



Q4 2025

Investment Outlook

End of the Cycle,
or Just the Beginning?



Key Takeaways

Macro Environment: A Market Caught Between the Last Mile and First Sparks

As we approach the end of 2025, we assess whether the economic cycle is ending or its engine is just revving up, and share potential implications for asset allocators.

Fixed Income Markets: Finding Opportunities in the Macro Fog

Despite the macro ambiguity, we believe there are still attractive sources of carry across fixed income asset classes, but selectivity and caution are critical.

Equity Markets: AI Offers a Rorschach Test for Investors

The AI theme's impact on equity markets is transformative yet uncertain and open for interpretation, requiring investors balance optimism with caution.

Equity Solutions: Our MSCI Rebalance Predictions

Our prediction accuracy score came in high for the third quarter in an environment with fewer index changes than the prior quarter.

Private Credit: Financing the AI Future

As AI investment accelerates, we believe private credit will play a crucial role in filling the projected AI financing gap. This is creating opportunities for investors, even as the outlook for AI remains uncertain.

Macro Environment

A Market Caught Between the Last Mile and First Sparks

As we approach the end of 2025, we assess whether the economic cycle is ending or its engine is just revving up, and share potential implications for asset allocators.



Jason Shoup
Chief Investment Officer,
Co-head of Global Fixed Income



Jason Becker
Head of US Credit Strategy

Over the past quarter, the macro environment has been marked by contrasts. Headline growth has remained resilient, but the labor market has clearly softened. Inflation progress has been uneven, and monetary policy has shifted incrementally more accommodative after a prolonged pause. Despite these crosscurrents, risk assets continue to reflect a base case of slow but steady growth. The underlying theme is that both the economy and markets are navigating a narrow path, where even small shifts in data or policy can have an outsized impact on sentiment. For allocators, the key question remains: Are we approaching the end of the current cycle, or are we on the verge of a new phase, one potentially driven by productivity gains that could alter the pace, if not the direction, of the cycle?

What the macro backdrop is telling us

Let's start with the labor market, which offers one lens for assessing where we are in the cycle. This summer, hiring softened and there were unusually large revisions to previous data that changed the prevailing market narrative. The US Bureau of Labor Statistics flagged significant preliminary benchmark adjustments to payrolls through March 2025, pointing to a cooling trend that began before recent trade frictions. These revisions, based on more comprehensive administrative data, serve as a reminder that initial labor market readings can be incomplete. The broader takeaway is that the labor market expansion may already be behind us, as further evidenced by the ADP private payrolls report for September, which showed a contraction in total jobs.

Policy is responding. In mid-September, the Federal Reserve delivered a 25 basis point (bps) rate cut and signaled a willingness to ease further if the labor market conditions deteriorate. Markets now anticipate two additional cuts by year-end, with ongoing debate about the pace of further easing into 2026. There is an active debate among investors. Are these moves best understood as mid-cycle adjustments to support continued expansion, or as late-cycle insurance cuts designed to cushion a potential slowdown? The Fed's communications have emphasized a cautious, risk-management approach, providing enough support to prevent a rise in unemployment, but not so much as to reignite inflation. This stance, along with projections for further reductions in 2025, is shaping expectations across asset classes.

Inflation remains a "two steps forward, one step back" story. The third quarter featured softer prints that encouraged the Fed, but also lingering stickiness and new uncertainties from tariffs. That mixture complicates the forecast as tariffs, which have proven a versatile tool for this administration and are unlikely to fade, may add upward inflation pressure into year-end.

Growth has been steadier than the sentiment around it. Some argue that part of the apparent disconnect between slower hiring and decent output lies in productivity. Here, the emerging artificial intelligence (AI) story deserves attention but not exaggeration. Major institutions project that AI could lift productivity and gross domestic product (GDP) over the next several years, but the near-term macro evidence is still tentative and uneven. If these gains begin to diffuse, they could reconcile softer payroll growth with acceptable overall activity. Employment could even contract while output per worker and margins offset a smaller labor force.

Markets have certainly treated AI as both a growth and earnings story, but the real economic test will be diffusion. Do cost savings and capability gains show up outside the tech complex, and on what timeline? If diffusion broadens into logistics, services and public-sector workflows, the "engine" case gains traction, and the key question will be whether consumer spending can remain resilient in an economy that is increasingly split between different groups of spenders. Should productivity gains fail to reach additional sectors, the late-cycle fears may prove correct.

Risk assets have thus far taken all of this in stride. Credit spreads, equities and even duration at various points behaved as if the "soft patch invites gentle easing" narrative has more signal than noise. Part of that resilience can be traced to the plumbing, or policy transmission from the Fed to markets, mentioned above; part is the absence (so far) of an acceleration in layoffs; and part is a belief that policy will shade supportive if labor weakens further. Still, the ledge is narrow. A meaningfully negative real-time payroll print would carry different sentiment weight than another revision. Conversely, a premature reacceleration in inflation would quickly challenge the easing path that markets have penciled in.

The implications for asset allocators

What might this mean for asset allocators over the next one to three quarters? We see four key implications.

First, treat the incoming jobs data with appropriate humility. Revisions are doing more of the narrative work than usual. That means reaction functions for the Fed and for markets may key off qualitative labor dynamics (hiring freezes, hours, claims) as much as headline nonfarm payrolls. In a revision-heavy regime, persistence matters more than any single print.

Second, remember that policy is now operating through three channels: the policy rate, the balance sheet and the rhetorical stance around inflation risks. The rate path may be gradual, but the balance-sheet slope has already changed meaningfully, and communications will keep toggling between labor vigilance and inflation vigilance. For cross-asset positioning and risk budgeting, the mix of the rate path, fiscal stance and corporate investment plans may matter more than market microstructure in the next few quarters.

Third, recognize that supply (public and private) could be the sleeper variable. The AI build-out has driven hyperscaler capex up several-fold since 2022, straining free cash flow and increasingly tapping external financing. Layer in ongoing Treasury issuance tied to persistent fiscal deficits, and the backdrop is one where fixed-income supply may be a sturdier headwind than in the immediate post-pandemic period. For credit allocators, that makes the technicals more path-dependent. Windows of strong demand can still compress spreads, but the medium-term impulse is less clear.

Finally, keep an eye on the interaction between tariffs and inflation psychology. Tariffs are policy choices that can be modified, extended or repurposed, sometimes quickly. Their macro footprint is uneven (and often smaller than the headlines), but their market footprint via expectations, supply chains and earnings guidance can be disproportionate in short bursts. The key risk is not an inflation reacceleration so much as a prolonged floor on goods disinflation that slows the last mile of the Fed's journey.

In 1995 the Fed eased into a mid-cycle wobble and productivity picked up, extending the expansion. In 2001 rate cuts met an investment overhang that had to clear before growth could resume. Today's environment rhymes with both. Modest productivity gains and better supply chains argue for an elongated cycle, yet the least discussed constraint is financing the build-out. Persistent fiscal issuance and AI-driven capex can tighten financial conditions even as policy rates drift lower. If the engine starts, we may see subdued hiring alongside rising productivity and better unit labor costs, unusual for an early phase but consistent with a period of capital deepening. Whether the cycle is winding down or the engine is just beginning to turn over, it's the interaction of productivity, investment and policy that will determine how far and how fast we move from here.

Figure 1: Our three-month macro scenario probability views

Base case: 50%

Consensus growth expectations remain around 1.5-2.0% for 2026 4Q/4Q, as AI productivity gains and the data center spending boom dominate headlines. Payroll gains continue to hover around the recent, lower range of 20-60k/month. However, upward pressure on the unemployment rate is relatively limited as reduced labor supply partially offsets slack from weaker labor demand, preventing further increases (above 4.3%). The housing market continues to slow as declining home prices, weaker residential investment, and an unattractive supply backdrop weigh on sentiment. The policy narrative increasingly pivots away from tariffs to the more favorable regulatory environment. Inflation remains sticky at ~3.0%, but the Fed cuts 2-3 times by year-end 2025, while market pricing for the top end of the Fed Funds range year-end 2026 remains ~3.0%.

Bear case: 24%

Soft data deteriorate while hard data also notably weaken. The impact of tariffs on inflation becomes more pronounced as companies increase pass-through of higher input costs to end consumers. Inflation expectations move higher as monthly CPI prints advance at a >3.5% annualized pace. Payroll growth stalls, and the unemployment rate inches higher to 4.5%, while housing market weakness deepens. Concerns around Fed independence intensify as President Trump continues to push for my influence over the Fed. 2026 4Q/4Q growth forecasts fall below 1.0%, as expected productivity gains are unable to keep up with a shrinking workforce. The Fed cuts 1-2 times by year-end 2025, and market pricing for the top end of the Fed Funds range at year-end 2026 increases from 3.0% to 3.5%, as investors expect the Fed to be more restrained considering escalating price pressures.

Bull case: 21.7%

The consensus moves to pricing in faster growth (2.0+%), as the tailwind from the AI boom looks poised to exceed even bullish expectations. Realized inflation moderates (<3.0% annualized pace), fueling expectations that the Fed will retain latitude to ease monetary policy despite stronger economic momentum. Payroll growth reaccelerates (60k+/month), as companies increase hiring amid a less uncertain backdrop. Tariffs become an afterthought as deregulation and the OBBBA stimulus package (which stands to incentivize capex and R&D) serve as focal points. The Fed cuts 2-4 times by year-end 2025, and market pricing for the top end of the Fed Funds range at year-end 2026 remains ~3.0%.

Recession: 4.3%

Negotiations with multiple trading partners fall apart and/or agreements are breached, leading to a resurgence in trade tensions and a spike in volatility and/or the AI “boom” falters. The deterioration in the labor market accelerates as the layoff rate moves appreciably higher, payroll prints turn negative, and the unemployment rate approaches the 5.0% threshold. Fiscal concerns intensify with domestic and foreign investors increasingly questioning the sustainability of government finances and US exceptionalism. Geopolitical tensions ratchet higher, exerting upside pressure on commodity prices. Inflation expectations ratchet higher as monthly CPI prints advance at a >4.0% annualized pace. The market prices in 200+ bps of rate cuts over the next 12 months, and the consensus shifts from pricing in a soft-landing to a deeper recession (-1.5% contraction or worse).

Source: L&G – Asset Management, America. Views as of October 14, 2025.



Fixed Income Markets

Finding Opportunities in the Macro Fog

Despite the macro ambiguity, we believe there are still pockets of attractive carry across fixed income, but selectivity and caution are critical.



Anthony Woodside, CFA, FRM
Head of Multi-Sector Fixed Income & Investment Strategy

Finding one's bearings amid limited visibility is hardly a straightforward task. For much of the year market participants have been forced to contend with elevated uncertainty, continuously torn between downside risks to growth and upside risks to inflation. This handicap has intensified of late, as underwhelming survey response rates and significant downward revisions to payrolls have compromised the signal of economic data releases. Yet perhaps the only thing worse than untrustworthy data is an indefinite data vacuum, which is exactly where we find ourselves at the start of the fourth quarter thanks to the government shutdown. Despite less-than-ideal conditions, we believe relative-value focused investors can add value in fixed income by exploiting select carry opportunities across asset classes and persistent volatility related to the macro-outlook narrative.

Third quarter in review

Fixed income valuations suggest that investors have taken a sanguine interpretation of the ongoing macro ambiguity. Despite concerns surrounding the trajectory of inflation, risk-free rates moved lower in the third quarter, as the market grew more confident that policymakers will prioritize risks to employment at this point of the cycle. Consequently, the yield curve bull steepened with 2-year rates falling roughly 11 bps, while 10- and 30-year yields declined by about 8 and 4 bps, respectively.

Moreover, corporate credit continued its run of strong performance. Total returns for investment grade (IG) were once again positive, with market and long credit indices finishing up about 2.6% and 3.9%, respectively. Excess returns were also solid as spreads continued to defy gravity, compressing by roughly 11 and 13 bps respectively. Finally,

US corporate high yield posted total returns of 2.5%, with excess returns aided by over 20 bps of spread tightening.

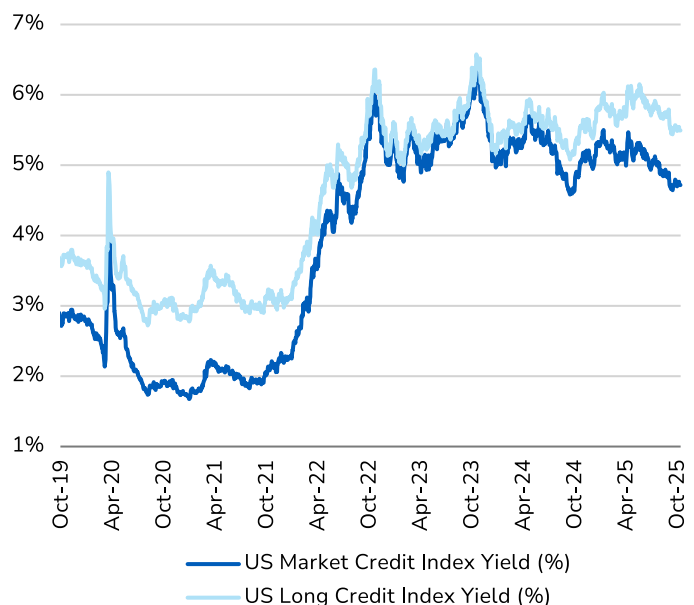
A more nuanced backdrop for corporate credit

For many, the dogmatic resilience of risk assets amid growing signs of vulnerability can be difficult to reconcile. The precipitous decline in payroll growth has set off alarm bells. Moreover, lower income consumers remain under duress, and recent bankruptcies of Tricolor and First Brands have done little to quell concerns. Meanwhile, the housing market, a bedrock of the economy, appears to be faltering with home prices starting to come under pressure. While we certainly acknowledge rising macro risks, there are asset class-specific tailwinds underpinning current valuations.

In IG credit, corporate margins remain healthy, as management teams have proven adept at preserving profitability amid a shifting policy backdrop. Encouragingly, a significant share of US-listed companies continues to upgrade earnings guidance, while analysts have similarly revised S&P 500 earnings estimates higher for the next 12 months. Corporate fundamentals also appear firm in the higher-quality segments of US high-yield, with net leverage ratios roughly on par with the lowest-rated cohorts in IG credit.

However, there is a risk that we are nearing an inflection point in the much-discussed technical backdrop. As labor market data have deteriorated and the Fed has shifted to a more dovish stance, all-in yields have started to decline, particularly for full market credit (Figure 2). Should downward pressure on yields continue, we could see some erosion in the insatiable demand for credit over the last few years. Conversely, there has also been a resurgence in strategic mergers and acquisitions (M&A) activity, with large-scale M&A (deals valued at \$5 billion or more at announcement) picking up in recent months. In tandem, these

Figure 2: Will all-in yields continue to decline, weakening demand technicals?



Source: L&G – Asset Management, America, Bloomberg. Data as of October 10, 2025.

trends threaten to weaken both the supply and demand sides of the equation for credit, likely limiting the potential for further spread compression in the coming months.

AI theme and the unique opportunity in securitized credit

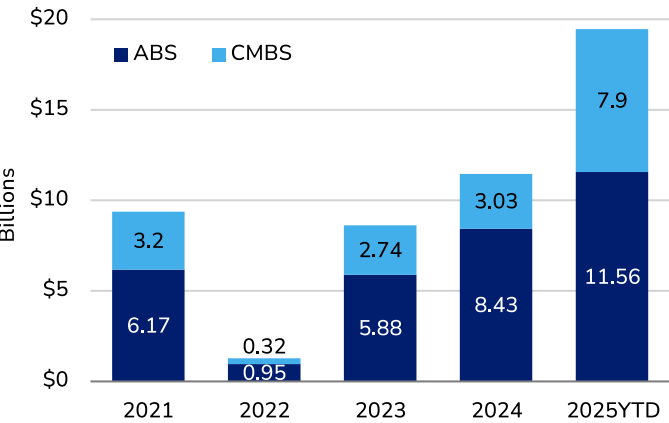
As the Macro Environment section highlights, the AI theme has played a central role in the debate around the medium-term trajectory of the US economy. While it may be premature to predict how technological advances will translate into real economic activity over the medium term, the impact of the capex build-out is already being felt in fixed income markets.

Back in July, Morgan Stanley published a report that forecasted nearly \$3 trillion in global data center spend through 2028, with the expectation of \$1.4 trillion being funded by the cash flows and capex of hyperscalers (Meta, Amazon, Microsoft, Google and Oracle). This level of investment would introduce a \$1.5 trillion financing gap, which is expected to be funded from all corners of the capital markets, including private credit, corporate debt and securitized products.

Data center asset backed securities (ABS) and commercial mortgage-backed securities (CMBS) have emerged as a key source of capital for data center developers & operators by providing relatively inexpensive and long-term funding for their stabilized assets. Given institutional investors' desire for higher-quality and longer-dated paper, issuers have leaned into this demand. To this point, year-to-date issuance of data center ABS/CMBS has eclipsed \$19 billion, which is 70% higher than the \$11.5 billion issued in 2024 (Figure 3). This supply has come from a diverse base of operators, with 15 unique issuers bringing deals this year—half of which are first-time issuers in the securitized markets.

We believe data center ABS/CMBS issuance offers compelling value relative to corporate debt and other securitized products. New issue spreads on recent data center ABS transactions have priced 150-200 bps over Treasuries and typically feature a 5-year weighted average life (WAL) and a single-A rating. These levels look attractive when compared to other securitized products such as whole business securitizations, where recent new issue spreads have priced closer to 115-130 bps over Treasuries. We prefer deals backed by operators that have scale and history, as well as assets with desirable characteristics such as location and connectivity.

Figure 3: US data center securitization issuance is on the rise



Source: J.P. Morgan, Bloomberg. Data as of October 5, 2025.

However, we recognize that obsolescence is a key concern given the pace of technological change, and future refinancings could be challenged if data center utilization declines due to a slowdown or reversal in this digital infrastructure megatrend. Lately these risks appear to be increasing as the race to embark on lofty projects tied to AI training facilities (often in remote locations) accelerates. While this flurry of capital deployment is something we continue to monitor, it is important to note that the data centers securitized in ABS/CMBS deals are stabilized (built-out and leased-up), with most workloads being for traditional cloud & connectivity services, rather than AI training.

A divided Fed may add to market volatility

The Fed resumed its cutting cycle in September, lowering the policy rate by 25 bps to a range of 4.25%-4.5%. The median dot for 2025 implies two additional 25 bps cuts by year end.

However, there appears to be plenty of disagreement over the outlook. In September, there was one dissent from a non-voter who preferred no change in rates for 2025. Moreover, six participants were against any further cuts this year. Unsurprisingly, Stephen Miran was an outlier. His dot implied 150 bps of cumulative easing in 2025, which represents 50 bps of cuts at each of the next two meetings (including the late October meeting) as well at his vote for a 50 bps reduction at the September meeting.

Market pricing has been largely aligned with the Fed dots for 2025, but traders are pricing in roughly 50bps more cuts in

Figure 4: Fixed income asset class views

	Underweight --	-	Neutral ◇	+	Overweight ++
US Investment Grade	○	○	●	○	○
US MBS	○	●	○	○	○
US Treasuries	●	○	○	○	○
US High Yield	○	○	●	○	○
US Securitized Credit	○	○	○	○	●
EM Hard-Currency Short Duration	○	○	○	○	●

Source: L&G – Asset Management, America. Data as of October 14, 2025.

2026 than the cumulative easing implied by the Fed's median dot. We believe the central bank will cut rates at both of its remaining meetings this year, and our base case calls for the 10-year to remain rangebound between 4.00% and 4.50% in the near term.

There are still attractive sources of carry in fixed income, but selectivity is critical

Investors trudge toward the end of the year with a tacit recognition of the dissonance between valuations priced for nirvana and expanding signs of trouble in paradise. Tariffs remain a substantial policy shock, while surging government debt continues to slowly strangle US and G-10 economies alike.

However, we believe there are sufficient catalysts to remain modestly constructive. Economic momentum remains solid overall, with the US economy growing at a revised 3.8% annualized pace in the second quarter, the fastest pace in nearly two years. Meanwhile, recent fiscal legislation looks poised to support growth through 2026.

Yet we note that a myriad of unanswered questions should serve to limit hubris at this point of the cycle: Will the slowdown in the labor market eventually turn disorderly? Will a rebound in inflation restrain the Fed's policy response? How transformative will AI ultimately be? Who will emerge as winners and losers, and perhaps most strikingly, what are the implications for the future of work? While we still find attractive sources of carry across the fixed income landscape, we recommend proceeding with caution as it can be challenging to navigate a macro fog without the benefit of headlights.



Equity Markets

AI Offers a Rorschach Test for Investors

The AI theme's impact on equity markets is transformative yet uncertain and open for interpretation, requiring investors balance optimism with caution.



Dave Chapman, CFA
Head of Multi-asset

In a pithy summary of the crosscurrents outlined in the Macro Environment section, I heard the current market described as a Rorschach test: We are all looking at the same data and drawing very different conclusions. I believe that is especially true when it comes to equities (and equity volatility) and the dominance of the AI theme. Some see massive productivity gains fueled by transformative investment; others see a speculative bubble akin to the late-90s.

My approach has been, admittedly, more circumspect. I was slow to form an opinion until I recently had an epiphany based on my own use of AI. I've found AI particularly effective for developing or modifying recipes. I'd speculate that effectiveness is in large part because of the rich language of the food-blog preambles I used to mock (I don't need a 2000-word preamble about being inspired by Patagonian lingonberries—just show me how to make vinaigrette). In other words, AI is unlocking value from things already created and previously unappreciated. Plus, I saw productivity gains from managing my pantry and fridge inventory more efficiently. This realization has greatly increased my risk appetite, although with some critical nuance.

The broader bull case for AI

A recent report by Barclays highlighted several metrics that support the continued bull case for AI. Despite explosive capex already underway, compute demand is still far outstripping supply.¹ Further, that capex as a proportion of sales is running at roughly 25% versus the 40% seen during the dotcom bubble. Firms making that investment are also now generating strong cash flow and operating with much more conservative balance sheets. To me, a crucial point is that this investment is being made in tangible assets—actual

facilities and goods versus intangible software and domain names. Interestingly, this also supports a bullish case for commodities (as critical inputs), and, as we highlighted in our Q2 outlook, commodities also have tremendous diversification value for portfolios.

The critical nuance

However, what concerns me about the AI boom is whether and how we can continue funding it efficiently. Despite equity index concentration, the same Barclays report highlights the proliferation and dispersion of earnings calls mentioning AI in association with improvements in productivity and profitability. The broader economy is becoming more levered to AI, so a pullback by the hyperscalers will also have greater knock-on effects. It is also notable that our REIT credit analyst recently mentioned the big uptick in demand for office space for AI start-ups. Yet, a refrain among early-stage AI ventures is worry that the business could be obsolete before reaching its target market because of the rapid pace of innovation. Are investors being selective enough about AI? And can we match the pace of funding to sustain what is already productive and support ongoing selectivity?

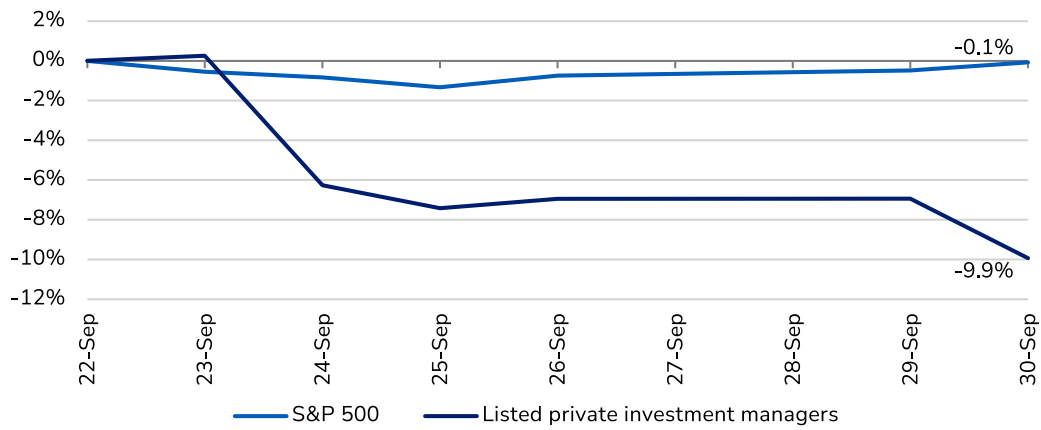
Meeting the desired amount and timing of funding resurfaces issues of liquidity challenges. Institutional investors still have significant capital locked up in private capital with little room to maneuver because private investment managers have struggled to make distributions. Concerns about the private investment market came to the forefront in September, as equities of many listed private managers sank during the last week of the quarter (Figure 5). This was attributed to concerns about the credit quality of existing deals or portfolio companies (but it also occurred conspicuously at quarter-end just before valuations are remarked...). If investors are unable or unwilling to provide more additional capital, where will the funding for AI come from?

The bottom line

Finally, I opened with an allusion to the equity volatility market and difficulty drawing conclusions from the abundance of data and commentary there recently. Both retail investors and some macro strategies are long CBOE Volatility Index (VIX) futures or VIX-related products, market positioning commonly taken as a contrarian (i.e., bullish) signal. This demand is creating richness across the S&P 500 volatility surface, enticing many other investors to sell volatility, potentially creating the conditions for a particularly sharp sell-off. But, yet again, dealers are supposedly long gamma, a dynamic that tends to ballast markets and is consistent with the very low realized volatility environment we are currently in. Taken all together, we see an ink blot of conflicting signals, not giving us a clear picture or pointing in a particular path forward, and warranting our cautious optimism.

Figure 5: Listed private investment manager equities fell in late September

Performance of listed private investment managers versus the S&P 500



Source: Bloomberg, L&G – Asset Management, America calculations. Data reflect the period September 22, 2025 to September 30, 2025. Listed Private Managers are represented by an equal weighted return of KKR, APO, ARES and OWL.



Equity Solutions

Our MSCI Rebalancing Predictions

Our prediction accuracy score came in high for the third quarter in an environment with fewer index changes than the prior quarter.



Dave Barron, CFA, CAIA
Head of US Equity Solutions

Demonstrating accuracy and reliability

Continuing our effort to track and assess the accuracy of our MSCI World rebalance predictions, we look back at the third quarter of 2025 and evaluate our performance during what was a quieter period of index adjustments.

In the third quarter, MSCI announced 14 adds and 16 deletes in the MSCI World Index, for a total of 30 total constituent changes. We correctly predicted 28 of the 30 and had no incorrect predictions. Consequently, our Rebalance Accuracy Score came in at 93.

This represents a steep increase from our second quarter score of 82, in an environment that exhibited both much less volatility and fewer index changes than the previous quarter.

With only 30 constituent changes in the third quarter, the impact of an incorrect prediction would have had a greater statistical impact on the final score. All of the predictions we made ended up being realized, and there were two extra deletions in Japan that we did not anticipate on the prediction list we published last quarter.

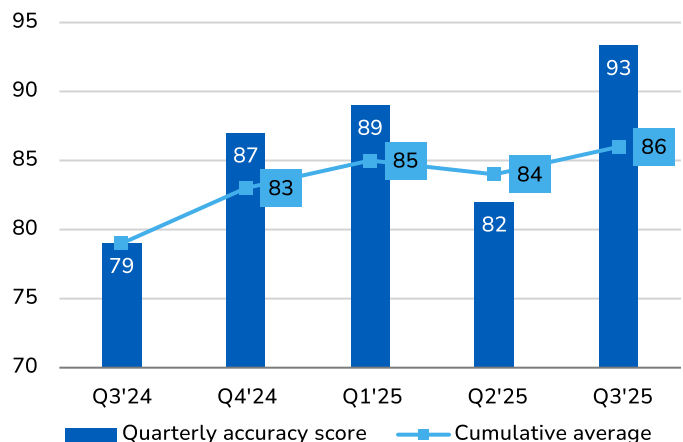
We always like to emphasize that every rebalance is different. This is why we tend to put more weight on the cumulative average score as an indication of the efficiency of our approach, rather than focusing on the score from a single quarter. Figure 6 shows an average prediction score of 86, which, this quarter, is on the higher range of what could be reasonably expected with an investment process that is robust and consistent.

Our latest predictions

Figure 7 highlights our predictions for the fourth quarter of 2025 MSCI rebalance. The key dates for this cycle are the following:

- 10 business day window: October 14 - October 27
- Announcement: November 5
- Implementation point: Close of Monday, November 24, but may be different for some markets (e.g., market holiday, exchange closures)

Figure 6: MSCI rebalance prediction history



Source: L&G – Asset Management, America. Data as of October 21, 2025.

Prediction process

- We have designed and implemented a low active risk approach to capture outperformance created by index micro inefficiencies. In our investment approach, we target a variety of opportunities, one being rebalance predictions, where we model widely followed approaches to predict index additions and deletions. This predictive capability provides an opportunity for us to optimize portfolio adjustments before official index announcements, potentially enhancing returns. Here's how it works for an MSCI rebalance:
- On a quarterly basis, MSCI will re-establish its market cap weighted index series using a publicly available methodology, which means it can be independently modeled with reasonable certainty.
- We identify which companies we believe will be reclassified between the Standard (Large + Mid Cap) indices and Small Cap indices.
- MSCI selects one of ten days at the end of the month prior to the actual rebalance to crystallize sizing classifications.
- A public notification of the changes happens approximately two weeks before the rebalance, with the

rebalance happening at the end of the month (February, May, August, November cycle).

After the rebalance period ends, we evaluate our predictions based on the following method:

- Correct prediction (i.e., true positive; 1 point)—We assign ourselves one point for every accurate add or delete prediction.
- Incorrect prediction (i.e., false positive; -1 point)—One point is deducted for every prediction that is not ultimately added or deleted by MSCI.
- No prediction (i.e., false negative; 0 points)—No points are assigned or deducted for an add or delete that was not originally predicted.
- We add up the total number of points and divide it by the total number of adds and deletes implemented by MSCI to determine the Rebalance Accuracy Score. While we do not expect to achieve perfect accuracy, our aim is to maximize correct predictions and minimize mistakes. Accurately predicting this information in advance is knowing what trillions of dollars are likely to do before they do it.

Figure 7: Our MSCI predictions for Q4 2025

Benchmark	Country	Name	Prediction
World ex USA	Australia	LYNAS RARE EARTHS LTD	Add
World ex USA	Australia	BLUESCOPE STEEL LTD	Delete
World ex USA	Austria	RAIFFEISEN BANK INTERNATIONAL	Add
World ex USA	Belgium	FINANCIERE DE TUBIZE	Add
World ex USA	France	TELEPERFORMANCE	Delete
World ex USA	France	ARKEMA	Delete
World ex USA	Germany	HOCHTIEF AG	Add
World ex USA	Italy	BUZZI SPA	Add
World ex USA	Japan	SEIBU HOLDINGS INC	Add
World ex USA	Japan	EBARA CORP	Add
World ex USA	Japan	JX ADVANCED METALS CORP	Add
World ex USA	Japan	KIOXIA HOLDINGS CORP	Add
World ex USA	Japan	NISSIN FOODS HOLDINGS CO LTD	Delete
World ex USA	Japan	YAKULT HONSHA CO LTD	Delete
World ex USA	Japan	MEIJI HOLDINGS CO LTD	Delete
World ex USA	Singapore	GENTING SINGAPORE LTD	Delete
World ex USA	Spain	NATURGY ENERGY GROUP SA	Add
World ex USA	Spain	MAPFRE SA	Add
World ex USA	Switzerland	SIG GROUP AG	Delete
World ex USA	United Kingdom	ENDEAVOUR MINING PLC	Add
World ex USA	United Kingdom	MONDI PLC	Delete
World ex USA	United Kingdom	WPP PLC	Delete
USA	United States	COREWEAVE INC-CL A	Add
USA	United States	FLEX LTD	Add
USA	United States	COMFORT SYSTEMS USA INC	Add
USA	United States	INSMED INC	Add
USA	United States	CIENA CORP	Add
USA	United States	CREDO TECHNOLOGY GROUP HOLDI	Add
USA	United States	ASTERA LABS INC	Add
USA	United States	BLOOM ENERGY CORP- A	Add
USA	United States	IONQ INC	Add
USA	United States	OKLO INC	Add
USA	United States	MOLINA HEALTHCARE INC	Delete
USA	United States	ALIGN TECHNOLOGY INC	Delete
USA	United States	ALBERTSONS COS INC - CLASS A	Delete
USA	United States	DAVITA INC	Delete
USA	United States	FACTSET RESEARCH SYSTEMS INC	Delete
USA	United States	MOLSON COORS BEVERAGE CO - B	Delete
USA	United States	AKAMAI TECHNOLOGIES INC	Delete
USA	United States	OWENS CORNING	Delete
USA	United States	BIOMARIN PHARMACEUTICAL INC	Delete
USA	United States	REVVITY INC	Delete
USA	United States	CROWN HOLDINGS INC	Delete
USA	United States	U-HAUL HOLDING CO-NON VOTING	Delete

Source: L&G – Asset Management, America as of October 21, 2025. For illustrative purposes only.

Private Credit

Financing the AI future

As AI investment accelerates, we believe private credit will play a crucial role in filling the projected AI financing gap. This is creating opportunities for investors, even as the outlook for AI remains uncertain.



Dan Dreher
Solutions Strategist

AI became a transformative force in tech starting in late 2022, shifting the industry from steady cloud growth and IT spending to an AI-driven revolution. This shift has sparked soaring demand for data center infrastructure and energy, fueled by the training of large language models (LLMs) and the anticipated expansion of AI inference and edge deployments—which, according to S&P Global Ratings, “seem to be at higher risk of being underestimated than overly ambitious.”

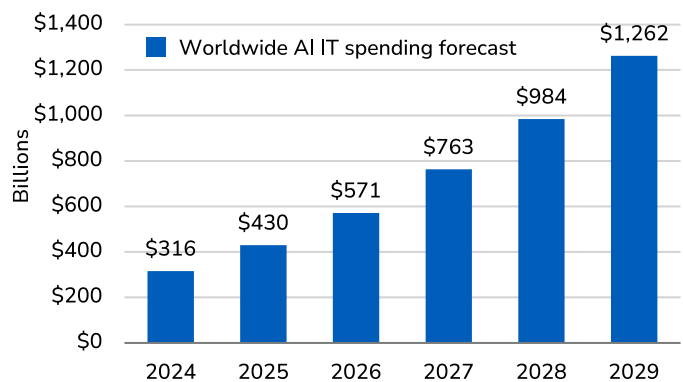
Over \$1 trillion in AI commitments have been announced since 2024, with over \$500 billion coming in the last two months. Most recently, Meta is reportedly in talks to raise a staggering \$29 billion, with \$26 billion expected to be from private credit. Companies like Meta are turning to private credit to fund the infrastructure needed to build frontier models. By securing private credit capital through a joint venture, Meta can fund this expansion with the operational flexibility offered by private credit markets while maintaining a very strong balance sheet.

The move is the latest, and one of the most dramatic, signs that the AI arms race has become so tremendously expensive that even the world's wealthiest tech companies are turning to outside financing for new and creative ways to fund their ambitions. As the scale and urgency of AI investment continue to accelerate, attention is now turning to future spending estimates and the necessary sources of financing to support this momentum in an environment where the need for capital is both vast and immediate. We believe private credit will play a crucial role in filling the projected AI financing gap, creating opportunities for investors even as the outlook for AI remains uncertain.

Sizing up projected AI spending

The transformative potential of the AI wave depends on large-scale capital expenditure, with data centers at its core. Currently, half of all commercial construction projects in the U.S. are data centers. And according to Morgan Stanley's predictions, global data center expenditure will reach approximately \$2.9 trillion by 2028, of which \$1.6 trillion will be for hardware (chips/servers) and \$1.3 trillion will be for building data center infrastructure. On an annual basis, this means that investment demand in 2028 will exceed \$900 billion. Independently, S&P cites IDC data suggesting the AI annual spend will reach \$1.2 trillion by 2029 (Figure 8). For reference, the total capital expenditure of all companies in the S&P 500 Index in 2024 was only about \$950 billion.

Figure 8: AI annual spend is projected to reach \$1.2 trillion in 2029



Source: IDC Market, S&P Global Ratings. Data as of September 30, 2025.

Capital expenditure on AI and data centers has been rising steadily, with spending by super-scale enterprises growing from \$125 billion two years ago to around \$200 billion in 2024 and expected to surpass \$300 billion in 2025. Historically funded through internal operating cash flow, this model is becoming insufficient as investment needs surge. According to Morgan Stanley analysts' predictions, super-scale enterprises may have \$1.4 trillion of capital expenditure funded by their cash flow, which will leave a financing gap of up to \$1.5 trillion.

Filling the financing gap

The broad credit market will play a role as the most efficient provider of capital to fill this gap. The credit market, especially the private side, has a large and growing pool of disposable funds and offers attractive real yield, which is appealing to a sticky group of end investors seeking scalable, high-quality asset exposure that can provide diversified returns. Morgan Stanley estimates the scale of various financing channels as follows: private credit at \$800 billion, private equity/venture capital/sovereign wealth at \$350 billion, unsecured corporate bonds at \$200 billion and securitized at \$150 billion.

Private credit is currently at the intersection of a higher interest rate environment, significant asset expansion, and the complex, globalized and customized financing needs required for AI development. The opportunities for investors

are expected in both the IG and sub-IG markets, with a large portion of the supply coming from IG entities.

Finding opportunities in IG

Large hyperscalers, REITs and utility / energy sponsors that enable AI prefer private, bespoke, long-dated debt (e.g., private placements, term loans and JVs) that won't appear in the public bond market in the same form. Further, and most importantly, the massive investments come from IG companies. Amazon (rated AA), Microsoft (rated AAA), Meta (rated AA-) and Alphabet (rated AA+) have each announced multiple AI and cloud data center buildouts and power sourcing deals in the tens of billions over the next few years.

S&P Global Ratings notes that even if we experience slower-than-anticipated AI adoption amid the massive investments, they don't foresee a significant impact on these four big tech companies' credit ratings. These companies are still expected to generate substantial free operating cash flow, allowing them to keep their credit metrics well below their downgrade thresholds for their ratings. Their financial strength and the competitive advantages of their non-AI businesses—especially their distribution channels—enable them to outspend competitors and mitigate potential threats from emerging AI challengers. Given that first-mover advantages and technological leadership provide substantial competitive benefits, S&P expects these incumbents to continue investing heavily, proactively nurturing the AI ecosystem to facilitate faster adoption.

Outside of these names, in IG or sub-IG, S&P also notes that any ratings approach largely hinges on structural considerations, noting assets are not the primary differentiator (Figure 9).

Navigating an uncertain outlook

AI remains credit-positive for leading tech companies, data center operators and power providers, but the sector faces growing risks as it matures—including competitive disruption, evolving pricing models, lease renewal uncertainty, the shift from model learning to inferencing, and constraints around power and permitting.

According to S&P, the most vulnerable are companies that have invested heavily but have yet to turn a profit, rely on external funding and operate in areas susceptible to rapid technological obsolescence. This includes firms such as OpenAI and Anthropic that focus on developing frontier AI LLMs and are increasingly investing in AI chip design and data centers. Despite experiencing exponential growth in valuation due to their AI models reaching unprecedented user adoption by certain metrics, their business models continue to evolve amid mounting losses and escalating ambitions.

The rapid rise of AI-driven investment has ushered in a new wave of supply, prompting a deeper reflection among investors: How will this influx reshape the landscape of debt channels, and where will it ultimately find its place? Private credit has emerged as a critical source of capital, helping bridge financing gaps and support continued innovation as traditional funding channels are tested by the scale and speed of AI investment.

While the long-term growth prospects for AI remain strong, the timing and scale of adoption—and the market's capacity to finance it—remain uncertain. The evolving role of private credit will be central to navigating these challenges and sustaining momentum across the AI ecosystem.

Figure 9: Ratings approach outside of big four hinges on structural considerations

	Corporate infrastructure	Project finance	Asset-backed securities
Issuer	Corporate	Limited-purpose entity	Bankruptcy-remote special-purpose vehicle (SPV)
Construction risk	Limited to expansion	May be present	Mitigated or limited credit
Operating risks	Full exposure	Full exposure	Limited (transferable and replaceable)
Renewal risk	Unmitigated (may have full market exposure)	Quantifiable (with impact on market exposure)	Quantifiable (re-leasing risk factored in)
Debt (typical)	Senior secured or unsecured	Senior secured	Multi-tranche, secured
Creditor protections	Typical corporate debt with limited covenants or security	Ring-fenced structure with covenants and security over assets, accounts, and key contracts	Ring-fenced with security over assets and/or cash flows, and ability to liquidate and sell
Debt features	Short-/medium-term legal final maturity dates	Medium-term legal final maturity dates	Shorter anticipated repayment with longer legal final maturity dates
Refinancing risk	Refinancing risk allowed; assessment of maturity profile and liquidity	Refinancing risk allowed; reliance on operating cash flows	Refinancing expected but not mandatory at ARD; reliance on operating cash flows and liquidation value

Source: S&P Global Ratings. Data as of September 30, 2025.



Footnotes

1. Source: Barclays, "Equity Strategy: Lost My Chain-of-Thought: Could the AI narrative stumble?"

Disclosures

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