

# Investment Strategy

Weekly guidance from our Investment Strategy Committee May 18, 2026

## Alternatives Spotlight: Global M&A surged as investors favor scale and quality ..... 2

- Global Merger & Acquisition (M&A) activity reached new highs in the first quarter despite macroeconomic headwinds, with notable concentration and a perceived flight-to-quality.
- We maintain our favorable view in alternative strategies that demonstrate resilience in the current environment, including Event Driven - Merger Arbitrage, Private Equity - Secondaries, Growth Equity and Small/Mid Buyouts sub-strategies.

## Equities: Hyperscaler Artificial Intelligence (AI) spending soars as ROI<sup>1</sup> questions emerge..... 4

- Hyperscaler capital expenditure (capex) continues to accelerate beyond expectations, now trending above prior consensus assumptions. However, the market narrative is shifting from growth to returns, as elevated capex raises questions around timing of monetization, free cash flow (cash remaining after expenses) durability, and capital efficiency.
- We believe consensus estimates for capex spending — particularly 2027 — remain too conservative, underestimating the persistence of the AI investment cycle. This implies further upside to capex, alongside near-term pressure on hyperscaler valuations.

## Fixed Income: Proposed balance sheet plans add upward pressure to yields... 5

- Incoming Chairman of the Federal Reserve (Fed), Kevin Warsh publicly has stated his intended priority to reduce the Fed's holdings of bonds on its balance sheet as a means to allow lower interest rates.
- These plans may not be implemented and won't happen quickly but represent yet another pressure higher for yields and further our unfavorable outlook for U.S. Taxable Long Term Fixed Income.

## Real Assets: Base metals show their mettle ..... 6

- Base metals prices continue to hit new highs, despite the Iran war clouding the global economic outlook. We believe this resilience can be attributed to demand growth outstripping supply growth, with copper being the clearest example.
- We remain favorable on the base metals sector within commodities and favor adding exposure on pullbacks.

## Current tactical guidance ..... 7

**Investment and Insurance Products: ➤ NOT FDIC Insured ➤ NO Bank Guarantee ➤ MAY Lose Value**

1. ROI = return on investment.

# Alternatives Spotlight

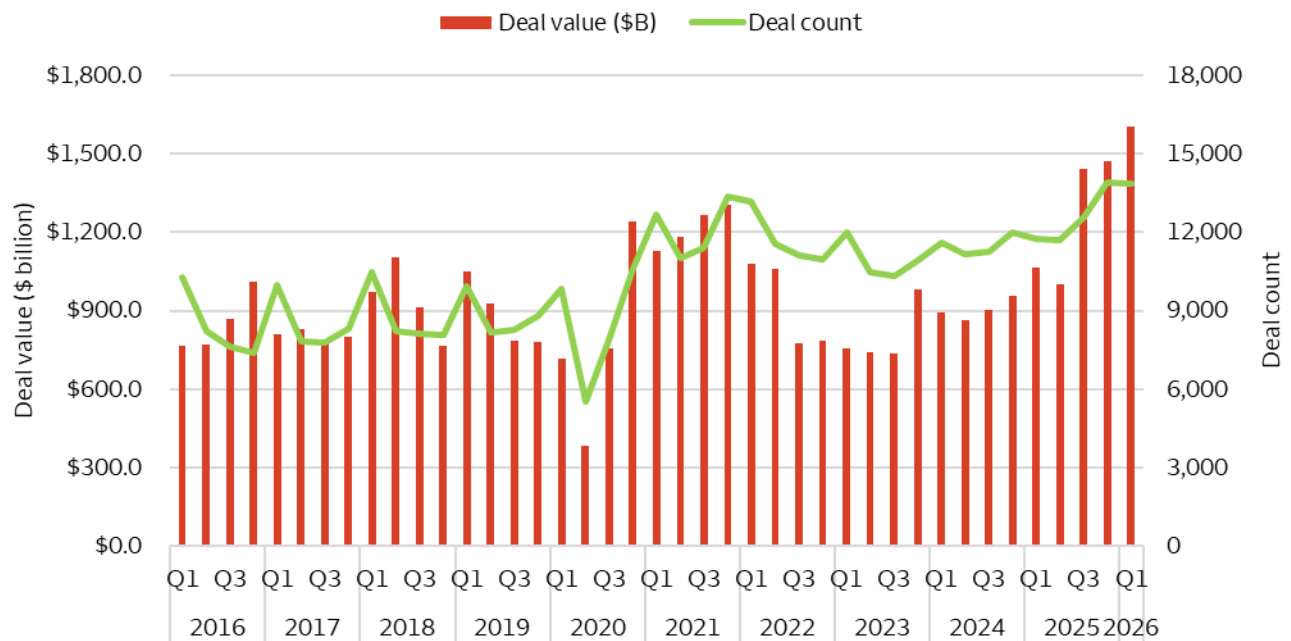
**Chao Ma, PhD, CFA, FRM**

Global Portfolio and Investment Strategist

## Global M&A surged as investors favor scale and quality

Global Merger & Acquisition (M&A) activity reached record levels in the first quarter, despite geopolitical headwinds, public market volatility, inflation concerns, and ongoing supply chain disruptions. According to Pitchbook, quarterly M&A deal value rose to \$1.6 trillion across nearly 14,000 transactions, marking a 9% increase from the prior quarter (see Chart 1). Regionally, activity was particularly strong in North America, which accounted for nearly two-thirds of total deal value.<sup>2</sup> We believe this strength likely reflects investor confidence in the region’s relative economic breadth and resilience.

**Chart 1. Global M&A deal value reached new record in Q1 2026**



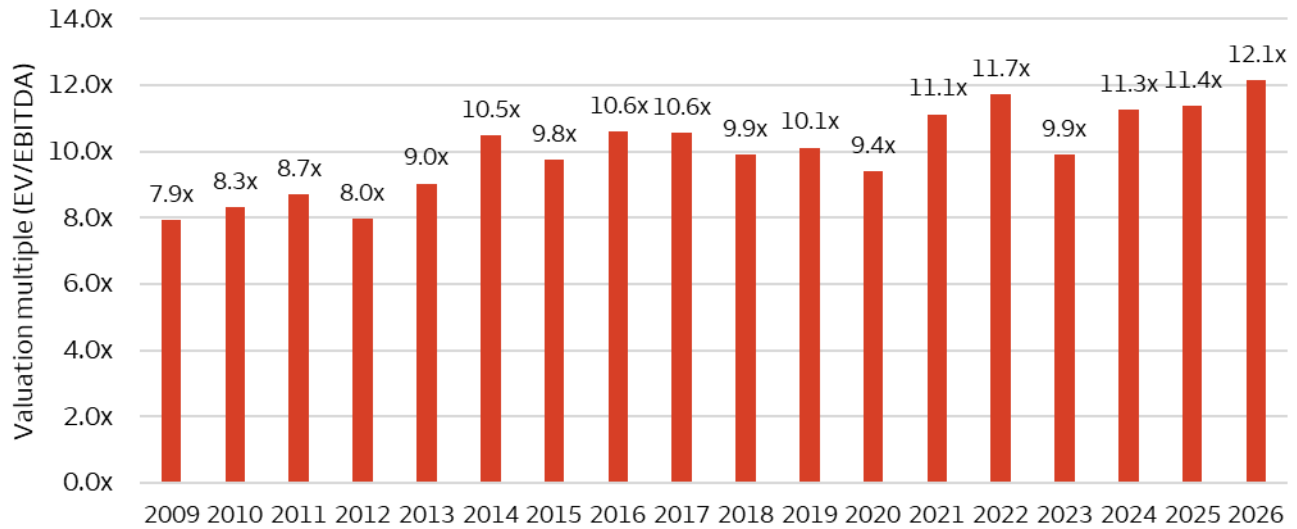
Sources: Pitchbook and Wells Fargo Investment Institute. Data as of March 31, 2026. B = billions. Q1 = First quarter. Q3 = Third quarter.

Beneath these strong headline figures, however, the market continued to exhibit notable bifurcation. The quarter was characterized by a top-heavy M&A deal landscape, with megadeals driving a lot of the growth in total value. We believe this suggests an investor preference for large, high-quality companies. According to Pitchbook, financing was more accessible for high-quality assets, while companies with weaker credit profiles experienced delays.<sup>2</sup> As competition for these high-quality assets intensified, valuation premiums have continued to expand — particularly in the U.S. (see Chart 2).

This bifurcation is also evident across sectors.<sup>2</sup> There has been a rotation in investor focus, away from sectors such as Information Technology, Financials, and Healthcare — where concerns around AI-driven disruption and tighter private credit conditions have become more pronounced. Instead, capital has shifted toward sectors such as Energy and Materials, supported by increased demand for infrastructure and energy transition investments amid geopolitical tensions and supply chain reconfiguration.

2. Pitchbook, “Global M&A Report,” April 29, 2026.

**Chart 2. M&A valuation multiple saw gradual expansion**



Sources: Pitchbook and Wells Fargo Investment Institute. Data as of March 31, 2026. Median EV/EBITDA multiple is shown for U.S. M&A transactions. EV/EBITDA stands for Enterprise Value-to-Earnings Before Interest, Taxes, Depreciation, and Amortization. It is a financial valuation ratio that measures a company’s total value relative to its operational cash earnings. **Past performance is not a guarantee of future results.** For illustrative purposes only.

Another notable trend is the resurgence of strategic corporate buyers as dominant participants in the M&A landscape. While private capital remains active, corporate buyers have largely regained leadership in M&As<sup>3</sup>, which we believe was supported by corporate strong balance sheets, healthy earnings, and their growing need to reposition business in response to shifting macroeconomic conditions.

### Our perspective

Looking ahead, we expect global M&A activity to continue its recovery trajectory, particularly as political and geopolitical uncertainties may begin to ease in the latter part of the year. We see the potential that the current concentration in deal activity may gradually give way to broader market participation as macroeconomic conditions improve.

From a hedge fund strategy perspective, a continued rebound in M&A activity — combined with sustained investor optimism — should support a stable pipeline of transactions, improved deal completion rates, and more stable pricing and spread levels. As a result, we maintain our favorable outlook on Merger Arbitrage sub-strategies.

In private markets, we believe the recovery in M&A activity, particularly alongside renewed private equity participation, should help catalyze the transition into a new growth cycle. In our opinion, the improved deal and exit activity can help reduce the backlog of mature private companies awaiting liquidity events and enable capital to be returned to investors, supporting future investment cycles.

That said, we continue to favor private equity sub-strategies that demonstrate resilience under current conditions, including secondaries, small- and mid- buyouts, and growth equity. Additionally, we expect continued dispersion in private market performance in the near term, given the persistent selectivity in deal-making. We believe strategies with strong track records, sector specialization, differentiated strategies, and a focus on operational value creation may be positioned to outperform in this environment.

**Alternative investments, such as hedge funds, private equity, private debt and private real estate funds are not appropriate for all investors and are only open to “accredited” or “qualified” investors within the meaning of U.S. securities laws.**

3. Pitchbook, “Global M&A Report,” April 29, 2026.

# Equities

**Thomas Christopher**

Equity Sector Analyst, Communication Services and Information Technology

## Hyperscaler AI spending soars as ROI questions emerge

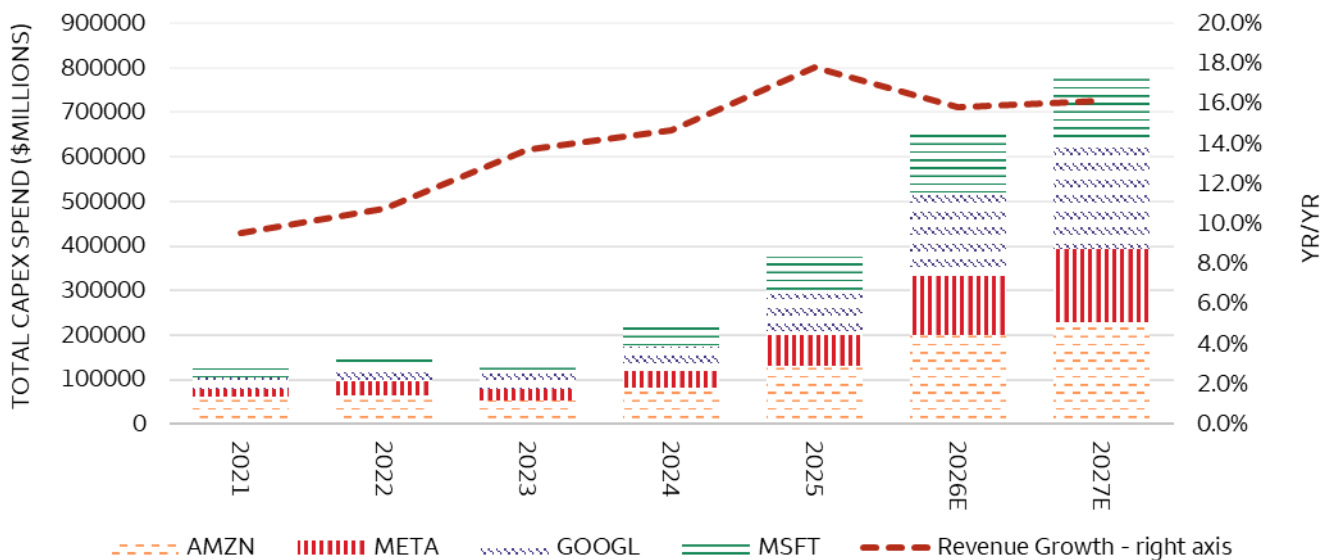
Hyperscaler<sup>4</sup> capex continued to accelerate beyond prior expectations<sup>5</sup>, driven by sustained investment in AI infrastructure across data centers, semiconductors, servers, and networking. While the strategic imperative to build AI capacity remains clear, investor focus has shifted decisively from how much is being spent to when and how those investments generate acceptable returns.

Following recent quarterly earnings, the four major hyperscalers reiterated their commitment to elevated, multi-year capex. Aggregate spending is now projected to exceed \$650 billion in 2026, roughly doubling year-over-year, and consensus is forecasting a 19% increase in 2027<sup>6</sup>. While a portion of the increase reflects higher component and memory costs, we believe forward estimates for 2027 remain conservative and do not fully capture the durability of the AI investment cycle. Incremental upside to capex expectations would likely place additional pressure on near-term free cash flow and capital efficiency metrics.

Hyperscaler (superscript for hyperscalers) management commentary has indicated a willingness to overbuild capacity in an effort to avoid missing near-term AI demand. The unprecedented scale of current spending has amplified scrutiny around return on investment visibility, payback timelines, and monetization pathways. As a result, hyperscaler valuations increasingly reflect concerns around sustained margin and free cash flow dilution.

We do not expect capex to decelerate meaningfully over the next several years, particularly given the long-lived nature of data center assets. Against this backdrop, we remain constructive on the AI infrastructure ecosystem — especially compute and memory semiconductors, power and cooling, networking, and AI stack enablers — where demand visibility and operating leverage remain attractive. By contrast, we are taking a more discerning stance toward hyperscalers amid heightened focus on capital efficiency and return timing.

**Chart 3. Capex spending by largest hyperscalers**



Source: FactSet, company reports, data as of May 11, 2026 and represents calendar year. Four hyperscalers include Amazon (AMZN), Meta Platforms (META), Alphabet (GOOGL), and Microsoft (MSFT). E = estimate. For illustrative and educational purposes only; not a recommendation to buy or sell any security or adopt any investment strategy.

4. Also known as hyperscale cloud providers, are companies who develop and operate networks of data centers to facilitate cloud computing.

5. According to FactSet estimates.

6. According to FactSet estimates, as of May 11, 2026.

## Fixed Income

**Tony Miano, CFA, CAIA**

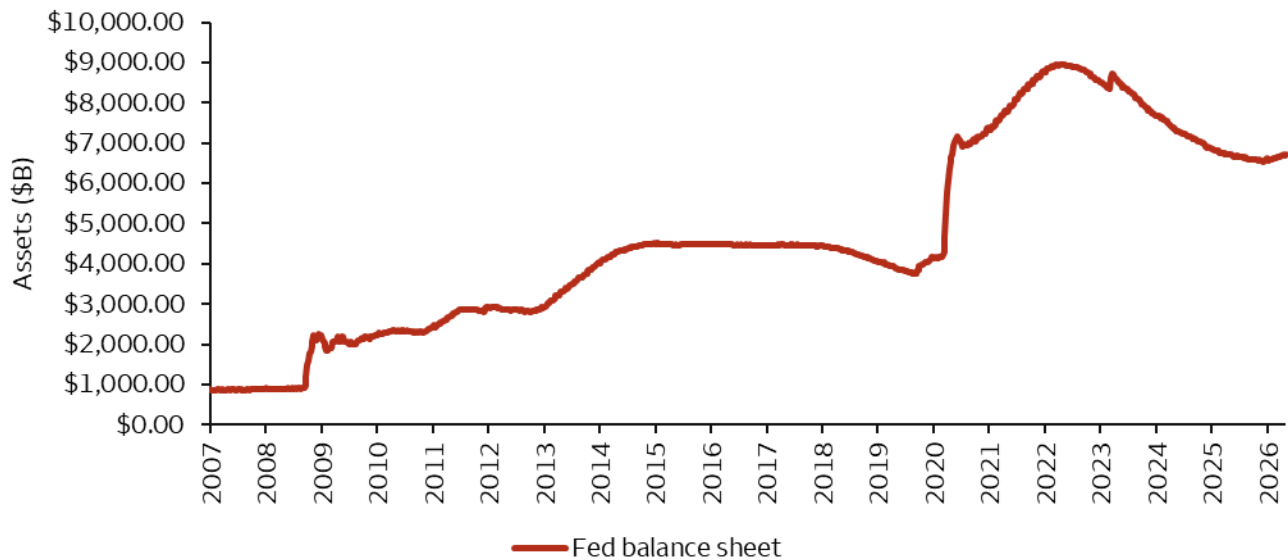
Investment Strategy Analyst

### Proposed balance sheet plans add upward pressure to yields

Since before his Senate confirmation as incoming Chairman of the Fed, Kevin Warsh publicly stated his intended priority to reduce the Fed's holdings of bonds on its balance sheet. While Warsh believes this approach will give the Fed flexibility to lower short-term policy rates, reducing the Fed's bond holdings could push long-term bond prices down and yields higher as fewer buyers would be supporting the market. This change isn't guaranteed, but is still a dynamic we believe investors should still be aware of.

Warsh points out a very real dynamic, that the Fed's balance sheet has ballooned in recent decades. The balance sheet at its peak in 2022 was more than eight times its pre-Great Financial Crisis value and almost doubled in the fallout from COVID-19 alone (see Chart 4). Even after attempts to rein in the balance sheet, it ultimately settled at well-above pre-COVID levels.

**Chart 4. Increase in the Fed balance sheet since 2007**



Source: Federal Reserve, date as of May 6, 2026. Measures total assets of the Fed less eliminations from consolidation. B = billions. The Fed's balance sheet primarily consists of Treasuries and Mortgage-Backed Securities.

What may be missed in this analysis is the impact the balance sheet has on the supply and demand dynamics of Treasuries, as the Fed is a significant buyer and holder of them. When the Fed decides to buy less securities or even sell them, more bonds would need to be absorbed by private investors, while one of the market's largest buyers steps back. We believe that this change in dynamic may negatively impact Treasury prices and lead to higher yields, particularly as significant debt must be issued to fund ongoing budget deficits in the coming years.<sup>7</sup>

It is important to note that Fed decisions are made by committee. Warsh does not have the authority to make these changes; a majority of Fed governors must agree, which should take some convincing. While shrinking the Fed balance sheet might not be a guarantee, it does pose another potential risk for long-term yields. With the potential for long-term taxable fixed income yields to continue their rise from here, we remain unfavorable. Intermediate-term bonds, in the 3-7 year maturity range, may provide a better mix of risks and returns.

7. See Wells Fargo Investment Institute report, "Paying America's Bills," May 11th, 2026, for more information on the budget deficit and debt.

# Real Assets

**Sameer Samana, CFA**

Head of Global Equities and Real Assets

## Base metals show their mettle

Within commodities, energy and precious metals often get most of the headlines given their larger weightings in most major indexes, especially during geopolitical turbulence like the Iran war. However, base metals, like copper, have quietly been hitting new highs in the background, increasing +35.37% as a group over the past year from May 12, 2025, to May 11, 2026 (see Chart 5). The core driver of this positive performance has been a structural shortage between demand and supply growth.

**Chart 5. Base metals continue their march higher**



Sources: Bloomberg and Wells Fargo Investment Institute. Daily data from May 12, 2023, through May 12, 2026. BCOMINTR = Bloomberg Industrial Metals Subindex Total Return. SMAVG (50) = 50-day simple moving average. SMAVG (200) = 200-day simple moving average. RSI = relative strength index.

Using copper as an example, demand is coming from a variety of industrial, electrical, and construction-related companies involved in everything from housing to the AI-related buildout of data centers. According to Bloomberg, that demand has been growing about 3% per year, while mined production has only been growing at about 2% rate per year. Scrap metal and recycling can help to alleviate some of the shortfall, but it is structural in nature, especially as AI demands further increase the need for data centers and power. Also, while copper producers might want to take advantage of this upswing in demand and produce more, it can take years to increase production at an existing mine and decades to bring a new one online.

These structural supply-demand imbalances are not isolated to copper and extend to other base metals, along with impacts from recently enacted tariffs. These reasons make us optimistic on the outlook for base metals, and we retain a favorable rating. Investors should look at pullbacks as opportunities to add exposure to the sector within commodities.

## Tactical guidance\*

### Cash Alternatives and Fixed Income

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
	U.S. Long Term Taxable Fixed Income U.S. Short Term Taxable Fixed Income	Cash Alternatives Developed Market Ex-U.S. Fixed Income Emerging Market Fixed Income High Yield Taxable Fixed Income	U.S. Intermediate Term Taxable Fixed Income	

### Equities

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
	U.S. Small Cap Equities	Developed Market Ex-U.S. Equities Emerging Market Equities	U.S. Large Cap Equities U.S. Mid Cap Equities	

### Real Assets

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Commodities Private Real Estate	Private Infrastructure	

### Alternative Investments\*\*

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Hedge Funds—Equity Hedge Hedge Funds—Macro Hedge Funds—Relative Value Private Equity Private Debt	Hedge Funds—Event Driven	

Source: Wells Fargo Investment Institute, May 18, 2026. Please see Wells Fargo Investment Institute's Asset Allocation Strategy Report for more detailed, investable ideas in each asset group.

\*Tactical horizon is 6-18 months

\*\*Alternative investments are not appropriate for all investors. They are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. Please see end of report for important definitions and disclosures.

### Risk considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Small- and mid-cap stocks** are generally more volatile, subject to greater risks and are less liquid than large company stocks. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation and other risks. Prices tend to be inversely affected by changes in interest rates. **High yield (junk) bonds** have lower credit ratings and are subject to greater risk of default and greater principal risk. Although **Treasuries** are considered free from credit risk they are subject to other types of risks. These risks include interest rate risk, which may cause the underlying value of the bond to fluctuate. The **commodities** markets are considered speculative, carry substantial risks, and have experienced periods of extreme volatility. Investing in a volatile and uncertain commodities market may cause a portfolio to rapidly increase or decrease in value which may result in greater share price volatility. **Real estate** has special risks including the possible illiquidity of underlying properties, credit risk, interest rate fluctuations and the impact of varied economic conditions.

In addition to the risks associated with investment in debt securities, investments in mortgage-backed securities will be subject to prepayment, extension and call risks. Changes in prepayments may significantly affect yield, average life and expected maturity.

Alternative investments, such as hedge funds, private equity/private debt and private real estate funds, are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. They entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than mutual funds. Hedge fund, private equity, private debt and private real estate fund investing involves other material risks including capital loss and the loss of the entire amount invested. A fund's offering documents should be carefully reviewed prior to investing.

Hedge fund strategies, such as Equity Hedge, Event Driven, Macro and Relative Value, may expose investors to the risks associated with the use of short selling, leverage, derivatives and arbitrage methodologies. Short sales involve leverage and theoretically unlimited loss potential since the market price of securities sold short may continuously increase. The use of leverage in a portfolio varies by strategy. Leverage can significantly increase return potential but create greater risk of loss. Derivatives generally have implied leverage which can magnify volatility and may entail other risks such as market, interest rate, credit, counterparty and management risks. Arbitrage strategies expose a fund to the risk that the anticipated arbitrage opportunities will not develop as anticipated, resulting in potentially reduced returns or losses to the fund.

Merger arbitrage involves investing in event driven situations such as reorganizations, spin-offs, mergers, and bankruptcies, and involves the risks that the proposed opportunities in which the fund may invest may not materialized as planned or may be renegotiated or terminated which can result in losses to the fund.

Sector investing can be more volatile than investments that are broadly diversified over numerous sectors of the economy and will increase a portfolio's vulnerability to any single economic, political, or regulatory development affecting the sector. This can result in greater price volatility.

### Definitions

The Bloomberg Industrial Metals Subindex Total Return measures the performance of a basket of industrial (base) metals futures contracts, including aluminum, copper, nickel, zinc, and other economically sensitive metals. The index reflects both price changes in the underlying commodities and the return from rolling futures contracts, as well as collateral yield from the investment of margin or cash positions.

Pitchbook uses a variety of publicly available sources found in targeted online searches including more than 1,000,000 web crawlers using natural language processing and machine learning, secondary sources (those authored by someone not directly involved in the deal or fund), news (largest source of information) and other online sources. Quality assurance uses preventive validations, corrective validations, and mutual reviews in an effort to ensure accuracy of data. Data is educational and illustrative purposes only and there are no guarantees as to accuracy of data or content.

An index is unmanaged and not available for direct investment.

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