Winter 2026 Market Outlook

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Winter 2026 Investment Outlook

Our outlook for 2026 is based on the following factors that we believe are likely to impact investment returns:

- Artificial Intelligence Investments and Commercialization of AI Applications
- Labor Market Conditions
- Inflation
- Fiscal and Monetary Policy

According to JP Morgan, as of late 2025 approximately 47% of the S&P 500's total market capitalization was attributable to companies directly involved with AI.

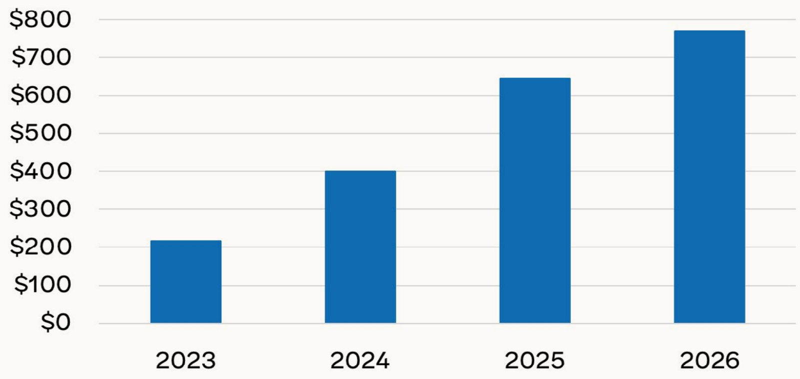
We expect demand for AI semiconductor chips and related equipment to remain strong in 2026. However, consensus forecasts obtained from Bloomberg call for capital expenditures growth at big technology companies to slow substantially in 2026, from 61% last year to 20% this year. Forecasts for AI investment spending have been revised upward consistently, so actual growth could ultimately exceed the current forecast.

Investors' scrutiny of AI capital spending intensified in Q4 2025, and the stocks and bonds of some big tech companies, including Oracle and Meta, traded sharply lower. Questions emerged about OpenAI's (owner of ChatGPT) ability to finance roughly $1.4 trillion in spending commitments it has made to various AI service providers over the next seven years, especially a $300 billion deal with Oracle. Oracle's stock and bonds declined in Q4 as these concerns grew. Additionally, Meta's shares fell sharply after providing higher-than-expected capital expenditure guidance on its Q3 earnings call.

We believe these events marked an important shift in sentiment towards AI spending. Through most of 2024 and 2025, big tech stocks rose along with capital expenditure forecasts. That dynamic began to break down in Q4 2025 for some big AI spenders. We expect investor scrutiny to continue in 2026, with the market demanding clear evidence that massive AI capital expenditures are translating into top-line revenue growth or meaningful margin expansion. If evidence does not emerge, we believe additional selling pressure could develop in the stocks and bonds of some big AI capital spenders, along with greater pressure on management teams to moderate capital spending growth. We also believe that such a development would likely weigh on shares of AI infrastructure providers.

One event we are monitoring closely in Q1 2026 is OpenAI's reported effort to raise $100B in a private financing round. We believe the outcome is likely to play a meaningful role in shaping sentiment towards AI infrastructure providers in 2026.

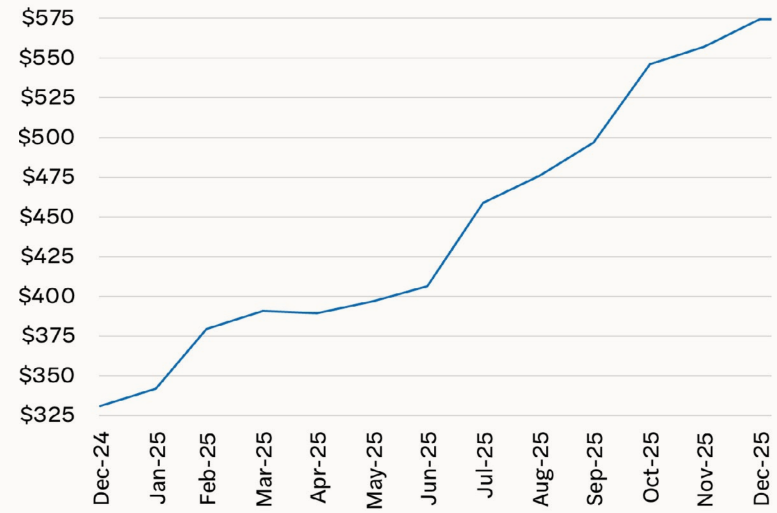
BIG TECH CLOUD SERVICE AND INTERNET COMPANIES TOTAL CAPITAL EXPENDITURES FORECAST



Source: Bloomberg, 2025 and 2026 consensus forecasts for MSFT, META, GOOG, AMZN, ORCL, TSLA, AAPL, BABA and Tencent

Companies that sell infrastructure for AI applications, such as semiconductor and semiconductor equipment manufacturers, have performed extremely well over the past three years and according to data from Bloomberg, they have outperformed companies that use AI, such as software companies, by about 150%. Software companies have been plagued by an intensifying investment narrative that AI may harm or even obsolete them due to AI's ability to write software code and lower entry barriers for new competitors.

CONSENSUS FORECAST REVISIONS FOR BIG TECH 2026 CAPITAL EXPENDITURES (BILLIONS)

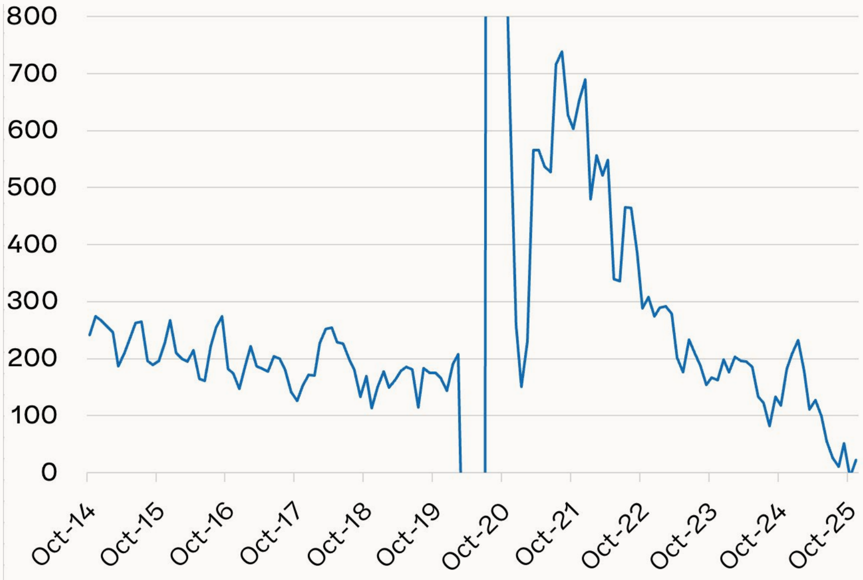


Source: Bloomberg, consensus forecast for Microsoft, Meta, Alphabet, Amazon, Oracle, Apple, Tesla, Tencent, Alibaba

We do not broadly share that view. In our opinion, AI is more likely to expand software opportunities than to eliminate them. Additionally, we don't believe AI infrastructure spending is likely to grow as expected if AI undermines one of its primary users, software companies.

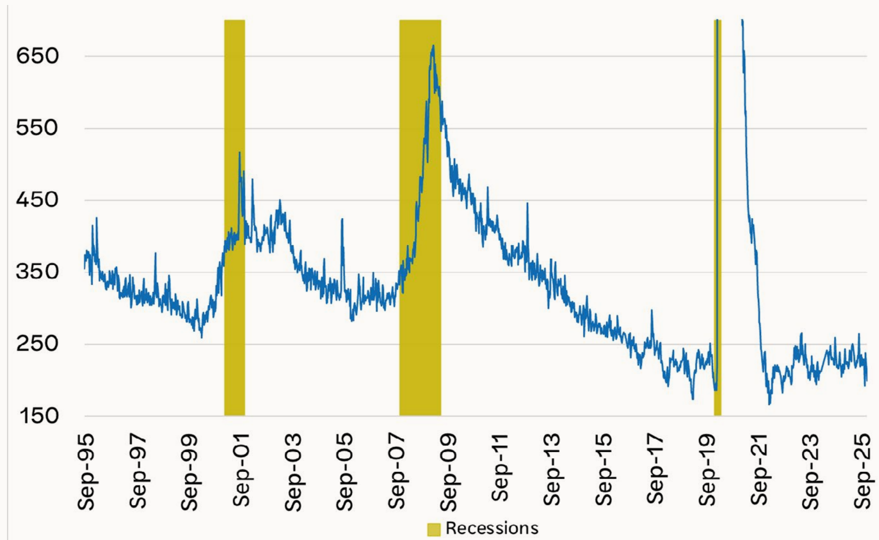
Job growth slowed notably in 2025, raising concerns about the strength of the labor market and economy. In contrast, initial unemployment claims remained near the low end of their long-term range.

NONFARM PAYROLL ADDITIONS
(3 MONTH AVERAGE, THOUSANDS)



Source: Bloomberg, Bureau of Labor Statistics

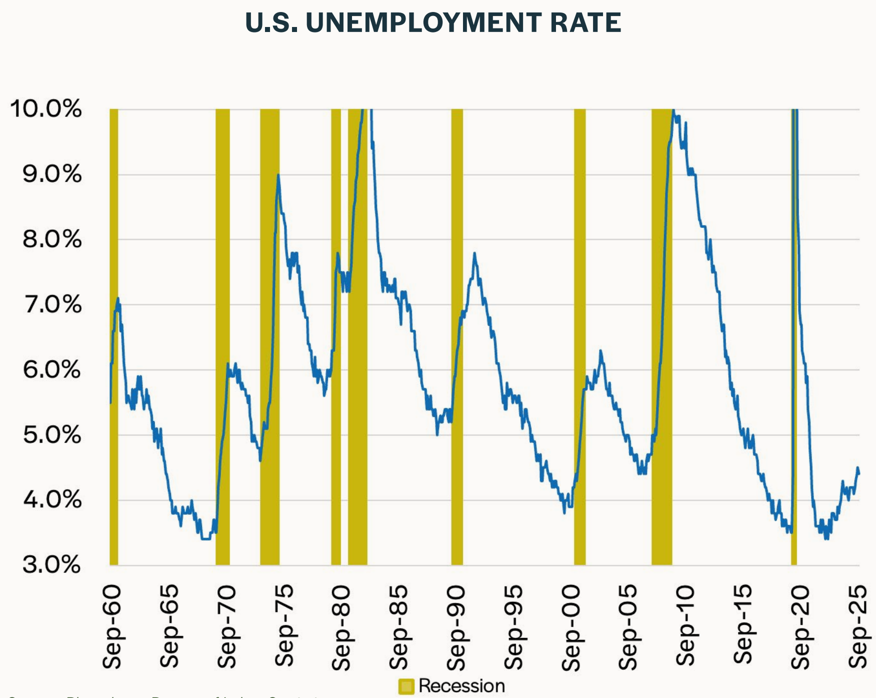
U.S. WEEKLY INITIAL UNEMPLOYMENT CLAIMS
(THOUSANDS)



Source: Bloomberg, Bureau of Labor Statistics

In our view, sharply lower immigration has reset the level of new job creation needed to maintain labor market equilibrium. The San Francisco Fed estimates that immigration declined 77% year over year in 2025, reducing the number of new jobs needed to keep the labor market in equilibrium. The Federal Reserve Bank of Kansas City estimates that just 29,000 to 77,000 new jobs per month are needed to maintain balance, well below historical averages. The most recent reading from the Bureau of Labor statistics from December 2025 shows 50,000 new jobs were created, solidly in the Kansas City Fed's equilibrium range. In addition, adoption of technology, including artificial intelligence, may be boosting output per worker, in our opinion, reducing the need for new employees. Labor productivity surged in 2025, and according to the St. Louis Fed, the increase is likely partially explained by AI and broader technology adoption.

While the low level of job losses is positive, the unemployment rate has risen due to the dearth of new job creation. Historical data shows that once the unemployment rate begins to climb, the rise has rarely brief and innocuous. Rather, initial upticks are often followed by more pronounced labor market deterioration.



Source: Bloomberg, Bureau of Labor Statistics

We believe the health of the labor market is a key risk to both the economy and stock returns in 2026. However, our base case is that job growth will remain positive. In our view, some of the decline in new job growth is explained by lower immigration and technology efficiency gains. Additionally, as described below, we believe both fiscal and monetary policy will provide a stimulative tailwind in 2026.

While headline inflation remained above the Federal Reserve's 2.0% target in 2025, the underlying drivers shifted. Services inflation continued to moderate, but goods inflation accelerated to the highest rate since mid-2023 and rose above the pre-pandemic range. The acceleration has been widely attributed to the implementation of new tariffs. If tariff rates stabilize or decline in 2026, we believe goods inflation will decelerate later in the year.

We expect services inflation to continue moderating in 2026, largely due to our view on housing inflation. Housing carries a 58% weight in core CPI services and is 35% of total CPI. Due to the way housing inflation is calculated in CPI, it lags real-time housing inflation measures, such changes in the list price of homes for sale and rent inflation. Currently, both the list price of homes for sale and rent inflation are well below CPI housing inflation, they continue to decline and are below their pre-pandemic ranges.

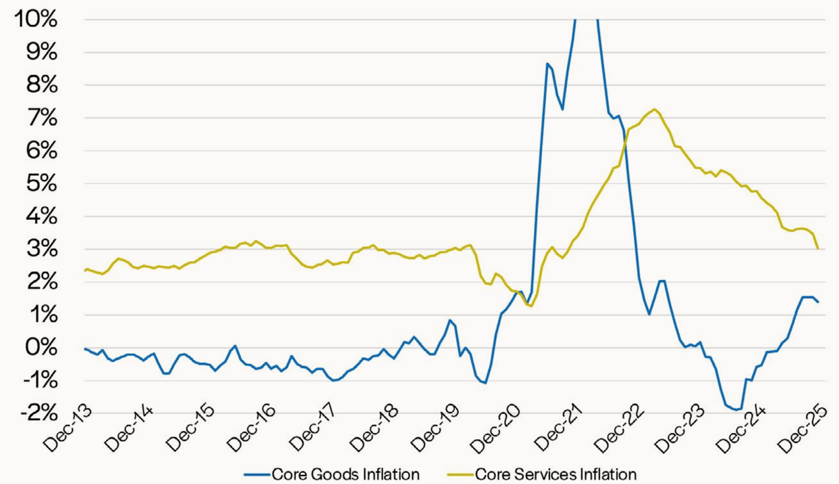
Wage growth is another key driver of services inflation and it has continued to decelerate. Considering the increase in the unemployment rate, we believe wage growth is more likely to moderate further in 2026 than reaccelerate. For these reasons, we believe CPI inflation will decelerate in 2026, though remain above the Fed's 2% target.

In our view, the primary risk to this outlook is that excessive monetary and fiscal stimulus keeps inflation anchored near the current level for longer than expected.

CONSUMER PRICE INDEX YEAR OVER YEAR CHANGE

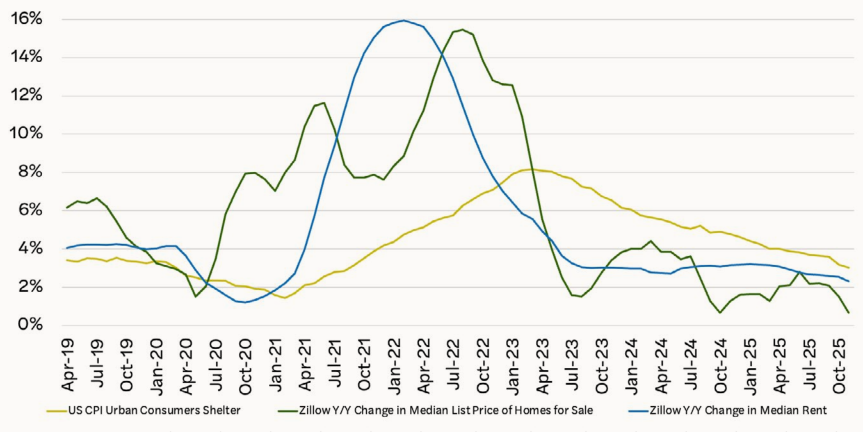
Source: Bloomberg, Bureau of Labor Statistics

CORE GOODS AND SERVICES CPI YEAR OVER YEAR CHANGE



Source: Bloomberg, Bureau of Labor Statistics

SHELTER INFLATION DATA



Source: Zillow, Bureau of Labor Statistics, Bloomberg

MEDIAN WAGE INFLATION

Source: Bloomberg, Atlanta Federal Reserve

FISCAL POLICY

Tax cuts included in the One Big Beautiful Bill Act will take effect in 2026 and, according to the nonpartisan Congressional Budget Office, they are projected to boost GDP growth by approximately 0.9% in 2026.

More broadly, the United States continues to run a federal budget deficit of more than 5% GDP. Historically, deficits of this magnitude have been associated with post-recession stimulus efforts, with the longest such episode occurring in the four years following the Global Financial Crisis. Notably, this is the first time the government has maintained a budget deficit of this magnitude more than four years removed from a recession.

MONETARY POLICY

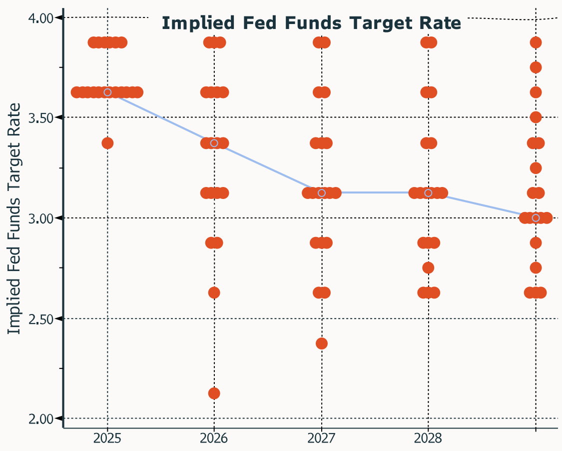
After spending much of 2025 assessing the inflationary impact of new tariffs, the Federal Reserve resumed its easing cycle in September. The Fed cut rates again in October and December due to growing concern about the health of the labor market.

Jerome Powell's term as Federal Reserve Chairman ends in May 2026, and President Trump is expected to announce his nominee for the role in early 2026. President Trump has called for large and rapid cuts to the federal funds rate, and in a late December 2025 post on Truth Social he stated, "Anybody who disagrees with me will never be Fed Chairman!" While the nominee must be confirmed by the Senate, approval only requires a simple majority, and Republicans currently hold 53 seats.

Although decisions on federal funds rates are made by a committee of twelve voting members, in our opinion, candidates being considered for the Fed Chair nomination are likely to advocate for rate cuts.

During the quarter, fixed income markets reflected evolving Federal Reserve policy, elevated issuance across several sectors, and generally stable underlying fundamentals. Treasury yields moved modestly, municipal markets continued to absorb historically high supply, and investment-grade credit remained supported by disciplined corporate balance sheets. Portfolio positioning remains focused on quality, diversification, and risk management as market and policy conditions continue to evolve.

FED DOT PLOTS



Note: Each dot represents one FOMC member's forecast. Source: Bloomberg

Federal Reserve Policy and Outlook

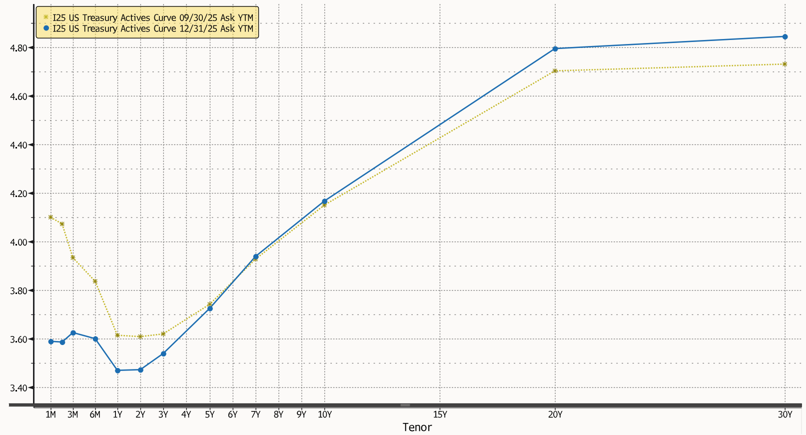
The Federal Reserve implemented three quarter-point interest rate cuts over the course of 2025, reflecting a change in the stance of monetary policy. The December meeting highlighted a notable degree of internal disagreement, with three formal dissents - the highest number since September 2019 - indicating a wider dispersion of views within the Committee. The updated dot plot reflected this divergence, with the median projection indicating one rate cut in 2026, while several participants projected either tighter policy or more substantial easing.

Policymakers appear more evenly balanced between dovish and hawkish perspectives, which has coincided with greater variability in policy expectations. This dynamic has been further complicated by delayed economic data releases following the U.S. government shutdown, making near-term assessment of economic conditions more challenging for both policymakers and market participants

Market expectations for rate cuts fluctuated throughout 2025, ranging from as few as one to as many as four at various points during the year. The FOMC median projection remained at two cuts for much of the year before shifting at the December meeting, when policymakers delivered a third reduction and revised the dot plot accordingly. Policy adjustments in 2026 remain less clearly defined as the federal funds rate has moved closer to estimates of neutral.

The December decision followed earlier guidance indicating that additional easing was not predetermined. The accompanying Summary of Economic Projections showed limited consensus regarding the degree of monetary restrictiveness or the expected path of the economy, consistent with the Federal Reserve's data-dependent policy framework.

US TREASURY YIELD CURVE



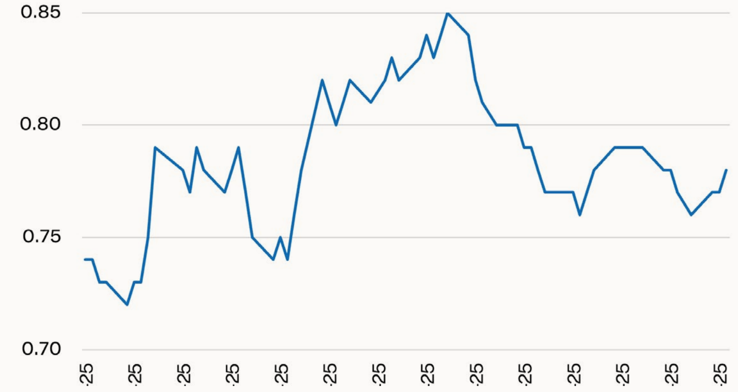
Note: Yellow line – Treasury yield curve 09/30/25 & Blue line – Treasury yield curve 12/31/25. Source: Bloomberg

The U.S. Treasury yield curve moved modestly steeper during the quarter amid mixed signals surrounding economic momentum and the future path of Federal Reserve policy. In December, Bloomberg's benchmark U.S. Treasury Index declined by 0.33%, with weakness concentrated at the long end of the curve. Despite the month's decline, Treasuries finished 2025 with a 6.32% total return, marking the strongest annual performance for the index since 2020.

By the end of December, market expectations for Federal Reserve policy over the subsequent twelve months were largely unchanged from late November, leaving two-year Treasury yields just under 3.50%. Longer-dated yields moved higher early in the month and remained elevated as economic data continued to point to economic data that remained generally consistent with ongoing growth.

The combination of stable intermediate yields and modest increases at the long end resulted in a gradual steepening of the yield curve. On December 30, the spread between two- and ten-year Treasuries reached its widest level since January 2022. At approximately 69 basis points, the curve remains relatively flat compared with historical norms observed during prior easing cycles. Yield-curve dynamics continue to reflect a combination of policy expectations, Treasury issuance patterns, term premia, and incoming economic data.

INVESTMENT GRADE CREDIT SPREADS



Note: Bloomberg US Agg Corporate OAS 09/30/25 – 12/31/25. Source: Bloomberg

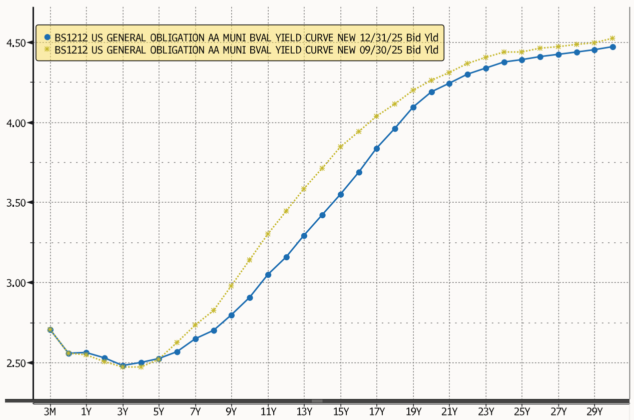
Investment-grade corporate credit conditions in 2025 reflected generally stable fundamentals and steady investor participation. As of December, option-adjusted spreads on the Bloomberg U.S. Aggregate Corporate Index were near 79 basis points, a level that remains narrow relative to longer-term historical averages. At these levels, market commentary has increasingly focused on the potential for spread widening should conditions change

Greater attention has been directed toward supply dynamics. Following several years of balance-sheet discipline, corporate issuance has shown signs of increasing, driven in part by higher capital expenditures in select sectors and a pickup in merger and acquisition activity. While estimates vary, issuance levels discussed by market participants could exceed prior highs, surpassing the elevated issuance observed during the low-rate environment of 2020.

From a fundamental perspective, earnings and revenue trends have remained generally positive, while leverage ratios and other key credit metrics have stayed near long-term norms. Capital spending has remained measured across most industries, with limited evidence of broad-based excesses. Taken together, these observations align more closely with conditions typically associated with a mid-cycle environment than with periods of widespread late-cycle stress.

INTEREST RATES

MUNI YIELD CURVE



Note: Yellow line – Muni yield curve 09/30/25 & Blue line – Muni yield curve 12/31/25. Source: Bloomberg

Municipal bond yields declined across much of the curve during the fourth quarter of 2025. Shorter maturities experienced higher volatility but ended the period with limited net change, as market pricing adjusted to shifting expectations around Federal Reserve policy. Intermediate maturities showed comparatively stronger performance, reflecting relative valuation differences compared with other high-quality fixed income sectors.

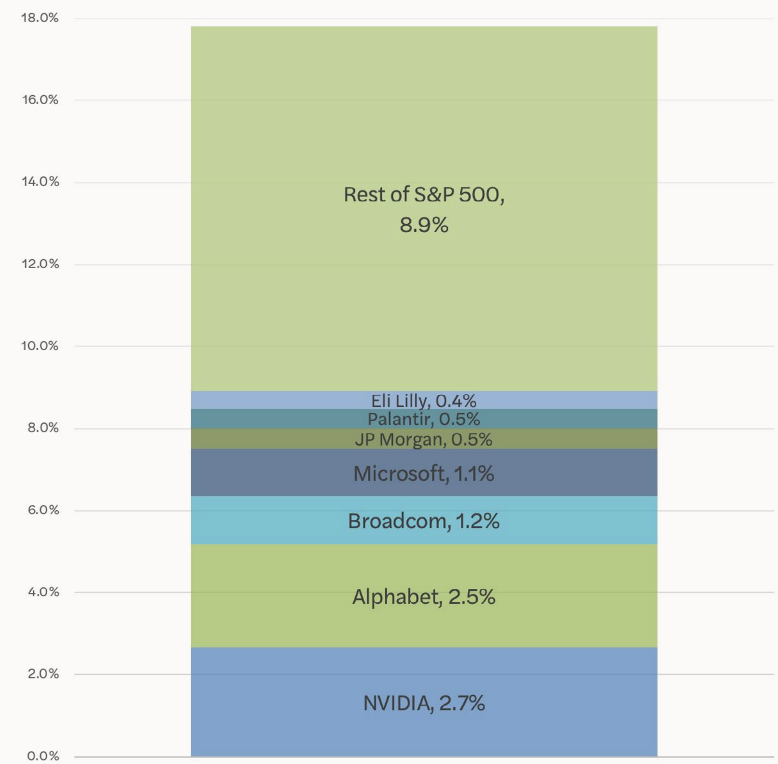
Issuance remained elevated, with fourth-quarter municipal supply exceeding $150 billion for the second consecutive quarter of record issuance. For the full year, municipal issuance totaled approximately $580 billion, marking the second consecutive year of record supply and reflecting continued borrowing activity by state and local governments.

Despite the elevated issuance environment, performance was relatively stable. Year-to-date total returns for the intermediate municipal index we monitor, the Bloomberg Municipal Bond: Quality Intermediate Index, were approximately 6%, representing the highest returns among maturity segments. Nominal and taxable-equivalent yields remain elevated relative to recent history, while relative valuations versus taxable fixed income markets have shifted over the period.

2025 REVIEW OF EQUITIES

The S&P 500 Index posted a total return of 17.9% in 2025, marking the third consecutive year of double-digit gains. The index remains highly concentrated compared to history, and a handful of the very large companies once again accounted for a disproportionate share of index returns. Just three stocks, Nvidia, Alphabet (Google) and Broadcom accounted for 36% of the total return of the S&P 500, and seven stocks accounted for 50% of the return. Based on our analysis of historical data from Bloomberg and Goldman Sachs, periods of elevated market concentration have, at times, coincided with broader economic slowdowns.

CONTRIBUTION TO 2025 S&P 500 TOTAL RETURN



Source: Bloomberg

Another notable feature of U.S. equity returns in 2025 was the outperformance of lower quality and high-volatility stocks over their counterparts. In fact, high beta (a measure of a stock's volatility relative to broader market swings) was the top performing factor within the Russell 3000 Index. Quality characteristics, including earnings stability, profitability, and balance-sheet strength, were out of favor in 2025 as investor preferences shifted toward more speculative exposures, despite their historical role in risk management across market cycles. Compared to history, this dynamic is an outlier, as over the last 20 years the highest-quality stocks (top quintile) have outperformed the equal-weight Russell 3000 by approximately 5.5% annually.

Sector performance in 2025 was driven by beneficiaries of the AI build-out. Communication Services led the market with a 34% return, followed by Information Technology at 24% and Industrials at 19%. The common thread across these leaders was robust growth and continued enthusiasm for the artificial intelligence build-out.

After a long period of underperformance, international stocks outpaced U.S. stocks in 2025, with the MSCI ACWI Ex-US Index gaining 32.4%. This outperformance was driven by currency movements and a relative valuation rebound. The U.S. dollar declined 9.4% against a basket of major currencies in 2025, materially boosting international returns for U.S.-based investors. In addition, international stocks began 2025 trading at an all-time valuation discount relative to the S&P 500 Index, which helped fuel a valuation bounce.

Our Outlook

We expect moderate real economic growth in 2026, as strong productivity gains compensate for continued slow labor growth. We believe evidence of AI efficiency gains may become clearer in 2026.

Given the slowdown in labor growth, the political dynamics of mid-term elections, and the impending change in Fed leadership, we expect a year defined by both fiscal and monetary stimulus. Our base case assumes that fiscal policy will be stimulative in 2026. Simultaneously, we believe a new Fed Chair will usher in a more dovish monetary regime, as the Trump Administration has made it clear it wants a nominee committed to aggressive rate cuts to support its pro-growth agenda.

We believe inflation is likely to moderate further in 2026, primarily driven by a decline in shelter inflation. However, we believe headline CPI will remain above the Fed's 2% target for the sixth consecutive year.

We expect the AI trade to broaden in 2026, shifting from a narrower focus on infrastructure beneficiaries toward software and services companies that are beginning to monetize these technologies.

In our opinion, investors appear to have strong conviction in a "run it hot" economic scenario, as cyclical sectors have outperformed defensive sectors significantly since April 2025. Cyclical sectors such as Industrials, Financials and Consumer Discretionary trade at premiums to their historical valuation averages. In contrast, defensive sectors such as Health Care and Consumer Staples trade at sizable relative valuation discounts.

We believe this leaves little margin for error in the outlook. In our opinion, any downward revisions to economic growth expectations or a shift to a less accommodative monetary policy stance could trigger a rotation into defensive investments. We are also monitoring the risk of excessive fiscal and monetary stimulus. In our view, this dual stimulus environment raises the risk of either

Our Outlook

a renewed acceleration in inflation or an increase in long-term interest rates due to concern about fiscal sustainability.

We continuously monitor economic, policy and valuation data and adjust portfolios as our outlook evolves. However, we will not deviate from our disciplined investment approach, which requires all investments to fit one of our investment strategies and trade at a discount to our estimate of fair value.

Portfolio positioning continues to reflect a cautious and quality-focused approach within fixed income allocations. Emphasis remains on higher-quality securities across sectors, consistent with an environment characterized by tighter credit spreads, elevated issuance, and ongoing uncertainty around monetary policy and economic conditions.

Curve exposure is managed selectively to reflect changes in fiscal conditions and differences in central bank policy paths, with diversification implemented as appropriate within each strategy's investment mandate. Maintaining sufficient portfolio liquidity through security selection and structure remains a priority, allowing portfolios to adjust as market conditions and policy expectations evolve.

Overall, current market conditions highlight the importance of disciplined portfolio management, diversification, and risk control. An active and measured approach remains central to portfolio management, with positioning adjusted as economic data, policy developments, and market dynamics change over time.

MACRO TEAM

QUESTIONS? LET'S CHAT

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