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4 September 2025

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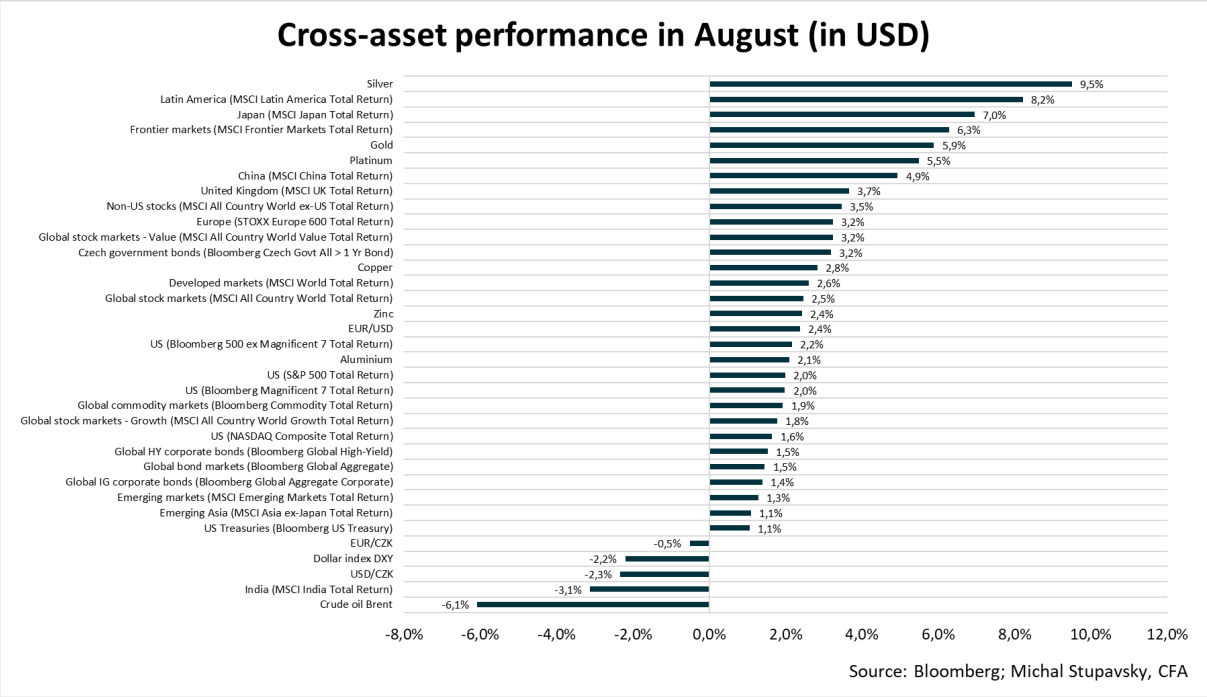
Cross-asset performance in August and year-to-date

Michal Stupavský, CFA

Head of Research

Chart 1 – Cross-asset performance in August (in USD)



Source: Bloomberg; Michal Stupavsky, CFA

Chart 2 – Bond yields and credit spreads change in August(in USD)

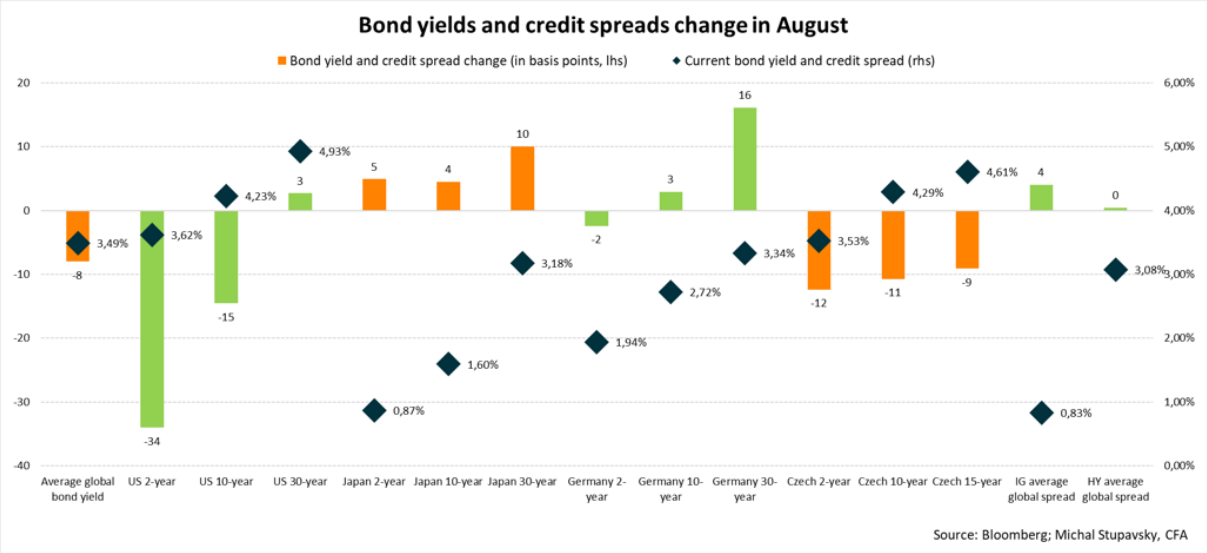


Chart 3 – Cross-asset performance year-to-date (in USD)

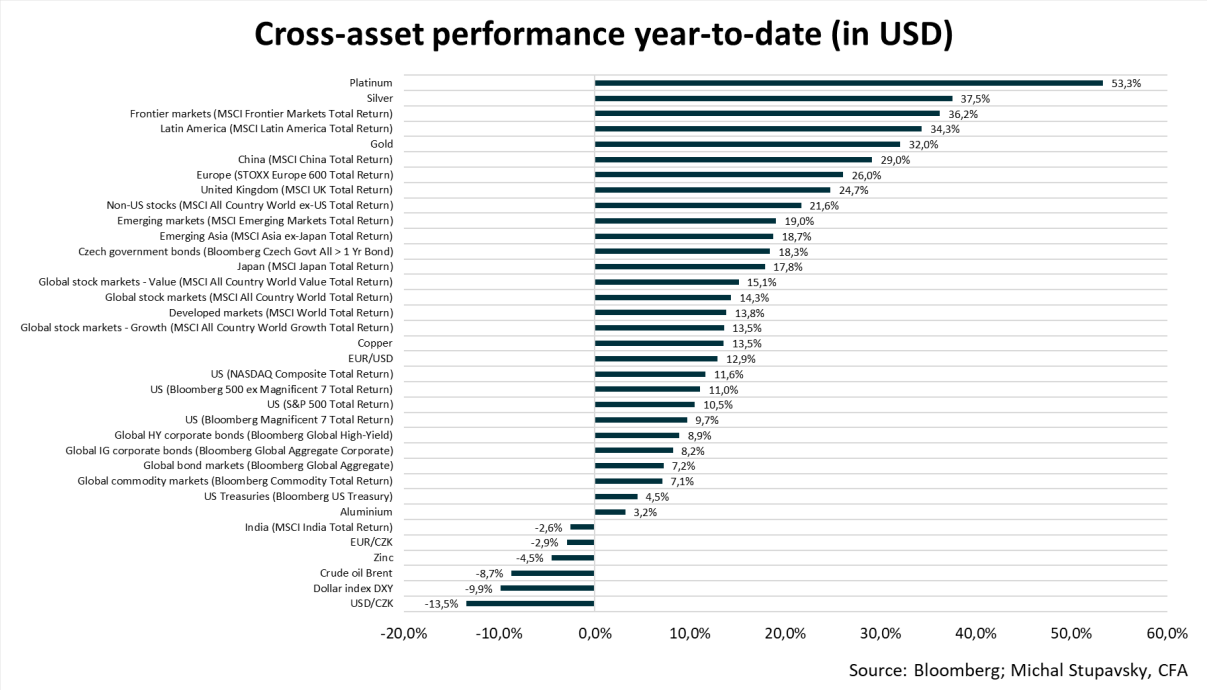
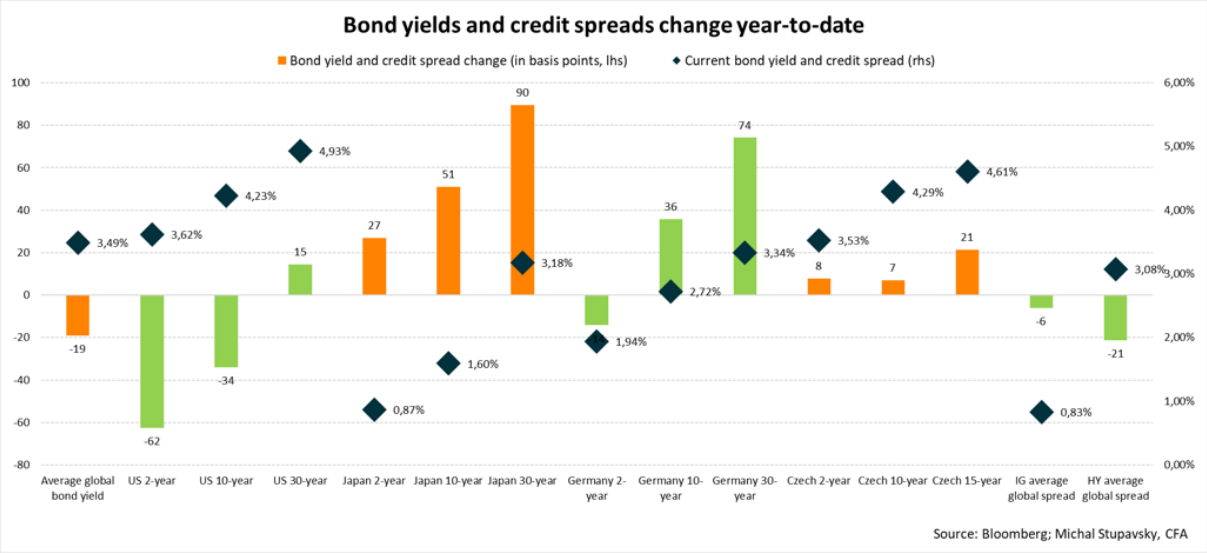


Chart 4 – Bond yields and credit spreads change year-to-date



Interview

Petr Šimčák, CFA

Group CIO, Broker Consulting & Vice Chairman of the Board, Moneco investiční společnost

The interview was conducted in mid-August by **Michal Stupavský, CFA**, Head of Research at the Prague Finance Institute.

Let's start with a general but very important question. What is your current view on the world in general, and on the global economy and financial markets in particular? Which major themes have been especially important to you recently?

Let me set aside the usual suspects—trade wars, artificial intelligence, stagflation risks, the extreme concentration of equity market gains in a handful of U.S. technology and growth stocks, and soaring public debt levels worldwide—not to mention the overarching shadow of heightened geopolitical risk.

The issue that's been on my mind most lately is the rise in political risk—it's something investors now need to factor in much more than in the past. Let me give you two recent examples that, frankly, make traditional investment analysis a lot more complicated. First, there's the risk to the Fed's independence. Second, what is the future credibility of U.S. economic data.

Let me start with the data credibility risk. Payrolls in the U.S. rose by 73,000 in July—a softer number, but not enough to unsettle markets on its own. The real concern is the revisions: May and June were marked down by a combined 258,000

jobs. Outside of recessions, that's the largest two-month revision since 1968. Here comes the politics: Erika McEntarfer was removed because the figures didn't support the narrative of a booming Trump economy, and she's been replaced by E.J. Antoni, a loyalist. A national statistics agency should be boring and nonpartisan. If it turns partisan, the trust that markets rely on is at risk. Everyone already treats Chinese data with caution, using proxies. I would hate to see the day when investors feel they need proxies for U.S. data.

President Trump has also made a temporary appointment at the Fed—Stephen Miran, who was Chair of the Council of Economic Advisers, is stepping in after Adriana Kugler resigned. And this is where politics start to matter again. Chris Giles at the *FT* pointed out that Mr. Miran co-authored a paper just last year suggesting U.S. government bonds should carry terms that would allow the U.S. to weaken the dollar and, in effect, make other countries pay for military protection they've had for decades as "free riders." They even had a name for it—the "Mar-a-Lago Accord." Needless to say, investors hated that idea. And he also co-wrote another paper, *Reform the Federal Reserve's Governance to Deliver Better Monetary Outcomes,* which argued that board members and Reserve Bank leaders should be removable at will by the president—all in the name of "accountability to the democratic process." Now, that's not happening right now, but the fact that this line of thinking is in the mix worries me. The next Fed chair will be appointed in May.

If we look locally, in the Czech Republic, it's been interesting to watch how the bond market completely repriced for 2025—we went from expecting several rate cuts to expecting none. The CNB's latest forecast was quite a shift from April: they lifted the 2025 interest rate outlook by about 0.6 percentage points and GDP growth by half a point. And if you look further out, the 2027 3M PRIBOR projection at 3.7% basically says: rates are going to stay where they are, or maybe even tick up slightly, rather than get cut as people thought before. So the latest outlook really reinforces the CNB's hawkish stance—and what's new here is that the Monetary Department is now very closely aligned with the Bank Board.

The dollar has materially weakened and U.S. equities have significantly underperformed rest-of-the-world equities since the beginning of this year. Do you think that the period of U.S. exceptionalism is already over?

For decades, America's dominance has really stood on three big pillars: energy superpower, military strength, and technological leadership—all anchored by a resilient democracy and the rule of law. That's been the foundation of U.S. exceptionalism. The question for investors today isn't whether those strengths still exist—they do—but whether they're shifting, and by how much.

Now, if one of those pillars weakens, the impact really depends on how far it slips and how strong the rest of the world is in comparison. Is there anyone out there who can replace the U.S., or even close the gap? Right now, no. But markets trade on change, not absolutes. They care less about whether something is good or bad in isolation, and more about whether it's getting better or worse. That's where the so-called "base effect" comes in—an improvement in a weak area can drive strong returns, while a deterioration in something excellent can trigger sharp declines.

And here's where the concerns come in: I fear we are witnessing the erosion of certain democratic principles, the weakening of the rule of law, questions around the Fed's independence, doubts about the reliability of official data, and falling public trust in institutions. Decision-makers are showing less diversity of opinion and—putting it mildly—there's a reluctance to challenge one particular leader. And we're also seeing a quiet brain drain, with some of the brightest minds leaving top U.S. universities for positions abroad. Over the long term, that could prove very costly. One of America's real strengths has always been the trust it commanded globally—its status as a reliable partner in alliances. That's now under threat too, and that could chip away at U.S. exceptionalism in a broader sense.

If the U.S. stumbles, could others step up? Europe, in many ways, is "loaded"—with capital, with talent, with a mandate for change. It's got ambitious military and infrastructure plans, and its markets are trading at historically deep discounts to the U.S. But rhetoric and early action aren't enough. Real structural results need to follow, and they will take time—though visible progress has to come quickly if Europe wants to be seen as a credible alternative. The Draghi report, in my view, gives us a pretty good roadmap.

And remember, markets move ahead of reality. In 2025, they've rallied mostly on the expectation of reform and resilience. But over the long run, it's EPS that will decide the outcome of equity markets—and that valuation advantage only matters if fundamentals improve. I'm cautiously optimistic—maybe because I'm European, maybe because I think failure here would be dangerous and incredibly discouraging... or maybe it's just rose-tinted glasses.

So, is U.S. exceptionalism over? No. But America is doing plenty to give Europe—and Asia—a chance to strengthen. Whether they seize that opportunity... well, that's still an open question.

What is your view on the extreme U.S. stock market concentration and its implications for global asset allocation and portfolio diversification?

John Authers recently spotlighted a landmark study by Hendrik Bessembinder, asking "Do Stocks Outperform Treasury Bills?" The answer is startling: over the past 90 years, just 86 stocks have created around $16 trillion—half of all equity-market wealth—while the remaining 96% of companies delivered returns no greater than those of a one-month Treasury bill. In fact, only 4.3% of stocks account for all the net wealth creation since 1926; the rest were essentially T-bill performers.

This isn't market perversion; it's capitalism's toughest reality. A handful of firms—superstars in their respective eras—drive the vast majority of gains. For the average investor, that's great news if you hold even one such winner. But it also makes active stock picking a high-stakes gamble.

D.E. Shaw has highlighted that the top 10 companies in the S&P 500 now account for more than half of the market's risk exposure, yet investors receive no extra return for that risk. It is worth remembering, however, that markets do not deliver this degree of concentration by accident. The leading names have, in recent years, posted far stronger earnings growth than the rest of the index.

Sure, concentration is a risk—no question about that. But ignoring those big names entirely, or drastically underweighting them, is also a risk that long-term investors can't really afford to take.

Now, why does this concentration stick around? One pretty compelling explanation is fiscal dominance—Mike Wilson at Morgan Stanley has talked about this. Basically, when governments lean heavily on private-sector resources, it shifts the advantage to the large, resilient firms. Smaller companies get squeezed, or they get acquired before they become big. Over time, that just reinforces the concentration we're seeing in markets.

So what do you do as an investor? It's not about dumping U.S. equities. It's about diversifying your exposure smarter. First, you could diversify beyond cap-weighted indices—Goldman's David Kostin is a big advocate for equal-weight or more balanced sector exposure as a hedge against mega-cap concentration. Second, think globally. If European financials and industrials are getting a boost from fiscal stimulus and steeper yield curves, then it makes sense to take advantage of it.

So I'd stick with the broader MSCI ACWI—it gives you much better diversification than just the S&P 500, and you still get exposure to those top U.S. mega-caps. But I'd also put a bit extra into some strategic satellites—India, Europe's old economy, energy, materials. They're tiny weights in the index right now, but I think they've got a big role to play in the future.

And if I had to put some numbers on it—when you model the market index data back to the long-term averages, you're looking at roughly a 7.6% annualized expected return for the MSCI ACWI over the next ten years. That's the dividend yield plus historical average earnings growth, minus about one and a half percentage points per year from the P/E ratio coming back down to its long-term median. On that basis, ACWI small caps and the Europe index look the most compelling right now—good value and good growth. The U.S. and emerging markets are below average in my view: EM doesn't have much room for multiple expansion, and the U.S. still faces that valuation drag.

What is your opinion on the ever-increasing market share of passive investments? Does this structural trend pose any significant risks to investors?

You know, the two models—active stock-picking and passive indexing—they're really joined at the hip. The free riders in passive rely on the active guys to do the price discovery, and in return, those passive flows give the market liquidity and depth. But if that balance tips too far one way... that's when you start getting systemic risks creeping in. Are we there already? Only time will tell.

Research by Bessembinder and others shows how wealth creation is concentrated in a tiny fraction of stocks. That makes passive ownership of an index efficient—but it can also amplify market concentration, especially when market-cap weighting channels more capital to the largest names. This creates feedback loops: index heavyweights can rise further simply because they are index heavyweights, leading to overvaluation at the top and undervaluation off-index. Academic studies (Wahal & Wang, Haddad et al.) find that a high share of passive ownership weakens price sensitivity to fundamentals and raises correlations across stocks.

Other risks are subtler. In fixed income or small caps, where underlying assets are less liquid, the promise of daily liquidity in passive products can become a liability in stressed markets. Passive managers also tend to engage less with corporate governance, reducing shareholder oversight. These are valid concerns—though, in my view, not yet at the systemic levels sometimes claimed by active managers frustrated at their shrinking market share. I prefer active management to blind index replication, but the risks from passive dominance are more slow-burn than imminent crisis.

Major equity indices and equity valuations are at or close to all-time highs. What do you think about it as a behavioral finance expert? Which behavioral biases have been at play here in your opinion?

Yes. As always. Fundamentals matter, but so too does investor psychology—and several well-documented behavioral biases are helping to sustain these market levels. Some of them might be: Representativeness bias fuels the belief that today's market leaders will continue to deliver, just as their predecessors did. Herding and its more emotive cousin, FOMO, have channeled flows into the same crowded trades—most visibly the "Magnificent Seven" tech giants—despite already elevated multiples.

But allow me one local bias. I think that interest rate expectations in CZK are a perfect example of recency bias. Not long ago, it was common to hear predictions that mortgage rates would soon return to 3%. Yet a sober look at the mechanics—where the repo rate would need to be, and the corresponding interest rate swaps on three- and five-year maturities—suggests this was wishful thinking based on the expectation of the repo rate going back under 1%. When such views surface even among seasoned property developers, I think it is a textbook case of recency bias at work.

Daniel Kahneman, the founder of behavioral economics and behavioral finance, was awarded the Nobel Memorial Prize in Economic Sciences in 2002. Very good knowledge of behavioral finance has become a must for all investors since then in my opinion. What major advancements have you noticed in the field of behavioral finance in recent years?

We are not descended from those who, on stepping out of a cave and seeing sweet fruit to the left and a bear to the right, chose the fruit tree. Those genes did not survive—and a few centuries of modern history of financial markets have not rewired them. Loss aversion remains hard-coded: we register negative events more sharply than positive ones, and we instinctively seek the safety of the herd.

Recency bias is another constant. Back in the Stone Age, if you were tracking a mammoth, the fresher the tracks, the better. But in investing today, if you just chase the freshest tracks—recent past performance—chances are, you'll end up in tears. In PwC's CEO survey at the start of 2024, half of respondents expected inflation to remain above 5% for the year. On the surface, that was unsurprising: 2023 had closed at 6.9%. Yet the data already showed January 2023's spike accounted for most of that—6% month-on-month—while the rest of the year delivered a cumulative 0.9%. Any forecast north of 3% for 2024 was either a prediction of a catastrophic January or succumbing to a simple, powerful mix of recency bias and anchoring.

Naturally, there have been developments in the field. Technological shifts have added fresh complications. The rise of artificial intelligence, combined with the engagement-driven architecture of social media, is not just eroding public discourse—it is actively deepening polarization among people. In the U.S., disagreement now extends to the basic facts of an election result. You know, both our cognitive and emotional biases get amplified by these algorithms that keep feeding us the same kind of information. And the thing is, these echo chambers are now big enough to make you feel like you're in the safety of the crowd—which, in the real world, just wasn't physically possible before. Hence, within them, there is no incentive to verify facts or re-examine beliefs. As Daniel Kahneman explained in *Thinking, Fast and Slow*, moving from intuitive "System 1" thinking to deliberate "System 2" is costly—in mental effort, in ego, and in self-image.

And this is where AI gets genuinely dangerous. Yuval Noah Harari makes the point in *Nexus* that an algorithm doesn't need to be conscious to be a threat. Intelligence, autonomy, the ability to learn, and above all the commercial drive to maximize engagement—that's already more than enough to fracture societies. And we've seen where that can end up. Look at Facebook's role in Rwanda in 2015, where its engagement-driven algorithms amplified hate speech against the Tutsi minority, pushing targeted, incendiary content that fueled ethnic violence. Now, layer on the rapid development of AI—if we don't get a grip on it, if we just let it run without oversight—the same forces become far more powerful, and the damage could be on a completely different scale.

And one area I'm especially worried about is the rise of social scoring systems—you already see them in some authoritarian regimes. With AI in the mix, those systems could go to levels that, not so long ago, you'd only find in dystopian fiction like *Black Mirror*. Here, I'm hoping Europe's safeguards—GDPR, the Digital Services Act—can hold the line, even though the general policy direction should be towards lighter regulation.

Turning to markets, I see a striking asymmetry in accountability. If you are a bear, you get airtime; if your pessimism proves wrong, there are no real consequences. If you are an optimist and a bull, you also get airtime—but if you are wrong, you may face criticism, even regulatory scrutiny, for allegedly exposing retail investors to undue risks. Yet over the long term, equities tend to rise. In aggregate, pessimists have done more damage than optimists, but they bear no responsibility; they can always claim they warned of danger. It is short-termism applied to an inherently long-term investing.

The same psychology underpins our response to climate change and defense spending: if it's not burning now, it can wait—until the fire is already raging. *Don't Look Up*, the 2021 satire, captured this dynamic perfectly. In defense, the bill is already due. On climate, the price we will eventually pay is likely to be far higher than it would have been had we acted sooner.

What are your favorite books about behavioral finance? Could you make any recommendations to our readers?

I'd definitely recommend Richard Thaler's Nudge and Daniel Kahneman's Thinking, Fast and Slow and Noise. And then there are some, perhaps less obvious, but still very insightful picks—Hans Rosling's Factfulness, Yuval Noah Harari's *Nexus*, and even the classics of Benjamin Graham (*The Intelligent Investor*) along with Warren Buffett's many timeless aphorisms. On top of that, Dan Ariely's books—*Predictably Irrational, The Honest Truth About Dishonesty*, and *The Upside of Irrationality*—plus his TED talks are always worth exploring.

And then my favorite movie *The Big Short*. It all just happened in the real world — not this exact story, but the financial crisis it portrays, with some characters based on real people. I am preparing for a discussion with a quantum physicist friend who once walked me through *Interstellar*—pausing at every scene to draw a line between hard science and Hollywood fiction. Now, having seen *The Big Short* twice, he wants me to do the same for him. He says there are "a number of things" he still can't quite follow. My plan is simple: I will not stop the film once. There is no reason. At the end I will tell him that, unlike *Interstellar*, there is no science fiction.

What is your current global investment outlook till the end of 2025?

Warren Buffett once remarked that he has never had a view on where markets or interest rates will be a year from now. In my view, the most dangerous strategy is to invest at the start of the year based on a 12-month forecast. Still, to answer your question: As of mid-August, the sell-side consensus for the S&P 500 by the end of 2025 stands at 6,276.39—roughly 2.5% below current levels. Analysts expect earnings per share to grow by an average of 2.6%, while the price/earnings ratio is projected to fall 5.3%, from 25.23 to 23.91. Across 28 strategists, forecasts range from 6,000 to 6,600, and the index will likely finish within that band. The trigger for movement in either direction could be almost anything. With valuations already high, further upside requires companies to deliver earnings growth above expectations and at least to avoid downward revisions. Any disappointment is likely to be punished asymmetrically on the downside.

Locally, I expect the Czech National Bank to hold rates at 3.5%—broadly in line with market expectations. On the longer end of the yield curve, I doubt yields will fall below 4%, largely for fiscal reasons. In fact, I believe analyst forecasts remain too low: a 4% yield is less likely than one closer to 4.5%.

What are currently the major investment risks which investors all over the world have to face right now?

Markets are priced for perfection—particularly in the United States, and especially in the growth segment. A record 91% of managers in the BofA Global Fund Manager Survey describe U.S. equities as overvalued—a sentiment they have held for much of the past decade. And yet, the recent flow of capital from the U.S. to European equities has halted.

One big short-term risk I see is what I'd call a "stagflation-ish" scenario—you know, a bit more inflation than we'd like, combined with softer growth. That's the kind of mix that could create political pressure to cut interest rates, especially in the U.S. And Jim Bianco at Bianco Research makes a great point here: in the last 40 years, the Fed has only cut rates once when core inflation was above 3% and the three-month change was more than 0.3%—that was back in the Gulf War and the recession of 1990–91.

The bond market is another source of risk. If the 10-year yield pushes up toward 5%, you could easily see equities react the same way they did in the sell-off earlier this year. And that could happen if the Fed cuts rates while inflation is still closer to 3% than the 2% target.

Europe right now is really at a crossroads. If it doesn't bring down energy costs, cut through the layers of regulation, and build serious military capabilities, it's going to stay a junior partner on the world stage. But let's not forget—Europe's got some huge strengths: world-class basic research, deep democratic traditions, enormous wealth, and a consumer market of 450 million people.

With the right focus and ambition, it could be more than just an economic pillar—it could actually become a leading player in advanced technologies and AI. That's not the consensus view today, but I think the potential is there. Strategic autonomy won't come from signing communiqués; it means cheap, reliable energy, a truly competitive business environment, and a defense posture strong enough to be respected by the superpowers.

And of course, geopolitical risk could fill an entire chapter on its own—it's growing every month. The global order is fragmenting. For investors, the biggest danger might be assuming that the old rules still apply.

BIO

Petr Šimčák (b. 1973) is a Czech investment professional with over 25 years of experience in asset management and financial advisory. He holds degrees in Economics (1996) and Psychology (2015) from Masaryk University and is a Chartered Financial Analyst (CFA).

He began his career in 1997 at MONECO, serving as Deputy Editor-in-Chief of Fond Shop and providing fee-based financial advice. From 2004 to 2018, he was Director of Sales and a member of the board at Pioneer Asset Management. He later served as Deputy Director of Sales at Amundi Czech Republic (2018–2021) and as Chief Investment Officer and board member (2021–2024). Since 2024, he has been Group CIO at Broker Consulting and Vice Chairman of the Board at Moneco investiční společnost.

He is also a member of the board of trustees of the Charter 77 Foundation.

Chart of the month

US equity risk premium hovering at multi-year lows

Michal Stupavský, CFA

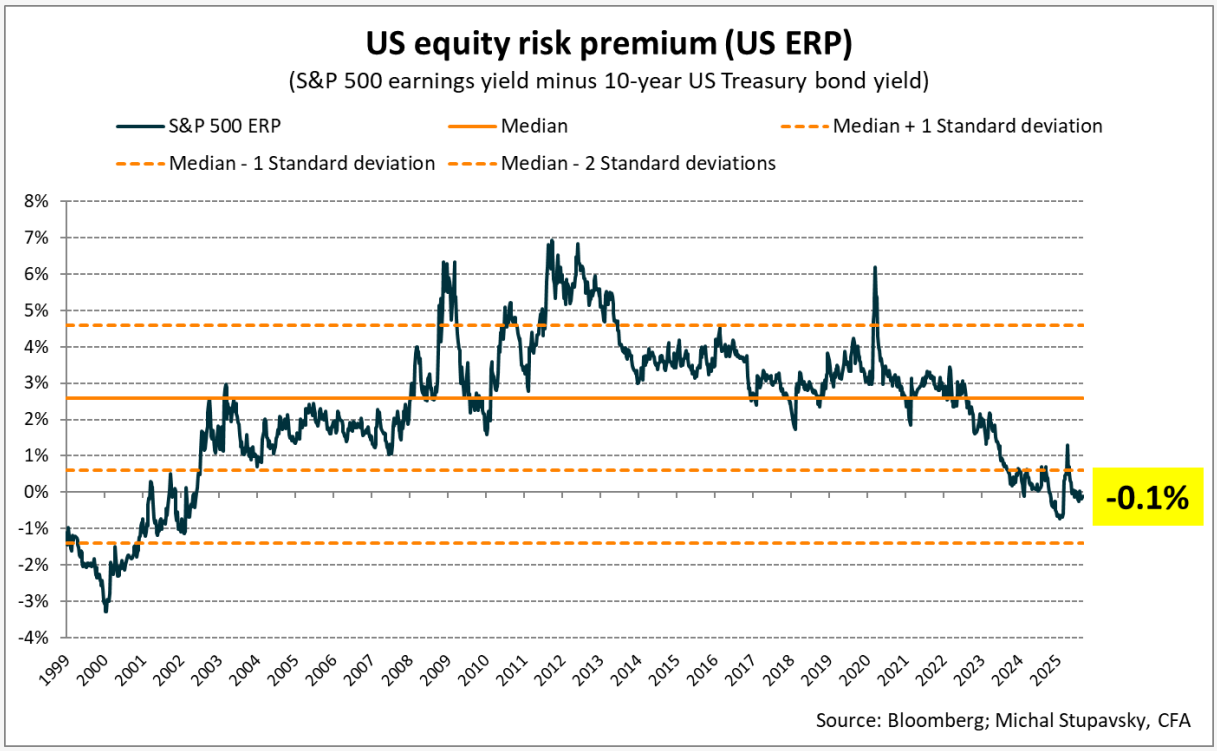
Head of Research

US equity risk premium (US ERP) – defined as S&P 500 earnings yield minus 10-year US Treasury bond yield – stands currently at -0.1%. This value corresponds with 13th percentile across the time-series since 1999. That said, US equity risk premium has been hovering at multi-year lows around zero approximately since the summer of 2023.

Such an extremely low equity risk premium, now even slightly negative, means that US equities seem to be rather overvalued vis-à-vis US Treasury bonds on the relative cross-asset basis, because equity investors are not compensated at all for the equity risk embedded in US equities.

How can this significant cross-asset valuation discrepancy be corrected, i.e. how can the US equity risk premium be increased? There are three principal ways: 1) equity valuations, i.e. P/E ratios, will decline and earnings yields will increase correspondingly; 2) US Treasury bond yields will decline; or 3) a combination of 1) and 2).

Taking into an account the very bad dynamics of US government debt indicators, realization of the second option, i.e. US Treasury bond yields decline, is not much likely in the mid-term horizon in my opinion. Thus, the only plausible way is the first option, i.e. equity valuations decline and earnings yields corresponding increase. In other words, there would have to be a significant US equities de-rating, i.e. valuations normalization (valuations mean-reversion).


US equity risk premium (US ERP)
(S&P 500 earnings yield minus 10-year US Treasury bond yield)
S&P 500 ERP
Median
Median + 1 Standard deviation
Median - 1 Standard deviation
Median - 2 Standard deviations
8%
7%
6%
5%
4%
3%
2%
1%
0%
-1%
-2%
-3%
-4%
1999
2000
2001
2002
2003
2004
2005
2006
2007
2008
2009
2010
2011
2012
2013
2014
2015
2016
2017
2018
2019
2020
2021
2022
2023
2024
2025
-0.1%
Source: Bloomberg; Michal Stupavsky, CFA

Global macro insights of the month

The U.S. dollar has weakened sharply this year. Will the depreciation of the world's primary reserve currency continue?

Michal Stupavský, CFA
Head of Research

The U.S. dollar has weakened more this year than in several past decades. The U.S. Dollar Index (DXY), which measures the dollar's performance against a basket of major global currencies—primarily the euro, Japanese yen, and British pound—has fallen 10% year-to-date to 98 points. Against the euro, the dollar has depreciated by 13% to 1.169 USD per EUR, and against the Czech koruna it has fallen by 13% to 21.0 CZK per USD. In my view, over the medium- to long-term horizon, the dollar is likely to continue to gradually weaken. This investment stance is based on the following fundamental factors.

First, U.S. federal public finances are in very poor condition. Total federal debt stands at $37 trillion, government debt-to-GDP is 121%, the federal budget deficit amounts to $1.8 trillion, and the budget deficit-to-GDP ratio is 7%. Moreover, annual interest costs on U.S. government debt now exceed $1 trillion, making interest payments the single largest item in the federal budget. Interest costs account for 25% of budget revenues and 3.5% of GDP.

Looking ahead, annual interest costs could climb toward $2 trillion as the absolute level of government debt continues to rise rapidly due to record budget deficits, and as newly issued Treasuries are repriced at much higher interest rates compared to the pre-pandemic years. To put this in perspective, the yield on the key benchmark 10-year Treasury reached a historic low of around 0.5% in August 2020, while the current yield stands at 4.2%.

Furthermore, it is not just the current unfavorable fiscal ratios that are troubling, but also the dramatic deterioration of these metrics in recent years. For example, prior to the Global Financial Crisis in 2007, total federal debt amounted to "only" $9 trillion. The surge to the current $37 trillion corresponds to an unprecedented compound annual growth rate (CAGR) of 8%.

Second, the U.S. economy suffers from significant external imbalances. The current account deficit amounts to 5% of GDP, and the Net International Investment Position (NIIP) stands at -$25 trillion, equivalent to -82% of GDP. The U.S. NIIP primarily reflects cumulative current account deficits built up over past decades. A notable statistic in this regard is that foreign investors currently hold a record volume of U.S. assets. On public markets, foreign investors own about 20% of U.S. equities, 30% of U.S. Treasuries and 30% of U.S. corporate bonds.

Third, relatively price- and interest-insensitive investors such as central banks and sovereign wealth funds stopped purchasing U.S. Treasuries on a net aggregate basis as early as 2014. This means the U.S. Treasury has had to increasingly rely on domestic investors. A key question is how much additional absorption capacity U.S. investment funds still have at this stage.

Fourth, under the new U.S. administration, political pressures on the Federal Reserve have increased notably, which could, at least in the eyes of some investors, undermine the perceived independence and credibility of the U.S. monetary authority.

All things considered, I believe the U.S. dollar will continue to face significant headwinds in the periods ahead. In my base case scenario, I therefore expect a gradual further depreciation of the dollar. The implications for Czech investors are clear: they should strongly consider hedging at least part of their USD-denominated assets into CZK.

Global macro insights of the month

Inflation is down, but it still feels expensive: the problem with inflation targeting

Štěpán Drábek

Analyst

There exists a persistent mismatch between how central banks approach inflation and how the economic agents experience it. Central banks, like the Czech National Bank (CNB), target the rate at which prices rise, aiming for low, stable, and predictable inflation over time. This approach, known as inflation targeting, has been in place in the Czech Republic since 1998 and focuses on preventing runaway price growth, not on reversing past increases.

Yet for most households, what matters is not whether inflation is at 2%, but whether things are still expensive. From the perspective of a consumer at the supermarket, the inflation rate may well have come down, but groceries still cost more than they did two years ago, and that's what truly matters for him.

This difference in focus is more than just semantic. As my colleague Jiří Schwarz, advisor to the Bank Board of the Czech National Bank, and I highlighted in our article most people do not distinguish between falling inflation rate and falling prices. Survey data from Czech households in 2024 showed that only about a quarter of respondents correctly understood that prices, once elevated, are unlikely to fall back. The majority still expected that after a temporary shock (such as a spike in fuel prices), prices would eventually "normalize" and go back down. But this expectation contradicts the very design of inflation targeting, where prices grow steadily over time and do not return to previous levels after a shock emerges.

This gap in understanding has real economic consequences. From the central bank's point of view, once inflation is back near target, the job is largely done. But households, still seeing high price tags, feel that the problem persists. They may hold back on spending, waiting for a price correction that will never come. In doing so, they dampen consumption and hinder economic recovery.

The data indeed show unusually high savings rates among Czech households, consistent with this "wait and see" attitude. Businesses, in turn, face weak demand, hesitate to invest, and struggle to set prices in a way that reflects both costs and customer sentiment. This feedback loop slows down the return to normal economic functioning, even when monetary conditions are no longer restrictive.

Ultimately, the divergence between central bank logic and household intuition is not just a matter of communication; rather it's a fundamental challenge. If people expect price declines that monetary policy is not designed to deliver, frustration and mistrust may follow. As we argue in our article, improving economic literacy is key. The public needs to understand that monetary policy aims to slow price growth, not reverse it. That prices won't "go back" is not a failure of the central bank – it's just how modern price stability approach works.

Financial markets insights of the month

Data matters

Joachim Klement, CFA

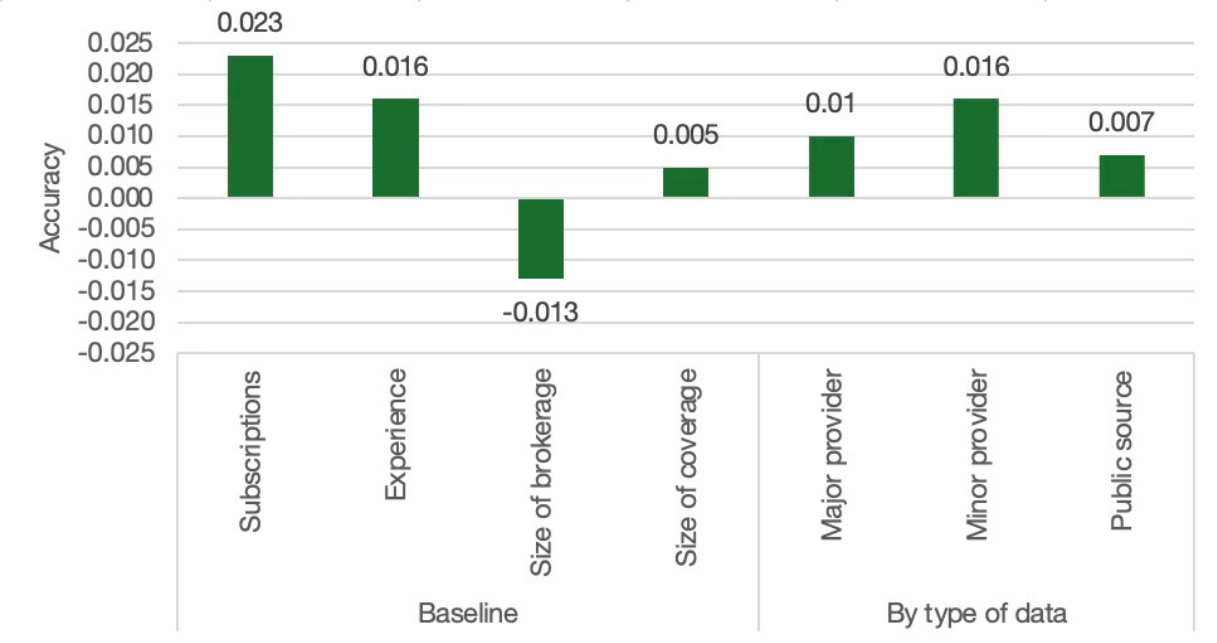
Managing Director, Strategy, Economics, and ESG, Panmure Liberum

Guest contributor

One of the constant pressures throughout my career in finance has been the drive to cut costs. That inevitably leads to some guy in my firm asking me to downgrade from Bloomberg to FactSet or unsubscribe from specialist data providers. The bean counters don't realise that if you work in investment research or are managing assets, these data subscriptions can make the difference between good and poor performance and thus between getting more clients (and higher revenues) and losing clients (sorry for the mini rant).

Braiden Coleman, Travis Dyer, and Mark Lang examined more than 200,000 analyst reports from equity brokerages and tried to find out what effect the data sources these analysts use in their reports have. The chart below is a mix of three different regressions I pulled together in one chart. Plus, unfortunately, the researchers always put every variable into deciles, so the numbers cannot be directly translated into an x% increase or decrease in accuracy. However, it allows us to compare the effect size of data subscriptions with other factors.

Effect of data subscriptions on analyst forecast accuracy



Source: Coleman et al. (2025)

Let's look at the four bars to the left of the chart, which are taken from their baseline results. We can see that the number of data subscriptions positively affects analyst forecast accuracy more than analyst experience. A young analyst with many different data sources will be better than the 20% most experienced analysts.

On the other hand, the chart also shows that analysts at larger brokerage firms tend to be less accurate than analysts at smaller houses – something that I attribute to the juniorisation in large firms, where experienced but expensive analysts have been replaced by younger, cheaper ones for years.

Let's move to the right half of the chart, where I have pulled together two separate regressions in one chart. We can see that the five major data providers (Bloomberg, S&P Capital IQ, FactSet, LSEG, Morningstar) do provide some boost to analyst accuracy. But smaller data providers with more specialised data provide a 60% larger impact on analyst forecast accuracy. Publicly available data sources, meanwhile, provide only limited benefits.

But unfortunately, these smaller, more specialised data providers are often cancelled before the large ones. That means that cost-cutting happens where analysts tend to get the biggest bang for their buck when doing their job.

Even worse, the study also finds that analysts who use the same sources as other analysts tend to make similar forecasts. As the cost-cutting in our industry leaves more and more of us with one of the five large data providers and nothing else, that means that we lose our ability to differentiate ourselves in the marketplace. And that means there is less independent thinking and more groupthink in markets. Plus, if you are an investor who has to pay for sell-side research (thank you, Mifid), why would you pay for research that isn't differentiated? You can simply stop paying for the research and use consensus data, which is available on the major data providers like Bloomberg or LSEG Workspace.

In short, cutting costs by removing analyst and investor access to data is self-defeating. It only accelerates the downward spiral, which may, in the long run, lead to lower revenues and more cost-cutting. As I said before, you cannot cut your way to profitability.

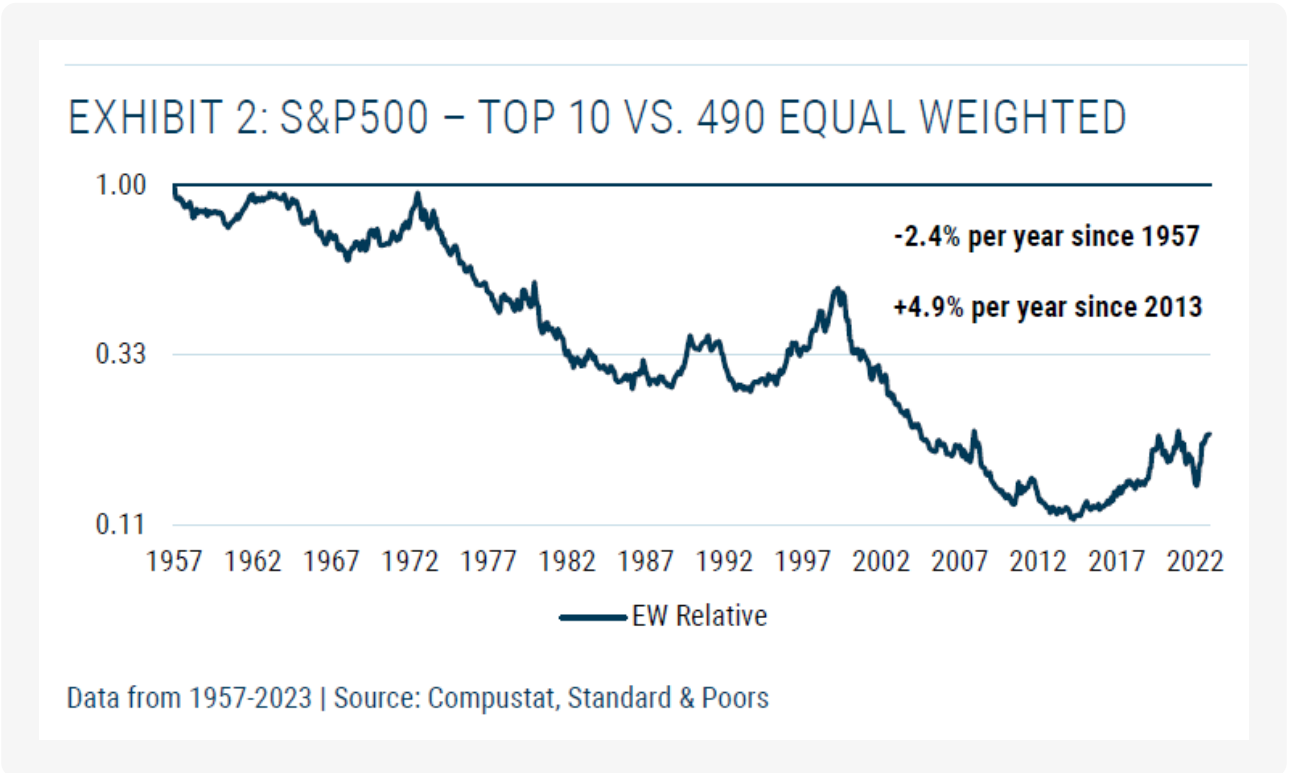
Editor's note: The article was originally published on Joachim's Substack on 13 August 2025.

Financial markets insights of the month

Simple but not easy; it's all about AI

Laurent Millet, CFA
Analyst

Investors continue chasing the recent outperformance of a handful of large-cap U.S. growth stocks, ignoring long-term evidence on valuation's importance for returns. This behaviour reflects classic recency bias—the tendency to overweight recent events even when older, more instructive patterns exist. By fixating on recent winners, investors overlook a consistent historical truth: decades of data show that the largest index stocks systematically underperform equal-weighted portfolios over the long term.



The current surge in index concentration reflects a familiar pattern that has historically preceded sub-par returns. US stocks now represent more than 70% of the MSCI World index, with the top 10 stocks (all American companies) accounting for 26% of global equity markets. Within the US itself, the top 10 stocks represent over 36% of total market capitalization, an extreme level of concentration not seen in more than 50 years. Most tellingly, while their price performance has driven index gains, these companies' share of actual earnings remains well below their market weight, creating a valuation gap that mirrors previous bubbles like the dot-com era. Just as in 2000, investors are betting that recent winners will maintain their dominance, ignoring how fleeting such market leadership typically proves to be.

Figure 2: Weight to Top 10 Has Increased While Earnings Contribution Has Been Steady.

Date Range: 12/31/1964 to 12/31/2024. Represents the top 10 stocks based on market cap from the largest 500 US stocks.

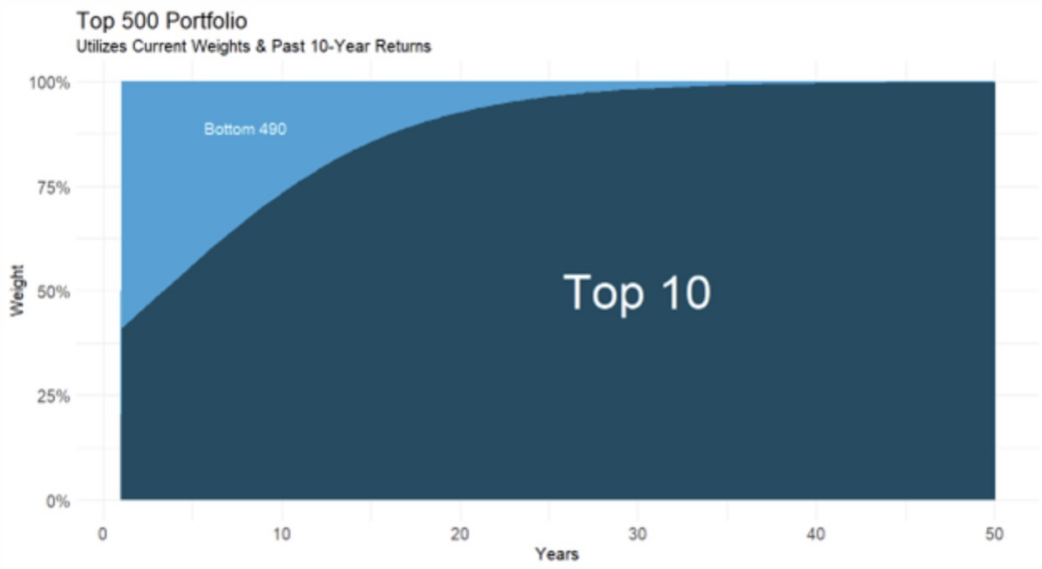
Source: Compustat. Calculation: Hartford Equity Modeling Platform.

The historical evidence for these concentration risks is both extensive and sobering. Research by Bill Pauley, Kevin Bales, and Adam Schreiber documents multiple "lost decades" following periods of extreme market concentration. In the decade after the technology bubble burst, the top 10 stocks (equal-weighted) lost 6.63% annually while the bottom 490 gained 2.55% annually. A similar pattern emerged during 1964-1974, when the top 10 stocks lost 0.44% annually compared to 3.09% gains for the bottom 490, following the concentration buildup of the 1960s.

The relationship between concentration and performance is remarkably consistent. Between 1964 and 2024, when top 10 concentration remained below 19%, smaller stocks outperformed only 39% of the time. But when concentration peaked, the bottom 490 stocks outperformed in 88% of five-year periods. Market-cap weighting works best during periods of lower concentration.

These patterns suggest today's concentration levels are unsustainable. If the current largest stocks continue outperforming at their recent pace, Pauley, Bales and Schreiber calculate they would represent 73% of the S&P 500 within a decade, a mathematically implausible outcome that highlights how extended current trends have become.

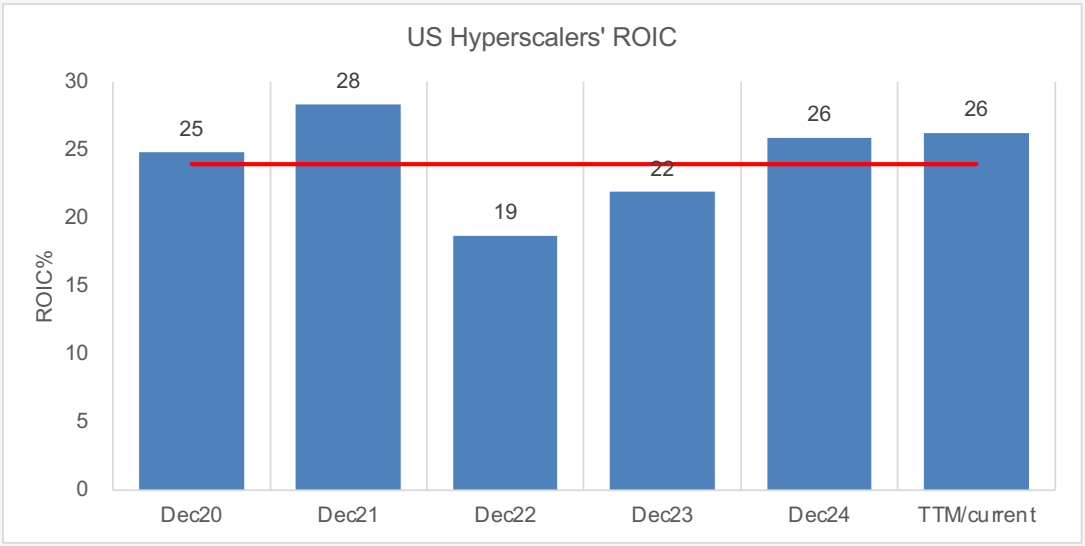
Figure 3: Current Trajectory of Top 10 is Unsustainable.



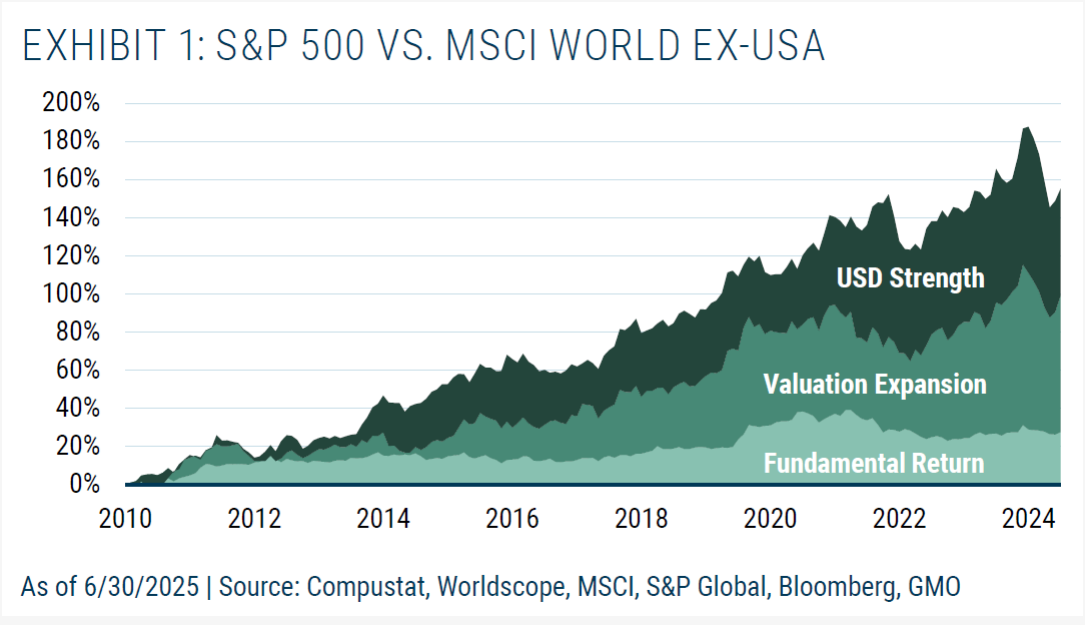
Top 500 based on the 500 largest US stocks. Chart uses current weights and past 10-year returns and applies them for 50 years into the future. Past performance does not guarantee future results. Source: Compustat. Calculation: Hartford Equity Modeling Platform.

Such extreme concentration poses broader market dangers. Extreme market concentration creates systemic risk by concentrating investor wealth in a handful of mega-cap stocks, amplifying volatility when these giants stumble. This narrow leadership makes markets vulnerable to sector-specific shocks while reducing diversification benefits. When concentrated positions eventually unwind, selling pressure intensifies, creating cascading effects that can destabilize broader market stability and liquidity.

Could this time be different? Today's U.S. large-cap tech leaders may distinguish themselves from past market darlings through genuinely durable competitive advantages. The major hyperscalers benefit from powerful network effects, global scale, and entrenched ecosystems that make disruption increasingly difficult. Their exceptional profitability, cash generation, and fortress balance sheets set them apart from the debt-fuelled speculation of earlier bubbles. Most importantly, these companies underpin critical economic infrastructure like cloud computing, digital payments, AI, and online advertising, creating persistent, structural demand.

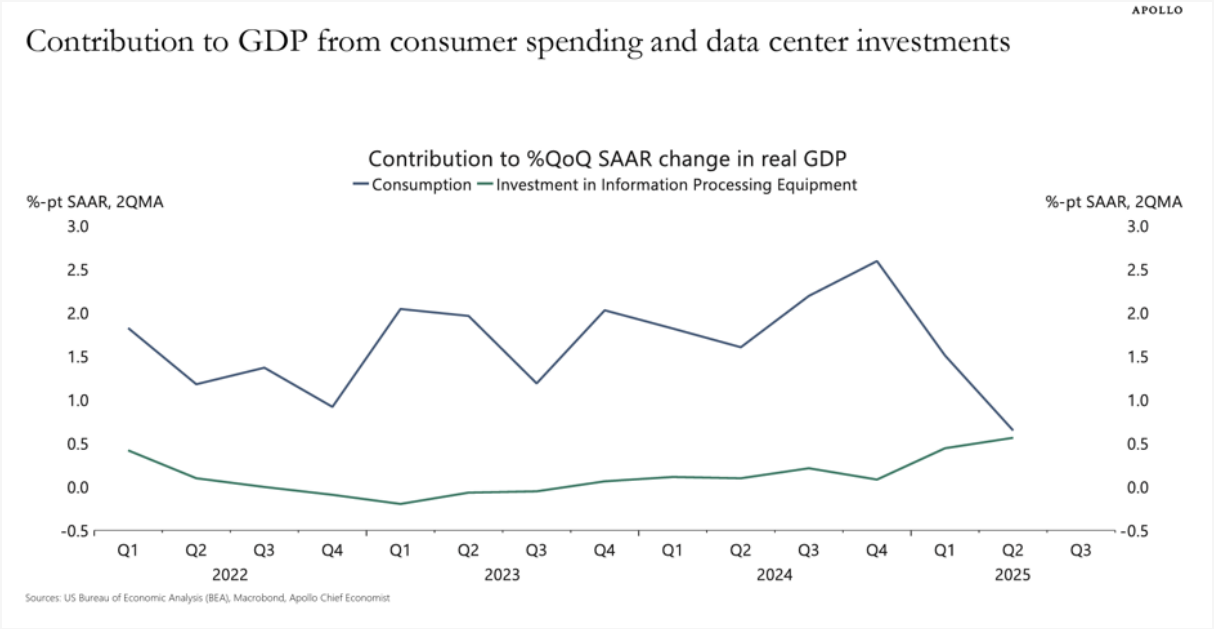


The composition of recent gains raises serious questions about durability. GMO's analysis of S&P 500 performance in their Q2 2025 Quarterly Letter exposes the fragility of current market leadership. When they decomposed the index's outperformance into distinct components, a startling pattern emerged: superior earnings growth accounted for merely 20% of the gains, while 80% came from expanding valuations and dollar strength, two factors unlikely to persist indefinitely.

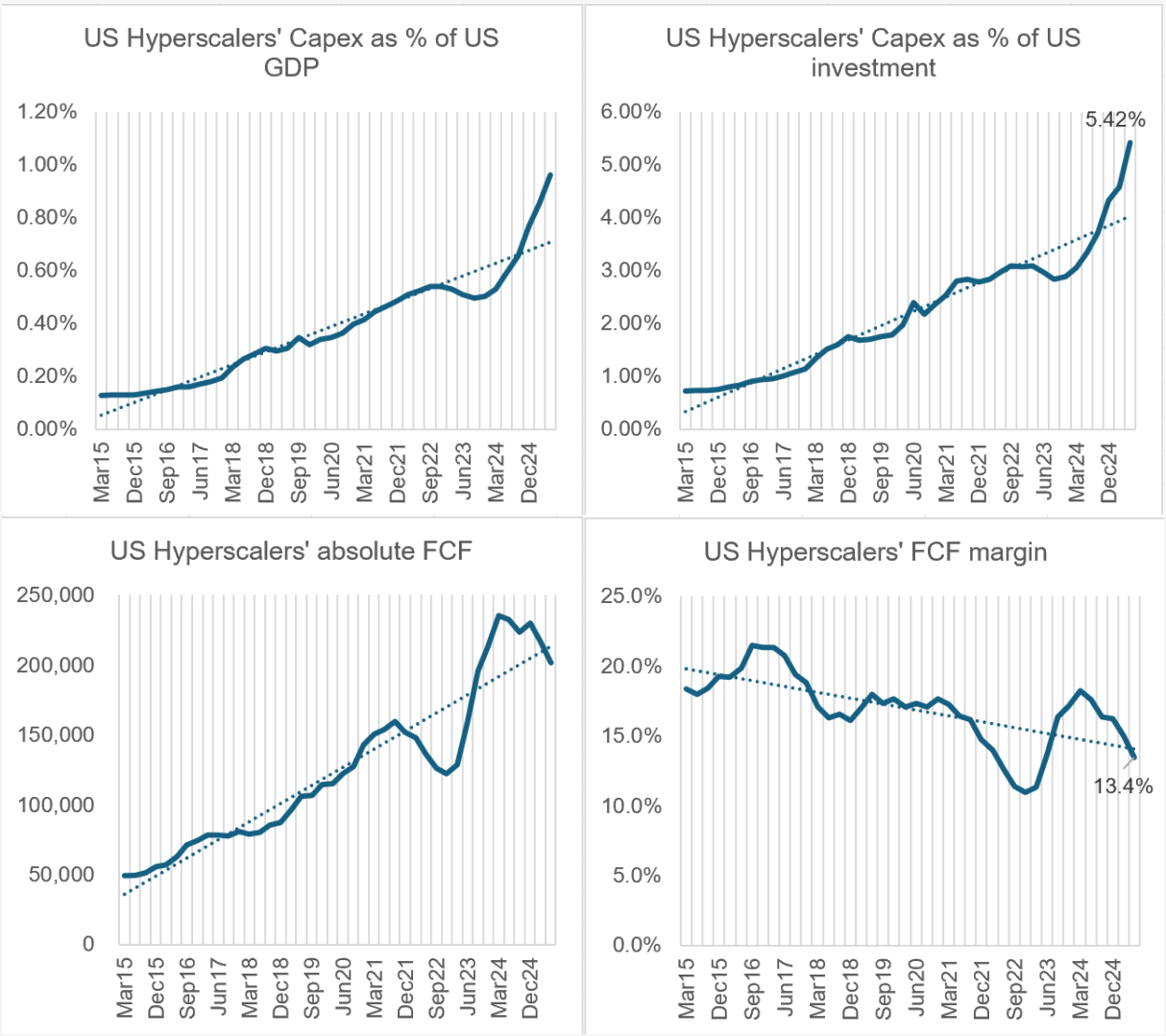


The valuation expansion story becomes even more concentrated when examined closely. While US stocks generally trade at premiums to global equities, the primary drivers of multiple expansion have been NVIDIA and the major hyperscalers: Amazon, Alphabet, Microsoft, and Meta. This creates a remarkably insular ecosystem where 88% of NVIDIA's Q2 2025 revenue came from datacenter sales, a market dominated by these same hyperscalers. NVIDIA's two largest customers, widely believed to be Microsoft and Amazon, alone represented 39% of the company's revenue.

This circular dependency reflects a broader capital allocation shift that may prove unsustainable. Leading US technology companies are undertaking an unprecedented expansion in capital expenditure to build AI infrastructure, fundamentally transforming how these historically asset-light businesses deploy capital. NVIDIA, now representing 8% of the S&P 500 and 5.6% of the MSCI World, has emerged as the primary beneficiary of this dramatic spending surge. In the 12 months through Q2 2025, Microsoft, Meta, Amazon, and Alphabet collectively invested $291 billion, more than four times their investment levels from five years earlier. This corporate spending spree has become so massive that datacenter investments now contribute more to U.S. economic growth than consumer spending, according to economist Torsten Slok.



This spending surge represents a fundamental shift in how technology giants operate their businesses. Technology companies that built their dominance on asset-light business models have transformed into capital-intensive operations, funnelling unprecedented cash flows into datacenter infrastructure. Throughout the past decade, these same companies generated substantial free cash flow that was primarily returned to shareholders through aggressive buyback programs and growing dividend payments. Today, they channel nearly all incremental free cash flow into expanding AI computing capacity. What were once the most capital-efficient businesses in the market have become some of the most capital-hungry, driven by fears of missing the AI revolution.



This spending frenzy is driven more by fear than financial logic. The fear of missing the AI race has created a classic prisoner's dilemma among technology giants. The existential nature of AI competition means no company dares to stop spending, even when facing sub-par returns on invested capital. Each firm recognizes that falling behind in AI capabilities could threaten their long-term survival, yet collectively their aggressive spending may be destroying value for shareholders. The rational individual decision (continue investing heavily) becomes collectively irrational, trapping all players in an escalating cycle of capital expenditure that may ultimately benefit no one.

From an investment perspective, the key question becomes one of future returns. In investing, success comes not from analyzing what's already known, but from understanding what markets haven't yet recognized or priced in. The game is meta-analysis, identifying companies that will meaningfully exceed or fall short of their current growth expectations, regardless of whether those expectations start high or low. This framework makes historical financial data merely a reference point. What truly matters for future returns is a company's evolving return on invested capital (ROIC), not its past performance. Changes in ROIC drive future shareholder returns, as evidenced by top-quintile companies that decline: their total shareholder returns drop sharply as they fall through performance quintiles, illustrating both mean reversion and the dangers of assuming past leaders will maintain dominance without continued innovation.

Exhibit 9: Annual 3-Year TSRs for Combinations of Beginning and Ending Quintiles, 1990-2022

		Ending Quintile				
		(Best) 5	4	3	2	(Worst) 1
Beginning Quintile	(Best) 5	20%	7%	0%	-4%	-11%
	4	25%	14%	6%	0%	-10%
	3	28%	18%	10%	2%	-6%
	2	28%	20%	14%	6%	-5%
	(Worst) 1	33%	23%	15%	8%	-3%

Source: FactSet and Counterpoint Global.
Note: Excludes financials and real estate; Past performance is no guarantee of future results.

Since stock prices reflect market expectations of future performance, changes in these expectations drive excess returns. Applied to today's AI spending boom, this logic leads to an uncomfortable conclusion: if AI investments prove unprofitable, the US hyperscalers will have misallocated capital on an epic scale. Their profitability will decline, and their valuation multiples will almost certainly contract.

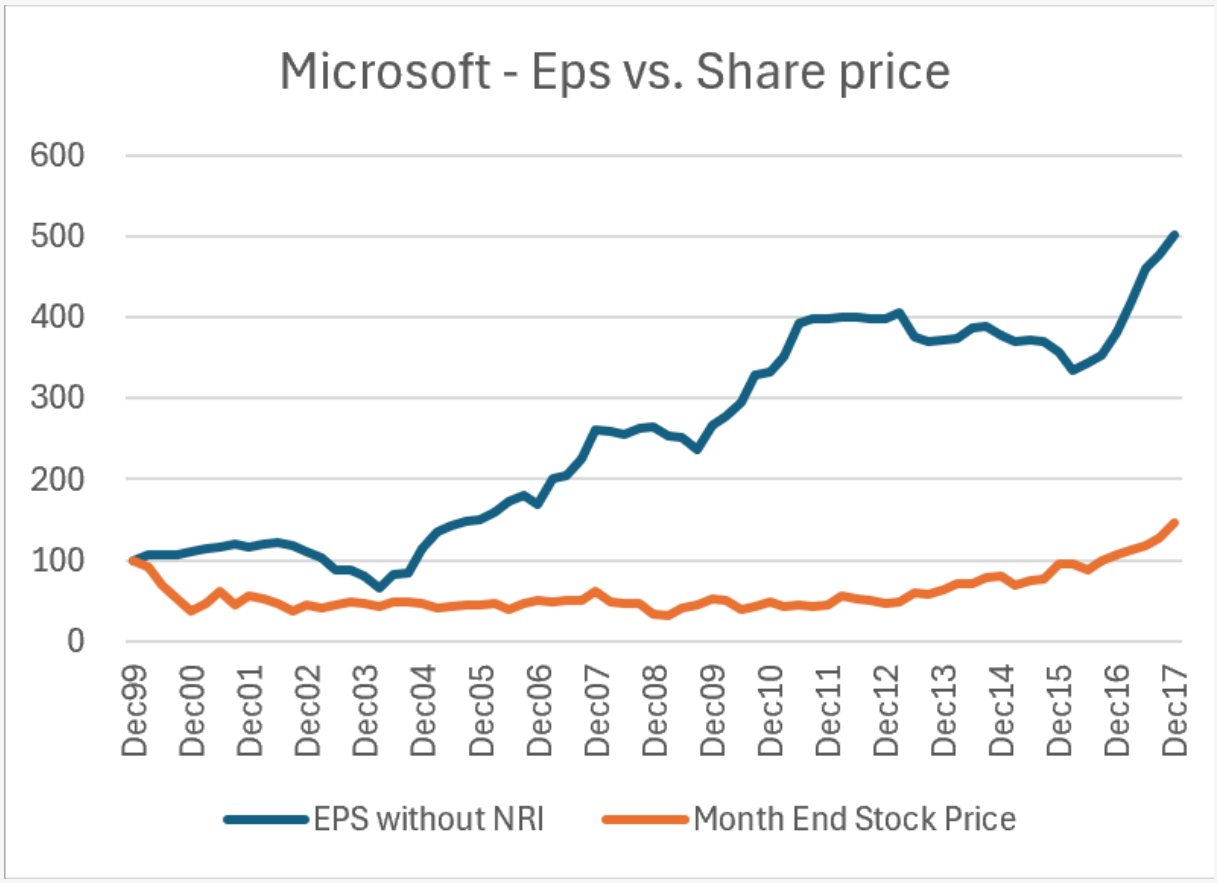
This dynamic fits within a broader historical pattern of innovation-driven market cycles. Innovation often fuels irrational exuberance in both the real economy and stock markets. The internet boom of the late 1990s provides the most recent parallel to today's AI craze. Research by Alina Sorescu, Sorin M. Sorescu, Will J. Armstrong, and Bart Devoldere examined 51 major innovations spanning 1825 to 2000, discovering that 73% of transformative technologies coincided with statistically significant bubbles in their parent companies.

The pattern is remarkably consistent. The largest bubbles emerged around three distinct categories: highly radical technologies like telegraphs and smartphones that generated massive price appreciation; products benefiting from network effects, particularly railways, where value increased with adoption scale; and innovations receiving extensive media coverage that saw public attention translate directly into investment flows.

While destructive to many investors, bubbles serve a crucial economic function by accelerating infrastructure buildout and technology deployment. Without speculative capital injection, many transformative innovations might never achieve the widespread adoption necessary for societal impact. Stock market bubbles effectively fund societal progress through private capital markets rather than government spending, representing an imperfect yet effective mechanism for financing innovation at the required scale and speed.

Yet this historical perspective offers little comfort to current AI investors. Revolutionary technology does not automatically create profitable investments. The internet transformed society, but most internet companies failed financially. Fiber optic cables revolutionized communications, but fiber companies went bankrupt. AI represents a genuine technological breakthrough that will reshape entire industries, but this does not make current AI investments profitable or sustainable. Today's AI infrastructure will likely prove valuable for decades to come—current AI investors may still regret their participation.

The Microsoft precedent from 1999 illustrates this paradox perfectly. Despite gross margins above 90%, ROIC around 30%, and free cash flow margins of 63%, the stock traded at 85 times earnings. Over the following decade, ROIC remained stable around 30% and earnings per share grew 11% annually. Yet the share price fell almost 50% and didn't recover to its 1999 level until December 2016—17 years later. The culprit was multiple contraction: Microsoft's price-to-earnings ratio collapsed from 85 to 17 between 1999 and 2009, even as the underlying business remained exceptionally profitable.



Investing is simple but not easy. Today's equity markets orbit around AI spending, and the fate of portfolios hinges on positioning in dominant US technology firms. Reputations will be built or broken depending on whether investors judged this capital cycle with foresight or folly.

AI will likely reshape industries and create enormous societal value, justifying the optimists' faith in the technology. But the pessimists may prove equally right about investor outcomes, as speculative excess destroys capital even while funding genuine innovation. Revolutionary technologies often enrich society while impoverishing their early financial backers. Being right about the future and making money are not the same thing.

Financial markets insights of the month

Earnings season propelled US equities to all-time highs, but the risks are mounting

Tomáš Pfeiler, CFA
Analyst

US equities have continued their inexorable march upwards. An extraordinary earnings season combined with mounting hopes of a September cut propelled S&P 500 to new all-time highs in August. However, there is a reason to believe that investors have become overly complacent. There is a plethora of risks on the horizon.

S&P 500 briefly surpassed 6 500 points last month. It is worth reminding that at the start of the year, only the most sanguine forecasts envisioned the index closing the year at this level. Earnings of tech behemoths in late July were the primary source of such euphoria. Huge capital expenditures of hyperscalers confirmed money managers' conviction that AI boom shows no signs of abating.

Furthermore, the US central bankers are moving more decisively towards cut in September. Jerome Powell's Jackson Hole speech was principally about shifting balance of risks. At this stage, the Fed seems to be determined to avert broader economic slowdown. The central bank has started to focus on the labour market faltering in spite of the fact that inflation remains well above target.

Nevertheless, there is some controversy in such a U-turn. The inflation remains sticky. The US central bank struggles to eradicate it. Core CPI for July reached 3.1 per cent. And tariffs are starting to bite. It is quite probable that inflationary pressures will accelerate in following months as companies need to increase prices to avoid margin dilution. I dare say it is somewhat irresponsible to cut interest rates at this stage.

Investors should be shocked by Donald Trump's incursions into the Fed's independence. Conversely, stocks just slightly below all-time highs suggest they have barely noticed. If the president succeeds in replacing Lisa Cook, it would effectively grant him control over the FOMC and the rate setting process would be politicised.

Short term rates would decline under such a scenario amid the inclination to looser monetary policy. However, longer term rates would spike as there would be a threat of inflation expectations de-anchoring. Abrupt rise in longer UST yields could be painful for investors and it could derail current market rally.

Moreover, the AI trade has become increasingly overcrowded. Investors have been comforted by the massive capex of the biggest tech companies. Alphabet, Amazon, Meta and Microsoft plan to invest around $350bn to AI or data centres in 2025. Nevertheless, there are first signals that the AI boom is losing momentum.

The report of Massachusetts Institute of Technology (MIT) reverberated across the market in late August. The MIT report suggests that 95 per cent of organizations do not generate any revenue or cost savings from their AI projects. Therefore, there are concerns that massive amount of capital, which is pouring into AI infrastructure, might be misallocated.

Furthermore, China pursues autonomy in chips and artificial intelligence. DeepSeek, the young Chinese start-up which developed an AI model similar to GPT but at fractional costs, published that it was able to train its large language models on Chinese chips. E-commerce giant Alibaba announced that it would design its own chips in near future. Such ambitions threaten the position of US chipmakers – they hoped to reap large profits from the Chinese markets.

Nvidia's results failed to dispel these doubts and reinvigorate investors' enthusiasm. Company's 3Q guidance shows that the leading AI chip designer cannot defy gravity forever. Even other designers of chips for the artificial intelligence disappointed portfolio managers – for instance Marvell Technology. Given that the AI theme underpins a large part of the recent stock market growth, any slowdown would be disastrous for equity performance.

While the dramatic market slump is not inevitable, markets seem to be vulnerable to a correction at the moment. Stocks are priced for perfection and the global environment is far from perfect. Monetisation of the AI and the Fed's interest rate path are the key areas to watch.

Financial markets insights of the month

August 2025: A sleeping month that still delivered surprises

Ondřej Koňák

Analyst

August is often seen as a **sleepy month for financial markets**. Trading volumes typically thin out as investors and policymakers head for holidays, leaving markets vulnerable to exaggerated swings but rarely producing lasting headlines. Seasonality studies confirm this: **MSCI World shows an average August return of just +0.15% compared to +0.60% in other months, with liquidity often at its lowest**.

Yet August 2025 showed that even during this "quiet" period, events can surface with broader implications for global investors.

Low liquidity, high sensitivity
Academic research has long documented that low summer liquidity can amplify price moves, especially if unexpected news hits. This year, several developments challenged the idea of a sleepy August:

UK bank tax fears
Rumors of a potential windfall tax on UK banks triggered sharp losses across the sector, wiping off over GBP 6bn in market cap within days. With NatWest, Lloyds, and Barclays particularly hard hit, the episode reminded investors how fragile sentiment can be when trading volumes are roughly 25% below annual averages.

U.S. rate-cut expectations intensify
A softening U.S. labor market and a widening trade deficit, the largest in two years – fueled speculation that the Federal Reserve may cut rates as early as September. By the end of the month, **Fed funds futures priced in a 60% probability of a September rate cut**. The dollar weakened roughly 2% against major peers over the month, underlining how markets are quick to price in monetary shifts when liquidity is shallow.

Geopolitical theater
The Trump–Putin summit in Alaska drew headlines mid-month. While direct market impact was muted, the event highlighted ongoing geopolitical undercurrents that can easily unsettle investors in a low-volume environment.

Why this matters
While none of these events by themselves created systemic dislocation, their **confluence during August** illustrates three important dynamics:

1. **Thin markets magnify risk**: even modest headlines can move prices disproportionately.
2. **Policy uncertainty never sleeps**: from fiscal populism in Europe to monetary easing in the U.S., investors must remain vigilant even during the summer lull.
3. **Geopolitical noise adds fragility**: August often becomes the stage for "surprise diplomacy" that can ripple through risk sentiment.

Investor takeaway
August 2025 reaffirmed that "quiet months" can still matter. For long-term allocators, the lesson is not to dismiss the summer as irrelevant. Managing liquidity risk remains crucial, as bid–ask spreads in global equities typically widen by 10–15% during the summer. On the other hand, volatility should be seen as an opportunity rather than a threat — in past decades, two-thirds of August drawdowns were reversed within three months.

Banking sector insight of the month

When three pillars grow too thick, should they become one?

Michal Mesík, CFA
Analyst

In 2004, Basel II introduced the three-pillar framework of the Basel Accord: minimum capital requirements (Pillar I), supervisory review (Pillar II), and market discipline (Pillar III). Over the past 21 years, the boundaries and purposes of these pillars have become increasingly confluent. This article argues for moving away from the three-pillar structure in favor of a single-pillar system centered on the current Pillar II. While this suggestion may seem extreme, it aims to provoke critical thinking about whether the regulatory framework has grown unnecessarily complex. At the same time, the author acknowledges that the arguments presented are more applicable to the European context than to other jurisdictions.

Pillar I was designed to produce standardised metrics, in particular a key capital adequacy ratio comparable across banks and jurisdictions. In contrast, Pillar II was intended to allow for a true and subjective view of the bank's own risk profile, going beyond the three main risk types covered by Pillar I - credit, market and operational risk. Further, in support of market discipline, Pillar III was established to enforce banks' public disclosure of information on their risk exposures.

However, the lines between the three pillars have become increasingly blurred over time. Pillar II is now heavily regulated and supervised, with the ECB challenging nearly all the governance choices and modelling assumptions within banks' internal risk management frameworks. The ECB is using the assessment of Pillar II frameworks to prescribe minimum capital requirements, which was originally the domain of Pillar I.

Both Pillar I and Pillar II aim to safeguard the going concern of banks, ensuring that a bank can continue operating following a crisis. This is further complemented by the Minimum Requirement for Own Funds and Eligible Liabilities (MREL), focusing on gone concern situations, i.e. having sufficient capital and other resources for an orderly resolution of a bank in case of failure. As a result, the capital situation of banks is known to authorities under both going and gone concerns perspectives.

Moreover, thanks to the information collected in the annual Supervisory Review and Evaluation Process (SREP), the ECB nowadays disposes of sufficiently granular data and contextual information, to be able to approximate the market disclosures required under Pillar III. While the ECB cannot yet fully replicate the (semi-) annual Pillar III reports issued by banks, a combination of ECB-collected data and banks' own commentary would likely get very close.

So why maintain a three-pillar system if the pillars are so intertwined? One possible argument would be that Pillar I only covers the main risk types - credit, market and operational risk - while Pillar II addresses any risk type that a bank considers material, which hinders direct comparability among banks. Still, the ECB has long compared banks using not just Pillar I data, but also Pillar II metrics and ICAAP/ILAAP information collected for SREP purposes. Hence, within the EU, this argument does not hold. Similarly, outside EU, the argument is week as even Pillar I tends to diverge across jurisdictions, as illustrated by the weakening of Basel III rules and their implementation in the U.S.

Pillar III would also struggle to defend its existence as a separate pillar. Much of the information disclosed by banks is already available to supervisors through regular reporting, EBA stress testing, on-site inspections, and portfolio reviews. On the other hand, concentrating disclosures in the hands of supervisors may weaken transparency and undermine investor and depositor confidence, especially in crisis situations. This is a valid point that needs to be considered, however, not an insurmountable obstacle to the integration of the three Pillars of Basel.

In summary, this contribution argues in favor of a strengthened role for Pillar II that could effectively integrate Pillars I and III, as their functions are either implicitly covered by Pillar II or can be derived from it. The enhanced Pillar II would consequently need to further evolve, to provide for the increased transparency towards market and comparability among banks currently provided by the other two pillars. This way the three pillars could eventually grow into one.

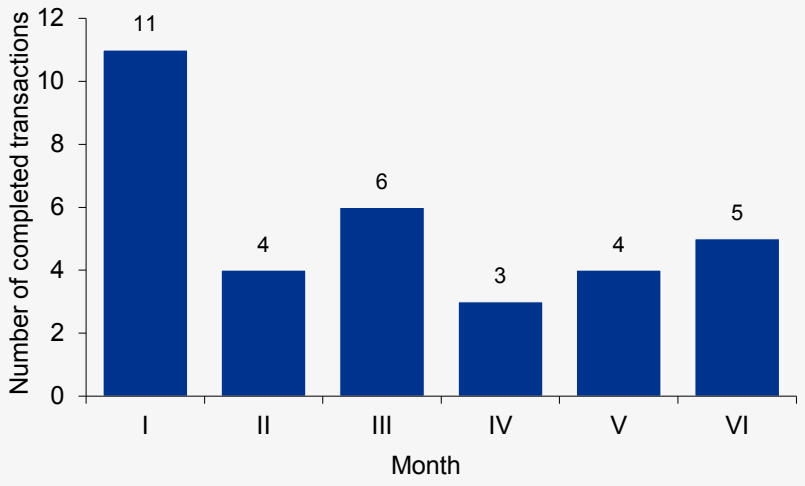
Czech M&A market insight of the month

Czech M&A in H1 2025: Deal flow and market trends

Tamara Lorencová
Analyst

The Czech M&A market opened 2025 with a sprint and then settled into a steadier jog. Completions were heavily front-loaded: 33 Czech-target deals closed in H1, 21 in Q1 and 12 in Q2, with January the clear outlier month for activity.

Chart 1: Number of Czech targets acquired by month (H1 2025)



Source: Mergermarket and author analysis

Sector activity: Czech targets

The sector mix stayed tight. Technology, media, and telecommunications (TMT) remained the growth engine, accounting for 28 % of deals, powered by ongoing digitalization and the country's robust engineering and software sector. Healthcare (including pharma and biotech) contributed approximately 12 %, reflecting resilient demand and innovation. Leisure and consumer sectors together accounted for roughly 15 %, as confidence continued to normalize. Beyond these pillars, activity was more dispersed, with automotive, construction, financial services, logistics, industrials, and real estate each adding a smaller but steady share of transactions.

Outbound expansion of Czech bidders

Czech buyers were notably active and increasingly outward-facing. They completed 42 acquisitions in H1 2025 across 15 countries: 14 domestic and 28 outbound (≈67 %). The busiest corridors were Germany (6) and Poland (6), followed by the UK, Italy, Romania, and Australia (2 each). Single-deal forays included the USA, Switzerland, Spain, Estonia, Croatia, Serbia, Israel, and Slovakia. This breadth underscores Czech buyers' confidence competing for assets across Europe and beyond.

Strategic and financial buyers

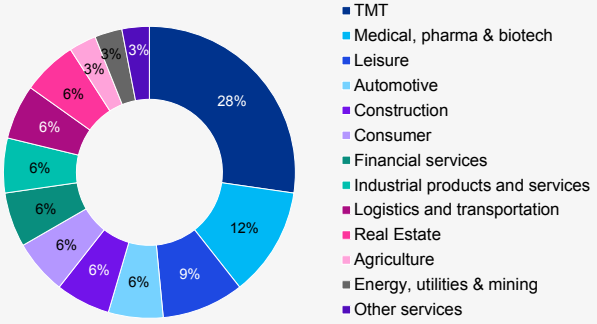
Strategic acquirers led with 22 transactions, many tied to multi-year consolidation. Among the most active bidders were Penta Hospitals International, which expanded its CEE healthcare platform with two acquisitions, and the EAG group, which completed two deals in technology and services—illustrating corporates' drive to scale internationally and move into higher-margin niches.

Financial sponsors closed 20 deals, with activity spread across a broad investor base. Genesis Capital Growth stood out as the most active PE buyer, completing three acquisitions across software, consumer, and manufacturing. PPF Group followed with two transactions spanning telecoms and agriculture. Venture investors also played a visible role, with Soulmates Ventures the most active, participating as a co-investor in two acquisitions abroad.

Outlook for the second half of 2025

Looking ahead, the set-up for H2 is balanced but constructive. With financing costs still elevated, selectivity will remain high. TMT and healthcare are expected to stay the anchor sectors, while industrials and logistics should benefit from nearshoring trends and infrastructure capex. With strategics and sponsors nearly evenly matched, the Czech market should remain orderly and competitive, with the country continuing to punch above its weight as both a target destination and a regional bidder powerhouse.

Chart 2: Czech target acquisitions by sector (H1 2025)



Source: Mergermarket and author analysis

Table: Country of the target acquired by Czech bidders (H1 2025)

Country of the target	Number of deals completed
Czech Republic	14
Germany	6
Poland	6
United Kingdom	2
Australia	2
Italy	2
Romania	2
USA	1
Switzerland	1
Spain	1
Estonia	1
Croatia	1
Serbia	1
Israel	1
Slovakia	1
Total	**42**

Source: Mergermarket and author analysis

Private equity insight of the month

Are private equity still leads long-term?

Lukáš Baloga

Analyst

Private Markets: *The past two to three years have tested private equity investors. Elevated interest rates, persistent macroeconomic uncertainty, and delayed exits as GPs wait for more favourable conditions have constrained liquidity. This has created a challenging environment for both general partners (GPs) and their limited partners (LPs).*

Public Markets: *Market growth has been driven largely by capital inflows into market-weighted index ETFs, particularly the S&P 500 and Nasdaq. A significant share of this momentum is linked to the AI boom, which has pushed market concentration to historic levels. Today, the 10 largest stocks account for more than one-third of total market capitalization, surpassing the levels seen during the dot-com bubble.* (link)

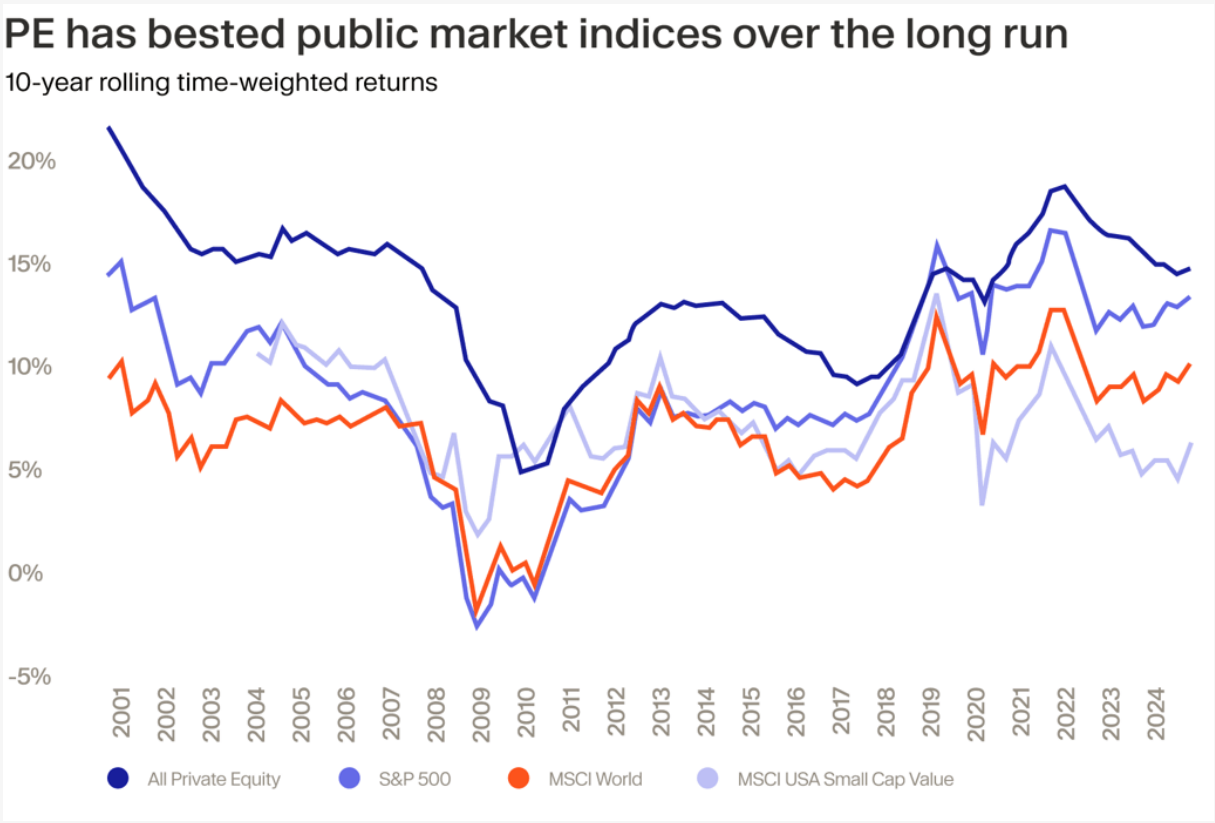
Looking beyond ordinary public market comparison

Moreover, today's public markets are highly concentrated in a single sector, primarily technology and AI. Private equity, by contrast, tends to allocate more capital into more resilient industries such as healthcare, software, and business services. This stands in sharp contrast to public indices, which are heavily weighted toward consumer discretionary and industrials, segments more exposed to cyclical headwinds.

Recent market growth has been driven largely by capital inflows and thus multiple expansion. However, history shows that companies trading at elevated multiples often face significant multiple contraction during economic slowdowns. This dynamic makes broad public market indices a less relevant benchmark for a diversified private equity portfolio.

Long-term outperformance

Hamilton Lane's 2025 Market Overview shows that $1 invested in private equity in 2015 would have grown to $3.96 by 2024, compared with $3.51 in the S&P 500 and $2.61 in the MSCI World. Rolling 10-year return analysis underscores the consistency of this outperformance, with private equity ahead of public markets in nearly all periods. The only exceptions were 2010 and 2019, when public markets briefly led.



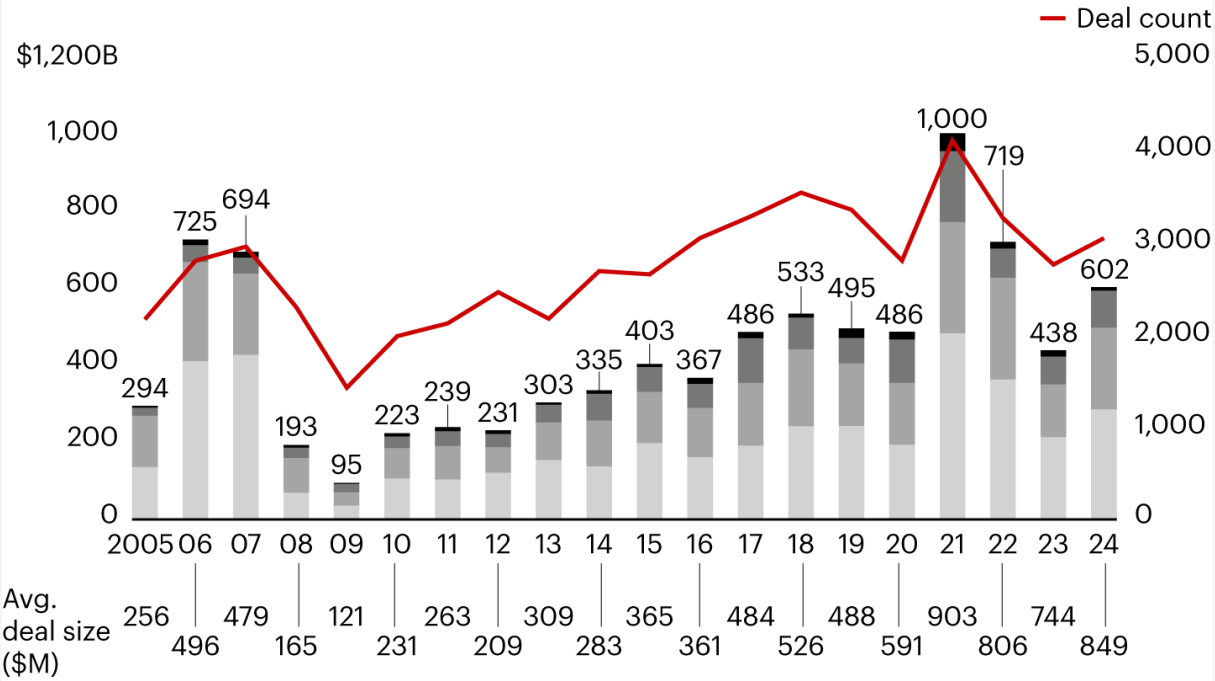
Source: Hamilton Lane, 2025 Market Overview, published 2025

Signs of recovery?

North American deal value rose 34% on a 9% increase in deal count, while Europe saw even stronger momentum with deal value up 54% on the same 9% uplift in transactions. The debt markets continued to evolve, and valuation multiples remained elevated near 10-year highs—ending 2024 at 11.9x EV/EBITDA in the US and 12.1x in Western Europe.

Globally, deal flow increased 10% year-over-year to around 3,000 transactions. Yet, deal value grew much faster, as the average deal size surged to $849 million, second-highest level on record. Notably, transactions of $1 billion or more accounted for 77% of total deal value, underscoring the outsized role of large-cap deals in driving market activity.

Global buyout deal value, by region



Change in deal value

	2024 vs. 2023	2024 vs. 5-yr. avg.
Rest of world	–44%	–64%
Asia-Pacific	33%	–6%
Europe	54%	5%
North America	34%	–5%
Total	**37%**	**–4%**

Sources: Dealogic; Bain & Company, Global Private Equity Report – Private Equity Outlook 2025: Is a Recovery Starting to Take Shape?, March 3, 2025

According to White & Case and Dealogic, global private equity exit value reached $175.6 billion in the first quarter of 2025, almost triple the $65.4 billion recorded in Q1 2024 and the strongest quarter since Q2 2022. (link)

Preqin's outlook for H2 2025 points to persistent fundraising headwinds and geopolitical uncertainty, but also a stronger focus on liquidity through secondaries and GP-led continuation vehicles. LPs face mounting pressure to free up capital, fueling record secondary activity, even at NAV discounts. (link) While deal momentum has cooled, larger transactions are gaining share, and optimism remains that easing rates and growing capital pools could support a recovery ahead.

Behavioral finance insight of the month

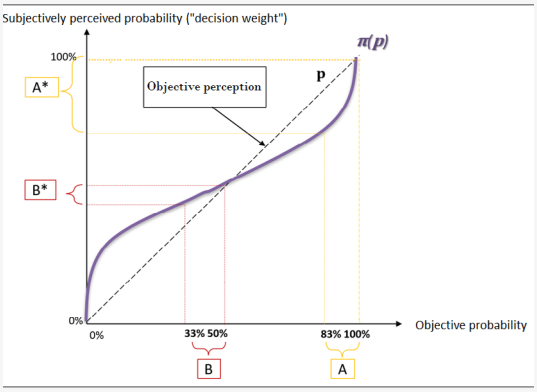
Why probabilities deceive us: The weighting function and its extension in Cumulative Prospect Theory

Jana Přílučíková, PhD

Analyst

According to Kahneman and Tversky (1979), people do not evaluate probabilities objectively. In other words, people do not treat probabilities proportionally to their true values. Instead, they assign decision weights—subjective values that distort real probabilities, investors not excluded – as we are prone to systematic deviations from rational, statistically consistent reasoning.

Fig. 1. The Prospect Theory Weighting Function



Source: Přílučíková (2024)

The weighting function of Prospect Theory captures two key insights:

- Overweighting of small probabilities: We are prone to attach too much significance to rare events (e.g., lottery wins, market crashes).
- Underweighting of large probabilities: We tend to discount high-probability outcomes (e.g., stable investments), making us more cautious than rational models predict.

Graphically, this creates an S-shaped curve that departs from the 45° rational line (where perceived and actual probabilities would match).

In other words, the weighting function shows that people tend to behave as if probabilities were distorted — for example, a 1% chance might "feel like"- perceived as closer to 5%, while a 90% chance might "feel like" only around 70%.

Why this matters for investors?

These distortions have concrete implications:

- Risk-seeking in unlikely gains: Investors chase lottery-like stocks, speculative options, or crypto assets, hoping for outsized returns.
- Overreaction to rare threats: Market crashes or "black swan" events often trigger exaggerated fear and sell-offs.
- Caution in likely gains: Even high-probability investment opportunities may be avoided due to overweighted fears of loss.

This behavior connects to well-known biases such as base rate neglect, the certainty effect, and overconfidence bias—all of which skew how we weigh financial risks.

From Prospect Theory to Cumulative Prospect Theory

In their later refinement, Kahneman and Tversky (1992) introduced Cumulative Prospect Theory (CPT). CPT extends the original model by

- Applying the weighting function in a cumulative manner across ordered outcomes,
- Incorporating reference dependence and loss aversion,
- Explaining why investors often display four patterns of risk attitudes:
  - Risk-averse for high-probability gains
  - Risk-seeking for low-probability gains
  - Risk-seeking for high-probability losses
  - Risk-averse for low-probability losses

This framework helps us understand real-world puzzles such as the disposition effect (holding losing stocks too long while selling winners too early). We will explore this powerful bias in more depth in the next Behavioral Finance Insight.

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Real estate insight of the month

CRE market recovery thesis remains intact

Lukáš Štieber

Analyst

The 2022–2023 period saw an exceptional rise in bond yields, accompanied by widespread recession fears. This environment put significant downward pressure on cyclically expensive CRE assets, resulting in sharp market value declines. By 2024, however, market consensus had formed that the first half of the year likely marked the cyclical trough across most European CRE sectors.

Throughout 2024, market dynamics in net initial yields (NIY) and rents reinforced the CRE recovery thesis: a large proportion of markets reported stable or contracting NIY alongside stable or rising net operating income. This suggested that fundamentals were stabilizing despite broader macroeconomic headwinds.

Entering 2025, financial markets became volatile. In April, recession risks triggered falling equity prices, widening bond spreads, and renewed pressure on government bond yields. Even so, CRE pricing reflected cautious optimism, supported by stronger fundamentals and falling debt costs. As of Q2 2025, updated data for European private prime CRE indicated broad stabilization. Office and retail segments showed 100% of markets with either stable or declining NIY, while industrial properties showed similar dynamics in 97% of cases. On the income side, 97% of office markets, 100% of retail markets, and 94% of industrial markets reported stable or rising rents. This resilience supports the CRE recovery thesis, even amid tariff uncertainty, policy headwinds, and sluggish European economic growth.

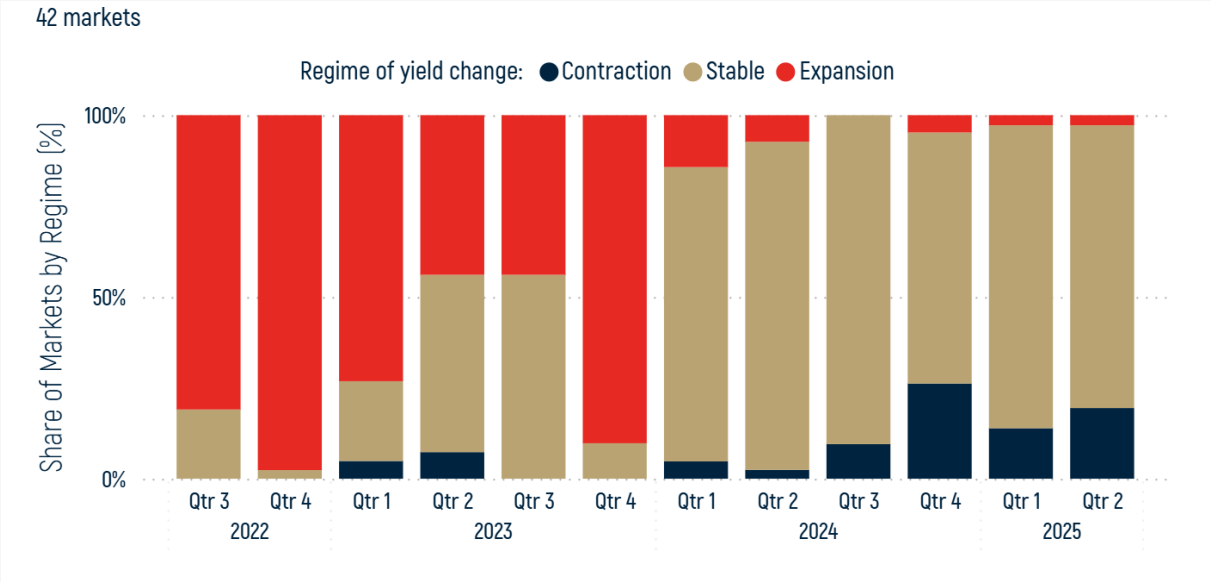
Still, risks remain tied to recessionary pressures, which could undermine fundamentals through rising vacancy rates.

In H2 2025, sentiment toward CRE was lifted by broader capital market optimism. However, equity gains were largely concentrated in AI-driven themes and expectations of cheaper capital, which may not fully reflect the true health of the underlying economy.

Structurally, European security priorities—including defense, supply chain resilience, and industrial capacity—supported by fiscal policy measures such as Germany's large-scale industrial stimulus, are providing a positive tailwind for the industrial segment.

Overall, market conditions remain encouraging. However, fund outperformance will depend critically on geographic and sectoral allocation, as performance is expected to diverge significantly. We do not expect cap rate compression back to pre-pandemic levels. Instead, total returns will be primarily income-driven, with income growth as the key driver, while capital appreciation is likely to remain limited in light of elevated bond yields.

Chart: Share of European industrial CRE markets by yield regime (contracting, stable, or expanding)



Source: C&W, Arete

Quantitative methods insight of the month

From Lucas to modern empirics: The cost of business cycles

Vojtěch Šikl

Analyst

Business cycles, the periodic fluctuations in economic activity around long-term growth trends, have important implications for human welfare. While economic growth raises living standards over time, the volatility around this trend creates uncertainty, unemployment risk, and consumption instability that may significantly reduce welfare. The measurement of these welfare costs has been important to macroeconomic policy debates, shaping our understanding of whether governments should prioritize stabilization policies over growth-enhancing reforms. This issue gained particular importance following Robert Lucas's controversial 1987 calculation. His result implied that research and policy attention should focus more on long-run growth trends than on short-term business cycle fluctuations.

Lucas (1987) introduced a welfare-theoretic framework to quantify the cost of business cycles. The basic idea was to compare the lifetime utility of a representative agent in two economies: one with perfectly smooth, continuous growth, and another subject to cyclical fluctuations around the same trend. The central question was how much additional consumption would need to be given to agents in the volatile economy to make them indifferent between living with shocks and enjoying smooth growth. Formally, Lucas considered an infinitely-lived representative agent with constant relative risk aversion (CRRA) preferences, a specification widely used in macroeconomic modeling where consumption C generates utility equal to

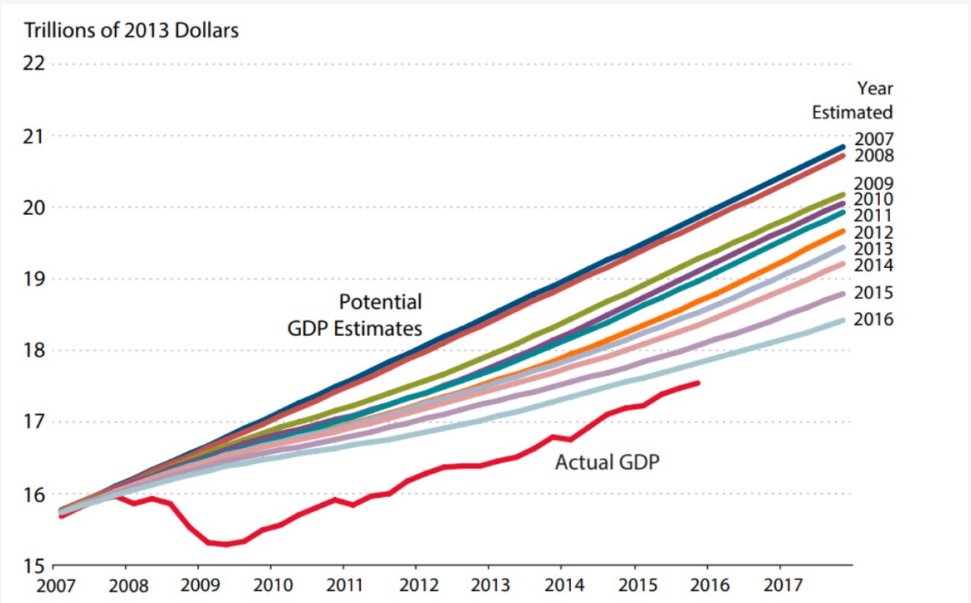
$$\frac{C^{1-\gamma}}{1-\gamma}, \gamma > 1$$

Aggregate consumption grows along a deterministic trend but is subject to shocks. The comparison can be written as:

$$\sum_{t=0}^{\infty} \beta^t \frac{(\lambda^t C_0)^{1-\gamma}}{1-\gamma} = E_0 \sum_{t=0}^{\infty} \beta^t \frac{[\lambda^t C_0 (1+\varepsilon_t)(1+\chi)]^{1-\gamma}}{1-\gamma}$$

On the left-hand side of the equation is the lifetime utility under smooth growth, while the right-hand side represents the expected utility under cyclical growth, where shocks ε_t generate random deviations around the trend and χ is the compensating wealth transfer needed to make the agent indifferent between the two environments (the additional terms are highlighted in blue). The parameter $0 < \beta < 1$ is the time discount factor reflecting the preference for present over future consumption. The coefficient γ, which is usually above 1, measures how much agents dislike uncertainty. The initial consumption is denoted by C_0, while $\lambda > 1$ is the deterministic trend growth rate of consumption. Finally, ε_t are identically and independently distributed mean zero shocks, whose standard deviation is calibrated from the cyclical component of post-war U.S. consumption after removing the trend using the Hodrick-Prescott filter. The expectation operator E_0 reflects uncertainty about future shock realizations (we do not know how severe a recession will be beforehand). By solving for χ, Lucas found that the required compensation was only about 0.04% of consumption, leading him to conclude that the welfare cost of business cycles was essentially negligible. In other words, his result suggested that Americans would sacrifice at most 0.05% of average consumption to eliminate business cycles entirely, which corresponds to roughly 25 dollars per year for someone consuming 50,000 dollars. Lucas's negligible cost estimate has faced sustained criticism on several fronts. One major limitation is that his framework ignores heterogeneity in wealth, income, and risk exposure across households. Krusell et al. (2009) showed that households with very little wealth would be willing to sacrifice up to 4% of consumption to eliminate cycles, whereas wealthy households might even benefit from volatility through investment opportunities. Barlevy (2004) offered a different critique, arguing that business cycles affect not only consumption volatility but also long-run growth. Incorporating efficiency losses from investment timing (firms delaying factory construction during recessions) and adjustment frictions (workers stuck in declining industries unable to quickly move to growing sectors), he found that eliminating cycles could raise annual consumption growth, with agents willing to forgo up to 8% of consumption each year to avoid fluctuations and their drag on growth.

The 2008 recession provides compelling evidence for such persistent effects. The chart below reveals how successive downward revisions to potential GDP estimates reflect permanent damage to productive capacity. The red line shows actual real GDP from 2007 to 2017, while the colored lines plot successive estimates of potential GDP made at different points in time. Following the crisis, potential GDP was revised downward repeatedly. In 2007, projections anticipated a continued strong expansion, but by 2016 estimated potential output was more than $2 trillion lower than the pre-crisis forecast. This evidence supports the view that business cycles can leave lasting scars on the economy, reducing productive capacity rather than merely creating temporary output gaps.



Estimates of Potential Real Gross Domestic Product for the U.S.
Source: Summers (2017) based on Congressional Budget Office data

Three mechanisms explain these persistent effects: labor market scarring (unemployed workers lose skills and exit permanently, young workers miss crucial early development), reduced investment (firms slash R&D and capital spending, permanently lowering innovation and capital stock), and growth rate reduction (the economy shifts to a flatter trajectory rather than returning to trend). These findings contradict Lucas's assumption of temporary fluctuations around an unchanged trend. If recessions permanently reduce both the level and growth rate of potential GDP, welfare costs far exceed Lucas's 0.04% estimate. The $2 trillion annual gap between pre-crisis projections and actual potential GDP supports modern estimates of the cost of business cycles and hence robust stabilization policies.

The recognition of these persistent effects has sparked numerous extensions to Lucas's framework. Models incorporating labor market frictions show that unemployment affects workers beyond temporary income loss through lasting damage to job prospects and human capital. Additionally, research documents how recessions reduce school enrollment, permanently lowering lifetime earnings and future productive capacity. To mention one recent empirical survey, Georgarakos et al. (2025), surveying households across thirteen advanced economies, found that individuals would sacrifice 5–6% of lifetime consumption to eliminate business cycle fluctuations - over one hundred times Lucas's estimate. This willingness to pay varies systematically with individual characteristics and country-level factors: those with more procyclical consumption, greater economic uncertainty, and residence in historically volatile countries express higher willingness to pay. Cross-country variation is considerable, with German and Dutch households willing to sacrifice 3–4% of consumption versus 6% for Spanish and Greek households, perhaps reflecting different historical experiences with economic instability.

Lucas's calculation, despite its limitations, catalyzed decades of research on business cycle costs. The evolution from his 0.04% estimate to modern calculations of 3–8% reflects advances in incorporating household heterogeneity, incomplete markets, and growth effects that revealed how aggregate volatility captures only a fraction of true welfare costs. Empirical evidence now demonstrates substantial costs through permanent output losses and human capital destruction. These findings imply that preventing recessions is important for maintaining long-run growth potential, complementing rather than constraining growth-oriented policies.

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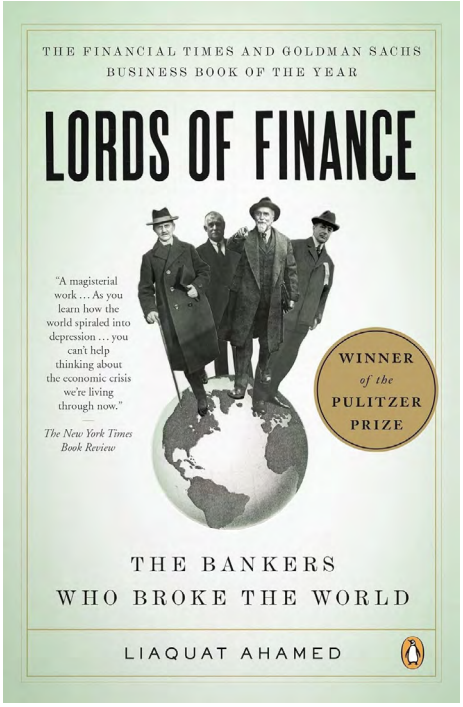
Book review of the month

Lords of Finance: The Bankers Who Broke the World, Liaquat Ahamed, 2009

Michal Stupavský, CFA

Head of Research



This genuine masterpiece and the Pulitzer Prize Winner in 2010 describe the true story of "The Most Exclusive Club in the World" – the quartet of central bankers – who were literally running the world during 1920s and 1930s. This quartet of the heads of the most important central banks of the time consisted of the following figures:

- Benjamin Strong, Governor of the Federal Reserve Bank of New York, 1914 – 1928
- Montagu Norman, Governor of the Bank of England, 1920 – 1944
- Hjalmar Schacht, President of the Reichsbank, 1923 – 1930 and 1933 – 1939
- Émile Moreau, Governor of the Banque de France, 1926–1930

The book covers key economic topics of the time with a major focus on the key central banks, such as financing of the war efforts during World War I, the German reparations and war debts, the very inflexible and inherently unstable international gold standard system of the time, the German hyperinflation at the beginning of 1920s, the stock market bubble at the end of 1920s bursting on Wall Street in 1929 and the subsequent Great Depression of 1929 – 1933, the subsequent uneven economic recovery including Roosevelt's New Deal Recovery programs, and finally the establishment of the Bretton Woods monetary system in 1944.

I must admit it has been a very long time since I had been amazed by professional literature to such an extent. Liaquat Ahamed managed to tell the whole story in such a way that I dare say that the book is kind of an economic thriller in the positive sense of the word. Extreme attention to every detail, particularly personality characteristics of the main characters, including John Maynard Keynes, and behind the scenes of the highest levels of politics and central banking, has immediately made me an enthusiastic student of economic history. I strongly believe that every serious economist should read this book because a reader will be also able to find many intriguing economic parallels between 1920s & 1930s and the last 30 years, including the Asian currency crisis, the dot-com stock market bubble, the subprime real estate bubble and the Global Financial Crisis, and the current global debt super cycle.

Investománie – Competition for young investors

Could you handle managing millions of investors' capital?

The ECONET Association is launching another year of Investománie, a competition for young investors.

The motivation for creating Investománie was the effort to bring the world of finance closer to high school and university students and to awaken their interest in investing. The competition also aims to discover new talents among young people who could enrich the Czech and Slovak investment scene in the future. Last year showed that there is more than enough potential among students. Analyses that would stand up to professional scrutiny made it to the finals.

The five best investors will receive not only a financial reward, but also the opportunity to complete an internship at J&T Investiční společnost. Just follow the official website of Investománie and fill out the application in September. It is intended for all students from the Czech Republic and Slovakia who are not yet 23 years old, regardless of whether they already have experience with investing or are just starting out. The competition capacity is limited to 250 participants, so it is not worth delaying registration.

Participants will have three months to prepare an investment strategy for a fictitious client with clearly defined requirements via a demo account on the StockTrack platform. The contestants will present their thoughts and ideas in three rounds. First, they will prepare a written report, the most successful will advance to the round where they will film a short video defending their investment plan, and the best will finally present their strategy in person to a panel of experts.

This year, the expert jury consists of leading figures from the Czech investment community. It will include the CEO of J&T Investiční společnost Tomáš Martinec, portfolio managers Aleš Vávra and Jan Hájek, the CEO of the Prague Stock Exchange Petr Koblic, and the Regional Director of XTB Vladimír Holovka.

If you or someone you know is interested in investing, do not miss this opportunity. For the most up-to-date information and detailed information about the assignment, follow the official Investománie website, as well as the profile on social media.

About

Prague Finance Institute (PFI)

Non-profit organization affiliated with CERGE-EI

PFI aims to connect experienced and young finance professionals, including students, especially through educational and networking events

Our key activities

- **PFI Macro Anchor podcast** hosted by PFI Chief Economist Andre Chelhot, CFA
- **PFI Talks podcast** in cooperation with the daily E15 (e.g. Daniel Kahneman, Jeffrey Sachs, Aswath Damodaran, Marc Faber, Barry Eichengreen or Peter Oppenheimer)
- **Panel discussions** (roundtables)
- **Valuation Masterclass** (semester-long business valuation course)
- **Technical Analysis Masterclass** (unique six lectures on technical analysis)
- **Research** (PFI Monthly magazine)
- **PFI Scholarship**
- **Platform for sharing interesting job opportunities** in the financial sector
- **Social media**, especially LinkedIn

Contacts

Prague Finance Institute, z.s.
The Schebek Palace
Politickych veznu 936/7
110 00 Prague 1
Czech Republic
www.praguefi.com

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