2026 MIDYEAR EDITION

# Outlook

## Long-term perspective on markets and economies

CAPITAL GROUP™

# 2026 **Midyear Outlook**

"Despite a challenging geopolitical environment and apprehension about the path of global economic growth, many companies are doing well.

**Rob Lovelace**
Chair of Capital International, Inc

As we reach the midpoint of 2026, a recognizable theme has emerged. In the first few months of the year, stocks have reached a series of new highs in the face of daunting world events. Market volatility – triggered by wars in the Middle East and Ukraine, fluctuating oil prices, elevated inflation, nervous consumers and concerns about a potential AI bubble – has so far failed to derail the upward march of key market indices.

Are investors not focused on world events, or is there something else going on here? To answer that question, we need to look at corporate earnings. Despite a challenging geopolitical environment and apprehension about the path of global economic growth, many companies are doing well. Revenues are rising (in aggregate), profitability is improving, and buybacks are soaring. Stock prices reflect those trends.

For all the talk of market concentration, it's not just the well-known large-cap technology stocks driving the advance. With higher interest rates, banks are generating better profit margins. With innovative drug development, healthcare companies are enjoying rapid sales growth. With increased spending on defence and infrastructure, stocks in Europe, Asia and emerging markets are gaining ground. In fixed income markets, bonds are doing their job protecting against downside risk and helping smooth the ride for investors during periods of heightened market volatility.

In my view, adding up the pluses and minuses around the world, there are enough pluses to support the market's general upward trajectory. The question then comes down to the multiple. What are investors willing to pay for these earnings? There is room for disagreement here, and many smart investors are questioning today's valuations, particularly in the U.S. But at the end of the day, I'd rather see a market that is paying up for solid earnings than a market that is rising without that fundamental underpinning.

As the remainder of the year unfolds, rather than focusing too much on front-page news, we hope you'll explore the equity and fixed income investment themes covered over the next 20 pages. With that, I invite you to read and share our 2026 Midyear Outlook.

# Global growth hinges on war resolution, pace of AI rollout

| Variable | Global growth | U.S. economy | European economy | Canadian economy | Fed policy | Inflation | Currency |
|---|---|---|---|---|---|---|---|
| Consensus | 2.9% | 2.1% | 1.2% | 1.2% | 3.75%-4.0% | 3.5% | USD weaker |
| Capital Strategy Research (CSR) views vs. consensus | In line | Mixed | Above | Slightly below | Below | In line | In line |
| Summary of CSR view | Global growth is slowing but resilient as the U.S. and Iran work toward a resolution to the war in the Middle East. | The economy continues to hold up as strong AI support helps offset high energy costs. The labour market shows signs of stability. | We expect slightly stronger euro-area growth and inflation. The ECB is likely to hike rates in 2026. Look for less fiscal tightening in the U.K. and France. | Encouraging signs are emerging on fiscal and investment fronts, but momentum is weak amid trade uncertainty and a soft labour market. Inflation has risen from commodity shocks, though less than feared; significant BoC tightening unlikely. | CSR views the prospect of rate hikes as less likely than the market may be pricing in. Look for the Fed to move cautiously. | The inflation picture looks stickier beneath the surface as high oil prices, geopolitics and tariffs continue to pressure prices. | The U.S. dollar may face downward pressure as its interest rate advantage relative to other economies continues to narrow. |

Global economic growth is coming under pressure due to the Iran war, rising oil prices and ongoing trade disputes, but one powerful engine is more than making up for it: AI-related investment spending.

The artificial intelligence boom is so massive that even if activity in all other sectors fell to zero, economic growth would remain in positive territory, especially in the United States, says Capital Group economist Darrell Spence.

"I remain on the cautious side when it comes to the outlook for U.S. growth," Spence explains, "but it remains possible that GDP could be significantly higher than expected – in the range of 2.5% or more. That's how much the AI arms race is overshadowing every other area of the economy."

Much, of course, depends on stabilization in the Middle East, mounting inflationary pressures, weakening consumer fundamentals, and whether the AI boom marches on or fizzles out. There is a tug of war between these economic forces, and it could be a while before a clear winner emerges, Spence adds.

Elsewhere, Europe is facing a stagflationary shock before year-end, as higher energy prices weigh on activity, says economist Beth Beckett. "I do expect a much smaller shock than we saw in 2022, thanks in part to stronger manufacturing activity and looser fiscal policy in Germany."

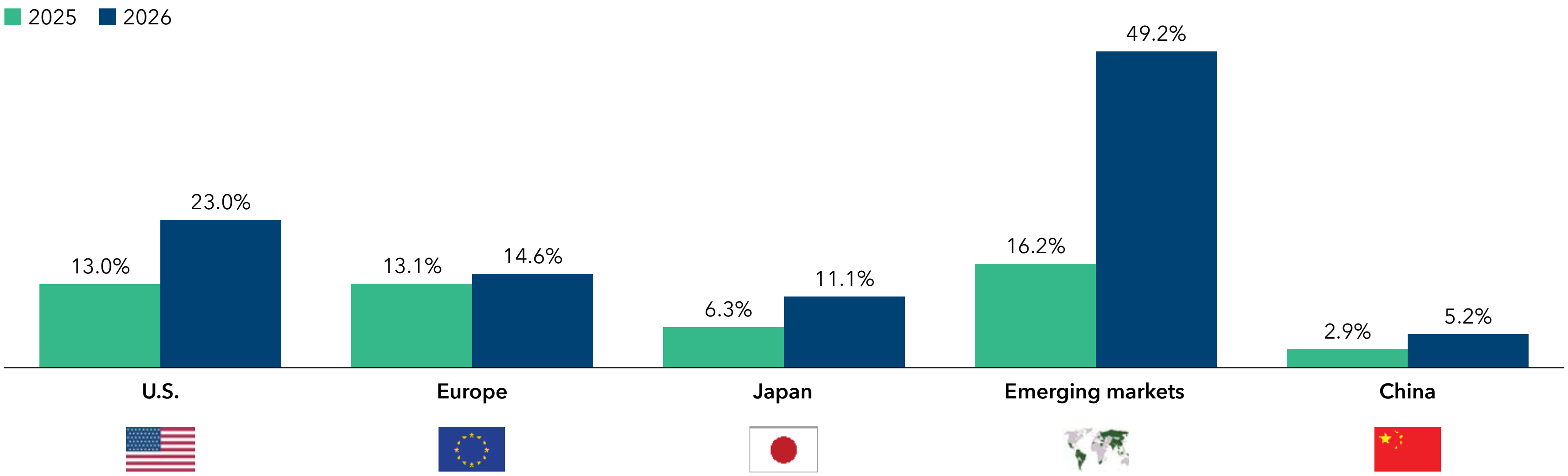
In Asia, look for a weak housing market and slowing exports to weigh on China's economy while Japan also remains sluggish.

Sources: Capital Group, Bloomberg. As of May 31, 2026. Consensus figures are based on mean Bloomberg consensus estimates for U.S. CPI change in 2026 ("U.S. inflation") and 2026 year-over-year GDP growth for the world ("global growth"), the United States ("U.S. economy"), the European Union ("European economy") and Canada ("Canadian economy"). Consensus figures for "Fed policy" are based on the implied U.S. federal funds target range based on futures pricing for December 2026. Consensus "currency" figure is based on DXY futures pricing through December 2026. The views of individual portfolio managers and analysts may differ from Capital Strategy Research (CSR) views. Stagflationary: economic environment categorized by high inflation coinciding with slow economic growth (GDP) and high unemployment. ECB: European Central Bank. BoC: Bank of Canada. DXY: U.S. Dollar Index.

# Robust earnings growth may fuel stock market gains

## Earnings growth is expected to rise across several markets

Estimated annual earnings growth across select global benchmarks




Why does the stock market keep hitting new highs when the world seems to be falling apart? The simple answer: Corporate earnings are on a tear. This is partially explained by the many companies benefiting from massive AI spending, but it's not all about AI.

For instance, in the healthcare sector, Eli Lilly's first-quarter sales rose 56% to US$19.8 billion, fueled by surging demand for weight loss and diabetes drugs. In the energy sector, companies such as ExxonMobil, Shell and TotalEnergies are pumping up their profits as the Iran conflict sends oil prices sharply higher. Meanwhile, Apple reported blockbuster earnings in April, not due to any AI-related news, but because iPhone 17 sales skyrocketed.

Looking forward, consensus earnings estimates are on the rise – particularly in emerging markets where they are expected to grow 49.2% in aggregate this year. That is largely due to the positive impact the AI boom is having on chip-related companies such as Taiwan Semiconductor Manufacturing Company (TSMC), Samsung and SK hynix.

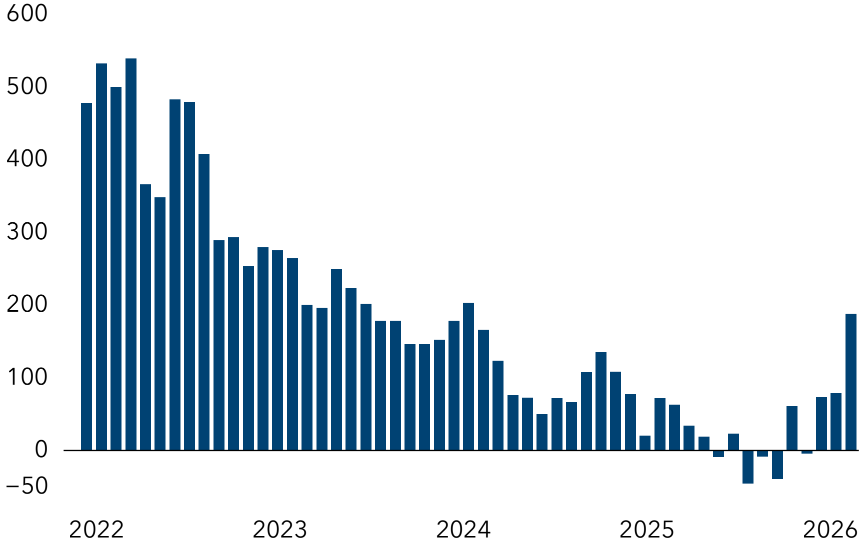
"When I look at the market going forward, the key element is this underpinning of strong corporate earnings," says equity portfolio manager Rob Lovelace. "This growth has been evident for the last three years, and it doesn't look like it's slowing down."

Sources: Capital Group, FactSet, MSCI, S&P Global. Estimated annual earnings growth is represented by the mean industry analyst consensus earnings per share estimates for the year ending December 2026 across the S&P 500 Index (U.S.), the MSCI Europe Index (Europe), the MSCI Japan Index (Japan), the MSCI EM Index (Emerging markets) and the MSCI China Index (China). Earnings growth represented in USD. Estimates are as of May 31, 2026.

# The labour market may guide the Fed's next moves

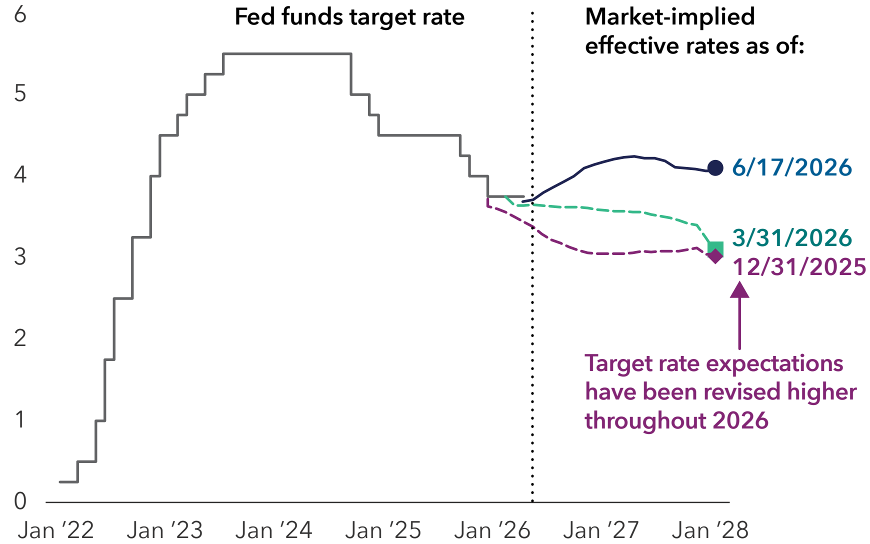
## U.S. labour markets have stabilized after decelerating

Rolling three-month average nonfarm payrolls (thousands)




## The Fed has room to respond

Fed funds actual vs. market implied (%)




Even as war-driven inflation has remained elevated, the job market may hold the key to the U.S. Federal Reserve's policy decisions.

Labour markets are weaker than they were a few years ago but steady overall, says Chitrang Purani, bond manager. "The war is keeping inflation above the Fed's 2% target and is likely to weigh on non-AI business investment as well as consumer demand. That combination increases the risk of a more pronounced slowdown in growth."

Consumer spending has shown resilience, but middle- and low-income households may be more fragile than in the past, given savings have fallen and real wage growth appears to be moderating.

Purani believes policymakers will remain patient. "The labour market has been stable with slower job growth offset by slower labour force expansion – but if this balance were to shift toward a rising unemployment rate, the Fed will likely look past near-term inflation risks."

The composition of the Fed may also affect how it responds. New Fed Chair Kevin Warsh may resist rate increases – leaving the hurdle to hike rates higher than the market is pricing.

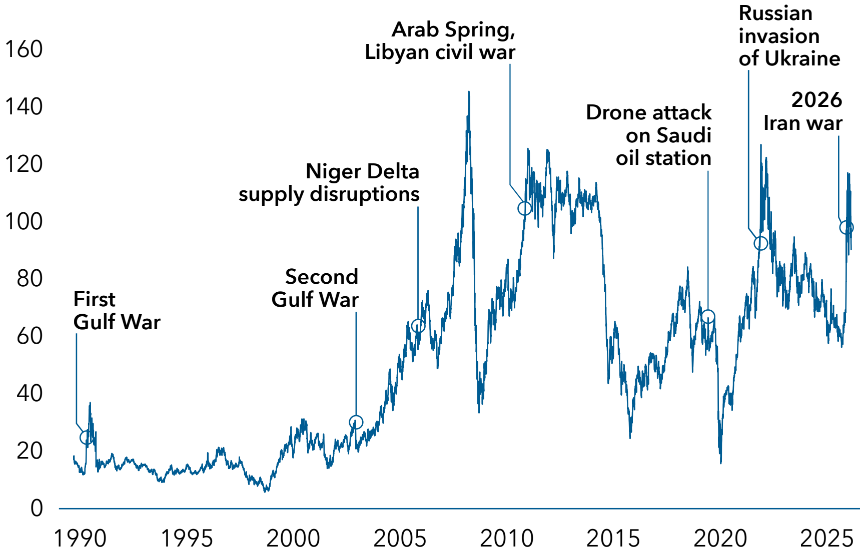
Sources: Capital Group, U.S. Bureau of Labor Statistics. April and May 2026 are preliminary figures and subject to change. Latest data available is May 2026 as of June 5, 2026.

Sources: Capital Group, Bloomberg, U.S. Federal Reserve. Fed funds target rate reflects the upper bound of the Federal Open Markets Committee's (FOMC) target range for overnight lending among U.S. banks. As of June 17, 2026.

# Market sell offs tied to oil supply shocks have been short-lived

## Conflict has often triggered spikes in oil prices

Daily Brent crude price (USD per barrel)



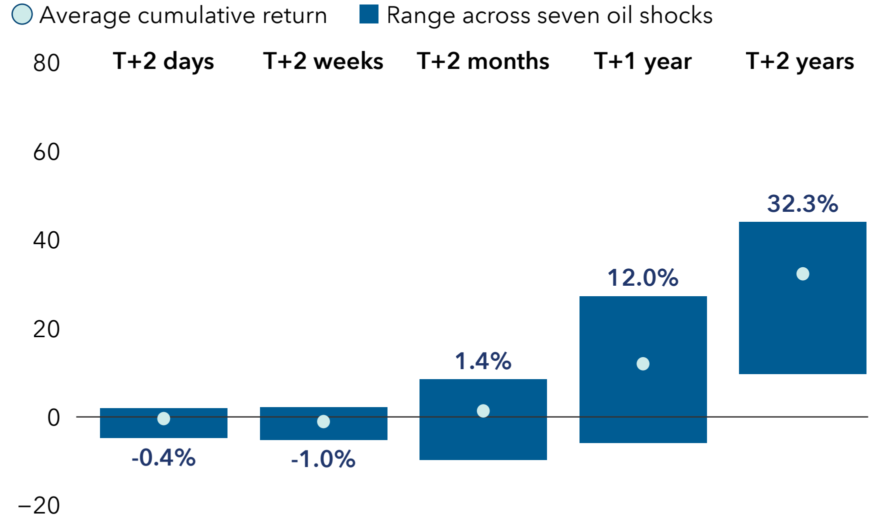

The Iran war is a stark reminder that the world still runs on oil. When supply is threatened, the impact of higher oil prices spreads quickly to businesses, consumers and global markets.

About one-fifth of the world's oil supply moves through the Strait of Hormuz, so any disruption there is almost immediately reflected in fuel prices. Even in the United States, the world's largest oil producer, the price of gasoline at the pump has jumped nearly 42% since the war started.

"There are very real economic risks, and the costs would only compound as the war drags on," says equity portfolio manager Paul Benjamin. "A persistent conflict would trigger weaker equities, a stronger U.S. dollar and widening credit spreads."

## But U.S. stocks have recovered relatively quickly

S&P 500 Index returns following geopolitical-related oil supply disruptions 1990-2024 (%)




Over the past two decades, stock markets have generally bounced back from geopolitical shocks because they haven't resulted in prolonged physical supply outages. Across seven oil supply shocks since the First Gulf War in the 1990s to Russia's invasion of Ukraine in 2022, equities fell on average by 1% two weeks following the disruption, then rose 1.4% a month later, 12% a year later and 32.3% over the next two years.

It's a good reminder that markets are forward-looking and may already be anticipating a resolution to the present crisis.

Sources: Capital Group, Bloomberg. Figures reflect daily settlement prices between January 1, 1990, and May 31, 2026. Event dates are aligned to the nearest observable market price. If an event occurs on a non-trading day, the prior trading day is used as the start date.

Sources: Capital Group, Bloomberg, S&P Global. Geopolitical shocks include: Gulf War (8/1990), Second Gulf War (3/2003), Niger Delta supply disruptions (2/2006), Arab Spring, Libya Civil War (2/2011), Hormuz closure risk, Iran sanctions (12/2011), drone attack on Saudi installations (9/2019), Russian invasion of Ukraine (2/2022). Event dates are aligned to the nearest observable market price ("T"). If a shock occurs on a non-trading day, the prior trading day is used as the start date. Horizon returns are measured using the first available trading day on or after the stated calendar horizon (e.g., "T+2 days"). Figures reflect total returns in USD. As of May 31, 2026. Past results are not predictive of results in future periods.

# Index investors face elevated concentration risk

Investors in index strategies may be exposed to more risk than they realize.

While cyclical growth has been challenged by the Iran war, inflation and uncertainty, artificial intelligence has provided the most compelling secular growth opportunity in today's market.

Enthusiasm for AI has sent shares of chipmakers like Broadcom, Micron Technology and NVIDIA soaring. While other tech giants in AI development – Microsoft, Alphabet, Amazon and Meta – have recorded subpar returns, they remain among the largest weightings in the S&P 500 Index. These conditions have produced market concentration.

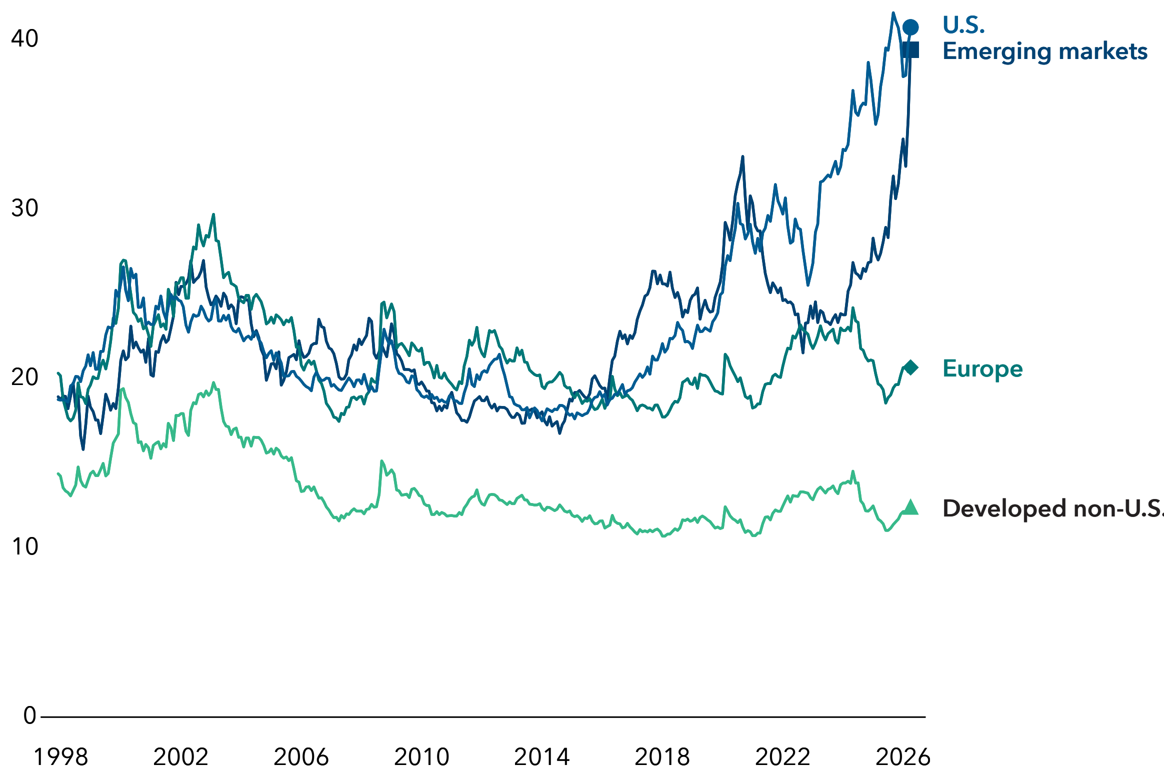
"I'm excited about the incredible advances in AI and the investment opportunities they represent," says Martin Romo, portfolio manager for Capital Group U.S. Equity Fund™ (Canada). "At the same time, I'm uneasy that the largest companies in the United States and Asia, as well as the companies with the strongest returns, are all driven by a single fundamental driver – artificial intelligence."

The question is not whether to invest in these companies, but how much. "It always comes back to balance. Careful stock selection, flexible positioning, and diversification can improve long-term outcomes for investors," Romo adds.

Investors should consider opportunities across sectors such as healthcare, energy and industrials, while also thinking globally rather than on one dynamic region like the U.S.

## U.S. and emerging market stock indices have grown more top-heavy

Percentage of market capitalization in top 10 companies




Sources: Capital Group, FactSet, MSCI, S&P Global. Figures represent the index concentration of the top 10 companies by market capitalization across the S&P 500 Index (U.S.), the MSCI Europe Index (Europe), the MSCI World ex USA Index (Developed non-U.S.) and the MSCI EM Index (Emerging markets). Data shown is monthly, from January 30, 1998, through May 31, 2026.

# What's next for CUSMA?

| CUSMA, high level | |
|---|---|
| | Successor trade agreement to NAFTA effective 2020 |
| | Provides for tariff relief for 98% of Canadian exports to the U.S. |
| | Six-year review period scheduled for July 2026 |
| | Set to expire in 2036 if not extended |

Tom Cooney is an international policy advisor for Capital Group. Here, he presents his outlook for the Canada-United States-Mexico Agreement (CUSMA).

**Q: What's your outlook for CUSMA going into the review period?**

**Tom:** While the CUSMA review could determine whether the agreement is extended for another 16 years, my base case is that it won't be quickly renewed. Instead, we will likely shift into an annual review cycle. Importantly, that doesn't mean disruption as CUSMA remains in place, continuing to provide trade stability and duty-free access for most goods.

**Q: How will the trade framework evolve from here?**

**Tom:** I believe we'll see bilateral agreements layered on top of CUSMA, specifically U.S.–Canada and U.S.–Mexico deals. These will tackle more targeted issues like dairy, lumber and digital trade that are difficult to resolve in a trilateral format.

**Q: Where do these bilateral talks stand?**

**Tom:** U.S.–Mexico discussions are further along and could conclude this year. U.S.–Canada talks have lagged, reflecting ongoing political and trade tensions and Canada's perception of leverage following the recent U.S. Supreme Court decision, which curtailed the use of certain emergency tariff authorities and reshaped the negotiating dynamic.

**Q: What are the key U.S. priorities?**

**Tom:** Expect a push to strengthen Regional Value Content requirements – rules that determine how much of a product must be produced within North America to qualify for duty-free treatment, currently at 75% in key sectors like autos. The U.S. is seeking to raise this North American content requirement above 80%. Further, the U.S. also seeks to ensure that at least 50% of the content of a vehicle built in North America is of U.S. origin. The existing CUSMA pact has no minimum U.S. content requirement, so this would be new. The U.S. also wants to tighten restrictions on Chinese investment in supply chains and minimize taxation and other restrictions on digital trade. Labour enforcement and critical minerals cooperation are also central themes.

**Q: What happens if the agreement isn't renewed at the review?**

**Tom:** It is important to understand that if all three countries don't agree to extend CUSMA at the July 2026 review, the agreement doesn't terminate. Instead, it moves into annual reviews until 2036, giving policymakers time to negotiate changes while keeping the deal in force. The fact that CUSMA would remain in place even if forced into annual reviews is important because it guarantees that about 85%–90% of Canadian exports still enter the U.S. duty free.

**Q: What's the bottom line for markets and businesses?**

**Tom:** CUSMA survives without necessarily being embraced. It provides a stable foundation, while bilateral deals evolve at different speeds and are layered on top of the CUSMA foundation. As the July review proceeds, expect more public brinkmanship and volatility in headlines. But the most likely outcome is continuity with incremental change, not wholesale disruption, despite noise you may hear.

# AI build-out may surpass China's industrial boom

The artificial intelligence phenomenon may be far bigger than you think.

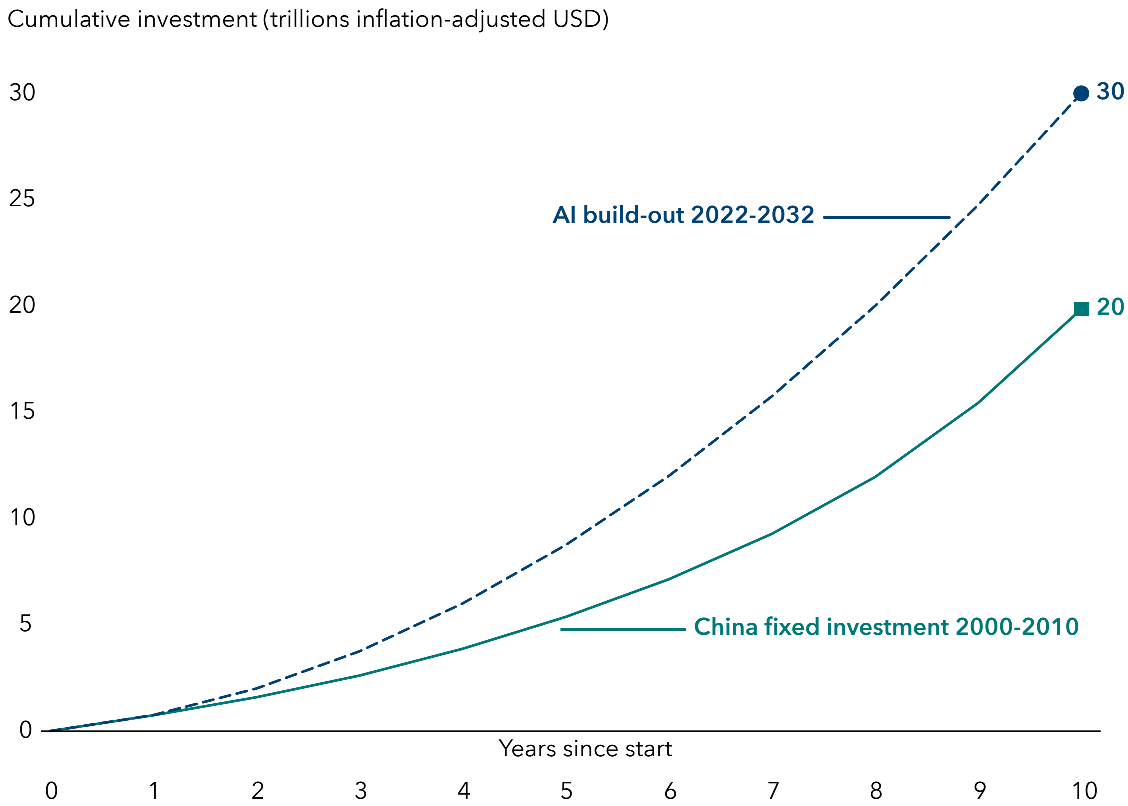
In the race for AI supremacy, tech giants are making capital investments at a scale and speed on track to surpass China's industrial boom of the early 2000s, considered by many to be the largest in modern history.

After joining the World Trade Organization in 2001, China invested about US$20 trillion to industrialize its economy over the following 10 years. "This reshaped global trade, commodities, inflation, labour markets and politics for a generation," explains U.S. economist Jared Franz. Today's AI investment appears to be comparable in size and potential impact.

"The AI debate should not be framed as a tech sector cycle or a question about whether NVIDIA's valuation is justified," Franz says. "The pace of investment and advancement suggests AI may have a lasting effect on GDP growth, power demand, capital allocation, labour markets and asset prices across every sector."

Historic spending by hyperscalers Amazon, Alphabet, Meta, Microsoft and Oracle has translated into soaring demand for the offerings of semiconductor makers NVIDIA and Broadcom, as well as semiconductor foundries like TSMC. "AI is potentially the highest impact technology in a generation and the most significant force in the economy," says equity portfolio manager Mark Casey.

## AI investment is on pace to exceed China's 10-year industrial boom




Sources: Capital Group, Federal Reserve of St. Louis (FRED), Haver Analytics, National Bureau of Statistics of China. Hyperscalers are large-scale cloud service providers that offer computing power and storage to organizations and individuals globally. Values are adjusted for inflation using the U.S. Consumer Price Index (CPI) as of March 2026. AI build-out estimates assume annual spending ramps linearly from $0.5T in 2022 to $5.5T in 2032. Cumulative values are estimated using the trapezoidal method, which assumes linear change between observations and sums the average across intervals. Figures presented are for illustrative scale only. As of May 31, 2026.

# Physical economy stocks are poised for a comeback

We may be living in an AI world – NVIDIA's market capitalization is larger than three entire sectors – but that's no reason for investors to ignore old economy companies.

For starters, the tidal wave of cash being poured into the build-out of data centres is translating into historic revenue opportunities.

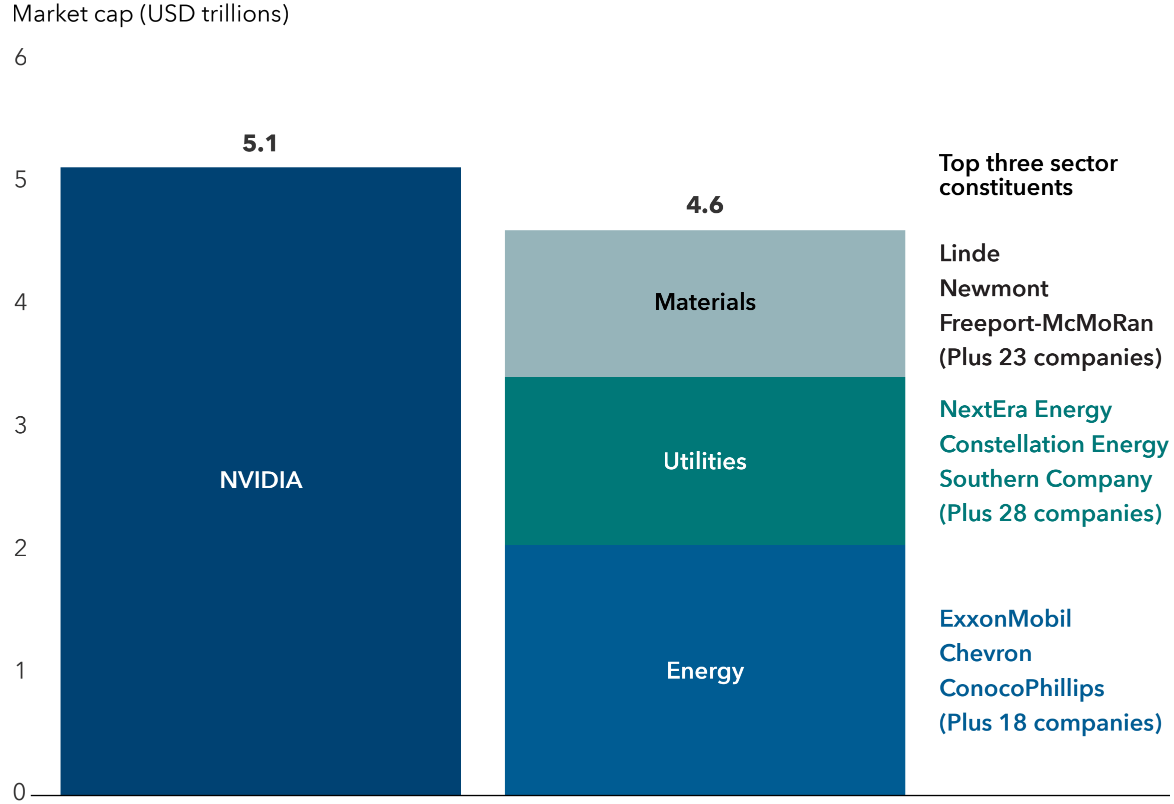
Demand for steel, copper, heavy construction services and power generation equipment has soared. For example, sales in Caterpillar's construction division jumped 38% in the first quarter.

"Pick-and-shovel companies, both the semiconductor supply chain and the infrastructure developers, are where I see the clearest opportunity," says Chris Buchbinder, portfolio manager for Capital Group U.S. Equity Fund™ (Canada). "I expect this cycle to last longer than perhaps the market believes."

Some areas of the market associated with physical goods and services posted strong gains early in the year because of their perceived insulation from AI disruption. "One focus of mine has been companies that I believe are largely immune to AI," Buchbinder says. "Consider, for example, Royal Caribbean. It's unlikely that we're going to have AI replacing cruise ships."

Among industrials, jet engine maker GE Aerospace entered the year with a US$190 billion order backlog.

## NVIDIA is now larger than three market sectors



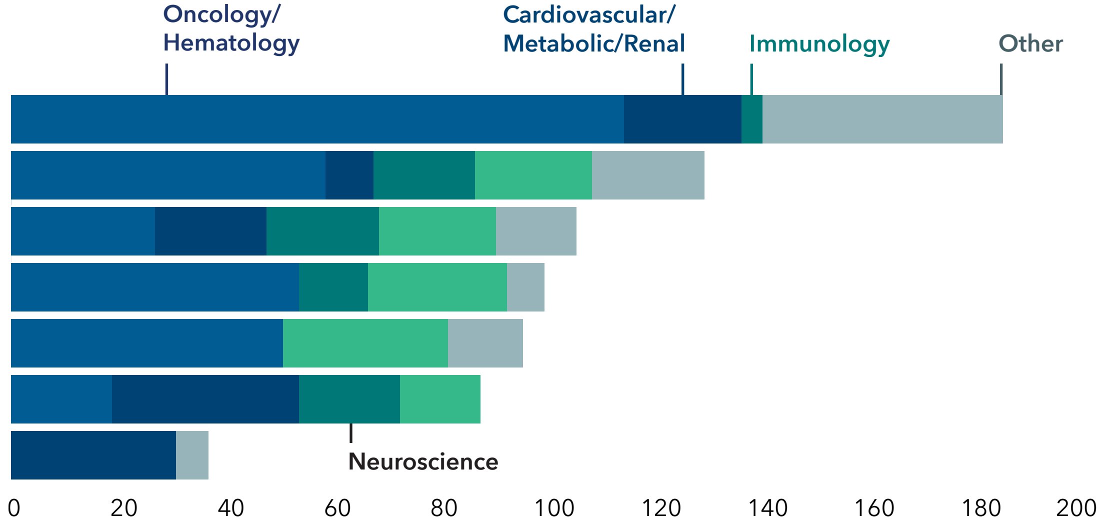

Sources: Capital Group, FactSet, RIMES, S&P Global. As of May 31, 2026. Companies shown are the three largest in their respective sectors within the S&P 500 Index. Caterpillar is the S&P 500 Index industrials sector's largest company by market capitalization.

# Innovation and income: Healthcare's powerful combination

## Robust pipelines are paired with strong cash flow generation

| | Dividend yield (%) | Annualized free cash flow growth 2025-2027(%) |
|---|---|---|
| **AstraZeneca** | 2.7 | 22.3 |
| **Roche** | 3.0 | 8.4 |
| **Novartis** | 2.3 | 6.8 |
| **Johnson & Johnson** | 2.4 | 16.5 |
| **Pfizer** | 6.6 | 3.6 |
| **Eli Lilly** | 0.6 | 61.6 |
| **Novo Nordisk** | 4.7 | 18.0 |

Number of indications in pipeline across top pharma companies




At a time when long-term growth feels harder to find, the seeds of drug discovery are bearing fruit.

Deep pipelines provide pharmaceutical companies with a powerful growth engine and reduce reliance on any single product. Many also generate healthy free cash flow, allowing them to return capital to shareholders through dividends or strengthen pipelines through targeted acquisitions.

AstraZeneca, for example, has a well-established range of oncology franchises. To drive future growth potential, it has assets targeting heart disease, chronic kidney problems and metabolic conditions.

However, much of this potential remains underappreciated by the market.

The same is true of its China business. "China accounts for around 13% of sales," notes equity portfolio manager Noriko Chen. "We're excited by the innovation emerging there. With its scale and deep partnerships, AstraZeneca can fund both its pipeline and a healthy dividend, which may make the business more durable than the market assumes."

"Pharma companies have shown discipline with their cash, investing in growth but not at the expense of income," Noriko adds. "Many focus on progressive dividends, and yields are attractive; Roche and Novo Nordisk for example, both yield more than 3%."

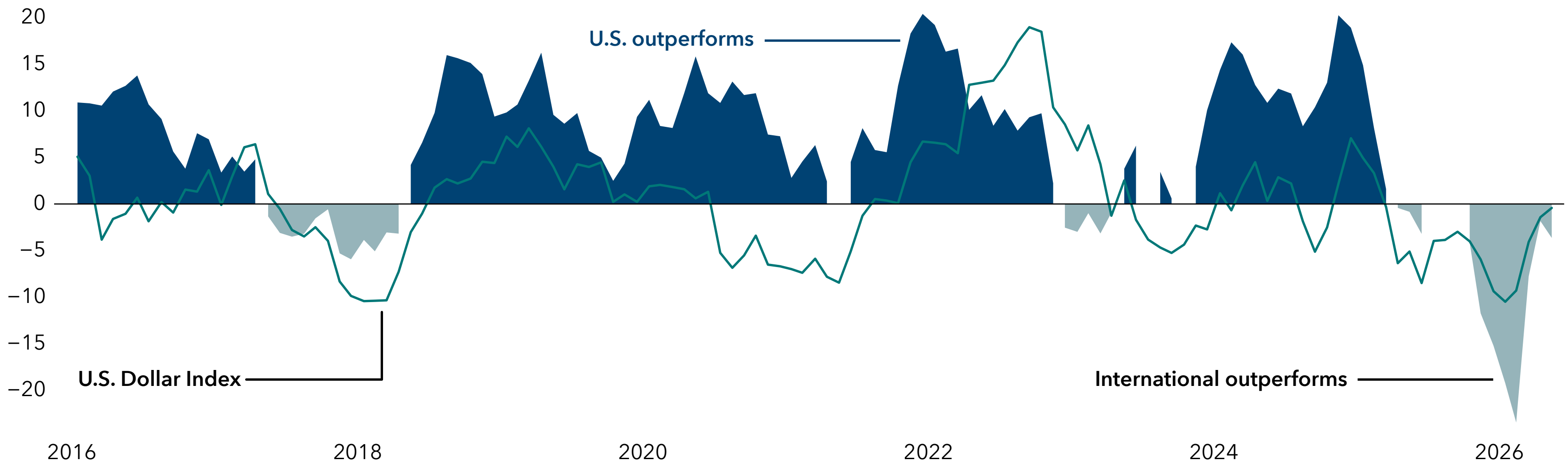
The combination of innovation-led growth and dividend defensiveness can potentially enhance portfolio resilience while still offering compelling upside.

Sources: Capital Group, Bloomberg, MSCI, RIMES, company reports. Dividend yield is represented by the forward 12-month dividend yield based on latest consensus figures and company announcements. Free cash flow growth is annualized based on 2026 and 2027 consensus estimates. Pipeline figures based on data available from individual company webpages and includes drugs in Phase 1 to 3 of clinical trials or in the filing stage. Pharmaceutical companies listed represent seven of the largest constituents of the MSCI All Country World Pharmaceuticals Index. Pipelines up to date as of calendar Q1 2026 financial reporting except for Eli Lilly, which is as of calendar year 2025. As of May 31, 2026.

# Investing outside the U.S. can continue to pay off

## Non-U.S. stocks have led U.S. shares since the start of 2025

Relative return comparison: S&P 500 Index vs. MSCI All Country World ex USA Index rolling one-year returns (%)




After more than a decade in the wilderness, international and emerging markets stocks are enjoying their time in the sun. The powerful rally in non-U.S. markets that started in 2025 has continued, driven by attractive valuations, a weak dollar and strong corporate earnings.

For anyone who thought the 2025 results were a head fake, markets outside the U.S. are demonstrating their resilience in 2026. On a year-to-date basis as of May 31, the MSCI All Country World ex USA Index gained 14%, compared to roughly 11% for the S&P 500 Index.

This shift in investor sentiment has essentially taken us back to the future – recalling a time when U.S. and non-U.S. markets traded leadership positions every few years.

"I see it as a return to the norm, when U.S. and non-U.S. markets would pass the baton back and forth," says Steve Watson, portfolio manager for Capital Group Monthly Income Portfolio™ (Canada). "There are just so many fantastic companies outside the U.S. trading at attractive valuations. I think there's a good chance that the strength we're seeing in international and emerging markets still has room to run."

International diversification doesn't mean compromising on quality either. "Many of these non-U.S. companies – Airbus, ASML, AstraZeneca, Safran and TSMC – are leaders in their industries," Watson adds. "They just happen to be headquartered somewhere else."

Sources: Capital Group, Intercontinental Exchange (ICE), MSCI, S&P Global. U.S. relative returns are represented by the S&P 500 Index; international returns are represented by the MSCI All Country World ex USA Index. Relative returns are measured on a rolling one-year monthly total return basis in USD. As of May 31, 2026. Past results are not predictive of results in future periods.

# Look beyond magnificence to the Emergent Seven

Emerging markets today resemble U.S. markets in one important way: Just as the Magnificent Seven – Alphabet, Amazon, Apple, Tesla, Meta, Microsoft and NVIDIA – lead the S&P 500 Index, seven companies that play a key role in the artificial intelligence revolution have come to dominate emerging markets.

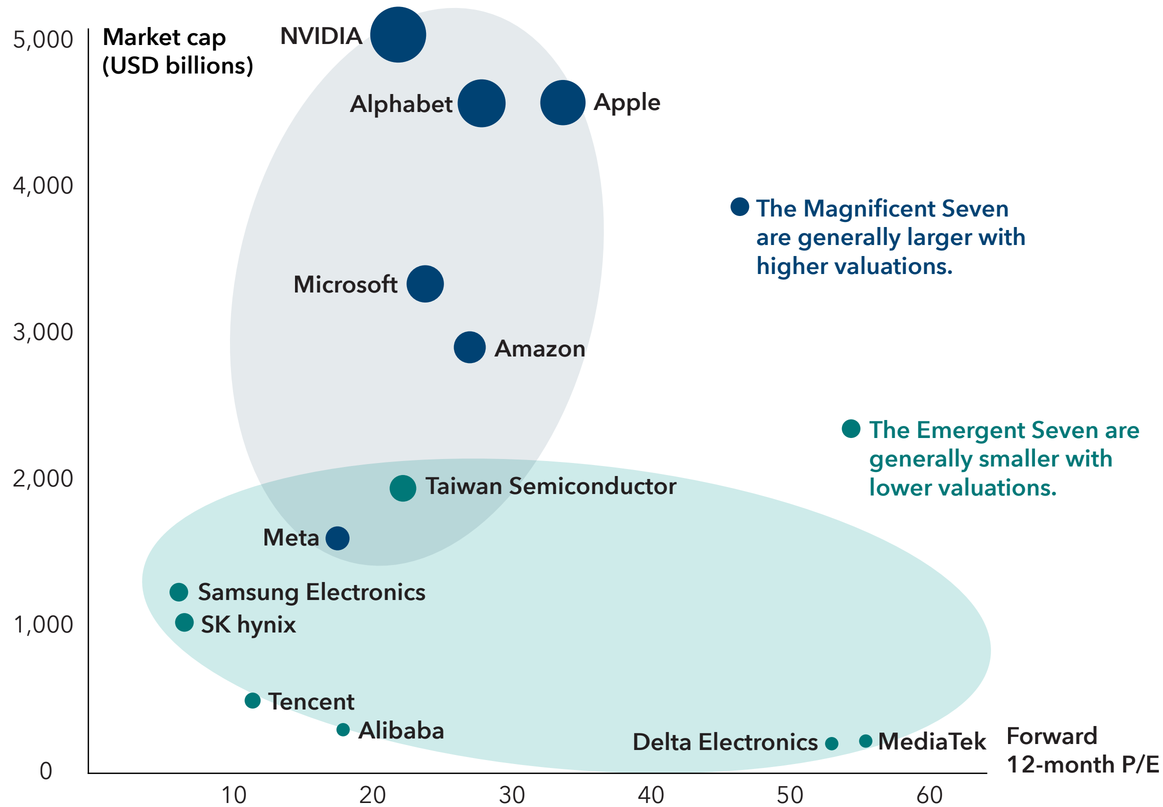
The top seven companies by market capitalization in the MSCI Emerging Markets Index are all tech, making up 36% of the index. At Capital we refer to them as the "Emergent" Seven. They have smaller market capitalizations and lower valuations than many of their U.S. counterparts.

Taiwan Semiconductor, Samsung Electronics and SK hynix are common names, but lesser known companies MediaTek and Delta Electronics are also asserting leadership. Tencent and Alibaba have access to the largest market in the world by operating in China.

Investors focused on U.S. equities may not fully grasp the scope of these opportunities. As equity portfolio manager Brad Freer puts it, "It's becoming clear that TSMC, Samsung and SK hynix are every bit as important as a U.S. semiconductor maker like Micron Technology."

Overall, the Emergent Seven stocks represent a broader shift to higher value sectors within emerging markets. Investors just need to look across the globe for potential long-term compounders on par with U.S. companies.

## As in the U.S., seven tech stocks dominate emerging market returns

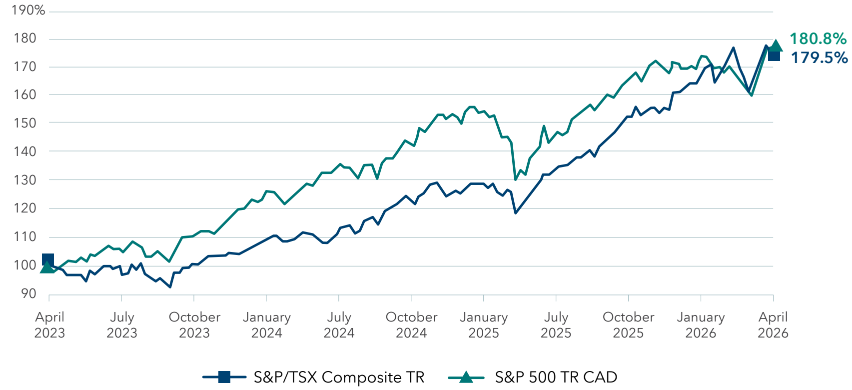



Sources: Capital Group, FactSet, MSCI, RIMES. Emergent Seven represents the seven largest companies in the MSCI Emerging Markets Index: TSMC, Samsung Electronics, SK hynix, Tencent, Alibaba, MediaTek and Delta Electronics. The Magnificent Seven refers to a group of seven dominant U.S.-based technology companies: Alphabet, Amazon, Apple, Meta Platforms, Microsoft, NVIDIA and Tesla. The forward 12-month price-to-earnings (P/E) ratio is calculated by dividing each company's current share price by the mean industry analyst consensus estimate of its earnings per share over the next 12 months. Tesla's forward 12-month P/E of 220x places it outside of the graph axis and is thus excluded above. As of May 31, 2026.

# Can Canada's multi-year rally continue?

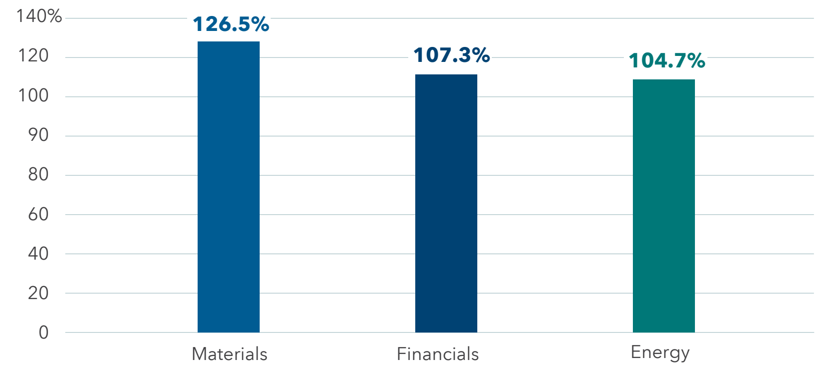
## Canada holding its own

S&P/TSX Composite Index vs. S&P 500 Index, April 30, 2023 – April 30, 2026




## Leaders of the pack

Materials, financials and energy sector results, April 30, 2023 – April 30, 2026




Canadian equities have delivered a quietly impressive run over the past three years, notching double-digit results in 2023, 2024 and 2025, primarily supported by strength in the materials, financials and energy sectors.

"This leadership is not surprising to Canadian investors, with our market heavily tilted toward commodity and banking companies," says equity investment director Kathrin Forrest.

Materials sector companies ranging from base metals to gold producers have been standouts, benefiting from firm commodity pricing and tight supply conditions. Financials have also advanced, reinforcing the Canadian market's resilience even amid economic and trade uncertainty, while the energy sector has helped drive gains and cash flow across Canadian producers.

According to Forrest, parts of this rally may still have room to run. The outlook for the physical economy remains constructive, with energy demand tied to global growth and industrial activity, while supply constraints across commodities continue to support pricing. This backdrop could sustain earnings strength in both energy and materials.

Still, diversification remains key, across sectors as well as geographies. Robust domestic sectors are a solid source of investment opportunity, but in certain adverse conditions they may limit or even hold back portfolios.

"Investors should be mindful of concentration risk, as it creates vulnerability," says Forrest.

A more balanced approach consists of complementing Canadian holdings with companies outside Canada in sectors such as information technology and healthcare, which have been historically underrepresented in the Canadian market. This can help enhance diversification and improve risk-adjusted outcomes by reducing reliance on a narrow set of drivers at home.

"Canada's rally may continue, but the most durable domestic portfolios are likely those that combine some of the country's best-in-class companies with broader global opportunities," says Forrest.

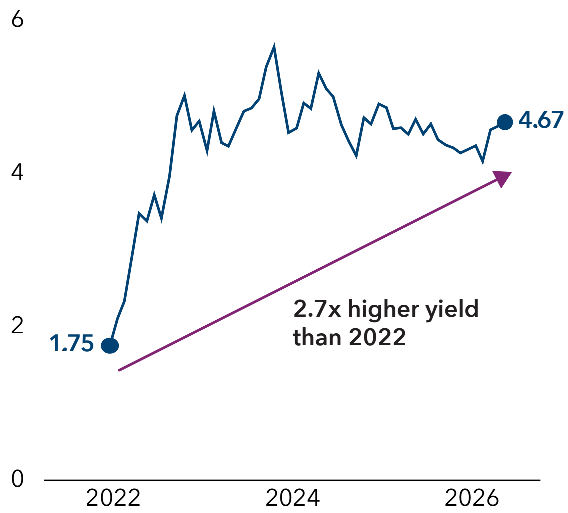
Sources: Capital Group, S&P Global. Returns are in CAD.

Sources: Capital Group, S&P Global. Sector information reflects the S&P/TSX Composite Index. Returns are in CAD.

# Bonds hit a sweet spot for income and diversification

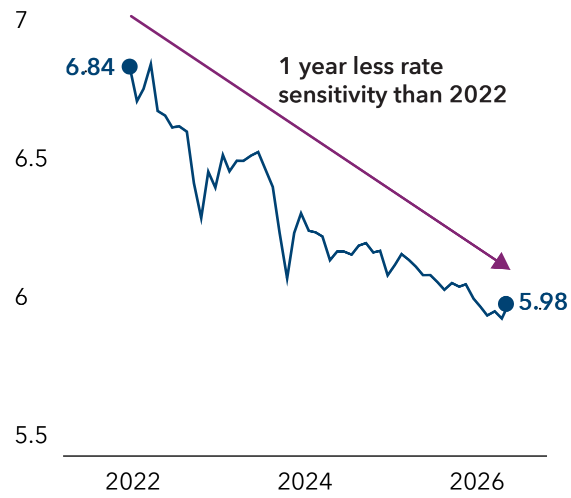
## Higher return potential

Bloomberg U.S. Agg. yield to worst (%)



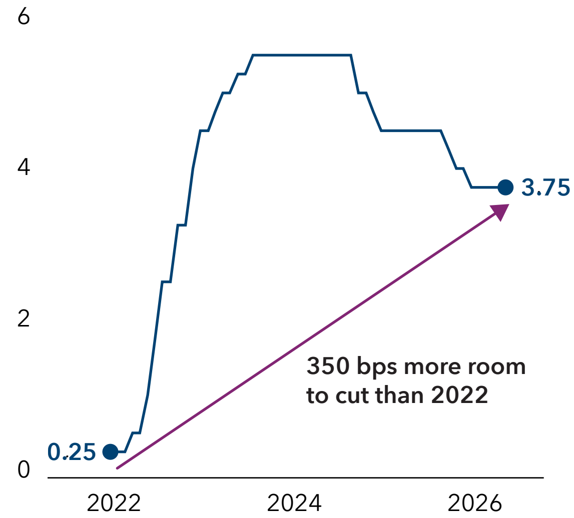

## Less interest rate risk

Bloomberg U.S. Agg. duration (years)




## Stronger diversification from equities

Fed funds rate (%)




Bonds have reclaimed their role in portfolios, offering stronger return potential and better diversification at a time when investors need both.

Starting yields of roughly 4.5% to 5% for the benchmark Bloomberg U.S. Aggregate Bond Index provide a solid baseline return expectation and have historically correlated with subsequent forward returns. That higher income can also help support returns even as the war in Iran adds uncertainty to growth and inflation.

"The U.S. economy may well remain resilient," says bond manager Pramod Atluri. "Either way, investors can be in high-quality bonds without giving up attractive yield. That's a stark contrast to the beginning of 2022, when yields were below 2% and the Fed had limited room to cut."

Higher income potential can also help buffer price volatility. In the unlikely scenario interest rates climb 100 basis points (bps), the income from bonds could largely offset the resulting price decline over a year. Importantly, duration in core indices has declined since 2022, reducing sensitivity to interest rate moves.

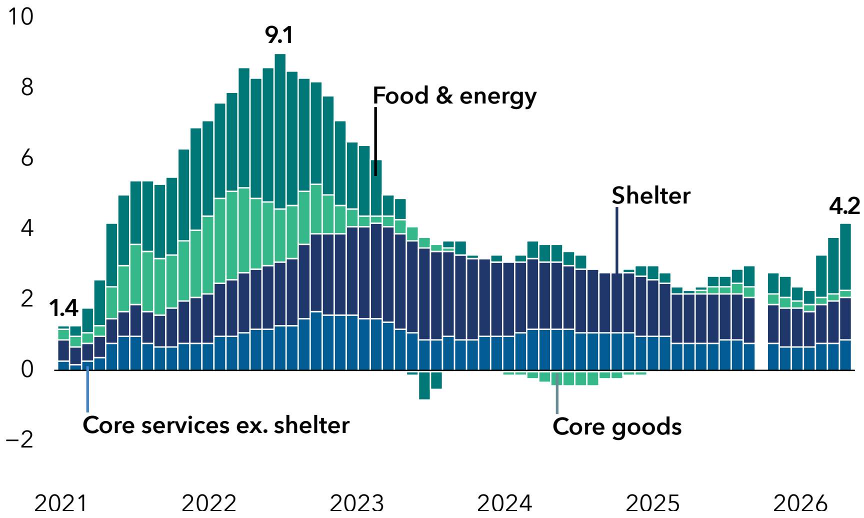
The ability of bonds to provide diversification in a growth shock should be greater, given the Fed could lower interest rates by as much as 350 bps. While some market participants may look to cash as an alternative to reduce volatility in a hypothetical 60/40 portfolio, history suggests the trade-off is particularly unfavourable today. Investors could forgo roughly 1.4% in annual returns, with only a limited reduction in volatility, by allocating 40% to cash over a five-year period.

Sources: Capital Group, Bloomberg. As of May 31, 2026. Duration is a measure of a bond's price sensitivity to interest rate changes, expressed in years. Yield to worst is the lowest possible annualized return an investor could receive, assuming no default and that the bond is called, put or held to maturity. Fed funds target rate reflects upper bound of range. A 60/40 portfolio consists of roughly 60% stocks and 40% bonds. Past results are not predictive of results in future periods.

# U.S. rate fears create an opening to extend duration

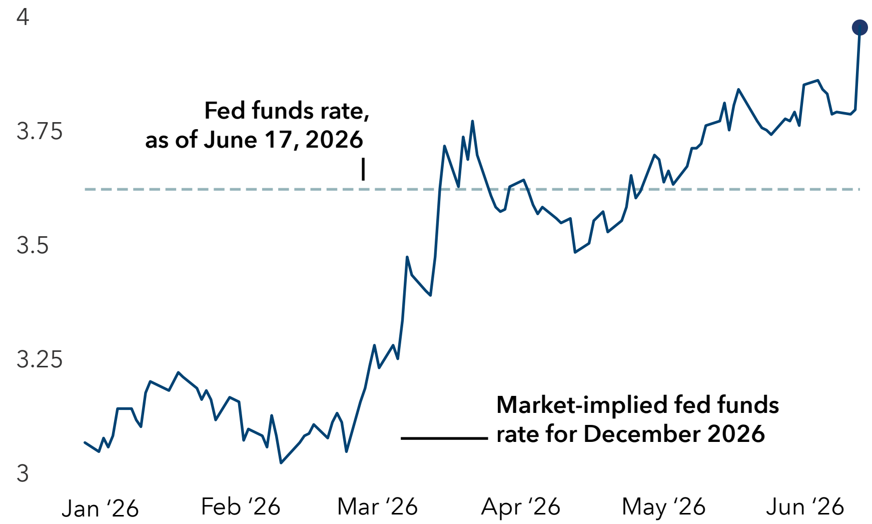
## Core U.S. inflation holds steady amid high energy prices

Year-over-year growth (%)




## Markets expect rate hikes, but we see a patient Fed

Actual fed funds rate vs. market-implied rate (%)




Inflation concerns tied to the Iran war have pushed yields upward, creating room for a reversal if pressures ease or growth risks build.

While headline inflation figures may tick higher, core inflation has remained steady, contained by reduced consumer savings and tepid wage growth. Muted money supply and credit growth also point to less underlying momentum, reducing the likelihood of a sustained inflation cycle. This should allow the Fed to prioritize the employment side of its mandate.

A Fed that remains on pause is more likely than an interest rate hike over the next several quarters, according to portfolio manager Ritchie Tuazon.

"When the market gets nervous about hikes, that's usually a favourable time to extend duration," he adds. Owning duration, which is usually measured in years, can benefit a portfolio by capturing price appreciation from falling rates. The position also serves as a potential hedge against further economic softening.

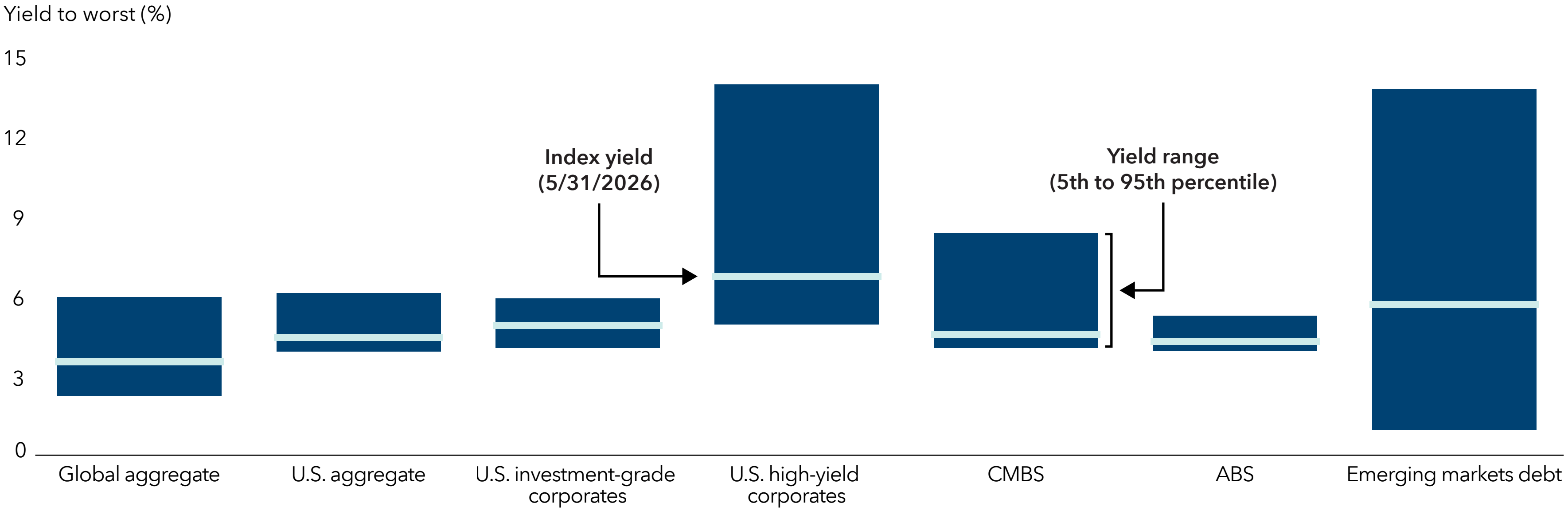
Longer term forces such as artificial intelligence may also support lower rates across a range of outcomes. Strong productivity gains could help dampen inflation, while potential disruption to labour markets or risk sentiment could accelerate the need for a Fed response.

Sources: Capital Group, Bloomberg, Bureau of Labour Statistics. Data shown is U.S. CPI for all items. October 2025 CPI data is unavailable due to the U.S. government shutdown. Latest data available is May 2026 as of June 10, 2026.

Sources: Capital Group, Bloomberg. As of June 17, 2026. The federal funds rate shown is the midpoint of the upper and lower bounds of the Federal Reserve's target range for the federal funds rate. Market-implied federal funds rates are derived from federal funds futures pricing and reflect market expectations. These expectations are subject to change and may differ from actual Federal Reserve decisions.

# Credit opportunities remain despite narrow spreads

## Key credit sectors offer attractive yield




A resilient U.S. economy, strong corporate balance sheets and attractive yields should support most credit sectors, though tight valuations reinforce the case for a flexible, multi-sector approach to income.

Companies have generally operated conservatively amid high interest rates and rolling concerns about an economic slowdown, most recently tied to the Iran war, says Damien McCann, portfolio manager for Capital Group Multi-Sector Income Fund™ (Canada) and Capital Group Multi-Sector Income Select ETF™ (Canada). "A sustained rise in oil prices may dampen growth, but resilient consumer spending and significant investments in AI infrastructure should help keep U.S. economic growth positive."

Credit spreads reflect a broadly favourable environment and the higher quality of today's high-yield market. "I am still finding plenty of good investments across the broad credit market," adds McCann. "Moreover, we remain in a period of elevated yields relative to history, which is a strong setup for income seeking investors."

Differing yields and spreads present opportunities across and within investment-grade corporate bonds (BBB/Baa and above), high-yield bonds, emerging market debt and securitized credit such as commercial mortgage-backed securities (CMBS) and asset-backed securities (ABS). That dispersion stems from varying fundamentals and sensitivity to economic conditions. A diversified approach can help provide steady income potential and relative stability, while targeted investments in bonds offering incremental yield, including certain AI-related debt issuance, could help enhance returns.

Sources: Capital Group, Bloomberg, J.P. Morgan. As of May 31, 2026. Global aggregate is the Bloomberg Global Aggregate Bond Index. U.S. investment-grade corporates is the Bloomberg U.S. Corporate Investment Grade Index. U.S. high-yield corporates is the Bloomberg Corporate High Yield 2% Issuer Capped Index. CMBS is the Bloomberg CMBS: Erisa Eligible Index. ABS is the Bloomberg ABS Index. Local currency emerging markets debt is the J.P. Morgan GBI-EM Global Diversified Index. Past results are not predictive of results in future periods.

# Canada's bond market is evolving, but the gap remains

Canada's investment-grade bond market is taking small steps to close the gap with the U.S., helped by growing demand among large U.S. issuers for Canadian dollar funding. AT&T, Verizon and Alphabet are some of the high-profile U.S.-based companies with new issuances over the past year, while Amazon's record-setting $14 billion maple bond deal in June ranks as the largest such issuance on record.

"This is a much-needed, welcome development for the Canadian bond market, which is smaller and less liquid with fewer issuers and less sector diversity than the U.S.," says fixed income investment director Naoum Tabet.

This shift to the Canadian market is not occurring in isolation, Tabet says. The U.K., eurozone and Switzerland are just some of the other regions that have seen a sharp rise in U.S. bond issuance.

Canada has, however, emerged as a beneficiary of this trend, with a key consideration: Canadian investment-grade yields are hovering around 4%, generally lower than comparable funding levels in other developed markets, with the U.S. at about 5.1%. As a result, foreign issuers can achieve attractive all-in borrowing costs while accessing a stable investor base.

"The influx of high-quality U.S. issuers is great news," says Tabet, "but it's worth remembering that the Canadian bond market remains more limited in scale and depth relative to the U.S."

## Head to head

Investment-grade bond markets as of May 31, 2026

| | Canada | U.S. |
|---|---|---|
| **Size** | $305 billion | $7.5 trillion |
| **Issuers** | 132 | 915 |
| **Yield average** | 4.0% | 5.1% |

Sources: Capital Group, MSCI, Bloomberg. Canadian bond markets represented by the MSCI CAD Investment Grade Corporate Bond Index. U.S. bond market represented by the Bloomberg U.S. Corporate Investment Grade Index. Dollar values in CAD.

**Commissions, trailing commissions, management fees and expenses all may be associated with investments in investment funds. Please read the prospectus before investing. Investment funds are not guaranteed or covered by the Canada Deposit Insurance Corporation or by any other government deposit insurer. For investment funds other than money market funds, their values change frequently. For money market funds, there can be no assurances that the fund will be able to maintain its net asset value per security at a constant amount or that the full amount of your investment in the fund will be returned to you. Past performance may not be repeated**

Investing outside North America involves risks, such as currency fluctuations, periods of illiquidity and price volatility. These risks may be heightened in connection with investments in developing countries.

Bond ratings, which typically range from AAA/Aaa (highest) to D (lowest), are assigned by credit rating agencies such as Standard & Poor's, Moody's and/or Fitch, as an indication of an issuer's creditworthiness.

GDP (gross domestic product) measures the monetary value of final goods and services produced in a country in a given period. It counts all the output generated within the borders of a country.

Market indices are unmanaged and, therefore, have no expenses. Investors cannot invest directly in an index.

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

**Bloomberg U.S. Aggregate Bond Index** represents the U.S. investment-grade, fixed-rate bond market. **Bloomberg Global Aggregate Bond Index** represents the global investment-grade, fixed-rate bond market. **Bloomberg U.S. Corporate Investment Grade Index** represents the universe of investment-grade, publicly issued U.S. corporate and specified foreign debentures and secured notes that meet the specific maturity, liquidity and quality requirements. **Bloomberg U.S. Corporate High Yield 2% Issuer Capped Index** covers the universe of fixed-rate, non-investment grade debt. The index limits the maximum exposure of any one issuer to 2%. **Bloomberg U.S. Asset-Backed Securities Index** is a broad-based flagship benchmark that measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. **Bloomberg CMBS (Commercial Mortgage-Backed Securities): Erisa Eligible Index** measures the market of U.S. agency and U.S. non-agency conduit and fusion CMBS deals with a minimum current deal size of US$300mn.

**JP Morgan Government Bond Index – Emerging Markets (GBI-EM) Global Diversified** covers the universe of regularly traded, liquid fixed-rate, domestic currency emerging market government bonds to which international investors can gain exposure.

**MSCI All Country World ex USA Index** is designed to measure equity market results in the global developed and emerging markets, excluding the United States. **MSCI China Index** 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 Emerging Markets (EM) Index** captures large- and mid-cap representation across 24 emerging markets (EM) countries. **MSCI Europe Index** captures large- and mid-cap representation across Developed Market (DM) countries in Europe. **MSCI Japan Index** captures the large- and mid-cap sections of the Japanese market. **MSCI World ex USA Index** is designed to measure equity market results of developed markets. The index consists of more than 20 developed market country indices, excluding the United States. **MSCI All Country World Pharmaceuticals Index** is composed of large- and mid-cap stocks across 23 Developed Market countries that are classified in the pharmaceuticals industry group according to the Global Industry Classification Standard (GICS®). **MSCI CAD Investment Grade Corporate Bond Index** measures the performance of Canadian dollar-denominated investment-grade corporate bonds.

**S&P 500 Index** tracks the stocks of around 500 primarily large-cap, U.S.-based companies. **S&P/TSX Composite Index** is the headline index for the Canadian equity market.

**U.S. Dollar Index** is a measure of the value of the U.S. dollar relative to the value of a basket of currencies of the majority of the U.S.'s most significant trading partners.



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# 2026 **Midyear Outlook**

## Equity themes / Fixed income themes

| | Equity themes | | | Fixed income themes | |
|---|---|---|---|---|---|
| Themes | Dynamic and structural growth | Defend with dividends | Diversify with international | Diversify for ballast | Dynamic approach to income |
| | **AI build-out may surpass China's industrial boom** | **Leading drugmakers offer a powerful combination of income and innovation** | **Investing outside North America can continue to pay off** | **Bonds are providing income again, with higher return potential** | **Don't let tight credit spreads distract from opportunity** |
| Mutual funds | **Capital Group U.S. Equity Fund™ (Canada)**<br>A – CIF 847; F – CIF 827<br>**Capital Group Global Equity Fund™ (Canada)**<br>A – CIF 843; F – CIF 823 | **Capital Group Capital Income Builder™ (Canada)**<br>A – CIF 143; F – CIF 123;<br>AH – CIF 8243; FH – CIF 8223 | **Capital Group International Equity Fund™ (Canada)**<br>A – CIF 846; F – CIF 826 | **Capital Group Canadian Core Plus Fixed Income Fund™ (Canada)**<br>A – CIF 841; F – CIF 821<br>**Capital Group World Bond Fund™ (Canada)**<br>A – CIF 140; F – CIF 120;<br>AH – CIF 8240; FH – CIF 8220 | **Capital Group Multi-Sector Income Fund™ (Canada)**<br>A – CIF 544; F – CIF 524;<br>A(US$) – CIF 7244;<br>F(US$) – CIF 7224 |
| Exchange-traded funds (ETFs) | **Capital Group Global Equity Select ETF™ (Canada)**<br>CAPG | | **Capital Group International Equity Select ETF™ (Canada)**<br>CAPI | **Capital Group World Bond Select ETF™ (Canada)**<br>CAPW | **Capital Group Multi-Sector Income Select ETF™ (Canada)**<br>CAPM |
| Other mutual funds for a broad investment range | **Capital Group Canadian Focused Equity Fund™ (Canada)**<br>**Capital Group Emerging Markets Total Opportunities Fund™ (Canada)**<br>**Capital Group Global Balanced Fund™ (Canada)**<br>**Capital Group Monthly Income Portfolio™ (Canada)**<br>**Capital Group Canadian Money Market Fund™ (Canada)** | | | | |

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