# Investment Outlook 1q26

December 2025

FUTURE PLANNING

- **Selectivity matters**
- **Debt affordability remains in focus**
- **A return to spheres of influence**


## Key points

1. Equity valuations are stretched in some part of the market, but concentration risk is a choice, not an obligation.

2. Debt affordability remains in focus - productivity growth is a key variable.

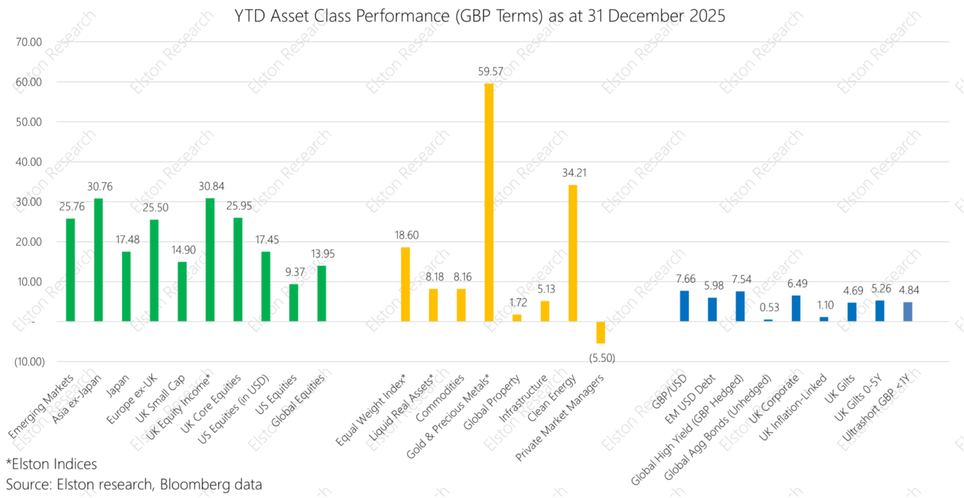
3. Geopolitical risk remains elevated as the world returns to "spheres of influence."

## Equities delivered another strong year recovering from the US tariff shock

## Top Line

Equities have recovered strongly from the tariff shock earlier in the year. Dollar weakness vs Sterling has weighed on the relative performance of US equities; however, this was a step-change and there are concerns for Sterling too. Gold has continued to perform very strongly on the "debasement trade" and Central Bank buying. Within Bonds, Emerging Markets are in better shape than Developed Markets, in our view.

Fig.1. YTD Asset Class Returns




*Elston Indices

Source: Elston research, Bloomberg data

## Selectivity is key

Valuations (as measured by the Price to Earnings Ratio (PER) - the valuation placed on a company's or market's earnings stream) are stretched in some parts of the market, particularly the Technology sector (and not in a bubble yet). But US/Tech concentration risk in world equities is a choice not an obligation. Selectivity is key: by pairing traditional equity exposure with more attractively valued, lower beta (defensive) parts of the equity market.

## Concentration risk is a choice not an obligations

Fig.2. Equity market valuations by region, sector and factor

| REGIONAL EQUITIES | PER | PER+1Y |
|---|---|---|
| Global Equity | 22.98 | 21.92 |
| World (DM) Equity | 24.11 | 23.12 |
| EM Equity | 17.34 | 16.09 |
| US Equity | 27.57 | 25.88 |
| UK Equity Core | 15.05 | 14.85 |
| UK Equity All | 15.48 | 14.83 |
| UK Equity Mid Cap | 21.30 | 14.31 |
| UK Equity Small Cap | 18.74 | 14.32 |
| Europe ex-UK Equity | 17.82 | 17.75 |
| Asia ex-Japan Equity | 18.62 | 17.23 |
| Japan Equity | 18.69 | 18.57 |

| EQUITY INCOME | PER | PER+1Y |
|---|---|---|
| Global Equity Income | 14.07 | 13.10 |
| US Equity Income | 19.26 | 19.07 |
| UK Equity Income | 14.75 | 13.75 |
| Europe Equity Income | 19.18 | 19.04 |
| Asia Equity Income | 13.61 | 13.35 |
| EM Equity Income | 10.16 | 9.72 |

Source: Elston research as at 31st December 2025

| FACTOR EQUITIES | PER | PER+1Y |
|---|---|---|
| World Equity Min Vol | 18.89 | 19.47 |
| World Equity Quality Factor | 27.16 | 25.45 |
| World Equity Value Factor | 17.63 | 17.65 |
| World Equity Momentum Factor | 24.08 | 24.64 |
| World Equity Size Factor | 20.79 | 20.06 |

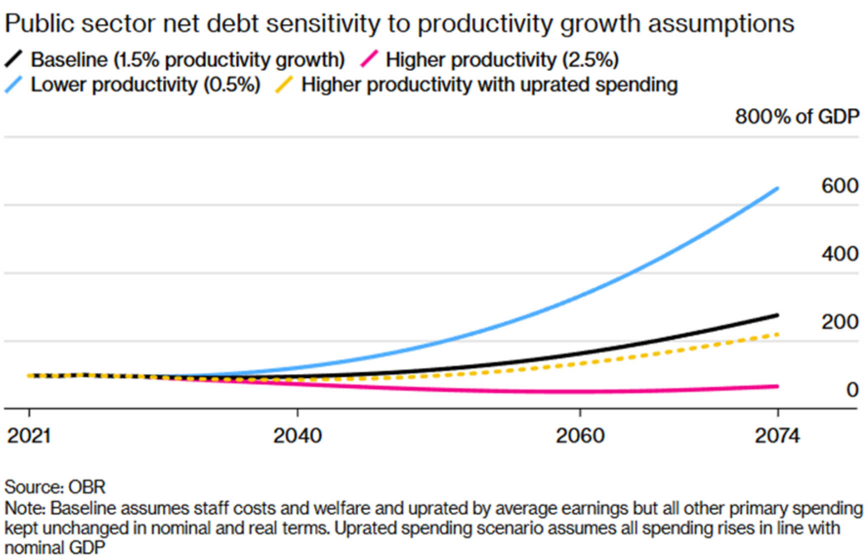
| SECTOR EQUITIES | PER | PER+1Y |
|---|---|---|
| Consumer Discretionary | 29.82 | 27.20 |
| Consumer Staples | 20.18 | 20.42 |
| Energy | 15.92 | 15.26 |
| Financials | 15.83 | 15.51 |
| Health Care | 20.71 | 19.77 |
| Industrials | 26.47 | 25.74 |
| Materials | 22.02 | 21.39 |
| Real Estate | N/A | |
| Technology | 40.45 | 36.20 |
| Communication Services | 23.67 | 22.74 |
| Utilities | 17.38 | 18.22 |

UK Debt/GDP ratio is on an unaffordable trajectory, unless productivity growth comes to the rescue

## Debt affordability remains in focus

Concerns remain on affordability (the UK Government's ability to fund longer-dated debt). But higher productivity growth, lower inflation and lower interest rates could create more "headroom" for the Chancellor. Productivity growth is a small assumption with a big impact – productivity growing at 0.5%, 1.5% or 2.5% makes a material impact in long-term debt affordability. We expect the Treasury to issue more shorter-dated bonds.

Fig.3. Boosting productivity is key to keeping Debt/GDP under control




Source: Bloomberg.com

Geopolitical risk remains elevated as the US, China and Russia vie for spheres of influence.

## A return to spheres of influence

We are moving from an era of great power competition, to contest, wit the desire to avoid proxy conflict. A return to great power diplomacy, realpolitik and spheres of influence is envisaged by the US's new National Security Strategy. This is the stated intention and actions will continue to follow policy. A review of the recent US National Security Strategy reflects the current US administration's thinking is summarised below.

**Americas:** a "Trump corollary" to the Monroe doctrine means American primacy in the Western Hemisphere and cultivating alliances and economic ties to keep other powers out
**UK/Europe:** US and European position on Ukraine have reversed under the Biden and Trump administrations, which is a challenge for the UK which typically prefers to be aligned with the US. The current US administration is also critical of the European liberal establishment.
**Russia/Ukraine:** a potential pathway to peace in Ukraine would likely take some geopolitical uncertainty out of the system and reduce the level of risk that is currently priced into markets. This could involve painful compromises.
**China:** the US focus is on China's economic, technological (AI) and military influence and ensuring it is contained.

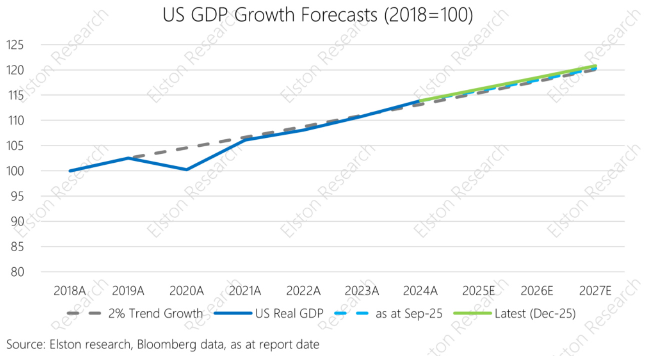
Whilst the strategy is a high-level document, this will continue to inform foreign and military policy in the geopolitical context.

## Outlook

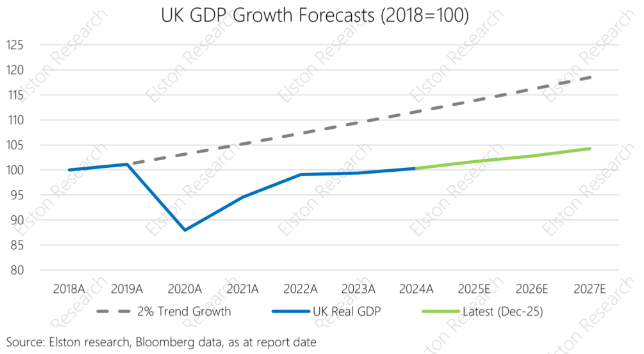
For our Outlook, we consider three key macro factors which are key drivers to markets: Growth, Inflation and Interest Rates.

## Growth

In the US, the 2025E and 2026E growth estimates have both been revised moderately higher to 1.99% and 2.00%, up from 1.76% and 1.80% in September. The 2027E growth projection remains unchanged at 2.00%. Stronger investment in AI, government spending and expected Fed rate cuts have been driving the upward revisions.

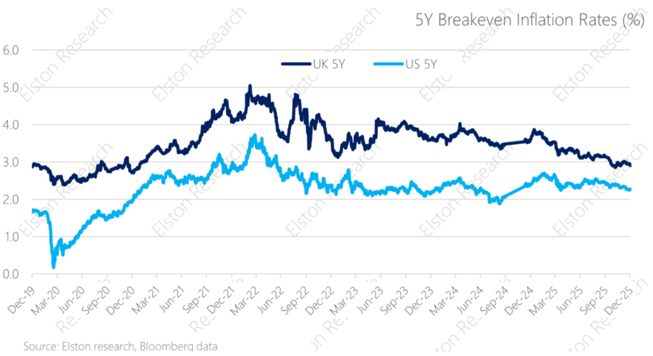



In the UK, the forecast for GDP growth in 2025E has been adjusted upwards to 1.40% over the last quarter compared to 1.30% in September. The upward revision is mainly due to temporary front-loading of property transactions and exports ahead of stamp duty changes and new import tariffs in early 2025. However, the 2026E projection has been lowered from 1.15% to 1.10%. The growth forecast of 2027E has been downgraded from 1.50% to 1.40%. The OBR expects UK to grow more slowly over medium term due to falling productivity growth.




## Inflation

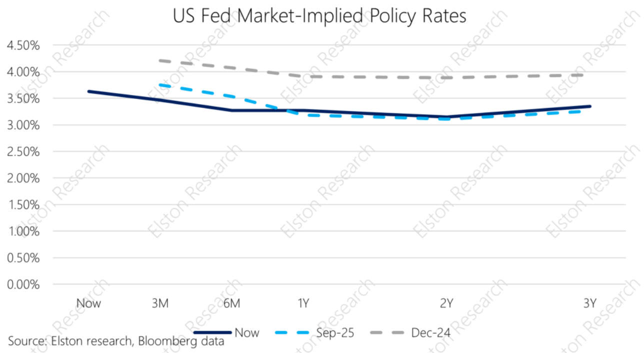
Inflation expectations has moved moderated for both US and UK. US 5Y Break-even Inflation Rates ("BEIRs"), a market-implied expected inflation rate, were 2.27% end Dec-25, vs 2.45% end Sep-25. UK 5Y BEIRs decreased to 2.91% end Dec-25, vs 3.15% end Sep-25.




## Interest Rates

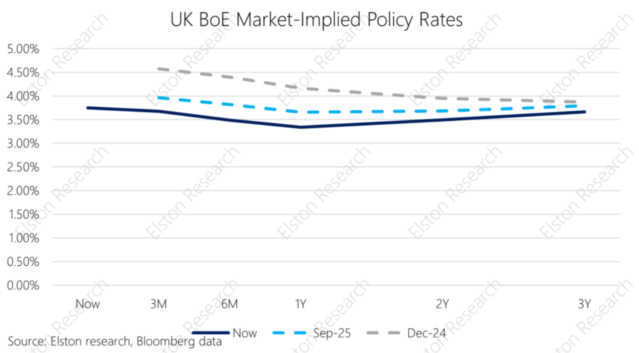
The Federal Funds rate target range currently stands at 3.50%-3.75%, following 25bps cut in both October and December, with both decisions including significant divergence within the committee. Policymakers differed on the pace and scale of easing amid heightened uncertainty around inflation and a cooling labour market. Chair Powell characterised the easing cycle as a prudent response to evolving risks and noted in December that policy now sits broadly around estimates of neutral, signalling a more cautious approach to further adjustments.

US Policy Rate expectations



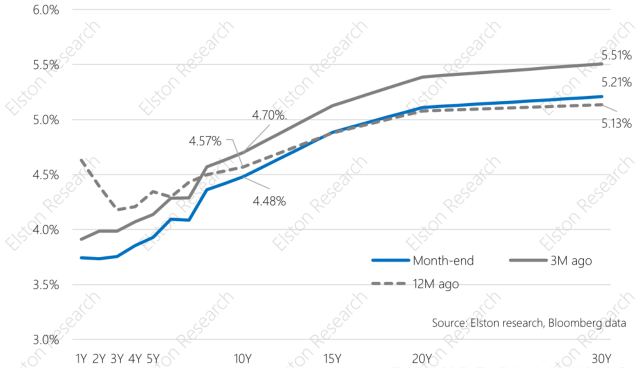

The BoE delivered a 25bps cut in December and is expected to cut 1-2 times more in 2026 depending on growth outlook. The decision was narrowly passed by a 5-4 MPC vote, with four members voted to keep rates unchanged at 4%, highlighting continued divergence within the committee.

UK policy rate expectations




The UK "yield curve" (gilt yields across each maturity) has continued to normalise (now 1 as well as 2 year yields are lower than 10 year yields) and has experienced an downward shift over the past three months. Benchmark 10 year yields decreased to 4.48% end Dec-25 compared to 4.70% 3 months ago and decreased from 4.70% 12 months ago.

UK Yield Curve



## Bottom Line

Stronger US economic and earnings growth has supported US (in local terms) and global equity markets. Valuation expansion of other non-US equity markets has led to strong performance as global investors sought out diversification. Moderating UK inflation is positive for the gilts market, but concerns remain for long-term affordability. Gold & Precious Metals performed strongly in the year owing to downward pressure on currencies and bonds as well as concerns around geopolitical risks.

## What does this mean for portfolios?

Whilst portfolios we recommend have clear long-run strategic investments, adapting portfolios to align to changing market and economic conditions can help mitigate near- to medium-term risks and help navigate market risk. Our Investment Committee keeps those portfolios under continuous review.

## Getting in touch

If you would like to find out more or discuss any of the above, please contact your financial adviser.

## Disclaimer

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## Notice

Investments carry risk. The value of your investment (and any income from them) can go down as well as up and you may not get back the full amount you invested. Past performance is not a reliable indicator of future performance. Investments should be considered over the longer term and should fit in with your overall attitude to risk and financial circumstances.

## Contact us

For more information, please contact your financial adviser.