CIO View

CIO Special

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Marketing material

Europe’s absolute and relative charm

Markets don't move on headlines alone. Structural shifts are changing Europe's investment story.

IN A NUTSHELL

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- Europe is stronger than it appears. Reforms and an economic upswing are reinforcing a resilience that has proved striking in the face of two wars and hostile U.S. trade policy.
- In our view, Europe’s institutional stability and deep integration into global trade and capital markets add to its attractiveness for foreign investors.
- For global investors concerned about rising concentration around U.S. AI leadership, Europe could offer both diversification and exposure to a range of structural growth sectors.

Europe is playing to its strengths as it confronts its challenges. Investors are taking note.

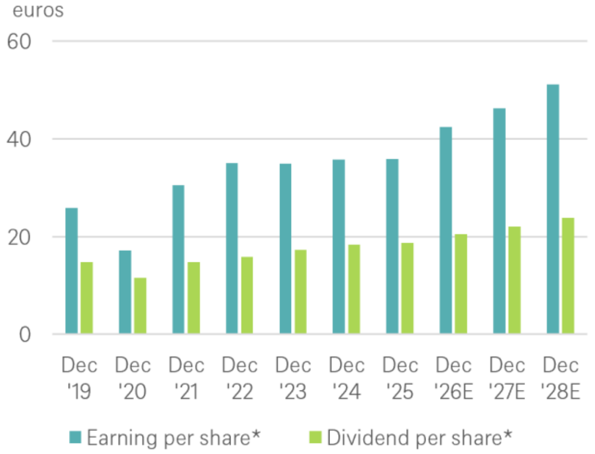
Europe is neither roaring ahead nor falling apart. It is moving in the right direction and in many cases, its companies are moving faster still.

International investors rarely pay much attention to European politics, unless it threatens the integrity of the euro (EUR), as it did during the sovereign debt crisis in 2011 or unless improving sentiment is reflected in markets, as it is today with European equities near record highs. Yet old reflexes persist: Europe will never be as dynamic as the U.S.; its assets will never be as attractive. To which we would reply: capital markets are driven not by absolutes, but by changes in perception and relative valuations. While Europe’s starting point may be admittedly low, the direction of travel is increasingly positive. As we aim to show in this report, those shifts rest on structural as well as cyclical foundations. We believe that Europe is in the middle of its most profound transformation since World War II as a result of various exogenous shocks it has faced over the past decade. As for the cyclical part, various indicators (gross domestic product (GDP), order intake, exports) are all pointing in a positive direction. In fact, in the first half of the year, the Eurozone was almost growing at the same pace as the U.S.,[1] showing surprising resilience in the face of the Ukraine war, U.S. tariffs and the Iran war.

[1] The Eurozone (ex. volatile Ireland) GDP run rate for 2026 is 1.2% after 1H26; close to potential growth of 1.25% and not far behind the U.S. with 1.5%.

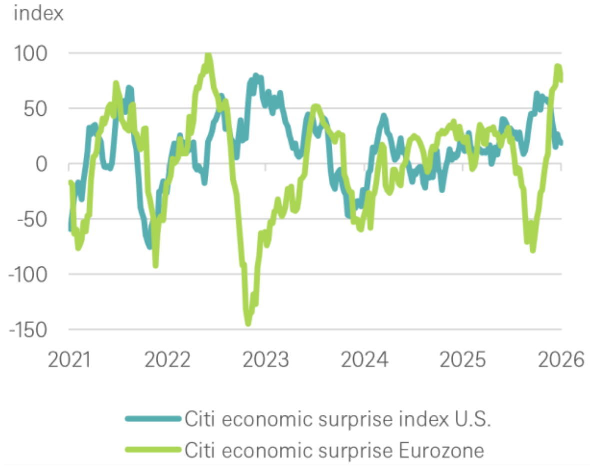
European economy and corporates are exceeding expectations

Figure 1: European earnings on upward slope



Sources: DWS Investment GmbH, FactSet consensus as of 8/18/26. *STOXX Europe 600

Figure 2: Economic surprise indicators mirror Europe's unexpected resilience in the face of wars and tariffs



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 09/04/26

Europe is in transition, and transitions create opportunities

Concerning relative valuation, we believe that Europe's discount to the U.S. is exaggerated, not least because putting all eggs in the U.S. basket comes with various strings attached. Three stand out. First, the U.S.' business model as well as its capital markets have become heavily skewed to the AI trade, increasing concentration risk. Second, U.S. growth is being supported by large fiscal deficits, pushing public debt ratios higher[2] and raising long-term borrowing costs with 30-year Treasury yields hitting 20-year highs;[2] which in turn also contributes to thirdly, a declining willingness of the rest of the world to deepen ties with the U.S., which has shown a growing preference for bilateral deals and transactional flexibility over multilateral rules and institutions. Against this backdrop, Europe's supposedly "boring" consensus-driven approach begins to look rather more attractive. At the same time, Draghi's competitiveness agenda[3] provides a roadmap for stronger investment, deeper capital markets and higher productivity growth. Critics might argue that implementation is proceeding at characteristically "European speed." We would focus instead on the change in direction: the need for reform is now widely recognized across most European capitals, the political pressure to act has arrived, and change is coming.

Investors are beginning to take notice. European stock markets have broadly kept pace with the U.S. over the past 12 months, supported by the strongest earnings season since 2021[4] (earnings per share (EPS) year-over-year (y/y) up by over 20%, the strongest pace since 3Q2022, despite the headwinds already mentioned). This matters because it suggests that the case for Europe is no longer simply one of attractive valuations. After years of relative earnings stagnation, Europe is increasingly becoming an earnings growth story. The opportunities are also changing. Equity market leadership is increasingly shifting towards the sectors of "New Europe" exposed to rising investment, electrification, defense and strategic autonomy. Beyond public equities, infrastructure, private credit and real estate stand to benefit directly from Europe's emerging capital expenditure cycle, while European fixed income is supported by comparatively favorable debt-sustainability dynamics. More importantly, this is unlikely to be a story measured in quarters. Europe's transformation will likely take years to unfold; we therefore consider it a strategic investment opportunity rather than simply a tactical trade.

[2] Congressional Budget Office (CBO), The Budget and Economic Outlook: 2026 to 2036, February 11, 2026
[3] European Commission (September 2024). The Draghi report on EU competitiveness
[4] Goldman Sachs Research, August 20, 2026

1 / Europe’s economy is in transition

1.1 Why Europe is what it is – or was what it was

Playing by the rules was Europe’s idea to stop internal conflicts and expand global trade…

Europe's post-war development was built on the principle of "Wandel durch Handel" or "change through trade." Trade was not merely viewed as an economic tool but also as a mechanism for preserving peace. The European Coal and Steel Community, founded in the early 1950s, deliberately linked national economies together to make future military conflict economically impossible, enabling Europe to become one of the world's most integrated economic regions. Over time, trade delivered both political stability and economic prosperity. Globalization expanded Europe's economic reach and reinforced its manufacturing leadership.

Tabe 1: Europe: Past – Present – Future

	Past	Present	Future
Overarching theme	Peace & prosperity	Transition	Resilience
Characteristics	• Trade-openness • Manufacturing-heavy • Social market economy	• Russian aggression • China’s competition • U.S. retrenchment	• Defense • Autonomy • Diversification

Source: DWS Investment GmbH, as of September 2026

In our view, Europe thus enters this transition from a position of greater strength than many investors appreciate. The region combines global leadership in innovation, strong institutions, deep industrial expertise, a large consumer market, substantial household savings and comparatively healthy sovereign balance sheets. The challenge is not a lack of resources, but rather the effective deployment of capital toward strategic priorities.

… but the international rule-based trade framework is no longer of everyone’s liking

The strategic environment has changed. Europe now faces trading partners and geopolitical competitors that do not necessarily share the same assumptions about openness and interdependence. As a result, Europe is shifting from maximizing efficiency toward balancing efficiency with resilience.

1.2 The triple whammy that made reforms no longer an option but a necessity

Covid, wars and tariffs should have hit Europe disproportionately hard

Europe is undergoing its most profound economic and geopolitical transformation since World War II. The post-war model that prioritized trade openness, manufacturing competitiveness and economic interdependence delivered decades of prosperity but also created strategic vulnerabilities in energy, defense and technology: Trade openness reached roughly 50% of GDP,[5] manufacturing remained significantly larger than in many developed peers, energy dependence increased, defense spending remained comparatively low and its dependence on non-European digital infrastructure and technology platforms continued to grow.

Four major developments in the 2020s have accelerated Europe's strategic rethink. First, China's rise has transformed a key export market into an increasingly formidable industrial and technological competitor. Second, the Covid pandemic exposed the vulnerabilities embedded in globally integrated supply chains. Third, Russia's invasion of Ukraine triggered an energy crisis that laid bare Europe's dependence on external suppliers for critical resources. Finally, the United States has signaled a reduced willingness to shoulder Europe's security burden.

[5] Trade openness is defined as ratio of external trade to GDP. European Centre for International Political Economy (ECIPE), March 2024.

What previously appeared to be strengths increasingly became sources of vulnerability. The challenge facing policymakers today is not to abandon globalization but to ensure that openness does not translate into excessive dependency.

1.3 Rebuilding Europe's sovereignty – from an underappreciated base

Autonomy, efficiency, resilience

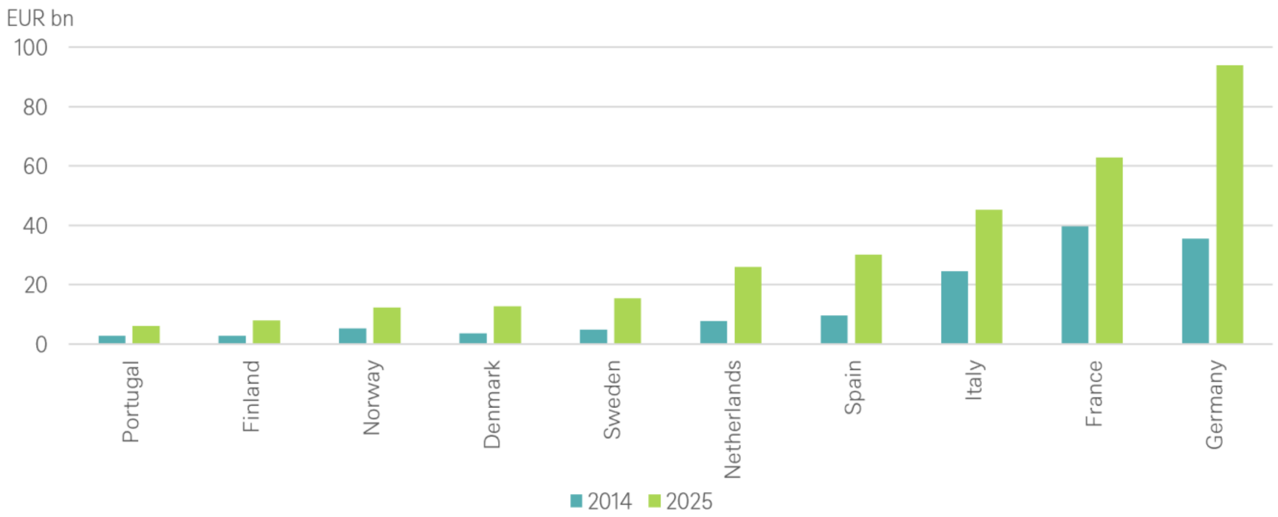
Despite concerns about competitiveness, Europe retains substantial structural advantages. The region combines a large consumer market, significant R&D spending, strong universities, global industrial champions and considerable household savings. Europe also benefits from strong institutions and governance. These institutional strengths provide an important foundation for long-term capital formation and economic resilience. The key issue is therefore not a lack of capability. Rather, it is a question of perception, execution and capital allocation. If Europe successfully mobilizes its existing resources, the region could achieve a meaningful re-rating in the eyes of global investors.

How to regain autonomy in critical fields

Europe is not abandoning its traditional principles. Instead, it is adapting them. Trade remains important, but diversification is becoming a priority. Rules remain important, but pragmatism is increasing. Fiscal discipline remains important, but investment is becoming more prominent.

The roadmap for this transition is the Draghi Report. Its objectives include scaling annual investment, accelerating innovation, deepening capital markets and improving energy competitiveness. Some two years after it was presented, 16% of the recommendations are dealt with and another 25% are already being addressed actively according to Draghiwatch.eu.

Figure 3: European defense spending has seen extreme growth



Source: NATO, DWS Investment GmbH; as of 6/3/26

The significance of the plan lies less in any individual measure and more in the recognition that Europe's competitiveness challenge requires a coordinated response. For investors, this provides visibility in the sectors most likely to benefit from future policy support.

Germany is at the core of Europe's transformation...

Being Europe's largest economy and the one with the greatest fiscal leeway (debt to GDP ratio below 65% compared to an average of 88% for the Eurozone and more than 120% for the U.S.), Germany sits at the heart of Europe's re-invention. If reforms can be implemented and investment unlocked there, the benefits should extend well beyond Germany's borders. The turning point came in 2025, when Chancellor-designate Friedrich Merz backed substantially higher spending on defense and infrastructure and, crucially, a reform of Germany's constitutional debt brake. Long regarded as a symbol of German fiscal discipline, the debt brake had become unusually restrictive compared with the fiscal frameworks of many other developed countries. In July 2026, the governing coalition followed up with an impressively broad reform package. The

34-point reform package targets some of Germany's most persistent structural weaknesses: excessive bureaucracy, chronic underinvestment and supply-side constraints. We believe the prospects for meaningful implementation are relatively high. Taken together with other measures already approved or underway, these reforms have the potential to mark a structural turning point for the German economy. If successfully implemented, their significance could ultimately be comparable to "Agenda 2010," Gerhard Schröder's landmark 2003 reform program. These measures helped to reduce labor costs, increase employment flexibility and support Germany's export competitiveness during the following decade.

Figure 4: German industrial orders are picking up; we expect production to follow

*3 months moving average. Sources: Haver Analytics Inc., DWS Investment GmbH as of 9/7/26.

Despite widespread skepticism, the German economy was already showing tentative signs of improvement in 2025, before the recovery was disrupted by punitive U.S. tariffs and, more recently, the economic fallout from the war in Iran. We now see Germany returning to an expansionary trajectory, reflected in solid growth in industrial orders since autumn 2025. We think the combination of structural reforms and an improving cyclical backdrop could create an increasingly favorable environment for German capital markets particularly at a time when global investors search for alternatives to highly valued, AI-related sectors concentrated in the U.S. and Asia. Indeed, some of the most important elements of Germany's reform agenda may also be underappreciated. Beyond the headline increases in defense and infrastructure spending, measures to streamline bureaucracy, improve labor market flexibility, reform the tax system and deepen domestic capital markets could have an even more lasting effect on Germany's growth potential.

... and might finally catch up with international pension scheme standards, potentially boosting German assets

Germany's pension reform marks the most significant overhaul of the system in two decades, with the key shift being a gradual move toward funded, capital-market-based pension investment. Germany's pension system rests on three pillars: state pensions, occupational pensions and private savings. The first pillar faces demographic pressure and rising fiscal costs, while the second pillar has limited coverage and the third needs to draw more savers into capital-market investments. The current reform focus is on Pillar 1, under which part of future income is expected to be invested over time.

Germany remains underrepresented in global pension assets, producing 4% to 5% of global GDP but holding only about 1% of global pension assets. Pension assets amount to only around 10% of GDP, far below some OECD countries where funded pension assets are as high as 150% of GDP.[6] This means the reforms start from a low base but could gradually increase capital-market participation.

Investment behavior may also change. As non-guaranteed products emerge in Pillars 2 and 3, and funded investments are introduced into Pillar 1, we believe allocations are likely to shift toward riskier long-term assets such as equities. If 2% of

[6] Thinking Ahead Institute, 2025

income flows into funded Pillar 1, about EUR 35 billion could be added annually,[7] creating a sizeable pool over time once returns are included.

The final market impact will depend on who manages the assets and how they are invested. A globally diversified approach would limit local effects, while a stronger home bias could support German markets. Even a 25% allocation to German equities could have a meaningful impact, although the final outcome remains uncertain.

Potential repercussions of election outcome in Sachsen-Anhalt

On September 6, regional elections in the eastern German state of Saxony-Anhalt delivered a decisive victory for the right-wing Alternative für Deutschland (AfD), which came close to securing an outright majority. Further regional elections in Berlin and Mecklenburg-Vorpommern, also in eastern Germany, are scheduled for September 20.

While the outcome in Saxony-Anhalt had been broadly anticipated and therefore should not have come as a surprise, we are nonetheless somewhat concerned by the apparent shock with which the established parties have reacted to the result. Our primary concern is that these election outcomes could prompt one of the governing coalition partners in Berlin to reconsider its support for key elements of the reform agenda.

That said, with more than two years remaining in the current legislative term, our base case remains that the federal coalition will continue to view the reform package as a compelling proposition for voters. Although we do not expect all 34 measures to be implemented in their current form, we believe the coalition remains committed to preserving the core pillars of the reform program.

1.4 Where are we standing? Economic growth close to U.S. and potential growth

Growth despite biggest energy crisis in history

We expect 1.3% GDP growth for the Eurozone in 2027. Is that really a reason to get so excited? Yes, it is, for three reasons: First, don't forget that as a result of demographics, Europe's potential growth is as low as 1.25%. Second, keep in mind that the U.S.' growth (we expect 2.0% for 2027) is dependent on the state running a budget deficit that is not only around twice that of the European Union for 2026 and 2027 but is also excessively high in absolute terms: 6.6% according to our estimates for 2026 and 2027. And third, one needs to acknowledge that European growth has been achieved despite what the Head of the International Energy Agency back in late April called the biggest threat to energy supply in history,[8] obviously affecting Europe disproportionately harder given it is a large energy importer compared to the U.S.'s status as a net energy exporter.

The euro area recovery is showing broader signs of gaining traction. GDP for the second quarter expanded by 0.4% QoQ,[9] the strongest quarterly growth in over a year, twice the consensus expectation while Germany grew by 0.3% QoQ and 1.0% YoY (real, seasonally adjusted). This stronger-than-expected performance has contributed to an upgrade in our 2026 German GDP growth forecast from 1.0% to 1.3%.[10]
August's survey data suggest that manufacturing is becoming an increasingly important driver. The final euro area manufacturing PMI rose from 51.9 to 52.7 in August, its highest level since May 2022, while Germany's PMI increased from 52.2 to 54.3 in the same month, the strongest reading in more than four years. In addition, new export orders in the euro area increased for only the second time in four-and-a-half years, with particularly strong overseas sales reported in Germany.

This has translated into a strong improvement in the Eurozone Citi Economic Surprise Index, which recently had its highest reading since 2022, and is now outperforming the U.S. (Figure 2). Taken together, these data point to a recovery that is becoming more industrial and export-led, although its durability will depend on whether stronger orders translate into a sustained pick-up in investment and production.

[7] Bundesministerium für Arbeit und Soziales (BMAS), 2026
[8] In the same interview he said "The global energy crisis caused by the war in Iran is equivalent to the combined force of the twin oil shocks of the 1970s and the fallout of Russia's invasion of Ukraine"; The Guardian; 04/26/26
[9] All data Bloomberg Finance L.P. as of 8/14/26
[10] Please note that part of the adjustment is due to us publishing non-calendar-adjusted numbers going forward in order to make our forecasts comparable with discussions in the German media

1.5 Europe is in transition, but not beyond all recognition

Demography, regulation and resources

Enough has been said about Europe's tendency to over-discuss, over-regulate and over-caution. Its demographic challenges are real – birth rates of around 1.34[11] – but hardly unique among the world's major economies. More distinctive are Europe's strategic dependencies on imported energy and critical raw materials, on the U.S. for defense, and on foreign technology, software and payment systems, well beyond AI. Yet herein lies part of the opportunity. Many of Europe's most obvious vulnerabilities are precisely those that it is now seeking to address. This has become part of the positive investment case for the region.

Table 2: Europe: The underappreciated leverage

Demand & balance sheet power		Innovation & knowledge scale		Corporate execution at scale	
450mn consumers ~€9-10tn consumption	Large, resilient consumer base	€400bn annual R&D >3% annual R&D/GDP	Strong intellectual capacity	Airbus	Proven cross-border coordination
13–15% saving rate ~€2tn NIIP*	Excess savings push deployable capital	700+ top universities	Deep talent pipeline	45% GER share global	Hidden champions engine ("Mittelstand")
82% debt/GDP	Sovereign balance sheet optionality	43% European patents (EPA)	Applied innovation strength		

* The net international investment position provides an aggregate view of the net financial position (assets minus liabilities) of a country. Source: Eurostat, World Bank, ECB, European Commission, EPA, DWS Investment GmbH, as of June 2026

What about Europe's hot summer blues:

Low water levels, such as those currently affecting the Rhine, are no longer exceptional events. Companies have repeatedly faced similar conditions in recent summers and, where reasonably possible, have adapted their operations accordingly. In more severe cases, however, transport bottlenecks and water shortages may still force some companies to scale back production. More broadly, while prolonged hot weather and drought can weigh on agriculture, industrial output and some forms of tourism, these effects are partly offset by gains elsewhere in the economy. We therefore expect the overall impact on annual GDP growth to remain relatively modest and below the threshold at which it would materially alter the macroeconomic outlook.

For expectation management's sake: this is a marathon, not a sprint

All being said, we believe many investors are likely to remain skeptical about Europe's reform capacity and speed of implementation. We see the opportunities created by the reform package less in a short-term market reaction than in a gradual rebuilding of confidence. Visible progress on implementation, investment momentum and reducing bureaucracy should, over the medium term, help improve international investors' perception of German and European assets.

2 / Asset Classes

2.1 U.S. vs. Europe – not a one-way street

Size is important, but relative growth has its limits

The dominance of the U.S. in global capital markets is undeniable. The question is whether this dominance is self-reinforcing or whether we are approaching an inflection point. A similar question hangs over U.S. debt: at what point does the relentless rise begin to rattle bond investors and put sustained pressure on the U.S. dollar and Treasury market. Even as U.S.

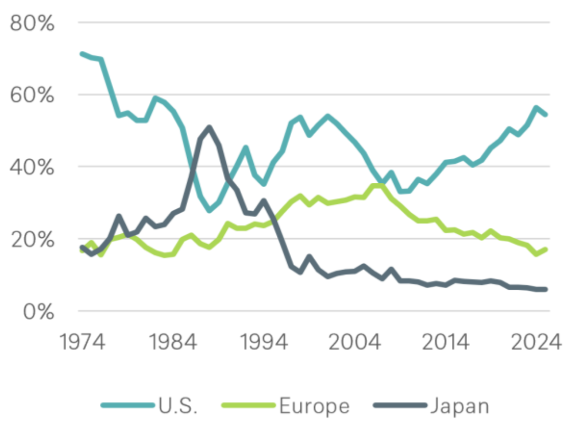
[11] Eurostat, September 2026.

government debt has broken through the USD 40 trillion mark, debt servicing costs have continued to climb, reaching USD 1.4tn over the past 12 months – and are still growing - and long-dated Treasury yields have hit 20-year highs, the response remains remarkably nonchalant: what, after all, is the alternative to U.S. capital markets?

For now, that remains a powerful argument, but it should not be mistaken for an immutable law. The U.S. accounts for roughly a quarter of global GDP (when measured in USD, not on purchasing power parity) but sits at the center of a vastly disproportionate share of global financial assets and borrowing. Scale is one of America's greatest financial strengths, but, increasingly, the debt required to sustain it may also become a source of vulnerability. The question for investors is therefore not necessarily whether the U.S. will lose its pre-eminence, but whether other markets will become more attractive for global capital to diversify.

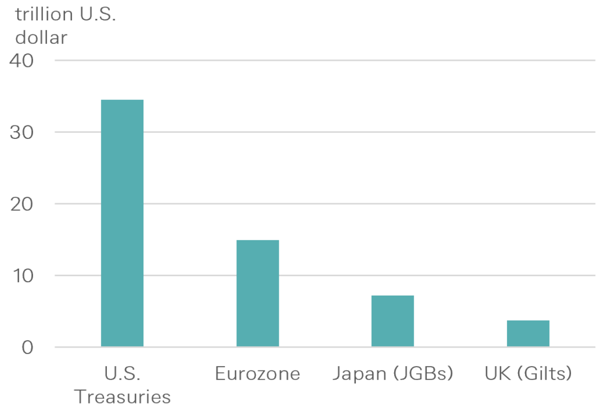
Capital markets – U.S. dominate. Still, despite or increasingly?

Figure 5: Equity markets: share of total global market cap



* Regional Equity indices from LSEG/ Datastream
Sources: LSEG, DWS Investment GmbH as of September 2026

Figure 6: Absolute size of bond markets



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 8/18/26

Returning to equity markets, the usual explanation for their disproportionate size is the higher valuation multiples they command – an issue we will return to later. But there are two other important issues. First, the gap between labor and capital income in the U.S. is large and has been widening, allowing U.S. companies to capture an increasing share of domestic GDP as profit; and second, U.S. companies have also been securing an increasing share of global profits, as Bloomberg's Simon White recently highlighted (see figure 7). This raises an important question: can this (mainly tech-driven) trend continue unabated, particularly as a growing number of countries seek to reduce their dependence on the U.S. wherever possible?

Figure 7: U.S. claims an ever-larger share of global profits: MSCI US share of MSCI World earnings

Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 09/04/26

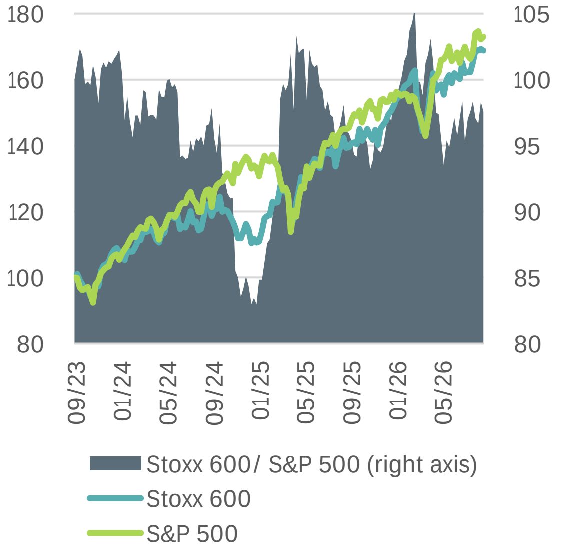
U.S. dominance also has an important implication for international capital flows. Because U.S. assets account for such a large share of global portfolios, investors do not need to make especially large reallocations away from the U.S. for other markets to experience substantial net inflows. Even modest portfolio diversification can therefore have an outsized impact on the relative demand for, and valuations of, non-U.S. assets. This brings us to the next point: relative outperformance has its limits.

Europe’s performance needs no excuses

Looking at entire markets, which is what Figure 8 is doing, shows: a) that European stocks have delivered rewarding absolute returns over the past decade. More recently and particularly over the past two years, they have also outperformed U.S. equities on a relative basis. The same pattern can be observed at the sector level. European banks are a prime example of how prolonged relative underperformance can eventually give way to renewed outperformance. After remaining largely untouchable for many years following the Global Financial Crisis, European banks have not only demonstrated that they can once again generate respectable returns on equity; they have also shown that they can keep pace with some of the “hottest”. sectors in the U.S.

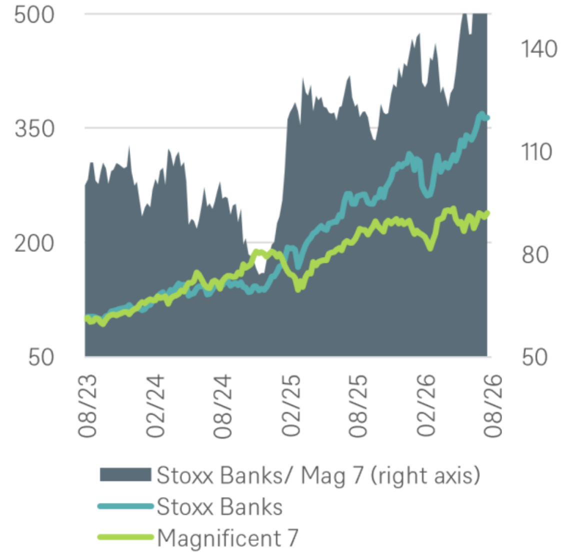
Europe compares quite well with U.S. since post Covid recovery, some sectors even outperforming the U.S. elite

Figure 8: Stoxx 600 and S&P 500 (indexed: 9/8/23 = 100)



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 8/28/26

Figure 9: European banks vs Mag7 (indexed: 9/8/23 = 100)



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 8/28/26

2.2 Why diversifying a U.S. (AI) centric portfolio might make sense

In our view, looking beyond the United States and towards European capital markets when seeking diversification is increasingly justified. Although the U.S. continues to benefit from technological leadership and stronger economic growth, many of the forces behind its outperformance are also creating vulnerabilities.

As discussed earlier, high public-debt ratios are becoming an increasingly important concern, particularly as persistent budget deficits show little sign of abating. This leaves AI as a more immediate risk factor. The U.S. economy has become heavily reliant on an investment boom with a significant share of current GDP growth linked to AI-related spending. Yet the sustainability of this trend is increasingly being questioned. Massive investment in data centers, semiconductors and computing infrastructure is driving corporate leverage higher and may add to inflationary pressures. Investors are also asking whether future revenues justify current spending levels, particularly in light of intensifying competition from China, uncertain monetization prospects, regulatory risks and bottlenecks in the infrastructure required to support further expansion.

The AI boom has also increased concentration risk. The ten largest U.S. stocks, predominantly technology companies, now account for nearly 40% of total U.S. market capitalization. In Europe, the top ten constituents of the MSCI Europe Index represent only around 20%. Concentration risk is not confined to equity markets as it is increasingly evident in bond markets as well. AI-related companies already account for nearly 40% of longer-duration IG corporate bond issuance, while their financing needs continue to grow. Additional concerns stem from the complex financing arrangements developing across the AI ecosystem, including vendor financing and interconnected investment structures. These relationships could amplify risks if growth expectations disappoint or projected returns fail to materialize.

Questions are also emerging about the quality of earnings among some large technology companies, as growth in reported earnings per share increasingly outpaced underlying cash-flow generation.

Beyond economics, geopolitical developments also strengthen the case for greater diversification. The U.S. appears less and less committed to promoting multilateral trade frameworks and open global commerce, encouraging other countries to reduce their dependence on the dollar-based financial system and on U.S. leadership in areas such as trade, defense and technology.

Against this backdrop, we believe Europe offers investors an interesting diversification opportunity. Valuations remain generally more attractive, market concentration is significantly lower, and the region provides exposure to a broader range of sectors, including industrials, healthcare, financials and luxury goods. European capital markets may therefore offer a way to reduce dependence on U.S. fiscal policy, technology valuations and the AI investment cycle while retaining exposure to global economic growth.

The case for Europe is not that the U.S. is losing its innovative edge. Rather, it is that portfolios have become increasingly dependent on a narrow set of U.S. drivers. As concerns about debt, deficits, market concentration and AI-related risks grow, European capital markets could offer a valuable source of diversification and resilience.

2.3 European Fixed Income - diversity, yield and depth

We believe that European fixed income is no longer just a low-yield defensive allocation. In our view, it is a credible, income-generating and increasingly diversified opportunity set for global investors. Government bonds can provide diversification and fiscal differentiation, while investment grade credit could add spread, carry and sector breadth.

European Government Debt - fiscal credibility in a world repricing debt sustainability

In our view, European sovereign debt offers a relatively stronger fiscal anchor in a world where investors are once again pricing debt sustainability very carefully. Across developed markets, these concerns show up differently - both in fundamentals and in pricing: in the U.S., concerns center on expansionary fiscal policy, political uncertainty and worries around Fed independence and learning how to read the new Fed chair.

In Japan, long-end yields have recently moved higher, reflecting concerns about fiscal stability following election-driven spending. In the UK, political instability has translated directly into higher risk premia and pronounced yield spikes. In these three cases, long-end yields have repriced significantly – with up to 172 bps for Japan during the last two years. Against this backdrop, Europe appears more stable. Not because it is free of fiscal challenges - it is not - but because the starting point is comparatively stronger and it has stricter fiscal rules.

European Investment Grade Corporate Bonds (Credit)

European investment grade credit has changed. It is no longer just a defensive, regionally concentrated market. It is becoming broader, more diversified and increasingly relevant for global issuers - including high-quality technology and AI-related borrowers. Historically, EUR IG was heavily associated with financials, utilities and telecoms - solid sectors, but also a market with clear concentration risk. That picture is changing. The market is broadening across sectors, geographies and business models.

In many ways, EUR credit is moving closer to the U.S. model: more diversified and more globally relevant. One of the clearest examples is the arrival of large global technology issuers in the euro market. Alphabet is a good illustration: it moved very quickly from being effectively absent in euro credit to becoming the eighth largest index member. Indeed, U.S. corporates already account for a fifth of the EUR IG benchmark, with the country on track to overtake France as the largest single issuing country within the index. This changes the EUR IG market. U.S. issuers often bring very high credit quality, long-duration supply and spreads that can look attractive relative to the underlying balance-sheet strength. This is an important structural shift - the euro market is increasingly being used not just as a regional funding market, but as a global funding currency.

2.4 European Equities: earnings growth finally back, but it is not a cyclical play anymore

Rebalanced and record highs, profit estimate upgrades and relatively cheap

The three things we consider most notable about European equities today are: European companies do not earn most of their money in Europe; the market's sector composition is changing in ways that make it less cyclical and more structurally driven; and earnings are growing again. European equities are no longer supported solely by a valuation discount. Increasingly, they are backed by a strengthening earnings story.

The first point is particularly important. European equities are often treated as a direct reflection of the European economy, yet the listed market is far more global than many investors appreciate. Around 80% of DAX revenues are generated outside Germany, while approximately 55% of Stoxx Europe 600 revenues originate outside Europe and the UK. As a result, European corporate earnings are influenced at least as much by global investment cycles, U.S. demand, emerging-market growth and commodity markets as by domestic economic conditions. In our view, European equities should therefore not be viewed simply as a leveraged bet on Eurozone GDP growth.

At the same time, the composition of the European market is undergoing a profound transformation. The traditional image of Europe was built around consumption, exports and cost efficiency, with sectors such as autos, chemicals and consumer goods dominating investor attention. While these industries remain important, a new set of growth drivers is emerging. Increasingly, earnings growth is being generated by companies exposed to defense spending, industrial automation, electrification, grid infrastructure, data centers, semiconductor technology and financial services. These sectors benefit directly from Europe's pursuit of energy security, strategic autonomy, digitalization and industrial modernization.

This evolving market structure is gradually changing the nature of European equities. Rather than behaving as a highly cyclical market driven primarily by global trade and manufacturing activity, Europe is becoming increasingly exposed to long-term investment themes. Bank of America estimates that the domestic portion of European revenues, which accounts for roughly 45% of total sales, is heavily concentrated in financials, defensive sectors and commodities. At the same time, Europe has greater technology exposure than many investors assume. Approximately 14% of the MSCI Europe Index consists of companies directly exposed to AI-related capital expenditure. These companies continue to rank among the strongest contributors to positive earnings revisions, while earnings momentum is broadening well beyond pure AI beneficiaries.

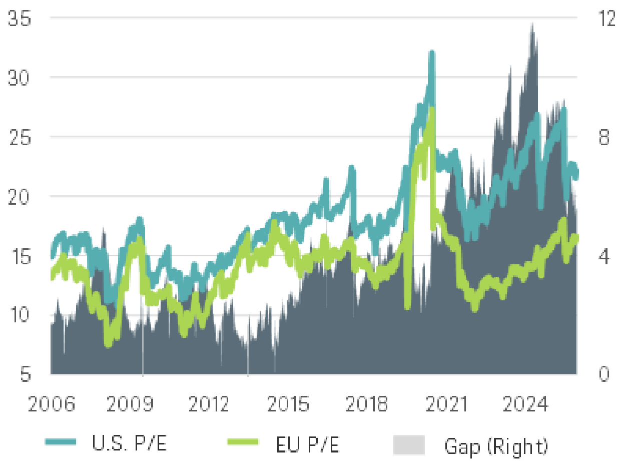
Valuation

European equities continue to trade at a meaningful discount to U.S. equities. The Stoxx Europe 600 currently trades at roughly a 25% discount to the S&P 500 on a price-to-earnings basis, compared with a long-term average discount closer to 20%. Part of this valuation gap is justified by sector composition. The U.S. market remains more heavily weighted toward technology and structural growth sectors, which typically command higher multiples.

However, aggregate index comparisons risk overstating the valuation difference. When sectors are compared on a like-for-like basis, the discount narrows substantially and, in some cases, disappears altogether. Furthermore, the sector composition

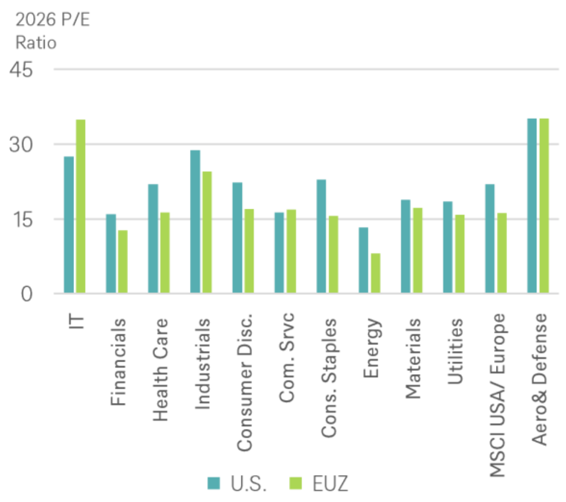
Near-record high valuation gap – only partly justified

Figure 10: Next 12m P/E Ratio MSCI US vs MSCI EUZ



Sources: Bloomberg Finance L.P., DWS Investment GmbH as of 8/14/26

Figure 11: P/E Ratio comparison by sector, 2026 earnings estimates



Sources: LSEG Data and Analytics., DWS Investment GmbH as of 8/18/26

of European markets is gradually shifting towards areas of structural growth, including industrial technology, electrification, semiconductors and infrastructure-related businesses. European companies are also increasingly adopting shareholder-friendly practices such as share buyback programs, historically a stronger feature of U.S. markets. Taken together, these developments suggest that the valuation gap could narrow further over time as investors increasingly recognize the changing quality and composition of European earnings.

Earnings season – strong quarter led to full year earnings upgrades

Perhaps the strongest argument for European equities today comes from earnings. The current reporting season has delivered some of the most encouraging results in years. Second-quarter revenues are growing by approximately 7% year-on-year, while earnings per share have increased by more than 20%, the strongest pace since the third quarter of 2022. First-half earnings growth is tracking close to 14% year-on-year, also representing the fastest expansion in three years. Equally important, the earnings′ revision cycle continues to improve. Consensus expectations for full-year earnings growth have risen to nearly 17%, and analysts continue to revise forecasts upward rather than downward.

This strength is closely linked to several sectors driving the market. Real assets, banks, infrastructure-related businesses and technology enablers continue to generate positive earnings′ surprises and upgrades. Far from fading, earnings momentum appears to be broadening. In our view, this is providing a more durable foundation for equity returns than valuation expansion alone.

Our preferred sectors – investing in the New Europe

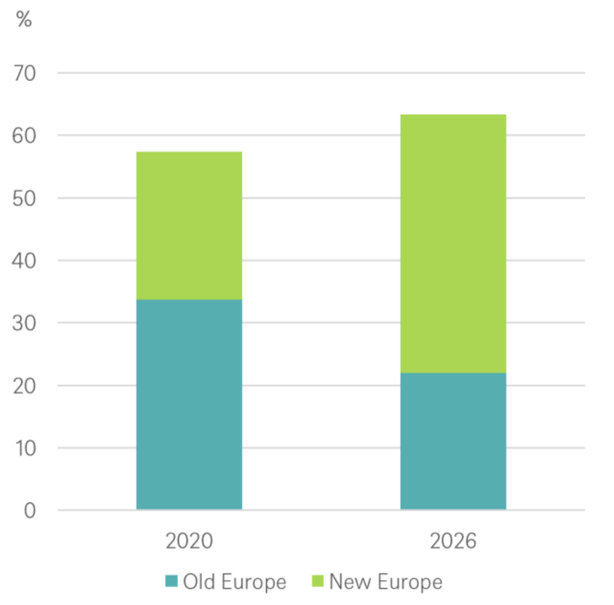
The distinction between "Old Europe" and "New Europe" provides a useful framework for understanding where opportunities lie. Old Europe was built around consumption, exports and efficiency. New Europe is being shaped by investment, resilience and strategic autonomy.

Europe was not the primary beneficiary of the first phase of the AI boom, which was dominated by U.S. hyperscalers and technology platforms. However, Europe may become one of the largest beneficiaries of AI deployment across manufacturing (think robotics, for example), industrial processes and services. The continent's strength lies not in building the largest AI platforms, but in applying technology across a broad industrial base.

Against this backdrop, our preferred sectors remain Capital Goods, Banks, Semiconductors and Utilities. The combined market capitalization weight of these sectors has risen from around 25% in 2015 to approximately 40% today, highlighting the extent of Europe's structural transformation.

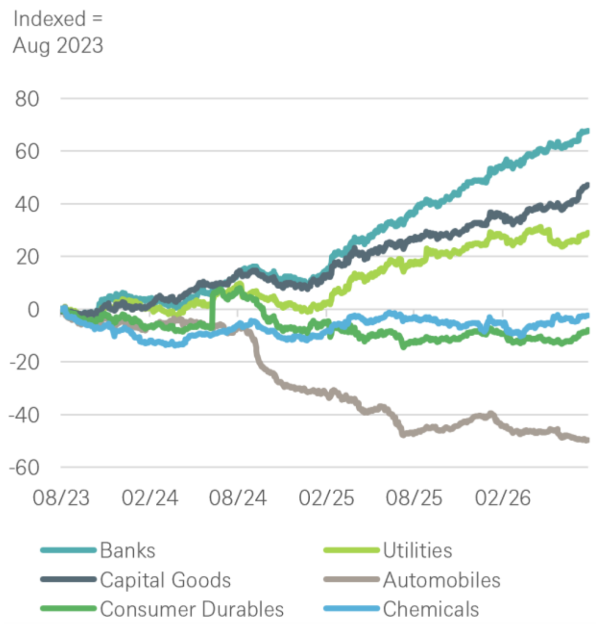
New versus Old Europe, according to DWS

Figure 12: "New" sectors gain weight in MSCI Europe



Old Europe sectors: Materials, Food & Beverages, Consumer Durables, Communication Services, Household Products, IT Services, Automobiles
New Europe sectors: Capital Goods, Banks, Semiconductors, Utilities; Sources: Bloomberg Finance L.P., DWS Investment GmbH as of June 2026

Figure 13: "New" sectors with stronger EPS growth*



* based on consensus next 12m EPS forecasts.
Sources: Bloomberg Finance L.P., DWS Investment GmbH as of June 2026

Importantly, markets still tend to value Europe as an old-economy market, while an increasing share of earnings growth is generated by sectors aligned with the new economy. Order books, capital-expenditure cycles and earnings revisions all point toward continued strength in banks, utilities, industrial champions and technology leaders.

In our view, Europe is undergoing a transition from a macro-driven market to a stock-picker's market. Electrification, industrial modernization, defense spending, infrastructure investment and digital transformation are creating a widening gap between winners and losers. Assessing Europe through the lens of its past may mean missing the opportunities emerging from its future. The New Europe is already visible in earnings growth, sector leadership and capital allocation trends. Market recognition of this transformation may still have further to run.

2.5 Alternatives: main beneficiary of fiscal packages?

Real Estate - structurally low supply in residential

European real estate benefits from exceptionally strong supply-demand fundamentals. Vacancy rates across residential, logistics and office markets remain below U.S. levels, while development activity has fallen to historic lows due to planning restrictions, ESG requirements, financing constraints and construction costs. Despite strong and persistent rental growth over the past five years, in many sectors, current rents remain below the level required to justify new developments, limiting future supply, particularly for new, high-quality stock.

As European fiscal and capital expenditure programs accelerate, we expect demand for space to increase while supply remains constrained. This should support high occupancy, rental growth and asset value appreciation. Europe's more regulated market structure should also reduce the risk of overbuilding, creating a less volatile and more predictable occupational market, which, when well understood and appropriately priced, could provide a structural advantage over less regulated regions.

We expect European real estate to outperform both the U.S. and Asia-Pacific over the next five years, with the logistics and residential sectors forecast to see some of the highest risk-adjusted returns over this period. In our view, both will in themselves be an important part of Europe's growth story, from supply chain resilience to urban vitality, and we expect both to benefit from sustained structural demand. Residential, with occupancy rates closing in on 100% in many cities, looks very well placed to us, providing a strong and stable income return or an attractive opportunity for investors to deliver space into stock starved markets through refurbishment or repositioning non-core real estate.

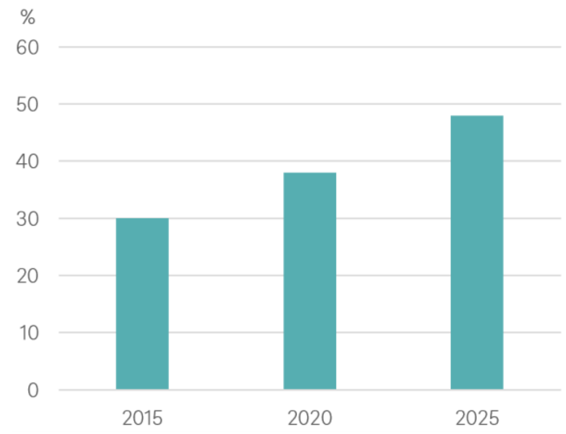
Infrastructure – focus of transformation

Europe's infrastructure investment case is driven by three strategic priorities: energy security, digital sovereignty and economic resilience. This is creating a multi-decade investment cycle across power, digital, transport, communications and industrial infrastructure that is expected to drive sustained demand for private capital. We believe Europe already offers a compelling infrastructure investment proposition, offering these significant capital investment requirements along with strong policy support, visible long-term demand drivers and a broad spectrum of investable opportunities. In our view, European midmarket infrastructure in particular offers significant potential for attractive entry valuations with prospect of creating truly pan-regional assets.

To us, the energy transition remains one of the most significant investment opportunities. Europe is seeking to reduce dependence on imported fossil fuels while meeting increasingly ambitious decarbonization targets, requiring unprecedented investment in renewable generation, electricity transmission and distribution networks, battery storage, interconnection assets and energy efficiency infrastructure. Electrification of transport, industry and heating is expected to place considerable strain on existing networks, creating substantial opportunities for grid expansion and modernization. Importantly, these investments are not only driven by climate policy but also by economic and energy security considerations, providing multiple layers of support across market cycles.

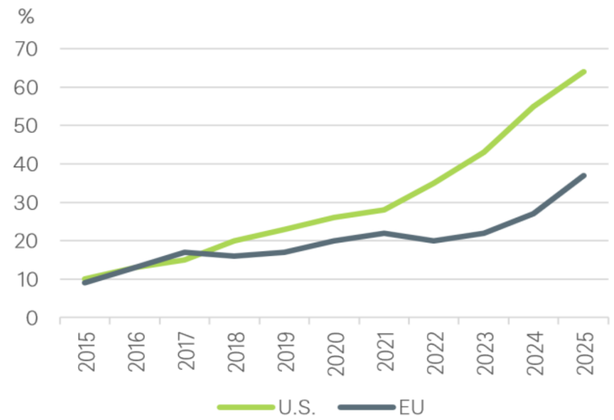
The Old Continent is not stuck doing old things – there is ongoing transformation

Figure 14: Share of electricity production from renewables in Europe



Sources: Our World in Data as of June 30, 2026

Figure 15: Share of AI-related financing in Venture Capital



Sources: ECB as of March 23, 2026

Alongside the energy transition, Europe is rapidly expanding its digital infrastructure footprint. The growth of artificial intelligence, cloud computing, digital services and data-intensive industries is driving significant demand for data centers, fiber networks, telecommunications infrastructure and associated power assets. While this is true in most regions, European

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policymakers increasingly view digital infrastructure as a strategic asset, recognizing the importance of retaining technological capabilities and reducing reliance on external providers, thus creating demand for European digital capacity, capability and financing.

Beyond energy and digitalization, Europe is entering a broader phase of economic transformation and reindustrialization. Initiatives designed to strengthen supply chains, enhance industrial competitiveness, increase defense capabilities and support advanced manufacturing are expected to require significant investment in transport networks, logistics facilities, ports, industrial infrastructure and defense-related assets. These themes are reinforced by evolving European policy frameworks focused on competitiveness, strategic autonomy and industrial development, which together are helping to create a stable backdrop for long-term infrastructure investment.

Private Corporate Credit: addressing Draghi Report core points

The Draghi Report highlights Europe's structural economic challenges, including a significant innovation gap, a fragmented Single Market, and a need for substantial investment in key strategic sectors like deep tech and industrial innovation. We believe that private credit can play an important role in supporting the growth and competitiveness of the European private sector, particularly the "Mittelstand" (mid-sized companies), which are crucial to the European economy.

3 / Summary – Europe’s comeback – the European way

Europe is stronger than many perceive. Despite two wars on its borders and a hostile U.S. trade stance, reforms and a cyclical upswing are driving resilience. At the same time, global investors’ heavy reliance on the U.S. and the AI trade comes with growing risks. In our view, Europe offers diversification, institutional stability, reform momentum and relatively attractive valuations.

While Europe lacks U.S.-style dynamism, we think change is moving in the right direction. Economic indicators are improving, growth has proven resilient, and the Draghi agenda provides a roadmap for stronger investment, deeper capital markets and higher productivity growth. Investors are taking notice: European equities have matched U.S. performance over the past year, supported by robust earnings growth. Opportunities are emerging in sectors tied to investment, infrastructure and strategic autonomy, while we see fixed income benefiting from comparatively sound debt dynamics. Europe’s transformation will take years, making it a compelling long-term investment story to us rather than a short-term trade.

Glossary

Agenda 2010 refers to the reform program launched by the German government in 2003 to modernize the labor market and social welfare system.
The Alternative for Germany (AfD) is a nationally-conservative and right-wing political party in Germany.
Alternative investments are asset classes or strategies outside traditional stocks, bonds, and cash, such as real estate, commodities, private equity, hedge funds, or infrastructure.
Asia Pacific (APAC) is a term used to describe the economic region Asia-Pacific.
Asset allocation is the division of investments into individual asset classes (e.g. stocks and bonds).
A balance sheet summarizes a company's assets, liabilities and shareholder equity.
A budget deficit is created whenever the spending in a public budget exceeds the income within a given time period
Capital expenditures (capex) are funds used by a company to acquire, maintain, or upgrade long-term physical assets such as property, buildings, or equipment.
Carry (of an asset) refers to the net return or cost of holding an asset over time, typically derived from income such as interest or dividends minus any associated financing or holding costs. A carry trade is an investment strategy that seeks to capture this carry by exploiting differences in yields or interest rates between assets, typically by funding at a lower rate and investing in assets with higher returns.
A company's cash flow is comprised of its inflows and outflows which arise from financing, operational or investing activities.
The Citi Economic Surprise Index (CESI) tracks for various locales how actual economic data compares to consensus forecasts.
Cloud computing encompasses technologies and services that offer the dynamic and flexible use of a third party's IT infrastructure.
Commercial real estate (CRE) refers to properties that are used for business or commercial purposes, such as office buildings, retail spaces, warehouses etc.
Concentration refers to the degree to which a portfolio, market, or index is exposed to a limited number of securities, issuers, sectors, or positions.
A consensus estimate is a figure that depicts the average of different analysts' estimates about the performance of a particular asset.
Core government bonds are debt securities issued by especially credit-worthy governments both within the Eurozone and in other developed markets.
Corporate bond is a bond issued by a company to raise financing for business activities.
Corporate governance refers to the systems, rules, and practices by which companies are directed, managed, and controlled.
Cyclical describes an economic variable, sector, or asset whose performance rises and falls in line with the business cycle.
DAX is Germany's main blue-chip equity index, comprising 40 major companies listed on the Frankfurt Stock Exchange.
Debt brake is a fiscal rule limiting German federal structural borrowing.
Decarbonization is the reduction or elimination of carbon dioxide emissions from a process such as manufacturing or the production of energy.
Diversification refers to the dispersal of investments across asset types, geographies and so on with the aim of reducing risk or boosting risk-adjusted returns.
Duration is a measure expressed in years that adds and weights the time periods in which a bond returns cash to its holder. It is used to calculate a bond's sensitivity towards interest-rate changes.
Earnings per share (EPS) is calculated as a company's net income minus dividends of preferred stock, all divided by the total number of shares outstanding.
Emerging markets (EM) are economies not yet fully developed in terms of, amongst others, market efficiency and liquidity.
The euro (EUR) is the common currency of states participating in the Economic and Monetary Union and is the second most held reserve currency in the world after the dollar.
The European Economic Area (EEA), established in 1992, extends the European Union's single market to specific non-EU member countries.
Eurozone is the group of European Union member states that have adopted the euro as their common currency and legal tender.
Fiscal policy describes government spending policies that influence macroeconomic conditions. Through fiscal policy, the government attempts to improve unemployment rates, control inflation, stabilize business cycles and influence interest rates in an effort to control the economy.
Fixed Income broadly refers to those types of investment security that pay investors fixed interest or dividend payments until its maturity date.
The gross domestic product (GDP) is the monetary value of all the finished goods and services produced within a country's borders in a specific time period.
Inflation is the rate at which the general level of prices for goods and services is rising and, subsequently, purchasing power is falling.
The International Energy Agency (IEA) is a autonomous intergovernmental organization which works to ensure reliable, affordable and clean energy for its 30 member countries and beyond.
Investment grade (IG) refers to a credit rating from a rating agency that indicates that a bond has a relatively low risk of default.
Market capitalization is the total market value of a company's outstanding shares, calculated by multiplying the share price by the number of shares outstanding.
An expansionary monetary policy is a type of macroeconomic monetary policy that aims to increase the rate of monetary expansion to stimulate the growth of the domestic economy. The economic growth must be supported by additional money supply.
The MSCI Europe Index is designed to measure the performance of the large- and mid-cap segments of 15 developed markets in Europe.
A multiple is a ratio that is used to measure aspects of a company's well-being by setting various of the company's metrics against each other and thereby building indicative ratios.
OECD is the Organisation for Economic Co-operation and Development, an international organization that promotes policies supporting economic growth, trade, and social well-being.
Primary issuance is the sale of newly issued securities, such as bonds or shares, directly by an issuer to investors.
Private credit is an asset defined by non-bank lending where the debt is not issued or traded on the public markets.
Purchasing Managers' Index (PMI) is a survey-based indicator of business activity in manufacturing, services, or the broader economy.

Renewables are natural resources or sources of energy that is not depleted by use, such as water, wind, or solar power.
The risk premium is the expected return on an investment minus the return that would be earned on a risk-free investment.
The S&P 500 is an index that includes 500 leading U.S. companies capturing approximately 80% coverage of available U.S. market capitalization.
A semiconductor is a material with electrical conductivity between that of a conductor and an insulator.
Share buybacks are transactions in which a company repurchases its own shares.
A smart grid is an electricity grid that uses information about production and consumption to more efficiently manage distribution.
The spread is the difference between the quoted rates of return on two different investments, usually of different credit quality.
Stagnation in economics is referring to a period characterized by a lack of growth.
The Stoxx Europe 600 is an index representing the performance of 600 listed companies across 18 European countries.
A tariff is a tax imposed by one country on the goods and services imported from another country.
Treasuries are U.S. government debt securities, including Treasury bills, notes, bonds, and inflation-protected securities.
The U.S. dollar (USD) is the official currency of the United States and its overseas territories.
The U.S. Federal Reserve, often referred to as "the Fed," is the central bank of the United States.
Valuation attempts to quantify the attractiveness of an asset, for example through looking at a firm's stock price in relation to its earnings.
A valuation discount means that a stock or market is trading for less than its perceived intrinsic value. For example, European stocks might be trading at lower multiples of their earnings, cash flow, or other fundamental metrics compared to their U.S. counterparts, indicating a lower price relative to their underlying value.
Yield refers to the income generated by an investment, such as interest or dividends, usually expressed as an annual percentage of its value.

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