PRINCIPAL

Investment Report
Q1 2026

Market Outlook 2026: Opportunities and excesses

In 2025, the year-end rally commenced earlier than anticipated. Supported by globally expansionary monetary and fiscal policies, growth momentum carried through the fourth quarter. Numerous asset classes reached new all-time highs, while geopolitical tensions intensified.

Gold once again emerged as a key beneficiary of rising uncertainty. During the fourth quarter, the price of the precious metal advanced by +12.1% (in EUR), reaching a new all-time high of USD 4'547 per troy ounce. Silver and platinum also recorded peak price levels during the period.

Global equity markets similarly climbed to fresh record highs (+3.2% in EUR). Over the course of the quarter, investor sentiment gradually shifted towards a more risk-averse stance, triggering notable rotations across styles and sectors. Defensive value stocks in Switzerland attracted strong capital inflows, while cyclical U.S. growth stocks underperformed.

In currency markets, the U.S. dollar entered a phase of stabilization. Following a pronounced depreciation earlier in the year, the greenback found support in the fourth quarter and traded largely unchanged against both the euro and the Swiss franc.

2026 Market Outlook

The year 2026 presents meaningful opportunities alongside idiosyncratic risks. We expect U.S. economic growth to moderate, yet continue to surprise on the upside. This outlook is supported by rising productivity, expansionary monetary and fiscal policies, and a strengthening investment cycle.

In the Eurozone, we maintain a stance of cautious optimism. The German automotive industry, in particular, remains under pressure from the transition to electromobility, persistent supply chain challenges, and intensifying competition from Asia.

Following four key interest rate cuts by the European Central Bank in 2025, we expect a pause in the easing cycle in the coming year, with the Swiss National Bank (SNB) likely to follow a similar path. Given political resistance from pension funds and insurance companies, the SNB is expected to refrain from reintroducing negative interest rates in 2026. Instead, we anticipate increased foreign exchange interventions aimed at limiting excessive currency appreciation and safeguarding the international competetiveness of the Swiss industry.

In currency markets, we initially expect a technical countermovement for the U.S. dollar. However, due to the unexpectedly sharp compression in yield differentials over the course of the year, renewed depreciation pressures are likely to re-emerge. Emerging markets stand to benefit from this development. In particular, we see attractive earnings potential in equities from China, India, and Vietnam in 2026.

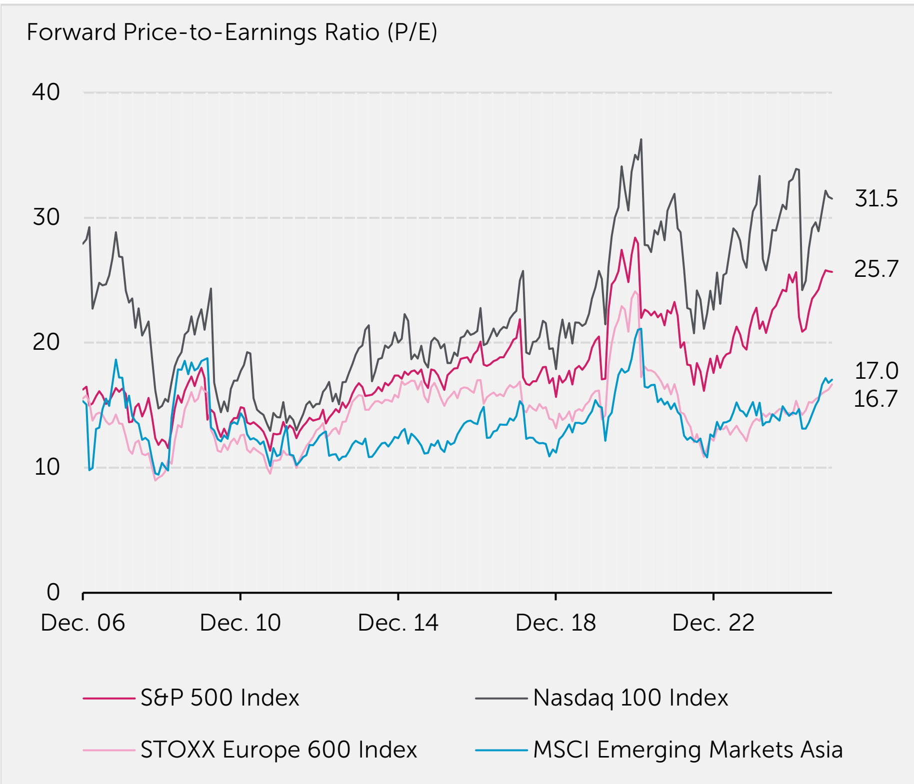
Against the backdrop of escalating geopolitical tensions and the strategic ambitions of Asian emerging markets, demand for gold is expected to remain robust. We anticipate that gold will reach new all-time highs in 2026, targeting levels of USD 5'000 per troy ounce.

Elevated valuations across the Atlantic

Despite the broadly constructive economic outlook, a notable concern remains. The reduction in key interest rates in recent years has driven not only higher equity prices, but also a significant expansion in valuation multiples. Valuations are currently elevated, particularly in the U.S. market. The price-to-earnings (P/E) ratio of the S&P 500 stands at 25.7, well above its historical averages over the past five and ten years (21.6 and 20.5, respectively). Valuations are even more stretched within the technology sector. The Nasdaq 100 currently trades at a P/E ratio of 31.5, exceeding levels observed prior to the 2007–2008 financial crisis.

These elevated valuation levels warrant a cautious approach, as they increase the risk of abrupt price corrections. Accordingly, broad diversification across asset classes, regions, and sectors will be essential in 2026.

INTERNATIONAL STOCK VALUATIONS SINCE DECEMBER 2006



Portfolio strategy and positioning

With a deliberate overweight allocation to gold, the managed portfolios have benefited from the sustained price appreciation that culminated in a new all-time high in December. This trend is supported by continued strategic purchases by the central banks of India and China, rising geopolitical fragmentation, and the apparent erosion of the rules-based global order.

During the fourth quarter, we realized partial profits on our gold holdings following further price gains. Nevertheless, in light of President Trump's repeated attempts to influence the Federal Reserve's interest rate policy, we have maintained a high allocation to gold. During periods of heightened equity market volatility, gold fulfils an important stabilizing role within our strategic asset allocation.

Against the backdrop of robust earnings momentum and expectations of a Federal Reserve easing cycle, we implemented a tactical overweight in equities at the beginning of October. The allocation to U.S. biotechnology equities significantly outperformed the global equity index in the fourth quarter. The sector continues to benefit from elevated takeover activity, characterized by substantial acquisition premiums, as companies increasingly leverage advances in artificial intelligence.

The allocation made in September to an equity fund focused on metal mining companies, positioned to benefit from secular themes such as AI-driven growth, grid expansion, and energy storage, has since generated a return of +57%. We continue to view the surge in electricity demand driven by AI adoption, alongside structurally higher demand for metals such as copper, silver, lithium, and rare earths due to the energy transition, as a compelling long-term investment theme.

We interpret the sharp pullback in inflated growth stock valuations within the technology and artificial intelligence segments during November and December as a technical correction within an intact upward trend. However, given the elevated valuation multiples of large-cap U.S. growth stocks in the communication services and technology sectors, we remain underweight cap-weighted strategies and continue to favor equally weighted U.S. equity investments.

Our passive China allocation contributed negatively to the performance in the fourth quarter. In contrast, the heavily overweighted and attractively valued defensive Swiss dividend stocks outperformed the global equity index, as did the allocations to US biotech and Japanese equities. While German equities (DAX 40) consolidated, European value stocks extended their positive momentum.

Due to the depreciation of the U.S. dollar, portfolios denominated in Swiss francs and euros recorded negative currency-related performance contributions since the beginning of the year. Following a base-building phase over the summer months, U.S. dollar exposure was opportunistically increased. Despite the SNB's zero interest rate policy, Swiss franc exposure remains a core element of the strategic currency allocation in euro-denominated portfolios.

Anticipating rising long-term yields and steeper yield curves in both euros and U.S. dollars, we divested our exposure to long-dated U.S. bonds during the summer following a temporary decline in yields. This was offset by an allocation to local-currency bonds issued by frontier market sovereigns, which have since delivered a gain of +7%. Even after the recent rise in long-end yields, we maintain a short duration of approximately 3.5 years across bond investments. Given unattractive credit spreads, we remain underweight fixed income overall.

In an environment characterized by extremely elevated valuations in certain segments of the U.S. equity market, alternative investments, such as commodities, hedge funds, and catastrophe bonds, are gaining importance due to their low correlation with traditional asset classes.

TACTICAL ASSET ALLOCATION (IN EUR)

	Underweight		Neutral		Overweight
Asset Classes					
Liquidity		◆			
Bonds	◆				
Equities				◆	
Gold					◆
Alternatives			◆		
Equity Regions					
Eurozone		◆			
Switzerland					◆
USA	◆				
Emerging Markets					◆

Conclusion

We continue to prioritize high-conviction diversification within the managed portfolios, with gold allocations, Swiss franc exposure, and alternative investments serving as stabilizers. We reaffirm our underweight position in overextended U.S. growth stocks within the technology and artificial intelligence segments, given the heightened risk of technical price corrections. At the same time, we maintain an overweight in attractively valued defensive Swiss dividend stocks. In light of ongoing geopolitical crises and elevated uncertainty, our strong overweight in gold remains firmly in place.

Special topic: Liquid and semi-liquid alternative investments

Over the past three years, equity valuations have expanded almost continuously, resulting in elevated valuation levels. In this environment, broad portfolio diversification is paramount. A key element of effective diversification is ensuring that portfolio components exhibit low correlation with each other, an attribute offered by alternative investments.

Alternative investments encompass strategies that fall outside traditional asset classes such as equities, bonds, and real estate. Many of these investments are only partially accessible to private investors and require specialized expertise to navigate their inherent complexity, capabilities provided by Principal Asset Management. Our focus lies on liquid and semi-liquid alternatives, including catastrophe bonds, hedge funds, and commodities.

Cat bonds

Catastrophe bonds (cat bonds) are insurance-linked securities that allow issuers, typically insurance companies, to transfer the risk of natural disasters, such as earthquakes, hurricanes, or floods, to capital markets. If a defined catastrophe occurs and exceeds a predetermined threshold (e.g., a category 5 hurricane or an earthquake above category 7.5), the bond loses value. If no such event occurs, investors receive an attractive risk premium.

Hedge funds

Hedge funds employ a wide range of investment strategies, including long/short equity, event-driven, global macro, and managed futures. Liquidity profiles vary depending on strategy, instruments used, and prevailing market conditions. Absolute return strategies, which aim to generate positive returns across market environments, generally offer more flexible liquidity terms.

Unlike traditional funds, hedge funds can take short positions, enabling them to profit from declining asset prices. As such, hedge funds can generate returns in both rising and falling markets, with the objective of delivering attractive risk-adjusted performance. In our selection process, we prioritize strategies with minimal correlation to equity markets, deliberately avoiding long/short equity exposures.

Commodities

Commodity investments provide exposure to the price dynamics of natural resources. Our focus includes energy commodities (crude oil, natural gas, coal) as well as industrial and precious metals (aluminum, copper, gold, silver). While many commodities are cyclical, they typically experience smaller drawdowns than equities during market corrections and crises. Moreover, as tangible assets, commodities offer a degree of protection against inflation.

Conclusion

Alternative investments offer a compelling means of diversifying portfolio risk while providing attractive return potential. Although access to these strategies is often limited for private investors and requires specialized expertise, their benefits are substantial. In view of the advantages outlined above, carefully selected alternative investments form an integral part of our client portfolios.

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