

Market perspectives

Vanguard's monthly economic and market update

The views below are those of the global economics and markets team of Vanguard Investment Strategy Group as of June 24, 2026.

KEY HIGHLIGHTS

- AI-driven earnings momentum is strong in the near term, but uncertainty around where long-term value will accrue is rising.
- The U.S. outlook remains resilient, but persistent inflation is likely to keep Fed policy on hold through 2027.

Vanguard's forecasts of asset class performance

Our 10-year annualized nominal return and volatility forecasts are based on the March 31, 2026, running of the Vanguard Capital Markets Model®.

EQUITIES	RETURN PROJECTION	MEDIAN VOLATILITY
U.S. equities	4.9%–6.9%	15.3%
Global ex-U.S. equities (unhedged)	5.0%–7.0%	18.9%
Developed markets ex-U.S. equities (unhedged)	5.4%–7.4%	18.1%
Emerging markets equities (unhedged)	3.6%–5.6%	25.3%
U.S. value	5.9%–7.9%	18.9%
U.S. growth	4.3%–6.3%	16.4%
U.S. large-cap	4.8%–6.8%	15.1%
U.S. small-cap	5.8%–7.8%	19.9%
U.S. REITs	3.8%–5.8%	17.9%
FIXED INCOME		
U.S. aggregate bonds	4.2%–5.2%	6.3%
Global ex-U.S. aggregate bonds (hedged)	4.5%–5.5%	5.0%
U.S. Treasury bonds	4.1%–5.1%	6.7%
U.S. short-term Treasury bonds	3.4%–4.4%	1.7%
U.S. intermediate-term Treasury bonds	3.5%–4.5%	5.2%
U.S. long-term Treasury bonds	5.1%–6.1%	10.4%
U.S. credit	4.3%–5.3%	6.5%
U.S. high-yield corporate bonds	4.7%–5.7%	9.4%
Emerging markets sovereign bonds (hedged)	5.6%–6.6%	10.9%
U.S. TIPS	3.1%–4.1%	5.0%
U.S. mortgage-backed securities	4.6%–5.6%	4.0%
U.S. municipal bonds	3.6%–4.6%	4.7%
U.S. high-yield municipal bonds	4.2%–5.2%	8.1%
U.S. cash	2.9%–3.9%	1.1%
U.S. municipal cash	2.5%–3.5%	0.5%
COMMODITIES	4.4%–6.4%	16.5%
U.S. INFLATION	1.5%–2.5%	1.7%
VANGUARD U.S. DOLLAR INDEX	-1.0%–0.0%	8.2%

IMPORTANT: The projections and other information generated by the VCMM regarding the likelihood of various investment outcomes are hypothetical in nature, do not reflect actual investment results, and are not guarantees of future results. Distribution of return outcomes from VCMM are derived from 10,000 simulations for each modeled asset class. Simulations are as of March 31, 2026. Results from the model may vary with each use and over time. For more information, please see the Notes section below.

Source: Vanguard Investment Strategy Group.

Notes: Equity forecasts reflect a 2-point range around the 50th percentile of the distribution of probable outcomes. Fixed income forecasts reflect a 1-point range around the 50th percentile. More extreme returns are possible. These return assumptions depend on current market conditions and, as such, may change over time. We make our updated forecasts available at least quarterly.

Between earnings momentum and AI-enabled profitability

At the start of 2026, we anticipated continued earnings momentum, with risks skewed to the upside. At midyear, that view has largely been borne out. The near-term backdrop remains favorable, supported by a still-powerful AI investment cycle, strong earnings momentum, and room for further positive earnings surprises.

Yet a central point of tension has come into focus between the durability of earnings momentum in the near term and the ability of AI investment to deliver broad-based, sustainable profitability in the medium term. With elevated earnings expectations already priced in, the path for sustained return momentum beyond the near term appears narrow.

Returns are being earned, so far

U.S. equities have continued to climb, rising roughly 10% so far this year. Those gains have been driven by earnings growth—both realized earnings and upwardly revised expectations—rather than further valuation expansion.

Returns across global markets have similarly tracked strengthening earnings. Indeed, markets with the largest upward revisions to earnings expectations have delivered the strongest returns. Asia-Pacific ex-Japan—notably South Korea and Taiwan—has performed the best, with earnings expectations for the next few years having risen by more than 30%.

In contrast, European markets have lagged most other regions, reflecting their relatively modest 2% increase in expected earnings growth.

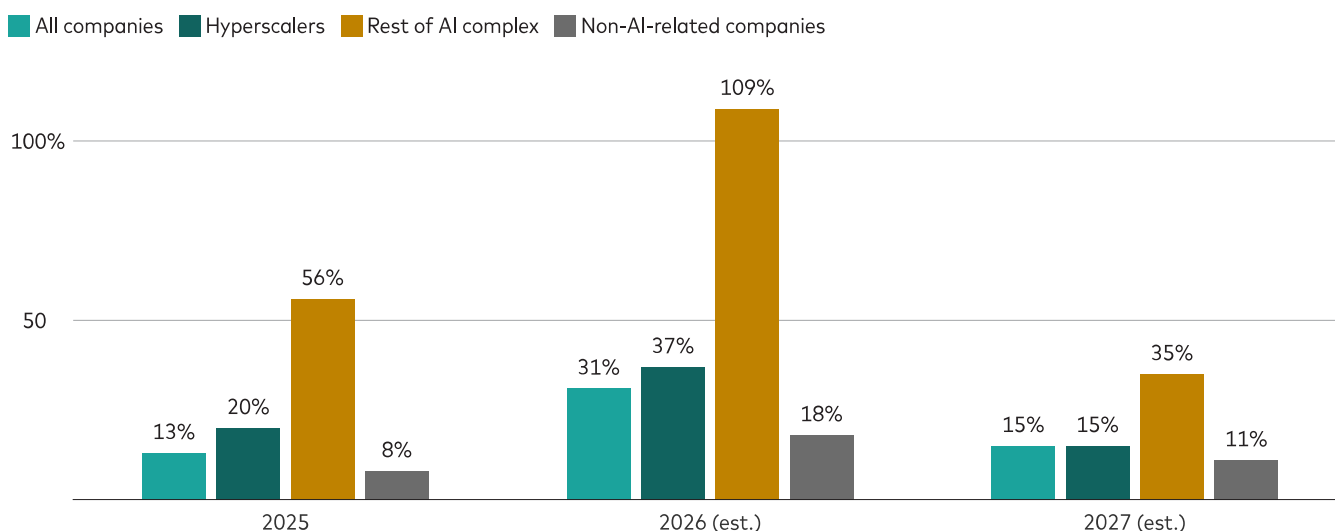
A similar pattern has played out in the U.S. market. Firms in semiconductors, semiconductor equipment, and technology hardware subsectors have delivered the highest returns—again backed by upward earnings growth revisions of more than 30% over the next few years. Health care and financials, with minimal revisions to earnings, have lagged markedly.

The expected rate of earnings growth for the rest of 2026 is running meaningfully above the pace of recent years. AI capital expenditure, surpassing earlier projections, is at the center of this dynamic.

A relatively small group of roughly 70 companies globally is driving a historically large, physically intensive buildout centered on semiconductors and AI infrastructure. This “AI complex” comprises companies undertaking AI infrastructure buildout—including “hyperscalers” Alphabet, Amazon, Meta, Microsoft, and Oracle—and companies across the semiconductor stack, data centers, and networking infrastructure that benefit from hyperscaler spending. For this year and next, we expect this AI complex to generate more than half of all U.S. earnings growth.

Where U.S. earnings growth is coming from

Earnings growth (Year-over-year percentage)



Sources: Vanguard calculations, based on data from Bloomberg, as of June 12, 2026.

Notes: “Hyperscalers” refer to the five firms that are driving AI capital expenditure: Alphabet, Amazon, Meta, Microsoft, and Oracle. “Rest of AI Complex” refers to roughly 30 firms in the U.S. that are benefiting from this AI-buildout-driven surge in demand.

Near-term momentum is intact, but the bar keeps rising

In the near term, the forces supporting earnings momentum are likely to persist, perhaps even strengthen. Most hyperscalers—the large cloud service providers funding the AI buildout—appear able to balance continuing earnings growth with the demands of funding historic capital expenditure, supported partly by increased debt issuance and equity offerings. With the AI investment cycle strengthening, near-term risks to AI complex earnings remain tilted to the upside.

Nonetheless, we anticipate significant market volatility. Although swings may be triggered by rates or geopolitics, market drivers are increasingly tied to the AI buildout. As we continue to learn what the economics of AI look like in practice—the trajectory of AI capital expenditure, how effectively hyperscalers can monetize AI investment, and the size and shape of AI's addressable market—the market's sensitivity to the ups and downs is likely to be significant. Investors should expect a bumpy ride.

From AI buildout to AI diffusion: Where long-term value accrues

Our outlook for the medium term is more guarded than for the near term, for two reasons:

- **The historic scale of investment by hyperscalers raises questions about whether returns will ultimately justify the capital deployed.**

Outcomes are unlikely to be uniform. Some firms may emerge as more profitable and with significant competitive advantages, while others—and parts of the broader AI complex—could be vulnerable if spending slows.

- **The question that ultimately determines returns is not just who builds AI infrastructure, but who captures its economic benefits.** As AI adoption broadens, opportunities may shift beyond the AI complex to areas such as U.S. value stocks and developed markets, where companies can improve productivity without bearing upfront investment costs.

Diversification remains the best defense against concentrated risk

Where does this leave investors? If this outlook holds, volatility is likely to remain elevated as markets balance near-term earnings strength with uncertainty around where AI benefits ultimately will accrue. Time horizon matters. Earnings momentum may drive returns in the short term, but over longer periods, valuations tend to anchor outcomes. Fixed income also remains a key diversifier given its current risk-return profile.

In this environment, clarity and discipline are critical. Staying focused on investment goals—and maintaining diversification across asset classes and themes—can help avoid overconcentration in the AI buildout.

ECONOMIC FORECASTS

United States: Trajectory of inflation to constrain policy

Near the halfway point of the year, our U.S. outlook remains constructive, supported by strong AI-driven investment, resilient consumers, and solid job growth.

However, inflation pressures have reemerged, with core inflation now expected to finish the year above 3%, driven by persistent services inflation and factors such as tariffs and higher energy prices.

The labor market remains healthy, though hiring may slow in the near-term. We expect unemployment to stabilize in the mid-4% range, consistent with full employment.

Given this backdrop, the Federal Reserve is likely to remain on hold. We no longer expect a rate cut in 2026 and anticipate policy will stay at current levels through 2027.

	GDP GROWTH	UNEMPLOYMENT RATE	CORE INFLATION	MONETARY POLICY
Year-end 2026 outlook	2.3%	4.6%	3.2%	3.6%
Year-end 2027 outlook	3.0%	4.4%	2.7%	3.6%

Sources: Vanguard.

Notes: GDP growth is defined as the fourth-quarter-over-fourth-quarter change in real (inflation-adjusted) GDP in the forecast year compared with the previous year. Unemployment rate is as of December for each year. Core inflation is the year-over-year percentage change in the Personal Consumption Expenditures price index, excluding volatile food and energy prices, as of December for each year. Monetary policy is the rounded midpoint of the Federal Reserve's target range for the federal funds rate at year-end.

All investing is subject to risk, including possible loss of the money you invest. Be aware that fluctuations in the financial markets and other factors may cause declines in the value of your account. There is no guarantee that any particular asset allocation or mix of funds will meet your investment objectives or provide you with a given level of income. Diversification does not ensure a profit or protect against a loss.

Prices of mid- and small-cap stocks often fluctuate more than those of large-company stocks.

Investments in bonds are subject to interest rate, credit, and inflation risk.

Investments in stocks or bonds issued by non-U.S. companies are subject to risks including country/regional risk and currency risk. These risks are especially high in emerging markets.

Funds that concentrate on a relatively narrow market sector face the risk of higher share-price volatility.

U.S. government backing of Treasury or agency securities applies only to the underlying securities and does not prevent share-price fluctuations. Unlike stocks and bonds, U.S. Treasury bills are guaranteed as to the timely payment of principal and interest.

Municipal bond fund distributions, including any market discount recognized by the Fund's investments, may be taxable as ordinary income or capital gains. A majority of the income dividends that you receive from the Fund are expected to be exempt from federal income taxes. However, a portion of the Fund's distributions may be subject to federal, state, or local income taxes or the federal alternative minimum tax. You should consult your own tax advisor with respect to any particular U.S. or non-U.S. tax consequences of your investment in the Fund.

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The VCMM projections are based on a statistical analysis of historical data. Future returns may behave differently from the historical patterns captured in the VCMM. More important, the VCMM may be underestimating extreme negative scenarios unobserved in the historical period on which the model estimation is based.

The Vanguard Capital Markets Model® is a proprietary financial simulation tool developed and maintained by Vanguard's primary investment research and advice teams. The model forecasts distributions of future returns for a wide array of broad asset classes. Those asset classes include U.S. and international equity markets, several maturities of the U.S. Treasury and corporate fixed income markets, international fixed income markets, U.S. money markets, commodities, and certain alternative investment strategies. The theoretical and empirical foundation for the Vanguard Capital Markets Model is that the returns of various asset classes reflect the compensation investors require for bearing different types of systematic risk (beta). At the core of the model are estimates of the dynamic statistical relationship between risk factors and asset returns, obtained from statistical analysis based on available monthly financial and economic data from as early as 1960. Using a system of estimated equations, the model then applies a Monte Carlo simulation method to project the estimated interrelationships among risk factors and asset classes as well as uncertainty and randomness over time. The model generates a large set of simulated outcomes for each asset class over several time horizons. Forecasts are obtained by computing measures of central tendency in these simulations. Results produced by the tool will vary with each use and over time.



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