FRANKLIN TEMPLETON | Institute

November 2025

Global Investment Outlook

2026 and beyond

Not FDIC Insured | No Bank Guarantee | May Lose Value

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Executive summary

- In 2026, we foresee **broadening opportunities** across global capital markets, driven by attractive profits growth outside the United States and by global monetary policy easing.
- Yield curves look poised to **steepen**, and the US dollar will remain **weak**.
- We believe **emerging debt and equity markets**, **European equities**, and **US smaller-capitalization** stocks should lead the way in 2026. Still, US equity returns, including in the leading **information technology** sector, should remain solid, in our view.
- Within private markets, commercial **real estate debt**, **infrastructure** and **secondary offerings of private equity** are our preferred areas.
- Longer term, the key driver of returns remains **innovation**, above all in the **information technology sector**, **private investments** and **digital finance**.
- That all said, we think a health warning is in order. We have entered an era of **big and intrusive government**, which risks lowering returns and increasing risk across capital markets over the remainder of this decade.

Introduction

As 2025 draws to a close, it is time to turn our attention to 2026 and beyond. In what follows, we highlight our top investment ideas, both for the coming year and over the longer run.

We encapsulate our 2026 (cyclical) and our long-term (secular) investment analysis into two separate categories of three themes each.

For 2026, our cyclical themes are: *Broadening, Steepening* and *Weakening. Broadening* reflects our conviction that investment opportunities across regions and asset classes are expanding. *Steepening* refers to yield curves, where falling short-term interest rates will incentivize investors to move out of cash holdings and into risk assets, including equities, credit and fixed income duration. *Weakening* regards the US dollar, which bodes well for emerging debt and equity markets, and is also an important development for portfolio management and hedging strategies.

As we elaborate below, our cyclical themes intersect—akin to Venn-diagrams—with reinforcing implications across investor portfolios.

Turning to the longer term, we believe the following themes will dominate the coming half-decade: *The Age of Intelligence, the Mainstreaming of Private Markets and An Era of Big Government*. Each has profound implications for strategic investment decision-making.

In what follows, we first consider the short-term outlook for 2026. We then turn to the long-term view. We conclude with the risks to our views and a summary of the key investment implications.

Three themes for 2026

Broadening

US outperformance has dominated investment returns in recent years—colloquially referred to as US exceptionalism. Since the global financial crisis (2008-2009), risk-adjusted US equity and fixed income returns have trounced those of other countries and regions.

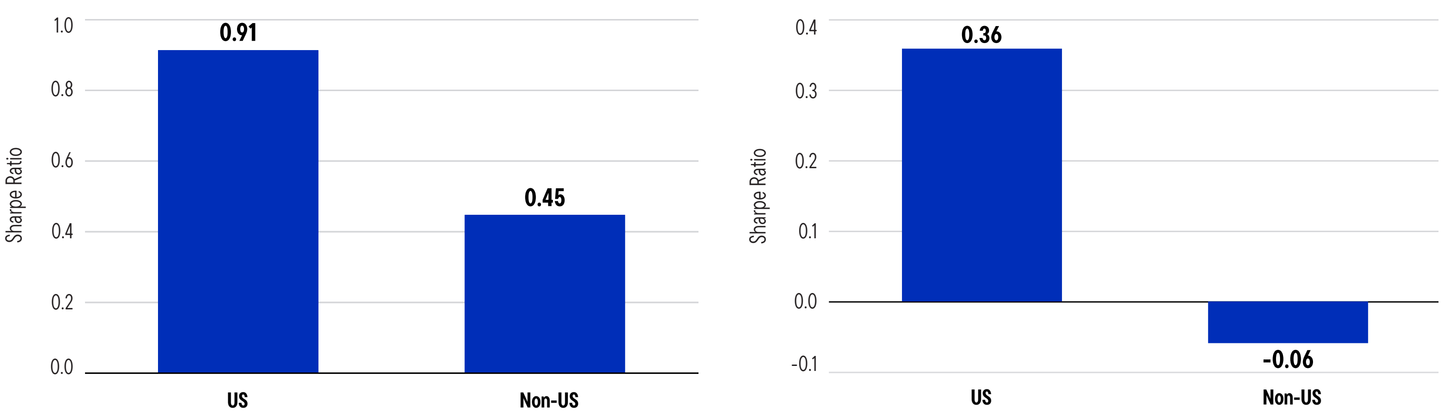
Make no mistake about it: The United States remains a magnet for global investment flows. Its corporate and market fundamentals remain superb. The US boasts superior profitability, liquidity and a breadth of investment options—which we believe are unmatched anywhere.

But in important ways, the global investment landscape is evolving. Changes are primarily about new opportunities, based on improving profitability and more attractive valuations in sectors and regions that so far have underperformed. Support also comes from expected monetary policy easing globally.

Within the US equity market, the earnings outlook has brightened for small-capitalization stocks, industrials and financials. Small-cap stocks and industrials, which are typically more highly leveraged than the rest of the market, will see profitability rise as the Federal Reserve (Fed) trims interest rates and debt servicing costs fall. Financials should benefit from a steeper yield curve, improving net interest margin and from innovations in capital markets.

Exhibit 1: Sharpe Ratios Comparing US to Non-US Equity and Fixed Income

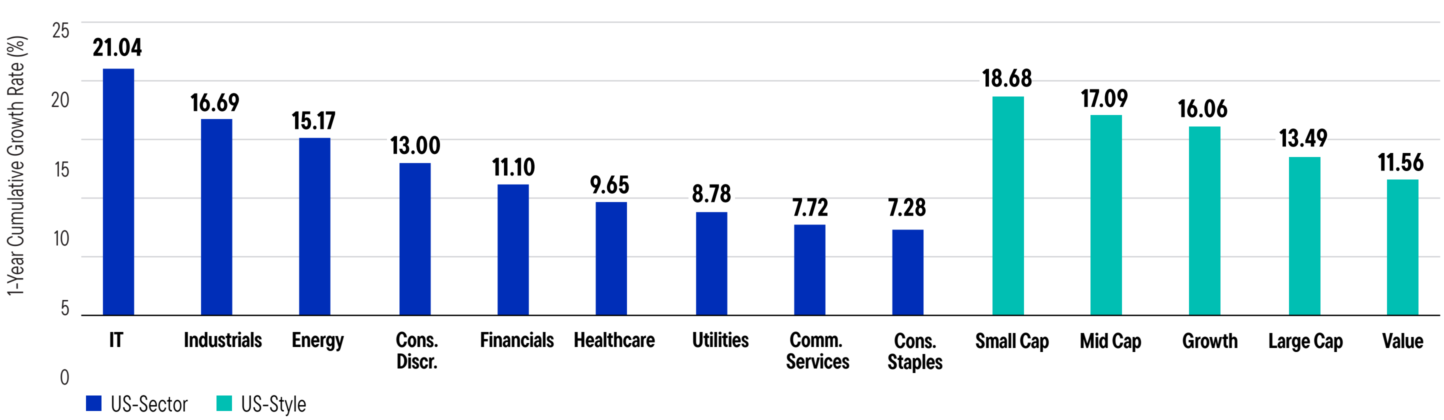
As of September 30, 2025



Source: FactSet. Analysis by Franklin Templeton Institute. Indices used (USD unhedged): US Equity: S&P 500; Non-US Equity: MSCI World ex USA; US Fixed Income: Bloomberg US Aggregate Total Return; Non-US Fixed Income: Bloomberg Global Aggregate ex-USD Total Return. The 3-month U.S. Treasury bill yield is used as the risk-free rate when calculating the Sharpe ratio. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. **Past performance is not an indicator or a guarantee of future results.**

Exhibit 2: Expected 2025-2026 Earnings Growth by Sector and Style

As of September 29, 2025



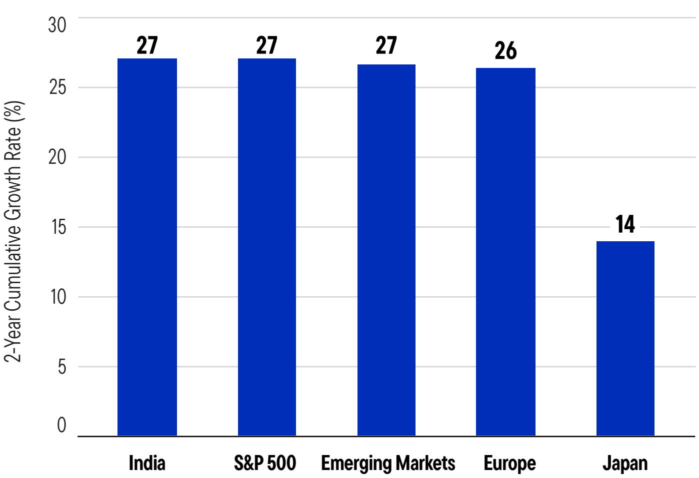
Source: FactSet. Analysis by Franklin Templeton Institute. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. **Past performance is not an indicator or a guarantee of future results.**

The implication is that US equity market performance can broaden sustainably away from the still-compelling leadership of large capitalization growth, technology and artificial intelligence (AI) companies.

Similarly, prospects appear to be brightening outside the United States. Over the next 12 months, earnings growth is expected to be as high in emerging markets as in the United States. That outcome owes much to the macroeconomic growth impulse delivered by monetary easing across the emerging complex. Even Europe may participate, nudged ahead by both monetary and fiscal easing, paving the way for an upturn in the European growth and earnings cycles in 2026.

Exhibit 3: Expected 2025-2026 Earnings Growth by Region

As of October 1, 2025



Source: FactSet. Analysis by Franklin Templeton Institute. MSCI indexes used for international countries, in USD. United States represented by the S&P 500. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. There is no assurance that any estimate, forecast or projection will be realized.

Policy stimulus outside the United States is a welcome offset to the drag induced on world trade via US tariffs. A cyclical upturn outside the United States also creates diversification opportunities, as accelerating economic and earnings growth in emerging economies and Europe contrasts with a potential US "soft patch."

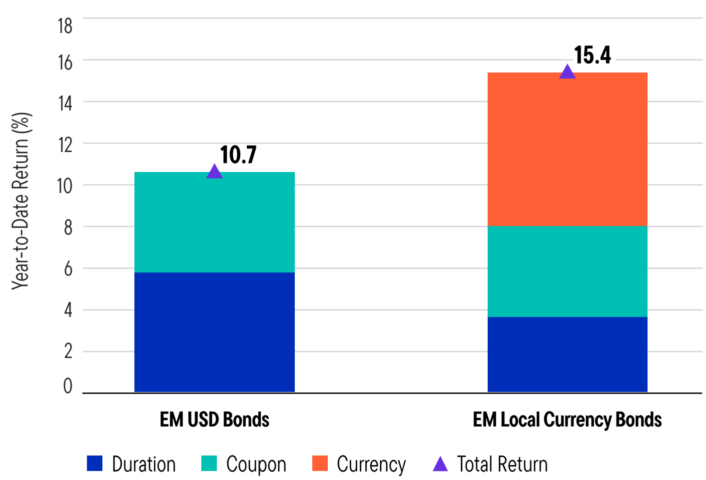
Our broadening thesis extends beyond equities. Alongside various emerging central banks and major global central banks, the Fed has resumed its easing cycle. As US short-term interest rates fall, investors will be confronted with rollover risk in their money market holdings. Accordingly, we anticipate that many will shift from cash into fixed income (public as well as private) with exposure to duration or credit returns.

A key beneficiary will be emerging market (EM) debt, sovereign and corporate, local as well as hard currency denominated. For US investors, a weakening of the dollar adds to the appeal of emerging local currency securities. But as the Fed cuts US rates, investors from other regions (e.g., Europe, the United Kingdom or Japan) will see the cost of currency hedging decline, which would increase their net (of hedging) returns in emerging fixed income assets.

Moreover, an appreciation of emerging currencies against a weakening US dollar lowers import prices and hence overall inflation, allowing emerging central banks to ease further next year. That outcome would underpin EM bond prices. Accordingly, even after a year of stellar returns, emerging debt markets are poised to deliver again in 2026.

Exhibit 4: 2025 EM Debt Performance

As of September 30, 2025



Source: FactSet. Analysis by Franklin Templeton Institute. EM USD Sovereign = JPM EMBI Global Diversified (Face Constrained) Index, EM Local Sovereign = JPM GBI-EM Global Diversified. Returns are shown in USD, the base currency for the indices. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. **Past performance is not an indicator or guarantee of future results.**

Steepening

In September 2025, the Fed resumed cutting rates, a policy that had been on pause for the preceding nine months. The Fed is expected to continue easing into the first half of 2026, perhaps for longer. It joins other central banks that have already cut rates (e.g., the European Central Bank [ECB]) and those whose rate-cutting cycles are also likely to continue, for example, in many emerging economies.

For the Fed, easing comes at an awkward time, given that its preferred core inflation gauge of personal consumption expenditures (PCE) prices remains stubbornly above target and will tick higher as tariff costs pass-through. Partly for that reason, the US Treasury yield curve is likely to steepen as the Fed cuts short rates, with long rates only grudgingly following.

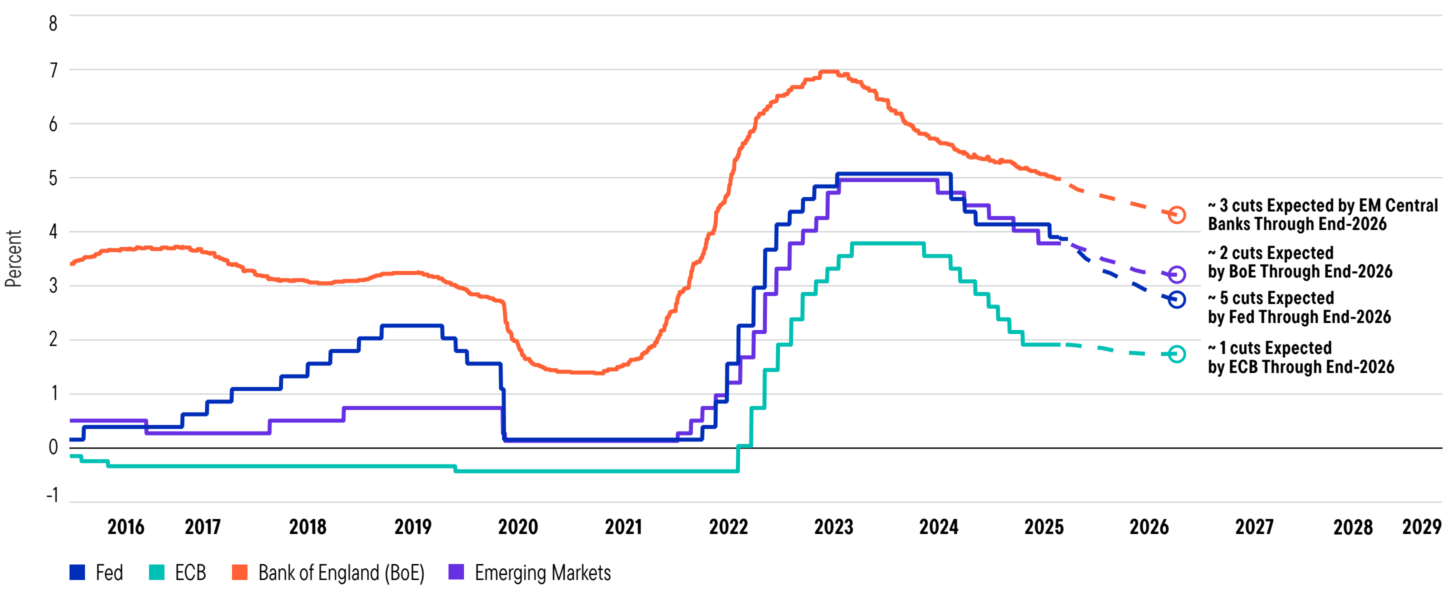
We think two additional factors will also contribute to steeper yield curves globally.

The first is the tremendous demand for capital to fund surging investment in innovation, above all in AI and the energy infrastructure it requires. In the United States, that investment boom will also be fueled by favorable tax treatment of depreciation.

The second is the arrival of massive new government borrowing in the United States, Germany, much of the European Union, China and perhaps even in Japan.

Exhibit 5: Central Bank Policy Rate Expectations

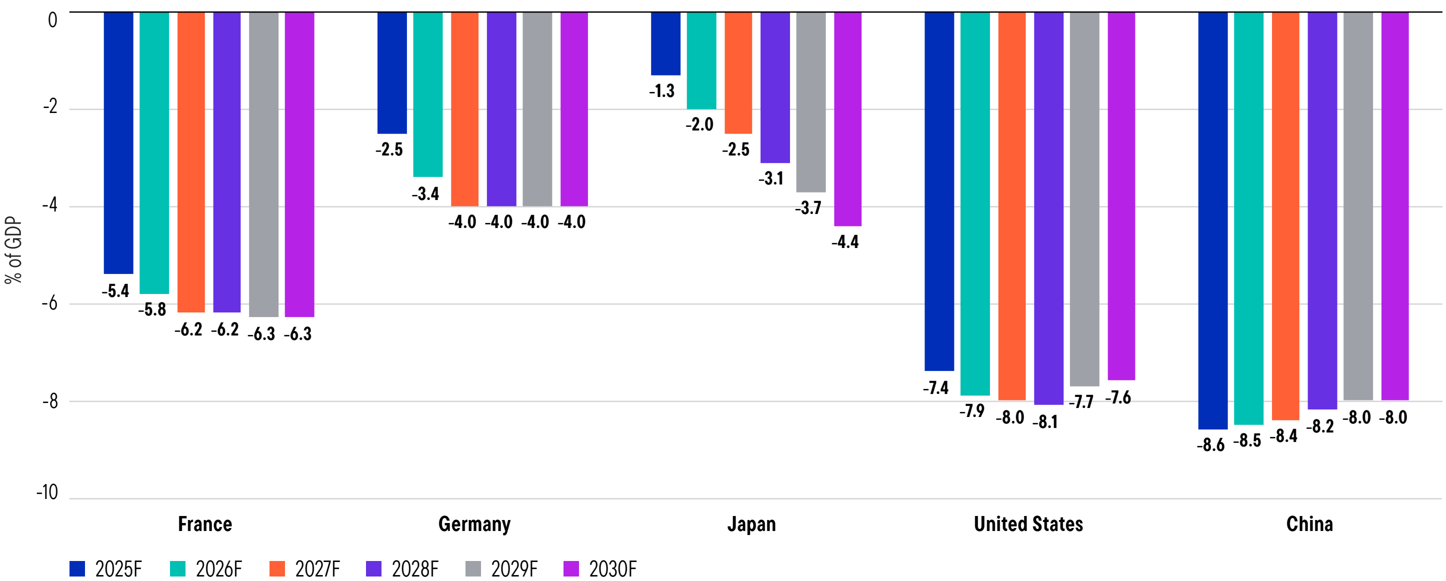
As of October 22, 2025



Sources: ECB, ICE, BoE, Fed, CME Group, Bloomberg, Macrobond. Analysis by Franklin Templeton Institute. Implied rates for the Fed, ECB, and BoE are based on Fed Funds futures, €STR futures, and SONIA futures, respectively. Policy rate for Emerging Markets represents a simple average across 16 EM countries, based on Bloomberg surveys: Mexico, Brazil, Indonesia, India, China, Taiwan, South Korea, South Africa, Poland, Malaysia, Thailand, the Czech Republic, Hungary, Chile, Peru, and Colombia. Expectations are based on consensus economic forecasts sourced from Bloomberg. There is no assurance any estimate, forecast or projection will be realized.

Exhibit 6: General Government Fiscal Balance Projections

As of October 7, 2025



Source: International Monetary Fund, Fiscal Monitor - October 2025 Edition. IMF staff estimates and projections presented. There is no assurance any estimate, forecast or projection will be realized.

For investors, steeper yield curves pose both challenges and opportunities.

For investors sitting on large cash balances, falling short-term interest rates pose rollover (or reinvestment) risk, namely the likelihood that income derived from short-term deposits and cash will also fall as short rates decline.

At the same time, gargantuan needs to finance private investment and public borrowing will tend to push up real interest rates, particularly at longer durations and in the credit arena. That creates income opportunities further along the duration and credit curves.

Accordingly, the steepening of yield curves reinforces our previous broadening thesis, as investors will be incentivized to seek new opportunities in duration, credit, equities and elsewhere.

Typically, a steepening of the yield curve is also seen as a bullish indicator for future growth, particularly if it is driven by monetary easing. Other potential beneficiaries of steeper yield curves, therefore, include cyclically sensitive sectors and styles such as industrials, financials or small-cap firms.

Falling cash yields should also prompt investors to move into alternative assets, including private credit and private real estate, as they seek to boost income and find ways to diversify portfolio holdings.

Weakening

Year-to-date, the trade-weighted value of the US dollar has fallen by about 10%. Various factors suggest its decline is not yet over. Among them are probable further Fed rate cuts owing to a softening US labor market. Shifting global portfolio flows, reflecting more attractive equity and fixed income opportunities outside the United States, should also contribute to dollar weakness.

Exhibit 7: Nominal US Dollar Index Performance Since 2010

As of October 17, 2025

Sources: Federal Reserve, Bloomberg, Macrobond. Index shown: US Fed Trade-Weighted Nominal Broad Dollar Index. Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. **Past performance is not an indicator or a guarantee of future results.**

Dollar weakness has important implications for investors. EM debt denominated in local currency is a potential winner, reinforced by the likelihood that EM currency appreciation will push domestic inflation down, allowing emerging central banks to ease. Lower interest rates, of course, also boost EM equity valuations.

Similarly, a weaker dollar could nudge Eurozone inflation below target, prompting further rate cuts from the ECB. Lower Eurozone rates, in turn, would provide additional support for European equity and credit markets.

For euro, sterling, yen, and other non-US-dollar investors, falling US interest rates reduce the costs of currency hedging. That means that a greater fraction of the returns in EM debt can also accrue to investors in Europe, Japan and elsewhere.

A softer dollar also tends to push up the dollar price of many commodities, including gold and other precious metals. Accordingly, dollar weakness offers opportunities in various commodity markets, either directly (via futures) or indirectly (via the shares of commodity producers). Floating digital currencies may also appreciate against a softer US dollar.

Crude oil, however, may be an exception in the commodity universe. Recent US sanctions against Russian energy notwithstanding, weak oil prices in 2025 reflect ample supply. And should a resolution to the Russia-Ukraine war arrive, anticipation of a resumption of Russian oil supplies could push crude oil prices even lower.

In short, weakening of the US dollar tends to reinforce a broadening of returns across capital markets, by region, sector, and asset class.

The long-term outlook

We now turn to the long-term outlook, which comprises of three themes: *The Age of Intelligence, Private Assets Becoming Mainstream*, and *An Era of Big Government*. In what follows, we summarize the nature of these themes and then explore the strategic investment implications associated with each.

The age of intelligence

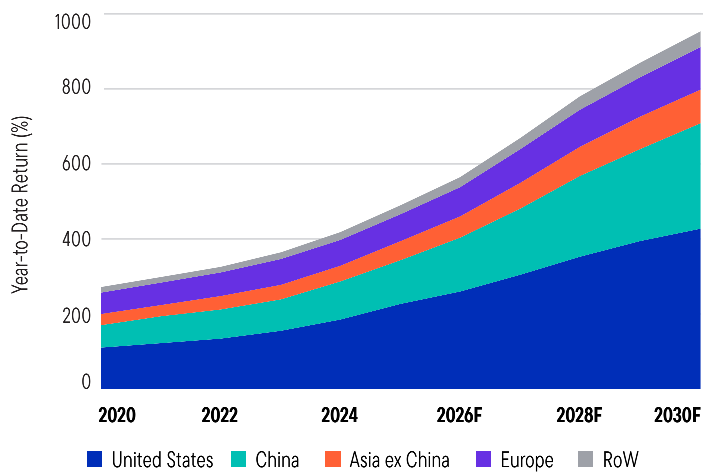
We live in an era of AI. To date, the primary beneficiaries have been those firms that provide the hardware to launch its rapid growth, and those that have made it accessible to businesses and individuals to enhance data gathering, search, and analytics.

But the deployment of AI is only in its initial phase. Its contribution to growth, social welfare, and investment returns is just beginning. Promising investment opportunities remain in the build-out of its infrastructure, including data centers. New and more powerful chips will revolutionize the speed and scope of AI applications.

Of all the investible themes associated with AI, one of the most compelling is the need to "feed the beast" to sate its vast energy appetite. New investment will be required in electricity production, transmission and storage. To meet that need, both public and private markets will attract capital, with powerful spillovers to sectors such as engineering, basic materials, rare earths, and industrial metals.

Exhibit 8: Electricity Demand for Data Centers

As of September 30, 2025



Source: The International Energy Agency, MIT Technology Review. There is no assurance any estimate, forecast or projection will be realized.

AI will also transform how we work, live and play. Some of those transformations are plainly visible. AI is replacing low-skilled work, such as basic coding or paralegal writing. Online search is also being displaced. Here, too, we are at the early stages of creating new efficiencies. The scope to boost economy-wide efficiency is enormous, particularly in low-productivity sectors such as health care, education, and public services. Whether that happens is less a function of the ability to innovate than the willingness to adapt.

Private markets go mainstream

We've seen this movie before.

Whether the origins are in academia or on Wall Street, financial innovation is typically first adopted by a few investors, usually institutional. But if the innovation improves investment returns durably or increases diversification benefits, then eventually it is adapted to the needs of all investors and becomes "mainstream."

In history, that was true for innovations as diverse as mutual funds, modern portfolio theory, derivatives, hedge funds, and exchange traded funds.

Today, private equity, private credit, and other "alternatives" are on the cusp of going mainstream. In the coming years, fund innovation, regulatory changes and the application of information technology will hasten the mainstreaming of private investments.

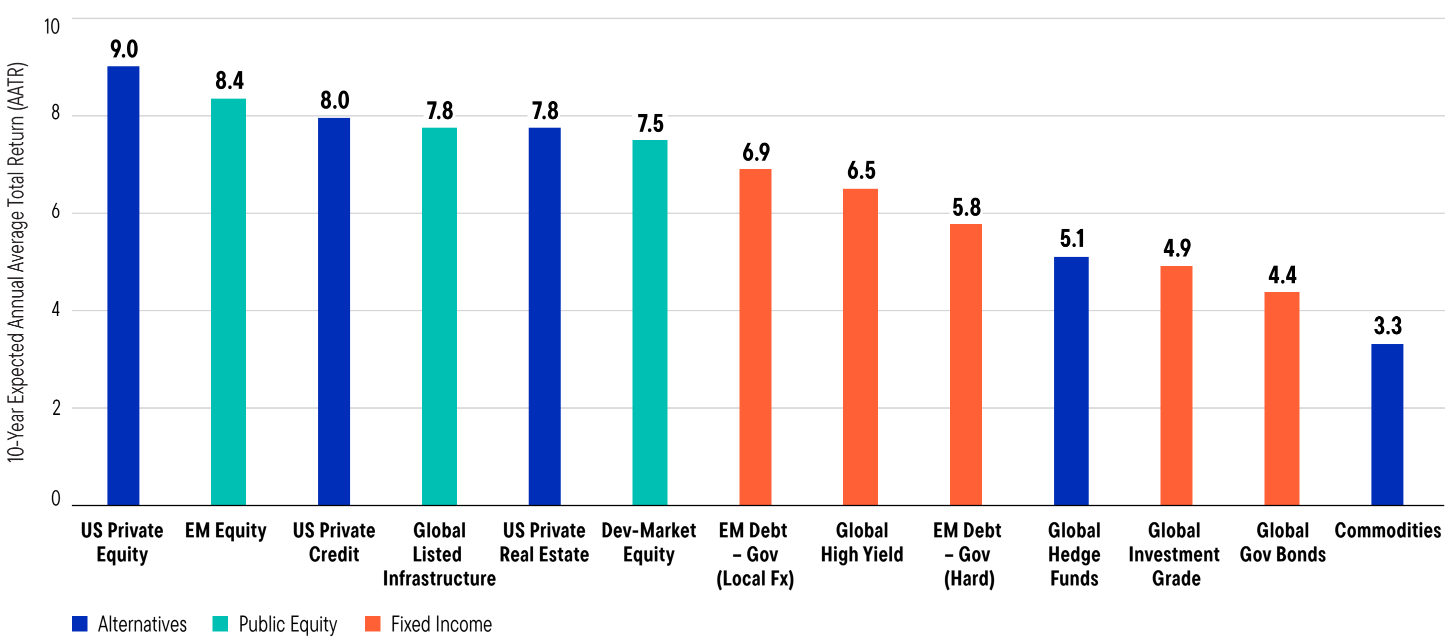
The signs are already evident. Governments and industry leaders are in discussions about the eligibility of such assets for individual portfolios, potentially even for self-directed retirement accounts. The explosive growth of alternative asset fund structures puts pooled funds within reach of more investors. And vast increases in data analytics allows advisors, ratings agencies, regulators and investors to better assess the opportunities and risks in what traditionally have been opaque investment instruments.

In doing so, the mainstreaming of private markets creates opportunities for a larger number of savers to partake in sources of higher and more diversified returns.

Finally, the mainstreaming of private markets implies larger inflows of capital. Accordingly, mainstreaming of private markets implies that, over time, average returns will be falling. The mainstreaming opportunity, therefore, is greatest for first-movers.

Exhibit 9: 10-Year Annualized Capital Market Expectations

As of October 31, 2024



Source: Franklin Templeton Investment Solutions. As of October 31, 2024. There is no assurance any estimate, forecast or projection will be realized.

An era of big government

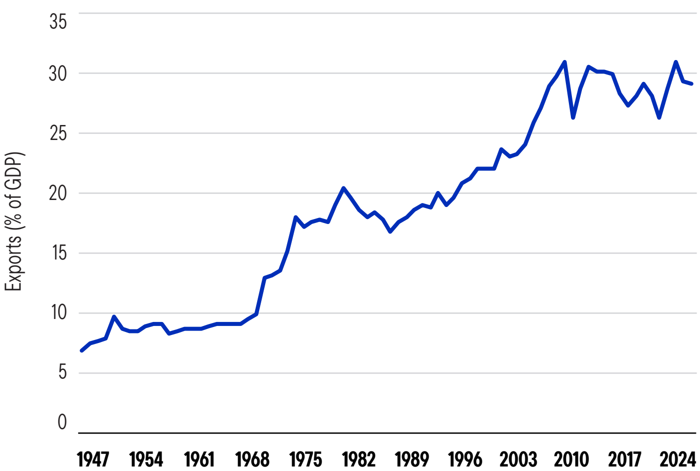
We live in changed times. Long gone is the era of unbridled faith in free markets, deregulation, unfettered capitalism, small government, globalization, and fiscal orthodoxy. Even the independence of central banks has come into question. The collapse of the liberal order arrived with the global financial crisis, which shattered public faith in the ability of orthodox economics to deliver rising living standards.

The reverberations of that collapse continue. And they manifest increasingly in a larger role for government in areas of trade, fiscal, and industrial policy. In what follows, we outline the implications for strategic investment decision-making.

We begin with trade. Globalization is over. Brexit and US tariffs are visible manifestations of the backlash against trade and migration. But even earlier, globalization was already stalling.

Exhibit 10: World Trade as a Share of World Gross Domestic Product (GDP)

As of December 31, 2024



Source: Our World In Data, Michel Fouquin & Jules Hugot, 2016, Two Centuries of Bilateral Trade and Gravity Data: 1827-2014, CEPII Working Paper 2016- 14, CEPII. World Bank, October 7, 2025. Data for period 1947-1969 is value of global merchandise exports as a share of GDP (Fouquin and Hugot; CEPII 2016; national data). Data from 1970 onwards is value of global exports of goods and services as a share of GDP (World Bank).

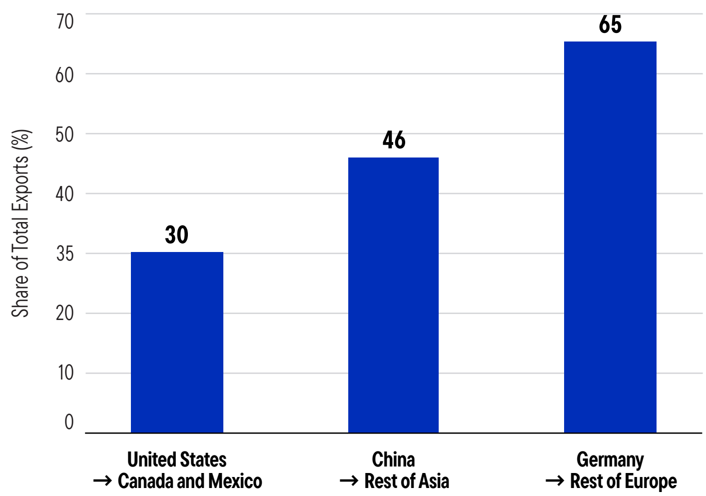
Anti-globalization is more than mere populism. National security and supply-chain concerns exposed during the pandemic are also important.

The reversal of globalization is not costless. The desire to boost efficiency and profitability drove decisions made over the past 75 years to outsource manufacturing and services, to hire immigrants and to allocate capital globally. Moving in the opposite direction implies a less-efficient allocation of resources and hence increases costs and lowers returns on capital.

Of course, de-globalization is not universal. Countries still interested in trade will find like-minded partners. And since most trade takes place with neighbors, regionalization is the likely successor to globalization, most probably centered on three major trading blocs—North America, Europe, and Asia.

Exhibit 11: Regional Export Shares

As of December 31, 2023



Source: OEC, Analysis by Franklin Templeton Institute. Data accessed on October 24, 2025. Exports from the United States to Canada and Mexico, China to the rest of Asia, and Germany to the rest of Europe are shown.

After de-globalization, the next manifestation of big government is large fiscal deficits (see Exhibit 6). Their sources are many, ranging from political dysfunction, to demographics, national security needs and "mere" fiscal stimulus. But whatever the drivers, swelling budget deficits are visible across major economies, including the United States, much of Western Europe, China and perhaps once again in Japan. Only in smaller emerging economies is a counter-move apparent.

Yet unlike periods accompanying the global financial crisis or the pandemic, today's fiscal imbalances compete with surging private sector investment in areas such as artificial intelligence, data centers and energy infrastructure. That means that big government represents compounded demand for savings. The likely result will be higher real interest rates for the remainder of this decade.

Higher real interest rates will have profound impacts on revenues and profitability across most sectors. But for broader investment strategy, the chief implication is that higher real rates raise the bar for returns across all asset classes. And if higher returns on capital don't accompany higher real interest rates, the result will be falling equity valuations. That outcome need not be cataclysmic—but to us it does suggest lower expected returns over the long run.

Larger budget deficits, in tandem with the potential erosion of central bank independence, pose other challenges. Most obvious is a rise in risk premia in sovereign credit as well as term premiums. But those impacts could one day be blunted if governments resort to "financial repression," or policies designed to force investors to hold government debt.

In either case, however, investors may accelerate their consideration of risk mitigation approaches, including the adoption of floating digital currencies or precious metals.

The final dimension of big government is industrial policy, which refers to government intervention to support chosen industries via subsidies or protection (e.g., tariffs). Here, too, the shift is global and does not fit neatly into ideological categories. The United States and China stand side-by-side as major adopters of industrial policies.

Subsidies for health care, alternative energy, electric vehicles or domestic computer chip manufacturing are "industrial policy." So, too, are tariffs to protect domestic industries, as well as public ownership stakes in "critical" sectors. Parts of Europe, above all France, have long advocated for policies to pick winners.

While promoting strategic industries can be highly profitable in specific instances (i.e., "first mover" advantage in sectors with natural monopoly characteristics), over the long history of industrial policy, the odds of recurring success are poor. As unfashionable as it may be, free markets generally allocate capital best. Governments don't. Hence, at the broadest level, industrial policy represents a further risk to falling returns on capital (including via excess investment) and hence points toward lower long-term returns.

Risks to our view

With respect to our cyclical calls for *Broadening*, *Steepening*, and *Weakening*, a primary risk is that the Fed does not ease policy as expected. A pause in the Fed's rate-cutting cycle would probably flatten the US Treasury yield curve and boost the value of the US dollar. For the reasons we have outlined above, those twin outcomes could inhibit some of the broadening opportunities that we envisage.

For similar reasons, upside surprises to US growth or inflation would alter the capital markets outlook. Higher inflation, for example, could result in weakness in both stock and bond markets.

Geopolitical shocks, including shocks to global energy supplies, would similarly alter the outlook by introducing unanticipated risk premia in equity, credit and other risk assets. An unexpected default or increase in financial risk could similarly change outcomes from those we envisage.

Summary and conclusions

In sum, over the coming year we anticipate a broadening of investment opportunities, driven by global profits growth and by monetary policy easing. We expect yield curves will steepen and the US dollar will remain weak. The likely winners include emerging markets, European equities and more cyclically exposed US equities, such as smaller-cap stocks. But returns in the stalwart US information technology sector will likely remain solid. Within private markets, we prefer real estate debt, infrastructure plays and secondary offerings of private equity.

Over the longer term, innovation remains the critical success factor and will be best served via information technology, private market and digital finance opportunities.

All the same, health warnings are in order. Geopolitical divisions are key sources of risk. Inflation remains persistent and the Fed could still disappoint.

But above all, we must recognize that much of the world has abandoned faith in free markets, free trade and the free movement of factors of production. In its place an era of big and intrusive government has arrived. Rarely has that outcome served investors well. Vigilance remains warranted.

Glossary

Sharpe ratio: The Sharpe ratio is a widely used metric for evaluating risk-adjusted returns of an investment or portfolio.

S&P 500 Index: The S&P 500 is a free-float adjusted, market-cap weighted index of 500 of the largest US publicly traded companies and is commonly used as a measure of US large-cap stock market performance.

MSCI World ex USA Index: The MSCI World ex USA Index captures large and mid-cap representation across 22 of 23 Developed Markets (DM) countries—excluding the United States. The index covers approximately 85% of the free float-adjusted market capitalization in each country.

Bloomberg US Aggregate Total Return Index: The Bloomberg US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment-grade, US dollar-denominated, fixed-rate taxable bond market. The index includes Treasuries, government-related and corporate securities, fixed-rate agency MBS, ABS and CMBS (agency and non-agency).

Bloomberg Global Aggregate ex US Total Return Index: The Bloomberg Global Aggregate ex US Index is an investment grade, multi-currency benchmark including treasury, government-related, corporate and securitized fixed-rate bonds from both developed and emerging markets issuers. This index is a subset of the Global Aggregate Index, which excluded USD-denominated securities.

MSCI India Index: The MSCI India Index is designed to measure the performance of the large and mid-cap segments of the Indian market. The index covers approximately 85% of the Indian equity universe.

MSCI Emerging Markets Index: The MSCI Emerging Markets Index tracks large and mid-cap stocks across emerging markets, covering 85% of free float-adjusted market capitalization.

MSCI Europe Index: The MSCI Europe Index captures large and mid-cap representation across Developed Markets (DM) countries in Europe. The index covers approximately 85% of the free float-adjusted market capitalization across the European Developed Markets equity universe.

MSCI Japan Index: The MSCI Japan Index is designed to measure the performance of the large and mid-cap segments of the Japanese market. The index covers approximately 85% of the free float-adjusted market capitalization in Japan.

US Fed Trade-Weighted Nominal Broad Dollar Index: A weighted average of the foreign exchange value of the US dollar against the currencies of a broad group of major US trading partners, using weights based only on trade in goods.

WHAT ARE THE RISKS?

All investments involve risks, including possible loss of principal.

The **allocation of assets** among different strategies, asset classes and investments may not prove beneficial or produce desired results.

Equity securities are subject to price fluctuation and possible loss of principal. **Small- and mid-cap stocks** involve greater risks and volatility than large-cap stocks.

Fixed income securities involve interest rate, credit, inflation and reinvestment risks, and possible loss of principal. As interest rates rise, the value of fixed income securities falls. **Changes in the credit rating** of a bond, or in the credit rating or financial strength of a bond's issuer, insurer or guarantor, may affect the bond's value. **Low-rated, high-yield** bonds are subject to greater price volatility, illiquidity and possibility of default.

Sovereign debt securities are subject to various risks in addition to those relating to debt securities and foreign securities generally, including, but not limited to, the risk that a governmental entity may be unwilling or unable to pay interest and repay principal on its sovereign debt.

Investments in many **alternative investment strategies** are complex and speculative, entail significant risk and should not be considered a complete investment program. Depending on the product invested in, an investment in alternative strategies may provide for only limited liquidity and is suitable only for persons who can afford to lose the entire amount of their investment.

Currency management strategies could result in losses to the fund if currencies do not perform as expected.

Investing in **privately held companies** presents certain challenges and involve incremental risks as opposed to investments in public companies, such as dealing with the lack of available information about these companies as well as their general lack of liquidity.

International investments are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in **emerging markets**.

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