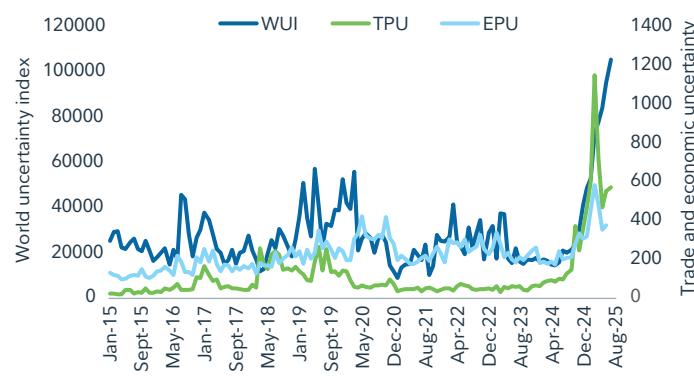
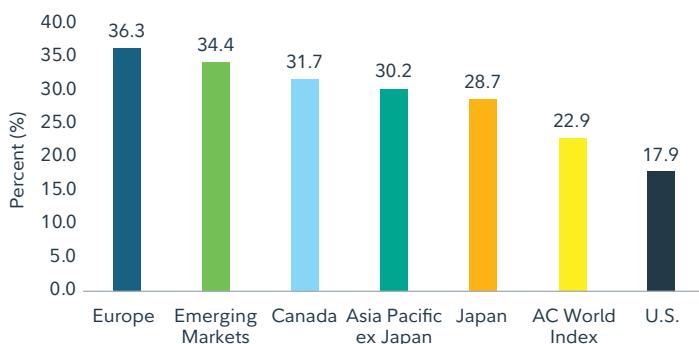


InFocus

- The drag of a shifting economic and trade policy landscape in the U.S., developments in the field of artificial intelligence (AI), and significant investment in AI training and data centres influenced financial markets in 2025. There was significant early-year volatility, specifically surrounding the success of China-based AI startup DeepSeek and the April 2 "Liberation Day" tariff announcement, but both episodes proved temporary as global growth remained solid. Strong earnings, robust consumer demand and aggressive corporate buybacks helped equities outperform other asset classes. Growth in AI-linked investment dominated market narratives, driving record technology capital expenditure and a surge in U.S. investment-grade debt issuance, as corporates financed data centre and infrastructure expansion. Europe, Korea and several emerging economies outperformed U.S. equity markets over the year. Global growth held near 3% in 2025, while inflation continued to moderate across most major economies, though it remained above central-bank targets in several cases. Risks persisted from concentrated U.S. equity exposures, elevated valuations and widening fiscal imbalances. The year concluded with markets focusing more on the earnings outlook than on valuation expansion, while expectations for AI-driven productivity improvements and greater sector and geographic diversification influenced investor positioning for 2026.
- Within the MSCI All Country World Index, the communication services and materials sectors emerged as leaders. Materials benefited from elevated gold prices. The communication services and information technology sectors delivered strong advances, supported by broad-based gains across companies tied to AI development. Semiconductor equipment manufacturers and other participants in the AI value chain stood out as major contributors to performance. Industrials and financials also outpaced the broader benchmark, reflecting solid cyclical momentum. Utilities gained from surging power demand driven in part by rapid data centre expansion. In contrast, real estate, consumer staples and energy lagged.
- Asian equities advanced on steady economic growth, a constructive earnings outlook and relatively lower interest rates. Japanese equities posted strong, broad-based gains. Sustained improvements in corporate-governance standards, attractive valuations and ongoing share-buyback programs supported investor sentiment. The AI theme further contributed to gains in Japan, South Korea, Taiwan and China. In China, the emergence of DeepSeek, a large-language-model chatbot, partially offset weakness from the ongoing U.S. trade dispute and continued softness in the domestic economy, particularly the real-estate sector.
- Fixed-income markets delivered modest gains as deficit concerns among developed-market governments dampened demand for sovereign bonds. Performance in investment-grade and high-yield segments was defined by an AI-driven financing surge, with technology and data-centre investments fuelling record issuance and reshaping sector dynamics. Japanese government-bond (JGB) yields rose after the Bank of Japan (BoJ) lifted its policy rate to approximately 0.75% in response to rising inflation, reflecting expectations of further tightening and renewed fiscal-strain concerns.

Trade and policy uncertainty, AI innovation and market diversification



Sources: Left chart: LSEG DataStream, as of 31 December 2025. Index: MSCI Europe U\$, MSCI EM U\$, S&P/TSX Composite Index, MSCI Asia Pac ex Japan \$, Nikkei 225 Stock Average, MSCI AC World U\$, and S&P 500 Composite. Right: International Monetary Fund (IMF) World Economic Outlook, October 2025. Note: The uncertainty measures are news- and media-outlet-based indices that quantify media attention to global news related to overall uncertainty (WUI), economic policy uncertainty (EPU), and trade policy uncertainty (TPU).

Strong earnings expectations



Source: LSEG DataStream, December 2025.

Canada: international merchandise trade



Source: LSEG DataStream, Statistics Canada, as at August, 2025. Data are on balance of payments basis and are seasonally adjusted.

Gold and financials lifted Canadian equities.

Canadian equities delivered strong performance, supported by positive earnings and moderate multiple expansion, supported by improving profitability in financials and steady contributions from resource sectors. Market returns were not solely earnings-driven; valuations also re-rated modestly, with the TSX trading around 19.9x forward earnings, above its long-term average. Despite this, Canadian equities remained materially cheaper than U.S. peers, as the S&P 500 continued to trade at a substantially higher forward multiple.

Materials was the best-performing sector, as gold-mining leaders benefited from rising gold prices amid heightened economic uncertainty, persistent inflation and strong demand for gold as both a portfolio diversifier and an inflation hedge. Central-bank purchases and robust ETF inflows further supported the rally. Financials also performed well, with diversified revenue growth, disciplined expense management, and ongoing investment in technology and AI supporting a positive earnings outlook, particularly among banks. Elsewhere, factors such as strong demand for AI data centres and AI-enabled tools combined supported investor optimism in technology companies such as Celestica and Shopify. In the consumer sector, resilient consumer spending, operational improvements and supportive investor sentiment supported gains. Companies that focused on margin expansion, loyalty engagement and strategic capital allocation were particularly well rewarded by the market.

Canada's economy expanded by a stronger-than-expected 2.6% in the third quarter of 2025, even as final domestic demand remained flat. High-frequency data indicated that real GDP declined 0.3% in October, with 11 of 20 industries contracting. Durable goods, machinery and wood products were particularly weak, reflecting

reduced export demand and U.S. tariff impacts. Overall, merchandise exports fell 3.0% in August, while imports rose 0.9%, widening the trade deficit. Despite softening output, labour conditions remained resilient, with unemployment at 6.5% in November.

Moderate fixed income performance

Canadian investment-grade bonds, as measured by the FTSE Canada Universe Bond Index, ended the year with modest gains. Fixed-income markets were shaped by a transition from restrictive to easing monetary policy, as the Bank of Canada reduced interest rates throughout the year, while inflation remained close to the Bank of Canada's 2% target. Short-term yields declined in response, while longer-term yields rose. Federal bond issuance increased, reflecting higher levels of government spending and funding needs. Within credit markets, investment grade corporate bonds were among the strongest performing segments, benefiting from steady investor inflows, attractive all in yields, and modest spread compression, particularly in longer duration issues.

Rate cuts announced as inflation falls.

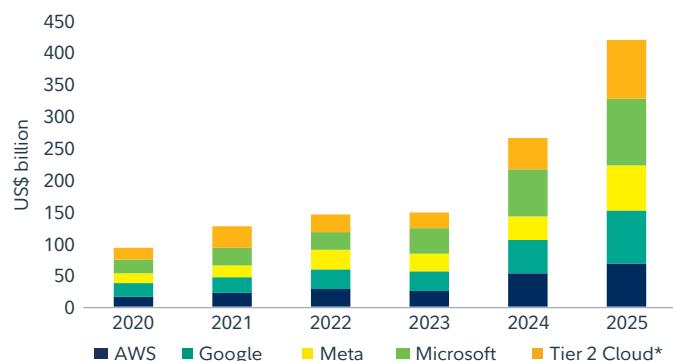
With inflation remaining near target and trade disruptions introducing growth fears, the Bank of Canada (BoC) reduced its overnight rate to 2.25%, from 3.25% at the start of the year. The BoC expects final domestic demand to expand modestly in the fourth quarter of 2025, though overall growth is likely to remain subdued, as trade frictions persist. Headline CPI inflation stayed contained in November, with easing goods-price pressures offset by persistent services inflation. The BoC's analysis suggests that U.S.-Canada trade tariffs have raised price levels modestly but have not generated sustained inflation, as weaker demand has offset cost pressures.

Rising profit margins



Source: Bloomberg, as at December 31, 2025. RHS Chart: The Bloomberg Intelligence Interactive Capex Model provides our estimates for Hyperscale and Cloud Service Provider capital expenditures, as well as spending vertical. Spending vertical disaggregates the spending into respective deployments: AI training, inference, and traditional cloud workloads.
*Tier 2 Cloud provider's capture: Oracle, Coreweave, Apple, Alibaba, and Baidu.

AI-linked capex boomed.



U.S. equities were volatile, but resilient.

U.S. financial markets in 2025 were shaped by a combination of policy shocks, technological exuberance and macroeconomic resilience. Equities delivered strong headline performance despite pronounced volatility, while fixed income and credit markets reflected both easing monetary policy and rising structural risks. The year marked a transition from narrowly concentrated leadership toward a broader, but still fragile, market advance.

The defining macro feature was policy-driven volatility. President Trump's renewed tariff agenda culminated in "Liberation Day" in April, triggering a sharp but short-lived equity sell-off. Markets rapidly stabilized once tariff implementation was paused and negotiations resumed, reinforcing investor confidence that protectionism would slow growth but not derail it. Over the year, tariffs lifted the effective U.S. import tax rate to multi-decade highs, reshaped trade flows away from China and supported domestic manufacturing investment, while inflation pass-through proved less significant than feared.

Equities remained dominated by the AI theme. Mega-cap technology stocks drove index returns for much of the year, supported by strong earnings and unprecedented capital expenditure on data centres, chips and energy infrastructure. However, sentiment shifted as the year progressed. The "DeepSeek" episode early in 2025 highlighted the market's vulnerability to competitive disruption, while growing acknowledgement of an "AI bubble" emerged among corporate leaders and investors. Although valuations moderated later in the year, the U.S. equity market remained expensive by historical standards, with concentration risk elevated and market breadth uneven.

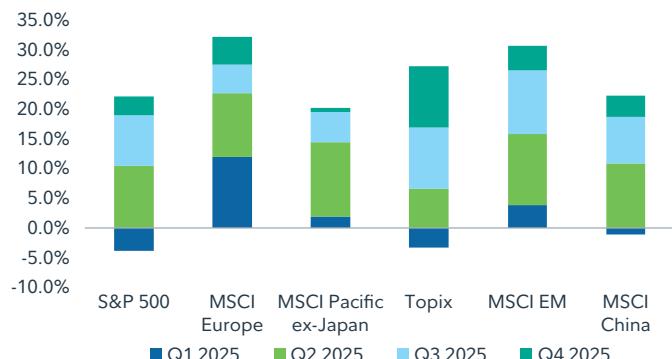
Modest gains in fixed income.

In fixed income, 2025 was notable for the scale of corporate issuance. U.S. companies sold close to \$1.7 trillion of investment-grade bonds, driven largely by AI-related borrowing. While spreads remained relatively contained for much of the year, investor concern increased around leverage, refinancing needs and the mismatch between near-term cash flows and long-duration AI investments. Investors remain cautious of systemic risk in key areas of fixed income markets, including private credit and lower-quality borrowers. In the U.S. market, volatility eased as three consecutive rate cuts by the Federal Reserve (the Fed) reduced recession risks. Still, risks remain with markets becoming increasingly focused on the U.S. fiscal outlook, amid large and persistent deficits, rising interest expenses and elevated issuance.

The Fed delivered three 25-basis-point rate cuts between September and December, formally pivoting into an easing cycle as signs of slowing labour market conditions overshadowed sticky. November CPI rose 2.7% year-on-year, slightly below market expectations but above the Fed's 2% target. Looser financial conditions supported equity valuations, housing activity and risk appetite, while also easing recession fears.

Finally, third quarter U.S. GDP growth surprised to the upside, as robust consumer spending and rising exports drove growth. Government spending also contributed to headline growth, while business and residential investment slowed. A bar chart showing the 10-year average price to 12-month forward earnings multiples against the current price to 12-month forward earnings multiples of U.S., Europe, Pacific ex Japan, emerging markets and China.

Quarterly performance of key equity markets; rest of the world outperformed U.S. equities.



Source: LSEG DataStream, as at December 31, 2025. EM = emerging markets. In U.S. dollar terms. MSCI emerging markets index includes China. MSCI indices used for all markets except Japan. TOPIX index used for Japan equity market performance in local currency terms.

Global equities more attractively valued, relative to history and the U.S.



Source: Bloomberg, Quarterly data in percentage points, as at December 31, 2025. EM = emerging markets. In U.S. dollar terms. MSCI emerging markets index includes China. MSCI indices used for all markets except Japan and the U.S. TOPIX index used for Japan equity market performance in local currency terms. S&P 500 index used for U.S. equity market performance.

Europe beat expectations.

European equities entered 2025 at deep valuation discounts to the U.S., reflecting years of pessimism around growth, energy dependence and geopolitics. A broad re-pricing of undervalued assets supported by earnings resilience, favourable sector exposure, easing financial conditions, and a shift in fiscal and investor narratives contributed to strong relative performance of European equities. As recession fears failed to materialize and earnings proved more resilient than expected, Europe experienced a valuation re-rating, which contributed to total returns.

European companies benefited from positive earnings revisions, particularly in the financials, industrials and information technology sectors. Germany's pivot toward fiscal expansion, infrastructure and defence spending marked a structural change away from austerity and export dependence. This helped improve growth expectations for Europe and benefited cyclical sectors tied to domestic demand.

China's 2025 performance was shaped by resilience in exports and persistent domestic weakness. Despite elevated U.S. tariffs and reduced access to American markets, Chinese exports held up through diversification toward ASEAN, Europe and the Global South. Domestically, consumer confidence, private investment and the property sector remained subdued, keeping inflation near zero and reinforcing deflationary pressures. Policymakers relied on targeted fiscal support and

selective monetary easing rather than large-scale stimulus. The strategic focus remained on technological self-reliance and advanced manufacturing, though concerns persisted around excess capacity, weak household demand, and rising public-sector leverage.

Japan experienced a rare combination of constructive growth momentum and policy normalization in 2025. Wage growth improved meaningfully, supporting consumption as inflation moderated. Corporate profits remained strong, and capital expenditure was underpinned by labour-saving automation, digitization and AI-related investment. The Bank of Japan continued its gradual exit from ultra-loose policy, raising rates modestly while maintaining accommodative financial conditions given deeply negative real yields. A weaker yen supported exports but raised import costs. Longer-term challenges remained, including demographics, high public debt and sensitivity to global trade and AI cycles.

A constructive outlook

European and Asian financial markets enter 2026 with a constructive backdrop. In Europe, easing inflation, lower interest rates and supportive fiscal policy are improving the outlook for growth and corporate earnings, while relative valuations remain attractive. In Asia, accommodative monetary and fiscal policy, the potential for a weaker U.S. dollar and accelerating corporate reforms, particularly in Korea and Japan, aim to support growth resilience.

Appendix

Global Markets (returns in Canadian dollar terms)			
Indexes	2025	2024	Return (%)
S&P/TSX Composite	31,711.39	24,727.94	31.71%
S&P 500	6,845.50	5,881.63	12.38%
NASDAQ	23,241.99	19,310.79	15.54%
DJIA	48,063.29	42,544.22	9.58%
Russell 2000	2,481.91	2,230.16	7.55%
FTSE 100	9,931.38	8,173.02	28.83%
Euro Stoxx 50	5,791.41	4,895.98	32.07%
Nikkei 225	50,339.48	39,894.54	23.24%
Hang Seng	25,630.54	20,059.95	26.07%
Shanghai Comp.	3,968.84	3,351.76	21.21%
MSCI ACWI	1,014.62	841.33	17.18%
MSCI EM	1,404.38	1,075.48	28.08%
Fixed income	2025	2024	Return (%)
FTSE Canada Uni.	1,206.36	1,177.01	2.49%
BBG Global Agg.	501.29	463.44	8.17%
TSX Preference Shares	2,446.01	2,108.00	16.03%
Bond yields	2025	2024	Change (bps)
10 yr Canada Govt.	3.44%	3.24%	20
10 yr U.S. Govt.	4.16%	4.57%	-41
30 yr Canada Govt.	3.86%	3.34%	52
30 yr U.S. Govt.	4.84%	4.79%	6
Commodities	2025	2024	Return (%)
Oil (\$/bbl.)	57.42	71.72	-19.94%
Natural gas (\$/Mmbtu.)	3.69	3.63	1.46%
Gold (\$/Oz.)	4344.00	2614.00	66.18%
Silver (\$/Oz.)	71.29	28.90	146.70%
Copper (\$/lbs.)	5.63	3.99	41.24%
Currencies	2025	2024	Return* (%)
CAD/USD	0.7286	0.6953	4.79%
USD/EUR	0.8514	0.9659	-11.85%
CAD/EUR	0.6204	0.6715	-7.61%
USD/JPY	156.6325	157.3475	-0.45%
USD/CNY	6.9801	7.3417	-4.93%
USD/MXN	18.0080	20.8829	-13.77%
GBP/CAD	1.8494	1.7998	2.76%
GBP/USD	1.3475	1.2514	7.68%

Source: Bloomberg, LSEG DataStream. Total returns, *Price return. **Commodities are quoted in USD.

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