

Global Equity Observer

Quality “on sale”



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After a very strong 2025, with the MSCI World Index up 21%, a third boom year after a +19% return in 2024 and +24% in 2023, global equity markets enter 2026 at a pivotal juncture. The close of 2025 was marked by a dynamic tension between those optimistic that artificial intelligence (AI) will drive a visible transformation in corporate profitability in the near term, justifying the massive capital expenditures, and the growing voice of those questioning whether these high expectations can be realised in the near term.

Against this backdrop of uncertainty, not just around the path of AI adoption, but also growth, inflation, trade policy, government debt and geopolitics to name just a few, the MSCI World Index continues to trade at around 20x forward earnings, with the S&P 500 Index at 22x, valuations that imply far more certainty than seems to be warranted. And these steep valuations rest on the assumption of robust 14% earnings growth for the MSCI World over each of the next two years, driven by further margin expansion from already elevated levels.

A regime of seeming market certainty in a distinctly uncertain world has naturally not been favourable for quality as a style, which has underperformed the broader market to an extent not seen since the dot-com era.¹ In terms of our outlook, **historically, such periods of quality underperformance have been followed by a meaningful relative resurgence in quality stocks**, which contributes to our view that **quality offers one of the greatest opportunities in markets today**.

In fact, we'd argue many of the companies we own across a range of sub-industries are double-discounted, being punished not just for being “quality” but also viewed as being at risk from advanced AI disruption.² This has hit software companies within information technology, a variety of professional services within industrials, and information services within financials. Our

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“Some of the highest quality companies in the world, trading at an unusually discounted price versus the market, suggests a generational opportunity to take advantage of quality on sale.”

¹ Source: S&P 500 Quality Index, as at 31 December 2025

² Advanced AI: generative AI [GenAI] and agentic AI

view is that the market has taken an indiscriminate view, not differentiating enough between industries and business models. As we've discussed in previous GEOs, we believe companies such as MSCI, S&P Global, RELX and Experian are not only likely to be robust against the advanced AI threat but should actually be long-term beneficiaries. As such, we disagree with the market about these companies' prospects. This is not to say that we are complacent; we continue to reassess our holdings' moats and focus on names where we are most confident about their resilience against advanced AI risks. While their derating has adversely affected their performance in 2025, it does improve their prospects going forward.

Our quality portfolios also have exposure to those providing advanced AI, mainly through select hyperscalers—companies that have decent growth prospects even without advanced AI—alongside reasonable valuations, which we believe should limit the downside from any deflation of advanced AI expectations. Where we have limited direct exposure to semiconductors, we prefer businesses that serve as key bottlenecks in the supply chain with broad use cases that are not wholly reliant on generative AI prospects. We are particularly wary of players where planned capital expenditures are highly dependent on debt financing rather than their own cash flow generation. These advanced AI

exposures are deliberately balanced by holding traditional defensives such as high quality consumer and health companies.

Overall, our portfolios are built around companies with the capacity for sustained earnings growth, supported by pricing power and recurring revenues. These are businesses that have demonstrated resilience through cycles, with lower earnings and price volatility than the broader market. In the past, the market has charged an insurance premium for this resilience, with quality significantly pricier than the overall index. This is far from the case today. Our portfolios are projected to grow faster than the market, but despite the attractive combination of this higher topline growth and its traditional resilience, **the portfolios are trading at a significant free cash flow discount to the market**, a level of discount not seen in the past decade—a rare opportunity.

Looking forward, we expect fundamentals to reassert themselves, as they have typically done historically.

Against the uncertain backdrop, a portfolio of some of the highest quality companies in the world, trading at an unusually discounted price versus the market, suggests a generational opportunity to take advantage of quality on sale.

Source for data cited, unless otherwise stated: MSIM, FactSet, as of December 31, 2025.

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