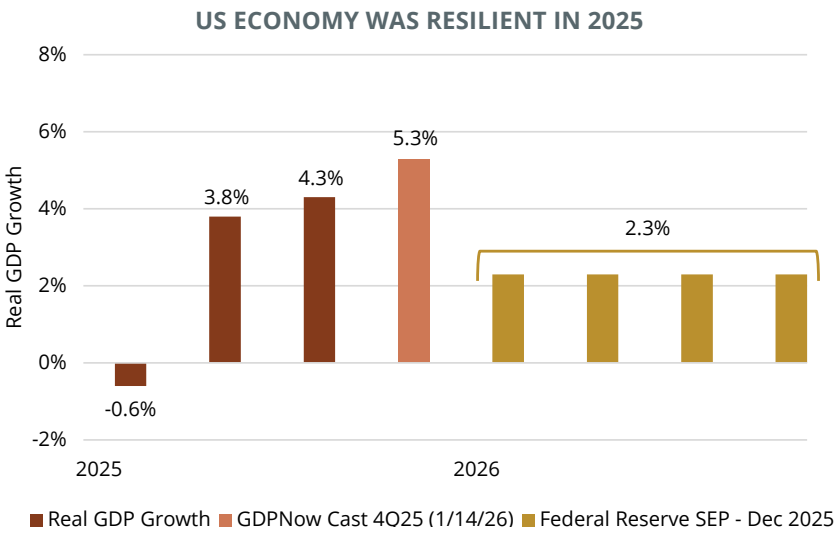
Madison INVESTMENTS

2026 Outlook & Positioning

The Madison Multi-Asset Solutions team shares key investment themes for 2026

Economic Growth

— The US economy posted another solid year, supported by massive capital expenditure for the ongoing Artificial Intelligence (AI) buildout. As we move into 2026, we anticipate that economic momentum will continue to outperform expectations, while sectors and industries outside the AI complex will begin to benefit from easier monetary policy, accommodative fiscal policy, and continued deregulation.



— A unique aspect of the US economy is that productivity has been running above trend well before the impacts of AI can be measured. From a historical perspective, technological advancements have driven increases in productivity. We fully anticipate that AI will be one of those technologies.

Summary

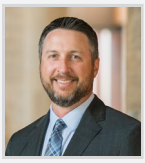
The past year was a surprisingly strong year for the economy and markets. Our outlook for 2026 suggests continued resilience with potential opportunities for investors:

— US economic momentum to continue

— Monetary and fiscal policy will remain accommodative

— Anticipating broader equity markets

Madison Multi-Asset Solutions Team



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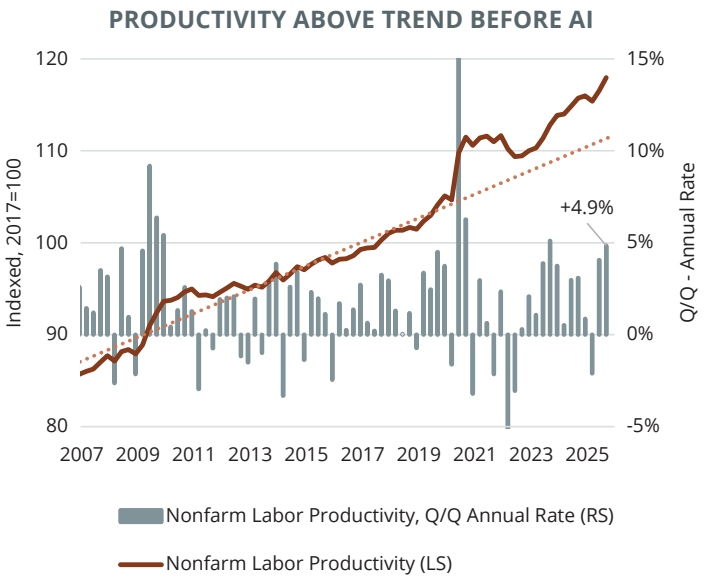
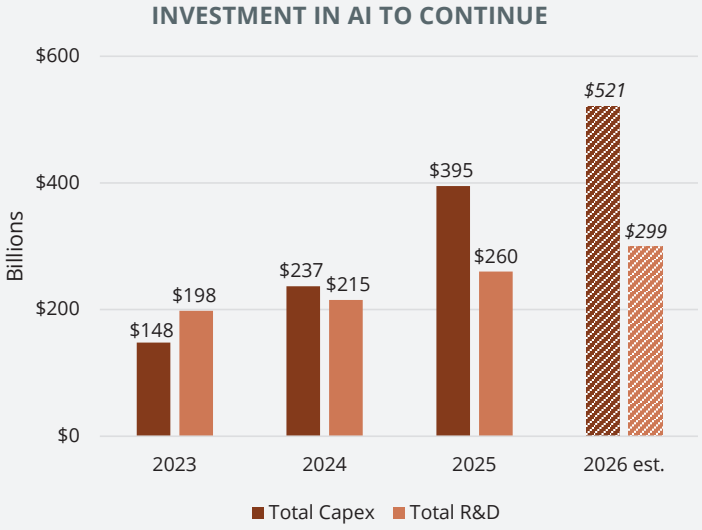
— Attributing the above trend productivity growth that we've seen since the pandemic entirely to AI might be jumping the gun, as Fed Chair Powell commented at the December Federal Open Market Committee (FOMC) meeting, "I never would have thought I would see a time when we had five or six years of productivity growth. This is higher, definitely higher. It was before it could be attributed to AI."

— **Our take:** The US economy will continue to outperform developed market peers as both monetary and fiscal policy are accommodative, despite the US economy being surprisingly strong. Simply put, policymakers in the US have chosen to take a "run it hot" approach. In addition, productivity growth in the US continues to run above trend, allowing for economic growth to continue despite a stagnant labor market.



AI Investment Growth

— Over the last couple of years, the sheer scale of investment in data center buildout to accommodate AI efforts by the hyperscalers (Google, Meta Platforms, Microsoft, Amazon, and Oracle) has been impressive and is anticipated to continue in 2026.



— **Our take:** As capital expenditures continue to rise for data-center buildouts and large-language-model training, market participants are likely to remain focused on the ultimate return on investment from these growing commitments, even as the long-term strategic importance of AI infrastructure remains clear.

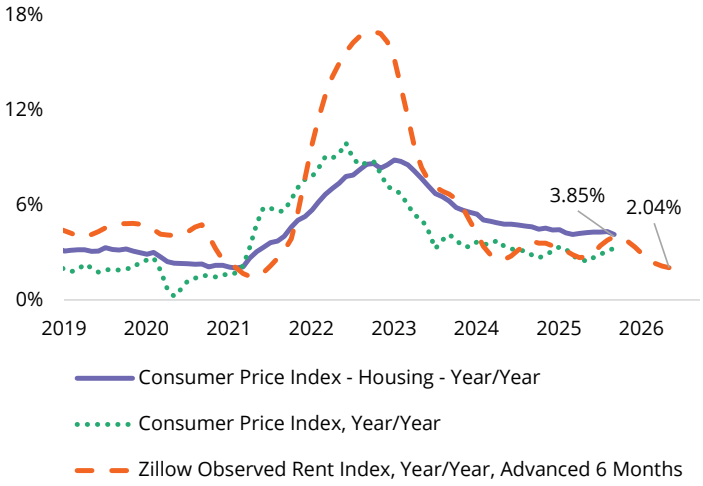
Inflation

— Inflation moderated throughout 2025, and Core CPI hit its lowest level in the past four years, falling from 3.0% to 2.6%. However, it remains above the Federal Reserve's (Fed) stated 2% target for price stability.

— Encouragingly, the price impact from tariffs has been modest. The Federal Reserve partially attributes inflation remaining over its target to tariffs, while simultaneously admitting that the impact tariffs have had on inflation has been less than anticipated.

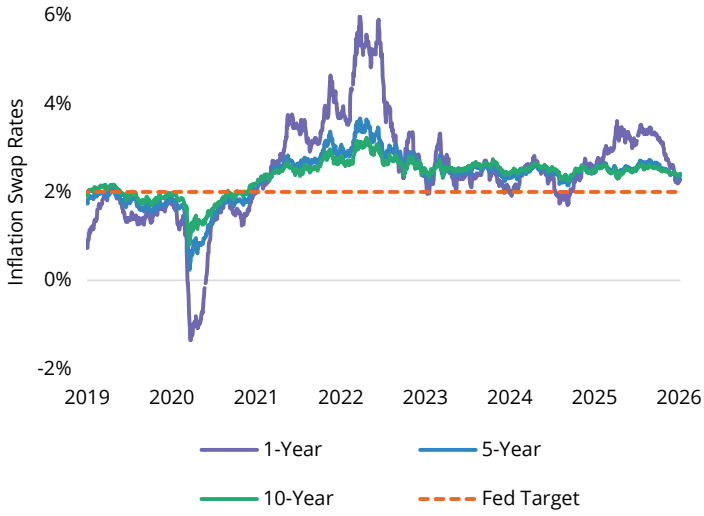
— There are encouraging signs that inflation will continue to ease in 2026. The Zillow Observed Rent Index has moderated throughout the past year. This is a positive development as the series has historically led to shelter inflation, which has been a sticking point in achieving lower inflation.

PRESSURE FROM HOUSING IS SUBSIDING



— As the labor market is not strengthening in a way that would push wages and the employment cost index higher, there appears to be little basis for an inflationary wage-price spiral to pressure inflation higher. Furthermore, energy prices, as measured by crude oil prices, also remain subdued, another encouraging sign that an inflation shock isn't likely around the corner.

ANTICIPATED INFLATION REMAINS SUBDUED

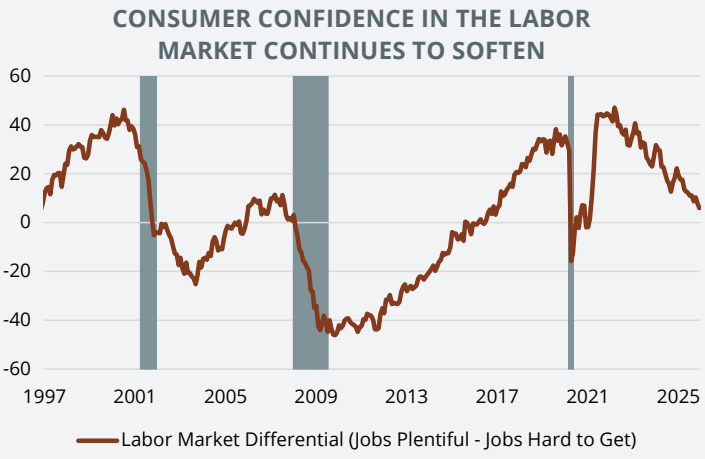


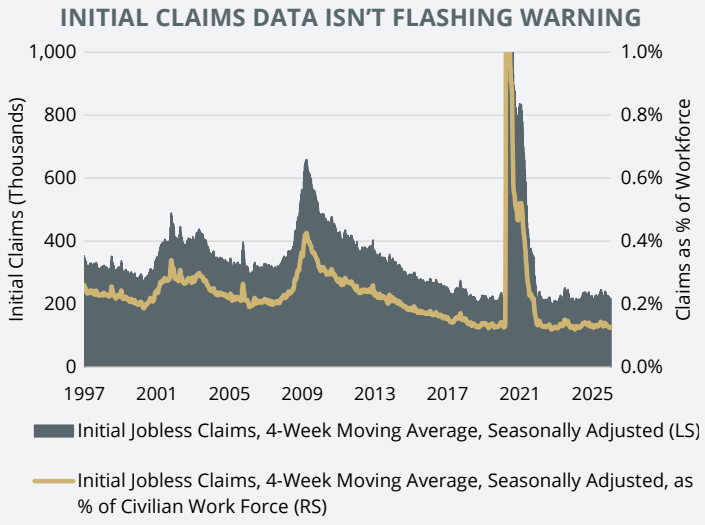
— Traditional measures of inflation, such as the Consumer Price Index (CPI) and Personal Consumption Expenditure (PCE), are inherently backward-looking. Anticipatory measures of inflation aren't showing signs of stress, as short-, medium-, and long-term inflation expectations remain at unconcerning levels. If these were moving higher, we would be more hesitant on our inflation outlook.

— **Our take:** We continue to monitor the prospect of a resurgence in inflation, especially given accommodative monetary and fiscal policy. However, we don't anticipate inflation being a primary issue for the economy and markets in the year ahead.

Labor Market

- As we enter 2026, consumer confidence in the labor market is falling as the threat of AI lingers and immigration enforcement is limiting labor supply. Will this new technology be labor-enhancing or labor-replacing?
- Unemployment has been steadily rising, hitting 4.5% in the fourth quarter. While the level of unemployment is worth noting, the pace at which it is rising is also important. If the unemployment rate continues to drift higher, equities would likely benefit from an environment that allows the Fed to continue to gradually ease monetary policy.
- **Our take:** The risks to the labor market appear to be tilted to the downside as we enter 2026. While we don't anticipate sharp labor market weakness, we don't expect marked improvement either. However, for equity markets, each scenario comes with its own risks. Should the labor market weaken dramatically from here, the Fed will appear behind the curve on interest rate cuts, a realization that could cause stress in equity markets. Contrarily, an upside surprise to employment could generate a headwind for equity markets, as expectations for rate cuts would fade, likely pushing rates higher across the curve, creating a difficult environment for equities.

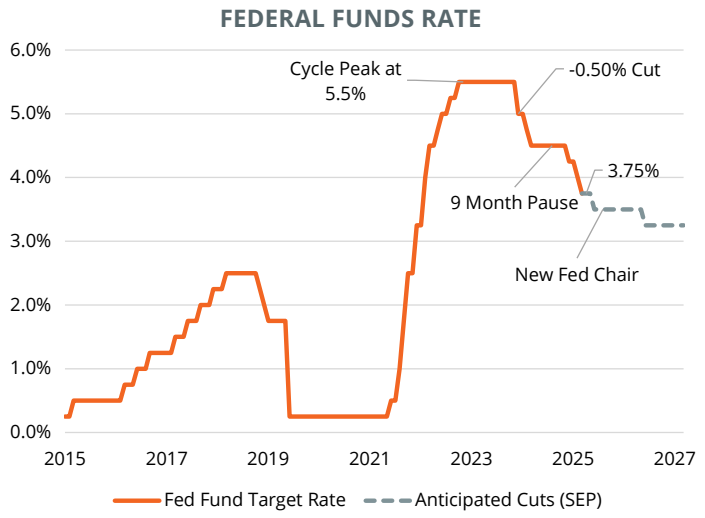




Policy

MONETARY POLICY:

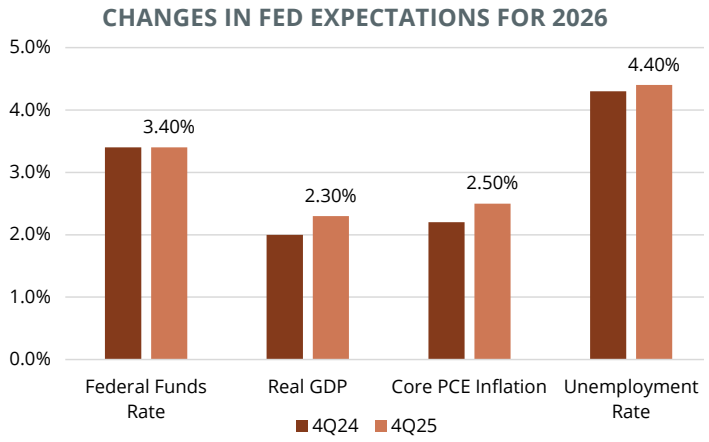
- The Fed is in full easing mode to accommodate a vulnerable labor market despite inflation remaining above its stated 2% target. While seemingly somewhat unsettled by the persistence of inflation, they believe that it would be harder to address a weak labor market with the blunt tools of monetary policy than to be wrong on inflation.
- At their final meeting in December, the FOMC decided to cut interest rates for the third time in 2025, taking the policy rate to a target range of 3.50% to 3.75%, and released their fourth and final Summary of Economic Projections (SEP) for the year.

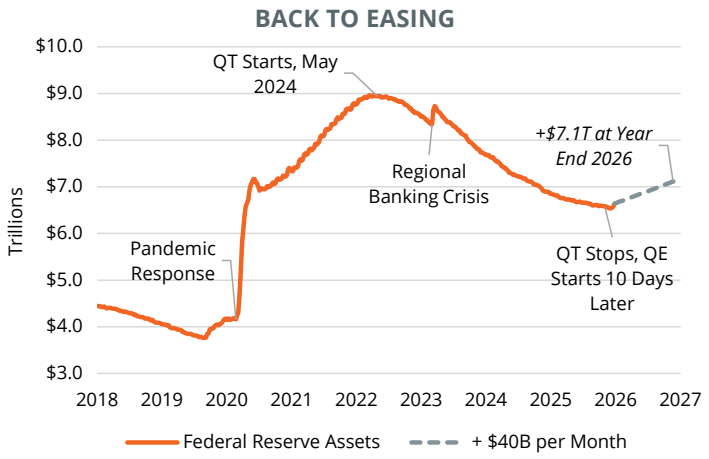


— The SEP report, commonly referred to as "The Dot Plot", indicated that the FOMC currently believes it will be appropriate to cut interest rates once in 2026 and once in 2027. As the US economy broadly outpaced expectations throughout 2025, the FOMC revised its 2026 GDP growth forecast from 1.8% to 2.3%.

— Jerome Powell's term as Chairman of the Fed is up in May of this 2026, at which point the current administration's nominee will be appointed. While a SEP report will be released in March, we anticipate the one scheduled for June will be the most impactful for markets in 2026.

— Since the spring of 2022, the Fed has implemented a quantitative tightening (QT) campaign in an effort to reduce its balance sheet. The Fed ended its QT efforts on December 1st, and not even two weeks later, communicated they would resume expanding their balance sheet (quantitative easing, QE) by purchasing up to $40 billion a month in Treasury Bills and Notes of up to 3 years in duration, to accommodate strains in the overnight funding markets.



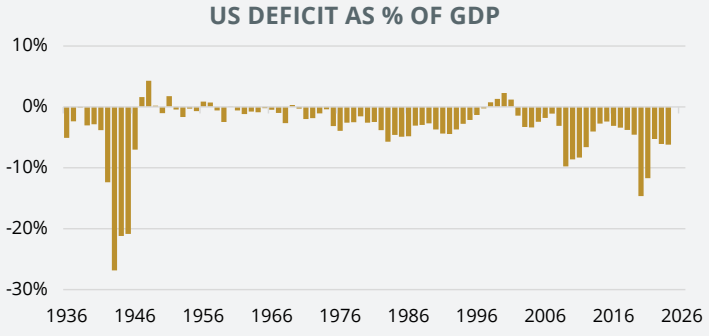


— **Our take:** The Fed is clearly in accommodation mode, which will provide continued support for the economy and markets in 2026.

FISCAL POLICY & REGULATION:

— In early July 2025, the One Big Beautiful Bill Act (OBBBA) was signed, extending much of the tax policy set to expire at the end of this year from the Tax Cuts and Jobs Act (TCJA) of 2017. In addition, accelerated depreciation for corporations will continue to encourage capital investment over the next few years.

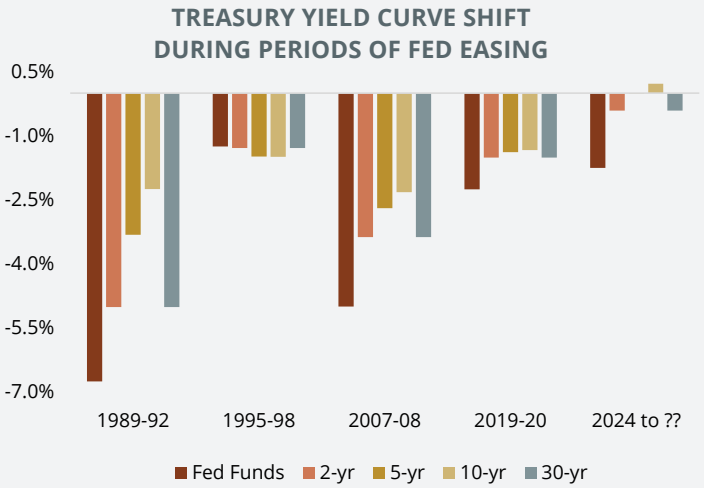
— In addition to a continuation of tax benefits, fiscal spending, funded partially through increased tariff revenues and additional borrowing, is set to continue in 2026, providing additional support to the economy.



— **Our take:** With the combination of fiscal stimulus provided to individuals and corporations by the OBBBA, and a mid-term election on the horizon, the administration will likely be inclined to maintain an accommodative stance to keep both the economy and consumers moving in the right direction.

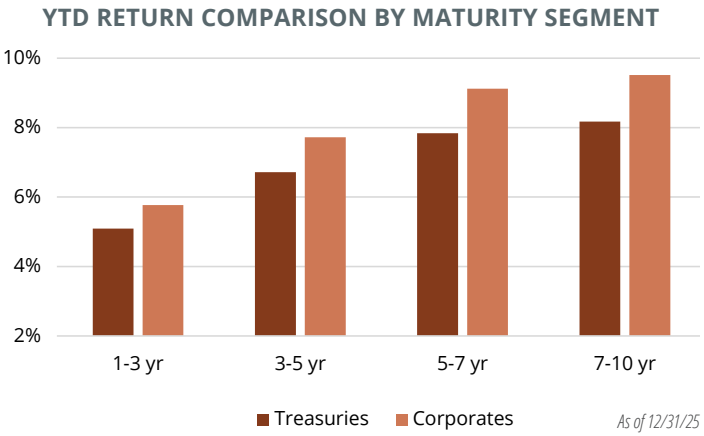
Interest Rates

- Since the Fed began its most recent interest rate-cutting campaign, starting in September of 2024, it has lowered the Federal Funds Rate by 1.75%. Despite this move in the policy rate, Treasury yields have been less impacted than in previous interest rate-cutting campaigns.
- There is a growing risk that longer-term rates will move higher, regardless of where shorter-term interest rates end up, due to uncertainties surrounding US tariff policy, potential inflation, and expanding federal debt.
- **Our take:** The front end of the yield curve will be biased lower as the Fed continues to ease monetary policy to support the labor market; however, (outside of a severe economic downturn that we don't foresee at this time), longer-term interest rates may not follow them lower.



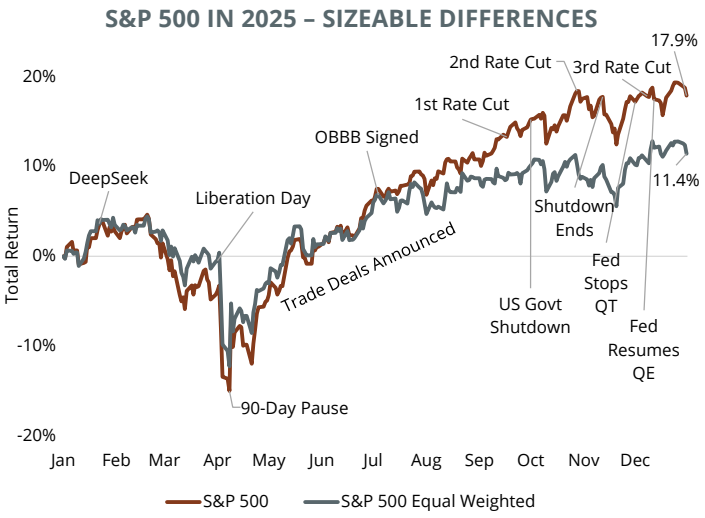
Fixed Income/Credit

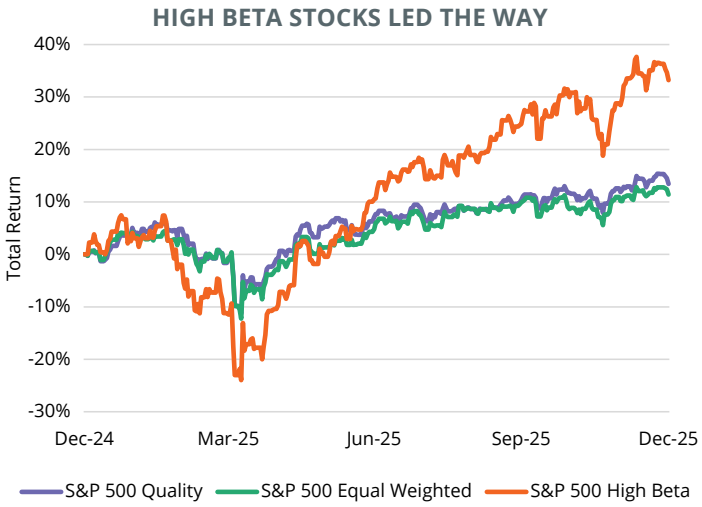
- Fixed income investors enjoyed a year of strong absolute returns, benefiting from elevated coupon income as well as price appreciation on short and intermediate bonds as interest rates fell throughout 2025.
- Over the last year, stress emerged in some opaque areas of the credit markets, prompting many to question whether it was an early sign of broader systemic risk or more idiosyncratic in nature. Stories of distressed borrowers continued to make headlines last year, but fortunately, the ripple effects were limited.
- **Our take:** Investment-grade fixed income remains an attractive asset class in the year ahead as yields remain at or above long-term averages. The steepness of the yield curve will also serve as a benefit to investors.



US Equities

- US equity markets narrowly escaped a bear market, falling nearly 20% from the mid-February high to early-April lows on tariff-induced uncertainty brought on by Liberation Day. A handful of days later, a 90-day pause on tariffs was instituted, and it was off to the races for equity markets, led by high beta and momentum stocks.
- Off the April lows, high beta stocks led the way, which is common after a sharp market decline. But the magnitude of the return differential was exceptional, outpacing the S&P 500 by over 36%. We don't anticipate this dichotomy to continue in 2026.

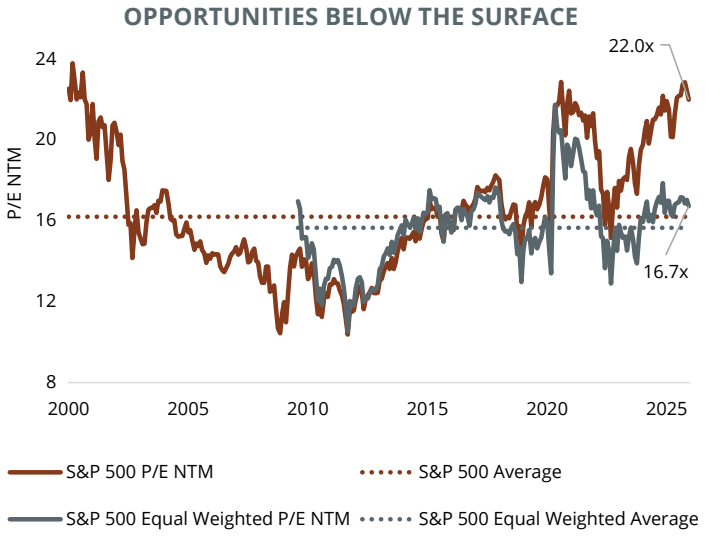




US EQUITY RETURNS (%)

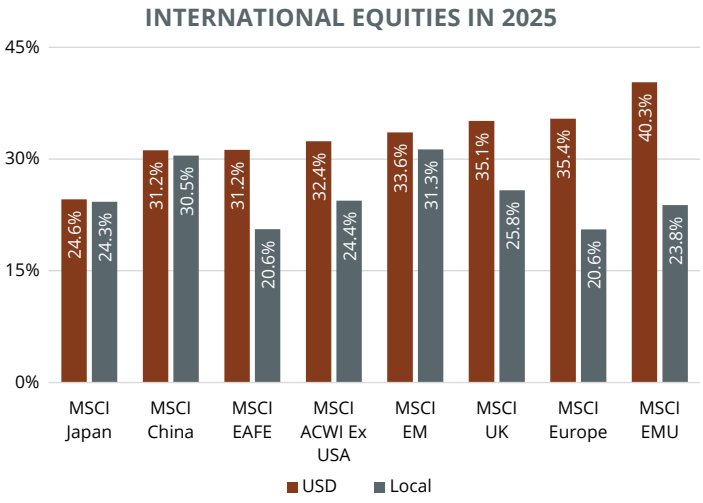
	Off April Low	2025	Drawdown
S&P 500 High Beta	75.2	33.2	-29.2
Russell 1000 Growth	48.4	18.6	-23.0
S&P 500 Momentum	45.4	26.9	-19.6
Russell 2000	42.4	12.8	-22.7
S&P 500	38.7	17.9	-18.7
Russell Mid Cap	30.1	10.6	-18.9
Russell 1000 Value	27.9	15.9	-14.6
S&P 500 Quality	27.9	13.4	-16.5
S&P 500 Equal Weighted	27.0	11.4	-16.0

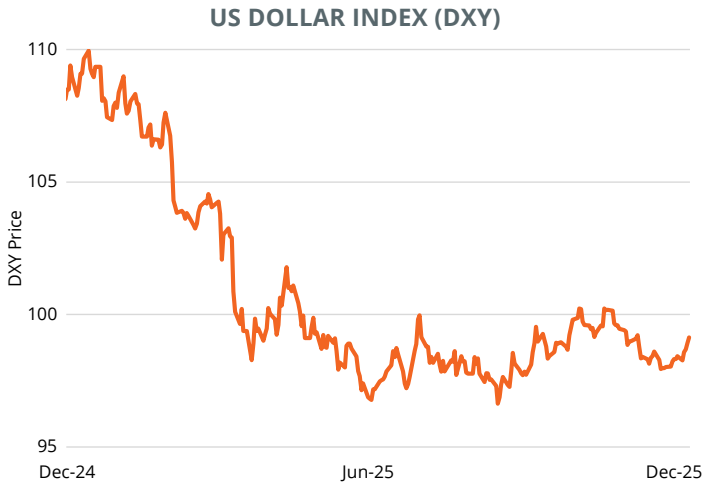
- While valuations appear full on a market-cap weighted basis at 22x, opportunity remains below the surface for equity investors. Encouragingly, the Next Twelve Months (NTM) Price-to-Earnings (P/E) multiple for the S&P 500 Equal Weighted Index is much less demanding at 16.7x.
- **Our take:** Valuations are demanding, however the Fed's easing of monetary policy and an accommodative fiscal policy stance will be incrementally supportive of equity markets maintaining valuation levels. Outperformance, however, will be driven by stocks that deliver on earnings and earnings growth.



International Equities

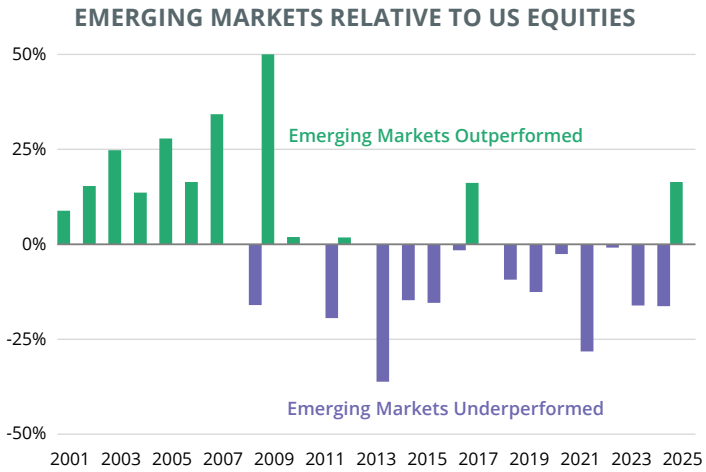
— In a change of events, international equities outpaced US equities to the upside for the first time since 2017, as central bank easing (outside of Japan) and a weakening US dollar, which fell nearly 10% in 2025, provided favorable tailwinds.





— Emerging market (EM) equities posted a strong year against US equities. Valuations for EM were low coming into 2025, and despite a strong year of performance, they do not appear overly stretched as we enter 2026, as earnings growth kept pace with that of US equities.

— **Our take:** International equities continue to do well. Specifically, we believe emerging markets are well-positioned for the year ahead. We are closely monitoring the awkward policy stance in Japan as loose fiscal policy is weakening the Yen while the Bank of Japan is tightening monetary policy, and long-term interest rates are rising, a sign of caution.



MSCI EAFE (Europe, Australasia & Far East): free-float adjusted market cap index designed to measure developed market equity performance, excluding the US and Canada.
MSCI ACWI ex USA: captures large and mid cap representation across 22 of 23 Developed Markets countries (excluding the US) and 23 Emerging Markets countries.
MSCI Emerging Markets: captures large and mid cap representation across 24 Emerging Markets (EM) countries.
MSCI Japan: designed to measure the performance of the large and mid cap segments of the Japanese market.
MSCI China: captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs).
MSCI UK: designed to measure the performance of the large and mid cap segments of the UK market.
MSCI Europe: captures large and mid cap representation across Developed Markets countries in Europe.
MSCI EMU (European Economic & Monetary Union): captures large and mid cap representation across the 10 Developed Markets countries in the EMU.

Positioning – Selectively Constructive

— We anticipate that 2026 will be yet another favorable year for asset owners as the US equity market continues to broaden out and fixed income assets maintain the fundamentals to provide solid absolute returns.

— Economic momentum coming into 2026 is strong, and the combination of an accommodative Federal Reserve and stimulative fiscal policy provides a strong base for the economy and markets for the year ahead. This is not to say that it will be smooth sailing, quite the contrary. We fully anticipate pockets of volatility in 2026, but will likely view these as opportunities for long-term investors.

EQUITIES

After three years of dominant performance, we anticipate that the strongest returns in US equity markets will be away from the market-cap weighted S&P 500 index, as accommodative policies and improving earnings breadth pave the way for a broadening out of returns.

International equities are well-positioned moving into 2026, specifically emerging market equities. Valuations for EM were low coming into 2025, and despite a strong year of performance, they do not appear overly stretched as we enter 2026, as earnings growth kept pace with that of US equities.

Overweight

⊕ US Large, Mid & Small Cap

⊕ Emerging Markets Asia

Underweight

⊖ US Mega Cap

⊖ Growth

FIXED INCOME

Fixed income markets are entering the year in a similar posture to how they entered last year. Credit spreads are tight, but opportunity remains. The securitized sector remains attractive on a relative basis; however, after a strong year of performance, the relative advantage has come in. Encouragingly, all-in yield levels are attractive, with opportunities across investment-grade sectors at or above their long-term historical averages.

Overweight

⊕ Securitized Sector

⊕ Short & Intermediate Duration

Underweight

⊖ Long Duration

⊖ High Yield Corporates

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All investing involves risks including the possible loss of principal. There can be no assurance the asset allocation portfolios will achieve their investment objectives. The portfolios may invest in equities which are subject to market volatility. In addition to the general risk of investing, the portfolio is subject to additional risks including investing in bond and debt securities, which includes credit risk, prepayment risk and interest rate risk. When interest rates rise, bond prices generally fall. Securities rated below investment grade are more sensitive to economic, political and adverse development changes.

Equity risk is the risk that securities held by the fund will fluctuate in value due to general market or economic conditions, perceptions regarding the industries in which the issuers of securities held by the fund participate, and the particular circumstances and performance of particular companies whose securities the fund holds. In addition, while broad market measures of common stocks have historically generated higher average returns than fixed income securities, common stocks have also experienced significantly more volatility in those returns.

Investing in foreign markets involves additional risks, including exchange rate changes, political and economic unrest, relatively low market liquidity and the potential difference in financial and accounting controls and standards.

Each portfolio is subject to the risks and expenses of the underlying funds in direct proportion to the allocation of assets among the underlying funds.

Upon request, Madison may furnish to the client or institution a list of all security recommendations made within the past year.

Indices are unmanaged. An investor cannot directly invest in an index. They are shown for illustrative purposes only, and do not represent the performance of any specific investment. Index returns do not include any expenses, fees or sales charges, which would lower performance.

S&P 500: large cap market index that measures the performance of a representative sample of 500 leading companies in leading industries in the US.

S&P 500® High Beta: measures the performance of 100 constituents in the S&P 500 that are most sensitive to changes in market returns.

S&P 500 Momentum: designed to measure the performance of securities in the S&P 500 universe that exhibit persistence in their relative performance.

S&P 500® Quality: tracks high-quality stocks in the S&P 500 by quality score, which is calculated based on return on equity, accruals ratio, and financial leverage ratio.

Russell Midcap: measures the performance of the mid-cap segment of the US equity universe.

Russell 2000: measures the performance of the 2,000 smallest companies in the Russell 3000® Index.

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GDPNowcast: from the Federal Reserve Bank of Atlanta, a nowcasting model that provides a running estimate of the seasonally adjusted annual rate of real GDP growth. It's designed to offer timely GDP estimates before the official release by US Bureau of Economic Analysis (BEA).

Consumer Price Index (CPI): a measure of the average change over time in the prices paid by urban consumers for a market basket of consumer goods and services.

Personal Consumption Expenditures Price Index: a measure of the prices that people living in the US, or those buying on their behalf, pay for goods & services.

Zillow Observed Rent Index: a measure of typical observed market rate rent across a given region. Designed to reflect the typical value for homes in the 35th to 65th percentile range, ensuring representativeness across the entire market rather than just those homes currently listed for rent.

Basis Point: one-hundredth of a percent.

The federal funds rate: the target interest rate range set by the Federal Open Market Committee (FOMC) for banks to lend or borrow excess reserves overnight. It influences monetary and financial conditions, short-term interest rates, and the stock market.

Yield Curve: a line that plots yields (interest rates) of bonds having equal credit quality but differing maturity dates. The slope of the yield curve gives an idea of future interest rate changes and economic activity. There are three main types of yield curve shapes: normal (upward-sloping curve), inverted (downward-sloping curve), and flat.

Duration: a measure of the sensitivity of the price of a bond or other debt instrument to a change in interest rates. Duration measures how long it takes, in years, for an investor to be repaid the bond's price by the bond's total cash flows.

Price-to-Earnings (P/E) Ratio: measures how expensive a stock is. It is calculated by the weighted average of a stock's current price divided by the company's earnings per share of stock in a portfolio.

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