

In The Know: Episode 63

Outlook for global equities: what could surprise markets in 2026



Announcement (00:00):

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Host (00:14):

This is In The Know a monthly investment podcast brought to you by Magellan Investment Partners.

Alan Pullen (00:20):

The markets are pushed around in the short term by greed and fear. We know that we know that impacts people's psyche. People get scared when stocks are going down. They love it when stocks are soaring, but the fundamentals don't change that quickly.

Host (00:34):

That's Alan Pullen, global equities portfolio manager at Magellan Investment Partners. Welcome to In the Know. What Could Derail Markets or Fuel the Next Rally After Years of Gains in this conversation, investment director, Elisa Di Marco, is joined by portfolio managers Alan Pullen and Casey McLean to unpack 2025's volatility, the AI fueled rally and the outlook for 2026. Against a backdrop of elevated valuation, they discuss expectations for more moderate returns and a potential rotation toward quality and true AI execution. They also explore potential upside surprises and key wild cards from private credit risks to AI-led productivity gains. To kick things off, a welcome from your Host, Elisa Di Marco.

Elisa Di Marco (01:32):

Welcome to our first Magellan in the Know podcast for 2026. My name is Elisa Di Marco, investment director at Magellan, and today I'm joined by Alan Pullen and Casey McLean, portfolio managers within our global equities strategies. Welcome team.

Casey McLean (01:47):

Hi, Elisa.

Alan Pullen (01:47):

Great to be here.

Elisa Di Marco (01:48):

Awesome. Okay, so today's podcast we're going to focus on the year ahead, that is 2026. We're going to talk through our outlook for the year and the risks that we're considering when forming our global portfolios here at Magellan. All right, Casey, so starting with you, when we look back on 2025, it was a very volatile year. But once that Trump uncertainty did settle, AI hype took over and we saw that the MSCI world was up 12% in Aussie

dollars and 21% in US dollars. Are you expecting a continuation of this market strength that we saw last year for 2026, or is it a change in sentiments on the horizon?

Casey McLean (02:27):

You're right, Elisa. It was a pretty strong year of returns. In fact, the last three years have been really strong returns of 20% type returns for the US, which you don't normally get those sort of years back to back. And now where we stand today, valuations are fairly full. The S&P is trading on about 23 times. Earnings growth is pretty strong at the same time. Estimates have it at running at 13, 14%, and that rate of growth does support that multiple. But if there's any hiccups in the growth outlook, there is a risk of derating.

[\(03:04\):](#)

I think the other factor that we need to think about is a rotation in what's been driving the market. In 2025 in particular, it was really all about momentum. And some of the other factors like quality or low volatility, they significantly underperformed the market. Quality by over double digits in 2025. And we know that quality outperforms over the long term. Then there's a good fundamental basis for that. The companies that are high quality, they've got high returns, they can reinvest in their growth and that means they're able to compound their earnings growth over the long term.

[\(03:41\):](#)

What that means historically, as we've seen, quality does outperform, but we have these periodic periods where it does underperform by even 10% or more. It happens maybe every four or five years, but we often see a really sharp snap back after that. So that is on the cards for 2026 or beyond. And what would that look like? Well, I don't think you'd necessarily need to see the death of the AI trade, which one of those key drivers of 2025, but you probably see a bit of a rotation in what's been leading the market. Moving away from that AI hype, that speculative momentum, and into a bit more of the AI execution, the companies that are really executing and delivering real earnings growth out of that.

[\(04:29\):](#)

And we'll probably also see a bit of a broadening out of the drivers of the market. Last year was really narrow. 33% of stocks contributed positively to returns, normally that's 50%. And we're starting to see that already. We're starting to see some of the defensive stocks perform better in so far in 2026. Seeing commodities, not a sector we invest in, that is starting to perform as well, and even small caps as well. So that broadening out is a positive sign I think for markets overall.

Elisa Di Marco (04:59):

Thanks, Casey. That was a really nice backdrop for the expectations for 2026, and I think really highlighting there that there is likely to be elevated risks given where valuations are at the moment. And I think the start of the year, it's only not even been two months yet and we have seen this elevated volatility in the market.

[\(05:19\):](#)

So, Alan, can you start with the macro geopolitical backdrop that has led to some of this volatility this year? A lot of it induced by our favorite politician, Donald Trump. He's been talking about affordability. We've had Venezuela, Greenland, the Fed, the list goes on there. How does all of that dynamic impact your view and your outlook for markets?

Alan Pullen (05:40):

You're right, Elisa. I mean, it's been a pretty strong start to the year, following last year. Obviously we had all the tariff disruption early in the year and then Trump went a little bit quieter, I'm not going to say silent, but a little bit quieter over the second half of the year, which was positive for markets overall. Well, he's certainly come out with a bang this year. As he mentioned Greenland, he's been talking up Greenland. Obviously we had

Venezuela. We're talking about Iran at the moment as he's moving a second aircraft carrier into the region. So more possible action there as well.

[\(06:12\)](#):

What I would say though is that so far when he has pushed, when push came to shove, he has continued to kind of de-escalate where required. So we remember he pushed pretty hard on Greenland and then when it looked like the Europeans were pushing back, he actually stepped away from kind of ruled out military force and so on in terms of that negotiation. I think an important one here has actually been with the Fed. We've been talking about the risks to the US over the longer term and one of those was the degradation in US institutions.

[\(06:44\)](#):

The US is a very attractive market for capital, strong venture capital, lots of fundraising, strong markets, but the rule of law is essential to allow that entrepreneurial spirit to kind of flourish in the US, and we did see pressure on some of those US institutions, most particularly the Federal Reserve. Well his nomination for the Federal Reserve chairmanship in May is Kevin Warsh and he is actually quite well respected by the markets. So this has kind of eased some of those fears that he would have a complete, let's say, toady put in place who will just slash rates but lose the confidence of the market. So once again, once the market started to push back a bit, he actually came up with a more rational choice. We still expect Kevin to cut rates. He's obviously been put in to do that job, but to do it more judiciously I guess over time.

[\(07:34\)](#):

So we continue to expect volatility coming up to the midterms that's later this year. Trump is pretty unpopular at home and a lot of affordability issues in the US, particularly amongst the lower income consumer. So some of those noise will continue to come. Recommendations like credit card caps on interest rates, we expect to continue to hear stuff like that, but not the really more impactful stuff so far he's been walking back from that. So continued noise and we'll watch it closely, but not something we are considering in our base case as a major disaster yet.

Elisa Di Marco [\(08:09\)](#):

So likely the TACO trade round two perhaps coming through for 2026. Now, Casey, we've also seen a lot of volatility in the first two months of this year that's been technology induced. So we've had these weekly announcements come through from Anthropic's Claude AI, which has been dividing the technology but also the services sectors. We've often viewed that some of these names, they're often capital light, they're high quality. How are these announcements changed your view and the outlook for these sectors that we often held in really high regard?

Casey McLean [\(08:46\)](#):

Yeah, that AI disruption theme narrative has really ramped up this year in the start of 2026. And it's not just software that's getting hit, it's all of these companies, like the data providers, the exchanges. The list is really lengthening every day. Our view is that this is a pretty indiscriminate sell-off really. It's the entire sector. It's an oversimplified narrative. And really at the moment the market is lumping everyone in this sector into that AI losers bucket. We think it's much more nuanced than that.

[\(09:20\)](#):

There are going to be some losers, but there's definitely going to be some big winners out of the AI in this sector. And if you think about it, the market's pretty efficient most of the time. It generally gets it right, but it does get it wrong at times and it's generally when sentiment goes to an extreme, be it positive or negative. We only need to look back less than 12 months ago at Google. It was trading at lowest multiples in long time, at 16 times, and that was because search was being disrupted. They're going to lose market share, their own AI model wasn't that great and ChatGPT was going to take all their lunch.

[\(09:58\)](#):

Fast-forward to today, that model was rerated to over 30 times. Search growth is accelerated. They've got the leading model, that model and AI in general is generating more and more queries coming through their search and they're able to monetize it in different ways. So when these extremes happen we need to take a new one's view. And I think if you look at today, there's some good examples where this dichotomy is there like SAP and Adobe for instance. SAP has been sold off just as much as Adobe. We think SAP has really strong fundamentals that mean it can win in the AI era. They are the system of record, they own the data or they manage the data for these really complex multinational customers and they're able to integrate AI into that.

[\(10:47\)](#):

Would Coke, for instance, trust a start-up AI company to autonomously come in, run their data and do things to their company? Would they even trust an internally developed system or would they trust SAP that's been doing it for them for years? Whereas if you think about Adobe, on the other hand, I think their moat really was the skill barrier that you needed, the 10,000 hours, the mythical 10,000 hours of experience on Photoshop or Illustrator to really master the system. Once you've done that, you're locked in for good AI comes in that democratizes that. You now can press a few buttons and you can master generating photos and editing images as well. So when we are at these really sort of extreme moments where everything is being sold off, it creates some great opportunities and we're seeing that now.

Elisa Di Marco [\(11:39\)](#):

So with that backdrop of the themes and market dynamics that we're expecting for 2026, Alan, to start off with, can you talk us what sectors you're leaning into this year?

Alan Pullen [\(11:50\)](#):

Well, I mean we are always leaning into quality. As you know, that underpins everything we're kind of doing here at Magellan and those quality companies compound and deliver value over the long term. And as Casey mentioned early on, looking particularly attractively valued at the moment given their under performance last year. So we're continuing to lean in and upgrade the quality of the portfolio where those opportunities are coming. We don't churn the portfolio. I mean the idea here of course is to hold these really great companies over many years as they compound their earnings and their value over that long-term period as long as structurally nothing is impacting them and going wrong.

[\(12:27\)](#):

So we are watching very carefully for structural changes within the market, within industries. We talked about the disruption from Gen.AI and analyzing each of our companies to see which ones are more immune, as Casey talked about, SAP, and which ones could potentially be disrupted. And we are leaning into those opportunities both in those high quality space, which isn't really being impacted by AI one way or another. We talked about the opportunities in healthcare last year, in consumer staples last year that offer lower risk to investors, which was again those low volatility stocks very much out of favor last year as speculation which driving the markets. So we've still got really good exposure there.

[\(13:10\)](#):

And right now looking at those opportunities that Casey was talking about where the indiscriminate selling, which has gone from based on a reasonable premise that disruption is coming, to really being driven by fear. And it seems like that indiscriminate nature of the selling in parts of the market at the moment, it's really driven by do you happen to be in the wrong part of the market in the wrong index as quants starts selling and short-term fear takes over.

[\(13:35\)](#):

So where we can find opportunities there, we will lean in as well, but we're going to be very selective given we do believe the disruption is coming for some of those companies. So we want to be very selective in that part of the market. But which we retain pretty good exposure to tech as well. We're just being very selective. SAP is a

good example we've already talked about. We're looking at some of the data and analytics companies. This is another area that, as Casey had mentioned, being sold off. Some of these companies are not actually kind of pure data companies, they're benchmarking businesses with strong network effects around them, again, sold off indiscriminately.

[\(14:13\)](#):

So we'll be looking at some of those high quality companies who potentially to add to the portfolio. But overall selective exposure in tech, we still like it. We still want good exposure to the hyperscalers, for example. We still want good exposure to selective parts of software and of course to the semiconductor industry, which is a key beneficiary of this sell out as well. So big positions in TSMC, for example, continue to do well for us as well. And we think that will continue, they're beneficiary, under any of these scenarios people are talking about. So high quality companies, selective exposure to those artificially sold off in this exposure, but mostly seeking to those high quality companies who are going to compound their earnings with resilience through time.

Elisa Di Marco ([14:57](#)):

So yeah, the importance of bottom-up analysis I think is really shining through there and just understanding which companies we're seeing the most attractive valuations, but also those long-term opportunities that are less likely to be disrupted. I want to pivot the conversation now a little bit. So we've spent time now talking about our views and what's most likely to happen in markets, but now let's talk about the surprises. So in sporting terms, these are our long shots, they're unlikely to come in, could be the 50 to 100 to one odds, low probability of occurring, but high impact. So let's start, Casey, with the surprises to the downside.

Casey McLean ([15:36](#)):

Yeah, absolutely. We've always got to monitor these downside risks. They're always present and they can pop up when you least expect it. But one we have been thinking about, I guess, is what I call the private credit liquidity trap. Now if you think back over the last five or 10 years, the credit markets have changed, they've evolved and much more of the credit these days is being funded by these private credit institutions rather than the banks, and they've been particularly active in the mid-market companies in the US.

[\(16:08\)](#):

And there is a potential scenario where some of these mid-market companies, they're really being supported by this ample liquidity that they're getting and some of them fail if there's a slight turn down in growth. That could have a bit of a spiral effect that more of these private credit providers aren't able to meet redemptions and the contagion spreads, that their investors, the pension funds, the insurers, they're locked out of their capital. And the problem with that scenario is, unlike with the banks, the Fed doesn't really have a direct mechanism to bail out the private credit funds, and that leads to a freezing of credit markets for these medium-sized companies and they're the lifeblood. They're the key hiring mechanism in the US, and that triggers a pretty sharp and steep recession as well.

[\(16:59\)](#):

So yeah, again, this is not something we think it's going to happen, but it is a risk that you have to be aware of and even more so I think the linkage now also comes through in the AI sector given the amount of private credit, the amount of debt funding that's going to funding these massive investments we're having in data centers as well. So, yeah, there are cracks showing, but we'll have to monitor that.

Elisa Di Marco ([17:22](#)):

Yes, we'll watch out for the cockroaches, as Jamie Dimon says in the private credit space. What about your roughie, Alan?

Alan Pullen ([17:29](#)):

Well, I mean we've been talking a lot about GenAI and the driver it's been for markets this year and the AI trade in general. I was out late last year, there was a lot of talk about bubbles at that time, if we recall. Everybody's saying this AI is a bubble that's going to burst at some point. We were arguing a bit more nuance than that. We argued it wasn't a bubble because we do believe in the underlying transformational change that GenAI is going to bring, and we think that's going to create a lot of winners and a lot of value for a lot of people. So, yes, we saw a lot of CapEx go into that sector, but we're the view that it was not a bubble at that stage.

[\(18:06\)](#):

Now fast-forward again, and I think we've seen some big CapEx announcements coming from the hyperscalers and others. You continue to see a ramp in that AI trade and it's even started impacting the AI loser bucket that we've been talking about, with a lot of companies being pushed into that as if this is now a done deal and everybody knows where this is going. Well they don't. Really, there's still a great deal of uncertainty out there. And my roughie, this is in our base case, is that it's all unwinds at some point this year. We get towards the second half of the year, the returns on the AI CapEx is not what people are hoping for. Perhaps the models stall, perhaps there's a new DeepSeek moment.

[\(18:46\)](#):

We do believe that the model costs will continue to get cheaper and cheaper at times and that everybody has to start dramatically reassessing that potential CapEx growth requirement, as we look into 2027, of course. Markets are forward-looking. So my roughie is that we get a real heavy unwinding of this AI trade in the second half of this year, and you get some of those semiconductor players who have really benefited, like NVIDIA, significantly impacted halving perhaps in the second half of the year. Not our base case. Remember we're speculating here about what might happen. It's always interesting to think about. But that's one thing that could be coming into focus second half of the year as a surprise.

Elisa Di Marco ([19:28](#)):

All right, Alan and Casey, thanks for giving us the more negative surprises. What about on the positive side, Casey, what are you thinking about that could surprise to the upside?

Casey McLean ([19:39](#)):

Yeah, it's important to think about that as well. Equity markets generally go up and it pays to be optimistic over the long term. And I think one of the inverse scenario, I guess, to what Alan was talking about is something called perhaps the immaculate deflation scenario. And this is really where AI adoption moves from being this experimental testing ground where companies are just fiddling around at the edges to moving into exponential growth. And that's because they're really seeing productivity gains that they're flowing through at an unprecedented rate.

[\(20:16\)](#):

I mean the general thinking is when you get productivity growth, it trickles through to the economy really slowly. But AI has the potential to supercharge that. And what I think that would mean is inflation declines down to perhaps near zero and that forces central banks to slash rates, which is really positive for equity markets. At the same time, the productivity growth is going to show up in the growth rates and the margins of these companies accelerating their growth. And that there is scenario at the same time where wages stay stable because the amount of new job creation coming out of this growth and from the new industries offsets any job losses.

[\(21:01\)](#):

So it's this immaculate scenario where everything falls into place. And in that scenario I can see equity markets performing extremely well. You can do 20% in kind a normal year, why can't we do double or we'll triple that in the perfect scenario. Again, not a base case, but it would be great to see.

Elisa Di Marco (21:20):

That'll be very interesting to see that play out and if it could play out in that pace. I will be here watching for that outcome. Alan, what about yourself?

Alan Pullen (21:29):

I don't think I can top that one 56% growth for the year would be remarkable given where we're starting the year. But under that great AI future, it's not impossible, which is why it's important to think about these scenarios. I'm going to go more specific to the portfolio and just talk about what I think could be... Would this be a surprise here that we have kind of software as the best performing part of the portfolio for the remainder of the year? Now, I think this would be a surprise given where we are today. We're recording this in early February for everybody's calendars, and software started the year with down 20%, 25% in many high quality names.

(22:11):

So I think people would be quite surprised if we get to the end of the year and they find out that these companies are actually some of the best performing stocks over the remainder of the year. So that's going to be my somewhat surprise. I wouldn't be that surprised, given the level of fear that is in those stocks right now, but I think the market would be pretty surprised by that one.

Elisa Di Marco (22:29):

Well thanks for your predictions guys. We've noted them down and we'll check back in at the end of the year to see if any of the roughies came out to play. Okay, so just to wrap up today, our discussion, it's been very wide-ranging. Our base view is that market returns will be more moderate this year. The risks are a little bit more elevated. To close out, starting with you, Casey, what should investors be most mindful of when they're thinking about their own investment decisions in 2026 and overall a longer investment horizon?

Alan Pullen (23:01):

I think it's getting back to basics, really. It's sticking to your knitting, it's investing for the long term and not getting caught up into the hype. I think it's when you change your strategy and adjust to what the market is doing, the sentiment in the market, that's when you can come unstuck. For us, that means sticking to our philosophy and I think it rings true for our investors as well.

Casey McLean (23:25):

Yeah, so I'm going to agree completely with that. The markets are pushed around in the short term by greed and fear. We know that. We know that impacts people's psyche. People get scared when stocks are going down. They love it when stocks are soaring, but the fundamentals don't change that quickly. So it's really important as an investor, not a speculator, not a trader, as an investor, to think about the underlying fundamental strength of a company as competitive advantages. Yes, absolutely taking into account any potential disruption to those going forward, but then take a sensible view on valuation and invest for the long term.

(24:02):

And if you've got a high quality company that you are confident will perform through the cycle, don't get impacted by these short-term trends, neither the greed nor the fear, and invest for the long-term and you'll do fine.

Elisa Di Marco (24:14):

Some great insights there team. So patience, investing in fundamentals and investing for the long-term. Well big thank you, Casey and Alan, for your time today. And thank you for listening in and we look forward to hearing from you soon.

Host ([24:29](#)):

That was investment director, Elisa Di Marco, in discussion with portfolio managers, Alan Pullen and Casey McLean. We trust you've enjoyed this episode. For more information on previous episodes, visit MagellanInvestmentPartners.com/podcast where you can also sign up to receive our regular investment insights program. Thanks for listening.

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