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Monthly Market Commentary

January 2026

US Economy

As reported in January, combined US business surveys ticked higher in December, signaling a good head of steam by an economy skewed increasingly toward services growth. Reports of a reasonably good holiday shopping season masked signs of another wind down in housing activity during the final weeks of the year. Labor market conditions still are not showing the kinds of strength consistent with other economic data. The December unemployment rate did tick lower to 4.4%. However, payrolls posted average monthly declines in the fourth quarter, led by jobs in economically sensitive industries.

We anticipate a reacceleration of economic activity this year after what likely amounts to a growth slowdown even milder than the shallow one we expected during last year's fourth quarter. Looking ahead, we anticipate stronger US economic growth in 2026. We believe unique features of this economic cycle could back another year of above-average growth. Subdued inflation should buoy real (inflation-adjusted) incomes and restrain longer-term interest rates, contributing to adequate, if not ample, financial liquidity conditions. We also anticipate an added boost from unusual late-cycle fiscal stimulus in the wake of last year's tax legislation. Finally, we believe subdued inflation may justify further monetary easing by the Fed, potentially lifting the economy's credit-sensitive sectors (like housing) as well as financial-market liquidity, equities, and other financial assets supporting household wealth and consumer spending.

US Markets

US equities entered the new year with positive momentum, extending gains from late 2025. Against this backdrop, fourth-quarter earnings season is underway, and results will be critical in determining whether recent market strength can be sustained. Markets will also be watching business capital spending and consumer trends for the remainder of the year as earnings season unfolds. Looking ahead, we anticipate investment in and revenues from artificial intelligence (AI) to remain key contributors. However, we also anticipate lower short-term interest rates, favorable tax policy changes, and the lapping of tariff-related pressures to result in broader participation from non-tech sectors and more asset classes outside of just US large cap equities. As such, we believe diversification will continue to play an important role in portfolios.

Fixed Income

The Federal Open Market Committee (FOMC) met in January and as anticipated, left the federal funds rate unchanged at 3.50% - 3.75% after delivering three 0.25% rate cuts in 2025. The Fed stated that available indicators suggest that economic activity has been expanding at a solid pace. Job gains have remained low, and the unemployment rate has shown some signs of stabilization. The Fed noted they will also continue purchases of shorter-term Treasury securities to maintain an ample supply of reserves.

We believe there is potential for the Fed to deliver two additional rate cuts in 2026 as the Fed still attempts to reach neutral policy rate, that is neither restrictive nor stimulative, but there continues to be considerable disagreement from individual members on the appropriate target range for rates. Given a relatively robust economic environment, it seems likely that these cuts could be delayed until later in the year.

International Markets

Purchasing managers' reports through December showed Eurozone economic growth slowing in step with the stronger US pace as this year's tariff increases filtered through the global economy. Beyond cyclical pressures, structural weaknesses continued to constrain growth. These include stagnant demographics, onerous regulation, fragmented markets, and the absence of a fully unified financial system. Industrialized, export-driven northern Europe continued to lag due to a challenging trade environment. Less exposure to foreign trade allowed more services-oriented southern European economies to remain on the leading edge of late-cycle growth. Consumer and business confidence have been weakened by a combination of geopolitical concerns, along with fiscal- and trade-policy uncertainties.

Over in Asia, China's economic growth has been driven predominantly by its technology and export sectors, masking structural weaknesses in domestic investment and consumer spending. December business surveys showed the boon in AI contributing to manufacturing growth in Taiwan and South Korea, the latter overcoming headwinds to investment and consumer spending created by the boost to import costs from a weakening currency. AI-related investments also have supported manufacturing gains in Southeast Asia. A business survey showed Japan's services sector pacing an economic growth slowdown at the end of 2025 as the economy braces for further interest-rate hikes by the Bank of Japan in response to recent increases in inflation.

Commodities

Agricultural commodities were hampered by ample global supplies in 2025, which marked the second consecutive year of underperformance against the broader Bloomberg Commodity Index. Since the global supply disruptions of 2022 that resulted in a rapid appreciation of grain prices, the index has struggled to show life. We believe ample global supply, driven by an easing of supply disruptions stemming from the Russia-Ukraine war and strong harvests in Latin America, are key culprits behind the broad weakness in agriculture prices. Additionally, weaker demand for US exports amid US-China trade tensions contributed to excess supplies in the short term and were strong headwinds last year. Despite the federal government's announced $12 billion aid package for farmers, and China's promise to buy more US soybeans, we do not anticipate a material change in the global oversupply.

We suspect that these challenges impacting profitability could eventually drive US farmers to trim supply growth in the years to come. As it stands, the US remains a key producer of global corn, soybean, and wheat production. Therefore, if US producers were to begin curbing output growth, we believe it could be a tailwind for moderately improving prices and sector performance. We see the potential for improved sector performance and outperformances by select commodities that have experienced unique supply challenges. However, ample global supply and evolving trade policies temper our expectations for the Agricultural sector relative to the broader Bloomberg Commodity Index.

What Does This Mean to Me?

Looking ahead, we anticipate the US economy to remain the primary engine of global growth in 2026. This leadership could help stabilize the US dollar. We anticipate strong corporate earnings growth could drive equity market gains as economic momentum accelerates and as AI-related investment expands across sectors. We also highlight the direct late-cycle support from broadening investment beyond the AI-related boom and its ongoing integration with the rest of the economy, encouraged by investment tax credits and by solid corporate earnings growth tied to a vibrant economy. In turn, this could broaden equity market gains to more cyclically sensitive sectors forming the backbone of the industrial economy. As such, despite the recent uncertainty, we continue to advise clients to use any equity pullbacks as an opportunity to deploy sidelined cash.

If you have any questions or concerns, please do not hesitate to reach out to us at any time.

Sincerely,

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payments of interest and/or principal. This risk is heightened in lower rated bonds. If sold prior to maturity, fixed income securities are subject to market risk. All fixed income investments may be worth less than their original cost upon redemption or maturity.
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