

2026 Outlook

Navigating the rise of
the machines

December 2025



We are optimistic on risk assets in 2026 but the path to good portfolio performance is unlikely to be as linear as it was in 2025. Investors need to accept there will likely be more volatility than last year.

Against this backdrop, we highlight important investment themes for 2026.

AI has given but it can also take away:

Next year the global economy should see a modest pickup in growth, but it will feel different to 2025. US productivity is picking up due to cost cutting, restructuring and increasingly the broader adoption of artificial intelligence (AI) so data on output and income will likely be much stronger than employment.

Corporates will take the bulk of the machine-driven productivity gains, which is clearly positive for equities. But AI could also be a double-edged sword. Expectations about AI's ability to deliver future earnings are extremely buoyant and there is very little margin for error in risk asset prices. If these expectations are not realised, then an otherwise positive outlook could fade.

A more growth friendly White House:

The global economy has absorbed a lot of President Trump's America First agenda. But the last few months of 2025 showed the US political cycle is alive and well and already there have been signs that poor polling and heavy losses in gubernatorial elections are causing a rethink of economic policy which would likely be growth enhancing.

Midterm elections are scheduled for November, and the rising cost of living is emerging as an election issue. There also seems little tolerance for another government shutdown after the public just endured the longest on record. Negotiations to extend government funding are scheduled once more in January.

There is still more of the tariff increase to absorb, so more back peddling on tariffs could occur, or government handouts such as a baby bonus, or tariff rebate could come onto the agenda (which again would be growth friendly). There will also be continued pressure on the Fed to lower rates, particularly after Fed Chair Powell's term finishes in May.

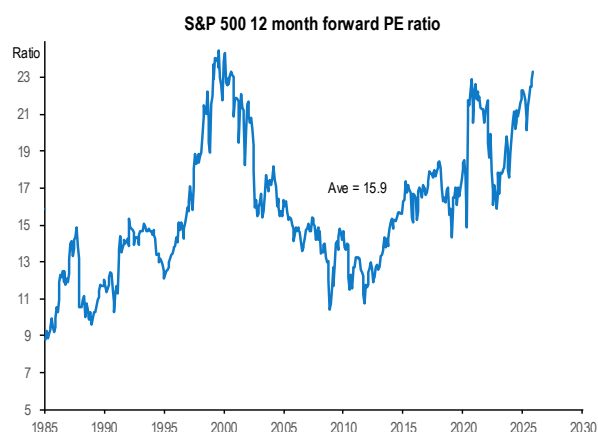
Inflation is a threat that still lingers:

Central banks are generally happy with the progress made on inflation even though it generally remains above or at the top end of their targets. Until it becomes clear the final leg down will occur it's hard to see significant further easing, unless the AI trade dislocates. In the US, there are more tariff increases in the pipeline to be passed though, and unemployment rates around the world are still relatively low.

US risk assets are priced for perfection:

The growth outlook is good, but analysts are expecting 14% US EPS growth and the market is trading on a 12 month forward PE of 23x (just below the 2000 dotcom peak). There is also stock concentration risk, with the Magnificent 7 accounting for ~70% of the return in the index this year and 34% of the market cap of the S&P 500. This leaves little room disappointment and the stakes around this are high because the US provides the direction for global markets.

The US market is priced for perfection



Source: www.Policyuncertainty.com, MWM Research, December 2025

The list of uncertainties is long, so investors should be prepared for increased volatility and be prepared to pivot if the fundamentals change. Diverse portfolios are the best way for investors to navigate this uncertainty, which can be achieved in several ways.

- In equities, we prefer EM, Europe and Japan over Australia and the US. Australia and the US are expensive and highly stock concentrated markets. Europe and Japan are more diversified with a solid earnings outlook with more attractive valuations.
- In fixed income, continue with a barbell strategy by locking in higher 'all-in yields' in quality fixed rate credit alongside floating rate senior secured private credit.
- Private and alternative assets are our preferred strategy for mitigating near-term volatility and protecting against downside risks to growth.

Overall, we are optimistic about the growth outlook and are confident that markets will have interest rate support even if that means no further rate cuts. It also seems likely the White House will become more growth friendly than it was in 2025. However, we remain watchful of increased volatility should the current investment and productivity driven AI narrative begin to fade.

Macquarie WM Investment Strategy Team

Key insights

➤ **The AI Acid Test**

2026 could be the year where the hype around AI either shows signs of transitioning into an engine of economic growth or fails to deliver on lofty expectations. It's difficult to say when this day of reckoning will occur but we know time is ticking. The impact on markets is likely to be binary in the short term and positive in the longer term like the emergence of any new technology. Markets care only about the shorter term and recent US labour market data and data on spending and investment suggest AI could be on the cusp of driving productivity gains. This would be a big positive for risk assets should this occur in 2026.

But the hype around AI is concentrated amongst a handful of US mega stocks that are driving the entire market. Investors shouldn't assume this relatively small number of names has market power or is the definition of a Warren Buffet moat. Microsoft is probably the only exception to this rule of thumb. The capex needed to fund the creation of assets may be a large barrier to entry but so too are ongoing operating costs such as electricity and it's not clear investors have factored all of this into future return expectations. Furthermore, China is rapidly closing the technology gap like any good competitor, and it has much lower energy costs.

➤ **Growth optimism with the AI wildcard**

The good news is that the work done by central banks this year should translate into a modest pickup in growth in 2026 even if it's relatively modest. Interest rate sensitive parts of the global economy such as housing and consumer spending should pick up. There's already evidence of this in Australia, where housing prices and discretionary household spending is rebounding.

The growth delta delivered by interest rate cuts must be squared up against the result of the AI acid test should it emerge. The upside risk to US growth comes from the AI evolution and whether productivity benefits are large enough to meaningfully lift economic growth. If this can kick in, inflationary pressures could ease, and this may provide room for policy to be eased as consensus expects. But downside risk to US growth in 2026 also sits with the AI evolution. Investment in AI accounted for nearly 50% of US GDP growth in 2025 leaving the economy vulnerable to a pullback in capex and a potential asset overhang, which could depress returns in the Tech sector for years.

➤ **America First; but let's fine tune that**

The political cycle in the US has shown itself to be alive and well as we enter 2026. The Trump administration began 2025 all guns blazing implementing its America First agenda. Federal government jobs were slashed, immigration was cut, the national guard was employed to do police duty, recession threatening tariff settings were announced, and taxes were cut with government debt set to increase by \$US3.4tn over the next 10 years.

But as the year went on the authoritarian political power of the President seen in the first half of year began to dwindle. Tariffs in key areas close to the consumer were cut, Republicans suffered gubernatorial election losses in New York, Virginia and New Jersey, and the government was shut down for a record 42 days despite Republicans having control of both houses. Fed rhetoric had eased but reemerged once more before the December FOMC.

Midterm elections are due next November, so fine tuning, or outright back peddling of harmful economic policy will likely be a feature of the Trump Administration for most of next year, which will undoubtedly be growth friendly. The big election promises have been delivered but this doesn't mean the President will go missing in action. One of the first tests will be in January when once again Congress needs to extend government funding. The US government budget doesn't have room for more fiscal stimulus but if the labour market remains soft there will be pressure to spend before midterms.

➤ **No clear path to lower inflation and rates**

Global central banks will generally be pleased with the progress made on inflation. However, there is still unfinished business. It remains above target in many jurisdictions, and this is limiting the ability for them to ease policy further.

The Fed is trying to balance the inflationary consequences of the increase in trade tariffs with keeping support for weakening labour market. The ECB doesn't have room to cut rates aggressively either and is absorbing the hit to exports from US tariffs by squeezing more out of the domestic economy. The BoJ is steering policy in the opposite direction, normalising rates to slow growth and bring inflation down after decades of fighting weak growth and deflation.

In China, the property downturn remains a significant brake on growth, but US tariffs have not stopped the economy posting record trade surpluses. The two-speed economic model of the past 4 years hasn't reached its use-by-date just yet. In Australia, the RBA is coming to grips with an inflation threat stronger than it envisaged and has finished cutting rates this cycle.

➤ **Risk assets are priced for perfection**

US and Australian equities are expensive, despite recent volatility, and would be hit hard during a sustained period of global risk-off. The big tech stocks have a large concentration in the main US indices so their direction will provide direction for global markets.

Investors don't seem to be questioning whether AI will deliver on productivity, but they are beginning to question the price that should be paid even though the heavy weight tech stocks have a proven track record of beating earnings estimates. To be clear we are positive on risk assets, but clients should diversify their equity portfolio.

Investment implications

Asset class	Asset class comment	Preference
Cash (Australia)	It is likely that the RBA has finished easing and cash rates will remain higher for longer, with the next move likely higher cash and short-term rates. Investors should also consider locking in higher 'all-in yields' further out on the yield curve to provide additional yield enhancement.	Maintain levels sufficient for transaction and liquidity purposes.
Equities	<p>Equities normally rally through slowdowns and provided this is what we see during the remainder of the year we maintain a 'neutral' stance on equities despite extended valuations, optimistic earnings projections, and the still uncertain path of trade policy.</p> <p>We favour value-oriented sectors, which benefit from more reasonable valuations, deregulation, and the broadening of economic activity beyond AI infrastructure-driven spending.</p> <p>Regionally, we identify better opportunities outside the US, driven by more compelling valuations and improving sentiment, supported by increased fiscal spending and accommodative central banks.</p>	<p>Markets: Favour allocations outside the expensive and highly stock concentrated US and Australian markets. Overweight Europe, Japan and emerging markets through underweights in US and Australia.</p> <p>Size: Bias toward small cap over large cap stocks but acknowledge that a more attractive entry point is needed to have strong conviction.</p> <p>Style: Favour value over growth, given central banks have room to lift cyclical economic growth next year, bond yields are likely to remain relatively high, and IT earnings growth is likely to slow. Additionally, ex-US equity markets are more 'value' than 'growth' oriented vs the US.</p>
Fixed income	<p>Higher all-in yields for fixed income provide an attractive longer-term allocation, downside protection and a ballast to an overall portfolio.</p> <p>A barbell strategy, balancing fixed rate, higher quality (mid-curve) assets against floating rate, senior secured non-cyclical private credit, remains a prudent approach into early 2026. Navigating credit markets will require diligent security selection, sector rotation, documentation analysis and an active management approach.</p>	<p>Sovereign: Prefer mid-curve maturities over the long-end, which will be less sensitive to tariffs and term premia. Developed market government bonds will be shaped by the tension between supportive rate cuts and the pressure of massive issuance and potential fiscal mismanagement.</p> <p>Investment Grade: Credit spreads are entering 2026 at historically tight levels, making security selection critical. We remain constructive on investment grade 'all-in' yields and positive demand and supply imbalances.</p> <p>High yield is supported by higher carry, lower breakevens, a pro-growth backdrop, and sound balance sheets, but it is much more susceptible to 'risk off' events. We prefer senior secured non-cyclical private credit for its attractive illiquidity premium and superior protections through covenants and documentation.</p>
Private credit	Continues to offer a premium (illiquidity) over public fixed income markets, while also providing structural protection in the form of seniority, documentation and a bias to defensive industries.	Core: Prefer segments where competitive pressures are less acute, including US middle market direct lending, European direct lending and asset-based finance.

<p>Alternatives</p>	<p>Private equity: Improving liquidity, steady financing markets and narrowing bid-ask spreads (improving exit dynamics) are all supportive of activity. However, market beta is no longer an easy driver of return, and earnings growth and disciplined execution will be the primary determiner of future performance.</p> <p>Hedge funds: Greater market and policy dispersion, and directional volatility should benefit hedge funds' ability to harvest alpha from market inefficiencies and dislocations.</p>	<p>Private equity: Prefer small to middle market buyout relative to large buyout, secondaries and recent vintages.</p> <p>Hedge funds: Prefer multi-strategy funds that employ disciplined risk frameworks and can nimbly allocate across asset markets.</p>
<p>Real assets</p>	<p>Real assets offer stable income, inflation hedging, and diversification, and are less impacted by tariff policies due to their contracted cash flows, positive correlation to inflation, and strong fundamentals.</p> <p>Infrastructure: Will continue to benefit from structural tailwinds of deglobalisation, digitalisation, the energy transition and supply/demand shortfall.</p> <p>Property: The commercial real estate cycle has turned positive.</p>	<p>Infrastructure: Prefer core, unlisted, infrastructure due to less correlation to listed markets.</p> <p>Property: Prefer core diversified exposures.</p>

Global economics: Not the typical response to lower rates

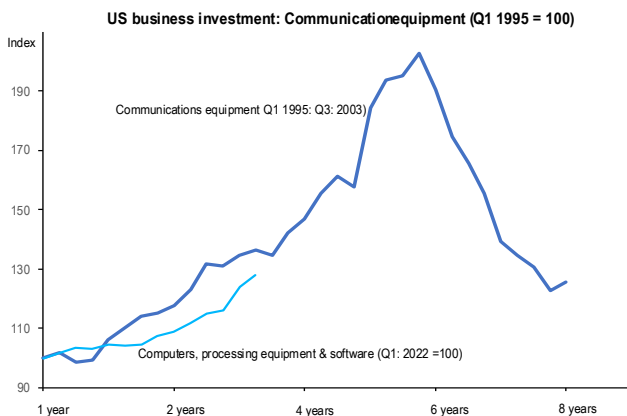
- Global economic growth is likely to pick up in 2026, but it won't feel like an interest rate-led rebound. Rates have not been aggressively cut and more tariff pass through needs to be absorbed. Macquarie expects US growth to rise from 2.0% in 2025 to 2.6% in 2026. The downside risk is if the AI bubble bursts.
- China has been able to maintain its two-speed economy and Macquarie expects this to continue and policymakers to achieve their 5% growth target.
- Australia and the Euro area have probably finished cutting rates. Inflation is under control in the Eurozone, but upside risks remain in Australia.

The US

The US has been the leader of global growth since the end of the pandemic and next year should see a modest pickup on the back of lower rates. Macquarie's economics team expects growth to rise from 2.0% in 2025 to 2.6% in 2026. However, home grown downside risks are also rising. Investment in IT investment as a share of GDP, is now back to the dotcom peak in 2000 on the back of investment in AI. But compared to back then, the stock market boom looks in its infancy.

There are three important economic effects that these types of investment booms have: 1) the direct impact on economic growth, 2) the indirect impacts or 2nd round effects and 3) the wealth effects created by the equity financing. The reverse of this happens during the bust with direct and indirect investment and wealth effects all contracting and if large enough could drag the economy into recession like the dotcom bust. But for now, the outlook seems positive.

The AI boom may continue for a while yet



Source: FactSet, MWM Research, December 2025

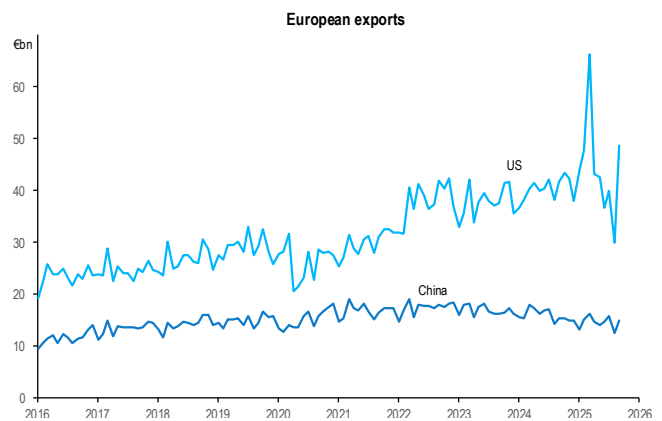
Europe

The ECB is one of the few major central banks that are comfortable with the outlook of its jurisdiction. Inflation has been between 2.2% and 1.9% since March and the ECB assesses that the current pace of growth is slightly below

trend. Macquarie's economics team expects that the ECB has finished its easing cycle and that growth should ease from 1.4% in 2025 to 1.1% next year.

The economy has room for consumer spending to pick-up, given the high household saving rate. Infrastructure and defence spending are also expected to provide lift growth. The economy is leveraged to movements in trade, and the region has struggled with the increase to US tariffs. The EU US trade deal saw tariffs on goods exported to the US fall from an effective rate of 20% to a broad 15% ceiling that included more access to each market.

European exports to the US are back to trend growth

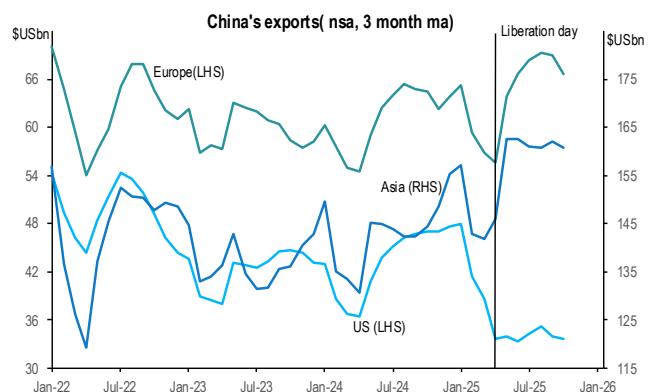


Source: FactSet, MWM Research, December 2025

China

China will most likely continue with its two-speed economic model of strong manufacturing and exports combined with weak consumer spending and property in pursuit of its GDP growth target (~5%). Trade performance was a positive surprise last year in the face of the US-initiated trade war. China used its relatively low-cost production capability to win share in markets in other parts of Asia and offset lost market share in the US. The agreed US tariff settled at ~30%, like Indonesia (19%), Malaysia (19%), and Vietnam (20%). As a result, China's exports to the US may increase in 2026 due to the reduced incentive for re-routing.

China's exports have been diverted to Asia and Europe



Source: FactSet, MWM Research, December 2025

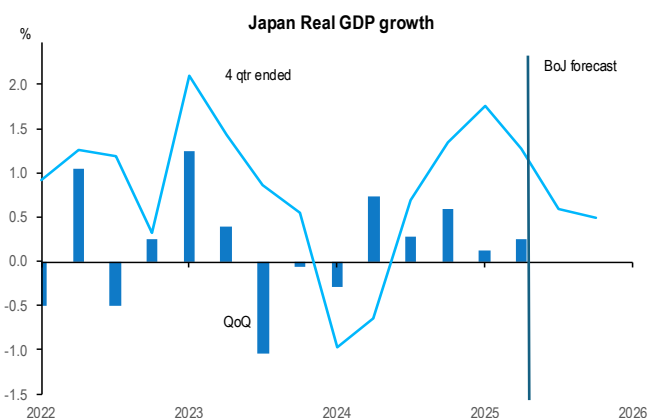
Japan

The latest BoJ forecasts show GDP growth of 0.6% in FY 2026 (0.7%) and 1.0% in FY 2027 and estimated potential growth of 0.5%. This forecast keeps alive prospects of further hike to normalise monetary policy while almost every other central bank has ended or is nearing the end of their easing cycles.

But even though growth is slowing, but the downside risks are limited by the government weighing in last month with a fiscal stimulus of Yen21.3tn (\$US153bn) targeting households and their struggle with persistent inflation. The package will include general spending of Yen 17.7tn (\$US113bn) and Yen2.7tn (\$US40bn) in tax cuts. It will be funded by an increase in tax revenue and government bond issuance.

Economic growth in Japan also depends on trade performance and the weaker Yen over the past few months has provided timely support for exports as the country absorbs a tariff of 15% on most its exports to the US.

GDP growth is slowing but still above potential



Source: FactSet, MWM Research, December 2025.

Australia

Inflation came back to bite at the end of this year, with the surprise increase in trimmed mean inflation during Q3 25 (1% QoQ vs expectations of 0.8% QoQ). This forced the RBA to raise its inflation forecast from 2.6% to 3.2% in Q4 25 and keep it at that rate until Q2 26. As a result, markets expect the target cash rate to now remain at 3.6% for all next year.

The RBA expects the unemployment rate to broadly remain around 4.4% over the next couple of years with wages growth of around 3%. Expectations of further interest rate cuts have evaporated as the 75bp of interest rate cuts since February is working through the economy and providing a boost to consumer spending and dwelling prices. But the economy has little room for a pickup in consumer spending, with underlying inflation rising to 3.3% in October. Financial market expectations are now implying an RBA hike by end of 2026.

The RBA expects wage growth to slow further

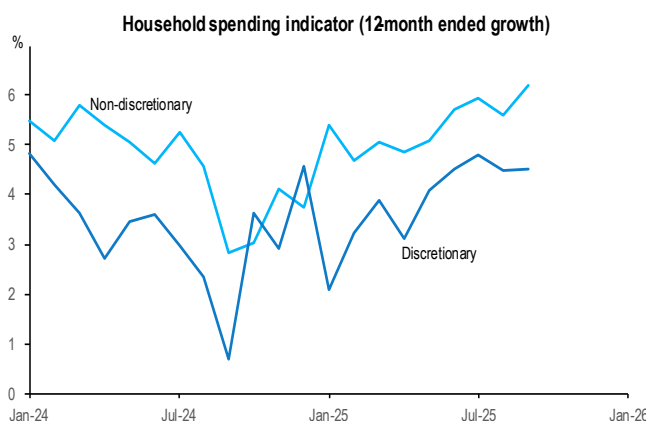


Source: FactSet, MWM Research, December 2025

Government spending has risen from 21% of GDP to 28% over the past 10 years squeezing out both consumer spending and business investment. However, lower rates and rising dwelling prices and turnover (apart from Perth) has helped boost discretionary consumer spending. The items seeing the largest increase in discretionary spending include recreation and culture, and furnishings and household equipment.

Non-discretionary spending has risen because of upward pressure on the price of electricity, rent and health care.

Consumer spending is picking up



Source: FactSet, MWM Research, December 2025

Employment growth slowed in the first half of the year with the trend monthly change slowing from 22k at the start of year to 11k by mid-year, but by October it had accelerated once again to 27k. The unemployment rate has drifted up to 4.3% but in the RBA's view the labour market remains tight.

Global equities: Diversification, not concentration

- A pickup in economic growth next year even with more tariff spillover is providing a generally positive backdrop for global equities. But a key risk is that the AI boom turns to bust, despite it having positive earnings fundamentals.
- US Tech capex plans are both large and ambitious, expected return hurdles are probably too high, and stocks remain priced for earnings perfection.
- Investors can manage this risk by diversifying into ex-US international equity markets, which are more 'value' than 'growth' oriented.

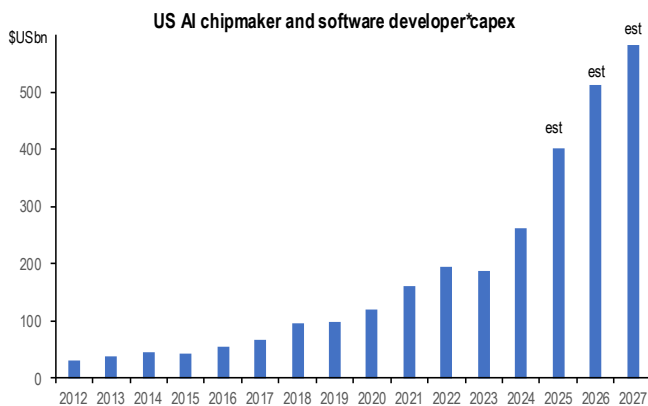
The starting point for 2026 is like the start of 2025 in many ways.

- The AI boom is continuing, and the pipeline of capex behind it is getting larger. US index valuations are stretched
- Europe, Japan and EM offer better value than the US, but more leverage to the downside risks of trade.

The major differences are:

- The absorption of tariff increases is well advanced and has not derailed markets.
- More interest rate support is less likely; and the earnings growth outlook delta on GDP growth is larger.
- Productivity benefits from the AI boom are becoming more apparent. But AI evolution is a two-edged sword. Just because returns to business are rising from the investment doesn't mean that boom can't become bust because expectations become overinflated.

US IT capex is set to ramp up

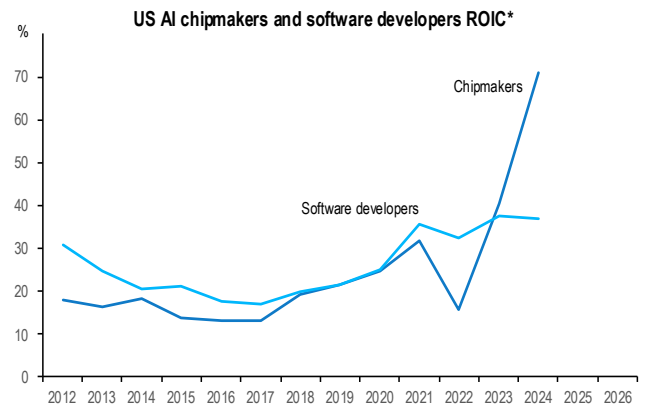


Source: FactSet, MWM Research, December 2025. *Chipmakers include Nvidia, AMD, Intel, Qualcomm. Software developers are Microsoft, Meta, Apple, Alphabet, Amazon and Oracle.

Capex amongst the large chip maker and software developers is set to increase from \$US400bn in 2025 to \$US640bn in 2027 according to consensus estimates.

The IT firms will continue to invest while they think their return on investment targets can be achieved. Both software developers and chip makers are seeing strong returns on invested capital and this feeds into their confidence about the outlook. But this is also a concentrated trade amongst a small group of mega cap stocks that has consequences for not only the stocks themselves but stocks globally.

Nvidia drives a surge in return on capital for chip makers.



Source: FactSet, MWM Research, December 2025. ROIC is net operating profit after tax/ invested capital market cap weighted. Chipmakers include Nvidia, AMD, Intel, Qualcomm. Software developers are Microsoft, Meta, Apple, Alphabet, Amazon and Oracle.

Regional tilts

The AI fundamentals still seem solid, but investors should manage the risk of a downturn by diversifying global equity portfolio into other markets such as Europe, Japan, and EM.

Exports are an important driver of earnings in these markets, but they weathered the tariff upheaval in 2025 and are well placed to benefit from the pickup in global growth that we expect next year. Valuations are not as stretched as the US, so they are more likely to outperform overvalued markets like the US if the AI trade begins to unwind.

In EM, China showed resilience to the increase in US tariffs, and it has a smaller weight in Tech stocks than the US. But it is a Tech offering that is attractive if our concerns about the Tech sector are misplaced.

Style

The lift in economic growth next year should provide an earnings delta for value stocks and they will likely outperform growth if there is a major correction led by the Tech sector. This also aligns with our regional preferences where we don't think it make sense to concentrate portfolios in the US.

Size

We prefer small cap stocks over large cap stocks because of the likelihood of a pick in economic growth next year. But investors with portfolio drift accumulated in large cap tech stocks could also derisk by diversifying into large cap defensive names, which should likely outperform small cap stocks if bloodletting in the tech sector led to a macroeconomic downturn.

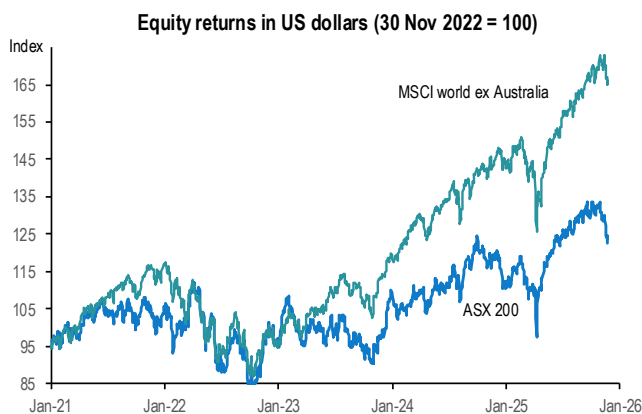
Australian equities: The key line of defence

- Australia may have underperformed the rest of the world since the launch of ChatGPT put a turbo under the global IT sector, but Aussie banks and Consumer discretionary stocks have delivered investors similar returns to global equities.
- Returns this year have been driven mostly by PE multiple expansion, with little contribution from earnings. Consensus expects 8% growth in earnings next year, but this may prove too optimistic.
- But Australia has shown that it is generally a good defensive market, particularly when global interest rates are rising and it should be a key part of the line of defence in portfolios.

The world changed for investors after the launch of ChatGPT in November 2022. Global capital flooded into anything Tech in the US and other markets, but we've seen this playbook before.

During the mid-late 1990s dotcom boom that incumbent Fed Charman Alan Greenspan called 'irrational exuberance'. But he made this comment in December 1996 some 3 years before the boom turned to bust. Robert Shiller had better timing releasing a book of the same name as the market peaked. During this period Australia was seen as an old-world equity market and underperformed for several years. The period following the launch of ChatGPT has a similar vibe. The ASX 200 has underperformed the rest of the world by 35%.

Australia has underperformed since the ChatGPT take-off



Source: FactSet, MWM Research, December 2025

However, just because there are none of the big global Tech stocks listed on the ASX 200 doesn't mean investors in the local market haven't had a good year. The Aussie banks and Consumer Discretionary stock have performed in line with the rest of the world since the launch of ChatGPT. Materials have outperformed these two sectors and Healthcare since the middle of this year.

Banks, Materials, Healthcare and Consumer discretionary account for around 70% of the market cap of the ASX 200.

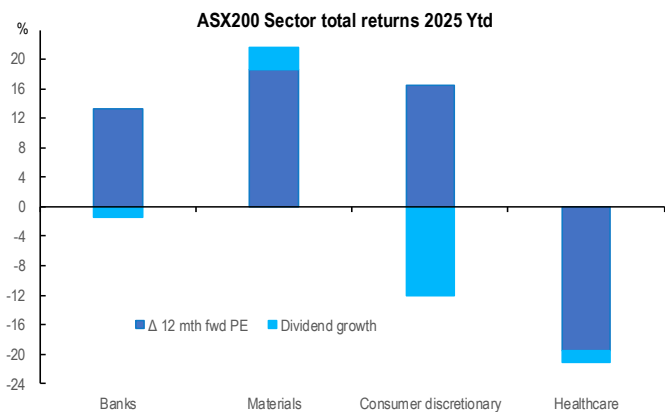
Aussie banks and consumer discretionary have not been left behind



Source: FactSet, MWM Research, December 2025

However, the returns of these sectors in 2025 were driven by PE multiple expansion rather than earnings growth and this leaves the market vulnerable to a global pullback. Consensus expects 8% growth in earnings next year but given the relatively small pickup in economic growth we think this may prove too optimistic.

PE expansion is driving returns



Source: FactSet, MWM Research, December 2025

We highlighted the number of risks for investors next year and Australian equities have a proven track record of providing a defensive buffer to portfolios in periods of global market volatility, particularly when interest rates are rising. Aussie equities should then be used as a key part of the diversification strategy in risk assets that we recommend for next year.

Fixed interest and public credit: The only certainty is uncertainty

- 2025 was shaped by shifting central bank policies and geopolitical uncertainty, US investment-grade corporates were the standout performer.
- Monetary policy will be the key driver of fixed income returns with a focus on yield curve, sector and region.
- Maintain a barbell strategy of public vs private.

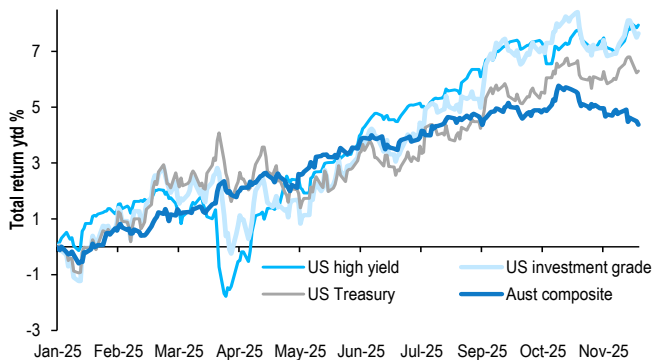
In 2025, markets were shaped by a complex interplay of shifting central bank policies, persistent geopolitical uncertainty, and fluctuating investor sentiment. As the global monetary easing cycle started to slow, central banks pivoted towards a more hawkish, data-dependent stance, with the Federal Reserve tempering market expectations into November. Ultimately, Australian rates "blinked," underperforming the US due to inflation concerns and implying no further easing expectations for the RBA into 2026.

While strong corporate fundamentals, loose financial conditions, and robust demand for yield supported global credit markets, government bonds saw significant volatility in the first half of the year, driven by the ongoing risks of trade wars and tariffs. Credit markets were also tested by two high-profile defaults, TriColor and First Brands. In response, both private and public markets defended their stability, noting no signs of underlying systemic credit deterioration or a turn in the credit cycle.

US investment grade corporates were the standout performer on a risk adjusted and outright basis. Credit spreads (excess returns) were generally flat year to date, whilst most of the performance came from short end rates sharply rallying and excess yield (carry) above government bonds.

Fixed interest and credit market performance year to date

Australian composite returns vs US investment grade and high yield YTD



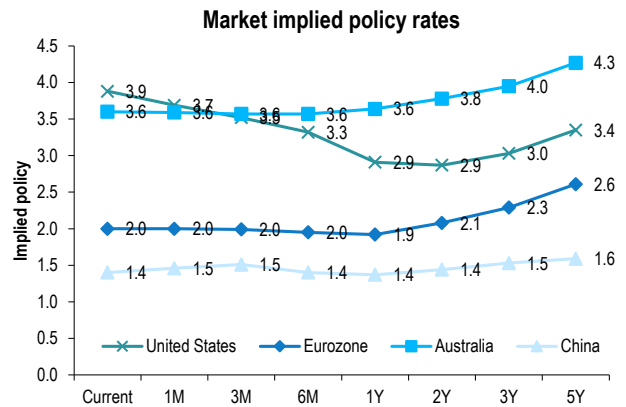
Source: Bloomberg, MWM Research, December 2025

Key themes in fixed income and credit for 2026

Monetary policy: Will be the central driver of fixed income returns. Whilst a general easing direction remains in place,

the pace going forward, central bank data dependency alongside sticky inflation and ongoing 'foggy' data from the US government shutdown and transmission of tariffs makes duration management challenging. Some regions have already diverged such as Australia, Europe and Japan.

Global market implied policy rates



Source: MWM Research, December 2025

The yield curve: There remains a consensus on steepening and term premia in the longer end as fiscal sustainability remains a structural theme. In a balanced portfolio, a focus on mid-curve positioning remains a prudent hedge against market shocks and excessive capital volatility from the long end of the yield curve.

Sovereign debt: The outlook for key developed market government bonds is shaped by the tension between supportive rate cuts and the pressure of massive issuance and potential fiscal mismanagement.

Credit markets: Credit spreads are entering 2026 at historically tight levels, making security selection critical. We remain constructive on investment grade 'all-in' yields and positive demand and supply imbalances. While high yield is supported by higher carry, lower breakevens, a pro-growth backdrop, and sound balance sheets, it is much more susceptible to 'risk off' events. We prefer senior secured non-cyclical private credit for its attractive illiquidity premium and superior protections through covenants and documentation.

Regional satellite views: Emerging market debt continues to offer some diversification and value from core fixed income benefiting from a weaker dollar and ongoing disciplined local policies.

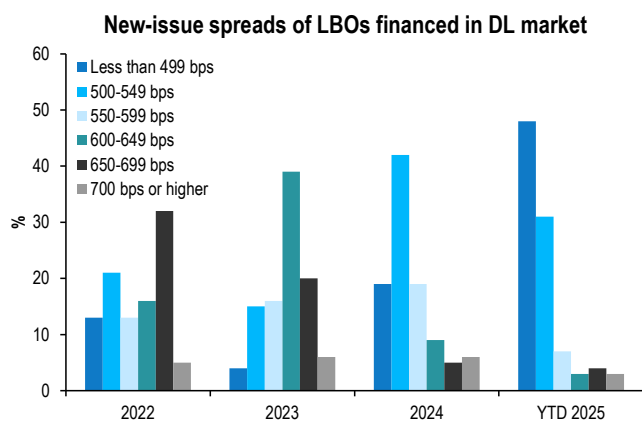
A post-mortem of 2025 and a look into 2026 highlights the many dimensions of risk in fixed income, including credit spreads and their beta to growth, outright interest rates, yield curve positioning, and term premiums, as well as regional positioning. This is why a barbell strategy, balancing fixed rate, higher quality (mid-curve) assets against floating rate, senior secured non-cyclical private credit, remains a prudent approach into early 2026. Navigating credit markets will require diligent security selection, sector rotation, documentation analysis and an active management approach.

Private credit: Discipline to defend against dispersion

- Private credit all-in yields remain attractive and continue to compare favourably to public credit alternatives. Stable interest rates and investor demand should continue to support primary market activity.
- But cracks are emerging given late-cycle dynamics, and investors should be aware of signs of stress in more cyclical sectors or mispriced loans with loose terms.
- Performance dispersion is accelerating across managers and borrowers, making origination, deployment and underwriting discipline and workout capability critical sources of alpha for coming vintages.

Private credit continues to offer investors a differentiated source of income, with additional yield pick-up to public credit markets. On one side, deal volumes have remained muted relative to recent years due to a slow-to-recover buyout market. On the other hand, fundraising has proven resilient, with mega funds, those raising over \$5 billion, accounting for ~42% of all capital raised by closed-end vehicles in 1H25, and ~89% from funds exceeding \$1 billion, according to Pitchbook data. This highlights the dominance of large asset managers and the intensified competitive landscape, particularly within direct lending, for attractive deals, making it harder for smaller players.

Spreads compress amid competition for quality deals

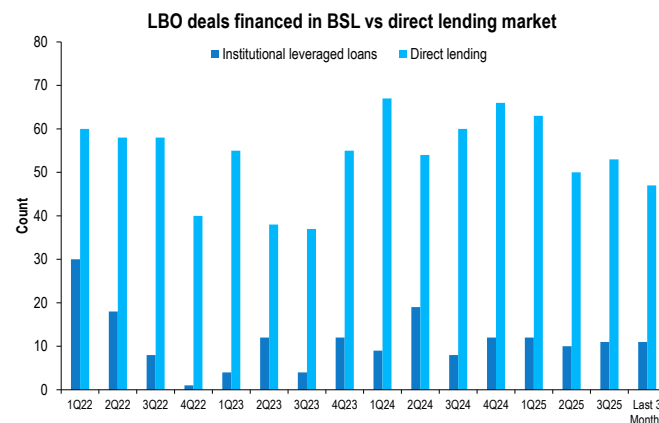


Source: PitchBook LCD, as of 31 October 2025. Region: US. Data reflects senior secured loans and unitranche facilities.

The imbalance between robust fundraising and moderate deal flow has put downward pressure on loan spreads and terms. Despite some improvement in deal activity towards the second half of 2025, lenders have yet to regain leverage on pricing. Competition for quality transactions has driven spreads to multi-year lows. In the US, direct lending spreads for buyout deals converged in the SOFR +450–500 bps range, with 45% of deals priced there as of October 2025, up sharply from 18% the previous year, according to Pitchbook data. Europe has mirrored this trend, with average spreads

tightening by 100 bps since 2020, although still command higher absolute spreads versus the US, with most deals now pricing between 500-600 bps over the base rate.

Direct lending LBO deal counts have seen a slowdown



Source: PitchBook LCD, as of 31 October 2025. Region: US. Deal count is based on transactions covered by LCD News.

The outlook in 2026 is broadly constructive, but the market is increasingly defined by widening performance dispersion – a ‘tale of two cities’. Lower interest rates and greater clarity on tariffs and macro policy should unlock buyout and M&A activity, providing essential exit pathways for sponsors and supporting improved deal volumes. This may reduce reliance on deals funding dividend recapitalisations, which have been prevalent amid subdued sponsor exits.

Still, risks linger beneath the surface. Deal flow is rebounding, but quality is mixed, and competition for attractive transactions continues to compress spreads to multi-year lows. Features such as PIK toggles and balance sheet repair transactions, such as LMEs and amends-and-extends, remain areas for monitoring as they can mask underlying weakness in free cash flows.

This bifurcation in borrower health will translate directly into performance dispersion among private credit managers. Larger, sophisticated managers hold a distinct advantage, with scale, origination networks, and risk management capabilities that enable access to higher quality deal pipelines and proactive portfolio oversight. Smaller managers, or those with concentrated exposures to challenged sectors, may struggle as competition intensifies and performance gaps widen.

For investors, we view direct lending in the US middle market to be more attractive relative to large caps, where spread compression is more acute. European direct lending has greater structural tailwinds vs the US, including regulatory-driven bank entrenchment and origination gaps due to regional fragmentation. Asset-based finance offers further portfolio and yield diversification through asset collateralisation. As competition intensifies, manager selection and active sourcing remain critical to capturing above-median returns and mitigating downside risk in a more complex, differentiated market landscape.

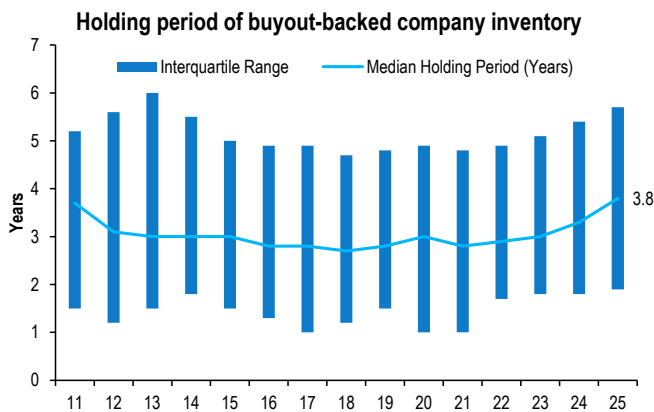
Alternative assets: Looking beyond beta

- Improving deal and exit activity signals a thaw in private markets – yet the strongest exits remain concentrated in top-quality assets with resilient fundamentals.
- Macro uncertainty and tighter credit conditions mean the days of easy beta are over. Return will hinge on operational value creation and asset quality.
- Multi-strategy hedge funds are benefitting from greater market dispersion and directional volatility but rising competition for talent mean manager selection and fee discipline is crucial.

Private equity: From reset to reacceleration

Private equity (PE) markets staged a solid recovery in dealmaking and exits through 2025, setting the stage for a more constructive 2026. Recent quarters saw a marked uptick, especially among larger sponsors. Aggregate deal values surged 38% y/y in Q3, according to Pitchbook, driven by megadeals and renewed investor risk appetite. Exit counts have also rebounded, surpassing prior-year levels, though most exit value remains concentrated in top-quality assets – those with resilient fundamentals and clear growth prospects.

Sponsor portfolios continue to age

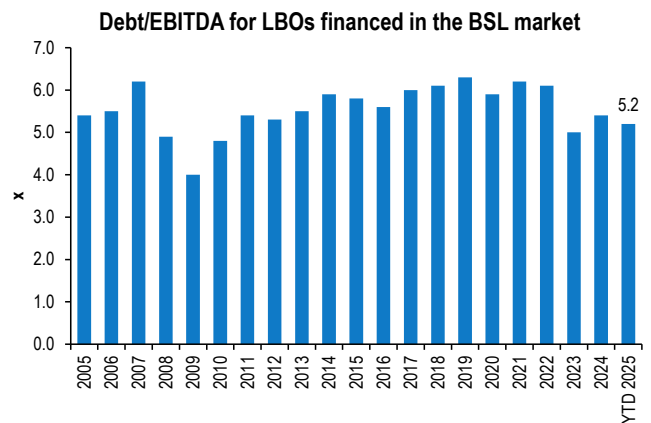


Source: Pitchbook, data as of 22 October 2025. Region: US. Note: Companies held for more than 15 years are excluded.

Yet, this rebound is far from uniform. The median holding period of buyout-backed companies is the longest since 2011, with 30% of companies having a holding period of more than five years. The return of exit activity has exposed dispersion in manager track records and asset quality. Investments made at peak valuations in 2021 and early 2022 now face tougher operating environments, with many requiring longer holding periods or creative exit structures to achieve target returns. Conversely, assets acquired at more conservative multiples in earlier vintages have delivered stronger exits. Investors continue to pay a premium for quality, and disciplined deployment remains essential. As liquidity returns, the market is likely to reward those who exercised patience and selectivity during the recent cycle of recalibration.

Looking deeper, signals are mixed. Core buyout fundamentals are stable; steady valuation multiples, contained leverage levels, improved debt burdens, and healthy cash coverage. However, credit markets show signs of stress: new issuance is rolling over, distressed exchanges are outpacing outright defaults, and downgrades exceed upgrades. Distribution yields, while improved from 2023 lows, remain below historical norms, with many managers relying on liquidity management tools such as continuation vehicles and dividend recaps to sustain distributions.

PE fundamentals appear stable with improved debt loads



Source: PitchBook LCD, data as of 30 September 2025. Region: US. Note: Includes issuers with EBITDA of more than US\$50 million.

Buyout's rebound appears real, but its sustainability depends on the broader economy and credit conditions. Interest rates are expected to remain rangebound, with central banks signalling only gradual easing. The era of easy monetary policy is over, and managers must navigate tighter credit and ongoing macro uncertainty. Generating returns from market beta alone is fading, making operational value creation through margin expansion and revenue growth a critical differentiator. Investors should focus on strategies with attractive entry valuations, operational value creation, and clear exit pathways. Small and mid-market buyouts, secondaries, and new vintages are poised to benefit from improved financing conditions and normalised valuations.

Hedge funds: Turning volatility into alpha

Hedge funds, especially multi-strategy platforms, remain a compelling source of diversification. The year delivered a rich opportunity set across equities, credit, and macro, supported by improved financing and greater market dispersion. The largest managers captured the majority of new capital inflows, leveraging scale and robust risk infrastructure to strengthen their competitive edge. The 2026 outlook is broadly supportive, with diverging central bank policies and increased earnings dispersion favouring multi-strategy funds able to deploy risk across diverse, uncorrelated trade ideas. Opportunities in equity issuance, M&A, and event-driven strategies should persist, while credit and quantitative strategies benefit from refinancing activity and single-stock volatility. However, intense competition for talent, capacity constraints in niche trades, and rising funding costs pose challenges. Tighter dealer balance sheets and regulatory scrutiny may restrict some strategies, making manager selection and fee negotiation increasingly critical for investors.

Real assets: Tailwinds for infrastructure & property

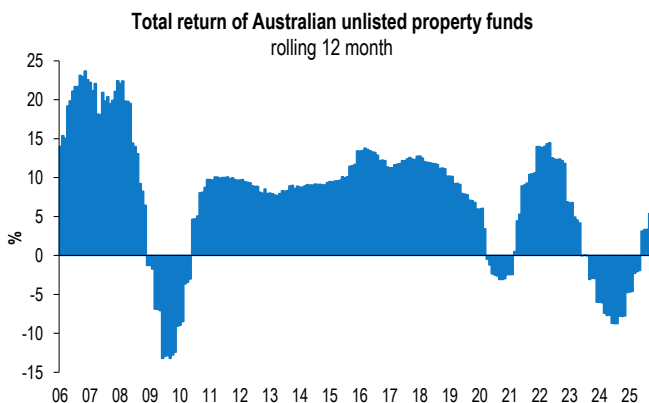
- We like real assets which we believe offer compelling risk-adjusted returns with limited directional exposure to public markets.
- Unlisted infrastructure offers attractive fundamentals, long-term visibility and structural tailwinds from decarbonisation, digitalisation, and deglobalisation.
- Property stands to benefit as the nascent upswing in the commercial real estate cycle continues to gather pace.

Real assets continue to provide a strategic role in portfolios, delivering stable income, inflation hedging and diversification amid slower global growth and persistent macro risks. Real assets are less likely to feel the transmission of tariff policy given their contracted cash flows, positive correlation to inflation and healthy fundamentals. Infrastructure remains well-supported by secular tailwinds, such as onshoring, digitalisation and decarbonisation.

Property

Commercial property prices in the US and Australia appear to have bottomed and are in an upswing, which is bullish for both unlisted and listed real estate. All three major sectors (office, retail and industrial) appear to be in an upswing, with cap rates having stabilised.

Australian unlisted property in an upswing



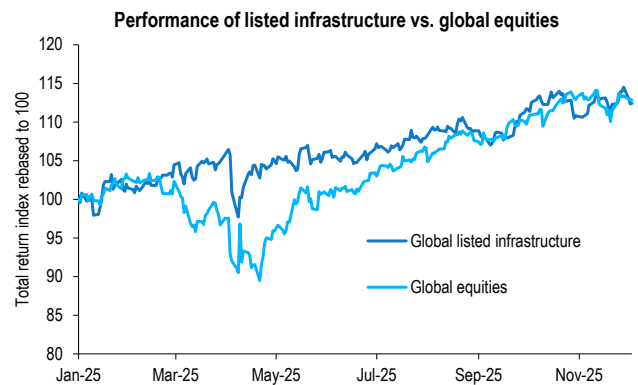
Source: ANREV, December 2025.

Infrastructure

Unlisted infrastructure looks compelling as its relatively defensive cash flows mean infrastructure returns are relatively less volatile than for other traditional asset classes. High barriers to entry, monopolistic positioning, and the strong cost pass-through of many assets make infrastructure less sensitive to the business cycle and positively correlated to inflationary pressures.

The long-term case for infrastructure remains strong. Structural tailwinds including deglobalisation, digitalisation, urbanisation and the energy transition are fuelling demand for both new infrastructure and the modernisation of existing assets. Current investment levels still fall short of what is needed to meet global demand. We believe core/core plus segments offer the most appealing risk/reward profile in the current environment. Investors should prioritise a diversified approach across sectors with a focus on assets that are less GDP-sensitive, which benefit from predictable cashflows and employ moderate leverage.

Infrastructure has displayed lower volatility than equities



Source: FTSE, MSCI, MWM Research, December 2025.

Macquarie macroeconomic forecasts

	Quarterly									
	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26	Dec-26	Mar-27	Jun-27	Sep-27	Dec-27
GDP, QoQ										
US	0.7	0.2	0.8	0.6	0.7	0.7	0.6	0.5	0.5	0.5
China	1.1	1.1	1.3	1.4	1.3	1.0	1.2	1.2	1.1	1.0
Eurozone	0.2	0.3	0.3	0.3	0.3	0.4	0.4	0.4	0.4	0.4
Japan	(0.4)	0.2	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.2
UK	0.1	0.2	0.3	0.3	0.1	0.2	0.3	0.3	0.3	0.3
Canada	0.6	0.0	0.2	0.5	0.6	0.6	0.6	0.5	0.4	0.4
Australia	0.4	0.6	0.7	0.7	0.6	0.6	0.6	0.6	0.5	0.6
New Zealand	0.7	0.5	0.6	0.6	0.6	0.7	0.7	0.7	0.6	0.6
Global (MER)	0.7	0.5	0.7	0.7	0.7	0.7	0.7	0.7	0.7	0.6
Global (PPP)	0.7	0.6	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
GDP, YoY										
US	2.0	1.7	2.7	2.4	2.3	2.8	2.6	2.5	2.3	2.1
China	4.8	4.6	4.8	5.0	5.1	5.0	4.6	4.6	4.5	4.5
Eurozone	1.4	1.2	0.9	1.0	1.1	1.3	1.4	1.5	1.6	1.6
Japan	1.1	0.6	0.6	0.4	1.0	1.0	0.9	0.8	0.8	0.8
UK	1.3	1.2	0.8	0.9	0.9	0.9	0.9	0.9	1.0	1.2
Canada	1.4	0.7	0.4	1.4	1.4	2.0	2.3	2.3	2.1	1.9
Australia	2.1	2.2	2.5	2.4	2.6	2.5	2.4	2.2	2.2	2.3
New Zealand	1.1	1.2	0.8	2.4	2.3	2.5	2.6	2.7	2.7	2.6
Global (MER)	2.7	2.5	2.6	2.6	2.7	2.9	2.9	2.9	2.8	2.7
Global (PPP)	3.2	2.9	3.0	3.0	3.1	3.3	3.3	3.3	3.3	3.2
CPI, YoY										
US (PCE)	2.7	2.8	2.6	2.8	2.8	2.7	2.7	2.7	2.6	2.6
China	(0.5)	0.2	0.3	0.3	0.3	0.2	0.4	0.5	0.5	0.6
Eurozone	2.1	2.1	1.8	2.0	1.8	1.8	1.8	1.8	1.9	1.9
Japan	2.9	2.5	1.7	1.5	1.6	1.4	1.6	1.8	1.8	1.8
UK	3.8	3.6	3.2	2.8	2.6	2.5	2.5	2.5	2.4	2.3
Canada	2.0	2.1	1.8	2.2	2.1	2.0	2.1	2.1	2.2	2.2
Australia	3.2	3.3	3.5	3.6	2.9	3.2	2.8	2.8	2.6	2.6
New Zealand	3.0	2.9	2.4	2.3	2.2	2.3	2.3	2.2	2.1	2.0
Policy Rate										
US (Fed funds rate)	4.13	3.63	3.63	3.63	3.63	3.88	3.88	4.13	4.13	4.13
China (1-yr MLF rate)	1.40	1.40	1.30	1.30	1.20	1.20	1.20	1.20	1.20	1.20
Eurozone (deposit rate)	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00
Japan (policy rate)	0.50	0.75	0.75	0.75	1.00	1.00	1.00	1.00	1.00	1.00
UK (base rate)	4.00	3.75	3.50	3.50	3.25	3.00	3.00	3.00	3.00	3.00
Canada (overnight cash rate)	2.50	2.25	2.25	2.25	2.25	2.50	2.75	3.00	3.00	3.00
Australia (cash rate)	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60	3.60
New Zealand (overnight cash rate)	3.00	2.25	2.25	2.25	2.50	2.75	2.75	3.00	3.00	3.00
10-year yield										
US	4.16	4.10	4.25	4.40	4.60	4.75	4.75	4.65	4.50	4.50
China	1.86	1.81	1.70	1.75	1.65	1.65	1.60	1.60	1.60	1.60
Germany	2.71	2.75	2.85	2.95	3.05	3.15	3.15	3.10	3.00	3.00
Japan	1.65	1.90	2.00	2.05	2.15	2.20	2.20	2.20	2.15	2.15
UK	4.77	4.50	4.50	4.45	4.30	4.10	4.00	3.90	3.80	3.80
Canada	3.18	3.20	3.40	3.50	3.60	3.75	3.75	3.65	3.50	3.50
Australia	4.30	4.65	4.65	4.70	4.75	4.80	4.80	4.75	4.65	4.65
New Zealand	4.19	4.50	4.60	4.65	4.75	4.80	4.80	4.70	4.65	4.60

Source: Macquarie Macro Strategy, December 2025

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This Report was finalised on 8 December 2025.

Recommendation definitions (Macquarie Australia/New Zealand): Outperform – return >10% in excess of benchmark return Neutral – return within 10% of benchmark return Underperform – return >10% below benchmark return.

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