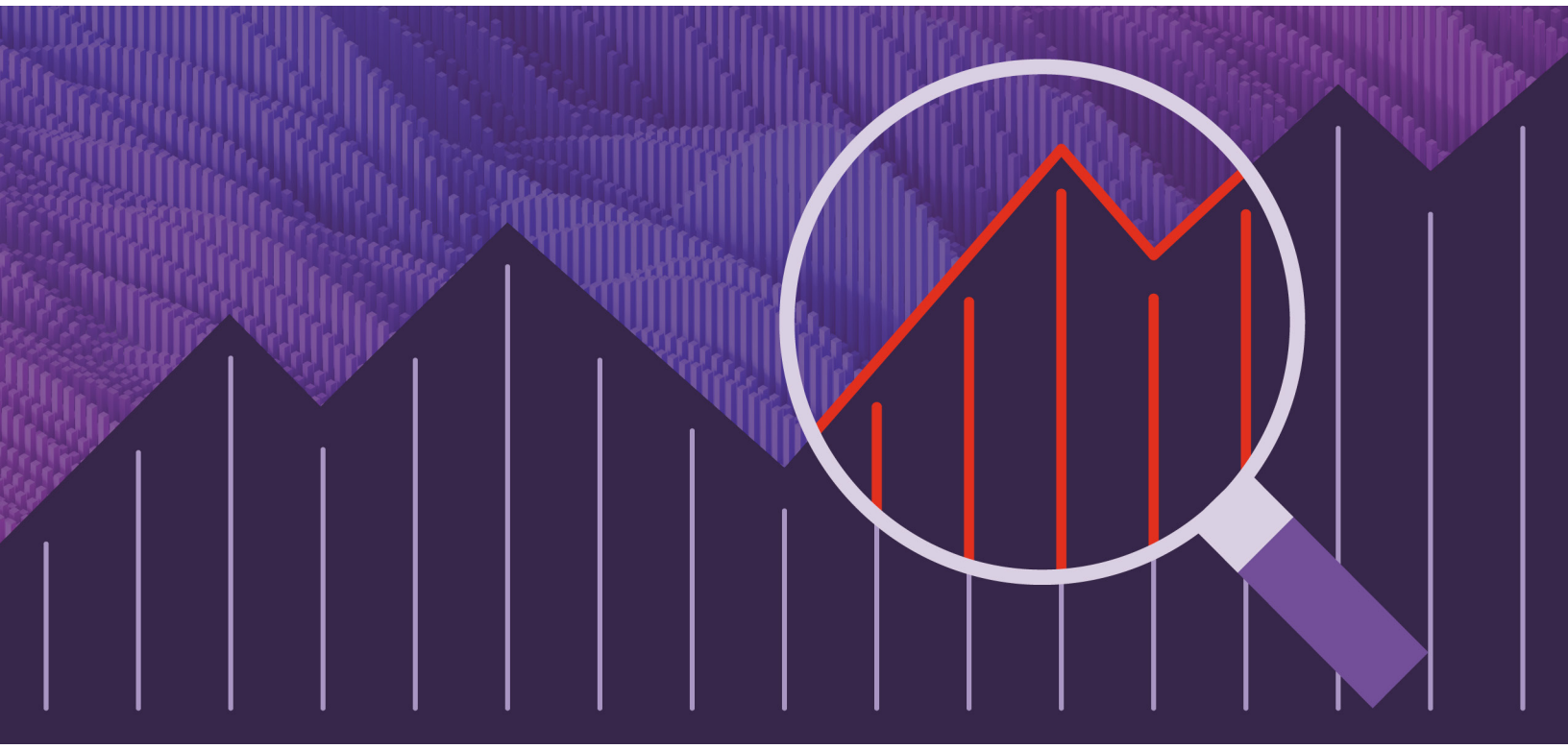
White Paper

A Market in Transition



The S&P 500 is up more than 100% since the October 2022 lows. As prices have risen, expectations have risen with them.

Coming out of the 2022 bear market, the average Wall Street analyst expected roughly a 4% return for the S&P 500 in 2023. Today, expectations look very different. The average estimate for 2026 is closer to 12%.

Exhibit 1: Evolution of Key Market Indicators (S&P 500)

	2023	2024	2025	2026
S&P 500	26.1%	24.9%	17.8%	?
Earnings Growth	0.9%	10.1%	12.4%	14.7%*
Starting Valuations	17.2x	20.5x	22.6x	23.0x
y/y growth	—	19.2%	10.2%	2.0%
Wall St Strategist Prediction Avg. among 10+ firm targets	3.9%	4.0%	10.0%	11.9%
Starting Sentiment	Fear	Greed	Neutral	Greed
US Equity ETF Flows CNN Fear & Greed Index	Below 2021 record	New record	New record	?

Source: Morningstar Direct, FactSet, Yahoo Finance. *FactSet 2026 consensus earnings estimates. For illustrative purposes only.

Higher expectations create higher hurdles. The market's price-to-earnings (P/E) multiple has increased 34%, rising from 17.2 to 23.0 at the start of this year.

That multiple expansion has been accompanied by strong execution. Corporate earnings among S&P 500 companies have reached new all-time highs in each of the past three years.

Still, investing based on what has worked in recent years is rarely a durable strategy. From today's starting point, execution risk among US large-cap companies is meaningfully higher than it was in 2023. Delivering double-digit earnings growth in back-to-back years is a very high bar.

It could happen—indeed, it's expected.

But for anyone advising clients, this may be an opportune moment to consider diversification to build portfolio resilience should those expectations fall short.

That raises a natural question: which parts of the market carry lower expectations—similar to where the S&P 500 stood in 2022?

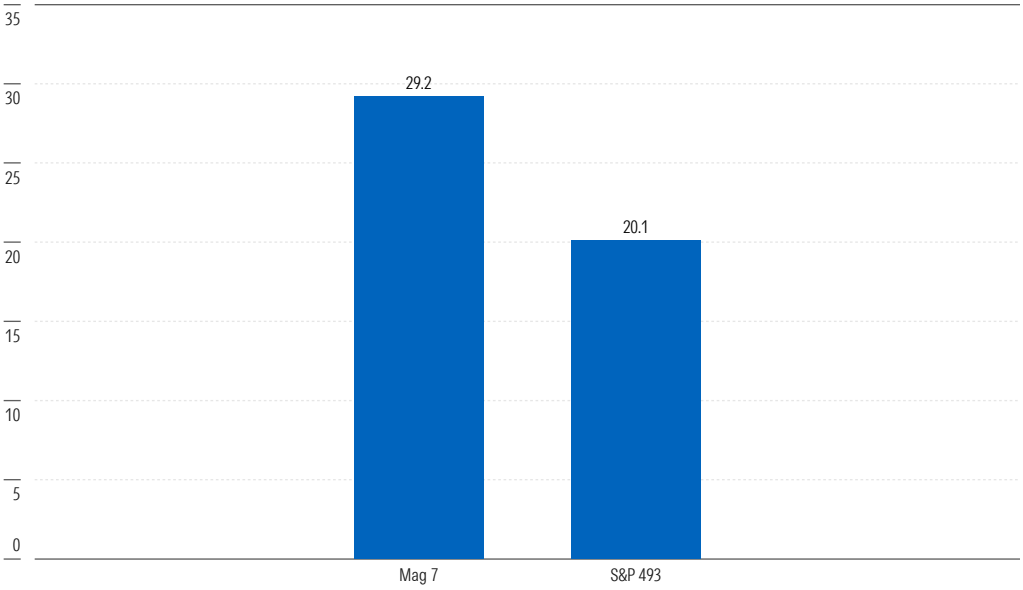
US Value Stocks

While the S&P 500 looks expensive at the index level, not everything inside the index is priced the same. A narrow group of mega-cap growth stocks—most notably the Magnificent Seven—has driven much of the market's multiple expansion.

Strip those companies out, and a different picture emerges.

While the average forward P/E among Mag 7 companies is north of 29, it's closer to 20 for the other 493 companies.

Exhibit 2: Under the Hood of the S&P 500 (Forward P/E)
While the index remains expensive that's not true of all stocks in the index.



Source: Morningstar Direct. Data as of December 31, 2025. Investments can't be made directly into an index. For illustrative purposes only.

Many value-oriented sectors and stocks within the S&P 500 still trade at more modest valuations, closer to long-term averages. Headline valuation metrics, in other words, are being skewed by a small number of very large stocks, masking pockets of value beneath the surface.

For investors willing to look past the index and focus on composition, US value stocks offer exposure to companies where expectations remain more restrained—and where the bar for positive surprise may be lower.

US Small Caps

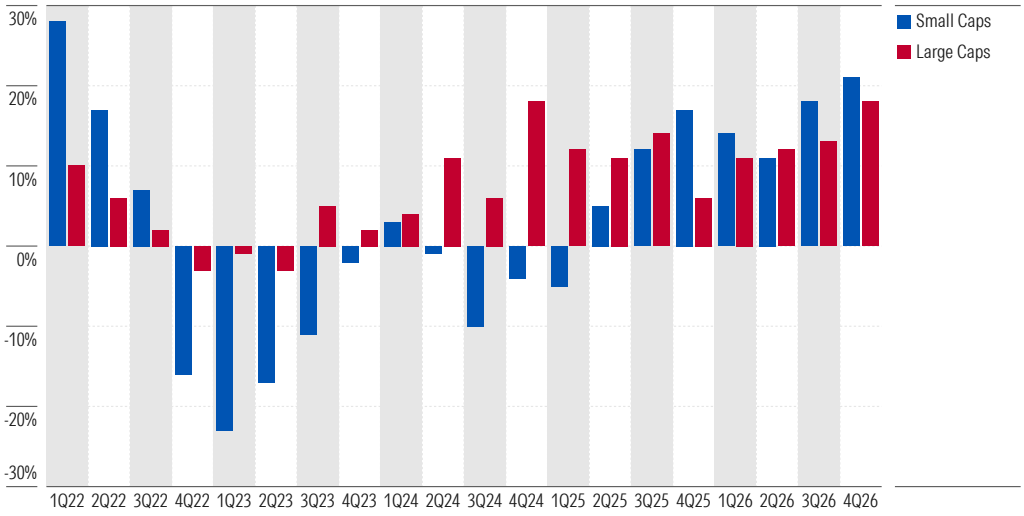
After a difficult decade relative to large caps, many observers have remarked that "large caps trend while small caps oscillate."

The logic is straightforward. Small caps have experienced brief periods of sharp outperformance in recent years, but those rallies have struggled to persist. The more important question, then, isn't whether small caps can rally—but whether they can sustain leadership.

Earnings are a good place to look.

According to Bank of America, small-cap earnings growth is expected to be positive in every quarter of 2026—the first time in nearly five years—and is projected to outpace large-cap earnings growth for the full year.

Exhibit 3: Small Cap Earnings Resurgence
Earnings growth expected to be positive in 2026 and eclipse large caps for the full year.



Source: Bank of America Global Research. FactSet data. Large caps = S&P 500. Investments can't be made directly into an index.

That provides a fundamental backdrop for recent performance. Of course, these are expected earnings, not guaranteed ones. Companies still need to execute.

But as JPMorgan's Michael Cembalest often reminds investors, markets tend to move well ahead of the news. During the Global Financial Crisis, bank stocks bottomed out when only 8% of eventual bank failures had occurred.

In short, markets don't wait for outcomes. They anticipate them. Small caps may already be pricing in better fundamentals ahead.

Non-US Stocks

Last year marked the strongest calendar-year performance for non-US stocks in more than a decade. Importantly, that strength has not erased their valuation advantage. Relative to US equities, international markets still trade at reasonable—and in many cases discounted—multiples.

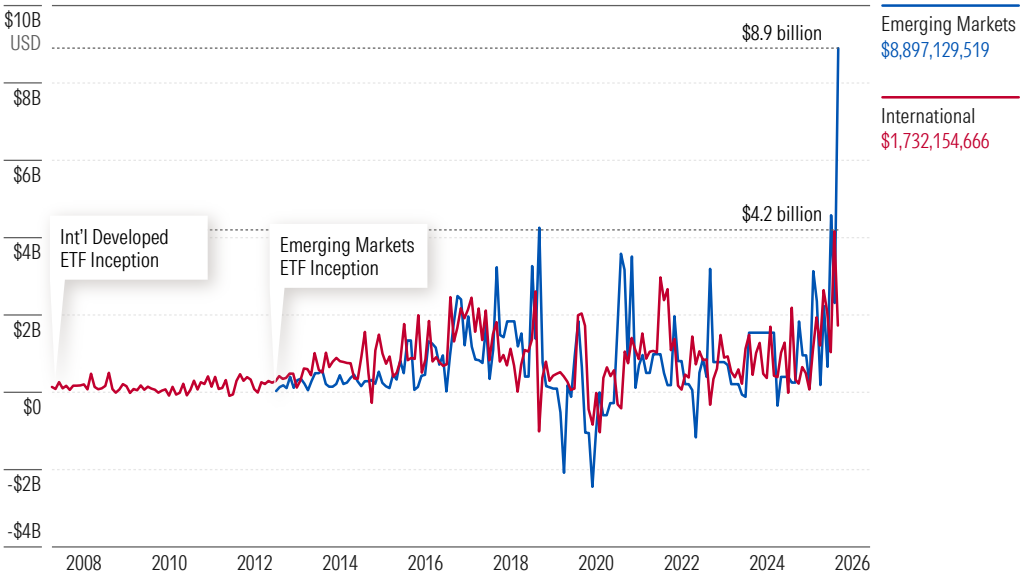
The macro backdrop has also improved. A declining US dollar has provided a tailwind for non-US returns, while fiscal policy abroad has shifted. Austerity, once common across Europe, has largely faded. Government spending has increased, creating a potential catalyst for growth and earnings.

And, as always, nothing changes sentiment like prices.

Non-US stocks outperformed US stocks last year by the widest margin in more than a decade. Investors now appear to be playing catch-up. December and January saw the largest inflows on record into the biggest international and emerging-market ETFs.

Exhibit 4: Record Inflows to Non-US Stocks

Monthly flows into largest international and emerging-market ETFs ($ billions)



Source: Morningstar Direct. Data as of February 2, 2026. iShares Core MSCI Emerging Markets and Vanguard FTSE Developed Markets used for analysis. References to specific securities not an offer to buy or sell. For illustrative purposes only.

For years, many allocators faced few questions about underweighting non-US stocks. After a year of decisive outperformance, that may be changing. These flows may reflect investors revisiting long-standing assumptions.

It's also worth remembering that non-US stocks still represent roughly 40% of global equity market capitalization. Choosing not to own them is a meaningful bet that they will continue to underperform.

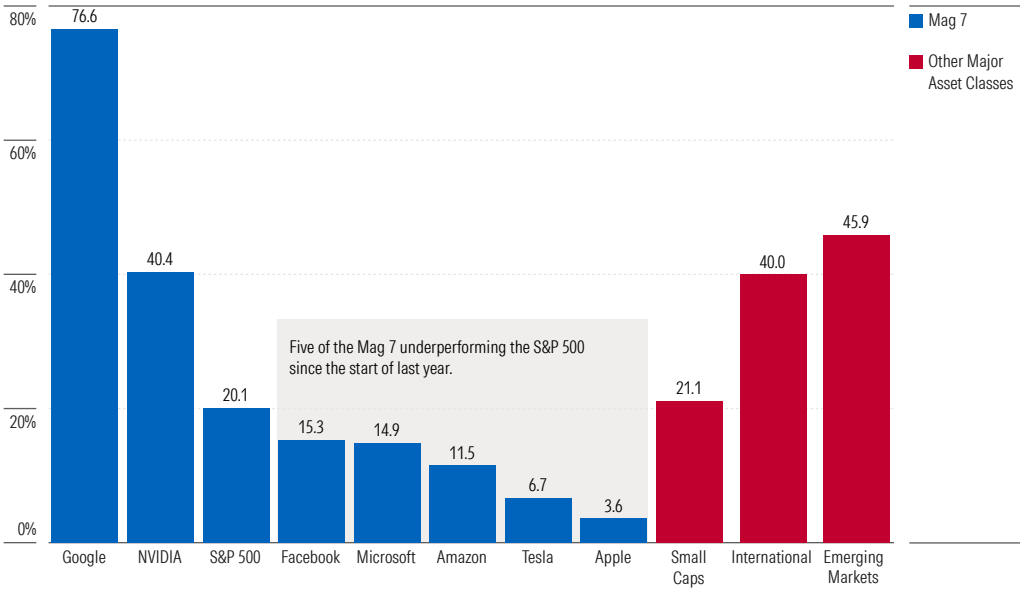
After years of muted returns and low expectations, non-US stocks now sit at the intersection of improving fundamentals, supportive currency dynamics, and renewed investor interest.

A Market That's Starting to Widen Out

Taken together, these trends suggest a market no longer driven by a single trade.

Since the start of 2025, the Magnificent Seven has begun to lose leadership. Five of the seven have underperformed the S&P 500—a sharp reversal from 2023 and 2024. Only Alphabet and Nvidia have continued to beat the index.

Exhibit 5: Magnificent Seven (Mag 7) Leadership Thinning Out
January 2025–January 27, 2026



Source: Morningstar Direct. Reflects performance from Jan. 2025 through Jan. 27, 2026. Past performance no guarantee of future results. References to individual securities not an offer to buy or sell. Investments can't be made directly into an index.

At the same time, small caps, international stocks, and emerging markets have all outpaced the S&P 500.

The fundamental case for US large caps isn't broken—but investing based solely on what worked most recently rarely is a winning strategy. The more relevant question is where expectations remain lower, and where the next phase of market leadership may emerge.

As leadership broadens, investors may want to look beyond the most crowded corners of the market toward areas that have been overlooked in recent years.

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