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The End of Low and Stable

From Low and Stable to High and Disruptive: Portfolio Implications

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The investment regime has changed

History is an essential guide to successful investing. Understanding the geopolitical and economic regime in which capital is being deployed is critical to constructing a durable investment strategy. Today's environment – and the one likely to prevail in the years ahead – differs profoundly from the decade following the global financial crisis.

The contrast provides a useful framework for assessing the macroeconomic outlook and its implications for portfolio construction. **The world has moved from an era defined by low rates, low inflation and relative stability to one characterized by higher costs, higher disruption and a higher and more powerful investment cycle.**

From low and stable to high and disruptive

The decade following the global financial crisis was a period of relatively low geopolitical tension and greater stability. While certainly not a perfect world, we were not confronting major wars on two fronts, widespread tariff disputes, or a fundamental reassessment of the global security architecture.

That relative stability allowed companies to embrace globalization, with businesses locating production wherever it could be done most efficiently and at the lowest cost. Efficiency was prioritized over resilience, and increasingly complex supply chains stretched across the world.

It was also a period of exceptionally low inflation, at times bordering on deflation, as central banks tried to create inflation rather than contain it. Interest rates consequently fell to extraordinary levels: mortgage rates approached 2% to 3%, government bond yields declined steadily, and, in parts of Europe and Japan, interest rates turned negative.

Governments were also generally pursuing fiscal consolidation. After the U.S. federal deficit reached close to 10% of GDP in the immediate aftermath of the financial crisis, it subsequently declined to approximately 2% at its low point during the following decade.

Economic growth was relatively subdued. There was relatively low capital investment, and many companies devoted a significant proportion of their cash flow to share repurchases. Earnings growth was respectable, particularly among the dominant technology platforms, but overall, broadly consistent with the long-term historical average of 8-10%.

New regime

Today, almost every part of that environment has changed. We have moved from low and stable to high and disruptive: higher geopolitical risk, higher government spending, higher inflation and interest rates…but also higher investment, greater innovation, higher productivity and, at least so far, dramatically higher corporate earnings.

1. Geopolitical disruption and fiscal expansion

The first profound change is geopolitics.

The war in Ukraine is approaching four and a half years in length. The conflict in the Middle East, which escalated again in July, is now entering its seventh month. But conflict in this decade is not limited to arms and ammunition; trade and tariffs have also become instruments of geopolitical pressure. The current confrontation between Canada and the United States – where Canada is matching new U.S. tariffs dollar for dollar – shows that even the closest historic allies can become engaged in what is effectively a tariff and trade war.

These developments are forcing governments and companies to reconsider the assumptions that underpinned globalization.

Energy provides a clear example. Europe can no longer rely on Russia for the same proportion of its oil and gas. Europe and much of Asia remain highly dependent on energy supplies moving through vulnerable maritime routes, including the Strait of Hormuz. Governments have consequently recognized that energy resilience, energy security, and energy infrastructure are matters of national security.

The same is true of defense. Questions about the reliability of the U.S. security umbrella and the future effectiveness of NATO are forcing European and other governments to increase their own defense capabilities.

Governments must therefore spend more on defense and energy security while simultaneously confronting aging populations and the rising cost of healthcare, pensions and other entitlement programs.

The result is a meaningful shift away from the fiscal restraint that characterized much of the post-financial-crisis period and toward structurally higher government spending.

U.S. government debt has now reached approximately $40 trillion, while the federal deficit remains close to 6% of GDP. That is an extraordinary deficit for an economy that is not in recession and is operating close to full employment.

These forces are likely to maintain upward pressure on government bond yields. This is almost the exact opposite of the previous decade, when yields generally moved lower and long-duration government bonds benefited accordingly.

2. Persistent Inflation and a Higher Cost of Living

The second important change is inflation.

Inflation surged during the pandemic and has remained above central bank targets for much of the period since; it is now above the Fed's 2% target for 65 months and counting according to Chair Warsh at the recent Jackson Hole Symposium.

Even when annual inflation moderates, the cumulative increase in prices does not disappear. Consumers continue to feel it in the cost of groceries, airfares, hotels, education, insurance, and almost every other part of daily life.

There are also structural sources of cost pressure. Bringing production closer to home is more resilient, but it is often more expensive. Defense spending, energy security and the enormous demand created by generative AI are placing pressure on power capacity, industrial inputs, and commodity markets. Prices for many strategically important metals have risen sharply as increased demand has encountered limited new supply.

Our expectation is not that we will experience runaway inflation but rather that **interest rates and inflation will be both higher and more volatile than during the decade following the financial crisis**.

3. Stronger Growth and a New Investment Cycle

The third feature of the current environment is much more positive: **economic growth has been remarkably resilient.**

Using the United States as an example, growth has generally been running above the rates experienced during much of the previous decade. The economy is being supported by several engines at once: the consumer, government spending and, most importantly, a remarkable increase in corporate investment.

The Consumer

The consumer accounts for roughly 70% of U.S. economic activity and remains relatively resilient. According to the Federal Reserve's household balance-sheet data, total U.S. household net worth reached approximately $188 trillion in the first quarter of 2026, double that of a decade earlier.

Four years of rising equity markets, higher home values, a strong employment environment, and the return of meaningful income on cash deposits have created a substantial wealth cushion. While that wealth is not evenly distributed and lower-income households remain under pressure, the aggregate household balance sheet continues to support consumption.

Government Spending

Government spending is another contributor. Defense, energy infrastructure, and entitlement spending are all likely to remain significant contributors to economic growth.

Corporate Investment

The greatest positive surprise, however, has been corporate investment. Non-residential investment has recently been growing at close to 10%, approximately two to three times the rate that prevailed during much of the prior decade.

Why are companies investing so heavily?

First, the economy is experiencing an extraordinary period of technological change. Generative AI has burst onto the scene, and the major hyperscalers are planning unprecedented, multiyear programs of capital expenditure.

That spending extends far beyond GPUs. It includes memory and other semiconductors, data centers, cooling systems, networking equipment, power generation, electricity grids, and the infrastructure required to connect all of it.

According to Axios, the United States entered 2026 with roughly 4,000 data centers and is now forecast to add thousands more. Electricity demand, according to the IEA, which had been essentially flat for years, is now accelerating. The IEA forecasts that global data-center power demand could more than double by 2030.

Second, recent tax legislation-the One Big Beautiful Bill-provides powerful incentives for companies to invest through accelerated depreciation and the immediate expensing of research and development and other qualifying expenditures.

Third, companies are reassessing their supply chains. The Kearney Reshoring Index shows that U.S, CEOs' bringing operations back to the U.S increased by 15% in 2025. Whether driven by government policy, tariffs, or a desire for greater resilience, businesses are bringing strategically important production closer to home.

As a result of these rising investment demands, companies have increasing need for credit. According to SIFMA, U.S. corporations issued $1.68 trillion of bonds in the first seven months of 2026 – 27% more than a year earlier – while the U.S. Treasury data shows the government is on course to borrow roughly $1.5 trillion during the same period. Concurrently accelerating corporate and federal borrowing also gives notable upward pressure to interest rates.

4. Echoes of the 1920s and 1990s

There are two particularly interesting historical comparisons.

The first is the 1920s, when electrification, automobiles, radio, mass production, and modern industrial infrastructure transformed the economy.

The second is the 1990s, when personal computing, telecommunications, the internet, and distributed processing drove a major increase in technology and communications investment.

In both periods, **technological innovation and industrial investment operated together.** The expansion of physical capacity enabled new technologies to spread, while those technologies produced significant productivity gains.

A similar interaction may be underway today. Companies are investing in an entirely new architecture of computing, power, and industrial production. If that investment allows businesses to produce more with fewer resources, it should ultimately translate into higher productivity and stronger earnings.

It is also noteworthy that in both periods, strong earnings growth coexisted with meaningfully positive bond yields.

5. Corporate Earnings

The final part of the macroeconomic picture is corporate profitability.

Bloomberg consensus currently expects S&P 500 earnings to grow by approximately 30% in calendar 2026 – roughly three to four times the high-single-digit growth rate of a typical year. That would make 2026 an extraordinary earnings year by historical standards.

The surprise component is equally striking. In FactSet's latest update, 90% of reporting companies delivered earnings per share above estimates, versus a 10-year average of 76%. Aggregate earnings were 29% above estimates; even excluding unusually large contributions from Alphabet and Amazon, second-quarter earnings growth remained approximately 32%.

The breadth is just as striking: ten of the eleven sectors are reporting year-over-year earnings growth, eight at double-digit rates, while all eleven are reporting positive revenue growth. This is a deeper and wider earnings cycle than a narrow mega-cap technology story. **Earnings have grown faster than share prices, allowing valuations to ease somewhat even as the market has advanced.**

This does not mean markets will rise in a straight line. As expectations get higher and higher, so too does the bar for success. We should expect corrections, changes in leadership, and meaningful differences between winners and losers, including volatility associated with tariffs, geopolitical conflict and changing interest-rate expectations.

For now, markets are still being driven principally by fundamentals. Nevertheless, history reminds us that both the Roaring Twenties and the late-1990s technology boom ultimately gave way to significant bear markets as exuberance, elevated valuations and tighter monetary conditions converged.

We do not see comparable excesses today, but we remain alert to the risk of "too much of a good thing" – closely monitoring valuations, financial conditions and any widening disconnect between market prices and underlying earnings.

Portfolio Implications

This investment regime has direct implications for the three principal building blocks of portfolio construction: **Stability, Diversified** and **Growth**.

STABILITY

The purpose of Stability is the preservation of capital and the reliable funding of near-term liquidity requirements. The objective is to ensure that near-term spending and liquidity requirements can be met without ever being forced to sell risk assets during a market decline.

During the previous decade, investors could own longer-duration bonds and benefit as yields declined and bond prices rose. Today presents a very different environment.

Government borrowing is exceptionally high, fiscal deficits are persistent, and long-term bond yields are volatile. This argues for caution in allocating to government debt and taking excessive duration risk.

That concern is reinforced by the U.S. Treasury's recent decision to expand its buyback program. Beginning in September, the U.S. Treasury doubled the size of its long-end liquidity-support buybacks from $2 billion to $4 billion per operation. While aimed at improving market liquidity, the program does not reduce government debt because the bonds being repurchased are replaced with new issuance.

The potential risk lies in the government's increasing reliance on shorter-term borrowing. While that may help alleviate some pressure on longer-term bond yields, it also means a larger share of the nation's debt will need to be refinanced more frequently. As a result, future government borrowing costs become more sensitive to movements in short-term interest rates. With debt approaching $40 trillion and deficits remaining substantial, this effectively exchanges some long-term financing certainty for greater exposure to future refinancing risk.

POSITIONING: **Within Stability, we favor shorter-duration, government and municipal debt**. The objective is to earn an attractive return on liquidity without exposing capital required for near-term needs to unnecessary interest-rate volatility.

DIVERSIFIED

The opportunity set within Diversified is considerably more attractive than it was during the previous decade.

When interest rates were close to zero, credit yields were limited, infrastructure struggled, and many diversifying assets offered relatively modest prospective returns. Today, the opportunities are much richer.

The objective is to identify assets that have a lower correlation with public equities, can potentially generate returns in the region of 8% to 10%, and provide explicit protection against inflation and the erosion of purchasing power.

This includes private credit, where senior secured lending high in the capital structure can offer yields of approximately 8% to 9% – substantially more than comparable strategies generated during the low-rate period.

Gold remains another useful diversifier, providing a potential hedge against geopolitical disruption, currency devaluation, and declining confidence in government finances.

Most compelling, however, is infrastructure. The demand drivers are exceptionally powerful: digital infrastructure, data centers, power generation, electricity grids, energy security, and trade and transportation links all require substantial new investment.

Infrastructure also offers attractive characteristics beyond growth. It is a durable real asset – often essential, difficult to replicate and supported by long-lived contractual or regulated revenues. Those revenues are frequently explicitly or implicitly indexed to inflation, allowing cash flows to adjust as price levels rise. Select infrastructure investments can therefore combine attractive return potential with meaningful protection of real purchasing power.

POSITIONING: Diversified assets play a more powerful role in portfolios today: income, diversification, and explicit inflation protection. Infrastructure is particularly compelling because it combines structural demand growth with durable real assets and revenues that are often linked to inflation.

GROWTH

The final building block is Growth, principally public and private equity.

Four years into a bull market, it is understandable that investors might become cautious. But the duration of a market advance is not, by itself, a reason to sell. Given the trajectory of economic growth, corporate investment and earnings, equity markets remain well supported.

The opportunity is also broader than the largest U.S. technology companies. Industrial companies in the United States, Europe and Japan are benefiting from reindustrialization and renewed capital investment. Emerging markets are participating in the expansion of semiconductor, manufacturing, and energy supply chains. Meanwhile, the adoption of artificial intelligence is creating both opportunities and disruptions across virtually every sector of the global economy.

Portfolio positioning should lean into several areas that reflect these themes.

Energy and power related equities are supported by rising demand due to energy security and Gen AI.

Specialist technology managers can help identify both the beneficiaries and the potential casualties of technological disruption. That insight is particularly valuable because the effects of AI will extend across sectors and geographies and both public and private markets.

A metals and mining allocation can provide exposure to another structural theme. Digital infrastructure, defense systems, electricity networks, renewable energy, and advanced semiconductor production all require enormous quantities of metals. In many cases, the supply response has been limited by years of underinvestment and the long lead times required to develop new mines.

POSITIONING: A carefully selected equity portfolio of passive and active tilts provides diversified exposure to the breadth of earnings across markets.

Conclusion

The current environment is profoundly different from the decade following the global financial crisis.

We have moved from low and stable to high and disruptive: higher geopolitical tension, higher government spending, higher bond yields, higher inflation, and a higher cost of living.

But the word “high” also applies to the positive side of the equation: higher investment, greater innovation, stronger productivity potential, and higher earnings growth.

For investors, the implications are significant. Portfolio construction must adapt to a world in which diversification, income generation, and inflation protection play an increasingly important role, while maintaining exposure to the growth opportunities being created by technological innovation, reindustrialization, and infrastructure investment. We have an eye on potential risks such as too much investor exuberance that could lead to extended valuations. Therefore, it is our view that diversification across asset classes is the best way to hedge against these risks, while positioning for the opportunities that lie ahead.

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