

Market outlook



NEW YEAR 2026

High hopes for 2026



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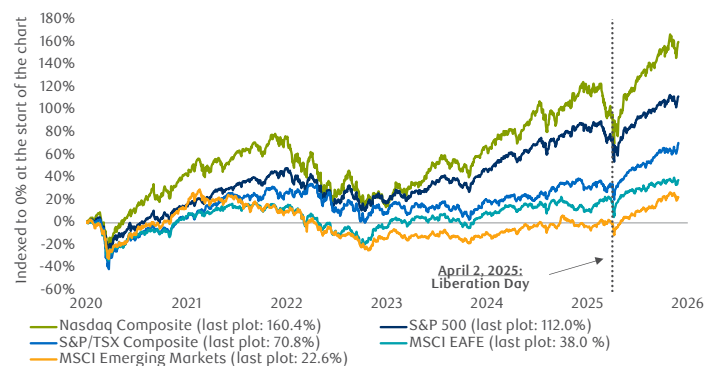
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Financial markets were highly volatile earlier this year as the economy faced a variety of intense challenges but, as time progressed, risks appeared to subside and growth ultimately prevailed. While large-scale tariffs initially created significant uncertainty, it became increasingly clear that many of Trump’s more extreme tariff announcements were negotiation tactics aimed at generating quick trade deals. Moreover, geopolitical tensions faded after a ceasefire in the Middle East and progress toward a peace plan between Russia and Ukraine, and declining short-term interest rates have provided a boost amid elevated levels of government debt. All in all, the challenges facing the economy are so far being managed, and the macroeconomic backdrop favours continued economic expansion. Growth may even accelerate in 2026, helped by falling interest rates and fiscal stimulus from the One Big Beautiful Bill.

In this macroeconomic environment, stocks performed remarkably well as investors grew increasingly excited about the benefits of artificial intelligence (AI). Most major stock-market indices enjoyed a powerful rebound following the tariff-induced slump earlier this year, climbing to records by the summer and extending those gains into the fall (Exhibit 1). Given concerns of an AI bubble, further stock gains may require other drivers, including confidence in the economic outlook and sustained earnings improvement. At this point, investors are extremely optimistic (Exhibit 2) and many expect that 2025’s strong profit growth will continue into 2026.

Bond markets have been relatively calm compared to equity markets this year, although yields fluctuated as investors weighed the impact of slower economic growth and falling short-term interest rates against a backdrop of higher

Exhibit 1: Major equity-market indices
Cumulative price returns indices in USD



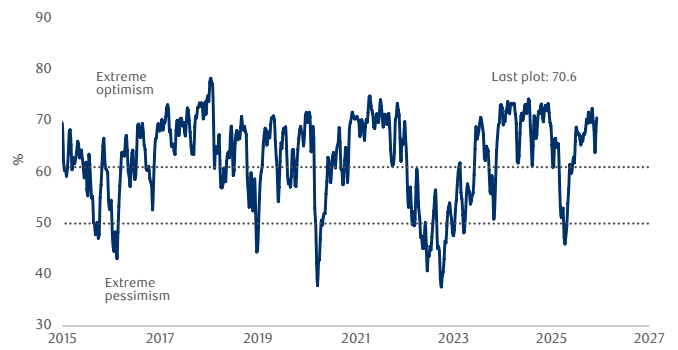
Note: As of November 28, 2025. Source: Bloomberg, RBC GAM

inflation and rising government deficits. The U.S. 10-year yield has settled near 4.0%, slightly below the 4.5% level at the start of the year. Our model suggests scope for continued declines in yields (Exhibit 3) as long as inflation stays under control and concerns about government deficits do not take centre stage.

Our base case scenario sees the economy continuing to expand at a moderate pace and inflation calming enough to allow the U.S. Federal Reserve (Fed) to continue cutting interest rates over the year ahead. Against this backdrop, we expect sovereign bonds to deliver cash-like returns and offer a ballast against equity-market volatility should the economy disappoint. Our current view is that stocks will continue to outperform bonds, though the potential for outsized gains in stocks has diminished after this year’s strong run lifted valuations to extremes in some areas.

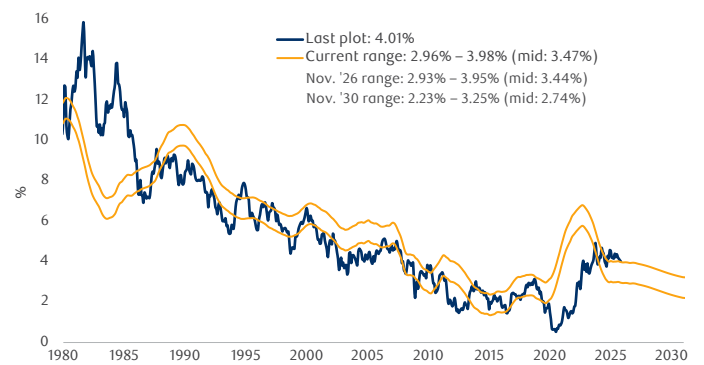
As a result, we have reduced our equity overweight position by one percentage point this quarter and placed the proceeds in cash. We have also used this opportunity to modify our regional equity allocations by increasing our exposure to U.S. equities in a move acknowledging that strong momentum in megacap technology stocks could persist. We nevertheless remain underweight U.S. equities given their relatively high valuations. Consequently, we have trimmed our exposure to international equities while maintaining a slight overweight position 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.

Exhibit 2: Ned Davis Research Crowd Sentiment Poll
Percent bulls



Note: As of December 4, 2025. Source: Ned Davis Research, RBC GAM

Exhibit 3: U.S. 10-year T-bond yield
Equilibrium range



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



Fed resumes interest-rate cuts

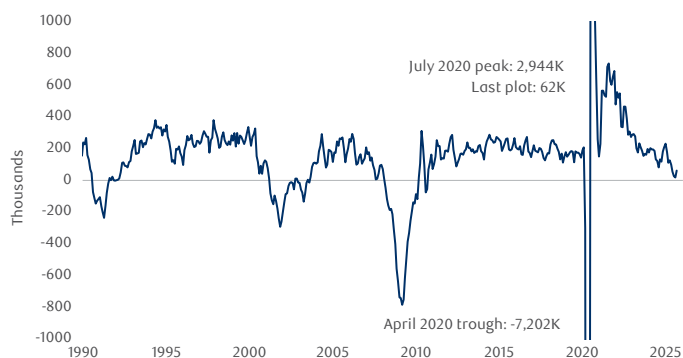
Softening labour-market data ultimately pushed an increasingly divided Federal Open Market Committee (FOMC) to lower interest rates after being on hold all year. The Fed lowered its policy rate by 25 basis points in September, October and December, and expects to continue lowering rates gradually over the year ahead amid slowing job gains and a rising unemployment rate (exhibits 4 and 5). Adding to the idea that the U.S. may continue cutting rates in 2026 is that a new Fed chair is expected to be appointed in the spring to replace Jerome Powell, and the U.S. administration would prefer someone who favours lower rates. As a result, market measures

indicate two more 25-basis-point reductions over the year ahead, in line with our own base case view (Exhibit 6).

Complicating this benign outlook on interest rates are lingering inflation pressures. At 3.0%, U.S. CPI headline inflation and core inflation remain modestly above the Fed’s 2% target, and both have been rising since the summer (Exhibit 7). FOMC members appear to believe, however, that elevated price pressures are a result of tariffs, a temporary effect on the year-over-year measure that should subside later in 2026. The risk is that if inflation proves more stubborn, as it did in 2021 and into 2022, the Fed may be limited in the degree of accommodation it can deliver.

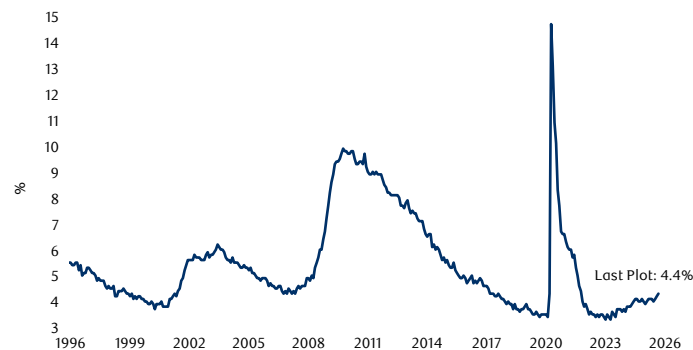
Exhibit 4: United States

Monthly change in non-farm employment (3mma)



Note: As of September 2025. 3mma = 3 months moving average. Source: Bureau of Labor Statistics

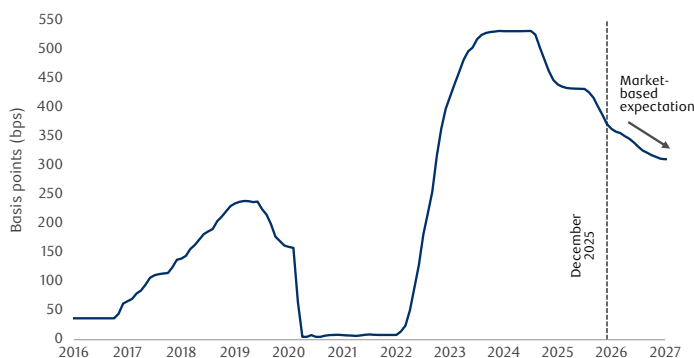
Exhibit 5: U.S. unemployment rate



Note: As of September 2025. Source: Bloomberg, RBC GAM

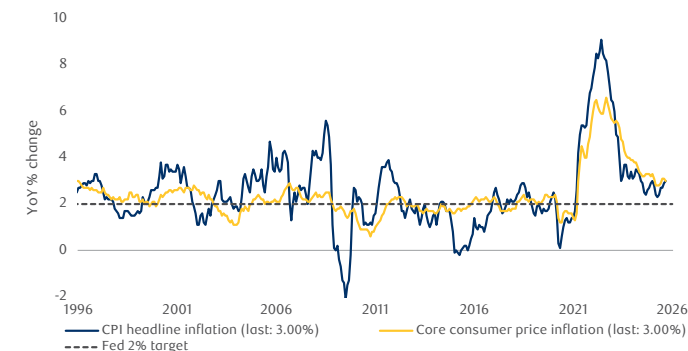
Exhibit 6: Implied fed funds rate

12-months futures contracts as of December 10, 2025



Source: Bloomberg, U.S. Federal Reserve, RBC GAM

Exhibit 7: U.S. inflation measures



Note: As of September 30, 2025. Source: Bloomberg, RBC GAM

Sovereign bonds offer at least cash-like returns with only modest valuation risk

The outlook for medium- and longer-term government bond yields is a bit different than it is for short-term interest rates because the risk premium embedded in real yields could keep the U.S. 10-year yield from falling meaningfully from here. Exhibit 8 breaks down our bond model, which combines an inflation premium with a real yield to generate an estimate for the nominal yield. As of this writing, the inflation premium is close to the modelled level, but the real (i.e. after-inflation) yield is 70 basis points higher than we would expect. The higher real rate is partly a reflection of investor concerns around ballooning U.S. fiscal deficits. Our model argues that the 10-year yield should fall from the current 4.0%, but we would emphasize that the modelled trajectory depends

not just on inflation pressures subsiding, but also on a diminishment in concerns about governments' fiscal health. In reality, yields are unlikely to fall much further unless these worries are assuaged.

Yields in most major government bond regions around the world are also being supported by high real interest rates. All 10-year government bond yields except Japan's are near or above the upper end of their modelled equilibrium bands (page 38). The Japanese 10-year yield is an exception because it started from a relatively low level and has been adjusting higher to firmer inflation pressures and a new prime minister who recently announced plans for sizeable fiscal stimulus. With governments all around the world expressing few qualms about running large deficits, we are

Exhibit 8: U.S. 10-year bond yield

Fair-value estimate composition



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

hesitant to bank on any meaningful capital appreciation from sovereign bonds over the year ahead. As a result, we forecast that government fixed-income assets will deliver coupon or cash-like returns.

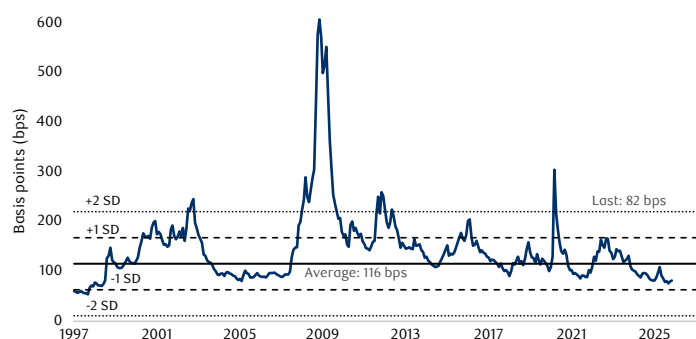
Credit markets offer little compensation for risk taking

Fixed-income investors looking for higher returns may find greater potential in corporate bonds, but the added compensation for taking this risk is historically small. The gap between government-bond yields and corporate-bond yields is the narrowest it has been since the aftermath of the 2008-2009 financial crisis for both investment-grade and high-yield securities (exhibits 9 and 10). The relatively limited

compensation that fixed-income investors are being paid for taking on credit risk suggests they may not want to take on excessive exposure to corporate bonds.

That said, the conditions for a sustained widening in spreads are not in evidence. Corporate leverage is the lowest it has been in the past decade and interest-coverage ratios have been strengthening since the start of the year (exhibits 11 and 12). These metrics suggest corporate balance sheets are strong and that companies are well positioned to meet their financial obligations. As a result, the risk of corporate defaults is low, and the narrow-spread environment could persist barring deterioration in the economy or corporate earnings. Indeed, this phase of the credit cycle is often a lengthy one, especially when recession concerns are relatively subdued.

Exhibit 9: ICE BofA Canada Corporate Index spread



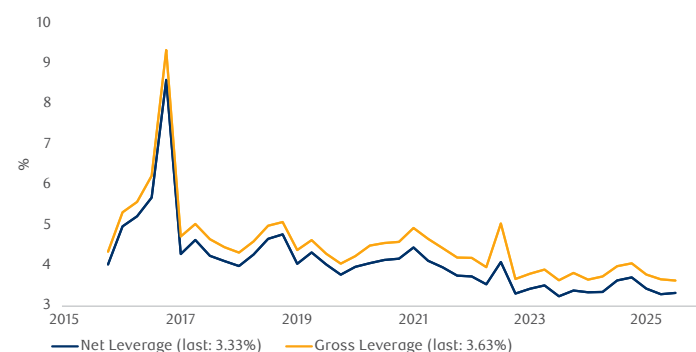
Note: As of November 28, 2025. Source: ICE BofA, Bloomberg, RBC GAM

Exhibit 10: ICE BofA US High Yield Index spread



Note: As of November 28, 2025. Source: ICE BofA, Bloomberg, RBC GAM

Exhibit 11: S&P/TSX Composite non-financial companies – Gross & net leverage



Note: As of Q3 2025. Net leverage means cash & equivalents are subtracted from total debt. Source: Bloomberg, RBC GAM

Exhibit 12: S&P/TSX Composite non-financial companies – Interest coverage



Note: As of Q3 2025. Source: Bloomberg, RBC GAM

Stocks delivered impressive gains, valuations creeping higher

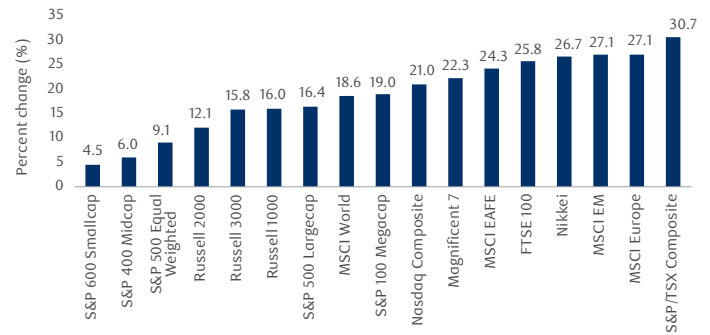
Equity markets ultimately found their footing in 2025 and rewarded investors with strong returns in most major markets. Exhibit 13 plots year-to-date price returns for a variety of indices in U.S. dollars. The rewards were such that the S&P 500 Index's impressive 16.4% gain situated it in the middle of the pack. Small-cap stocks underperformed, while most international markets outperformed the S&P 500 by a wide margin. The MSCI EAFE, MSCI Emerging Markets, MSCI Europe and S&P/TSX Composite rose 24.3%, 27.1%, 27.1%, and 30.7%, respectively.

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. At 13.6% above fair value, our global composite of equity-market valuations suggests stocks are now the most expensive they've been since early 2022 (Exhibit 14). Within the composite, 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 values. Stock indices in Europe and emerging markets continue to trade at attractive distances below their fair value (page 39). If we exclude the U.S. from our composite, global equities in aggregate are still 5.4% below fair value, indicating that a significant fraction of markets offer the potential for decent returns.

Expanding profit margins fueled double-digit S&P 500 profit growth

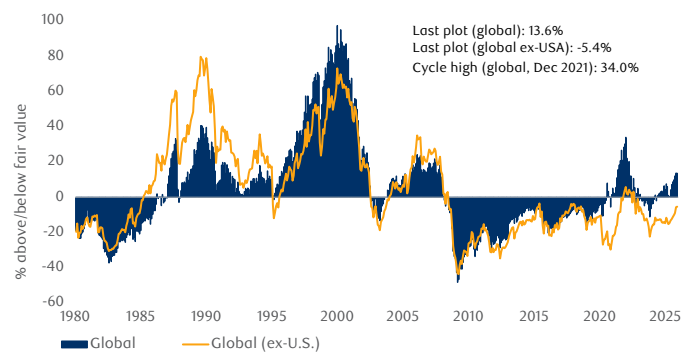
With the S&P 500 trading at an expensive valuation, profit growth will be increasingly critical to sustaining any further advance in stocks. The good news is that expansion in S&P 500 profit margins has helped to convert modest revenue growth into double-digit earnings growth. Any drag from tariffs was offset by falling interest rates and improved efficiencies helped in part by AI advancements, lifting profit margins by a full percentage point to 13% at the start of the year (Exhibit 15). This is a meaningful increase because every one-percentage-point increase in profit margin from current levels boosts earnings by 7% to 8%. As a result, even a slow pace of economic growth is sufficient to generate double-digit profit gains in an environment where profit margins are expanding at such a pace. Our forecasts suggest 5% revenue growth based on the historical relationship between sales

Exhibit 13: Major indices' price change in USD
2025 year-to-date



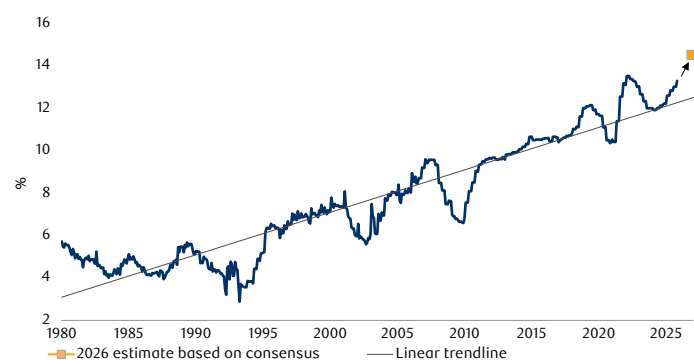
Note: As of November 28, 2025. Magnificent 7 includes Apple, Microsoft, Alphabet, Amazon, Nvidia, Meta and Tesla. Source: Bloomberg, RBC GAM

Exhibit 14: Global stock-market composite
Equity market indexes relative to equilibrium



Note: As of November 28, 2025. Source: RBC GAM

Exhibit 15: S&P 500
Net Margin



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

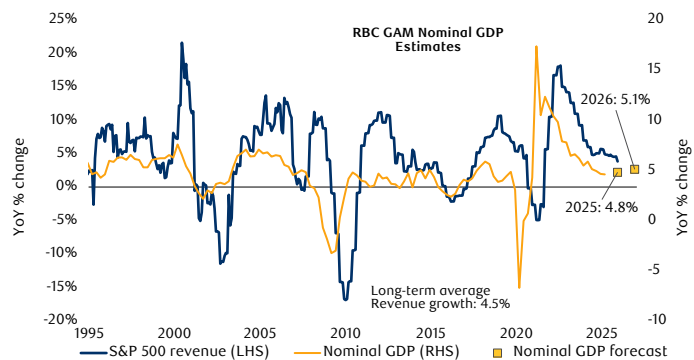
growth and nominal GDP (Exhibit 16). If analysts are right in their expectation for another one-percentage-point increase in profit margins next year, double-digit profit growth is attainable in 2026.

Earnings have been coming in significantly better than expected and analysts' estimates have been rising. In the latest period, 83% of earnings releases beat analysts' expectations, the most since early 2021 (Exhibit 17). The consensus earnings estimate is for 14.6% earnings growth in 2026 following expectations of 13.0% for the current year (Exhibit 18).

S&P 500 highly concentrated with Magnificent-7

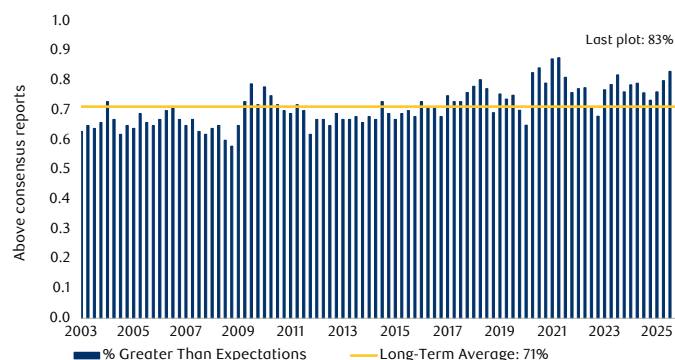
One of the main challenges for the U.S. large-cap equity market is that its performance has become increasingly dependent on a handful of companies that are trading at what may be very expensive valuations. The Magnificent-7 (Mag-7: Apple, Microsoft, Google, Amazon, Nvidia, Tesla and Meta), which now astonishingly accounts for just over a third of the S&P 500 weight, trades at 34 times next year's earnings forecasts compared with 21 for the S&P 500 excluding the Mag-7 (Exhibit 19). There has been a great deal of chatter in the media that U.S. stock market may be in bubble. We acknowledge that valuations are stretched, and investors will need to worry if lofty earnings expectations don't come to fruition.

Exhibit 16: United States
S&P 500 revenue and nominal GDP



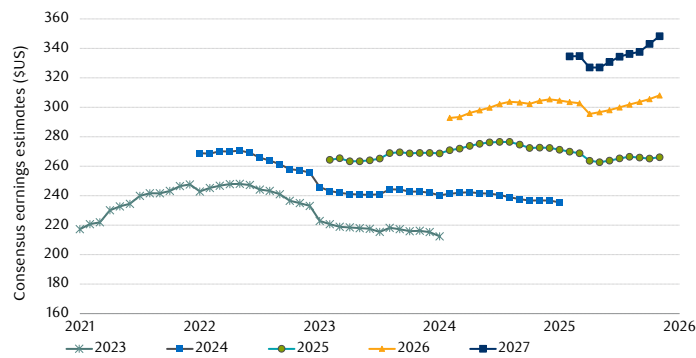
Note: As of November 28, 2025. Source: Bloomberg, RBC GAM

Exhibit 17: S&P 500 companies reporting results above consensus forecasts



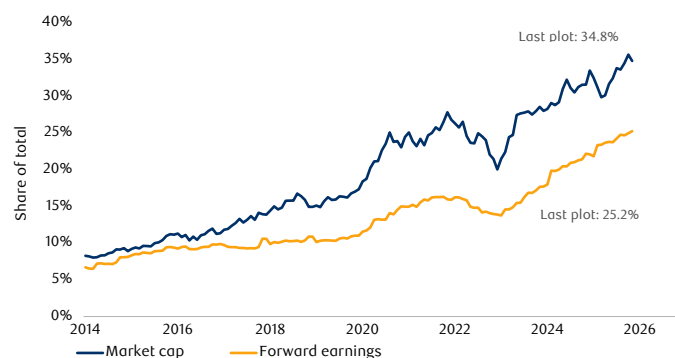
Note: As of November 28, 2025. Source: Refinitiv

Exhibit 18: S&P 500 Index
Consensus earnings estimates



Note: As of November 28, 2025. Source: Bloomberg, RBC GAM

Exhibit 19: 'Magnificent-7' as a share of S&P 500 Index



Note: Magnificent-7 includes Apple, Microsoft, Google, Amazon, Nvidia, Tesla and Meta. Tesla was added in Dec 2020 when it was included in the S&P 500. As of November 28, 2025. Source: RBC GAM

Exhibit 20: S&P 500 Index

Normalized (Equilibrium) Price/Earnings Ratio

Mag-7 versus S&P 500 ex. Mag-7 breakeven analysis: assumptions

As of November 28, 2025

	S&P 500 ex. Mag-7	Magnificent-7
Price	100.00	100.00
P/E	20.96	34.03
Trendline EPS	\$4.77	\$2.94
Trendline earnings growth	6.19%	17.93%
Discount rate	6.35%	6.35%

Earnings growth required to justify Mag-7 premium

As of November 28, 2025

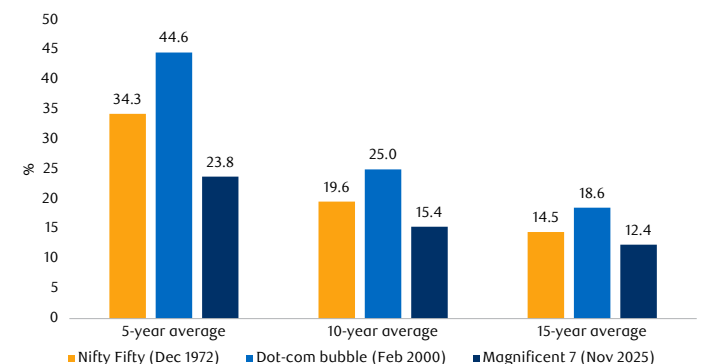
Years	S&P 500 ex. Mag-7 earnings	Cumulative earnings	Present value of cumulative earnings (S&P 500 ex. Mag-7)	Earnings growth required for Mag-7 to catch up to rest of S&P 500 (annualized)
0	\$4.77			
1	\$5.07	\$5.07	\$4.76	72.4%
2	\$5.38	\$10.45	\$9.52	45.5%
3	\$5.71	\$16.16	\$14.27	34.1%
4	\$6.07	\$22.23	\$19.02	27.8%
5	\$6.44	\$28.68	\$23.75	23.8%
6	\$6.84	\$35.52	\$28.48	21.1%
7	\$7.27	\$42.79	\$33.21	19.1%
8	\$7.72	\$50.50	\$37.92	17.5%
9	\$8.20	\$58.70	\$42.63	16.3%
10	\$8.70	\$67.40	\$47.33	15.4%
11	\$9.24	\$76.65	\$52.03	14.5%
12	\$9.82	\$86.46	\$56.72	13.9%
13	\$10.42	\$96.88	\$61.40	13.3%
14	\$11.07	\$107.95	\$66.08	12.8%
15	\$11.75	\$119.71	\$70.74	12.4%

Note: As of November 28, 2025. Source: RBC GAM

But it is entirely possible that the high price being paid for the Mag-7 stocks will ultimately be justified by extremely rapid earnings gains. To get an idea what that profit-growth rate might need to be, we ran a break-even analysis comparing the Mag-7 with the S&P 500 excluding the Mag-7. The analysis was performed over a variety of investment horizons with the results listed in Exhibit 20. If we assign a five-year horizon for the same amount invested in either the Mag-7 or the S&P 500 excluding Mag-7 to generate the equivalent amount of

earnings measured in today's dollars, the Mag-7 would need to grow their profits at 23.8% a year for the next five years to make up for its premium valuation. Extending that horizon to 10 years means that figure is 15.4% and pushing the time frame to 15 years makes the required growth rate 12.4%. These are demanding numbers, but not impossible, and they are lower than the returns required to justify the Nifty Fifty valuations in the early 1970s and technology stock valuations in the late 1990s/early-2000s dot-com bubble (Exhibit 21).

Exhibit 21: Earnings growth required to justify premium valuations



“It is entirely possible that the high price being paid for the Mag-7 stocks will ultimately be justified by extremely rapid earnings gains.”

Note: As of November 30, 2025. Magnificent 7 compares the Magnificent 7 to the rest of the S&P 500. Dot-com bubble compares the Russell 3000 Growth to the Russell 3000 Value. Nifty Fifty compares the Nifty Fifty to the S&P 500. Source: Bloomberg, RBC GAM

Scenario analysis reveals unfavourable risk/reward for S&P 500

Zooming out to the overall U.S. large-cap market, the S&P 500's current elevated valuation of 25.4x trailing earnings (or 1.6 standard deviations above our estimate of equilibrium) makes it difficult to generate significant further upside.

Exhibit 22 outlines combinations for the S&P 500 based on

consensus earnings and various P/E multiples. The historically normal P/E in the context of current levels of interest rates, inflation and corporate profitability – i.e. equilibrium – is 17.8, and the consensus of analysts' earnings estimates for 2026 is US\$309.30. The product of those two numbers implies a fair value for the S&P 500 by the end of next year of just 5513, which is a 17% decline from the close on November 28, 2025.

Exhibit 22: Earnings estimates and alternative scenarios for valuations and outcomes for the S&P 500

		Consensus 2025	Total Return 2025		Consensus 2026	Annualized Total Return 2026
	P/E	\$271.81		P/E	\$309.28	
+2 Standard Deviation	27.2	7380.2	8%	27.0	8347.2	21%
+1 Standard Deviation	22.5	6127.5	-10%	22.4	6930.3	2%
+0.5 Standard Deviation	20.2	5501.1	-20%	20.1	6221.9	-7%
Equilibrium	17.9	4874.7	-29%	17.8	5513.4	-17%
-0.5 Standard Deviation	15.6	4248.4	-38%	15.5	4805.0	-27%
-1 Standard Deviation	13.3	3622.0	-47%	13.2	4096.5	-37%
-2 Standard Deviation	8.7	2369.2	-65%	8.7	2679.7	-57%

Note: As of November 28, 2025. Total returns for 2026 are annualized. Source: LSEG I/B/E/S, RBC GAM

Less pessimistically, should the P/E trade at one standard deviation above equilibrium i.e. 22.4, then the resulting level for the S&P 500 improves to 6930, although that is still not far above the S&P 500's level at the time of this writing. Generating average or above-average returns from here would require the P/E to exceed 1 full standard deviation above equilibrium or for earnings to come in much better than expected. Then again, investors appear comfortable assigning a premium valuation to U.S. large caps, and it is hardly automatic that the market will change its mind over the coming year. The U.S. is undeniably a fertile environment for dynamic companies, and this is potentially a time of remarkable technological advancement. Still, with valuations at the upper end of their historic range (Exhibit 23), the market is vulnerable to any disappointment.

Styles: large-cap growth leads the way

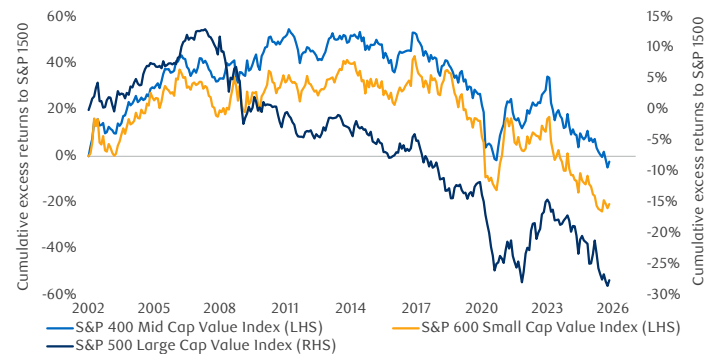
U.S. equity-market gains this year have been generated almost exclusively by large-cap growth stocks. Exhibits 24 and 25 plot charts the relative performance of growth and value stocks grouped by market capitalization. The only line rising on these charts is the one for large-cap growth, while all the other lines are in downward trends. For context on the numbers, large-cap growth stocks have gained 21.7% year-to-date as of November 28, 2025, whereas small-cap value stocks have only gained 3.6%, underperforming by 18.1 percentage points. This gap reflects the extent to which megacap technology stocks are benefiting tremendously from excitement around AI and the hundreds of billions of dollars in capital expenditures being announced to support it. While U.S. large-cap stocks may be expensive, we recognize that there is significant momentum behind them, and that shorter-term momentum can outweigh valuation concerns. As a result, being underexposed to megacap growth companies could be costly especially if their leadership of the U.S. equity market's advance remains concentrated.

Exhibit 23: S&P 500 Index
Normalized (Equilibrium) Price/Earnings Ratio



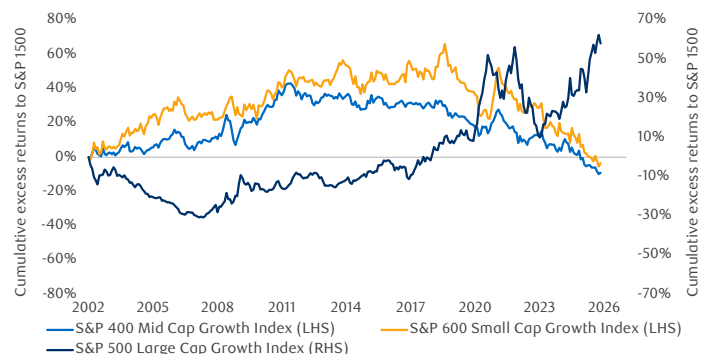
Note: As of November 28, 2025. Source: RBC GAM

Exhibit 24: Returns for Value
S&P value indices



Note: As of November 28, 2025. Source: S&P Dow Jones Indices, Bloomberg, RBC GAM

Exhibit 25: Returns for Growth
S&P growth indices



Note: As of November 28, 2025. Source: S&P Dow Jones Indices, Bloomberg, RBC GAM

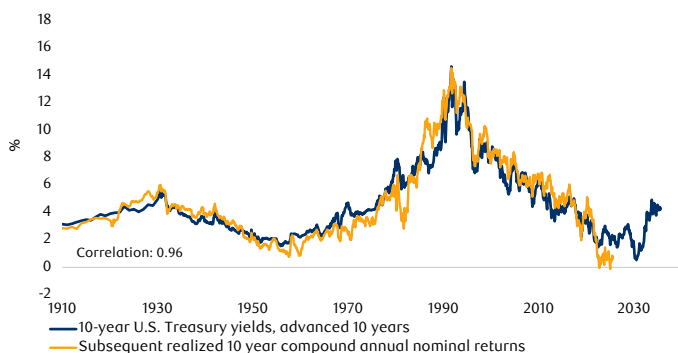
Asset mix – trimming equity overweight and narrowing tilt to non-U.S. regions

Our asset mix balances the risks and opportunities surrounding our base case scenario. We see the economy continuing to expand into 2026 and inflation pressures moderating, which should allow the Fed to continue lowering interest rates at a gradual pace. This benign outcome is subject to a variety of risks, the key ones being inflation, uncertainty around U.S. policy and elevated global government-debt levels.

Against this backdrop, we continue to expect stocks to outperform bonds. But the scope for outsized equity outperformance may be limited given that valuations are elevated, particularly in the area of U.S. large-cap growth. Exhibits 26 and 27 plot return-forecasting tools for U.S. 10-year bonds and the S&P 500, respectively. A good proxy for estimating long-term returns on 10-year Treasuries is the current yield, which is 4.01% at the time of this writing. For stocks, a high Shiller Cyclically Adjusted P/E (CAPE) has tended to predict inferior S&P 500 returns over the subsequent decade. The current CAPE of 32.8 is consistent with long-term returns of 4.50% in the stock market, which is only modestly better than the 4.01% expected for bonds.

As a result, in balancing the risks and opportunities to our base case scenario, we have decided to trim our equity overweight position by one percentage point this quarter, moving the proceeds to cash. This shift reflects our view that the risk/reward in stocks has diminished as a result of the strong run in equities over the past several months, pushing valuations in some markets to especially demanding levels. Still, a small equity overweight remains – consistent with the historical outperformance of equities, alongside a supportive macro environment including the prospect of moderate economic growth, falling inflation, central bank rate cuts and rising earnings. Simultaneously, we have used this opportunity to adjust our regional tilts by narrowing the underweight in North American equities. While we acknowledge that U.S. equities offer limited upside potential from a valuation standpoint, we observe strong momentum in large-cap growth stocks as well as their profit growth, and being underweight could be costly should those trends persist. Consequently, we have reduced our exposure to international equities but are maintaining a slight overweight position to these regions 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.

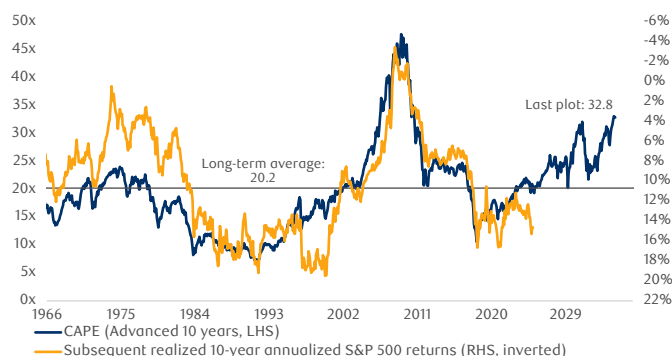
Exhibit 26: U.S. 10-year Treasury note and returns



Note: November 28, 2025. Source: Deutsche Bank, Macrobond, RBC GAM

Exhibit 27: Shiller’s CAPE

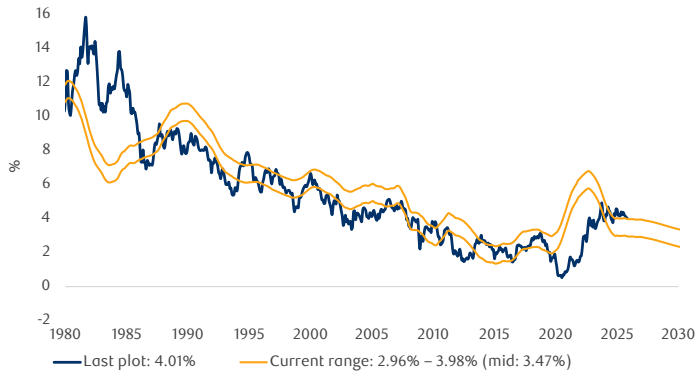
Real S&P 500 Index / 10-year average of real EPS



Note: As of November 28, 2025. Source: Macrobond, Bloomberg, RBC GAM

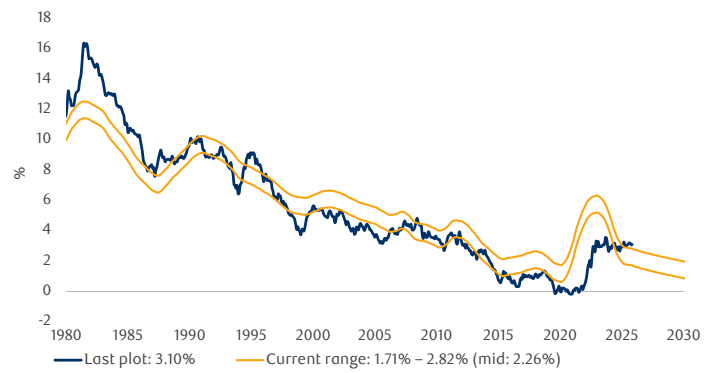
Global fixed income markets

U.S. 10-Year T-Bond Yield Equilibrium range



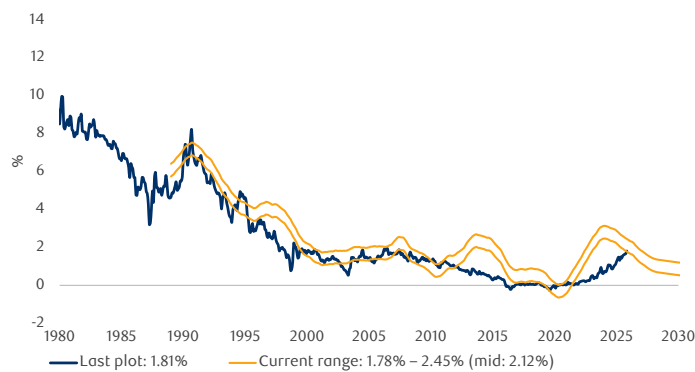
Note: As of November 30, 2025. Source: RBC GAM

Eurozone 10-Year Bond Yield Equilibrium range



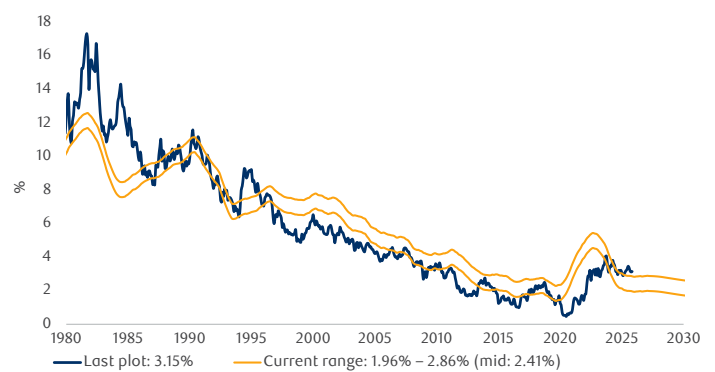
Note: As of November 30, 2025. Source: RBC GAM

Japan 10-Year Bond Yield Equilibrium range



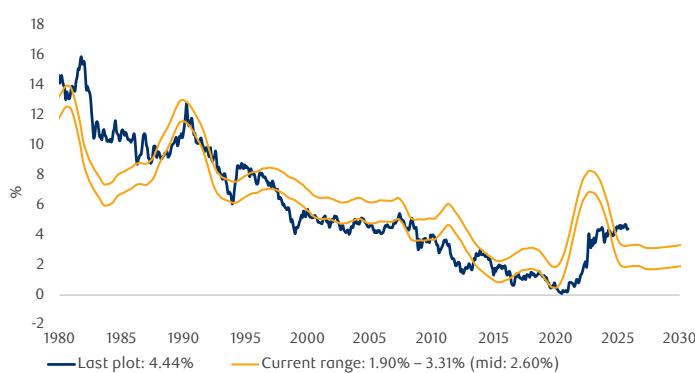
Note: As of November 30, 2025. Source: RBC GAM

Canada 10-Year Bond Yield Equilibrium range



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

UK 10-Year Gilt Equilibrium range



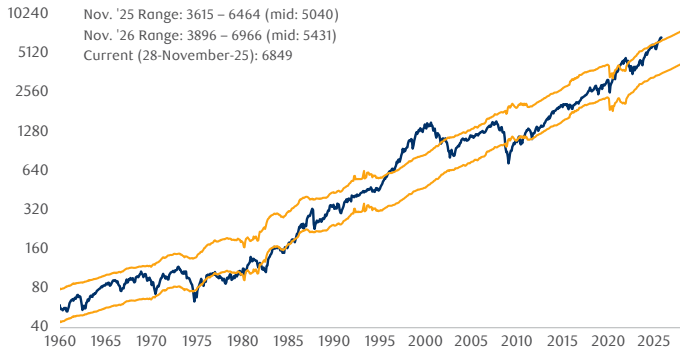
Note: As of November 30, 2025. Source: RBC GAM

“All 10-year government bond yields except Japan’s are near or above the upper end of their modelled equilibrium bands.”

Global equity markets

S&P 500 Equilibrium

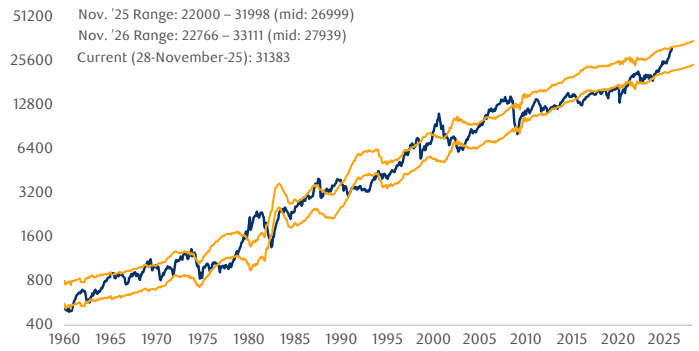
Normalized earnings and valuations



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

S&P/TSX Composite Equilibrium

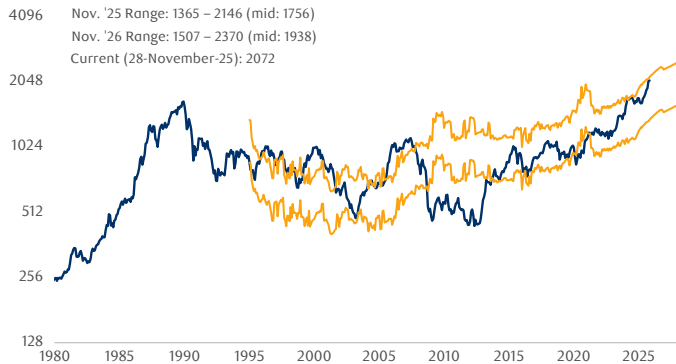
Normalized earnings and valuations



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

MSCI Japan Index

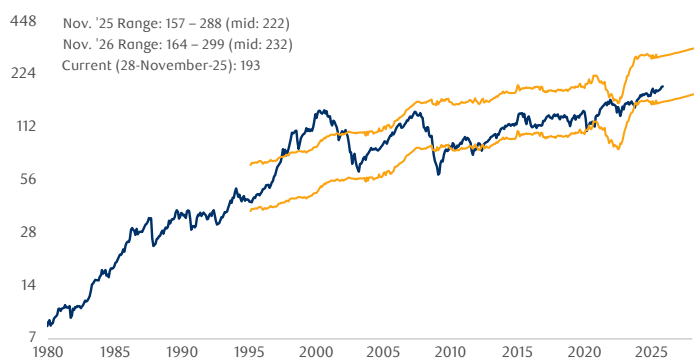
Normalized earnings and valuations



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

MSCI Europe Index

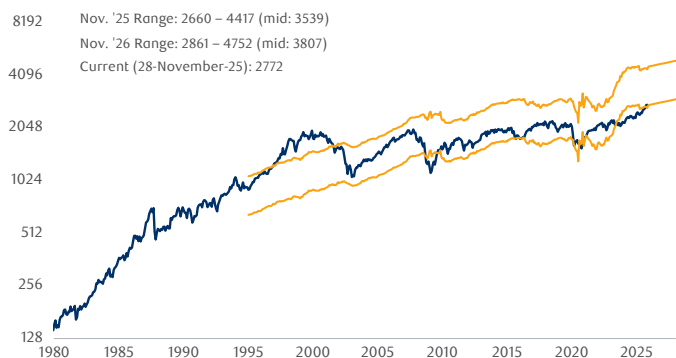
Normalized earnings and valuations



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

MSCI UK Index

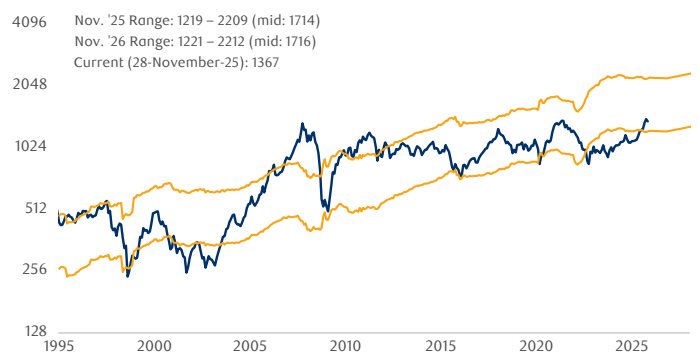
Normalized earnings and valuations



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

MSCI Emerging Markets Index

Normalized earnings and valuations



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

Note: The fair value estimates are for illustrative purposes only. Corrections are always a possibility and valuations will not limit the risk of damage from systemic shocks. It is not possible to invest directly in an unmanaged index.

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