

## Ignore the 'AI Bubble' Talk (for Now)

Hani Redha, CAIA, Global Multi-Asset Portfolio Manager

There has been a surge of attention around the scale of investment flowing into data centers and AI. Since the arrival of ChatGPT, it has become clear that this is a genuine general-purpose technology, and it has already become a meaningful contributor to US economic growth. Without this wave of investment, US growth would look quite a bit weaker. Over the past few quarters, the composition of US growth has shifted away from its traditional anchor in consumption toward greater investment activity, led, above all, by technology. The scale of investment and its accelerating pace together are leading to a lot of "bubble talk" and comparisons with previous manias. So, are we on the verge of an AI bubble pop?

Let's start with the technology itself. AI models are advancing quickly, with capabilities in some domains already approaching industry-expert level. The length of tasks AI can do is rising exponentially, doubling every seven months. Given this progress, CEOs of the hyperscalers indicate that their goal is artificial general intelligence (AGI) – the ability of AI to operate at or above human intelligence in a wide range of domains – and they believe this goal is within sight. In their view, the risk of underinvesting is existential and far exceeds the risk of overbuilding, particularly given that this investment is being funded primarily out of equity and cash flow as opposed to debt.

We can draw two clear conclusions from these observations. First, the scale of investment is likely to persist for some time, given the progress currently being achieved and the prospects ahead; we're only three years into this capex upswing. In parallel, the risk of an *eventual* overbuild is rising given the hyperscalers' assessment of the asymmetric risk they face.

On the demand side, the acceleration is also extraordinary. Google reported 5,000% year-over-year growth in inferencing tokens as of April, which doubled again just months later, while Microsoft cited growth of around 500%. On balance, despite hyperscalers and chipmakers showing no sign of slowing capital expenditures, demand is already running *ahead* of capacity and leading to supply constraints. This doesn't strike us as a bubble-like setup at this stage.

While much of the discussion has been US-focused, China is working to catch up. Its approach tilts toward quicker, cheaper use cases, while US efforts are broader and more ambitious. So far we see little evidence that China is ahead in productivity or use cases, with most observers estimating a one- to two-year lag. Still, the Chinese hyperscalers are also ramping up their investment plans: Alibaba recently announced a \$53 billion capex plan over three years, only to raise this forecasted level again last week.

So what could derail these investment plans? In the US, power availability remains a key bottleneck. Regulators are beginning to push data centers and hyperscalers to shoulder a larger share of energy costs. From a credit standpoint, this introduces new risks, particularly around stranded assets. Balance sheets are starting to be levered up in anticipation of sustained demand growth. This may work in the near term, but over the medium term new supply will be harder to deliver, given turbine shortages, regulatory hurdles, and the higher cost of new builds relative to acquiring existing assets. That said, the fact that most of the investments are being funded from free cash flow, as opposed to debt, reduces the macro risks of this particular capex cycle.

The technology-driven theme and the scale of these investments inevitably invites comparison with the late 1990s and the internet bubble. Yet the differences are also striking. Valuations are roughly half the levels seen then, and this time around we see

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### About This Report

PineBridge believes that not only do differences of opinion make markets, but they also foreshadow substantial moves ahead as these differences are resolved. Once a month, investment leaders from our global multi-asset, equities, and fixed income teams meet to share their diverse viewpoints. This report reflects those discussions and debates by providing insight on the topic of the month along with snapshots of our asset class views and convictions across the firm.

that real use cases are already visible. Companies such as Meta and C.H. Robinson are already reporting tangible improvements in margins and revenues from deploying AI at scale, with exceptional returns on investment. Even if only a few dozen firms achieve this in the near term, competitive pressure will push adoption across industries. Supply constraints may slow the pace, but cumulative spending in the trillions is not irrational against a \$130 trillion global economy if the use cases are real and imminent.

Exuberance is undoubtedly in the air. Yet whether it proves *irrational* depends on how quickly those applications scale. And unlike in 2000, some of the most promising use cases could be only a year or two away given the current pace of progress. Overall, while an eventual overbuild and market crash are certainly possible, neither the pace of investment nor current valuations suggest to us that anything of the sort is imminent. Given the challenges of navigating periods of exceptional technological change, a dynamic and active investment strategy will be paramount to both earning returns and – critically – keeping them.

## Conviction Score (CS) and Investment Views

The Conviction Scores shown below reflect the investment team's views on how portfolios should be positioned for the next six to nine months. 1=bullish, 5=bearish, and the change from the prior month is indicated in parentheses.

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### Global Macro

**Sam McDonald**  
Sovereign Analyst, Global  
Emerging Markets Fixed Income

#### CS 3.25 (unchanged)

While the Federal Reserve's dot plot signaled two more rate cuts in 2025, with more uncertainty for the path into 2026, another month of soft non-farm payroll numbers in August shifted the Fed's perception of the risk balance in its dual mandate. Chair Powell characterized the September cut as a risk-management response to the weakness in the labor market. Nonetheless, risks around the inflation side of the dual mandate remain, with the gradual pass-through of tariffs on core goods still underway and service inflation remaining sticky.

The post-meeting statement after the Fed's 25 basis point rate cut, bringing the target range to 4.0%-4.25%, was revised to the dovish side but noted that inflation had moved up. The median dot on the plot indicates one cut next year and another cut in 2027. Governors Waller and Borman also voted with the consensus, indicating that independence may be more resilient than expected.

August non-farm payrolls increased by only 22,000, while the unemployment rate reached the highest level since October 2021. Labor demand has slowed, with the vacancies-to-unemployed ratio falling below 1, as highlighted by Powell's comment that the labor market is "really cooling off." Nonetheless, there are tentative signs of some improvements in other indicators, including continuing claims, which have fallen back from their peaks, and initial claims that were affected by fraudulent claims in Texas.

At 2.9%, the August Consumer Price Index was in line with expectations, and core goods inflation remained firm, but the most exposed sectors still showed a gradual pass-through from the tariffs. The momentum in shelter prices strengthened in August, while core services ex-rents fell month-over-month to 0.33% from 0.48%, although that was still firmer than earlier in the year. Despite inflation remaining sticky, the Fed remains reasonably confident that inflation expectations are still anchored.

With third-quarter gross domestic product tracking above 2%, positive revisions indicated that August retail sales were stronger than anticipated. Consumption in the third quarter is on target to have been stronger than expected. Business surveys also point to a more optimistic view of activity, despite weakness in the labor market.

Looking ahead to 2026, with the increases in the tariffs largely behind us and the impact of immigration cuts already under way, growth is likely to be marginally stronger, although not at the exceptional levels seen in recent years due to weakening of some supportive factors.

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## Rates

**Gunter Seeger**

Portfolio Manager, Developed  
Markets Investment Grade

CS 4.00 (unchanged)

Since the March meeting, when we changed our score to 4.0, the 10-year note is higher, at 4.14%. We maintain our bearish score and repeat what we said last month: This year has been incredibly volatile so far, and we see no reason for that picture to change; in fact, it may get far worse.

The tone of the market has changed significantly as the Fed has become concerned with the labor aspect of its twofold mandate of price stability and full employment. The Fed's 25-basis-point rate reduction on 17 September was said to be an "insurance" cut to balance out lower non-farm payroll numbers. The payroll weakness may be explained by several individual factors or a combination: a three-plus-sigma standard deviation correction of prior numbers, DOGE cuts, and/or AI productivity gains without the need for more labor.

Meanwhile, many signs – equities, gold, 30-year Treasury rates, home prices, and current inflation numbers – are all pointing to higher inflation. In addition, the highly anticipated "tariff" goods inflation may be just in its infancy, or the Fed may prove to be correct in its view that tariff inflation will be transitory and its impact will be a brief, one-off occurrence.

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## Credit

**Steven Oh, CFA**

Global Head of Credit  
and Fixed Income

CS 3.50 (unchanged)

Every credit asset class is participating in a game of global credit limbo in which each competes to see how low its spreads can go. Despite the occasional and idiosyncratic problem credit popping up, overall market risk sentiment remains firmly positive.

As expected, the Fed commenced its easing with a September rate cut, and market expectations are constructive for ongoing monetary policy accommodation over the next year. This past summer's pervasive theme – strong investor demand coupled with a buy-on-dip mindset – is poised to carry through into the fourth quarter.

Our view remains the same, and we will repeat what we said last month: There is a case to be made that the current tight valuations are warranted in the face of an accommodative fundamental backdrop of low but positive growth combined with tailwinds from monetary stimulus and the upcoming positive impact from stimulative fiscal policy actions. However, history would guide toward having a more cautious bias whenever valuations are approaching such tight levels. While we do not believe this is a market environment in which to become hyper defensive, we are trimming the highest risk/beta positions within portfolios and adding back an element of dry powder.

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## Currency (USD Perspective)

**Anders Faergemann**

Senior Sovereign Portfolio  
Manager, Emerging Markets  
Fixed Income

CS 3.00 (unchanged)

The resumption of Fed easing will undoubtedly weigh on the US dollar in the near term. However, easier financial conditions support a moderate growth recovery in 2026, likely avoiding a US recession. This suggests the market may be underestimating US growth and the persistence of US exceptionalism in the context of the dollar. As a result, cyclical fundamentals are gradually turning more US-dollar-positive, contrary to market consensus, leading us to adopt a neutral stance on the dollar.

The Fed has turned more dovish, pivoting toward employment protection and largely disregarding tariff-driven inflation – a shift toward a shortfalls-based approach rather than a traditional Taylor rule framework. This introduces an asymmetric risk profile favoring rate cuts. Additionally, growing political pressure on members of the Federal Open Market Committee (FOMC) to lean dovish – potentially undermining Fed independence – raises the risk of front-loaded monetary easing.

While the US dollar remains vulnerable to further losses, the improvement in cyclical and structural fundamentals presents a buy-on-dips opportunity, particularly if the US economy bottoms out faster than current market expectations. We reaffirm our baseline "soft landing" scenario, though we see risks stemming from the divergence between what the Fed "should do" and what it "will do."

Fiscal dominance may limit the effectiveness of monetary easing and contribute to a steepening of the US Treasury curve. However, the dollar's reserve currency status is not under threat. Market fears of capital flight, asset rotation, and a sharp rise in foreign exchange hedging ratios appear overstated, especially considering strong US equity market performance. Thus, structural concerns over dollar weakness may be exaggerated and could pave the way for a US dollar reversal in 2026.

Uncertainty around the Fed's actual policy path – particularly in contrast to what many believe it should ideally pursue – combined with a sharp divergence in monetary policy expectations between the Fed and the European Central Bank (ECB), may delay a full normalization of flows. This dynamic could continue to work against the dollar in the short term.

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## Emerging Markets Fixed Income

**Sam McDonald**

Sovereign Analyst, Global  
Emerging Markets Fixed Income

**USD EM (Sovereign and Corp.)**  
**CS 3.00 (+0.25)**

**Local Markets (Sovereign)**  
**CS 3.00 (unchanged)**

Emerging market (EM) spreads remain supported by expectations of looser financial conditions – both domestically and externally – consistent with our “soft landing” macroeconomic scenario. Spread widening has been largely confined to issuers facing idiosyncratic challenges.

The domestic macro environment is favorable for most EMs, and we expect sovereign credit metrics to improve throughout 2025. EM economic data remain robust, and external buffers show increases. Domestic conditions in most countries still support policy easing. Our expectation is that credit rating agencies will lift several potential rising stars to investment-grade status (including Azerbaijan, Oman, and Serbia) and upgrade ratings out of the CCC bucket for Pakistan and Nigeria. September was a busier month for primary issuance, surpassing sovereign issuance in September 2024 before the month was over. This followed a subdued August, in line with historical seasonal trends.

In corporates, nearly 80% of our coverage has reported second-quarter earnings. Results have been mixed. On balance, Latin America has shown a softer skew in results, largely due to weaker performance in Colombia’s oil and gas and petrochemical sectors. Primary market activity remained slow in August, with issuance totaling \$24 billion. September saw a busier primary market, with \$31 billion issued through mid-month. However, we believe the market will absorb the supply well given the higher scheduled cash flows, strong demand from EM and crossover investors, and resilient market sentiment.

Commodity markets are expected to stay in a favorable range for EM countries, as recently announced tariff levels remain manageable. External balances for many EMs have benefited from elevated gold and metals prices, with the trend largely expected to remain intact.

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## Multi-Asset

**Sunny Ng**

Portfolio Manager,  
Global Multi-Asset

**CS 2.75 (-0.25)**

Recent economic data offered a broadly consistent backdrop for our long-held “slowdown before reacceleration” thesis. Purchasing Managers’ Indices are now inflecting up, suggesting that 2026 growth is likely to reaccelerate. Inflation metrics continue to show clear evidence of the pass-through from tariffs into goods inflation, even if it’s coming more slowly than expected, and it is still likely to build through at least year-end (yet at a manageable level).

The FOMC’s widely anticipated 25-basis-point rate cut came with guidance for potentially two more cuts this year amid a reaccelerating economy. This aligns with the dovish pivot signaled at Jackson Hole, yet the market’s reaction underscored a hawkish undertone as the yield curve shifted upward and the dollar strengthened, all while major indices were upbeat, reaching record highs.

Nonetheless, the People’s Bank of China (PBOC) has been creating and channeling liquidity into China’s stock market as a policy response to boost consumer confidence while in the midst of an anti-involution push, reducing supply and price competition. It will attempt to hold liquidity at this high level until the Fed joins in with multiple rate cuts. That frees up the PBOC to provide more liquidity without destabilizing its exchange rate. Having two large central banks cut rates is generally favorable for most markets, though not necessarily the long end of bond markets, which, for the last year of increasing fiscal dominance, have sold off when their central bank eased.

Overall, we maintain our view that the economy is on a choppy path to reacceleration amid sticky but manageable inflation, and that AI will need to permeate beyond the Magnificent Seven companies for pervasive disinflation. We upgraded our Risk Dial Score, focusing on adding more cyclicity while pruning duration and using gold as a diversifier to navigate near-term volatility and to position for the anticipated productivity-led upswing by 2026.

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## Global Equity

**John Song, CFA**  
Research Analyst

CS 3.00 (unchanged)

Developed equity markets extended gains into mid-September, with US indices at record highs. The Fed delivered its first rate cut of the year and signaled further easing, while softer inflation and labor data reinforced expectations for additional cuts. The ECB held rates steady with inflation near 2% and projected to dip below target in 2026. The UK's Consumer Price Index remained steady, pointing to a gradual Bank of England path. Markets are pricing in a 2026 backdrop of lower rates and improved visibility, though policy and trade risks remain.

Sector commentary was broadly constructive. Technology firms cited resilient AI infrastructure demand, with semis and hyperscale suppliers reiterating strong pipelines. Industrials reported healthy backlogs but flagged tariff-related supply chain and pricing challenges and softer Asian demand. Financials were mixed, with European banks highlighting stable credit quality and capital-return plans, while US peers noted pressure on net interest margins as cuts begin to be felt. Consumer spending held up among higher-income cohorts, but there was continued stress at the lower end; staples continued to face margin pressure from input costs. Healthcare saw a modest rebound, with pharma focused on innovation amid pricing pressure and managed care signaling higher medical costs. Overall, commentary suggests that tariff absorption remains on track for 2026, with management tone supportive of continued earnings expansion.

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## Global Emerging Markets Equity

**Taras Shumelda**  
Portfolio Manager,  
Global Equities

CS 3.25 (+0.25)

Emerging markets have shifted to a mode where they largely ignore tariff risks and the corporate earnings outlook and instead focus on US interest rates. In the last three months, consensus earnings expectations fell 3% while the benchmark rose 7.9%. Such seemingly endless bullishness by investors is not well justified from a bottom-up perspective but may nonetheless prove vindicated if the rate cuts come in size. Forward price-earnings ratios on the MSCI Emerging Markets Index are now at a premium to historical averages; higher multiples were seen only during periods of near-zero interest rates. In our view, equity valuations for global emerging markets stocks are becoming stretched in the near term, at least until we begin to see positive earnings revisions. For that reason, we have changed our score to 3.25, even though the long-term case for emerging markets remains intact.

The White House appears to have abandoned practicable attempts to end the war in Ukraine and declared that it would sanction Russia only if NATO members, and not just European Union members, meet conditions that they are certain to miss. The terms appear designed to create untenable terms and to give an excuse for the US president to walk away from this conflict. The administration's non-reaction to the Russian attack on Poland seems to confirm that the US is abandoning Europe and Ukraine in the war against Russia.

In China, all eyes are on the government's attempts to fight the involution, trade talks with the US, and what seems like an upsurge in AI-related news by several large local companies. Of note is that these announcements are coming out as trade talks heat up. India-US trade talks are back on, but it is unclear how meaningful the progress has been.

Overall, this month has continued the prior month's themes, where geopolitics and top-down factors again overtook bottom-up developments as the main stock drivers. We try to position the portfolio in companies that are relatively isolated from top-down shocks and focus on the long-term outlook, which is admittedly a challenging task in this environment.

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## Quantitative Research

**Yang Qian**  
Fixed Income  
Quantitative Strategist

Our US Conviction Score improved last month. While credit spreads remain tight, the curve has steepened 21 basis points.

Global credit forecasts remain negative, with improvement in developed markets and deterioration in emerging markets. In developed markets, our model favors technology, industrials, banking, and capital goods. It dislikes utilities, basic industry, transportation, and insurance. Among EM industries, the model likes technology, media, and telecommunications (TMT), financials, and utilities. It dislikes real estate, industrials, and diversified industries.

Our global rates model forecasts higher yields for Switzerland, Japan, and Denmark and lower yields for Oceania, the UK, North America, and most of the euro area. The model forecasts a steeper curve in Norway, Switzerland, and the US and a flatter curve for other countries.

The rates view expressed in our G10 Model portfolio is overweight global duration. It is overweight the UK, France, Italy, New Zealand, Canada, and Spain. It is underweight the US, Japan, and Germany. Along the curve, it is overweight the six-month, 10-year, and 20-year. It is underweight the two-year, five-year, Japanese Government Bond seven-year, and the 30-year.



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