2026 PREDICTIONS

Happy holidays! The current year has been another rewarding one for investors with truly exceptional returns in the global equity markets in particular. As the calendar turns to 2026, it's natural to contemplate what has been and re-evaluate the outlook. As I went through this exercise, the following observations struck me as notable. While certainly not an exhaustive list, I hope you find these thoughts and charts helpful as you consider your asset allocation and portfolio positioning for the year ahead.

Hope you have time to rest and reflect on the blessings in your life over the holiday season and wish you and your family a prosperous new year!!

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The practice of issuing annual outlooks as the calendar turns to a new year is a common one on Wall Street. What is less common is prognosticators publishing honest evaluations of their prior predictions! As often mentioned, the future is unknown and unknowable, making predictions of the future seemingly futile. However, thoughtful analysis and research can produce insights that help protect and grow wealth, even with an uncertain future. In that spirit, before sharing some thoughts on the outlook for 2026, a quick review of the 'hits and misses' published in last year's outlook.

2025 Outlook Review Scorecard:

Earnings Recession Ends	☑
Valuation Limits '25 Market Return	☒
Momentum Loses It's 'Mo'	☒
Stock/Bond Correlation Normalizes	☑
Employment Will Weaken	☑
Inflation Will Remain Elevated	☑

As expected, earnings growth accelerated for the broad market in 2025. Even excluding the 'Mag7' stocks, the rate of earnings growth has been strong this year and is expected to accelerate further into 2026. However, elevated valuations didn't dent returns with the S&P 500 Index posting a strong mid-teens percentage increase through the middle of December. Performance has been led by a small group of stocks with the best growth characteristics, defying my expectations. The stock/bond correlation has begun to normalize though both asset classes have positive returns for the year. And as expected, employment has clearly weakened and inflation, while receding, has remained elevated. Taking some encouragement from getting a few right, let's move on to the outlook for 2026!

2026 Outlook

Strong H1 Domestic GDP Growth

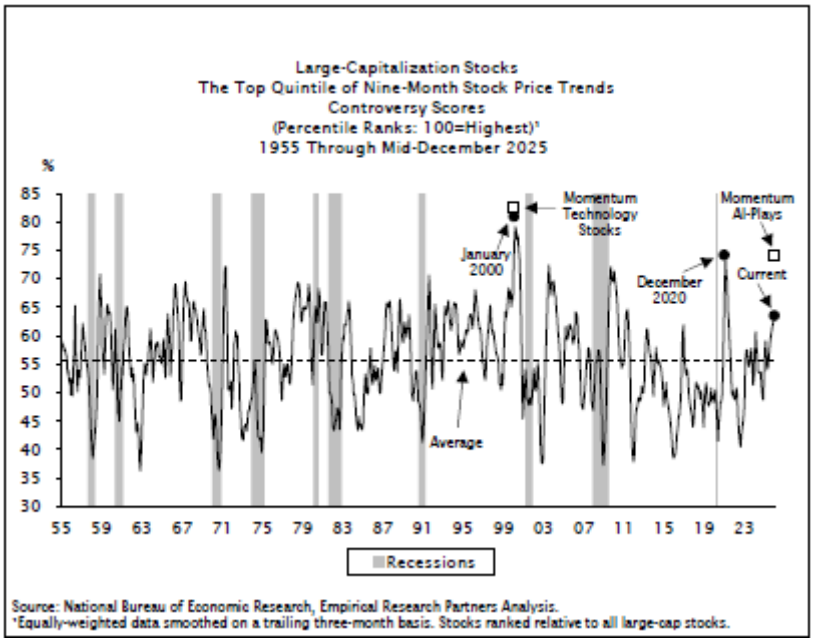
The economy has weathered an extended season of confusing crosscurrents and heightened levels of uncertainty. While the industrial and manufacturing sectors of the economy have struggled over the last year, the twin tailwinds of easing monetary policy and fiscal stimulus should drive economic acceleration in the first half of 2026. After a tumultuous year, the backdrop is becoming increasingly growth-friendly. In addition, as we move into the mid-term election cycle later in the new year, the incentive to initiate disruptive fiscal and/or trade policy should be low. As a result, I expect growing confidence that earnings growth for the broad market will improve and for the market breadth to expand.

Valuation will limit return potential for Equity Indexes in 2026

Yep, I'm 're-upping' this forecast! A lot of anticipated good earnings news is embedded in the valuation of large cap stocks. The S&P 500 is up ~16% this year while the earnings of its constituents have posted a gain of ~10%. The current consensus forecast anticipates ~13% earnings growth in 2026 which suggests that any disappointment could prove costly as investors adjust both earnings and the earnings multiple lower. On the other hand, if investors' optimism is proved correct, the 'reward' is likely to be modest unless the earnings outlook is meaningfully better than already elevated expectations. However, it is significant that the valuation excesses are most acute in the largest constituents of the S&P 500. The remaining companies also trade at a premium to their historical averages, but their forecasted earnings growth is accelerating. I am looking for investment opportunities in less popular areas of the market where valuations are reasonable, and the fundamental outlook is improving as economic growth recovers. While Index returns may be more muted in 2026, I see opportunities to generate excess return by investing outside of the most prominent names and themes.

Momentum likely loses it's 'MO'

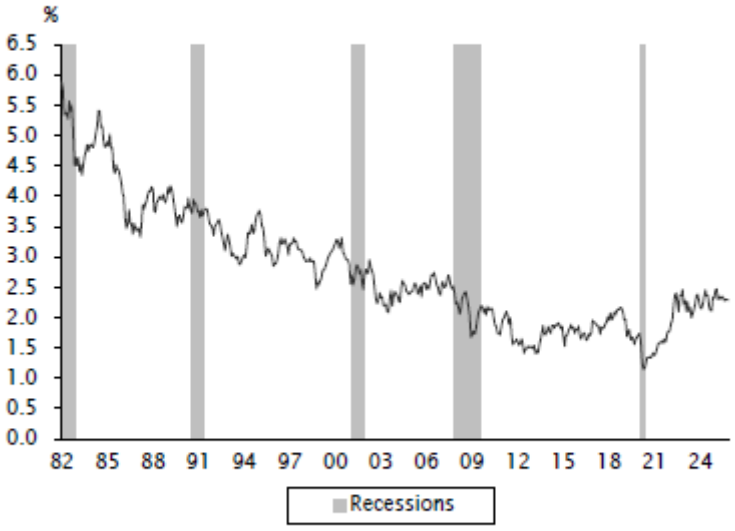
Yes, another repeat from last year's predictions. As opposed to confessing stubbornness, I'm reiterating this call because I think I was simply just early. 😊 The Momentum Factor has been on an epic run with the current streak ranking amongst the best in the last 70 years. This cycle's performance is comparable to the Meme Stock Mania in 2021; the Tech Bubble in 1999; and the Nifty 50 era in the late 1970's. The probability of that streak of outperformance continuing into 2026 is very low. History suggests that this factor is likely to surrender some of its relative outperformance over the next 12mo's. In fact, as we approach the final days of 2025, the performance of the Momentum factor has been weakening. The value of diversification is likely to be reinforced in the year ahead.



Inflation rates will be falling in 2026

While there is currently strenuous debate over the outlook for inflation, I expect inflation to return to the Federal Reserve's target level of 2.0% in 2026. Inflation rates have steadily decreased as the pandemic effects wore off despite protectionist trade policies. A significant deflationary force on the headline number has been shelter costs which account for approximately half of the CPI basket. As a result of elevated multifamily construction and a decrease in demand, in part resulting from tighter immigration policies, rental rates are in a clear downtrend that I expect to continue. Unfortunately, while there is hope for a productivity boost from the use of Artificial Intelligence, I don't believe the disinflationary impacts will be significant enough to noticeably impact reported inflation readings in the next twelve months. However, the goods inflation rate is likely to peak in the early part of 2026 and then fall later in the year as the tariffs anniversary and are included in the prior year base. Given the starting point of consumer finances, particularly for consumers in the middle- and lower-income cohorts, I expect companies to be reticent to push prices aggressively for fear of lost sales. As a result, I expect long-run inflation expectations, which have persistently hovered around 2.5% for the last three years, to decisively break lower in 2026.

Exhibit 15: Ten-Year Inflation Expectations
1982 Through November 2025



Source: Federal Reserve Bank of Cleveland, National Bureau of Economic Research.

The domestic housing market will recover

Housing has been in a bear market for over four years for a confluence of reasons. Mortgage rates dramatically increased as the Federal Reserve hiked rates to combat inflation, depressing demand for both new homeowners and those looking to 'move-up' into a large residence. New home construction has slowed significantly, reducing supply growth and helping keep home prices elevated. As inflation rates moderate next year, incremental cuts to the Federal Funds Rate will put downward pressure on mortgage rates. The average rate on existing mortgages is approximately 4.0% because of homeowners locking in very low rates pre-COVID. At current, the rate for an FHA 30yr mortgage is approximately 5.5% and I expect it to fall below 5.0% in 2026. I anticipate a significant release of pent-up demand as mortgage rates move sub-5.0% with demographic trends amplifying housing turnover.