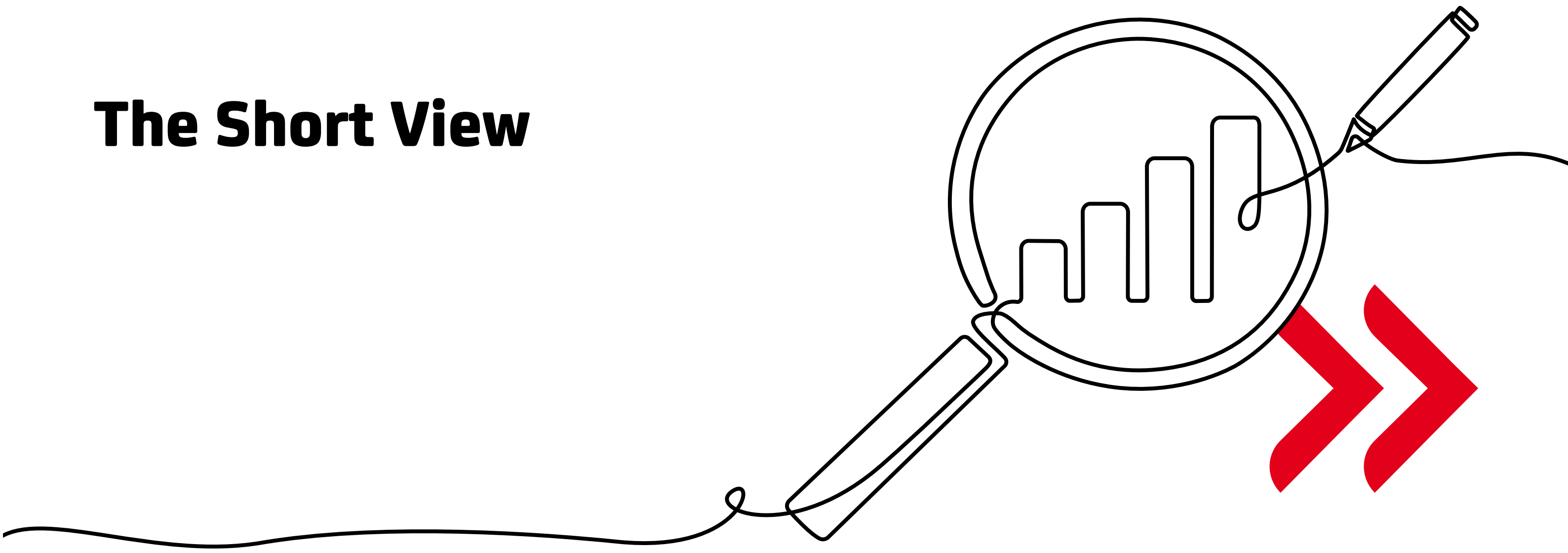
The Short View



The Short View offers insights on key macro and market stories and is designed to promote discussion and debate.

Industrials: the beneficiaries of converging investment cycles

27 August 2026

The extraordinary performance of technology stocks has shaped much of the investment narrative in recent years. Yet many of the forces transforming the global economy, from artificial intelligence (AI) and electrification to defence spending and supply-chain reorganisation, ultimately depend on industrial capacity. As governments and companies invest in infrastructure, energy security and economic resilience, the industrial sector is increasingly emerging as one of the most important enablers of structural change.

1. **Multiple structural investment cycles are supporting industrial demand.** AI infrastructure, electrification, defence spending and supply-chain diversification are collectively driving capital expenditure across developed and emerging markets.
2. **Geoeconomics has become a major earnings driver.** Tariffs, industrial policy, economic-security considerations and heightened geopolitical tensions are increasingly influencing corporate investment decisions and industrial activity.
3. **Opportunities differ markedly across regions.** The US offers the strongest exposure to AI-related infrastructure spending, Europe is benefitting from defence and electrification trends, Japan remains a leader in automation, while several emerging markets continue to benefit from manufacturing relocation.

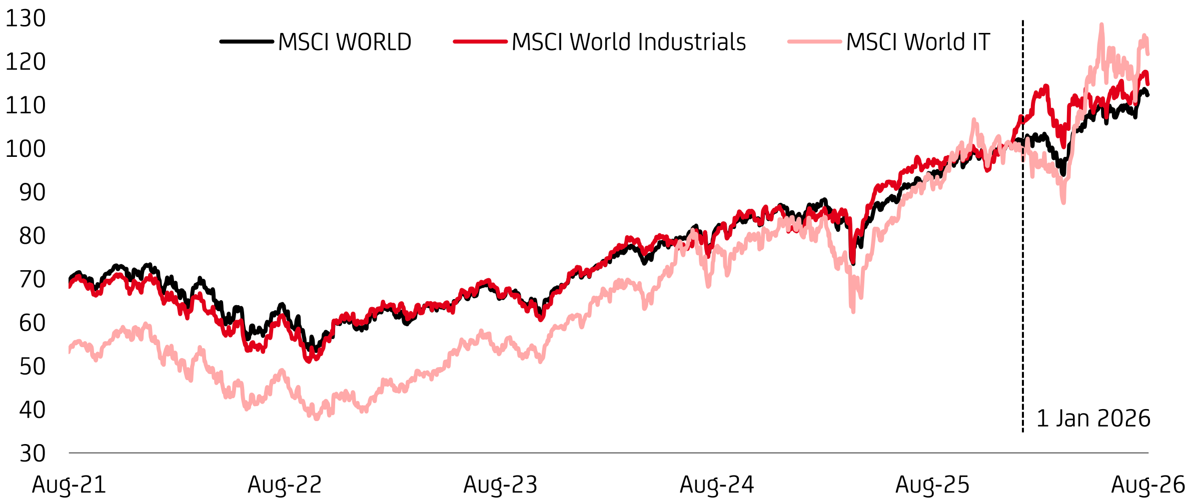
The remarkable rise of AI has dominated equity-market performance in recent years and months. However, while investor attention has naturally focused on semiconductors and software, a less-appreciated reality is that many of the technologies reshaping the global economy ultimately depend on industrial capacity. AI requires data centres, electricity networks, cooling systems and transmission infrastructure. At the same time, electrification, supply-chain diversification and rising defence spending are driving investment in factories, logistics networks and industrial equipment. What appears to be a technology-led era is increasingly becoming an infrastructure story, which is unfolding against a changing geopolitical backdrop. Governments increasingly view industrial capacity, energy systems and critical supply chains as strategic assets. As a result, capital expenditure is being shaped not only by commercial considerations but also by economic-security priorities.

These developments are arguably creating the most supportive backdrop for industrial companies in more than a decade. New factories, energy infrastructure, logistics networks and manufacturing capacity are being built not merely because they are the lowest-cost option, but because governments and corporations are placing greater value on resilience and redundancy. The challenge for investors is determining whether these structural tailwinds can continue to outweigh the costs associated with a more-fragmented global economy. The market has recognised this changing backdrop. After lagging behind the technology sector for much of the past decade, industrial equities have re-emerged as a notable source of performance in 2026 (see chart).

Unlike previous periods of industrial outperformance, typically driven by economic recoveries, the current environment is supported by a broader mix of structural themes. AI infrastructure, electrification, defence spending and supply-chain reorganisation are all contributing to higher levels of capital investment. Nevertheless, stronger performance has also raised expectations. The investment case for industrials is no longer simply about benefitting from favourable trends but rather whether those trends continue to justify increasingly ambitious forecasts for growth and profitability.

INDUSTRIALS REGAIN LEADERSHIP

MSCI WORLD INDUSTRIALS VS MSCI WORLD (INDEXED AS OF 1 JANUARY 2026 = 100)



Source: LSEG Datastream, The Investment Institute by UniCredit

Industrial policy is back

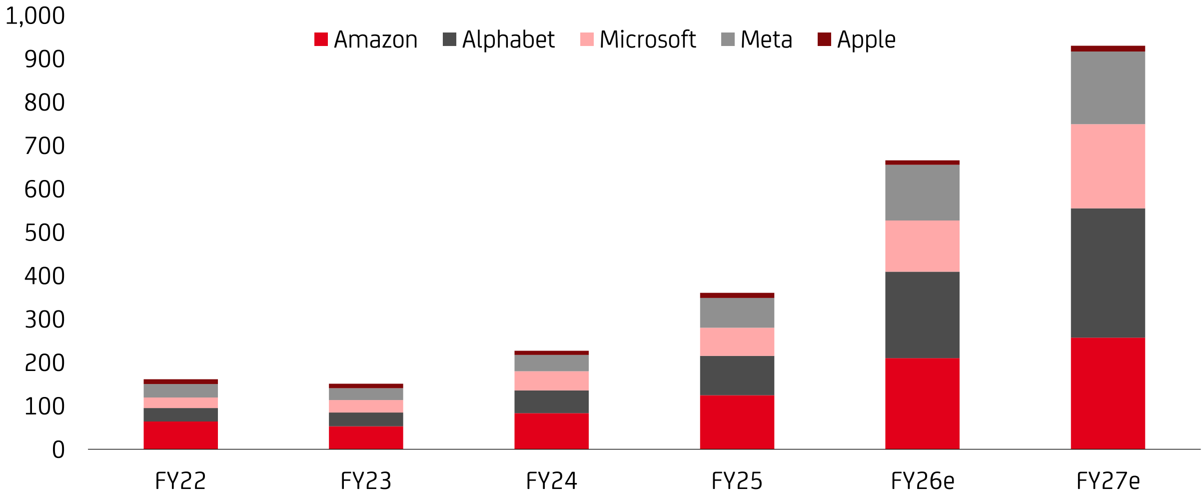
Industrial policy has returned as a major force in shaping capital allocation. Tariffs, subsidies, local-content requirements and strategic-investment programmes are increasingly influencing where companies build factories, source components and deploy capital. In the US, industrial policy is aimed at reducing strategic dependencies and supporting domestic manufacturing. Europe is increasingly prioritising defence capabilities, energy security and industrial competitiveness. Across Asia, governments remain focused on strengthening advanced manufacturing and technological self-sufficiency.

The cumulative effect has been a renewed wave of investment across a broad range of industrial activities. While resilience-driven investment remains a powerful driver of industrial activity, the resulting duplication of supply chains may gradually reduce global productivity and place upward pressure on costs, as greater fragmentation of global trade risks raising production expenses and reducing some of the efficiency gains created by decades of globalisation. For investors, the key question is whether the resulting increase in investment spending more than offsets these economic headwinds.

AI is becoming an industrial story

AI remains one of the most powerful investment themes globally. Increasingly, however, its beneficiaries extend far beyond the technology sector. The rapid expansion of data-centre capacity is creating strong demand for electrical infrastructure, cooling technologies, power-management systems and engineering services, linking the next phase of AI development directly to the industrial economy. The scale of investment is striking. Capital expenditure across the largest hyperscaler technology companies is estimated to rise from around USD 160bn in 2022 to more than USD 900bn by 2027, highlighting how quickly AI has evolved from a software innovation into a broad-based infrastructure build-out (see chart below). At a time when many industries remain cautious about capital spending, the technology sector is undertaking one of the largest investment programmes in recent history, creating significant opportunities across industrial supply chains.

CLOUD AND AI INVESTMENT DRIVES STEP-UP IN HYPERSCALER SPENDING
CAPITAL EXPENDITURE OF MAJOR US TECHNOLOGY COMPANIES (USD BN)



Source: LSEG, The Investment Institute by UniCredit
Note: Microsoft's fiscal year ends in June and FY26 is its last reported year; Apple's fiscal year ends in September. All other fiscal-year ends are December.

What distinguishes the current cycle from previous technology booms is its intensity of resource consumption. Generative AI requires vast computing power and electricity, increasingly making access to energy as important as access to computing hardware. In many regions, power generation, transmission networks and grid connections are emerging as critical constraints. As a result, the opportunity set is expanding beyond semiconductors and cloud computing towards the companies responsible for building and maintaining the physical infrastructure underpinning the digital economy.

At the same time, however, investors should not assume that current spending trends will continue indefinitely. A growing share of industrial activity is becoming linked to the capital-expenditure decisions of a relatively small group of technology companies. Should demand for AI infrastructure prove less durable than expected, parts of the industrial sector could face a sharper slowdown than implied by current market expectations. While the opportunities are substantial, so is the risk that AI enthusiasm creates pockets of overinvestment. As with previous technological revolutions, infrastructure build-outs may outpace demand, leaving current expectations difficult to justify over time.

Nevertheless, the significance of AI for industrials extends well beyond data centres. One of the largest infrastructure investment programmes in decades is emerging – encompassing power generation, transmission networks, cooling systems, automation equipment and specialised engineering services. In this sense, AI is increasingly becoming an industrial story as much as a technology story.

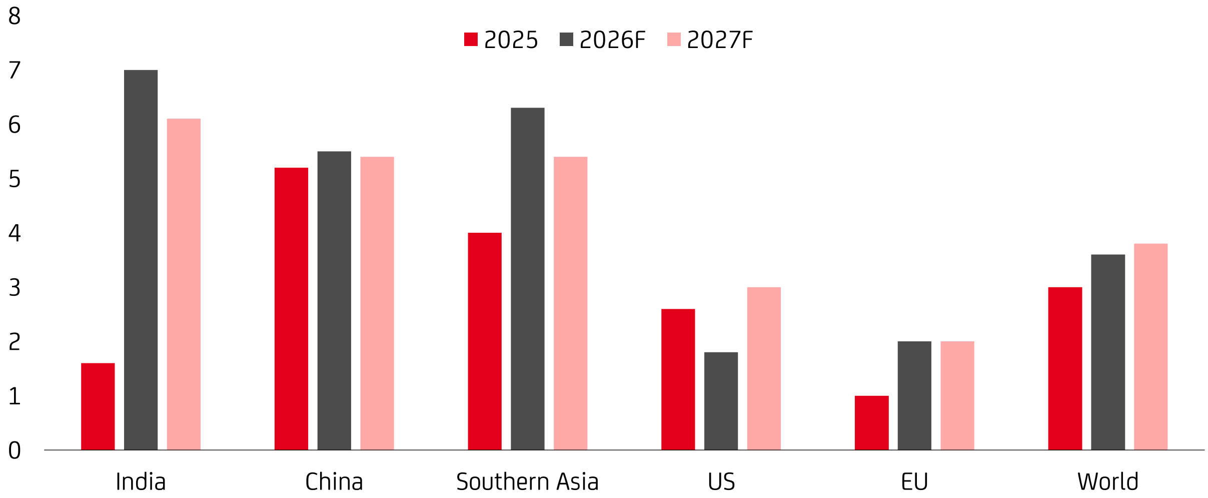
Electrification remains a secular growth story

The growing demand for electricity is another powerful driver of industrial activity. Data centres, electric vehicles, industrial decarbonisation and digital infrastructure are placing an increasing strain on global power systems, driving investment not only in generation capacity but also in transmission, distribution and energy-management technologies. Unlike many investment themes, electrification enjoys broad policy support. While governments may differ in their approach to climate policy, there is growing consensus around the need for energy security, grid resilience and reliable electricity infrastructure. Against this backdrop, global electricity demand is expected to accelerate by 3.6% in 2026 and 3.8% in 2027, up from 3% in 2025.

The opportunity is global. In the US, rising power demand from AI, data centres and advanced manufacturing is driving renewed investment across the electricity value chain. China remains central to the theme. As the world's largest electricity market and leading investor in power infrastructure, it continues to deploy capital at scale while increasingly setting the pace of innovation in electrification technologies. Europe occupies a distinctive position within this theme. Despite persistent concerns about growth and competitiveness, the region retains significant expertise in electrification, industrial automation and energy efficiency, providing a differentiated source of industrial earnings growth at a time when many investors remain sceptical about Europe's broader economic outlook.

ELECTRICITY DEMAND IS EXPECTED TO ACCELERATE

YOY CHANGE IN ELECTRICITY DEMAND IN SELECTED REGIONS (%)



Source: IEA, The Investment Institute by UniCredit

Defence spending reshapes Europe

If AI infrastructure is the dominant industrial theme in the US, defence has become one of the defining themes in Europe. The deterioration of the global security environment has triggered a fundamental reassessment of defence policy across the continent. Military spending has risen sharply since Russia's invasion of Ukraine, while governments continue to announce new procurement programmes and long-term capability investments. Defence is increasingly becoming a structural area of fiscal spending rather than a cyclical one. The ongoing US-Iran conflict has reinforced this trend. Disruptions to shipping, tensions around the Strait of Hormuz and concerns over critical infrastructure highlight how quickly geopolitical shocks can spill over to energy markets, supply chains and inflation.

The broader lesson is that national security has again become an important driver of economic policy and public investment. For Europe, the implications extend far beyond any single conflict. Russia's war against Ukraine remains the primary catalyst for higher defence spending but growing geopolitical fragmentation, uncertainty regarding global trade routes and renewed great-power competition have strengthened support for military investment, energy security and strategic autonomy. The shift is increasingly institutionalised. Having only recently reached NATO's longstanding 2% spending benchmark, allies have now committed to raising defence and defence-related spending towards 5% of GDP by 2035, underscoring that rearmament is likely to remain a defining feature of European fiscal policy and industrial strategy for years to come.

Supply chains continue to diversify as automation becomes a necessity

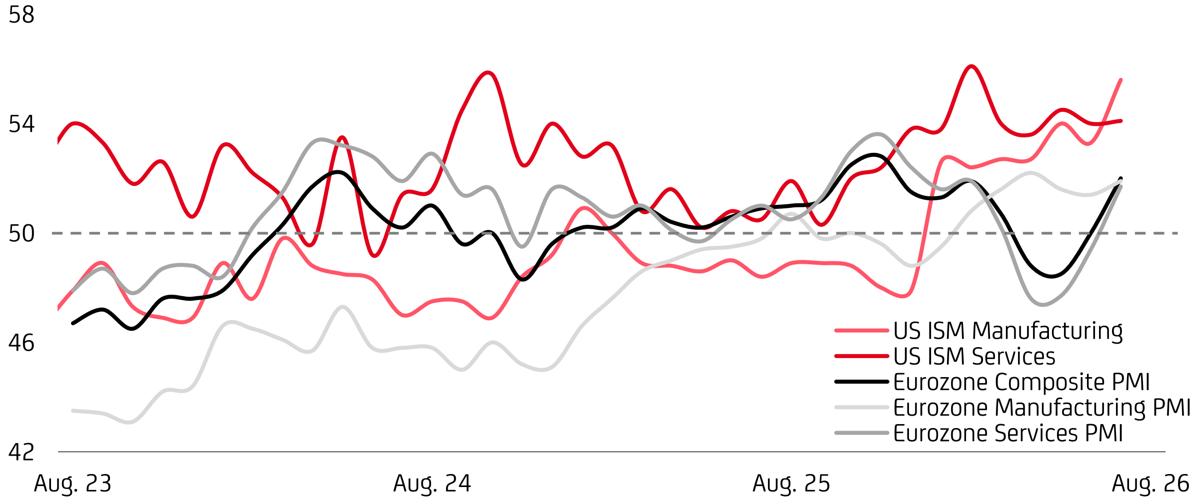
The same geopolitical forces are reshaping global supply chains. Trade tensions, tariffs and growing concerns about economic security have reinforced efforts by companies to diversify production networks and reduce concentration risks. Rather than abandoning globalisation altogether, businesses are increasingly pursuing more geographically diversified manufacturing strategies. This shift is producing distinct regional winners. The US continues to attract manufacturing investment linked to reshoring initiatives. While several southeast Asian economies continue to benefit from production diversification, China presents a more complicated picture. The country remains a critical source of industrial demand and continues to invest heavily in automation, manufacturing and electrification. At the same time, trade barriers, geopolitical tensions and concerns about excess capacity have increased uncertainty surrounding future growth. For many global industrial companies, China remains one of the largest opportunities as well as one of the largest risks.

As production footprints become more geographically dispersed, maintaining efficiency and competitiveness becomes increasingly important. A further driver of industrial demand is therefore the growing need to improve productivity. Ageing populations, labour shortages and rising wage pressures encourage businesses to invest in automation technologies. These trends are particularly visible in Japan and in parts of Europe, where demographic constraints are most acute. Following a cyclical slowdown during 2024 and 2025, industrial automation markets are expected to benefit from renewed investment activity and improving order trends. The long-term outlook remains underpinned by structural productivity requirements rather than purely cyclical demand. Reflecting this, global industrial robot installations are expected to exceed 700k units by 2028, up from 542k in 2024.

Earnings remain supportive but expectations are rising

Perhaps the most important development for industrials is that structural and cyclical forces are no longer pulling in opposite directions. Over the past several years, investment linked to AI, electrification and economic security has largely offset weakness in the broader manufacturing cycle. That tailwind is now beginning to fade. In the US, the ISM Manufacturing PMI rose to 55.6 in July, its highest level since May 2022, with both new orders (56.7) and production (58.5) pointing to strengthening industrial momentum. In the euro area, the manufacturing PMI climbed to 51.9, while the output index reached 52.9, its strongest reading since March 2022. If sustained over several quarters, this would mark a meaningful shift from a sector supported by a handful of structural themes to one benefiting from both secular and cyclical tailwinds. Improving manufacturing activity is thus broadening the earnings backdrop for industrial companies.

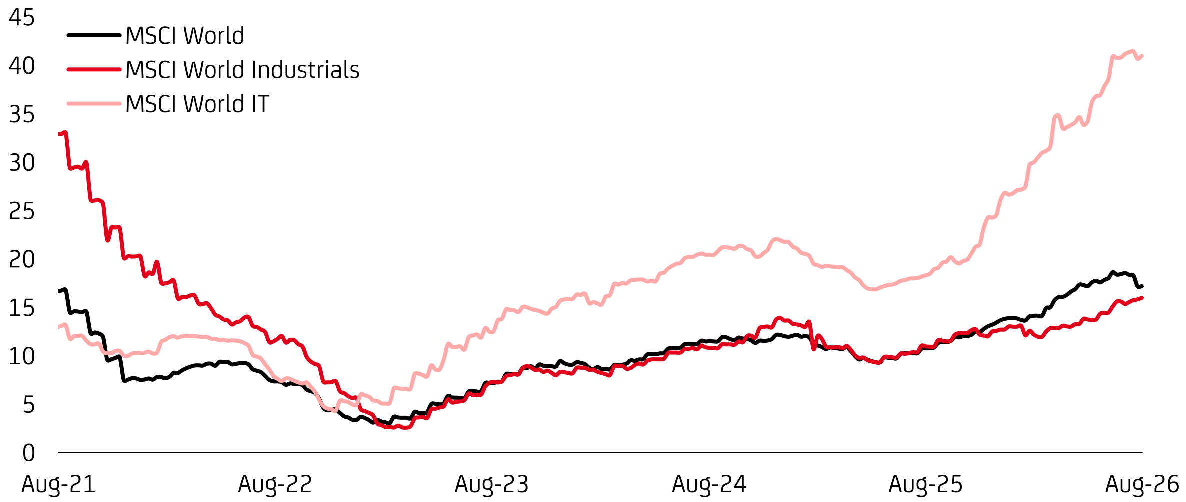
LEADING INDICATORS POINT TO A MANUFACTURING UPTURN
PMI AND ISM INDICES (50 = EXPANSION THRESHOLD)



Source: LSEG Datastream, ISM, S&P, The Investment Institute by UniCredit

Furthermore, consensus forecasts continue to point to healthy profit growth across most industrial markets. Unlike during previous industrial recoveries, earnings momentum is simultaneously being driven by several structural forces rather than by a traditional cyclical upswing alone. Importantly, earnings expectations remain robust but are not as demanding as in technology. On a 12-month forward basis, consensus expects earnings growth of around 16% for the MSCI World Industrials, compared with 18% for the MSCI World and an exceptional more-than-40% for the IT sector. Industrials therefore do not offer the strongest earnings-growth profile in the market but they provide exposure to many of the same structural investment themes driving technology-related spending, while relying on a broader and arguably more diversified set of end-markets. This may leave the sector less vulnerable should expectations surrounding AI-driven growth prove overly optimistic.

INDUSTRIALS EARNINGS FORECASTS REMAIN CONSTRUCTIVE
12M FWD EPS ESTIMATES (YOY GROWTH IN %)



Source: LSEG Datastream, The Investment Institute by UniCredit

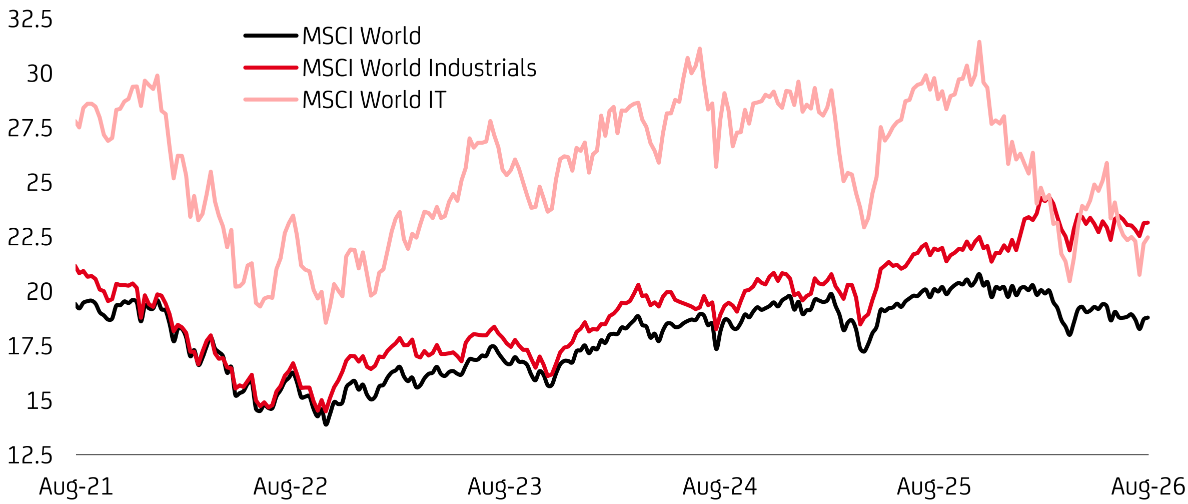
Regional differences also remain important. The US continues to benefit from strong investment spending and AI-related demand. Europe is supported by defence procurement and energy infrastructure programmes, while Japan remains leveraged to global automation trends. Several emerging markets are benefitting from manufacturing relocation and infrastructure development as supply chains become more diversified. The relative durability of these earnings drivers distinguishes the current environment from previous industrial cycles. Demand is increasingly being supported not only by economic growth but also by policy priorities, strategic-security concerns and corporate investment in productivity-enhancing technologies. Even so, expectations have become more ambitious. Should AI-related spending fade, defence procurement slow or global growth weaken materially, earnings forecasts could prove vulnerable.

Valuations leave less room for disappointment

Valuations no longer provide the margin of safety they did several years ago. Following a period of strong performance, many industrial markets now trade at or above their historical averages. Nevertheless, the sector remains considerably less expensive than technology. The MSCI World Industrials currently trades at a 12-month forward P/E ratio of around 21x, compared with roughly 28x for the IT sector, while the broader MSCI World trades at about 19x (see chart below). Investors are therefore paying a modest premium for exposure to the structural growth drivers of industrials, albeit far less than in technology. While valuation levels remain below those of technology stocks, many industrial companies now trade near the upper end of their historical valuation ranges, reducing the margin for execution disappointments.

INDUSTRIALS NO LONGER LOOK CHEAP

12M FWD P/E RATIOS



Source: LSEG Datastream, The Investment Institute by UniCredit

Valuation dispersion across regions also remains significant, with US industrials commanding a premium for stronger expected earnings growth and greater exposure to AI-related investment, while European and Japanese markets trade at more-moderate multiples. Accordingly, future returns are likely to increasingly depend on earnings delivery rather than further multiple expansion. Structurally attractive does not necessarily mean attractively priced. Investors have largely recognised the sector's favourable long-term drivers. The key question is no longer whether these themes exist but whether current expectations have become too optimistic.

Investment implications

Industrials have become one of the clearest equity expressions of a world characterised by geopolitical competition, growing energy demand and renewed industrial policy. AI requires data centres and power networks. Electrification requires grids and equipment. Reindustrialisation requires factories and logistics infrastructure. Defence requires manufacturing capacity. Few sectors sit at the intersection of as many powerful investment themes. This creates a more-favourable backdrop for industrial companies than a decade ago. Demand is simultaneously being supported by governments, corporations and strategic-security considerations, making the current investment cycle broader and potentially more durable than earlier expansions. The US appears best positioned to benefit from AI-related infrastructure spending and reshoring initiatives. Europe offers differentiated exposure to defence and electrification, while Japan remains the most direct play on automation and productivity growth. Selected emerging markets continue to benefit from the gradual reorganisation of global supply chains.

Nevertheless, investors should resist the temptation to view industrials as a pure structural-growth sector. The industry remains exposed to economic cycles, business confidence and capital-spending decisions. Tariffs may support domestic investment but could also raise costs. Defence spending may continue to rise but remains dependent on political priorities. AI infrastructure has become a powerful earnings driver, yet parts of the sector are increasingly dependent on the spending plans of a relatively small group of technology companies.

Unlike many sectors, industrials are not merely responding to change – they are enabling it. The infrastructure required for AI, energy security, automation and economic resilience cannot be built without them. Increasingly, the technologies attracting the greatest attention depend on industrial companies providing the physical foundations on which they operate. For investors, industrials therefore offer exposure not only to cyclical recovery but to some of the most important structural transformations reshaping the global economy. The challenge going forward lies less in identifying the themes rather than assessing how much of their promise is already reflected in prices. As long as earnings continue to validate current expectations, industrials appear well placed to remain important beneficiaries of these structural trends – although future returns are likely to increasingly depend on earnings delivery rather than continued valuation expansion.

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