



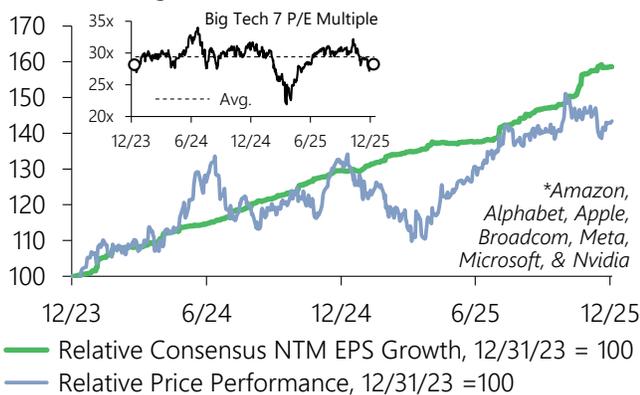
Key Points

- U.S. Growth Should Strengthen by Mid-2026 Following Resilient 2025
- Euro Area Growth Back to Trend, but China a Growing Threat to Exports
- China's Growth Remains Reliant on Exports as Domestic Demand Weakens
- New Federal Reserve Chair and Rate Path to Drive Bond Markets in 2026
- Income Likely to Be the Primary Driver of U.S. Municipal Bond Returns
- Broadening of Equity Market to Continue, but Do Not Dismiss Technology

Broadening Earnings Growth Beyond AI Supports Market, Though Valuations May Cap Upside

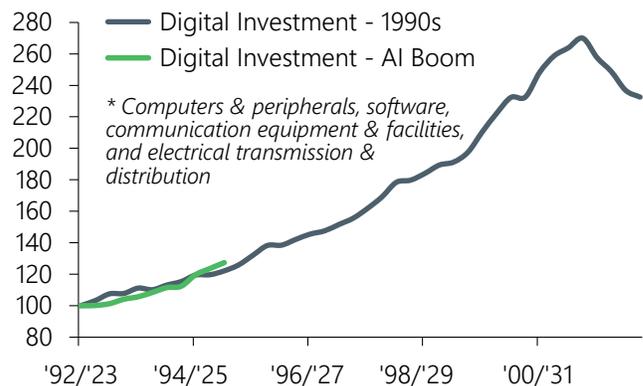
1 EPS Growth Driving Tech Outperformance

Big Tech 7* vs. Other 493 S&P 500 Stocks
Relative Earnings Growth and Stock Performance



2 Artificial Intelligence Still in Early Innings

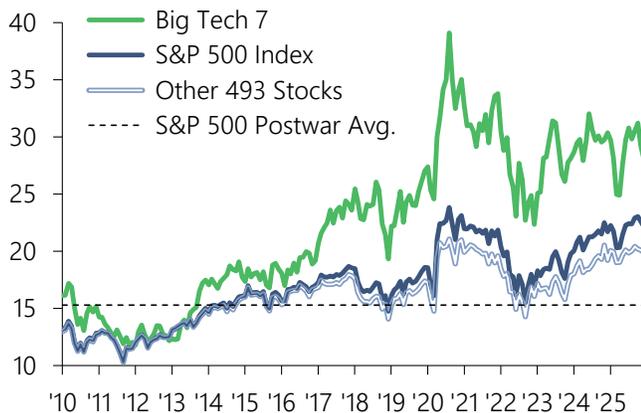
U.S. Digital Investment* Booms
Indexed, 1Q92 = 100, 1Q23 = 100



* Computers & peripherals, software, communication equipment & facilities, and electrical transmission & distribution

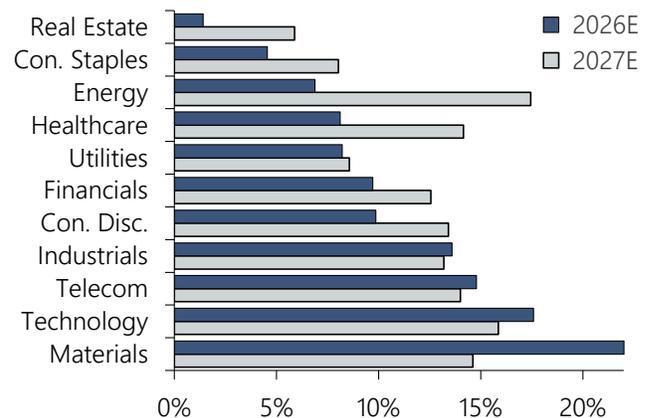
3 Onus on EPS Growth to Drive Stock Returns

S&P 500 Index Forward Price-to-Earnings Multiple



4 EPS Growth Broadening to Other Sectors

S&P 500 Equal Weight Index Consensus Earnings Growth



Sources: FactSet, Oxford Economics, 12/31/25

2026 Equity Investment Outlook and Strategy

We are generally optimistic about the outlook for stocks and, more so, stock picking in 2026. Tax cuts and other pro-growth policies, particularly those that incentivize domestic investment and lower regulatory burdens, are set to fuel the next leg of economic expansion. Even so, economic growth remains bifurcated, and much hinges on the promise of artificial intelligence (AI). Forty-two AI-linked stocks account for over 45 percent of the S&P 500 Index, leaving it highly exposed to one investment theme and the related headline risk. In short, following three years of stellar gains, market returns are likely to drift back toward their long-term mean, given elevated valuations and already optimistic earnings estimates.

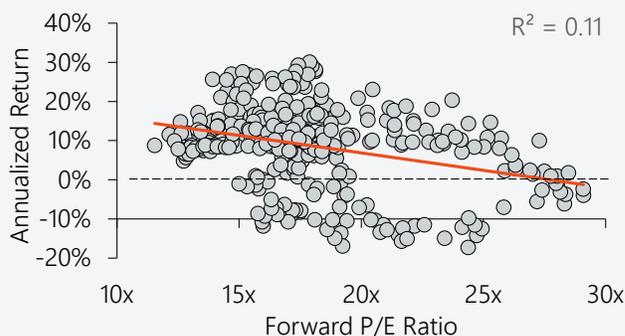
The S&P 500 Index has delivered double-digit gains for three calendar years in a row, resulting in a cumulative total return of 86.1 percent through year-end 2025, or 23.0 percent annualized. However, just seven megacap tech stocks, six of which are linked to AI, accounted for over half of its trailing three-year return. In contrast to the market-cap-weighted headline index, the S&P 500 Equal-Weight Index posted a cumulative total return of 43.4 percent, or 12.8 percent annualized, for the same period. There have only been five other instances since 1928 in which the S&P 500 Index was up double digits for three or more sequential years. Price returns in the fourth year range from -19.4 percent to 30.7 percent.

The far superior earnings growth of the seven megacap tech companies cited above—Alphabet, Amazon, Apple, Broadcom, Meta, Microsoft, and Nvidia—relative to the other 493 companies in the S&P 500 Index, and their considerable combined index cap-weighting (about 35 percent currently), accounts for most of the return gap since the end of 2022. The aggregate forward price-to-earnings ratio for the seven megacap tech stocks ended 2025 nearly unchanged from the end of 2023 and held steady for the other 493 stocks in 2025. However, the S&P 500 Index's year-end 2025 valuation ratio of 22.1 times remains well above its postwar average of 15.3 times, leaving it vulnerable to earnings misses, shifts in investor sentiment, and other factors.

There has historically been a strong inverse relationship between the S&P 500 Index's forward price-to-earnings ratio and its subsequent 10-year annualized return. In other words, high market valuations often lead to lower equity returns over a longer period, as earnings growth and valuations revert to their mean, or briefly below, in the event of a recession or bear market. However, the relationship between valuation and short-term returns is low. The R-squared, the percentage of total variation in returns explained by valuation at the beginning of a period, is 0.77 (out of a possible range of 0 to 1) over the following ten years. It is only 0.11 over three years and 0.26 over five years, indicating a weak relationship.

Valuation Not Predictive of Short-Term Returns

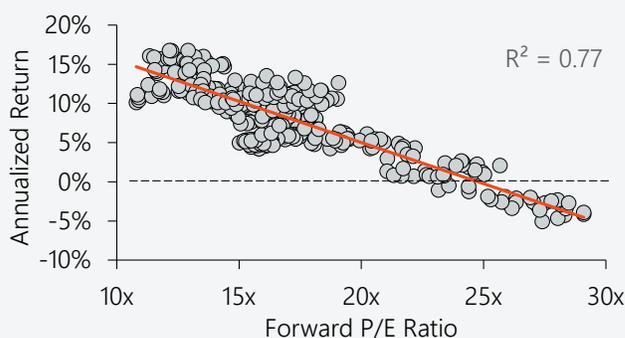
S&P 500 Index Forward P/E Multiple vs. Subsequent 3-Year Annualized Return



Source: FactSet, 12/31/25

But Has Been Over Longer Periods Historically

S&P 500 Index Forward P/E Multiple vs. Subsequent 10-Year Annualized Return



Source: FactSet, 12/31/25

As Federal Reserve Chair Greenspan did with his now-famous “irrational exuberance” speech in 1996, central bankers are warning about the risks posed by elevated valuations, especially for the top AI stocks, and about a correction that may undermine global financial stability and GDP growth if AI fails to meet optimistic forecasts. This time, it is the Bank of England and the European Central Bank raising red flags, not the Federal Reserve. Oxford Economics, which places the odds of an AI bust in 2026 at just 15 percent, estimates that global stocks would plunge by about 22 percent, global exports would fall by 4 percent as lower U.S. demand for tech imports transmits the shock globally, and world GDP would be at least 1.5 percent below its baseline forecast by 2027.

The Nasdaq Composite Index rallied nearly fourfold in the three years, three months, and five days following Greenspan's 1996 speech, as earnings projections and valuation ratios climbed ever higher into the heights of dot-com mania. As was the case then, concerns might be premature. Current equity valuations are well below the peaks of the dot-com bubble and may be justified if AI-led margin expansion drives faster earnings growth. Greater AI spending/adoption, stronger GDP growth,

and easier financial conditions all could push valuations even higher. Significantly, the composition of the S&P 500 Index has changed considerably over the decades. It is appreciably more weighted toward asset-light, less cyclical sectors with greater margins, earnings stability, and capital returns, thus warranting a higher valuation.

Record Operating Margin Supports Valuation

S&P 500 Index Operating Margin

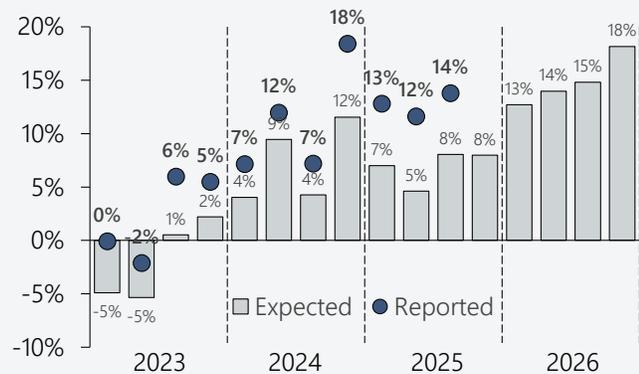


Source: S&P Global, 12/31/25

Concerns are also not meritless. Unlike in the last three years, sell-side analysts have set a high bar for growth in 2026 and 2027, lifting the risk of disappointments. Bottom-up estimates for S&P 500 constituents indicate aggregate earnings growth of 14.9 percent in 2026 and 15.0 percent in 2027. Earnings estimates for the seven megacap tech firms imply growth will decelerate from very high rates, while steadily accelerating for the other 493 companies to 13.3 percent by 2027, up from 4.8 percent in 2024, supporting equity market broadening. Tailwinds that suggest estimates are achievable include fiscal stimulus, the lagged impact of lower short-term rates, loosening lending standards, and lower oil prices.

Bar Set Much Higher for Earnings Growth in '26

S&P 500 Bottom-Up Earnings, Y/Y Percent



Source: FactSet, 12/31/25

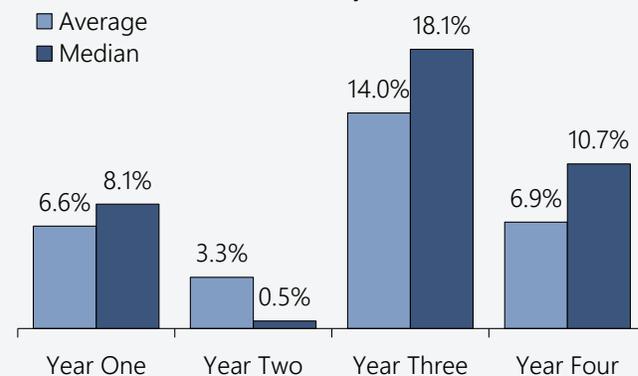
The outlook for stocks also rests, to some extent, on the path of interest rates. Fed funds futures are discounting about two 25-basis-point cuts by year-end. The Federal

Reserve might push the fed funds rate even lower under the new Chair, come May. The financial markets would welcome the move, provided inflation is well controlled and productivity is rising. Otherwise, it risks investors driving up longer-dated yields due to fears that overly loose monetary policy will overheat the U.S. economy and reignite inflation. Instead of rate cuts, the market's focus would pivot to hikes, which would depress asset valuations. The Federal Reserve must strike a delicate balance, which may be easier said than done.

There is one other matter, more of a phenomenon, that the U.S. equity market faces in 2026, though favorable economic forces may offset it. The S&P 500 Index has historically posted its weakest gains in the second year of a presidential cycle. Since 1929, the S&P 500 Index has generated a median price return of 8.1 percent in the first year after a presidential election, 0.5 percent in the second, 18.1 percent in the third, and 10.7 percent in the fourth. With their Congressional majority at risk, GOP lawmakers might cave if President Trump insists that the government distribute "tariff dividend" checks before the midterms. Here, too, they must be careful not to overheat the economy, given limited slack, or worsen the fiscal situation, or risk the wrath of bond investors.

Muted Returns in 2nd Year of Presidential Cycle

S&P 500 Index Price Returns, by Presidential Year



Source: FactSet, 12/31/25

The U.S. economy is set to start 2026 on a solid note, as tax refunds boost consumer spending and the effects of the federal government shutdown reverse. For their part, investors are bullish: 76 percent of respondents to a recent Evercore ISI survey expect the next 10 percent move in the S&P 500 Index to be up. Active managers are also close to fully invested, according to the NAIM Exposure Index. However, it also suggests a potential shortage of incremental purchasing capacity. On the retail side, flows into global equity mutual funds and ETFs surged by \$132.6 billion over the last four weeks, with almost \$50 billion flowing into U.S. equity funds. Nearly all sector fund groupings had positive inflows, consistent with expectations for market broadening.

With few to no compelling valuation dislocations across sectors, disciplined stock picking, rather than big sector bets, will be the primary driver of performance in 2026. We also expect market volatility to rise from historically low levels, as elevated valuations leave stocks especially vulnerable to uncertainties and headline risks. Even so, we expect U.S. market leadership to broaden beyond AI infrastructure stocks, a trend that commenced in 2025 and has further room to run. A supportive backdrop—characterized by OBBBA fiscal stimulus, lower interest rates, deregulation, and mounting AI adoption—should drive healthy earnings growth across multiple sectors. Consistent with this view, our favored sectors into 2026 are financials, industrials, healthcare, and technology.

Notwithstanding strong performance in 2025, the risk-reward for financials remains attractive. Deregulation, which impacts both capital requirements and operating costs, is anticipated to bolster earnings growth in 2026. With loan growth steady and credit costs manageable, commercial banks have been resilient, and a steepening yield curve should lift net interest margins. Investment banks are benefiting from a long-awaited recovery in capital markets activity, including equity issuance, debt financing, and mergers and acquisitions.

Bank Stocks Cheap Despite Recent Strength

State Street SPDR S&P Bank ETF NTM P/E
Relative to S&P 500 Equal-Weight Index



Source: FactSet, 12/31/25

Strength in the industrials sector has been concentrated in data centers, energy infrastructure, and aerospace, but we anticipate that it will broaden to other segments, including automation, industrial machinery, electrical equipment, and even the downtrodden housing market. Furthermore, the acceleration in the reshoring of U.S. manufacturing should be a significant tailwind for E&C and transportation companies.

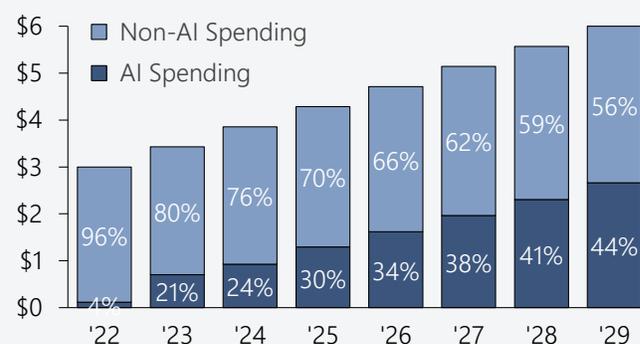
In healthcare, a sector fairly insulated from economic cycles and bolstered by strong demographics, we focus on innovative firms. Greater clarity on drug pricing has improved the outlook for the pharmaceutical industry. However, we continue to prefer investments in faster-growing medical devices, healthcare services, and bio-

technology companies. While investors have ignored the sector's typically defensive, low-beta attributes in a risk-on market, its stability may become increasingly valuable should volatility return.

In technology, investor concerns about a potential AI bubble persist despite robust investment. Significantly, the technology sector's long-term fundamentals extend well beyond AI, supported by enduring secular drivers such as digital transformation, cloud adoption, data analytics, and cybersecurity. While elevated valuations and earnings expectations insinuate that the period of outsized relative outperformance may moderate, these durable growth themes continue to justify a meaningful allocation to the sector.

Led by AI, Tech Spending Growing Broadly

IT Spending, AI vs Non-AI
\$ Trillion



Source: Evercore ISI, 1/9/26

Beyond sector-centric dynamics, we expect the market-broadening theme to extend across investment styles. After a significant period of underperformance, small-cap stocks regained momentum in the second half of 2025, a trend we expect will continue. Small-cap firms' greater interest rate and economic sensitivity align with improving growth and lower rates, with growing M&A activity providing an additional catalyst. Similarly, we expect many international markets to perform well in 2026, bolstered by attractive relative valuations, easier monetary policy, and greater clarity on the outcome of U.S. tariffs. While the weaker dollar lifted local market returns, the tailwind will likely diminish in 2026.

The next several years could be a period of remarkable economic and social transformation, as AI spurs higher productivity, lifts corporate margins and wage growth, inspires new business ventures, and rejiggers the labor force. But we are also mindful that the stock market has delivered exceptional returns over the past three years. An elevated valuation raises its sensitivity to negative surprises and could test the durability of "buy-the-dip." We believe portfolios built on diversification, quality, sustainable earnings growth, and valuation discipline are best positioned to navigate the years ahead.



Global Macro Developments

U.S. Growth Should Strengthen by Mid-2026 Following Resilient 2025

The U.S. economy in 2025 was marked by bifurcated strength that masked underlying fragility. A capital investment boom in artificial intelligence (AI) and a spending splurge by well-heeled households trumped downside forces, from a trade policy upheaval to a softening job market, to help keep the economy upright. The complete story is more nuanced, but it is one of overall resilience. Real GDP grew at an average pace of 2.5 percent over the first three quarters of 2025, in line with its 30-year trend. For the fourth quarter, the Congressional Budget Office estimates that the 43-day federal government shutdown, the longest in U.S. history, was a 1.5 percentage point drag on annualized GDP growth. Still, it expects most negative effects to reverse, resulting in a 2.2-percentage-point boost to first-quarter 2026 GDP growth. The reversal, along with the stimulative effects of the One Big Beautiful Bill Act (OBBBA) and looser financial conditions, should support continued solid real GDP growth in 2026. We expect growth to strengthen by mid-year 2026, with potential upside from any additional stimulus measures.

Bifurcated U.S. Consumer Spending Poised to Become Less So in Year Ahead

Real consumer spending growth steadily improved on a quarter-over-quarter, annualized basis through the third quarter of 2025, after a weak first quarter. Even so, the growth rate decelerated year over year throughout 2025, slowing to 2.6 percent in the third quarter from a recent peak of 3.4 percent in the fourth quarter of 2024, as consumers reduced purchases of goods, especially those affected by tariffs. We estimate that spending growth slowed to 1.9 percent in the fourth quarter, bringing the 2025 growth rate to 2.6 percent, down modestly from 2.9 percent in 2024. A reduced drag from tariffs and the OBBBA's tax cuts should contribute to another year of solid real spending growth, provided the job market regains its footing. Rubinson Research projects that the OBBBA's net effect will boost consumer spending by 60 basis points in 2026, with the benefits front-loaded and accruing particularly to middle-income households (Exhibit 1). The much-needed relief may reduce bifurcation, especially as gains in real estate and financial assets moderate, potentially dampening the wealth effect for higher-income households (Exhibit 2).

Favorable U.S. Economic Outlook Contingent on Job Market Stabilizing

The U.S. economic outlook hinges on the promise of AI and also on the job market stabilizing. Nonfarm payroll growth slowed to an average pace of only 14,500 new jobs in the second half of 2025, well below the estimated 50,000-75,000 per month needed to keep the unemployment rate firm. As with many other aspects of the current economic expansion, job growth has been highly bifurcated. Based on ADP data, firms with 500+ employees are driving job growth, while smaller firms began to shed jobs following "Liberation Day" (Exhibit 3). It is a theme playing out across the economy: those with the means to invest and counter the adverse impact of tariffs are doing well, while those without are struggling. Bifurcation is also evident across industries.

Exhibit 1: OBBBA's Effect on U.S. PCE Growth

Item (\$ Billion)	1Q26	2Q26	3Q26	4Q26	2026	2027
Tax Cuts	69.3	53.2	37.1	42.3	201.9	(32.9)
SNAP Benefits	(2.0)	(2.0)	(2.0)	(3.3)	(9.2)	(3.8)
Medicaid	0.0	0.0	0.0	(8.8)	(8.8)	(35.4)
ACA	(6.0)	(6.0)	(6.0)	(6.0)	(24.0)	0.0
Student Debt Adj.	(3.6)	(3.6)	(3.6)	(3.6)	(14.3)	0.0
Lost EV Credit	(3.5)	(3.5)	(3.5)	(3.5)	(14.0)	0.0
Total	54.3	38.2	22.0	17.1	131.6	(72.1)
Estimated PCE Growth Effect (Percentage Points)						
Bottom 20%	(0.1)	(0.3)	(0.5)	(1.9)	(0.7)	(1.4)
20-40%	1.1	0.7	0.3	0.1	0.6	(0.6)
40-80%	1.5	1.1	0.7	0.8	1.0	(0.2)
Top 20%	0.9	0.7	0.4	0.5	0.6	(0.1)
Total	1.1	0.7	0.4	0.3	0.6	(0.3)

Source: Rubinson Research, 12/29/25

Exhibit 2: U.S. Consumer Health Index

By Annual Household Income
Five-Day Moving Average



Source: Morning Consult, 1/8/26



While jobless growth is possible, the economy is unlikely to withstand the weight of meaningful job losses. The spike in policy uncertainty in 2025 hindered businesses' ability to plan ahead. Lower policy uncertainty, OBBBA incentives, and easier financing conditions should create a more favorable environment for hiring and investment (outside of AI) in the year ahead.

Fixed Investment in AI Will Stay Strong and Likely Broaden to Other Segments

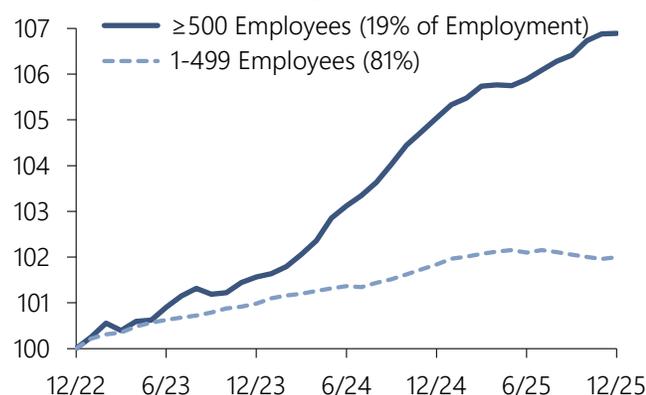
The AI boom fueled an average annualized growth rate of 25.8 percent (or 18.5 percent year to date) in fixed investment in computers, peripheral equipment, and software over the first three quarters of 2025, contributing meaningfully to GDP growth (Exhibit 4). However, as much of the AI equipment comes from overseas, its "real" impact on GDP is muted by higher imports. Excluding technology, nonresidential fixed investment declined at an average quarterly pace of 0.4 percent in 2025. While overall growth rates may slow due to base effects, AI will remain a powerful driver of fixed investment. Consensus estimates for the top four hyperscalers' capital spending have consistently missed the mark, with 2025 projections up nearly 50 percent since year-end 2024 (Exhibit 5). Consensus estimates project that capital spending by the top four will increase by 21 percent in 2026 and 15 percent in 2027. U.S. manufacturing reshoring, increased foreign investment, and supportive fiscal and monetary policies should also lead to incremental strength in non-AI segments of nonresidential and residential fixed investment.

Deregulation Could Revive Animal Spirits and Unlock Economic Growth Potential

It is difficult to draw a straight line between deregulation and its influence on the economy and corporate earnings growth. Still, complying with ever-increasing regulations is costly and time-consuming. Not to mention its adverse impact on competitiveness. As shown in Exhibit 6, the

Exhibit 3: U.S. Private Employment (ADP)

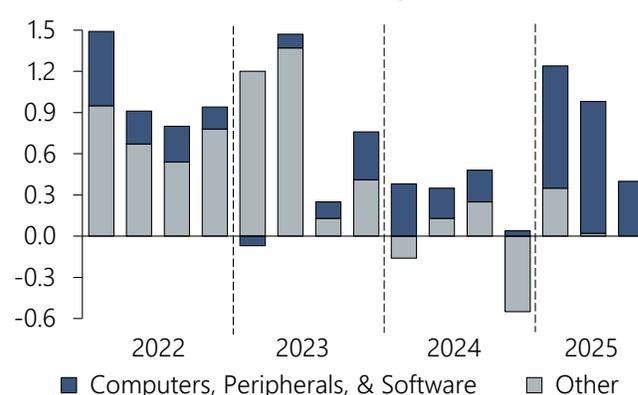
Indexed, 12/31/22 = 100, by Company Size



Source: ADP Research, 12/7/25

Exhibit 4: U.S. Nonresidential Fixed Investment

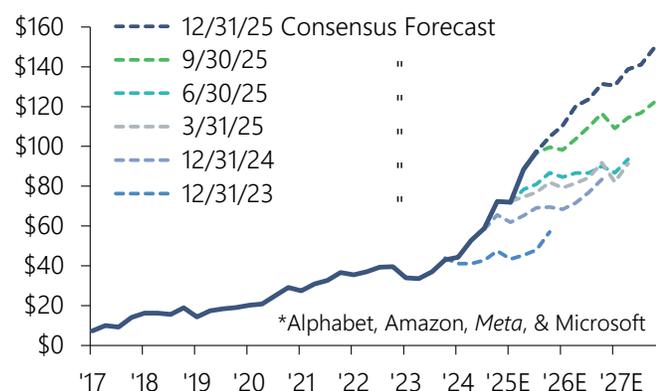
Contribution to Q/Q Percent Change in Real GDP



Source: Bureau of Economic Analysis, 12/23/25

Exhibit 5: Top Four Hyperscalers' Total Capex*

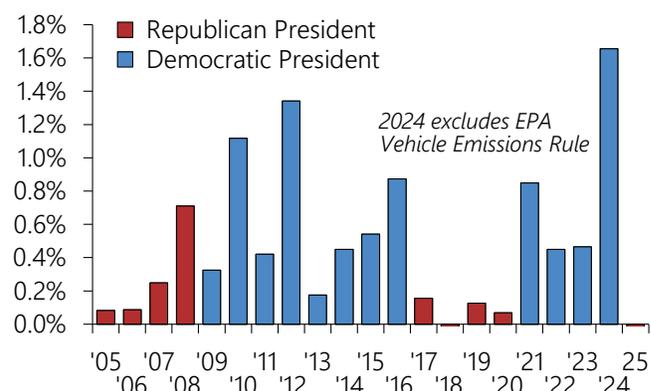
Quarterly, \$ Billion



Source: FactSet, 12/31/25

Exhibit 6: Total Cost of U.S. Regulations

Percent of Nominal GDP



Source: American Action Forum, Bureau of Economic Analysis, 12/31/25



American Action Forum estimates that regulatory costs have averaged 0.46 percent of nominal GDP over the last 20 years. Although Republican administrations have generally done a better job of containment, the number of economically significant final rules has steadily increased for decades. The Trump administration's deregulatory efforts in the financial sector, in particular, should positively impact economic growth. A proposal to reduce bank capital requirements for large banks will unlock \$2.6 trillion in additional lending capacity and bolster M&A. In addition, lowering manufacturing regulatory costs, which have steadily ballooned to 5.3 percent of sales, could revive animal spirits and support the administration's reshoring efforts.

Euro Area GDP Growth Back to Trend, but China a Growing Threat to Exports

The front-loading of Irish pharmaceutical exports ahead of looming U.S. tariffs helped drive an acceleration in Euro Area real GDP growth in 2025, which we estimate rose to 1.4 percent from 0.8 percent in 2024. Without Ireland, the Euro Area grew by about 1.0 percent in 2025. Rising defense spending, German fiscal stimulus, and real income gains will bolster economic growth in 2026. While it signaled that it will keep rates steady despite projecting that headline inflation will undershoot its 2.0 percent target, the European Central Bank also has room to ease further. Yet, China's renewed emphasis on export-led growth and ascent up the production value chain is a growing threat. Since 2018, China's share gains in global export volume have mirrored the Euro Area's losses (Exhibit 7). Assuming the trend continues, Goldman Sachs estimates that greater competition from China will reduce Euro Area GDP by around 0.5 percent by year-end 2029. The lagged effects from prior interest rate cuts, a modestly positive fiscal impulse, and a gradual recovery in investment should underpin real GDP growth of about 1.5 percent in 2026.

Japan Navigating Crosscurrents in Fiscal and Monetary Policy

Japan's real GDP is on track to expand by 1.2 percent in calendar 2025, a respectable outcome given tariff uncertainties, persistent inflationary headwinds, and an abrupt political leadership change. We anticipate modest, albeit fragile, real GDP growth of 0.5–1.0 percent in 2026 as a tight labor market supports wage gains, government measures temper inflation, and corporate investment remains supportive. Growing friction between the Bank of Japan's (BoJ) monetary policy normalization, the new administration's expansionary fiscal priorities, and high public debt levels may test our outlook. Financial markets increasingly reflect these tensions through increasing bond yields and a weakening yen (Exhibit 8). While the BoJ continues to tighten policy, the supplemental and proposed fiscal 2026 outlays risk exacerbating inflation pressures. The stepped-up spending also threatens to stall progress in fiscal consolidation, potentially reigniting concerns about long-term debt sustainability. Retaliatory Chinese trade measures in response to the Prime Minister's recent comments on Taiwan also threaten to dampen growth.

China's Growth Dependent on Exports as Domestic Demand Weakens

Exports were the bright spot in 2025, with China's merchandise trade surplus topping a trillion U.S. dollars (Exhibit 9). Despite an 18.8 percent plunge in exports directly to the U.S., China's

Exhibit 7: Global Export Volume Market Share
Percentage Point Change Relative to 2015 Average



Source: Netherlands Bureau for Economic Policy Analysis, 12/24/25

Exhibit 8: Japanese Government Bond Yields



Source: FactSet, 12/31/25



exports grew 5.4 percent year over year in the first 11 months of 2025, as it rerouted shipments and gained market share (Exhibit 10). Exports will likely remain a vital economic driver in the coming years, given China's structural growth in high-tech manufacturing, the government's push for self-sufficiency, and still-weak domestic demand. Consumer spending and property investment continue to disappoint, as confidence remains near historic lows. However, despite a sharp slowdown in the fourth quarter, better-than-expected economic growth in the first nine months of 2025 puts the government's growth target of "around 5.0 percent" well within reach. External strength diminished policymakers' urgency to stimulate the economy in 2025, but we expect fiscal spending to turn more supportive in 2026, the first year of the 15th Five-Year Plan. Export resilience and stimulus underpin our 2026 real GDP growth forecast of 4.5-5.0 percent.

China's Household Consumption Struggles Amid Prolonged Property Slump

Chinese household consumption has lost momentum since mid-2025, hindered by fading fiscal subsidies, an adverse wealth effect from a prolonged property downturn, and a weak job market. Policymakers prioritized domestic demand in 2025 and will surely do so again in 2026. Even so, increasing household consumption as a percentage of GDP has been a significant challenge. Consumers' willingness to spend has improved slowly since 2022 but remains well below pre-pandemic levels (Exhibit 11). And, while it could be viewed as dry powder for future spending, personal deposits have doubled since the end of 2019 and are 54.5 trillion yuan (\$7.8 trillion) above the pre-pandemic trendline. According to the recent Urban Depositor Survey Report, a near-record 62.3 percent of those surveyed prefer more savings, while only 19.2 percent prefer more spending. Consumer spending is unlikely to recover until Chinese policymakers plug the hole in the property market, which continues to sink, with no bottom yet in sight (Exhibit 12).

Exhibit 9: China Merchandise Trade Balance

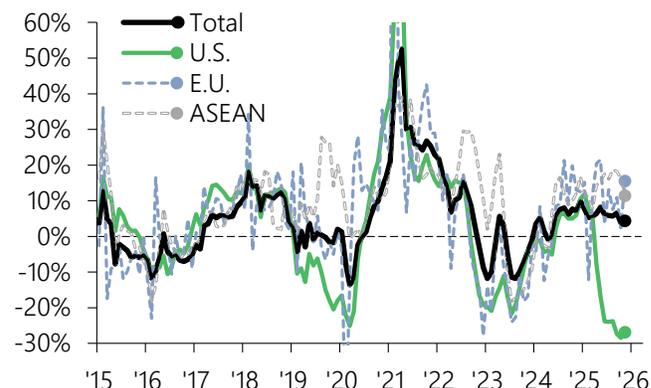
Rolling Twelve-Month Sum, Billions of U.S. Dollars



Source: China Customs, 12/8/25

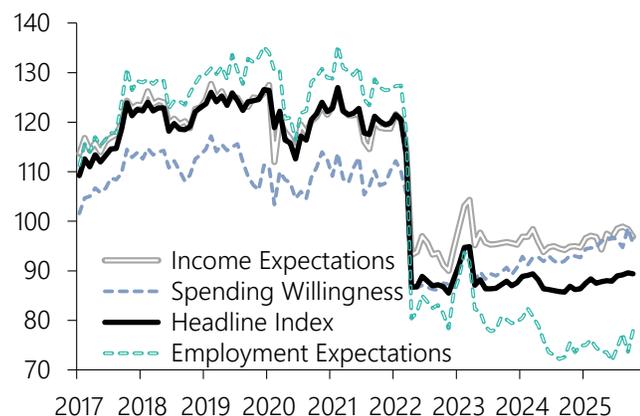
Exhibit 10: China Merchandise Exports

Three-Month Moving Average, Y/Y Percent



Source: China Customs, 12/8/25

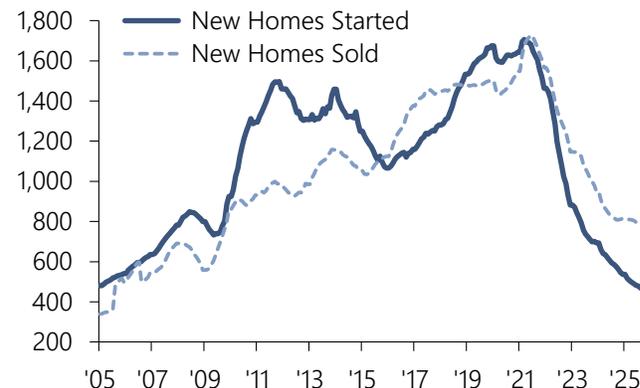
Exhibit 11: China Consumer Confidence Index



Source: National Bureau of Statistics, 12/11/25

Exhibit 12: China New Residential Floor Space

Rolling Twelve-Month Sum, Millions of Square Meters

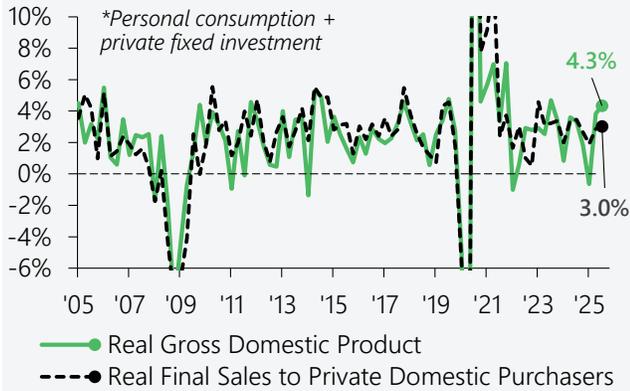


Source: National Bureau of Statistics, 12/15/25

United States: Other Notable Data Points

Private Domestic Demand Remains Resilient

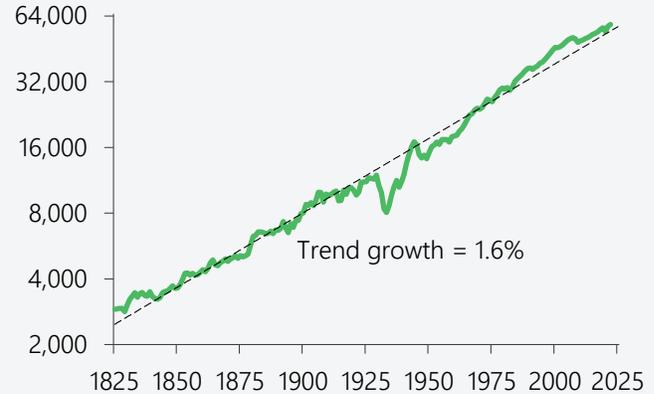
Real GDP vs. Real Sales to Domestic Private Purchasers*
Seasonally-Adjusted Q/Q Percent, Annualized



Source: Bureau of Economic Analysis, 12/23/25

200 Years of Relatively Consistent GDP Growth

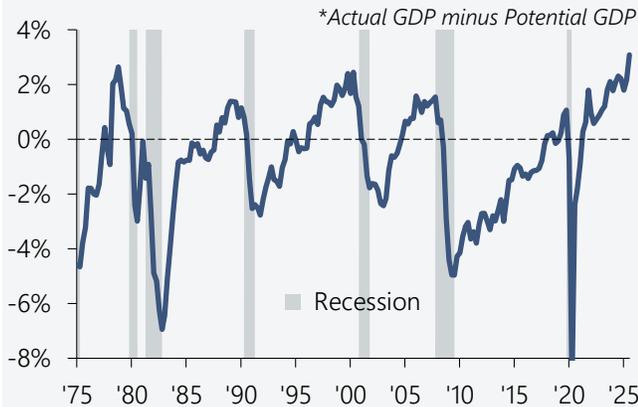
U.S. Real GDP per Capita
2011 Dollars, Log Scale



Source: Maddison Project Database, 12/31/25

Output Gap Implies Limited Economic Slack

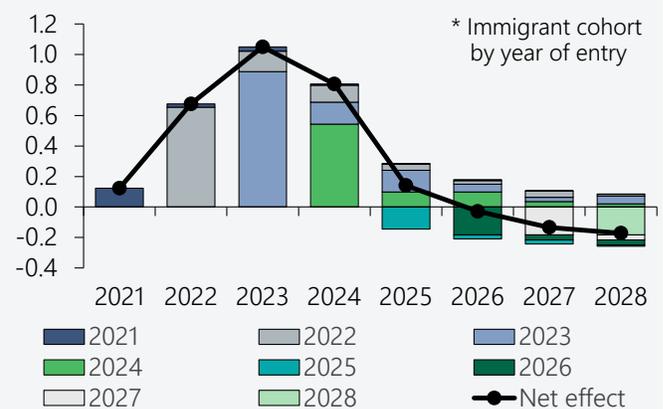
U.S. Output Gap*
Percent of Potential GDP



Source: Bureau of Economic Analysis, CBO, NBER, 12/31/25

Immigration May Become a Modest Headwind

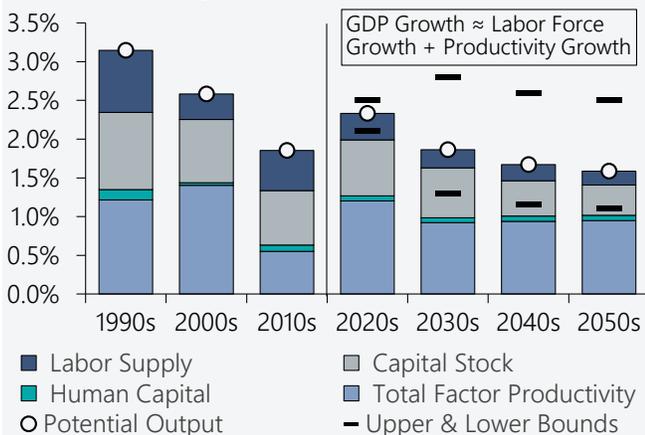
Impact of Above/Below-Average U.S. Immigration*
Estimated Effect on Annual Labor Force Gains, Million



Source: Oxford Economics, 11/24/25

Onus on Productivity to Drive GDP Growth

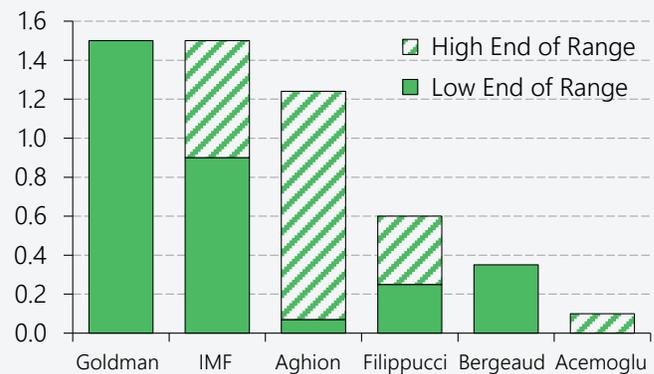
U.S. Potential Output Growth



Source: Oxford Economics, 12/9/25

Above-Trend Growth Hinges on AI's Promise

Predicted Increase in Annual Labor Productivity Growth
Over a 10-Year Horizon Due to AI (Percentage Points)

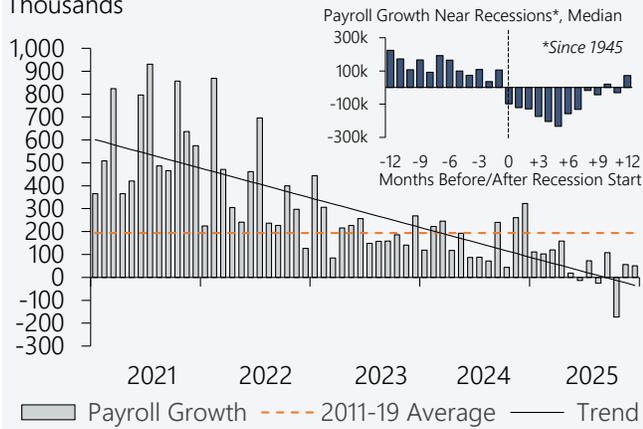


Source: Various, 12/31/25

United States and Euro Area: Other Notable Data Points

U.S. Payrolls Nearly Flat Over Last Six Months

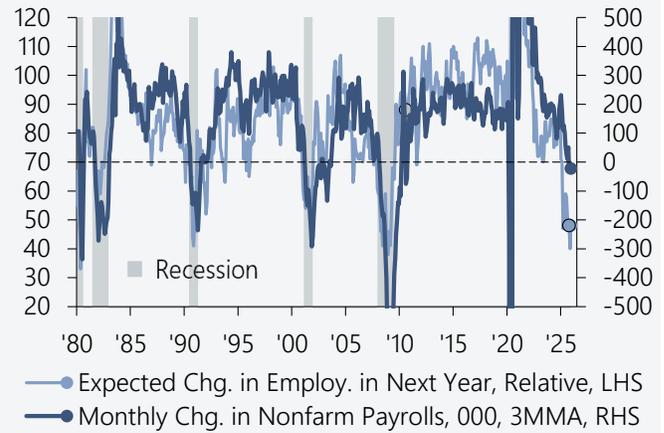
Monthly Change in U.S. Nonfarm Payrolls
Thousands



Source: Bureau of Labor Statistics, 1/9/26

U.S. Consumers Worried About Job Losses

Consumer Employment Expectations vs. Nonfarm Payrolls



Source: University of Michigan, Bureau of Labor Statistics, 1/9/26

Late '25 Jump in Low-/Mid-Income Confidence

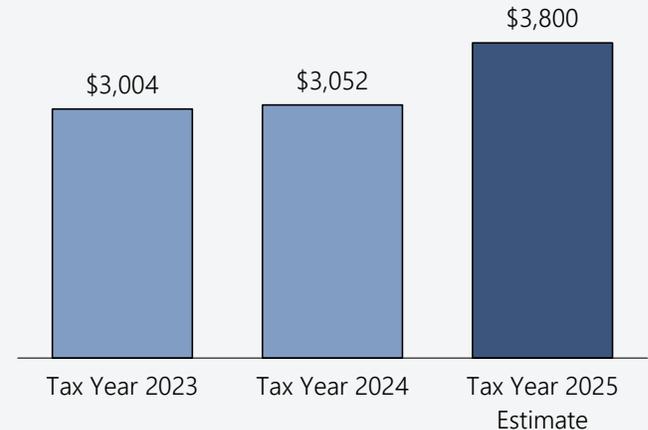
U.S. Consumer Confidence
By Annual Household Income



Source: Morning Consult, 1/5/26

OBBBA Will Boost U.S. Tax Refunds in 2026

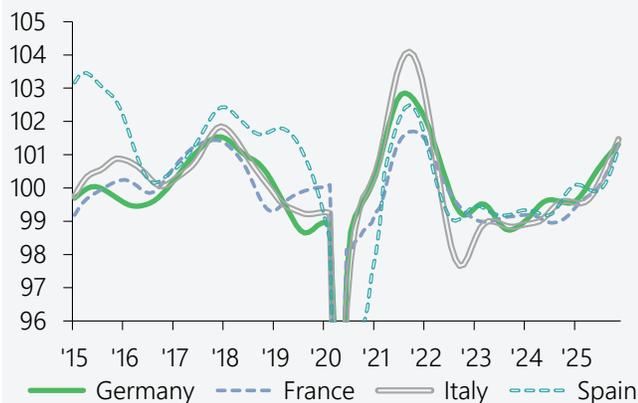
Average U.S. Tax Refunds



Source: Tax Foundation, 12/17/25

Euro Area Enters '26 on Solid Economic Footing

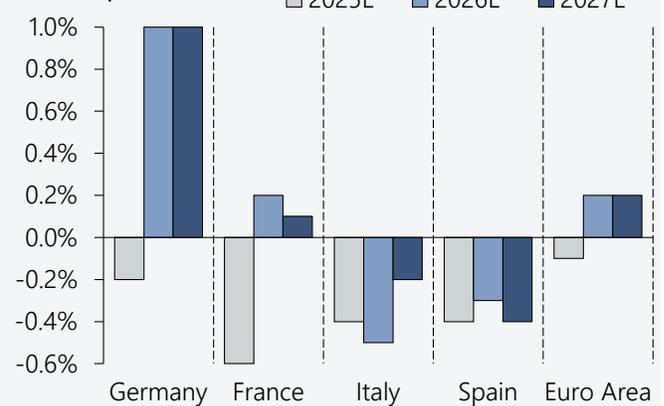
Composite Leading Indicators
Amplitude Adjusted, Long-Term Average = 100



Source: OECD, 12/8/25

Modest Economic Lift From EA Fiscal Impulse

Fiscal Impulse*



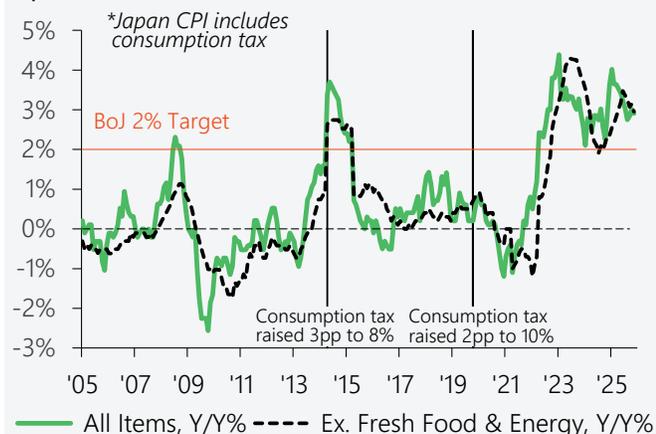
*Chg. in cyclically-adjusted primary balance as % of potential GDP

Source: IMF Fiscal Monitor, 10/15/25

Japan and China: Other Notable Data Points

Japan's Inflation Overshooting BoJ's 2% Target

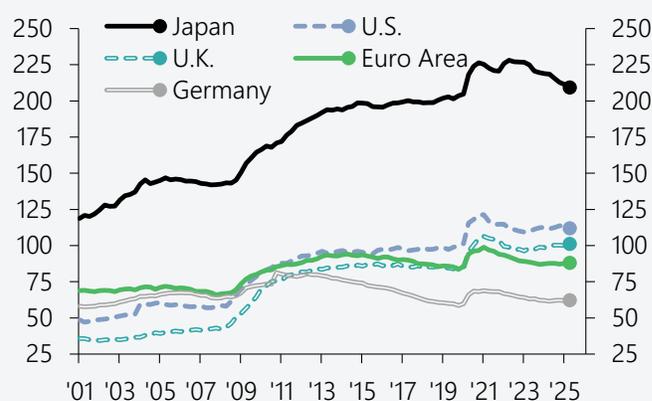
Japan Consumer Price Index



Source: Statistics Office of Japan, 12/19/25

Renewed Spending Tests Japan's Debt Progress

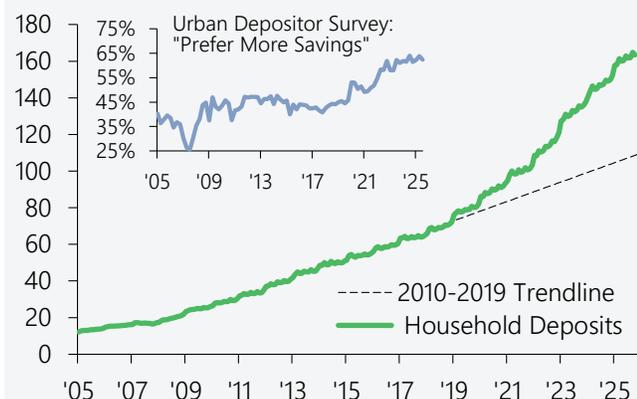
General Government Debt
Percent of GDP



Source: Bank for International Settlements, 12/8/25

Chinese Consumers Prefer Savings to Spending

China Household Deposits
Trillions of Yuan



Source: People's Bank of China, 12/31/25

Fixed Investment Growth Has Turned Negative

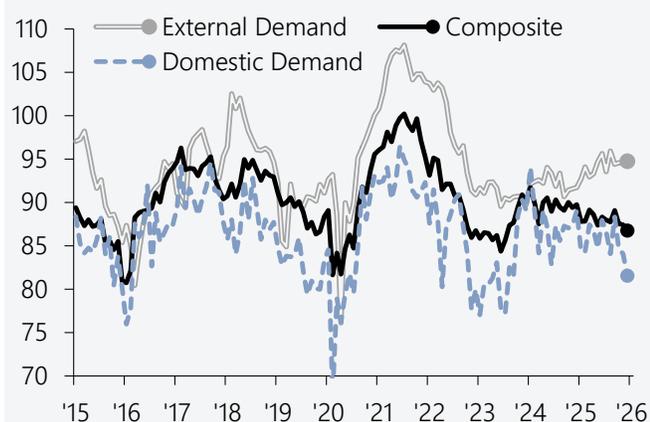
China Fixed Asset Investment
Monthly, Y/Y Percent



Source: National Bureau of Statistics, 12/15/25

China's Growth Dependent on External Demand

CICC Cyclical Momentum Index



Source: China International Capital Corporation, 12/31/25

China's Policy Easing Will Continue in 2026

Type	Instrument	2026F (2025)
Monetary (eop)	RRR	Large banks: 7.0% (7.5%) Medium-sized banks: 5.0% (5.5%) Small banks: 5.0% (5.0%)
	7-Day OMO	1.2% (1.4%)
	Augmented fiscal deficit (% of GDP)	5.1% (4.8)
Fiscal (full year)	Effective on-budget deficit (% of GDP)	12.2% (11.0%)
Housing	Housing policy	Further reduction to mortgage rates; further relaxation on home purchase restrictions in Tier-1 cities; cash-backed settlement of urban village renovation; government programs to help destock existing inventories

Source: Goldman Sachs, 1/5/26



December Rate Cut Sets the Stage for 2026

In December, the Federal Reserve (Fed) delivered its final rate cut of 2025, lowering the federal funds target range by 25 basis points to 3.50–3.75 percent, bringing the year’s cumulative rate reduction to 75 basis points. The decision was accompanied by two hawkish dissents to hold rates unchanged. Policymakers now view the fed funds rate as positioned at the plausible upper bound of neutral. Officials emphasized a cautious approach to further interest rate cuts, which will largely depend on labor market strength. The updated Summary of Economic Projections showed only modest changes, with no revisions to the expected policy rate path and an upward revision to the 2026 GDP growth forecast. We anticipate the labor market to remain soft and inflation to continue to ebb, which should support a few additional rate cuts in 2026, particularly with a new Fed Chair taking office in May.

Rising Fed Dissents Reflect Healthy Debate Amid Policy Tensions

Dissents within the Fed have become more frequent in recent months as policymakers debate the appropriate path for monetary policy. This increase has occurred amid heightened scrutiny of the Fed’s independence and reflects the challenging economic backdrop. Inflation remains stubbornly above its 2.0 percent target, while the labor market is exhibiting signs of softening, placing the Fed’s dual mandates of price stability and maximum employment in tension and naturally leading to differing policy views. We view this increase in dissents as a healthy and constructive development, underscoring the independence of Fed governors and the rigor of the policy debate. We have enjoyed relative conformity at the Fed recently. Historically, we have had decades in which multiple dissents were the norm. With a new Fed Chair taking office this year, we expect these discussions to become more deliberative as new leadership establishes the policy framework and priorities.

Economic Growth Key to Managing U.S. Debt and Deficits

The U.S. economy will need strong growth to contend with persistently large fiscal deficits and mounting government debt. Federal tax revenues have surged from roughly \$3.4 trillion pre-pandemic to about \$5.3 trillion today, a greater than 50 percent increase in just six years. Yet government spending has grown even faster, rising from approximately \$4.5 trillion to \$7.0 trillion over the same period. The result is a widening fiscal gap and mounting pressure on long-term sustainability. With limited political will to address spending or deficits, economic growth becomes increasingly critical. Persistent fiscal deficits and rising debt levels are likely to keep upward pressure on long-term yields and increase volatility across bond markets. In this environment, income generation becomes more important, yield curves may remain structurally steeper, and markets are likely to be more sensitive to surprises in growth and inflation. Strong economic growth can help offset these pressures; absent that, investors may face higher term premiums and uncertainty about future policy responses.

Taxable Fixed Income Strategy

Our strategy remains focused on generating strong interest income as the primary driver of returns. As the federal funds rate declined, the yield curve steepened in 2025, with short-term rates falling more than longer-term yields; 30-year rates ended the year modestly higher. We anticipate further yield-curve steepening as additional cuts are priced in, though the degree of steepening is likely to vary across maturities. Portfolios are positioned with durations modestly longer than benchmarks, with an emphasis on the three- to six-year maturity range where carry and roll-down opportunities are most attractive. We remain constructive on corporate credit, particularly in the latter half of 2026, as reduced regulatory burdens are expected to support economic activity. Easing tariff uncertainty and moderating inflation should further contribute to a favorable business environment. Agency and non-agency residential mortgage-backed securities continue to offer compelling spreads and strong structural credit support. Our primary objective remains to construct portfolios that deliver a meaningful income advantage, which we expect will be the dominant driver of long-term outperformance.



Long-Duration Bonds Outperform for the Quarter, While the Belly Takes the Year

The tax-exempt yield curve flattened slightly during the fourth quarter, as short-term yields rose by about ten basis points and long-term yields ended relatively unchanged. For the year, high-grade tax-exempt bond yields out to ten years decreased 30-50 basis points, while long-term bond yields increased by more than 30 basis points. Credit spreads were relatively stable during the quarter. For the year, investment-grade credit spreads widened slightly, while credit spreads on bonds rated BBB or below generally widened by about 15-25 basis points on average. Tax-exempt bond performance was strong for both the quarter and the whole year. Performance was broad-based across revenue bond sectors and credit quality for both the quarter and the year. Long-duration bonds outperformed during the quarter, while the 7-to-10-year maturity range delivered the strongest performance for the year (Exhibit 13).

Supply Tops Prior Record

As expected, total municipal bond issuance set a new record in 2025. Total municipal bond issuance for the year was nearly \$580 billion, according to the Bond Buyer, an increase of over \$65 billion from the prior record set in 2024. Fund flows were positive throughout most of the fourth quarter. Fund flows were also positive for the year, but have not yet fully recovered from the significant outflows in 2022-2023. By year-end, long-term mutual funds recovered roughly 25 percent of the total drawdown. However, when combined with exchange-traded funds, they recovered roughly 85 percent of the total drawdown. Secondary trading volume slowed in the fourth quarter and was the lightest bid list activity since the third quarter of 2024.

Tax-Exempt Fixed Income Outlook

We expect coupon income to be the primary driver of returns in 2026. While the Fed may ease further in 2026, we are less certain regarding the path of long-term interest rates. Inflation and overall government debt levels will continue to weigh on longer-term interest rates. Most municipal bond strategists expect the pace of issuance to remain robust in 2026, with totals close to or potentially exceeding this year's. Conversely, we think housing bond issuance may slow, particularly taxable housing bond issuance, as some issuers may begin selling loans directly into the TBA market as an alternative.

Tax-Exempt Fixed Income Strategy

Portfolios across all strategies continue to maintain significant yield advantages over their benchmarks. This income advantage will benefit returns in 2026. We continue to favor housing and other revenue bond sectors, such as transportation, with incremental purchases. Where appropriate, we also like premium coupon bonds that offer greater income levels and more defensive characteristics should longer-term rates rise or remain elevated. We also continue to favor new issues and secondary-market structures with short and intermediate-call provisions, provided they also have a premium coupon structure. Most portfolios remain longer than their benchmarks, although generally slightly shorter than where they started the year. Furthermore, we have continued to reduce the barbell in intermediate-duration portfolios by sourcing more intermediate-duration bonds where possible and appropriate. Looking ahead into 2026, we think portfolios are positioned to benefit from the steepness of the tax-exempt municipal yield curve.

Exhibit 13: Bloomberg Municipal Bond Index Returns, Percent

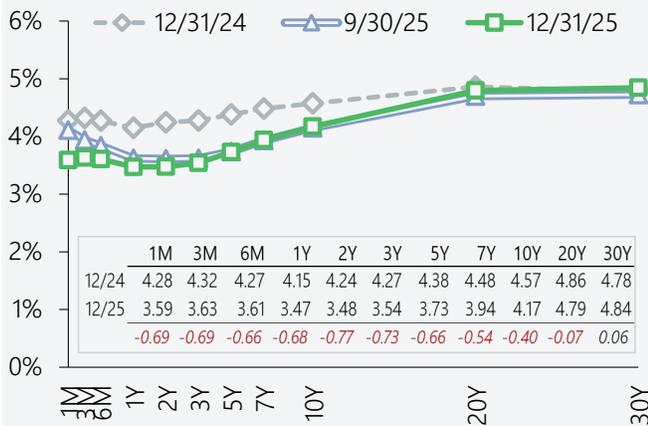
	4Q 2025		4Q 2025		4Q 2025		4Q 2025	
Muni Bond Index	1.56	4.25	AAA	1.57	4.25	GO Bond Index	1.60	4.31
3-Year	0.46	4.11	AA	1.57	4.21	Revenue Bond Index	1.57	4.21
5-Year	0.50	5.03	A	1.50	4.35	Electric	1.66	3.78
7-Year	0.83	5.70	BBB	1.77	4.13	Hospital	1.75	3.53
10-Year	1.74	5.92				Housing	1.77	5.74
Long	1.63	1.95				IDR/PCR	0.65	5.19
						Transportation	1.68	4.37
						Education	1.69	4.10
						Water & Sewer	1.61	4.06
						Resource Recovery	1.49	3.78
						Leasing	1.69	4.41
						Special Tax	1.49	3.70
						Tobacco Index	1.34	4.01

Source: Bloomberg, 12/31/25

Fixed Income: Other Notable Data Points

Bull Steepening in Treasury Curve Continues

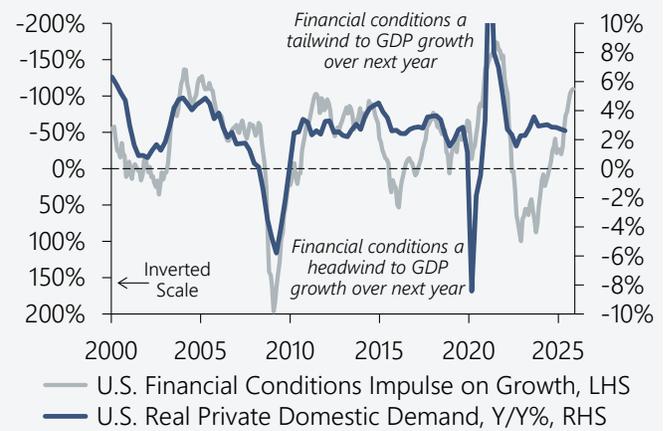
U.S. Treasury Yield Curve



Source: FactSet, 12/31/25

Easier Financial Conditions Support Growth

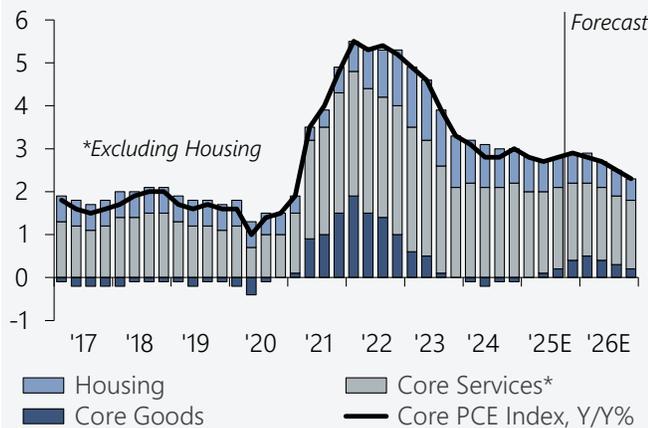
Financial Conditions Impulse vs. Private Domestic Demand



Source: Federal Reserve, Bureau of Economic Analysis, 12/31/25

Inflation Projected to Fall Toward 2% Target

U.S. Core PCE Index, Percentage Point Contribution



Source: Oxford Economics, 1/6/26

Betting Odds See Next Fed Chair as Close Call

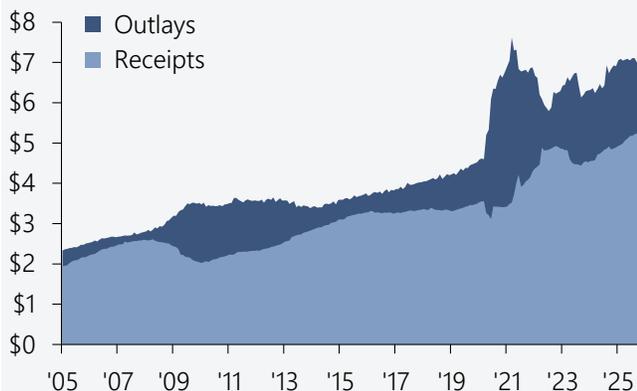
Who Will Trump Nominate as Fed Chair?



Source: Polymarket, 1/12/26

U.S. Fiscal Budget on Unsustainable Trajectory

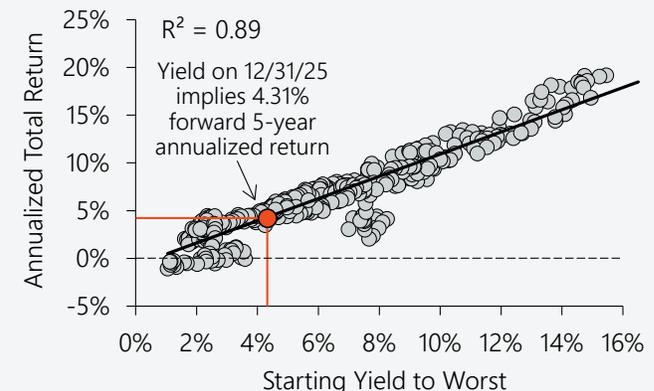
U.S. Federal Receipts and Outlays
\$ Trillion, Trailing Twelve Month Sum



Source: U.S. Treasury, 12/31/25

History Suggests Solid Five-Year Bond Returns

Bloomberg U.S. Aggregate Starting Yield to Worst vs. Subsequent 5-Year Annualized Return, 1976 to 2025



Source: Bloomberg, JP Morgan, 12/31/25



Global Equities: Environment and Strategy

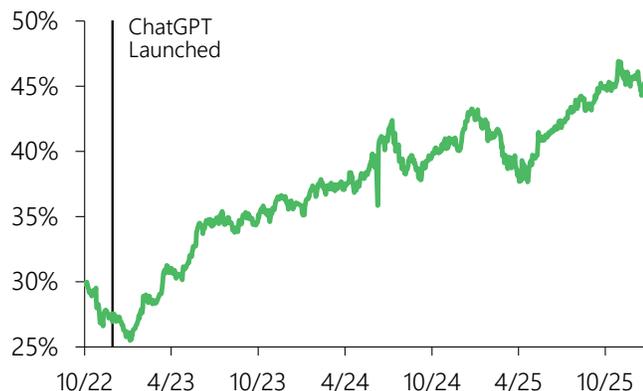
Strong Earnings Drove S&P 500's 2025 Returns Amid Narrow Stock Participation

The S&P 500 Index returned 17.9 percent in 2025, marking its third sequential year of double-digit gains and bringing its trailing three-year cumulative return to 86.1 percent, or 23.0 percent annualized. Earnings growth was, by far, the top driver of the 2025 return, accounting for 15.1 percentage points, compared with 1.2 and 1.5 percentage points for price-to-earnings multiple expansion and dividends, respectively. However, performance remained highly concentrated. Only 28 percent of S&P 500 constituents outperformed the index, similar to the prior two years. Seven stocks—Alphabet, Amazon, Apple, Broadcom, Meta, Microsoft, and Nvidia—comprised 48 percent of the 2025 S&P 500 return and 56 percent of the three-year return. A universe of 42 AI-related stocks accounted for 60 percent of the 2025 return and almost 70 percent of the trailing three-year return. The 42 stocks ended the year at 45.2 percent of the S&P 500 Index, underscoring the risk posed by any AI snafus (Exhibit 14). Still, accelerating earnings growth in other sectors has driven broader gains in recent months and should continue to do so.

International Stocks Get Their Day in the Sun, Helped by Valuation and Currency

As strong as S&P 500 Index returns were in 2025, they were still bested by many international equity indices (Exhibit 15). After the broad category significantly lagged the S&P 500 Index for much of the last 15 years, a catch-up trade was overdue (Exhibit 16). Unlike the S&P 500 Index, higher valuations and a weaker U.S. dollar were the main drivers of international index returns. As a result, price-to-earnings ratios are currently near or above 20-year averages (Exhibit 17).

Exhibit 14: AI-Related Stocks as a % of S&P 500
42 Stocks Spanning Direct AI, AI Utilities, & AI Cap. Equip.



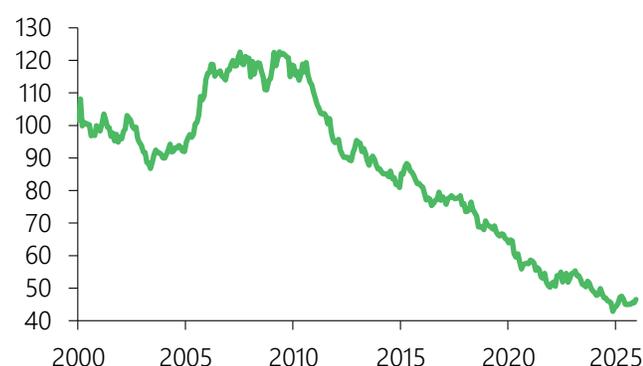
Source: FactSet, JP Morgan, 12/31/25

Exhibit 15: Equity Index Total Returns, Percent

Total Returns in U.S. Dollars and in Local Currency, %	Calendar 2025		15Y Annualized	
	USD	Local	USD	Local
EM Latin America	55.7	39.2	0.8	6.9
MSCI Europe	36.3	21.3	7.6	8.4
MSCI Emerging Markets	34.4	32.1	4.2	7.0
MSCI AC World (ex. U.S.)	33.1	25.1	6.4	8.4
MSCI EAFE	31.9	21.2	7.1	8.9
MSCI China	31.4	30.7	4.1	4.1
MSCI AC Asia Pac	28.6	27.1	6.2	8.8
MSCI Japan	25.1	24.7	6.9	11.7
S&P 500	17.9	17.9	14.1	14.1

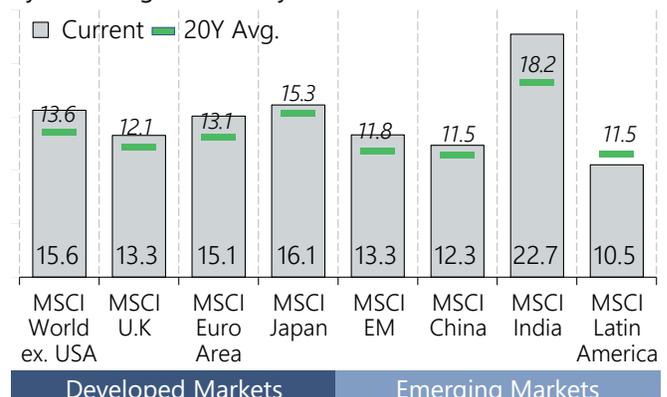
Source: FactSet, 12/31/25

Exhibit 16: International Equity Performance
MSCI AC World Index (ex. USA) Relative to S&P 500 Index
U.S. Dollar, 12/31/99 = 100



Source: FactSet, 12/31/25

Exhibit 17: MSCI Index P/E Valuation Ratios
By MSCI Region/Country



Source: FactSet, 12/31/25



However, relative to the S&P 500 Index, most international indices still trade at a considerable discount to their historical averages. Fund flows during 2025 reflected an improved outlook for international stocks, with a cumulative \$438 billion flowing to non-U.S. equity mutual funds and ETFs, up from about \$198 billion in 2024. Despite the “Sell America” theme that emerged following “Liberation Day,” better-than-feared tariff negotiations and strong corporate earnings led to a resurgence of inflows to U.S. funds into year-end. Still, U.S. funds’ share of global equity fund flows decreased to 45 percent in 2025, down from about 73 percent in 2024.

Global Equity Strategy

Three years of strong market performance have left U.S. equity markets trading at historically elevated valuations, putting the onus on corporate earnings to support equity prices. The good news is that earnings picked up steam during the second half of 2025, with momentum likely to extend into 2026, driven by a favorable mix of easing interest rates, fiscal stimulus, and the continued expansion of artificial intelligence. We expect market leadership to broaden beyond the “Magnificent Seven,” as earnings growth becomes more evenly distributed across sectors, with most industries positioned to deliver solid profit growth in the year ahead. Against this backdrop, we are focused on identifying attractively valued, high-quality companies capable of generating positive earnings surprises, supported by compelling secular or cyclical tailwinds.

While broader market participation should continue, technology is likely to remain a focal point for investors. Growth in the sector remains robust, despite periodic worries about an AI bubble. Speculative excess is a natural feature of a tech-led market, but the underlying fundamentals of AI remain compelling. Demand for AI infrastructure continues to accelerate, as evidenced by rising capex and robust AI-driven cloud revenue growth among leading hyperscalers, including Alphabet, Amazon, Meta, Microsoft, and Oracle. Significantly, the majority of this investment is funded by operating cash flows rather than by increased financial leverage.

AI adoption is also expanding rapidly across both consumer and enterprise markets. OpenAI’s monthly active users, for example, have grown to over 800 million, up from approximately 400 million in early 2025. AI usage has evolved from experimental pilots to mission-critical infrastructure, with virtually all large organizations now deploying AI in at least one business function. Research from Boston Consulting Group contends that we are still in the early stages of AI-enabled cost optimization, with companies realizing meaningful savings across procurement, marketing, research and development, and energy, often generating first-year cost reductions exceeding 10 percent.

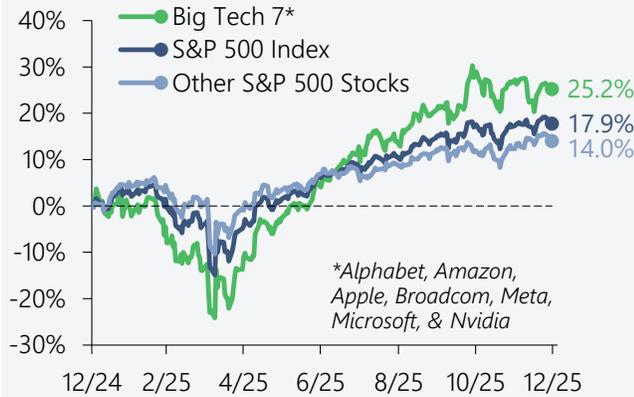
As the AI infrastructure buildout progresses, we continue to focus on areas of supply-chain constraint, including memory and storage, networking, power and power management, semiconductor equipment, and hyperscalers that provide core cloud infrastructure. Looking ahead, we also see opportunities in segments that were relatively overlooked in 2025 but may inflect in 2026—particularly end users of AI that can enhance operational efficiency, expand margins, and grow total addressable markets. Software companies, which generally lagged the broader market in 2025, are well-positioned to benefit as AI agents increasingly automate workflows and drive productivity gains.

In international portfolios, we are positive on stocks in China, South Korea, Taiwan, and India, due to strong earnings growth, robust AI demand, and attractive relative valuations. The MSCI Emerging Markets Index is projected to deliver 17 percent earnings growth in 2026, driven by improving domestic demand and strength in the AI-fueled tech sector. Although it trades at a forward price-to-earnings ratio of 13.4 times, at the upper end of its 10-year historical range, the MSCI Emerging Markets Index is attractive relative to other global stock indices. We are constructive on Chinese stocks, as the policy and regulatory cycle has become more pro-growth and pro-market. In addition, owing to AI breakthroughs and more stable U.S.-China relations, investor confidence is rising. Our China strategy focuses on structural growth stocks, including AI-focused plays and non-banking financials. In South Korea and Taiwan, our holdings are focused primarily on AI-related high-bandwidth memory and semiconductor memory.

Global Equities: Other Notable Data Points

Big Tech Rallied to Emerge Winner Again in '25

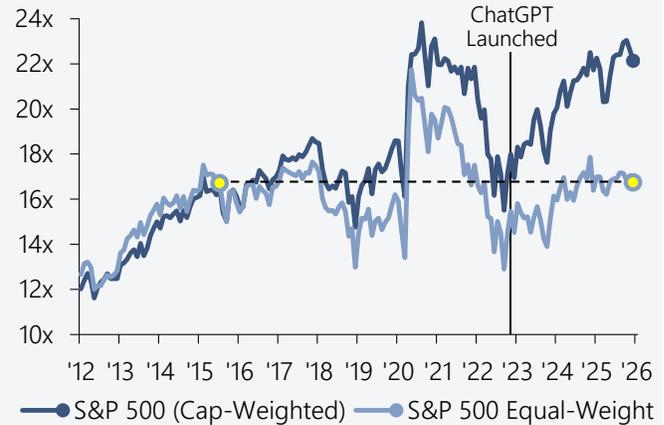
S&P 500 Index Cumulative Total Returns
12/31/24 to 12/31/25



Source: FactSet, 12/31/25

Equal-Weight Multiple Relatively Unchanged

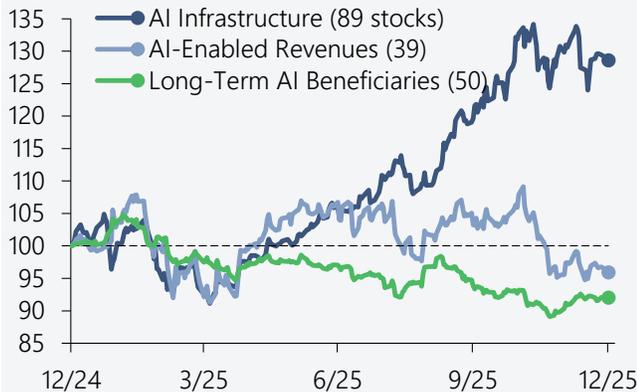
S&P 500 Forward Price-to-Earnings Ratio



Source: FactSet, 12/31/25

AI's Outperformance Limited to Infrastructure

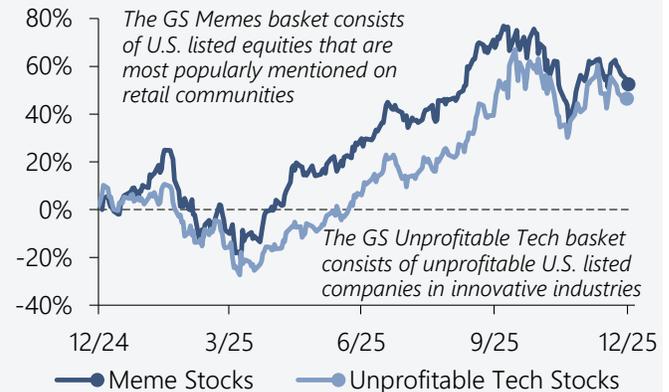
Performance of AI-Exposed Stocks in GS Equity Baskets
Relative to Equal-Weight S&P 500, 12/31/24 = 100



Source: Goldman Sachs, 12/31/25

Speculative Stocks Big Outperformers in 2025

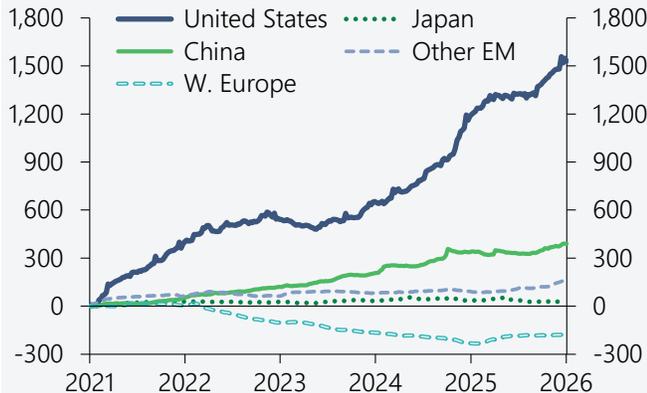
GS Memes and Unprofitable Tech Equity Baskets
2025 Cumulative Returns



Source: Goldman Sachs, 12/31/25

"Sell America" Trade Never Got Off Ground

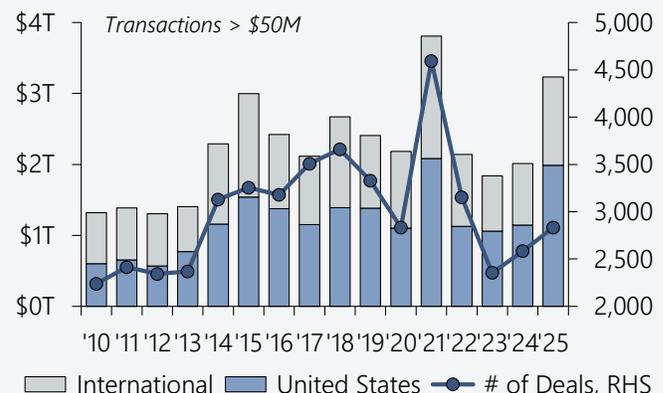
Global Equity Mutual Fund and ETF Flows
\$ Billions, Cumulative



Source: EPFR, 1/7/26

Global M&A Activity Continues to Rebound

Global M&A Transactions
Total Deal Value, \$ Trillion



Source: FactSet, 12/31/25

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