purecapital.eu | info@purecapital.eu

Siège social Luxembourg
2 rue d'Arlon, L-8399 Windhof | T : +352 26 39 86

Succursale Belgique
Sneeuwbeslaan 20, B-2610 Wilrijk | T: +32(0)3 246 04 65

manufacturers of AI-dedicated ASIC chips). **Hopes for productivity gains driven by AI, coupled with the US fiscal stimulus (OBBBA, an acronym for "** ***One Big Beautiful Bill Act*** **"), fueled investor optimism throughout the year.**

OUTLOOK 2026: MACROECONOMICS AND INTEREST RATE MARKETS

While the global economy's remarkable resilience to the 2025 tariff shock should be highlighted, it's also important to bear in mind that its full effects may not yet be behind us. Beyond further developments on this front, which are conceivable at any moment, **the main endogenous risk for the coming months stems from the US labor market** . The sharp slowdown in job creation and the gradual rise in the unemployment rate, if they were to persist for too long, would jeopardize the sustainability of this expansionary cycle. **However, we believe that a slide into recession will be avoided** thanks to the gradual reduction of trade uncertainty, the solid fundamentals of the private sector, favorable financial conditions, fiscal support from the Trump Administration, and investments related to artificial intelligence. **Europe has shown encouraging signs** in recent months and should begin to benefit more tangibly from the German spending plan, which could be further bolstered by a final wave of investments linked to the post-COVID recovery plan. Consumer purchasing power is supported by normalized inflation and a stable labor market, and their high savings rate provides a buffer against unforeseen shocks. **China is expected to slow** to below 5% in 2026, facing increased protectionism from trading partners and persistently weak domestic demand. **Overall, the economy is projected to post another year of growth around its current pace** .

inflation front , it is plausible that the transmission of the impact of tariffs to the US consumer will continue, maintaining the trajectory around 3% for a few quarters before beginning to slow down at the end of the year. Conversely, in Europe, the slowdown in wage growth and the strengthening of the currency suggest the possibility of a move slightly below the 2% target.

In this context, **the ECB may well have completed its mission** . With encouraging activity, normalized inflation, and a near-neutral monetary policy, it would take a major surprise to dislodge its governors from their prolonged pause. The **Fed** finds itself in a considerably less comfortable position, **torn between the conflicting forces** of inflation that has been above target for too long and the cracks appearing in the labor market... all **under pressure from a Trump administration** willing to do anything to secure more aggressive rate cuts. **We anticipate one or two further reductions in key interest rates in the first half of 2026 to ensure that unemployment stabilizes** , but **the specter of increased politicization of the institution looms** with the end of Chairman Powell's term and other issues surrounding the restructuring of the Governing Council.

bond front **, we expect long-term sovereign yields to remain broadly stable in 2026** (4.25% for the 10-year US Treasury yield, 2.85% for the German Bund). The potential for a cut in **the Fed's policy rates** could be seen as a supporting factor, but it is already well priced in by the market and limited in magnitude… except in the adverse risk scenario of compromised Fed independence. On the long end of the yield curve, concerns about **recurring budget deficits** persist, but the **return of steeper slopes** may provide an incentive to exit money market instruments. Overall, we believe that **decent carry and the potential for diversification in interest rate markets** under certain extreme scenarios should generate sufficient appetite from global investors. We continue to value **credit markets** in a **favorable macroeconomic environment** and given the **strong fundamentals of companies** – although increased mergers and acquisitions and the financing of artificial intelligence spending could lead to a slight deterioration. **However , risk premiums** (credit *spreads) are* **extremely compressed** , in line with the lows of the last thirty years. **Given the risk asymmetry, we are adopting a rather defensive stance at this stage, favoring** ***investment-grade debt*** for new investments. **Close attention will continue to be paid to the selection and diversification of securities** .

In the **foreign exchange market , we maintain our EUR/USD forecast range of 1.15-1.20** , implying **further but limited upside potential** for the single currency. This potential could materialize primarily at the beginning of the year, with favorable **momentum for the European cycle combined with downside risks to dollar rates,** both for fundamental reasons (deteriorating labor market) and in the context of credibility issues (Fed independence). Increased market focus on the **twin deficits** (budget and current account) and a still somewhat elevated **valuation** are other risk factors for the greenback. We believe, **however, that the dollar could stabilize, or even recover slightly, later in 2026** after the job market stabilizes and there are signs that the Fed is maintaining its independence. **Within diversified portfolios, the dollar also remains a An interesting tool for hedging against certain types of cyclical and geopolitical risks** .

WHAT CAN WE EXPECT FROM THE STOCK MARKETS?

Indices are highly valued, risk premiums are heavily compressed, leaving little room for unpleasant surprises, especially in New York and in sectors driven by the AI revolution (semiconductors, data center equipment, energy infrastructure, power producers, etc.). However, this high valuation was already observed at the beginning of 2025. Expectations of earnings growth in 2026, which are not unreasonable, are supporting investor optimism (around +15% in the Eurozone and on Wall Street). Hopes for productivity **gains fueled by AI, coupled with the effects of a slightly more favorable** ***policy mix*** **(monetary policies and budget deficits) globally (Eurozone, United States, China), are fueling this enthusiasm for risky assets, even if questions about the return on massive investments in AI will remain prominent in the coming months.** In any case, the behavior of Wall Street, whose size accounts for nearly two-thirds of all global stock exchanges, will remain the determining factor in the trajectory of financial markets. In this respect, investors will closely monitor the

Pure Capital S.A., société de gestion régulée par la CSSF (Luxembourg)
www.purecapital.eu | info@purecapital.eu

Siège social Luxembourg
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Succursale Belgique
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evolution of American household consumption and the investment cycle of companies that Washington is seeking to stimulate beyond the sole sphere of AI (OBBBA budget law), if necessary through the threat of trade sanctions against foreign companies (see, for example, the intense political pressure on the pharmaceutical sector to relocate production sites to the United States).

In a world that has become far more conflictual, markets seem to recognize the remarkable adaptability of private companies, including European ones, which have integrated geopolitical risks into their business management and investment choices. The spectacular stock market recovery of eurozone banks (aided by the interest rate environment), whose *business model* was considered, until recently, to be seriously threatened by new entrants (the *fintech sector*) and regulation, testifies to this robustness in the face of change. Since the 2008 *subprime mortgage crisis* , the underestimation of this adaptability and resilience in the face of numerous political upheavals and multiple financial crises has been the most glaring error of bearish investors. While climate issues remain a pressing concern, the AI revolution will further strengthen this resilience and flexibility in a geopolitical environment far more chaotic than in the past.

The high concentration of technology stocks in indices, the high valuations of AI ecosystem sectors, and the overwhelming weight of US assets argue for greater diversification, both geographically and sectorally. This allocation strategy already proved successful in 2025 during the sharp depreciation of the dollar against the euro. Europe and emerging markets, whose industrial leaders are exposed to global growth, remain cheaper than Wall Street. The European financial sector, benefiting from the steepening yield curve, being more domestic and less directly exposed to trade tensions, remains attractive from a shareholder return perspective (dividends and share buybacks). The small-cap segment continues to offer value on both sides of the Atlantic, despite the strong rebound observed last year in Europe. Chinese technology remains undervalued compared to its US competitors, despite its remarkable successes in AI. Finally, many sectors will undoubtedly benefit from the large-scale deployment of AI in the coming years. We can cite the pharmaceutical sector, which is inexpensive outside the segment driven by anti-obesity drugs, and whose R&D productivity will be boosted by the use of these new technologies. More generally, while the service sector will see many tasks automated, the combination of AI and robotics promises increased productivity in industrial sectors.

In short, the stock market is by no means limited to Wall Street and the "Magnificent Seven." The trajectory of corporate profits will determine the performance of the indices. From this perspective, we are not hesitant to adopt an optimistic outlook at the start of this year, while emphasizing the need for optimal portfolio diversification to allow them to best absorb the inevitable spikes in volatility.

OUR WISHES FOR 2026

We take this opportunity, with the first letter of the year, to thank you for your interest in our monthly newsletter, and wish you all the best for a prosperous 2026.

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