Equity Newsletter

1st Quarter 2026

First Trust

We hold a balanced, moderately positive view of U.S. equities, and we expect continued economic expansion. We expect outsized investment in artificial intelligence (AI) infrastructure, diminished tariff uncertainty and policy incentives to support robust capital expenditures (CapEx), which we see not only supporting top-line growth, but also potentially enhancing productivity and corporate profitability.

Policies implemented in the One Big Beautiful Bill Act such as the increased section 179 deduction to allow for the immediate expensing of equipment, and the immediate expensing of domestic research and development costs create a favorable environment for capital spending, in our view. However, in the first half of 2025, policy uncertainty was highly elevated as the Trump administration used tariffs to gain leverage during trade negotiations (Chart 1).

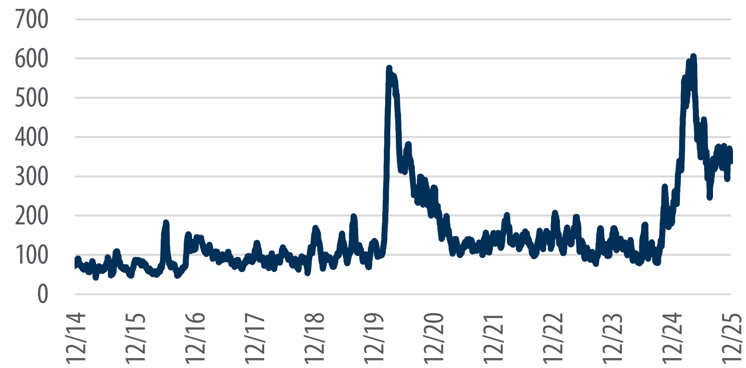
Policy uncertainty adds complexity and greater risk to the corporate investment decision making process. Chart 2 illustrates this impact as CapEx intention surveys weakened considerably in the first half of 2025 despite the aforementioned incentives.

Tensions on trade diminished somewhat as deals were negotiated, especially when a trade truce was agreed to by the U.S./China after Trump traveled to South Korea in October to meet Chinese leader Xi Jinping. CapEx intentions have been on an upswing in recent months, as corporate decision-makers are eager to take advantage of incentives and return to a focus on growing their businesses (Chart 2).

Banks are also more likely to lend for commercial and industrial (C&I) purposes in a less volatile policy environment. Senior Loan Officer surveys indicated a tightening in standards mid-2025, which has since reversed (Chart 3).

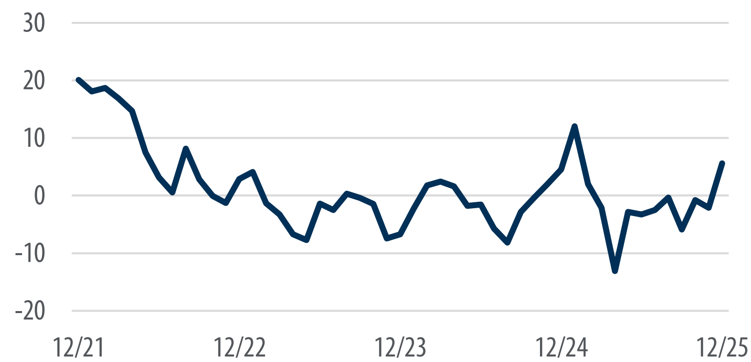
In summary, we believe an acceleration in broad based capital spending is possible, supported by catch up demand from last year, policy incentives and our expectation for robust commercial lending in 2026.

Chart 1: Economic Policy Uncertainty Index (20-Day Moving Average)



Source: Bloomberg. Data from 12/31/14 to 12/31/25.

Chart 2: U.S. Average of Regional Federal Reserve CapEx Intention Surveys



Source: Bloomberg. Data from 12/31/2021 to 12/31/25. Average of CapEx expectation surveys for the Kansas City, Chicago, Philadelphia, New York Empire, Richmond and Dallas regional surveys.

Chart 3: U.S. Senior Loan Officer Survey - Net % Tightening Standards for Commercial and Industrial (C&I) Loans

Source: Bloomberg. Data from 1/12/2016 to 1/12/26.

CapEx is a strategic investment in long-term assets that is depreciated over time on a company's financial statements.

Sector Views

Communication Services
- Cloud service providers increasing CapEx to build-out AI capacity as adoption increases. Return on CapEx investment is the key question for the industry, in our view.

Consumer Discretionary
- While unemployment remains relatively low, job additions have been modest in recent months. Solid wage growth and relatively low unemployment are current positives for consumption, but job additions are meager.
- Cumulative impact of inflation in recent years remains painful for consumers, especially on the lower end of income distribution, while high income consumers benefit from a strong wealth effect from rising asset prices.
- Easing Federal Reserve policy may buttress demand for rate sensitive purchases such as housing or autos.
- Increasing e-commerce penetration and automation of warehouses are secular positives to profitability.

Consumer Staples
- Defensive sector, but offers what we see as relatively meager growth.
- Valuation not particularly attractive, in our view.

Energy
- We are relatively neutral towards energy, as we expect ample supply to remain a headwind to oil prices, but note that energy sector equities provide strong free cash flow generation.
- The U.S. economy is a key source of demand for energy, and we believe the U.S. will avoid recession in the immediate term. Potential improvement in Chinese macro would present a source of demand upside, but we expect supply growth to remain robust.
- Risk to global oil demand from any tariff re-escalation.
- Geopolitical risks to supply include recent Iranian unrest and tensions in Middle East between Israel and Iran. Venezuelan production may improve over time after the recent U.S. actions to oust Nicolas Maduro.

Financials
- We expect a more industry friendly regulatory stance towards banking, including less scrutiny of mergers, and easing of capital requirements.
- Investment banking revenue and trading expected to strengthen amid increased capital markets activity and market volatility, respectively.
- Commercial and industrial (C&I) loan growth may accelerate in upcoming quarters amid pent-up demand, and potentially lower rates. Businesses may also borrow more if the regulatory environment becomes more favorable with the current administration.
- Credit quality remains reasonable. That said, any significant rise in unemployment would likely increase delinquencies.

Healthcare
- Provides potential opportunity to invest in growth that is less correlated to the business cycle.
- We believe healthcare policy uncertainty may lessen in comparison to last year.
- Lower interest rates lower funding costs for biotechnology firms to develop innovative therapeutics, and we see the possibility of consolidation in the industry as big pharma replenishes their pipelines.
- Life science tools industry may see recovery as policy uncertainty diminishes, potentially resulting in greater willingness for the biopharma industry to invest in capital equipment. We expect bioprocessing growth to accelerate, as well. Government and academic research spending is also important to the industry.
- Valuation is attractive in the sector, in our opinion.

Industrials
- Demand for CapEx is a secular driver that may benefit the sector, as firms are motivated to reshore supply chains and increase productivity in a tight labor market.
- Increasing infrastructure requirements to support data centers is another key secular driver for some industrial firms.
- Tariff policy is a risk to industrial exports.
- Defense industry names tend to benefit from increasing geopolitical risk, as well as potential increases in defense spending on the part of U.S. allies over time.
- Valuation in sector is reasonable, in our view.

Information Technology
- We expect robust information technology corporate spending driven both by AI related capital spending, and in end markets outside of AI, such as traditional enterprise servers.
- Key semiconductor end markets such as AI, high bandwidth memory, and vehicle electrification tend to benefit from secular tailwinds.
- AI increases uncertainty in the software industry, in our view.
- We prefer quality within the sector.

Materials
- On a cyclical basis, risks to international growth from trade tensions, and weakness in Chinese construction are headwinds to basic materials demand.
- We believe incremental demand from clean energy grid infrastructure and electric vehicle transition is a secular positive for some metals, such as copper.
- We believe the materials sector may benefit over time from policies and investment designed to reshore supply chains and improve resource security amid geopolitical tensions.

Real Estate Investment Trusts (REITs)
- Higher yielding sector sensitive to interest rate movements, potential to benefit if rates decline.
- In our view, data center REITs provide a strong secular opportunity but are sensitive to the information technology spending environment on a cyclical basis.

Utilities
- Defensive, dividend paying nature typically more attractive in times of macroeconomic uncertainty.
- Utilities are sensitive to interest rate movements, a potential positive if rates have peaked.
- Data center power consumption is a source of secular growth in electricity demand.

DEVELOPED MARKETS

Europe

- Inexpensive valuation in comparison to U.S. stocks.
- While we believe European policymakers have expressed more willingness to stimulate their economies, which could support long-term growth, we believe the actual impact on the real economy may take place slowly, as infrastructure projects take time to plan and implement, and the multi-country bureaucracy of the EU slows decision making.
- The European Central Bank remained on hold in December but maintains a data dependent posture, in our view. Inflation has been moderating, however, and we believe easing may resume later in 2026.
- Chinese imports redirected from the U.S. may negatively impact balance of trade and potentially impact the competitive position of Europe's exports.
- European sentiment stands to benefit from any de-escalation of the Ukraine/Russia conflict.
- Geopolitical risk from increased influence of populism on national politics within Eurozone and tariff policy.

United Kingdom

- We expect sluggish growth as the labor market gradually weakens.
- The Bank of England may continue to ease interest rate policy, in our view, while we believe fiscal policy may tighten.
- Inexpensive valuation in comparison to U.S. stocks.

Japan

- We expect robust capital expenditures and exports to the U.S. and EU to support corporate profits.
- Bank of Japan may continue a modest tightening cycle as the Japanese economy improves, potentially strengthening the Yen as the Federal Reserve eases.
- Japan stands to benefit from "friend-shoring" and increased secular demand for advanced technology exports such as automation equipment.
- We expect corporate governance reforms to improve capital efficiency via increased share buybacks and less cross-shareholder ownership, offering the possibility for higher return on equity for Japanese corporations over time.
- Challenging demographics may limit long-run potential economic growth.
- Tensions with China bear watching, with China restricting rare earth mineral exports to Japan due to comments by the Japanese Prime Minister related to Taiwan.

Australia

- We expect solid economic growth, driven by business investment in data center and energy infrastructure.
- Exports of raw materials are another key driver of economic growth.

Canada

- U.S. is key trading partner and stands to benefit from strong U.S. growth; review of U.S.-Mexico-Canada Agreement (USMCA) in mid-2026 may lower tariffs and benefit Canadian exports, but outcome of review is uncertain.
- Energy and metals exporter, which stands to benefit when oil prices rise and demand for basic materials is strong, would suffer from a U.S. recession or a decline in oil prices.

EMERGING MARKETS

Emerging Asia

- Chinese policymakers have signaled a willingness to support growth with fiscal and monetary policy easing, and are taking steps to rationalize industrial overcapacity, as well. That said, we believe Chinese property market weakness remains a headwind.
- Rising geopolitical tensions present risk to supply chains for key technologies and materials, and complicate U.S. firms' decisions to invest in China.
- Despite a one-year trade truce announced in November, Chinese exports to the U.S. are likely to remain impacted by U.S. tariff policy, in our view. That said, we expect China's export share to countries outside the U.S. to potentially trend higher.
- India and the U.S. are currently in trade negotiations, which could buttress growth if any deal is finalized. We expect easier fiscal policy via tax reform, and dovish policy on the part of the Reserve Bank of India (RBI) to provide tailwinds to India's growth.

Latin America

- Mexican economy stands to benefit from exports to U.S., review of USMCA in 2026 may positively impact trade, but also creates uncertainty. Over time, supply chain diversification away from China may be a structural tailwind to exports.
- Populist election results impact sentiment towards the region, as fiscal discipline may be called into question.
- Brazil and Latin America overall are sensitive to demand for commodity exports.
- Tariffs are a risk to the region, but Mexico currently stands to benefit from more favorable terms for USMCA compliant goods.

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