

May 2026

**Insight into Fidelity's
capital market assumptions**

**Between fragmentation and
the AI revolution: Investing in
a rewired world**

For investment professionals only.



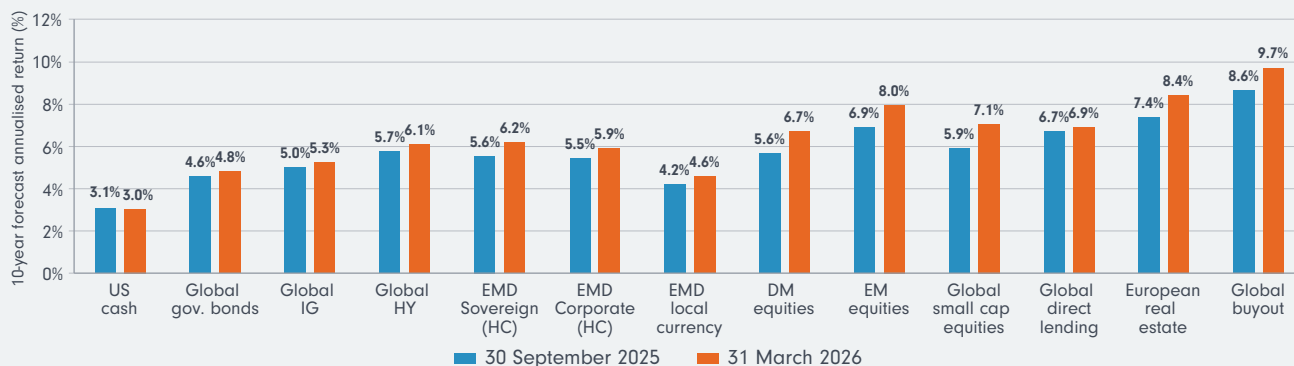
Executive summary

The below summary of expectations applies to our standard 10-year strategic capital market assumptions (CMA) forecast period, from the latest periodic six-month cut-off date of 31 March 2026:

- **AI:** We have developed a holistic framework that combines Fidelity's top-down macro scenario thinking with bottom-up analyst insights, captured regularly through our periodic Analyst Surveys. The weighted findings form our base case: somewhat higher long-term GDP growth. This is the first step in an ongoing process - we will evolve the framework as more data becomes available, focusing on labour impacts, investment dynamics, geopolitics and energy resilience.
- **Macro:** The effects of geopolitical fragmentation, elevated debt levels, and technological/energy transitions, will keep macroeconomic volatility above its average pre-Covid era level. Inflationary pressures will also remain elevated.
- **Equities:** Equities remains the key strategic portfolio growth driver. Expected returns have increased largely due to the positive effects of AI through the GDP channel. Profit margins remain above our forward-looking estimates across many regions in aggregate, even though their equilibrium level has shifted structurally higher, partly in reflection of the more innovation-driven environment. We will monitor our forecasts in this area closely as AI could create tailwinds and headwinds for profitability (e.g. through labour productivity gains / policy responses like taxation).
- **Fixed income:** Bonds remain attractive thanks to higher government yield curves, but bond market volatility and equity-bond correlations will remain elevated relative to the pre-pandemic era.. Expected credit returns are appealing, but tight spreads make risk/return trade-offs key. Short-term bonds are attractive shock absorbers and sovereigns should still diversify during recessionary shocks, although the latter may be less reliable during inflationary shocks.
- **Private assets:** Expected returns remain attractive for investors willing to take on more illiquidity risk. Manager selection will be key to delivering positive outcomes, especially due to the higher rate backdrop and elevated levels of dry powder. There are no clear signs of immediate stress in private credit, but the asset class warrants close monitoring.
- **FX:** The US dollar may not provide the same return tailwinds or safe-haven qualities as it has in recent decades.
- **Portfolio construction:** These dynamics call for a thoughtful active investment approach that incorporates greater regional/sectorial diversification and utilises a broader toolkit that includes tactical overlays, credit spectrum diversification, and differentiated sources of risk premia like absolute return or derivative strategies.

Figure 1: Aggregate long-term return potential remains attractive across asset classes

Projected ten-year average nominal returns, USD



For illustrative purposes only. Assumptions are based on proprietary modelling, reflecting the views of investment professionals at Fidelity International.

Source: Fidelity International, 31 March 2026. IG: investment grade; HY: high yield; EMD: emerging market debt; DM: developed market; EM: emerging market.

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A more fragmented world, an accelerating AI revolution



“The AI theme is best framed by weighting scenarios, given its interactions with geopolitics, energy security and labour-market disruption.”

Salman Ahmed, PhD - Global Head of Macro & SAA

The recent conflict in Iran is not an isolated shock, but another reminder that fragmentation is no longer a distant or theoretical theme for investors. Many of the rules, institutions and assumptions that characterised the previous decades can no longer be taken for granted. The institutional scaffolding of the previous era, from NATO in defence to the WTO in trade, still matters but no longer provides the same degree of certainty that it once did.

We have moved from a world shaped by the strength of politics, where cooperation underpinned defence, trade and capital flows, to one which is increasingly governed by the politics of strength. For markets, this is not simply a geopolitical observation, but a structural shift with implications for inflation, supply chains, policy volatility, risk premia, and the distribution of returns across and within asset classes.

Yet, markets continue to tell a more selective story. On the surface, resilience remains visible in growth, earnings and risk appetite. However, beneath lies a more fragile equilibrium, as geopolitical tension, fiscal pressure and a more transactional global order increasingly shape outcomes. In this environment, long-term investing becomes less about extrapolating the assumptions of previous cycles and more about understanding how structural change is rewiring the macro backdrop.

Accelerating AI revolution

Artificial intelligence (AI) sits at the centre of that rewiring. So far, it has been most visible in equity markets, where it has helped to drive capital spending, strong leadership from a narrow group of companies, and rising market concentration. However, its significance is broader than that. It is increasingly affecting the wider economy

through very high levels of both public and private investment, infrastructure build-out, and changes in corporate behaviour.

Crucially, we do not see AI as a force separate from fragmentation but increasingly embedded within it. Access to semiconductors, energy, data and critical minerals is becoming more strategic. Trade restrictions and export controls can shape the AI value chain as much as innovation itself, while AI's growing role in defence means that it is becoming deeply entangled with questions of national power and security.

At the same time, AI remains a complex macroeconomic issue rather than a simple profitability story. Its effects are unlikely to be linear, immediate, or evenly distributed. Beyond the technology sector, AI may reshape labour markets, alter the balance between labour and capital, influence productivity, and change how gains are transmitted through wages, prices and margins. This means that its implications cannot be gauged through a narrow sector lens alone; they will depend on adoption, market structure, policy choices and the extent to which productivity gains diffuse across the wider economy, rather than remaining concentrated in a small number of dominant firms.

Integrating AI into CMAs: An evolving framework

Our latest capital market assumptions (CMAs) aim to reflect this new reality. We continue to view fragmentation as a structural force and are beginning to incorporate AI considerations more explicitly, using a holistic framework that combines top-down Fidelity macro scenario thinking with bottom-up analyst insights captured regularly through our Analyst Survey. This will be a multi-year process, as AI is a complex theme with technological, economic and societal dimensions, and the evidence base remains incomplete. This edition therefore begins to integrate AI where the transmission channels are already relevant for long-term assumptions, starting with its potential implications for long-term GDP growth.

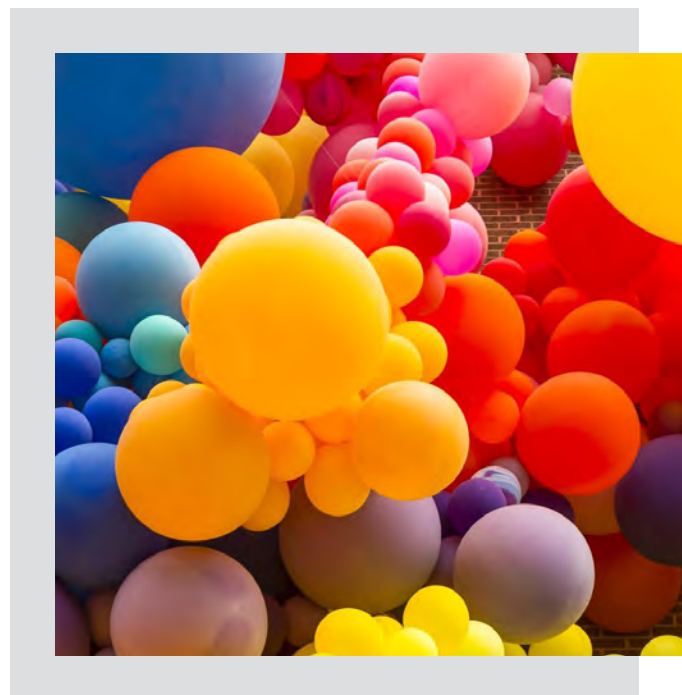
With this in mind, we plan to explore AI in greater depth in forthcoming papers. These will examine the key variables to watch in assessing the AI revolution, from energy demand to capital spending, and deliver scenario analyses showing how AI could shape labour markets, inequality and tax systems.

Macroeconomic implications: Uncertainty persists, while AI may gradually lift long-term growth

We argued in our [previous update](#) that inflation risks remained skewed to the upside and the pre-Covid regime of low volatility, low rates and synchronised expansion is unlikely to return. This was not because we were forecasting any single geopolitical event. Rather, it reflected our broader view that in a more [fragmented world](#) with weaker policy co-ordination, greater strategic competition, more contested trade routes and more active industrial policy, macro shocks are more likely to be larger, more frequent, and transmitted more quickly across commodities, supply chains and financial markets. Recent events have reinforced that judgement, leaving investors facing an environment in which macro volatility remains elevated, even if it does not always show up in markets immediately.

Fragmentation to help keep inflation and rates elevated

We continue to expect inflation to average above central-bank targets in both the US and the UK over the coming decade. Deglobalisation, supply-chain rewiring, tighter labour markets in parts of the developed world, higher defence and industrial spending, and a heavier sovereign debt burden all argue for inflation regimes that are structurally firmer than those seen in the post-GFC era. As a result, we believe that policy rates are likely to settle materially above pre-pandemic lows across most developed markets, helping to keep the level of yield curves higher than in the post-GFC period. Our ten-year average policy-rate assumptions are broadly unchanged in the US and China, while they have edged higher elsewhere (Figure 2).

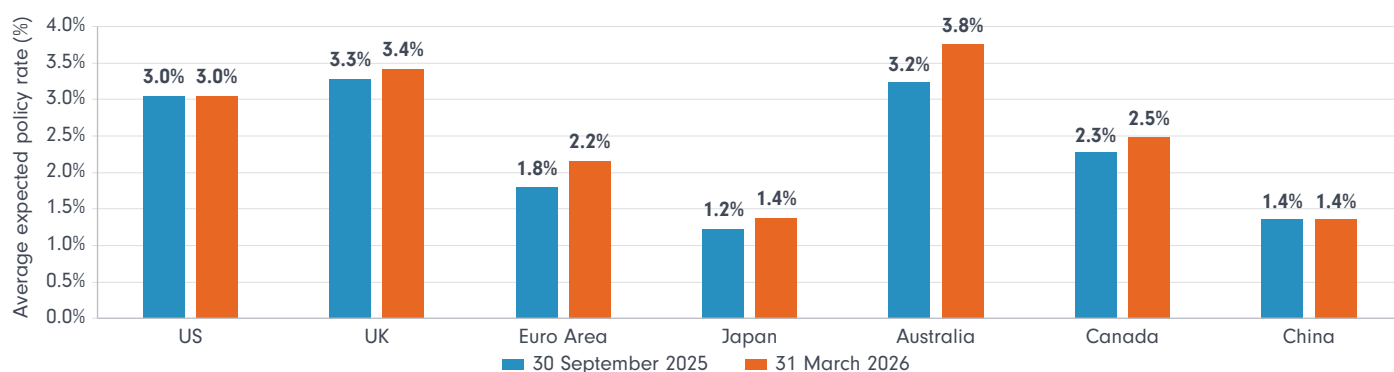


Expect uneven AI growth tailwinds and disruption

In terms of economic growth, we are now beginning to incorporate AI more explicitly into our real GDP assumptions, while remaining cautious about the speed, scale and distribution of the effect.

Our central view is that AI should be positive for global aggregate economic performance over time, but not in a simple, explosive or uniform way. The gains are likely to differ across economies depending on sector mix, labour-market structure, digital infrastructure, energy availability and the position each country occupies in the AI value chain. So, while the aggregate impact might be positive, we do not think it will be explosive, nor will it come without significant disruptions, particularly for the labour market.

Figure 2: Expectations of average long-term policy rates have increased



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Source: Fidelity International, 31 March 2026.

A recent OECD study¹ estimates that annual labour-productivity gains from AI over a ten-year horizon could range from 0.4 to 1.3 percentage points in the more AI-exposed economies, with gains up to 50% smaller in several others. There is however a key transmission question between labour productivity and GDP growth: hours worked. If AI boosts output per worker but also reduces labour demand or restrains hours worked, the lift to aggregate GDP may be materially smaller than the lift to productivity alone. The IMF estimates that around 60% of jobs in advanced economies are exposed to AI, and that roughly half of those could be negatively affected, while the rest may benefit through productivity-enhancing complementarity. In line with this concern, a recent survey of almost 6,000 executives across the US, UK, Germany and Australia finds that, while firms expect AI over the next three years to lift productivity by 1.4% and raise output

by 0.8%, it is also expected to reduce employment by 0.7%². For now, we therefore assume that only part of the productivity uplift from AI is transmitted into higher GDP growth in the countries we model.

The AI story cannot be simply reduced to chips, hyperscalers or a single national winner. It is a multi-dimensional macro theme entering an already complex system shaped by fragmentation, demographics and inequality. Its eventual impact will depend not only on model capability, but also on energy supply, capital intensity, workforce adaptability, skills formation, competition policy and the ability of tax and welfare systems to absorb disruption. This is only a first step in our modelling, and we will continue to refine these assumptions in our forthcoming research as harder macro evidence becomes available.

Framing AI uncertainty

Over the next ten years, AI outcomes can be framed through three scenarios: **high**, **mid** and **low**. These are not precise forecasts, but a way to structure uncertainty. Our current base case is a **weighted average** of the three, with different countries, sectors and social groups experiencing different versions of the transition.

High AI scenario

AI becomes a broad and positive productivity shock. Compute, energy, data and talent constraints are progressively managed, allowing frontier models to keep improving and diffuse across the economy. Governments and firms invest in digital infrastructure, electricity grids, reskilling and safety frameworks. Labour disruption is real, but managed through job redesign, new task creation, wage support, retraining and demand from new AI-enabled sectors. AI becomes a general-purpose technology, lifting productivity across services, manufacturing, science, healthcare, education, finance and government. Geopolitical competition remains intense, but does not fully fragment the technology stack.

Mid AI scenario

Adoption is significant but uneven. AI keeps improving, though less explosively than optimistic forecasts suggest. Energy, compute, regulation, organisational inertia and skills shortages slow diffusion. Some sectors move quickly, especially software, finance, media, customer service, drug discovery and professional services, while public services, small firms, education, healthcare delivery and regulated sectors lag. Productivity gains are meaningful but incremental.

Low AI scenario

AI remains powerful but destabilising. Labour disruption arrives faster than institutions can adapt, creating job losses, wage pressure and insecurity. AI becomes associated with inequality, surveillance, misinformation, concentrated corporate power and loss of control. Energy constraints, geopolitical fragmentation and backlash slow adoption. Populism rises, bringing pressure for higher corporate taxes, restrictive regulation and weaker macroeconomic gains.

Equities: Look globally for differentiated long-term capital growth opportunities



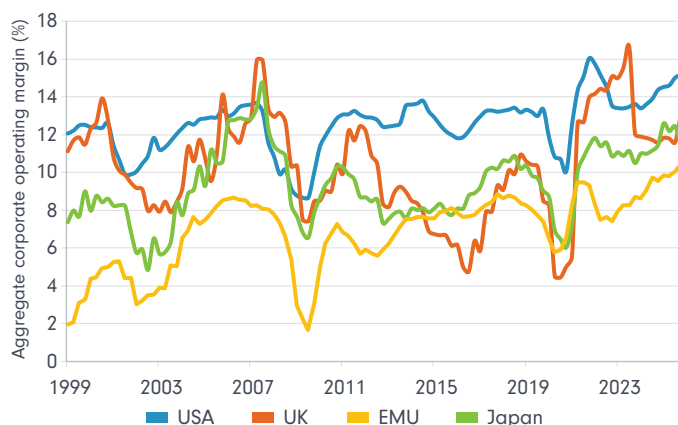
“Much of the recent strength in earnings has come from operating margins. The way that AI can reshape margins will be one of the key questions for investors over time.”

Edoardo Cilla, PhD - Director, Senior Strategist

As we argued in our [previous update](#), markets are increasingly driven by specific structural themes rather than by the broad economic cycle alone. This makes judgement on fundamentals more important than ever and strengthens the case for selectivity, but it does not weaken the case for equities in strategic asset allocation.

On earnings, and profit margins in particular, our previous update showed how the long tailwind from lower corporate taxes and interest costs had largely run its course. Since 2020, operating margins have instead done more of the heavy lifting across the major markets (Figure 3). This has left profit margins above our estimations of their long-term equilibrium levels, even though we view equilibrium levels as having risen above their historical averages due to how different today's structural conditions are from those that shaped margins in previous cycles.

Figure 3: Corporate operating margins remain above pre-2020 levels across key markets



For illustrative purposes only. Past performance is not an indication of future results.

Source: Bloomberg, Fidelity International, 31 March 2026.

AI effects should be monitored rather than extrapolated

AI is part of this, but not in a linear or uniform manner. Admittedly, profit margins could continue to surprise positively if AI drives a sustained improvement in productivity. However, the simple conclusion that higher productivity means permanently higher margins should not be assumed, as the relationship between AI, labour share and operating margins is complex.

Rather, margin effects should be monitored as key variables. For example, a lower labour share is only a first-round effect; in a general equilibrium, margin gains from AI can be competed away through lower prices, absorbed by higher depreciation and financing costs from AI-related capex, redistributed via higher wages for complementary workers, or partly offset by higher taxation of capital and profits. Just as importantly, if labour income weakens without any offset, revenues can come under pressure even as costs initially fall.

Equity valuation dispersion warrants selectivity and a granular view of fundamentals

On valuations, the picture remains differentiated. US large-cap equities continue to screen above our forward-looking equilibrium, although headline valuation metrics continue to conceal a more nuanced picture; excluding the so-called Magnificent 7 materially changes the market's valuation profile, reminding us that concentration remains one of its defining features. Meanwhile, several other markets now sit closer to fair value, including the euro area and both the UK and Japan, where scope for further valuation expansion appears more limited following strong rallies over the past year.

We note that broad market valuations are unlikely to revert meaningfully towards their equilibrium levels while earnings growth, cash-flow generation and balance-sheet resilience continue to validate investor optimism. Instead, elevated multiples could persist for longer than traditional mean-reversion frameworks might otherwise suggest. This is one reason why selectivity remains so important - even within a market that appears expensive in aggregate, there can still be segments where valuations are justified by healthy fundamentals and long-term earnings prospects. Equally, valuation compression need not be negative if earnings grow faster than prices. The implication is therefore not to disengage from US equities, but to access them selectively and with a sharper focus on fundamentals.

Expect higher long-term equity returns

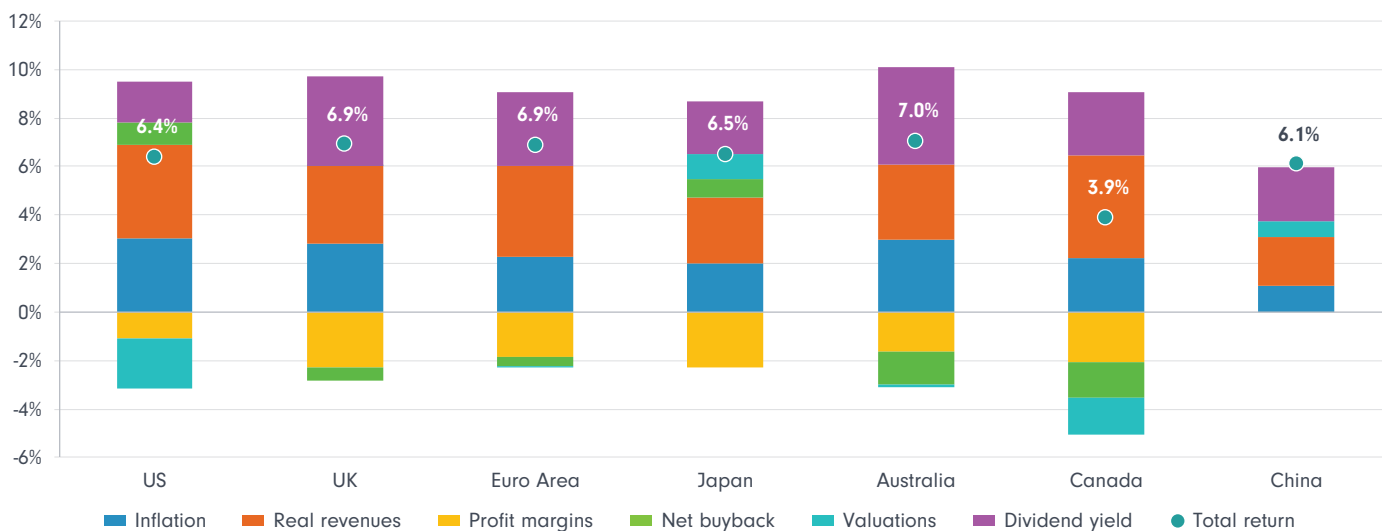
Overall, our expected returns on key markets are increasing primarily thanks to the role of AI in supporting revenue growth through the GDP channel discussed in the previous chapter (Figure 4). As such, we remain constructive on the role equities play in strategic asset allocation as a tool for long-term capital growth, including beating inflation.

That said, the opportunity set is increasingly one that requires selectivity. Outside the US, Europe’s renewed fiscal spending, continued reform and reflation in Japan, and exposure across Asia to the global AI value chain all point to opportunities beyond the most concentrated parts of the US market. At the same time, execution, policy and geopolitical risks remain material, reinforcing the case for diversified but fundamentals-driven exposure across regions, sectors and factors.



Figure 4: Differentiated equity return drivers across regions

Projected average annualised 10-year equity returns by component, local currency



For illustrative purposes only. Assumptions are based on proprietary modelling, reflecting the views of investment professionals at Fidelity International.

Source: Fidelity International, 31 March 2026.

Fixed income: Bonds remain attractive although selectivity is key

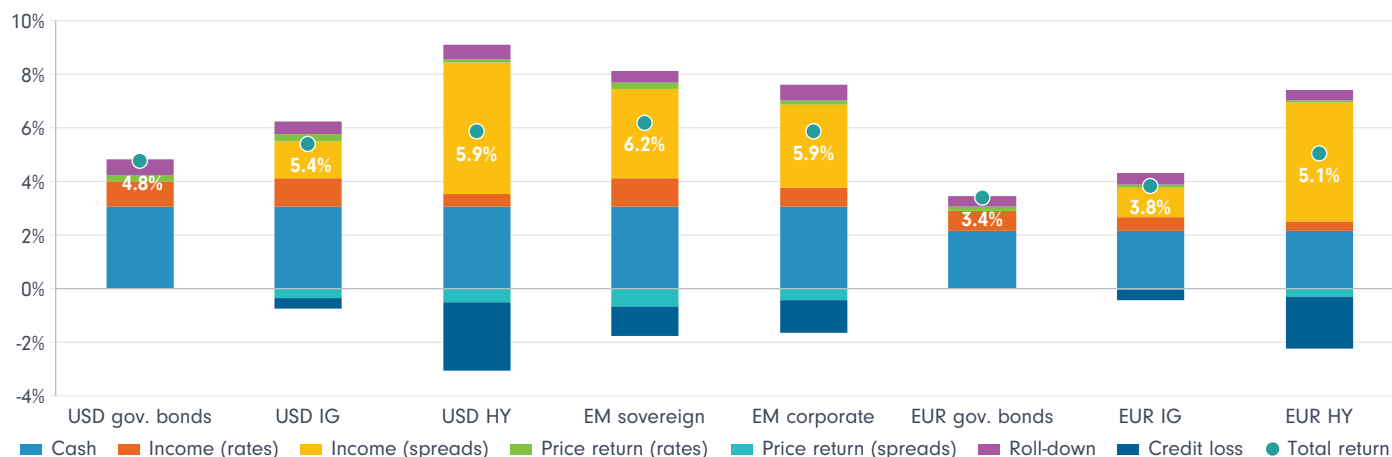
Yields have moved higher since our last update, particularly following the recent conflict. The increase has been most visible in Europe, the UK and Japan among the major markets, with 10-year yields rising around 40 to 60 basis points. Most of this move has been driven by higher inflation expectations and a higher term premium, in other words greater uncertainty around inflation and the future path of policy rates.

This is consistent with our broader macro view. Starting from our assumption of greater fragmentation, our research continues to point to a structural increase in term premia based on supply factors such as higher debt-to-GDP ratios, demand factors like the changing role of central banks in sovereign bond markets, and broader risk factors such as macro volatility. This marks a clear break from just a few years ago, when term premia were negative in some regions. It also aligns with a view we have held for some time that particularly in the US and UK, inflation is likely to remain above central bank targets.

Taken together, higher inflation and a higher term premium mean that yields are elevated today, but also likely to remain around these levels over the medium term. In other words, current yields are broadly in line with our forward-looking equilibria (Figure 5). This is positive news for bonds, because higher starting yields translate into higher expected returns. The trade-off is that investors need to be more active in managing duration risk, since inflationary shocks are now more likely.

Figure 6: Carry remains the main driver of expected fixed income returns

Projected average annualised ten-year fixed income returns by component

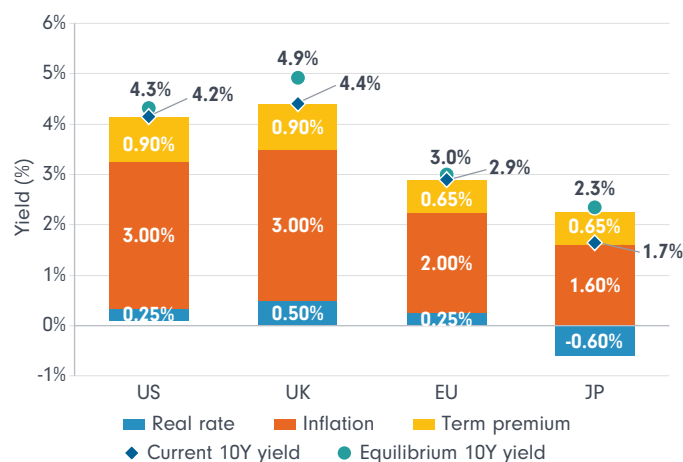


For illustrative purposes only. Assumptions are based on proprietary modelling, reflecting the views of investment professionals at Fidelity International.

Source: Fidelity International, 31 March 2026.

Figure 5: 10-year yields are close to our forward-looking equilibria

Breakdown of yield equilibria versus market pricing in major markets



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Source: Fidelity International, 31 March 2026.

Expected fixed income returns therefore remain attractive on a risk-adjusted basis, particularly in markets where starting yields are highest (Figure 6). Credit offers appealing carry, but spreads remain contained so returns should be weighed carefully against the risk of weaker growth. High-yield bonds tend to have lower duration than broad bond benchmarks, which can be helpful in an inflation-led supply shock such as that triggered by the war in the Middle East. So far, this shock appears to have raised inflation risks more clearly than it has damaged growth, although the uncertain outlook warrants caution.

Private assets: attractive long-term opportunities, with active selection increasingly important

Private assets continue to offer attractive compensation for investors willing to accept illiquidity in pursuit of higher long-term returns. That case remains intact, but selectivity is becoming even more important as private markets scale up and become more interconnected with banks, insurers and other non-bank lenders. Data gaps, infrequent pricing, semi-liquid fund structures and layered leverage all mean that risk can be harder to observe than in public markets. In this environment, the ability of managers to identify, structure and execute opportunities while maintaining discipline on leverage, liquidity and valuation remains the key differentiator of outcomes.

Global private equity (buyout)

We have revised our long-term return expectations for private equity upwards, primarily because the same forces that lift our public equity assumptions also support a higher expected return profile in buyout strategies. That said, the operating environment remains demanding. Competition for quality assets is still intense, with global buyout dry powder still high and broader pools of sovereign, corporate and private-market capital continuing to support elevated entry prices. Financing conditions have improved from the post-2022 shock, but leverage remains materially more expensive and less forgiving than in the previous cycle, limiting the scope for returns to be driven by cheap debt and multiple expansion alone. In this environment, manager skill in sourcing, underwriting and operational value creation should remain the key differentiator of outcomes.

European direct lending

European direct lending remains well positioned for investors with the time horizon and governance needed to harvest the illiquidity premium. Market activity has remained robust, even as competition has increased. Average direct-lending yields are still above public-market equivalents, even if the premium has narrowed from the unusually wide levels reached after the recent rate shock. That continues to support the view that carry remains attractive, but with less room for complacency on underwriting.

The private credit market in general has drawn greater scrutiny recently, particularly around software exposures and the increasingly complex financing of AI infrastructure. These are risks we are monitoring closely, but current fundamentals do not yet point to an imminent broad-based stress event. Rather, the key concern is a gradual build-up of structural vulnerabilities. The combination of opaque valuations, hidden leverage across borrowers, funds and end investors, growing semi-liquid vehicles, and deeper funding links with banks means periods of stress could become harder to diagnose and potentially more disorderly. Large AI-infrastructure financings are part of that story: off-balance-sheet borrowing structures are becoming more common, and Meta's \$29 billion private-credit financing illustrates how large and complex these transactions are becoming. That reinforces the importance of active selection through a robust framework.

European real estate

European real estate remains one of the more attractive private assets in our framework, but the investment case is now increasingly income-led rather than reliant on significant yield compression since long-term interest rates look set to remain elevated. That income case is reinforced by shortages of high-quality supply in selected segments and locations, which should help support occupancy and rental growth, particularly for modern, well-located assets. Performance is therefore increasingly likely to come from running yield, rental growth and active asset management. Selectivity across sectors, cities and assets should remain central to outcomes.

On AI, the implications for real estate remain mixed rather than one-directional. There is clearly supportive demand from AI-related occupiers in some gateway office markets, and demand for office space from AI companies is likely to rise. But the broader office effect remains uncertain and depends on how AI changes employment, utilisation and workplace strategy, not just on how much it lifts technology investment. In logistics, automation and AI can support efficiency and lower operating costs over time, but these investments can still be expensive and the benefits are likely to be uneven. For now, AI should be treated as both a potential tailwind and a source of uncertainty for real-estate demand, which again argues for selectivity at sector, city and asset level.

Investment implications: Rethinking diversification

Market behaviour since the 2024 US election has been highly informative of the ramifications of the ongoing shift towards global fragmentation. The tariff and Iran shocks can be seen as chapters of the same fragmentation story. The assessment of certain distinct periods can help guide investors through the current regime, which must be contextualised by the generally attractive asset class returns it has delivered, albeit with wide dispersion beneath the surface (Figure 7).

1. The Iran conflict

This has primarily represented an inflationary shock to date, from a market perspective. Equities fell initially but then rebounded, particularly in the US, while longer-duration bonds struggled as inflation expectations and yields moved higher. By contrast, short-dated bonds were far more resilient, underlining their role as a general shock absorber when inflation surprises matter again. High yield performed relatively better than government bonds once the initial risk-off phase started to ease, with lower duration, higher carry and sector composition providing support, while commodities excluding precious metals were among the best performers.

2. The tariff shock

The tariff shock was more recessionary or stagflationary in character and told a different story. Equities sold off more meaningfully, although non-US equities proved somewhat more resilient than the US. At the same time, government bonds and short-dated bonds offered some protection, albeit less powerfully than investors had become used to in the post-GFC era. It proved that sovereign bonds can still somewhat diversify recessionary risk, but they do not provide diversification across every type of macro shock.

Together with elevated ongoing macroeconomic risk, the vastly different consequences of these two market shocks demonstrate that diversification has become even more essential. However, ensuring it requires a differentiated approach as outcomes have become more conditional on the specific circumstances that surround each shock. Across public and private markets alike, active skill, forward-looking fundamental analysis, and the flexibility to adjust to shifting portfolio risk drivers have therefore become more central to delivering diversification and portfolio resilience.

Rethink exposures to capture opportunities while managing risks

Equities

Equities remain the main medium-term growth engine. For strategic investors, the implication is therefore not to reduce equity exposure, but to decide how to acquire it selectively. The global equity market remains concentrated, but leadership has broadened since the 2024 election, with global ex-US equities having outperformed their US counterparts. This makes it appropriate to diversify more deliberately across regions, sectors and factors, rather than rely on concentrated capitalisation-weighted strategies. We also reiterate that AI should not be treated as a simple one-way margin story; investors should seek to diversify their exposures across differentiated secular growth themes.

Fixed income

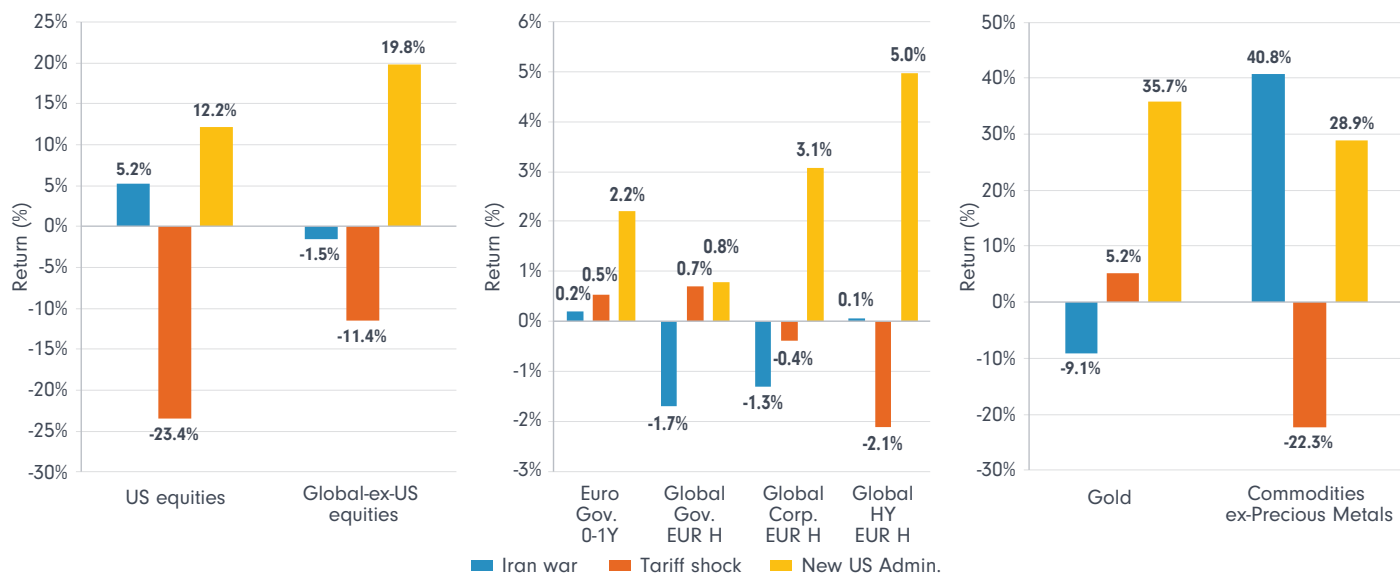
Bonds look more attractive as higher yields have restored long-term return potential, yet selectivity also matters more now within fixed income. Higher term premia and more volatile inflation mean duration needs to be managed more actively. In practice, this means distinguishing more clearly between the roles of different exposures: short-term bonds as shock absorbers, government bonds as recessionary hedges, and credit as a source of appealing carry, albeit one where risk-return trade-offs need to be assessed carefully.

Portfolio construction

A related implication is that investors may need to diversify their portfolio diversifiers. In an environment of higher inflationary volatility, geopolitical tension and a structurally less reliable negative equity-bond correlation, portfolio resilience cannot rely only on a simple 60/40 market cap framework. Moderate allocations to assets like gold can still help diversify geopolitical and monetary risks, while absolute return or derivative-based strategies can strengthen resilience when both equities and duration come under simultaneous pressure.

Figure 7: Diversification within and across assets can help navigate the new environment

Asset class returns and the effect of geopolitical/inflation shocks (in EUR)



For illustrative purposes only. Past performance is not indicative of future outcomes.

Source: Bloomberg, Fidelity International, April 2026. Total returns in EUR. "New US Admin." data from 1 Nov 2024 to date; "Tariffs shock" from 18 Feb 2025 to 21 Apr 2025; "Iran war shock" from 27 Feb 2026 to date. Latest date is 24 Apr 2026.



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