



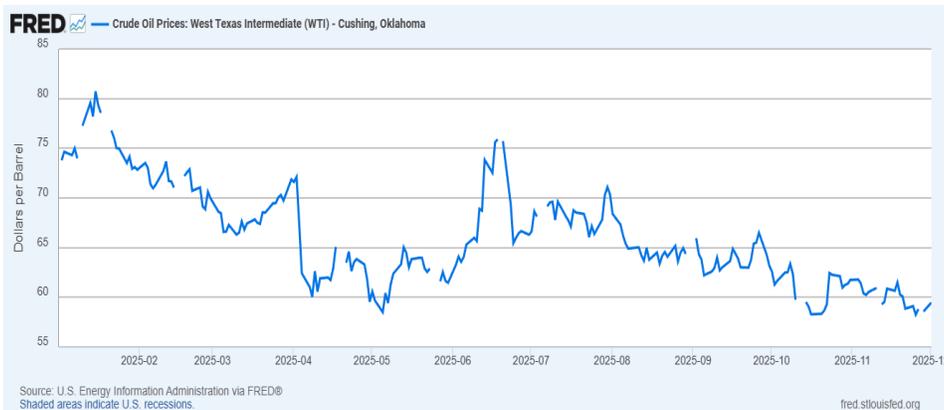
Financial Markets Perspective January 2026

A Look Back; a Look Ahead

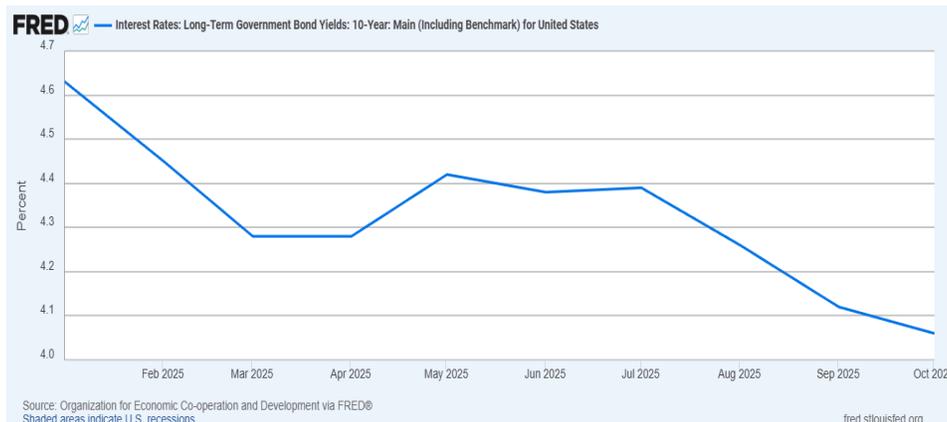
As most of our readers know, in our year-end review, we offer a forecast of the economy and financial markets for the coming year and evaluate our prior-year prognostications. This year is no different, so let's see how our forecasts for 2025 turned out (note: italics for the predictions) and what we see in our crystal ball for this year.

“For 2025, we expect to see relative stability in oil prices.”

Oil prices declined for most of 2025, as seen in the chart below, with two short-term blips that pushed prices into the \$75-\$80 range. As 2025 ended, oil prices were near year lows, dropping under \$60 per barrel, good news for consumers who saw gasoline prices fall. This \$15-per-dollar decline in prices from the beginning of the year was not in our forecast but contributed to lower inflation.



“Government bond yields (10-year) will fluctuate between 4% to 4.5%. This is one of our more accurate forecasts, as seen in the chart below. With a slight rise above 4.5% in early 2025 and a brief decline below 4% late in the year, our forecast was right on target, and the 10-year yield ended at 4.15%, at the lower end of our forecast range!



We made several forecasts regarding the decisions of the incoming Trump Administration. Here is how our expectations worked out.

“For equity investors, most of the announced programs will benefit the economy. First, reductions in tax rates or the commitment not to raise taxes are important components to stimulate further economic growth. History tells us that lower tax rates increase economic activity.”

The president’s decision to maintain the tax rate cuts from his first administration undoubtedly kept the economy on an even keel. The shock of the tariffs’ impacts temporarily depressed expectations, but as the terms of the tariffs swung back and forth, markets became accustomed to volatility. Amid economic forecasts of zero growth or a recession beginning in 2025, the economic consensus shifted toward more growth as the year progressed.

“The new Administration’s decision to increase fossil fuel production will help control inflation by lowering oil prices.”

As 2025 ended, U.S. oil producers were achieving record output. Natural gas prices also remain low. The U.S. is the largest oil producer and is impacting oil prices, which are currently trading below \$60 per barrel. Even though we experienced record oil output, the dollar weakened during the year. The positive outlook for exporting liquified natural gas remains strong.

“The stock market should be a beneficiary of these planned changes.”

As the year ended, major stock market indices were at record levels, even as economic indicators were negative and consumer confidence was near record lows. Economists are shrugging their shoulders, surprised by how little tariffs have affected the economy.

“The new President has some foibles that will cause some near-term dyspepsia as new policies roil both the status quo and, in turn, sectors of financial markets. Interest rates should remain stable, and equity markets should have another better-than-average year. There could always be an unidentifiable event that could upset this prediction, but a new “Golden Age of America” has arrived.”

President Trump has been an “unusual decisionmaker” when it comes to economic policy. Volatile financial markets and continued low consumer confidence support concerns about the impact of changing government policy. His surprise decision to implement global tariffs sent the stock market down about 20% in the first quarter, an “unidentifiable event” we predicted. Fortunately, reductions or eliminations of some of those tariffs allowed the stock market to recover and reach record highs by the fourth quarter of the year. Interest rates remained stable and equity markets had a better-than-average year. The new “Golden Age of America” is reflected in the health of financial markets, unexpected increases in corporate profitability, and the overwhelming influence of advances in artificial intelligence.

A Look Ahead to 2026

The outlook for 2026 is unusually positive for this stage of the business cycle. For equity investors, there have been three solid years of double-digit returns. Even though consumer confidence waned last year, unemployment increased only slightly; inflation remained relatively stable and is trending downward; interest rates were stable but gradually decreasing; and the dollar weakened, boosting our exports. From a macroeconomic perspective, the outlook is affected by the fact that consumers and businesses have never been wealthier. The dominant

factor determining equity market returns is corporate profits, which have been improving. And our regular readers are saying: “Here we go again!”

Our optimism about last year continues into 2026 for a couple of reasons. Firstly, global wealth is expanding. One reason is that foreign equity markets achieved record double-digit gains in 2025. Such gains contribute to optimism, increased consumer spending, and greater economic output. Domestically, we saw that consumer spending boosted third-quarter GDP to 4.3% -- even though overall consumer confidence is low. For the year as a whole, growth ran around 3%, which is not bad given all the calls for a recession. Equity markets finished well ahead of expectations, with the S&P 500 returning 18% on the back of a 23% return in 2024. Fixed-income markets experienced more volatility than normal but also rose.

Secondly, companies recognize that artificial intelligence (AI) could positively impact the way we live and work. By drawing together and analyzing data from internal and third-party sources, AI can help decision-makers with tasks such as predicting costs, identifying and responding to potential supply chain disruptions, and more accurately forecasting product demand. Last year’s equity markets were characterized by the dominance of the “Magnificent Seven,” a group of the largest-cap technology companies enjoying unusual growth driven by the application of artificial intelligence. In 2025, the emphasis shifted to other tech-related companies or those benefiting from AI spending. One example is Caterpillar that builds infrastructure for data centers. The stock was the best performer in the DJIA in 2025.

The implementation of AI across industries is the next step in significantly improving our lives. Gains from the implementation of AI could cause a continued increase in unemployment, but also an increase in corporate profits via rising productivity. AI can augment work by replacing and automating repetitive tasks or assisting with routine decisions, reducing the burden on workers and enabling them to perform other responsibilities more effectively. Some top companies using AI include Amazon, Apple, Google, Microsoft, and NVIDIA. For example, few companies are involved in as many industries as Amazon, including e-commerce, cloud computing, logistics, voice-activated technology, and even autonomous vehicles. Personal assistants like Siri and Alexa have made AI a part of our daily lives, and other companies have been infusing their products with AI to develop intelligent technology and services like self-driving cars, automated robots for use in warehouses and hospitals, content generators, cybersecurity threat detection, and customer experience analytics.

Corporate profits will likely continue in a positive trajectory given stable to falling interest rates and mildly positive fiscal policy. However, changes in future tax laws could impact that expectation and in an election year, such changes are uncertain. According to FactSet, earnings for S&P 500 companies are expected to grow by about 12% in 2025. Companies will start reporting their final quarterly financial results for this year in the next few weeks. Tax rebates are expected to be much larger than in 2025, so that consumer spending in the first half could be substantial and add to overall economic growth. This “windfall” for taxpayers could also bolster the chances for Republicans to retain control of Congress.

The executive branch's decisions are being challenged by judges across the country. So far, the Supreme Court has ruled in favor of the President. However, if the Court makes any major decisions that reverse the President’s economic policy, there could be additional impacts across

various economic sectors. Decisions by this Administration to reverse many of the policies of the previous government, such as reversing the surge in illegal immigration and related removal of those immigrants, coupled with the expiration of tax cuts, should lower costs for municipalities that had to absorb the costs of feeding and housing those illegals.

So, what is the potential bad news? Mostly, increased volatility related to our two-year Congressional election cycle. The first year of President Trump's second term was filled with economic decisions that affected both businesses and consumers. As his numbers have fallen in various popularity polls, so have expectations of Republican success in the mid-year elections. If they lose their majorities in either the House or the Senate, or both, there could be a return to policies that increase taxes and accelerate plans to redistribute wealth. Financial markets are likely to reflect expectations for the election outcome as early as the beginning of the third quarter of next year.

Conclusions:

The substantial increase in global wealth over the past year should contribute to a global golden age, even as conflicts persist in Europe and Asia. If oil prices continue to decline, that will boost consumers' disposable income. The explosion in AI spending globally will be another factor contributing to stronger economies. These are the primary factors that should benefit financial markets in 2026 and beyond.

In an easier Fed policy environment and lower inflation, short-term bonds should experience further gains, while long-term bonds should see lesser gains, along with a traditional stock market return in a 9-12% range, with obvious divergences brought about by circumstances. The expected Fed policy of continued lower interest rates, improving corporate productivity through broader AI use, rising global wealth that will boost global trade, and lower inflation give us optimism that financial markets will benefit from these trends. Interest rates should remain in a trading range, with the benchmark 10-year Treasury bond trading between 4% and 4.5%. The U.S. dollar will likely stay around current levels with our major trading partners.

We have had three strong years of equity market returns. Some forecasters say that we are repeating the market bubble of the late 1990s. We disagree because there is no endpoint event such as the Y2K risk. Therefore, gains will come down to the strong earnings and revenue growth of individual companies since profits are the foundation of strong stock markets.

Best Wishes for another great year in 2026!

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