Capital Markets

January 2026

Canada Edition - Canadian Dollars

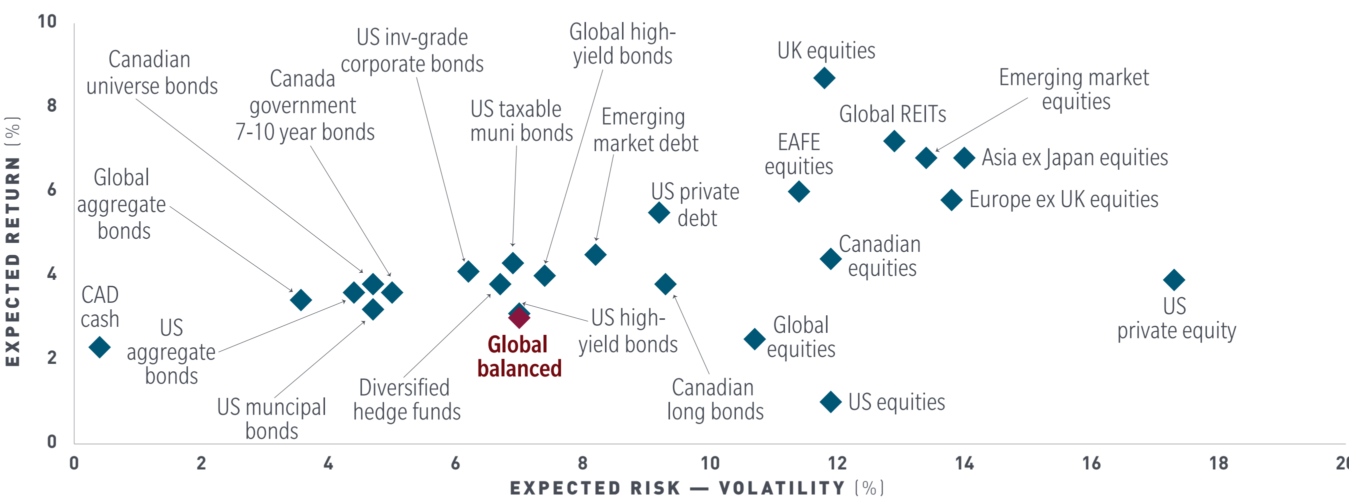
MFS Long-Term Capital Market Expectations

Executive Summary

MFS® is pleased to present the January 2026 edition of *Long-Term Capital Market Expectations*, offering its proprietary outlook on return and risk across a variety of asset classes and regions. Our 10-year nominal total return expectation for global equities is 2.5%, down from July's forecast of 3.0%. Despite significant volatility in the spring, most major asset classes posted positive returns in 2025, with stocks, bonds and precious metals all posting strong gains. In 2025, global equity markets posted their third consecutive year of strong gains, rising 16.5%. Despite tariff-related concerns, in a shift from prior years, developed international and emerging markets outperformed US equities handily with the MSCI AC World ex-US index posing a 26.1% total return, the first calendar year of outperformance since 2022. In the US, large caps continued to lead, but small and mid-caps were not far behind, another departure from recent years when performance dispersions across market capitalizations were significant with large cap growth leading the way.

Given the multitude of macro risks and policy events that markets needed to digest in 2025, it seems implausible that equities performed so well, but this is a stark reminder of how important it is to remain focused on fundamentals. In the US, the creation of the Department of Government Efficiency (DOGE) upended multiple government agencies to slash costs. Shortly thereafter, the US ignited the largest trade war in decades. Towards the end of the year, political grandstanding resulted in a 43-day government shutdown, the longest in US history. Inflation remained elevated and the labor picture weakened as companies slowed hiring amid economic uncertainty, but consumer spending remained resilient despite weakening consumer confidence. In addition, corporate fundamentals and earnings remained strong, and the fourth quarter is expected to be the 10th consecutive quarter of positive earnings growth for the S&P 500 index. From its tariff-related depths in early April through end of the year, the S&P 500 was up more than 30%.

Exhibit 1: MFS Long Term Market Expectations



Global balanced portfolio is 60% global equity, 40% global fixed income. Expected Risk-Volatility is represented by standard deviation.

A global balanced portfolio is expected to provide a nominal total return of 3.0% with a volatility of 7.0%.

US GDP accelerated in the second half of the year to more than 4% in the third quarter, following a weak first quarter when tariff-induced front loading weighed on net exports and consumer confidence plunged. Manufacturing activity faded throughout the year, defying expectations of an industrial renaissance, but services remained strong, keeping overall economic activity in expansionary territory. The tariff-driven panic that started in the first quarter faded throughout the year as trade deals were reached and carve-outs were announced. The Congressional Budget Office estimates that the effective tariff rate for goods now stands at approximately 16.5%, well above the 2024 level of 2.5%, but far below what was initially feared. An estimated $200 billion in tariff revenue was collected in 2025, with that figure expected to rise in 2026. While the net effect of tariff collections will allow a narrowing of the budget deficit, the US Supreme Court has yet to decide on the legality of the use of the acts under which the tariffs were implemented. Should the court rule against the administration's use of the International Emergency Economic Powers Act (IEEPA), the government could be forced to alter their methods of imposing tariffs. While there has been modest tariff pass-through to consumers and margins have been impacted in some industries, at the aggregate level, tariffs have largely been absorbed across value chains with minimal disruptions to the broader economy or corporate health.

Outside the US, the European economy continued to hold up well, with pockets of growth bolstering regional economies. Ongoing fiscal stimulus, including increased infrastructure spending, could provide support for the European economy, as countries such as Germany and Sweden increase defense, infrastructure and related spending. In addition, there is cautious optimism over a potential peace deal between Ukraine and Russia and the associated peace dividend that that could bring, although negotiations have been slow going. Ukraine will require significant reconstruction efforts given the damage that it has sustained over the past near four years of war.

The Fed's Rock and a Hard Place

Starting in September of 2024, the US Federal Reserve had been on a clear rate-cutting path as it sought to bring rates closer to its estimated neutral rate — the rate at which economic growth and inflation are optimal for a healthy economy. However, current data around its dual mandate of stable prices and full employment are pointing in different directions, increasingly wedging the Fed between a rock and a hard place. The labor market, which has been in solid shape for the past several years with low unemployment, steady job creation and rising wages, is starting to show some cracks. It's unclear what is behind the weakening, whether the implementation of artificial intelligence, uncertainty around tariffs, or other factors, but US job growth has slowed to a crawl. At the same time, inflation remains well above the Fed's 2% target, as it has for the last four years. While inflation began to decline following the rate hikes of 2021 and 2022, it became stuck in the high 2% level, where it remains today.

While too-high inflation may suggest keeping rates higher, a weakening labor market argues for rate cuts. As a result, Fed officials have become more conflicted regarding the near-term outlook for monetary policy. There were three dissents at the December FOMC meeting, with two votes to hold rates steady and one voting for a 50, rather than 25, basis-point cut (the vote of Trump-appointed Fed Governor Miran). Rate cuts could be more difficult to come by in 2026 if inflation remains sticky and economic growth remains strong, despite a weaker labor market. Muddying the waters further, the government shutdown of late 2025 resulted in the delay, cancellation or estimation of several critical economic data sets.

PORTFOLIO CONSIDERATIONS FOR 2026

All Ships Rise

With many equity markets up double-digit percentages, it's fair to say that 2025 was a standout year for global equity markets. As mentioned, the MSCI ACWI index was up 16.5% and US equities were up 12.3%, while global ex-US developed markets rose 25.0% and emerging markets rose 27.2% — a remarkable, broad-based showing. 2025 marked the first calendar year since 2022 where global ex-US outperformed US. This is significant because 2022 was a deeply negative year where the value orientation of global ex-US equities helped cushion the downside. In contrast, 2025 was a strong positive return year and global ex-US equities still outperformed, with areas such as the European banking sector outperforming US tech, a clear sign of global equity markets broadening. Following that theme, US value equities closed the performance gap with US growth, and small cap closed the gap with large cap, suggesting a broadening within US equities, a dynamic that many have been eagerly awaiting. Given the underlying fundamental momentum, this could be the beginning of a more significant rotation.

Growing Into Valuations

Global equities continue to trade at modestly elevated multiples, with a forward price-to-earnings ratio of 18x compared to a 10-year average of 16.4x. However, corporate earnings growth remains solid, as does the overall global economic and earnings outlook. Breaking down the regions leads to a more mixed view. US equities remain near the upper end of their historical valuation and margin ranges, leading to a modest 10-year return expectation of 1.0%. In contrast, developed ex-US and emerging markets equities are projected to deliver higher returns of 6.0% and 6.8%, respectively. This disparity is driven by cheaper valuations and expectations for profit margin expansion outside the US. Global equity profit margins, currently at 12%, are elevated compared to their 10-year average of 10.3%, but much of that is driven by the US. As a result, future returns are expected to be driven primarily by sales growth and dividends rather than further margin expansion or valuation increases.

Not So Artificial

Three years after the launch of ChatGPT, AI has permeated the psyche of both investors and the public with myriad potential applications for both consumers and businesses. We see this as the next phase of technological innovation that follows the internet revolution of the 1990s, the mobile boom of the mid 2000s and cloud computing growth of the 2010s. One notable aspect of AI is the expected high level of physical investment required to scale it effectively. Data centers, semiconductors, heating and cooling equipment, and the energy needed to power each of these is immense. It will take time before the full scope of investment is entirely understood, but the widespread adoption of AI could continue to fuel economies, the US in particular, for years to come. What is less clear are the return on investment that the implementation of AI will provide and the ongoing capital expenditures required for ongoing operations. It is still early days for AI and like many significant technological advances, we may yet not be able to imagine the resulting use cases.

In 2025, fixed income had a strong year as well, with US aggregate bonds returning 5.4% — its best performance since 2020. While we expect more muted returns going forward, the benefits of income and diversification were strong contributors for multi-asset investors. MFS long-term nominal total return expectation over the next 10 years is 3.4% for global aggregate bonds and 3.6% for US aggregate bonds.

Fixed Income: Tight Spreads, but Solid Yields

Despite concerns around tight credit spreads, credit markets continue to offer compelling total yields. Our fixed income expectations are built on key building blocks such as starting yield, yield curve roll-down, price change and credit spreads. Because starting yield has such a strong correlation to long-term total returns, starting yield is expected to be the key return driver. Investment grade spreads are running around 80 basis points, while high-yield spreads are around 270 basis points, both toward the tighter end of historical ranges. Overall, corporate balance sheets and earnings growth remain solid and overall credit quality has risen in recent years, lessening concerns of a near-term spread-widening event. Naturally there will always be idiosyncratic and industry-specific concerns, which is why we believe that despite placid credit conditions, security selection remains paramount.

Region	Asset class	Long-term return expectation[5]	Long-term risk expectation
	Inflation	3.0%	0.9%
Equities (Unhedged nominal total return)			
US	US equities	1.0%	11.9%
	US large-cap equities	0.7%	11.5%
	US small-cap equities	3.9%	16.5%
NON-US REGIONAL	Asia ex Japan equities	6.8%	14.0%
	EAFE equities	6.0%	11.4%
	Emerging market equities	6.8%	13.4%
	Europe ex UK equities	5.8%	13.8%
	Global equities	2.5%	10.7%
COUNTRY	Australian equities	5.3%	16.1%
	Canadian equities	4.4%	11.9%
	Japanese equities	4.0%	12.1%
	UK equities	8.7%	11.8%
Fixed Income (Hedged nominal total return)			
Canada	CA cash	2.3%	0.4%
	Canada government 7-10	3.6%	5.0%
	Canada universe bonds	3.8%	4.7%
US	US aggregate bonds	3.6%	4.4%
	US high-yield bonds	3.1%	7.0%
	US inv-grade corporate bonds	4.1%	6.2%
	US Muni Bonds	3.2%	4.7%
	US Taxable Muni Bonds	4.3%	6.9%
GLOBAL	Emerging market debt	4.5%	8.2%
	Global aggregate bonds	3.4%	3.6%
	Global high-yield bonds	4.0%	7.4%
	Global investment-grade bonds	3.9%	5.2%
NON-US REGIONAL	European aggregate bonds	3.4%	4.5%
	European high-yield bonds	3.6%	7.3%
	European investment-grade bonds	3.6%	4.8%
Alternatives (Unhedged nominal return)			
NON-LIQUID	US private equity[6]	3.9%	17.3%
	US direct real estate	4.6%	9.4%
	Diversified hedge funds	3.8%	6.7%
	US private debt	5.5%	9.2%
LIQUID	Global REITs	7.2%	12.9%
	Global infrastructure	5.5%	9.6%
	Commodities	5.3%	11.6%

[5] Geometric return.

[6] As of January 2022, the methodology for US private equity risk has changed from using a fund of funds proxy to using listed private equity companies.

Appendix

The MFS Long-Term Capital Markets Expectations (LTCME) for 2026 includes return and risk expectations for equity, fixed income and alternative asset classes across country, regional and global markets. The focus of these expectations is to provide a strategic, long-term, forward-looking view of various global markets. We use a proprietary top-down approach by employing quantitative, country-based models as the foundation for our expectations. Elements of these models are influenced by views from our fundamental equity and fixed income teams.

Our expectations are developed across 26 countries comprising 18 developed countries and 8 emerging market countries.

Equity expectations

MFS equity market expectations are displayed in unhedged, nominal total return and are developed using a building-blocks approach.

Elements of market history and mean reversion are incorporated into our models. Reversion speed and target levels are calibrated based on our analysis of historical data and forward looking expectations. Any return figure should be viewed as the mid-point in that range of outcomes.

Fixed income expectations

MFS fixed income market expectations are displayed in nominal total return, hedged to the investor's home currency. As with our equity model, our fixed income model employs a building blocks approach. And, again like the equity model, the fixed income model derives its reversion speed and target level parameters from careful historical research as well as forward-looking expectations.

In our forecast, we focus on the returns from carry, yield change, roll-down and credit loss (where appropriate). Using this framework, we develop expectations across a range of sovereign, global credit and regional credit markets, while being careful to tune our models in accordance with the unique attributes of the various fixed income markets.

Alternative expectations

Due to the unique characteristics and varying drivers of return in alternatives, we vary our approach for each category. Our equity and fixed income capital market expectations serve as key variables in our alternatives models.

Currency Expectations

We use a mean reversion approach to calculate currency expectations. Currency expectations represent the nominal excess returns which are nominal total return less domestic carry. Nominal total return is calculated as nominal prices change plus foreign currency carry. Domestic and foreign currency carry comes from the MFS Long -Term Capital Expectations cash forecasting model. Nominal price change is real price change plus inflation differential between currencies.

GLOSSARY

Equity Expectations Building Blocks

Our equity building blocks are measured at the index level for each country.

Price/Earnings (P/E) ratio Price to earnings ratio is the trailing 12-month P/E ratio as measured by the index level divided by the trailing 12-month earnings for the constituent members of that index. We use P/E ratio as a measure of valuation. Our very-long-term reversion target for P/E ratios is 18.

Profit margins Profit margins are a measure of profitability and are measured in percentage terms. Our margin expectations are assumed to revert toward a target based on long term history.

Sales growth Sales growth is a measure of increase or decrease in real sales per share. To estimate this, we incorporate elements of economic theory and examine current levels relative to trends.

Dividends Dividends are measured in percentage terms, and we assume that a country's dividend payout ratio, over our forecast horizon, will be equal to its trailing 5-year average.

Fixed Income Expectations Building Blocks

Our fixed income building blocks are measured at the index level for each country.

Nominal yield Nominal yield is the observed yield at the index level. Nominal yields consist of both a real yield component and an inflation expectation component.

Real yield Real current yield is a nominal yield less the trailing 5-year annualized change in the Consumer Price Index.

Carry The carry return is calculated as the average of the current nominal yield and the expected nominal yield.

Yield change return The yield change return is calculated as the expected yield change multiplied by the current duration and then annualized.

Inflation Inflation is measured as a 5-year trailing change in the US Consumer Price Index. We then assume that inflation reverts towards a global equilibrium value.

Roll down The roll down return expectations are based on index duration as well as localized curve steepness for the maturity being forecast.

Regional credit markets For regional credit markets, we take a building-blocks approach incorporating duration-matched risk-free return, spread return and loss return.

Duration-matched risk-free return This represents the estimated return of a sovereign bond portfolio with the same duration and nationality as the regional credit in question.

Spread return The spread return is measured by the differential between the yield in the index and the yield of the sovereign bonds for that country. This is the return that can be earned for taking on credit risk.

Credit losses Credit losses are determined based on historical rates of default losses and credit quality migration that are reflective of the index being forecast.

Global credit Because of the complexities of multiple durations and multiple loss provisions across several countries, we take the current yield of the index, assume a constant roll down and subtract any loss return expectations based on expected default rates.

US Treasury Inflation-Protected Securities For TIPS, we forecast a future real yield based on the same mean reverting assumptions we use for other sovereign indices. We then calculate a real carry return, a real yield change return, and a real roll-down return in the same manner with which we calculated nominal versions of these returns for sovereign indices. We then add back inflation expectations to produce a nominal return.

US cash Our estimate of future cash returns reflects the sum of expected real cash rates and expected inflation, both of which are based on mean reversion.

Alternatives Expectations Building Blocks

Real estate For global real estate investment trusts (REITs), we rely upon current dividend yield based on the fact that REITs pay out a considerable percentage of their funds from operations in the form of dividends.

For US direct real estate (RE), we capture the historical relationship between REITs and direct RE by unsmoothing direct RE returns and then estimating beta.

Private equity Our private equity approach starts with our capital markets expectations for global developed markets and then makes adjustments based on the higher levels of risk associated with private equity.

Global infrastructure Our global infrastructure expectations are calculated based off of the relationship between listed global infrastructure and real estate.

Hedge funds We would note that hedge fund investments are pools of capital invested at the discretion of the manager, and as such, risk and return are highly dependent on skill and timing. In addition, within the hedge fund universe, there is a divergent range of asset classes, strategies and implementation approaches. We take a diversified hedge fund portfolio approach where we assume an investment across multiple hedge fund types. To calculate hedge fund expectations, we use a regression based approach to estimate relationships between certain hedge fund styles and public markets. For hedge fund styles that do not appear to hold relationships to public markets, we use steady state expectations plus cash. Expectations for each hedge fund style are allocated to create a diversified hedge fund portfolio.

Commodities We develop our commodities expectations to represent broad exposure to the commodities market through a fully collateralized commodity position. Three primary building blocks — collateral return, spot return and roll return — are estimated and then added to determine our long-term commodities expectation.

Risk and correlations Our risk and correlation expectations are derived largely from historical observed risk and correlation patterns. Risk, as measured by standard deviation, and correlations across broad asset classes tend to be relatively stable over long periods of time. However, over shorter periods of time or during periods of market disruption, this stability can quickly break down. We use the 15-year historical standard deviation and correlations of proxy indices where available. Where a 15-year history is not available, we use the longest available history and make adjustments based on historical patterns and relationships to other asset classes.

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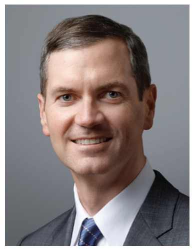

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