Janus Henderson
INVESTORS

Capital Market Assumptions: 2026 Update

View from the Janus Henderson Multi-Asset team

In this document, we set out our expected longer-term returns for 20 major asset classes across equity, fixed income, currencies and commodities. We then discuss the implication of our forecasts for each asset class. Forecasting asset class returns over an average market cycle, which we take to be around 10 years, helps both to frame shorter-term investment views and to construct the longer-term foundations of a portfolio. We focus on the major asset classes, but the same methodologies could be applied to a broader range of asset classes and currencies. We are looking to create expected returns that are model-based expectations, but also transparent and easily understood.

Why look at long-term expected returns?

Long-term expected returns form an integral part of our investment process. They are a key source of trade ideas and a useful anchor for understanding the potential returns that we may reasonably expect from a portfolio over the longer term. They are also an essential part of solutions design where they are used, together with our long-term estimates of risk, to formulate strategic asset allocations expected to deliver client objectives.

Thinking longer term has several benefits:

Greater predictability
Predictability improves as time horizons expand, allowing us to estimate returns with greater precision.

Greater stability
Over long periods of time, returns – and therefore expected returns – are less volatile, resulting in a more stable strategic allocation.

Capturing long-term themes
The determinants of long-term return can differ from the determinants of return over shorter time horizons.

Our philosophy

We believe that for a methodology to forecast returns going forward, past accuracy is important, but not enough. Markets are constantly evolving and what once was true may no longer be. Understanding why and when a forecast has worked is, we believe, essential for understanding whether it will continue to do so.

We examine our methodologies going back, in some cases, more than a century, so we can learn how they have behaved over time, when they have worked, and when they have struggled. We seek to select methodologies that have accurately forecasted returns across a wide range of market environments.

In equities, for example, we rely upon cyclically adjusted earnings yields and expected inflation to predict future equity returns across a wide range of global markets. Within fixed income, we add cash returns, the term premium, and credit premium to predict returns across fixed income categories. This methodology has proven effective in sovereigns and corporates, investment-grade, and high-yield, and over longer and shorter maturities.

All our methodologies are based on cutting-edge academic and central bank research, with clear economic rationale. We rely on equilibrium concepts, with a simple set of underlying assumptions, allowing us to better understand what the data are telling us and why. We believe a qualitative assessment of whether a methodology's assumptions still apply is a key part of assessing its potential effectiveness going forward.

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Our long-term expected returns

All assumptions below are shown in shown in USD, with fixed income currency hedged. Returns are annualised expectations over the next 10 years.

Equity	2026	2025	Change
World Equity	6.2	6.2	0.0
US Equity	5.7	5.5	0.2
UK Equity	7.7	8.1	-0.4
Eurozone Equity	7.7	7.9	-0.2
Japan Equity	7.0	7.2	-0.2
Asia ex Japan Equity	8.7	9.7	-1.0
Emerging Market Equity	9.3	10.6	-1.3

Global bonds	2026	2025	Change
Global Bond	4.7	4.8	-0.1

High Yield Debt	2026	2025	Change
US Dollar	4.4	4.5	-0.1
Euro	4.9	5.3	-0.4

Emerging Market Debt	2026	2025	Change
Hard Currency	5.9	6.7	-0.8

Investment Grade Debt	2026	2025	Change
US Dollar	5.1	5.1	0.0
Euro	4.0	3.9	0.1
Sterling	4.9	4.6	0.3

Government Bonds	2026	2025	Change
US 10 Year	5.6	5.4	0.2
German 10 Year	4.7	4.0	0.7
UK 10 Year	6.4	5.5	0.9

Index Linked Bonds	2026	2025	Change
US 10 Year Inflation Linked	6.2	5.8	0.4
UK 10 Year Inflation Linked	6.7	5.6	1.1

Cash	2026	2025	Change
USD Cash	2.6	2.8	-0.2

Source; Janus Henderson Investors. 2026 expected returns are as of 31 December 2025. 2025 expected returns are as of 31 December 2024. Returns are annualised and cover a 10-year period. See page seven for details of relevant indices and proxies.

The scenarios presented are an estimate of future performance based on evidence from the past on how the value of this investment varies, and/or current market conditions and are not an exact indicator. What you will get will vary depending on how the market performs and how long you keep the investment/product.

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2025 Summary

2025 was another year of heightened geopolitical uncertainty, notably the tariffs introduced by the US government on 'Liberation Day' in April. While significant near-term volatility followed the announcement of what was one of the largest changes to global trade dynamics in a generation, the S&P 500 Index rebounded to make significant gains over the year, rising 18%. Nonetheless, inverse to the previous year, 2025 was a good year to diversify away from the US, as international markets (as represented by the MSCI ACWI ex US Index) were up 33% in US dollar terms.

On the bond side, performance was more mixed. Treasuries delivered strong performance, as starting yields were elevated, and there was a significant contribution from the coupon. Outside the US returns were lower, with rising yields leading to capital losses.

The result for investors was a year where diversification overall was beneficial, delivering higher returns, and investors were rewarded for taking risk.

Outlook for expected returns

Long-term expected returns still seem attractive. Within fixed income, yields remain high, with investment grade fixed income instruments expected to deliver returns in excess of 4%. Within equities, valuations look attractive outside the US, but the gap has narrowed versus previous years. One area that looks expensive is mid-risk assets, specifically high yield, where already-tight spreads have narrowed further.

We expect this environment to have various implications for portfolios:

- Increased asset class diversification – bonds are expected to deliver meaningful returns versus equities, reducing the cost of diversification.
- Divergent outcome in equities – given persistent large valuation gaps, international exposure is expected to outperform.
- The 'barbell' – with credit spreads in mid-risk assets looking expensive, it becomes more attractive to combine equity and higher quality fixed income assets.

Equities

Strong price appreciation within the US has been offset by rising EPS, leading to a slight improvement in valuations and expected returns, given that earnings growth does not seem fully reflected in prices.

The US is still the lowest-returning equity market, in terms of assumed returns over the next 10 years, but the scale of relative outperformance from other markets in 2025 means the gap between the US and the rest of the world has narrowed.

Emerging markets continue to offer the highest expected returns, but given the level of recent price appreciation, expectations for future returns have declined more than for other regions.

Government bonds

Government bonds remain elevated versus recent history. Since the previous set of expected returns, across all markets there has been an increase in yields boosting expected returns both from yield and anticipated capital appreciation. This was muted in the US and more prominent in Germany.

Credit

Within credit, spread compression has reduced expected returns relative to 2025, with current spreads now very tight relative to history. This has been most prominent in the US high yield category, where expected returns now sit below investment grade, with higher default losses expected to offset any additional spread.

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Appendix

Methodology

The key drivers of all estimates are a combination of current valuations, together with expectations of the future economic environment.

Equity

Equity expected return = cyclically adjusted earnings yield + Inflation.

Campbell (2007) shows that, "When return on equity equals the expected return, as might be the case in long-run equilibrium," this implies that the expected real return equals the earnings yield. We combine earnings yield with forecast inflation to get a nominal expected return. For the earnings yield, we use a cyclically adjusted measure similar to Shiller (2000). We take earnings over the previous 10 years, using inflation gross up to current day price levels and then divide by the price to get a yield. The idea is to get an impression of whether prices look cheap based on where real earnings should be at this point in the cycle.

The merits of this approach are:

- It relies on one equilibrium condition and is not dependent on a wide range of assumptions (future growth, dividend payments, etc.) and because of this can be relied upon to give sensible results.
- It is easier to compare across different markets than dividend-based models, as different markets can have markedly different pay-out ratios due to differential tax treatment of dividends.
- Empirically, it has been an excellent predictor of long-term equity returns going back well over a century.

Fixed Income

Our fixed income model splits returns for each fixed income security into four components:

1. Cash return – the estimated long-term return of cash (we assume a 10-year period)
2. Term premium – the excess return paid to holders of longer-term bonds
3. Credit premium – the excess return paid for holding higher risk bonds
4. Inflation premium – the excess return paid to holders of securities whose cash flows are linked to inflation

Each bond is therefore a function of cash return and the different premia to which it is exposed. For the main types of fixed income securities, these premia are:

Developed government expected return = Cash return + term premium

Inflation linked expected return = Cash return + term premium + inflation premium

Credit expected return = Cash return + term premium + credit premium

Floating rate loans expected return = Cash return + credit premium

Cash Return

We estimate cash return by taking the current yield curve and removing the estimated term premium for different maturities of debt.

Term premium

Term premium = Treasury yield + roll return

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We start by estimating the term premia by comparing longer-term implied spot rates with our expectations of the equilibrium cash rate (see Rebonato 2015). If implied spot rates are above equilibrium, this indicates an excess return, and vice versa.

For shorter-term spot rates, we shrink the term premia, as term tends to be greater further up the curve (we use an approach similar to the affine model of Piazzesi et al to determine the magnitude of the shrinkage). Once we have term premia for the whole curve, we combine these estimates with current yields to estimate return, taking into account the roll return.

Credit premium

Credit Premium = Spread + Spread roll return – Estimated losses from default and losses/gains from downgrade/upgrade

Spread is simply the excess yield of a bond relative to a relevant government bond. Roll returns represents the expected capital gain or loss as the bond moves towards maturity. To estimate default and downgrade losses we use the realized capital loss over the previous cycle, which we calculate by taking the difference between the realized returns and an estimate of what historical returns would have been in the absence of default and ratings changes. This approach avoids making a wide range of assumptions (default probabilities, capital losses, etc.), which is very difficult to do accurately, particularly for lower grade debt.

Inflation premium

Inflation premium = Forecast inflation – Breakeven inflation

To estimate the inflation premium, we compare longer-term breakeven inflation with the forecast, shrinking the inflation premium for shorter debt in line with what we do for term.

Currencies

Currency expected return = Forecast domestic inflation – Forecast foreign inflation

This is equivalent to assuming PPP over/under valuation remains unchanged, and you do not get convergence to parity. This assumption yields a stable equilibrium where you cannot get arbitrarily large purchasing power deviations between different countries. It also accounts for the fact that some countries trade at a permanent discount/premium versus others (for example emerging markets have always traded at a discount versus the U.S. dollar). A corollary is that the highest-inflation countries are predicted to depreciate the most; Venezuela is a good example of this in practice.

Commodities

Energy, agriculture and metals

Energy, agriculture and metals expected return = Cash return + β_{Inf}*Inflation premium

Commodities with high storage costs tend to be linked to current inflation and demand, so we treat them as giving exposure to the inflation premia (see Fixed Income section). Generally, priced inflation, even for longer durations, is significantly less volatile than most commodities, so we leverage the inflation premium to reflect this. Leveraged inflation and commodities have behaved in a very similar way over the past decade as commodity prices, particularly oil, form one of the most volatile parts of the CPI basket.

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Gold

Gold expected return = Cash return + β_{Term}*Term premium + β_{Inf}* Inflation premium

As storage costs are lower for gold than other commodities, it is more effective as a store of real purchasing power. These characteristics give it a similar risk and return profile to longer dated inflation-linked bonds and, as such, we use the same expected return methodology for both. In line with our approach for other commodities, we leverage the premia to reflect the differences in risk.

Specialist equities and hedge funds

For specialist equity and hedge funds, we use a regression model to determine exposure to each of the asset premia listed above and then calculate an expected return consistent with this. We select the combination of relevant premia using proprietary machine learning techniques.

Economic forecasts

Long-term inflation forecasts
We forecast inflation using a 'through-the-cycle' average. There has been a lot of academic work that finds average inflation, although simple, has been a better forecast of future inflation than many more complicated models.

Long-term real interest rates
We follow the work of Bauer and Rudebusch, who show that a varying equilibrium real rate produces a better prediction of future rates than a simple static estimate. This makes intuitive sense; the world we are in today is very different from the world in of the 1970s, and there is far more flexibility in labor markets, a more internationalized economy, higher debt burden, etc. As such, we base the equilibrium real rate on the relationship between interest rates and inflation over the past cycle.

Equilibrium cash rate

Equilibrium cash rate = Long-term inflation forecast + long-term real rates

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Indexes and proxies

Equity	Index
World Equity	MSCI World
UK Equity	FTSE All Share
U.S. Equity	S&P 500
Japan Equity	TOPIX
Eurozone Equity	MSCI Eurozone
Asia ex Japan Equity	MSCI AC Asia Pacific ex Japan
Emerging Market Equity	MSCI Emerging Markets

Global Bond	Index
Global bond	Bloomberg Barclays Global Aggregate

High Yield Debt	Index
U.S. Dollar	Bloomberg Barclays U.S. Corporate High Yield
Euro	Bloomberg Barclays Pan-European High Yield (Euro)

Emerging Market Debt	Index
Hard Currency	Bloomberg Barclays Emerging Markets Sovereign

Investment Grade Debt	Index
U.S. Dollar	Bloomberg Barclays U.S. Corporate
Euro	Bloomberg Barclays Euro Aggregate Corporate
Sterling	Bloomberg Barclays Sterling Corporate

Government	Index
U.S. 10 Year	U.S. 10 Year Zero Coupon
German 10 Year	German 10 Year Zero Coupon
UK 10 Year	UK 10 Year Zero Coupon

Index Linked	Index
U.S. 10 Year Inflation Linked	U.S. 10 Year Inflation Linked Zero Coupon
UK 10 Year Inflation Linked	UK 10 Year Inflation Linked Zero Coupon

Cash	Index
USD Cash	Bloomberg 3 Month USD LIBOR Cash

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