

Q4 2026 investment outlook



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Executive summary

As we enter the final quarter of 2026, investors have good reason to remain engaged, but fourth quarter events could quickly reshape the path ahead. Consumers are earning and spending, banks are lending, and businesses are investing in technology and physical capacity. Those activities reinforce one another and have helped companies translate revenue growth and past productivity investments into strong earnings. That foundation has supported record stock prices for reasons grounded in business results, not simply in investors paying more for the same profits.

The fourth quarter calendar adds important tests. U.S. midterm elections may shift expectations for taxes, spending, regulation and trade. The Federal Reserve (Fed) and other major central banks have already pivoted from anticipated rate cuts toward actual and expected rate increases due to elevated inflation. Strong U.S. growth, high energy costs and heavy government and corporate borrowing have also pushed longer-term interest rates higher. Investors should watch both the next policy decisions and market adjustments if borrowing costs remain elevated.

Oil and energy costs provide the clearest link between geopolitics, the economy and broad market performance. The U.S.-Iran conflict has disrupted energy and transportation flows, lifting oil prices without providing a reliable timeline for normalization. Higher oil prices add to inflation, reduce household purchasing power, raise business costs and give central banks more reason to keep interest rates high. Those pressures can simultaneously affect stocks, longer-term bonds, real estate and utilities, while changing conditions for energy producers, pipelines and commodities. The relationship can also reverse abruptly. A durable restoration of supply routes or an end to the conflict could lower oil prices, ease inflation concerns and change expectations for interest rates and market leadership.

This range of outcomes calls for optimism with discipline. Broad equity exposure offers participation in earnings growth across companies, industries and regions. Higher bond yields provide more income than investors could earn through much of the past decade. Infrastructure connects portfolios to the physical buildout of power, data centers, transportation and productive capacity, supported by durable cash flows and the potential to benefit when inflation rises. For suitable investors, private market exposure can provide access to long-term themes, but manager skill, investment quality, fund structure and liquidity remain decisive considerations. The sections that follow explain how we are evaluating these crosscurrents and where thoughtful diversification may help investors participate in growth while preparing for change.

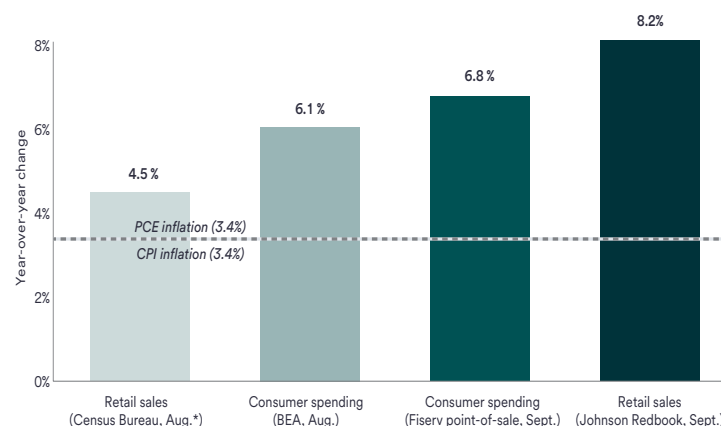
Global economic views

Quick take: U.S. growth is durable, with household spending and business investment offsetting higher energy and financing costs. Inflation, credit availability and employment will determine whether that balance holds.

- U.S. consumer income and spending power the expansion.** Consumer spending increased 5% to 9% from a year earlier in recent months even as confidence remained subdued. Employers added an average of 80,000 jobs per month through August, while broader personal income rose 4.3% from a year earlier in July. Low unemployment and layoffs near record lows also give households the ability to keep spending despite higher fuel and borrowing costs. The outlook would weaken if inflation persistently outpaced income or layoffs broadened, since either development would reduce purchasing power and confidence at the same time.
- Business investment adds a second engine of growth.** Analysts expect large U.S. companies to increase capital spending by approximately 41% over the next 12 months. Much of that investment relates to artificial intelligence (AI), but the activity extends well beyond software and computing. Companies are financing data centers, power systems, construction, equipment and land, creating demand for manufacturers, utilities, contractors and lenders. Wider use of AI tools may also improve productivity and profit margins over time. The cycle still depends on willing lenders and healthy cash flow, making bank lending and broader financing conditions important signals for the outlook.

- Higher energy costs and interest rates test the economy's adaptability.** U.S. consumer prices rose 3.4% from a year earlier in August, driven largely by energy costs tied to the U.S.-Iran conflict. The Federal Reserve and other major central banks have raised rates, and investors anticipate additional increases to combat inflation. Higher rates restrain activity by lifting borrowing costs, although strong demand and corporate earnings indicate that the economy has absorbed the pressure so far. Midterm election uncertainty may affect sentiment, while inflation, employment and credit will shape actual activity.
- Global growth remains constructive, but energy costs and AI-related spending are creating differentiation.** Growth forecasts are positive but slower in energy-importing regions such as the United Kingdom, Europe and Japan. Some emerging market countries like Taiwan and South Korea continue to benefit from strong AI-related spending, helping to boost economic activity.

Consumer spending is outstripping inflation



*Figure shown is rounded control group, which is less volatile than the headline figures.

Sources: U.S. Bank Asset Management Group, Bloomberg, September 30, 2026. "CPI inflation" is the Consumer Price Index; "PCE inflation" is the Personal Consumption Expenditures Price Index.

Equity markets

Quick take: Earnings growth supports stocks as investors demand clearer returns from AI investment. High prices, financing costs and concentrated growth increase the value of broad diversification and careful company selection.

- **Strong earnings explain this year's gains and support a positive outlook.** As of September 30, analysts project S&P 500 earnings of approximately \$363 in 2026 and \$417 in 2027, representing growth of 32% and 15%, respectively. Strong 2026 earnings growth helps explain this year's stock market gains; investors trimmed what they paid for each dollar of profit on the S&P 500. Expectations for further profit growth support a constructive view into 2027. However, U.S. large-company stock prices are above historical averages relative to expected earnings, leaving less room for disappointment. Persistent inflation, higher borrowing costs, weaker demand or pressure on profit margins could cause results to fall short and challenge our outlook.
- **Artificial intelligence investment is broadening across industries.** Companies are spending on semiconductors, networking, memory, data centers, power systems, cooling, cybersecurity and data management. The opportunity now extends to industrial companies that build facilities, utilities that supply electricity and financial firms that fund projects. Investors are also shifting attention from the construction of AI infrastructure to the business results that technology produces. Companies will need to show that AI investment creates revenue, raises productivity or improves profit margins. We favor businesses with visible demand, durable advantages and credible paths from spending to profits rather than treating every AI-related company alike.
- **Opportunities vary across company sizes and global markets.** Smaller U.S. companies trade at more attractive prices than large companies and their own history, but they also face greater pressure from higher financing costs. Analysts forecast 16% earnings growth for foreign developed companies through the remainder of 2026, above their 10-year average of 7%. Emerging markets are producing even faster earnings growth, led by a small number of technology companies whose results set a high bar for future performance. These differences reinforce the value of diversification across regions, industries and company sizes while maintaining a consistent emphasis on earnings quality.

U.S. equity performance

Index	2026 YTD	2025
S&P 500	13.0%	17.9%
Russell 2000	14.1%	12.8%
MSCI EAFE	10.8%	31.9%
MSCI EM	23.7%	34.4%
S&P 500 Sectors		
Communication Services	4.5%	33.6%
Consumer Discretionary	-5.9%	6.0%
Consumer Staples	7.8%	3.9%
Energy	40.3%	8.7%
Financials	-0.1%	15.0%
Health Care	11.7%	14.6%
Industrials	9.9%	19.4%
Information Technology	27.6%	24.0%
Materials	9.7%	10.5%
Real Estate	6.5%	3.2%
Utilities	-5.0%	16.0%

Through September 30, 2026. Returns include dividends.

Sources: FactSet Research Systems, S&P Global.

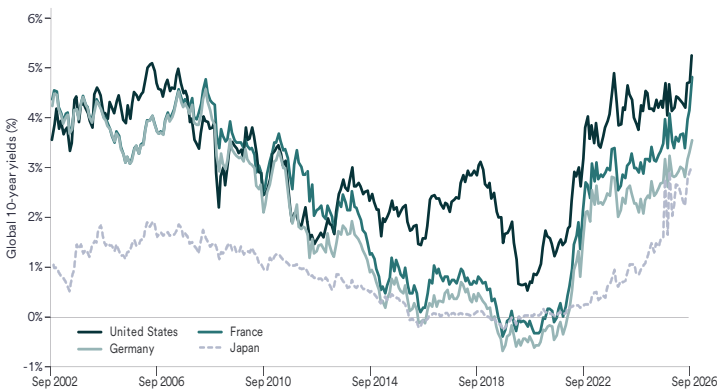
Bond markets

Quick take: Higher policy rates have lowered bond prices but improved prospective income. Government, corporate, municipal and specialty bonds offer distinct benefits, with credit quality and maturity choices shaping portfolio results.

- **Government bonds offer higher income amid persistent rate uncertainty.** The 10-year Treasury yield rose from 4.5% to 5.0% in the third quarter as investors responded to resilient growth, energy-driven inflation and expectations for further policy rate increases. Heavy government borrowing and corporate issuance to fund AI investment also increased the supply of bonds competing for investor demand. Rising yields reduce the value of existing bonds, particularly those with longer maturities, but they also improve the income available from new purchases. Today's starting yields provide more protection against future price changes than investors received during the low-rate years.
- **Corporate and municipal bonds are attractive when investors choose carefully.** Corporate bond yields range from 5.7% to 7.6%, depending on the borrower's financial strength. Healthy cash flow, manageable debt and strong earnings reduce the likelihood that many issuers will miss payments. However, investors receive relatively little additional income for accepting corporate credit risk compared with history, so weaker companies leave less room for error. Municipal bonds offer tax-exempt income, with after-tax-equivalent yields reaching roughly 10% in some cases for investors in the top federal tax bracket.

- **Specialty income strategies can diversify the sources of return.** Mortgages not backed by government agencies benefit from substantial homeowner equity and structures designed to absorb some loan losses before investors are affected. Reinsurance investments pay income in exchange for accepting defined natural disaster risks, with yields above 11%. Pools of high-quality business loans can provide income that changes with short-term interest rates, helping reduce sensitivity to rising rates. These investments involve specialized risks and require careful manager selection, but targeted exposure can complement traditional bonds, broaden income sources, improve overall portfolio flexibility and lessen reliance on a single interest rate or economic outcome.

10-year government bond yields (%)



Sources: U.S. Bank Asset Management Group, Bloomberg, September 30, 2002–September 30, 2026.

Real asset markets

Quick take: Real estate, infrastructure and commodities connect portfolios to property income, electricity demand and energy supply. Rising rates create pressure, while investment in physical capacity supports long-term opportunities.

- **Publicly traded real estate combines income with segment-specific growth.** Real estate investment trusts generate property income equal to about 5.7% of current prices, close to historical averages. Higher interest rates raise financing costs and make bond income more competitive, creating a near-term challenge for real estate shares. Property operations are healthy across many segments. Healthcare properties benefit from aging demographics, retail properties from consumer spending, industrial properties from manufacturing activity and data

centers from AI investment. The office sector remains under pressure but represents less than 3% of broad publicly traded real estate. Diversification across property types reduces the effect of weakness in any one segment.

- **Infrastructure participates directly in the physical investment cycle.** Utilities account for nearly half of broad infrastructure indexes and can provide income through regulated businesses. Rising electricity demand from data centers and broader economic activity supports revenue growth, while industrial companies benefit from construction, equipment spending and improving manufacturing. Pipelines and other energy transportation businesses can also gain as North America expands production and seeks reliable supplies. Rising Treasury yields may pressure infrastructure shares because investors compare their income with bonds, but the long-term need for power, transportation and productive capacity supports sustained investment across these essential systems.
- **Commodities offer inflation sensitivity with substantial price swings.** Oil, natural gas and related products represent nearly one-third of broad commodity exposure, making the U.S.-Iran conflict and global supply routes major drivers of near-term returns. Futures prices for near-term Brent crude oil rose almost 50% during the third quarter due to persistent supply disruptions. Gold and silver may attract investors during periods of geopolitical and fiscal uncertainty, although they produce no income and compete with higher bond yields. Copper may benefit from expanding electricity networks and data center construction. Each commodity follows a distinct supply-and-demand cycle, so broad returns can change quickly.

West Texas Intermediate oil, diesel and gasoline prices



Sources: U.S. Bank Asset Management Group, Bloomberg, September 30, 2021–September 30, 2026.

Private markets

Quick take: Improving deal activity and public listings increase private market liquidity. For appropriate investors, thematic opportunities are attractive when specialized managers combine disciplined analysis, suitable fund structures and patient capital.

- **Improving exit activity is creating a healthier market for private investments.** More public listings and merger activity give private companies additional ways to raise capital or return money to existing investors. These developments address a major challenge from recent years, when limited exits delayed distributions and kept capital tied up longer than expected. Progress will likely remain uneven because transactions depend on market stability, financing costs and buyer confidence. A more active exit market can improve capital flows, but investors should still evaluate each company's business quality and price rather than assume reopening markets make every private investment attractive.
- **Less crowded segments may offer better opportunities for operational improvement.** Capital is concentrated in a relatively small group of large companies and established investment firms. We prefer specialized managers that focus on founder-owned and lower-middle-market businesses, where competition can be less intense and managers can create value through operational improvements rather than borrowed money or rising market prices. Experienced managers can strengthen management, increase efficiency, expand products or enter new markets. This hands-on approach takes time, so investors should evaluate the manager, governance structure and realistic path to exit before committing capital.
- **Disciplined underwriting shapes how investors pursue durable private market themes.** We remain constructive on opportunities tied to AI adoption, rising power demand, aerospace and defense, government services, digital infrastructure and specialized businesses. These themes do not make every company, loan or fund attractive. Experienced managers can identify businesses with durable demand, sound finances and realistic paths to growth while avoiding crowded areas where prices leave little room for disappointment. Senior secured loans to midsize companies can offer income and a strong claim on company assets if problems arise. Certain commercial real estate and energy investments may also benefit from data centers and electrification. Investors must weigh cash flow, debt, collateral, governance, liquidity and fund terms before committing capital.

Alternative investments

Quick take: Widening performance gaps and shifting market conditions create opportunities for flexible hedge fund strategies. Manager skill, position size, liquidity terms and a clearly defined portfolio role remain essential.

- **Managers have reduced broad market exposure while preserving room to act.** Hedge funds, on average, responded to summer volatility by lowering borrowed exposure and reducing their overall dependence on rising markets. This positioning can limit losses if markets fall while giving managers capacity to add targeted investments when prices change. The approach does not eliminate risk, and funds may still take meaningful positions in individual companies or themes. It shifts the source of potential return away from a broad market forecast and toward decisions about which securities look mispriced, how much risk to take and when to adjust exposure.
- **Company selection has become more important than market direction.** Strategies designed to balance investments expected to rise with positions expected to fall have performed well this year. Managers have increasingly focused on differences among individual stocks and bonds instead of relying mainly on broad market hedges. That approach fits an environment in which earnings, financing costs and AI exposure create wider gaps between companies. It can also help when stocks and bonds respond in the same direction to inflation or interest rate changes. Results still depend heavily on security selection, trading discipline and the manager's ability to avoid crowded positions.
- **Flexible mandates can pursue changing opportunities, but design demands scrutiny.** Managers that can move among industries, securities and corporate events may find opportunities as economic conditions and investor preferences shift. Potential areas include companies using AI and machine learning, businesses affected by shareholder activism, and transactions tied to mergers or public listings. Some funds also offer periodic withdrawals, which can improve access but places greater importance on liquidity rules and the types of investments held. Alternative strategies can strengthen diversification for qualified investors when managers control risk carefully, communicate positioning clearly, maintain appropriate liquidity and ensure the allocation serves a specific purpose within the broader portfolio.

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Diversification and asset allocation do not guarantee returns or protect against losses. Based on our strategic approach to creating diversified portfolios, guidelines are in place concerning the construction of portfolios and how investments should be allocated to specific asset classes based on client goals, objectives and tolerance for risk. Not all recommended asset classes will be suitable for every portfolio.



Past performance is no guarantee of future results. All performance data, while deemed obtained from reliable sources, are not guaranteed for accuracy. Indexes shown are unmanaged and are not available for investment. The **S&P 500 Index** is an unmanaged, capitalization-weighted index of 500 widely traded stocks that are considered to represent the performance of the stock market in general. The **Russell 2000 Index** measures the performance of the 2,000 smallest companies in the Russell 3000 Index and is representative of the U.S. small capitalization securities market. The **MSCI EAFE Index** includes approximately 1,000 companies representing the stock markets of 21 countries in Europe, Australasia and the Far East (EAFE). The **MSCI Emerging Markets Index** is designed to measure equity market performance in global emerging markets. The **Consumer Price Index** is a measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. It is one of the most frequently used statistics for identifying periods of inflation or deflation. The **Personal Consumption Expenditures (PCE) Price Index** is a measure of the prices that people living in the United States, or those buying on their behalf, pay for goods and services. It is known for capturing inflation (or deflation) across a wide range of consumer expenses and reflecting changes in consumer behavior.

Equity securities are subject to stock market fluctuations that occur in response to economic and business developments. **International investing** involves special risks, including foreign taxation, currency risks, risks associated with possible difference in financial standards and other risks associated with future political and economic developments. Investing in **emerging markets** may involve greater risks than investing in more developed countries. In addition, concentration of investments in a single region may result in greater volatility. Investing in **fixed income securities** is subject to various risks, including changes in interest rates, credit quality, market valuations, liquidity, prepayments, early redemption, corporate events, tax ramifications, and other factors. Investments in debt securities typically decrease in value when interest rates rise. The risk is usually greater for longer-term debt securities. Investments in lower-rated and non-rated securities present a greater risk of loss to principal and interest than higher-rated securities. Investments in **high yield bonds** offer the potential for high current income and attractive total return but involve certain risks. Changes in economic conditions or other circumstances may adversely affect a bond issuer's ability to make principal and interest payments. The **municipal bond market** is volatile and can be significantly affected by adverse tax, legislative or political changes and the financial condition of the issuers of municipal securities. Interest rate increases can cause the price of a bond to decrease. Income on municipal bonds is free from federal taxes but may be subject to the federal alternative minimum tax (AMT), state and local taxes. There are special risks associated with investments in **real assets** such as commodities and real estate securities. For commodities, risks may include market price fluctuations, regulatory changes, interest rate changes, credit risk, economic changes and the impact of adverse political or financial factors. Investments in real estate securities can be subject to fluctuations in the value of the underlying properties, the effect of economic conditions on real estate values, changes in interest rates and risks related to renting properties (such as rental defaults). **Hedge funds** are speculative and involve a high degree of risk. An investment in a hedge fund involves a substantially more complicated set of risk factors than traditional investments in stocks or bonds, including the risks of using derivatives, leverage and short sales, which can magnify potential losses or gains. Restrictions exist on the ability to redeem or transfer interests in a fund. **Private capital investment funds** are speculative and involve a higher degree of risk. These investments usually involve a substantially more complicated set of investment strategies than traditional investments in stocks or bonds, including the risks of using derivatives, leverage, and short sales, which can magnify potential losses or gains. Always refer to a Fund's most current offering documents for a more thorough discussion of risks and other specific characteristics associated with investing in private capital and impact investment funds. Reinsurance allocations made to **insurance-linked securities (ILS)** are financial instruments whose performance is determined by insurance loss events primarily driven by weather-related and other natural catastrophes (such as hurricanes and earthquakes). These events are typically low-frequency but high-severity occurrences. **Private equity investments** provide investors and funds the potential to invest directly into private companies or participate in buyouts of public companies that result in a delisting of the public equity. Investors considering an investment in private equity must be fully aware that these investments are illiquid by nature, typically represent a long-term binding commitment and are not readily marketable. The valuation procedures for these holdings are often subjective in nature. **Private debt investments** may be either direct or indirect and are subject to significant risks, including the possibility of default, limited liquidity and the infrequent availability of independent credit ratings for private companies.

Includes AI-generated performers.