2026 EDITION

Outlook

CAPITAL GROUP®

Long-term perspective on markets and economies

2026 Outlook

Heading into a new year, I always have mixed feelings of excitement and unease. I'm excited about the investment opportunities emerging before our eyes, such as the incredible advances in the realm of artificial intelligence. At the same time, I'm uneasy over the lofty stock market valuations driven primarily by that same group of AI-related stocks. In this one corner of the stock market, we have a microcosm of the issues facing investors in 2026 and beyond.

How should we address these risks and opportunities? In my view, it always comes back to balance. We are moving from a binary market environment in which U.S. tech stocks dominated returns to a more balanced one with a broadening opportunity set. That means investing in the U.S. and international markets, growth and value, cyclical and secular trends, stocks and bonds. We're seeing solid value these days in fixed income, where investors can generate healthy returns with much lower volatility than stocks. Bonds are an excellent way to help smooth out the ride for investors worried about the risk of highly valued technology stocks.

> "We are moving to a more balanced market environment with a broader opportunity set."

Martin Romo
Chair and Chief Investment Officer
Capital Group

The resurgence of international stocks is a good example of what I mean when I talk about a broadening market. Yes, the S&P 500 Index has done well, up nearly 18% so far this year. But Japan is up 24%. Europe is up 30%. And emerging markets 30%* as well. It's been a long time since we've seen such a sustained rally outside the U.S., and it's a good reminder why diversification is so important. Even within the U.S., returns have been powered in recent quarters by a wider set of companies, not just the Magnificent Seven.† Today opportunities and risks are everywhere.

Over the next 20 pages, we'll delve into many market-driving issues, including the uncertainty over trade and tariffs, the challenge of high valuations, the outlook for corporate earnings, and the debate over whether we're experiencing an AI bubble. On the fixed income side of the market, we'll explore how sticky inflation and weakening labor markets are influencing the path of interest rates. And we'll wrap it up with a brief overview of investment themes and how they're influencing various asset classes.

Everything in this report is underpinned by The Capital System™ – our investment process that combines collaborative research with diverse perspectives and a long-term view. With that in mind, I invite you to read and share our 2026 Outlook report.

Footnotes:

*Market returns are quoted on a year-to-date basis as of November 30, 2025, for the S&P 500 Index, the MSCI Europe Index, the MSCI Japan Index and the MSCI Emerging Markets Index. Past results are not predictive of results in future periods.

†The Magnificent Seven refers to a group of seven dominant U.S.-based technology companies: Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA and Tesla.

Investments are not FDIC-insured, nor are they deposits of or guaranteed by a bank or any other entity, so they may lose value.

The global economy shows its resilience

Variable	Global growth	U.S. economy	European economy	Fed policy	Inflation	Currency
Capital Strategy Research (CSR) view	Real GDP growth **2.3% to 2.5%**	Real GDP growth **1.6% to 2.2%**	Real GDP growth **1.4%**	**3%**	**3% to 3.3%**	**USD weaker**
Market consensus	**3.1%**	**2.1%**	**1.1%**	**3%**	**2.6%**	**USD weaker**
Summary of CSR view	U.S. and European growth trajectories are converging, as the U.S. slows and EU benefits from fiscal tailwinds. China shows signs of stabilizing, and Japan is on track for fiscal expansion.	Tariffs and job market weakness could still create a drag in the first half of the year, but AI spending and favorable policies suggest the potential for upside surprises.	Euro-area growth and inflation could be slightly higher than last year. ECB to hike rates and BoE to cut rates in 2026. No end to the fiscal woes in the U.K. and France.	A dovish Fed is likely to continue with rate cuts, responding to labor market weakness.	Likely to remain above the Fed's target but could drift downward if one-off price increases from tariffs wane or economic activity weakens.	The dollar will weaken as rates in the U.S. come down and growth moderates.

Resilience looks like the overarching economic theme for 2026, after a year of uncertainty and slowing growth.

In our view, investors should expect improved economic stability in the year ahead, with the potential for reacceleration in the second half, as the path of global trade comes into clearer focus. The U.S. has negotiated trade deals with many countries, and tariffs generally have settled at much lower rates than initially feared.

"The clearer picture on tariffs should free up businesses to make capital decisions, like investing in reshoring supply chains," explains U.S. economist Jared Franz.

Elsewhere, the European economy is experiencing a resurgence, driven by increased fiscal spending, higher defense budgets and currency tailwinds. "Germany's substantial loosening of fiscal policy is a positive for growth, but it could also lead to renewed inflationary pressure," says Europe economist Beth Beckett. "I think the European Central Bank could be an outlier in 2026, hiking rates while many other central banks are cutting."

In Asia, China is showing signs of stabilizing, and Japan should be back on track for sustained reflation – better growth and higher inflation – in the second half of the year.

Sources: Capital Group, Bloomberg, International Monetary Fund (IMF) World Economic Outlook October 2025. Market consensus figures are derived as follows: real GDP growth estimates from the IMF for 2026 for the World, United States and Euro Area (real GDP growth); market-implied effective Fed Funds rate for December 2026 (Fed policy); one-year breakeven yield on Treaury-Inflation Protected Securities (inflation); consensus estimates for the U.S. Dollar Index value as of December 2026 (currency). GDP: Gross Domestic Product, CSR: Capital Strategy Research, BoJ: Bank of Japan, BoE: Bank of England. Figures reflect latest available data as of November 30, 2025.

Bold stimulus could boost the world economy

USA

Easy money
Lower interest rates, end of QT

Tax reform
Retroactive tax refunds
Made in USA incentives

Deregulation
Lower government oversight

EUROPE

German fiscal stimulus
€500 billion infrastructure and defense spending package

NATO defense spending
Members target
5% of GDP from 2%

ASIA

Corporate reform
Japan, Korea and China push to improve shareholder value

China stimulus

Signs of a global economic revival are emerging. Confronted with slowing growth and high trade barriers, governments worldwide are rolling out bold stimulus.

In the U.S., a dovish Federal Reserve is cutting borrowing costs – a tailwind for U.S. housing and the broader economy. Lower rates could lift demand for high-paying construction jobs, as well as materials like lumber and paint, benefiting companies like Home Depot and Sherwin-Williams.

Deregulation could increase lending activity, helping banks like Wells Fargo and supporting companies left out of the artificial intelligence boom.

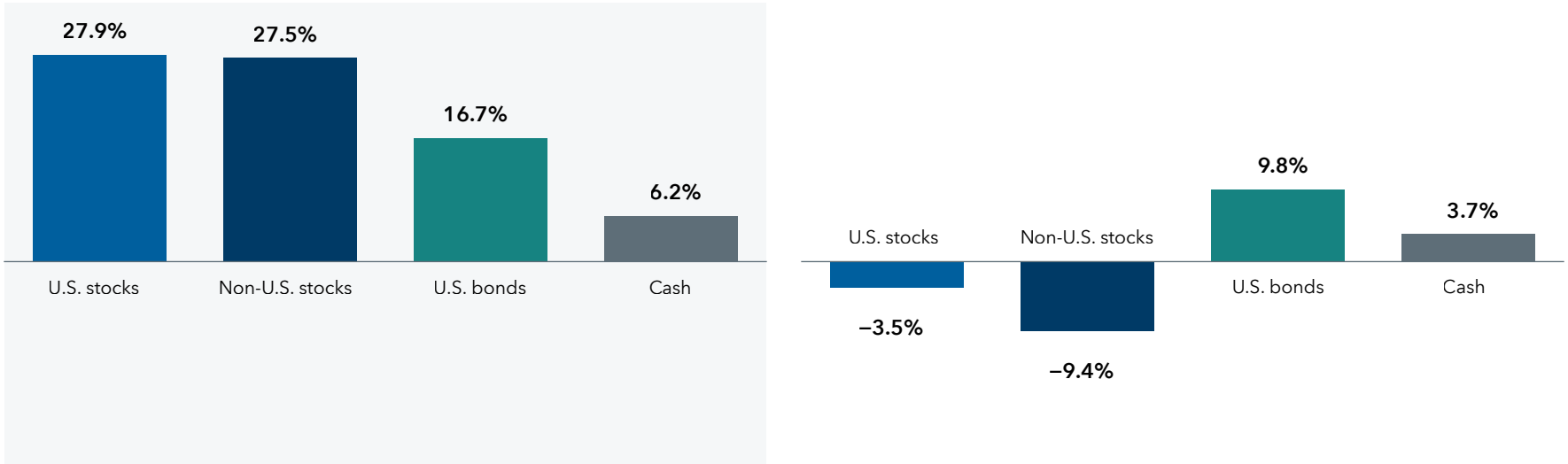
The One Big Beautiful Bill Act aims to supercharge U.S. manufacturing, helping industrial and technology sectors. Across the Atlantic, Germany has shelved fiscal restraint, unveiling a €500 billion package for infrastructure and defense. The move could boost earning potential for construction companies like Heidelberg Materials and arms manufacturer Rheinmetall.

NATO allies are likewise pledging to raise defense spending, generating even greater demand for the systems and products made by Northrop Grumman and Rolls-Royce. Japan is pushing corporate reform to unlock shareholder value, impacting companies like insurance provider Tokio Marine. Korea and China are similarly following suit. China also has introduced stimulus measures aimed at stabilizing its economy.

Source: Capital Group. As of November 30, 2025. QT, or quantitative tightening, refers to policies that reduce the size of the Fed's balance sheet.

Fed easing cycles can be good for both stocks and bonds

Average annualized returns across past seven Fed easing cycles



Despite stubborn inflation, interest rates appear set to fall in 2026 as the Federal Reserve focuses on sluggish job growth. "The Fed is worried about the labor market because historically, a weak job market leads to an economic slowdown," says bond portfolio manager Pramod Atluri. "Meanwhile, more stable tariff policies should help ease inflationary pressures."

The U.S. federal funds rate is expected to end 2026 near 3%, a level Atluri describes as neither stimulating nor restricting economic growth. The rate influences borrowing costs worldwide, and lower rates could support consumer spending. Historically, Fed easing cycles that occurred outside of a recession have lifted stock and bond markets, while cash lagged.

The Fed is cutting as AI spending ripples through the economy, alongside tariff concerns and labor market softness. "There's healthy debate over whether U.S. economic growth will slow or accelerate because of these forces," Atluri explains. "We may be entering an unusual scenario where U.S. gross domestic product accelerates well above 2% to 3%, even as job creation remains weak or turns negative. At the same time, unemployment could stay relatively low due to fewer layoffs and stricter immigration enforcement, reducing the overall number of workers."

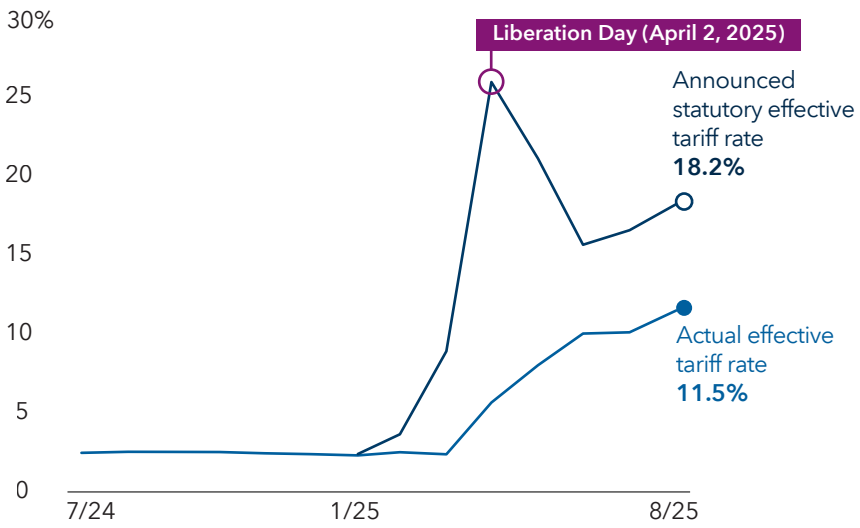
President Trump is also preparing to pick a new Fed chair, a move expected to shift the central bank toward a more dovish policy stance.

Sources: Capital Group, Bloomberg, Morningstar, Standard & Poor's. Returns reflect annualized total returns from the peak federal funds rate target to the lowest federal funds rate target for each cycle. Specific non-recessionary cutting cycles include: August 1984-August 1986, February 1995-January 1996, March 1997-November 1998. Recessionary cutting cycles include: May 1989-September 1992, May 2000-June 2003, June 2006-December 2008 and December 2018-March 2020. Benchmarks used are the S&P 500 Index (U.S. stocks), MSCI World ex USA Index (international stocks), Bloomberg U.S. Aggregate Index (U.S. bonds) and 3-month U.S. Treasury Bills (cash). Past results are not predictive of results in future periods. As of November 30, 2025.

Less policy uncertainty should support business confidence

Tariffs aren't as high as first expected

July 2024–August 2025



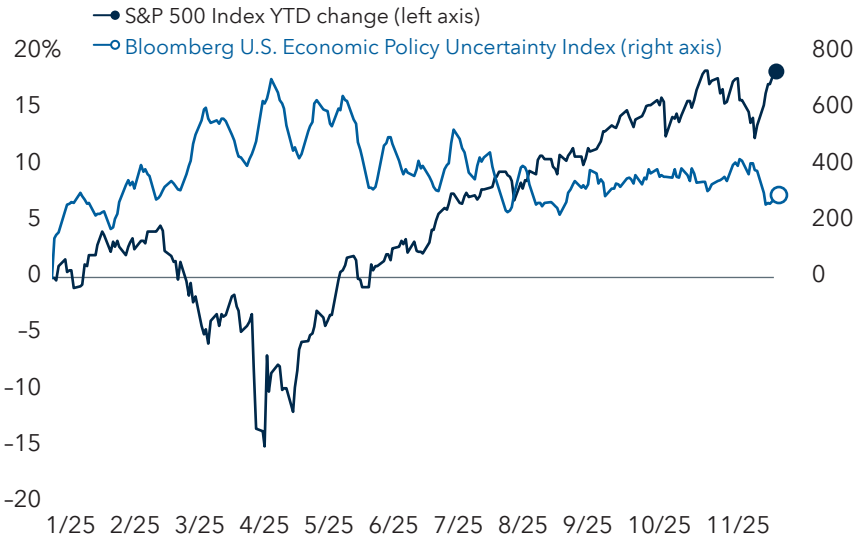
Raise your hand if you saw this coming: In April, President Trump unleashed the highest tariffs in nearly 100 years against every U.S. trading partner in what he called "Liberation Day." Stocks initially fell sharply, then reversed course and staged a remarkable months-long rally.

How that happened remains up for debate. But a big part of the reason is that policy uncertainty, which peaked in April, gradually declined over the ensuing months as world leaders announced new trade deals, Trump backed away from some of his threats, and investors concluded that tariff rates might not be as onerous as previously thought. In fact, the actual effective U.S. tariff rate has hovered around 11% in recent months, far lower than expected.

Sources: Capital Group, The Yale Budget Lab, U.S. Census Bureau, U.S. Department of the Treasury. Latest data available through August 2025 as of November 30, 2025. Announced statutory tariff rate is the legally specified tax on imports by a government whereas the actual effective tariff rate is based on the actual tariff revenue collected by the government divided by total import value.

Declining policy uncertainty has boosted markets

Cumulative percentage change YTD: U.S. stocks vs. trade policy uncertainty



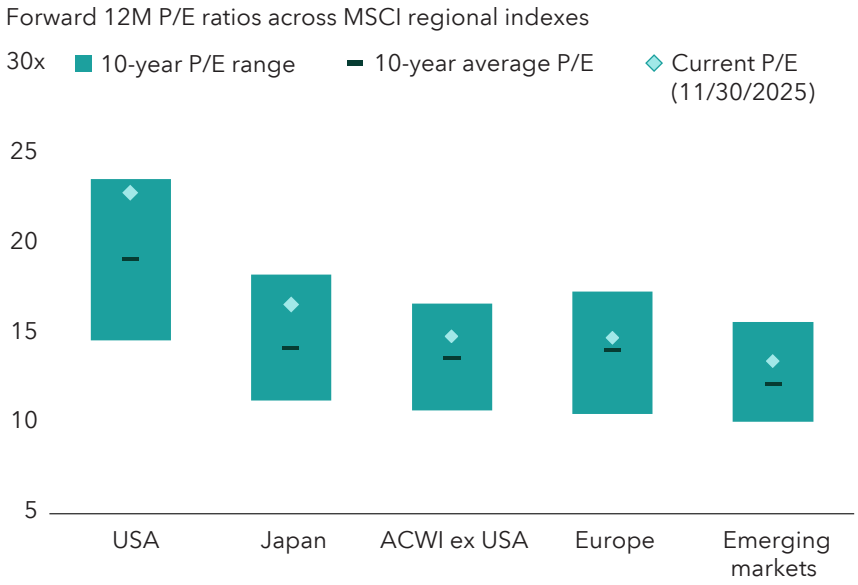
U.S. recession worries, widespread in April, have calmed and markets have reflected that shift. This positive investor sentiment could continue to boost stocks, as the U.S. economy avoids a downturn and grows at a moderate pace.

"It would probably take something akin to 'Liberation Day: Part Two' to really sink the U.S. economy," says Capital Group economist Tryggvi Gudmundsson. "The policy uncertainty has dissipated and markets have moved on. While it's likely that trade drama will flare up as new tariffs emerge, it will hopefully come with fewer market fireworks."

Sources: Capital Group, Bloomberg, RIMES, Standard & Poor's. Bloomberg U.S. Economic Policy Uncertainty (EPU) Index data calculated as a rolling seven-day average using daily index values. S&P 500 returns calculated as total returns. Bloomberg U.S. Economic Policy Uncertainty Index measures U.S. economic policy uncertainty by counting newspaper articles on the topic. Past results are not predictive of results in future periods. Data as of November 30, 2025.

A market pullback in 2026 would not be surprising

Valuations are elevated across global markets



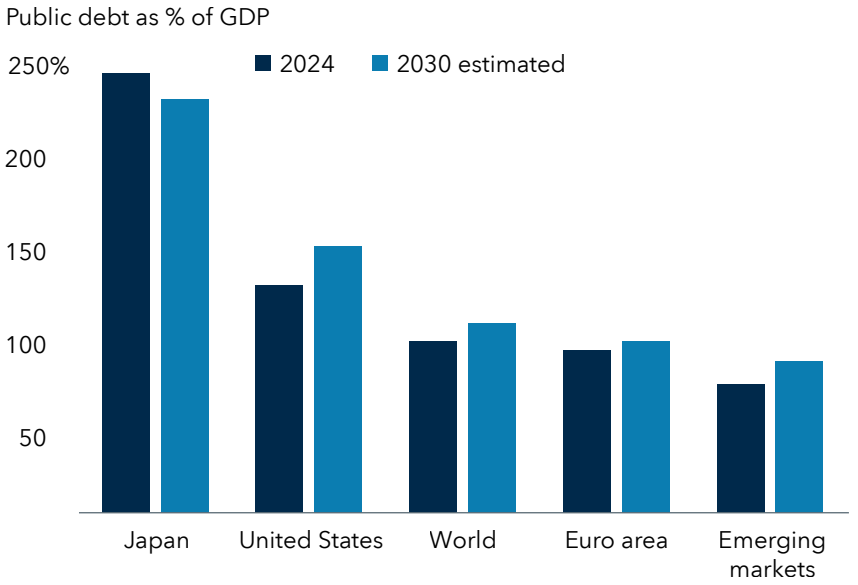
Although there are encouraging signs for the year ahead, clear risks are on the horizon, suggesting that investors should prepare for potential market pullbacks.

For starters, stocks are expensive. Most equity markets around the world have generated strong double-digit annualized returns over the past three years. While company earnings have generally been solid, price-to-earnings ratios (the ratio of a company's share price to the company's earnings per share) for U.S., developed international and emerging markets were all above their 10-year averages at the end of November 2025.

"The optimism priced into markets doesn't leave a lot of room for disappointment," notes U.S. economist Darrell Spence.

Sources: Capital Group, MSCI, RIMES. As of November 30, 2025. Countries and regions shown are represented by their respective MSCI indexes. The forward price-to-earnings (P/E) ratio divides the current share price of a company by the estimated future earnings per share of that company. References on this page to price-to-earnings ratios denote forward 12-month P/E ratios, which are based on latest consensus estimates.

Public debt is projected to continue rising in the U.S.



Sticky inflation and mounting government debt in the U.S., Europe and elsewhere are also cause for concern. Aggressive stimulus supporting growth in 2026 will only contribute to debt levels, with the total for the U.S. expected to exceed 140% of GDP by 2030.

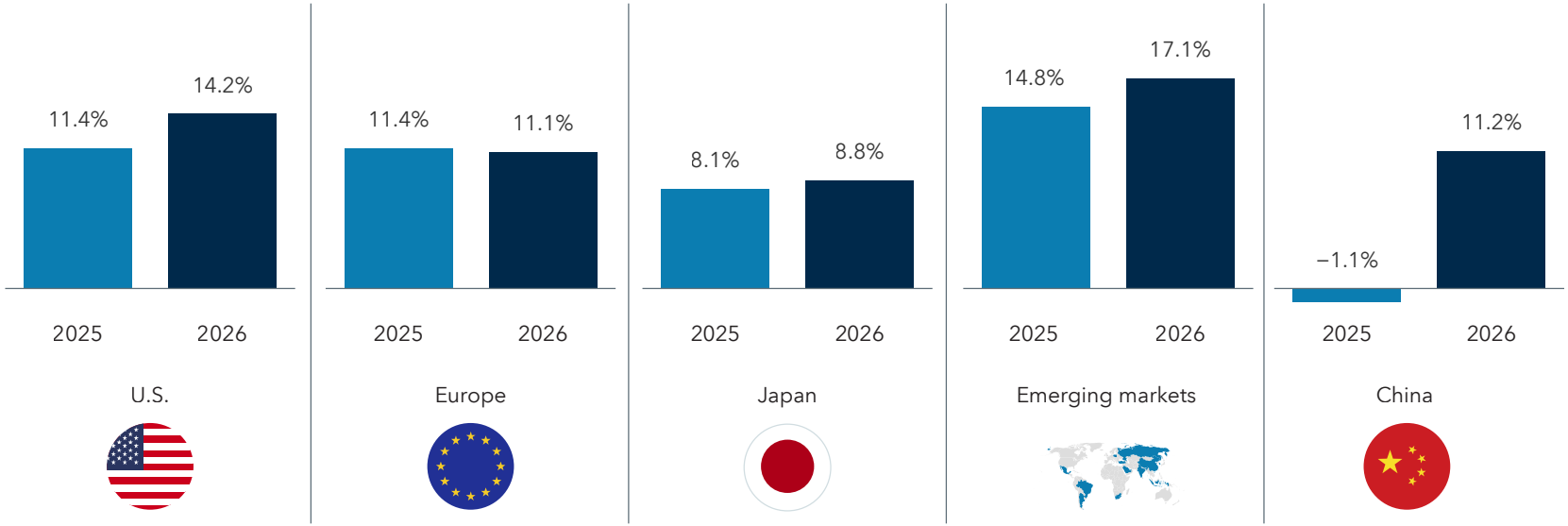
"There will almost always be the unanticipated surprises that occur every year, even when the outlook is positive," adds Spence.

Stock market declines are regular occurrences. The S&P 500 Index has experienced market corrections, or declines of 10 percent or more, about once every 16 months, whereas the index has had bear markets, or declines of 20 percent or more, about once every six years, according to market data from 1954 to 2025.

Sources: Capital Group, International Monetary Fund (IMF). Public debt as % of GDP estimates are sourced from the IMF's World Economic Outlook, October 2025, published October 14, 2025. The S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks.

Company profits are expected to rise across the globe

Estimated annual earnings growth across select global benchmarks



If 2025 was the year that tariff-induced uncertainty upended the outlook for corporate earnings, 2026 could be the year those numbers come back into focus.

Consensus earnings estimates for the new year are looking brighter, largely due to declining interest rates, government stimulus and a string of recently announced trade deals that have reduced policy uncertainty. Financial markets have responded by rallying off the lows of April, when the fear of sky-high tariffs reached its peak.

Another significant driver is the artificial intelligence boom, which has spurred strong demand for computer chips, data centers, and related spending on high-tech and low-tech equipment to support the buildout of AI infrastructure.

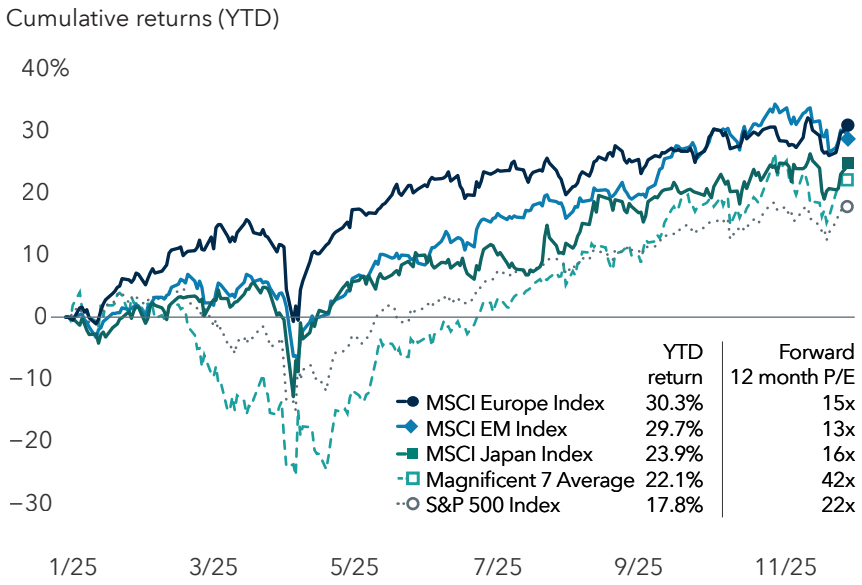
Emerging markets are expected to enjoy the strongest earnings growth, rising 17.1%, while the United States comes in just over 14% and Europe slightly above 11%.

Looking ahead, there are some powerful tailwinds that should drive earnings growth and support market gains beyond the tech sector, according to equity portfolio manager Diana Wagner, who singles out industrials, financials and consumer discretionary companies, among others. "There is a lot of support from a macroeconomic perspective but, ultimately, what's going to matter is corporate earnings growth."

Sources: Capital Group, FactSet, MSCI, Standard & Poor's. Estimated annual earnings growth is represented by the mean consensus earnings per share estimates for the years ending December 2025 and 2026, respectively, across the S&P 500 Index (U.S.), the MSCI Europe Index (Europe), the MSCI Japan Index (Japan), the MSCI EM Index (Emerging markets) and MSCI China Index (China). The S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks. Estimates are as of November 30, 2025.

Markets are broadening – a good sign for investors

Non-U.S. markets have outpaced the Magnificent 7



The dominance of the Magnificent Seven stocks may have passed its peak.

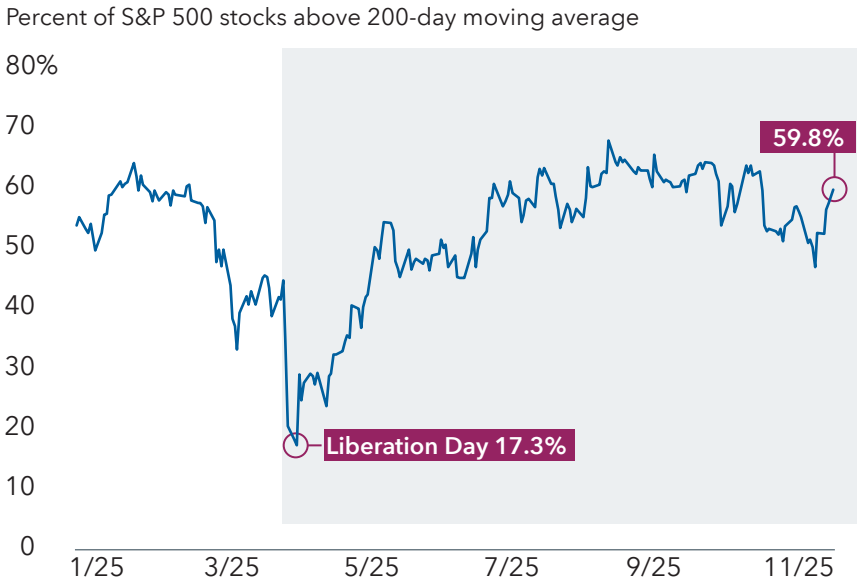
Global equity markets are broadening, with more companies driving returns outside the small handful of U.S. technology stocks associated with artificial intelligence.

Since April 2025, when the U.S. announced new tariffs on most trading partners, major non-U.S. markets have outpaced both the Magnificent Seven (Alphabet, Amazon, Apple, Meta, Microsoft, NVIDIA and Tesla) and the S&P 500 Index. This trend could continue as governments in Europe inject infrastructure and defense spending into their economies, and corporate reforms in Japan and other Asian economies boost companies.

Sources: Capital Group, FactSet, MSCI, Standard & Poor's. Fwd 12M P/E = forward 12-month price-to-earnings ratio. Returns reflect total returns in USD. PE ratio for the Magnificent 7 is the market-cap weighted average as of November 30, 2025. Data shown is from January 1, 2025, through November 30, 2025.

Past results are not predictive of results in future periods.

More U.S. stocks have joined the market rally



Within the U.S., a greater number of stocks also have joined the market rally, with nearly 60% of S&P 500 companies trading above their 200-day moving averages as of the end of November 2025.

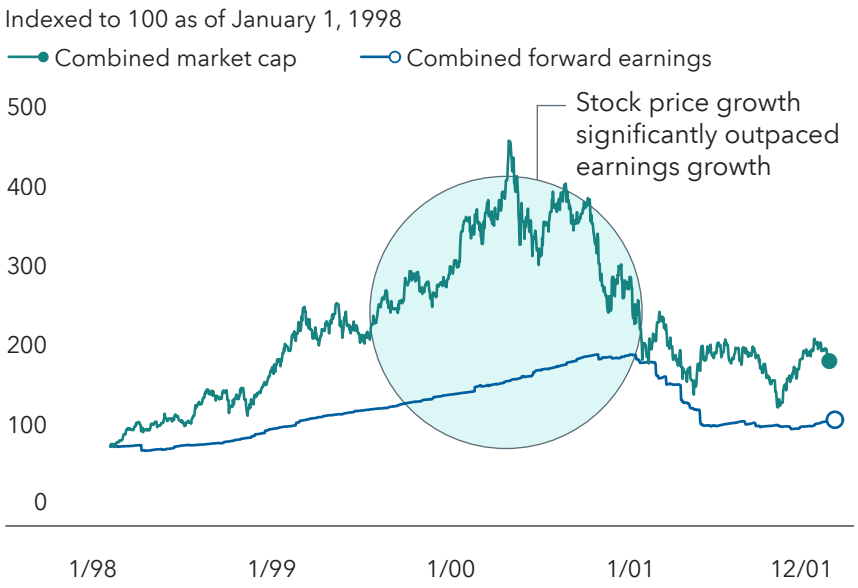
"Market broadening is an ideal environment for stock pickers like me," says equity portfolio manager Charles Ellwein. "Today there is no shortage of investment opportunities, whether they be industrial companies benefiting from a new capital spending cycle, tech companies participating in the AI boom, or financials benefiting from potential regulatory reform in 2026."

Ellwein is also looking for opportunities in sectors that had little to no growth over the last few years, such as energy and transportation.

Sources: Capital Group, Bloomberg. As of November 30, 2025. Liberation Day is the nickname coined by President Trump to refer to April 2, 2025, the day the U.S. announced tariffs on international imports.

Artificial intelligence: Boom, bubble or both?

Dot-com era: Price vs. earnings (1998-2001)



Are we in an AI bubble? Investors have been struggling with that question for more than two years. With AI-related stocks rallying like it's 1999, comparisons to the days of "irrational exuberance" are everywhere.

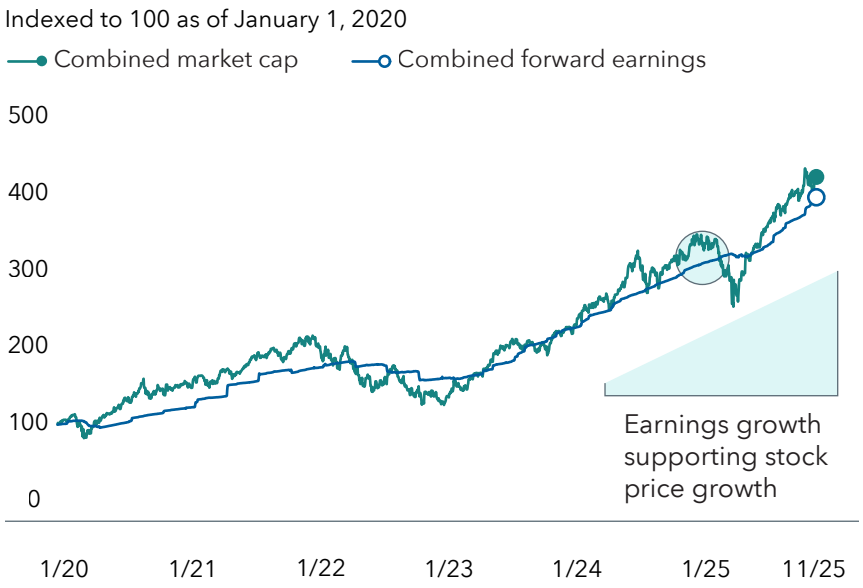
If there is a bubble in the making, it's important to determine where we might be on that late 1990s timeline. Is the year 2000 the appropriate analogy, which would imply a bubble is about to pop, or is it 1998, indicating that AI stocks still have room to run?

"I think we are closer to 1998 than 2000," says equity portfolio manager Chris Buchbinder, a former telecom analyst who experienced the dot-com euphoria. "It's possible we will see an AI bubble at some point, but I don't think we're there yet."

Sources: Capital Group, Bloomberg. Data aggregates forward 12-month net income ("forward earnings") and market capitalization ("market cap") for the "Four Horsemen" of the dot-com era: Microsoft, Cisco, Intel and Dell, four of the largest and best performing companies of that period. Indexed to 100 on January 1, 1998.

Past results are not predictive of results in future periods.

AI era: Price vs. earnings (2020-present)



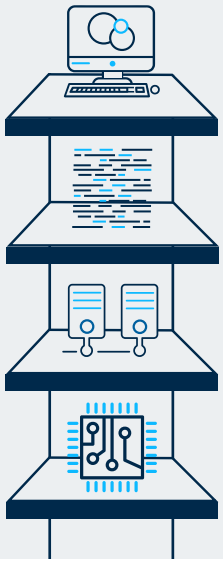
Today, stock prices for AI leaders are generally supported by solid earnings growth. What's more, companies making aggressive AI-related investments – Alphabet, Amazon, Broadcom, Meta, Microsoft and NVIDIA, among others – can support their massive capital spending far better than the upstarts of the late 1990s.

"In my view," Buchbinder adds, "it's too early to let the risk of a bubble overcome the compelling opportunities presented by this formidable technology."

Sources: Capital Group, Bloomberg. Data aggregates forward 12-month net income ("forward earnings") and market capitalization ("market cap") for NVIDIA, Microsoft, Apple, Amazon, Meta, Broadcom and Alphabet, seven of the largest AI-exposed companies. Data indexed to 100 on January 1, 2020. As of November 30, 2025.

AI opportunity set expands across the economy

AI tech stack



Applications
Microsoft Copilot
Alphabet Gemini
Salesforce

Models
Alphabet
OpenAI

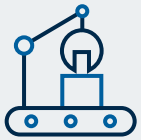
Infrastructure
Microsoft
Amazon
Arista Networks

Semiconductors
NVIDIA
Broadcom
TSMC

Secondary beneficiaries

Materials
Freeport-McMoRan,
BHP, Glencore,
First Quantum

Utilities
Constellation Energy
Southern Company



Industrials
Modine, Vertiv,
GE Vernova,
Schneider Electric

Third-tier beneficiaries

Financials
JPMorgan Chase
Mastercard
Capital One

Media/Entertainment
Alphabet
Meta
Netflix

Health care
UnitedHealth Group
Eli Lilly
AstraZeneca

With hundreds of billions of dollars invested in just the past few years, the AI build-out continues at a staggering pace. As the work continues, which companies may be best positioned to benefit over the long term?

Three distinct areas of AI investment opportunity have emerged: the four layer technology stack that powers AI systems, companies providing infrastructure for operations, and organizations adopting applications to enhance productivity.

"Microsoft, Alphabet, Meta and others have the incentive and resources to continue investing aggressively, generating greater demand for advanced semiconductors and infrastructure," explains equity portfolio manager Mark Casey.

AI developers are also seeking alternate sources of power to meet their rapidly growing power needs. For example, the market for small modular nuclear reactors (SMRs) is expected to grow to $13.8 billion by 2032, creating opportunities for SMR makers such as Rolls-Royce, GE Vernova and Hitachi.

Already, companies from financials to health care to media have adopted AI to seek competitive advantages. For example, JPMorgan Chase reported in May that it has saved $2 billion using AI to generate operational efficiencies.

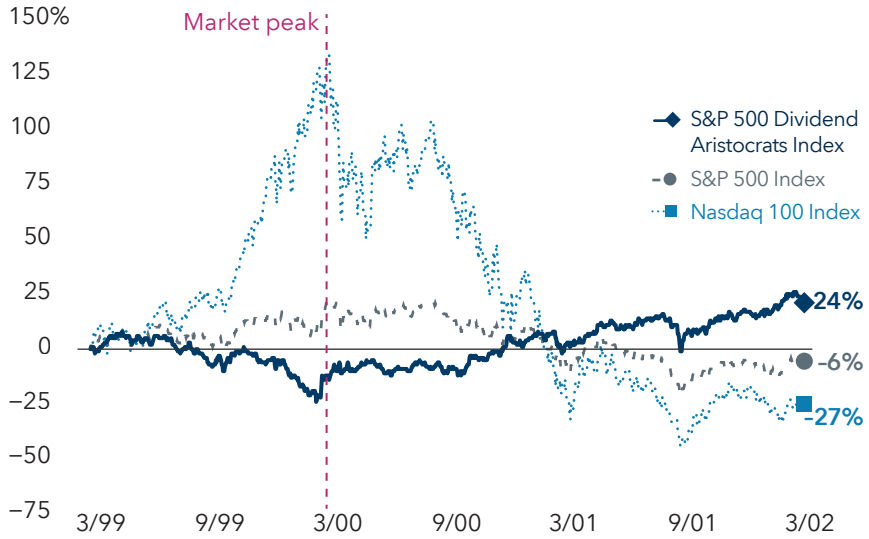
"We are still in the very early stages of both the development and deployment of AI," adds Casey. "Over the next decade, I expect AI to become pervasive in most software and hardware – and there will be many types of robots."

Source: Capital Group. AI tech stack represents Capital Group's interpretation of four layers of technology that enable AI to operate. Companies listed are examples of businesses that are among leaders of market share in each segment. TSMC is Taiwan Semiconductor Manufacturing Company. As of November 30, 2025.

Dividends can smooth the ride when markets are choppy

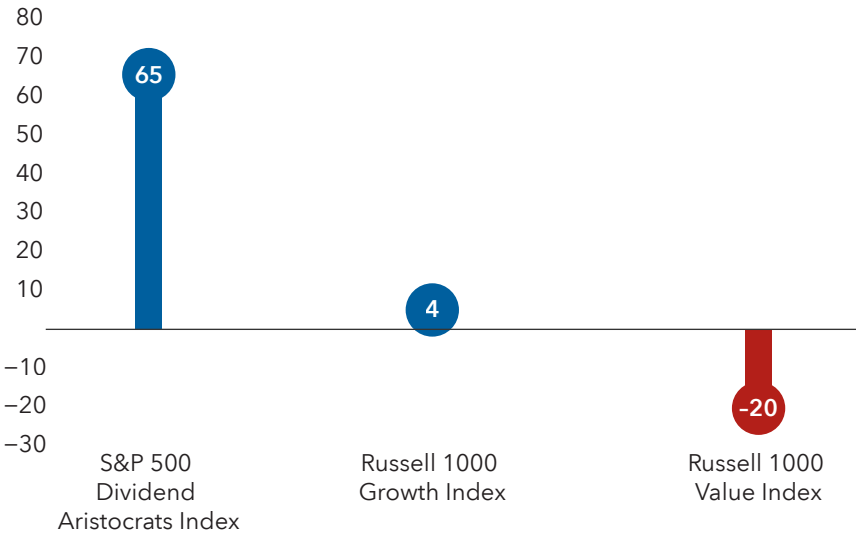
Dividend payers held up after dot-com fervor peaked

Cumulative total return % indexed to one year prior to dot-com bubble peak



Dividend payers outpaced the S&P 500 during declines

Average of monthly excess returns (bps) for 20 years ended 11/30/25



There are good reasons for continued enthusiasm over the AI-driven rally. But long bull markets – and periods of rapid innovation – periodically stall.

Investors would do well to remember the important role dividends can play in a stock portfolio. They have historically been resilient during market declines but have also generated positive returns when markets have advanced.

In periods that the S&P 500 Index declined over the 20 years ended November 30, 2025, the S&P 500 Dividend Aristocrats Index outpaced the broader market by an average 65 basis points. What's more, from the market peak following the 1990s tech bubble on March 31, 2000, through March 31, 2002, dividend payers generated positive returns while many tech companies and the overall market were negative.

"In my view, AI is going to transform the economy and will continue to be an important investment theme, but I also expect pullbacks along the way," says equity portfolio manager Brittain Ezzes. "While I maintain exposure to AI, I counterbalance the risk by looking in more defensive sectors for companies that could do well should markets falter."

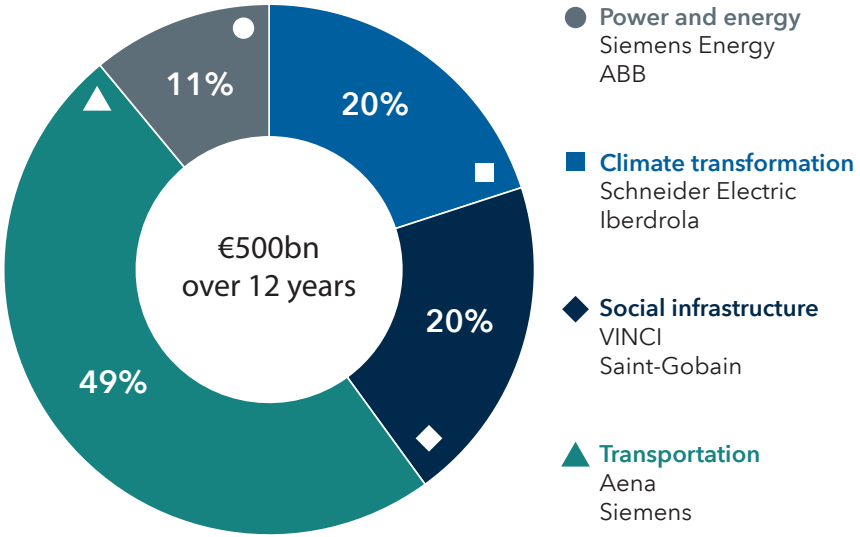
Today's universe of dividend payers includes companies like Starbucks and digital payment provider PayPal – that did not offer dividends when tech stocks dominated over 20 years ago. Technology giants Microsoft and Broadcom also pay substantial dividends today. What's more, investors can find dividend opportunities among companies across a range of sectors in markets outside the U.S.

Sources: Capital Group, Bloomberg, Nasdaq, Standard & Poor's. Dot-com bubble peak date used is March 24, 2000, the peak of the S&P 500 Index. Data shown is through March 24, 2002. Dividend payers are represented by the S&P 500 Dividend Aristocrats Index, which measures the performance of S&P 500 companies that have increased dividends the past 25 years. Past results are not predictive of results in future periods.

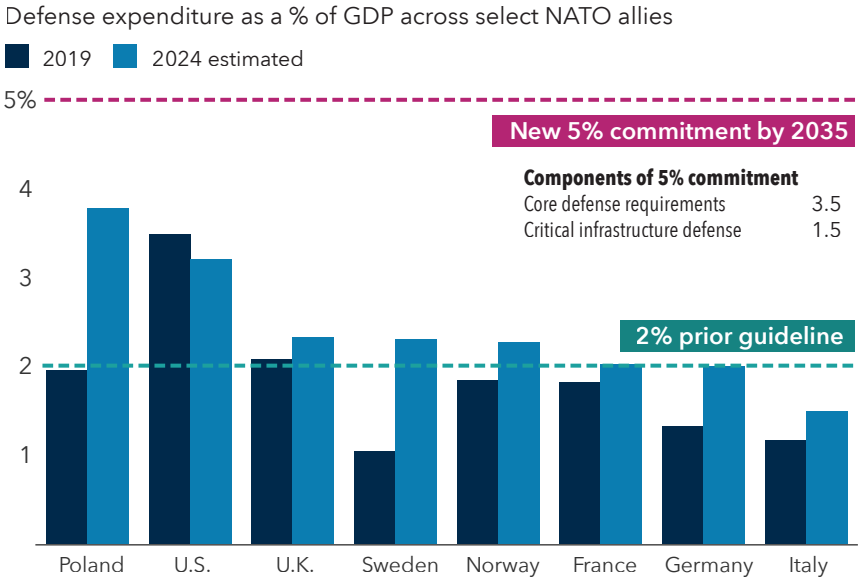
Sources: Capital Group, FTSE Russell, Morningstar, Standard & Poor's. Figures reflect the average difference in monthly total returns between the index specified and the S&P 500 Index, across all months in which the S&P 500 Index had a negative return. As of November 30, 2025.

Europe's investment wave could propel markets

Germany's stimulus unlocks growth potential



NATO commitments signal long-term tailwinds



Europe is investing in its future, and the results could be transformative.

Germany's bold €500bn infrastructure stimulus – roughly 12% of its gross domestic product (GDP) – is set to reshape Europe's economic landscape. With half the spending expected by 2029, the aim is to boost growth, spur competitiveness and strengthen regional security.

About 20% of the stimulus is earmarked for climate-related projects, which could provide opportunity for companies like Schneider Electric. With 81% of its revenue from energy management, including low-voltage distribution and automation, Schneider supports electrification across buildings, transport and infrastructure.

Germany's stimulus plans are likely to benefit a range of industrial companies, including businesses in the upper tiers of the value chain, such as industrial software developers. "Europe is home to prominent leaders in this field," explains equity portfolio manager Barbara Burtin. "For example, Siemens invests 8% of its sales into research and development, about twice that of U.S. peers," Burtin says.

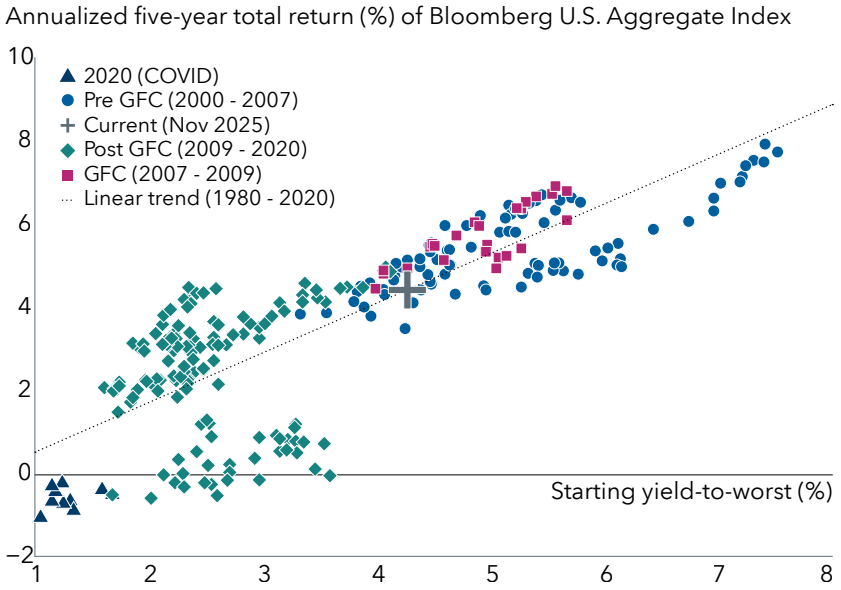
More broadly, NATO's pledge to raise defense spending to 5% of GDP by 2035 has sparked investor interest, but selectivity is key. Rolls-Royce's aerospace and defense division has delivered robust growth, but an escalating need for power generation could also boost demand for its small modular nuclear reactors.

Sources: Capital Group, German Bundestag proposed federal budget 2025, German Economic Institute, Federation of German Industries (BDI), Germany's Federal Office for Economic Affairs. Companies listed are meant to serve as examples only and represent the largest constituents by market cap within the MSCI Europe Index across their respective subindustries as of November 30, 2025.

Sources: Capital Group, NATO. Figures for 2024 are estimates based on most recently available data, as of November 30, 2025. New 5% commitment was announced June 27, 2025. Percentage of GDP is based on constant prices and exchange rates, indexed to 2021. Critical infrastructure defense consists of investments to defend networks, fund innovation and strengthen the defense industrial base.

Bonds should offer ballast

Starting yields often indicated long-term returns



Economic growth prospects are up, just as job growth is weakening. For investors, this unusual backdrop underscores the potential for bonds to offer steady income and a measure of downside protection.

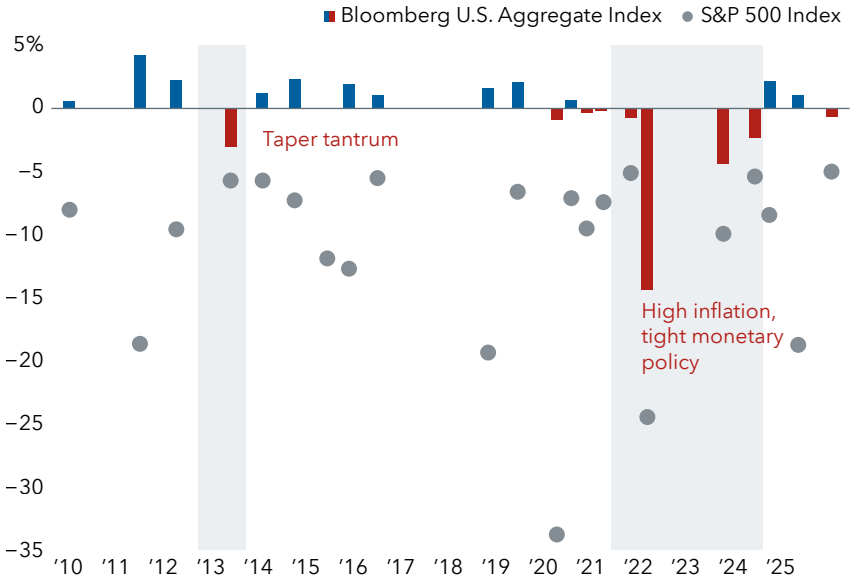
"The biggest question facing investors is whether the labor market weakness will weigh on consumption," says bond manager Chitrang Purani. "That would increase the risk of a sharper downturn in growth." Still, he expects ongoing interest rate cuts and accommodative fiscal and monetary policy will keep the economy steady in his base case.

Starting yields have historically been a strong indicator of long-term return potential. As of November 30, 2025, the Bloomberg U.S. Aggregate Index yielded 4.3%.

Sources: Capital Group, Bloomberg. Historical 5-year forward returns between 2007 and 2020. Dates for periods shown: Pre-GFC: 1/1/00-4/30/07; GFC: 4/30/07-4/30/09; Post-GFC: 4/30/09-2/28/20; COVID-19 pandemic: 2/28/20-10/31/20. Current yield as of November 30, 2025.

Past results are not predictive of results in future periods.

Bonds have offered balance when stocks declined



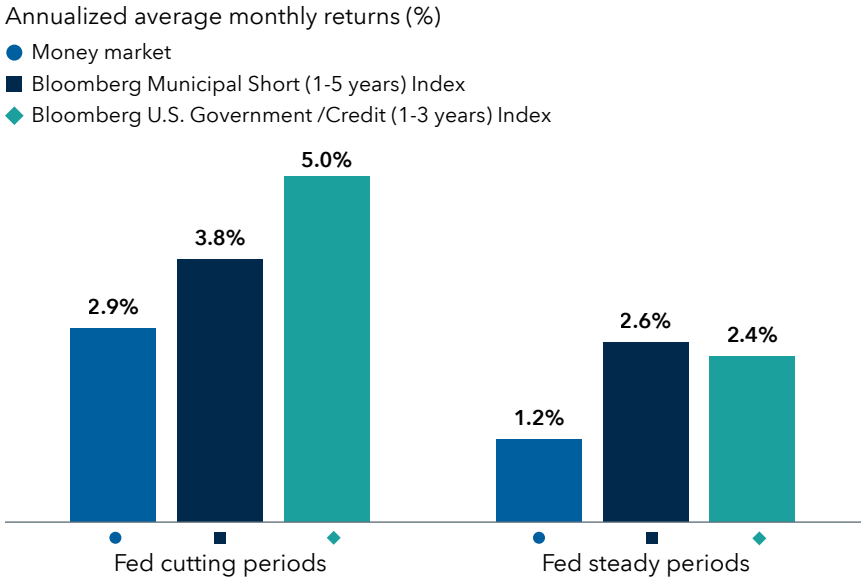
At today's valuations, Purani notes that high-quality bonds can play the dual role of generating income and acting as a buffer. In the event of a meaningful slowdown, the Fed has room to cut rates aggressively, potentially lifting bond prices. Historically, such rate-cutting cycles have delivered strong returns for high-quality bonds, reinforcing their role as a portfolio diversifier.

While Purani expects longer term interest rates to remain range bound in 2026, he cites opportunities in actively managing exposure along the Treasury yield curve, which could steepen in several scenarios, including both rising and falling interest rate environments.

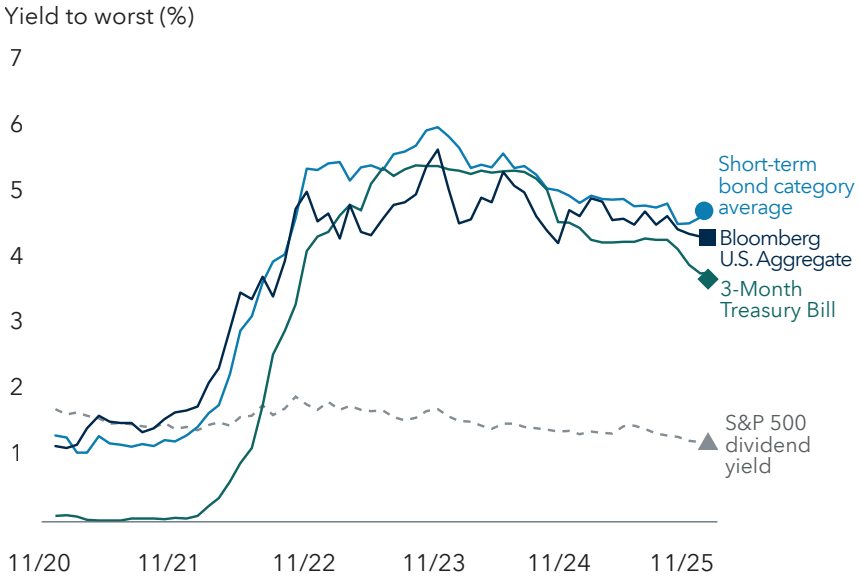
Sources: Capital Group, Bloomberg, S&P Global. As of November 30, 2025. Data reflects total returns across all S&P 500 drawdowns of 5% or greater since 2010. The 2013 "Taper tantrum" refers to the Fed's signal to reduce bond purchases as part of its quantitative easing policy following the global financial crisis (GFC).

Short-term bonds may offer income and defense

When Fed cut or held, short-term bonds beat cash



Short-term bond yields have shown relative strength



Economic uncertainty and stretched equity valuations are breathing new life into short-term bonds, once an overlooked segment of fixed income.

Their popularity comes as money market yields fall with Fed rate cuts. Short-term strategies can offer attractive yield and return potential relative to cash, with possible price appreciation from falling rates.

With duration — a measure of the price of a fixed income investment to a change in interest rates — under three years, they're also less vulnerable to anticipated upticks in interest rates. Moreover, short-term bonds can serve as a volatility reducer for investors looking to de-risk from equities or longer maturity investments while maintaining the potential for attractive income.

Historically, short-term bonds have outpaced cash during periods when the Fed cut or held rates steady. "Fed actions have a stronger impact on bonds with short maturities than other parts of the yield curve, and I believe the current easing cycle should continue to benefit the sector," says portfolio manager Vince Gonzales.

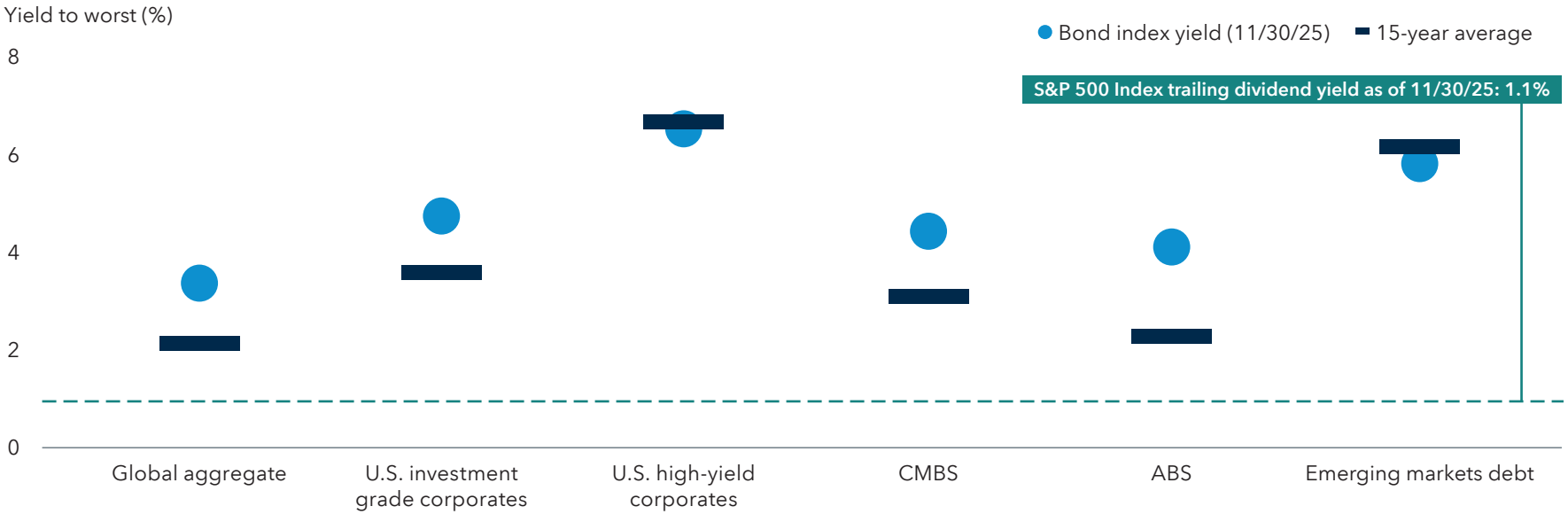
While many short-term portfolios may lean heavily on corporate credit, Gonzales sees broader opportunities across sectors to provide comparable yields with higher quality. "I'm finding value in a more balanced portfolio with short corporates alongside the spectrum of securitized credit products, with selective opportunities in agency mortgages." He believes the combination presents attractive risk-reward dynamics that reinforce short term's appeal: high-quality, competitive income and a source of diversification.

Sources: Capital Group, Bloomberg, Morningstar. Cycle returns reflect annualized average monthly returns for all months in each cycle period; cycle periods are defined as periods in which the federal funds rate trend changed (noted by peak or trough inflection) and then persisted for 3 months or more. Money market represented by 1-3 month T-bills. Data shown is from May 2005-November 2025.

Sources: Capital Group, Bloomberg, S&P Global, Morningstar. As of November 30, 2025. S&P 500 dividend yield represented by gross yields before taxes. Short-term bond category average is provided by Morningstar and based on more than 75 short-term bond funds.

Credit looks attractive amid pro-growth policies

Income-oriented bonds offering attractive yields



Major fixed income credit sectors may benefit as the Federal Reserve eases rates and certain pro-growth government policies take hold. "Despite policy uncertainties, the administration's overarching goal is economic expansion, particularly through deregulation," says bond manager Xavier Goss, adding he expects the U.S. economy to remain resilient.

This backdrop is constructive for corporate investment grade (BBB/Baa and above) and high-yield bonds, particularly as fundamentals remain supportive. Other sectors with attractive yields such as securitized and emerging markets debt, also benefit. Current yields in most sectors are at or above their 15-year averages.

With inflation above target, the Fed is poised to provide cuts modest enough to keep the income component of a bond's return potential strong.

Managers are emphasizing income opportunities sourced from diversified sectors that tilt toward higher quality. A mix of investment grade and high-yield corporate bonds paired with senior parts of securitized credit – across asset-backed securities (ABS), commercial mortgage-backed securities (CMBS) and residential mortgage-backed securities – offers the potential for atttractive overall yields while enhancing diversity and resiliency. Even parts of higher quality securitized markets like agency mortgaged-backed securities offer nominal yields rivaling corporate bonds, but with minimal credit risk and strong liquidity.

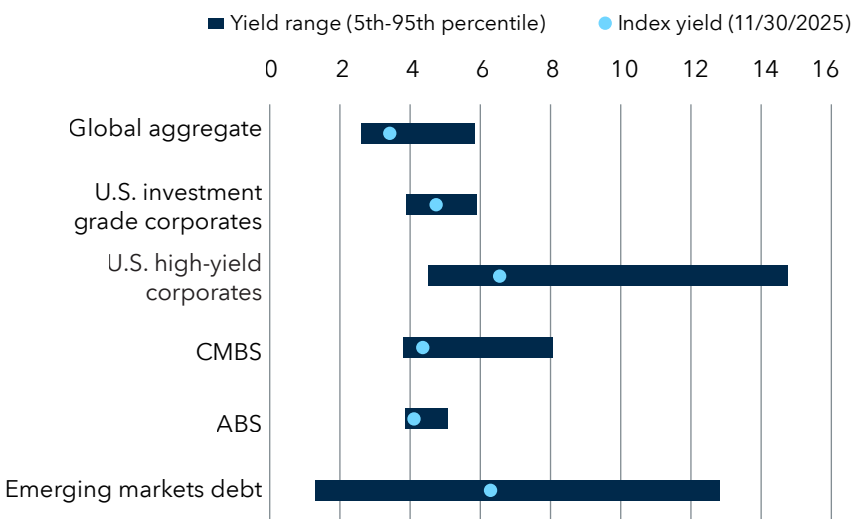
Beyond compelling overall yields, dispersion within different sectors allows for active selection to potentially add value.

Sources: Capital Group, Bloomberg, JPMorgan. As of November 30, 2025. Global aggregate is the Bloomberg Global Aggregate Index. U.S. investment grade corporates is the Bloomberg U.S. Corporate Investment Grade Index. U.S. high-yield corporates is the Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index, CMBS is the Bloomberg CMBS: Erisa Eligible Index, ABS is the Bloomberg ABS Index, Emerging markets debt is the JP Morgan GBI-EM Global Diversified Index.

Rich valuations make prudent credit selection critical

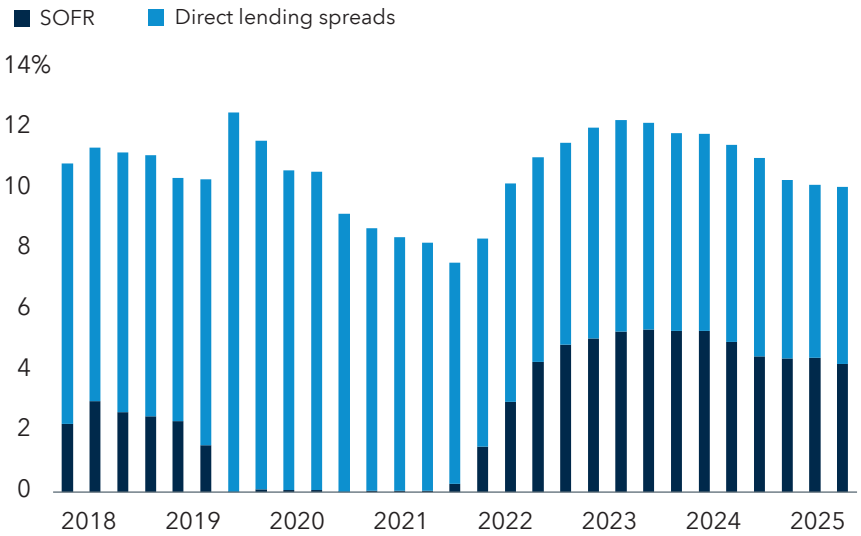
Opportunities vary across credit sectors

Yield-to-worst dispersion across sectors (%)



Investors demanded higher yields in private credit

Private credit direct lending yields



Attractive yields across credit sectors are creating compelling long-term opportunities, but at current valuations, security selection is critical.

Credit spreads reflect a benign outlook. Corporate fundamentals remain stable, with manageable debt and healthy earnings prospects, says bond manager Damien McCann. "I'm not seeing companies pile on unnecessary leverage. Most investment-grade firms aim to preserve their ratings."

In the high-yield space, credit quality has improved, which could keep defaults below the historical average of 3%. Although McCann favors higher quality assets, he isn't avoiding CCC-rated issuers. "Some companies face uncertainty three to five years out, but have near-term debt that's manageable," McCann explains. "Elsewhere, certain bonds are secured by strong assets, so even in a restructuring, investors can be protected."

Real estate investment trusts may benefit as commercial real estate continues to recover. Delinquency of office CMBS has surged with the rise of remote work, but that trend may moderate in 2026.

In emerging markets debt, McCann sees value in bonds from Latin American countries, including Mexico, Colombia and Panama, since they're more insulated from tariff-related volatility.

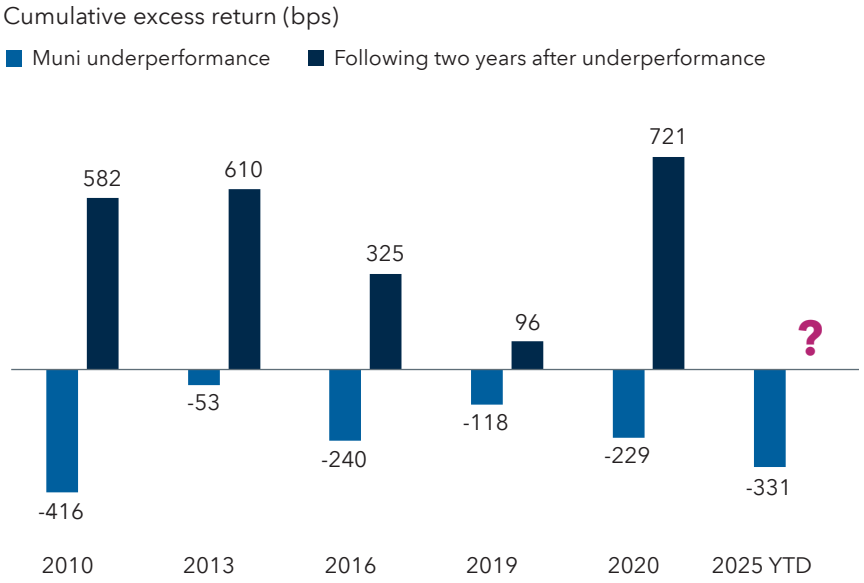
Private credit's strong yield has attracted investor demand, though the sector's limited liquidity and less transparency require additional due diligence and careful manager selection.

Sources: Capital Group, Bloomberg, JPMorgan. As of November 30, 2025. Global aggregate is the Bloomberg Global Aggregate Index. U.S. investment grade corporates is the Bloomberg Corporate Investment Grade Index. U.S. high-yield corporates is the Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index, CMBS is the Bloomberg CMBS: Erisa Eligible Index, ABS is the Bloomberg ABS Index, Emerging markets debt is the JP Morgan GBI-EM Global Diversified Index.

Sources: Capital Group, Bloomberg, Cliffwater. Latest data available is through Q3:2025, as of November 30, 2025. The Secured Overnight Financing Rate Data (SOFR) is a broad measure of the cost of borrowing cash overnight collateralized by Treasury securities. Direct lending (privately negotiated loans from non-bank lenders) spreads calculated by subtracting SOFR from direct lending yield to maturity.

Munis: An attractive entry point for strong after-tax income

After challenging years, munis have bounced back

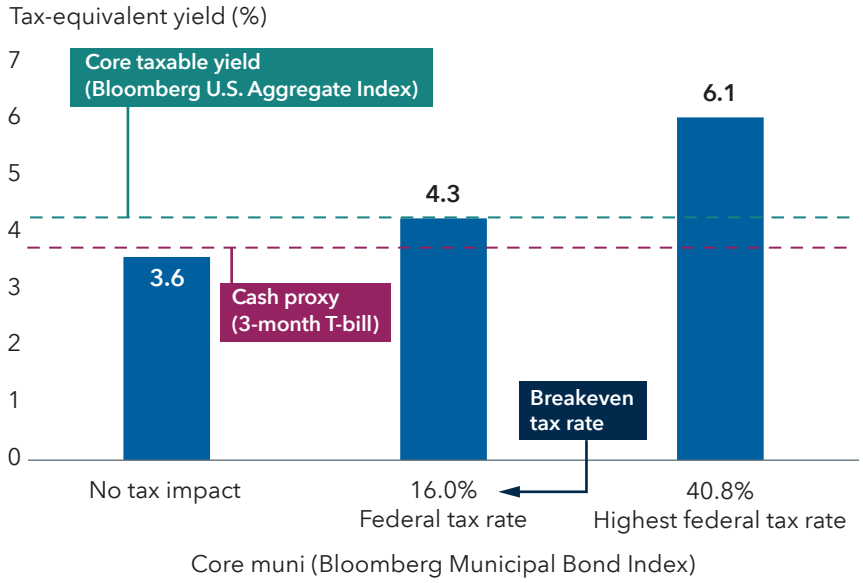


After a difficult year, municipal bonds may be the comeback story of 2026. Prices have dropped amid record supply, and it's creating a rare opportunity to access high-quality, tax-exempt income. Historically, munis rebounded following a year when taxable bonds outpaced munis.

"Based on fundamentals, the muni market remains really strong," notes Vikas Malhotra, municipal bond portfolio manager. "If you look at state balance sheets, as well as sectors such as toll roads, transportation and some others, their outlook appears to be solid. This market has typically experienced relatively few defaults." Malhotra also sees value in single-family housing, a high-quality segment of tax-exempt bonds.

Sources: Capital Group, Bloomberg, Morningstar. As of November 30, 2025. Data shown is the last five calendar years in which the Bloomberg U.S. Aggregate Index outpaced the Bloomberg Municipal Bond Index. The Bloomberg Municipal Bond Index is a market value-weighted index designed to represent the long-term investment-grade tax-exempt bond market.

Many investors may find stronger income in munis



The muni yield curve has seen a sharper steepening than the Treasury yield curve this year. The spread between five- and 30-year muni yields widened by 94 basis points, far more than the 66 basis points increase for Treasury yields across the same tenors. Malhotra expects the disparity between the muni and Treasury curves to converge over time and has adjusted curve positioning accordingly, with more exposure to longer maturities.

Despite early 2025 concerns, munis' federal tax exemption escaped legislative scrutiny. As such, munis remain attractive on a tax-equivalent basis for investors in the moderate to high-income tax brackets.

Sources: Capital Group, Bloomberg. As of November 30, 2025. Tax equivalent yield calculation is yield to worst divided by [1-(federal tax rate)]. The federal tax rate of 40.8% reflects the highest income tax rate of 37% and Medicare tax rate of 3.8%, respectively.

Investing outside the United States involves risks, such as currency fluctuations, periods of illiquidity and price volatility, as more fully described in the prospectus. These risks may be heightened in connection with investments in developing countries.

Bond ratings, which typically range from AAA/Aaa (highest) to D (lowest), are assigned by credit rating agencies such as Standard & Poor's, Moody's and/or Fitch, as an indication of an issuer's creditworthiness. If agency ratings differ, the security will be considered to have received the highest of those ratings, consistent with the fund's investment policies.

The market indexes are unmanaged and, therefore, have no expenses. Investors cannot invest directly in an index.

Bloomberg Global Aggregate Index represents the global investment-grade fixed-rate bond market. **Bloomberg U.S. Aggregate Index** represents the U.S. investment-grade fixed-rate bond market. **Bloomberg U.S. Corporate Investment Grade Index** represents the investment grade, fixed-rate, taxable corporate bond market. **Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index** covers the universe of fixed-rate, non-investment grade debt. The index limits the maximum exposure of any one issuer to 2%. **Bloomberg U.S. Treasury Bill: 1-3 Months Index** tracks the market for Treasury bills with 1 to 3 months to maturity issued by the U.S. government. **Bloomberg U.S. Government/Credit (1-3 Years) Index** is a broad-based benchmark that measures the non-securitized component of the U.S. Aggregate Index. It includes investment grade, U.S. dollar-denominated, fixed-rate Treasuries, government-related and corporate securities with 1 to 3 years to maturity. **Bloomberg Municipal Bond Index** is a market value-weighted index designed to represent the long-term investment-grade tax-exempt bond market. **Bloomberg Municipal Short (1–5 Years)** Index is a market value-weighted index that includes investment-grade tax-exempt bonds with maturities of one to five years. **Bloomberg U.S. Asset-Backed Securities (ABS) Index** measures ABS securities in the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. **Bloomberg CMBS: ERISA Eligible Index** measures U.S. agency and U.S. non-agency CMBS deals at least $300mn that are ERISA eligible under the underwriter's exemption. **Bloomberg U.S. Economic Policy Uncertainty Index** measures U.S. economic policy uncertainty by counting newspaper articles on the topic.

Cliffwater Direct Lending Index consists of private middle market loans.

JP Morgan Government Bond Index – Emerging Markets Global Diversified covers the universe of regularly traded, liquid fixed-rate, domestic currency emerging market government bonds to which international investors can gain exposure.

MSCI All County Word Index (ACWI) ex USA is a free float-adjusted market capitalization-weighted index designed to measure equity market results in the global developed and emerging markets, excluding the United States. **MSCI China Index** captures large- and mid-cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs). **MSCI Emerging Markets Index** captures large- and mid-cap representation across 27 emerging markets (EM) countries. **MSCI Europe Index** is designed to measure developed equity market results across 15 developed countries in Europe. **MSCI Japan Index** is a free float-adjusted market capitalization-weighted index designed to measure the equity market results of Japan. **MSCI World ex USA Index** is designed to measure equity market results of developed markets. The index consists of more than 20 developed market country indexes, excluding the United States. **MSCI USA Index** is a free float-adjusted, market capitalization-weighted index designed to measure the performance of the large- and mid-cap segments of the U.S. market.

Nasdaq 100 Index tracks 100 of the largest non-financial companies on Nasdaq, spanning sectors like tech, telecom, retail, and biotech. Financial firms, including investment companies, are excluded.

Russell 1000 Growth Index measures the results of the large-cap growth segment of the U.S. equity universe. Russell 1000 Value Index measures the performance of large-cap value segment of the U.S. equity universe.

S&P 500 Index is a market capitalization-weighted index based on the results of approximately 500 widely held common stocks. **S&P 500® Dividend Aristocrats® Index** is an equal-weighted index that measures the performance of S&P 500 companies that have increased dividends every year for the last 25 consecutive years.

U.S. Dollar Index measures the U.S. dollar's strength against a weighted basket of six major foreign currencies.

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2026 Outlook

CAPITAL GROUP®

Equity themes

Themes	Dynamic growth	Defend with dividends	Diversify with international
	AI build-out continues to offer compelling opportunities	**Dividends can smooth the ride when markets are choppy**	**New catalysts could propel markets in Europe and Asia**
Investment implications	The AI megacycle continues to advance at a rapid pace. With the competitive landscape shifting, selective investing is essential. A focus on earnings fundamentals is key.	Dividend payers have held up better than the broader market during periods of volatility. Investors can find dividend opportunities across a range of sectors and geographies.	Bold stimulus in Europe and corporate governance reforms spreading through Asia could help sustain recent rallies in equity markets outside the U.S.

Fixed income themes

Diversify for ballast	Dynamic approach to income	Defend with short term
Bonds are providing income again, with higher return potential	**Don't let tight credit spreads distract from opportunity**	**Preserve capital while earning quality income**
High-quality core, core-plus and municipal bonds may help provide balance amid heightened economic uncertainties and record-high equity valuations.	Intentional exposure to credit and other high-income sectors may provide relatively strong yields amid healthy fundamentals.	Short-term bond funds offer a measure of capital preservation amid market volatility, aiming to protect against a rise in rates while also capturing potential upside if rates decline.

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*Source: Marketing Support: The Advisor View, May 2025, June 2024, May 2023, July 2021, June 2020; Fund Intelligence, February 2020. FUSE Research surveys of 500-1,000 advisors identifying the "most-read thought leaders." Survey was not conducted in 2022.

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