CORBETT ROAD
CAPITAL MANAGEMENT

BARNES DENNIG
Private Wealth Management

MARKET MUSINGS

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OUR 2026 OUTLOOK

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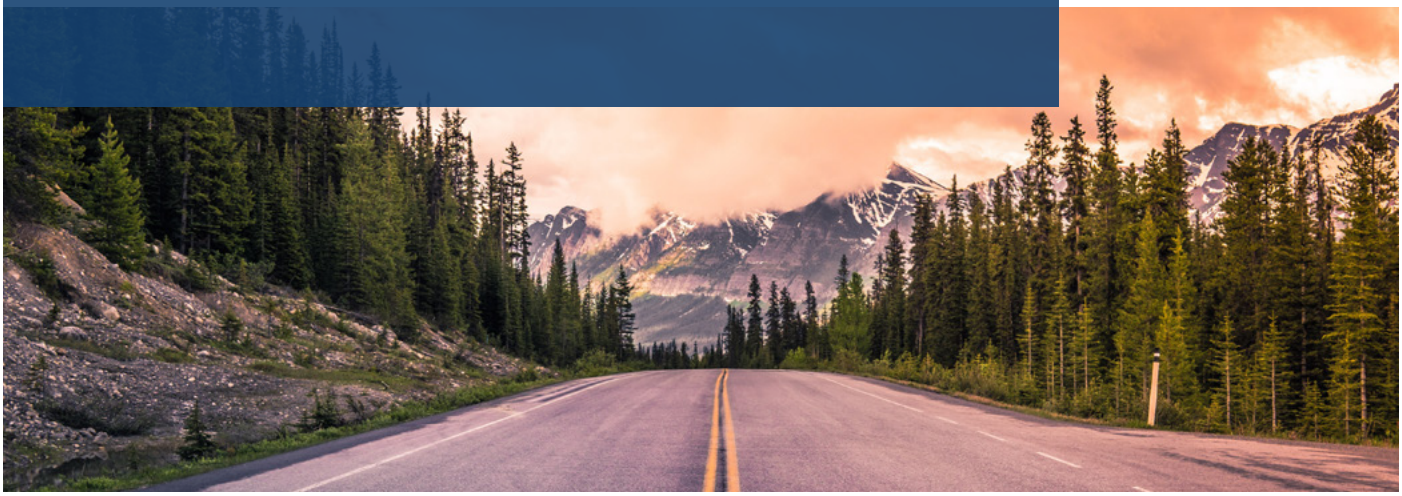

SUMMARY

- Our base case for 2026 is no recession. Accommodative monetary policy is set to deepen via Fed rate cuts, a dynamic further reinforced by fiscal stimulus to sustain economic momentum. While short-term volatility is possible, the combination of rate cuts, a stabilizing labor market, and continued economic resilience provides a constructive backdrop for markets.
- The incoming Fed chair will take office amid stubborn inflation, liquidity strains, and widening deficits, even as markets expect a more dovish policy stance. History suggests yields often rise after chair transitions, but subdued oil prices reduce the risk of an inflation reacceleration and give the Fed more room to ease if inflation remains in check.
- The S&P 500 has logged an 80% gain over the past three years. After comparable runs, forward returns have typically moderated and drawdowns have become more frequent. Absent a recession, the odds still favor positive returns, though the path is likely to be choppier.
- **macro**cast™ continues to suggest a low risk of a recessionary bear market. Our current **micro**cast™ signal remains at an aggressive allocation. Both models continue to suggest a positive environment for risk assets.

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See content within for additional information on the summary items discussed above

BOTH FISCAL AND MONETARY POLICY ARE SUPPORTIVE OF **THE ECONOMY HEADING INTO NEXT YEAR**

Our base case remains no recession in 2026. Absent an exogenous shock, the market environment tends to hinge on two factors: whether the economy is entering a recession and whether the Fed is tightening monetary policy. In our view, neither is likely next year.

On December 10, the Federal Reserve cut rates by 25 basis points, bringing the target range to 3.50%–3.75%. This marked the second reduction in as many months. As we noted last month, when the Fed eases policy with equities near all-time highs, subsequent one-year returns have historically been positive (table from SubuTrade):

S&P 500 after Rate Cut while the S&P is within 1% of an All-Time High

	1 Day Later	1 Week Later	2 Weeks Later	1 Month Later	2 Months Later	3 Months Later	6 Months Later	9 Months Later	1 Year Later
May 21, 1985	-0.57%	-1.03%	0.27%	-1.53%	2.48%	-0.82%	4.76%	17.18%	24.16%
December 17, 1985	-0.40%	-1.67%	-0.50%	-1.05%	5.60%	11.84%	16.30%	9.98%	18.70%
March 7, 1986	0.45%	4.87%	3.44%	3.52%	4.66%	8.91%	11.04%	12.18%	28.86%
April 21, 1986	-0.95%	-0.68%	-2.86%	-3.53%	-0.28%	-3.47%	-2.41%	10.05%	16.90%
July 26, 1989	1.17%	1.86%	2.63%	3.98%	1.83%	1.67%	-2.30%	-1.78%	5.63%
July 13, 1990	0.45%	-1.55%	-3.78%	-7.75%	-12.19%	-19.56%	-14.18%	3.56%	3.52%
March 8, 1991	-0.53%	-0.36%	-1.99%	-0.37%	0.95%	1.19%	3.77%	0.65%	7.87%
August 6, 1991	-0.02%	-0.26%	-2.86%	-0.38%	-2.40%	-0.09%	5.95%	6.71%	8.64%
July 6, 1995	0.43%	1.27%	-0.08%	0.89%	2.74%	4.96%	11.50%	18.39%	21.37%
January 31, 1996	0.38%	2.19%	3.08%	1.31%	2.78%	2.92%	0.62%	10.30%	21.46%
September 18, 2019	0.00%	-0.73%	-3.96%	-0.29%	3.78%	6.18%	-19.87%	3.61%	11.65%
October 30, 2019	-0.30%	0.98%	1.55%	3.09%	6.04%	5.87%	-7.09%	7.36%	8.64%
September 18, 2024	1.70%	1.85%	1.62%	3.97%	4.49%	7.70%	0.88%	7.24%	19.14%
November 7, 2024	0.38%	-0.40%	-0.41%	1.34%	-2.45%	1.60%	-1.45%	8.26%	14.62%
September 17, 2025	0.48%	0.57%	1.68%	0.44%	2.03%				
October 29, 2025	-0.99%	-1.37%	-0.58%	-0.60%					
December 10, 2025									
Average:	**0.10%**	**0.35%**	**-0.17%**	**0.19%**	**1.34%**	**2.06%**	**0.54%**	**8.12%**	**15.08%**
% Positive:	**56%**	**44%**	**44%**	**50%**	**73%**	**71%**	**57%**	**93%**	**100%**

The shorter-term picture has been more mixed. In the six-month period following similar cuts, several instances saw negative returns; most notably, 1990 and 2019, when stocks declined double digits. Both coincided with U.S. recessions—one driven by the oil shock around the Gulf War, the other by the pandemic. In each case, the market recovered over the subsequent six months.

Looking ahead to next year, the Fed is expected to continue cutting rates. While the exact number of cuts will depend on incoming data, even one or two additional cuts would provide incremental stimulus by lowering short-term borrowing costs. Futures markets currently price in two more reductions, though the next move is not expected until spring (table from DataTrek):

Number of Cuts	Fed Funds Rate	2026 FOMC Meetings Jan	Mar	Apr	Jun	Jul	Sep	Oct	Dec
0	3.50 - 3.75%	75.6%	50.5%	39.0%	18.6%	13.5%	9.3%	8.1%	6.9%
1	3.25 - 3.50%	24.4%	41.4%	43.5%	41.1%	34.9%	28.3%	25.8%	23.3%
2	3.00 - 3.25%	0.0%	8.1%	15.7%	30.2%	33.2%	33.7%	33.0%	32.0%
3	2.75 - 3.00%	0.0%	0.0%	1.8%	9.1%	14.9%	20.6%	22.3%	23.8%
4	2.50 - 2.75%	0.0%	0.0%	0.0%	1.0%	3.2%	6.8%	8.6%	10.6%
5	2.25 -2.50%	0.0%	0.0%	0.0%	0.0%	0.3%	1.2%	1.9%	2.9%
6	2.00 - 2.25%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	0.2%	0.5%

Green signifies highest probability scenario

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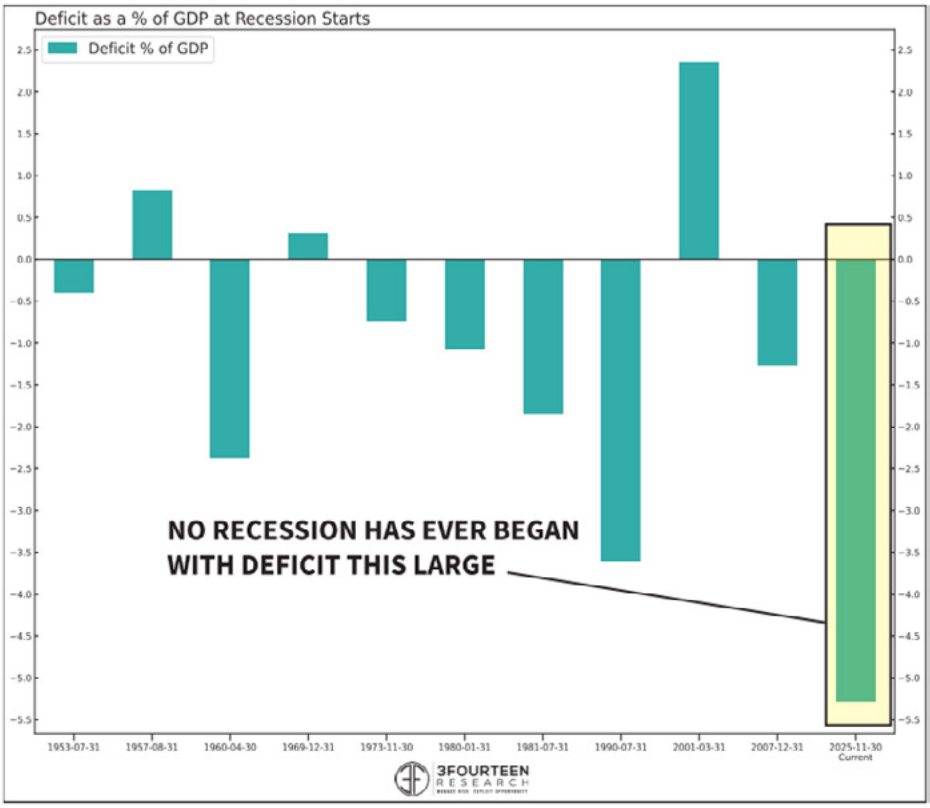
What about the labor market? If employment were to deteriorate meaningfully from here, the Fed would likely be forced to cut rates more aggressively. This would be an unwelcome development, as that pattern has often coincided with equity market stress.

Recent jobs data has been noisy, in part due to reporting disruptions from the government shutdown, and agencies are still working through the backlog. That said, there are signs the slowdown in employment growth seen over the past year may be stabilizing. Forward-looking, high-frequency indicators appear to be inflecting higher. If sustained, that would be a constructive signal for the broader economy (chart from Duality Research):

Further, fiscal policy is positioned to be meaningfully supportive next year. The federal deficit is currently more than 5% of GDP, a number that's expected to grow next year as tax cut extensions and new reductions from the "One Big Beautiful Bill Act" further expand the deficit. Historically, recessions have not occurred alongside that magnitude of fiscal stimulus (chart from 3Fourteen):



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For now, the combination of easing fiscal and monetary policy and a still-resilient economy provides a supportive backdrop for markets. That support should not be mistaken for a return to the ultra-accommodative regime of 2010–2020. The key difference is that inflation remains above target, leaving the policy path beyond the next few quarters far less certain.

A NEW FED CHAIR COULD FACE **STUBBORN INFLATION AND HIGHER RATES**

Later this month or in early 2026, the president will nominate a new Federal Reserve chair. If confirmed, the new chair would succeed Jerome Powell, who served eight years after his initial nomination by President Trump and subsequent renomination by President Biden in 2021.

The incoming chair will inherit a challenging situation. Inflation has proven resistant to falling below the Fed's 2% target, liquidity strains persist in short-term funding markets, and the federal deficit continues to widen. These issues collectively complicate the policy outlook at the outset of the new term.

Despite this, market consensus has coalesced around the view that the next chair will be more dovish, with a greater willingness to cut rates. That expectation has been reinforced by growing speculation that Kevin Hassett—a Trump administration official whose policy orientation is seen as more accommodative—is the leading candidate.

However, that expectation actually runs counter to the historical record following leadership changes at the Fed. Over the past 50+ years, and across the last seven Fed chair nominations, both the 2-year and 10-year Treasury yields have moved higher in the period following the announcement (table from Bank of America):

Table 1: Yields up in 3 months after last 7 Fed chair nominations
History of Fed chair nominations and bond yields

				Post-nomination 3mo UST yield change	
Fed Chair	President	Date of nomination	Start of term	2Y (bps)	10Y (bps)
Burns	Nixon	14-Jan-70	1-Feb-70	78	20
Miller	Carter	3-Jan-78	8-Mar-78	42	32
Volcker	Carter	27-Jul-79	6-Aug-79	211	147
Greenspan	Reagan	16-May-87	11-Aug-87	63	66
Bernanke	Bush	24-Jan-06	1-Feb-06	40	52
Yellen	Obama	9-Oct-13	3-Feb-14	4	16
Powell	Trump	2-Nov-17	5-Feb-18	15	7

Source: BofA Global Investment Strategy, Bloomberg

BofA GLOBAL RESEARCH

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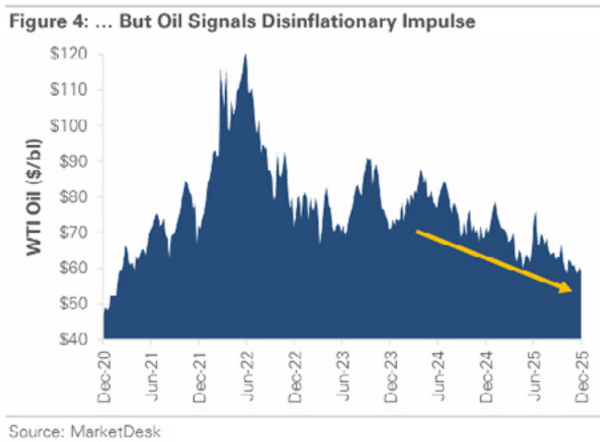
The good news is that the last two nominations were followed by relatively modest moves in yields, particularly compared with the five previous instances. Even so, borrowers expecting meaningfully lower rates in the near term should consider these historical trends.

The outlook for inflation is likely to be the incoming chair's biggest challenge. The last scenario the Fed wants to confront is a reacceleration in pricing pressure. One constructive development is that inflation has historically been most problematic when oil prices are rising, as they were in 2021 and 2022. Today, while inflation remains above target, oil prices are still notably subdued, making a renewed inflation surge less likely (chart from MarketDesk):



If inflation remains contained, the Fed has greater flexibility to support the economy through additional rate cuts without fear of overstimulating demand and driving prices higher. All else equal, this would make the new Fed chair's job considerably easier.

WHAT HAPPENED AFTER **THREE STRONG YEARS IN THE MARKET?**

The S&P 500 posted a gain of more than 80% over the past three years, a result that has occurred only 14 times since 1950. It's rare, and it reflects unusually strong momentum.

History suggests that after surges of this magnitude, returns tend to be more subdued. The larger the three-year advance, the more modest the average return over the following year as markets digest prior gains. That said, the near-term record has been constructive. Six months later, returns were positive in 13 of the 14 historical cases, with an average gain of roughly 7% (table from Bluekurtic Market Insights):

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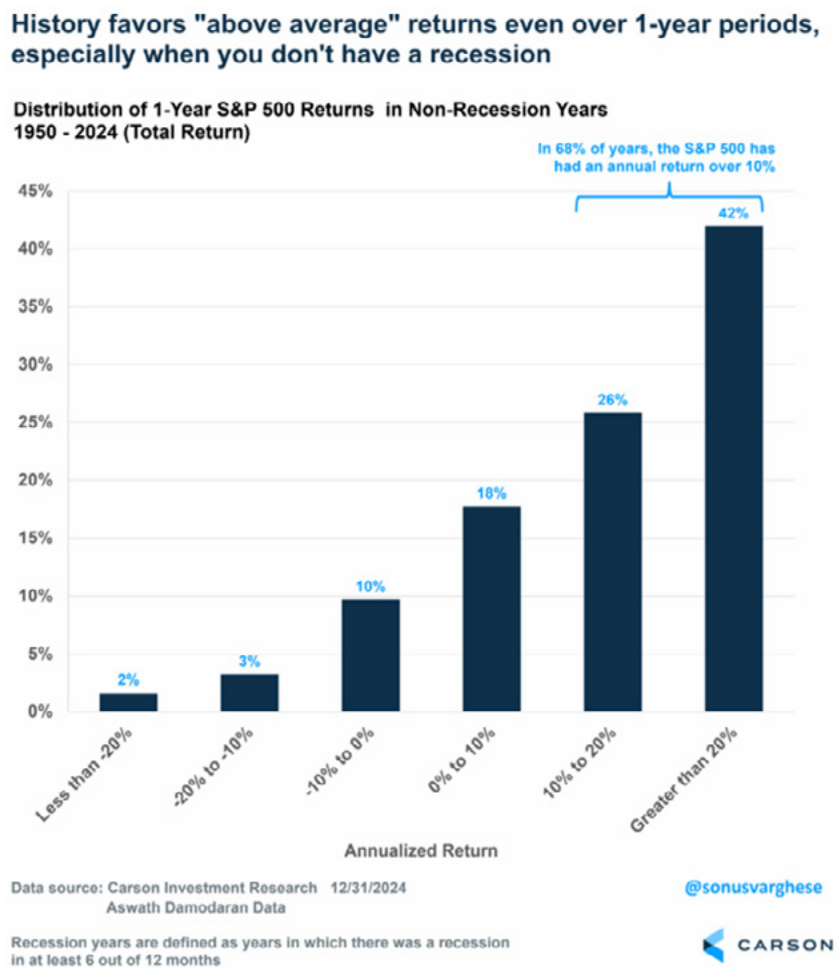
Event Date	Event Return %	1M Return %	2M Return %	3M Return %	6M Return %	9M Return %	12M Return %	12M Max Loss	12M Max Drawdown
9/8/55	82.38%	-6.22%	0.62%	4.42%	5.10%	2.87%	8.39%	-7.02%	-10.59%
2/28/56	84.60%	6.78%	6.49%	-2.93%	4.71%	-2.20%	-4.78%	-6.69%	-14.61%
12/3/56	84.44%	1.35%	-3.15%	-4.18%	3.02%	-1.17%	-10.03%	-15.22%	-20.66%
6/27/85	80.17%	-0.85%	-1.64%	-5.20%	9.61%	24.96%	30.52%	-5.53%	-7.66%
2/17/87	82.22%	2.44%	0.50%	0.41%	17.03%	-14.87%	-9.21%	-21.57%	-33.51%
2/20/97	80.18%	-2.51%	-5.29%	4.84%	17.01%	19.45%	28.83%	-8.12%	-10.80%
9/23/98	83.33%	0.43%	11.45%	15.24%	18.39%	25.04%	20.10%	-10.00%	-10.00%
10/6/99	81.67%	3.89%	7.39%	5.89%	13.27%	9.90%	6.31%	-5.88%	-11.19%
1/10/00	80.29%	-2.80%	-4.29%	3.21%	1.24%	-4.84%	-9.90%	-13.23%	-17.20%
1/24/12	87.59%	3.89%	7.75%	4.36%	1.80%	7.16%	13.70%	-2.78%	-9.94%
8/26/14	81.95%	-0.86%	-1.92%	3.64%	5.54%	5.21%	-2.98%	-6.88%	-7.40%
11/8/21	80.84%	-0.01%	-0.67%	-3.83%	-15.11%	-11.95%	-18.58%	-23.92%	-25.43%
2/14/23	84.86%	-5.24%	0.04%	0.00%	8.55%	8.69%	20.90%	-6.78%	-10.28%
9/4/25	81.77%	3.66%	4.14%						
	Average	0.28%	1.53%	1.99%	6.94%	5.25%	5.64%	-10.28%	-14.56%
	Median	0.21%	0.27%	3.21%	5.54%	5.21%	6.31%	-7.02%	-10.80%
	% Positive	50.00%	57.14%	69.23%	92.31%	61.54%	53.85%	-	-

Outcomes over the following twelve months were more mixed. Returns were still positive on average, but dispersion widened as markets worked through the excesses of the prior rally. Even in years that ultimately finished higher, average peak-to-trough drawdowns ran between 7% and 11%. After the S&P 500's strong three-year run, it would be unusual not to see at least a 7% pullback at some point in 2026.

Still, if the economy avoids recession, the backdrop argues for a positive return. In non-recessionary years, the stock market has finished lower only 15% of the time and has delivered double-digit gains nearly 70% of the time (chart from Carson Group):



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In summary, the setup for 2026 is constructive. Fiscal deficits remain large, monetary policy is easing rather than tightening, and the base case is an economy that avoids recession—conditions that have historically supported positive equity returns. At the same time, markets are coming off an unusually strong three-year run, which argues for lower forward returns and a higher likelihood of interim volatility. A pullback of at least 7% would be consistent with history, even in a year that ultimately finishes higher. Tame inflation would give the Fed room to cushion the cycle, but a new Fed chair, persistent deficits, and rates that may not fall as much as hoped add uncertainty. The balance of risks favors gains over the full year, with a bumpier path along the way.

Happy Holidays

All of us at Corbett Road would like to thank our clients and partners for your continued trust and partnership. We wish you a happy, safe holiday season and a healthy, successful New Year.

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