



**CROFT** FINANCIAL GROUP

MACRO-ECONOMIC RESEARCH

# The Golden Age?

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Richard N Croft, Chief Investment Officer

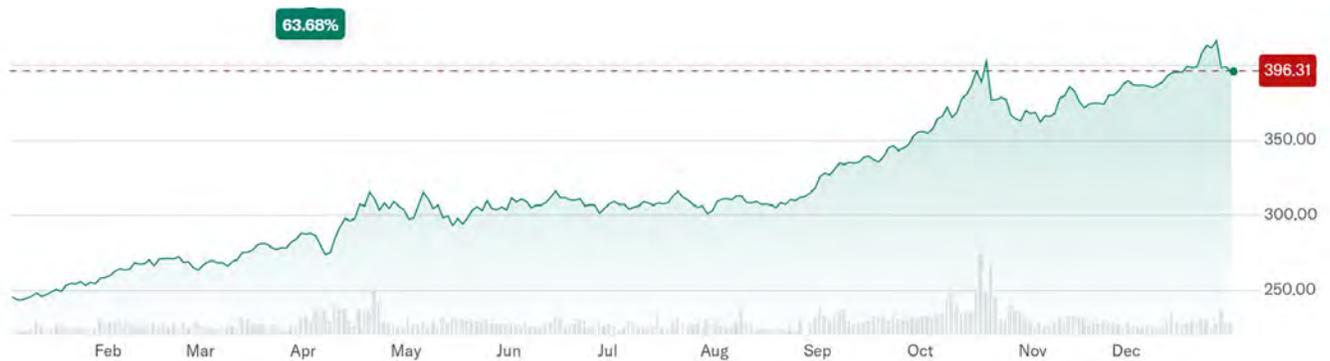
[rcroft@croftgroup.com](mailto:rcroft@croftgroup.com)

## THE GOLDEN AGE?

Calling 2025 a “good year” for gold would be a considerable understatement. It was more a full-blown victory parade. Up more than 60% year over year, cracking fifty all-time new highs in the process, gold is more expensive (inflation-adjusted) than at almost any moment in modern financial history. Not surprisingly, analysts are split about where gold goes from here; are we entering a new golden epoch, or is this just a breathless sprint before the metal face-plants?



### Performance During 2025 of iShares Gold ETF (Symbol: GLD)



But here’s where the plot thickens. Geopolitical sparks are flying, the US dollar is limping, and investors are stampeding into gold like it’s a door-crasher sale at Costco. The kicker is that central banks are doing the same thing. That almost never happens! Typically, central banks play the role of a shopkeeper, offloading their reserves to retail buyers, not joining them in the shopping frenzy. This odd coalition suggests that gold is morphing into a strategic shield for nations hedging against currency risk. If that narrative remains in 2026, central-bank demand could be entering a multi-year expansion.

### YTD 2025 performance of US Dollar Index (symbol: DXY)





The big unknown is whether gold can put on a 2026 encore worthy of its 2025 performance. Expectations vary widely, but several analysts think it may settle into a US \$4,500 to US \$5,000 per-ounce trading range, with an outside chance that bullish sentiment could push the upside limits of US \$5,500.

### **Motivating Factors**

The primary driver behind gold's surge has been geopolitical and economic uncertainty. Ongoing global conflicts and trade frictions have steered investors toward safe-haven assets, while mounting concerns over slowing growth and fragile supply chains have further amplified gold's appeal.

Monetary policy and interest rates have been another key driver of gold's rally. Anticipation of further US rate cuts in 2026 has buoyed prices, as lower real interest rates reduce the opportunity cost of holding non-yielding assets such as gold.

At the same time, a weaker US dollar has enhanced gold's appeal to international buyers, with dollar softness historically linked to stronger demand. Adding to this momentum, speculative flows surged as prices broke through key resistance levels, reinforcing bullish sentiment across the market.

Central banks have increased their appetite for gold, shifting reserves away from the US dollar. For some (think the countries within the G-7) the objective is to relieve the impact from a weakening US dollar, for others (think the BRIC's consortium) it is to remove the risk of having your foreign reserves frozen by the US.

Individual and institutional investors are hedging their portfolios against tariff-induced inflation by diversifying into Exchange Traded Funds (ETFs) and other gold-linked instruments. Adding to this momentum, strong jewelry and industrial demand, particularly across Asia, has provided additional support for the market.

### **Our 2026 Forecast for Gold**

We see three potential scenarios unfolding in 2026:

1. **Modest Correction** – Gold eases lower if global growth stabilizes.
2. **Crisis-Driven Rally** – Renewed geopolitical or economic shocks propel prices sharply higher.
3. **Reflation Cap** – Stronger growth and reflationary trends limit gold's upside.

Ironically, the greatest threat to gold's momentum in 2026 may be economic stability itself. A rebound in global growth could diminish safe-haven demand, while stronger equity markets might draw capital away from gold.

Another consideration is the cost-of-carry debate: rising real interest rates challenge the rationale for holding assets that produce no income. Even if rates remain steady, any hawkish signals from central banks could trigger sentiment-driven corrections in the price of gold. We doubt that would enter the discussion until the second half of the year.

Additionally, after gold's impressive 60% rally in 2025, some investors may choose to lock in profits by unwinding speculative positions. A recovery in the US dollar would add further pressure, potentially curbing gold's upside.

### **Portfolio Strategy 2026**

Regardless of where gold goes from here, one thing is certain, it is the essential hedge against uncertainty. Historically, gold can stabilize portfolios during periods of heightened volatility. And as we have noted in the past, option strategies can monetize volatility allowing gold holdings to generate cash flow.

We will continue to monitor central banks closely for any signs of policy shifts which we think is a real possibility. While most analysts believe that interest rates will decline in the first quarter of 2026 and then stabilize for the remainder of the year, that outlook is increasingly being challenged. A growing number of economists argue that, given persistent inflationary pressures, central banks may be forced to raise rates at some point in 2026.

What remains consistent, however, is the structural demand for gold from central banks and emerging markets. The BRICs nations have been pursuing the long-term goal of establishing a unified currency capable of challenging the US dollar's dominance as the global reserve currency.

Achieving reserve currency status is a formidable challenge, as US foreign exchange markets provide unmatched depth and liquidity - qualities essential for global acceptance. In practical terms, Brazil, Russia, India, and China remain at least a decade away from developing anything comparable.

In the meantime, as the BRIC consortium works to build the infrastructure needed to support such liquidity, they are likely to emphasize the optics of reserve credibility by advancing a currency backed by gold. This dynamic reinforces the expectation that major central banks will continue accumulating gold well into the foreseeable future.

### **Conclusion**

Gold's remarkable rally in 2025 was the product of a perfect storm - geopolitical uncertainty, monetary easing, and surging investor demand. As we enter 2026, the outlook remains nuanced: most forecasts point to stability near current levels, with modest upside potential of 10% or more should risks intensify.

Still, caution is warranted, as a rebound in economic growth, rising interest rates, or profit-taking could spark corrections.

Ultimately, gold's enduring strength lies in its role as a diversifier, a source of resilience, and a hedge against the unknown. In a world defined by volatility, it continues to shine both as a financial asset and as a timeless symbol of stability.

## CANADIAN BANKS REBOUND

Canada's banks have a reputation for being the "responsible adults" in the world of global finance. Canadian bankers believe in the nobility of risk aversion, showing up in starched shirts, button-down collars, and trousers so secure they're held up by a belt and suspenders.



While it may not be the Manhattan power suite vibe, for Canadian banks, it seems to work. At least based on last quarter's earnings parade, where the big six Canadian banks showed off their well-endowed capital adequacy ratios, better than expected profits, stronger net interest margins and a return on equity that would make even the Gordon Gekko's of the world blush. Translation: Canadian banks are making oodles of money while pretending not to enjoy it.

As we move into 2026, Canadian banks are positioned to maintain solid financial profiles, but they must navigate a complex macro-economic environment of shifting monetary policy, consumer leverage, and global uncertainties, all of which are beyond their control.

From the Canadian perspective, the minutes from the Bank of Canada's (BOC) December policy meeting made it clear that Canada's present yield curve aligns with what it describes as the Goldilocks framework - balanced conditions that are neither overly restrictive nor excessively slack.

The US yield curve paints a different picture. Economists are mixed in terms of where they think US rates will settle during 2026. Some argue that additional cuts are likely, especially with the U.S. administration preparing to appoint a new Federal Reserve chair who is expected to push for more aggressive easing in the name of supporting economic growth. But that creates its own set of problems.

Politically motivated rate cuts tend to trigger unintended consequences. Easing policy at the short end of the yield curve - central banks' primary arena - can ignite fears of future inflation. That, in turn, can push up mid-to-longer-term rates that matter most to consumers, driving up the cost of mortgages (and by extension rent), car loans, and financing for major durable goods. Those unintended consequences



haven't gone unnoticed, as an expanding chorus of US economists are warning that rates may climb in 2026, albeit primarily in the second half of the year.

For Canadian consumers, any talk of rate hikes inevitably circles back to the elephant in the room... leverage. If debt were an Olympic event, Canadians would sweep the podium. According to recent data, Canadian consumers have the highest household debt-to-GDP ratio among G-7 countries. While much of this debt is tied to "secured" mortgages, the risk is clear: elevated leverage leaves credit quality vulnerable, especially if housing prices take a serious tumble.

Fitch<sup>1</sup> Ratings has flagged geopolitical trade tensions as a looming challenge for Canadian banks in 2026. Ongoing uncertainty around tariffs, supply chains, and global trade could weigh on corporate lending and investment banking revenues. The wildcard is whether Canadian trade negotiators can navigate President Trump's unpredictable, "madman-style" bargaining tactics and manage to reset USMCA (or CUSMA) to lock in tariff stability. That outcome is, at best, a coin toss - but if successful, it would be a clear win for Canadian banks and the broader economy.

One of the most striking developments has been the Big Six banks' embrace of artificial intelligence. Their ongoing investments in fintech and digital platforms are designed to boost efficiency and, ideally, deepen customer engagement. The results were on display as all six banks reported improvements in return-on-equity.

Royal Bank stood out. Since acquiring HSBC's Canadian assets, it has steadily expanded its profit margin. In the latest earnings call, management revealed that they are ahead of schedule - posting a 16% margin as they push toward their target of 17%. That is a remarkable achievement, particularly when viewed within the context of global peers. In the US for example, J.P. Morgan Chase has long been the benchmark, posting a 15% return on equity.

Also of note was the continuing trend towards diversification into US and international markets. As the international heavyweight among the Big Six, Bank of Nova Scotia (symbol: BNS) has long benefited from its international reach, particularly through its strong presence in Latin America. More recently, however, BNS has been trimming some of its weaker Latin American holdings while steadily expanding its footprint in the United States.

The Big Six banks also hold a commanding position in Canada's wealth management industry, although their sheer scale often makes it challenging to foster deep, personal relationships with clients. Fortunately, this gap creates opportunities for smaller players to serve clients with a range of financial tools (insurance, tax preparation, estate and retirement planning), which are critical given the demand

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<sup>1</sup> Fitch Ratings is a major global credit rating agency, widely known as one of the "Big Three" alongside Moody's and S&P Global Ratings.



for personalized advisory services driven by the multi-trillion-dollar wealth transfer expected to move to the next generation over the coming decade.

### **Risks to Watch**

Sticky inflation could force more aggressive rate hikes, raising credit risks. Any sharp downturn in the housing market would test banks' resilience. Trade disputes or geopolitical crises could disrupt capital flows.

### **Conclusion**

The outlook for Canadian banks through 2026 is one of cautious resilience. Strong capital positions and stable profitability provide a buffer against challenges, but consumer debt, housing market risks, and potential rate hikes remain key vulnerabilities. Regulatory oversight will continue to reinforce stability, while opportunities in digital banking and wealth management offer growth potential. In short: Canada's banks are ready for 2026, but it's going to feel less like smooth sailing and more like curling on thin ice.

## **THE GHOSTS OF CHRISTMAS PAST**

As we enter 2026, it's time to take stock of the year that was in financial markets. Much like the Ghost of Christmas Past from Charles Dickens' *A Christmas Carol*, we find ourselves looking back at the twists and turns that shaped investor sentiment over the past twelve months.

What a ride it's been. From political upheavals and trade tensions to shifting central bank policies and the relentless buzz around artificial intelligence, markets faced what often felt like constant mayhem. Hardly the backdrop that would support the better-than-expected performance that defined 2025.

In our mind one theme stands out: confidence. Market participants, in what can only be described as an alchemy of the optimist moment, chose to look past the noise be it polarizing social media posts, political grandstanding, questionable leadership appointments in key US departments, or the constant drumbeat of tariff threats and corruption headlines.

Conventional wisdom and historical precedent both warn that ignoring these risks can be perilous. That's probably why so many analysts jumped on the valuation bandwagon, arguing that equity prices were "ahead of their skis." Optimists countered with a different historical lesson: "markets climb a wall of worry." The reality is that market turbulence often creates opportunity, giving investors a chance to build positions in out-of-favour sectors and lean into emerging technologies poised to reshape entire industries.

Remarkably, that optimism paid off. Equities held firm, bonds stabilized, and investors who stayed on the course were rewarded. In a year defined by uncertainty, resilience became the market’s defining trait. Ebenezer Scrooge would have been proud!

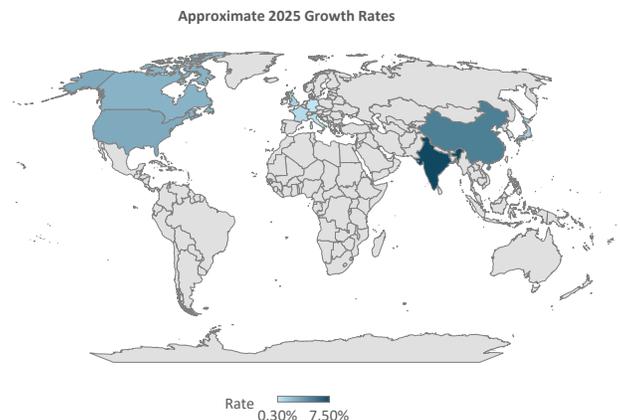
## The Global Economy

The global economy provided a passable foundation for financial markets as major industrialized economies (including China and India) delivered steady growth averaging about 3.0% worldwide. While that figure may not sound spectacular – especially when including China and India in the mix - it was enough to keep investor confidence intact and momentum alive.

In the United States, deregulation and resilient consumer demand gave the economy a meaningful lift, allowing equities to build on 2024’s above-trend performance. Across the Atlantic, the major European economies benefited from a “K-shaped”<sup>2</sup> recovery where industrial output, powered by high-end exporters such as Chanel, Hugo Boss, and Rolls-Royce, exerted an outsized influence on GDP and, in turn, helped fuel strong market performance despite lingering political risks.

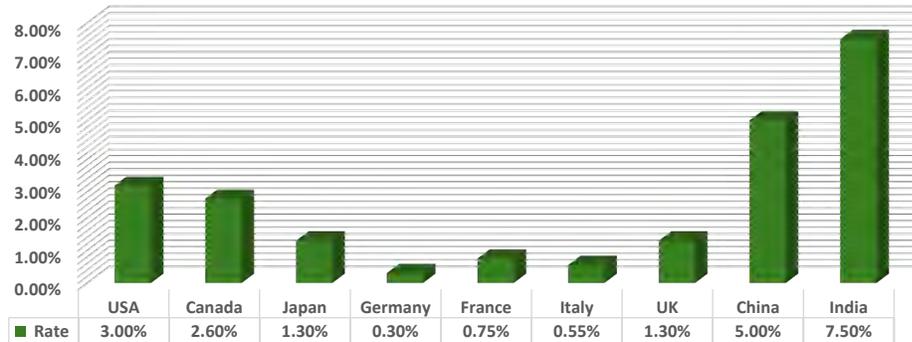
The Asia Pacific Basin delivered a more nuanced picture. India, with 2025 GDP growth of 7.5%, and China at 5.0%, continued to advance despite ongoing trade tensions. China, however, faces a series of significant headwinds ranging from weak productivity growth and industrial overcapacity to demographic pressures, softening domestic demand, and fragile investor and consumer confidence stemming from the prolonged property-sector downturn.

Although the European Union, Japan, and the United Kingdom reported comparatively modest outcomes (see chart), their growth was nonetheless sufficient to fuel above trend performance across European equity markets. As we reflect on 2025, the question naturally arises: was the global economic trajectory a glass half full or half empty? By historical standards, growth may look merely passable. Yet, considering the ruptures in global trade and supply chains, the outcome was better than many expected.



<sup>2</sup> A K-shaped recovery describes an economic rebound where different groups, sectors, or regions recover at very different speeds — some rising sharply while others continue to decline. Picture the letter K: one arm goes up, the other goes down. Segments of the economy on the rise include high-income households, technology and financial sectors, large corporations and luxury goods and premium exporters. Segments in a downtrend (lower arm of the “K”) include lower income households, small businesses, service industries (hospitality, travel, retail), and regions of the economy reliant on slower-growing sectors.

## 2025 GDP Growth Major Economies



This resilience provided the fuel to sustain investor confidence and deliver positive - if uneven - returns across equity markets worldwide. The divergence in performance among major indices served as a timely reminder that diversification isn't just a strategy, it's a necessity.

### Political Gamesmanship

The dominant storyline in 2025 was politics, with U.S. President Donald Trump at the forefront. His April 2<sup>nd</sup> "liberation day" tariff package strained relationships that were decades in the making. Disputes with China and the European Union introduced a degree of uncertainty that made long-term planning nearly impossible. Then, just as a bit of clarity appeared on the horizon, multinational firms were blindsided by sudden policy shifts. And yet as they often do, financial markets adapted.

Central banks were another key influence. The Federal Reserve kept interest rates high through much of the year, determined to keep inflation in check. But by late 2025, a series of rate cuts sparked rallies across equities and bonds. Canada's central bank took a slightly different path, cutting rates in March before pausing mid-year, reflecting its own inflationary pressures. Europe's policymakers walked a tightrope, balancing energy price shocks with growth concerns.

### THE GHOSTS OF CHRISTMAS PRESENT

Equity markets told a story of resilience. The S&P 500 finished the year up by about 16.39%, despite a mid-year correction that rattled investors. The Dow Jones, buoyed by industrial and energy stocks, posted solid gains as well. The Nasdaq was more volatile, reflecting both the excitement and the skepticism surrounding A.I.-driven companies. Investors couldn't get enough of the "Magnificent Seven" tech giants, but questions about overinvestment in A.I. infrastructure kept valuations in check.

Outside the US, international equities quietly stole the spotlight. European markets delivered double-digit returns, while Japan, India and China impressed with strong growth. The lesson was clear: diversification mattered in 2025, and those who looked beyond US borders were rewarded.

Country / Sector	Tracking Index	2025 Return	Underlying ETF
<b>USA Broad</b>	<b>S&amp;P 500</b>	16.39%	SPDR S&P 500 Depository Receipts (SPY)
<b>USA Technology</b>	<b>Nasdaq 100</b>	20.36%	Invesco QQQ Trust (QQQ)
<b>China Broad</b>	<b>MSCI China Index</b>	27.94%	iShares MSCI China Index ETF (MCHI)
<b>China Technology</b>	<b>MSCI China Internet Index</b>	16.97%	KraneShares CSI China Internet ETF (KWEB)
<b>Canada</b>	<b>S&amp;P TSX Composite Index</b>	25.98%	iShares S&P/TSX 60 Index Fund (XIU)
<b>EAFE</b>	<b>MSCI EAFE Index</b>	27.01%	iShares MSCI EAFE ETF (EFA)
<b>Emerging Markets</b>	<b>MSCI Emerging Markets</b>	28.75%	iShares Emerging Markets ETF (EEM)

Commodities added their own drama. Gold surged acting as a safe-haven whenever geopolitical uncertainty spiked. Oil prices swung between US \$60 and US \$90 a barrel, depending on the level of US sanctions. Agricultural commodities like wheat and soy were ravaged by tit-for-tat tariffs and climate events, providing additional evidence that food markets remain vulnerable to both politics and nature.

Bond markets were equally eventful. US Treasury yields fluctuated between 3.5% and 4.5%, mirroring inflation data and Fed signals. Corporate bonds looked attractive, with narrowing spreads suggesting investors were confident in credit quality.

But the big story centered on the currency markets as excessive tariffs pressured the US dollar. Nowhere was that more evident than in the performance of the Canadian dollar. The Loonie's 2025 performance against the US dollar looked like a version of a Texas two-step. It began the year on its' back foot, having fallen nearly 8% in 2024 to a two-decade low of US \$0.694. However, as 2025 progressed, the Canadian dollar staged a notable rebound, supported largely by a broad depreciation in the U.S. dollar and improving sentiment around Canada's macroeconomic outlook. By mid-year, the Canadian dollar had recovered a meaningful portion of its earlier losses, and analysts expect it to remain relatively stable through 2026.

Another defining feature of 2025 was the surge in new investment products. Exchange-traded funds (ETFs) reached unprecedented scale, with a record number of launches across the industry. Leveraged single-stock ETFs and individual stock covered call ETFs captured significant attention. Thematic ETFs tied to A.I., clean energy, and cybersecurity also gained a following. At the same time, private equity and venture capital committed billions to A.I. startups, wagering that the technology would reshape entire sectors.



Retail investors navigated their own set of challenges. Canadian households continue to grapple with high debt to equity ratios although economists noted modest improvement in savings rates by the latter half of 2025.

The lessons of 2025 were clear. At the top of the list was a simple truth: resilience pays. Investors who maintained their positions despite bouts of volatility ended 2025 with positive returns. Diversification matters: Canadian and international equities outperformed U.S. benchmarks, reinforcing the value of global exposure. Innovation created opportunity and risk. The increasingly complex and fast-evolving landscape in A.I. and ETF design demand a higher level of scrutiny. And finally, central bank policy decisions and trade developments shaped market sentiment and reminded investors that markets don't function in a vacuum.

Ultimately, 2025 was a year of contrasts - volatility and resilience, innovation and caution, geopolitical tension and global opportunity. It demonstrated the adaptability of financial markets and their capacity to absorb shocks while continuing to move forward.

## THE GHOSTS OF CHRISTMAS FUTURE

What we know is that 2025 was a year when virtually everyone, everywhere, made money. Had you downed a few celebratory cocktails on New Year's Day 2025, tossed darts at a world map, and bought stocks wherever they landed, odds are you would have come out ahead. Major global equity markets delivered double-digit gains, gold surged 63.68%, and silver more than doubled. By any measure, 2025 was extraordinary, not just for its above-average returns, but for the breadth and speed with which they materialized.

Naturally, the question investors must ask is whether markets can deliver an encore in 2026. Opinions vary, but many analysts remain optimistic. Across nine major U.S. investment banks, the consensus forecast calls for the S&P 500 to post returns exceeding 10%.

Several forces underpin this bullishness. The frenzy surrounding artificial intelligence remains front and center, not only for the hyper-scalers driving the technology, but also for the ecosystem supporting them, from semiconductor manufacturers to data-center builders to the utilities powering these massive operations.

Macro-economic conditions are expected to provide additional lift. Lower interest rates and softer oil prices should bolster both consumer spending and corporate balance sheets. Meanwhile, the tax cuts embedded in Trump's One Big Beautiful Bill Act, that come into effect on January 1<sup>st</sup>, including accelerated write-offs for business investment, are poised to support equity valuations.



In a classic feedback loop, rising stock prices would amplify the wealth effect, encouraging further spending and investment.

Such enthusiastic projections might tempt one to set caution aside. While 2025 made everyone feel like a commercial genius, financial markets have a wicked sense of humor. The moment you start thinking nothing can go wrong is usually the moment when markets blindside you.

Bearing in mind that a little caution is self-preservation, there are reasons to question the enthusiastic hyperbole emanating from the analysts on Wall and Bay Street. A strong case for maintaining some caution as we head into 2026 lies in valuations.

US stock prices appear elevated, a fact underscored by Warren Buffet's Berkshire Hathaway amassing over US \$350 billion in cash ready to strike when valuations cool. Canadian equities are showing similar signs of upward pressure. Not irrational exuberance but something close enough to make you check the exits.

Valuation is a slippery beast. You can dress it up with all kinds of subjective arguments: market position, competitive moats, industry buzz... but the cleanest test is brutally simple: compare what a company is worth to what it sells. That's the beauty of the price-to-sales ratio. No accounting magic, no glossy narratives, just hard numbers you can stack against decades of history.

When you look at North American valuations, the price-to-sales ratio is at its highest level in at least twenty years. Other Benjamin Graham valuation yardsticks such as price-to-earnings, price-to-book and the equity risk premiums tell a similar story. Not to put too fine a point on it, but FOMO (fear of missing out) is alive and well, and investors are paying up to participate.

At its core, FOMO is just momentum dressed up as urgency which is the belief that the path of least resistance is usually the one already in motion. That mindset goes a long way toward explaining the gap between current valuations and the underlying fundamentals.

If markets keep following the path of least resistance, most of the gains will likely come from a tight cluster of mega-tech giants. Momentum traders will have to buy into the hype and overlook the uncertainty around whether hyper-scalers can generate sufficient revenue to justify today's spending spree. If AI truly transforms society, as its champions insist, that path points upward. If it ends up looking more like the short-lived virtual-reality craze from a few years back, well... not so much.

Finding the sweet spot between promise and outcome is the financial equivalent of catching a falling soufflé. Talk to experts and the potential payoff looks more like a coin toss than a foregone conclusion. A July research report by MIT researchers noted that 95% of organizations do not see any or are seeing



limited returns on their A.I. investments. A few weeks later, Wharton researchers found that 75% of companies were earning positive returns from their generative-A.I. projects. Go figure!

We think a more useful approach is to follow the money. If we take the economic promise of A.I. at face value, its core contribution is greater efficiency and higher productivity. In practical terms, productivity comes down to how much a single employee contributes to the company's bottom line. This can be accomplished by calculating the company's profit relative to the number of people it employs. The objective is to examine specific trends which means that current data should be viewed through the lens of historical patterns.

To see this in action, consider Meta Platforms (META), a company that has aggressively deployed A.I. across its business lines. Meta's net income per employee has risen steadily since 2015, apart from a temporary decline in 2022 and 2023 tied to Meta's metaverse initiative. The broader trend, however, shows a clear and sustained increase in economic output per worker.

While we'd likely see a similar pattern if we analyzed the other major hyper-scalers, the efficiency gains they achieve through A.I. are relatively modest compared with the transformative impact A.I. can have on smaller private companies. Hard data is limited, but there is growing anecdotal evidence suggesting that A.I. delivers, or at least has the potential, to deliver meaningful advantages when integrated into mission-critical applications.

We draw attention to the 25% sell-off in Constellation Software (CSU) during 2025. CSU is a vertically integrated acquirer of software businesses that provide mission-critical tools to public - and private-sector clients. The decline reflects growing investor concern that A.I. systems could replace portions of this mission-critical software stack at a significantly lower cost.

While we accept the premise that A.I. is transformative, it's far less obvious who - if anyone - will walk away with *outsized* gains. That's the sticking point; "outsized" is doing the heavy lifting here, as many of A.I.'s biggest players are brushing up against the law of large numbers. How much upside is really left?

### **Looking Beyond A.I.**

In our view, we think 2026 will be a time to look beyond A.I. and see where a wider market lens might lead. Think about other sectors that should benefit from our list of macro-economic tailwinds. Lower US interest rates should stimulate economic activity which would be good for US money center banks and more importantly, for the big-six Canadian banks. We should also see a surge in IPOs through 2026, as many private companies will look to provide exit packages for their angel investors.

Lower oil prices would provide some punch to consumer spending and provide the Trump administration with a welcome economic talking point. That is likely one of the reasons the US military is flexing its

muscle off the coast of Venezuela. An invasion that leads to the ouster of Venezuelan President Nicholas Maduro would put one of the world's richest oil reserves within reach. More importantly, Venezuelan crude is similar in composition to reserves in the Canadian oilsands, and US West Coast refineries could be adapted to process it with relative ease.

If you're confused about 2026, you're in good company. We see 2026 shaping up as a cautionary tale in which A.I. still dominates the spotlight, but with less blind enthusiasm and more aggressive scrutiny. We expect investors to broaden their exposure to other sectors and along that line, we suspect financials will lead the way.

In sum, we believe the positives outweigh the negatives and that those positive factors could be, to borrow a phrase from Jeff Silbar and Larry Henley (and popularized by Bette Midler), "the wind beneath our wings" carting markets to another year of double-digit gains.

But as with any forecast it comes with the accuracy of a weather app in a hurricane. Which is to say, never enter the game without a backup plan... preferably one that works.

## INTEREST-RATE THEORY MEETS MORTGAGE-RATE REALITY

Since mid-2024, the Bank of Canada has slashed its benchmark rate by almost three full points. Mortgage rates, however, have reacted with the speed and grace of a sleepy sloth... dropping by less than a third of that before throwing in the towel.

The story is no different south of the border. The Fed cut rates by 1.75% in 2025, and mortgage rates have responded with a polite half-step downward, as if to say, "There, we did something."

Cue the closing credits! From here, we suspect that mortgage rates will remain at or close to current levels, and there is an outside chance mortgage rates could rise at some point in 2026, because apparently, gravity is optional in the mortgage universe.

Ordinarily, when central banks cut interest rates, the rest of the financial system politely follows along. But lately, "ordinary" has packed its bags and left the building. From the central-bank vantage point, we've been living in a long-running episode of *Stranger Things*, minus the Demogorgon but with just as much confusion.

For decades, Western central banks had a simple two-part mission: keeping inflation low and employment high. But after the inflationary trauma of the 1970s, central bankers focused their attention



"We can mortgage your future for a very attractive low interest rate."



on inflation and avoided reading the want ads much like someone who once burned their hand on a stove and now refuses to go near the kitchen. The theory was that low inflation would magically produce a healthy economy, like a macro-economic multivitamin.

Central bankers had such a single-minded obsession about how to prop up economic growth that inflation got demoted to a part-time job. When inflation started creeping back a few years ago, the Fed brushed it off as “transitory,” the economic equivalent of saying, “It’s just a phase.” Fast forward to the last year of Biden’s Presidency and the first year of the Trump 47 run and “transitory” has become synonymous with “famous last words of central bankers.” We think of it as the short form of “don’t worry about it until you absolutely should.” That watershed moment came about when voters realized their grocery bills were stuck in the stratosphere and decided it was time to reinstate Trump 47.

Meanwhile, investors and governments had grown so addicted to cheap money that they behaved as if interest rates would stay low forever providing a cosmic all-you-can-eat buffet of easy credit. Borrowing soared, and today public and private debt across most of the major industrialized countries are at levels that make previous peaks at the ski slope look like cute little practice runs.

Central banks used interest rates to counter whatever mood governments were in. If governments were spending freely, central bankers would hike rates to siphon money back out of the system. After all, nothing cools an overheated economy like making everyone suddenly very interested in paying down their credit cards.

When governments tightened their belts – something that no longer appears on the government’s finance menu - central banks would reward them with lower rates, letting consumers and businesses borrow cheaply and feel good about life again. And through the ’80s and ’90s, this arrangement worked surprisingly well, like a sitcom marriage that somehow never got cancelled.

Then came the 2008 crash, which tossed all those assumptions into a woodchipper. Inflation collapsed, central banks slashed rates, and the economy responded with all the enthusiasm of a cat being asked to take a bath. So central bankers turned to new tools most notably quantitative easing, which is essentially the monetary equivalent of saying, “Fine, I’ll just throw money directly at the problem.”

QE was controversial from the start, but for a while it seemed to do the trick, helping economies crawl out of recession without immediately igniting inflation. But the real legacy is psychological: just as one generation of central bankers was scarred by the stagflation of the 1970s, today’s policymakers carry the emotional baggage of the 2008 crisis, when the global economy looked like it was auditioning for the role of “systemic collapse.”

Which brings us back to mortgage rates. We're now being reminded – without the benefit of a classic Canadian “I’m sorry” – that while central banks control short-term rates, mid and long-term rates on which mortgages are priced, are the domain of the bond market.

As Western governments pile on debt like it's a competitive sport, bond investors (pensions, hedge funds, and other professional buzzkills) are demanding higher returns. And since central banks seem less panicked about inflation these days, bond buyers are guarding against its comeback by asking for even higher interest rates. It's basically financial déjà vu, but with more spreadsheets.

Unless central banks decide to revive quantitative easing and start buying bonds at prices no sane investor would accept - a move most of them now treat like a bad tattoo from their youth - they can't force long-term rates down.

Borrowers could switch to variable-rate loans to take advantage of cheaper short-term credit. But doing so means accepting the risk of unpredictable interest rate adjustments. Several G-7 treasuries are taking a similar gamble by issuing short-term debt to keep borrowing costs down. Think of it as the financial equivalent of ditching your fixed-rate mortgage for a variable one because... “what's the worst that could happen?”

In this setup, threading the needle between best- and worst-case outcomes means exposing taxpayers to higher rates next year when today's debt rolls over. And that, we might add, is precisely what bond investors are betting on. It's the fiscal equivalent of scheduling your vacation during hurricane season and hoping for sunshine.

Hoping to tilt the playing field, the administration is pressing the Federal Reserve to cut rates aggressively in the first half of 2026. With the US Treasury leaning heavily on short-term borrowing, the supply of long-term bonds should remain tight, theoretically pushing prices up and long-term yields down. At least that's the theory.

The reality is that mid- and long-term yields are rising while the U.S. dollar weakens as global investors quietly drift toward the exits. Just goes to show... even the United States government can't strong-arm the bond market indefinitely.