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Earnings and the economy will tell the tale

Key points

- Rising estimates for earnings and GDP growth are supportive of more new highs in 2026.
- Policy uncertainty remains a headwind in the U.S., and could be accentuated by the coming midterm elections.
- We remain committed to equities but not over-committed.

The S&P 500 rose by a healthy 16% over the past 12 months. Japan's Topix and Canada's S&P/TSX Composite, as well as the UK and Europe MSCI indexes were all up by considerably more (see table). This despite the fact none of the latter have anything like the S&P 500's exposure to the market-leading, megacap AI stocks, and all are contending with significant trade upheavals.

All the indexes are trading at price-to-earnings (P/E) ratios well above their long-term averages. That said, the S&P 500 is nowhere near as richly valued in relation to earnings as it

was in 2000 through the last upward leg of the tech bubble.

We expect all the major equity indexes will post further new highs in 2026. Most, including the S&P 500, should end the year higher than they were at the beginning. RBC Capital Markets, LLC Head of U.S. Equity Strategy Lori Calvasina draws on five different models to develop a year-end 2026 S&P 500 price target of 7,750—an advance of 13% over the 2025 ending value.

The principal underpinning to this target would be a similar percentage gain in S&P 500 earnings per share

Equity views

Region	Current
Global	=
United States	=
Canada	=
Continental Europe	=
United Kingdom	=
Asia (ex Japan)	=
Japan	=

+ Overweight; = Market Weight; – Underweight
Source - RBC Wealth Management

Percentage appreciation over 12 months to Jan. 30, 2026

	S&P 500 (U.S.)	S&P/TSX Composite (Canada)	MSCI Europe	MSCI UK	TOPIX (Japan)
In local currency	16%	29%	12%	18%	28%
In U.S. dollars	16%	38%	27%	30%	28%

Source - RBC Wealth Management, FactSet

Produced: Feb. 3, 2026, 12:17 ET; Disseminated: Feb. 3, 2026, 14:30 ET

All values in U.S. dollars and priced as of market close, Jan. 31, 2026 unless otherwise stated.

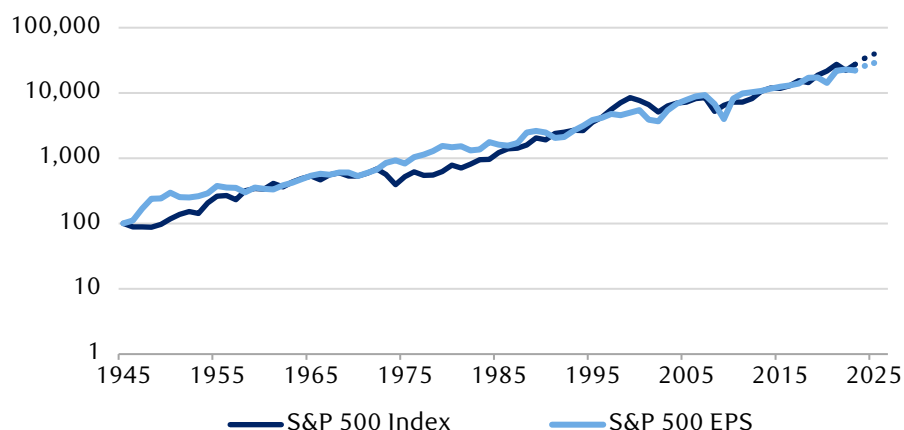
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S&P 500 earnings have kept pace with the index level

S&P 500 Index and EPS indexed to 100 at 1945 (log scale)



Over the long term, the index has appreciated (7.7% per annum) almost exactly as fast as earnings have grown (7.4% per annum). Dashed lines represent RBC estimates.

Source - RBC Wealth Management, FactSet, Bloomberg

(EPS) for the year. Consensus estimates for those earnings currently sit at \$313 per share, up 14% from 2025's estimated \$273 per share.

To make the 13% estimated upside for the index plausible, U.S. GDP would need to expand at a sufficient pace to produce the necessary above-average EPS growth. For some time, consensus estimates for 2026 GDP growth were mired in the stagnant 1% to 2% range. However, recently those estimates have begun to ratchet higher fueled by stronger-than-expected Q3 results and solid consumer spending data in Q4 (despite the government shutdown).

RBC Economics recently boosted its 2026 U.S. GDP growth projection to 2.4% (up from 1.6%). As we've noted here previously, in prior years where U.S. GDP growth landed in the 2.1% to 3.0% range the median S&P 500 return has been 11%–13%.

From where we stand today, not much has to change to make a GDP number north of 2% a likely outcome.

Fed policy acts with a lag. RBC

Economics forecasts no more rate cuts from the U.S. Federal Reserve this year. (The consensus is somewhat more optimistic.) But 175 basis points of rate cuts have already been put in place over the past 16

months. And we would note that monetary policy changes typically act with a lag of about a year on the economy. Right on schedule, the 100 basis points of cuts put in place back in Q4 2024 showed up as better-than-expected consumer spending growth in Q3 and Q4 this past year. And they'll likely go on having a stimulative effect in the first half of this year, while the 75 basis points of cuts made in late 2025 should show up as better economic activity in the latter half of this year.

No consumer heroics needed. The consumer backdrop looks mildly positive to us. The unemployment rate is steady, while layoffs and unemployment claims are trending lower. A majority of small businesses and CEOs of large companies surveyed by Chief Executive magazine and the National Federation of Independent Business are planning to hire more and raise compensation. They all report skilled/qualified workers are in short supply. Real consumer incomes should grow moderately, while an estimated boost of \$50 billion in tax refunds should give an assist to consumer spending in the first half. Bank lending standards on most types of consumer loans, including credit cards, are easing.

GLOBAL EQUITY

Capex looks solid. Both CEO and small business surveys reveal a growing proportion of businesses are planning to increase capital expenditures in the coming months. Reshoring—stimulated by tariff policy—spending on AI applications, and the data centre buildout continue to be in play.

Not all a bed of roses

However, there are a number of factors keeping the U.S. economic picture somewhat clouded. Consumers within the bottom half of household incomes are having trouble making ends meet. Rising utility rates are not playing well in an unusually cold winter while fueling a growing backlash against data centre construction. Power availability is already a constraint for those AI-based developments and is likely to be an even bigger headwind beyond 2026, in our view, as it will be difficult for grid additions to keep pace with the number of new data centres already announced.

The shortage of skilled workers is only getting worse. The CEO of Ford Motor Company has said he needs 6,000 highly skilled technicians in dealerships “tomorrow” and can’t find them. Commitments to build chip factories, especially those needed to establish the capacity to fabricate the most advanced chips required by AI, are being slowed or stymied by the dearth of specially skilled workers and the highly restricted ability to bring them in from abroad.

While the 250 CEOs polled in Chief Executive’s survey indicated they are going to hire more, pay more, and spend more, they are apparently doing so while feeling a growing sense of unease about the economy. The January reading of that publication’s CEO Confidence Index was notably weaker, and Chief Executive noted that it “marks the first time CEOs have begun a new year with such a sharp drop in sentiment.” Most CEOs surveyed cited the vagaries of U.S. federal government policy as the principal

concern weighing on their 2026 outlook.

Growth prospects encouraging elsewhere

European economies are benefitting from increased commitments to defense spending and energy security. More than 50% of the EU’s power generation now is delivered by low-cost renewables with more to come. Manufacturers everywhere are spending to lower costs as an offset to tariffs. Canada is part of the NATO defense buildup and has committed to fast-tracking a growing list of major developments including long-delayed mining projects, major additions to liquefied natural gas and port capacity, grid building initiatives, significant capacity expansions to existing oil pipelines, and probably one new greenfield pipeline.

All these non-U.S. projects have what we see as multiyear runways that speak to durable contributions to employment and GDP in those countries.

Midterm election volatility

As we noted here last month, “U.S. midterm election years have often experienced a noteworthy market pullback. At what point in the year those corrections have started and finished has been all over the map. However, the market rebound off the eventual lows has typically been quite energetic and frequently taken the indexes to new all-time highs.

“The probabilities favour both a pullback and a subsequent bullish upleg to new highs. However, markets and the economy are unaware of how they are ‘supposed’ to behave according to past experience. They can and do toss unexpected curveballs.”

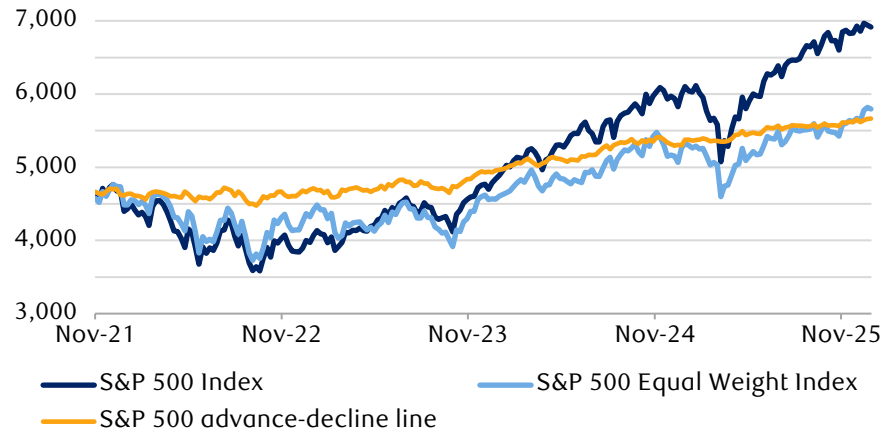
Market breadth remains in gear

In the case of the S&P 500, the majority of stocks are moving in the same direction as the index itself, as indicated by commensurate new highs for both the advance-decline

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‘New highs’ all around

It’s not just the megacap growth stocks; the majority of S&P 500 stocks have been moving higher for most of the past 39 months



Note: The advance-decline line is a series built over time from the difference in each day’s trading between the number of issues rising and those falling.

Source - RBC Wealth Management, FactSet, stockcharts.com; weekly data through 1/23/26

line and the unweighted version of the index (see chart above). In our opinion, this suggests the ultimate high-water mark for this bull market may still lie a fair way ahead since the majority of stocks have usually rolled over into downtrends several months before the index itself sets its final peak.

The same is true for other major equity markets where unweighted indexes are setting new highs alongside their capitalisation-weighted brethren.

Invested but watchful

We currently expect global stock markets to set more new highs over the remainder of this year. We also think it’s prudent to expect some potentially unnerving volatility along the way, as has typically been the case during U.S. midterm election years.

At some point during the year, investors will want to be assured 2027 too will bring more GDP and earnings growth. For our part, we think portfolios should remain committed to equities up to but not beyond an investor’s long-term targeted exposure.

Research resources

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