Flash Economics

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What structural changes in economies, and therefore in financial markets?

We believe that financial markets will be driven by developments stemming from the structural situation of economies. These are :

- the rise in general government deficits and the shortfall of saving relative to investment, which are leading to a rise in long-term real and nominal interest rates;
- disinflation resulting, in time, from the fall in energy prices after the end of the war in the Middle East, and from the adoption of artificial intelligence, which will allow short-term interest rates to fall and will imply a steepening of the yield curve;
- the very high level of investment linked to artificial intelligence, hence the strong growth in the revenues of hardware and cloud providers, and hence the continued rise in equity indices, driven by technology stocks, in the United States and in Asia (Korea, Japan), albeit with high volatility linked to uncertainty over the future profitability of artificial intelligence;
- the rise in political risk in Europe (particularly in France and the United Kingdom), hence the underperformance of European equity indices and the rise in European long-term interest rates.

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First structural change: a rise in long-term real interest rates

We are currently seeing :

- **a widespread rise in general government deficits** (**Chart 1**). In Japan, the Prime Minister has taken measures to stimulate consumption (a cut in the consumption tax, transfers to households) that will increase the government deficit from 2026 onwards;
- **a rising investment rate**, particularly in the United States (**Chart 2**).

Chart 1
Budget deficit (% of GDP)

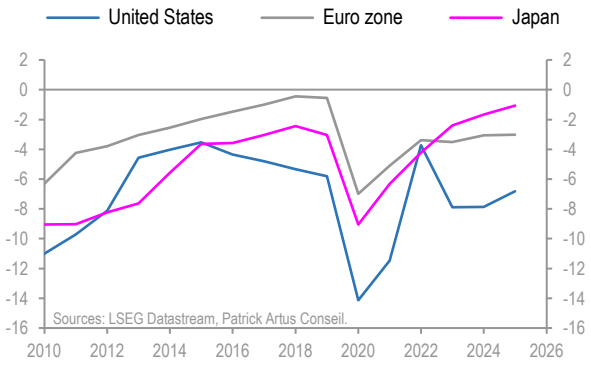
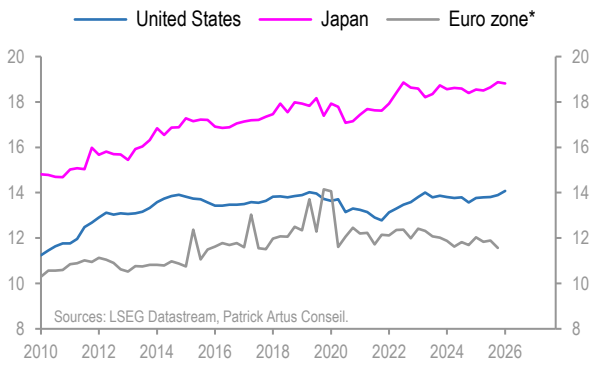


Chart 2
Private non-residential fixed investment (as % of GDP)



*Eurozone : non financial corporation's investment

With large government deficits, rising public debt ratios in the United States and the euro zone (**Chart 3**), and investment needs (in particular investment linked to artificial intelligence), **the economic equilibrium has become one in which savings are insufficient** (*ex-ante*, before rebalancing), **hence a rise in long-term real interest rates has already been observed** (**Chart 4**) **and should accelerate in the future**.

Chart 3
General government debt (% of GDP)

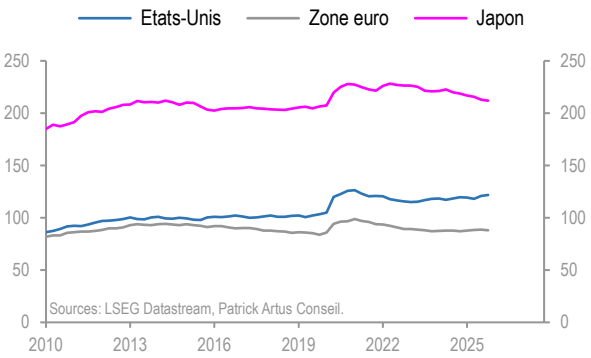
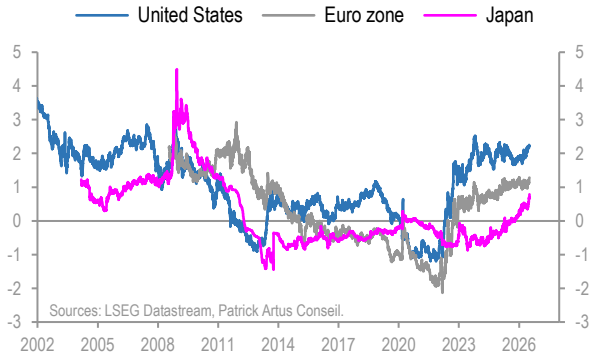


Chart 4
10-year real government bond yield (%)



As 10-year expected inflation is highly inert (**Chart 5**), this rise in long-term real interest rates will also lead to **a rise in long-term nominal interest rates** (**Chart 6**).

Chart 5
5-year, 5-year forward inflation swap rate (%)

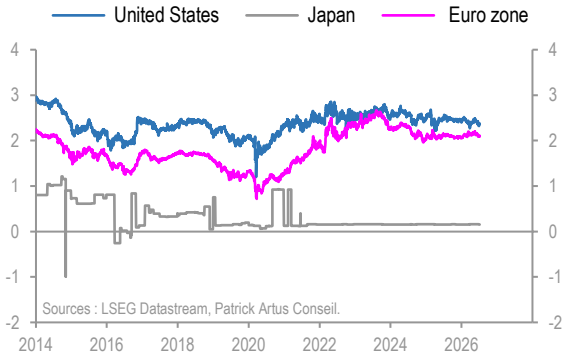
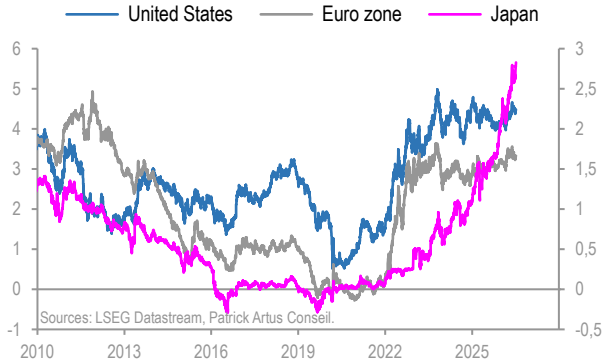


Chart 6
10-year government bond yield (%)



Second structural change: a decline in inflation

With the end of the war in the Middle East, **energy prices will fall sharply**, especially oil prices, since the market is heading towards **a situation of excess oil supply** (with rising production notably in the United Arab Emirates, Iran and the United States; **Charts 7** and **8**).

Chart 7
Oil price (Brent, $/bbl)

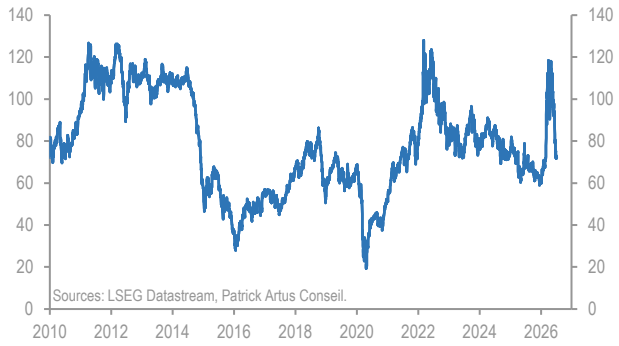
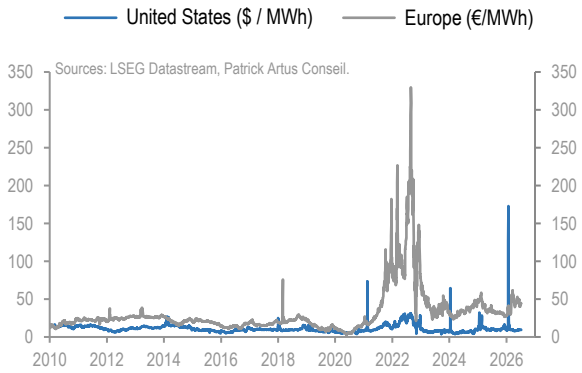


Chart 8
Natural gas price



After the peak linked to the war in the Middle East, **industrial commodity prices are also declining** (**Chart 9**).

Chart 9
Industrial metals price index (01.01.2010 = 100)



Moreover, **the development of artificial intelligence** will in time generate significant productivity gains, which will reduce production costs and prices. Beyond the current period, still marked by the inflation resulting from the war in the Middle East, we will therefore see **a decline in inflation** (**Chart 10**) **and a fall in short-term interest rates** (**Chart 11**), **except in Japan**, since the Bank of Japan reacted very slowly and very belatedly to the rise in inflation, which in Japan results from the acceleration in wage growth.

Chart 10
Inflation (%)

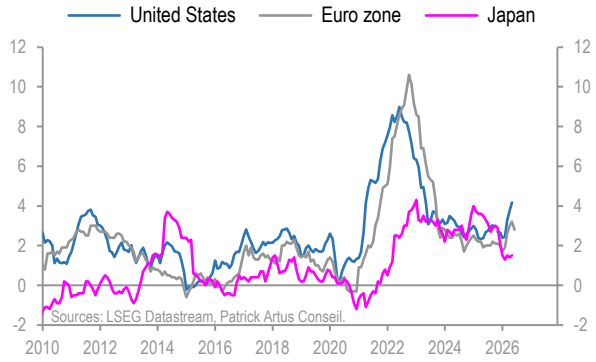
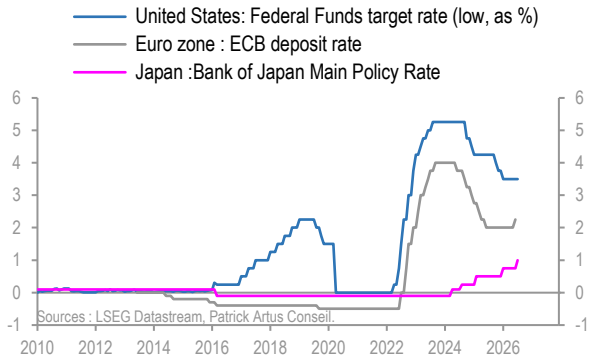


Chart 11
Central bank policy rates (%)

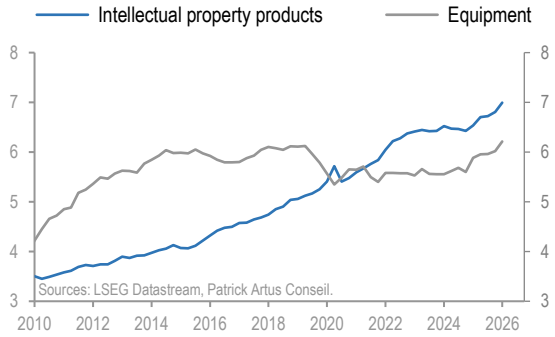


In the United States and Europe, **the yield curve will therefore steepen**, with a fall in short-term interest rates and a rise in long-term interest rates.

Third structural change: massive investment linked to artificial intelligence

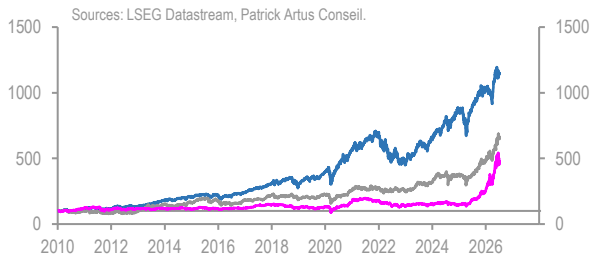
Over the past few years, **investment by companies developing artificial intelligence models has been rising**, with this increase concentrated in the United States (**Chart 12**).

Chart 12
United States: private investment by component
(as % of GDP)



This has led **to strong growth in the revenues and profits of these companies' suppliers** (providers of hardware, semiconductors, memory chips, hard drives, cloud services). For example, Nvidia posted earnings per share of USD 2.99 in 2024 and USD 4.77 in 2025, and earnings per share are estimated at USD 8.94 in 2026 and USD 12.50 in 2027; Intel posted earnings per share of USD 0.42 in 2025, and it is expected at USD 1.09 in 2026. In Korea, Samsung's profits grew by 756% between the first quarter of 2025 and the first quarter of 2026. As a result, **technology stock indices will continue to rise in the United States, Japan and China** (**Chart 13**), i.e. in the countries where the weight of the technology sector in the economy is high.

Chart 13
Stock market indices (01.01.2010 = 100)



However, **high volatility** in these indices cannot be ruled out, owing to the concerns raised by the high valuation of technology stocks (the Nasdaq's price/earnings ratio currently stands at 31.8, against a historical average of 28.8) and by the very high level of investment in artificial intelligence.

Fourth structural change: political risk in Europe

The risk of **a shift towards a populist government** is particularly high in France (opinion polls give around 35% of the vote to the Rassemblement National candidate in the first round of the presidential election) and in the United Kingdom (opinion polls give 27% of the vote to Reform UK in the next general election). The immigration, fiscal and anti-European policies of populist parties will increasingly worry investors. This results in :

- **the underperformance of the French equity index** relative to the European equity index (**Chart 14**);
- **the lag of the European equity index since 2023** relative to the US equity index (**Chart 15**);

Chart 14
Stock market indices (01.01.2022 = 100)

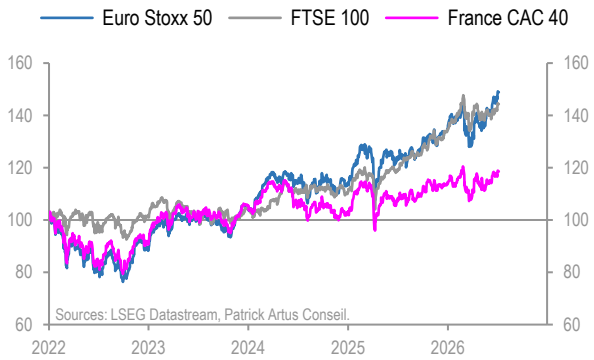
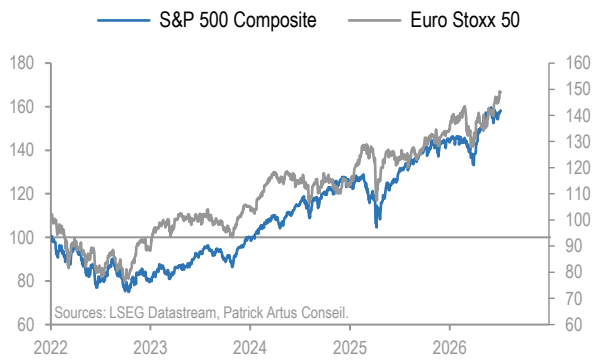


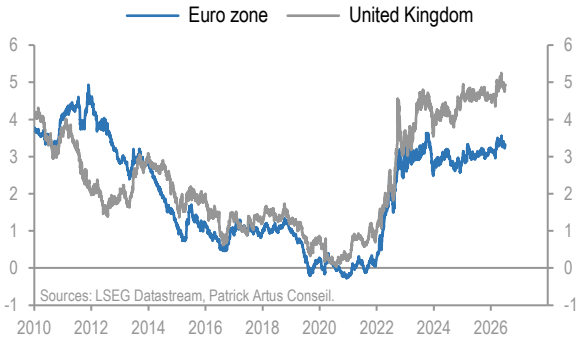
Chart 15
Stock market indices (01.01.2022 = 100)



- **the rise in European long-term interest rates** (**Chart 16**);

with all three trends being set to continue.

Chart 16
10-year government bond yield (%)



Summary: the economy and financial markets

Economic developments drive those of financial markets as regards:

- government deficits, investment needs and therefore long-term real interest rates;
- commodity prices, particularly energy prices, inflation and long-term interest rates;
- the profits of technology companies, particularly those supplying the developers of artificial intelligence models, and equity indices;
- political risk in Europe, equity indices and long-term interest rates.

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