Global Asset Allocation Perspectives & Investment Backdrop

2026 OUTLOOK

Scotia Global Asset Management®

Market recap

Global markets proved remarkably resilient in 2025 as moderating inflation, solid earnings and a softer U.S. dollar supported risk assets despite tariffs and geopolitical tensions. Artificial intelligence remained the key driver of large-cap technology returns, yet leadership gradually broadened beyond these areas across regions and sectors. At the same time, AI's rapid build-out is encountering physical and financial constraints, prompting investors to reassess how sustainable current growth expectations may be on these AI-linked names. Beyond technology, diversification was crucial, as Canadian and emerging-market equities outpaced the U.S. market, while fixed income benefited from declining yields in the fall and tighter credit spreads. Against this backdrop, **AI is set to remain a central theme for financial markets in 2026, but its influence is likely to be expressed through a broader range of sectors and companies than in 2025**.

Equities

- **The S&P/TSX Composite delivered a standout 31.7% return in 2025**, fueled by exceptional gains in Materials (100.6%) and strong performance in Financials (35.3%), despite gloomy Canadian economic headlines.
- **The S&P 500 returned a solid 12.4% for the year**, even as U.S. consumer sentiment sat near historical lows, with leadership broadening beyond the initial AI frontrunners; AI themes remained evident through strong results in Communication Services (27.3%) and Information Technology (18.2%), particularly among the large U.S. technology leaders, referred to as the "Magnificent 7" (Apple, Microsoft, Alphabet, Amazon, Meta, Nvidia and Tesla), and other AI-linked names.
- **MSCI Emerging Markets (28.1%) and MSCI EAFE (25.7%) posted strong gains**, outpacing U.S. equities as AI adoption, particularly amid China's recovery, together with supportive currency moves reinforced the value of global diversification for investors.

Fixed income

- **The FTSE Canada Universe Bond Index returned 2.6% in 2025**, as the bond market notched a solid fourth quarter and ended the year on a high note, supported by declining yields across the curve and broad price gains.
- **The Federal Reserve (Fed) lowered its policy rate to 3.75% after three consecutive 25-basis-point cuts** in the second half of 2025, while the Bank of Canada reduced its policy rate by 1%, further extending its aggressive easing cycle.
- **Short-term yields declined toward year-end as the Fed continued to cut rates**, setting the stage for further yield-curve steepening as investors demanded greater compensation for holding longer-dated government bonds relative to shorter maturities.

Alternatives

Private markets in 2026 are expected to be resilient and opportunity-rich, with stable growth and lower interest rates supporting deal activity and liquidity, while AI-driven innovation and business transformation underpin value creation.

- **Private equity enters 2026 with renewed deal and exit momentum that began in the second half of 2025**, driven by take-privates, carve-outs, and mid-market buyouts, supported by lower rates and broadly available credit, while elevated public market valuations have helped revive IPO activity and bolster liquidity alongside continued growth in secondary transactions.
- **In private credit, available yields have moderated from late-2023 highs but still offer an attractive premium over liquid public-market equivalents**, the market remains healthy with default rates below long-term averages, and loan volumes are expected to be robust in 2026 as M&A accelerates on the back of improving conditions in the private equity market.
- **In real assets, infrastructure is expected to be a major contributor to global growth in 2026**, supported by strong fundraising for energy-transition, digital-infrastructure, and essential-services strategies, while AI drives substantial capital demand for data centres, power generation, and grid upgrades.

Market outlook

As we enter 2026, the investment landscape presents a compelling mix of opportunities and complexities. Global equities are well-positioned for continued gains, supported by resilient corporate earnings, moderating inflation, and broadly accommodative central bank policy. Leadership is evolving beyond the narrow AI-driven concentration of recent years, with strength broadening across sectors and geographies – particularly in Canadian cyclicals, international markets and select emerging economies. Meanwhile, fixed income remains attractive despite rate-cutting cycles nearing completion, as credit fundamentals stay solid.

Portfolio view

- **We favour a modest overweight to equities relative to a traditional 60/40 benchmark**, reflecting confidence that the current expansion can continue as corporate earnings, inflation, and interest rates remain broadly supportive.
- **We anticipate stocks will trend higher over the next 12–18 months** as earnings momentum broadens and policy remains supportive.
- **Our view reflects optimism around resilient economic conditions** and the ongoing strength of global equities across regions.
- **Active risk management and broad global diversification remain essential** elements of prudent portfolio positioning in this environment.

Here's what we are watching

- **Concentration risk** could trigger broader market weakness if mega-cap technology stocks remain extremely concentrated or underperform.
- **Earnings deceleration** could signal economic slowdown if corporate earnings growth slows or margin compression accelerates.
- **Inflation persistence** could force central banks to reverse their easing course if core inflation reaccelerates or wage growth remains elevated.
- **Policy missteps** could create instability if central banks tighten prematurely or maintain accommodation too long.
- **Credit market stress** could indicate deteriorating corporate health if investment-grade and high-yield spreads widen significantly.
- **Geopolitical escalation** could alter growth if energy supply chains face disruption or tariffs materially impact trade flows

"As we look to 2026, our outlook remains positive: the opportunity set is still attractive, even if volatility arises. Earnings momentum is broadening well beyond a handful of mega-cap names, and global growth remains resilient. Today's tech leaders are profitable and well-capitalized, differentiating this cycle from past bubbles. While market concentration remains a risk, it highlights why true diversification is essential for long-term resilience. We continue to focus on building resilient portfolios that can capture opportunity and manage risk… ready for whatever lies ahead."

- Craig Maddock, VP & Senior Portfolio Manager, Head of Multi-Asset Management

Forecasts of asset class performance

Fixed Income	Outlook	Comments
Overall Fixed Income	–	Bond yields remain elevated, providing attractive income alongside the potential for capital appreciation. At the same time, global rate cutting cycles appear at or near their end, and while labour markets have softened, the equity market has shown notable resilience and offers greater upside potential than bonds.
Rates		
Canada and U.S.	+	The Fed is likely to deliver more cuts over 2026 than the Bank of Canada, which appears to be at the end of its easing cycle, with markets even pricing a rate hike as the next move. The US yield curve can steepen under several scenarios, including a sharper than expected slowdown that forces larger policy easing, or renewed concerns over Fed independence that push long-term yields higher.
Global	+	UK gilts have been a focal point for global bond market concerns, with skepticism over the fiscal trajectory and recent budgets pushing yields higher. Target long duration in the UK, as the latest budget has helped calm bond vigilantes and stabilize sentiment, creating room for yields to move lower and better reflect underlying fundamentals. By contrast, favour short duration in Germany, where plans to ease borrowing constraints to support growth are likely to increase bond issuance and put upward pressure on yields.
Credit		
Investment Grade	0	Credit spreads spent most of last year at historically tight levels, despite a brief widening episode in April, leaving limited room for further compression. At current valuations, prefer to stay patient and wait for a more attractive entry point before increasing exposure.
High-Yield	0	High yield bonds, like investment-grade, are trading at historically tight spreads. Recent signs of deterioration in the lowest-rated CCC segment suggest greater risk of spread widening than scope for further compression. In this context, the additional yield currently available in high yield is not sufficient to warrant an overweight allocation, and instead supports a cautious stance to high yield.
Equities	**Outlook**	**Comments**
Overall Equities	+	Quarter-over-quarter, our view has not changed – pockets of concern remain present, but the overall global economy is proving very resilient and adaptive in the face of shifting trade and policy dynamics. Under the surface, technological progress, particularly around AI and automation, continues at an accelerated pace, driving genuine productivity gains and earnings growth even as it contributes to elevated valuations and rising market concentration in a handful of global leaders. While inflation remains somewhat sticky in certain regions, it has moderated meaningfully from prior peaks, and labour markets have transitioned from extremely tight to more balanced conditions, which, together with softer growth momentum, tilts central banks toward gradual policy easing rather than further tightening. As a result, should a slowdown occur, there is now more room for monetary policy to be supportive, which helps to cushion downside risks and reduces the probability of a disorderly, systemic selloff in risky assets, even if periodic volatility spikes are likely.
Region		
Canada	0	The outlook on Canadian equities remains neutral when compared with other global stock markets. From a monetary policy perspective, the Bank of Canada has delivered substantial monetary easing, but is now at end of this rate-cutting phase, so incremental stimulus from here is likely to be limited. On the trade front, despite headline risks around new U.S. tariffs, Canada's USMCA framework keeps effective U.S. duties on Canadian exports well below those faced by many other countries, preserving a relative competitive edge. At the same time, Canadian stocks have significantly outpaced many peers, driven largely by outsized gains in gold-linked miners and the banking sector, which together make up a large share of the TSX. For domestic investors, that strength has been very positive, but from a portfolio-construction standpoint it makes it harder to assume that Canada will keep outperforming, so a more balanced weighting is preferred rather than betting on ongoing leadership.
U.S.	0	The stance on U.S. equities remains broadly neutral when compared to other global stock markets. While the recent pace of policy shifts has eased somewhat, the current U.S. administration has a history of abrupt decisions, creating an operating backdrop that can be challenging for American businesses. Beneath the surface, many of the world's most innovative and dynamic public companies can be found in the U.S., but the enthusiasm around these leaders has pushed their valuations to increasingly stretched levels. If even a few of the dominant U.S. mega-cap names disappoint, the downside could be significant, given that the S&P 500 has effectively evolved into a concentrated, tech-heavy growth index with other sectors playing a shrinking role. Because an overall tilt toward equities already results in a sizeable tactical allocation to U.S. stocks, there is little justification to amplify our portfolios' concentration risks.
International	0	We continue to have a neutral view to international equities relative to other markets. Although risks remain to trade-dependant international markets from changing US trade policies, they're offset by the opportunity presented by far more compelling valuations. Meanwhile a shift to increasing fiscal stimulus for infrastructure and defense initiatives has helped boost overall competitiveness, notably in Europe. From a currency perspective, there continues to be the potential for tailwinds as many European and Asian currencies are undervalued vis-a-vis the US dollar. The valuation and growth opportunities are seen as balanced with the US trade policy uncertainty risks, and while we are overweight global equities generally, it has not led us to further concentrate in International equities within that allocation.
Emerging Markets	0	We continue to have a neutral view to emerging market equities relative to other markets. Trade related risks have narrowed as various deals have been made with several countries, most notably with China. While risks remain high for emerging markets these have changed from more trade related to geopolitical. Economic data out of China remains challenged, but excitement over new AI and technology sectors is offseting those headwinds within Chinese equity markets. Outside China, economic growth has been resilient and could benefit from a modest upswing in the developed markets. While these factors continue to support recent positive momentum, shifts in sentiment can be abrupt and unpredictable. Thus, it remains prudent not to allow portfolios to become overly concentrated in emerging market equities, even as the near-term outlook is favourable.

Legend: ++ Overweight + Neutral-overweight 0 Neutral – Neutral-underweight –– Underweight

Market performance - as at December 31, 2025

Fixed Income						
Bonds	**3-mth**	**6-mth**	**YTD**	**1-yr**	**3-yr CAGR**	**5-yr CAGR**
FTSE Canada Universe Bond C$	-0.32%	1.19%	2.64%	2.64%	4.51%	-0.35%
Universe Canada All Corporate C$	0.34%	2.16%	4.48%	4.48%	6.60%	1.49%
Morningstar CAN High-Yield Fixed Inc C$	1.06%	4.01%	6.74%	6.74%	8.62%	3.83%
ICE BofAML U.S. Corporate C$	0.28%	2.46%	5.86%	5.86%	4.90%	-0.79%
ICE BofAML U.S. High Yield C$	-0.19%	4.20%	3.35%	3.35%	10.37%	5.98%
Bloomberg U.S. Aggregate Bond U$	1.10%	3.15%	7.30%	7.30%	4.66%	-0.36%
Bloomberg Global Aggregate U$	0.24%	0.84%	8.17%	8.17%	3.97%	-2.14%
Equities						
Canadian Equities	**3-mth**	**6-mth**	**YTD**	**1-yr**	**3-yr CAGR**	**5-yr CAGR**
S&P/TSX Composite C$	6.25%	19.53%	31.68%	31.68%	21.42%	16.32%
U.S. Equities						
S&P 500 C$	1.13%	11.50%	12.35%	12.35%	23.48%	16.11%
Dow Jones Industrial Avg C$	2.52%	10.69%	9.58%	9.58%	15.87%	13.19%
NASDAQ C$	1.20%	14.97%	15.46%	15.46%	32.45%	15.09%
Global Equities						
MSCI World C$	1.67%	11.30%	15.90%	15.90%	22.19%	14.32%
MSCI Asia Pacific ex-Japan C$	1.85%	17.84%	29.79%	29.79%	17.08%	5.60%
MSCI Japan C$	1.72%	12.21%	19.19%	19.19%	18.42%	8.56%
MSCI Europe C$	4.69%	10.66%	29.86%	29.86%	19.43%	12.62%
MSCI Emerging Markets C$	3.23%	16.79%	28.05%	28.05%	17.43%	6.21%

Source: Bloomberg, Morningstar

Multi-Asset Management Team

Craig Maddock, CFA, MBA, CFP, FICB
VP & Sr. Portfolio Manager, Head of Multi-Asset Management

Wesley Blight, CFA
VP & Portfolio Manager

Ian Taylor, CFA, CAIA
VP & Portfolio Manager

Yuko Girard, CFA, MBA, CAIA, FRM
VP & Portfolio Manager

Mark Fairbairn, CFA
VP & Portfolio Manager

Jenny Wang, CFA, MA
Portfolio Manager

Richard Schmidt, CFA
Portfolio Manager

In collaboration with:
2 Associate Portfolio Managers | 8 Analysts
1 Trader & Portfolio Manager | 2 Portfolio Specialists

As Portfolio Managers for ScotiaFunds and Dynamic Funds managed-asset programs, the Multi-Asset Management Team oversees over $140 billion* in multi-asset solutions and strategies. The Team is responsible for portfolio construction, asset allocation policy, and investment strategy research and selection. The Team is also involved in the due diligence and day-to-day management of all portfolio solutions.

*As at December 31, 2025

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