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Chief Investment Office GWM
Investment Research

Position for a broadening rally

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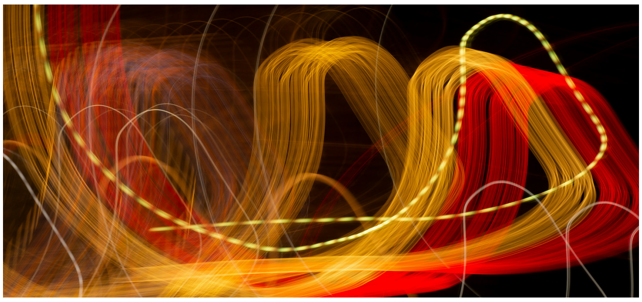
- **Why?** (1) Historical innovation cycles show a performance handover from the enablers of a new technology to those able to generate revenue from it. (2) An improving global growth outlook and a pickup in corporate earnings should drive further equity gains across markets. (3) The push for strategic autonomy globally will create beneficiaries across geographies.
- **Why now?** (1) Markets have responded more positively to the results of companies that are showing progress on monetizing AI. (2) In the US, fiscal expansion, loose financial conditions, and AI productivity gains should lift other sectors that have lagged over the past year. (3) European equities should benefit from fiscal spending, Chinese stocks are likely to be supported by tech advances, while Japan stands to gain from earnings recovery and corporate reforms.



With global equities poised for double-digit gains by 2026, investors should consider broadening their exposure across sectors and regions to capture the rally and manage risk. Source: Unsplash

The US remains the core engine for global equities, and we expect AI to remain a key driver of overall equity performance. We forecast S&P 500 earnings per share to reach USD 310 in 2026—up 12% year over year—and see the index advancing to 7,700 by year-end.

But we also expect the rally to broaden, as historical innovation cycles show a performance handover from the enablers of a new technology to those that are able to generate revenue from it. We believe that the leadership of the AI trade will broaden, from the semiconductor firms in the enabling layer that have led the rally in recent years, toward the companies in the application layer selling AI solutions to consumers and businesses. We also expect fiscal expansion, loose financial conditions, and AI productivity gains to lift other sectors that have lagged over the past year.

Health care

The US health care sector has emerged from a period of policy uncertainty, and we expect improved performance supported by M&A activity and strong demand from aging demographics. We like select companies with exposure to large and growing markets such as obesity, while the sector's less correlated earnings profile could prove valuable if economic growth slows.

Utilities

We also favor US utilities, with the sector benefiting from AI-driven power demand and ongoing digital infrastructure buildout. Electricity demand growth—driven by AI data centers and industrial manufacturing—is accelerating, prompting increased capital investment in power infrastructure and supporting robust earnings growth. With more than half the sector by market cap having significant leverage to these trends, we see a compelling combination of growth and defensive income potential.

Banks

Banks—in the US and globally—are increasingly well-capitalized and profitable, with return on equity rising to 11.5% in 2025 and further gains expected. Supported by favorable net interest margin trends, improving loan growth, and strong capital market activity, we think the sector offers both attractive valuations and potential for shareholder returns. Any impact from the potential one-year cap on credit card interest rates should be temporary and manageable, in our view.

Consumer discretionary
This sector is likely to benefit from an environment of growing wages, tailwinds from the One Big Beautiful Bill Act, and potential policy actions to support lower- and middle-income groups linked to the "affordability" agenda.

Opportunities beyond the US
Beyond the US, we also see opportunities in Europe, Japan, China, and emerging markets.

Europe
After three years of stagnant earnings, profit growth should accelerate to 7% in 2026 and 18% in 2027, driven by recovering goods spending, disciplined cost control, and supportive European Central Bank policy—including the 200bps in rate cuts already delivered. Germany's plan to invest over 20% of GDP in infrastructure and defense strengthens the fiscal outlook and boosts capital investment. Banks are healthier, with rising loan growth, asset repricing, and fee income, while Eurozone equities offer meaningful exposure to power and resources, and longevity. Within Europe, we favor industrials, technology, and utilities, as well as "European Leaders" positioned to benefit from both policy and structural growth.

Japan
The House of Representatives election scheduled for early February could be positive for equity markets if the Liberal Democratic Party secures a majority, boosting the stability of the Takaichi administration. Beyond the election, additional catalysts include a shift to "good" inflation driven by a turnaround in real wages. Further progress in equity market reforms—such as in corporate governance (due around June) and the Topix (October)—should also increase incentives for companies to enhance corporate value.

Quant exposure
Investors can also benefit from including quantitative strategies as part of their equity allocation. The main advantages of quantitative strategies are: (1) diversification, as the main performance drivers are only weakly linked to macro fundamentals, if at all, and (2) their unsentimental nature, which leaves them unaffected by common behavioral biases often displayed by individual investors. Quant strategies can also be viewed as a natural framework to exploit recent advances in machine learning and AI.

Global asset class preferences definitions
The asset class preferences provide high-level guidance to make investment decisions. The preferences reflect the collective judgement of the members of the House View meeting, primarily based on assessments of expected total returns on liquid, commonly known stock indexes, House View scenarios, and analyst convictions over the next 12 months. Note that the tactical asset allocation (TAA) positioning of our different investment strategies may differ from these views due to factors including portfolio construction, concentration, and borrowing constraints.
Most attractive – We consider this asset class to be among the most attractive. Investors should seek opportunities to add exposure.
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Neutral – We do not expect outsized returns or losses. Hold longer-term exposure.
Unattractive – We consider this asset class to be unattractive. Consider alternative opportunities.
Least attractive – We consider this asset class to be among the least attractive. Seek more favorable alternative opportunities.

Appendix

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