# Border to Coast Pensions Partnership Limited

## Joint Committee

**Date of Meeting:** **24 November 2026**

**Report Title:** **Border to Coast Investment Update**

**Report Sponsor:** **Joe McDonnell – CIO**

### 1. Executive Summary

1.1. This report provides a brief overview of investment markets, responsible investment and stewardship activity over the quarter. We have also introduced a quarterly "thematic" section to the report, designed to provide deeper insight into an investment issue that is shaping markets, portfolios or long-term investment outcomes for Partner Funds. The intention is both to share evolving thinking on topics that may materially affect Partner Fund portfolios and to provide a framework for Partner Funds to input into our thematic views and research agenda.

1.2. In this instance, Border to Coast is not providing financial advice or making any personal recommendation regarding the suitability of making specific investments. The information supplied is intended to be factual and should not be interpreted as advice tailored to the circumstances of any Partner Fund or individual.

1.3. A separate item on the agenda provides detail on performance of Border to Coast propositions.

### 2. Recommendation

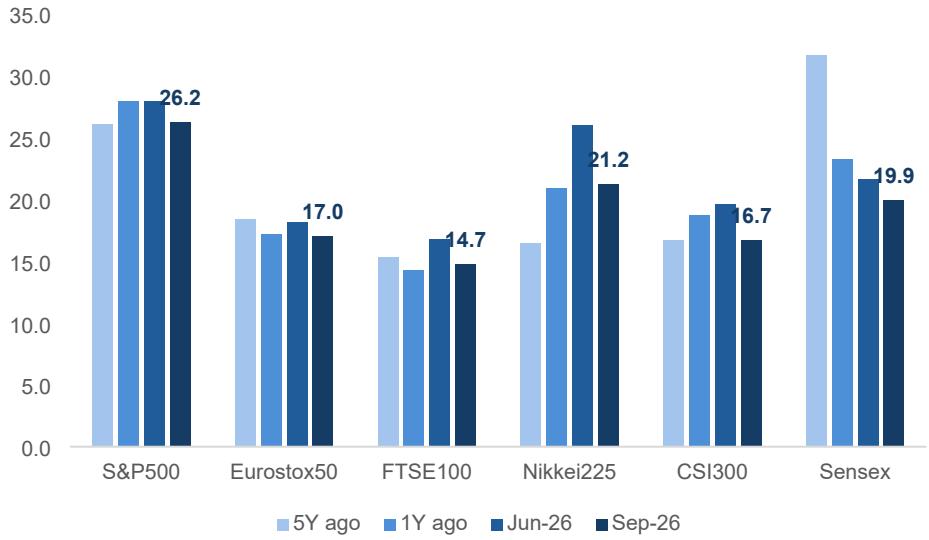
2.1. That the Committee notes the report.

### 3. What happened in markets over the quarter?

3.1. **Global equities** delivered generally positive returns over the quarter, supported by a resilient macroeconomic backdrop and continued earnings growth. Valuation multiples tightened across most regions, but this largely reflected stronger corporate earnings rather than weaker share prices. Europe was an exception, with equity markets moderately declining on the quarter despite improved earnings (Chart 1). This divergence is consistent with point-in-the-cycle indicators, where the euro area appears closer to a slowdown than other major regions.

3.2. The combination of solid growth and healthy earnings outcomes helped equity markets absorb higher interest rates without a significant impact.

***Chart 1: 12-month trailing price/earnings ratios***




3.3. Following the end of the quarter, the market reacted to both the US midterm election results and the company-specific news of the involvement of the Nvidia CEO, Jensen Huang, in a chip smuggling probe by US authorities. In the former instance, analysis of voting patterns indicated unexpected Democratic outperformance was at least in part driven by local hostility toward data centre build out. This resulted in 5.5% decline in the tech-heavy NASDAQ index on the day following the election. In the latter instance, concern about the knock-on from the investigation to Nvidia's high revenue growth expectations (currently 225% over the next two years), resulted in an 18% decline in Nvidia stock price (currently the second largest stock in a global index) in the week following the initial revelation.

3.4. **Cash** became materially more attractive during the quarter as investors reassessed the outlook for monetary policy. By the end of Q3, markets were pricing around 0.75% of interest rate rises from The Federal Reserve, European Central Bank and Bank of England. This represented a substantial shift from the end of Q2, when investors were effectively undecided as to whether any further rate increases at all would be required. By the end of Q3 the12-month money market rate in the UK was 0.57% higher on the year, with 0.43% of that increase occurring during Q3.

3.5. In **fixed income** markets, the gilt curve flattened modestly as expectations for higher policy rates and rising inflation exerted greater pressure on the yields of shorter-dated maturities. Although higher real yields continued to explain most of the increase in nominal gilt yields, inflation expectations began to play a more important role during the quarter. (See Section 5, *'The Investment Implications of Higher Yields'* for more detail)

3.6. All of the rise in long-term inflation expectations seen over the previous year occurred during Q3, suggesting that investors became more concerned about the persistence of inflationary pressures even as central banks signalled increasingly restrictive policy settings.

3.7. Although the October 2026 UK Budget forecast 0.5% of GDP more government borrowing over the three-year forecast period than at the time of the November 2025 forecast, this was within the expected range, given the already observed increase in debt service costs. As such, there was no appreciable financial market reaction following this increased borrowing forecast - illustrating both the impact of and the cushion provided by higher yields.

3.8. **Commodities**, particularly energy, also contributed to this changing inflation narrative. The key development here was not simply an increase in oil prices, which are inherently volatile, but a more sustained shift higher in expectations for future oil prices. During Q2, the price of oil futures beyond one year were broadly unchanged; by contrast, during Q3 prices increased across much of the future maturities, in fact extending almost four years into the future

3.9. This mainly reflected ongoing Saudi supply restrictions and growing scepticism that these supply constraints would be resolved quickly. There were also signs that this more persistent upward pressure was spreading beyond energy markets. Raw industrial commodity prices rose by 15% over the quarter and were approximately 35% higher over the year, reinforcing concerns that inflation could remain elevated for longer than previously expected.

## 4. Looking ahead

4.1. The investment backdrop remains broadly supportive for risk assets, despite growing uncertainty around the medium-term economic outlook, particularly inflation expectations. In most regions, growth has moderated from the exceptionally strong post-CoVID period but continues to be expansionary. Equity investors have also been encouraged by evidence that many companies, including large tech companies, retain pricing power and the ability to protect margins – the avoidance of margin compression being particularly important when the main challenge facing sustained earnings growth is often higher input costs.

4.2. Against this backdrop, equities continue to offer the most compelling long-term return potential. While valuations are no longer universally attractive, earnings growth remains strong - and is the dominant driver of returns over time. Given heightened expectations of tech company earnings growth, periods of market volatility are more likely but should be viewed more as opportunities than as signs of a fundamentally weaker outlook.

4.3. Within fixed income markets, higher government bond yields have materially improved the opportunity set available to investors. After many years in which sovereign bonds offered limited income and little protection against inflation risks (*"Return free risk"*, to use a much-repeated phrase of the 2010s), current yield levels provide a more balanced combination of income, valuation support and diversification potential. This represents a significant improvement in the asset class's prospective return profile.

4.4. Note that for a pension scheme investor, it is important to be aware of both sides of the balance sheet. Index-linked gilts remain the optimal low risk asset for the LGPS, with interest rate and inflation-linkage that represent a good match for uncapped, inflation-linked liabilities. Choosing to invest in fixed interest gilts rather than linkers is essentially reflecting a view that inflation expectations are overpriced.

4.5. The attractiveness of government bonds in general has, in turn, reduced the relative appeal of some areas of credit. Corporate balance sheets remain generally healthy and default expectations are contained, but investment-grade credit spreads offer only limited compensation relative to government securities.

4.6. Notwithstanding these valuation concerns, higher-yielding segments of the credit market continue to benefit from attractive income characteristics. The combination of elevated running yields (the yield level on bonds at the time of their purchase) and supportive corporate fundamentals means that credit can still play an important role in generating income.

4.7. Real assets present a more mixed picture. Infrastructure and other private market investments continue to offer diversification benefits and access to differentiated return drivers. By contrast, real estate remains challenged by a combination of sensitivity to higher interest rates and operational pressures that have weighed on both valuations and investor sentiment, while remaining a useful long-term asset for predictable cashflows.

4.8. Given these cross-currents, maintaining a meaningful level of liquidity, and the ability to respond to change, remains valuable. The macro environment remains supportive of growth assets, underpinned by resilient earnings growth, but needs to be balanced against the importance of liquidity and the ability to respond to change.

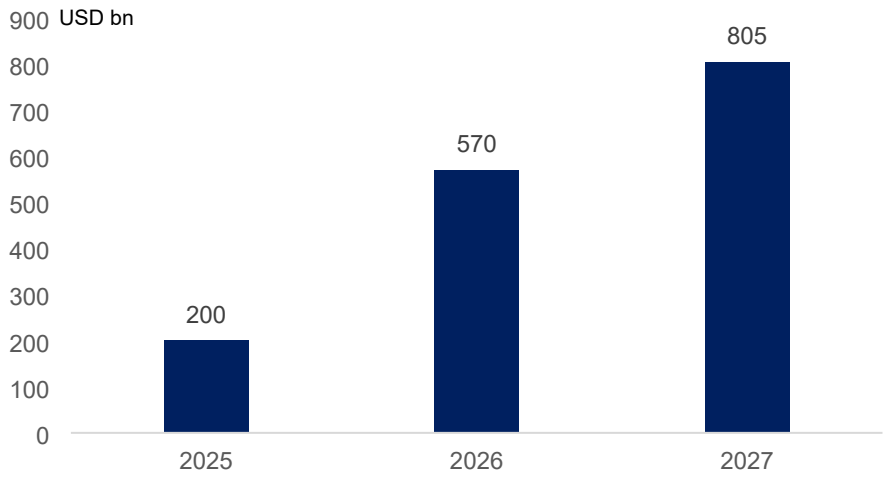
## 5. Quarterly theme – The Investment Implications of Higher Yields

5.1. Alongside the concentration of equity returns in mega-cap US technology stocks (see Joint Committee CIO Report, 23 September 2026, here), the sharp rise in government bond yields has been one of the most important developments in financial markets in recent years. Government bond yields also matter for equity investors because they influence how future earnings are valued. Equity prices reflect the present value of expected future cashflows. When yields are low, this increases the value placed on profits expected many years ahead. As yields rise, the present value of those earnings falls, particularly for growth companies whose profitability lies further in the future. Higher yields also improve the relative attractiveness of fixed income investments, encouraging some investors to reallocate capital away from equities.

5.2. Because government bond yields underpin the valuation of other financial assets and pension fund liabilities, a key question for long-term investors such as the LGPS is whether the recent increase in yields is primarily cyclical or reflects a more durable secular shift. A common explanation for higher yields focuses on inflation. While inflation undoubtedly contributed to the repricing of yields in 2022, it is less convincing as an explanation for developments over the last year. Market inflation expectations have remained broadly stable despite substantial increases in nominal government bond yields. This suggests that much of the recent increase in yields has reflected higher real interest rates rather than rising inflation expectations. (Japan is an important exception here.)

5.3. A further explanation for higher real rates is increased competition for capital. Governments across developed markets are running larger fiscal deficits than was typical before the Covid pandemic (Chart 2), requiring sustained and substantial bond issuance. At the same time, private-sector demand for capital has risen sharply. Investment associated with artificial intelligence, particularly data centres and supporting infrastructure, is now measured in hundreds of billions of dollars annually. As governments and companies compete for financing, investors are able to demand higher real yields as compensation for supplying capital.

***Chart 2: Estimates of AI-related bond issuance***




5.4. A second structural factor is the term premium; the additional compensation investors require to hold long-dated bonds rather than continuously rolling short-term debt. This premium tends to rise when future inflation and interest rates become more uncertain, increasing the risks associated with holding long-maturity securities.

5.5. Estimates from the Federal Reserve Bank of New York[1] suggest that the ten-year US Treasury term premium has increased by around 2.0%, rising from approximately -1.3% in the immediate post-Covid period to positive territory today. This appears to represent a reversal of the unusually low term premia that characterised much of the decade following the Global Financial Crisis. During that period,

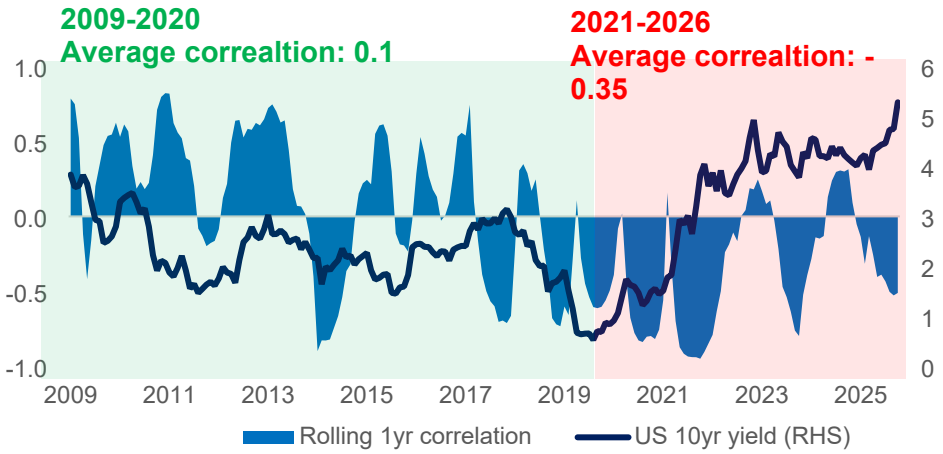
[1] *"Treasury Term Premia"*, Federal Reserve Bank of New York, here

quantitative easing and consistently low inflation encouraged investors to have a high degree of confidence in the future path of interest rates.

5.6. Evidence from the UK points in the same direction. Recent Bank of England analysis suggests that the UK's neutral real interest rate has risen structurally by around 0.9% relative to its pre-Covid level.[2] If correct, this implies that higher bond yields are not merely a temporary response to the economic cycle but may reflect a lasting shift in the pricing of capital. The implications for equities depend not only on the level of yields but also on how equity valuations respond to changes in yields. At relatively low yield levels, rising yields can coincide with stronger economic growth and improving earnings expectations. However, as yields move higher, their effect on equity valuation increasingly dominates.

5.7. Recent market evidence suggests this transition may already be underway. As government bond yields have returned towards levels last seen before the Global Financial Crisis, rolling correlations between equity valuation multiples and bond yields have turned negative (Chart 3).

***Chart 3: MSCI World 12m fwrd P/E and US Treasury yield correlations***




5.8. Rising yields increasingly appear to be a headwind for valuations rather than a signal of stronger growth. This does not mean higher yields must result in poor equity returns. Earnings growth remains the most important long-term driver of equity market performance, and many periods of rising yields have coincided with strong economic activity and robust corporate profits. Nevertheless, investors should recognise that the valuation tailwind created by the exceptionally low-yield environment of the 2010s is no longer present.

5.9. The key conclusion is that, if government bond yields remain structurally higher than in the previous decade, equity valuations will need to rely more on actual earnings growth and less on anticipated earnings growth. With the opportunity cost of waiting for future profits now higher, markets may place greater value on companies capable of generating cashflows today. As such, higher yields could provide one mechanism through which leadership rotates from growth-oriented strategies towards quality-focused approaches, even if overall equity market performance remains robust. Diversified equity strategies which are not reliant on a single factor are a useful way of navigating these challenge

## 6. Risks

6.1. Effectiveness of Oversight: There is a risk that the Joint Committee does not receive sufficient information, context and insight to effectively oversee Border to Coast's investment activities and understand the implications of market developments for Partner Fund outcomes. The existing oversight framework is currently being reviewed and developed through work being undertaken by the Joint Committee Oversight Working Group and the Officer Operations Group. This report forms part of the current framework and provides market context, emerging themes and forward-looking

[2] *"The Long Run Equilibrium Interest Rate"*, Bank of England, Monetary Policy Report, Feb 2025, here

analysis to support informed discussion and challenge while the future approach to oversight is being developed.

6.2. Risk of Narrow Perspectives: There is a risk that investment oversight and strategic discussions become reliant on a limited range of viewpoints, resulting in insufficient challenge to prevailing assumptions and a reduced ability to identify emerging risks, opportunities or changes in market structure. This risk is mitigated through Border to Coast's engagement with a broad range of external stakeholders, including investment managers, advisers, research providers and market participants. The Pool also draws on a wide range of external research and market intelligence when developing its investment views and thematic analysis, helping to ensure that discussions are informed by diverse perspectives and evidence from across the investment industry.

6.3. Risk of Insufficient Market Context: There is a risk that proposition performance and investment outcomes are considered without sufficient understanding of the wider market environment in which they are delivered, potentially leading to incomplete conclusions regarding performance, risk and long-term outcomes.

## 7. Author

Richard Batley, Investment Specialist

30 October 2026

## 8. Supporting Documentation

Appendix 1: Market performance Q2 2026

**Important Information**

Border to Coast Pensions Partnership Ltd is authorised and regulated by the Financial Conduct Authority (FRN 800511). The information provided in this paper does not constitute a financial promotion and is only intended for the use of Professional Investors. The value of your investment and any income you take from it may fall as well as rise and is not guaranteed. You might get back less than you invested. Issued by Border to Coast Pensions Partnership Ltd, Toronto Square, Leeds, LS1 2HP.