Seventy-Five Horses and Two Pieces of Plastic

JAN 2026

2026 MARKET PREVIEW LETTER FROM THE DIRECTOR OF RESEARCH

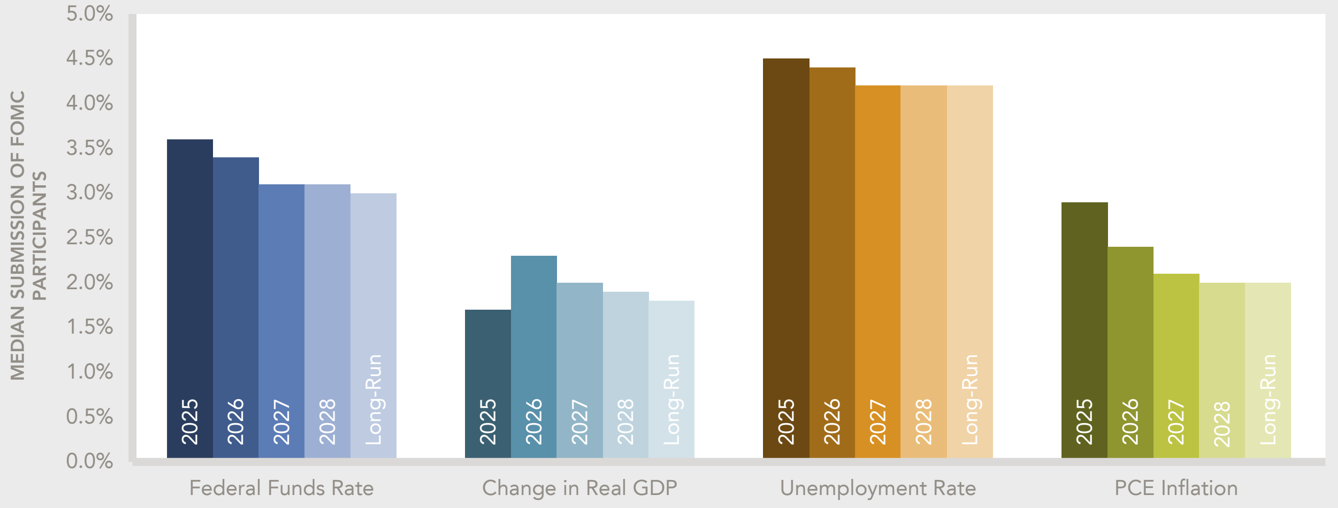
Anyone who has gone snowmobiling knows it can be simultaneously exhilarating and terrifying. Throttling across snow and through a forest powered by a 75-horsepower engine with two plastic skis to steer makes it hard to feel like one has complete control; 30 mph in the open air feels more like 100!

Nonetheless, operating a snowmobile is pretty straightforward: The throttle is a right-thumb button, the brake is a left-hand squeeze lever. Beyond those two controls, it's up to the driver to effectively navigate the trail, with the critical concession that the terrain is out of anyone's complete control. Which brings me to our 2026 market outlook.

The "throttles" for portfolios are the usual constituents: equities, below investment grade credit, and private markets. The "brakes" are investment grade fixed income, particularly Treasuries which can slow a portfolio's losses if the market tumbles. The terrain is naturally the actual path that each of these asset classes will follow in 2026. Since 2022 the equity market ride has been mostly exhilarating, save for some of the terrifying moments like the market dip after Liberation Day. But that's in the rearview mirror, and the focus is what is around the bend. Will the thrill continue, or should we ease up on the throttle?

If we think of the U.S. economy as the overall weather forecast, conditions look clear. Projections suggest a modest uptick in GDP growth, with small pullbacks in interest rates, unemployment, and inflation.

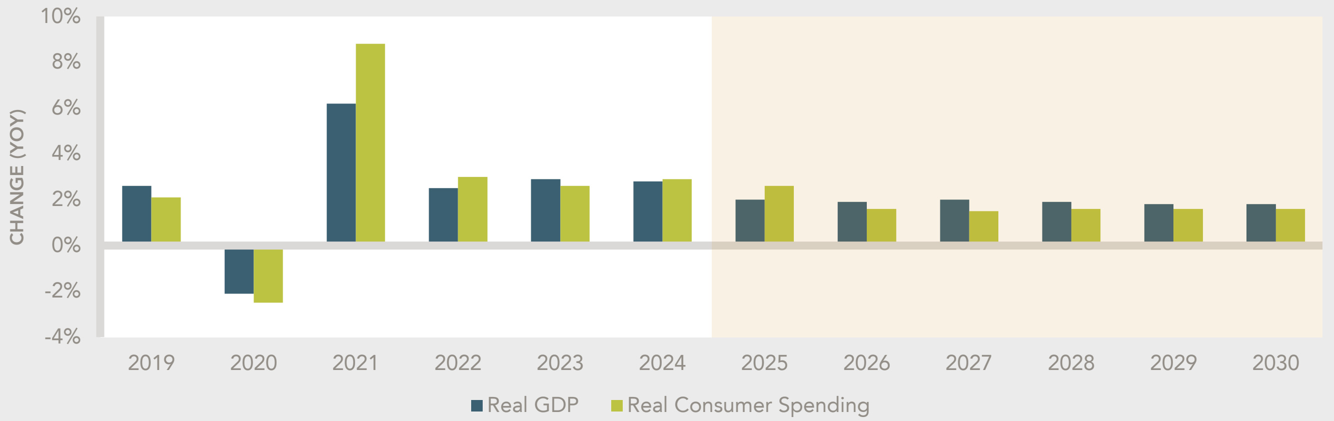
POSITIVE ECONOMIC OUTLOOK



Source: Federal Reserve as of December 10, 2025. Long-run projections are defined as representing each participant's assessment of the value to which each variable would be expected to converge, over time, under appropriate monetary policy and in the absence of further shocks to the economy. "Appropriate monetary policy" is defined as the future path of policy that each participant deems most likely to foster outcomes for economic activity and inflation that best satisfy his or her individual interpretation of the statutory mandate to promote maximum employment and price stability.

The most likely sources of snow squalls are labor market weakness and geopolitical disruptions, but the strength of the American consumer has proven resilient and there is no reason to doubt that trend continues.

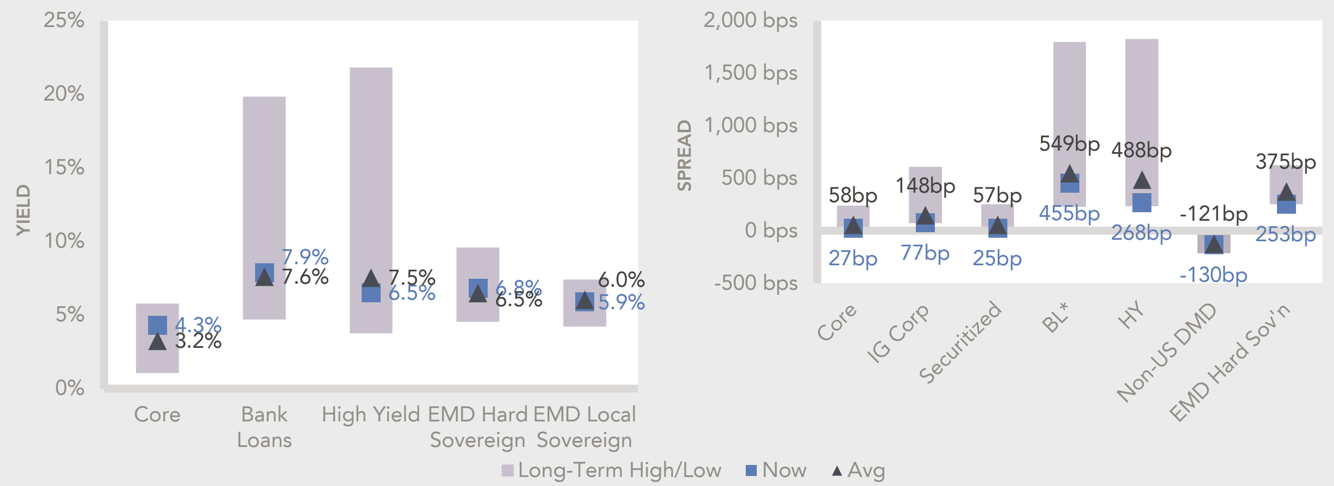
STRONG CONSUMER FUELS POSITIVE GROWTH



Source: Deloitte as of January 1, 2026. Shading indicates forecasts.

Looking at asset classes, the easiest part of the ride should again be the fixed income trail: The path appears smooth and predictable. Yields are still attractive on an absolute basis — albeit it down moderately from a year ago — and income is expected carry the asset class in 2026. Spreads are tight which implies that valuations are rich but risk is low, which should translate to minimal stress for the asset class.

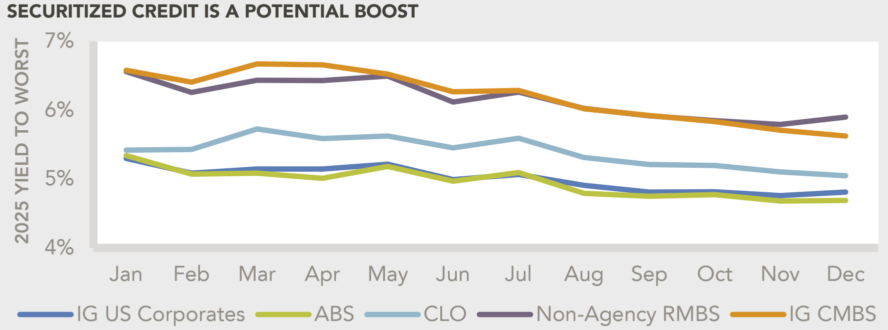
YIELDS ARE HIGH AND SPREADS ARE TIGHT



Source: Bloomberg, Credit Suisse, JPMorgan as of December 31, 2025. Long-term high, low, and average based on longest available data for each index. *BL spread over LIBOR, not over Treasuries.

If investors are looking to go off trail for some more adrenaline on their rides, securitized credit sectors present a yield premium relative to similarly rated corporate credit — more "throttle" for bond portfolios.

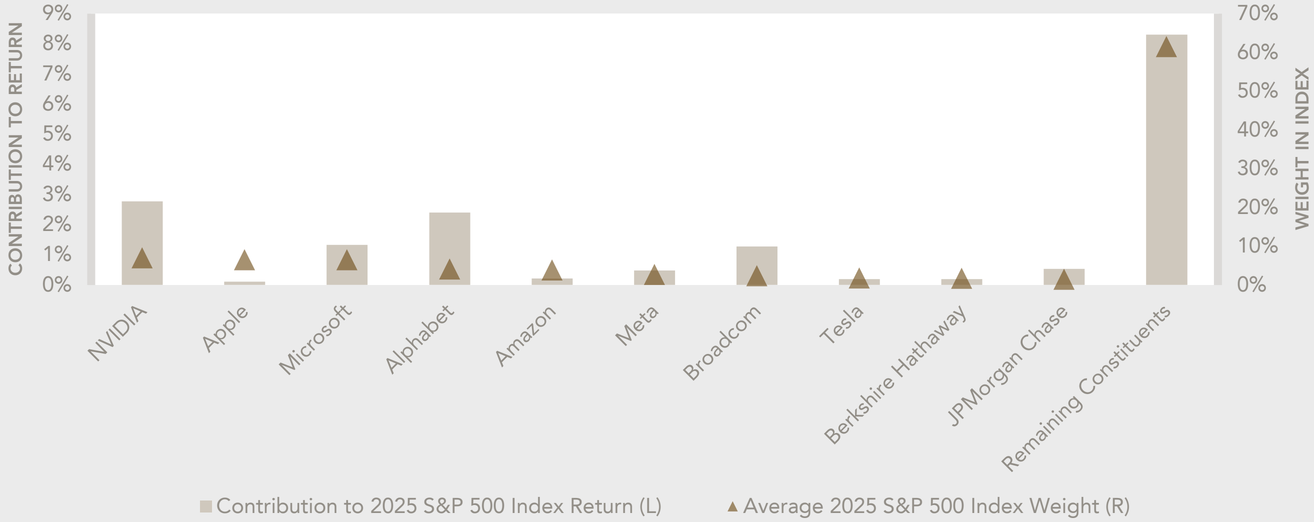
SECURITIZED CREDIT IS A POTENTIAL BOOST



Source: Bloomberg, J.P. Morgan as of December 31, 2025; IG CMBS YTW is an average of the J.P. Morgan IG Conduit , SASB Fixed, and SASB Floating Indices

For U.S. equities, the trail has been narrow, steep, and well-traveled. The Magnificent 7 have fueled spectacular returns while creating unprecedented concentration risk in the bellwether S&P 500 index.

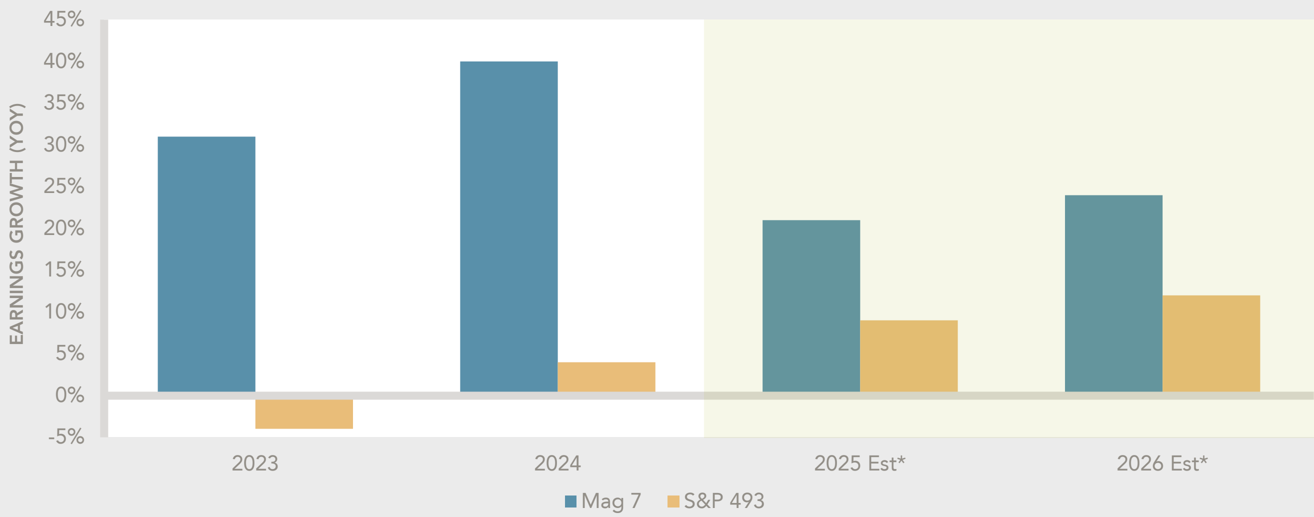
NARROW AND STEEP LEADERSHIP



Source: FactSet as of December 31, 2025

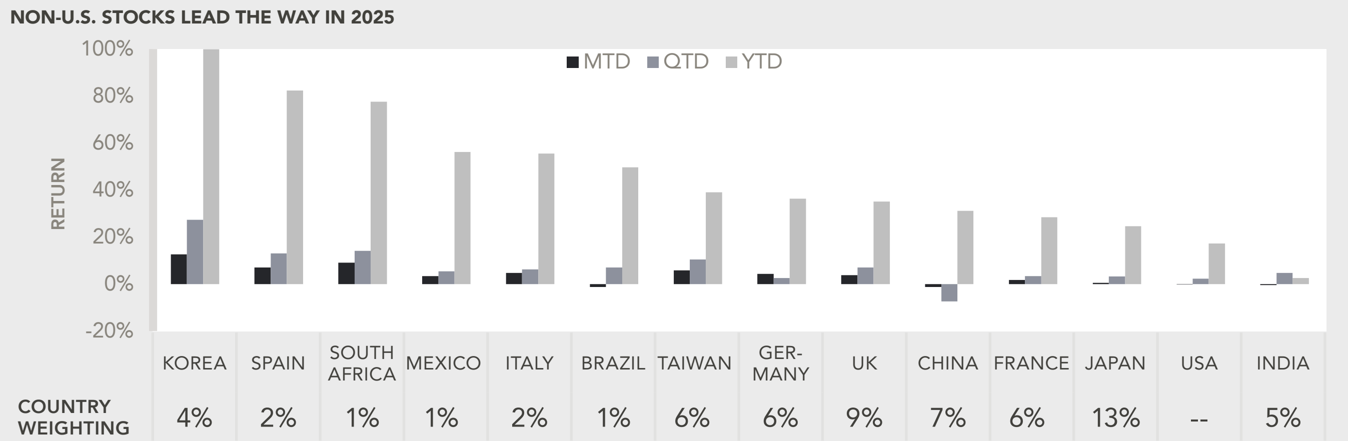
Going forward, more varied terrain in terms of market leadership will help support further gains and while mega caps are likely to remain strong, broader earnings growth could help fuel rallies in small caps and under-owned large caps.

EARNINGS ESTIMATES FAVOR MARKET BROADENING



Source: FactSet as of December 31, 2025. Shading indicates forecasts.

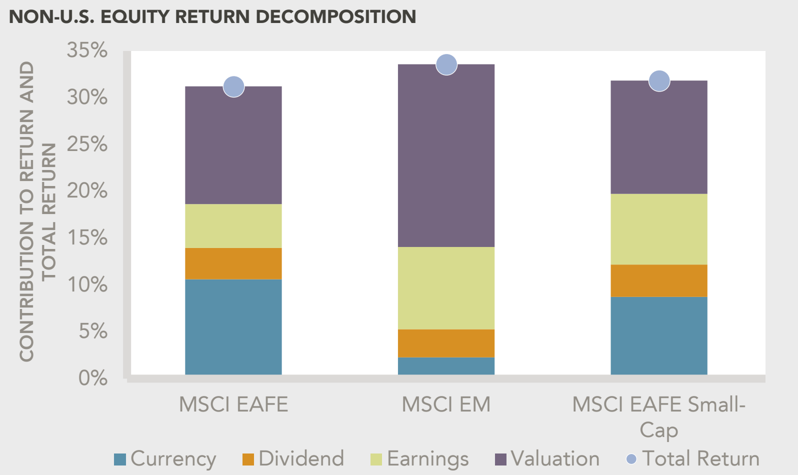
Sometimes the conditions will look perfect for a thrilling ride but an unexpected headwind turns a promising tour into disappointment. Until last year, that had been the story for non-U.S. equities: Past years weren't negative, but were also not as strong as underlying metrics suggested they could be. That all changed in 2025 as non-U.S. equity markets led the way, with all major countries except India outperforming the U.S.



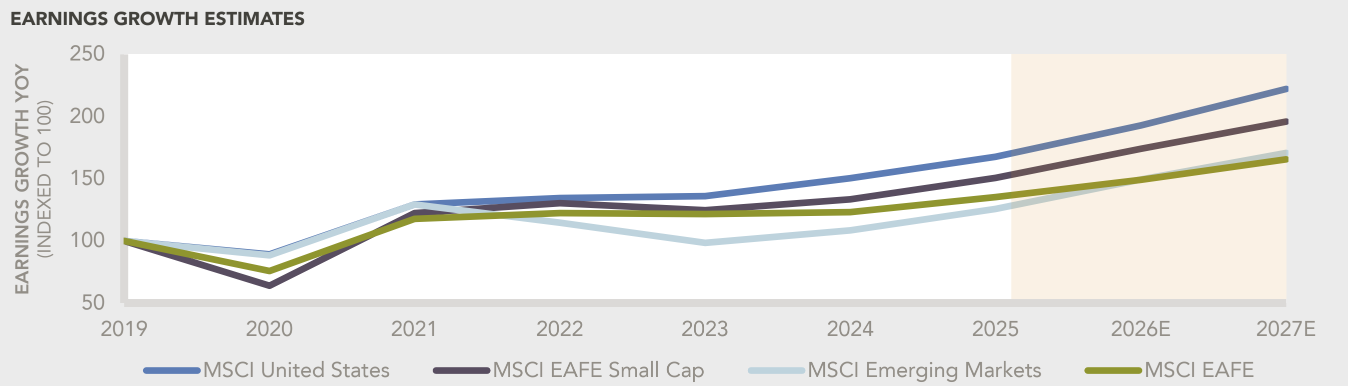
Source: Bloomberg as of December 31, 2025. Returns based on individual MSCI country indices; country weights based on the MSCI ACWI ex-U.S. Index.

However, investors should be aware of the ice underneath these return figures: Most of these returns were driven by currency (via a weaker dollar) and multiple expansion ("valuation" in the chart at right). Neither of these sources are long-term support mechanisms for equities and companies will have to deliver on return expectations for non-U.S. return momentum to continue.

The good news is that earnings projections across markets — both U.S. and non-U.S. — are expected to increase in 2026 and 2027. Deviations from these expectations will create headwinds for returns.



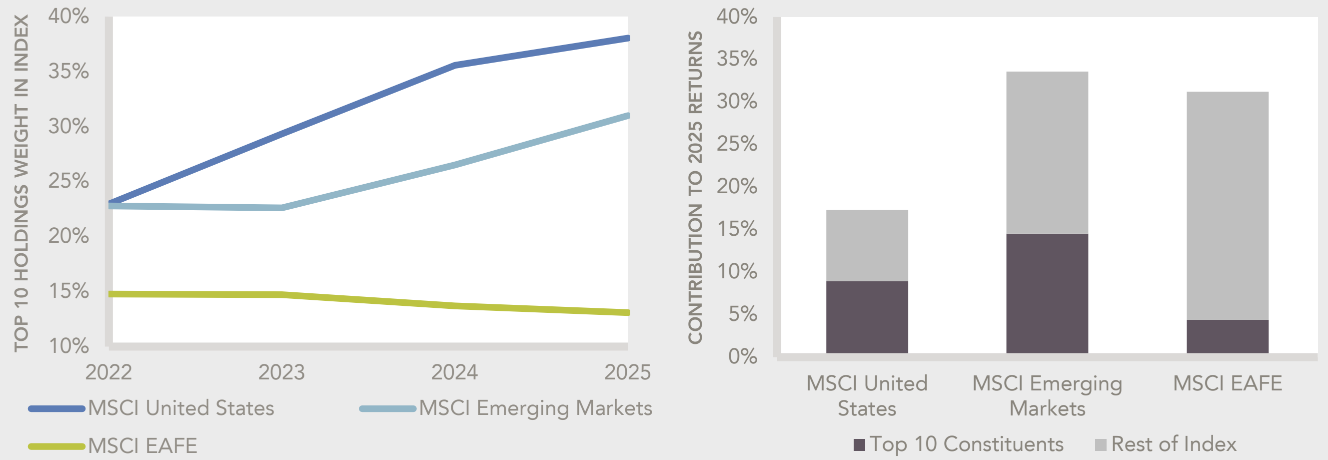
Source: Bloomberg as of December 31, 2025



Source: FactSet; estimates as of January 5, 2025. December 2019 = 100. Shading indicates forecasts.

It should also be noted that the path for emerging market equities is now similarly narrow like U.S. indices, largely on the back of AI-related stocks in Taiwan, South Korea, and China. While not quite at the level of U.S. indices, concentration and return contribution within the emerging market index is notably top-heavy. A pullback in AI-related stocks would likely be dilutive for both markets.

MARKET CONCENTRATION RISES FOR EMERGING MARKETS

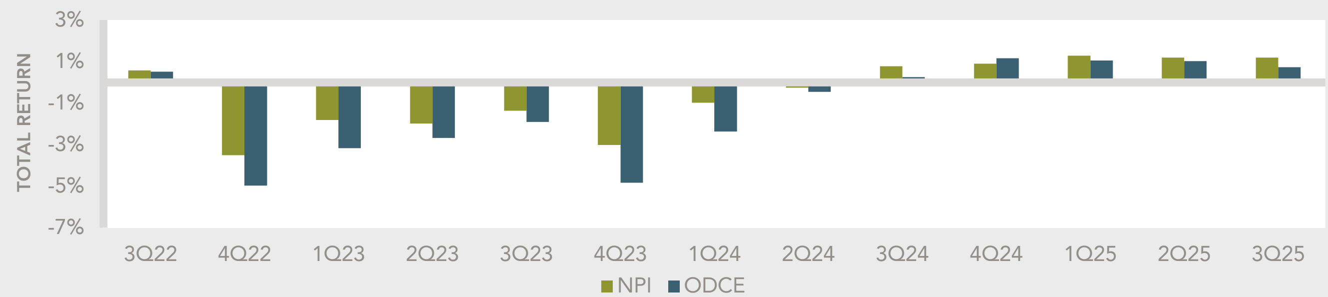


Source: FactSet as of December 31, 2025. Top 10 Holdings calculated as of December 31 of each calendar year.

On the other hand, the large-cap developed markets index ("MSCI EAFE" in the chart above) is not as exposed to AI stocks and thus offers more diversified returns.

As we think about the alternatives landscape, the terrain looks promising. Real estate appears to have bottomed and while not back to pre-pandemic levels, the current cycle is showing signs of stability, with returns driven almost exclusively by income.

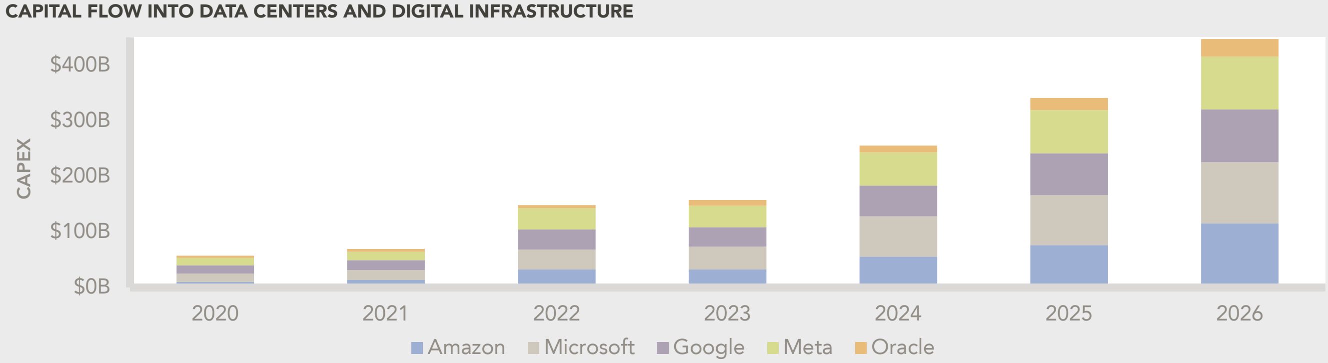
REAL ESTATE RETURNS STABILIZE



Source: NCREIF as of September 30, 2025

Infrastructure is also a beneficiary of the AI movement as investments flow into data centers and overall digital transformations, with a majority of the spending coming from Magnificent 7 companies. Long term, this is further support for the asset class and return potential.

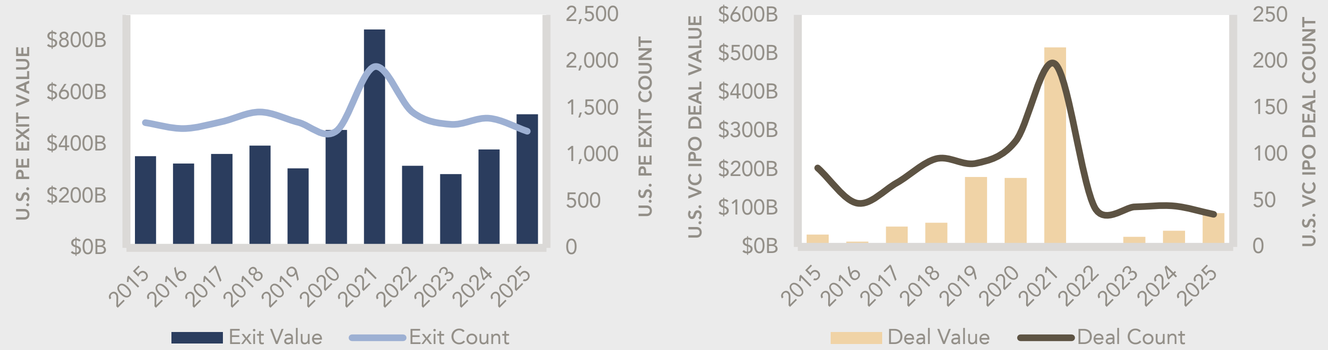
CAPITAL FLOW INTO DATA CENTERS AND DIGITAL INFRASTRUCTURE



Source: Green Street, McKinsey & Company, Voya, Principal Real Estate as of September 30, 2025. Shading indicates forecasts.

The last leg of the trail covers private markets. Private equity looks to have a few less obstacles than previous years with exits improving and the IPO market starting to re-open. Valuations are still stubbornly high but better liquidity should open up the trail for better cruising.

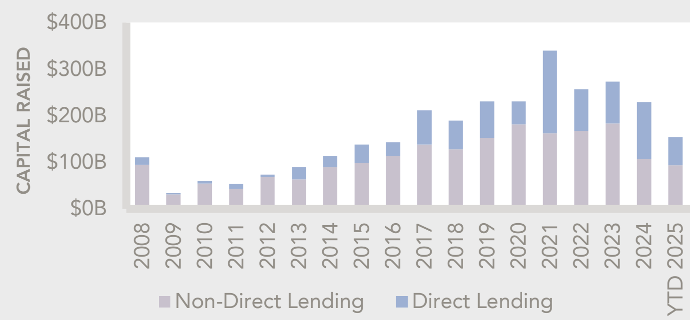
IMPROVEMENTS TO LIQUIDITY AND IPOS



Source: PitchBook U.S. PE Breakdown and PitchBook U.S. Venture Capital Outlook as of September 30, 2025

Private credit also appears to add a more diversified terrain in the coming years as investors are increasingly diversifying into other market segments, particularly asset-based lending. And while we wouldn't label this an "experts-only" trail, investors are highly encouraged to vigorously review the space and potential managers before making an allocation. There is notable upside, but it is critical to understand the surroundings before plowing in.

DIRECT LENDING STILL LEADS, BUT INVESTOR ARE DIVERSIFYING

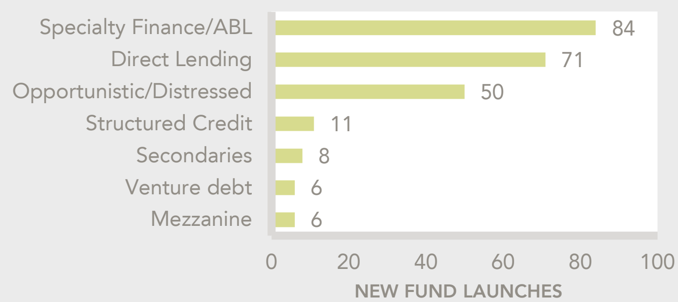


Source: Pitchbook LCD as of September 30, 2025. Reflects estimated U.S. volumes and deal counts for reported deals.

Have fun out there, but don't drift far from the trail

Overall, portfolios should enjoy a favorable ride in 2026, barring any massive changes to trail conditions. Investors shouldn't feel compelled to pull back on the throttle, but asset classes may not run as quickly as they did in 2025. A commitment to diversification and rebalancing are the best guides for a successful program and no matter how thrilling or terrifying the ride may be, investors should be mindful of obstacles and operate responsibly.

ASSET-BASED LENDING LEADS THE WAY IN 2025



Source: With Intelligence. 2025 funds in development by strategy as of September 30, 2025

Until next time,

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