



# CAPITAL MARKET ASSUMPTIONS

2026



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# CONTENTS

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<b>1. Key Forecast Updates</b>	<b>3</b>
<b>2. Overview</b>	<b>4</b>
<b>3. Asset Class Forecasts</b>	<b>7</b>



# CHAPTER 01

## KEY FORECAST UPDATES

Relative to Q4 2025, our long-term outlook for fixed income assets has broadly improved across both sovereign and spread exposures:

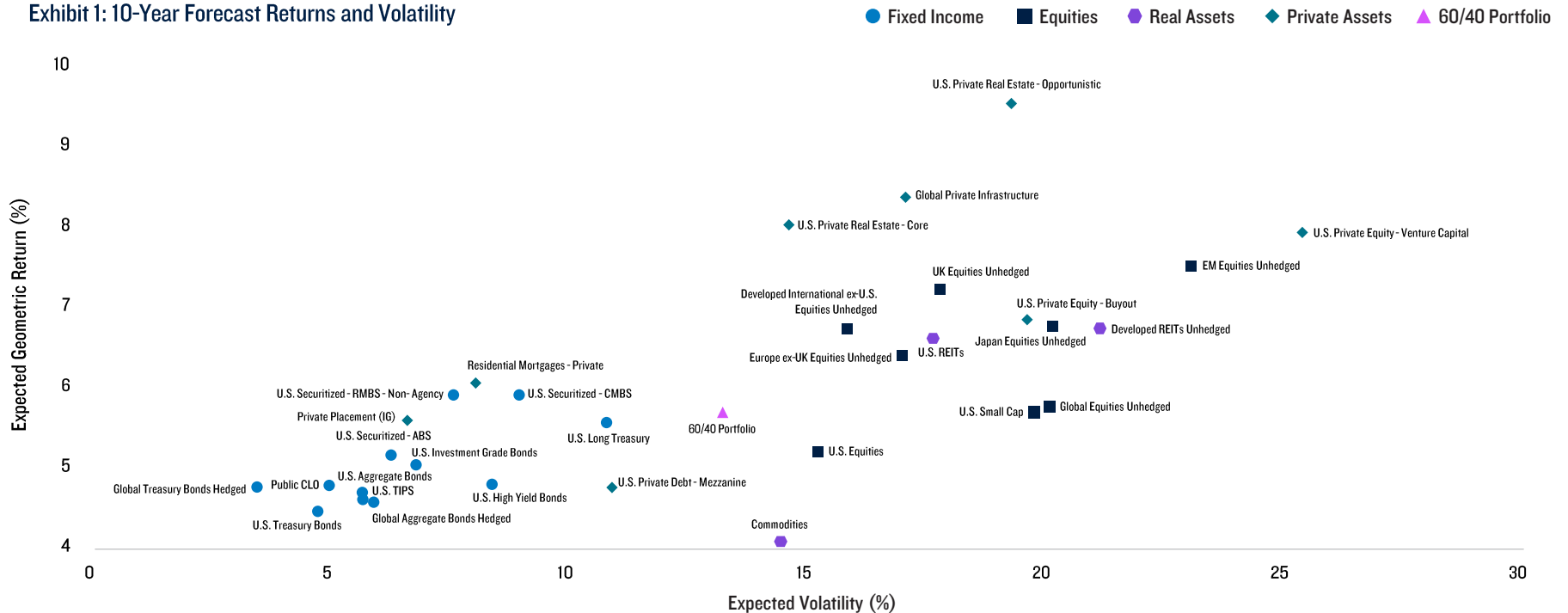
- U.S. Aggregate Bonds: Revised to 4.7% from 4.6% last quarter.
- U.S. Long Treasury Bonds: Revised to 5.6% from 5.2% last quarter.
- U.S. High Yield Bonds: Revised to 4.8% from 4.3% last quarter.

Our 10-year forecasts for equity markets declined modestly across regions as last quarter's 3.3% gain in global equities weighed on valuations:

- U.S. Large-Cap Equities: Revised to 5.2% from 5.3% last quarter.
- International Equities ex-U.S.: Revised to 6.7% from 7.1% last quarter.
- Emerging Markets Equities: Revised to 7.5% from 8.1% last quarter.

Given increased relative attractiveness of securitized credit and private credit, especially as corporate spreads continue to tighten, we broadened our capital market forecasts to include some of these asset classes.

Exhibit 1: 10-Year Forecast Returns and Volatility



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## CHAPTER 02

# OVERVIEW

### Q4 2025 Developments Informing Our Long-Term Forecasts

The global economy ended the year on a firm footing, despite continued policy uncertainty, primarily emanating from the U.S. Policy uncertainty in Q4 was centered on the U.S. government shutdown, spanning from the beginning of October through mid-November, which temporarily disrupted many government services, including a number of economic releases.

Nevertheless, the available data suggest that economic activity and the labor market, especially when excluding government workers, remained resilient. U.S. real GDP grew over 4% quarter-over-quarter (annualized) in Q3, with the Atlanta Fed GDPNow Q4 estimate exceeding 5% as of mid-January. Reflecting this strength, we slightly increased our 10-year U.S. GDP growth forecast to approximately 2%, which remains close to the average following the Global Financial Crisis.

Strength in the real side of the economy has also kept upward pressure on inflation. U.S. CPI ended December at 2.7% year-over-year, down from 3% at the end of Q3, but consistent with the average pace for 2025. Our 10-year U.S. inflation forecasts remain roughly unchanged at around 2.5% in this quarter's Capital Market Assumptions (CMAs).

The Federal Reserve (Fed) continued its rate-cutting cycle in Q4, implementing two additional cuts after resuming the cycle in September, even as inflation remained elevated. However, the December meeting's Summary of Economic Projections suggests a slower pace of rate cuts in 2026. As of this writing, tensions between the Trump administration and the Fed remain high.

Central bank policies are diverging across global markets. The European Central Bank (ECB) has held the deposit facility rate at 2% since mid-2025. The ECB has been able to lower rates more aggressively than the Fed due to greater progress on inflation, with CPI returning to its 2% year-over-year target in December.

In contrast, rising inflation and yen weakness prompted the Bank of Japan to raise its target rate by 25 bps to 0.75% in December, the second increase of 2025. Newly inaugurated Prime Minister Takaichi is pushing for more aggressive fiscal stimulus, which could provide near-term support for Japanese growth. Meanwhile, as Japanese inflation rises and the yen weakens, China is trending in the opposite direction, with falling inflation and a strengthening yuan.

# OVERVIEW

## Capital Market Assumptions Framework

Our Capital Market Assumptions (CMAs) underpin the long-run outlook for strategic allocations in certain strategies and multi-asset portfolios. They are the product of a highly systematic process for generating consistent projections across capital markets.

CMAs provide 10-year expectations for the most widely held equity, fixed income, and non-traditional asset classes, measuring both return and risk. The process for our CMAs begins with evolving asset-class fundamentals and macroeconomic assumptions at the country level.

For each asset class, we decompose local return expectations into three broad categories: income, growth, and valuation adjustment. We also forecast relative currency adjustments for investors in different domiciles to allow for conversion to hedged or unhedged returns. Our core building blocks and final forecasts are reviewed at their component levels by an investment council of our most senior investment professionals.

### Asset Class Specific Inputs

- Current Equity Market Valuations
- Dividend Yields
- 10-year Treasury Yield Credit Spreads
- Credit Spreads

### Macro Inputs

- GDP Growth
- GDP Potential and Inflation Forecasts

### Economic Assumptions

- Future Real Interest Rate Forecasts
- Real Rates
- Future Valuation Forecasts
- GDP Growth
- Credit Spread Forecasts

### Capital Market Return Expectations

- Global and Integrated Across Regions
- Internally Consistent Across Assets
- Guided by Investment Council

### Investment Council Review of Primary Inputs

- Including GDP Growth and Inflation Expectations
- Equilibrium Valuation and Real Interest Rates

Shown for illustrative purposes only. Source: PGIM. As of 12/31/25.

# OVERVIEW

## Global Economic Outlook

Forward-looking views for economic growth and inflation are among the most critical building blocks of our CMAs. We currently compile these for 16 countries. Based on our forecasts, long-term real economic growth in developed economies over the next 10 years is expected to continue to moderate, as it has for the last three decades. This is due to the limited growth of the labor force, which is constrained by domestic demographics and based on an assumption of no significant offset from improved productivity growth over the decade timeframe.

Our forecasts for near-term economic growth and inflation are comparable to last quarter's. We expect longer-term economic growth in developed economies to be led by Australia as well as other countries with younger populations and more liberal immigration policies. We anticipate growth to be slowest in Japan and parts of Western Europe, where the labor force is expected to contract further over the next decade.

Inflation in Developed Markets is anticipated to moderate over the next 10 years relative to current levels, which still exceed most central bank targets. Our 10-year forecasts for Developed Market inflation range from a 2.8% annual rate in Australia to a low of 2.0% in the Eurozone. Emerging Markets, however, are expected to produce real economic growth and inflation at annualized rates of 3.2% and 2.4%, respectively, driven by younger populations and higher rates of return on capital than in Developed Markets.

## Evolution of Our Market Outlook

During the decade leading up to 2017, rising valuation ratios and moderating expectations for Developed Market growth and inflation drove a steady decline in our long-term Capital Market Assumptions for Global Equities. These assumptions stabilized at historically low levels from 2017 onward.

Declining equity markets in 2022 and an upward revision to our longer-run inflation expectations partially reversed this trend, moving forecasts temporarily higher. More recently, strong equity market returns from 2023 onward have again made valuations less attractive, reducing our equity forecasts to historically low levels. Our outlook for returns of Global Equities over the next 10 years is 5.8%, a decrease of 0.1% from our forecast of 5.9% for the fourth quarter of 2025.

Our Capital Market Assumptions for Global Fixed Income assets have moved materially higher over the past three years, coincident with the significant increase in global interest rates in response to heightened developed market inflation in 2021 and 2022. Moderating inflation in the U.S. and Europe has prompted a reduction in short-term interest rates over the past two years, though longer-term rates have held steady in a higher range, generally supporting our forward-looking global fixed income forecasts.

Exhibit 2: Expected 10-Year Return for Global Equities



Exhibit 3: Expected 10-Year Return for Hedged Global Aggregate Bonds



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# ASSET CLASS FORECASTS

## Global Fixed Income Markets

Long-term fixed income forecasts begin with our view of 10-year forward policy rates for each of the major Developed Market central banks. We derive expected policy rates for each central bank jurisdiction as a function of current and future equilibrium real interest rates, the expected GDP output gap over the next 10 years, and the expected rate of inflation.<sup>1</sup> Our forecasts for short-term interest rates also incorporate a forward-looking central bank reaction function, placing less weight on current interest rate levels. While the 2010s were a period of low and stable short-term interest rates, the 2020s have been characterized by a much more volatile period for short-term rates as central banks responded to the pandemic and inflationary aftermath.

Moreover, the volatility in short-term rates flows through to our assumptions about future rates, as elevated current rates tend to push our forecasts higher. Since our overall methodology takes a building block approach, this volatility also flows through to forecasts for other asset classes, making this a more forward-looking approach that helps to stabilize our long-term forecasts.

Our long-term forecasts for short-term interest rates are comparable to those for the fourth quarter of 2025. For the U.S., policy rates in 10 years are expected to be roughly 40 basis points lower than the 3.6% policy rate midpoint that prevailed at the end of the fourth quarter of 2025 given our forward views of inflation and growth relative to potential.

Our bond return forecasts are largely predicated on income and valuation factors. At a given maturity point, the forecast income return for a government bond will consist of the average expected coupon yield over the forecast horizon, as well as proceeds (losses) from bonds maturing to lower (higher) yields. Changes in yield at a given maturity point over the forecast horizon will determine the necessary valuation adjustment. If yields are forecast to rise (fall) over the next 10 years, the valuation adjustment will be negative (positive).

1. GDP-weighted Eurozone country average for European Central Bank. As of 12/31/25

For longer-maturity government bond returns, we forecast each country's expected long-term slope to define a term structure of yields across their respective government yield curves. The forecast slope for each country is a function of forecast and potential real economic growth and will evolve countercyclically. When economic growth is forecast below potential, the slope of the yield curve is expected to be steeper (early cycle), whereas if growth is forecast to be closer to, or above, potential (late cycle), the yield curve is forecast to be flatter.

### Exhibit 4: Interest Rates

Country	Current Short-Term Interest Rates (%) (Dec 31, 2025)	Long-Term Forecast of Short Interest Rates (%)
United States	3.63	2.66
United Kingdom	3.89	2.31
Eurozone	1.82	1.84
Japan	0.58	1.86
Australia	4.14	3.17
Canada	2.20	2.51

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## ASSET CLASS FORECASTS

U.S. 10-year Treasury yields at 4.2% were nearly unchanged in the fourth quarter of 2025. Looking forward, yields for the Bloomberg U.S. Treasury Index are expected to decrease from current levels over the next 10 years, resulting in a positive valuation adjustment and an expected return of 4.5%.

Unhedged Developed Market government bonds outside the U.S. are forecast to return somewhat less over the next decade, given lower initial yields. Long-run returns in Developed Market government bonds for a U.S. investor are forecast to be 4.4% on an unhedged basis and 4.8% on a hedged basis given the differentials in forecast short-term interest rates.

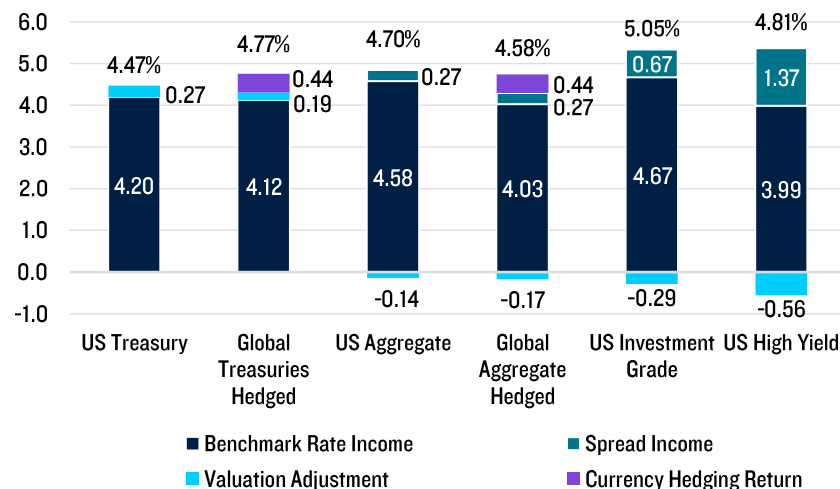
Our long-term forecast for U.S. Aggregate Bonds is 4.7%, which includes an expected spread return of 0.1%. Our forecast for hedged Global Aggregate Bonds from a U.S. investor perspective is 4.6%, given similar assumptions for credit spreads and defaults, as well as gains from currency hedging, which partially offset lower starting levels for underlying government yields outside the U.S.. For both U.S. Investment Grade and U.S. High Yield Bonds, spreads at the end of the first quarter of 2025 were considerably tighter than expected averages for the next 10 years.

Beginning this quarter, in partnership with PGIM's Strategic Capital Group, we are introducing additional 10-year Fixed Income forecasts for publicly traded Collateralized Loan Obligations (CLOs), Securitized Asset Backed Securities (ABS), and Commercial Mortgage-Backed Securities (CMBS) as well as Non-Agency Residential Mortgage-Backed Securities (RMBS).<sup>2</sup>

We calculate the expected returns for fixed income credit indexes to include any additional income expected from an average credit spread yield over comparable government bonds, adjusted for expected default and downgrade losses over the forecast horizon.

We then calculate the valuation adjustment for expected changes in spreads. Our long-run return forecasts for U.S. Investment Grade and U.S. High Yield Bonds are 5.1% and 4.8%, respectively.

Exhibit 5: Decomposition of Fixed Income Return Forecasts



	U.S. Treasury (%)	Global Treasuries Hedged (%)	U.S. Aggregate (%)	Global Aggregate Hedged (%)	U.S. Investment Grade (%)	U.S. High Yield (%)
<b>Total</b>	4.47	4.77	4.70	4.58	5.05	4.81
<b>Benchmark Rate Income</b>	4.20	4.12	4.58	4.03	4.67	3.99
<b>Spread Income</b>	0.00	0.00	0.27	0.27	0.67	1.37
<b>Valuation Adjustment</b>	0.27	0.19	-0.14	-0.17	-0.29	-0.56
<b>Currency Hedging Return</b>	0.00	0.44	0.00	0.44	0.00	0.00

Data in chart can be found in table below the chart.

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2. **Residential Mortgage:** The expected return reflects loss-adjusted and option-adjusted spread of non-agency residential mortgage loans as of 12/31/2025.

**ABS:** Reflects 12/31/25 spread relative to ICE BofA U.S. Fixed Rate ABS Index.

**CLO:** Reflects 12/31/25 spread associated with a sample portfolio of public CLOs with credit quality ranging from AAA through A.

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**RMBS:** Reflects 12/31/25 spread associated with a sample portfolio of non-agency RMBS with credit quality ranging from AAA through BBB.

# ASSET CLASS FORECASTS

## Global Equity Markets

All of our long-term asset class forecasts, including equities, are based on income, growth, and valuation considerations.

Consistent with historical precedent, and assuming the continuation of current dividend taxation regimes, the U.S. equity market has a large share of expected income returns coming from share buybacks, equal to about 1.8% in our long-term forecasts. Outside the U.S., the expected impact of net buybacks in developed economies on long-term income returns is anticipated to be a much more modest 0.7%. For Emerging Markets, an expected drag on income returns from net share issuance is forecast at 0.3%.

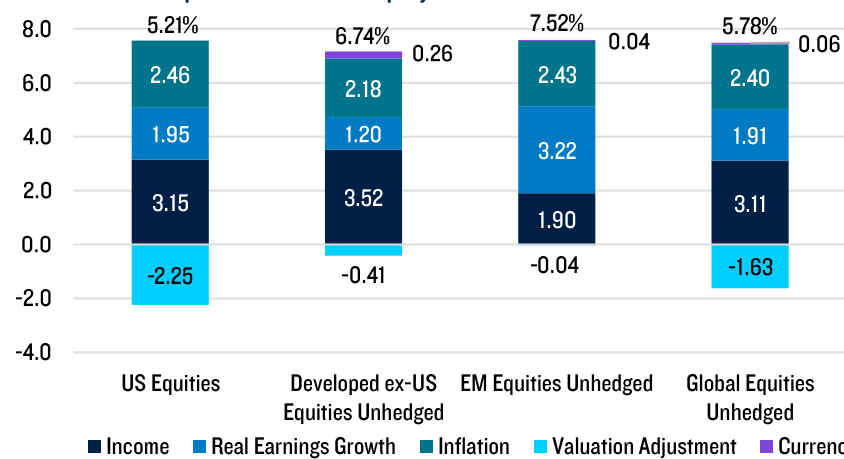
**To build the income component of our long-term equity forecasts, we calculate each country's expected income contribution based on current and anticipated levels of dividend yield as well as the expected returns attributable to buyback activity (positive) or net positive share issuance (negative).**

For the growth component of our equity return forecasts, nominal GDP growth over the next 10 years is expected to approximate long-term nominal earnings growth for each equity market. We calculate this as the combined annualized rate of expected inflation plus real GDP growth. As noted earlier, our near-term growth and inflation expectations are similar to those from last quarter. Our 10-year forecast for U.S. real annualized GDP growth is now 1.9%, with 2.5% for inflation translating to an earnings growth component of 4.4%. While the impact of tariffs may elevate inflation over the next few quarters, over the longer term we anticipate inflation will continue to moderate to a level closer to the Fed target of 2%. For Developed Markets outside the U.S., our 10-year expectation for real GDP growth is 1.2%, while inflation is expected to average 2.2%. This assumption would provide nominal earnings growth of 3.4%.

For Emerging Markets, higher nominal GDP growth relative to Developed Markets is expected to result in long-run nominal earnings growth of 5.7%. Among Developed Markets, the U.S. maintains a negative expected long-term valuation adjustment of -2.2% annually, attributable to still historically elevated valuation

ratios. Developed equities outside the U.S., in contrast, are expected to have negligible valuation repricing given historical valuation ratios that are close to long-run averages. Emerging Market equities are currently viewed as fairly priced from a historical valuation perspective.

**Exhibit 6: Decomposition of Global Equity Return Forecasts**



	U.S. Equities (%)	Developed ex-U.S. Equities Unhedged (%)	EM Equities Unhedged (%)	Global Equities Unhedged (%)
<b>Total</b>	5.21	6.74	7.52	5.78
<b>Income</b>	3.15	3.52	1.90	3.11
<b>Real Earnings Growth</b>	1.95	1.20	3.22	1.91
<b>Inflation</b>	2.46	2.18	2.43	2.40
<b>Valuation Adjustment</b>	-2.25	-0.41	-0.04	-1.63
<b>Currency</b>	0.00	0.26	0.04	0.06

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## Private Assets

Our methodology for forecasting Buyout Equity, Venture Capital Equity and Mezzanine Debt ties the forecast outcomes of these assets to those of public market assets and assigns a premium consistent with historical empirical outcomes, acknowledging the underlying illiquidity and potential leverage employed in these asset classes relative to public market counterparts. Our forecasts for private Real Estate incorporate data from the NCREIF Property Index (NPI) to determine yields and relative valuations in addition to linkages to forecast macroeconomic inputs. Investors in Private Assets must also evaluate cash flow considerations that may impact other liquid allocations in a multi-asset portfolio. For further reference about these considerations please see Shen et al. (2021).<sup>3</sup> Private equity funds that take a buyout strategy invest in equity ownership in mature companies, resulting in a change of control. These are typically large transactions that use leverage. Our 10-year annualized forecast for U.S. Buyout Private Equity is 6.9% versus a forecast of 5.2% for public U.S. Equities. Venture capital funds seek private equity stakes in startups and small- to medium-sized companies with strong growth potential. Our annualized 10-year forecast for U.S. Venture Capital Private Equity is 7.9% versus a forecast of 5.7% for public U.S. Small Cap Equities.

Private mezzanine debt invests in loans that are subordinate to other debt in a firm's capital structure and that are backed by little to no collateral. Our annualized forecast for U.S. Mezzanine Private Debt is 4.8%, which is identical to our current forecast for U.S. High Yield Bonds. Given the increasing role of private

infrastructure investments in institutional portfolios, we are now also producing a forecast for Global Private Infrastructure. Our annualized 10-year forecast for Global Private Infrastructure is 8.4% versus a forecast of 6.8% for Global Listed Infrastructure. Private real estate funds covered in the NPI for our forecasts include properties that have been acquired, at least in part, on behalf of tax-exempt institutional investors and held in a fiduciary environment. The property types allowed into the NPI are hotels, office buildings, industrial properties, apartments, and other retail-use properties.

Allowed properties can be wholly owned or even jointly owned properties. Returns on investment are required to be reported without leverage. From the unlevered initial forecast, we then calculate a core real estate forecast to represent funds with 20% leverage and an opportunistic real estate forecast to represent funds with 40% leverage. Our forecasts for Core and Opportunistic Private Real Estate this quarter are 8.01% and 9.6%, respectively.

Beginning this quarter, in partnership with PGIM's Strategic Capital Group, we are introducing additional 10-year private market forecasts for Private Placement Investment Grade Bonds and Private Residential Mortgages.<sup>4</sup>

3. Shen et al. (2021), "Harnessing the Potential of Private Assets: A Framework for Institutional Portfolio Construction," PGIM Institutional and Advisory Solutions.

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# ASSET CLASS FORECASTS

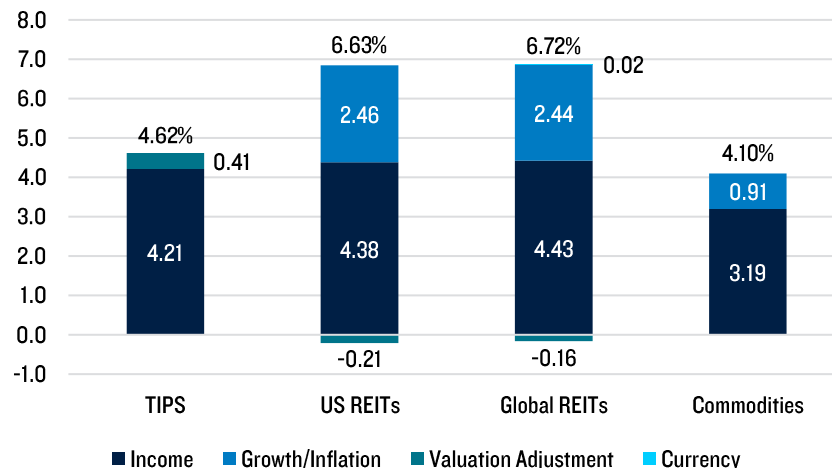
## Real Assets

We group together Commodities, REITs, and TIPS as Real Assets in our Capital Market Assumptions. For U.S. TIPS, we assume that expected inflation and break-even inflation converge over time, implying that the inflation risk premia and liquidity risk premia in TIPS offset one another. Under these assumptions, we forecast a long-term return from TIPS of 4.6%, which is somewhat above the expected return of U.S. Treasuries given the slightly higher duration of U.S. TIPS. Our forecast returns for U.S. and Global REITs include current and forecast dividend payments, expected appreciation linked to forecast price level changes, and a valuation adjustment based on current payout ratios. Our long-run forecasts for U.S. and Global REITs are 6.6% and 6.7%, respectively. Our long-run expected return for Commodities is 4.1%, reflecting a return on cash investment of 3.32%, assuming investment through liquid futures and a growth premium of 0.9%, consistent with historical spot returns over cash and a linkage to forecast inflation.

## Currency and Currency Hedging Returns

Our long-term forecasts for currency returns and return to currency hedging are based on our forward views of local relative price levels and short-term policy rates. These views allow us to provide our long-term forecasts for a range of domiciles outside the U.S. Over the next 10 years we are forecasting generally negative returns for the U.S. dollar relative to Developed Market peers with outcomes ranging from an annualized loss of -0.3% for the Australian dollar to a gain of 1.3% for the Swiss franc. Forecast outcomes for Emerging Market currencies range from an expected loss of -2.0% for the Indian rupee to a gain of 0.8% for the Taiwan dollar. Long-term currency hedging returns against a market-weighted basket of Developed Market exposures are forecast to be net positive for U.S. investors as short-term interest rates are anticipated to be higher over the long term in the U.S. relative to the Eurozone and Japan.

Exhibit 7: Decomposition of Real Asset Return Forecasts



	TIPS (%)	U.S. REITs (%)	Global REITs (%)	Commodities (%)
<b>Total</b>	4.62	6.63	6.72	4.10
<b>Income</b>	4.21	4.38	4.43	3.19
<b>Growth/Inflation</b>	0.00	2.46	2.44	0.91
<b>Valuation Adjustment</b>	0.41	-0.21	-0.16	0.00
<b>Currency</b>	0.00	0.00	0.02	0.00

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# ASSET CLASS FORECASTS

## Global 60/40 Portfolio

Based on our long-term forecasts, a balanced portfolio of 60% Global Equities unhedged and 40% Global Aggregate Bonds hedged is forecast to return 5.7% annually over the next 10 years, a decrease of 0.1% from our forecast for the fourth quarter of 2025.

### Exhibit 8: Q1 2026 10-Year Capital Market Assumptions

	Asset Class	Expected Geometric Return (%)	Expected Arithmetic Return (%)	Expected Volatility (%)	Expected Sharpe Ratio
Fixed Income	Cash	3.19	--	--	--
	U.S. Treasury Bonds	4.47	4.58	4.69	0.30
	U.S. Long Treasury	5.57	6.15	10.74	0.28
	Global Treasury Bonds Hedged	4.77	4.83	3.41	0.48
	U.S. Aggregate Bonds	4.70	4.86	5.61	0.30
	Global Aggregate Bonds Hedged	4.58	4.76	5.85	0.27
	U.S. Investment Grade Bonds	5.05	5.28	6.74	0.31
	U.S. High Yield Bonds	4.81	5.15	8.33	0.24
	Public CLO	4.79	4.91	4.92	0.35
	U.S. Securitized - ABS	5.17	5.36	6.21	0.35
	U.S. Securitized - CMBS	5.92	6.32	8.91	0.35
	U.S. Securitized - RMBS - Non-Agency	5.92	6.20	7.53	0.40
	U.S. TIPS	4.62	4.77	5.62	0.28
Equities	U.S. Equities	5.21	6.37	15.18	0.21
	U.S. Small Cap	5.71	7.66	19.72	0.23
	UK Equities Unhedged	7.24	8.81	17.74	0.32
	Europe ex-UK Equities Unhedged	6.41	7.84	16.94	0.27
	Japan Equities Unhedged	6.77	8.79	20.10	0.28
	Developed International ex-U.S. Equities Unhedged	6.74	7.99	15.79	0.30
	EM Equities Unhedged	7.52	10.17	23.01	0.30
	Global Equities Unhedged	5.78	7.78	20.04	0.23
Real Assets	U.S. REITs	6.63	8.17	17.58	0.28
	Developed REITs Unhedged	6.72	8.95	21.09	0.27
	Commodities	4.10	5.13	14.38	0.14
Private Assets	U.S. Private Real Estate - Core	8.04	9.10	14.57	0.41
	U.S. Private Real Estate - Opportunistic	9.55	11.40	19.24	0.43
	Residential Mortgages - Private	6.07	6.39	7.99	0.40
	Private Placement (IG)	5.60	5.82	6.56	0.40
	U.S. Private Debt - Mezzanine	4.77	5.36	10.85	0.20
	U.S. Private Equity - Buyout	6.86	8.78	19.58	0.29
	U.S. Private Equity - Venture Capital	7.95	11.16	25.35	0.31
	Global Private Infrastructure	8.38	9.83	17.03	0.39
60/40 Portfolio	5.71	6.57	13.18	0.26	

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Source(s) of data (unless otherwise noted): PGIM as of January 2026.

**All investments involve risk, including the possible loss of capital. Past performance is not a guarantee or a reliable indicator of future results.**

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