Q2 2026 investment outlook

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Executive summary

In our 2026 outlook, we set a full-year view for the year that leaned positive, supported by resilient consumer spending, technology investment and policy settings expected to help growth. As the first quarter concludes, those building blocks remain, but the road ahead has more twists. Markets moved higher early in the year on improving foreign growth and strong artificial intelligence (AI) spending, while investors also debated AI's impact on software and watched for tighter liquidity in some private lending.

March brought a major new variable: The U.S. and Israel struck Iran over nuclear concerns, and the Strait of Hormuz was closed. The disruption tightened energy supply and raised inflation risk, which pressured global risk assets. Even so, after three strong years for markets, the second quarter of 2026 begins with solid underlying drivers, even with headline risk and uneven performance.

The key near-term question is how long the Strait disruption lasts, since duration will influence how much higher energy costs show up in broader inflation and how sensitive stock valuations become. The U.S. economy entered the conflict from a position of relative strength, with wage growth outpacing inflation and layoffs remaining low even as job growth has slowed. Tax refunds are tracking ahead of last year and can help household cash flow as families adjust to higher costs, while business spending and AI infrastructure investment continue to support activity.

Outside the United States, energy can play a bigger role because many major economies import a larger share of their supply, including Japan and the European Union. That dependence can translate into more pressure when prices rise and quicker relief when prices ease, leaving overseas markets more sensitive to changes in shipping and supply conditions. Volatility is part of investing, and history shows that trying to time short-term moves can lead investors to miss strong rebound days that often arrive during unsettled periods.

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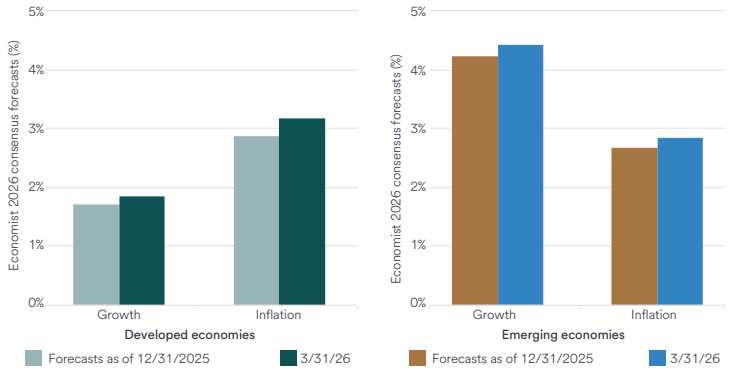
Opportunities can still show up in any environment, but they are rarely spread evenly, which increases the value of selectivity and diversification. We are watching how credit conditions evolve and how the list of winners and losers changes as AI spending spreads across the economy. Looking further out, the 2026 World Cup, the United States' 250th anniversary celebration, a potential Federal Reserve (Fed) leadership change and November midterm elections add both opportunity and policy uncertainty. The sections that follow summarize what we are watching for the second quarter and the rest of the year.

Global economic views

Quick take: Consumer spending, business investment and 2025 monetary policy easing continue to support the economy. The key near-term question is whether higher energy costs remain temporary or begin to more meaningfully pressure inflation, global growth and central bank policy.

- **Consumer spending and business investment continue to anchor U.S. growth.** Consumer spending has grown at roughly 5% year over year, corroborated by transaction data and company commentary. Wage growth near 4% has helped households keep pace with inflation even as hiring slows. Business investment adds another layer of support, particularly through AI spending. AI-related companies increased capital expenditures 72% and global capital spending 13% in 2025, helping sustain a slower but still-constructive expansion.
- **The U.S. labor backdrop has softened, but it still looks more like cooling than contraction.** Monthly payrolls increased by a modest 34,000 in January and February, and the unemployment rate inched higher to 4.4%, confirming that hiring has become less consistent than earlier in the cycle. Even so, layoffs remain relatively contained, and the combination of slower hiring and limited job cuts points to a labor market that is cooling rather than breaking down. A slower labor market can coexist with continued growth if household income and business demand remain intact.
- **The global economic outlook remains supportive pending Middle East conflict outcomes.** Economists project real gross domestic product (GDP) to rise by 1.8% across developed economies and 4.4% in emerging economies in 2026, with emerging Asia continuing to benefit from AI-related demand. At the same time, higher sustained oil prices could weigh more heavily on non-U.S. economies, especially in Europe and parts of Asia that rely more on imported energy and liquefied natural gas. Growth continues, but energy sensitivity abroad may keep international inflation and policy expectations more volatile than in the United States.
- **Energy remains the key swing factor for inflation, growth and policy.** Before the Iran conflict intensified, the headline U.S. Consumer Price Index held at 2.4% year over year and the broader inflation trend was improving as shelter costs cooled gradually. The concern now is whether disruption through the Strait of Hormuz, which handles roughly 20% of global petroleum liquids and 20% of global liquefied natural gas trade, keeps oil and transport costs elevated long enough to affect household budgets, business margins and central bank decisions. If the disruption fades, the global economy can likely continue expanding. If it lasts, inflation may worsen just as growth slows, creating a more difficult backdrop for both the Fed and foreign central banks.

Growth and inflation projections



Sources: U.S. Bank Asset Management Group research, Bloomberg; December 31, 2025-March 31, 2026.

Equity markets

Quick take: Earnings growth still supports equities, even as investors weigh elevated valuations, geopolitical risk and uneven returns from technology spending. Selectivity, diversification and a continued focus on durable business fundamentals remain important.

- **Earnings growth remains the clearest support for U.S. stock prices.** Consensus analyst expectations forecast S&P 500 earnings of $321 per share in 2026 and $373 in 2027, representing increases of 16.4% and 16.2%, respectively, from year-ago projections. Mid- and small-company earnings expectations also remain strong, with analysts projecting 2026 earnings growth of 13.8% and 17.4%, respectively. Strong profit growth helps support equities even when valuations already look full by historical standards.
- **Valuations remain elevated, but they still rest on fundamental strength.** The S&P 500 is trading at roughly 20.5 times 2026 earnings and 17.5 times 2027 earnings, which is above long-term averages but still consistent with a market backed by earnings growth. Fourth quarter 2025 corporate results reinforced that support, with revenues rising 9.2% and earnings increasing 13.6%, both above expectations. The key risk is not simply that valuations are high, but that valuations could become more vulnerable if inflation rises, interest rates move higher or profit growth falls short of what investors now expect.
- **Technology remains a long-term driver, but investors are becoming more selective.** Computing power, data capture, storage, analytics, security and electrification demand continues to support the infrastructure behind AI. Software looks more mixed as investors ask harder questions about which business models may benefit from AI and which may face pricing pressure or disruption. This favors companies with stronger positions in privacy, security, governance and mission-critical workflows rather than assuming all technology businesses will benefit equally.
- **Global equity opportunities remain important, even with added energy sensitivity abroad.** Foreign developed and emerging market equities continue to offer valuations closer to historical norms and dividend yields that remain more attractive than many U.S. large-company stocks. Earnings expectations abroad remain constructive, with analysts still forecasting 7.5% earnings growth for developed markets and 35.5% for emerging markets. International markets may remain more volatile if energy disruption persists, but broader participation across regions and among small to large companies strengthens the case for staying diversified rather than relying too heavily on one part of the market.

U.S. equity performance

Index	2026*		2025
	MTD	YTD	
S&P 500	-5.1%	-4.6%	16.4%
Dow Jones Industrials	-5.4%	-3.6%	13.0%
S&P 500 Sectors			
Communication Services	-7.3%	-7.1%	32.4%
Consumer Discretionary	-5.7%	-9.3%	5.3%
Consumer Staples	-7.7%	7.0%	1.3%
Energy	10.3%	37.2%	5.0%
Financials	-3.7%	-9.8%	13.3%
Health Care	-8.3%	-5.3%	12.5%
Industrials	-8.5%	4.3%	17.7%
Information Technology	-3.9%	-9.3%	23.3%
Materials	-7.1%	9.3%	8.4%
Real Estate	-6.6%	1.9%	-0.3%
Utilities	-3.4%	7.5%	12.7%

*Through March 31. MSCI Index numbers through March 30. Excludes dividends.
Sources: FactSet Research Systems, S&P Global.

Bond markets

Quick take: Bonds remain an important source of income and portfolio balance. Yields across core and selective income sectors continue to offer a stronger return starting point than investors had during much of the previous decade while fundamentals remain solid.

- **High-quality bonds continue to offer meaningful income and diversification.** U.S. Treasury yields still provide reasonable compensation for a market balancing slower growth, sticky inflation and uncertainty around future Federal Reserve policy. Market prices currently imply inflation could rise from about 2.4% to an average of roughly 3.2% over the next year, suggesting investors are already demanding some protection against renewed price pressure. Today's yield levels give core bonds a stronger starting point for both income generation and portfolio balance than investors had in the low-rate years.
- **The rate outlook still depends heavily on inflation and energy.** Markets are pricing a Fed that is likely to hold rates steady through 2026, while policymakers continue to weigh labor market softness against inflation risk. If the recent energy shock fades, that path may still hold. If oil and transportation costs remain elevated, the timeline for easier policy could shift, especially if higher prices begin to affect inflation expectations more broadly in the United States and abroad.

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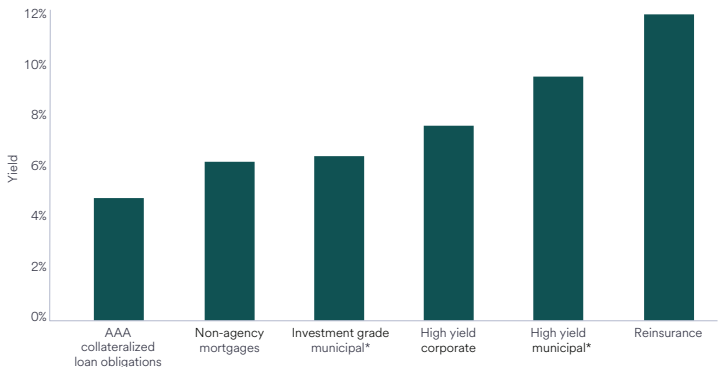
- **Corporate credit still offers attractive income, but issuer selection remains important.** Investment-grade corporate bonds currently offer about 0.9% more yield than Treasuries, while high yield corporate bonds offer about 3.2% more. Most issuers still appear supported by cash balances, cash flow and the expectation of continued profit growth through 2026, and default trends have shown signs of easing. Recent stress in certain sectors of leveraged loans and private credit reinforces the need to focus on diversification, sector exposure and underlying business resilience rather than simply stretching for yield.
- **Tax-advantaged and specialty income sectors remain valuable complements.** For investors in the top tax bracket, investment-grade and high-yield municipal bonds offer tax-equivalent yields of roughly 6.4% and 9.6%, respectively, which remain compelling relative to many other fixed income options. Select specialty sectors can also add value, with non-agency mortgages offering about 1.0% additional yield over Treasuries and insurance-linked securities generating current coupon income of more than 10% annually. For appropriate investors, these areas can improve portfolio income and broaden diversification without relying on one single rate or credit outcome.

Bond yields



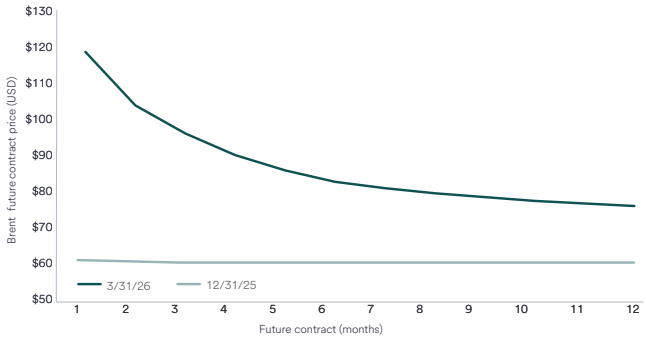
Sources: U.S. Bank Asset Management Group research, Bloomberg; March 31, 2026.
Data reflects benchmarks, fund proxies, and other sources that fairly represent yields.
*Municipal bond categories show tax-equivalent yields using the top federal tax bracket.

Real asset markets

Quick take: Real assets can help diversify portfolios and respond to inflation risk. Public real estate and infrastructure offer income and long-term cash flow potential, while commodities are more sensitive to near-term supply disruptions and changes in demand.

- **Public real estate continues to offer selective strength and meaningful income.** Public real estate prices remain at reasonable levels relative to the income these properties are generating. Property fundamentals also remain healthier outside of the office sector, with occupancy rates near 95% in industrial, retail and apartments. Office occupancy is closer to 87% and represents only a small share of diversified real estate exposure. Investors should focus on property types tied to stronger demand trends rather than letting weakness in office dominate their outlook.
- **Fundamentals of certain real estate sectors appear well positioned.** Health care, industrial, residential and data center properties continue to benefit from durable demand tied to demographics, logistics and digital infrastructure. Net operating income, a common measure of property profitability, continues to grow across several major property types, including industrial, retail, health care and residential. In a market where investors value steady income and reasonable valuations, those segments can make public real estate a useful complement to both stocks and bonds.
- **Infrastructure remains tied to both stable income and long-term global demand.** Analysts forecast about 15.9% earnings growth in 2026 for global infrastructure, supported by utilities, industrial businesses and energy systems that provide essential services. Rising electricity needs tied to AI, data centers and broader electrification strengthen the long-term case for utilities and pipelines in both North America and global markets. Because many of these businesses can increase prices as costs rise, infrastructure can also offer some protection in environments of elevated inflation.
- **Oil and gas are likely to remain the biggest drivers of broad commodity performance**, because the Strait of Hormuz remains an important route for global energy trade. The cost of oil for near-term delivery rose by more than 60% in March after the Iran conflict disrupted supply, and markets continue to watch whether those pressures fade or persist. Gold and silver may still attract interest as hedges during periods of geopolitical stress, but after strong gains over the past year, they may also remain vulnerable to sharp sentiment shifts. Global central bank purchases will likely slow or halt as countries deal with energy price spikes in the near term.

Oil futures



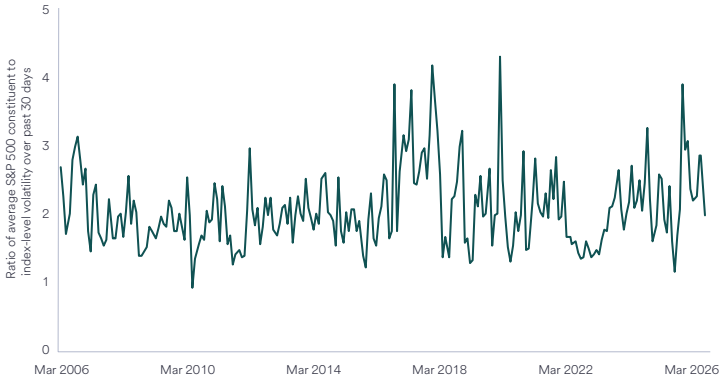
Sources: U.S. Bank Asset Management Group research, Bloomberg; March 31, 2026.

Alternative investments

Quick take: Hedge funds appear well positioned for a market with wider asset class performance gaps, changing economic conditions and elevated volatility. Flexibility, selective risk taking and lower dependence on broad stock and bond market direction remain central advantages.

- **The environment for hedge funds improved as market outcomes became less uniform.** Recent performance benefits from higher volatility, shifting interest rate expectations and economic uncertainty, which create more frequent repricing across sectors and securities. This backdrop often gives active managers more ways to generate results, because returns no longer depend on one broad market trend. It also helps explain why hedge funds have delivered strong results at the start of 2026 after already posting double-digit gains over the prior two years.
- **Wider performance gaps across companies create more room for skilled security selection.** Major stock indexes can appear stable on the surface while individual companies move far more sharply beneath them, especially when investors reassess earnings, interest rates and the business impact of AI. This kind of market can reward managers who distinguish clearly between stronger and weaker businesses rather than relying on broad market exposure. In practical terms, stock picking may matter more than index direction alone.
- **Investor interest is rising in alternatives as traditional stock and bond portfolios provide less diversification.** Stock and bond prices have, at times, responded similarly to the same concerns about inflation, policy and growth, which has reduced the benefit of relying only on traditional asset classes for diversification. Hedge funds can help, because many strategies aim to produce returns that are less tied to whether broad public markets rise or fall together. For qualified investors, hedge funds are more relevant when macroeconomic shocks can affect several parts of a portfolio at once.
- **Flexibility and manager design remain critical.** Not every hedge fund approach is equally well suited to this environment, and investors should still focus on managers that can adjust exposure as conditions change. Strategies with flexible mandates may be better positioned to respond to shifts in volatility, interest rate expectations and company-level opportunities than approaches tied too closely to one style. Hedge funds can add value, but only when paired with disciplined manager selection and a clear role in the broader portfolio.

Ratio of individual stock to index-level volatility



Sources: U.S. Bank Asset Management Group research, Bloomberg; March 31, 2006-March 31, 2026.

Private markets

Quick take: Private capital still offers selective opportunities in 2026, even as recent private credit headlines raise caution. Long-term themes, disciplined underwriting and patience remain more important than short-term market stress or changing investor sentiment.

- **Private credit headlines highlight structure and discipline more than broad fundamental collapse.** Recent concern centers on loan quality in some vehicles marketed to individual investors, especially where investors expected periodic redemption opportunities but the underlying loans trade infrequently, if at all, prior to maturity. That mismatch received more media attention; some funds have limited or eliminated withdrawals through gating provisions, and investors have asked harder questions about underwriting

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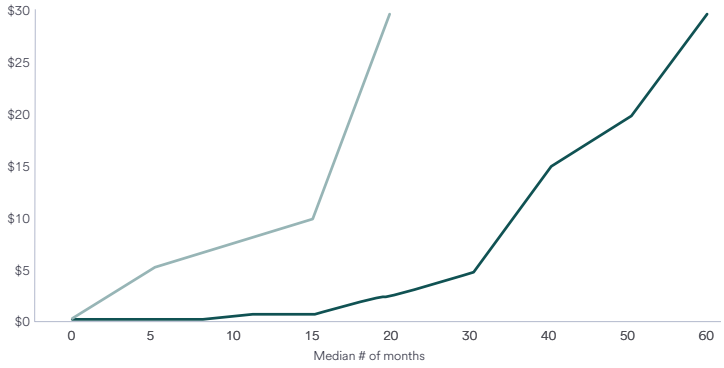
and loan pricing. Even so, recent private credit default rates remain within a long-term average range of about 5% to 6%, supporting a more measured interpretation than the headlines might suggest.

- **Private equity deal activity and public listings entered the year with momentum.** Activity improved because the economic backdrop included lower borrowing costs, a healthier pipeline of companies prepared to exit and a more constructive policy environment for transactions. Near-term volatility tied to the Iran conflict may delay some deals, but the larger reopening story remains intact if market conditions stabilize. Several large private companies, including SpaceX, Anthropic and Open AI, have reinforced the view that the market for new listings could improve further if confidence returns.
- **Investor access to private markets continues to expand, but design matters.** More institutions are pursuing individual investors through non-traded or limited-liquidity vehicles and other structures designed to broaden access beyond traditional institutional pools of capital. That can create new opportunities, but it also creates new responsibilities because liquidity terms, portfolio construction and valuation practices matter more when investors expect periodic withdrawals. For qualified investors, the central question is not simply whether to own private assets, but whether the manager and fund structure match the investor's time horizon and liquidity tolerance.
- **Long-term themes still shape the strongest opportunity set.** Areas such as aerospace, defense, government services, essential services businesses, rising power demand, limited-partner secondary transactions and selective opportunistic private credit continue to stand out. The common feature across these themes is durable demand rather than short-lived market excitement. Private capital remains appealing in 2026 for investors who can stay patient, focus on manager quality and commit capital to long-term opportunities rather than near-term headlines.

Time to $30 million in revenue

AI native companies vs. historical SaaS (software as a service) companies



Sources: Source: U.S. Bank Asset Management Group Analysis; Hamilton Lane, February 2026.

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