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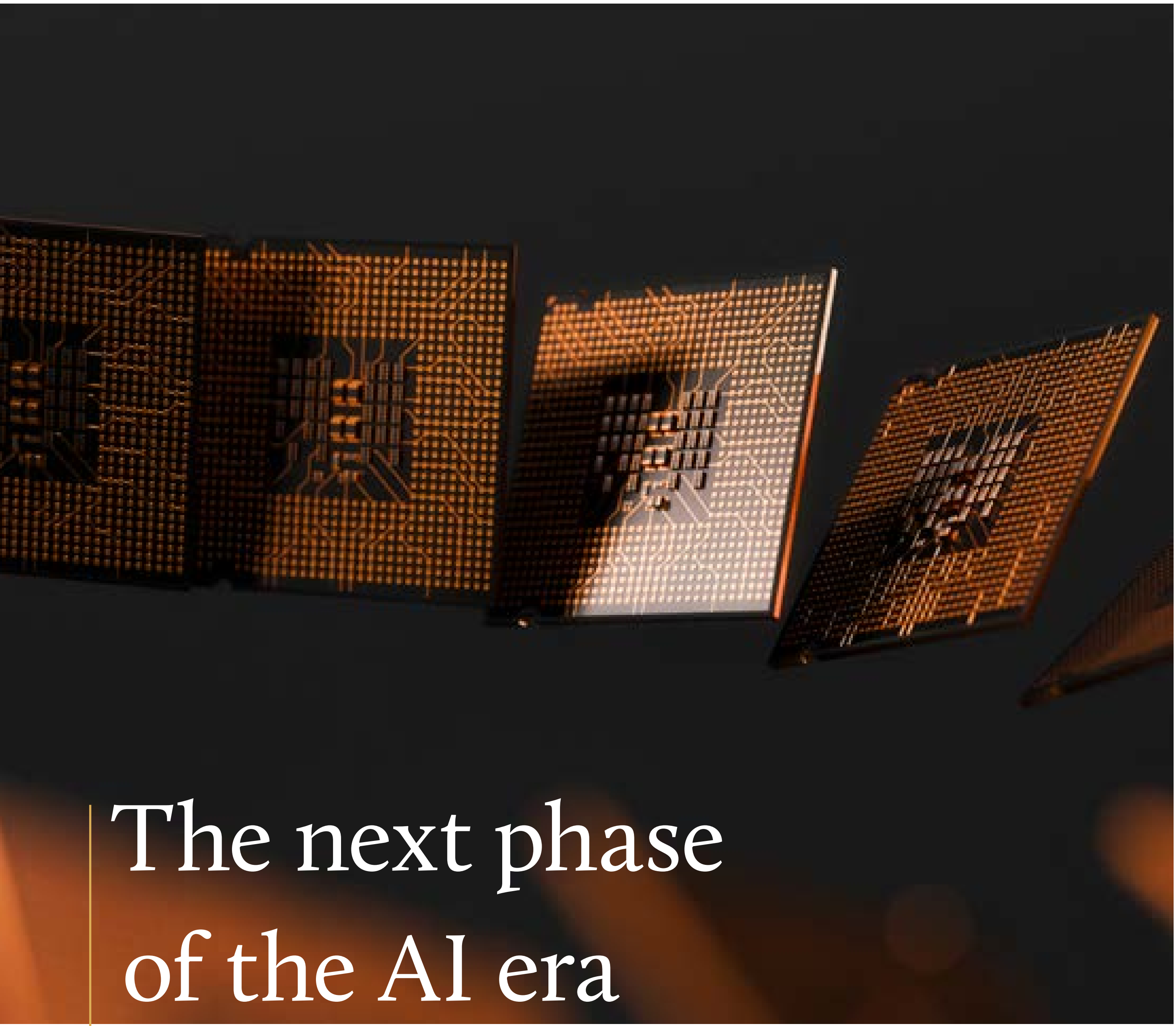

The next phase of the AI era

Three possible scenarios for the year ahead

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Foreword

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Despite a difficult geopolitical backdrop, an ongoing mix of economic resilience, falling interest rates and AI momentum delivered solid market gains in 2025. The tariffs which were the focus of last February's scenarios materialised, but on a scale (so far) which did not interrupt business – in line with our central scenario then. That said, for euro and franc-based investors, a weak dollar muted returns. Meanwhile, our decision to take profits on an overweight stock position in late 2024 proved premature (though at least we were not underweight).

The new year has started noisily, and the dollar has weakened further. However, the impact of currency moves of course varies with portfolio denomination, and we focus for our scenarios instead on a more general – but still hugely topical – theme, namely the evolving impact of AI. As usual, our current Mosaique view is the central one, with variants which might be seen as "better" and "worse" cases for portfolios.

Our central view is little changed, at a broadly neutral asset allocation (the exception being gold, which we raised to overweight in the summer). We still think inflation risk will limit the room for interest rates to fall further, and AI-led stock market valuations are even higher now. However, within our equity holdings we recently moved underweight the US and overweight emerging Asia. We also cancelled our long-standing sector overweight in technology.

The "worse" case here reflects the possibility of the AI boom turning into a 2000, TMT-style bust. This could trigger a pronounced market setback, and a switch to safe haven assets. Interest rates would likely fall by more, which might affect the regional and sectoral winners. Defensives might lead initially, but – as after 2000 – the eventual winners might be more cyclical.

The "better" case here is one in which wider profitability – that is, outside the AI-related sectors themselves – receives a material boost from the successful adoption of the new technology. This might sustain even higher average stock valuations, but perhaps under new sectoral and regional leadership. Because such a productivity-led boost to growth would be non-inflationary, some safe havens might actually do well in this scenario too.

What if?
Three market scenarios (i)

AI's failure or success is the determinant of this scenario exercise. Our central Mosaique view is compared with a 2000-style failure ("worse") and a productivity-boosting success ("better")

Scenario	**Dotcom-style bust**	**Mosaique views R&Co central scenario**	**AI-led disinflationary boom**
Position	Worse case	Base case	Better case
Definition	Excessive valuations and a reappraisal of AI business model leads to a big stock market reversal. Earnings collapse, defaults rise and a recession ensues	Growth continues - partly supported by ongoing AI-related spending – but also accommodative monetary and fiscal policy. But stubborn inflation prompts an eventual rethink on interest rates	Rapid AI innovation and adoption lead to increased productivity and reduced costs, leading to sustained economic growth, while simultaneously damping inflation and keeping interest rates low
Macro implications			
GDP	Expectations for GDP growth fall markedly as AI capex falls, layoffs rise, and output goes into reverse	GDP grows at a healthy pace, with unemployment staying low. Profitability remains historically elevated	Global growth surges to firmly above-trend levels and corporate profits rise strongly driven by topline growth and further margin expansion
Inflation	Consumer prices slow sharply as aggregate demand weakens - deflation talk revives	Sticks above target in in 2-4% range, and begins to move towards the top half of that range	Headline inflation falls below target, kept at bay by rising productivity and supply-led growth
Monetary policy	As recession approaches, central banks cut interest rates sharply, but the economy takes time to respond	Central banks initially continue to cut, but by less than markets expect, and expectations of a rebound in rates build by year-end	Real policy rates and long-dated yields stay close to current levels
Investment implications[1]			
Equities	★☆☆	★★☆	★★★
Fixed income	★★★	★★☆	★★☆
Cash	★★☆	★★☆	★★☆
Gold	★★☆	★★☆	★☆☆
Investment positioning			
Equity regions to favour	▪ Safe havens and defensive markets (Switzerland and UK, but in this context maybe not the US) may outperform ▪ Avoid high beta/cyclical markets (Europe and Asia) and overvalued markets (US)	▪ Cyclical exposure leads the way. Europe and emerging Asia may return to favour as global growth accelerates. ▪ Richly priced US stocks may struggle to keep pace. Defensive markets also likely to underperform	▪ Initially favour those indices with a significant 'growth' tilt, including the US and Asia. Longer-term, the benefits will be become more diffuse as reflation gives way to a broader cyclical revival
Equity sectors to favour	▪ Tilt towards staples, healthcare and utilities. ▪ Avoid technology, and cyclical and momentum segments	▪ Continue to favour cyclical segments - materials, industrial and financials Tech/growth may do well too ▪ Avoid rate sensitive sectors and defensives	▪ IT (specially semis) and discretionary may outperform, but wider productivity gains will benefit cyclical 'growth' sectors

[1] Investment implications stars are shown on a relative basis of one asset class vs the overall scenario result.

What if?
Three market scenarios (ii)

The regional and sectoral rankings below reflect a mix of judgement and quantitative analysis, with most weight given to the former

Scenario	Dotcom-style bust	Mosaique views R&Co central scenario	AI-led disinflationary boom
Equity regions			
North America	★☆☆	★★☆	★★★
Euroland	★☆☆	★★☆	★★★
Switzerland	★★★	★☆☆	★☆☆
UK	★★★	★☆☆	★★☆
Japan	★★☆	★★☆	★★☆
EM Asia	★☆☆	★★★	★★★
Equity sectors			
Communications	★☆☆	★★☆	★★★
Consumer discretionary	★☆☆	★★☆	★★★
Consumer staples	★★★	★☆☆	★☆☆
Energy	★☆☆	★★☆	★☆☆
Financials	★☆☆	★★★	★★☆
Health care	★★★	★★☆	★★☆
Industrials	★☆☆	★★☆	★★☆
Information technology	★☆☆	★★☆	★★★
Materials	★☆☆	★★☆	★★☆
Real estate	★★☆	★☆☆	★☆☆
Utilities	★★★	★★☆	★★☆

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