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2026 Investment Outlook

You Gotta Believe!

"For those who believe, no proof is necessary. For those that don't believe, no proof is possible."

– Stuart Chase – American economist

"Are we in phase where investors as a whole are overexcited about A.I.? My opinion is yes. Is A.I. the most important thing to happen in a very long time. My opinion is also yes."

– Sam Altman – CEO of OpenAI - NY Times interview, November 20

"There can be no way to participate fully in the potential benefits from the new technology without being exposed to losses that will arise if the enthusiasm and thus investors' behavior prove to have been excessive."

– Howard Marks – Is It A Bubble? – Memo 12/9/25

The U.S. stock market finished 2025 with another year of very strong returns that were well above its long-term historical average. As of 12/31/25, the 10-year annualized return for the Russell 3000 Index, which measures the broad U.S. stock market, was +14.4% compared to the 100-year annualized return of +10.5%. The 10-year annualized return of the S&P 500 Index was slightly higher at +14.9%, reflecting the sizable outperformance of U.S. mega cap tech stocks during the past three years, which were significantly impacted by the rapid development of and investor euphoria over artificial intelligence (AI).

As the next table shows, it has been a richly rewarding past decade for U.S. stock investors. Returns were positive in eight of the past 10 years including six years when returns exceeded 20%. Clearly, the past decade has been an exceptional period of investment returns with 2022 the only major decline of any magnitude.

Year	Russell 3000 Total Return
2025	+17.5%
2024	+25.0%
2023	+26.0%
2022	−19.2%
2021	+25.7%
2020	+20.9%
2019	+31.0%
2018	−5.2%
2017	+21.1%
2016	+12.7%

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After an extended period of exceptional returns, investor behavior and sentiment typically takes on a strongly bullish bias and a belief that the good times will continue (buy the dip or FOMO). Younger investors under the age of 35 have only experienced a backdrop of well above average investment returns and only one year in the last 10 when the U.S. stock market generated an outsized negative return. The large decline in 2022 was due to the Fed's significant increase in interest rates to address elevated inflation combined with the negative implications of the Ukraine/Russia War. Even the devasting global economic impact from a once in a century global pandemic in 2020 couldn't keep the stock market down for long as stocks returned over 20% that year and primarily due to the Fed cutting interest rates to 0% to counteract the plunge in economic activity caused by C-19 related shutdowns.

After several years of exceptionally robust stock returns, the 22.0X forward price/earnings (PE) ratio for the S&P 500 Index is in the top 10th percentile of its trailing 25-year history. As a result, the bar is significantly higher for U.S. stocks to continue to deliver above average returns (>10%). The next three charts from the December Bank of America Global Fund Manager Survey capture the heavily bullish bias of institutional investors. They show cash levels are at 20-year lows (top), investor sentiment at the top end of the bullish range (middle), and allocations to equities also at the top end of the 20-year range (bottom). It's interesting to note that US stock allocations during 2025 decoupled from soft ISM manufacturing readings, which until recently were tightly correlated with each other over the past 20 years.
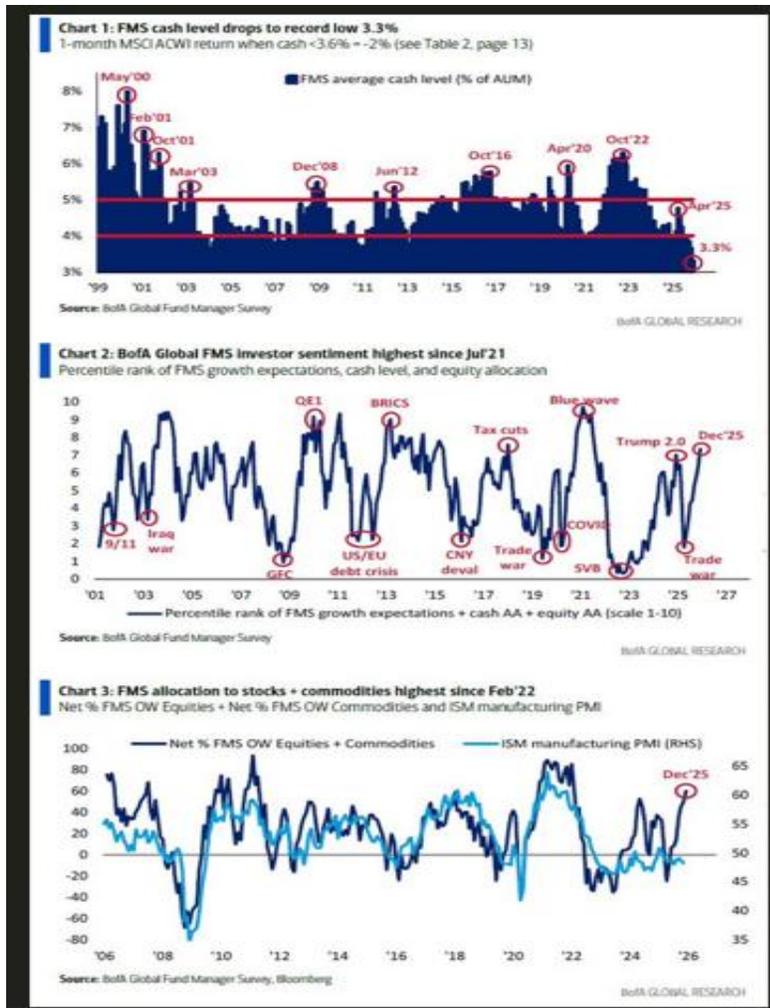
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There are five major assumptions investors need to believe are likely to occur for 2026 to be another year of double-digit returns for the broad U.S. stock market.

1) U.S. stocks as measured by the S&P 500 Index will meet or exceed the current consensus expectation of +12.6% year-over-year operating earnings growth.
2) The high concentration of market weight in the Top 10 stocks and the elevated valuation profile of these stocks does not become a major risk.
3) AI optimism and capital expenditures on AI capacity build out continue to drive U.S. economic growth and propel the U.S. economy to a mid-2% real GDP growth rate.
4) The outcome of the U.S. mid-term elections won't meaningfully alter the economic growth initiatives of the Trump Administration in the last two years of his term.
5) The appointment of a new Federal Reserve Chairman does not go against the market's strong preference for an independent Fed Chair and cause bond yields to rise and in turn negatively impact the stock market's elevated valuation profile.
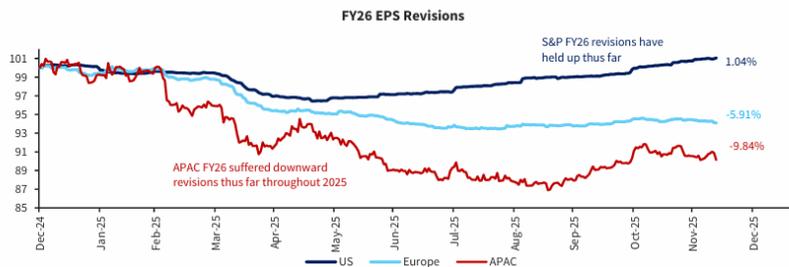
The next chart shows operating earnings data for the S&P 500 Index. The latest 2026 consensus forecast (red) is for the S&P 500 Index to earn $305.83/share compared to $271.53/share in 2025, reflecting year-over-year operating earnings growth of 12.6%. Operating earnings growth from 2024 ($246.19/share) to 2025 was +10.3% so the consensus expectation is for a stronger level of earnings growth in 2026 compared to 2025.
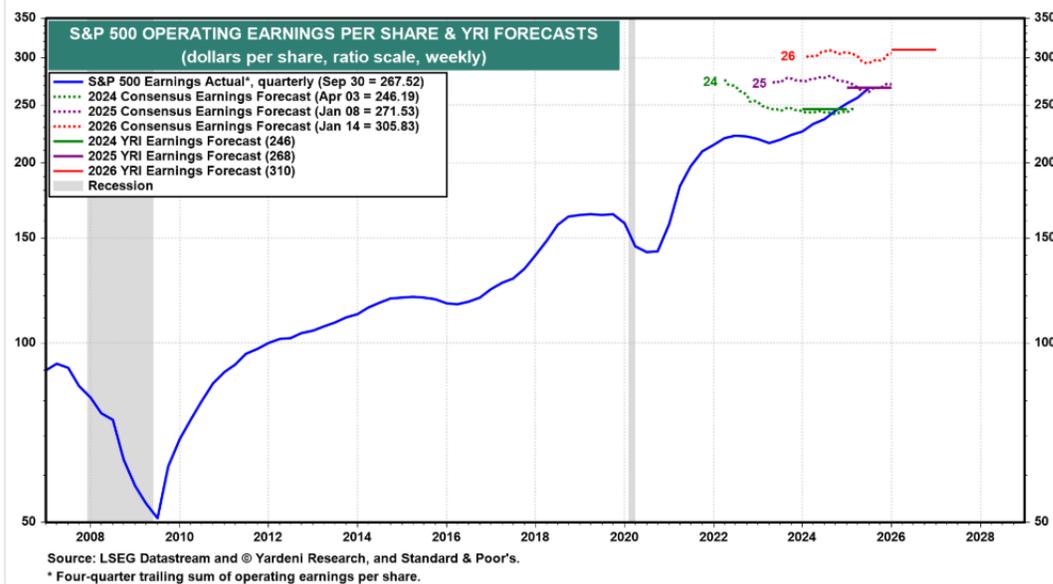
The next chart shows that starting in April 2025, 2026 earnings revisions turned negative as analysts factored in the detrimental impacts from the Trump Administration's Liberation Day tariff policy announcement. However, after a large negative stock market reaction, the Trump Administration either paused or lowered the initial high tariff levels. From mid-year 2025 onward, earnings revisions turned positive and the 2026 earnings level recovered back to original expectations at the start of 2025. While not meaningfully different, the latest 2026 consensus earnings growth forecast is now 1% higher than it was at the beginning of 2025. While tariffs were not eliminated, their expected impact on U.S. corporate earnings turned out to be much less than expected. In addition, U.S. economic growth surprised to the upside in the second half of 2025 and therefore offset some of the negative impact's tariffs had on U.S. real GDP growth.
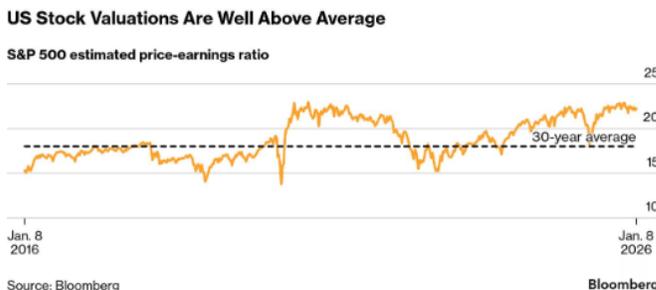
In contrast, since the start of 2025, the 2026 earnings growth outlooks for Europe (blue) and Asia Pacific (red) are lower by 5.9% and 9.8%, respectively over the past year.

FY26 EPS Revisions

S&P FY26 revisions have held up thus far — 1.04%

-5.91%

-9.84%

APAC FY26 suffered downward revisions thus far throughout 2025

US — Europe — APAC

Data as of 12/12/2025
Source: LSEG Data & Analytics, Bloomberg, Barclays Research

Stocks rallied from mid-April onward, helped by multiple factors including the earnings recovery. As the next chart shows, the S&P 500 Index ended 2025 trading about 22% above its 30-year PE average.

US Stock Valuations Are Well Above Average

S&P 500 estimated price-earnings ratio

30-year average

Jan. 8 2016

Jan. 8 2026

Source: Bloomberg   Bloomberg

The next table breaks down valuations of the MSCI regional indices by market cap and sectors. The MSCI US Index, which has a profile like the S&P 500 Index, trades in the 91st percentile of its trailing 10-year PE history. By comparison, U.S. small caps trade in the 37th percentile and U.S. mid-caps trade in the 51st percentile and so both are notably cheaper than large caps. While not significantly cheaper, the MSCI Europe Index trades in the 80th percentile while the MSCI Asia Pacific Index trades in the 85th percentile of their respective 10-year histories. European small and mid-cap stocks are the cheapest segments of global equities.

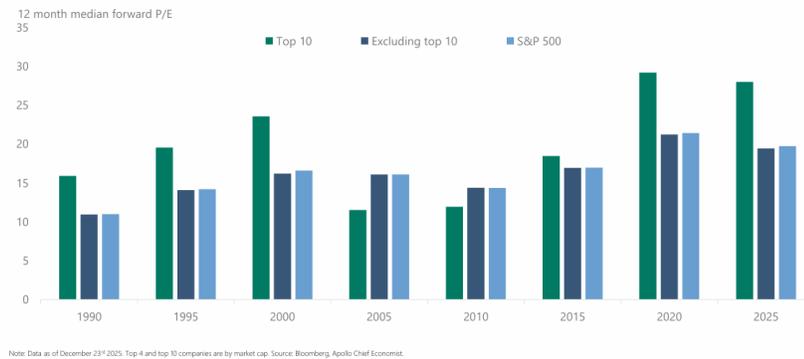| NTM P/E	USA			Europe			Asia Pacific		
	Current	10y Pctle	vs. SPX	Current	10y Pctle	vs. MXEU	Current	10y Pctle	vs. MXAP
Overall	23.0x	0.91		15.1x	0.80		15.2x	0.85	
Small	17.0x	0.37	0.10	13.6x	0.33	0.07	16.0x	0.86	0.54
Mid	17.3x	0.51	0.17	14.2x	0.30	0.00	17.0x	0.90	0.81
Large	23.0x	0.91		15.3x	0.87		14.8x	0.83	
COMM	21.7x	0.88	0.69	16.2x	0.77	0.59	19.4x	0.75	0.50
COND	29.7x	0.78	0.60	16.3x	0.81	0.80	16.1x	0.74	0.53
CONS	21.1x	0.77	0.10	15.4x	0.04	0.00	20.3x	0.07	0.02
FINL	16.1x	0.88	0.25	10.8x	0.71	0.59	11.0x	0.95	0.54
HLTH	18.4x	0.90	0.23	15.8x	0.23	0.14	22.7x	0.09	0.03
INDU	25.0x	0.87	0.83	21.2x	0.85	0.94	17.2x	0.89	0.96
INFT	29.4x	0.88	0.72	29.8x	0.90	0.89	16.5x	0.59	0.24
MATR	19.3x	0.67	0.14	16.3x	0.79	0.71	15.7x	0.88	0.87
UTIL	18.2x	0.46	0.08	13.9x	0.49	0.22	12.2x	0.43	0.22

10y Pctle = 10y daily percentile relative to its own history. Whereas, 10y Pctle calculations vs SPX, vs MXEU, and vs MXAP are calculated against these benchmarks. Europe = MSCI Europe (MXEU), Asia Pacific = MSCI Asia Pacific (MXAP). Data as of 12/11/2025
Source: LSEG Data & Analytics, Bloomberg, Barclays Research

What differentiates the U.S. stock market versus other regions and explains its higher valuation profile is a much higher weight of technology stocks in the U.S. benchmarks combined with the much higher valuation profiles of its largest weighted tech stocks. In the S&P 500 Index, the weight of the technology sector is at an all-time high of 33.5% compared to only 15.8% in the MSCI ACWI Ex US Index of international stocks. The next chart shows how the median valuation profile of the Top 10 stocks in the S&P 500 Index have driven the overall forward PE profile of the S&P 500 Index since 1990. The median forward PE of the Top 10 stocks was nearly 30X compared to a 18X median PE for the remaining 490 stocks in the S&P 500 Index. Going back 35 years, the Top 10 stocks are at the widest valuation premium relative to the other 490 stocks in the index.

The AI bubble today is bigger than the IT bubble in the 1990s

Note: Data as of December 23rd 2025. Top 4 and top 10 companies are by market cap. Source: Bloomberg, Apollo Chief Economist.

The major theme in the U.S. stock market over the past several years is how much market capitalization has accrued to a small group of large / mega cap tech stocks. The next chart shows the weight and earnings contribution of the Top 10 stocks in the S&P 500 Index going back to 1980. By December 2025, the Top 10 stocks comprised 41% of the weight and 32% of trailing 12-month earnings. In other words, the Top 10 stocks have a much higher weight than their earnings contribution warrant. This imbalanced setup last occurred during the 1998-2000 Tech Bubble era but even at the top of the tech bubble the weight of the Top 10 stocks only reached 25% compared to 41% today. Therefore, it is not an overstatement to say that the U.S. stock market is heavily reliant upon the continued success of and investor support for this select group of mega cap tech companies. 41 cents of every incremental $1 invested in a passive S&P 500 Index fund now goes into only 10 stocks, not exactly the definition of broad diversification.

Data as of 12/16/2025
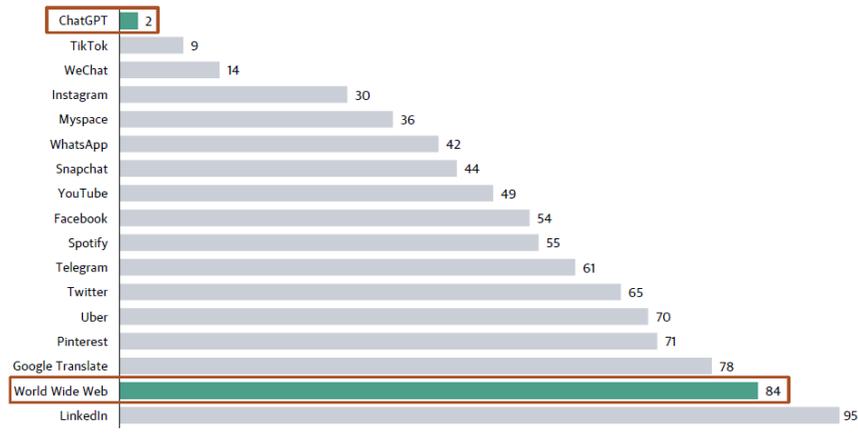Source: LSEG Data & Analytics, Bloomberg, Barclays Research

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AI has become a critical driver of the Top 10 stocks and had a major impact on the overall U.S. stock market performance. The next chart shows the pace of adoption over the past two decades of major technology platforms/applications and how many months it took each of them took to reach 100 million users. The massive adoption of AI-related models like ChatGPT (OpenAI and other AI models include Gemini, Claude, DeepSeek, Llama, and Grok) happened almost instantly and reached 100 million users in just two months, an unprecedented achievement in the history of technology.

AI adoption is happening at unprecedented speed

Months to Reach 100M Active Users[1]

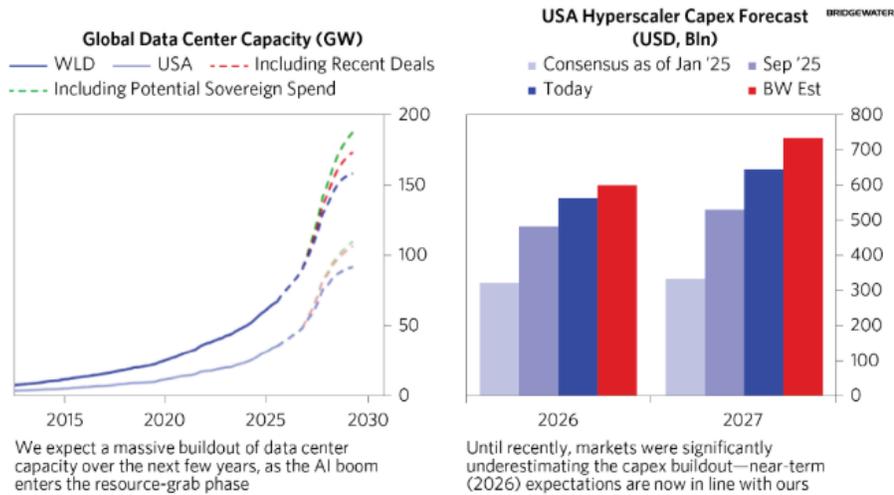| Platform	Months
ChatGPT	2
TikTok	9
WeChat	14
Instagram	30
Myspace	36
WhatsApp	42
Snapchat	44
YouTube	49
Facebook	54
Spotify	55
Telegram	61
Twitter	65
Uber	70
Pinterest	71
Google Translate	78
World Wide Web	84
LinkedIn	95

Note: There is no guarantee that the trends depicted herein will continue or will not reverse.
(1) Source: PwC, UBS, Threads as of July 2023 (latest available).

The importance of AI to the U.S. economy and the capital expenditures (capex) associated with building the infrastructure to support its growth cannot be understated. According to Bridgewater Associates, 1/3 of U.S. real GDP growth (excluding inflation) during 2025 came from AI capex. Without AI capex, and considering the weak U.S. consumer spending trends during 2025, the U.S. economy would have had much weaker economic growth than the 1.7% real GDP growth forecast by the Fed. While AI capex was a major contributor to the U.S. economy during 2025, the size of its contribution also means the U.S. economy is now subject to a greater level of risk if AI capex disappoints, especially given the expectations for a continued high level of AI capex in the years ahead.

Datacenters are where AI processing occurs. The left side of the next chart shows the explosive growth of AI datacenter capacity globally and in the U.S. that is forecasted by 2030. The right-side chart shows consensus expectations for 2026 and 2027 AI capex by the five major Hyperscalers including Alphabet/Google, Amazon, Microsoft, Oracle, and Meta/Facebook. At the beginning of 2025, the 2026 AI capex forecast was approximately $325 billion and by the end of the year (dark blue bars) it was $550 billion, an increase of $250 billion or a 69% increase in just 12 months. Also at the beginning of 2025, the consensus expectation for 2027 AI capex was also approximately $325 billion and today it is $650 billion, an increase of $325 billion or a 100% increase. These capex forecasts provide a clear indication of the accelerating buildout and adoption of AI. According to Bank of America, 2025 AI capex was approximately $400 billion and so the cumulative 2025-2027 AI capex is forecast to be $1.6 trillion. Goldman Sachs estimates that between 2025 and 2035, there will be a cumulative $7 trillion spent on AI in 10 years or an average of $700 billion per year. It should be noted that all the Hyperscalers say that AI demand exceeds supply by a wide margin and so it is the limitations of datacenter capacity and electricity availability that are constraining a faster rollout of AI. AI related infrastructure capex required to expand AI usage will be an important contributor to U.S. economic growth in the years ahead.

Global Data Center Capacity (GW)
— WLD   — USA   ---- Including Recent Deals
---- Including Potential Sovereign Spend

We expect a massive buildout of data center capacity over the next few years, as the AI boom enters the resource-grab phase

USA Hyperscaler Capex Forecast (USD, Bln) BRIDGEWATER
■ Consensus as of Jan '25   ■ Sep '25
■ Today   ■ BW Est

Until recently, markets were significantly underestimating the capex buildout—near-term (2026) expectations are now in line with ours

How has the stunning and rapid adoption of AI translated into the investment domain? The table below shows annual returns for the S&P 500 Index for the past five years and how much the Magnificent 7 stocks, which include the primary AI technology providers and Hyperscalers building out the AI capacity, contributed to the S&P 500 Index return by year. ChatGPT was introduced in the middle of 2022 and so for the past four years, the contribution to the S&P 500 annual return from the Magnificent 7 averaged 55%. While U.S. stock returns were extremely robust for four of the past five years, a disproportionate amount of the returns were attributable to just seven stocks. As a result, a lower percentage of stocks have outperformed the S&P 500 Index in recent years with the latest reading at only 35%.

Returns	'21	'22	'23	'24	'25
S&P 500	27%	-19%	24%	23%	16%
S&P 493	23%	-12%	11%	14%	13%
Mag 7	40%	-40%	76%	48%	23%
Return share*	33%	56%	63%	55%	46%

Source: JP Morgan Asset Management

Stocks beating SPX, 1y rolling
35%
Daily
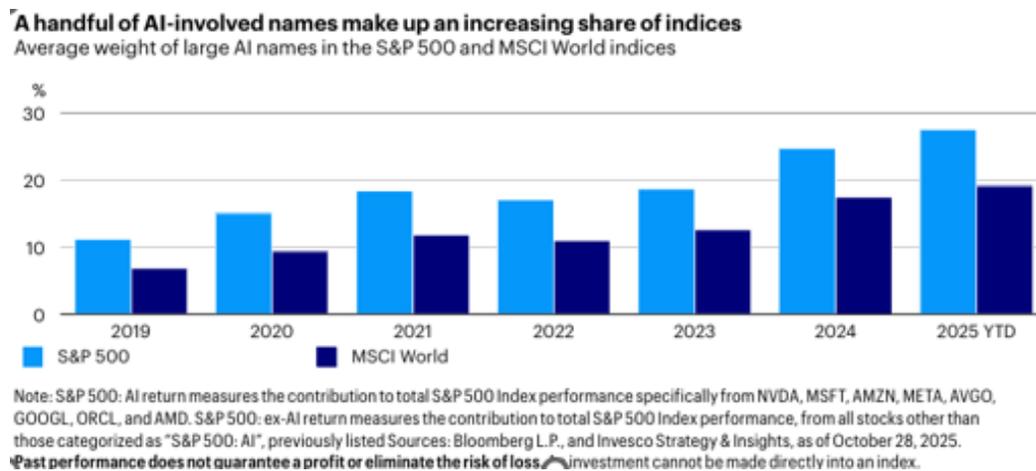
Data as of 01/13/2026
Source: LSEG Data & Analytics, Bloomberg, Barclays Research

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The next chart shows the cumulative weight of eight AI related U.S. stocks (see the note for the tickers) in both the S&P 500 Index and in the MSCI World Index, which captures all global stock markets. Since the introduction of Chat GPT in 2022, the weight of these eight stocks has dramatically increased in just four years in both benchmarks.   For the S&P 500 Index, the weight increased from 17% in 2022 to 28% in 2025. For the MSCI World Index, the weight increased from 11% in 2022 to 19% in 2025. It's mind-boggling to consider that only eight stocks represent nearly 20% of the world's stock market capitalization and primarily due to global investors willing to pay a high premium to have AI exposure in their portfolios. AI has not only had a dramatic impact on returns but also on the increased concentration of weight of a select group of AI-related stocks in major stock benchmarks. Even as AI has been an overwhelmingly positive to stock market returns the past several years, it is important to keep in mind that the risks associated with AI have also substantially increased given the concentrated weight of AI stocks in the major benchmarks.

A handful of AI-involved names make up an increasing share of indices
Average weight of large AI names in the S&P 500 and MSCI World indices

Note: S&P 500: AI return measures the contribution to total S&P 500 Index performance specifically from NVDA, MSFT, AMZN, META, AVGO, GOOGL, ORCL, and AMD. S&P 500: ex-AI return measures the contribution to total S&P 500 Index performance, from all stocks other than those categorized as "S&P 500: AI", previously listed Sources: Bloomberg L.P., and Invesco Strategy & Insights, as of October 28, 2025. Past performance does not guarantee a profit or eliminate the risk of loss. An investment cannot be made directly into an index.

2026 is a mid-term election year.   Since 1974, during mid-term election years, U.S. stock returns have averaged low single-digits, well below the long-term historical average of 10.5%. A major reason is that mid-term elections introduce more uncertainty about whether the current Administration's policies that were moved forward during its first two years will continue if there is a change in control of either the Senate or House of Representatives. Given how divergent the policies of the two political parties have become in the past decade, a change of political control poses a greater risk of increased market volatility and investor uncertainty. Mid-term election years typically experience large stock market drawdowns too. The next chart shows the intra-year drawdown in 20 mid-term election years going back to 1946. The average drawdown is 18%. It's important to highlight that during its first year, the Trump Administration has been able to pass very pro-growth economic policies (OBBBA, deregulation) and benefited from 0.75% of interest rate cuts by the Fed. If control of either the House or Senate flip, additional pro-growth economic policies are probably dead in the water for the last two years of his administration and could become a major headwind to U.S. stocks. Stock market volatility is likely to increase in the second half of 2026 as the mid-term election draws nearer and outcome takes on more prominence.

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Midterms Bring Selling Pressure
The average intra-year drawdown during midterm elections is 18%

■ S&P 500 Index

Source: CFRA

Bloomberg
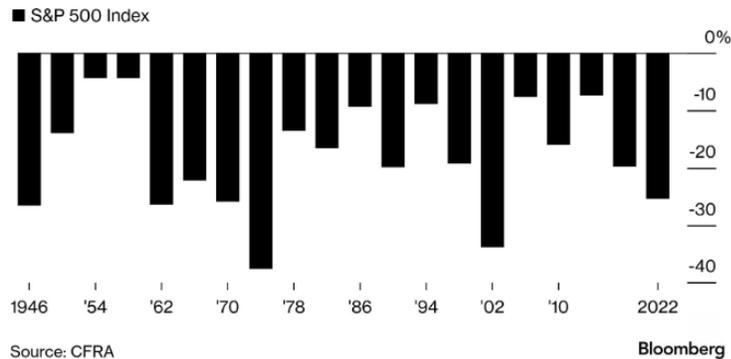
Soon, President Trump will nominate a new Chair of the Federal Reserve, a term that last four years. The President makes the Fed Chair appointment, but the appointee needs to be approved by Congress. The two mostly likely finalists are Kevin Warsh and Kevin Hassett, with the latter considered more tied to President Trump and his desire for the Fed to cut interest rates. However, most financial market participants strongly prefer an independent Fed Chair, which outgoing Fed Chair Jerome Powell has been.

Even though President Trump wants to appoint someone who strongly supports additional interest rate cuts, the bond market has a way of making its preference known via the bond yield curve. If the bond market believes the new Fed Chair will push hard for additional interest rate cuts, even if economic conditions don't warrant them, then bonds will get sold, pushing yields higher for longer maturity bonds (mostly 10-to-30-year maturities). Higher bond yields not only make U.S. Treasury borrowings more expensive but also create a headwind for stock market performance because of downward pressure on valuations from higher interest rates.

The bond market has a strong influence on government fiscal and monetary policies, a term coined bond vigilantes by Ed Yardeni of Yardeni Research. The most famous quote related to the bond market's power to dictate policy decisions was made by James Carville, President Clinton's policy advisor, who said, "I used to think that if there was reincarnation, I wanted to come back as the president or the pope or as a .400 baseball hitter but now I would like to come back as the bond market. You can intimidate everybody." Treasury Secretary Scott Bessent is acutely aware that bond vigilantes are ready to act if Trump's Fed Chair selection appears to be a rubber stamp appointee. The U.S. federal government is running historically high fiscal deficits, despite a non-recessionary economy, and outstanding federal debt now exceeds $38 trillion (!!!!) and annual interest on the federal debt approaching $1 trillion. Bond vigilantes are not in any mood to see their bond holding values negatively impacted by a weak Fed Chair appointee who bends the knee to the President as opposed to adhering to proper monetary policy decisions dictated exclusively by U.S. economic conditions.

Based on a recent public comment made by President Trump, with Mr. Hassett in the audience, it does not appear that Mr. Hassett will be the next Fed Chair. The bond vigilantes spoke and President Trump got the message. However, it is not clear that Mr. Warsh is now the presumptive choice either.

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Summary

The past ten years have richly rewarded investors with U.S. large/mega cap stock exposure. Returns have been substantially above the long-term stock market return average, especially the past three years when AI euphoria had a significant positive impact on U.S. large / mega cap tech stocks. To keep the hot streak going and to achieve another double-digit gain in 2026, multiple factors need to align positively. The bar is much higher, not only because U.S. stock valuations are in the top decile of their history, but also because the U.S. stock market has also become more concentrated in and dependent upon a select group of AI related tech stocks and their ability to meet or exceed expectations.   In addition, U.S. economic growth in 2026 has also become more dependent upon another big year of AI related capex spending. Other important factors that could impact the U.S. stock market in 2026 are the mid-term election outcome and choice of Federal Reserve Chair. You gotta believe multiple factors come out on the positive side of the ledger for U.S large/mega cap stock returns to continue dominate returns and propel U.S. stocks to a 4th straight year of double-digit gains.

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