

Executive summary



NEW YEAR 2026



Eric Savoie, MBA, CFA, CMT
Senior Investment Strategist
RBC Global Asset Management Inc.



Daniel E. Chornous, CFA
Global Chief Investment Officer
RBC Global Asset Management Inc.

We forecast an environment of moderate economic growth with inflation subsiding sufficiently to motivate continued interest-rate cuts by the U.S. Federal Reserve (Fed) and foster strong corporate profit growth. We still expect stocks to outperform bonds, but recognize the potential for outsized gains has diminished following this year's strong performance that pushed some valuations to extreme levels.

Important tailwinds support modest growth acceleration in 2026

Slowing growth due to U.S. tariffs and tumbling immigration was partially offset in 2025 by fiscal stimulus and continued interest-rate cuts by central banks. We believe economic growth should accelerate moderately in the year ahead and may pleasantly surprise relative to consensus expectations. Tariff headwinds should fade, and important tailwinds are set to blow. These beneficial forces include

interest-rate cuts, further fiscal stimulus, low oil prices, a positive stock-market wealth effect, further growth in artificial-intelligence (AI) expenditures and the early stages of an AI-driven productivity boost. The U.S. economy should remain among the developed-world's economic growth leaders.

Modest inflation improvement expected in the year ahead

Inflation remains too high in the U.S. and is slightly elevated in several other developed markets due to tariffs and post-pandemic scarring. Our CPI forecasts are slightly above consensus for 2026, reflecting aggressive central-bank easing amid persistent inflation and large fiscal deficits that may encourage higher inflation tolerance.

However, this should still allow year-over-year inflation to peak in spring 2026 and then slowly ease. Several factors support this view: the U.S. labour market is cooling, the tariff impact on inflation is relatively tame, shelter costs are easing and oil prices are low. On the whole, inflation may not fall by quite as much as consensus expectations, but there is room for improvement in the year ahead.

New year could bring renewed U.S.-dollar weakness

The two-year-long fall in the U.S. dollar appears to have temporarily halted, challenging our forecasts that the greenback would continue to decline through 2025 and into next year. The dollar's modest rally since September stems from a view that stronger-than-expected U.S. economic growth and continued technology investments will underpin Treasury yields, at least in the short term. We note that the

dollar is still down by 9% so far this year, and there is good reason to expect a resumption in the greenback's weakness sometime in 2026. Emerging-market currencies, in our opinion, will continue to be the main beneficiary of further U.S.-dollar depreciation given improving fiscal situations and attractive bond yields.

Monetary easing cycle still has room to run

The clock has not yet run out on this monetary easing cycle. We budget for a bit more economic help, both due to the lagged effect of earlier rate cutting and future impact of additional easing to come. The U.S. Federal Reserve (Fed), in particular, can afford to deliver several more rate cuts

as it moves from a restrictive to a neutral stance, and the Fed's recent move to end quantitative tightening is also supportive. The prospect of a more dovish board voting lineup in 2026 supports this view. In our view, the Bank of England also appears to have space for further easing.

Upside is limited in sovereign and corporate bonds

The outlook for medium- and longer-term government-bond yields differs from short-term rates because risk premiums embedded in real yields could keep the U.S. 10-year yield from falling meaningfully from here. Our model argues the 10-year yield should theoretically fall from the current 4.0%, but in practice this depends not just on inflation pressures subsiding, but also on a diminishment in concerns about governments' fiscal health. With governments seemingly content to continue running large deficits, we forecast that government fixed-income assets will deliver coupon or cash-like returns.

The added compensation for taking credit risk is historically small with the gap between government-bond yields and corporate-bond yields at its narrowest since the Global Financial Crisis. That said, conditions for sustained spread widening are not present as corporate default risk is low. The narrow-spread environment could persist, and this phase of the credit cycle is often a lengthy one, especially when recession concerns are relatively subdued.

Equities soared to records but value remains in some areas outside of U.S. megacap stocks

Equity markets ultimately found their footing in 2025 and rewarded investors with strong returns in most major markets. The strong gains mean that valuations have been creeping higher almost everywhere, and the overvaluation story is no longer just a U.S. large-cap phenomenon. The S&P 500 is the most expensive, but equity markets in Canada and Japan are also close to a full standard deviation above their fair values. Stock indices in Europe and emerging markets continue to trade at attractive distances below their fair value.

Profit growth will be increasingly critical to sustaining any further advance in the S&P 500. The good news is that expansion in profit margins has helped to convert modest revenue growth into double-digit earnings growth. If profit margins rise by one percentage point next year, as they did this year and as analysts expect, double-digit profit growth is attainable in 2026. Generating decent returns from here would require the P/E to remain at least 1 standard deviation above equilibrium or for earnings to beat expectations. A positive outcome is certainly possible but given that valuations are historically stretched, the market is vulnerable to any disappointment.

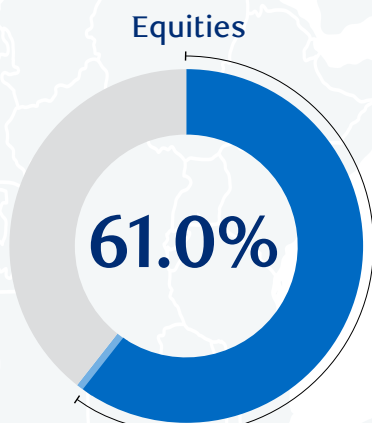
Asset mix – trimming equity overweight and narrowing tilt to non-U.S. regions

Our base case is for moderate economic growth and inflation calming enough to allow the Fed to continue cutting interest rates. Against this backdrop, we expect sovereign bonds to deliver cash-like returns and offer ballast against equity-market volatility should the economy disappoint. We expect stocks will continue to outperform bonds but note that potential for outsized gains has diminished after this year's strong run lifted valuations to extremes in some areas. Accordingly, we have reduced our equity overweight by one percentage point this quarter and placed proceeds in cash.

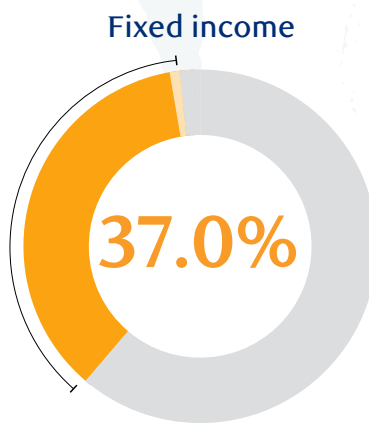
We also used this opportunity to modify regional equity allocations by increasing U.S. equity exposure, acknowledging that strong momentum in megacap technology stocks could persist. However, we remain underweight U.S. equities given their relatively high valuations. Consequently, we trimmed international equity exposure while maintaining a slight overweight given their relatively appealing valuations. For a balanced global investor, our current recommended asset mix is 61.0% equities (strategic neutral: 60.0%), 37.0% bonds (strategic neutral: 38.0%) and 2.0% cash.

Recommended asset mix

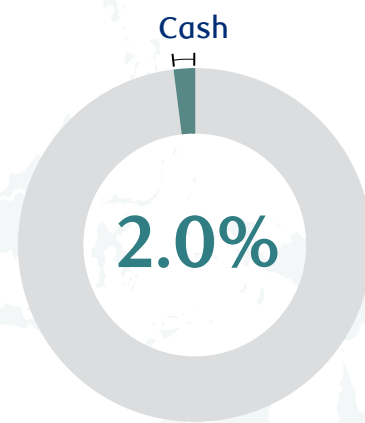
RBC GAM Investment Strategy Committee



Strategic neutral position:
60 percent



Strategic neutral position:
38 percent



Strategic neutral position:
2 percent

Note: As of November 30, 2025. Source: RBC GAM

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Publication date: December 15, 2025

32467 (12/2025)

EXECUTIVE SUMMARY_NEW YEAR 2026_E 12/15/2025

