Mid-year market outlook

NEI

Key takeaways

Executive summary

Markets have remained resilient despite geopolitical conflict, a major oil shock and higher global interest rates. Strong earnings growth, significant AI-related capital spending and continued strength in the U.S. economy have helped support returns.

At the same time, the market backdrop is changing. Leadership is beginning to broaden beyond a narrow group of U.S. mega-cap technology companies, with more signs of participation across sectors, regions and styles. That shift may create a more constructive environment for diversification and active decision-making.

AI remains a powerful market theme, but the opportunity set is evolving. The buildout is becoming more capital intensive, with potential benefits extending beyond chips to areas such as power, infrastructure, cooling, industrials, real estate, energy and financing. As capital needs rise and valuations come under greater scrutiny, investors appear to be placing increased emphasis on execution, profitability and return on investment.

Rates remain an important part of the outlook. Inflation is still above target, and markets are increasingly considering the possibility that rates stay higher for longer. In that environment, balance-sheet strength, valuation discipline and income generation become more important. Higher starting yields may also improve the role of bonds as a source of income and portfolio diversification.

For Canadian investors, there's a more nuanced picture. While economic growth has been uneven, Canadian equities have been supported by improving expectations for sectors such as energy, financials and industrials, alongside growing investment activity. More broadly, the markets are becoming more dispersed, which raises the importance of thoughtful portfolio construction.

Markets are no longer moving in lockstep. The gap between winners and losers is widening, which means portfolio construction matters more than it has in the past several years.

Key takeaways

1. **Market leadership is broadening.** After several years of narrow market leadership, participation is expanding across sectors, regions and styles. That may create a more supportive environment for diversification, particularly as opportunities emerge beyond a narrow group of market leaders.
2. **AI is moving from a chip story to a capex cycle.** The AI theme remains important, but the investment implications are becoming broader. There are potential second-order beneficiaries across power, infrastructure, cooling, real estate, industrials, energy and financing.
3. **Earnings remain a key support for markets.** Strong earnings growth has helped offset concerns around geopolitics, inflation and higher rates. Earnings strength is becoming more broadly distributed across sectors, rather than concentrated solely in technology.
4. **Higher rates require more discipline.** With inflation still above target and real yields moving higher, investors may need to place greater emphasis on balance-sheet quality, valuation discipline and income resilience.
5. **Bonds are becoming more relevant again.** Higher starting yields may improve the role of bonds in portfolios, both as a source of income and as a potential buffer against equity volatility. This is a meaningful change from the low-yield environment of recent years.

6. **Supply and dispersion could create more volatility.** A large pipeline of technology and AI-related listings could create short-term flow and index effects. Over time, however, fundamentals, valuation and profitability are likely to matter more, reinforcing the importance of fundamental research, valuation discipline and active decision-making.
7. **Portfolio construction matters more in a dispersed market.** Markets are no longer moving in lockstep. As the gap between winners and losers widens, thoughtful diversification across sectors, regions and asset classes becomes increasingly important.

The bottom line

After years of narrow market leadership, opportunities are beginning to broaden across sectors, regions and asset classes. In a more dispersed market, investor outcomes may depend less on finding the next market leader and more on building resilient, diversified portfolios.

Watch the Mid-year market outlook webinar for deeper insights on market trends, portfolio construction and opportunities shaping the second half of the year.