

VALUES-ALIGNED INVESTING

# Rally to New Highs, *Retreat, Repeat.*



Q2 2026 · PREPARED BY

**Theresa Gusman**

Chief Investment Officer, Formative

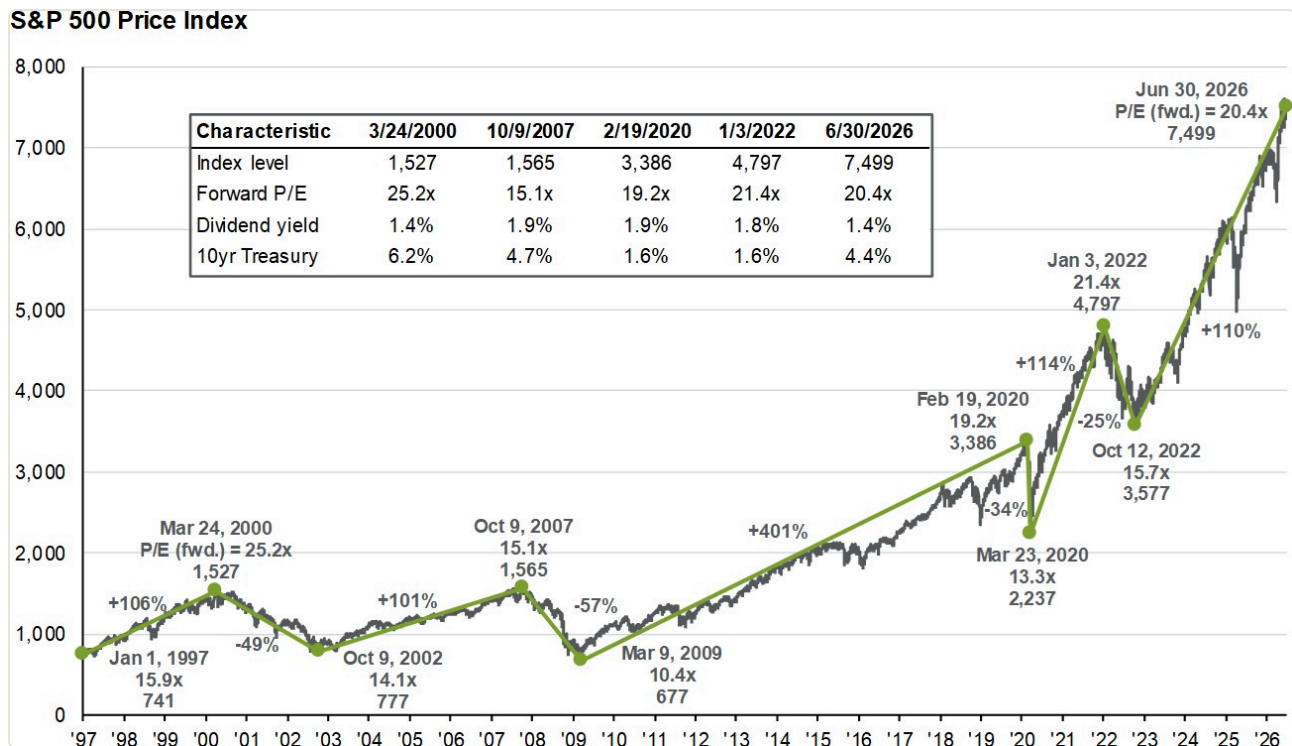
## Rally to New Highs, Retreat, Repeat

Global markets have spent 2026 violently repricing war risk, inflation risk, and AI skepticism, only to snap back to record highs as strong earnings growth prevails. The S&P 500 started 2026 at 6,858.47, sat essentially flat at 6,878.88 on Friday, February 27th, the day before the Iran conflict began, and closed effectively unchanged at 6,886.24 on Monday, April 13th, the day the US initiated its first naval blockade of the Strait of Hormuz. At the same time, the US economy is resilient; consumer spending remains strong, despite abysmal consumer sentiment; oil prices have retreated and inflation is in check; and corporate earnings continue to surge higher.

After retreating 4.3% in the first quarter, the S&P 500 rallied 15.20% in the second quarter, resulting in a six-month gain of 10.19%. As we saw in 2025, markets continue to move rapidly from resiliency → panic → new highs, reinforcing the importance of staying invested during volatile periods. In the wake of the Iran conflict and its aftermath – modestly higher oil prices and inflation and a defanged Iran – AI volatility, and a persistently strong earnings outlook – the market focus shifted from pricing energy shock to pricing earnings resilience. Now the renewed fighting in Iran and AI-related concerns have ushered in the summer doldrums. As the war fades into the background and oil prices fall below \$70 in the coming months, we anticipate a return to the growth themes that outperformed in the second quarter – including agentic AI and all its inputs large and small.

The first six months of 2026 reinforced our view that uncertainty is a feature, not a bug for the current Administration, and we must learn to live with volatility as President Trump initiates aggressive actions and issues sweeping edicts to bring adversaries to the table, only to retreat to pragmatism. Amidst chaos, the US economy remains resilient; inflation is only modestly higher; unemployment is in check; and corporate earnings and valuations are not overly stretched.

Figure 1. S&P 500 at Inflection Points — Bull and Bear Markets, 1996 to Date

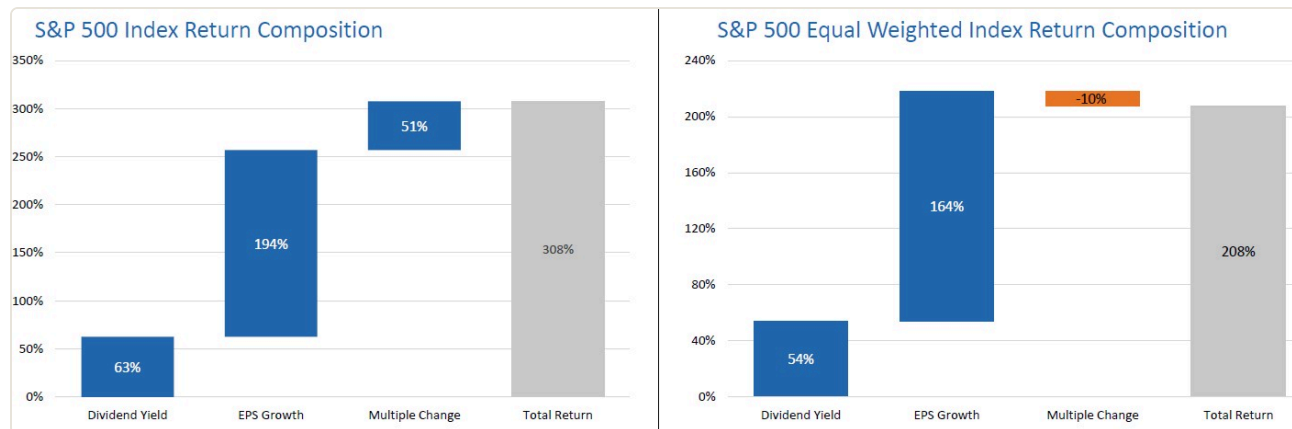


## EARNINGS, MULTIPLES & TOTAL RETURNS

# Earnings Growth, Multiple Expansion, Total Returns

The return of an index can be decomposed into the contribution from dividends, earnings growth, and the change in the P/E multiple. The S&P 500 has returned a cumulative 308% over the past 10 years. Over the past decade, nearly two-thirds of the 308% increase in the S&P 500 (194%) can be attributed to earnings growth. P/E expansion accounted for only 17% of the index return over the past decade – despite higher earnings expectations, which normally would drive multiple expansion. For the equal weighted S&P 500, the P/E multiple contracted over the past decade despite strong earnings growth (see Figure 2).

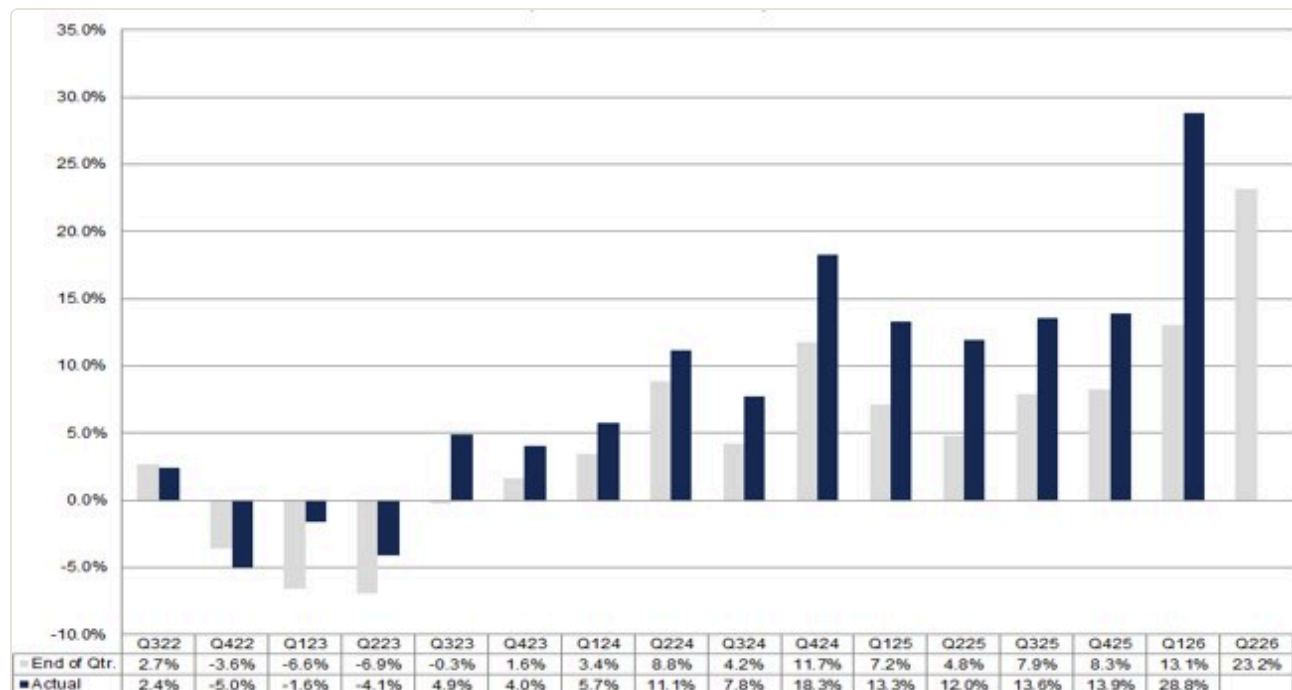
**Figure 2. S&P 500 Total Return Composition, 10 Years Ended June 30, 2026**



Source: Touchstone Investments – Bloomberg. Cumulative total returns over the last 10 years through June 2026.

According to FactSet, the S&P 500 is poised to post strong 23.6% in the second quarter, marking the second consecutive quarter of year-over-year earnings growth above 20% for the index. Most S&P 500 companies report actual earnings above estimates, however, and based on the average improvement in the earnings growth rate during the earnings season, the index will likely report earnings growth above 29% for Q2 (see Figure 3). This would be the highest earnings growth rate reported by the index since Q4 2021 (32.0%).

**Figure 3. S&P 500 Earnings Growth — End of Quarter Estimate v Actual, Q322–Q226**

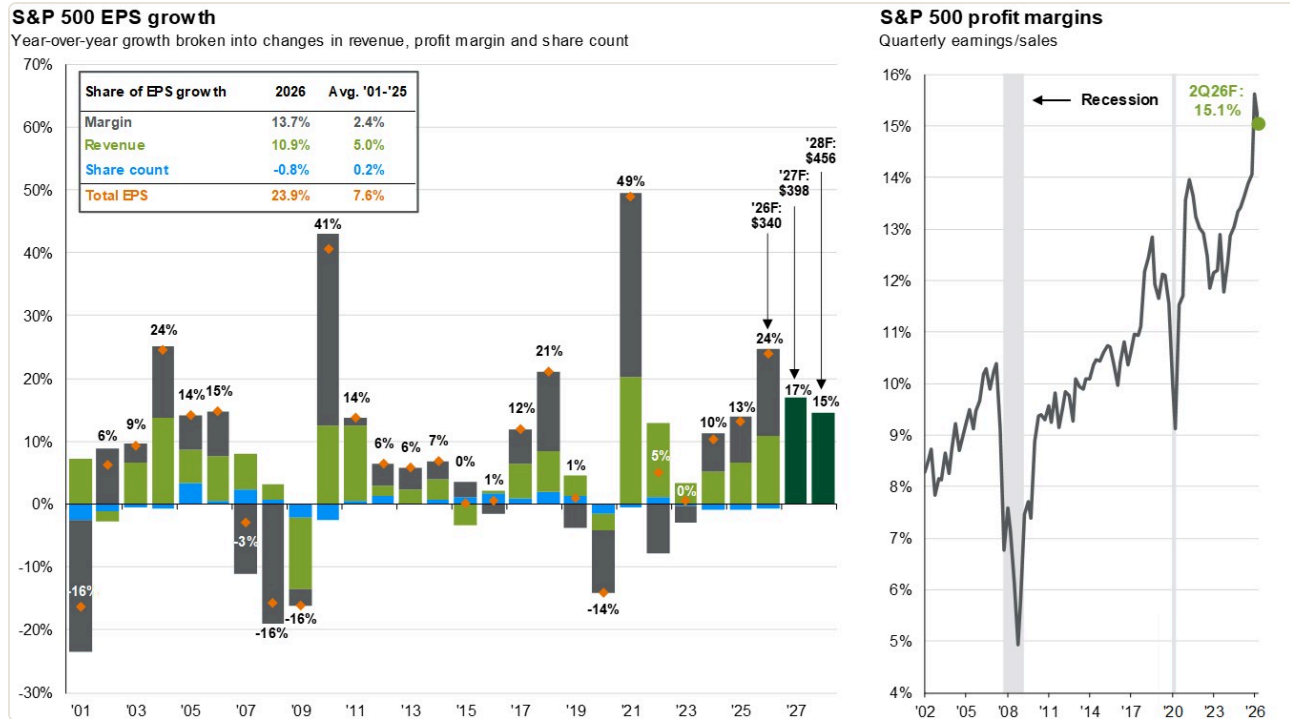


Source: FactSet.

For the full year 2026, JP Morgan targets 23.9% earnings growth for the S&P 500, with 10.9% of that growth coming from revenue increases and an extraordinary 12.7% coming from margin expansion. The

expansion in net profit margins has been remarkable (see Figure 4), with margins approaching 16% in the first quarter and set to exceed 15% in the second quarter, with significant margin disparity across sectors and companies.

**Figure 4. Sources of Earnings Growth and Profit Margins, 2021–28E**



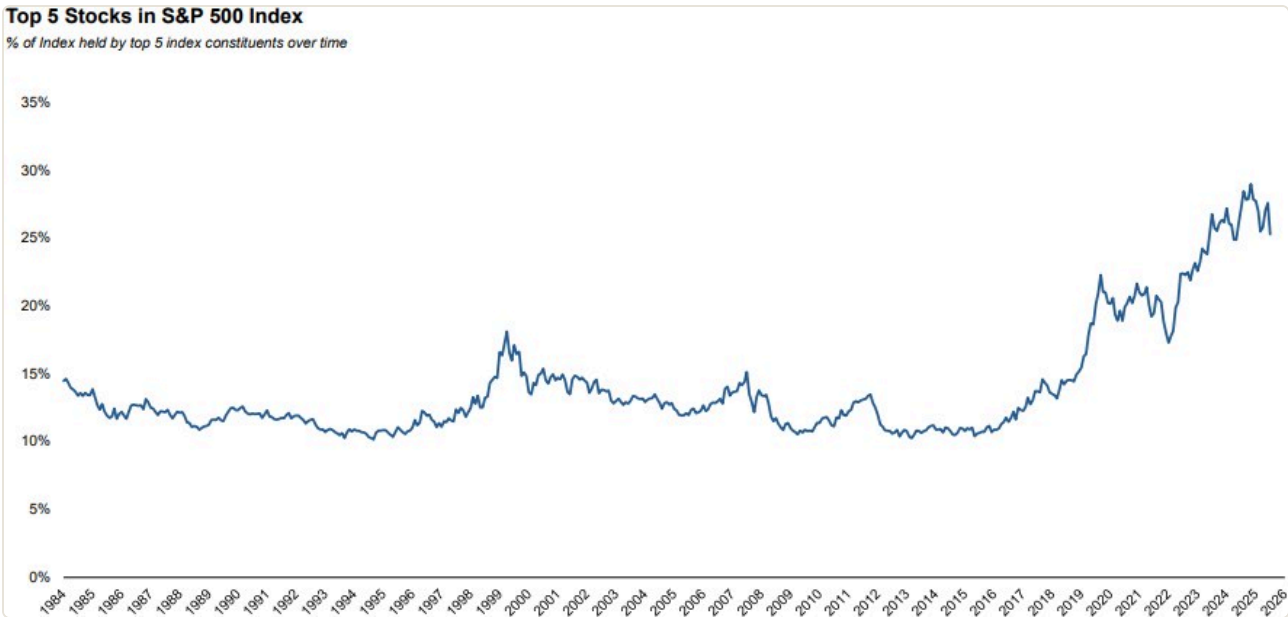
Source: J.P. Morgan Asset Management Guide to the Markets – U.S. Data are as of June 30, 2026.

## GLOBAL MARKET COMPOSITION

# The Changing Face of Global Equity Markets

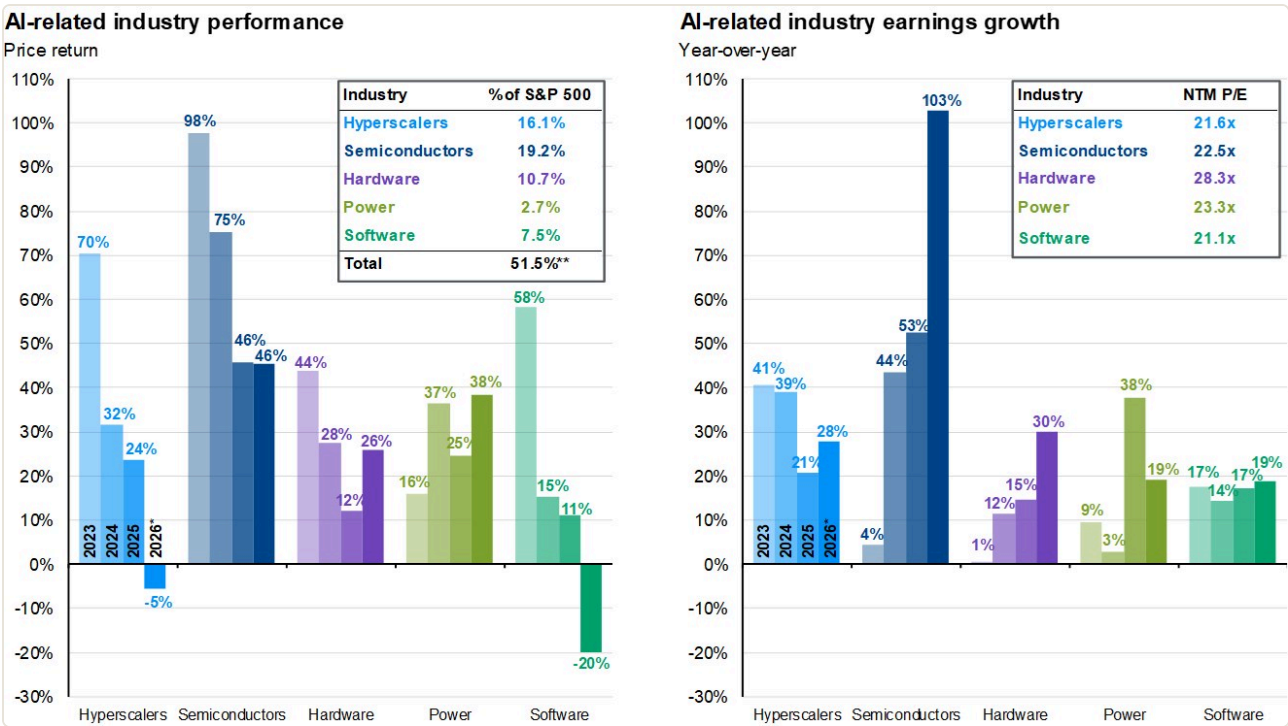
The earnings growth and margin expansion over the past decade have been fueled by the dramatic shift in market composition with the advent of Artificial Intelligence and massive associated capital expenditures. This is reflected in the market concentration chart below (see Figure 5) – which shows the dramatic rise in the weight of the Top Five stocks in the S&P 500 over the past several years. Figure 6 shows the exceptional returns and earnings growth of AI-related companies – including the hyperscalers, plus semiconductor, hardware, power, and software companies – in recent years. With their extraordinary performance, according to JP Morgan, these companies now comprise 51.5% of the S&P 500. Their earnings growth remains strong, and their next 12 months (NTM) P/E ratios remain reasonable, suggesting further gains.

Figure 5. Market Concentration, 1984–2026



Source: FactSet as of 6/30/2026.

Figure 6. AI-Related Industries — Performance and Earnings Growth, 2023–26

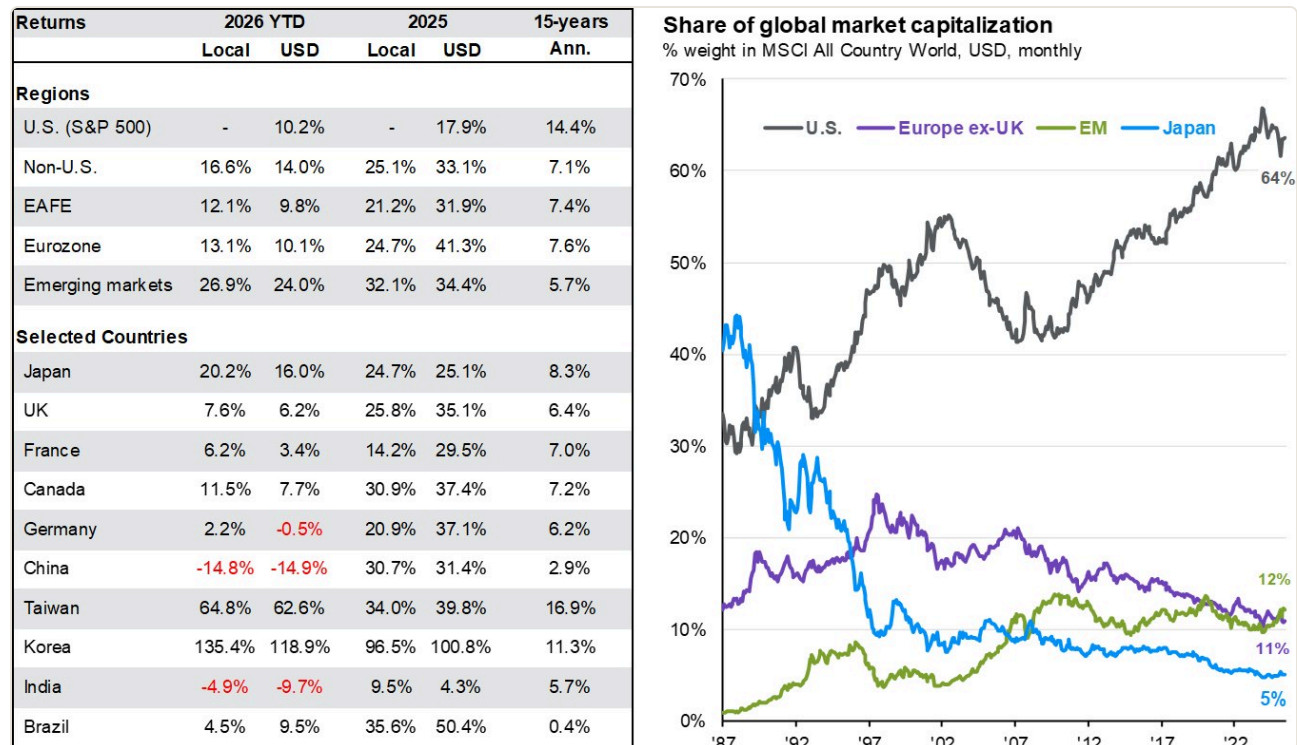


Source: J.P. Morgan Asset Management Guide to the Markets. MSCI, Standard & Poor's, J.P. Morgan Asset Management. Data are as of June 30, 2026.

Changes in market composition extend well beyond the composition of the S&P 500. As shown in Figure 7, S&P 500 performance has been nearly two times the performance of the rest of the world over the past 15 years, and the US now comprises 64% of the MSCI All Country World Index (ACWI). The divergent performance of AI “haves and have nots” is dramatically reflected in the performance

emerging markets in the second quarter. The MSCI Emerging Markets index advanced 24.0% (in USD) in the first half of 2026, with Korea surging 118.9% and Taiwan rising 62.6%, while China fell 14.9%. Korean and Taiwanese equity market performance has been driven by Samsung Electronics and Taiwan Semiconductor (TSMC), which have been fueled by the AI boom. These stocks now comprise 31.5% and 46.0% of the Korean and Taiwanese Morningstar Country Indices, respectively (see Figure 8). The Dutch equity market is even more concentrated, with ASML – the world’s largest manufacturer of semiconductor production equipment – comprising 50.7% of the Morningstar Country Index.

**Figure 7. Global Equity Markets — Performance and Share of Global Market Capitalization**



Source: J.P. Morgan Asset Management Guide to the Markets, June 30, 2026.

**Figure 8. Selected AI-Related Stocks, Weight in Morningstar Country Indices, May 2025–26**

| Company              | Country     | Weight in Morningstar Country Index (%) May 2026 | Weight in Morningstar Country Index (%) May 2025 |
|----------------------|-------------|--------------------------------------------------|--------------------------------------------------|
| Alphabet             | USA         | 3.6                                              | 2.1                                              |
| Broadcom             | USA         | 2.9                                              | 2.0                                              |
| Taiwan Semiconductor | Taiwan      | 46.0                                             | 41.5                                             |
| Samsung Electronics  | Korea       | 31.5                                             | 19.7                                             |
| ASML                 | Netherlands | 50.7                                             | 33.2                                             |
| Alibaba              | China       | 9.0                                              | 8.8                                              |
| Tokyo Electron       | Japan       | 2.1                                              | 1.3                                              |

Source: Morningstar Direct for Indexes and PitchBook Equity Data. Data as of May 29, 2026, for index data.

The extreme concentration across global equity markets suggests an increase in correlation across selected markets (including the US, Korea, Taiwan, the Netherlands) and volatility, amid periodic shifts in AI sentiment from euphoria to despair.

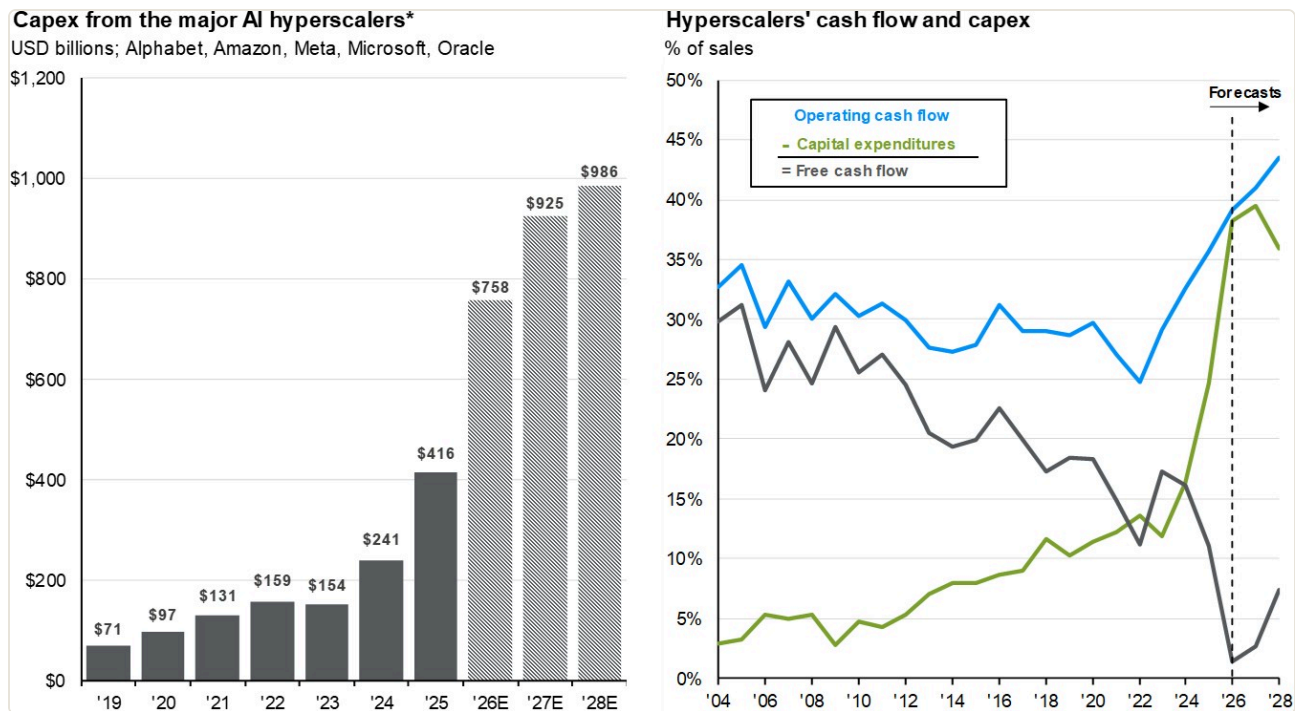
#### ARTIFICIAL INTELLIGENCE

## AI Growth Will Continue

We spent three years talking about the performance of the Magnificent 7 (hyperscalers) and their earnings-driven performance. The AI trade has broadened and will continue to do so as AI adoption increases, and margin expansion extends to other industries. According to Goldman Sachs Asset Management, corporate uptake of AI started gradually, but enterprises are beginning to rapidly deploy the technology in a development that will affect the entire AI ecosystem. The catch is that the AI industry's ability to scale is constrained by the availability of computer power – which feeds into the excess demand story that is driving industries ranging from energy (specifically natural gas) to commodities to power generation to semiconductors to hyperscalers.

Until demand is satisfied, AI-related capital expenditures will continue to increase, with AI hyperscaler investment slated to increase by 82.2% from \$416 billion in 2025 to \$758 billion in 2026 and approach \$1 trillion by 2028 (see Figure 9). Of course, there will be obstacles (i.e., New York's recent data center moratorium). However, with compute demand surging, supply will “find a way,” and the evidence suggests AI-driven growth will continue. However, with capital expenditures eating into cash flows, the performance of the hyperscalers pulled back in the second quarter as investors followed the capital expenditure dollars from the spenders to the biggest bottlenecks. This includes semiconductors, specifically memory. With the market disciplining big spenders and earnings growing rapidly, valuations have remained reasonable – despite the strong second quarter performance of global equity markets.

**Figure 9. Artificial Intelligence: Hyperscaler Investment, 2019–28E**



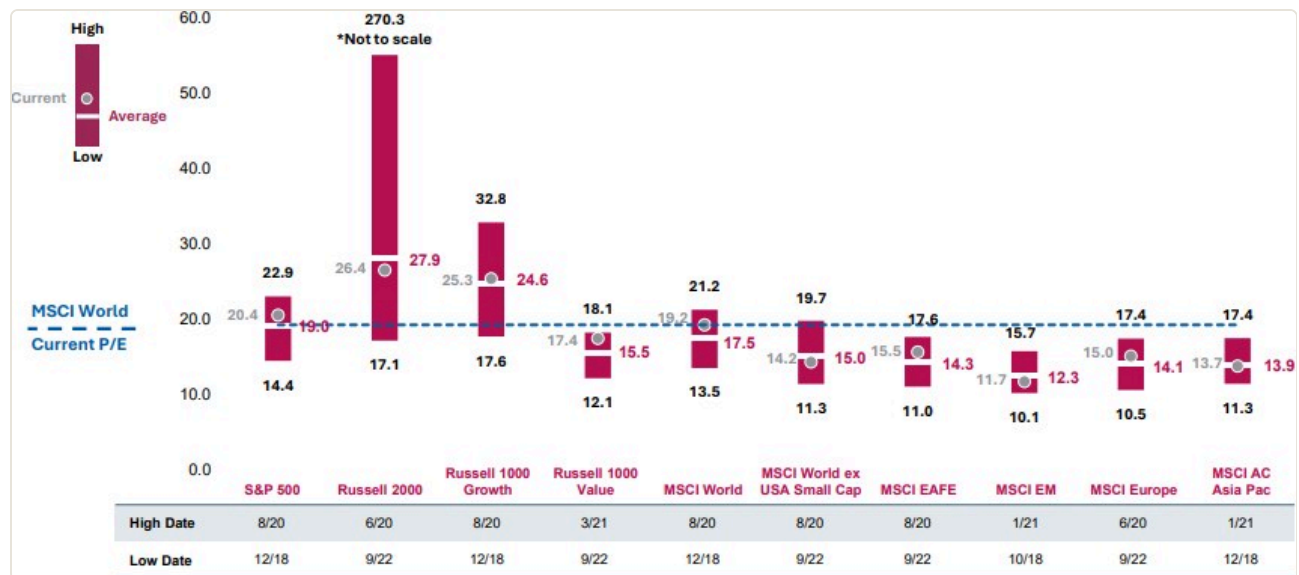
Source: J.P. Morgan Asset Management Guide to the Markets; Bloomberg. Data for 2026–2028 reflect consensus estimates; capex shown is company total.

## VALUATIONS

# Valuations — Not Stretched

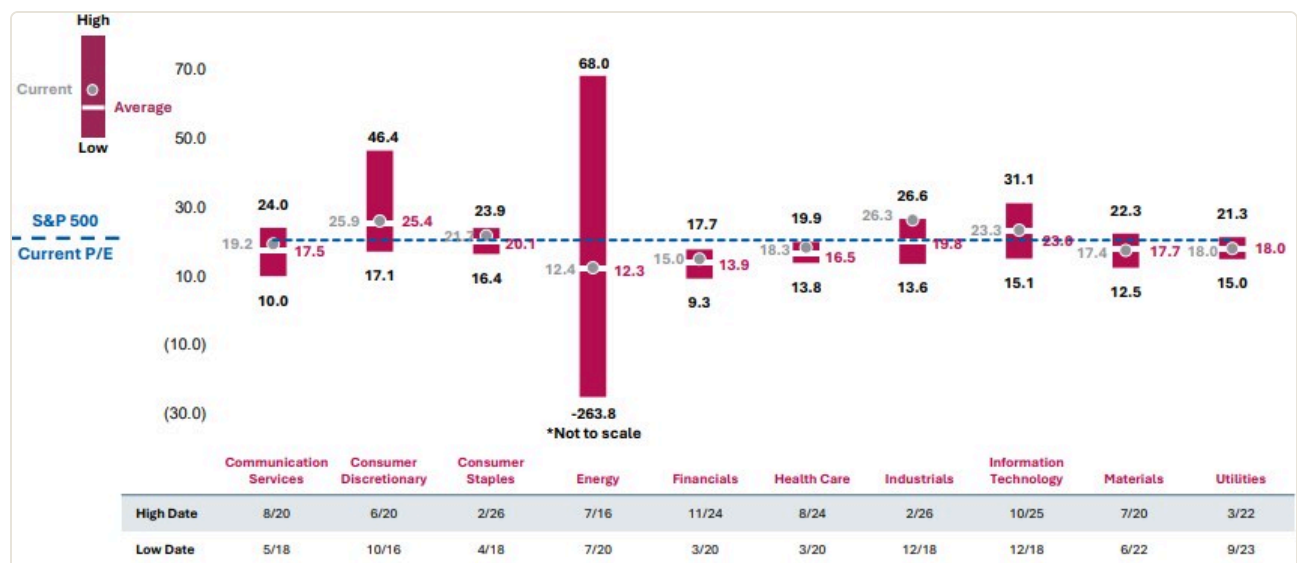
With the US (especially the S&P 500) likely to continue to post strong earnings growth valuations are approximately in line with their 10-year averages (see Figure 10) across most sectors (see Figure 11). This is remarkable given that S&P 500 earnings growth has exceeded the 10-year average over the past several quarters and strong earnings growth is poised to continue. The valuations of non-US markets will be scrutinized as investment decisions are made in 2026. Whereas international valuations were attractive going into 2025, valuations outside the US “caught up” last year and in the first half of 2026 and are now about in line with their long-term averages, as are earnings growth expectations.

Figure 10. Valuation Analysis — Regions/Styles: Current NTM P/E v 10-year High, Low, Average, June 30, 2026



Source: Eaton Vance, The Beat June 2026; FactSet as of 6/30/26. NTM P/E is market price per share divided by expected earnings per share over the next twelve months.

Figure 11. Valuation Analysis — S&P 500 Sectors: Current NTM P/E v 10-year High, Low, Average, June 30, 2026



Source: Eaton Vance, The Beat June 2026; FactSet as of 6/30/26.

## MARKET OUTLOOK

# The Market Outlook — Rally to New Highs, Retreat, Repeat

The MSCI ACWI and the S&P 500 both surged just over 15% in the second quarter and have since retreated 1%–2% in the wake of yet another China AI scare, higher oil prices, and general nervousness. Most recently, the news that China's Moonshot AI launched a model that appears to rival Anthropic's most powerful AI engine at lower cost added to worries about the tech sector. At the same time,

resurgence of the Iran war is again driving up oil prices. With earnings being reported and most exceeding expectations, we remain convinced that after the current pullback, we will see yet another surge to new highs.

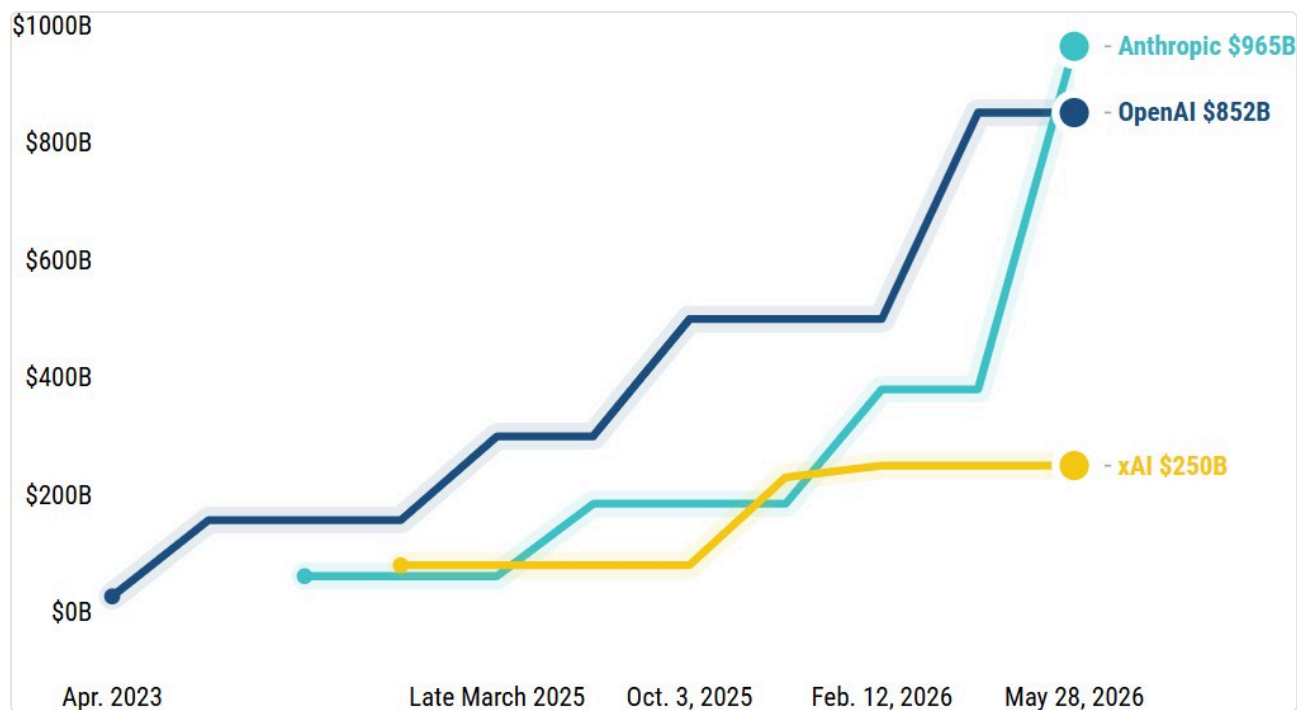
Recent and upcoming mega-IPOs (Initial Public Offerings) and their likely impact on equity markets are also a concern. The massive SpaceX and SK Hynix IPOs, which were completed over the past month round-tripped – surging initially and returning to around their offer prices, and Anthropic and OpenAI are waiting in the wings. The eye-popping valuations, unconventional valuation methodologies, and stair-step rises in valuations over time (see Figure 13) of the SpaceX, Anthropic, and OpenAI IPOs hearken back to the early stages of the dotcom boom. However, given the likelihood that at least one of these companies will “be the next...”, small positions in all three (if you can handle the surrounding management and corporate governance issues) may be warranted in long-term oriented portfolios. Beyond these headline-grabbing equity raises, the broader AI build-out is still funded primarily through hyperscaler operating cash flow, supplemented by a rapidly growing debt load – roughly \$108 billion of AI-related debt issuance in 2025 alone, with market estimates pointing to as much as \$1.5 trillion over the next several years.

**Figure 12. Major IPOs and Equity Raises — Completed or Pending**

| DEAL                  | STATUS                          | SIZE RAISED                                  | VALUATION                               | USE OF PROCEEDS                                                                                   |
|-----------------------|---------------------------------|----------------------------------------------|-----------------------------------------|---------------------------------------------------------------------------------------------------|
| <b>SpaceX (SPCX)</b>  | Priced June 11, debuted June 12 | ~\$75B<br>largest IPO ever                   | <b>\$1.77T</b>                          | Starship, Starlink, xAI compute buildout — Q1'26 capex alone was \$10.1B, \$7.7B of it AI-related |
| <b>SK Hynix (ADR)</b> | Priced July 10                  | \$26.5B<br>largest foreign IPO in US history | <b>~\$1.35T KOSPI</b>                   | Yongin fab, Cheongju packaging plant, EUV tools — FY26 capex guided to KRW 35T+                   |
| <b>Anthropic</b>      | Confidentially filed June 1     | TBD                                          | <b>~\$965B last private round</b>       | Compute / infrastructure buildout; targeting late-2026 debut                                      |
| <b>OpenAI</b>         | Confidentially filed May 22     | TBD<br>~\$60B raise reported                 | <b>~\$730–850B some reports to \$1T</b> | Compute buildout; timing uncertain post-SpaceX pullback, possibly slips to 2027                   |

Source: SEC / exchange filings (SpaceX, SK Hynix); press coverage (Anthropic, OpenAI). Note: xAI merged with SpaceX in February 2026 at a \$250B valuation.

Figure 13. Valuation Over Time — SpaceX, Anthropic, OpenAI



Source: PitchBook data and company filings • As of May 28, 2026. Note: xAI merged with SpaceX in February 2026 at a \$250B valuation.

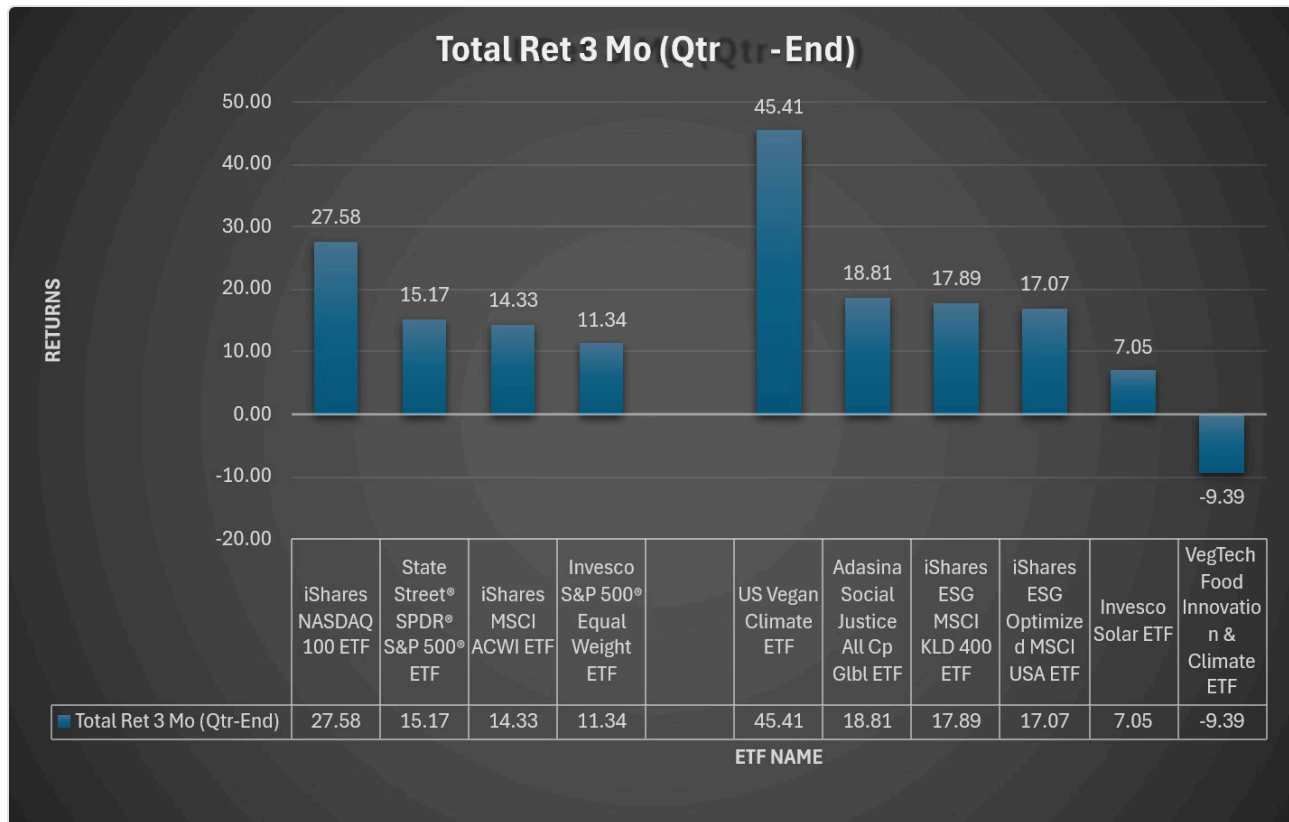
#### VALUES-ALIGNED INVESTING

## What Impact Does Your Portfolio Have on the World?

After nearly three years of underperformance, many values-aligned strategies outperformed their benchmarks in the second quarter. We continue to see persistent backlash against environmental, social, and governance (ESG) principles and investing. Despite these headwinds our resolve remains strong. Investors must be allowed to invest their money their way, incorporating their personal values preferences into their portfolios and advocacy efforts.

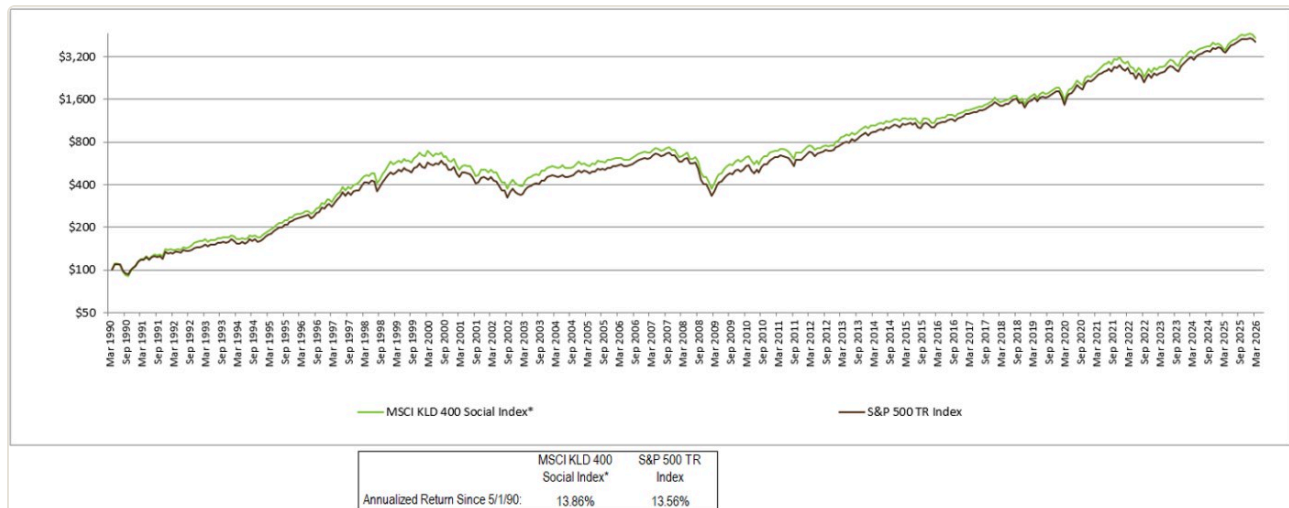
At Formative, we remain convinced that investors must take responsibility for the impact their money has on the world. The market reflects the world as it is today. Values-aligned investors invest in the world as they want it to be and look to achieve long-term financial and impact goals aligned with their values. Our VADIS portfolios performed well in the first half of 2026, and other Values Aligned strategies – including the MSCI KLD 400, and the sustainable mutual funds and ETFs we monitor – turned the corner in the second quarter.

Figure 14. Performance of Selected Values-Aligned Funds, March 31, 2026



Source: Formative.

Figure 15. MSCI KLD 400 vs S&P 500 Indices, June 30, 2026



Source: Morningstar. Data prior to 9/1/2010 is that of the MSCI KLD 400 Social Index GR; data since 9/1/2010 is that of the MSCI KLD 400 Social Index NR. Indices are unmanaged groups of securities and cannot be invested in directly.

## ABOUT & DISCLOSURES

# About the Author



## Theresa Gusman

Chief Investment Officer, Formative

Theresa is Formative's Chief Investment Officer, responsible for producing and delivering values-aligned investment solutions to advisors and their clients. She leads the firm's investment strategy and market research, translating the macro backdrop into what it means for values-aligned portfolios.

[TheresaGusman@formativefinancial.com](mailto:TheresaGusman@formativefinancial.com)

### FIRM

#### Formative

First Affirmative Financial Network, LLC  
5475 Mark Dabling Boulevard, Suite 320  
Colorado Springs, CO 80918  
Registered Investment Advisor · SEC File #801-56587  
[www.formativefinancial.com](http://www.formativefinancial.com)

### ADVISOR INQUIRIES

phone: 719-478-7036  
[businessdevelopment@formativefinancial.com](mailto:businessdevelopment@formativefinancial.com)

### BUSINESS DEVELOPMENT, MARKETING & MEDIA

phone: 719-478-7036  
[businessdevelopment@formativefinancial.com](mailto:businessdevelopment@formativefinancial.com)

### SERVICE INQUIRIES

phone: 719-478-7036  
[service@formativefinancial.com](mailto:service@formativefinancial.com)

### GENERAL INQUIRIES

[service@formativefinancial.com](mailto:service@formativefinancial.com)  
phone: 719-478-7036

### DISCLOSURES

*The opinions and concepts presented are based on data believed to be reliable; however, no assurance can be made as to their accuracy. Mention of a specific company or security is not a recommendation to buy or sell that security. Past performance is never a guarantee of future results. For information regarding the suitability of any investment for your portfolio, please contact your financial advisor.*

*The views expressed herein are those of First Affirmative, doing business as Formative, and may not be consistent with the views of individual investment advisors or Broker-Dealers or RIA firms doing business with First Affirmative. Network Advisors may offer securities through various Broker-Dealers and Registered Investment Advisory firms. These affiliations, and all fees charged to clients, are clearly disclosed. First Affirmative's ADV Disclosure Brochure is available any time. Please write or call for a copy or visit [formativefinancial.com/about-us](http://formativefinancial.com/about-us).*

Copyright © 2026. A publication of First Affirmative Financial Network, LLC, doing business as Formative. Registered Investment Advisor (SEC File #801-56587) · 5475 Mark Dabling Boulevard, Suite 320, Colorado Springs, CO 80918 · p: 719-478-7036 · [www.formativefinancial.com](http://www.formativefinancial.com)