

Autumn
2026

market outlook.

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contents.

2 UK

3 Europe

4 US

5 Japan

6 Asia & Emerging

7 Fixed Interest

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The UK Economy

The UK economy has remained more resilient than many expected, with employment holding up relatively well and consumers continuing to spend despite subdued confidence. While confidence remains below its long-term average, it reached a two-year high in September, suggesting sentiment may be improving. The summer weather also provided a timely boost, with retail sales volumes rising by 0.9% in the three months to August and standing 2.4% higher than a year earlier. Although the labour market has continued to cool, with unemployment rising to 4.7% in June to August, wage growth moderating and vacancies falling, the adjustment has so far been gradual rather than a sharp deterioration. Importantly, household finances are generally in a healthier position than following previous downturns, providing a degree of resilience to consumer spending.

However, we may find that there are some headwinds for household finances as we look ahead. As the colder months approach, rising energy costs could present an issue for household budgets - current forecasts suggest the energy price cap could increase by more than 20% in January. At the same time, more homeowners are coming to the end of mortgage deals fixed at historically low rates, leaving them to refinance at significantly higher borrowing costs. While consumers have so far proven to be remarkably resilient, the combined impact of higher mortgage payments and energy bills could put finances under some pressure over the coming months.

The Budget delivered few major surprises, with markets responding positively to the absence of significant unexpected policy changes, although most measures are unlikely to materially alter the economic outlook in the near term. The Government remains focused on growth, infrastructure, and housing delivery, reflecting a broader political backdrop in which voters appear increasingly receptive to policymakers who prioritise public services and local investment. However, while such priorities appear to resonate with the electorate, some business groups remain cautious about policies perceived as increasing regulation or costs. Meanwhile, household finances are likely to remain driven primarily by wages, inflation, and interest rates. Inflation remains a key concern, with CPI expected to move higher in the near term, partly reflecting elevated energy costs, although there is currently limited evidence that these pressures are feeding through meaningfully into broader prices and wage growth. Against this backdrop, the Bank of England has maintained a cautious stance, and we believe there is little need to rush into further policy changes, particularly as the recent energy shock may yet prove temporary. Nevertheless, market pricing currently implies around two further rate hikes by the end of Q2 2027, suggesting investors expect policymakers to remain focused on containing inflationary pressures.

The UK market continues to look attractive, with valuations remaining significantly below those of many international markets, particularly the U.S. Unlike some overseas markets, the UK has relatively limited exposure to highly valued AI and technology companies that have driven much of the recent market performance. While this lack of exposure to fashionable, momentum-driven stocks may have weighed on returns in the short term, it could prove advantageous if investor sentiment towards expensive growth companies begins to weaken.



The European Economy

The European economy has continued to expand, with Eurozone GDP growing by 0.4% in the third quarter, despite a challenging global backdrop. However, the combination of rising inflation, higher energy prices, and elevated borrowing rates threatens the momentum of future growth. Dependence on imported energy leaves it particularly vulnerable to the ongoing Middle East conflict. Limited direct exposure to disrupted gas supplies reduces the risk of significant shortages, although elevated oil and gas prices continue to place upward pressure on inflation and constrain household spending and industrial activity. The sustainability of Europe's economic resilience will therefore depend heavily on the duration of the energy disruption.

European economic growth and labour markets have remained resilient despite challenges. The European Central Bank (ECB) raised interest rates twice this year, taking the deposit rate to 2.50%, before holding rates steady in October. However, the outlook has become more uncertain, with global borrowing costs rising and energy prices moving higher, both of which are likely to weigh on growth and confidence. Policymakers have therefore focused on whether higher energy costs feed through to underlying inflation rather than reacting to short-term price pressures. For investors, although higher borrowing costs and energy market volatility warrant some caution, the resilience of the European economy and the ECB's balanced policy stance provide a supportive backdrop if conditions deteriorate.

Corporate earnings have been stronger than expected despite ongoing economic uncertainty. However, much of this resilience has been concentrated in energy companies and firms benefiting from AI and data centre investment. European manufacturers, particularly automakers, continue to face challenges from elevated energy costs, weak productivity growth, and increasing competition from China, where producers have gained significant cost and technological advantages. Whilst there are ongoing EU-China trade talks, competitive pressures remain intense. Meanwhile, Europe's luxury goods sector is facing softer demand and changing Chinese consumer preferences, creating potential headwinds for earnings. While European banks remain resilient, supported by strong earnings and capital positions, the earnings outlook across the broader market remains less certain.

Political uncertainty and constrained public finances remain key risks for Europe, particularly as several countries approach important elections in 2027. Higher borrowing costs and fiscal pressures in heavily indebted economies such as France and Italy have weighed on investor confidence. In Germany, the anticipated benefits of increased infrastructure and defence expenditure have yet to translate into a meaningful improvement in industrial production, although the longer-term economic impact could become more apparent as spending gathers momentum. If energy prices continue to ease, the regional growth outlook could improve further, however, caution remains warranted.



The US Economy

Following the U.S. midterm elections, Democrats secured control of both the House of Representatives and the Senate, reshaping the balance of power in Washington after a challenging period for Republicans marked by President Trump's declining approval ratings, the conflict with Iran, and rising living costs. President Trump has accepted the result and indicated a willingness to work with Democratic lawmakers, easing concerns over political instability. This outcome has generally been viewed positively by both domestic and global markets, particularly in China. A reduction in policy control is expected to lessen uncertainty and reduce the scope for disruptive policy shifts. While the president would retain executive authority, Democratic control of Congress is likely to increase oversight and make the administration's broader legislative agenda more difficult to implement. Historically, midterm elections that weaken the incumbent party's grip on power have often been associated with stronger equity market performance. The reduced likelihood of significant legislative shifts may provide a more predictable backdrop for markets and support investor confidence in U.S. equities.

The U.S. economy remains relatively well positioned, with resilient consumer spending and robust corporate earnings, particularly within the technology and AI sectors. However, the conflict in the Middle East has persisted for considerably longer than initially anticipated, with ongoing disruptions to global energy markets contributing to higher oil prices, renewed inflationary pressures, and increased costs for households and businesses. While these developments warrant close monitoring, the underlying strength of the U.S. economy has helped absorb much of the impact to date. The majority now sits with the Democrats in the House and Senate which may increase pressure for a diplomatic resolution to the conflict and reduce the likelihood of further war-related spending. Any meaningful de-escalation could see oil prices fall rapidly, easing inflation concerns, reducing expectations for further monetary tightening, and providing an additional tailwind for U.S. equities.

Although valuations among some of the largest U.S. technology companies remain elevated, they continue to be supported by strong earnings growth, profitability, and significant investment in artificial intelligence. While the technology sector came under pressure globally towards the end of the quarter, there was little evidence of any meaningful deterioration in underlying demand or revenues. Earnings across the major technology companies remained robust, supported by continued growth in cloud computing and artificial intelligence. Microsoft reported strong revenue growth, while Amazon increased operating profits by 61%, highlighting the resilience of both corporate and consumer demand. With investor expectations remaining exceptionally high, periods of increased scrutiny and short-term volatility have become commonplace and present buying opportunities for long term investors. Nevertheless, underlying fundamentals remain supportive, and opportunities continue to exist both within and beyond the largest technology and AI beneficiaries.

The US Economy Continued...

U.S. annual core inflation (excluding food and energy) remained relatively contained at 2.6% in September, suggesting broader inflationary pressures remain limited. Although labour market data has been mixed, economic growth and consumer spending have remained resilient, with GDP growth accelerating to an annualised 3.4% in the third quarter. Reflecting the economy's underlying strength and persistent inflation risks, the Federal Reserve raised its target interest rate by 25 basis points in September to 3.75%-4.00%. Following the midterms and the loss of Republican control of Congress, this reduces Trump's ability to put pressure on the Federal Reserve, which will be supportive for markets. Therefore, as it stands markets may be overestimating the extent of further monetary tightening required, with policymakers likely to favour a measured approach and any additional increases expected to be gradual. A less restrictive policy path than currently anticipated could provide a supportive backdrop for U.S. equities, particularly if corporate earnings remain resilient. A relatively strong U.S. dollar could further enhance returns for UK-based investors when gains are converted back into sterling.



The Japanese Economy

Having once been a global leader in technology, Japan is now seeking to re-establish its position among the world's leading technology nations, particularly as the U.S. and China continue to make significant advances. Investment in artificial intelligence and semiconductor technology has become a strategic priority for the Japanese government, which is working to integrate semiconductor manufacturing with AI infrastructure, data centres, robotics, automation, and next-generation computing. Reflecting the scale of this ambition, Japan has outlined plans to support more than ¥102 trillion of public and private investment in AI and semiconductors, while encouraging major investments from companies such as TSMC. Together, these initiatives aim to strengthen Japan's position within AI-related supply chains, rebuild domestic semiconductor capabilities, reduce reliance on overseas production and position the country to benefit from further developments in the global technology cycle.

Japan is in a relatively unique economic environment. While further interest rate rises may be necessary, the Bank of Japan (BoJ) will need to consider that much of the country's inflationary pressure stems from imported energy costs, reflecting its reliance on overseas oil and gas. As a result, monetary tightening may have limited effectiveness in addressing these external pressures. Equally, should geopolitical tensions ease and disruption around the Strait of Hormuz subside, energy prices could moderate, helping to bring down imported commodity-related inflation pressures. In that scenario, policymakers would be better placed to assess underlying domestic inflationary trends and, if economic conditions warrant it, raise interest rates in a more measured and appropriate manner. With this in mind, the BoJ is likely to remain cautious, assessing incoming economic data before making significant changes to monetary policy. It will also need to consider Japan's close financial relationship with the U.S., particularly given its position as a major foreign holder of U.S. Treasuries. This interconnectedness reinforces the importance of global financial conditions, meaning the BoJ is likely to remain attentive to the actions of other major central banks when determining its own policy path, at least over the short term.

We believe Japanese smaller companies offer an attractive long-term investment opportunity, supported by a range of government initiatives aimed at strengthening the domestic economy. Significant backing for the semiconductor and AI industries, government-supported wage growth, and ongoing corporate reforms are helping to improve productivity, capital efficiency, and shareholder returns. Together, these structural changes could create compelling opportunities for investors to identify smaller companies well positioned to benefit.

Japan's economy continues to demonstrate modest resilience, with GDP growing at an annualised rate of 1.4% in the second quarter. While recent trade figures have been subject to some short-term distortion, partly reflecting the release of strategic oil reserves and disruption to energy imports, exports have shown signs of improvement, supported by demand from the U.S. and other key markets. The government's commitment to strengthening trade and investment ties with the U.S., alongside policies designed to support domestic businesses, provides a positive backdrop for economic growth. Whilst pricing power has improved, pointing to a gradual recovery in wage growth, persistent inflation continues to weigh on consumer sentiment. As a result, the outlook for household spending remains uncertain, suggesting caution is still warranted.



Emerging Markets & Asia Economy

China’s economy has remained resilient, expanding by 4.5% in the third quarter and remaining on track to meet the government’s growth target. While domestic consumption and the property sector remain weak, exceptionally strong exports and investment in technology-related industries have helped sustain growth. Chinese manufacturers, particularly in the automotive sector, continue to strengthen their global competitiveness through scale, integrated supply chains and greater control over key raw materials. China has so far reacted positively to the U.S. midterm results, with the prospect of a more stable policy environment. Although some near-term volatility may persist, improved policy predictability and a lower risk of additional trade and regulatory measures could support sentiment, particularly for Chinese technology companies. Against this backdrop, China continues to offer compelling long-term investment opportunities, particularly in sectors driven by innovation and increasing global competitiveness.

The rapid expansion of artificial intelligence continues to create significant investment opportunities across Asia and Emerging Markets, particularly in semiconductors. South Korea's benchmark KOSPI index has experienced periods of heightened volatility, with markets seeing sharp moves both higher and lower as investors reassess growth expectations and reposition around evolving AI-related themes. Similar dynamics have played out across global markets, particularly in the U.S., although the effect has been more pronounced in South Korea due to the higher concentration of semiconductor and technology companies. While near-term fluctuations are likely to persist, the opportunity extends well beyond the largest companies to the broader semiconductor ecosystem, including equipment suppliers, specialist manufacturers and infrastructure providers. The long-term investment case remains attractive, supported by structural growth drivers, ongoing innovation and increasing AI adoption.

India’s long-term growth prospects remain attractive, supported by favourable demographics, infrastructure investment and rising domestic consumption, although 2026 has proved a challenging year for Indian equities. As a major oil importer, the prolonged Middle East conflict continues to create inflationary pressures and weigh on corporate profitability. Government efforts to contain retail fuel prices have provided some protection for consumers, but have also squeezed suppliers’ margins, with some restricting sales volumes to limit losses. Investor interest has increasingly shifted towards AI-driven opportunities elsewhere in Asia, contributing to India's relative underperformance. The resulting moderation in valuations may create attractive opportunities for long-term investors, particularly if lower energy prices and easing inflation support investor confidence and earnings growth.

In Brazil, President Lula's re-election led to market volatility, as markets had anticipated that a Flávio Bolsonaro administration might pursue a more market-friendly policy agenda. Looking ahead, policy continuity under Lula could provide greater stability, although investor confidence will remain closely tied to fiscal discipline. While Lula and U.S. President Trump have clear policy differences, the relationship may prove less fractured than often portrayed. Trump's loss of control over Congress is likely to reduce his ability to exert trade pressure on countries such as Brazil, a development that has been viewed positively by Brazilian markets. A less confrontational trade stance will help lower external risks, allowing Brazilian equities to function more freely without disruption. With much of the recent weakness in equities reflecting election-related uncertainty rather than any deterioration in the country's long-term outlook, higher commodity prices could provide an additional tailwind for Brazil as a major exporter of oil, agricultural products and industrial commodities. Together with more attractive valuations, this may create compelling opportunities for long-term investors.



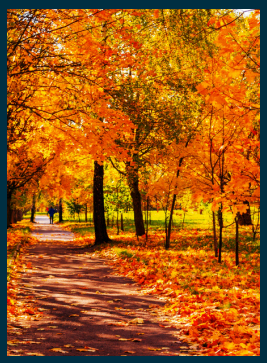
Fixed Interest

Government bond yields have continued to be pressured this quarter, and we have seen spreads widen. However, despite rising yields, corporate bond returns have been only marginally negative, as the higher income they now offer has largely offset the impact of the yield increases. It is important to note that while yields have increased this year, bond markets have remained orderly.

Yields have been pushed higher by a combination of factors, including changing interest rate expectations, fiscal deficits, inflation expectations, and an increase in bond supply across both government and corporate markets.

Hyperscale debt issuance – a relatively new phenomenon – is beginning to change the composition of the global corporate bond market (including the sterling market). While we are cognisant that large changes can draw concern, it must be noted that company balance sheets are still robust, and leverage metrics are not concerning. Further issuance is expected, and we will continue to monitor the market closely for any emerging risks. While significant shifts in index composition would inevitably alter passive exposure to the sector, we believe this creates an opportunity for our actively managed funds to demonstrate their value. Our fund managers can assess each issuance on its individual merits, rather than taking a broad-brush approach.

Ultimately, the higher yields we now see across the sector mean forward returns are likely to be much more substantial. Additionally, while spreads remain relatively tight, they have also widened. Of course, there are further obstacles to contend with, such as the UK Budget, U.S. midterms, and European political issues, which may contribute to some volatility in the short term. However, the long-term opportunity remains attractive across the maturity spectrum.



If you would like to discuss this or any other aspect of your portfolio, please do not hesitate to contact us on 0800 049 2011, Monday to Friday 9am-5pm or you can email us at affinity.advise@wealthatwork.co.uk

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