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UBS Asset Management
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Macro Quarterly

Insights on market dynamics and investment themes

Q3 2026

UBS

The bull market can survive higher rates

1. We see continued resilience in the global economy, supported by an improving US labor market and accelerating global manufacturing activity.

2. While lower oil prices should bring headline inflation down, we expect US core inflation to remain sticky and elevated, keeping Fed rate hikes firmly on the table.

3. Monetary policy uncertainty may generate volatility, but we think strong and broadening earnings growth can continue to fuel equity market gains this year.

4. AI hardware remains supported by surging earnings growth, but crowded positioning and rising leverage warrant diversification into broader markets in case the AI narrative becomes challenged.

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As oil prices return to pre-Iran war levels, we expect continued resilience in the US and global economy. Lower oil prices should help reduce headline inflation and support real consumer spending. Still, we expect underlying inflation in the US to remain sticky and elevated, keeping the risk of Fed rate hikes alive.

The key investment implication is that higher US rates may create volatility, but we do not think a somewhat higher Fed Funds rate is likely to derail the equity bull market as long as earnings growth remains strong and continues to broaden beyond artificial intelligence (AI). We believe that corporate earnings will remain robust, supported by the ongoing boom in AI spending as well as continued profitability across non-tech companies.

We have conviction that earnings growth will power global equities higher over the second half of the year, even if gains are accompanied by increased volatility from monetary policy uncertainty.

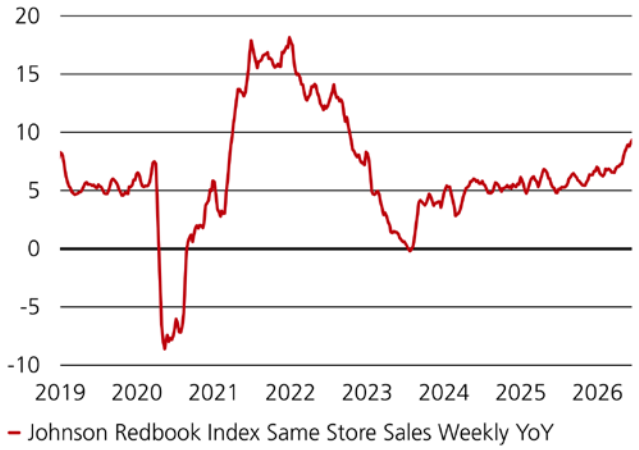
In fixed income, we expect increasing divergence. We see upward pressure on US rates, while rates should remain steadier in other markets where underlying inflation is less sticky and growth cooler. These moves in relative rates can keep the US dollar supported versus other major currencies. We also see opportunities in selective EM FX, but prefer to fund those positions via the lower yielding Swiss franc.

Resilient growth, sticky inflation

The US labor market has accelerated this year after near-zero employment growth in 2025. The three-month moving average of job growth reached a very strong 188,000 through May. While employment growth is unlikely to remain quite that robust, even a step down would still be healthy, given that the breakeven pace needed to keep the unemployment rate steady is estimated to be closer to 60,000. We believe the improvement in the labor market should support consumer spending, which has remained solid despite the oil shock.

Much has been made of the K-shaped economy, where overall economic health and spending are driven far more by higher-income than lower-income consumers. However, there is incremental evidence that the "bottom of the K" is inflecting higher, with banks and credit card companies recently reporting improving spending among lower-income consumers.

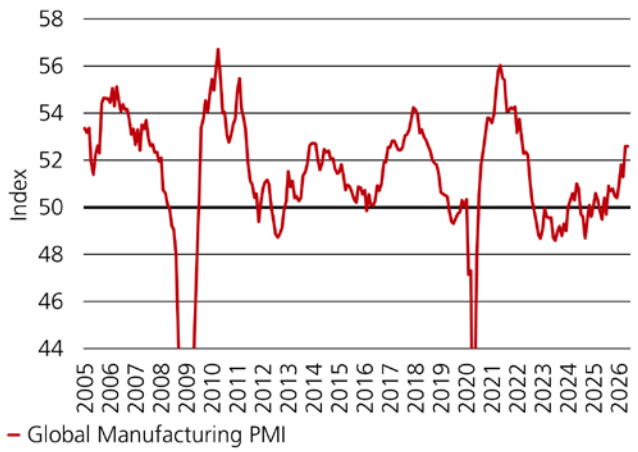
Exhibit 1: US nominal spending is picking up
Johnson Redbook Index Same Store Sales Weekly YoY, 4 week moving average



Source: UBS Asset Management, Johnson Redbook, Macrobond. Data as of June 2026.

Resilience extends beyond the US. Global manufacturing. PMIs have moved well into expansionary territory, with increasing breadth across regions and sectors. The AI capital expenditure (capex) boom supporting the US and EM Asia is well established, but we increasingly see non-tech capex inflecting higher as well. This reflects both a cyclical rebuilding of inventories and a structural trend toward investment in national resilience, including defense spending and the reorientation of supply chains.

Exhibit 2: Global Manufacturing PMI is at a multi-year high

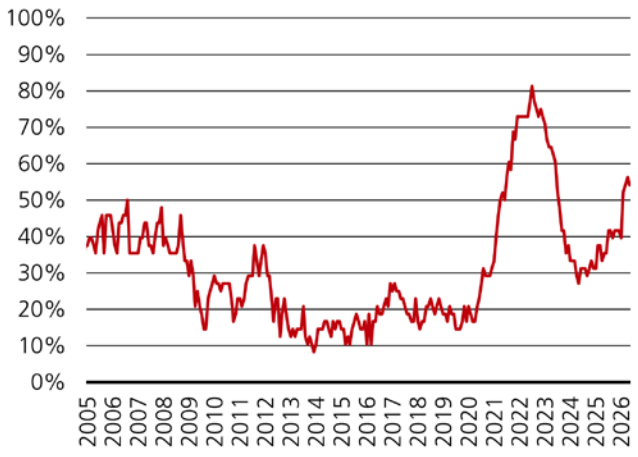


Source: UBS Asset Management, Macrobond. Data as of May 2025.

On inflation, the decline in oil prices below pre-conflict levels should put downward pressure on headline inflation and limit pass-through to some core measures. That said, we continue to view underlying inflation as sticky and above the Federal Reserve's (Fed) 2% target. Core services inflation excluding housing has rebounded to above 3%. In addition, more than half of the components of core PCE are running above 3%. In short, inflation is not just an oil story.

Exhibit 3: Underlying US inflation has been broadening out

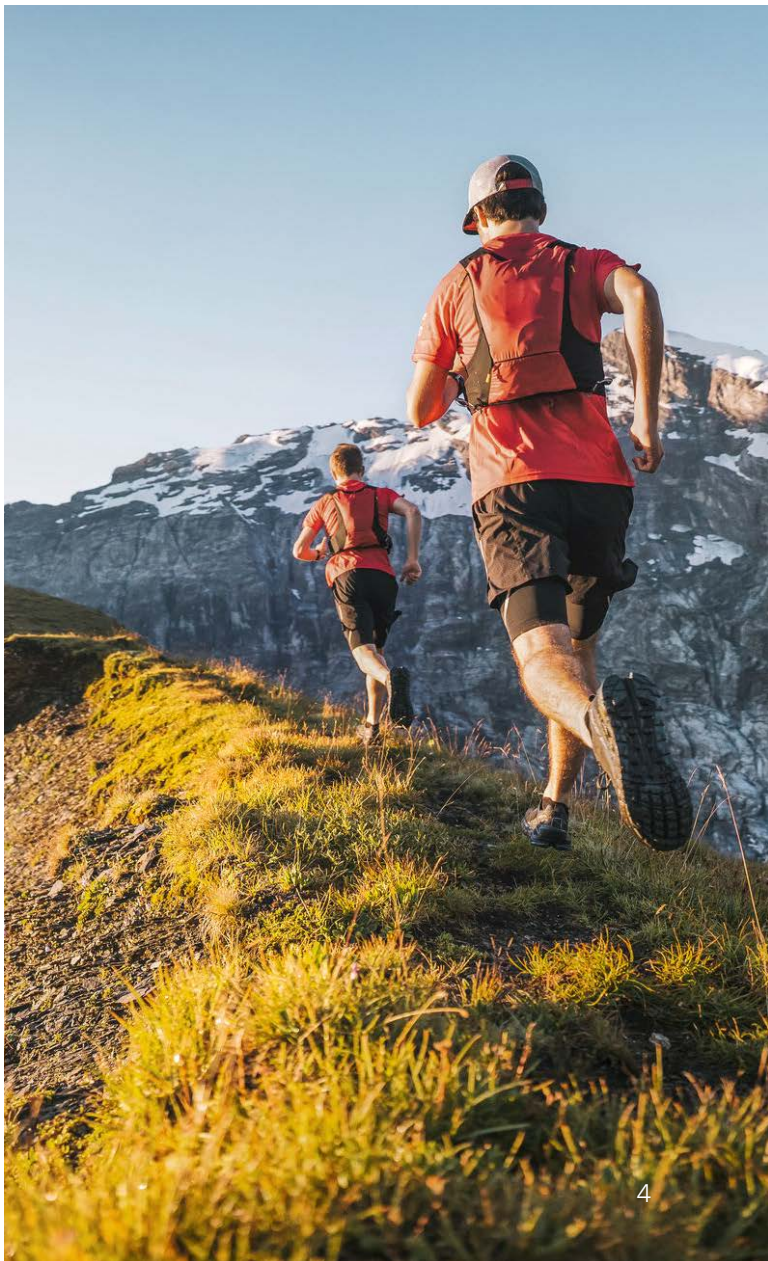
United States, % of Core PCE Line items >3% (Level 5 of 9:50 items)



Source: UBS Asset Management, U.S. Bureau of Economic Analysis (BEA), Macrobond. Data as of June 2026

The rebound in the labor market and the persistence of inflation have shifted the Fed in a hawkish direction. Nearly all FOMC members now view risks to price stability as skewed to the upside, while labor market risks have shifted to a more balanced assessment. An increasing number of FOMC members are signaling a willingness to hike rates this year.

Moreover, new FOMC Chair Kevin Warsh has gone out of his way to stress the importance of delivering price stability, as defined by an unchanged 2% inflation target, after five years of missing that target to the upside. Our conversations with clients suggest there is underlying skepticism that the Fed will hike rates this year because of political considerations. We think a Warsh-led Fed will be more willing to deliver rate hikes if labor market strength and core inflation justify action, which looks increasingly likely.



Markets can withstand Fed hikes

In our view, the increasing potential for Fed tightening is a manageable headwind rather than a reason to abandon risk assets. With US household and corporate leverage still near multi-decade lows, we do not view a few hikes as a meaningful risk to the economy. A few rate hikes could cool very strong nominal GDP growth and create some market volatility, but we doubt they would spell the end of this bull market.

The reason is straightforward: equities are ultimately driven by earnings growth, and earnings growth remains very robust. The blistering earnings growth seen in the US and emerging markets is driven in large part by the surge in demand for AI hardware. But beneath the surface, earnings growth is fairly broad. The median S&P 500 stock delivered 14% earnings growth in Q1, one of the strongest quarters in a decade. Given that capex spending is increasingly broadening into non-tech areas and that consumer spending should remain resilient, we see room for non-tech cyclicals to play a greater role in driving market performance in the second half of 2026.

There is also increasing attention on the rising supply of equities, both from mega IPOs and secondary issuance. Goldman Sachs estimates a potential increase in issuance of USD 700 billion this year. As with rate hikes, we view this as a modest headwind rather than a major risk to the market. Buybacks are expected to remain strong at USD 1 trillion, meaning net issuance should still be negative, though less negative than in recent years. Looking historically, we do not see convincing evidence that major IPO activity is a major driver of forward equity market performance.

The primary risk we see to the market is a meaningful downward shift in expectations for AI capex spending. The AI capex cycle has been a boon to markets and household wealth, so a change in the narrative could undermine markets and potentially weigh on consumer confidence. We are also aware that the AI narrative can shift well before earnings expectations. As a result, we are tracking several indicators that we think will be central to sustaining optimism around AI capex spending. These include adoption rates, token spending, GPU prices, and memory prices. At the moment, these indicators are generally still pointing in a positive direction, but they merit close monitoring.

Asset allocation

We remain overweight equities and prefer emerging markets and Japan, where our leading indicators point to the strongest earnings growth. Maintaining exposure to AI-linked stocks makes sense given surging earnings growth, but increased crowdedness and growing participation in leveraged single-stock ETFs highlight the need for diversification. Indeed, increased concentration in tech across both US and EM equities strengthens the case for more active selection.

The macro backdrop also supports a more differentiated approach across asset classes. Sticky US inflation and a more hawkish Fed leave us cautious on US duration, and we expect US Treasuries to underperform equities as the rates market increasingly skews toward rate hikes. However, we do see value in UK and Australia duration as those economies cool.

Similarly, we expect the US dollar to remain strong as the Fed stays hawkish while other central banks slow their tightening cycles, reflecting more energy-driven inflation indexes and slower growth. We selectively like EM carry, particularly the South African rand, but prefer to fund those positions in Swiss francs rather than US dollars.

Asset class views

The chart below shows the views of our Asset Allocation team on overall asset class attractiveness for global equities, rates and credit as of 30 June 2026. The rest of the ratings pertain to the relative attractiveness of certain regions within the asset classes of equities, bonds, credit and currencies. Because the Asset Class Views table does not include all asset classes, the net overall signal may be somewhat negative or positive.

Asset Class	Relative weight	UBS Asset Management's viewpoint
Global equities	Overweight	We remain overweight global equities, supported by strong earnings and still solid growth. We prefer emerging markets and Japan vs. Europe and Switzerland.
US	Neutral	In our view, earnings should remain strong in the US and fundamental backdrop is solid with nominal GDP elevated. Earnings growth has been broadening out even as the tech sector continues to lead.
Europe	Underweight	We are underweight European equities, as earnings growth remains weaker than other regions. Still, we like European banks, which should benefit from strong earnings and elevated rates.
Japan	Overweight	Japanese equities screen best on leading EPS revisions, supported by stronger economic surprises and improving activity data. The broad TOPIX index provides exposure to broader cyclicals beyond just AI, offering diversification beyond the US and EM.
Emerging markets	Overweight	We are overweight EM equities as earnings are strong across most regions. The MSCI EM index is heavily weighted toward North Asian tech giants, which benefit strongly from the ongoing AI capex cycle.
Global government bonds	Neutral	Rates curves have repriced higher amid resilient economies and inflationary pressures. There is significant differentiation across economies so we prefer to position in relative value.
US Treasuries	Underweight	US Treasuries are expected to underperform other regions given underlying cyclical strength and sticky underlying inflation which may lead to a few rate hikes.
Bunds	Neutral	The market has priced in meaningful tightening from the ECB even as recent growth data have disappointed. We still prefer gilts on better valuations and a weaker economic outlook, given the ongoing ramp up in German fiscal spending.
Gilts	Overweight	We remain overweight gilts as we find valuations attractive. Very restrictive policy is being priced for the BoE which should eventually hamper growth and keep a lid on how much higher 10yr yields can go. We are keeping an eye on political developments and potential for fiscal slippage.
JGBs	Neutral	We are neutral on Japanese government bonds. Although the BoJ is likely to raise interest rates further, we expect it will act slowly, while carry costs of shorting JGBs are elevated due to the low BoJ policy rate.
Swiss	Neutral	We are neutral on Swiss bonds. While the domestic economy remains lackluster, valuations are expensive on a relative basis.
Global credit	Neutral	Backward-looking fundamentals look strong amid low default rates and solid corporate earnings. That said, spreads at these levels still maintain an unattractive asymmetry, particularly considering increased issuance to fund AI capex spending.
Investment grade credit	Neutral	IG spreads remain historically tight, supported by solid earnings and balance sheets, which limit downside risks. At the same time, the market must increasingly absorb supply tied to AI capex financing needs.
High yield credit	Neutral	We expect spreads to remain range-bound at current tight levels, with default rates rising but contained. Investors interested in hedging private credit exposures may do so via more liquid public markets.
EM debt hard currency	Neutral	We are neutral on EMD in hard currency but overweight local currency, where selective carry remains attractive. We remain attentive to the reaction function of EM central banks as they face possible inflation spillovers from the Iran conflict.
FX	N/A[1]	N/A[1]
USD	Neutral	We expect USD to be neutral to firmer should the Fed deliver rate hikes this year. A broad improvement in global manufacturing may limit some of the USD's upside.
EUR	Neutral	Pressure on the EUR should ease as oil prices normalize. We expect the ECB to deliver at least one more rate hike.
JPY	Neutral	USDJPY is likely to continue to face upward pressure unless the BoJ becomes significantly more hawkish or Japanese institutional flows turn JPY supportive. Potential FX intervention keeps us neutral the currency.
CHF	Underweight	Low yields and expensive valuation make CHF an attractive funding currency, especially with geopolitical risk easing.
EM FX	Overweight	We favor high carry EM currencies, including ZAR, which offer high real interest rates and attractive valuations.
Commodities	Neutral	We see energy trading two-way as low current inventories square up against a normalization of supply as the Strait of Hormuz gradually opens. Gold faces headwinds from potential Fed tightening, but central banks continue to buy.

Source: UBS Asset Management Investment Solutions Macro Asset Allocation Strategy team. The views expressed are general guide to the views of UBS Asset Managementas of 30 June 2026. Views are provided on the basis of a 3-12 month investment horizon, are not necessarily reflective of actual portfolio positioning, and are subject to change.

1 N/A (consistency) was added for accessibility purposes. For FX, our view is shown according to its respective currencies (USD, EUR, JPY, CHF and EM FX).

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