

Global Markets Overview

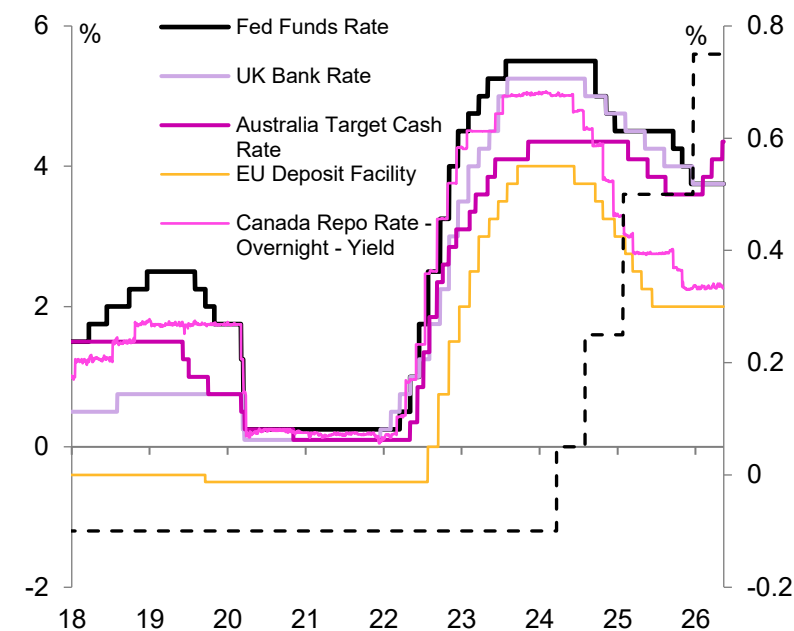
Asset Research Team

May 2026

How are central banks responding to the likelihood of higher inflation in 2026 from the U.S.-Iran conflict?

- Across the major advanced economies, the overall central bank stance can be characterized best as 'keeping policy rates unchanged but monitoring inflation.' In the last month, we observed the following:
- United States:** The Federal Reserve voted to keep its policy rate range unchanged, but with an 8–4 vote split. This signalled reduced confidence in the likelihood of any interest rate cuts in the near-term and reinforces a higher-for-longer policy outlook – which we agree with.
- Canada:** The Governing Council of the Bank of Canada decided to maintain its policy rate at 2.25%. They are “closely monitoring the impact of the conflict in the Middle East and how the economy is responding to U.S. tariffs and trade policy uncertainty.”
- Euro area:** The European Central Bank kept its policy rate on hold. It emphasised upside risks to inflation from energy prices and a data-dependent stance, leaving the door open to future tightening if inflation pressures persist.
- United Kingdom:** The Bank of England also maintained its policy rate (8–1 vote), balancing inflation risks from the energy shock against growth concerns. Policy communication pointed to a cautious and steady approach.
- Japan:** The Bank of Japan maintained its policy rate (6–3 vote), with a divided board highlighting concern over rising inflation and suggesting the potential for future tightening.
- Australia:** The Reserve Bank of Australia raised its policy rate by 0.25% to 4.35% in a decisive 8-1 vote, marking the third consecutive hike of 2026. Staff forecasts project headline CPI to peak at 4.8% in Q2, with core inflation remaining above target through to end-2027.

Most central banks in advanced economies are in 'wait and see' mode



Sources: FactSet, WTW

Government bonds

At current yield levels we believe select bond markets offer value in the medium-term

What happened over the past month:

Despite intra-month volatility, aggregate yield moves have been relatively flat across the major developed bond markets since the end of March (as of 06 May 2026). Japan was the main outlier, with yields rising by around 15bps. Elsewhere, movements were modest, with only small increases in yields in Canada, the Euro area, US, UK, and Switzerland. Australian rates fell slightly.

Factors influencing market trends:

Earlier in the year, bond yields declined notably, with a backdrop of softer economic data (e.g., a weakening US labour market) and lower inflation (especially in Europe), which increased expectations for central-bank easing. UK bonds also benefited from a record budget surplus. However, conflict in the Middle East has reversed these moves recently, with yields rising. Oil and gas prices have jumped notably on the back of the US-Iran military action and disruption to the Strait of Hormuz. If sustained, these pressures raise the risk of higher inflation (March headline CPI prints have already increased), particularly for

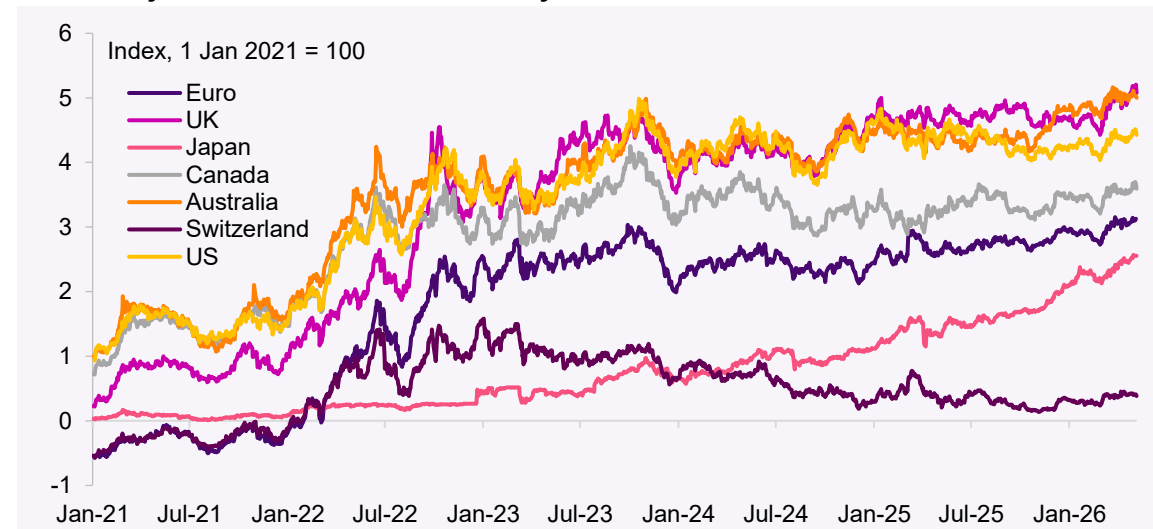
energy-importing economies, where bond yields have risen the most.

Looking ahead:

While we are monitoring developments closely, our base case is for the energy price spike to be temporary. In the US, a combination of easier fiscal policy and strong business capex suggests GDP growth will still be strong in 2026/27, putting upward pressure on core inflation. Consequently, in our view, the recent rise in US bond yields was warranted. We continue to see select opportunities in certain markets, such as UK gilts, where the expected path for the policy rate and the bond risk premium – the excess yield for holding longer-dated bonds – appear high relative to fundamentals.

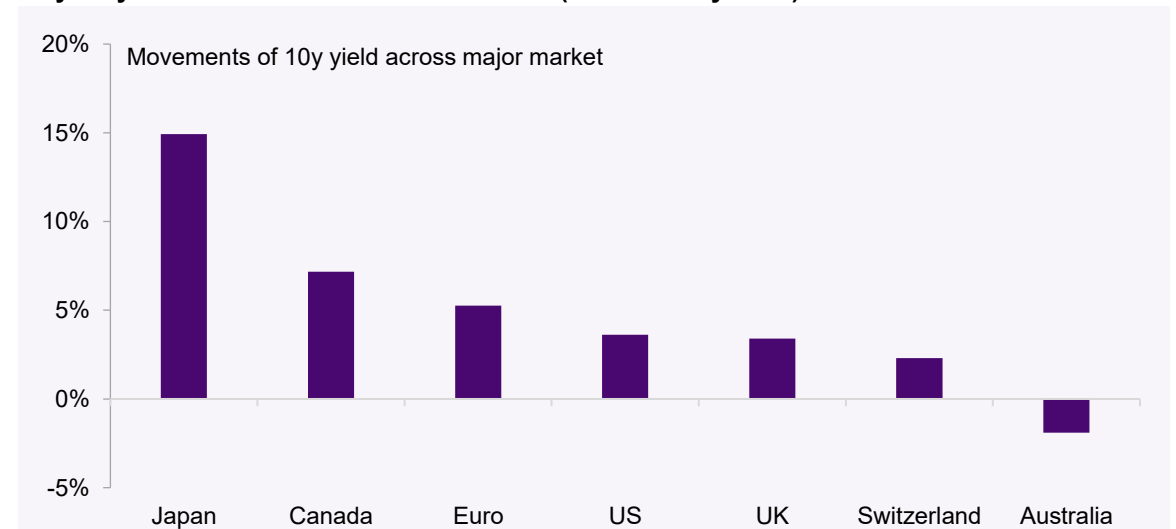
Overall, it remains appropriate to maintain bond exposure for liability hedges and downside protection. However, for some investors, the macro backdrop may suit moderating duration in downside-protection portfolios. Dynamic investors may also find opportunities to overweight select bond markets on a relative value basis. We encourage investors to discuss the portfolio implications with their advisers.

Global 10-year benchmark nominal bond yields



Sources: FactSet, WTW

10-year yield moves since end-March 2026 (as of 06 May 2026)



Sources: FactSet, WTW

Credit

Over five years we expect investment grade credit to outperform government bonds moderately

What happened over the past month:

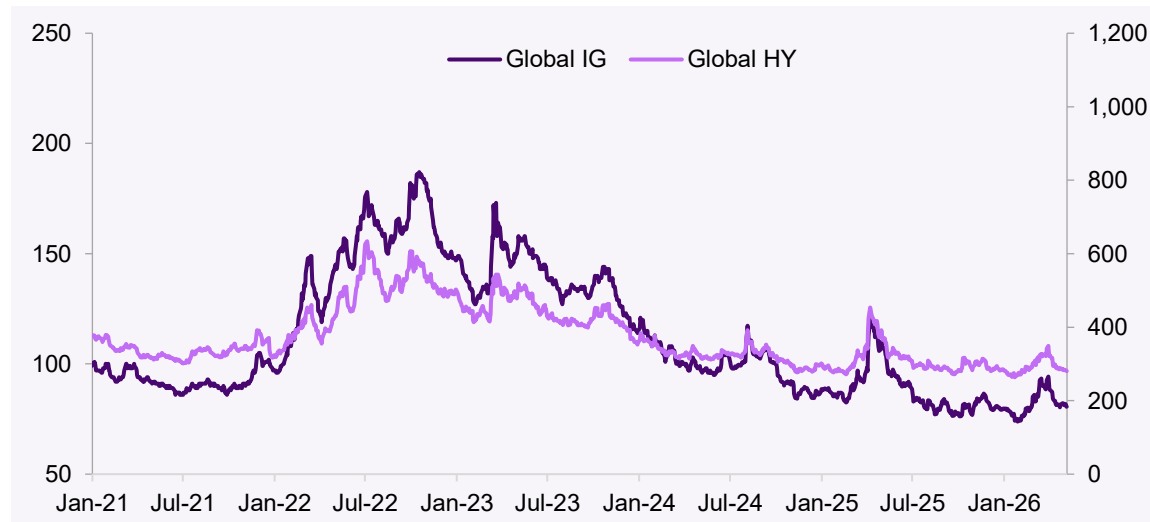
Credit spreads tightened meaningfully over the month, with the US-Iran ceasefire in early April supporting risk sentiment. High yield corporate credit outperformed, with global HY spreads tightening by around 56bps as of May 6th, with similar levels of tightening in both the US (-55bps) and Europe (-53bps). Investment grade spreads also fell, though to a lesser extent, with global IG tightening by around 12bps. This was driven primarily by Europe (-16bps), with US (-11bps) and UK (-8bps) spreads also declining notably.

Current spreads continue to look through the geopolitical shock and spreads remain below their 15-year historical ranges across key IG and HY markets.

What has influenced recent market dynamics?

IG credit spreads, measured over government bond yields (OAS), are still low relative to history. In contrast, spreads which are measured relative to swap rates (ASW) are not as compressed versus history.

Global spreads relative to government bonds



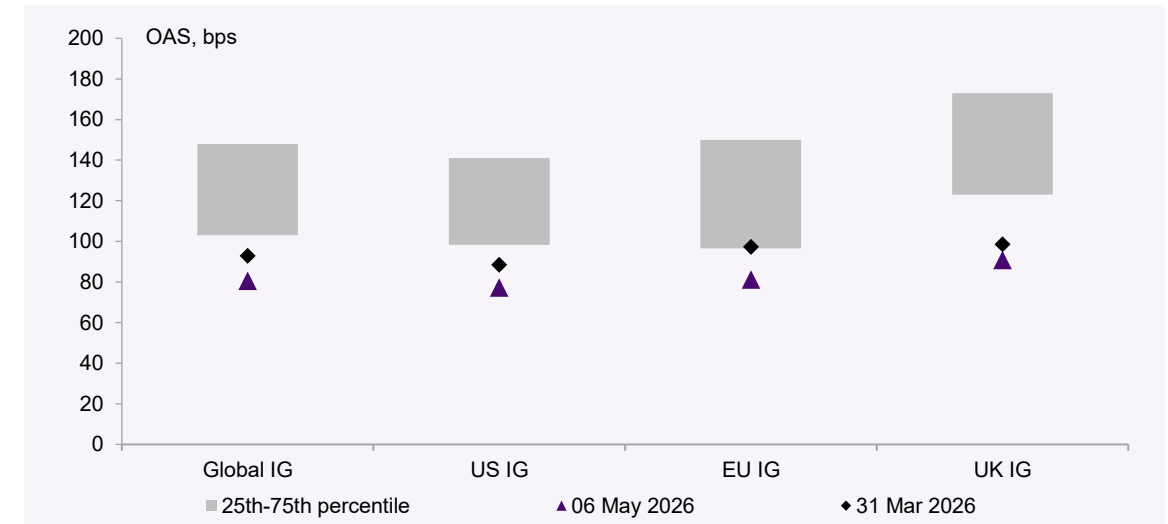
Sources: FactSet, WTW

We think this is an important consideration when evaluating compensation for credit risk, particularly in US and UK IG markets, where divergence between OAS and ASW based spreads is more pronounced. This means: (1) corporate credit is not as expensive as it might appear; and (2) high government deficits and sales of government bonds by central banks have increased the risk premium and yield on government bonds, compared with swap rates, making bonds more attractive. That said, IG spreads on both a government bond and a swap basis are still pricing-in expectations of a low default and downgrade environment.

Looking ahead:

Over a three-to-five-year horizon, we expect global investment grade corporate credit to provide reasonable returns above government bonds. Similarly, we expect global high yield credit to outperform government bonds and investment grade credit over the medium-term.

Investment grade credit spreads relative to government bonds, by country



Sources: FactSet, WTW

Equities

Overall, we are positive on equities on a one-year horizon

What happened over the past month:

Global equities rose significantly over the month, with gains broad-based but uneven across regions. Emerging markets rose the most, with MSCI EM increasing +12.2%, while developed markets also delivered a high return (MSCI World: +11.4%). The US was the standout among the major markets, with a +13.8% increase. Returns across other countries were: Eurozone (+7.3%), Canada (+7.0%), Japan (+6.1%), Switzerland (+5.1%), Australia (+2.1%), and the UK (+2.7%). Performance was supported by strong earnings results and the continuation of the AI technology theme.

Broad market trends:

First, mega-cap US technology stocks continue to deliver strong earnings growth, supported by and supporting the AI boom. This profit growth continues to underpin a large, concentrated presence in equity indices, reflecting ongoing US leadership in innovation.

Second, tariffs and trade policy uncertainty still present some challenges to wider business investment and near-term earnings momentum in specific countries. However, these factors highlight the benefits of active

management and careful risk assessment, rather than a risk of a major drawdown in equity prices, in our view.

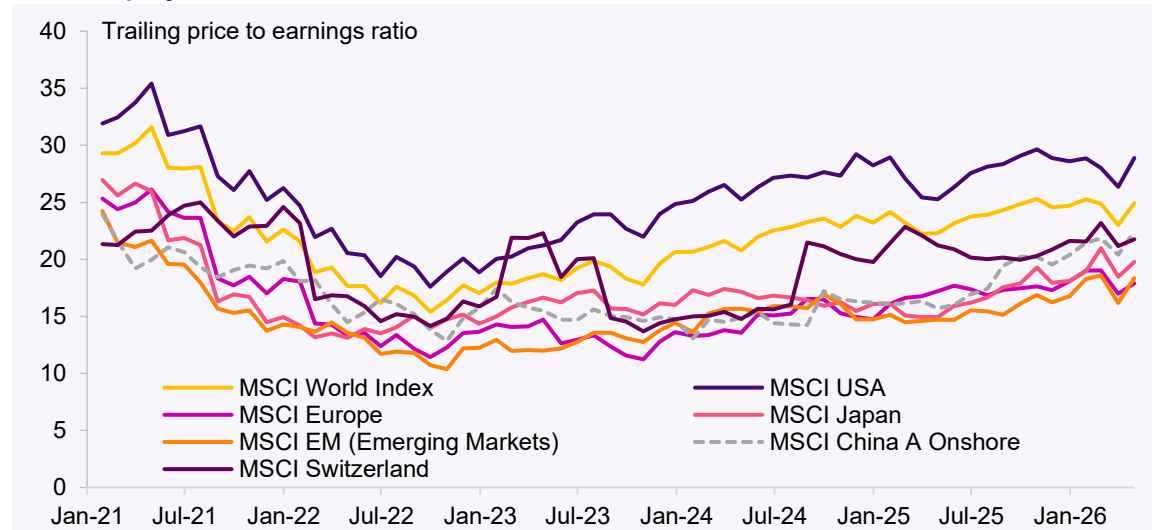
Third, the US-Iran conflict has been a clear headwind to global equity returns in the last two months, with country dispersion increasing. Nevertheless, US equities have repeatedly hit new index highs, with investors focusing more on the strength of earnings and the longer-term potential impacts of innovation-led growth – which we expect to both continue and be very significant.

Fourth, we expect monetary and fiscal policy to remain supportive in the near term, helping to underpin growth conditions and reinforce investor confidence.

Looking ahead:

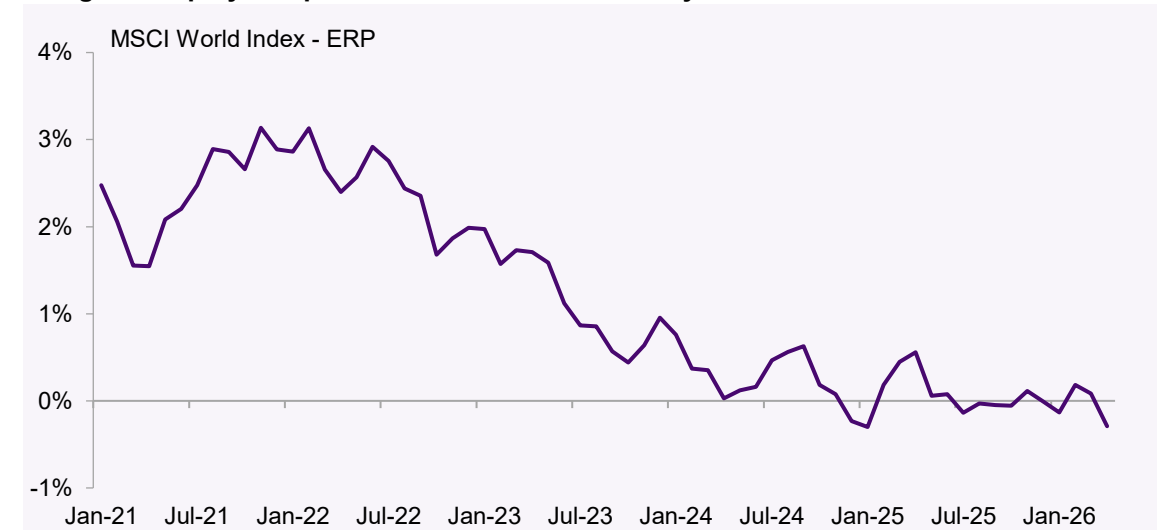
- Over the next 12 months equities should be supported by strong earnings (driven in part by significant AI capex) compounded by policy support on both the fiscal and monetary side.
- We hold a neutral view on equities over longer horizons.

Global equity valuations



Sources: FactSet, WTW

The global equity risk premium remains low currently



Sources: FactSet, WTW

FX

We hold a positive view on most developed currencies relative to the US dollar over the long term

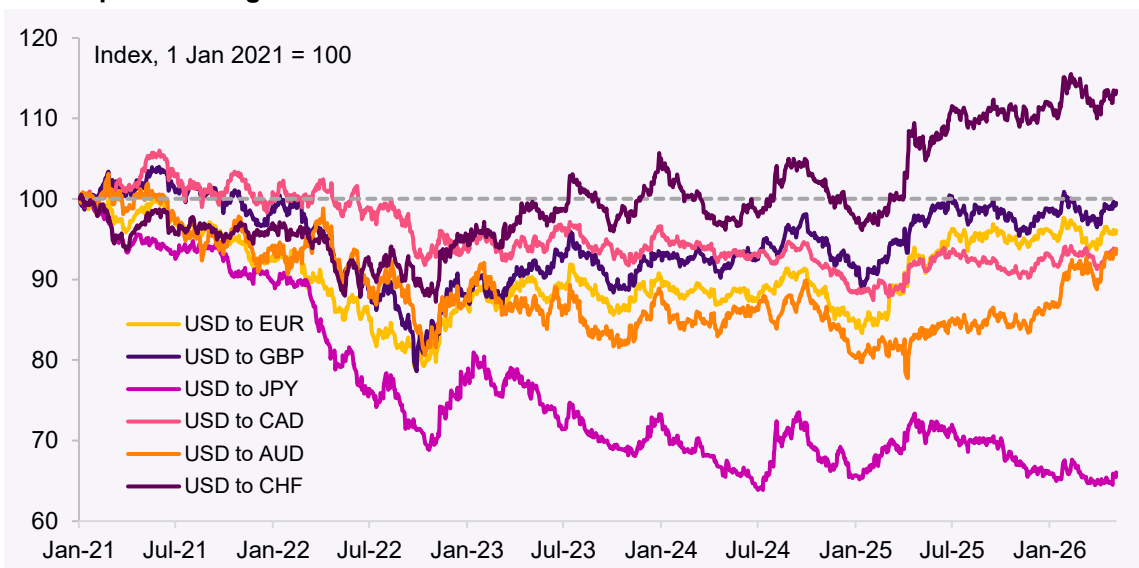
What happened over the past month:

The major currencies have appreciated against the US dollar since the start of April. The Australian dollar saw the largest move, strengthening by around +5.7%, followed by sterling (+3.2%) and the Canadian dollar (+2.5%). The euro (+2.0%) and yen (+1.8%) also appreciated, while the renminbi saw a more modest gain of approximately +1.4%.

Broad market trends:

Outside of recent geopolitical developments, periods of heightened macro uncertainty and elevated equity volatility over the past year, which would typically favour the US dollar, have generally weighed on the currency. Investors have diversified their currency exposure given the US-centric nature of many policy risks. This move has been reinforced by a decline in US interest rate differentials, with US 2-year treasury yields falling materially relative to Japan, Australia and Europe since late 2024.

Developed exchange rates versus the US dollar



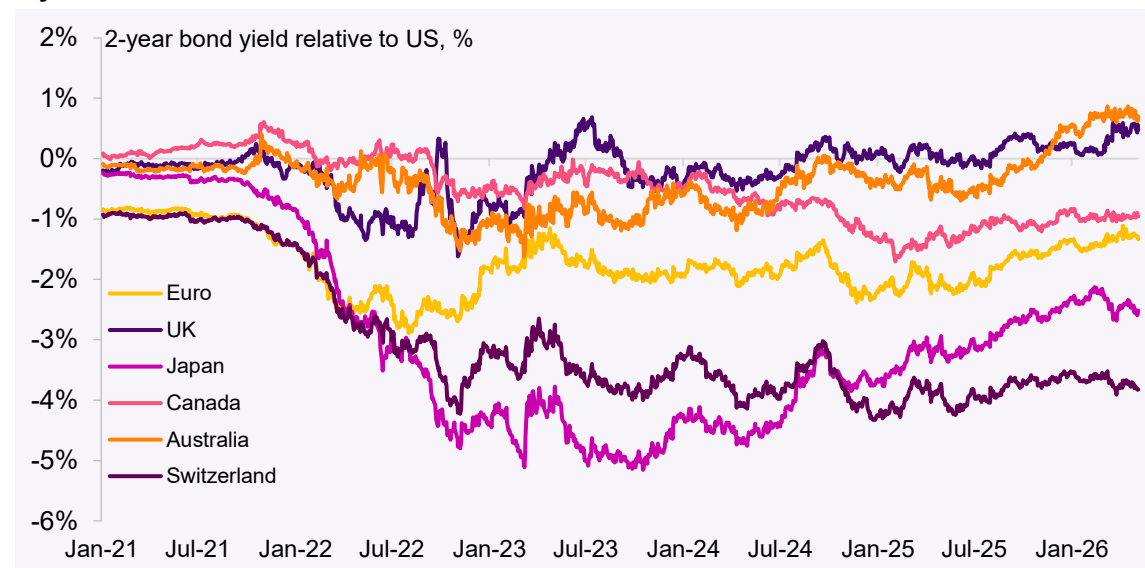
Sources: FactSet, WTW

Longer term, the US dollar has strengthened significantly versus most currencies, supported by higher interest rates than other countries and economic and corporate earnings growth consistently above other economies.

Looking ahead:

Following a sustained period of appreciation, the US dollar has become more expensive against most other major currencies on our medium-term fair value metrics. This suggests downward pressure over a 3- to 5-year horizon and a positive outlook for most developed market currencies against the dollar. Shorter-term, we hold a neutral dollar view against most currencies, except for a more positive view on the euro and the Japanese yen. Both are net trade surplus currencies with significant holdings of dollar-denominated assets that stand to benefit from shifts in global capital flows.

2-year interest rate differentials



Sources: FactSet, WTW

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