

AMPERSAND

AI'S POWER PROBLEM

BEYOND BANKS

FISCAL FAULTLINES

DEATH OF THE OFFICE?

THE PERCEPTION EDITION

 **M&G**
Investments







Welcome to the sixth issue of Ampersand

Welcome to the latest issue of Ampersand. In this **perception** edition, we explore the importance of using our investment senses to retain perspective and capitalise on opportunities in a rapidly changing world.

Inside, we look at the changing nature of portfolio diversification, we consider the increasing impact of artificial intelligence on the global energy value chain, and we ask whether government bond investors are being sufficiently compensated for the risks posed by the greater participation of more price-sensitive investors in sovereign debt markets. With private credit evolving to become something of an alternative banking system, we look at the importance of investor perception in thinking less like passive allocators of capital and more like long-term lenders; and in the world of real estate, we investigate the 'second life' of assets nimble enough to respond to a changing urban landscape.

Elsewhere, with a nod to our sense of sound, we explore the case for investment in music (and wider) royalties, and we invite a number of our colleagues to share the songs they can't live without, as well as the market signals that make them sit up and listen.

Throughout this edition, we see the importance of using our senses to find perspective and adapt. As traditional assumptions about investment and the financial market environment continue to be upended, we believe more than ever in going beneath the surface and connecting our collective intelligence to make sense of where long-term value really lies for our clients.

I hope you enjoy this edition of Ampersand.

Joseph Pinto
CEO, M&G Asset Management

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ULTRA-PROCESSED PORTFOLIOS

THE QUESTION

Is the diversification ‘free lunch’ still on the menu?

THE INGREDIENTS

Concentrated markets

Positive correlation between equities and bonds

Misleading asset classifications

THE STORY

Diversification is one of investing’s most enduring ideas – and one of its most misunderstood. Unsurprisingly, with concentrated markets and positive correlation between equities and bonds over the last five years, there has been increasing discussion about the topic.

Mason Woodworth, Head of Investment Solutions, argues diversification still offers investors what Harry Markowitz called “the only free lunch in investing”, but that the way the industry serves it has stopped delivering. One of the problems, in his view, is not diversification itself; it is that a classification system designed to make investing manageable has been mistaken for a description of how portfolios actually behave.



The economist Harry Markowitz, who won a Nobel Prize for the mathematics of building portfolios, called diversification “the only free lunch in investing”. It is probably the most quoted line in portfolio construction. The principles behind it seem almost like common sense: don’t put all your eggs in one basket. Combine assets that do not move for the same reasons, and the whole carries less risk than the sum of its parts. No forecasting required. It is just arithmetic.

But it is worth being honest about the analogy, because the industry has leaned on it rather heavily. Just because a lunch is free does not mean it tastes good, and it certainly does not mean it is good for you.

Markowitz was making a claim about covariance – the statistical behaviour of investments held together. He was not making any claim about the quality of the ingredients. Somewhere along the way, ‘low cost, broad and technically uncorrelated on paper’ became accepted shorthand for ‘healthy’. Those are not the same thing, and the difference between them is now a source of a significant amount of portfolio risk.

Ultra-processed portfolios – the illusion of variety

An interesting and potentially powerful parallel comes from a current debate happening outside financial markets. I have been reading *Ultra-Processed People*, a book by doctor and broadcaster Dr. Chris van Tulleken,¹ which argues that a large share of what fills our supermarkets is not really food, but “an industrially produced edible substance”. It is engineered for shelf life,

low cost and repeat consumption, and strongly implicated in obesity, chronic illness and environmental damage.

What is interesting is the difference between apparent variety and actual nutrition. A supermarket aisle offers dozens of brands, flavours and formats, which can all be reduced to the same handful of cheap engineered inputs: refined sugars, refined fats, salt and starch.

The variety is real at the level of the label, but largely illusory at the level of the eating. And because these products are designed to be convenient, often low cost and moreish, they encourage you to keep consuming.

There is a parallel with modern portfolio construction. A top-down asset allocation populated with low-cost passive building blocks delivers genuine variety at the level of the label: thou-

sands of holdings, dozens of countries, and multiple ‘asset classes’, each with a distinct and reassuring name.

For many years, this looked like an excellent investment solution, and in fairness it was a considerable improvement on the huge variety of less structured approaches that came before it.

But count the underlying portfolio nutrients rather than the labels, and the picture changes. A striking proportion of the return and risk in many modern portfolios actually reduces to a small number of common drivers – US mega-cap technology and the artificial-intelligence (AI) theme, duration, and the dollar. Many different names; the same few things actually creating the outcome.

¹Chris van Tulleken, *Ultra-Processed People: Why Do We All Eat Stuff That Isn't Food... and Why Can't We Stop?* (Cornerstone Press, 2023).



If Dr. van Tulleken's formulation is right about food, something similar can be said about the building blocks of the 'ultra-processed portfolio'. A vehicle tracking a capitalisation-weighted index is not, by design or construction, a true economic exposure or a genuinely diversifying asset. It is an 'industrially produced investible substance' that is manufactured to be cheap, liquid, administrable and easy to allocate to – engineered for convenience and to support the system that distributes it rather than for the nourishment of the portfolio that consumes it.

That is not an argument against ever using one; it is simply an argument for knowing what you are eating. I like a can of soda, crisps, ice cream and chocolate as much as anyone, but I know that is not a diet that is going to help my body become strong or resilient.

‘A striking proportion of the return and risk in many modern portfolios actually reduces to a small number of common drivers.’

When the map started running the territory

How did this happen? Largely through the quiet conversion of a filing system into a philosophy.

The taxonomy of asset classes we all use – equities and bonds, developed and emerging markets, investment grade and high yield – grew out of an entirely reasonable need. Global markets are complex to the point of illegibility, and institutions have to govern their participation in them: to report, to benchmark, to set risk budgets, to hold managers to account and to explain to a board what has been done with the money. Grouping exposures under names made that possible. It was, and remains, a sensible administrative solution to a genuine problem.

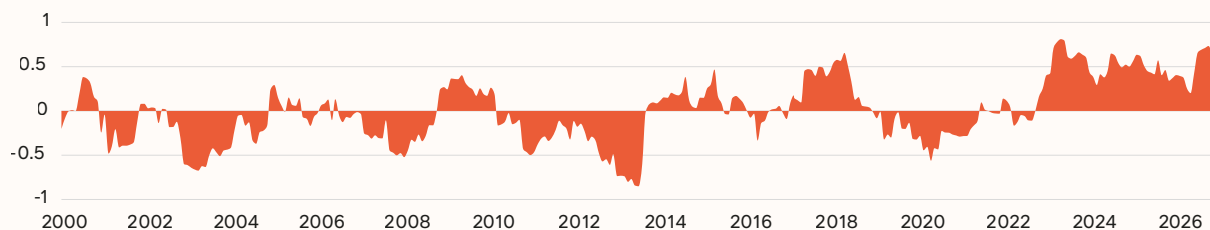
The difficulty is that a classification system designed for governance has gradually been treated as a description of economic reality. Investors no longer merely use the taxonomy to describe what they own; increasingly they allocate to the taxonomy, letting the categories drive the decisions. The map, having been drawn for convenience, has started running the territory.

And critically, the map has not kept pace with the ground it claims to represent. 'US equity' once described a broad exposure to American companies and the US economy; today its contours are established by a handful of companies pursuing a single technological theme with global, not domestic, revenue bases. The US label essentially describes where an asset sits on a map, not what actually drives its return or its risk.

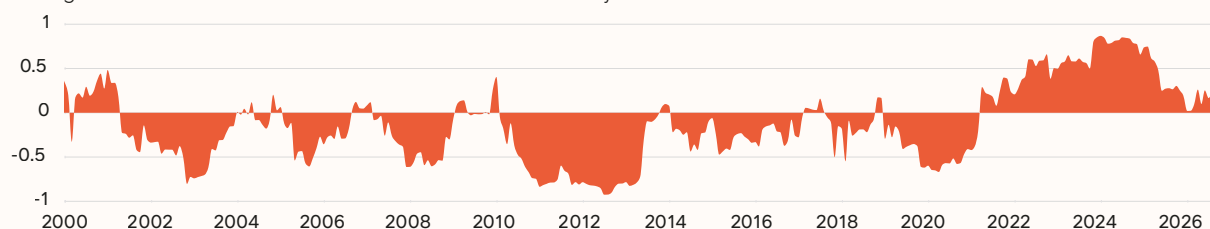


Equities and bonds: A complementary relationship?

Rolling 12-month Return Correlation of FTSE All-share vs UK Gilt 15yr+ Index



Rolling 12-month Return Correlation of SPX 500 with UST 30yr Index



Source: Bloomberg, October 2026. Past performance is not a guide to future performance. Investors cannot invest directly in an index.

When broad becomes narrow

There is a reinforcing mechanism at work here: a capitalisation-weighted index allocates the most capital to whatever has already risen most, regardless of whether that rise reflects improving fundamentals or simply narrative, capital flow and momentum.

Index weight attracts flow, flow supports price, price increases index weight. Within that loop, buying 'the market' is not a neutral, diversified stance at all: it is a position that systematically rewards price momentum rather than the underlying economic drivers of growth at a company or market level, and it concentrates further precisely when concentration is already rising.

The numbers make the point more powerfully. It is now a well-known fact that something like half the entire value of the S&P 500 sits in around 20 companies.² Widen out to the global index and roughly 10 names – every one US-listed, eight of them in the same artificial-intelligence and technology cluster – make up close to a quarter of the whole world's stock market, with about two-thirds of the index tied to a single country.³

It is fair to say that these weights are not arbitrary. Market capitalisations reflect the collective judgement of millions of investors about what each company is worth, and that judgement may well be right. But it is a judgement about the value of each separately.

No one is actively voting on whether a quarter of the world's equity market

'Half the entire value of the S&P now sits in around twenty companies.'

should depend on a single technological theme. That outcome is the sum of thousands of separate pricing decisions, not a decision about diversification, and correct prices can still add up to a concentrated portfolio.

None of this is an argument against index investing, which has given savers low-cost access to markets and remains a perfectly sensible building block when used deliberately. It is an argument against mistaking an administrative convenience for an assurance of diversification.

Rethinking the equity/bond partnership

The same question applies to the relationship between equities and bonds – what is it really driven by? For most of the past 40 years, the relationship has created a well-used construct for diversification. The two broad asset classes complemented each other well: when share prices fell in a growth scare, government bond prices usually rose, because the market expected central banks to cut interest rates to cushion the blow.

Believing this relationship would hold particularly in tough times, people bought bonds if they were expecting a crisis or just perceiving a crisis, making the relationship expectation almost self-fulfilling.

But the pairing depends on a specific condition: the central bank having room to cut. An inflation shock removes it – with prices already rising too fast, policymakers cannot come to the rescue. In 2022 we saw the result, as equities and bonds fell together.

That was not a freak occurrence. For much of financial history, the two have moved together; the reliably offsetting relationship of recent decades was itself the exception. The lesson is not that bonds have stopped being useful, but that the relationship was never a property of the labels – it was a property of the policy environment, which we can argue has changed.

²BlackRock, 'Mega-Cap Exposure: Manage Concentration Risk in the U.S. Market', April 2026.

³MSCI World Index, August 2026.

Nutrition, not calories: what genuinely active investing means

Put all this together and the conclusion is encouraging rather than gloomy. Diversification has not stopped working. But it can no longer be inherited from a set of labels – it has to be built actively and deliberately, from the bottom up, by understanding what drives the fortunes and ultimately the price of each holding.

There is an important distinction to be made. A great deal of what is sold as active investment today is index-relative decision making. It starts from benchmark index weights – most commonly cap-weighted indices – and then takes modest positions around them.

While this type of active investing is fundamental to ensuring efficient indices, the approach cannot solve the problem of diversification described here – because it inherits the very concentration it claims to manage. If the benchmark is a levered bet on a handful of names, then a portfolio built as a small deviation from that benchmark is also a bet on those names. To borrow the analogy once more, reformulating an ultra-processed product does not make it real food.

Genuinely active investing starts from a different place: not with the index weights, but with an understanding of each asset you intend to invest in. It asks what a company actually earns and why, what a borrower actually depends on and whether they can repay, and what a private asset's cash flows are genuinely tied to. It builds the portfolio where each holding earns its place and builds aggregate exposures on purpose rather than starting with a price-related index.

That is hard work. It requires genuine research depth across equities, credit and private assets, and requires building sufficient conviction to hold positions that you believe will deliver superior returns rather than match some kind of index. It is the work that determines whether a portfolio is 'nutritionally' diverse rather than just varied by names and labels.

‘Genuinely active investing starts... with an understanding of each asset you intend to invest in.’





Building a nutritious portfolio

Looking through the equity index

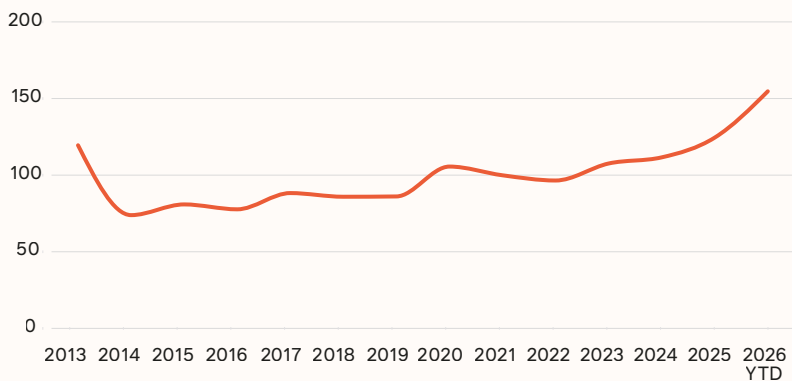
If passive ownership of global stock markets has quietly become a bet on a few large names, genuine equity diversification has to be constructed on purpose. That means selecting companies on the basis of what they actually do and how good they are at generating earnings. Once you know this, you can start to have a genuine view about how they may behave in different conditions.

Encouragingly, the raw material for this within equity markets is abundant. In the S&P 500 Index, the so-called Mag 7 grab the attention and their market capitalisation continues to dominate. However, if we exclude these seven stocks, the dispersion between the best and worst performers has been increasing and is historically wide (estimated by deciles). Over the last decade, the top decile ex-Mag 7 has outperformed the Mag 7 in the majority of years. The companies that make up this decile in each year have changed often but this further demonstrates the opportunity for looking beyond the index.

Broadening opportunities

Dispersion of returns in S&P 500 Index, ex-Mag 7

(%) Top – Bottom decile

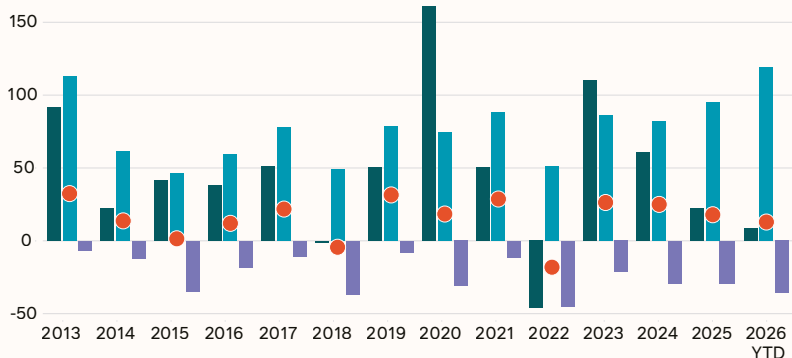


Source: Bloomberg, October 2026. Investors cannot invest directly in an index.

Opportunities beyond the index

■ S&P 500 Index ■ Magnificent 7 Avg ■ Top Decile ex-Mag-7 ■ Bottom Decile ex-Mag-7

(%) Dispersion of S&P 500 returns



Source: Bloomberg, October 2026. Investors cannot invest directly in an index.

Careful bond selection

Bonds are typically considered the ballast of a portfolio, and after years of uncertainty about whether they could still perform that role, they merit a fresh look: real, inflation-adjusted, yields are positive for the first time in years.

But a bond index carries its own version of the same flaw, and arguably a worse one. The largest weightings go to whoever has borrowed the most, which common sense suggests is the opposite of how to actually diversify bond risk.

Active bond selection means identifying where the most attractive yield genuinely resides, and judging credit quality by company fundamentals and by their position in their market – and this is increasingly the same for a government or a corporation. The label ‘credit’ says nothing on its own about whether that judgement has been made.

As with equity, the story of an index or a rating bucket doesn’t characterise the full extent of the opportunity or the risk.

Broadening horizons to private markets

Some of the genuinely distinctive exposures available to investors sit outside public markets. Private credit, infrastructure and real assets are driven by things the stock market often is not: the rent on a specific building, the contracted cash flows of a toll road or power grid, the terms of an individual loan. Infrastructure frequently carries built-in inflation protection; in private credit, the close relationship between lender and borrower means any trouble tends to surface early.

‘Sourcing and originating specific assets is what produces genuinely differentiated exposure.’

This is also where the distinction between owning an exposure and originating one matters most. Buying broad, pooled access to private markets risks reproducing exactly the problem this article describes – a reassuring label covering a set of drivers you may not have actually examined. Sourcing and originating specific assets is what produces genuinely differentiated exposure, and it is a capability rather than an allocation.

A healthy lunch, not just a free one

Markowitz was right about the principle, and the mathematics have not changed. What has changed is that the industry built a system of names on top of it, and then began to mistake the names for the thing itself. A taxonomy created to make global investing governable has become the way investing is done. That taxonomy is also intrinsically self-reinforcing. Growth accrues to things that

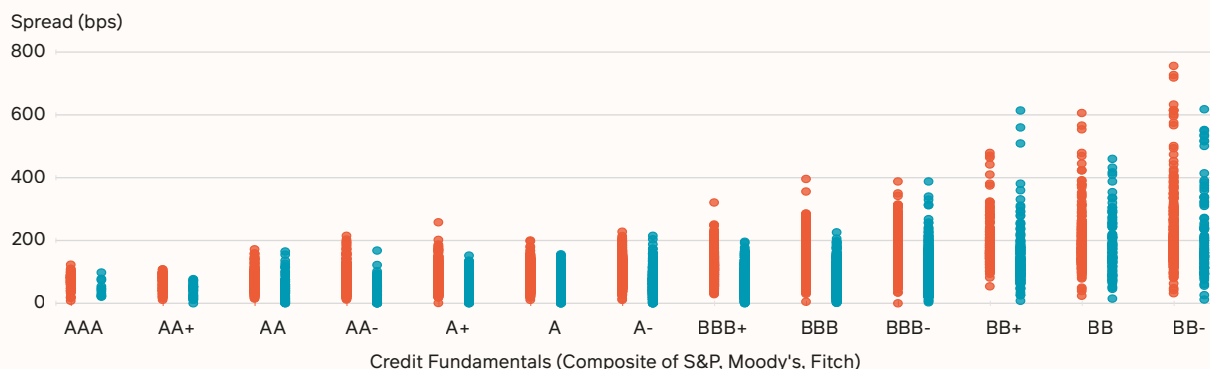
have grown the most. This investing behaviour has been quietly concentrating portfolios at the time when investors may need real diversification.

The remedy is not to abandon the idea of diversification, but to take it more seriously than just holding a portfolio of things with different names. It means looking through the names to the economic drivers underneath, building portfolios with specific exposures that each contribute to the desired outcome and bring something different.

This is harder than buying an index. But this kind of free lunch is still available. As with food, the question is no longer whether the meal is free or even whether it offers plenty of choice. It is whether what is on the plate will actually nourish the portfolio – or make me feel really good while eating it, but sick and probably guilty when I’ve finished. That’s something to think about when you plan your diversification menu. □

Spread dispersion can present opportunities for active credit investors

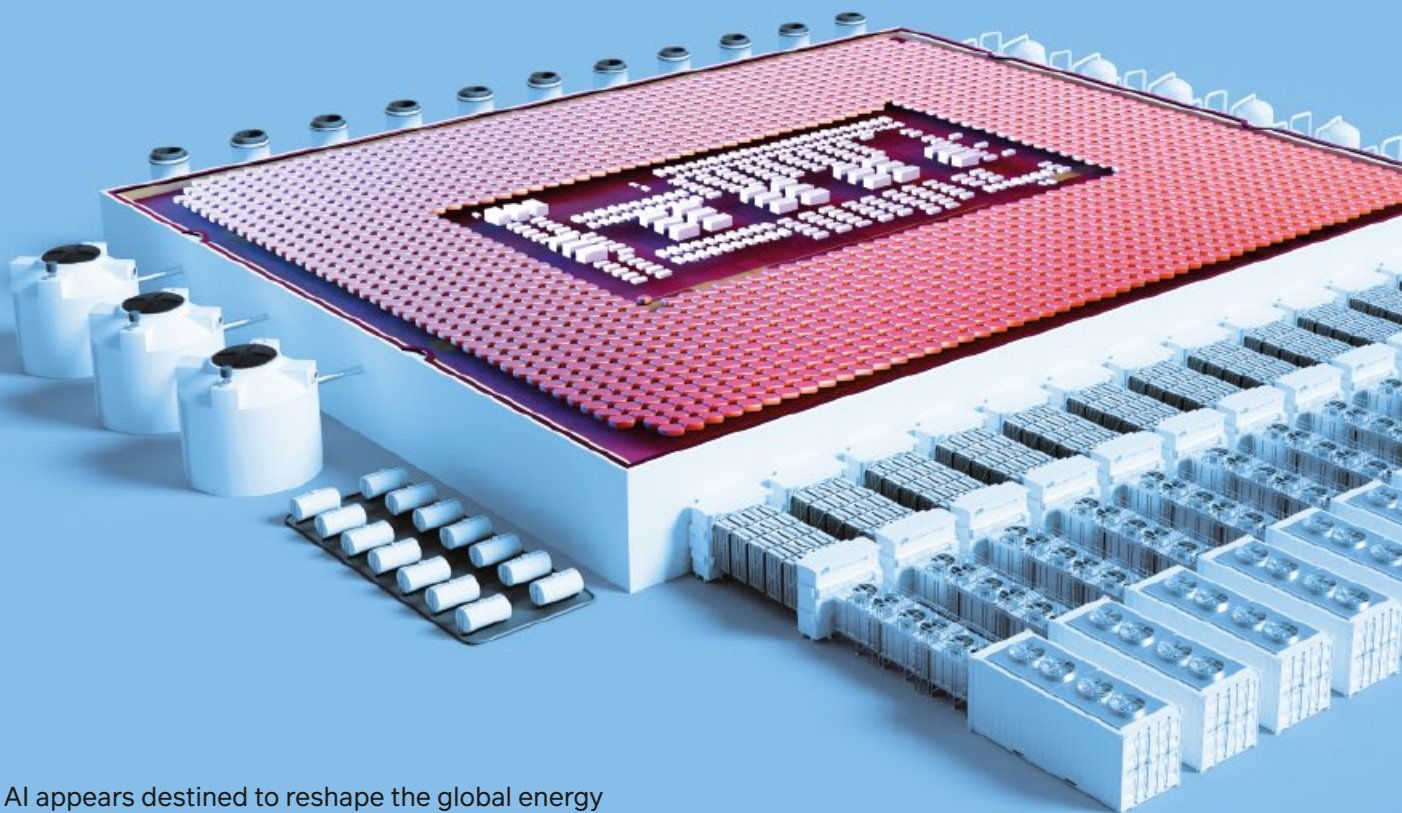
● US IG & US BB HY ● Euro IG & Euro BB HY



Source: MSG, ICE BofA Euro Corporate Index (Ref. EROO), Non-Financial High Yield Constrained Index (Ref. HEAD), US Corporate Index (Ref. COAO), and US High Yield Index (Ref. HOAD), composite credit rating derived from average of S&P/Moody's/Fitch. Data as at 31 August 2026.

THE POWER BEHIND THE CHIPS

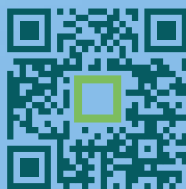
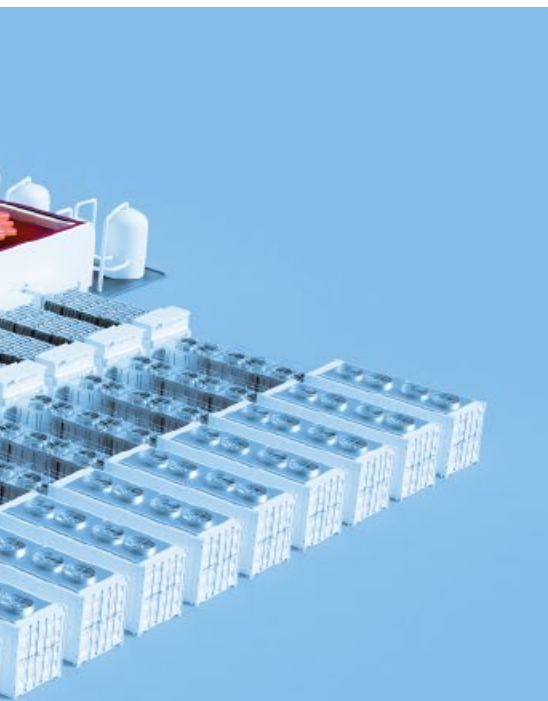
how
energy
matters
in
the
AI
race



AI appears destined to reshape the global energy landscape as the race for power gathers momentum. Dominic Howell speaks to Michael Rae, manager of the M&G Global Energy Opportunities Strategy, about the importance of energy to the AI revolution and how the technology's demand for power could create investment opportunities right along the energy value chain.

The number of technological changes in modern history that have left a visible mark on global energy demand can be counted on one hand. The steam engine and railways helped propel the rise of coal in the 19th century; the automobile transformed oil into the dominant fuel of the transport age; and mass electrification brought an expanding universe of appliances, motors and machines into homes and factories in the second half of the 20th century.

Artificial intelligence (AI) appears to be the latest technology which will drive meaningful changes in energy flows. The International Energy Agency (IEA) expects global data centre electricity consumption to more than double from around 415 terawatt-hours (TWh) in 2024 to approximately 945 TWh by 2030¹ – an addition roughly equivalent to the annual power demand of Germany.²



We've transformed the data throughout this article into sound, have a listen.

Reconfiguring the energy system to meet this anticipated increase will inevitably require major investment. It could also unlock diverse investment opportunities as the required capital works its way through the physical economy: into power generation, electricity grids, cooling systems and the equipment needed to deliver usable power to AI chips.

A structural shift in energy demand

The most powerful driver of the changes in the energy sector has always been persistent growth in global energy demand. As Michael Rae, manager of the M&G Global Energy Opportunities Strategy, says, "rising wealth, population growth and human progress through innovation have all historically been associated with increased energy use."

In the past decade, these forces have been masked by economic volatility and the COVID pandemic, but they have not gone away. The IEA forecasts global electricity consumption will increase by 3.6% a year between 2026-2030, fuelled by demand from industry, the take-up of electric vehicles (EVs), increased use of air-conditioning, and the adoption of AI. This growth is 50% higher on average compared with the rate across the previous decade.³

As AI data centres become more pervasive, the focus of the debate is increasingly turning to power demand, with the US set to add a record 86 gigawatts (GW) of new power capacity in 2026 to meet that demand.⁴ Rae notes that "the power needs of AI have been talked about for some time, but 2026 is the first year in which the phenomenon has been visible in system-level demand trends and, to an extent, power prices".

The sheer scale of the power demand for AI projects is coinciding with robust economic growth in emerging markets, especially China, and a generational upgrade of the grid in many countries. Combined, these factors could mean we are at a defining moment for the global energy sector.

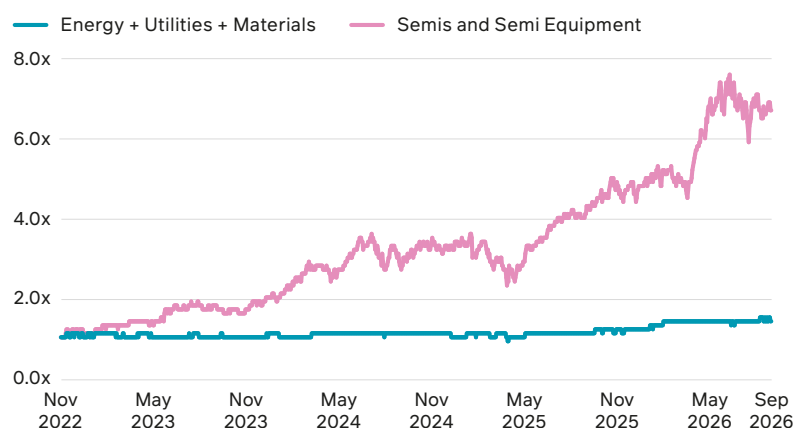
With the world also on a path to cleaner energy sources, it is plausible that the energy landscape is set to be transformed by massive capital investment in the coming years. The question for investors is where the opportunities will lie.

Powering the chips

Since the launch of ChatGPT in November 2022, AI has dominated headlines and market narratives. However, the so-called AI trade has mostly been focused on technology and computing equipment, rather than the wider framework that makes it possible.

Chips have attracted most of the AI attention, thus far

Increase in market capitalisation of MSCI World sectors since launch of ChatGPT*



Past performance is not a guide to future performance. Investors cannot invest directly in an index. Source: Bloomberg, September 2026. *ChatGPT was launched in November.

¹IEA, Energy and AI, (www.iea.org) April 2025.

²According to the Bundesnetzagentur, Germany's generation in 2025 amounted to 437.6 terawatt hours. (Bundesnetzagentur, January 2026).

³IEA, 'Electricity 2026', (iea.org), February 2026.

⁴US Energy Information Agency, 'New U.S. electric generating capacity expected to reach a record high in 2026', (eia.org), February 2026.

FROM SUNLIGHT TO SILICON

Artificial intelligence may appear weightless, but every calculation depends on an immense physical network. We follow the journey of an electron from a photovoltaic solar panel, through the electricity grid and into a semiconductor inside an AI data centre.

1 HARVESTING LIGHT

A modern utility-scale solar panel converts roughly 20% of incoming sunlight into electricity. A large solar farm can generate hundreds of megawatts (MW), enough to power hundreds of thousands of homes under favourable conditions, or a single hyperscale AI campus.

2 POWER ELECTRONICS: THE FIRST BOTTLENECK

Solar panels generate direct current, but grids operate on alternating current. Inverters synchronise every solar installation with grid frequency and voltage. Modern power electronics have become one of the most critical components in the global energy transition.

3 RAISING THE VOLTAGE

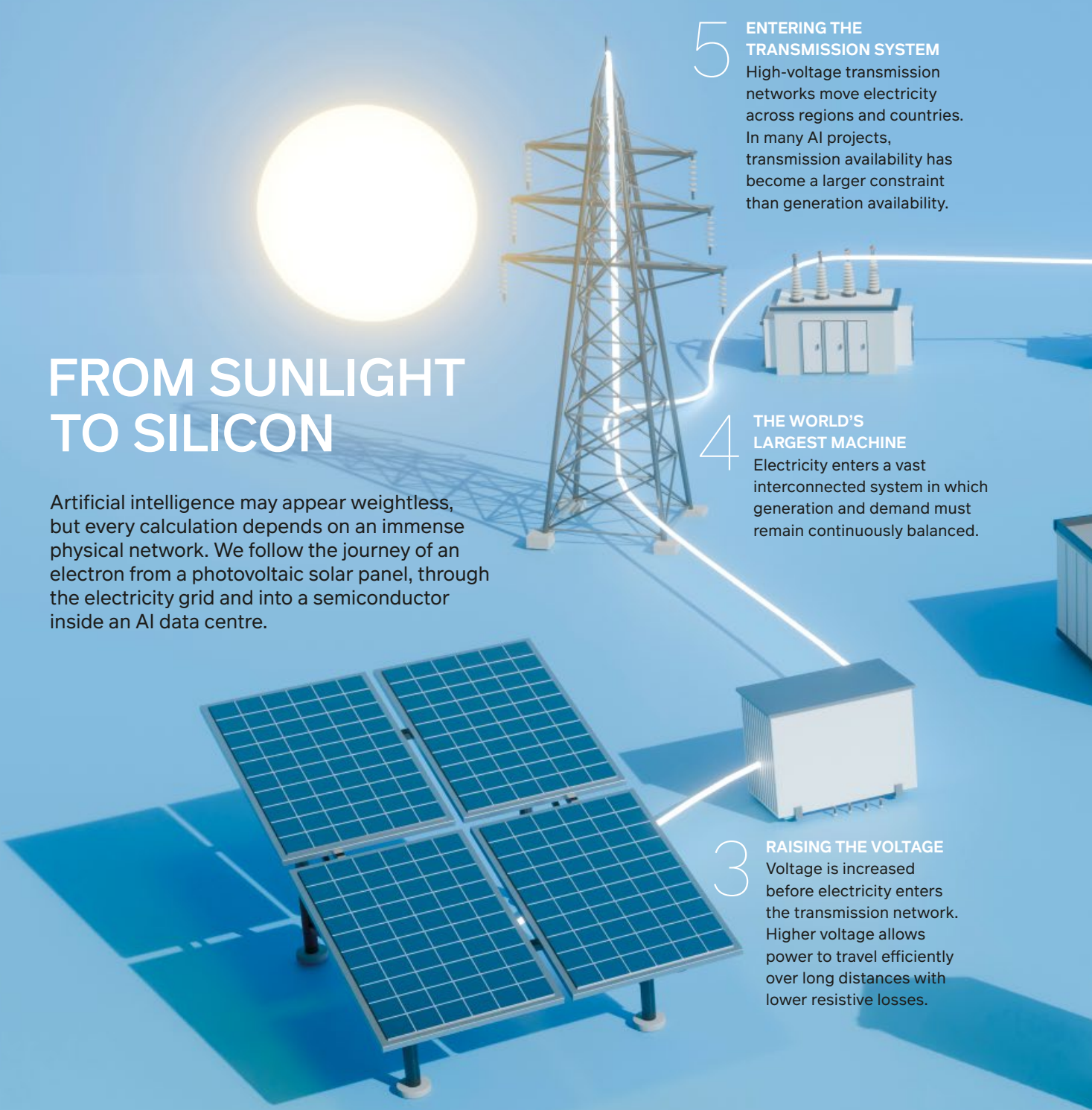
Voltage is increased before electricity enters the transmission network. Higher voltage allows power to travel efficiently over long distances with lower resistive losses.

4 THE WORLD'S LARGEST MACHINE

Electricity enters a vast interconnected system in which generation and demand must remain continuously balanced.

5 ENTERING THE TRANSMISSION SYSTEM

High-voltage transmission networks move electricity across regions and countries. In many AI projects, transmission availability has become a larger constraint than generation availability.



6

REDUCING THE VOLTAGE

Electricity must be stepped down as it approaches end users. For new data centres, access to local substations is often the binding constraint. Grid connection delays can exceed the construction time of the data centre itself.

7

THE FINAL GRID CONNECTION

Electricity is distributed to homes, businesses, industry and critical infrastructure. Data centres require high-capacity, reliable connections and can place significant new demands on local networks. Hyperscale campuses increasingly seek 500 MW to 1 GW (gigawatt) connections, equivalent to a large industrial complex or a small city.

8

THE PHYSICAL HOME OF AI

Data centres consume vast amounts of electricity, not only for computation, but also for cooling, networking, data storage, lighting and operational resilience.

9

PRECISION POWER

Before electricity reaches a processor, it pass through multiple conversion and regulation stages, with energy lost at each step. At hyperscale, efficiency is valuable.

10

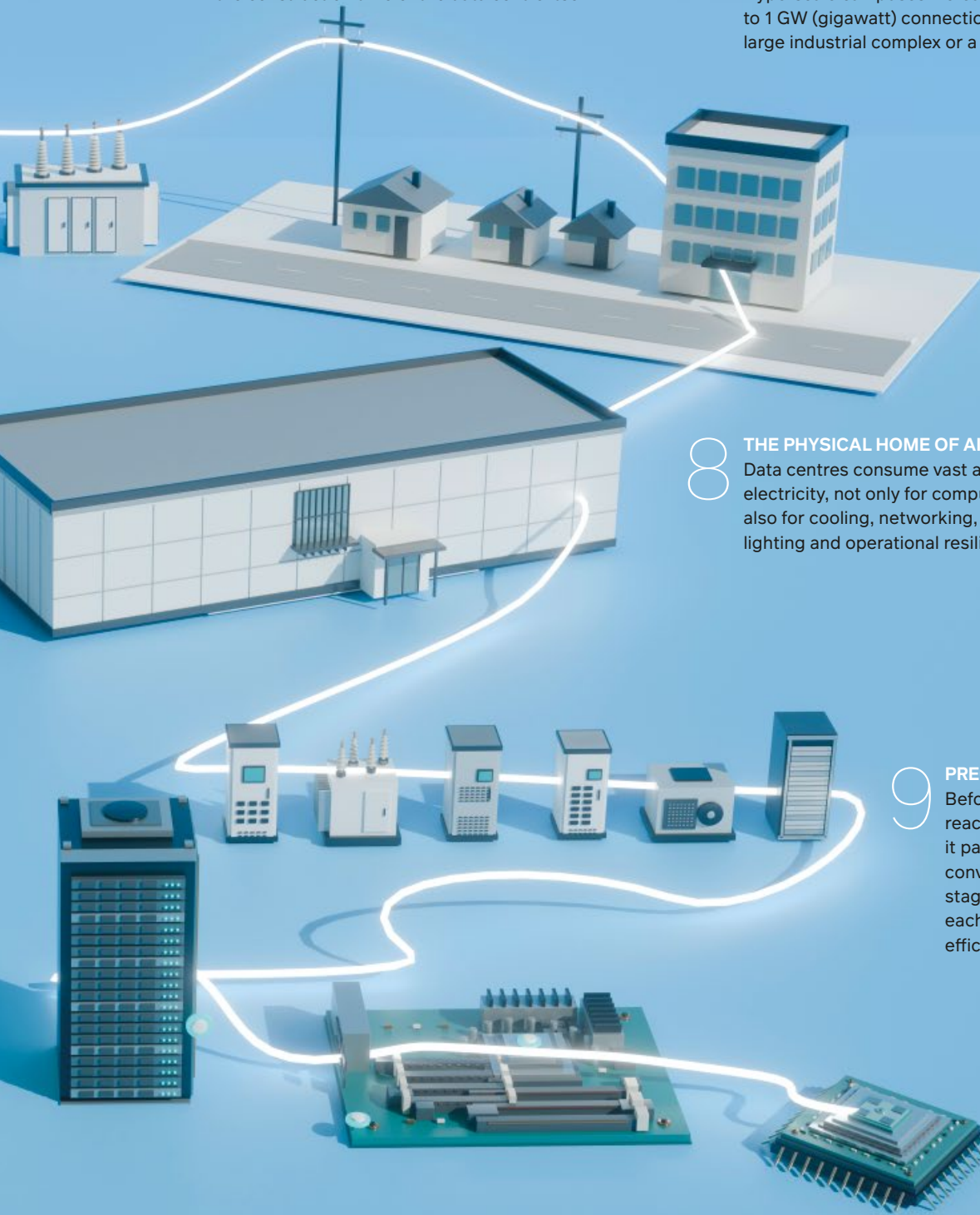
FROM MEGAWATTS TO MICROELECTRONICS

At server level, electricity is converted again and delivered at the exact voltages required by processors, memory and networking equipment.

11

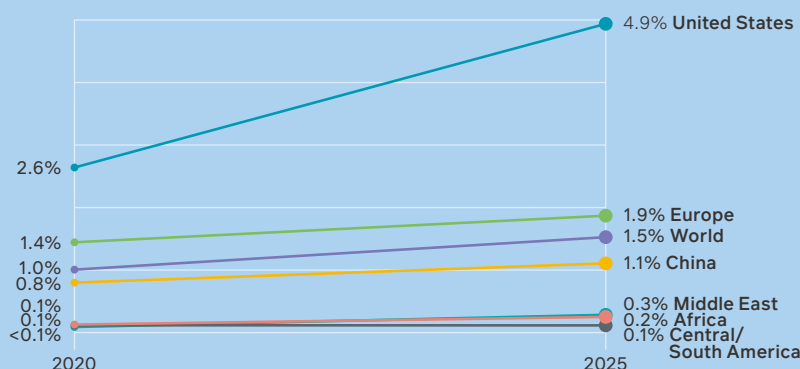
WHERE COMPUTATION HAPPENS

Inside the semiconductor, billions of transistors manipulate electrical signals to perform the calculations behind AI models.



AI data centres consume large amounts of power

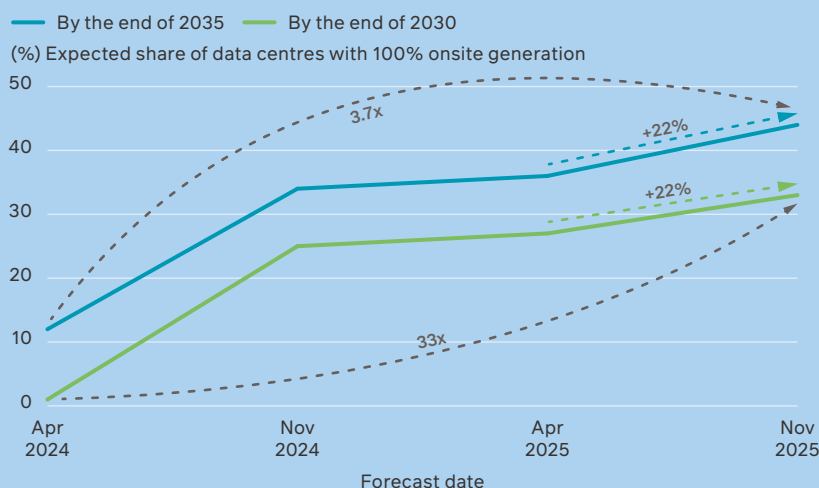
Share of total electricity demand used by data centres, 2020-2025



Source: International Energy Agency (2025, 2026); Ember (2026) – with major processing by Our World in Data.

Beating the queues:

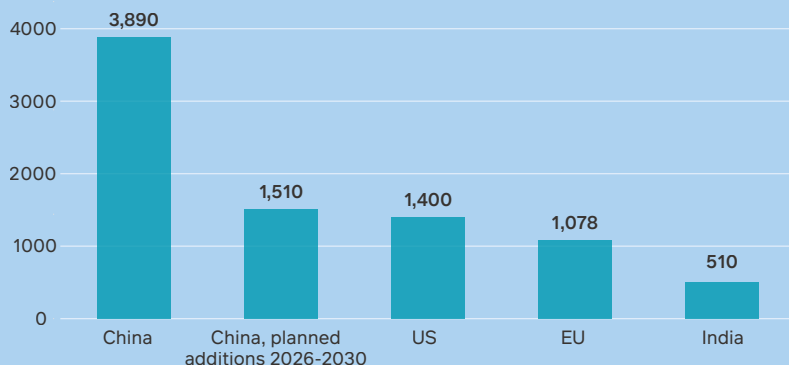
AI firms are looking to secure their own power supply



Source: BloomEnergy Data Center Survey, November 2025.

China's medium-term capacity addition plans are larger than the entire existing US power sector

(GW) Installed power capacity



Source: China National Development and Reform Commission, 15th Five-Year Plan for Building a New Energy System, June 2026; Edison Electric Institute, Fraunhofer ISE 2025, Ministry of New & Renewable Energy India, June 2026.

This is evident from the phenomenal increase in the market capitalisation of the global semiconductor and semiconductor equipment sectors in the past couple of years.

As the proverbial 'picks and shovels' companies that supply the chips used in AI models and data centres, firms like Nvidia and TSMC are expected to play an important role. However, as data centre construction activity accelerates in the physical economy, the focus is increasingly turning to power.

AI data centres require energy for computing and cooling. According to the IEA, they already accounted for around 1.5% of the world's electricity consumption in 2024.⁵ Unsurprisingly, given US companies are at the forefront of AI, data centres tend to be concentrated in the US, but many are located in China, Japan and Europe, with notable clustering in certain areas. In fact, in Ireland, they consumed over 20% of the country's electricity in 2025.⁶

With many more data centres being planned, the energy intensity of AI means that energy infrastructure is critical to its success. However, the market caps of the energy, utilities and materials sectors suggest that this is not being fully recognised by investors.

Energy: The real AI bottleneck

The importance of sufficient electricity supply for AI's future needs has not escaped the CEOs of large technology firms, though, including Elon Musk. Although there has been much discussion about a shortage of memory chips, the real AI bottleneck is power, with demand racing ahead of capacity deployment.

The scale of the power constraint can be seen from the current grid connection queue. This represents all the power projects that are being planned to supply data centres and need to be connected to the electricity grid. Currently, the amount of proposed capacity is massive and very unlikely to be fully realised. In Texas, for example, where many US data centres are being built, the requests add up to 474 GW, which is more than five times Texas's record peak demand.⁷

⁵ IEA, Energy and AI, (www.iea.org) April 2025.

⁶ RTE, 'Data centres accounted for 23% of electricity usage last year', (rte.ie), July 2026.

⁷ Office of the Texas Governor, 'Governor Abbott Directs Comprehensive Data Center Audit', (gov.texas.gov), August 2026.

Public pushback and concerns around grid capacity are forcing large technology firms, or hyperscalers, to adopt 'behind the meter power', which entails building power generation, typically gas-fired, specifically for their data centres. This means that they can proceed without a grid connection and also avoid some of the concerns about their data centres putting strain on the grid and driving up energy prices.

Firms that are able to resolve this huge energy supply-demand mismatch could be in a promising position. For example, NextEra Energy, the largest utility firm in the US, is one of the companies that has been identified as enabling the hyperscalers to secure reliable, long-term power supply.

Gas turbines: Integral to future power demand

Beyond the utility companies, another industry that could benefit from the power crunch is gas turbine manufacturing. Leading firms in this market such as Siemens Energy and GE Vernova are seeing demand increase dramatically, as more gas-fired power plants are being constructed to supply data centres.

With an imbalance between orders and global manufacturing capacity, turbine prices have also rocketed. Wood Mackenzie, an energy industry research firm, estimates that by 2027 the cost of turbines will have risen by 195% since 2019.⁸

Although data centre projects are currently the main driver of demand for turbines, the reliability of gas-fired power stations means that they are also being introduced to complement intermittent renewable power sources, such as wind and solar.

As a result, the gas turbine sector is booming, with companies reporting multi-year order backlogs. While the sector's integral role in the AI buildout and the energy transition makes it a potentially attractive investment proposition, it remains a cyclical industry and it is important for investors to think about the durability of demand, as well as any potential risks with contracts.

However, in the near term, as the race for power continues and bottlenecks in the energy supply chain are increasing, gas turbines appear to be attracting wider attention as an essential part of solving the current electricity capacity constraint.

Modernising grids for the Age of Electricity

Besides the bottleneck in power generation equipment, another challenge in meeting AI's rising electricity demand is the state of the grid. In many developed markets, grids have not been upgraded for several decades.

To prepare for what the IEA has called the 'Age of Electricity', grid infrastructure around the world will have to be expanded and modernised to meet increased demand and integrate renewable energy sources.

China has been preparing for this new era by investing heavily in renewable power generation in recent years. It is planning to spend a further ¥5 trillion yuan (US\$722 billion) on its power grid over 2026-2030, up from ¥2.85 trillion during 2021-2025.⁹

"As is often the case, the scale of China's ambition is in a category of its own – it will add the equivalent of the entire US power base in five years," Rae observes. If the AI race eventually becomes more of an energy cost battle than a compute battle, China could find itself in a very strong position. It will also help with the country's path to decarbonisation.

The European Union has also recognised the importance of a digitalised and flexible power network and is planning to spend €584 billion on its grids by 2030.¹⁰ Meanwhile, the UK is replacing old components and connecting renewables as part of its £30 billion 'Great Grid Upgrade' by 2029.¹¹

These long-term and major capital investment projects may present potential opportunities for businesses that can provide the cables, interconnectors and transformers required for this huge modernisation effort.

For example, cable suppliers like Prysmian and Nexans are currently involved in many projects around the world, including sub-sea and offshore solutions, providing power connections for the infrastructure of the future.

Building tomorrow's world is not simply dependent on silicon and AI models. The energy sector has an essential role to play and the potential investment opportunities exist along the entire energy value chain.

Recognising the true value of energy

Energy has been described as 'the only universal currency',¹² given it is fundamental to the functioning of our world. This concept is apt when considering how AI is expected to transform the economy and society.

The vast amount of capital expenditure involved in deploying AI has been widely discussed. However, this typically focuses on the cost of chips rather than the amount of money needed for energy infrastructure to power them. At some point, the true value of AI's power demand will have to be recognised.

AI is not the only factor expected to reshape the global energy sector in the next few years. Rising wealth in emerging markets may also fuel increased power demand, and the pending transformation of the entire energy system from generation to transmission to adapt to the Age of Electricity is seismic in nature.

Rae believes that "the question for investors is: Are these forces adequately reflected in current equity market valuation?" He points to the fact that the combined weighting in the MSCI World Index of the energy and utilities sectors is only 6.5%, approximately half its level of a decade ago.¹³

Given the increasing reliance of innovative growth sectors such as AI, robotics and EVs on energy, it is questionable how long this apparent market ambivalence to the currency that makes it all possible can last. □

⁸ Wood Mackenzie, 'Gas turbine prices soar 195% as market faces supply-demand crisis', (woodmac.com), April 2026.

⁹ China Daily, 'China to invest 5 trillion yuan in power grid over next 5 years', (global.chinadaily.com.cn), February 2026.

¹⁰ European Commission, 'European Grids', (energy.ec.europa.eu), accessed September 2026.

¹¹ National Grid, 'The Great Grid Upgrade: what's happening and why?', (nationalgrid.com), accessed September 2026.

¹² Vaclav Smil, 'Energies: An Illustrated Guide to the Biosphere and Civilization', 1998.

¹³ Source: MSCI.com, M&G Investments, September 2026.



A test of nerves

The new anatomy of government debt

Government debt levels and interest costs have surged, but no fiscal reckoning has materialised. Harriet Habergham speaks to Purvi Harlalka and Eva Sun-Wai about shifting investor bases, financial stability and opportunities for bond investors.



Global public government debt amounted to \$111 trillion in 2025, equal to 94.7% of GDP.¹

Historically, foreign central banks and regulated financial institutions were the dominant buyers of many reserve-currency sovereign bonds. Today, a large portion of ownership has moved into private hands. The largest foreign owners of US federal debt by country are Japan, the UK and China. But other players have entered the scene: non-bank financial institutions (NBFIs).

In this article, we ask: how does this shift impact financial stability and what does this mean for bond investors?

The kindness of strangers

The 'marketable' US government bond (Treasury) market amounts to \$31 trillion,² the largest amount of debt ever amassed in history. One of the cornerstones of US economic policy has been the nation's ability to borrow at attractive rates – part of the its so-called 'exorbitant privilege'. For lenders, the fact that Treasuries are backed by the US government and therefore considered almost risk free has led to their position as the world's largest and most liquid sovereign bond market.

'Hedge funds alone now control 8.5% of the entire Treasury market, making them bigger players than Japan, China and Saudi Arabia combined.'

At the time of the Global Financial Crisis (GFC), foreign and private ownership of Treasuries was dominated by China and Japan, and their holdings formed a portion of their foreign exchange reserves. Since then, the share of Treasuries held by foreign official investors has declined steadily, with China's reported Treasury holdings falling by about \$400 billion between 2011 and 2024, even as the Treasury market grew.³

In contrast, the holdings of foreign private investors have increased. By mid-2025, foreign private holdings stood at about \$7 trillion, outstripping the \$3.9 trillion held by foreign institutions.⁴ Hedge funds alone now control 8.5% of the entire Treasury market, making them bigger players than Japan, China and Saudi Arabia combined.⁵

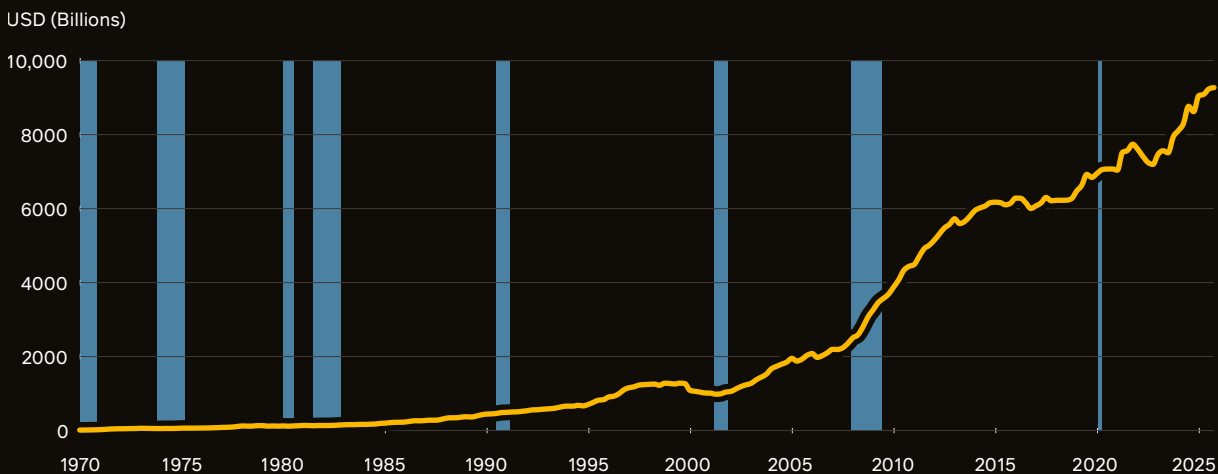
The US is not alone. By the end of 2024, NBFI assets reached \$260 tril-

lion globally.⁶ NBFIs have increasingly become a key source of government financing in the 30 largest economies as central banks have scaled back sovereign bond purchases.

Why does this matter?

Ultimately, the change in ownership makes the market more uncertain. The US has "less of a safe-haven status by default if its holders' focus is on value and they are more likely to switch at a dime", suggests Purvi Harlalka, senior emerging market sovereign debt strategist. She adds that "the private sector is going after profits, where the public sector is more invested in stability and security." This creates an entirely different environment and a Treasury market that is more vulnerable to shifts in global risk appetite and geopolitical downturns.

Chart 1: Federal debt held by foreign and international investors



Source: US Department of the Treasury, Fiscal Service via FRED®, June 2026.
Shaded areas indicate U.S. recessions.

¹Visual Capitalist, 'The State of World Debt 2025', (visualcapitalist.com), November 2025.

²Bipartisan Policy Centre, 'Bond market tracker', (bipartisanpolicy.org), July 2026.

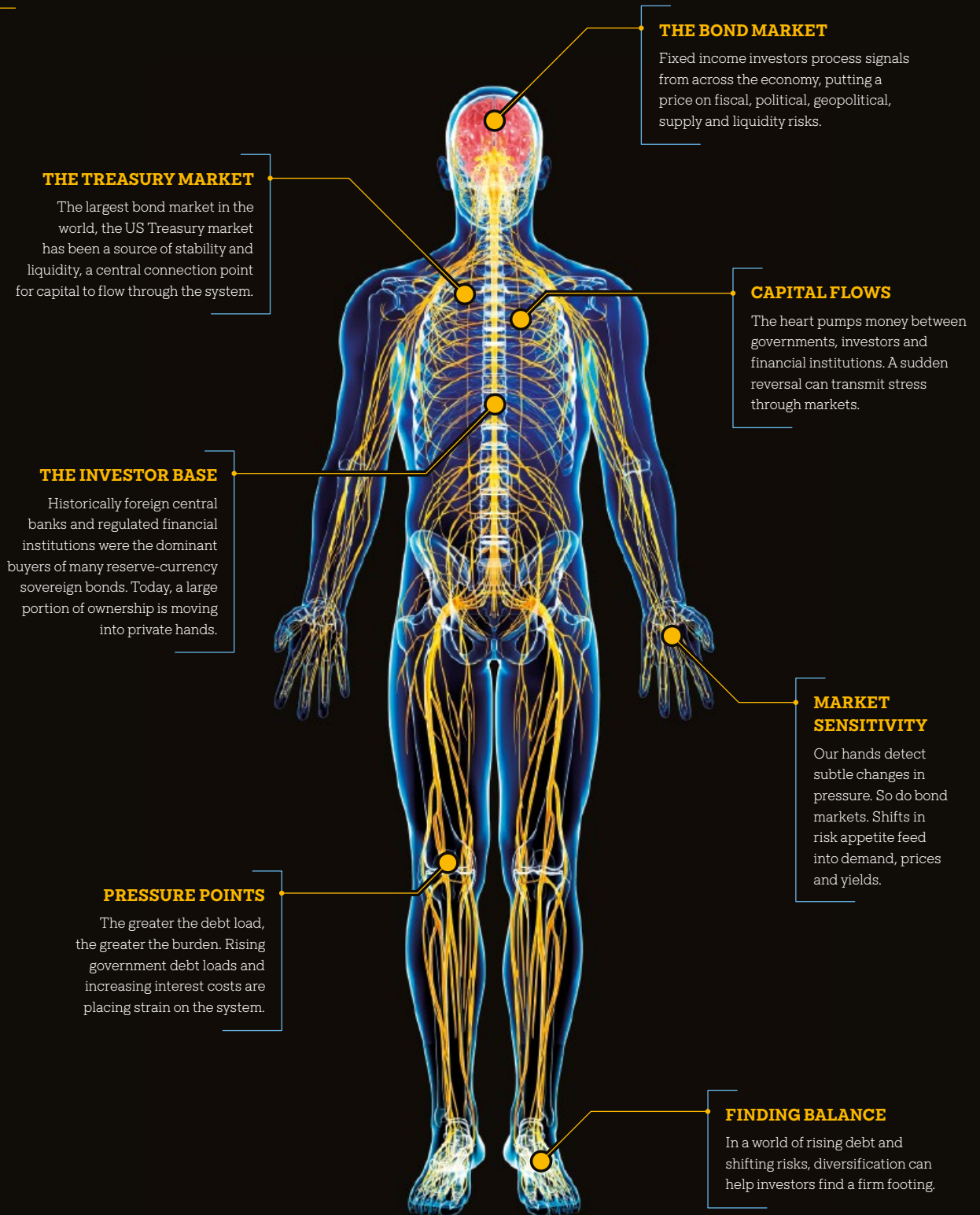
³Brookings, 'Who's buying US treasury debt and why?', (Brookings.edu), August 2026.

⁴Bipartisan Policy Centre, 'Bond market tracker', (bipartisanpolicy.org), July 2026.

⁵Federal Reserve, 'Decomposing hedge funds' US treasury exposures', (Federalreserve.gov), June 2026.

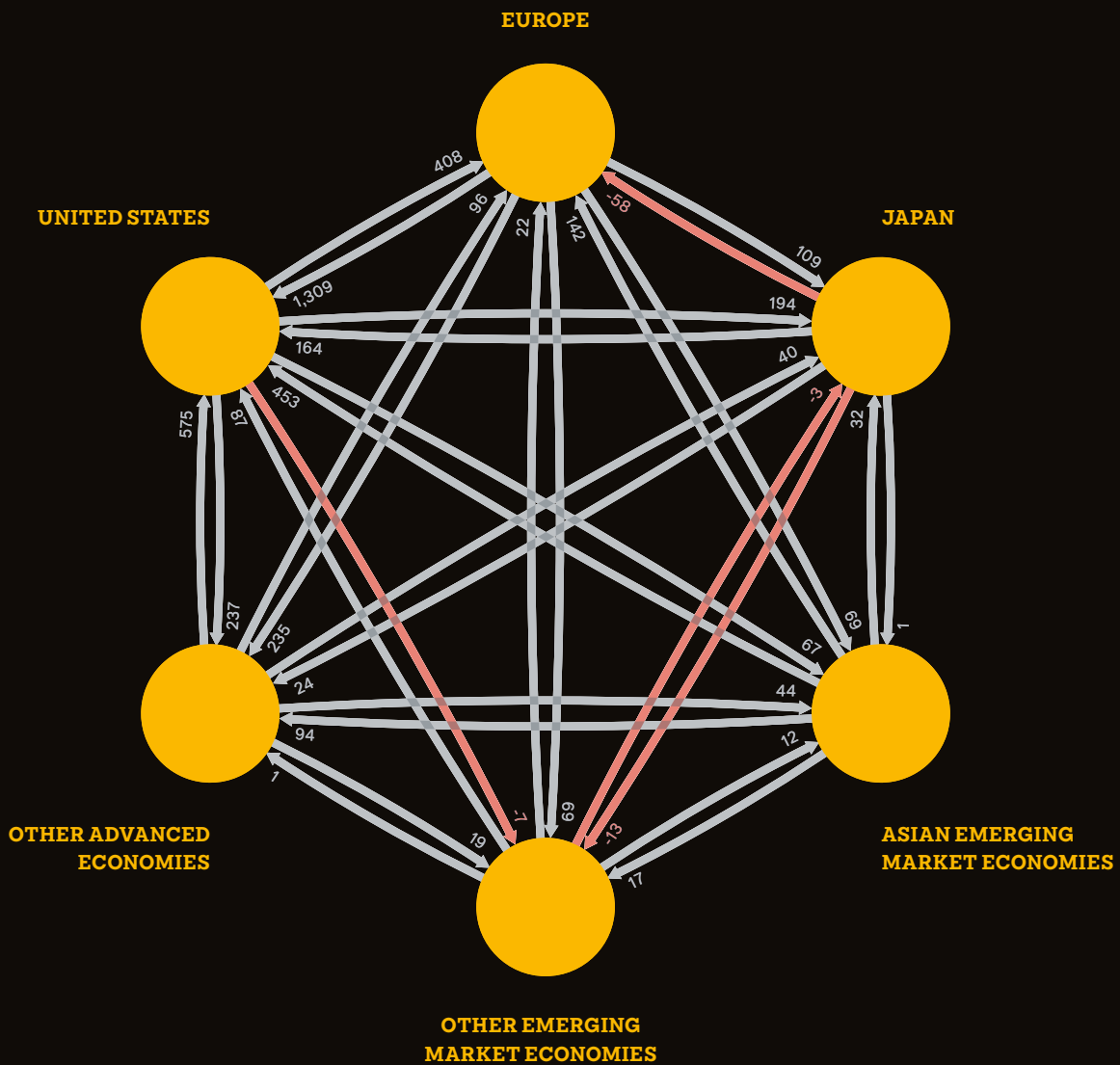
⁶Financial Stability Board, 'Global monitoring report on nonbank financial intermediation', (fsb.org), December 2025.

THE ANATOMY OF GOVERNMENT DEBT MARKETS



TRACING THE PULSE: GLOBAL PORTFOLIO FLOWS

CHANGES IN PORTFOLIO HOLDINGS, 2015–23 (USD BN)



Regions



Increase in holdings



Decrease in holdings

Source: BIS, 2025; IMF.

Historically, one major appeal of Treasuries lay in their counter-cyclical nature: when other markets fell, investors flocked to Treasuries which drove their yields down. For example, during the GFC, the 10-year Treasury yield fell to 2.25% in December 2008 as investors sought the safety net provided by a stable sovereign.

However, more recent crises and turbulent episodes have seen Treasury yields spike. We first saw the breakdown of this traditional dynamic in 2020. As the COVID crisis intensified in March 2020, Treasury yields spiked sharply, a move which can be largely attributed to a negative demand shock, rather than traditional causes such as increased default risks, inflation and illiquidity.

The cause was largely the sale of Treasuries by foreign institutions, mutual funds and the household sector (including hedge funds). These sales amounted to \$287 billion, \$266 billion and \$196 billion for each group respectively in the first quarter of 2020.⁷

The effect of this sale was quickly suppressed by Federal Reserve (Fed) Treasury purchases. However, this 'dash for cash' episode is emblematic of how an unwinding of Treasuries could occur in a crisis.

The Centre for Economic Policy Research (CEPR) has highlighted the persistent rise of US net external liabilities, as well as the country's unsustainable fiscal trajectory, the gradual loss of its exorbitant privilege and its dependence on private capital inflows intermediated by NBFIs as a key risk to global financial stability.⁸

Harlalka highlights the risk that as the private sector is invested in many areas of the market, a loss in one part of their portfolio could cause them to jettison the most liquid part of their portfolio – US Treasuries. She adds that the risk is exacerbated as these positions are often leveraged and can therefore be vulnerable to large forced unwinding. "This could destabilise markets far more quickly," she concludes.

'Just four economies, the US, China, Germany and Japan, account for roughly two-thirds of global imbalances.'

Rollover risk

The overall government debt level and shifting ownership of the debt are just parts of the problem. Growing interest costs are adding to the burden, with the US now spending over \$1 trillion a year to pay interest on its debt, triple the figure in 2020.⁹ Harlalka notes that as interest payments consume a larger portion of a government's revenues, the risk of a fiscal crisis increases.

Governments are responding by shifting to issuing shorter dated maturities. "It's classic – when a sovereign with high interest revenue ratio runs into trouble, its go-to tactic is to move to the shorter end – it's a stop gap, not a long-term solution," Harlalka says. She adds that having to rollover debt more frequently can cause a government to run into trouble if it finds itself unable to find buyers.

Historically it has been an emerging market (EM)-style problem to have to issue at the short-end to keep the show on the road, while "a hallmark of developed markets (DM) has been the ability to issue long-dated debt at low rates because investors have confidence in governments' ability to manage the economy over the long-term".

Imbalanced and unstable

A cornerstone of developed market policy is the continued appetite for global government bonds. If flows were to suddenly reverse, the situation would be exacerbated by the substantial imbalances upon which financial stability currently rests. Data from the International Monetary Fund shows that just four economies, the US, China, Germany and Japan, account for roughly two-thirds of global imbalances.¹⁰

According to Mark Carney, the former governor of the Bank of England, "From the Lawson boom to the Tequila and Global Financial Crises, a common lesson is that large current account deficits are one of the most trenchant early warning signs of financial instability."¹¹

He likened today's situation to the Great Depression of the 1930s when monetary policy was exhausted and fiscal policy was in abeyance. Meanwhile, the CEPR noted that global imbalances often end in financial crises.

Harlalka points out that when there is a period of adjustment, the burden often falls to deficit countries. Given the largest deficits are concentrated in some core economies, such as the US and the UK, markets could find themselves in uncharted territory.

Risks or opportunities?

Markets are not complacent about these risks. This year, government bond yields have been rising globally at the long end, with more term premium required. Fed policymakers have commented on this change, noting that the shift from relatively price-insensitive official-sector holders to more price-sensitive private investors "could have implications for the term premium component of yields".¹² Average bond yields across Group of Seven (G7) countries hit their highest level since 2008 in mid-August 2026.¹³

According to Eva Sun-Wai, fund manager of the Global Government Bond Strategy, the price dynamics reflect myriad considerations: "There are so many different factors in the valuation of a government bond. Investors do not put a price on fiscal risk alone, but they need a premium for political risk,

⁷ Bank for International Settlements, 'The Treasury market in spring 2020 and the response of the Federal Reserve', (bis.org), October 2021.

⁸ Centre for Economic Policy Research, 'The new global imbalances', (cepr.org), April 2026.

⁹ Council for Foreign Relations, 'The national debt hit \$40 trillion', (cfr.org), August 2026.

¹⁰ International Monetary Fund, 'Understanding global imbalances', (imf.org), April 2026.

¹¹ Bank of England, 'A fine balance', (bankofengland.co.uk), June 2017.

¹² Federal Reserve, 'Minutes of the Federal Open Market Committee', (federalreserve.gov), June 2026.

¹³ Bloomberg, 'Why high yields on government bonds are causing alarm', (Bloomberg.com), September 2026.

geopolitical risk, for term premium, for supply risk and for liquidity risk.” However, she notes, fiscal risk is becoming an increasingly important element and this is reflected in the elevated term premium. “Bond deals look more interesting now that curves are offering some roll and some carry as the steepness has come back into the market.” This marks a change from the 2021/2022 period when yield curves were inverted and investors couldn’t take advantage of tools such as roll-down, which is the return generated as a bond moves down the yield curve over time.

On a typical, upward sloping curve, longer dated bonds offer higher yields because they embed more term premium. For example, a 10-year bond has historically yielded more than a seven-year bond. After three years, that 10-year bond effectively becomes a seven-year bond. If market conditions are unchanged, its yield could ‘roll-down’ to the lower yield associated with seven-year maturity. This decline in yield results in a higher bond price. As a result, the investor may earn not only the coupon income but also a capital gain from the roll-down effect.

Where is the diversification?

With global risks rising and traditional safe havens being called into question, investors are inevitably looking for a new source of relative safety. Harlalka highlights that the recent multi-year rise in gold prices speaks to investors’ search for alternatives. “As a finite resource, it is stable but as an asset, it yields nothing – you are banking entirely on price appreciation”, she notes. In her view, “when there is no alternative safe haven, diversification is the safe haven.”

Sun-Wai highlights the opportunity to look across government bond markets for relative value. She points to Australia, where long-dated government bond yields are higher than those in the US and France despite Australia’s stronger credit rating and fiscal position. She also highlights countries such as Norway and New Zealand which, while differing in their own fiscal metrics, generally have lower debt burdens and stronger fiscal profiles than more indebted developed markets. Yet, their government bond yields remain broadly similar. From a fiscal risk perspective, these markets appear more attractive on a cross market basis. However, she adds “Is 5% ultimately good value for a bond? That’s a very different question and a much harder one to answer.”

This divergence in fiscal scenarios is not confined to developed markets. As a whole, emerging market (EM) debt has had to contend with non safe-haven status for longer, Harlalka points out. As a result, EM authorities have run policy accordingly and have strengthened their fiscal and monetary frameworks over the last decade.

Sun-Wai argues that historically EM debt was held by ‘faster money’, resulting in volatility in the instance of a risk-off event. But this is changing; the market is becoming less flighty as investors come to understand just how much diversification EM can offer. She adds that EM’s position is aided by its increased institutional credibility, its relative fiscal health and the responsiveness of central banks to crises, inflation, political and geopolitical events. “Investors are becoming more comfortable with the breadth and depth of EM debt as an asset class,” she notes.

The corporate conundrum

If sovereigns are issuing vast quantities of debt at higher yields, does that leave corporate issuers vying for buyers? Despite the resurgence of the ‘higher-for-longer’ narrative, spreads on corporate bonds haven’t significantly widened, as traditional market patterns might have suggested they would. In part, Harlalka argues, this reflects “confidence in the fundamentals of higher yielding markets”.

Sun-Wai notes that in some cases, individual corporate bonds can trade inside their sovereign equivalent, reflecting issuer-specific strengths or market dynamics. However, corporate bonds would generally be expected to compensate investors for additional risks, including default and liquidity. As she points out, “the mechanics of bonds mean that corporate debt remains at the mercy of the underlying government bond”: if the interest burden rises for the sovereign, it is likely to rise for companies as well.

Harlalka points to the new dynamic entailed in the massive amount of issuance by AI-related companies. She notes that “when investment grade-rated tech companies’ capital needs become so high over time that they are issuing multi-billion dollar deals every few weeks, they could start to compete with the sovereign market.” Hyperscalers alone are expected to issue \$317 billion of debt in 2026.¹⁴

The key question is whether markets are being sufficiently compensated for the risks they are taking. Rising debt levels alone do not cause crises, but how those debt levels are financed, their associated interest costs and the credibility of the policymaking that shapes their backdrop are instructive of the likelihood of a crisis. As those factors increasingly diverge across countries, diversification and relative value are likely to become increasingly important tools. ■

“When there is no alternative safe haven, diversification is the safe haven.”

¹⁴ Bloomberg, ‘JP Morgan boosts tech bond sales outlook as AI debt binge expands’, (Bloomberg.com), August 2026.

1931 CLUB



NOTES OF CEDAR, LEATHER
AND QUIET CONFIDENCE

BENEATH THE SURFACE



Private markets: An essential layer of economic infrastructure

Private credit is now one of the primary channels through which capital flows into the whole economy, financing companies, infrastructure, housing, trade, consumer assets and capital-intensive projects that traditional banks are increasingly reluctant or constrained to support.



For many years, private markets were described primarily through the language of portfolio construction: an alternative asset class, a source of illiquidity premia and a diversifier from public equity and bond markets. These descriptions still hold, but they no longer tell the full story. Private markets, and private credit in particular, are playing an increasingly prominent role as a parallel financing system.

That creates opportunity, but it also adds to the role of investors. If private credit is becoming more important to the supply of capital, investors are no longer simply buying exposure to an asset class. Through the managers they appoint, they are deciding which borrowers receive credit, on what terms, with what protections and at what price. They are assuming a more active role in the allocation of capital across the economy, and with it a greater responsibility to ensure capital is deployed with discipline.

This is not just a story about investors seeking higher yields. It is a story about the migration of credit creation itself. Private credit has become the destination where lending decisions are made, capital terms are negotiated and real-economy financing is delivered. For a growing range of corporate borrowers, typically, though not exclusively, small and mid-sized enterprises, the first call is no longer to a bank or to the public bond markets, but instead to a private lender. These private lenders have the potential to offer certainty, scale, confidentiality and a structure specifically tailored to the asset or business in question.

This is a functional shift in the plumbing of capitalism. Refinancing an acquisition, funding a battery-storage project, financing capital equipment, or funding a pool of consumer receivables? Today, the chances are that the capital supporting these activities has ultimately come from a pension fund, insurer, sovereign wealth fund or other institutional investor. Credit is still flowing to the economy, but the balance sheet behind it is changing.

The whole economy's new lender

In many parts of the economy, private credit is now increasingly the preferred or primary source of credit.¹ That matters because credit is not an abstract financial product. It is the mechanism through

which companies invest, infrastructure is built, inventories are financed, homes are purchased, goods move through supply chains and new technologies scale. If private lenders are now helping to finance the flows that keep the economy moving, then private credit has moved from the edge of the financial system and into its operating core.

Historically, the focus for private credit has been on the 'middle market' – companies too large, complex or acquisitive for relationship-bank lending, but too small or private to issue bonds efficiently. These businesses are, in our opinion, the 'real economy', the backbone of employment, services, manufacturing, healthcare, software and regional economic activity. Historically, their financing needs were largely met by banks; today, they are increasingly funded by private credit managers willing to underwrite bespoke loans, hold them to maturity and provide follow-on capital.

On a regional basis, this shift towards non-bank lending is accelerating faster in Europe than elsewhere. While in Europe 85% of corporate debt is still provided by banks, in the US, with its more mature direct lending/private credit market, this figure is only 50%.² However, this gap is closing: despite the US private debt market growing 10X since 2007, this has been outpaced by Europe, registering growth of 29X over the same period.³ This dynamic suggests the European market may prove more compelling over the longer-term.

Wherever the economy requires capital that is asset-based, long-duration, operationally complex or poorly suited to bank balance sheets, private credit has stepped in. It now finances, what is arguably, the backbone of the modern economy, from transport networks and data centres to renewable energy, housing and social infrastructure. These are not peripheral financial assets. They are the working assets of the productive economy.

For investors, its importance lies not only in providing a new source of return, but also in increasingly determining the availability, price and structure of credit for borrowers outside public markets. Private credit has become a transmission mechanism between long-term savings and productive investment. Institutional capital is being transformed into loans secured against companies, projects, receivables and hard assets.

¹Morgan Stanley, 'Evolution of Direct Lending', September 2026.

^{2,3}UBS, 'Structural shifts in Europe's credit ecosystem', June 2026.

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This has macroeconomic implications. Some focus has been on whether private credit is becoming 'bank-like' in a narrow regulatory sense, but the more important question is whether the economy's capacity to borrow, invest and grow is increasingly dependent on non-bank capital. The answer seems to be yes. Banks still matter, but no longer are they the sole gatekeepers of credit. Often they have become arrangers, distributors, warehouse providers or counterparties to a financing ecosystem in which credit risk increasingly sits with institutional investors.

The journey: From asset class to a new financial system

The growth of private credit has been striking not only in size, but also in breadth. Banks remain vital to the financial system, but their balance sheets are finite, regulated and increasingly expensive to deploy in areas requiring long-duration or bespoke capital. Private lenders have stepped in, with increasing volume, to fill the gaps.

Institutional investors have stepped in, with liabilities that are often better matched to long-term credit assets. Insurers, pension schemes and closed-end private funds do not face the same daily funding profile as deposit-funded banks, making them natural owners of illiquid, amortising or long-duration credit exposures. Crucially, it also means these investors are now deciding which real-economy borrowers receive capital, how that capital is structured, and what protections are required before it is deployed.

New lenders, new borrowers

The providers of credit are changing, and the range of financing needs they serve is expanding. Nowhere is this more evident than within digital infrastructure. The AI build-out is usually seen as a technology story, but it is also a financing story. Data centres need land, power connections, cooling systems, fibre networks and significant upfront capital. These assets have infrastructure-like characteristics: high initial investment, long operational lives and revenue streams linked to contractual demand. This makes them well suited to private-market structures in a variety of forms, including senior debt, mezzanine finance, hybrid instruments and equity-like structures.

This same dynamic is visible within energy transition. Grid upgrades, battery storage, distributed generation, renewable projects and transmission assets all require capital at a scale that government budgets and bank balance sheets may struggle to provide alone. Private credit can help bridge that funding gap, particularly where cash flows are supported by regulated returns and long-term contracts.

The wider asset-backed finance segment is another important frontier. Consumer receivables, auto loans, equipment leases, trade receivables, music royalties and other pools of contractual cash flows can be financed through structures that sit outside traditional corporate lending. This offers investors diversification and returns linked less to a single borrower's enterprise value and more to the performance of an underlying pool of assets.

For investors, the investment case is changing

Perceptions of the investment case for private credit have shifted. However, private credit has long been underpinned by a set of distinctive characteristics: an illiquidity and complexity premium, potentially higher yield, stronger covenants, tighter documentation control and lower market-to-market volatility than many public credit markets. These have been long-standing attributes, and they remain central to the appeal of the asset class. They help explain why private credit can offer investors access to income, contractual protections and risk exposures often difficult to replicate in more liquid or broadly syndicated markets.

What has shifted is the recognition of the specialised skills asset managers bring. Assessing borrower quality, structuring appropriate protections, evaluating collateral and enforcing documentation have always mattered. But as private credit supports a greater share of the economy's financing needs, the quality of those capabilities becomes increasingly consequential.

For investors, the private credit premium is no longer viewed simply as a reward for locking up capital. Increasingly, it represents compensation for assuming and managing risks that require highly specialised skills and capabilities.

What does this mean for portfolios?

This credit migration is leading investors to evaluate its impact on portfolio construction. The first implication is income. In a world where spreads on public corporate credit are tight and government bonds volatile, private credit appears alluring. It offers the potential for contractual income linked to loans, originated, negotiated and often held to maturity against a range of underlying assets. Its floating-rate structure further helps provide investors the opportunity to manage interest-rate sensitivity.

The second implication is diversification. Private markets are not automatically a diversifier: a portfolio of leveraged corporate loans may remain exposed to the same economic cycle as public high yield. But the broader private-credit universe offers exposures that may behave differently: senior infrastructure debt, consumer asset-backed securities, insurance-linked financing, receivables finance and other contractual cash-flow assets. These could reduce reliance on a single source of return and hence can offer a diversifying effect.

Finally, resilience. Private credit could provide stronger documentation, tighter covenants and greater lender control than public markets, but only when investors insist on those protections. The absence of daily pricing should not be confused with lower risk. Illiquidity has the potential to be a strength when it prevents forced selling, but it can also hide deteriorating fundamentals. Resilience depends on underwriting discipline before capital is deployed, not on the reporting frequency after the fact.

The risks of becoming essential

To offer balance, it has to be acknowledged that the success of private credit has introduced new risks. Its rapid ascent has led to regulators paying closer attention to it than before. As recently highlighted by the Bank of England, in any future financial crisis, the new unknown is the impact private credit will have – it simply wasn't 'a thing' last time around and is far less transparent than either banking or public bond markets. A downturn affecting borrowers, loan valuations or fund liquidity could create second-order effects across multiple parts of the financial system.

While these concerns may be understandable, in reality, unknowns should not automatically be equated with fragility. Most private credit is held in closed-end funds, backed by long-duration capital. These do not promise instant redemption, and managers are not forced to sell illiquid assets in falling markets. Further, while private loans may not have daily pricing, lenders receive highly detailed, borrower-level information not available to public bondholders. Private credit may appear opaque to outsiders, but it is arguably highly transparent to the investors bearing the risk.

The concentrated ownership of a private loan also creates a strong incentive for lenders to underwrite carefully and monitor diligently because they typically retain a direct economic interest in the credit they originate. More broadly, the growth of private credit reflects a dispersion of credit risk across a wider institutional ecosystem, rather than its concentration on leveraged, deposit-taking bank balance sheets. Long-horizon investors, such as pension funds, insurers and sovereign institutions can be well suited to holding certain forms of illiquid credit where exposures are appropriately underwritten, diversified and matched to their liabilities.

Seen in this way, the migration of credit beyond banks does not imply weaker risk discipline: it represents a broader distribution of credit intermediation across institutions with different capital structures, investment horizons and risk-management frameworks, in our view.

There is also a risk of crowding. When capital floods into a strategy, the terms available to lenders can deteriorate. In direct lending, this can appear through lower spreads, weaker covenants, higher leverage or more aggressive adjustments to earnings. We note here that European private credit is less crowded, and it is our belief that key risk and control metrics compare favourably with those in the more saturated US market.

Liquidity also matters. Institutional investors particularly are often well placed to own illiquid assets, but liquidity needs can change. Defined benefit pension schemes mature, insurers face capital or ratings constraints, open-ended vehicles need to manage redemptions. The implication for investors is to size allocations appropriately, match them to liabilities and avoid treating illiquid assets as if they were a substitute for liquid fixed income.

The bigger responsibility

The great credit migration is changing the role of investors because it is changing who funds the productive economy. Allocating to private markets increasingly could mean helping finance the physical and financial infrastructure of growth: the data centres powering artificial intelligence, the grids enabling electrification, the receivables supporting supply chains, the housing finance supporting households and the equipment loans that allow companies to expand.

That creates opportunity, but it also raises the standard required of investors. They must think less like passive allocators and more like long-term lenders. They need to ask not only what yield is available, but what economic function their capital is performing, how that capital is protected, and whether the return adequately compensates them for illiquidity, complexity and credit risk.

Private credit is not replacing banks, and nor should it. Banks remain central to money creation, payments, deposits and the functioning of the financial system. But the boundary between banking and asset management is shifting. Credit is no longer created only on bank balance sheets. It is increasingly originated, structured and held across a broader institutional ecosystem.

This presents a tremendous opportunity for private credit to play a powerful role channelling capital into the whole economy, supporting companies, infrastructure, energy transition projects and other productive assets.

Ultimately, the significance of private credit extends beyond portfolio construction, in our view. By connecting long-term capital with the businesses, infrastructure and innovations that drive economic activity, it has the ability to help finance real-world outcomes and potentially back the economy's future growth. □

**‘THE
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THE DEATH OF THE OFFICE OR THE START OF ITS SECOND LIFE?

Predictions of the office's demise rest on the idea that if people spend less time at their desks, offices will be worth less. Noura Tan, together with the M&G Real Estate team, looks beyond vacancy rates and office attendance patterns to examine how buildings adapt when the economic and social forces that once shaped them begin to change.





Few real estate sectors generate such contradictory narratives as the office. In the same week, investors can read about rising vacancy rates, shrinking corporate footprints and the supposed demise of the daily commute, while watching firms compete fiercely for space in the world's leading business districts. Ageing office blocks sit half empty across many cities, even as occupiers pay record rents for buildings capable of attracting talent and bringing people together.

Hybrid working, tighter environmental standards and advances in AI are widening the divide between those two outcomes. Across key western European markets, vacancy rates in central business districts generally remain between 2%–8%, while wider office space vacancy ranges from 6%–18%, reflecting a growing accumulation of ageing and unwanted stock beyond the urban core.¹ Paris alone ended Q2 2026 with more than 6.5 million square metres of vacant office space, roughly double pre-pandemic levels.²

Vacancy figures can create the impression of dwindling demand, yet much of what has changed is where that demand is directed. As AI and digital tools absorb more routine work, the office is increasingly reserved for higher value interactions that benefit most from people being together: knowledge-sharing, talent development, idea generation and decision-making. For investors, the question is how buildings will create value as the assumptions on which they were developed begin to change.

The office as a destination

Hybrid working has reduced the amount of office space many organisations require while raising expectations of the space they retain. Buildings conceived around fixed attendance now compete for a narrower place within the working week, judged on their environmental performance, convenience and experience alongside the more familiar considerations of location and cost. With offices below EPC B³ expected to become non-compliant in



**‘HYBRID WORKING HAS
REDUCED THE AMOUNT
OF OFFICE SPACE
MANY ORGANISATIONS
REQUIRE WHILE RAISING
EXPECTATIONS OF THE
SPACE THEY RETAIN.’**

¹ M&G Real Estate based on local broker reports, Q2 2026.

² ImmoStat, 'Market data', (immostat.com), July 2026.

³ The second highest rating on the UK's energy performance scale.

⁴ Real Estate:UK, 'BPF research on EPC ratings and commercial buildings in the UK', (realestateuk.org), February 2025.

⁵ Under France's Décret Tertiaire regulation, commercial buildings must progressively reduce energy consumption, with targets of 40% by 2030, 50% by 2040 and 60% by 2050, compared with a historical baseline.



3 AVENUE HOCHÉ

the UK in the next five years, and only 19% of London's commercial buildings currently achieving an EPC B rating or higher,⁴ sustainability has become a prerequisite for commercial relevance rather than a secondary consideration.

3 Avenue Hoche in Paris sits within that wider story. A short walk from the Arc de Triomphe, it occupies one of the French capital's most established business addresses, where appetite for premium space has proved resilient across repeated market cycles. The location has retained its appeal. Behind

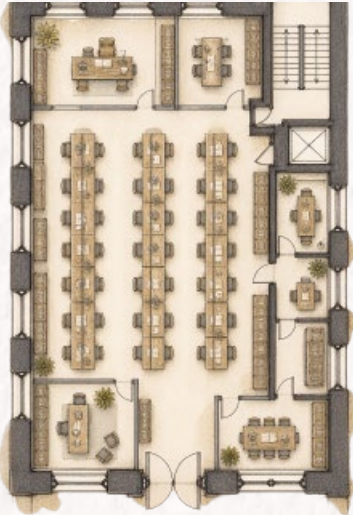
the façade, however, stood a building conceived in the 1970s, when employees typically arrived five days a week, energy consumption attracted limited scrutiny and amenities rarely stretched beyond the office floor itself. Its refurbishment captures how much that brief has changed.

An improvement in the building's EPC rating from E to C, and its alignment with France's *Décret Tertiaire* targets⁵ placed environmental performance at the heart of the project. The addition of a gym, food court and

bicycle storage also demonstrate how offices are increasingly expected to absorb functions that were once scattered across the working day.

Many of the world's most desirable business districts face the same tension where their addresses remain valuable, but the buildings occupying them were designed for working patterns that have receded. Refurbishment can preserve the advantages of an established location while bringing the space inside it closer to what modern occupiers require.

The evolution of the human office

	1900	1960	2000
	THE INDUSTRIAL OFFICE	THE CORPORATE OFFICE	THE KNOWLEDGE OFFICE
			
PURPOSE	OVERSIGHT Physical presence was often used as a measure of work.	COORDINATION The office became a hub for coordination and communication.	COLLABORATION Knowledge sharing became increasingly central to office work.
THE DOMINANT SENSE	 SEE Work was understood through what could be observed.	 HEAR Information increasingly travelled through conversations and calls.	 SEE + HEAR Knowledge was shared and teams solved problems together.

2025

THE HYBRID OFFICE



CONNECTION

The office became a destination rather than a requirement.



AWARE

Work extends across people, places and digital environments.

2040+

THE HUMAN OFFICE



HUMAN EXPERIENCE

As work becomes more digital, the office becomes a place for connection and community.



FEEL

Experience, culture and relationships play a larger part of the office's role.

As information becomes digital, human connection becomes more valuable



The office is not disappearing. It is evolving from a machine for managing work into a place designed for trust, creativity and shared experience.

When the best use is no longer an office

Not every building can be refurbished back into relevance, nor is office use always the most productive use of scarce urban land. As demand for workspace has become more selective, housing shortages have intensified across much of Europe. Housing completions fell by 10% in 2025,⁶ while permitting remains well below the level required to ease longstanding shortages.⁷ Many of the offices struggling to attract occupiers occupy precisely the places where new homes are hardest to build: established neighbourhoods close to employment, transport and amenities.

These dynamics intersected at One Vincent Square, a vacant 27,000 square foot office building occupying a prominent corner site overlooking Vincent Square in Westminster. With rare triple street frontage in a prime residential district close to the West End, Victoria and Pimlico, it sat within one of London's most constrained housing markets.

Changes to permitted development rights, which streamlined the conversion of offices into residential use, facilitated the transformation of the former office building into 26 apartments, supported by additional planning consents for balconies, terraces and façade enhancements. At a time when housing delivery in Westminster has fallen to a 10-year low, the project demonstrates how repositioning can unlock value by aligning an asset with the strongest source of demand in its surrounding market.

Research suggests that office conversions could create more than 50,000 homes in Paris⁸ and over 40,000 in London.⁹ Capturing that opportunity depends on recognising that the most productive use of a site is not fixed. Household formation, housing shortages, transport investment and shifting neighbourhood dynamics can all alter the role a location is best placed to perform.

From business district to mixed use ecosystem

What made One Vincent Square a housing opportunity forms part of a broader reorganisation of urban space. Although much of the post-pandemic office debate has centred on what happens inside buildings, many of the more consequential changes are unfolding in the streets and districts beyond them.

The daily commute once provided the organising rhythm of the central business district, sustaining a predictable ecosystem of retail, hospitality and transport. As attendance patterns become less regular, commercial districts are being reshaped around a broader mix of activities and reasons to visit.

Positioned where Sydney's commercial core meets its retail heart and transport network, 400 George Street occupies a stretch of the city that has already adapted to those changing patterns. The 30-storey tower stands on a section of George Street transformed from a traffic-heavy artery into a pedestrian boulevard served by light rail,



ONE VINCENT SQUARE



reshaping both the character of the precinct and how people move through it.

A redesigned lobby, cafe and expanded food offering sit alongside a new pedestrian route linking George Street with Sydney Arcade and Pitt Street Mall, drawing the activity of the surrounding district through the site itself. Shared meeting rooms, wellness facilities and upgraded end-of-trip amenities reflect the extent to which workplace, transport, retail and public space have become intertwined.

The building also sits within a market where the divide between prime and secondary space has widened sharply. In Sydney, the rental gap between those spaces expanded from around 30% in 2022 to a record 60% in the first half of 2026⁶, as occupiers increasingly favour high quality buildings. With stock removals and demolitions expected to outpace completions over the coming years, prime rents are expected to rise further. Against that backdrop, repositioning assets such as 400 George Street

can help future-proof buildings and capture demand where it is becoming increasingly concentrated.

Altogether, a modern office can no longer be understood solely as the space above its lobby, particularly when the rhythms of occupier attendance have become less predictable. The increasingly porous relationship between office buildings and their surroundings points towards a broader conception of workplace value. Rather than viewing the office as a self-contained destination, investors should consider how well it participates in the life of the district around it.

The office's second life

If the death of the office has been oversimplified, so too has the idea that all buildings share the same future. Patterns of work change, environmental standards tighten, housing pressures build and commercial districts evolve, creating different paths for different assets. 3 Avenue Hoche, One Vincent Square and 400 George Street fol-

low different trajectories because the forces acting upon them are different.

The future of office real estate will therefore be shaped by more than vacancy rates or attendance patterns. Value will increasingly depend on recognising where demand is heading, and whether a building is prepared to follow it. ▣

The buildings referenced in this article are held within portfolios managed by M&G Real Estate.

⁶ifo Institute, 'European construction to grow by 2% in 2026', (ifo.de), February 2025.

⁷Eurostat, 'Building permit index overview', (ec.europa.eu), April 2025.

⁸ORIE, 'What to do with the millions of square metres of obsolete space in the French region', (transformation-bureaux-logements.fr), February 2025.

⁹CBRE, 'FROM VACANCY TO VITALITY: Repurposing London's secondary offices for housing', (savills.co.uk), 2025.

¹⁰JLL, as of Q2 2026.

THE CONTRARIAN WAY: A GUIDE TO VALUE INVESTING

Shane Kelly

Manager of the M&G Global Strategic Value Strategy

Value investing may sound simple, but buying what others do not want can be uncomfortable and lonely. Shane Kelly, manager of the M&G Global Strategic Value Strategy, explains why discipline, patience and a team willing to be challenged are essential for contrarian investors. He also discusses why today's unusually concentrated markets and a broad spectrum of overlooked opportunities support the value equities team's view that the 2020s could be the 'decade of the cheap asset'.

The value playbook is appealingly simple in theory: buy a stock when expectations are depressed, wait for the market to recognise that reality is better than feared, and sell when the valuation recovers.

In practice, it is much harder. Buying what others do not want, when sentiment is manifestly negative, can be deeply uncomfortable. In a world where attention spans are shortening and patience is in limited supply, owning 'cheap stocks' without an obvious catalyst to re-rate can feel like a lonely place to be.

The importance of discipline

I take comfort from the fact that financial-market participants can be myopic. Investors can become carried away by a particular theme, leaving other parts of the market behind. What keeps us rational is the evidence, repeated through market history, that extreme misalignments eventually normalise. The timing is never certain, which is precisely why maintaining a consistent value discipline matters so much.

A disciplined process is also essential both to finding undervalued stocks and to building portfolios with attractive risk-return characteristics. Our starting point is deliberately sceptical: rather than looking for reasons to own a stock, we try to find reasons not to invest. Turning the question around helps us avoid companies that are cheap for good reason, the so-called 'value traps'.

We will never eliminate every mistake. Some unloved companies will experience further problems, which is why we build balanced, diversified portfolios. We are not relying on one or two heroic forecasts. We are assembling a collection of companies where, in aggregate, we believe the balance of risk and reward is skewed in our favour.

Value investors have a reputation for being pessimists. There is some truth in that. The job requires you to think hard about what can go wrong, particularly when a low valuation may be signalling a genuine problem. But useful pessimism needs to be paired with open-mindedness. You have to recognise when the market has become too gloomy and be prepared to act.

That is where being part of a team makes a real difference. Working closely with Richard Halle and Daniel White, who manage our European and North American value strategies, respectively, gives me two highly experienced colleagues who understand that discipline. Just as importantly, our conversations extend across M&G's wider equity team. We also talk to our fixed income colleagues to get a different perspective on relevant companies and investment themes.

Colleagues with different investment styles, sector expertise and perspectives challenge our views and help us avoid living in a 'value bubble'. Contrarian investing should never mean becoming closed to contrary evidence.



"YOU HAVE TO RECOGNISE WHEN THE MARKET HAS BECOME TOO GLOOMY AND BE PREPARED TO ACT."

Sticking to value through long periods of underperformance requires conviction, but it should not require dogmatism. The best team environment combines the confidence to take different views with enough humility to keep asking whether we might be wrong.

Decade of the cheap asset

While cheap stocks will always come with challenges, we believe several of the headwinds faced by value investors a decade ago have eased. We went so far as to suggest that the 2020s could be the decade of the 'cheap asset'. That reflected our belief that the market regime was changing. Inflation had returned, interest rates were no longer anchored at zero, globalisation was going into reverse, and the world was becoming less stable and more volatile.

These changes have forced investors to reassess many of the assumptions that prevailed in the 2010s. Those include the sustainability of businesses built around a zero cost of capital, the pathway to net zero, the organisation of global supply chains, and the prospects for capital-intensive industries in an environment of higher defence and infrastructure spending. In many cases, that reassessment began at a point of maximum tension, when valuation differences were already extreme.

The opportunity for value investors comes from a simple observation: when the world changes, the companies that prosper can change too. Different stocks start to do well and different stocks start to struggle. When valuation differentials have been stretched like a rubber band, a shift in expectations can produce a powerful snapback.

Six years into the decade, we have seen evidence of that reassessment, particularly in Europe. Yet we believe there is further to go as investors consider which companies may benefit from the rebuilding of supply chains and renewed investment in industries and markets that were previously neglected.

Geopolitical uncertainty also creates more frequent dislocations. We do not know where the next crisis will come from, but volatility can offer us the chance to buy what we believe to be fundamentally sound businesses at prices that reflect excessive fear. For a patient value investor, both the structural changes under way and the turbulence around them can be fertile ground.

Opportunities in overshadowed areas

One of the biggest conundrums for investors today is the dominance of technology. The sector represents a very large share of major global equity indices, while equity-market performance has become concentrated in a narrow group of companies associated with artificial intelligence (AI).

We have almost always been underweight in technology, but today that underweight is material and the largest it has ever been. That creates an obvious headwind when the biggest technology names lead the market. Yet sector exposure and stock selection are not the same thing. Despite the underweight, technology has been a significant source of alpha for us.

That outcome came from decisions that were difficult at the time. When excitement was elsewhere and parts of the technology supply chain were deeply out of favour, we held compa-

nies such as Samsung Electronics and Seagate. Both were exposed to cyclical areas where expectations had become depressed. There was no guarantee that sentiment would turn quickly, and holding them through the discomfort required patience.

We do not buy a stock because we think we can identify the precise catalyst for its success. We are more interested in good businesses where the valuation implies a bleak future and where reality is susceptible to positive surprise. In these cases, the acceleration in AI-related demand helped produce exactly that kind of surprise, supporting strong recoveries and meaningful stock-specific returns.

For me, the lesson is not that we should chase the dominant theme. It is that a dominant theme can cast useful shadows. Capital and attention crowd into the obvious winners, while other businesses, including some connected to the same underlying trend, can be overlooked or mispriced.

The AI trade can appear all-encompassing, but we invest globally and see many other developments creating opportunity. The challenge is to keep searching where others are not, rather than allowing the index, or the prevailing narrative, to dictate where we look.

Widespread value

Six years into the decade of the cheap asset, the world is certainly different. We cannot claim credit for forecasting the events we have lived through, from trade tensions to energy shocks. But some of the valuation extremes we highlighted have begun to unwind, and markets previously ignored by global investors, including Japan and South Korea, have reawakened.



Even after those moves, we believe the value opportunity remains significant and widespread. Europe is still priced against a backdrop of limited optimism. In Asia Pacific, there are businesses that have not participated in the AI-driven rally, while the governance and shareholder-return reforms under way in Japan and South Korea are, in our opinion, still in their early stages.

The US is perhaps the most striking example of the tension building beneath the surface. Market leadership has become exceptionally concentrated, while the valuation gap between the cheapest and most expensive stocks remains very wide. The longer that concentration persists, the more normal it can feel. But it also stretches the rubber band further. If expectations or market leadership change, the resulting effect could be enormous.

History reminds us that the companies defining one cycle do not necessarily define the next. Our opportunity set is therefore always moving. Some of the high-quality businesses that dominated the last decade have already begun to derate and move towards 'value land', while previously overlooked companies are improving and returning capital to shareholders.

Value investing begins with scepticism, but it does not end there. We spend much of our time asking what can go wrong because that is how we protect against permanent loss. Yet buying a cheap stock is ultimately an optimistic act. It is a belief that a company can endure, that reality can be better than feared, and that the market will eventually recognise the difference.

With the breadth of attractively priced stocks available today, continued global instability and the extraordinary concentration in parts of the market, I believe the opportunity for value remains substantial for the rest of this decade. Who says value investors are all pessimists? □



The Bond Vigilantes

BLOG TEAM



ANDREW
CHORLTON

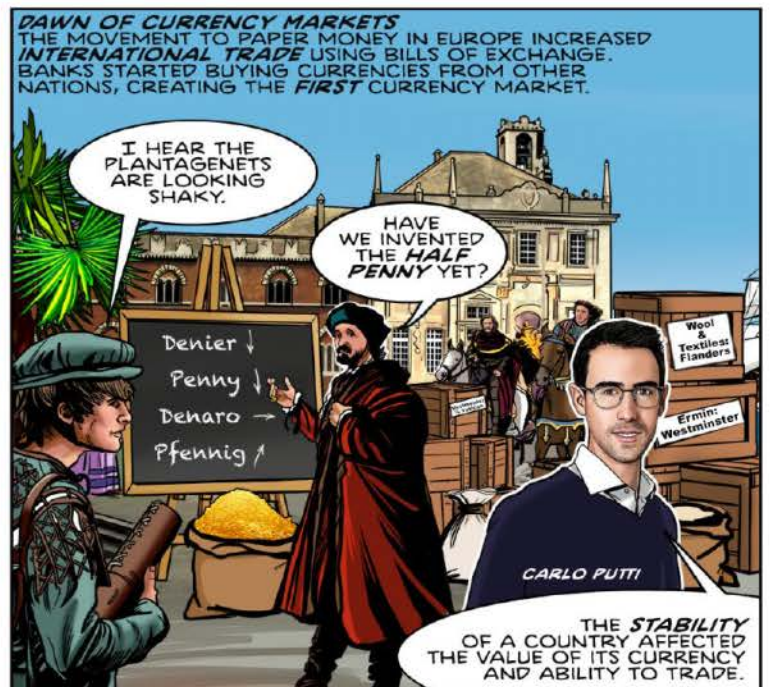
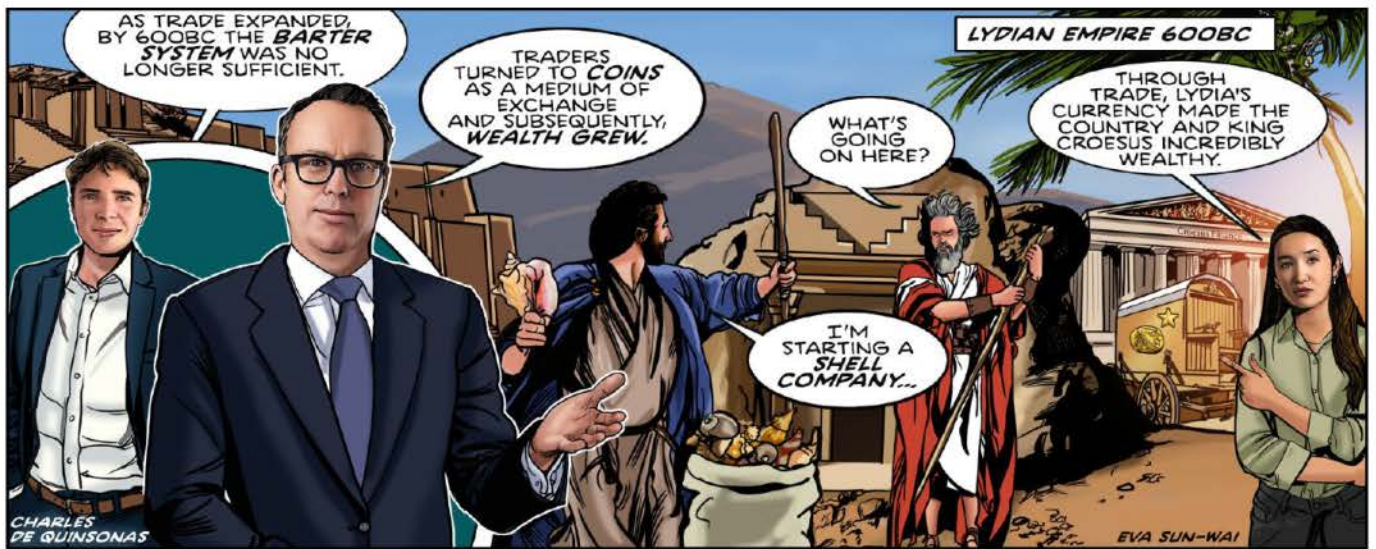
MONEY HAS
BEEN PART OF HUMAN
HISTORY FOR 5,000
YEARS, FROM SEASHELLS,
TO PAPER, TO A STRING
OF CODE.

ITS VALUE
IS ABOUT PEOPLE,
PERCEPTION AND
EXCHANGE.
NEVER MORE SO
THAN TODAY.

THE PERCEPTION GAME

HOW CURRENCIES ROSE, FELL AND
ENDURED, SHAPING ECONOMIES,
MARKETS AND INVESTMENT ACROSS CENTURIES.

EDITION 7



THE GOLD STANDARD

BEGINNING IN THE 1800S, THIS **TIED** A COUNTRY'S CURRENCY DIRECTLY TO GOLD, MEANING IT WAS BACKED BY A PHYSICAL COMMODITY RATHER THAN GOVERNMENT TRUST. HOWEVER, IN THE 20TH CENTURY, POLITICS, WAR AND ECONOMICS SAW THE GOLD STANDARD BECOME **REDUNDANT**.

RICHARD WOOLNOUGH

YOU WOULD NEED **AROUND 1M TONNES** OF GOLD TO COVER TODAY'S M2 MONEY SUPPLY. ONLY **220,000 TONNES** OF GOLD IS EVER THOUGHT TO HAVE BEEN MINED.

THE GREAT DEPRESSION OF THE 1930S RESULTED IN THE COLLAPSE OF THE GOLD STANDARD AS INVESTORS FLOCKED TO **WITHDRAW DEPOSITS**. TO STEM THE TIDE OF OUTFLOWS, THE US GOVERNMENT REVALUED GOLD TO SUPPORT ITS ECONOMY AND IN DOING SO, CORNERED THE WORLD'S GOLD MARKET.

THE BRETTON WOODS AGREEMENT

AFTER WWII, WESTERN POWERS DEVELOPED THE BWA, A FRAMEWORK FOR GLOBAL CURRENCY MARKETS. THE US GOVERNMENT PLEDGED TO CONVERT USD INTO GOLD AT A **FIXED RATE** OF \$35 AN OUNCE.

44 NATIONS PEGGED THEIR EXCHANGE RATES TO THE USD, MAKING THE DOLLAR THE WORLD'S RESERVE CURRENCY.

JACK RIDGE

KING DOLLAR

THE USD REMAINED KING THANKS TO DEEP FINANCIAL MARKETS, INSTITUTIONAL TRUST AND GLOBAL DEMAND. USD STRENGTH STILL SHAPES BOND MARKETS, INFLUENCING CAPITAL FLOWS, BORROWING AND INVESTMENT RETURNS. IN TIMES OF TURMOIL, INVESTORS HISTORICALLY **FLOCK** TO THE USD.

LOOKS LIKE THEY'RE ARRIVING FROM THE EAST?

GOLD OUT, MARKETS IN

BY 1973, THE BWA COLLAPSED AND COUNTRIES SWITCHED TO THE **FREE-FLOATING** FINANCIAL SYSTEM, ALLOWING EXCHANGE RATES TO ADJUST TO ECONOMIC AND MARKET DEVELOPMENTS.

EXORBITANT PRIVILEGE? FRENCH POLITICIAN **VALÉRY GISCARD D'ESTAING** COINED THE PHRASE, DESCRIBING A DOLLAR AT THE CENTRE OF THE GLOBAL ECONOMY.

KING DOLLAR STILL REIGNS BUT RISING DEBT, GEOPOLITICAL TENSIONS, LOSS OF INSTITUTIONAL CREDIBILITY AND THE RISE OF ALTERNATIVES COULD SLOWLY RESHAPE THE GLOBAL MONETARY ORDER.

FOR TOO LONG, THE US HAS HELD THIS **'EXORBITANT PRIVILEGE'**.

WHERE SHOULD THE NEW CENTRE BE?

PARIS!

BEIJING!

ALTERNATIVE WORLD?
IMPETUS TO REDUCE DOLLAR DEPENDENCE HAS INCREASED, WITH COUNTRIES SUCH AS THOSE IN THE **BRICS** ORGANISATION WORKING TO ESTABLISH AN ALTERNATIVE FRAMEWORK.

THE **DE-DOLLARISATION** TREND HAS GATHERED PACE AS THE US HAS BECOME INCREASINGLY PROTECTIONIST AND POSITIVE DEVELOPMENTS OUTSIDE THE US HAVE BOOSTED THE CREDIBILITY OF COMPETING CURRENCIES.

HUFF!
AND PUFF!

DECENTRALISED & DIGITAL
THE IDEA OF CURRENCY FREE FROM CENTRAL CONTROL IS NOT NEW.

FINANCIAL INSTITUTIONS, INTRIGUED BY **DECENTRALISED** DIGITAL CURRENCIES, ARE LOOKING TO STABLECOINS, BLENDING DIGITAL INNOVATION WITH THE RELIABILITY OF **RESERVE-BACKED MONEY**. THE US IS INTRODUCING A FEDERAL FRAMEWORK.

ROBERT BURROWS

BITCOIN
QUICKLY MOVED FROM A FRINGE EXPERIMENT TO A WIDELY TRADED CURRENCY. THE FIRST REAL-WORLD TRANSACTION TOOK PLACE IN 2010 WHEN 10,000 BITCOINS WERE EXCHANGED FOR **TWO PIZZAS** WORTH \$41.

SPECIAL OFFER

TWO LARGE DEEP CRUST
\$41 \$576,869,717*
*PRICES MAY VARY BY THE SECOND.

THE FX DRIVER
CURRENCY MOVEMENTS TEND TO BE VOLATILE. BOND INVESTORS IGNORE FX MOVEMENTS AT THEIR PERIL BUT THEY HAVE CHOICES - HEDGING CAN BE AN IMPORTANT TOOL TO REDUCE RISK.

Bond
Returns
→



FX IS A HIDDEN DRIVER OF **BOND RETURNS**. CURRENCY MOVES SHAPE CAPITAL FLOW, INFLATION DYNAMICS AND YIELDS. CURRENCY MANAGEMENT ALLOWS INVESTORS TO EXPRESS MACRO VIEWS, CAPTURE OPPORTUNITIES AND IMPROVE **RISK-ADJUSTED** RETURNS.

THE FUTURE

CURRENCIES HAVE EVOLVED OVER THOUSANDS OF YEARS, BUT MORE RECENT CHANGES HAVE SEEN THE MARKET **MOVE** AT PACE.

NEW TECH, SHIFTING GEOPOLITICS AND CHANGING TRADE PATTERNS ARE ALL PART OF THE STORY. FOR BOND INVESTORS, **CURRENCY** IS A KEY TOOL, AS WELL AS DETERMINING THE RISK PROFILE OF GOVERNMENT BOND INVESTMENTS.

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IN CONVERSATION WITH...

NADIA NIKOLOVA

CEO of responsAbility

A year into her tenure as CEO of responsAbility, Nadia Nikolova reflects on leadership, the evolution of impact investing and the expertise required to uncover opportunities across emerging markets.

It's been almost a year since you became CEO of responsAbility. Looking back on your career in private credit and infrastructure finance, what has shaped your approach to leadership and how has the conversation around impact investing changed over that time?

One of the most important lessons I've learned is that you need to listen. When you're trying to build something that isn't yet mainstream, success depends on understanding what various stakeholders, including investors, actually need and challenging the assumptions they bring to the conversation.

Twenty years ago, much of what we would now describe as impact investing in emerging markets sat largely within the world of development finance. Today, investors can look at microfinance, renewable energy or infrastructure and see compelling investment fundamentals in their own right. What was once driven primarily by intention is now increasingly supported by economics. For me, the next challenge is turning that growing conviction into investment solutions that institutions can allocate to repeatedly and at scale.

IN CONVERSATION WITH...





That shift from intention to economics reflects how significantly impact investing has matured. As the industry has evolved, how do you preserve the expertise that helped make that transition possible in the first place?

That is the real challenge. Scale matters, but expertise matters even more. In emerging markets especially, successful investing requires local presence and local knowledge. You need people on the ground who understand culture, regulation, risk and changing conditions because you'll often hear that something is happening before you see it in the numbers. That's very difficult to replicate from London or New York. That's one of the reasons I believe specialist expertise remains so important in emerging markets.

It's also important because we still talk about emerging markets as though they're a single investment story. They aren't. The opportunities in Latin America may centre on agriculture and natural capital, while in parts of Asia the focus is energy, infrastructure and population growth. The label is useful shorthand, but the opportunities themselves are local and contextual.

Much of your answer comes back to understanding what's actually happening on the ground rather than relying on broad assumptions. Yet much of the public debate around impact investing remains focused on terminology. Has the industry become too distracted by labels?

There's certainly been a lot of noise around ESG. I have always been a fan of understanding the value ESG and impact lens brings to the investment, rather than the label. In private markets, ESG and impact practices ultimately come down to value creation and risk management. If you invest in a business with weak governance or poor operating practices, you're more likely to lose money. It's as simple as that.

What I'm seeing is a shift away from labels and towards more practical questions. How is a business creating value? How is the manager engaging with it? What is actually changing as a result?

We worked with one agricultural business where improving conditions for seasonal workers led to better outcomes for employees while also strengthening the business. Retention improved, productivity increased and financial performance followed.

"What was once driven primarily by intention is now increasingly supported by economics."

Over time, I think we'll talk less about ESG as a distinct category because material ESG considerations will increasingly become part of good investing. At the same time, not every investment in a climate or social solution should automatically be considered impact investing. Intentionality and investor contribution still matter.

If the conversation is moving away from labels and towards value creation, the next challenge is translating that into investment decisions. What would help move institutional investors from interest to action?

I actually think the answer is simpler than people assume. One of the most powerful things investors can do is signal intent.

The Dutch pension industry is a good example. By making clear that it wanted exposure to impact investments, it encouraged asset managers to build expertise and new strategies to emerge. Demand created supply. Importantly, the objective was not to ask investors to accept lower returns or higher risk. It simply gave the market confidence to develop credible, investable opportunities at scale. For managers, that signal changes the question: what commercially viable propositions can we offer at scale to these institutional investors?

The same principle applies to blended finance, where success depends on trust and an acceptance that different investors will have different priorities. The manager's role is often to bridge those objectives and make them investable. Ultimately, though, it comes back to beneficiaries. When asset owners understand the outcomes their beneficiaries care about and translate that into clear mandates and portfolio requirements, capital is much more likely to follow.

Assuming more capital does begin to flow, where do you think investors are still underestimating the opportunity set?

I would say natural capital and food systems. At its core, it's a supply and demand story. We have a growing

global population, finite land resources and increasing pressure on agricultural systems. That creates opportunities across food production, logistics, waste reduction, regenerative agriculture and technologies that can improve yields.

I would also point to ageing populations. They will drive greater demand for healthcare, broader social services and infrastructure. These aren't simply social needs. They're long-term demand trends that will require capital and innovation.

More broadly, what gives me optimism is technology. The pace of innovation is extraordinary. In agriculture, we're seeing advances that can improve productivity far more quickly than before. In education, technology can expand access to high quality learning. In many markets, renewable energy has become cheaper than conventional generation.

The question for me is where Europe sits in that story. When I look at what's happening in Asia and the US, the pace of change is remarkable.

Throughout our conversation, you've touched on everything from technology and energy to food systems and global development. Outside your day-to-day work, what are you reading, listening to or thinking about that is shaping how you see the world?

Well, I have a young daughter, so I spend a lot of time thinking about what she'll need to learn in order to thrive in the future.

More broadly, I think a lot about the tension between increasingly local politics and challenges that are global in nature. Recently, I attended a conference in Amsterdam where one of the Dutch royals spoke about helping technology companies scale in the Netherlands. What struck me was how practical the ambition was. It wasn't about grand statements. It was about understanding what an ecosystem needs and helping make it happen.

That stayed with me. We often talk about global challenges, but solutions still start locally. The real task is helping the best ideas scale, and I think we need more leadership focused on exactly that. 

AMPER





A SENSE OF PERSPECTIVE

Markets make demands on all the senses. Prices flash, headlines scream for attention and opinions compete to be heard. To escape from the constant stimulation, we're giving our investors the chance to take a step back: by inviting them to share the songs and food they can't live without, as well as the market signals that make them sit up and listen.



Which sounds bring comfort? Which tastes evoke home? And, most interestingly perhaps, when the noise of the markets fades into the distance, what signals become clear? In an edition where we've translated senses into insights, we ask our investors to explore their senses to gain some perspective.



Richard Gwilliam
Head of Property
Research



Fiona Hagdrup
Head of Private
Corporate Credit



Michael Rae
Global Equities
Manager



Shane Kelly
Global Value
Equities Manager



Mason Woodward
Head of Investment
Solutions



Charles de Quinsonas
Head of Emerging
Market Debt

01

What song or piece of music helps you escape the world around you?

RG *'What a Wonderful World' by Louis Armstrong.* I've loved this song ever since first hearing it as a kid, and it will always hold a special place in my heart. It was the music for the first dance at my wedding, and despite my raspy tones being more grating than dulcet, I think each of my children enjoyed me singing it to them when they were little. The song causes us to cast our worries aside and realise that we're all very lucky to be here.

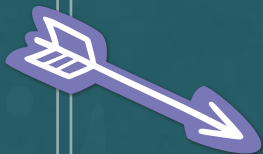
FH I sang in a Rock & Soul band for over 20 years. So... I daydream with bands that have gritty, distinctive female lead vocals, *The Pretenders, Fleetwood Mac, Blondie.*

MR I'm in charge of the music in the kitchen for approximately ten minutes each day, before the kids come in and put on Ariana Grande's new album, 'Petal'. I would choose things like American indie folk band *Beirut*, but, like I say, that doesn't get much airtime!

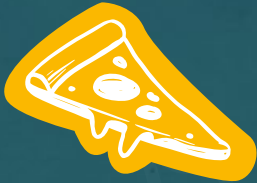
SK Nothing sophisticated here, it's usually some mix of mild rock – don't judge! On the more challenging value-investing days *'Here I Go Again' by Whitesnake* can often make it on the playlist – the lyrics can feel surprisingly relevant.

MW *'One Particular Harbour' by Jimmy Buffett.* As a sailor growing up on the East Coast of the US in the '80s, Buffett was a staple. The first time I listened to this song, it transported me to a place of peace. Older me has realised that if you are always seeking that 'one particular harbour' you are never going to find it. This song helps me appreciate the harbour I am in at the moment and everything great about where I am. I still love a sunrise from the deck of a sailboat, but not as escape.

CdQ *Moby's Play* is my favourite album.



02



What is your comfort food that makes you feel at home?

- RG** *Baked beans on toast*, with a splash of Worcestershire sauce, and grated cheese sprinkled on top – sublime! Just beware the fallout...
- FH** *Fresh bread* and far too much salty butter.
- MR** After years of near-misses, I feel I have arrived at the definitive home-made **butter chicken curry** recipe, so I would choose that. I'm lucky enough to have three discerning and highly-opinionated food critics at home who, invited or otherwise, will share their detailed feedback on my efforts. I find this important to keep my feet on the ground in case my comfort food becomes too enjoyable or comforting.
- SK** *Pavlova* topped with passionfruit and kiwifruit. A New Zealand original and something that always reminds me of home!!
- MW** Simple, a **classic roast dinner** – the smell through the house, cooking together with family, eating together – and the roast potatoes, the slow cooked roast, buttered cabbage connected by rich gravy. Basically the definition of comfort food.
- CdQ** The food that makes me feel at home is **boeuf bourguignon**, followed by marrons glacés.



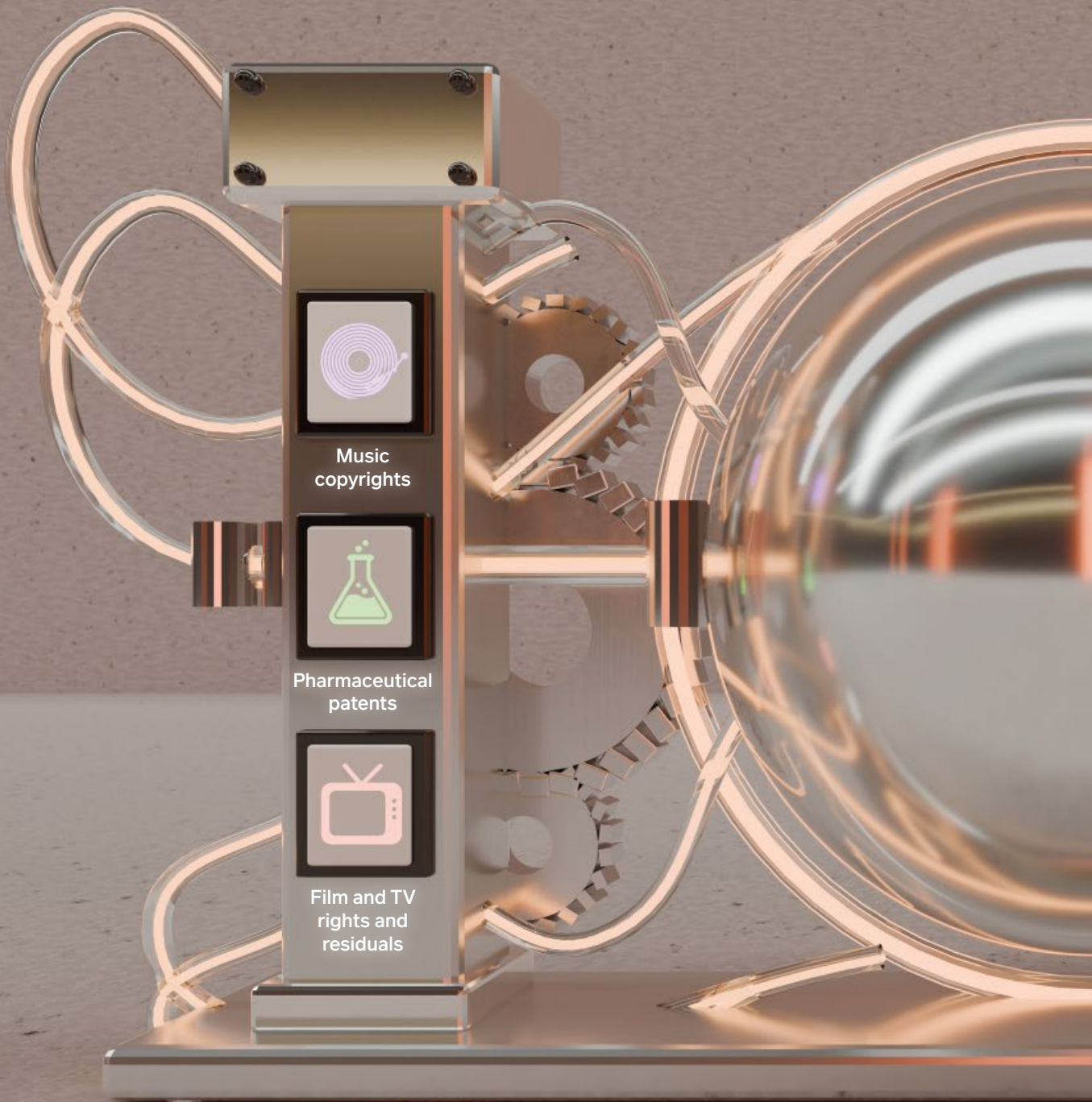
03



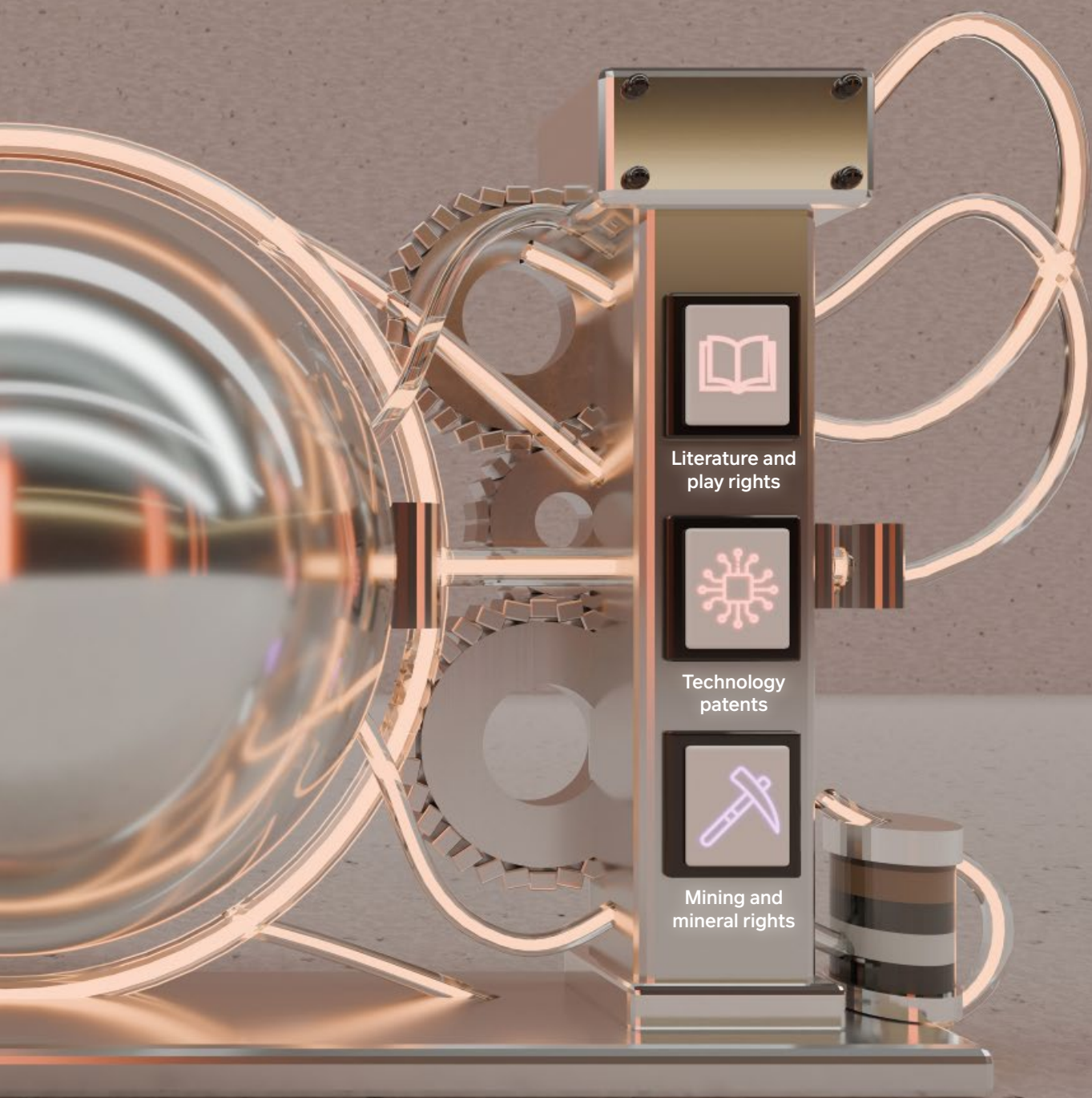
Which market signals are worth listening to and which noise do you tune out?

- RG** Because real estate is a long-term investment, short-term political and market volatility can be a distraction. Daily moves in equities and bond yields often come with narratives that imply more explanatory power for real estate than they warrant. More meaningful are signals that persist over time, particularly when they point to lasting shifts in occupier preferences.
- FH** The debt. More specifically, the cost and coverage. Debt is increasingly drowning out hubris.
- MR** From an energy perspective, X (Twitter) has become increasingly difficult to ignore this year. It's probably best treated as a weathervane, rather than a compass, but compared to a few years ago, it has become much more useful for interpreting events across the energy complex.
- SK** A lot of it is just noise. If there's one area I'll pay closer attention to, it's the bond market, as it can often be better at identifying underlying financial stresses.
- MW** To understand whether we are in a period of risk-taking or one that requires more caution, I watch signals that help identify the volatility regime and the level of market concentration. Coupled with good valuation anchors, I believe this is a sound foundation. Besides so-called 'news', the noise I try to tune out is price momentum, which can trigger fear and greed and undermine good investment decision-making.
- CdQ** It's worth listening to: what the elites don't listen to.
The noise I tune out: financial investors' opinions on (geo)politics.

ROYALTIES: EXPANDING THE PRIVATE MARKETS TOOLKIT



Private markets have grown well beyond the traditional domains of private equity, direct lending, infrastructure and real estate. As explored in the lead article, investors are increasingly searching for differentiated sources of return and greater portfolio diversification. One area attracting growing interest is royalties, which offer access to a broad universe of assets spanning music, film and television, life sciences, brands, technology and natural resources. So what sets royalties apart, where do the opportunities lie, and what role can they play in a diversified portfolio?



What makes royalties different?

A royalty is a right to receive a share of the revenues generated by an underlying asset – such as a music catalogue, a pharmaceutical product, a brand, a technology patent or a mineral resource. Investors can gain this exposure either by acquiring the underlying rights outright, as is common with music copyrights, or by acquiring a contractual entitlement to a share of the revenues an asset generates, as is typical of pharmaceutical or natural resource royalties.

A distinguishing feature of many royalty investments is that returns are driven primarily by the income the underlying asset generates over time. Unlike certain private market strategies in which much of the return is realised at exit, many royalty investments are substantially self-liquidating and distribute cash throughout the life of the investment. Investors may therefore be less reliant on favourable exit conditions or terminal valuations to achieve their target returns.

‘MANY ROYALTY INVESTMENTS ARE SUBSTANTIALLY SELF-LIQUIDATING.’

The royalties investment universe

Royalties are not a new concept. Creators, inventors, resource owners and other rights holders have long received payments linked to the use and commercialisation of the assets they own. Royalties are also part of everyday life: behind much of the music we listen to, the medicines we take and the brands we buy sits intellectual property that generates royalty income. More broadly, royalties arise wherever intellectual property – such as copyrights, patents and trademarks – or natural resources are commercialised under licence. Although royalties remain a relatively nascent allocation for many institutional and professional investors, M&G estimates that the addressable market exceeds \$2.5 trillion, highlighting the scale and breadth of the opportunity set.

Key sectors of interest

- Media and entertainment – income from music, film, television and other media rights, earned when content is streamed, broadcast, performed, licensed or sold.
- Life sciences – royalties on sales of pharmaceutical products and medical technologies, typically paid under patent licensing agreements.
- Brands and technology – income from the licensing of trademarks, brands and technology patents.
- Natural resources – payments linked to the production or sale of minerals, metals, oil and gas, or renewable energy.

Some royalty sectors are more established than others, but the market's continued growth reflects both the increasing use of royalty financing by asset owners and growing investor demand for differentiated return drivers and diversification.

Why investors are paying attention

Much of the investor interest in royalties stems from their potential to add diversification to a portfolio. Royalty cash flows depend primarily on the use of the underlying asset, such as how often a song is streamed, how widely a medicine is prescribed or how much a mine produces. These drivers are largely unaffected by shifts in interest rates, credit spreads or equity valuations and, as a result, royalty income has historically shown low correlation with the performance of traditional asset classes. Several royalty sectors, notably pharmaceuticals and music, are also relatively non-cyclical, as demand for medicines and music has tended to prove resilient through economic downturns.

Because royalty income is typically calculated as a share of revenue rather than profit, investors are largely insulated from rising operating costs and margin pressure. Where the prices of the underlying products or services rise over time, royalties can also provide a degree of long-term inflation linkage.

Royalty holders have a contractual right to the cash flows an asset generates but, unlike the coupons on a traditional fixed income instrument, those cash flows are not fixed: they can grow as use of the underlying asset

increases. It is this combination of contractual income and potential for growth that can give royalties the potential to deliver compelling returns with limited risk characteristics.

‘ROYALTIES HAVE THE POTENTIAL TO DELIVER EQUITY-LIKE RETURNS WITH CREDIT-LIKE RISK CHARACTERISTICS.’

In some royalty sectors, active management can also create additional value by increasing the use of an asset, aggregating complementary assets or identifying new commercial applications. In music, for example, songs can reach new audiences through placements in film, television, advertising, video games and social media. Existing copyrights can also earn additional income when reused in new releases, through sampling, which incorporates part of an original sound recording, or interpolation, which incorporates elements of the underlying composition such as melody or lyrics.

Duration is another important consideration. Depending on the asset and its stage of life at the point of investment, a royalty stream may have anywhere from a few years of income remaining to several decades. Pharmaceutical royalties typically run until the relevant patents expire or the product loses market exclusivity. By contrast, copyright in a song generally lasts for the lifetime of its writer plus 70 years. Natural resource royalties can last for the entire productive life of a mine or field. This range allows managers to build portfolios with a mix of revenue drivers, durations, and risk characteristics.

SEEKER MUSIC: ACTIVE MANAGEMENT IN PRACTICE

Seeker Music is M&G's dedicated music rights platform. Launched by M&G in 2020 and led by award-winning songwriter and music executive Evan Bogart, Seeker acquires, manages and develops music publishing rights and master recordings, combining institutional investment discipline with deep creative and industry expertise.

Its catalogue now comprises more than 19,000 copyrights and master recordings, including songs written or recorded by artists such as Beyoncé, Christopher Cross, Drake, Joan Jett, Lewis Capaldi, One Direction, Maroon 5, Miley Cyrus, Shawn Mendes and Justin Bieber, to name a few.

Seeker pursues an active management strategy designed to grow the income its catalogues generate over time.

Its creator-led approach includes working with songwriters, artists and producers to reimagine songs from its catalogue for new audiences, alongside licensing, social media campaigns and new visual content for older songs. One notable success is Shaboozey's Grammy-nominated 'A Bar Song (Tipsy)', which interpolates J-Kwon's 2004 hit 'Tipsy' from Seeker's catalogue and spent 19 weeks at No. 1 on the US Billboard Hot 100.

In 2026, Seeker closed its inaugural \$267 million asset-backed securitisation – a milestone that reflects growing institutional recognition of high-quality music rights as a long-term asset class. Fast Company also ranked Seeker second in its list of the Most Innovative Music Companies of 2025.¹

For investors, Seeker illustrates that royalties need not be passive income streams: in the right sectors, specialist managers can play a meaningful role in enhancing the value of the underlying assets over time.

¹Seeker Music, 'Seeker Music makes Fast Company's Most Innovative Companies 2025' press release.

Structurally attractive characteristics

Royalty investments could offer attractive income characteristics, with yields and risk profiles varying across sectors, asset types and transaction structures.

They are also underpinned by well-established legal frameworks, including copyright, patent, trademark and contract law. Protections vary by structure but may include security over the underlying asset, financial covenants and minimum payment provisions. Although performance ultimately depends on the ability of the asset to continue generating revenues over time, these features can provide a meaningful degree of downside mitigation.

The role of royalties in private markets portfolios

For many investors, royalties may serve as a complementary allocation within a broader private markets portfolio. They can be accessed through a range of approaches, from single-sector strategies, such as music, to diversified portfolios spanning multiple royalty sectors, asset types and vintages. Given the long-dated nature of royalty income, evergreen fund structures offering periodic, but limited, liquidity could be well suited to the asset class, allowing investors to build and maintain exposure over time.

As with any specialist private markets strategy, manager expertise, underwriting discipline and active asset management are key determinants of investment outcomes.

An increasingly relevant allocation

Royalties have evolved from a niche area of finance into an established and growing part of private markets. Their appeal lies in the combination of contractual rights to typical long-term income, differentiated return drivers and cash flows with low correlation to traditional asset classes. For investors seeking to broaden their private markets allocations, royalties offer access to revenue streams that are difficult to replicate through traditional public or private market investments, making them, in our opinion, an increasingly relevant addition to the private markets toolkit. □



QUESTION
CHALLENGE
THINK
LONG TERM





20

YEARS
OF INSIGHT
SINCE THE FIRST BLOG

BOND
VIGILANTES

20 YEARS OF THINKING AHEAD

DISCIPLINE
PATIENCE
PERSPECTIVE
PRINCIPLES



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