The Pulse of the Market

London Fog

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In a Nutshell

In *Pulse,* we tackle hot topics and other updates to the indicators we track regularly. The big things you need to know: First, the investors we met with this past week were keen to explore other opportunities in US equities beyond Semis/Tech/AI, but had difficulty envisioning what those were. Second, we highlight continued outperformance of high price momentum in our factor work and what we're seeing in our valuation work for this part of the market, a pick up in the rate of upward EPS estimate revisions for the S&P 500 as reporting season slows down, and the signal we're currently getting from S&P 500 and Russell 2000 forward P/E's.

London Fog: Investors We Spoke With This Past Week Were Interested In Exploring What Else Might Offer Opportunity Beyond Semis/Tech/AI, But Had Difficulty Envisioning What Those Were

This past week we met with equity investors in the UK and Switzerland. Some of the topics they were most interested in discussing were AI, earnings, and sector views. The midterm elections came up in several meetings as well (with curiosity about our thoughts on whether additional stimulus ahead of the event was likely, and interest/surprise when we noted that betting markets have been starting to turn more optimistic about the possibility of a Republican sweep, page 94-95). The health of the US consumer and our thoughts on Small Caps were other recurring questions. Iran came up less than we expected where we sensed wariness over the conflict as opposed to panic. Fed discussion was light, similar to what we've seen in our US conversations of late, though the implication of higher yields came up later in the week on the heels of the US CPI and PPI releases which brought inflation back to the list of hot topics (we walked investors through the potential impact of higher inflation and interest rate assumptions on our S&P 500 outlook via assumptions in our valuation/EPS model, page 41).

The conversations we had on AI, earnings, and sectors were subsets of a bigger discussion. Most clients we met with were very much on board with the idea that the Tech sector broadly and the AI theme specifically were extremely bright spots in the earnings outlook and had been driving upward revisions to the S&P 500 EPS outlook for 2026 (we highlighted our charts on pages 22 and 24, showing expanding dominance of AI related EPS growth relative to the rest of the S&P 500 and how Tech, Communication Services, and the commodity sectors had seen upward revisions to 2026 EPS growth forecasts since early April while other sectors had moved very little). Despite the appreciation of the earnings power of the Tech/Semis/AI part of the market, and some noting that they'd had plenty of exposure to it and had been performing well, there was a keen interest in exploring what other areas might offer better opportunities going forward, though several also noted it was difficult to understand what those would be.

In these discussions, we were frank in our view that sector selection seems particularly tough these days. As we talked through the options, we found that investors seemed most interested in our thoughts on the following:

- *Commodity sectors:* As noted above, Energy and Materials, like Tech, are among the very few sectors that have seen upward revisions to consensus 2026 EPS growth forecasts recently in percentage terms. Valuations also look slightly attractive in both sectors in the S&P 500, unlike what we see in Tech (page 54). We noted our preference for Materials (which we are overweight, and has seen funds flows improve after a recent period of weakness – page 102) over Energy (which we are market weight and has deteriorating flows, but where valuations admittedly still look attractive). Both are also areas we'd also inherently expect to benefit in a higher inflation environment.
- *Financials:* We highlighted our overweight amid attractive valuations and improving funds flows. We also highlighted how the Capital Markets industry's valuations had been extremely extended in the past including when private credit fears first began to escalate, but that these have become much more reasonable (page 65). Some investors were more interested in discussing this sector than others.
- *Consumer Staples:* We noted our market weight on the sector alongside its attractive valuation profile and low ranking in our April analyst outlook survey for the US. In these discussions, we indicated that while we understood the fundamental challenges of the sector with regards to low/middle end consumer and commodity exposure, this sector seemed more derisked to us than Consumer Discretionary (which we've been underweight due in part to a slightly unfavorable valuation profile). Generally, we found that investors were interested in looking at parts of the market in which known fundamental challenges are already baked in. We also found that while some investors were interested in discussing Health Care (where valuations are also attractive) that others shared our frustrations with the sector (which we recently downgraded in part due to weaker earnings revisions trends midway through 1Q26 reporting season and outflows from Health Care dedicated sector funds, page 101).
- *Small Caps:* Several investors asked about our thoughts on Small Caps, which we noted we like, just not quite as much as Large Cap Growth. Here, we pointed out that the likely absence of Fed cuts in the year ahead (an idea reinforced by this past week's inflation prints) removed a tailwind for Small Caps relative to Large Caps (page 92). Fundamentals for Small Caps seemed mixed (strong ISM manufacturing and NFP reports on the positive side vs. weaker consensus GDP expectations on the negative side – pages 75-76 and 90). Positioning is favorable (net shorts in place on CFTC's US equity futures positioning data for Small Caps). Valuations are moving up but not yet back to recent highs on FY2 P/E, though they look more concerning on NTM P/E. Consensus EPS growth forecasts favor big cap AI names in 2026, but Russell 2000 in 2027 (page 23).

Quick Hits: What Else Jumps Out

- *Momentum monitor.* We're keeping a close eye on our work that looks at the performance of high price momentum relative to low price momentum within the S&P 500 (page 15). On our work, high price momentum has continued to rise and outperform low price momentum stocks. In a new slide, we've started looking at the NTM P/E of both high and low price momentum stocks. We've seen P/E expansion in high price momentum and contraction in low price momentum. Relative to low price momentum, high price momentum valuations are a little above average but not highly stretched (page 53).
- *Revisions revving up.* With the busiest part of reporting season behind us, we're now seeing a meaningful uptick in earnings sentiment, the rate of upward EPS estimate revisions, for the S&P 500, its biggest market cap names, AI focused names, the rest of the index, and the Russell 2000 (pages 32-34). We're also now seeing more S&P 500 sectors in positive revisions territory on both an EPS and revenue basis (page 36). Geographically, strengthening upward EPS estimate revisions in the US stands in contrast to continued deterioration for Canada, Australia, UK, and Japan and could help extend the US leadership trade (page 39).
- *Keeping an eye on the stock market's temperature.* Forward P/E's are approaching past highs for the S&P 500 and Russell 2000 on an NTM basis but not an FY2 basis (pages 44-45). This explains both the increased angst we've noticed among some investors of late, along with the stock market's continued climb higher. We could say the same thing about investors' desire to find opportunities beyond the Semis/Tech/AI trade for opportunity and difficulties in doing so.

For more thoughts on the US equity market, see page 3 for a rundown on our S&P 500 outlook and key positioning trades, page 4 for our thoughts on hot topics, and pages 5-6 for our sector views.

Summary / Update of Our US Equity Market Outlook

- **Our 12-month S&P 500 price target is 7,900.** This implies a gain of 7.7% from the May 7th close, when we last froze our models. Our price target is maintained on a rolling 12-month-forward basis (it is not a December 31st estimate) and is updated monthly. We view it as a compass and general navigation tool designed to articulate where stocks are headed and why. The average and median of the five models (which we typically use to set our price target) is 8,100, which suggests there is some upside risk to our view. We've decided in our latest update, however, to link our price target to the model that is best equipped to bake in the idea of a two-speed economy and earnings backdrop (AI in the fast lane, Middle East in the slow lane). In that model, we trim bottom-up consensus EPS forecasts for 1Q27 by 5%, putting yr/yr growth at 12% (which assumes 28% growth for AI focused stocks and 6% growth for the rest of the index), and bake in 3.3% CPI, a flat Fed, and 10-year yields of 4.5% to our trailing P/E calculation. Note, that if we were to adjust the macro inputs into our P/E projection to bake in 3.8% CPI, a few Fed hikes, and 10-year yields of 5%, using the same EPS assumption our fair value projection for the S&P 500 would fall to the 7,400-7,500 range.

- **Tactical risks we're monitoring.** We don't expect the S&P 500's move higher to be linear but anticipate that any pullbacks would be no worse than a tier 1 garden-variety pullback in the 5-10% range. But in our view, unless recession concerns return, it is unlikely the S&P 500 would enter a tier 2 growth-scare drawdown (14-20%) or worse. We are keeping an eye on valuation levels in the S&P 500 and Russell 2000, which could indicate a return of short-term overbought conditions when they return to past highs, but aren't seeing that condition in place broadly yet. One potential catalyst for a pullback later this year could be downward adjustments to late-2026 or 2027 EPS outlooks due to war impacts. Profit-taking in Semis, which have been an important pillar of the recent move in the S&P 500 and have strong earnings revisions trends but look pricey, is another. Mid-term elections could be another stumbling block for the S&P 500 later this year given the poor history for stocks around this event, including 2018 (Trump 1) and 2022 (Biden), but we suspect heightened expectations around a Democratic sweep in Congress contributed to the 9.1% drawdown in the S&P 500 in 1Q26 given an increase in odds around that scenario in betting markets earlier this year, and note that anticipation of a split Congress has been on the rise again in betting markets (a possible tailwind to US equities of late) even though it is not yet the most expected outcome. Setbacks in the war are another obvious potential downside catalyst in the short term. We've tended to view private credit as more of a narrative problem than a fundamental one but are also keeping an eye on this corner of the market as well. Higher interest rates were top of mind as the past week came to an end. We reminded investors that higher yields tend to impact stocks mostly through the P/E channel (generating multiple compression) since debt levels among S&P 500 companies have come down over time and shifted more towards fixed rate and long-term debt. That being said, in 2H23 the S&P 500 did experience a 10% drawdown as 10-year yields marched higher.

- **We continue to have a bias in favor of Growth over Value within Large Cap.** We think US equity market performance will reflect trends in earnings over the next 12 months, and our data suggests that the earnings story is simply stronger for Growth than Value at the moment, driven by the AI theme. When we look at earnings sentiment, the rate of upward EPS estimate revisions has been stronger for Growth broadly and the biggest market cap names in the S&P 500 in particular than Value and the rest of the market, and impacts from the Middle East conflict seem likely to be more of a headwind for earnings revisions for Value and the rest of the market going forward. Meanwhile, data on bottom-up consensus net income estimates points to eroding dominance for the Mag 7 relative to the rest of the S&P 500 since 2024 and in the years ahead, but we have not yet seen an outright shift in earnings leadership to the rest of the market, which we believe has allowed the mega cap Growth/AI theme to fight back to maintain its leadership. Note that we have started to look at this data on a broader AI basket, and find similar trends relative to the S&P 500 ex that AI basket – but we are seeing a sharp pickup in anticipated growth dominance of that AI basket in 2026, which we think has helped to invigorate the AI theme even more in recent trading. Net income growth is expected by consensus to be stronger in the AI basket than the Mag 7 in both 2026 and 2027, which we think is also supportive of a broadening of leadership within the AI theme.

- **We continue to give an edge to US equities over non-US equities.** Ahead of the Iran war, US equities looked cheap relative to non-US equities on a five-year time frame, and no longer looked overvalued on a 20-year time frame. We think that that helped to get US leadership started. Following the outperformance that the US saw after the war began, the US/non-US P/E has now moved back to levels slightly above the five-year average but doesn't look highly stretched yet. On a 20-year time frame, the US/non-US relative P/E has moved up but is not yet back to past highs. This tells us there is still some room for the US to outperform non-US. In recent EPFR updates, US equity flows were improving and back in firmly positive territory, while flows to Europe remained negative. We aren't getting terribly strong signals on the US relative to other developed markets geographies on our economic indicators where GDP forecasts are starting to slip broadly. However, we are starting to see indications that earnings revisions are stronger in the US than other regions and major countries. Fundamentally, we do buy into the idea that the US has had less exposure to Middle East/energy disruption than Europe or Asia, and may incur less impact from residual damage going forward (something supported by our recent global analyst survey work). In our meetings, we've continued to emphasize to clients that there has historically been a link between the Growth/Value trade in the US and the US/non-US equity trade. Over the past 20 years, US underperformance relative to non-US tends to be accompanied by Growth underperformance vs. Value within the US. Note, our recent global analyst survey work suggests that Europe is less appealing than the US in terms of perceived valuations, demand, and war impacts. Note, we would not be surprised to see Europe lead and the US lag if a clear end of the war occurs, but for now we would view that as a short-term trade.

- **We like Small Caps, but not quite as much as big cap growth.** Some of the positives we have seen for Small Caps include the strong March and April jobs reports, recent improvement in ISM manufacturing and futures positioning (where CFTC data points to a net short in place but not deeply oversold levels). That being said, some of the negatives we have seen for Small Caps are the continuation of less robust earnings revisions trends relative to Large Caps (though both Large Cap and Small Cap have shown improvement on this metric at the end of 1Q26 reporting season), a lack of optimism about Fed cuts in 2026 among financial market participants generally (since Small Caps tend to see bursts of leadership when dovishness increases), and downward pressure on consensus GDP forecasts due to the war (since Small Caps tend to get a boost from improved cyclical expectations and come under pressure when the economic outlook is called into question). Valuations are moving up but still have some room to return to recent highs on an FY2 basis. Note on the earnings front, Small Caps are expected to see better net income growth than the S&P 500 and Mag 7 in 2026, but aren't expected to see better net income growth than the broader AI basket we're tracking until 2027.

Our Thoughts on Hot Topics

Issue	Our View
The Fed	Our US Rates Strategy team expects neither cuts nor hikes in the year ahead. Consensus views on the Fed do tend to evolve over time. From our seat in US equity strategy, baking in hikes tends to be a negative for P/E multiples and Small Cap performance relative to Large Caps, while baking in cuts tends to be good for P/E multiples and Small Cap performance relative to Large Cap. This view is based on our work showing an inverse correlation between the Fed funds effective and target rate and the S&P 500's trailing average P/E since the 1960's, and our work analyzing the linkage between Small/Large relative performance and expectations for Fed moves in the year ahead since COVID. We are keeping a close eye on how the process of communicating Fed views to the market may change under Warsh. A reduction in forward guidance and an increase in truly live meetings could make it more difficult for equities to price the path of the Fed ahead of time and lead to more volatility in stock prices.
Mid-Terms	Mid-term election years have a poor track record for US equity market performance over time, and in the past two Presidential cycles in particular. Given the history, we have viewed the mid-terms as a risk in our outlook, and an event that could potentially help spark a pullback ahead of time or after the fact. That being said, we typically view trades around political events as temporary repricings, as stocks tend to find a way to reposition for a new political regime. At the moment betting markets lean towards a Democratic sweep outcome (something that we think could be a markets negative in the short-term given the tendency of investors to see Republican control as more business friendly and for the S&P 500 to trade in sync with polling and better market data on Republican outcomes in recent years). However, expectations for a Democratic sweep have been fading in recent updates while expectations for a Republican sweep have been moving up. We think this reflects improving polling on a number of key policy issues (the economy, inflation, foreign policy, and immigration), and, more recently, court decisions that have favored Republicans in the redistricting battle that has been underway. Investor attention on the mid-terms has been light, but does appear to be picking up. In a recent survey we conducted of RBC's equity analysts, Defense and Utilities stocks were highlighted as areas that seem vulnerable in a Democratic sweep scenario. We will be keeping an eye on what issues Democrats will focus on in the campaign season, once we are past the primaries, but are concerned that a focus on affordability may include negative commentary around data centers and AI, which could be a negative catalyst for the broader S&P 500 as well. In terms of outcome, our expectation has been that the House will flip to the Democrats (though this could change as we gain a better understanding of redistricting), and the Senate will remain in Republican control. We see a (difficult) path for the Democrats to take back the Senate if they win Ohio, Maine, North Carolina, Georgia, Michigan, and Texas.
Quarterly Reporting	We have not gotten a lot of color on the SEC proposal to allow companies to report on a semi annual basis from investors yet. Our initial impression is that if too many companies take advantage of this potential rule change, it could reduce transparency in financial markets and lead to greater volatility around the release of results.
Private Credit	We have tended to view private credit risks as more of a narrative problem than a fundamental one, but acknowledge that there is simply much that we don't know here. Private credit fears picked up when valuations for the Russell 3000 Capital Markets industry (a group that contains investment banks along with alternative asset managers that have private credit exposure) were looking extremely overvalued. That valuation problem essentially resolved in March when valuations returned to levels slightly below long-term averages and don't look extreme again yet.
Iran War	From our seat in US equity strategy, we think the S&P 500's decline of 9.1% through the March 30th, 2026, low was in line with how deep an S&P 500 pullback should go if investors are not worried about recession. While the geopolitical community has highlighted potential recession risk from the conflict in Iran, that has not been the view of most of the investors in US equities that we have spoken to in recent months when it comes to the US economy. If that changes, we'd expect the S&P 500 to fall 14-20% (similar to past post GFC growth scares) in a situation where investor concerns about a recession manifest but don't come to fruition and to fall in the 25-33% range (in line with median and average recession drawdowns over time) if a recession does occur. On the March 30th low, we think a foggy/fragile bottom in US equities was put in place not because valuations and sentiment got washed out or priced in a recession, but because the stock market tends to see turning points in times of distress when conditions start to get less bad at the margin, and that the cease fire put in place, while far from a clear resolution, checked that box. We tend to agree with the view of the geopolitical community that there has been lasting damage to commodity markets from the conflict, and as a result have made some downward adjustments to the outlook for S&P 500 EPS from non-AI focused companies into our valuation/EPS modeling. That being said, public company commentary since the war began has emphasized the ability to manage through crises like COVID and tariffs and has also highlighted buffers in terms of inventories of impacted materials, hedging, and other offsets like FX tailwinds to earnings and some tariff relief. We think these buffers will help to keep the 2026 earnings outlook largely intact, but do worry that those buffers won't last beyond 2-4 quarters and that there may be some downside risk to 2027 earnings. We also think that it is important for investors to remember that S&P 500 performance is supposed to track or forecast S&P 500 profitability, and that the AI component of S&P 500 earnings is sizable, strong, and generally insulated against Middle East impacts.

S&P 500 Sector Snapshots – Consumer & Growth Oriented Sectors

S&P 500 Sector	Recommendation	Details
Communication Services	**Overweight**	Positives that we see for the sector include strong upward sales and EPS revisions trends and attractive absolute and relative valuations. Flows to the Telecom sector as tracked by EPFR (the closest comparison for this sector) have stalled a bit in recent updates. In our April analyst survey, the sector came in mixed across the questions we asked, with positive answers on the outlook on performance in an Iran de-escalation scenario and the overall demand assessment. We will monitor the sector as the Iran war continues, as the sector scored negatively on performance in that scenario and when asked about the knock-on and ripple effects of the war. Within the sector (at the Russell 3000 level), Interactive Media & Services, Wireless Telecommunication Services and Diversified Telecommunication Services all look attractive on relative valuations and have positive EPS revisions.
Consumer Discretionary	**Underweight**	We are seeing negative EPS and sales revisions, and the sector is expensive on an absolute FY2 P/E. The sector is slightly more attractive on a relative FY2 P/E basis, however, flows to global consumer funds have generally been negative. In our April analyst survey, the sector came in mixed across the different questions that were asked. We will monitor the sector as the Iran war continues, as the sector scored negatively on performance in that scenario and on the knock-on and ripple effects of the war. There could be opportunity in the sector if we see de-escalation in the war, as that is where the sector scored the most positively, and captured one of the most constructive views across sectors. Within the sector (at the Russell 3000 level), Diversified Consumer Services stands out for having attractive relative valuations and positive EPS revisions.
Consumer Staples	**Market Weight**	The most positive data point we see for the sector is attractive valuations on an absolute and relative basis. Negatives for the sector include negative EPS revisions and flows to consumer funds have generally been negative. In our April analyst survey, our analyst was the least constructive across all of the sectors, which helps keep us market weight the sector despite some positive signals on our quant work. The sector scored negatively across all questions asked, with the most bearish outlook on sector performance if the Iran war continues. This is another sector we will monitor for knock-on effects and consumer health if the war drags on for longer, though the thought has crossed our minds that when it comes to the war, the impacts to this sector seem fairly well understood and there may be more risk lurking in other sectors where problems have not yet come to light. Within the sector (at the Russell 3000 level), no industry jumps out as looking compelling on both valuations and EPS revisions trends. Tobacco and Consumer Staples & Distribution Retail look expensive and have negative EPS revisions.
Health Care	**Market Weight**	The most positive data points we see for the sector are its attractive absolute and relative valuations and improving EPS and sales revisions in the most recent update. Meanwhile, the most negative data point we see is the deep outflows in recent funds flow data. In our April survey, the sector came in middle of the pack compared to the other sectors, with mixed answers across the questions asked. Our analysts did have slightly positive outlooks on valuations and the performance of the sector if the Iran War continues. One thing we are continuing to monitor is policy uncertainty, as this sector captured one of the most negative scores on our US domestic policy question. Within the sector (at the Russell 3000 level), Pharmaceuticals has attractive relative valuations and positive EPS revisions.
Information Technology	**Market Weight**	Positives that we see for the sector include positive EPS and sales revisions and positive and improving fund flows. The biggest negative we see for the sector is expensive absolute and relative valuations. In our April analyst survey, the sector came in neutral to positive on most of the questions we asked, excluding the negative outlook on potential ripple effects of the Iran War. Overall, the sector was one of the most constructive across all sectors. Within the sector (at the Russell 3000 level), Software, IT Services and Technology Hardware, Storage & Peripherals stand out as having attractive relative valuations and positive EPS revisions, but we aren't tempted here given lingering existential AI concerns that still seem relevant from a sentiment perspective. Semis revisions are quite strong and close to past peaks, levels that can admittedly endure for quite some time, but also have expensive valuations. We'd be more intrigued on a pullback here.

Source: RBC US Equity Strategy

S&P 500 Sector Snapshots – Cyclical, Value & Old Economy Oriented Sectors

S&P 500 Sector	Recommendation	Details
Energy	**Market Weight**	Positives that we see for the sector include solid upward EPS and sales revisions trends, alongside attractive absolute and relative valuations versus the broader market. In our April analyst survey, Energy also had one of the most constructive scorecards, with strong demand views, a positive domestic policy backdrop, and a relatively favorable read-through from geopolitical developments. Negatives have included weak sector fund flows, but recently we have started to see inflows again. Within the Russell 3000 Energy sector, Oil, Gas & Consumable Fuels continues to look more appealing than Energy Equipment & Services, supported by positive EPS revisions and reasonable valuations. Going forward, we are watching commodity prices and geopolitical developments from Iran and the Middle East. Tactically, we do like this sector if the Iran War is prolonged given that there is still some valuation opportunity in it.
Financials	**Overweight**	Financials continue to screen attractive on both absolute and relative valuations, while also scoring well in our analyst survey across performance, valuations, demand, and the domestic policy backdrop. Revisions trends have also improved recently at the broad sector level, though fund flows have been improving and are becoming less negative. Within the Russell 3000 Financials sector, Banks and Consumer Finance continue to look most compelling, while Capital Markets screens less attractive with valuations back in expensive territory alongside weak revisions trends. Going forward, we are watching capital markets activity with a particular focus on private credit.
Industrials	**Market Weight**	Industrials continue to see solid upward EPS and sales revisions trends, while our analyst survey highlights constructive views on performance, demand and the domestic policy backdrop. Fund flows into the sector have also remained positive, though they have moderated recently. The main offset is valuation, with Industrials screening as one of the more expensive sectors on both an absolute and relative basis. Within the Russell 3000 Industrials sector, few groups screen attractive on both valuations and revisions trends. Electrical Equipment and Construction & Engineering continues to see revisions momentum but now screens as expensive, while several cheaper groups still face weaker revisions trends. We continue to monitor manufacturing activity and the sustainability of AI infrastructure capex spending.
Materials	**Overweight**	Materials continues to screen attractive on valuations especially relative to the broader market, while revisions trends for the sector have improved recently as well. Fund flows into Materials have improved and are beginning to stabilize following a stretch of weakness earlier in the year. In our April analyst survey, the sector scored positively on valuations and the domestic policy backdrop, though views on demand were more mixed. Metals & Mining and Chemicals continue to see positive EPS revisions trends, while Construction Materials screens expensive despite weaker revisions trends. We continue to monitor commodity price trends and the durability of infrastructure and reshoring-related spending.
REITs	**Market Weight**	REITs continue to screen attractive from a valuation perspective, with the sector's median price-to-FFO (P/FFO) ratio sitting below long-term averages. The sector is also seeing improving fund flows. In our April analyst survey, the sector screened mixed overall. We continue to monitor interest rate trends (with concerns about impact from a prolonged higher interest rate environment), housing affordability dynamics, and commercial real estate activity. Note, while we are still market weight, we do consider this sector to be our preferred defensive in a pullback.
Utilities	**Market Weight**	Positives that we see for the sector include strong upward sales and EPS revisions trends. Negatives we see for the sector include expensive valuations and weakening funds flows. In our April analyst survey, the sector came in neutral or negative for most of the questions we asked, with a positive score on demand being the one bright spot. Going forward, we're keeping an eye on midterm election dynamics and the debate around affordability, which for now seems like a potential headwind for this sector. Within the sector (at the Russell 3000 level), no industry jumps out as looking compelling on both valuations and EPS revisions trends.

Source: RBC US Equity Strategy

The Four Tiers of Fear in Modern US Equity Markets

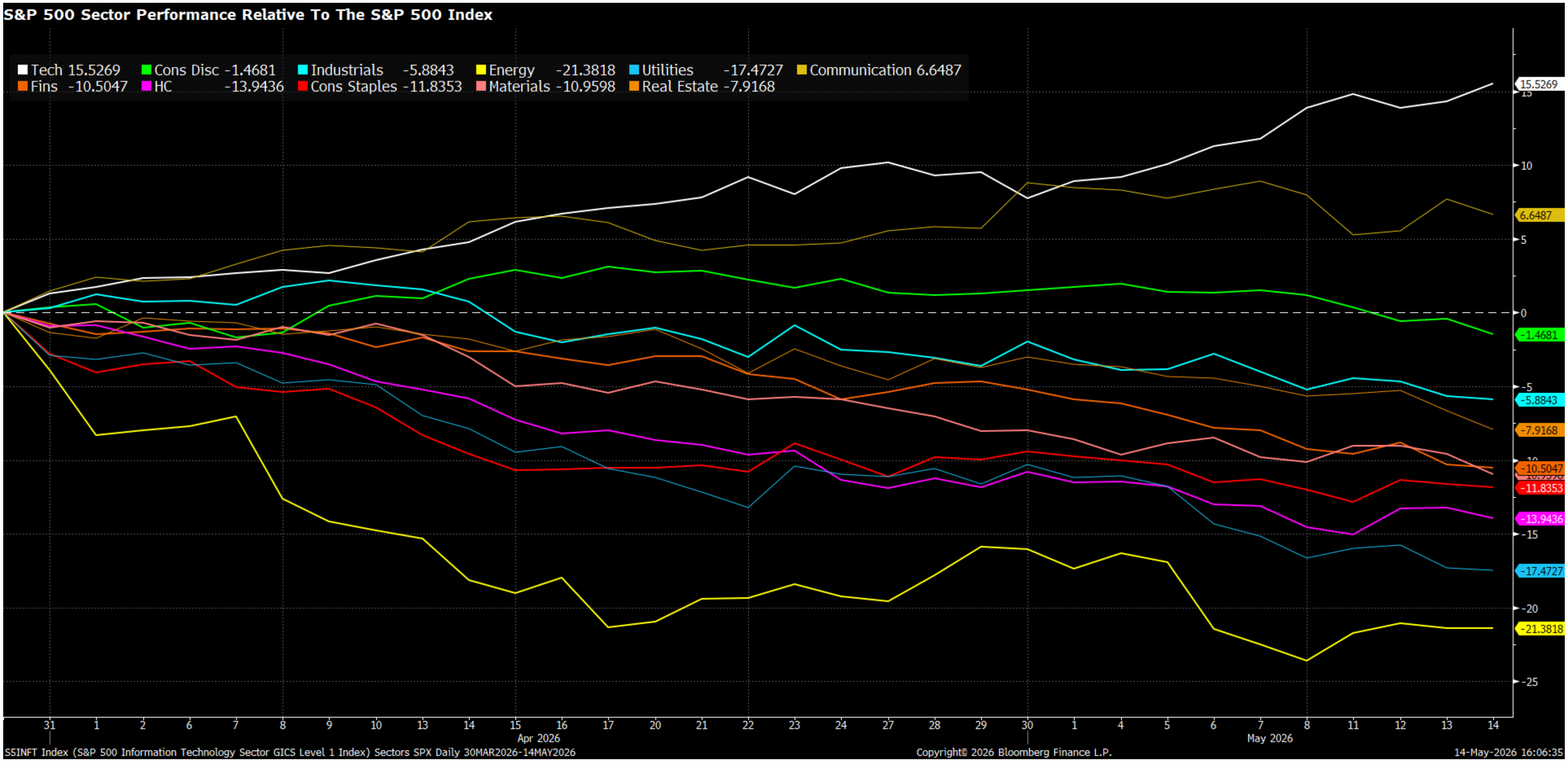
- This is a framework we've developed to think about potential downside levels in the S&P 500 whenever a period of stress and uncertainty emerges.
- We came into 2026 assuming the S&P 500 would experience at least one 5–10% tier-1 pullback this year, which occurred during 1Q26 – a 9.1% drawdown from the late-January peak through the late-March low.
- To the extent equities become weak again, a new pullback would begin from the latest May high. We think it would take a clear return of recession concerns to push the S&P 500 down into tier-2 pricing or worse.

	What A Peak-To-Trough Drawdown Looks Like Historically In The S&P 500	Equivalent S&P 500 Downside Levels To Keep In Mind Today	Additional Thoughts
Tier 1 **Garden-Variety Pullback**	▪ 5–10% drawdown	▪ 6,751–7,126 vs. the 5/14/26 high	▪ This is what the major pullbacks in the S&P 500 had typically looked like since 2022. ▪ This is a natural starting point for thinking about downside risk whenever a major source of uncertainty arises.
Tier 2 **Growth Scare**	▪ 14–20% drawdown	▪ 6,001–6,451 vs. the 5/14/26 high	▪ The US equity market experienced four of these: in 2010 (European debt crisis), 2011 (US debt downgrade), 2015-2016 (industrial recession), and 2018 (trade war / Fed fears over balance sheet unwind). ▪ The tariff tantrum of 2025 fit this category with an 18.9% drawdown from late February through early April. ▪ These were all periods in which equity market participants began to significantly price in a crisis or recession that ultimately did not materialize. All of these but 2010 also saw at least one quarter of real GDP growth in the +/-1% range.
Tier 3 **Recession & Major Wars**	▪ Median & average drawdown of 27% and 32%	▪ Roughly 5,101–5,476 vs. the 5/14/26 high	▪ Recession drawdowns have ranged from 14% to 57% since the late 1930s. ▪ Recent, major wars have been similar to recessions, with the drawdowns around 9/11 and the two Gulf Wars ranging from 20% to 34%. 2022's Russia-Ukraine war contributed to a 25% drop.
Tier 4 **Major Crisis**	▪ Drawdown of around 50% or more for a general rule of thumb	▪ 3,751 vs. the 5/14/26 high	▪ 49% drawdown for the Tech bubble ▪ 57% for the Great Financial Crisis ▪ 43% drawdown for WW2 vs. the high at the start of the war (more than 80% vs. the pre-Great Depression high)

Source: RBC US Equity Strategy, S&P

Tech & Comm Svcs Have Outperformed Within the S&P 500 Since the March 30th Low

- These sectors are pillars of the Large Cap Growth trade.
- Energy is the weakest-performing sector in April and May after seeing strength throughout March but is showing some stabilization in recent updates.



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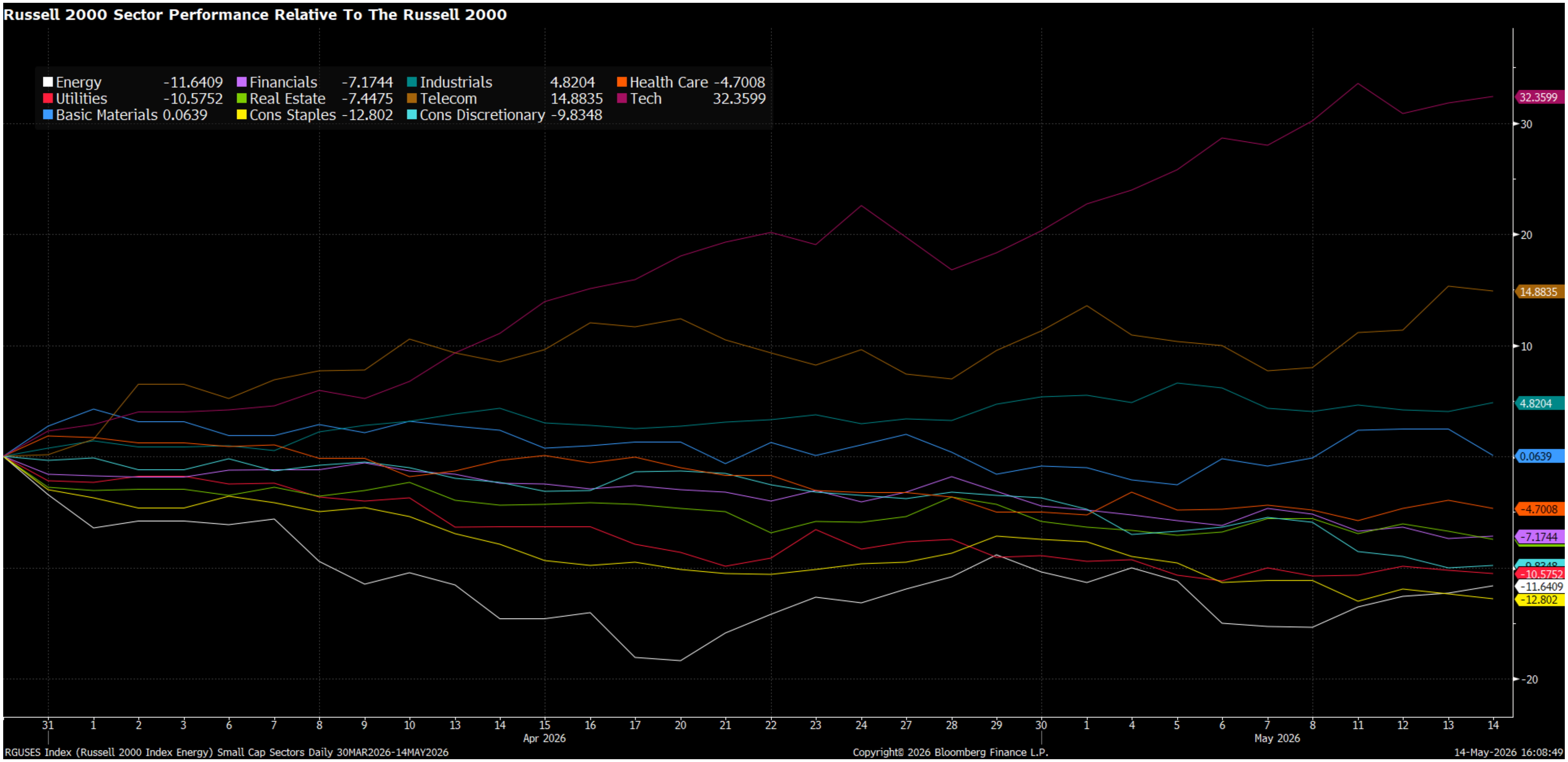
Source: RBC US Equity Strategy, S&P, Bloomberg; as of May 14, 2026

Similar to Large Cap, Tech Has Also Outperformed in Small Cap Since the End of March

- Telecom has also seen strong performance in April and May. Unlike what we are seeing in Large Cap, Industrials has shown some leadership in Small Cap, while Materials has been an in-line performer.
- Energy remains a laggard since the broader market low in late March, but has perked up again in recent days.



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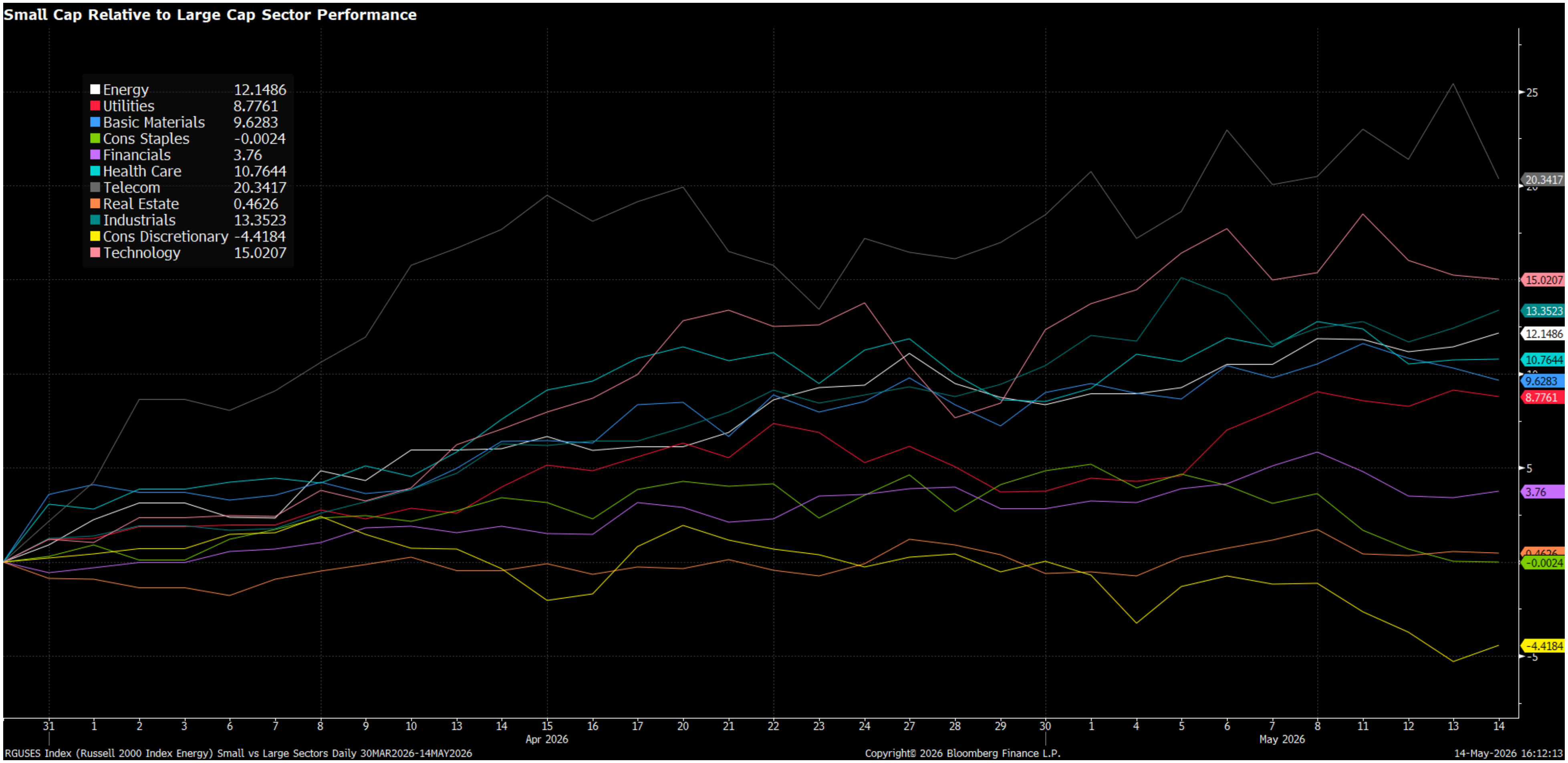
Source: RBC US Equity Strategy, Russell, Bloomberg; as of May 14, 2026

Almost All Sectors Have Gotten a Lift in Small Cap Relative to Large Cap in April and May

- Since the end of March, Telecom has seen the strongest outperformance in Small Cap relative to its Large Cap peer, followed by Tech then Industrials. However, Telecom has faltered in recent trading.
- Consumer Discretionary and Consumer Staples are the two exceptions, which have seen underperformance in Small Cap relative to their Large Cap peers since the end of March.



Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg, Russell (both Large Cap and Small Cap sector inputs), as of May 14, 2026

Growth Has Attempted a Comeback in Leadership vs. Value Within Large Cap in April and May

- This follows a brief return of Growth leadership in early March after the war began, then a renewed period of Value dominance in the second half of the month.
- In 2025, Value worked best to start the year, but after the tariff lows in the market, the Growth trade dominated.

Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg, Russell, as of May 14, 2026

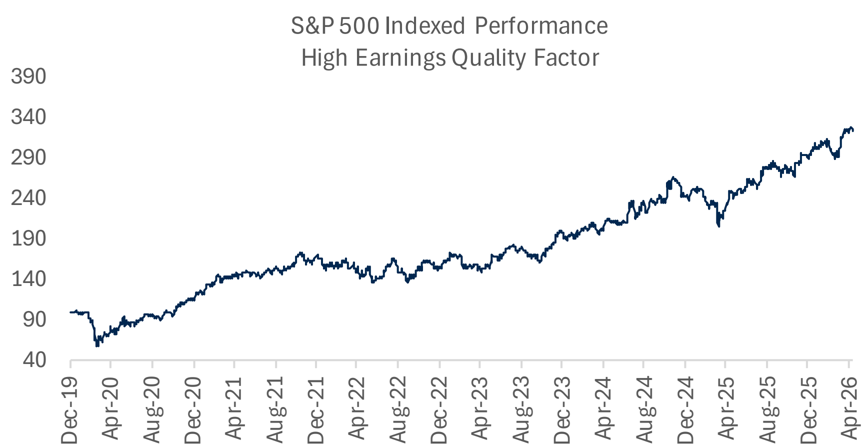
The Russell 2000 Has Stumbled vs. the S&P 500 in Recent Trading

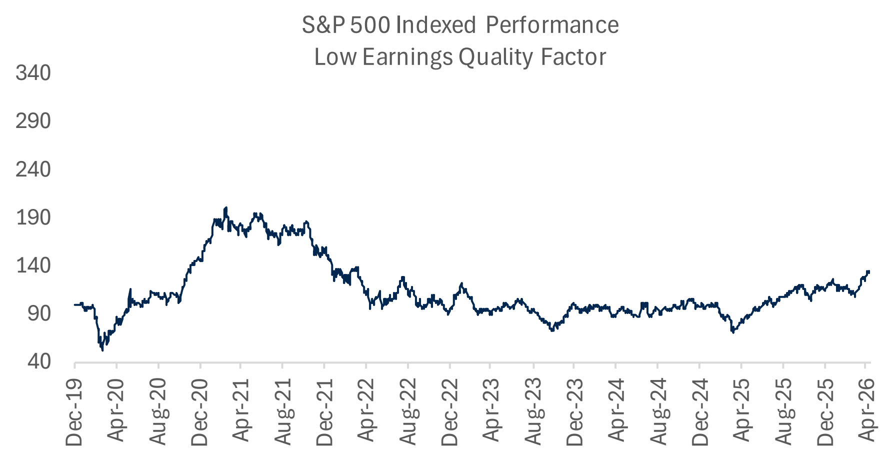
- Small Caps technically remain in an uptrend vs. Large Caps since last fall, but the price action has been choppy.
- The latest outperformance period in Small Cap began in mid-March but has been unable to break out to a new high yet, stalling a bit in recent updates.

Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg, S&P, Russell, as of May 14, 2026

Low EPS Quality Outperforming Recently In Small Cap

- The outperformance of high earnings quality within Small Caps peaked in early-April 2025, when the broader market bottomed a few days after the Liberation Day tariffs were announced, after which the market embarked on a fierce recovery. After that, low earnings quality led, as the market priced in rate cuts, looser financial conditions, and a hot economy in 2026. It's also worth noting that the Russell 2000 hit a recession low on our P/E model on April 8th, and that low-EPS-quality outperformance is a classic post-recession recovery trade. Starting mid-October 2025, high EPS quality fought back and started to outperform again, but as 2025 wound down, the trade turned choppy. So far in 2026, the high/low earnings-quality factor has been choppy, with the latest move favoring low earnings quality.

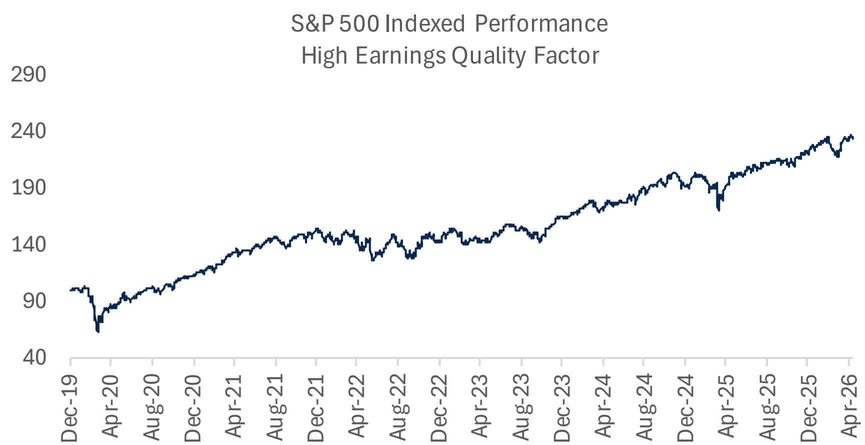


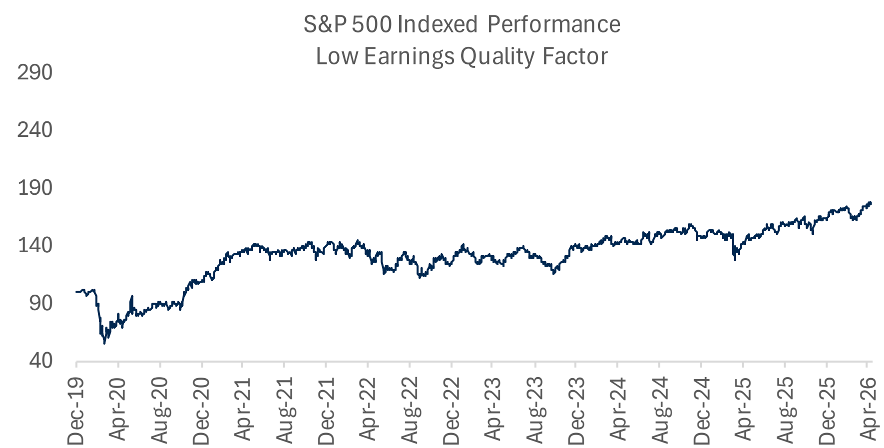


Note: The earnings quality factor is a sector-neutral, equal-weighted multifactor based on historical constituents that combines the trailing 12-month return on equity, earnings stability (measured as the ratio of the one-year change in EPS to the standard deviation of the one-year change in EPS across eight prior periods), and the distinction between positive and negative earnings based on whether EPS is above or below zero.
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of 5/12/2026

Low EPS Quality Leadership Also Leading Within Large Cap

- In Large Cap, high-earnings-quality stocks maintained steady outperformance from 2023 to 2025 but this trade peaked in May 2025. Between late October and mid-November, there's been a modest shift toward higher earnings quality. However, this trend then reversed, with low earnings quality gaining prominence in late 2025. This trend has continued so far in 2026.





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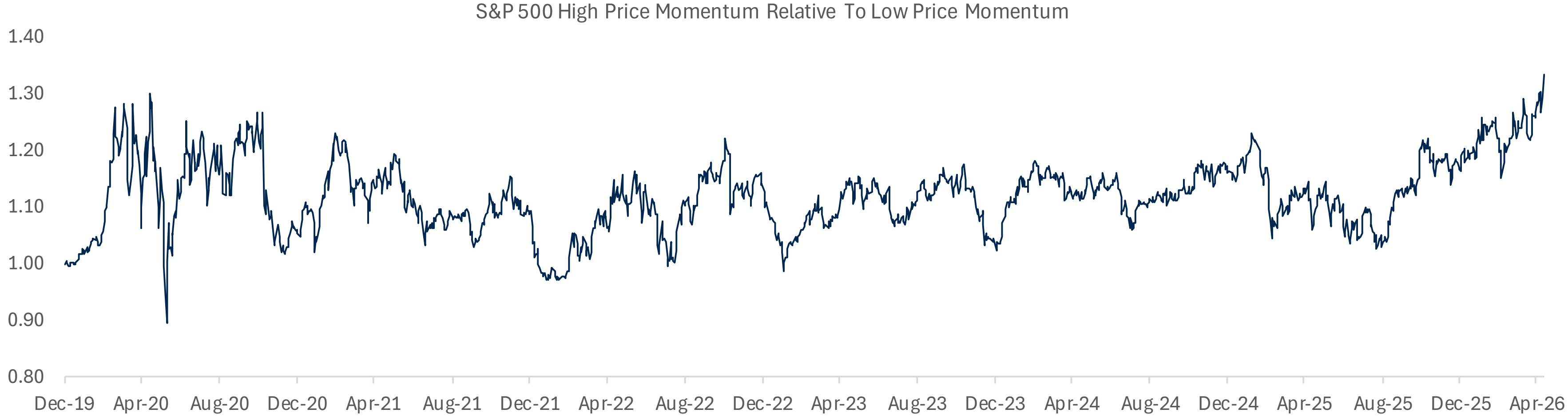
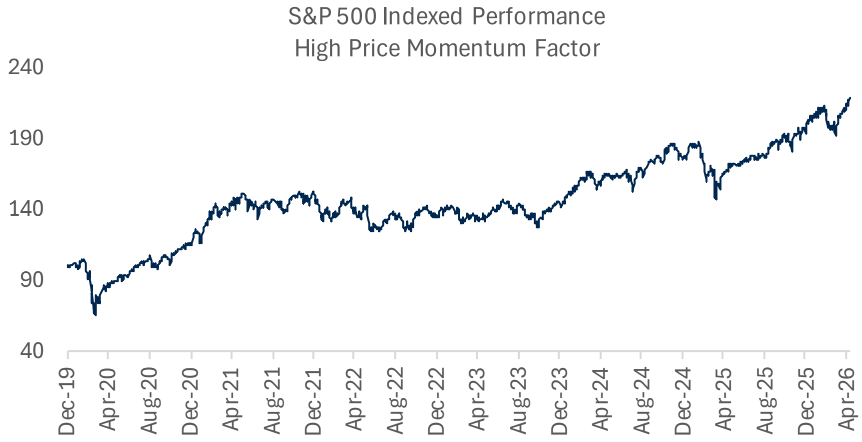
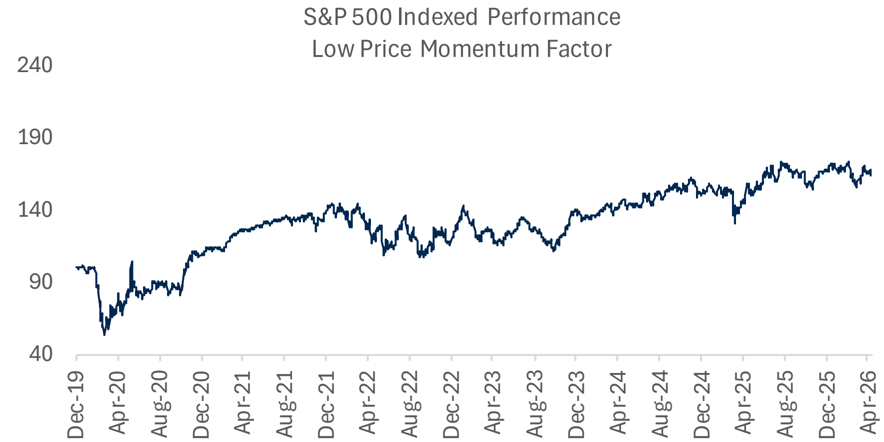
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of 5/12/2026

High-Price-Momentum Has Outperformed Sharply In Large Cap

- Within Large Cap, high-price-momentum stocks experienced a sharp underperformance during the Covid market downturn in 2020. From 2021 to 2024, the relative performance of high-price-momentum versus low-price-momentum stocks exhibited a choppy pattern, characterized by intermittent bursts of outperformance and underperformance. However, starting late summer of 2025, high-price-momentum stocks dominated again through much of the fall with the trade getting close to the high end of its range. We have seen some strength in high momentum relative to low momentum in very recent trading, with the relative ratio to low price momentum hitting a new high.



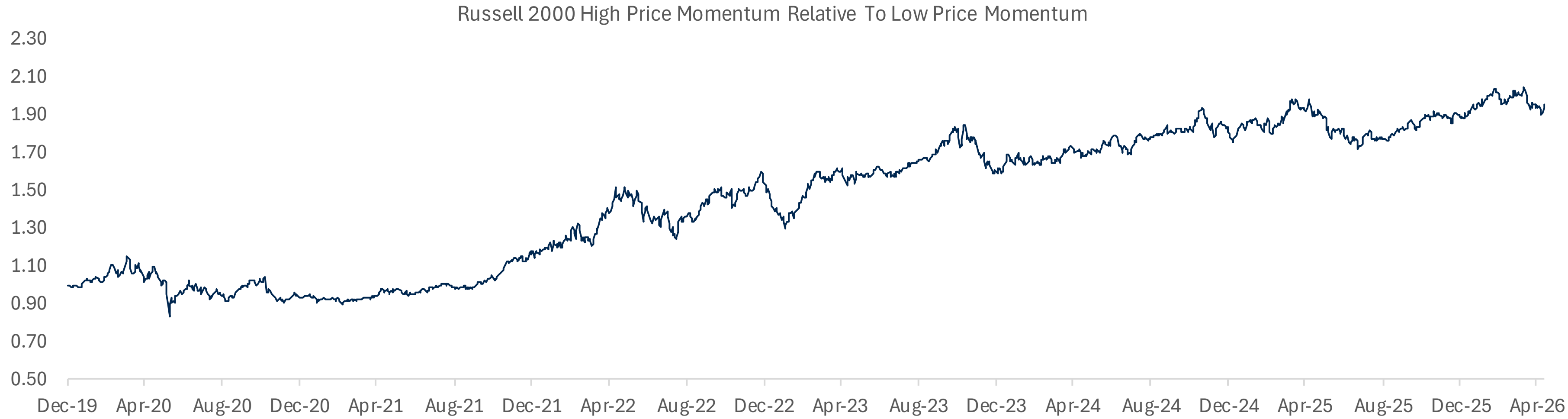


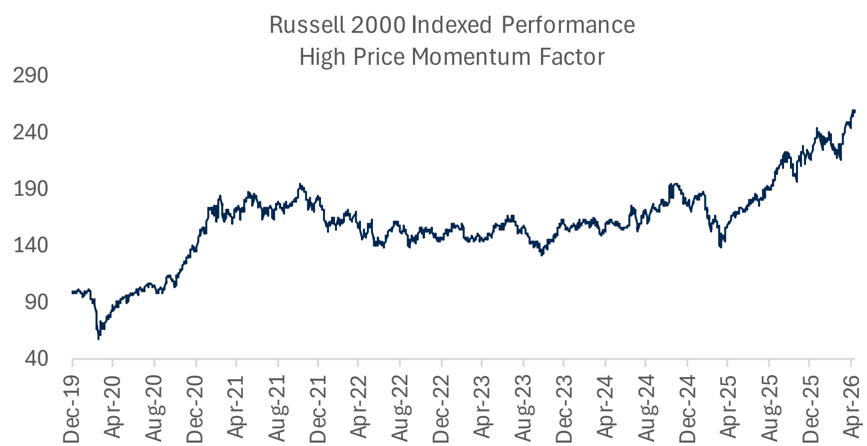


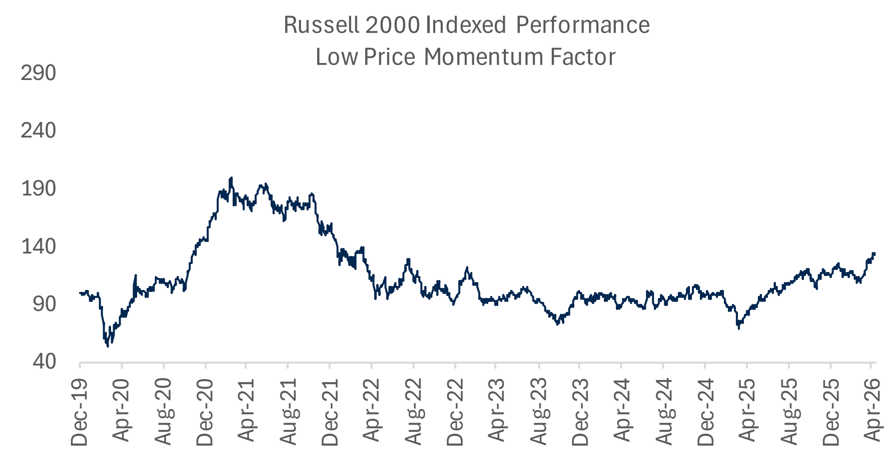
Note: The price momentum factor is a sector-neutral, equal-weighted factor based on historical constituents that measures the strength and the direction of a price movement depending on the direction of the 50-day moving average relative to the 200-day moving average.
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of 5/12/2026

High-Price-Momentum Has Lagged in Small Cap, However

- Within Small Cap, high-price-momentum stocks experienced sharp underperformance during the Covid market shock in 2020. However, they rebounded strongly, outperforming throughout 2021 and 2022. The high-price-momentum factor saw a significant deterioration in performance during the summer of 2022, following a late-spring peak where it outperformed low-price-momentum stocks. A similar pattern unfolded in late 2022 and early 2023. High-price-momentum stocks failed to lead through the majority of 2023 and 2024. In 2025 there was a notable uptick in the relative performance of high-price-momentum stocks, with the relative ratio to low price momentum approaching the high end of its range. So far in 2026 we have seen high momentum underperform the low-momentum factor.







Note: The price momentum factor is a sector-neutral, equal-weighted factor based on historical constituents that measures the strength and the direction of a price movement depending on the direction of the 50-day moving average relative to the 200-day moving average.
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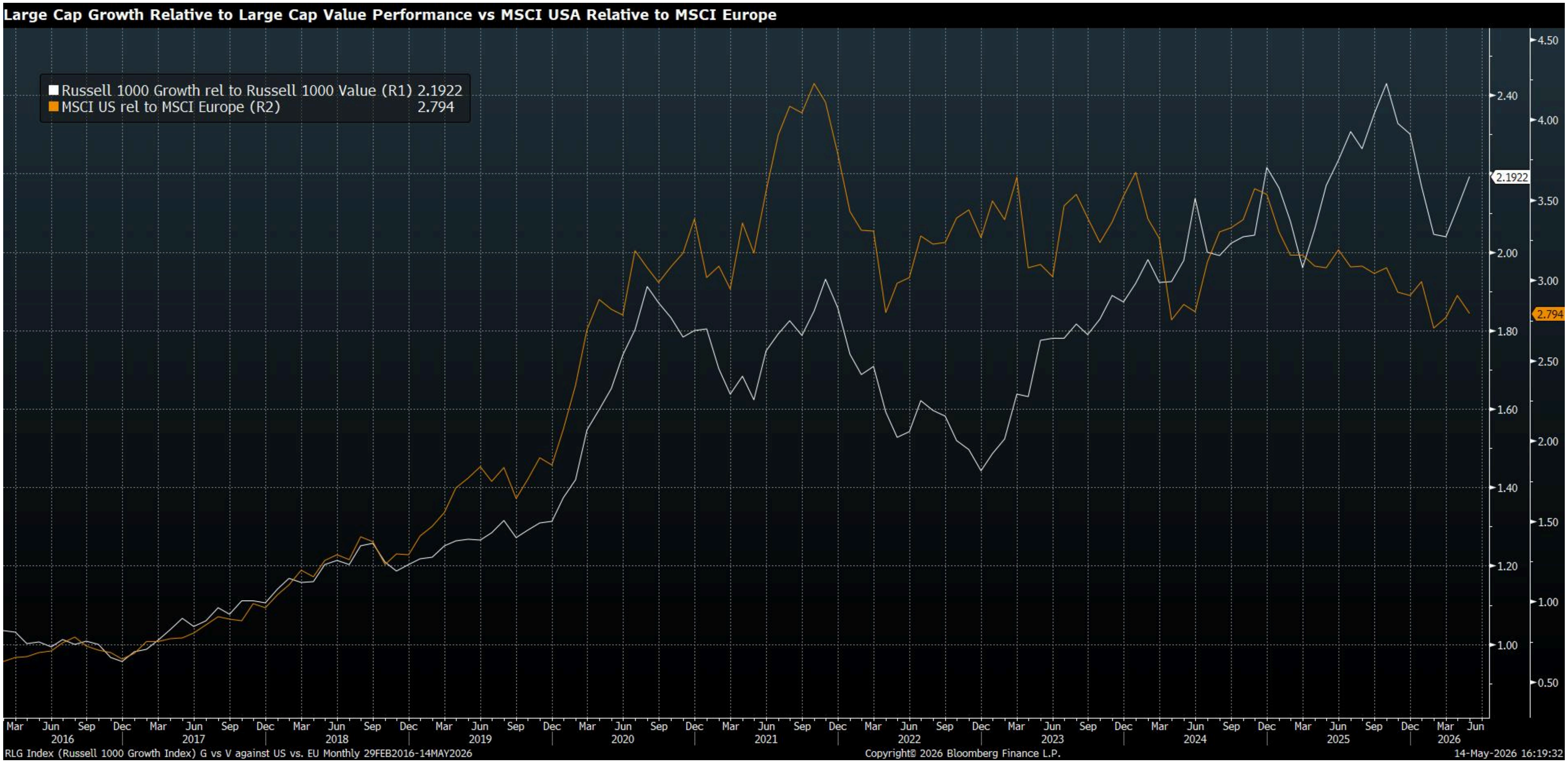
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of 5/12/2026

US Growth / Value Trade Has Tracked the US / Europe Trade in the Past

- The relationship broke down in 2022. It may be returning, however.



Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, MSCI, Russell, Bloomberg; as of May 14, 2026; please see the MSCI disclaimer at the end of this report

The US Has Outperformed The Other Biggest Developed Market Countries Since the March Low

- We are seeing some US underperformance vs. Singapore and Japan in recent updates, however.

Source: RBC US Equity Strategy, Bloomberg, MSCI; as of May 13, 2026; please see the MSCI disclaimer at the end of this report
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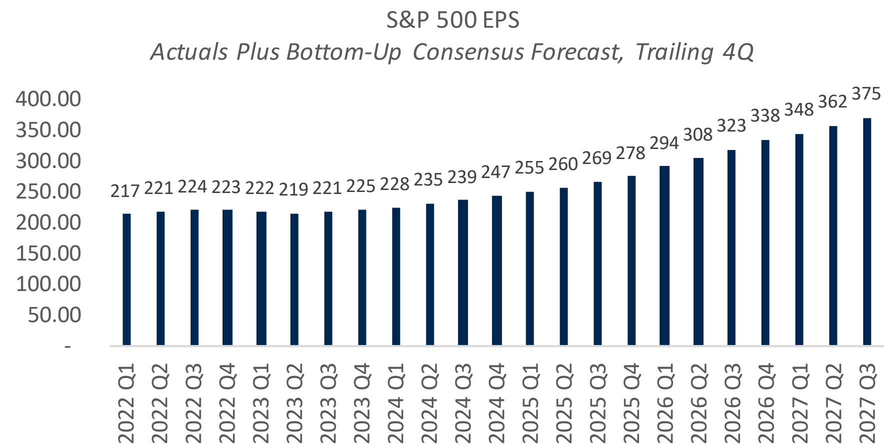
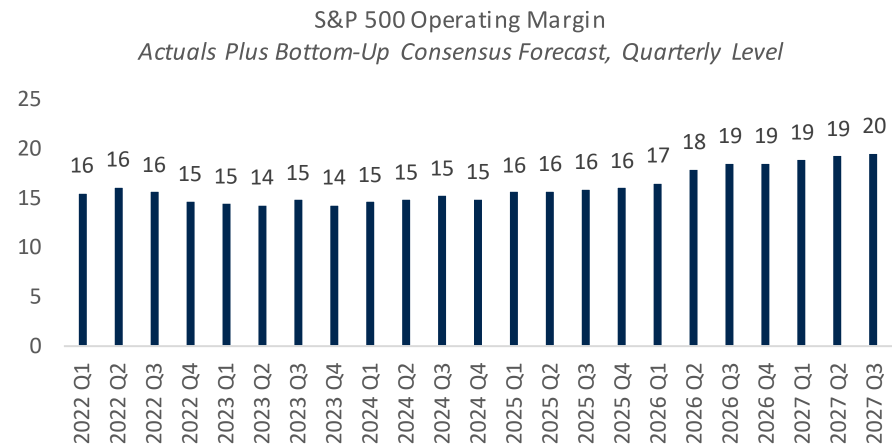
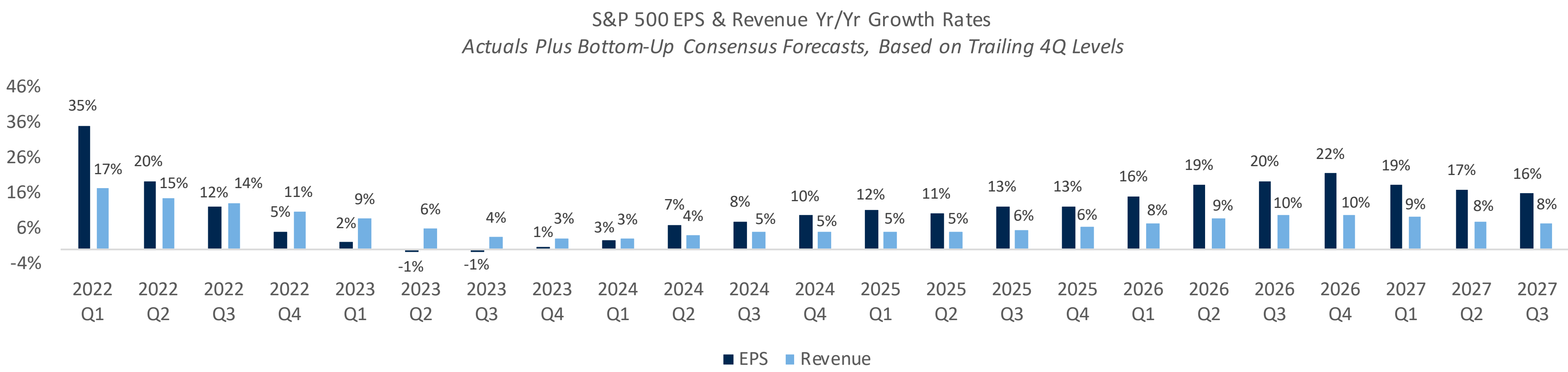
Tracking the Bottom-Up Consensus for S&P 500 EPS

- In our valuation and price target modeling, we are utilizing the bottom-up consensus S&P 500 EPS forecast as tracked by Bloomberg.
- For 4Q26, the trailing dollar value per share level is $338 (which also currently reflects a full-year, calendar-year 2026 level). This has improved significantly since the start of the year where it started out at $313.
- The current bottom-up consensus forecast bakes in some operating margin expansion for the broader index this year ahead and revenue growth of 10%.
- The anticipated yr/yr growth in EPS for 4Q26, on a trailing four-quarter basis, is 21.8%, up from the 12.6% growth rate anticipated for 2025.
- Note, our valuation/EPS modeling now uses 1Q27 as its starting point, where consensus anticipates $348 on a trailing 4Q basis for a growth rate of 19%.



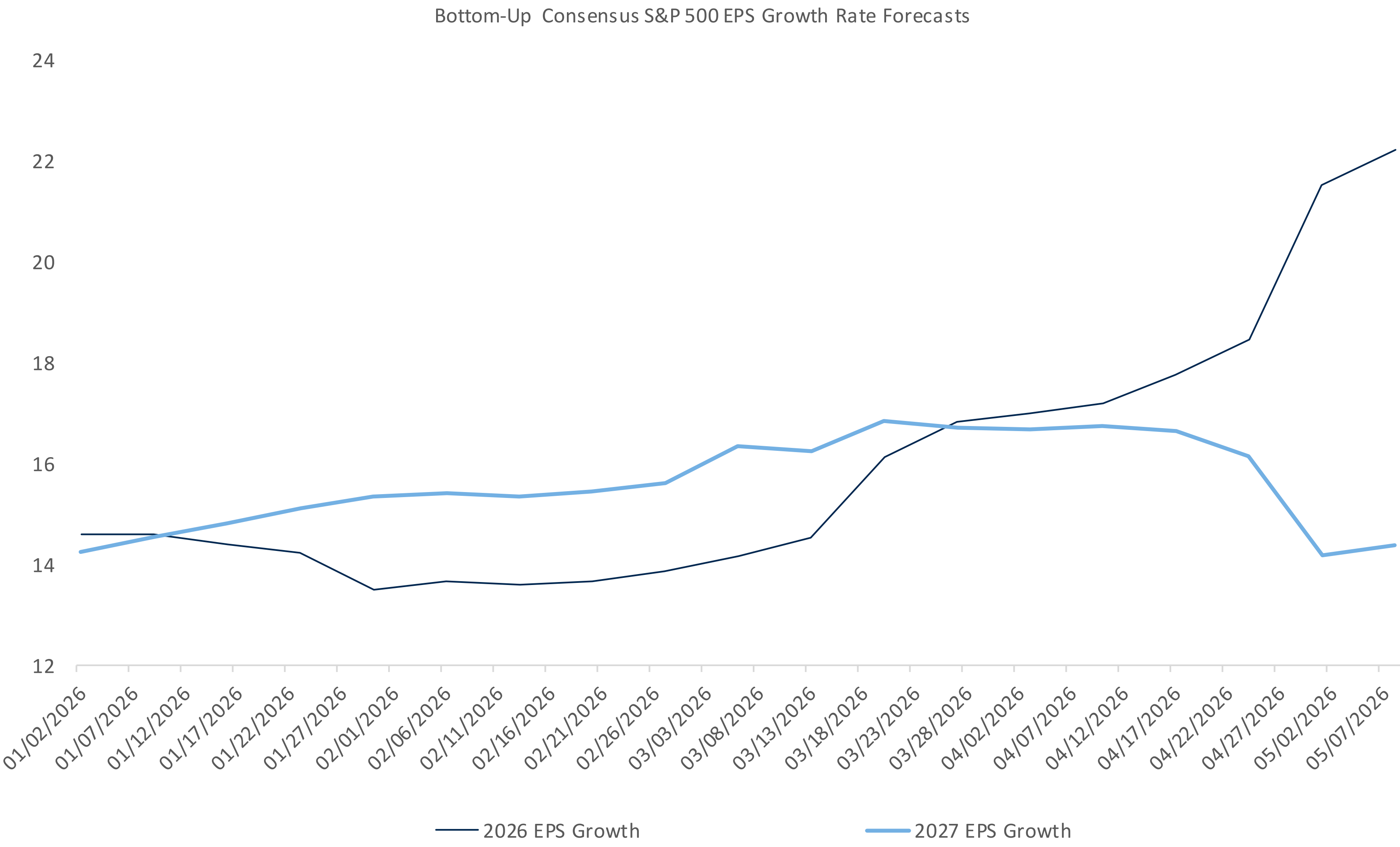




Note: Operating margin stats exclude REITs and Financials; this data is maintained by Bloomberg and can be found on the BI STOX page on Bloomberg – an interactive model is not available from the RBC US Equity Strategy team.
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg; latest available data as May 13, 2026

2026 Consensus EPS Growth Rate Forecast Has Moved Up, While 2027 Has Moved Down

- For 2027, the dollar value of consensus EPS has moved up, but the implied growth rate has come down.



Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
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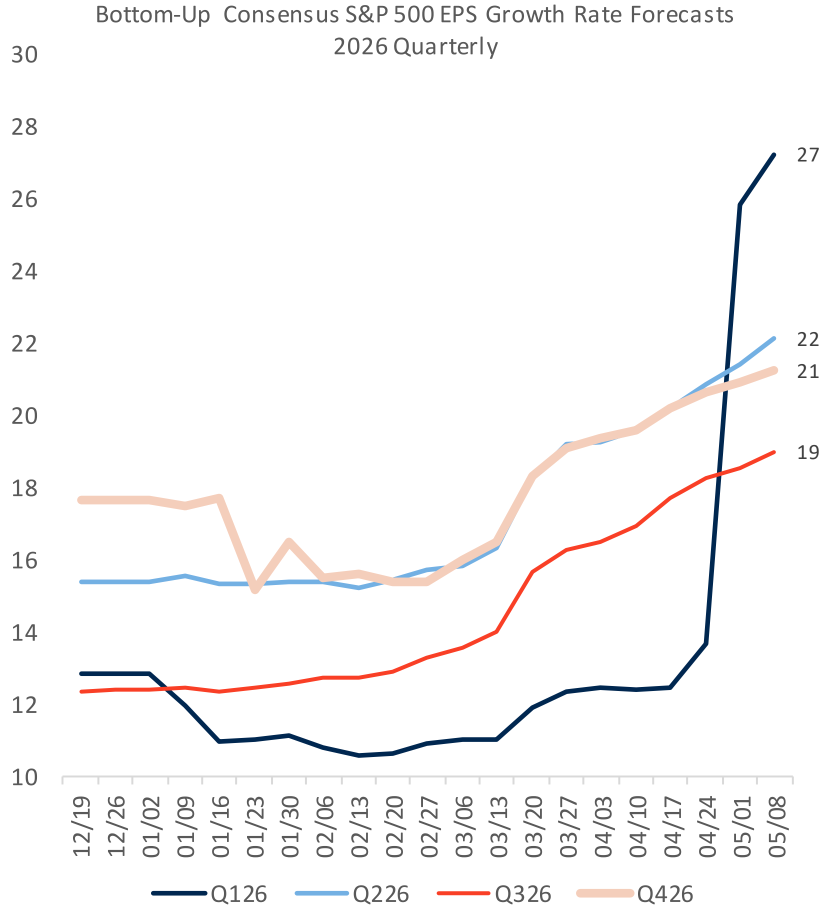
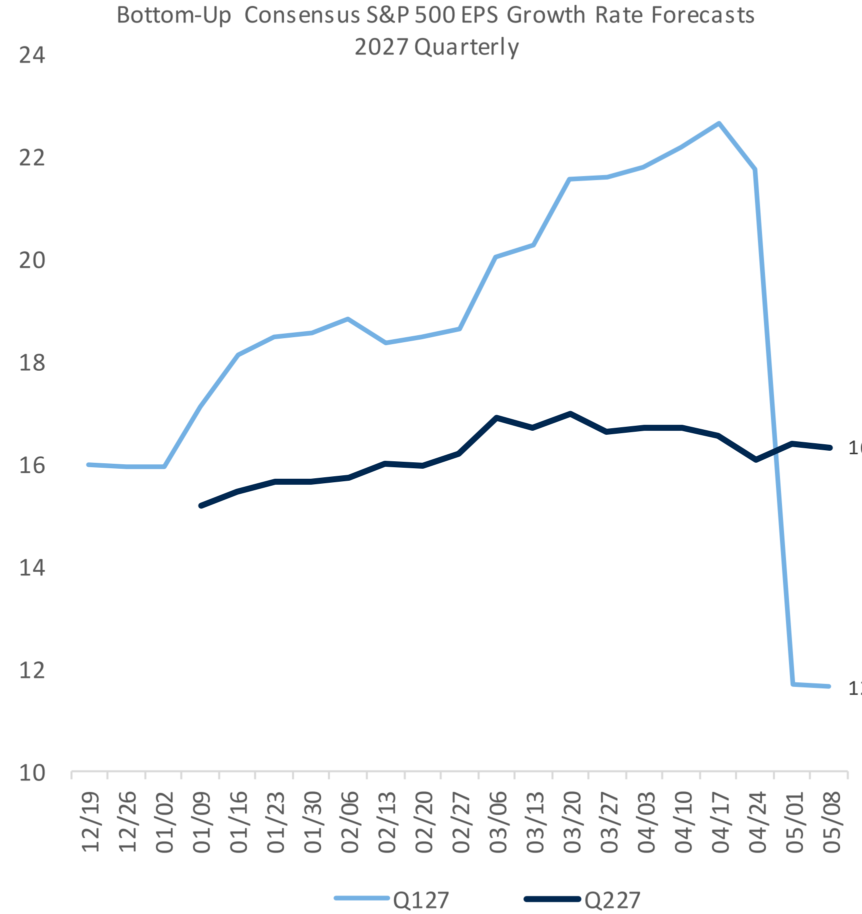
S&P 500 1Q26 Consensus EPS Growth Rate Forecast Has Moved Up Sharply

- Other quarters in 2026 have also moved up, but not as sharply.
- The bottom-up consensus EPS growth rate has fallen for 1Q27, while that of 2Q27 has been stable.





Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
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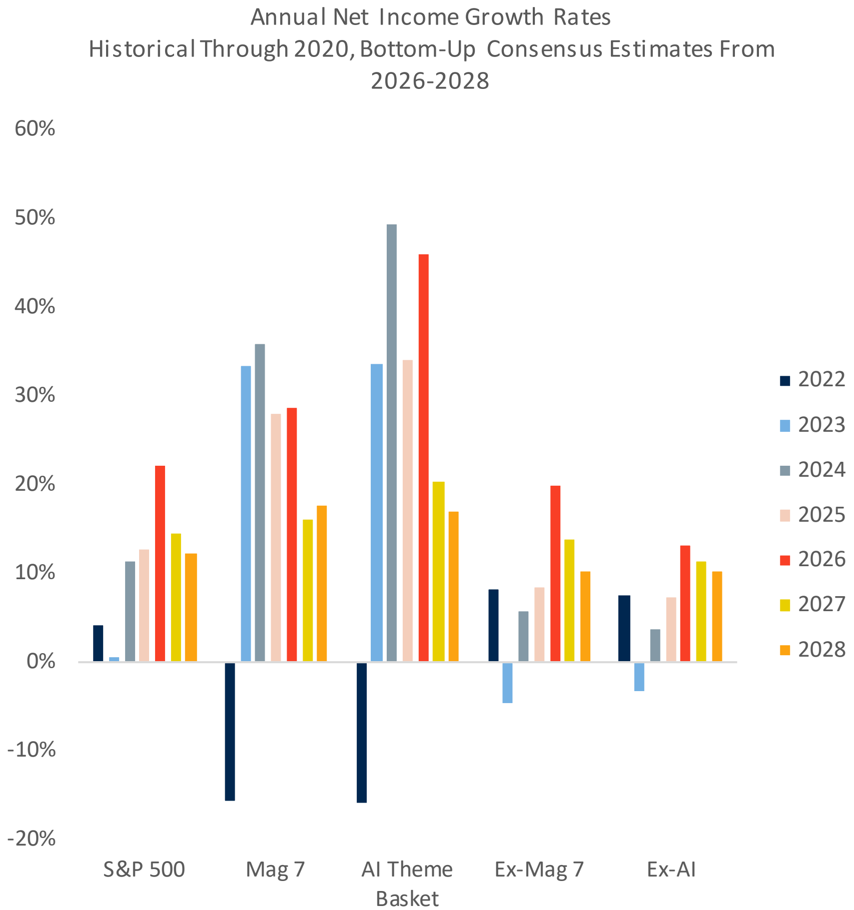
Consensus Expects AI Basket to See Superior Net Income Growth Through 2028

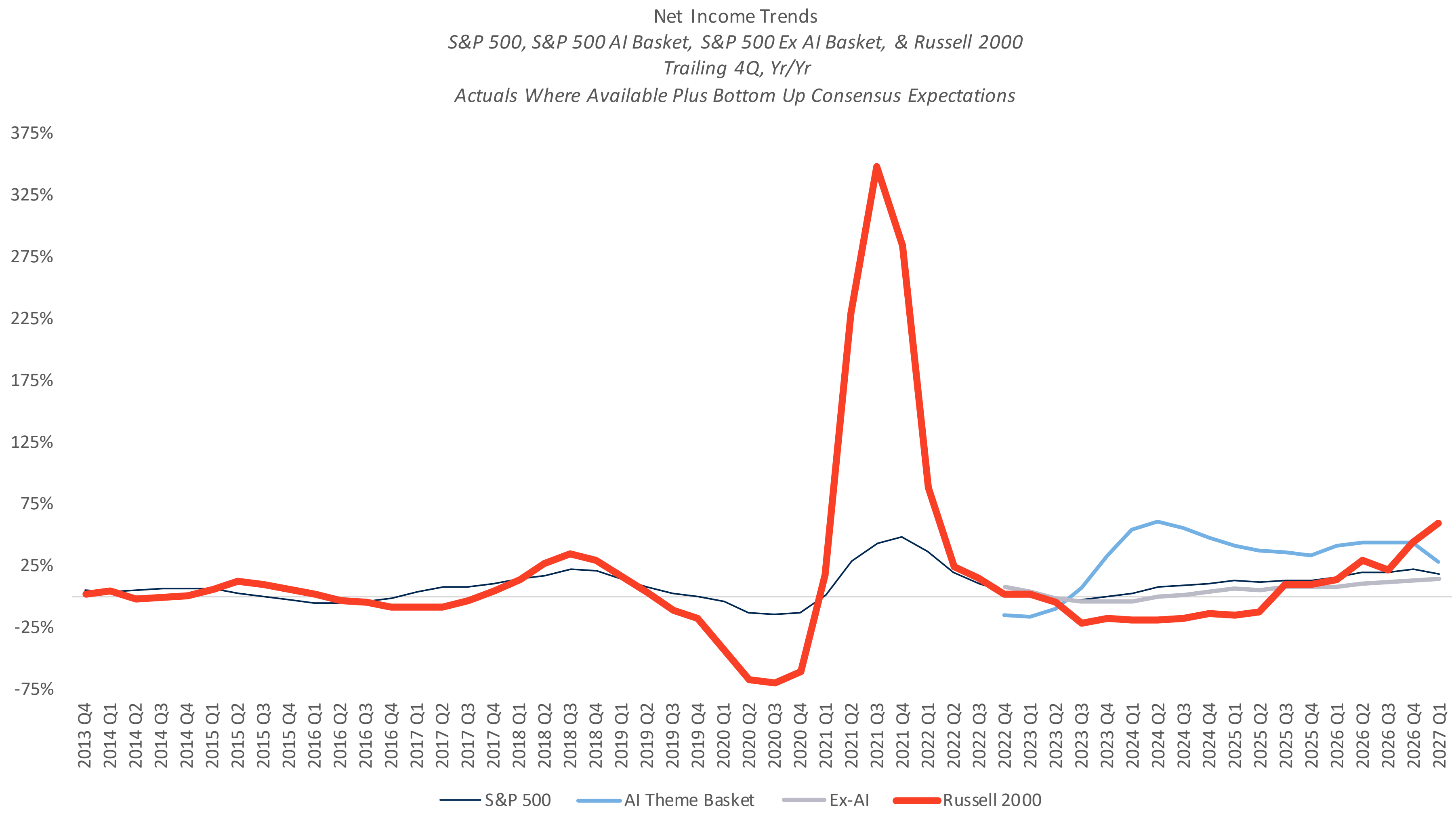
- S&P 500 net income is expected by consensus to peak in 2026, then decelerate in 2027 and 2028. The Mag 7 appears to have peaked in 2024, with deceleration expected through 2027 and some reacceleration anticipated in 2028. Meanwhile, a broader AI basket is anticipated to see far superior growth in 2026 to both the broader index and Mag 7, followed by deceleration in 2027 and 2028.
- The AI basket is expected to be stronger than the ex-AI basket in all three years going forward, and stronger than the Mag 7 in 2026 and 2027.
- The AI basket is also expected to expand its dominance over the ex-AI basket in 2026 relative to 2025.



Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026; S&P 500 AI Basket includes tickers: ACN, ADBE, AMD, GOOGL, AMZN, ANET, AVGO, DDOG, INTU, META, MU, MSFT, NVDA, ORCL, PLTR, QCOM, NOW, SMCI.

Consensus Expects Small Caps to Lag S&P 500 AI Names on Net Income Growth in 2026

- Small Caps' growth rate is now expected to keep accelerating through 1Q27. Throughout most of 2026, Small Cap's net income growth is expected to track a little below the S&P 500's AI-related names. But in 2027, Small Caps' growth rate is expected to pull ahead of the S&P 500's AI names.
- For 4Q26, Small Caps' growth rate is 44%, followed by the S&P 500 AI Basket (44%), the S&P 500 (22%), and the S&P 500 Ex-AI Basket (14%).
- For 1Q27, Small Caps' growth rate is 59%, followed by the S&P 500 AI Basket (28%), the S&P 500 (19%), and the S&P 500 Ex-AI Basket (14%).



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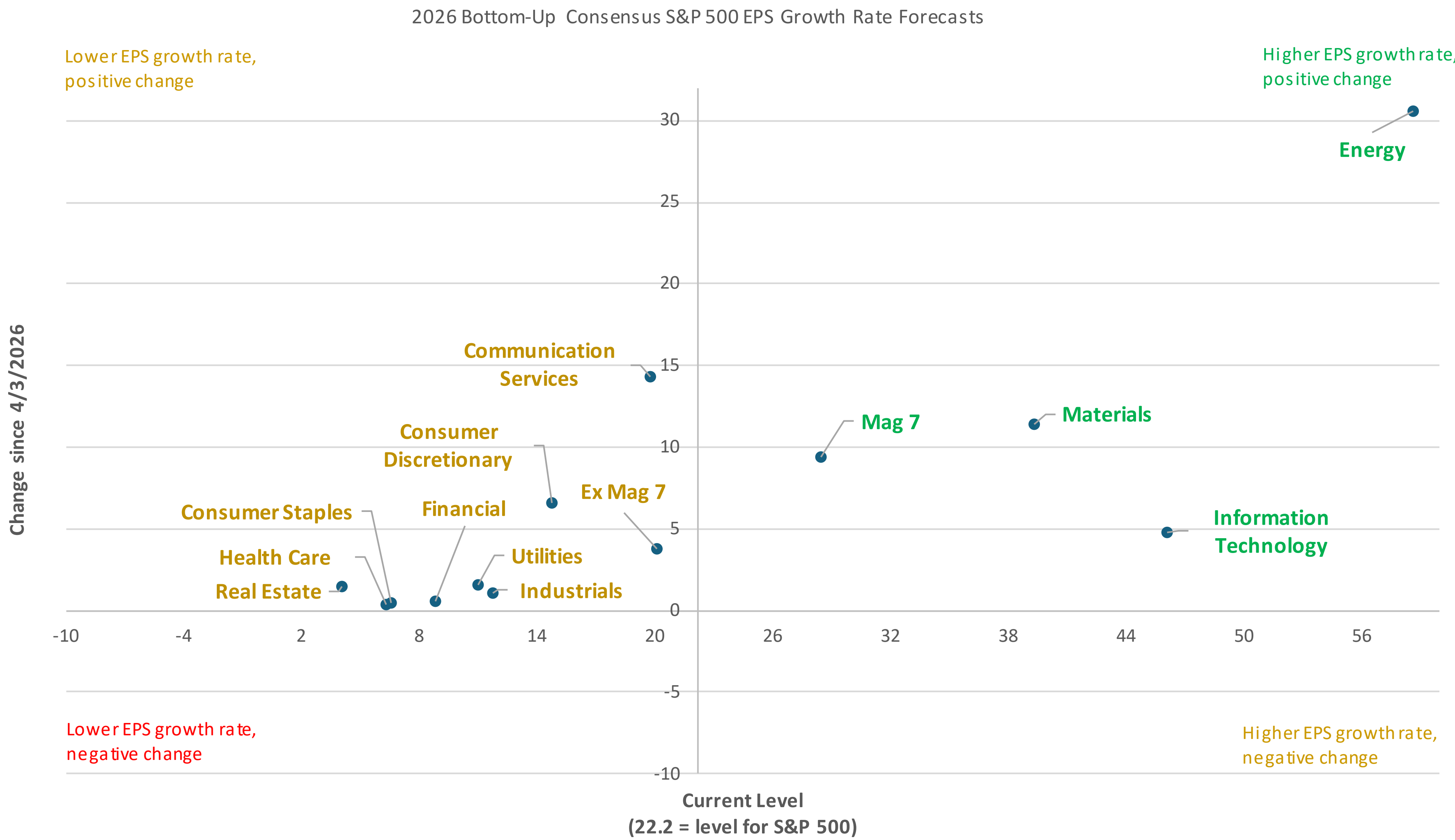
2026 Consensus EPS Growth Rates Strong & Improving for Energy, Tech, Mag 7 & Materials

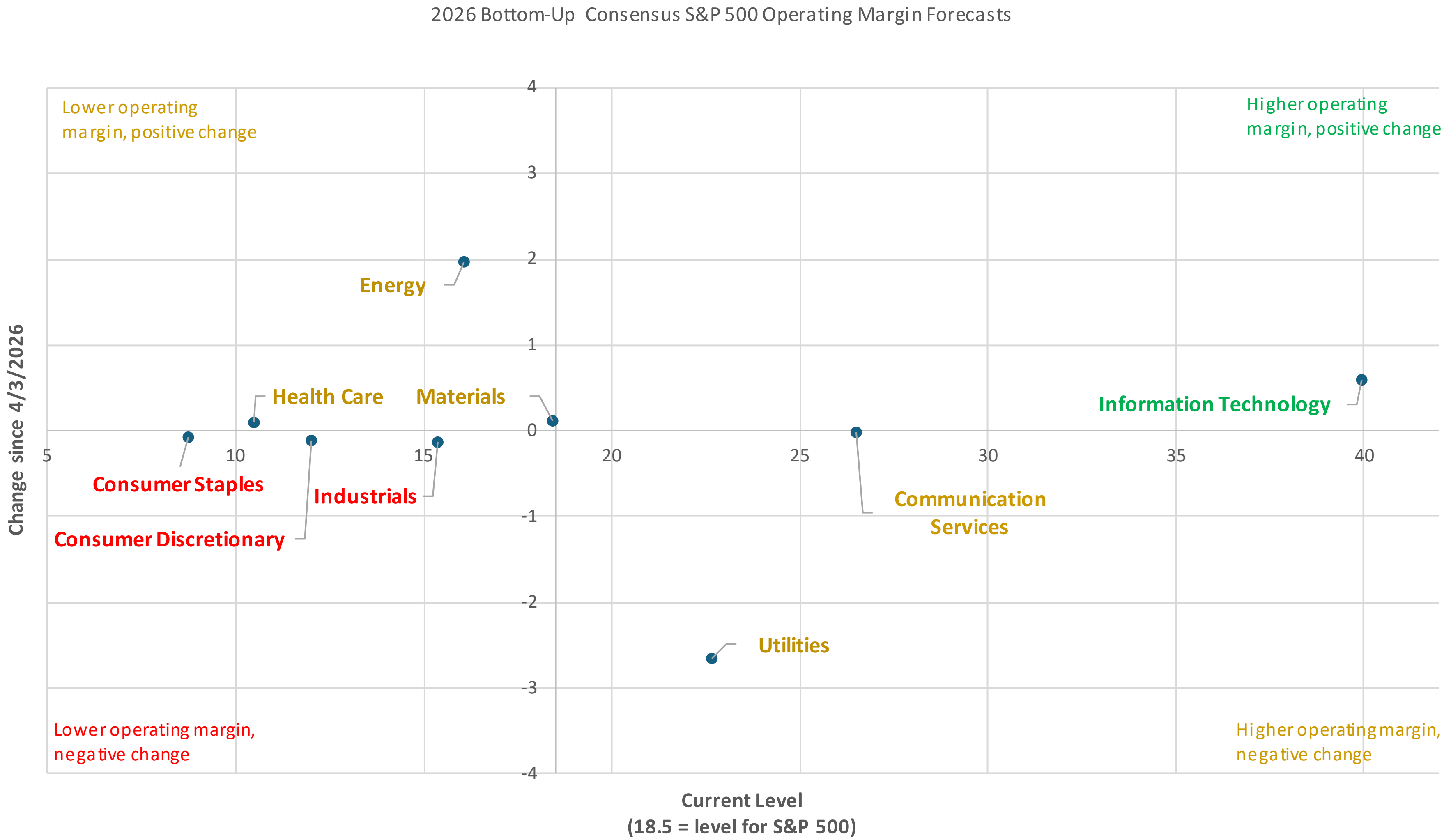
- Most sectors have seen their EPS growth rate forecasts stay essentially flat since the reporting season began, with only a modest increase.



Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.

2026 Consensus Operating Margin Forecasts Have Been Strong & Improving for Tech

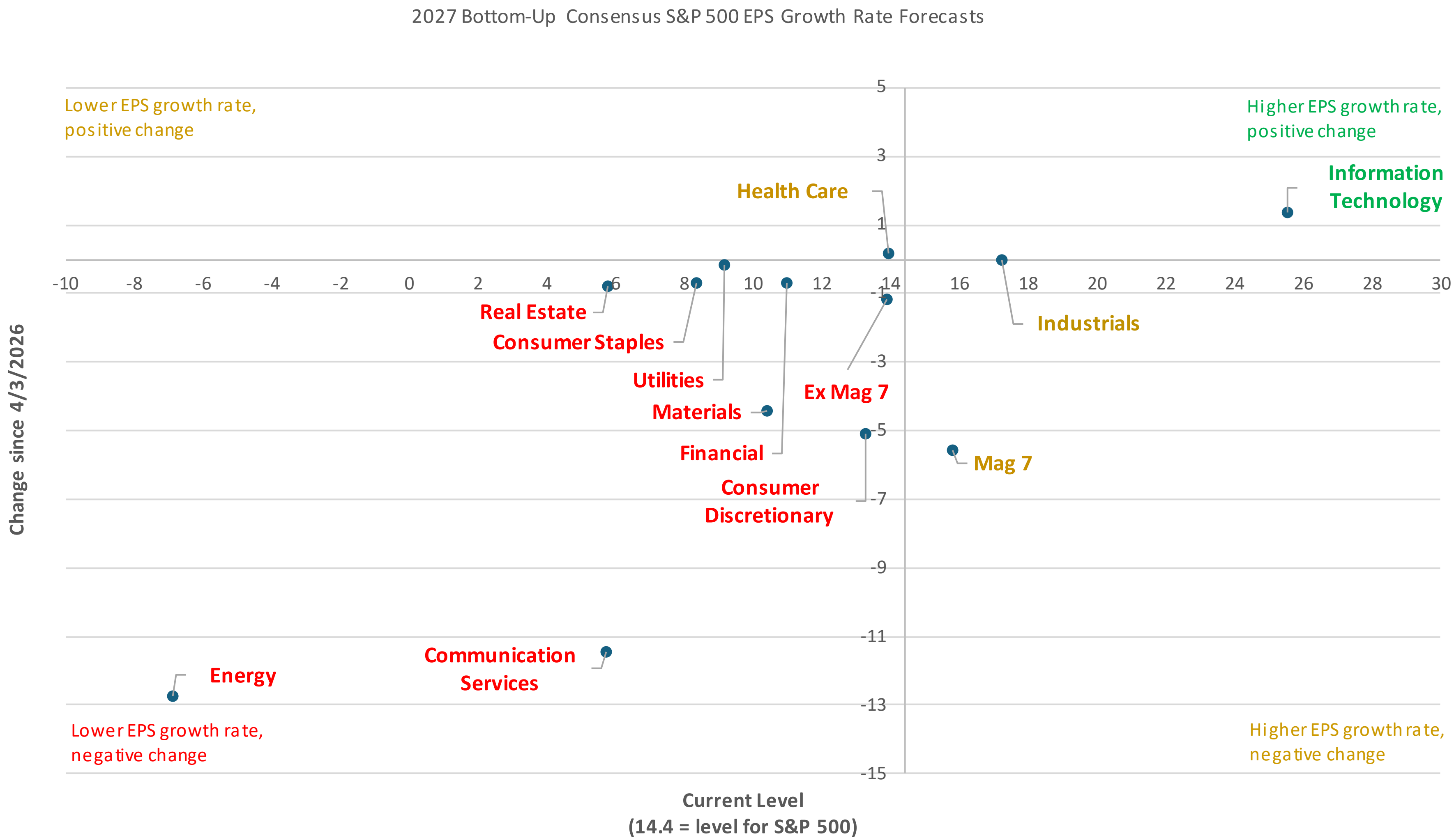
- Most other sectors haven't seen much movement of late.
- Energy has improved but remains below the broader market level.



Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.

Consensus 2027 EPS Growth Rates Have Been Strong & Improving for Tech

- Most other sectors haven't seen much movement of late or have dipped a little.



Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
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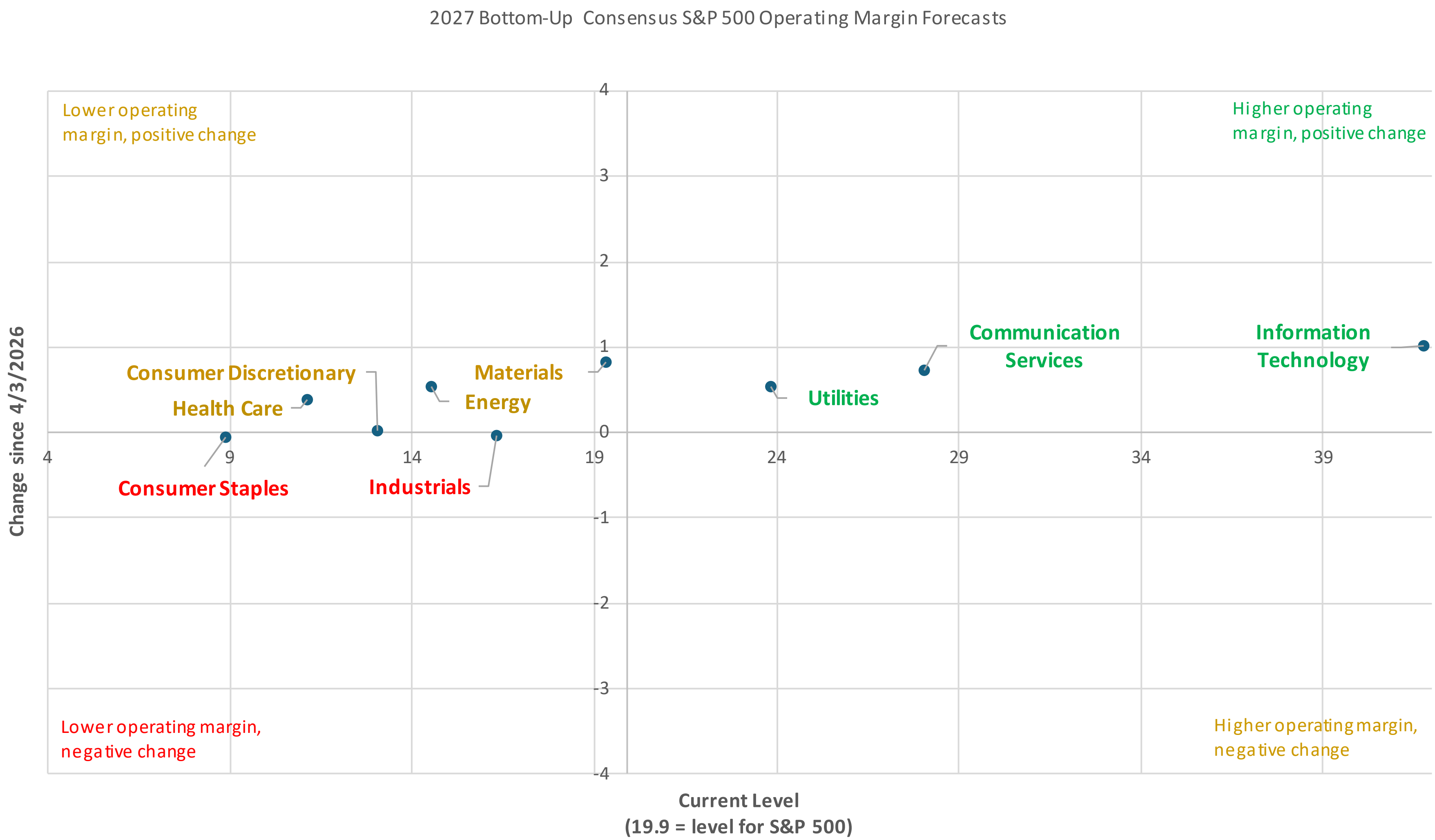
2027 Consensus Margin Forecasts Have Been Strong & Improving for Tech, Utilities & Comm Svcs

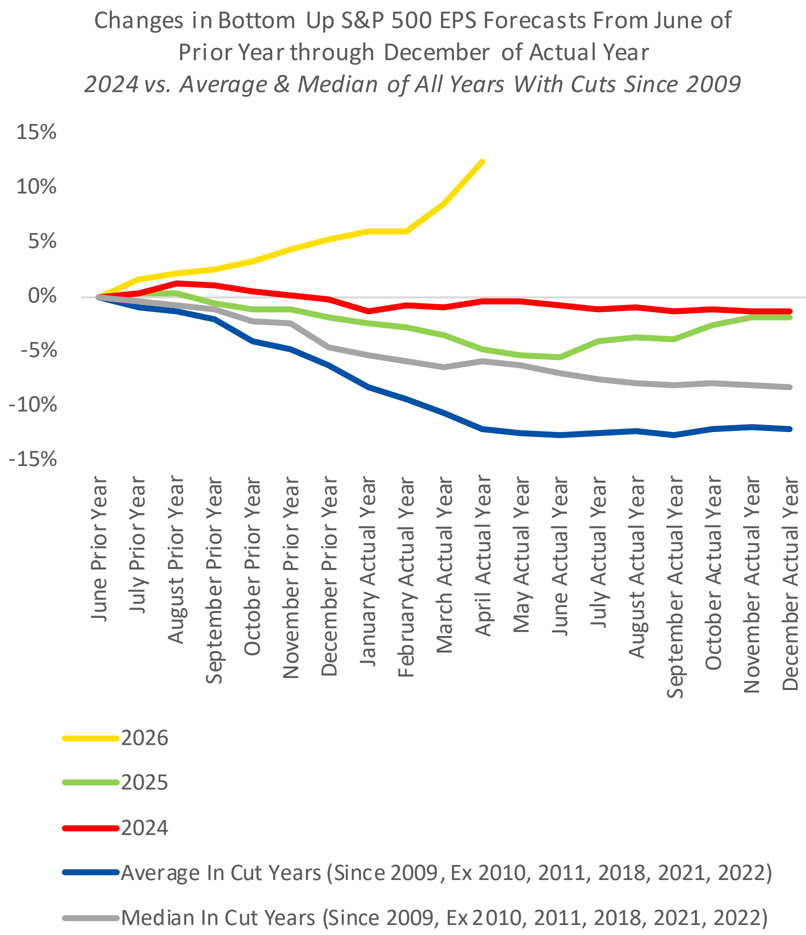
- Materials has also improved of late but remains in line with the broader market in terms of level.

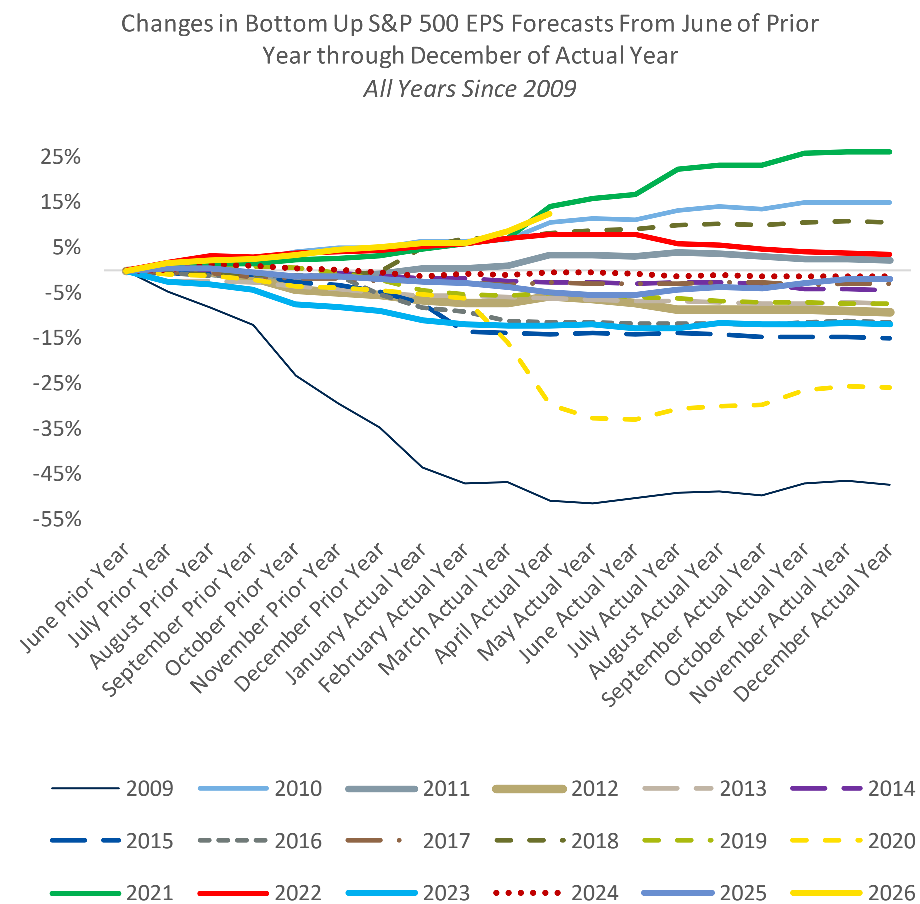


Source: RBC US Equity Strategy, Bloomberg, latest available data as May 13, 2026
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.

Consensus 2026 S&P 500 EPS Estimates Have Been Climbing Since Last Summer

- S&P 500 EPS tend to fluctuate as the year in question comes into view and then progresses. Most years, estimates start out too high. Looking back to 2009, there have been only five years in which the final number ended up being higher than the estimate in place in the June of the previous year.
- The median cut in downward adjustment years has been 8%, while the average downward adjustment has been 12%.
- 2026 has been an unusual year, with estimates climbing in a similar fashion to what we saw at this point in time for 2010, 2018, 2021, and 2022.

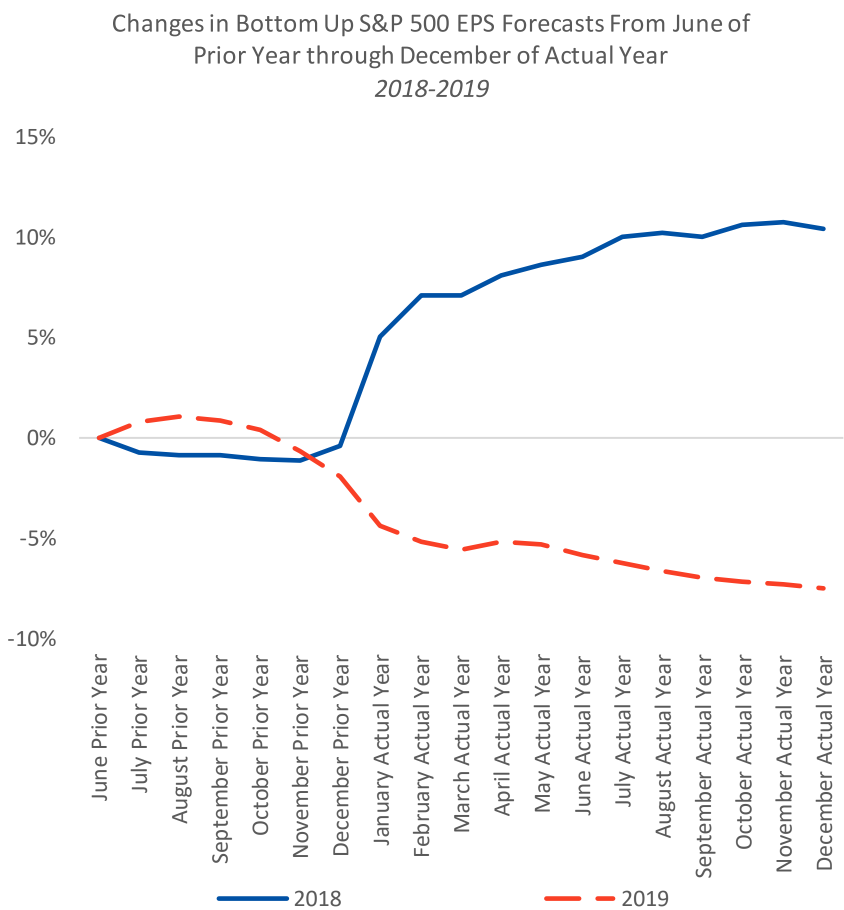


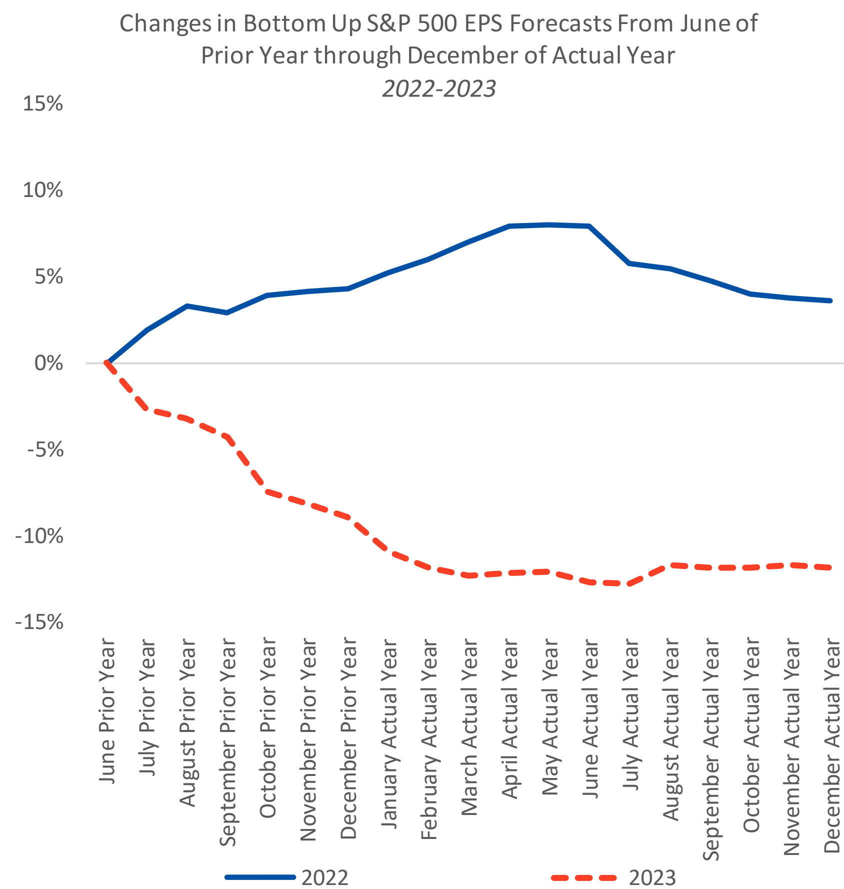


Source: RBC US Equity Strategy, Haver, S&P Capital IQ; through April 2026 (latest data point available)

Looking Back at 2018-2019 and 2022-2023 EPS Growth Forecasts

- Around the first Trump tariffs, S&P 500 EPS forecasts (bottom-up, consensus) were resilient for 2018, but steadily fell for 2019.
- A similar dynamic was seen around the Russia-Ukraine war. 2022 EPS forecasts fell a little in the second half of the year, but took a bigger hit for 2023 early on.
- This adds to our concern that earnings risks from the Middle East conflict may lie more in 2027 than 2026.

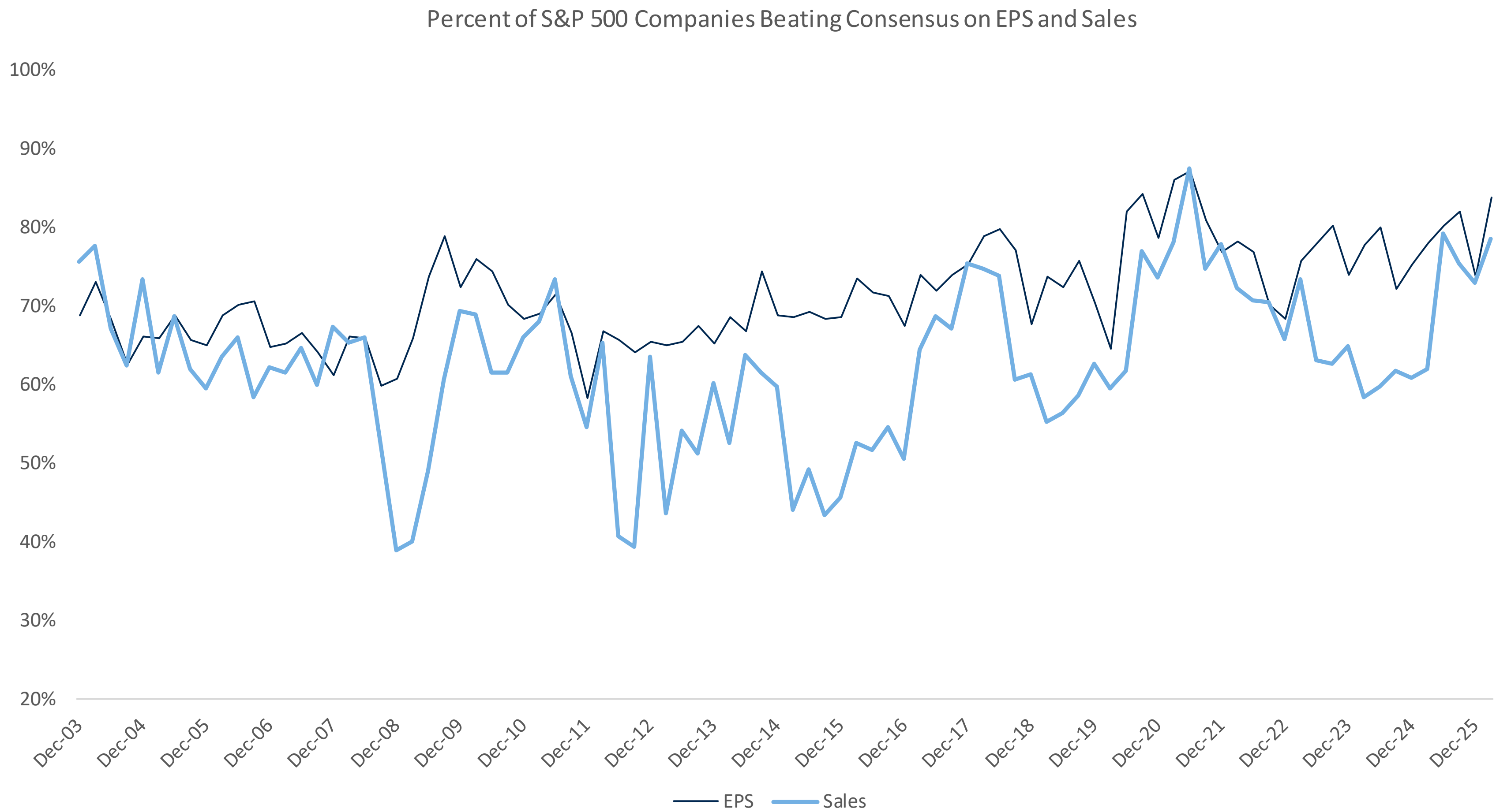




Source: RBC US Equity Strategy, Haver, S&P Capital IQ

In Large Cap, EPS and Revenue Beats for 1Q26 Have Been Stronger Than 4Q25 so Far

- 84% beating on EPS and 79% beating on sales for 1Q26 (vs. 74% on EPS and 73% on sales during 4Q25).



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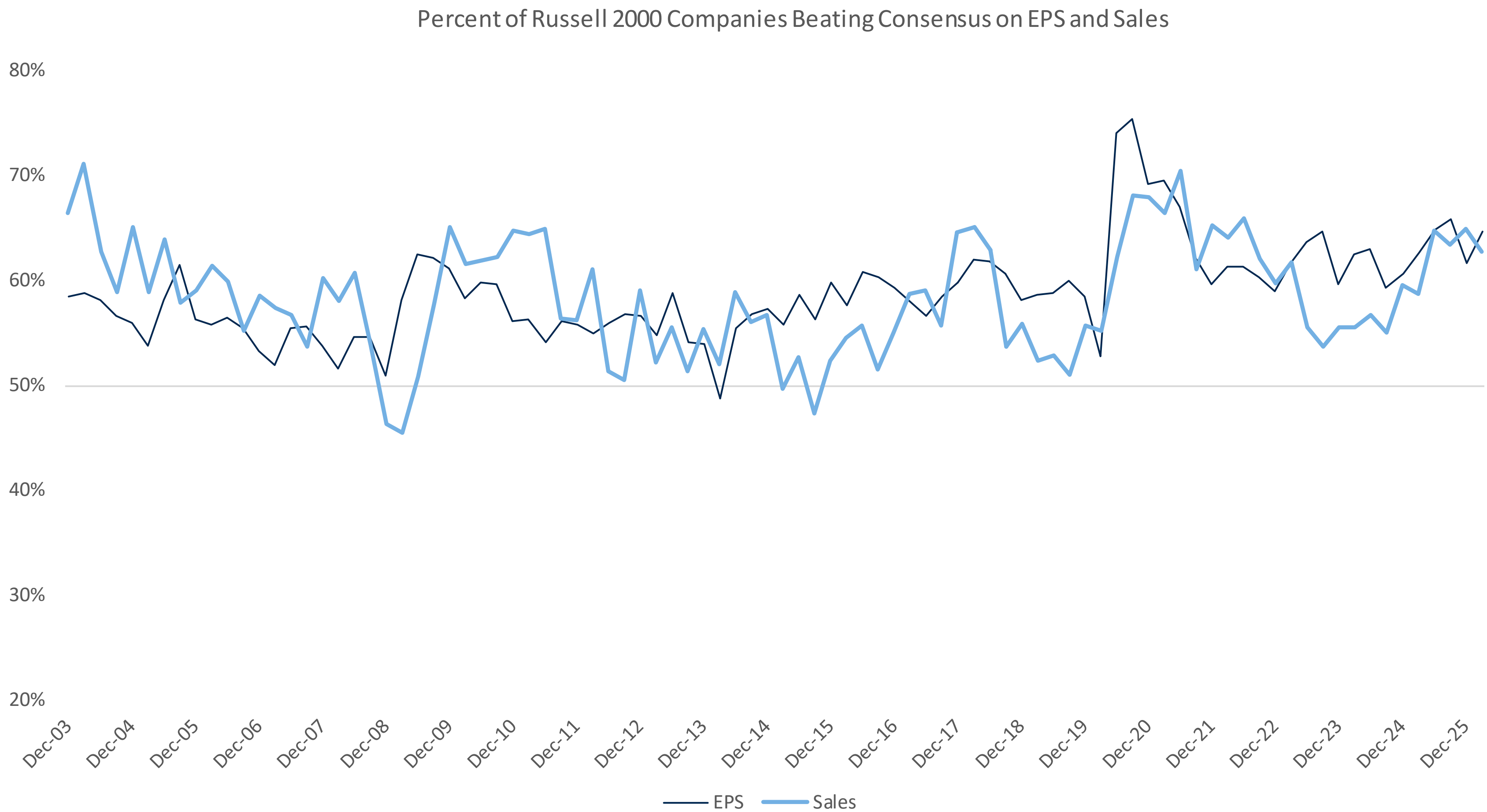
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi, CIQ estimates. S&P, Prelim data point for 1Q26 captured on May 12, 2026, with 89% of S&P 500 results in.

In Small Cap, EPS Beats Are Coming in Stronger Than Last Quarter so Far, but Not Revenue Beats

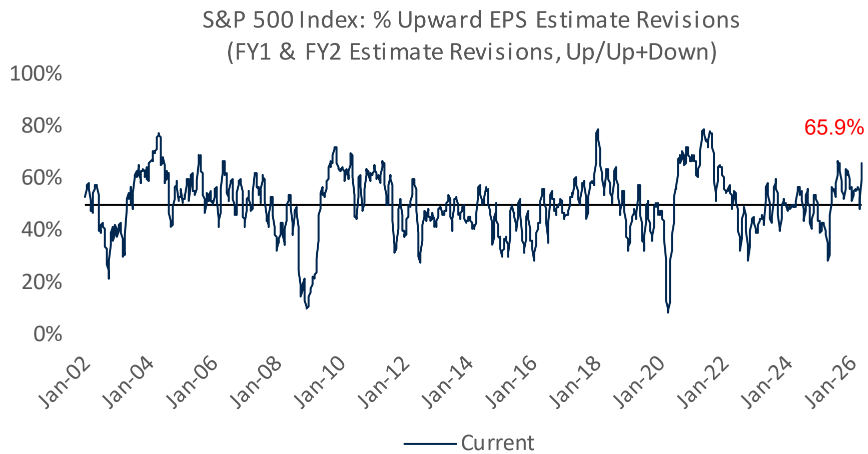
- 65% beating on EPS & 63% beating on sales for 1Q26 (vs. 62% on EPS and 65% on sales during 4Q25).

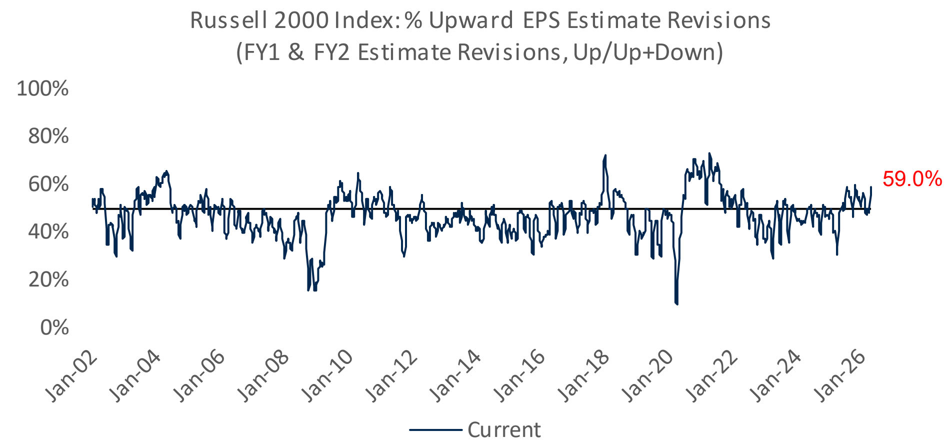


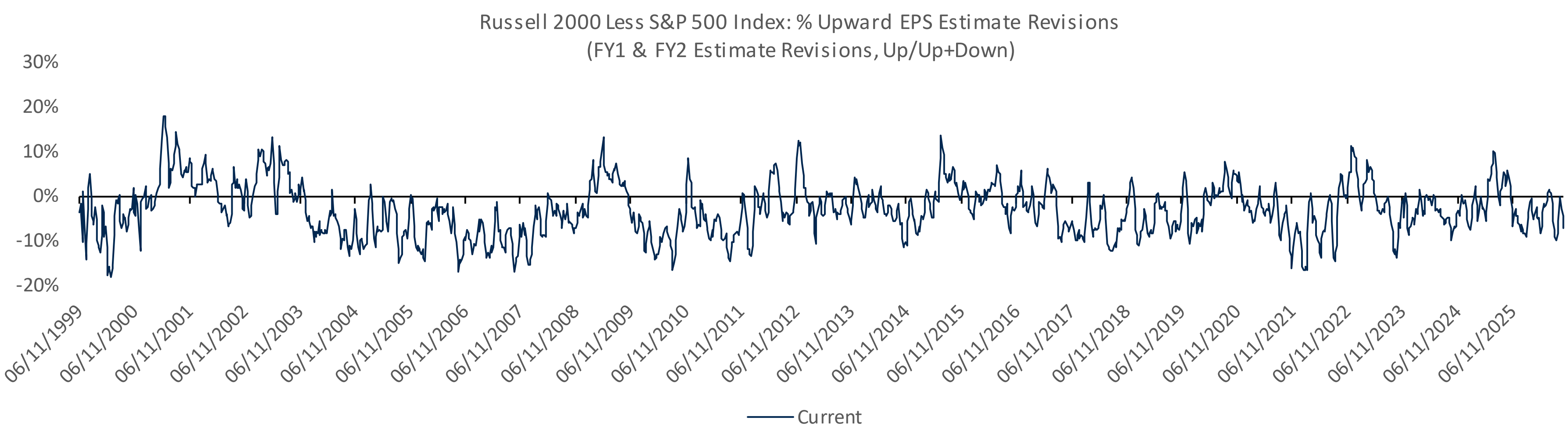
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi, CIQ estimates. Russell; Prelim data point for 1Q26 captured on May 12, 2026, with 59% of Russell 2000 results in.

EPS Estimate Revisions Have Strengthened for Both S&P 500 and Russell 2000 Recently

- Upward revisions are positive for Small Cap in the most recent update, while revisions moved higher for Large Cap as well.
- However, this gauge of earnings sentiment is still slightly below the highs of fall 2025 for both.
- Note that the S&P 500 reclaimed a slight advantage to the Russell 2000 on this stat earlier this year, and has continued to move that way in recent updates.







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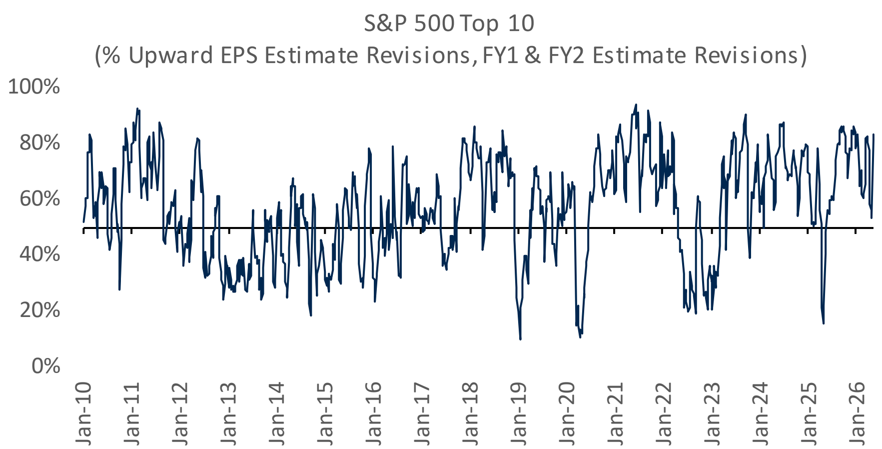
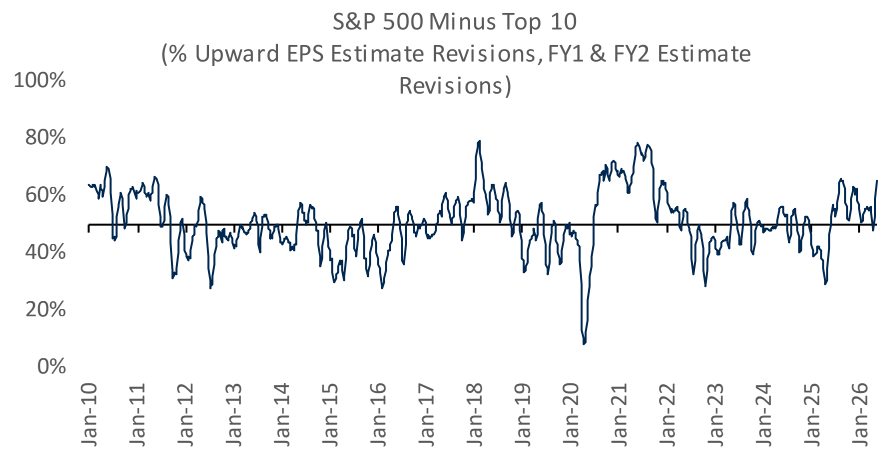
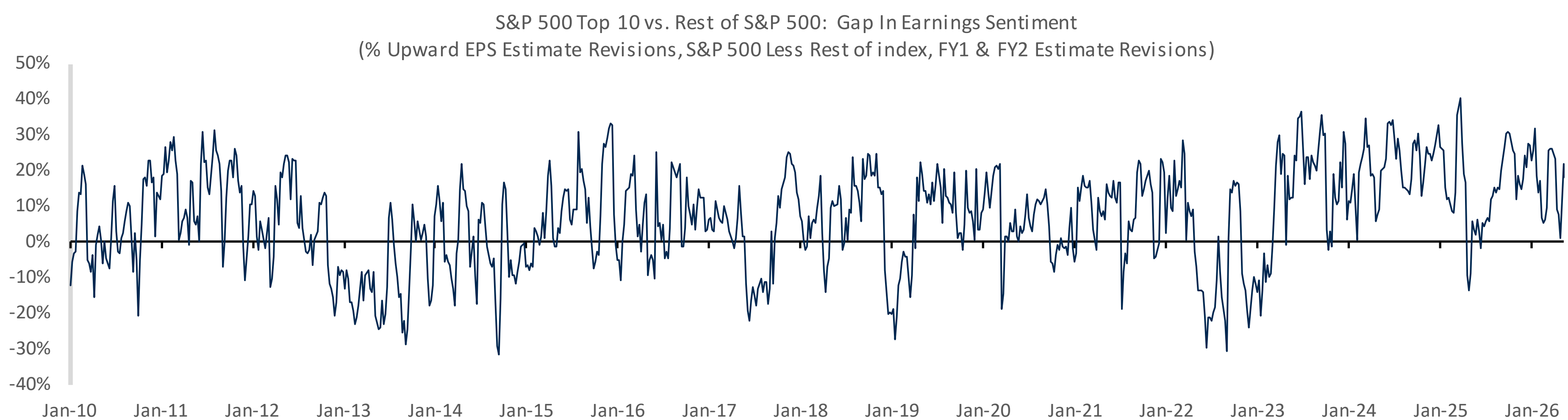
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi, CIQ estimates, S&P, Russell. For REITs, FFO/share revisions are used instead of EPS revisions; as of May 12, 2026.

EPS Revisions Have Surged For Both Biggest Cap Names in the S&P 500 and the Rest of the Index

- The dominance of the biggest market cap names continued to hold an advantage in the most recent update.







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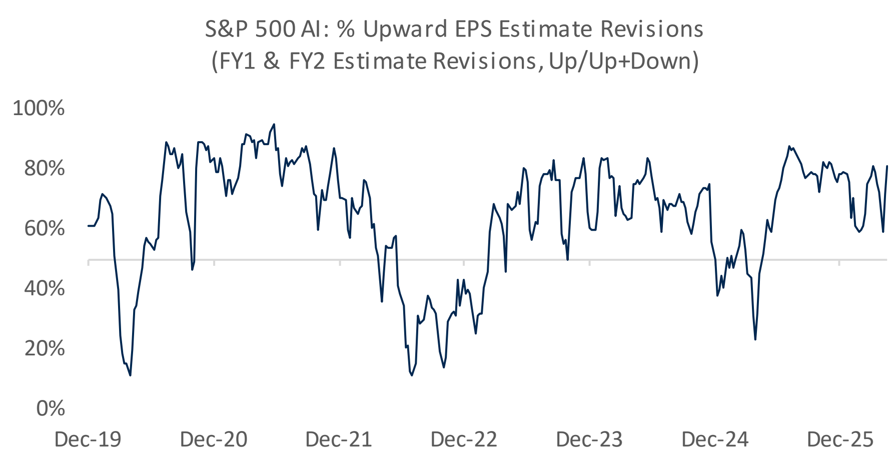
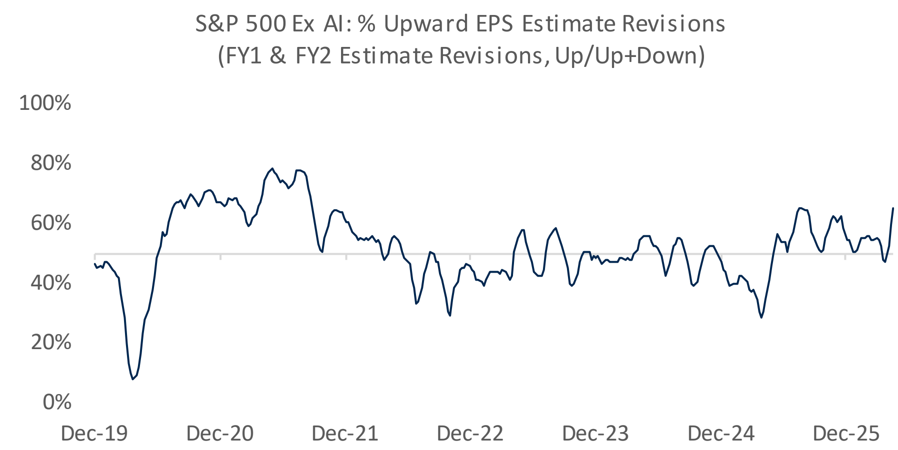
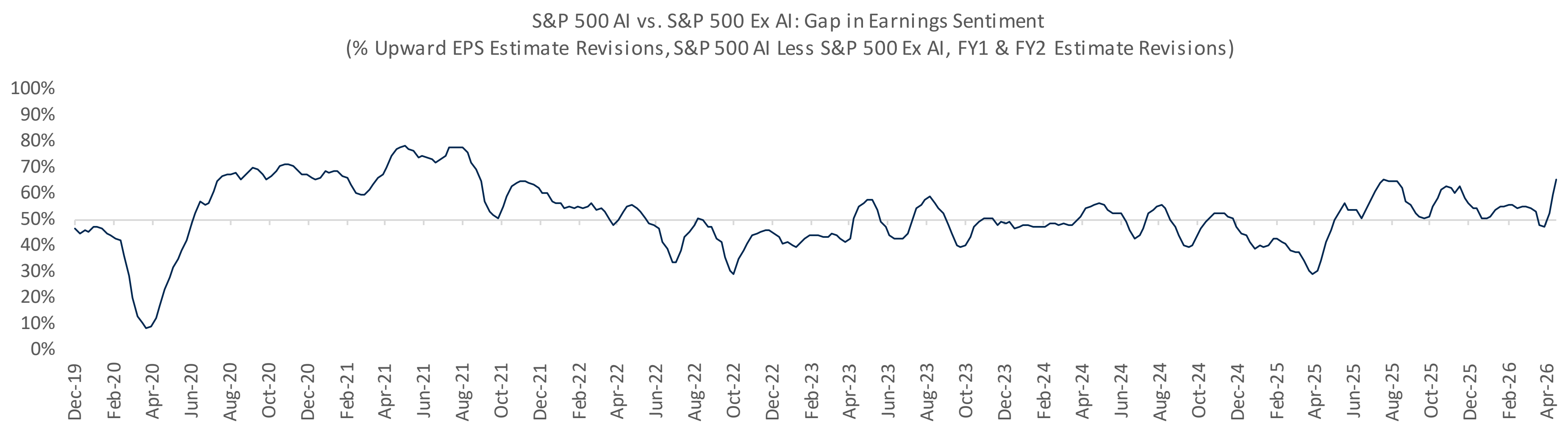
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi, CIQ estimates, S&P. For REITs, FFO/share revisions are used instead of EPS revisions; as of May 12, 2026.

EPS Revisions Have Surged For Both AI Focused Names in the S&P 500 and the Rest of the Index

- The AI focused basket has a clear advantage on this metric, however.



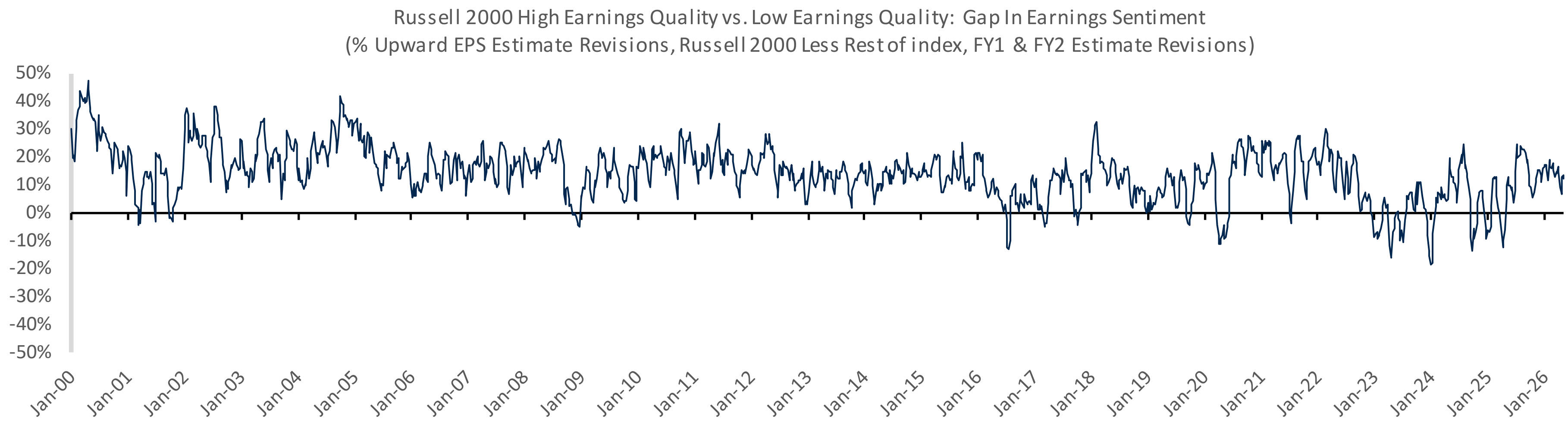


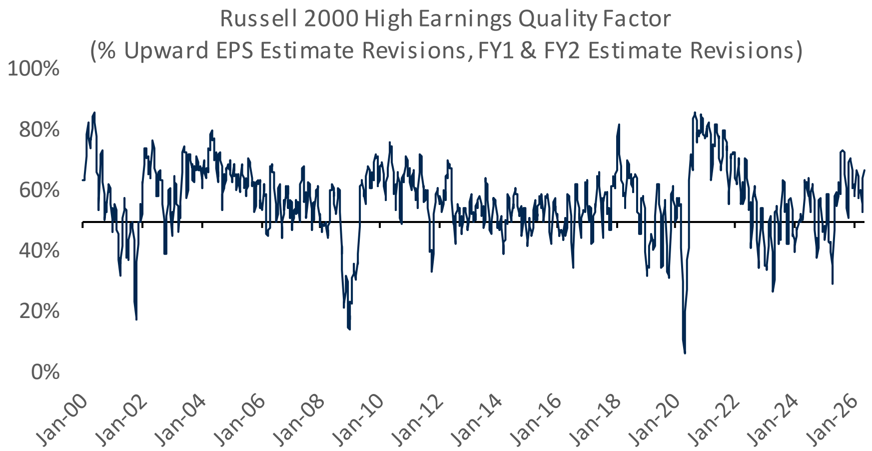


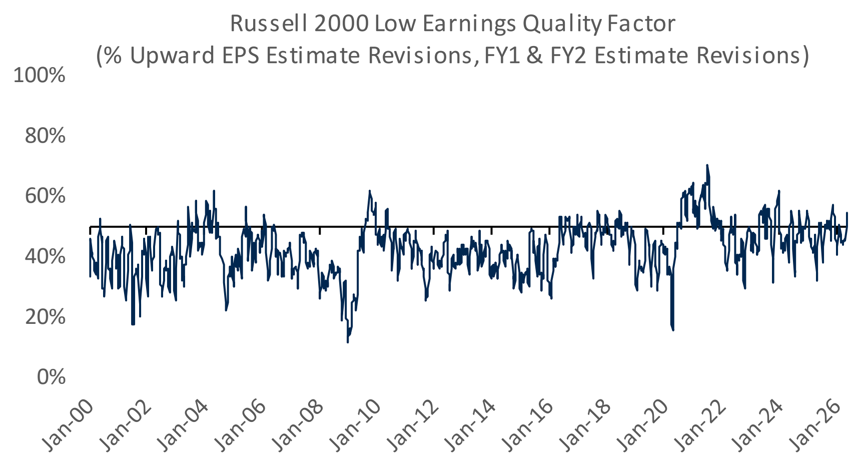
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi, CIQ estimates, S&P, latest available data as May 12, 2026; S&P 500 AI Basket includes tickers: ACN, ADBE, AMD, GOOGL, AMZN, ANET, AVGO, DDOG, INTU, META, MU, MSFT, NVDA, ORCL, PLTR, QCOM, NOW, SMCI.

Small Cap Stocks w/High EPS Quality Have Seen Better EPS Revisions Trends Than Low EPS Quality

- High EPS Quality Small Cap stocks are seeing rates of upward revisions that are positive. Low EPS Quality Small Cap stocks are also seeing rates of upward revisions that are positive. However, low EPS quality stocks are seeing better trends relative to their own history and are back in positive territory, which may be helping performance trends. The gap between high and low quality on EPS revisions has narrowed a bit of late.



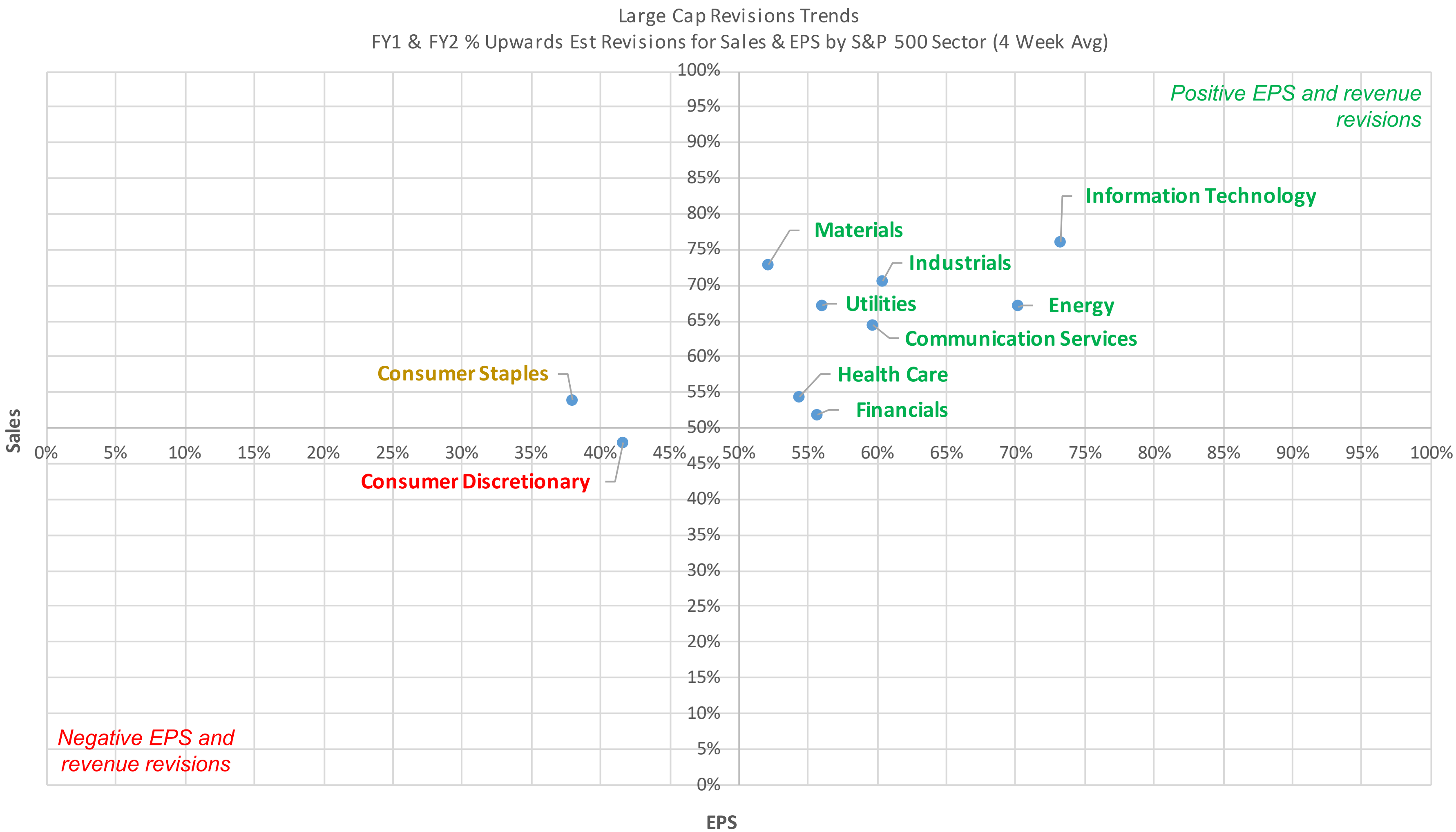




Note: The earnings quality factor is a sector-neutral, equal-weighted multifactor based on historical constituents that combines the trailing 12-month return on equity, earnings stability (measured as the ratio of the one-year change in EPS to the standard deviation of the one-year change in EPS across eight prior periods), and the distinction between positive and negative earnings based on whether EPS is above or below zero.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of May 12, 2026

Within Large Cap, Most Sectors Are Now Seeing Positive EPS and Sales Revisions

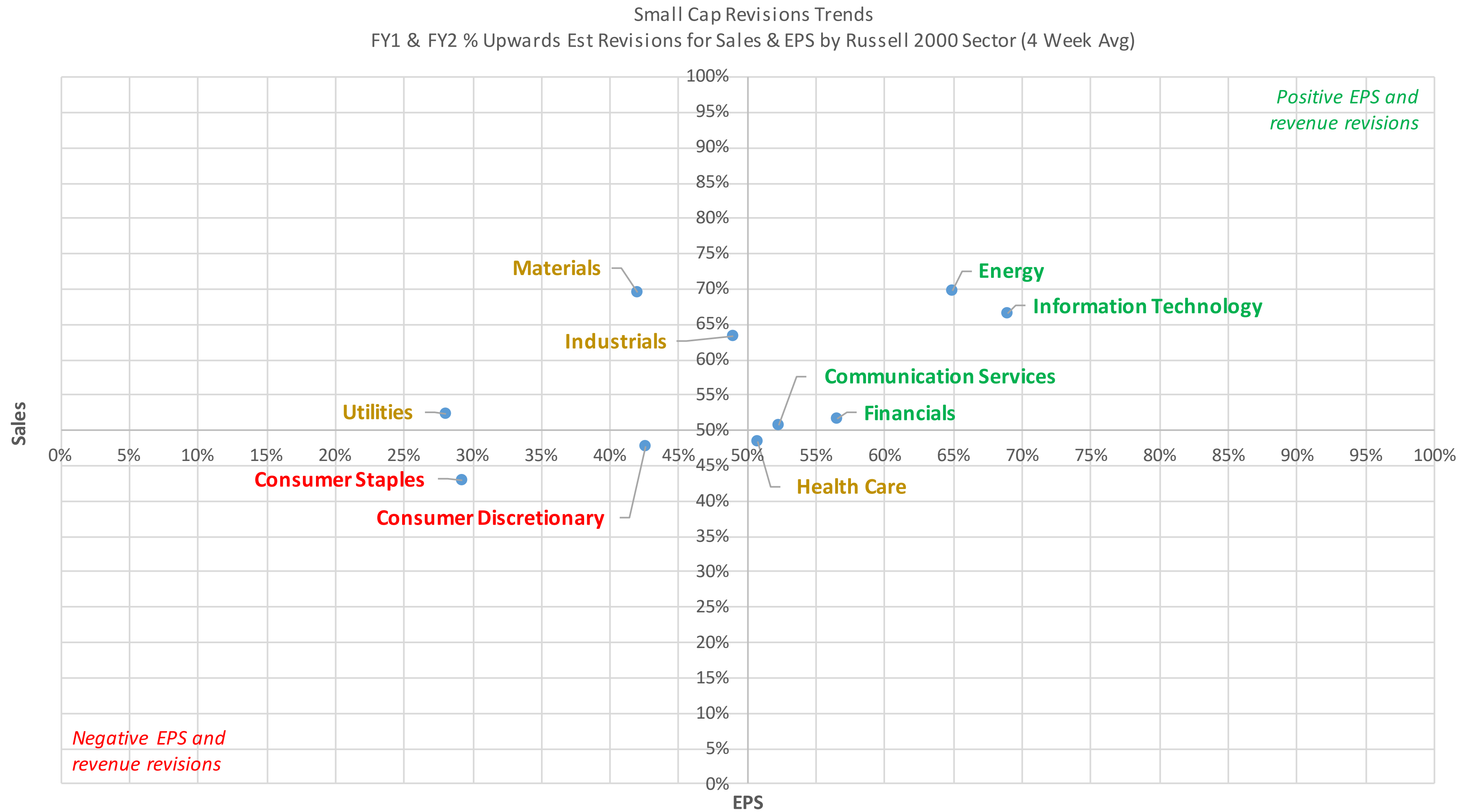
- Trends remain strongest in Tech and Energy. Industrials and Utilities also remain strong.
- Discretionary has seen EPS revisions deteriorate and turn negative – it's now the only sector in negative revisions territory on both EPS and sales.
- Staples improved in the most recent update, but its EPS revisions remain negative on the 4-week average.
- Health Care, Materials and Financials all improved in the most recent update and now sit in positive territory on both EPS and sales revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, CIQ estimates, S&P. Excludes REITs; as of May 12, 2026

Within Small Cap, Tech, Financials, Comm Svcs and Energy Are Seeing Positive EPS & Sales Revisions

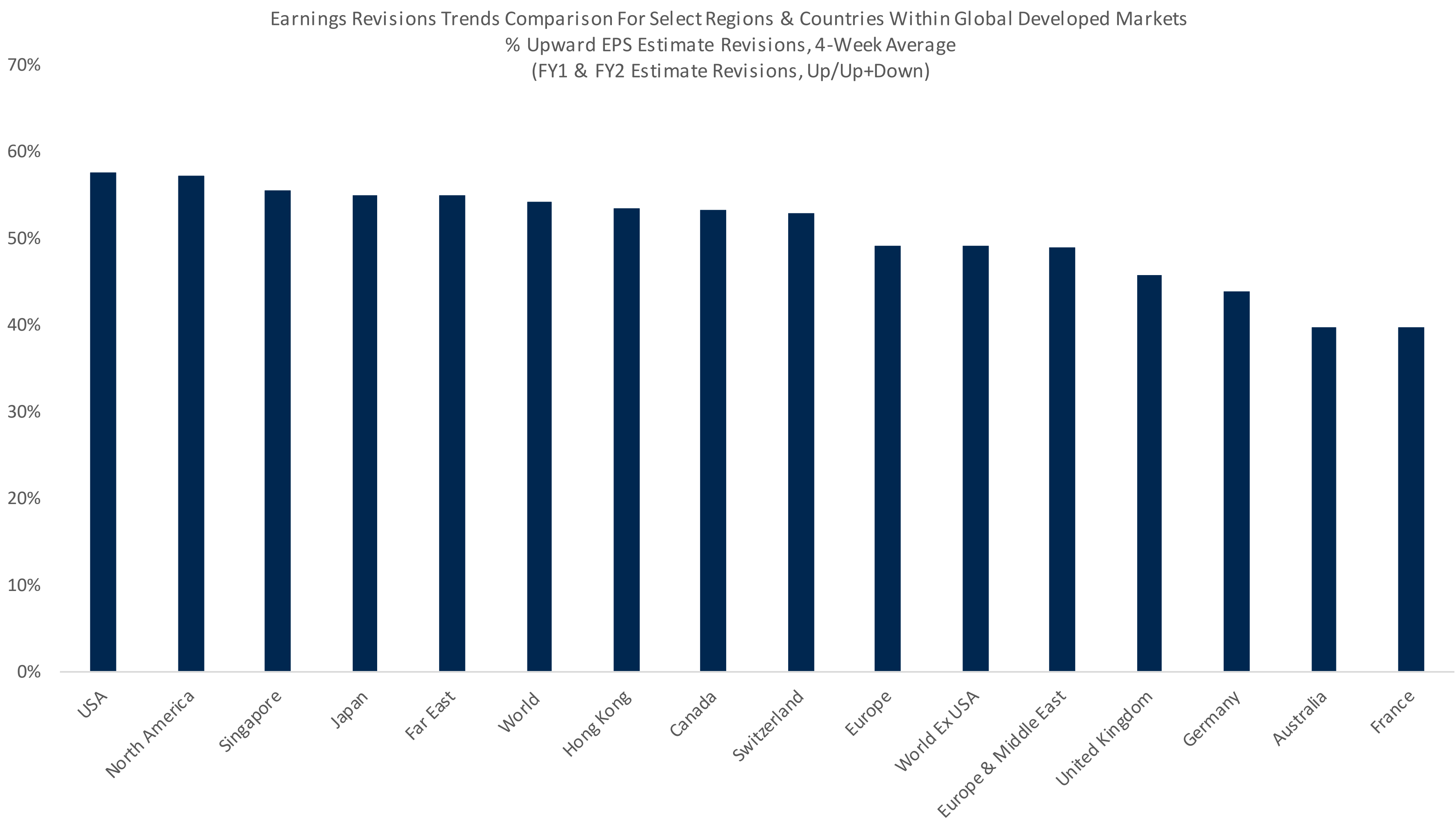
- Staples and Consumer Discretionary are seeing negative revisions for both EPS and sales.
- Communication Services improved on EPS and sales revisions in the most recent update, now sitting in positive territory on both.
- Meanwhile, Health Care improved on EPS revisions, but still doesn't look particularly compelling on this metric. Utilities is now positive on sales revisions on the 4-week average but continues to see challenges on EPS revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, CIQ estimates, Russell. Excludes REITs; as of May 12, 2026

EPS Revisions Have Been Strongest in the Far East & North America, Weakest in Europe

- Revisions for Europe have been balanced between upward and downward revisions.



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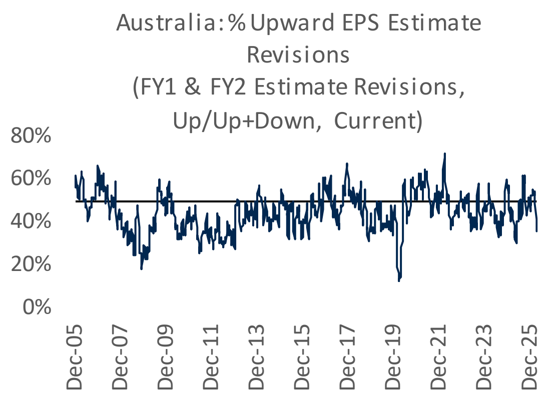
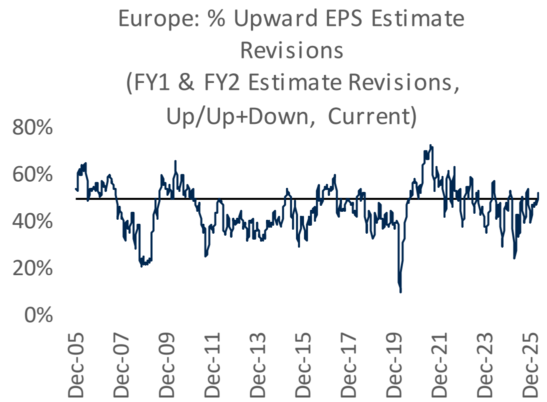
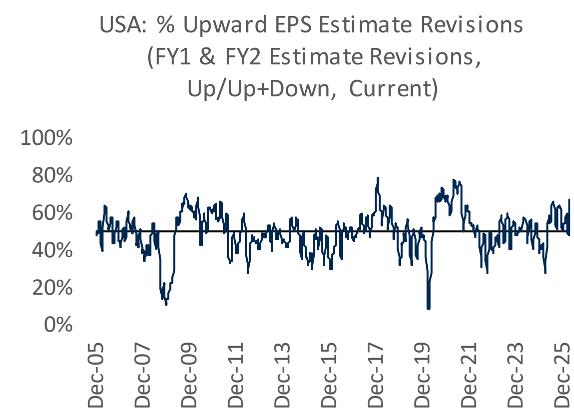
Source: RBC US Equity Strategy, MSCI, S&P Capital IQ Clarifi; as of May 12, 2026; please see the MSCI disclaimer at the end of this report; regions/countries based on MSCI constituents

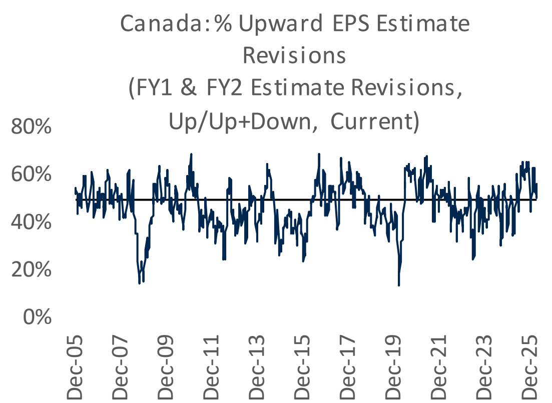
EPS Revisions Trends Are Mixed For the Biggest Developed Markets Countries & Regions

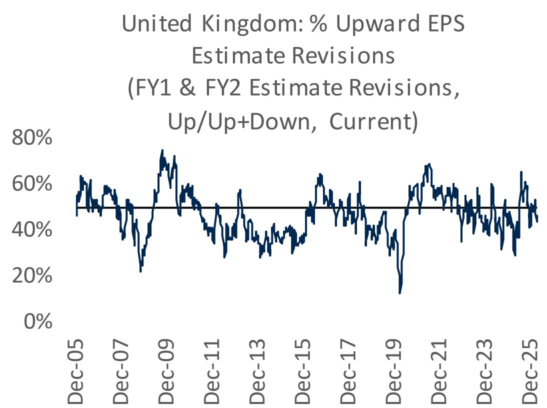
- Australia, the UK, Japan, and Canada are seeing downtrends, while Europe and USA are seeing improving trends – though Europe still looks weak overall.

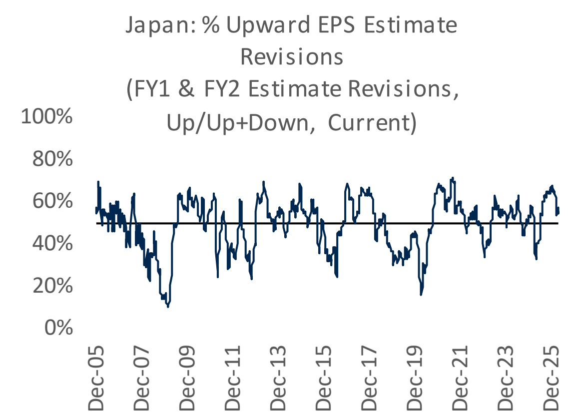












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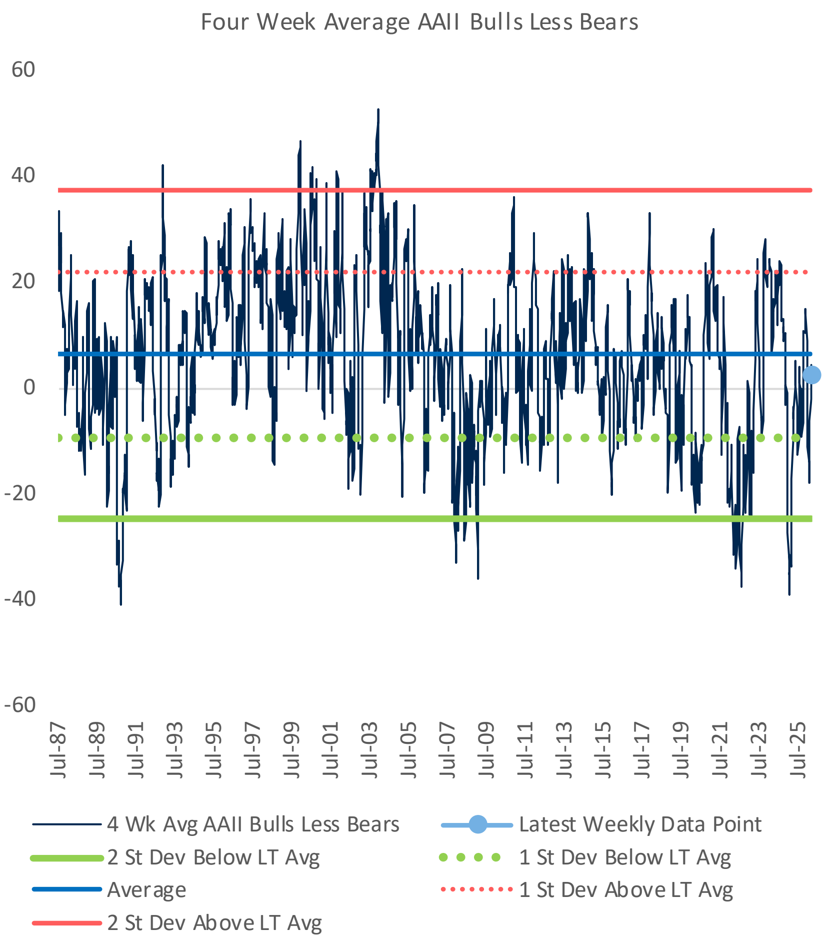
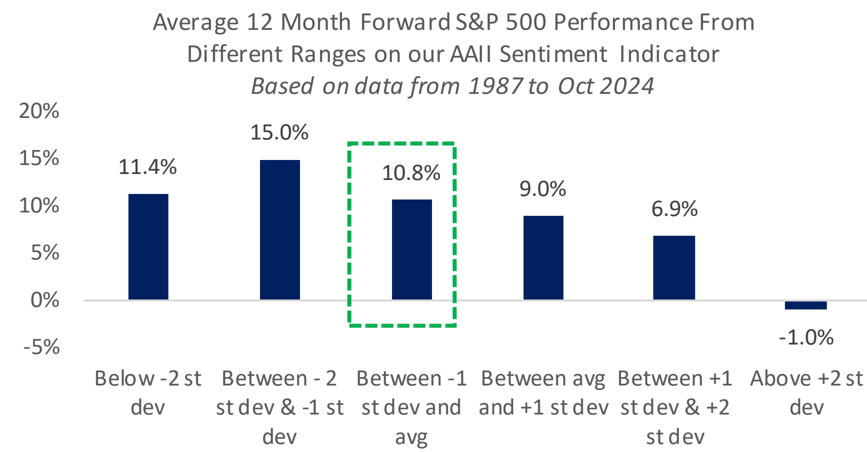
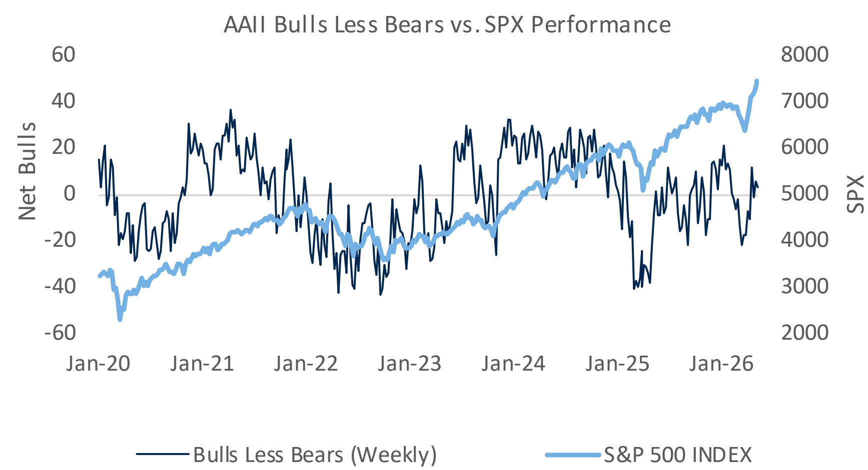
Source: RBC US Equity Strategy, MSCI, S&P Capital IQ Clarifi; as of May 12, 2026; please see the MSCI disclaimer at the end of this report; regions/countries based on MSCI constituents

Our Main Sentiment Model Points to a Gain of 10.8% Over the Next 12 Months

- As of 5/14/26, net bulls were at 2.7% on the weekly update (a deterioration vs. the prior week's 5.3%) and 4.5% on the four-week average (up vs. 1.05% the prior week).
- The four-week average is between average and one standard deviation below the long-term average, a level that has, on average, been followed by a gain of 10.8% in the S&P 500 on a 12-month-forward basis.
- Net bulls on the weekly data point hit an absolute low on 9/22/2022 (-43.2%) and on 2/27/2025 (-41.2%), but only fell to -21.6% in March 2026. The recent drop in sentiment to more than one standard deviation below average was consistent with what we'd expect in a tier 1 / garden variety (5-10%) S&P 500 drawdown. But if risk of a deeper drawdown (tier 2 or 3) emerges, those deeper lows of 2022 and 2025 are good reference points for how negative sentiment could turn.







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Source: RBC US Equity Strategy, Bloomberg, AAII, S&P; updated May 14, 2026

Current Assumptions and Stress Tests from Our Valuation / EPS Model

- This model is based on regression analysis using data going back to 1962. We use quarterly data series for CPI (yr/yr, 3-month average), Fed funds (the effective date, then the upper bound of the announced rate when available), and 10-year yields along with the trailing average S&P 500 P/E multiple. We have excluded the 2010s (the decade between the GFC and COVID) from our regression analysis, as the historical, inverse relationships between the macro variables and the P/E either reversed or eroded during that decade.
- In our S&P 500 price target process, we normally use a projected P/E that is generated by this model using consensus macro forecasts for CPI, the Fed, and 10-year yields with a reference period of four quarters from now as opposed to a static year-end level, along with the bottom-up consensus EPS forecast for the next four quarters. As of our April-2026 update, the reference point for all assumptions were changed to 1Q27 from 4Q26.
- In order to inject some conservatism into our S&P 500 price target modeling, we are, for now, utilizing an EPS assumption for 1Q27 (trailing 4Q basis, as of 5/4/26, after the busiest week of reporting season) that haircuts the consensus estimate by 5%, to roughly $329 (a slightly higher dollar value level than our last update in early April of $322), representing 12% growth yr/yr. This assumption is based on the idea that non-AI related earnings see only mid-single-digit growth yr/yr and come in 7.5% below the early-May consensus, while the AI-related consensus forecast ends up being correct). We are also leveraging macro assumptions in our P/E calculation that are more conservative than the consensus. On the P/E, we are bringing in 3.3% CPI (in line with a stress test for $100 oil that RBC's Economics team published after the war began), a flat Fed (no cuts or hikes), and 10-year yields of 4.5% (not quite the 5% threshold that equity investors tend to worry about, but a bit higher than where we are today). This math points to fair value for the S&P 500 for 1Q27 of 7,929. Note this version of our model has the P/E contracting to a little above 24x, down from the 26-28x levels that have been in place in recent quarters.

Scenarios and Stress Tests For 1Q27

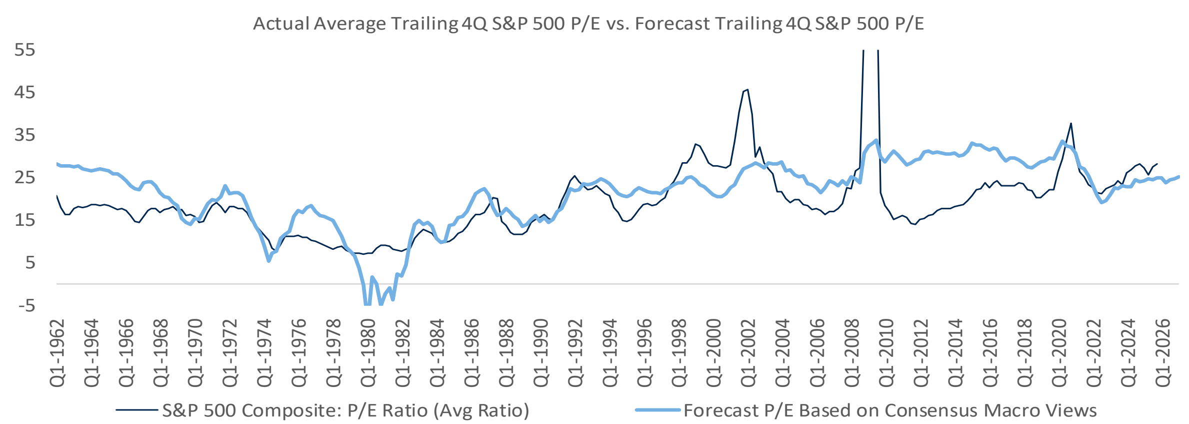
			Macro Assumptions		*Implied P/E*	*1Q27 T4Q EPS Assumptions*					
		CPI	**Fed Funds**	**10 Year Yield**	**Using Model**	**Bottom - Up Consensus**	**5% Haircut to Consensus**	**10% Haircut to Consensus**	**5% Gain vs. 1Q26**	**Flat vs. 1Q26**	**5% Drop vs. 1Q26**
		Y/Y, 3 Mo Avg	*Upper Bound / Qtr End*	*Quarter End*		*$346*	*$329*	*$312*	*$308*	*$293*	*$279*
Consensus Macro	*Used in model*	2.9	3.37	4.16	25.17	8,713	8,278	7,842	7,751	7,382	7,013
RBC Rates/Econ Inputs	*As of mid May 2026 monthly forecast update*	2.6	3.75	4.45	24.97	8,644	8,212	7,780	7,689	7,323	6,957
Higher Oil Scenario #1	*RBC Econ CPI stress, flat Fed, flat yields*	3.3	3.75	4.50	24.11	8,347	7,929	7,512	7,425	7,071	6,718
Higher Oil Scenario #2	*RBC Econ CPI stress test, cuts, yields lower*	3.3	3.00	4.00	25.14	8,704	8,269	7,833	7,742	7,374	7,005
Higher Oil Scenario #3	*Higher CPI, hikes, much higher yields*	3.8	4.25	5.00	22.71	7,861	7,468	7,075	6,992	6,659	6,326

P/E Test

Reference period for macro assumptions and trailing 4Q EPS is 1Q27; Consensus macro is latest available as of 5/15/2026; EPS consensus is as of 5/4/26; RBC Econ/Rates forecasts are as of 5/14/26 (updated monthly)

How we get to $329 for 1Q27....Net Income Sensitivity Analysis

Dollar Values (Trailing 4Q Basis, $M)	
3,136,157	Consensus for Total S&P 500 Net Income (Unadjusted)
947,770	Consensus for AI Basket
2,188,387	Consensus for Ex AI Basket (Unadjusted)
2,024,258	Adjusted Consensus for Ex AI (1Q27 Est Lowered by 7.5%)
2,972,028	Adjusted Consensus for Total S&P 500 Net Income
Key Percentages - Yr/Yr % Change	
18%	Consensus for Total S&P 500 Net Income
28%	**Consensus for AI Basket**
14%	Consensus for Ex AI Basket (Unadjusted)
6%	**Adjusted Consensus for Ex AI (1Q27 Est Lowered by 7.5%)**
12%	**Adjusted Consensus for Total S&P 500 Net Income**

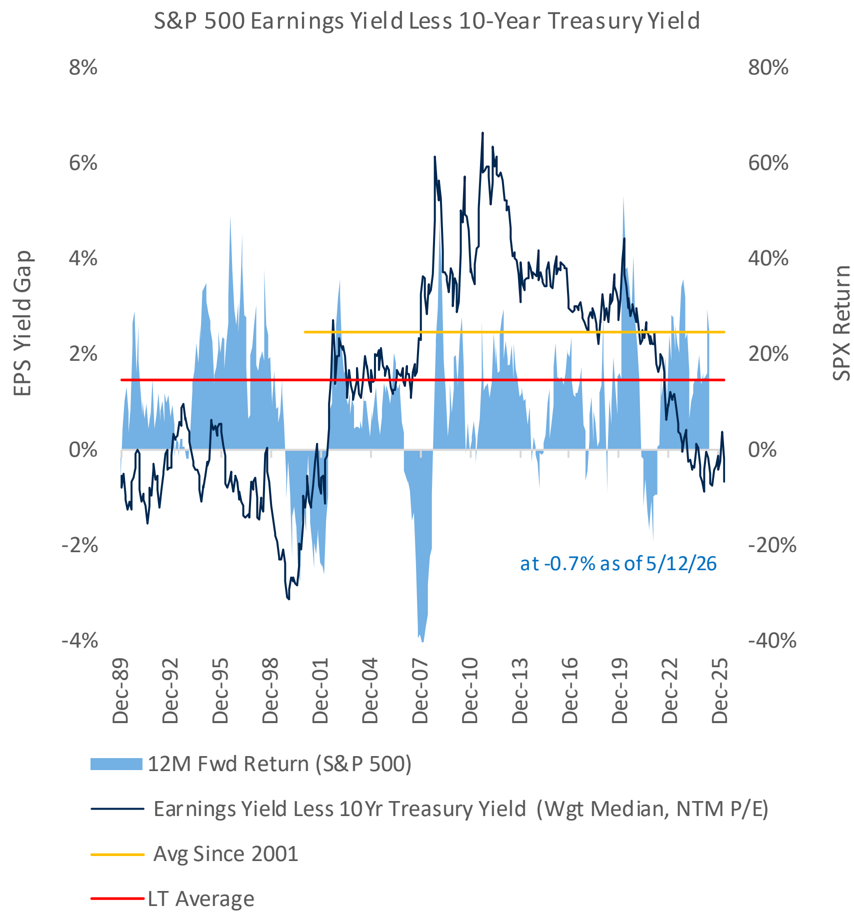


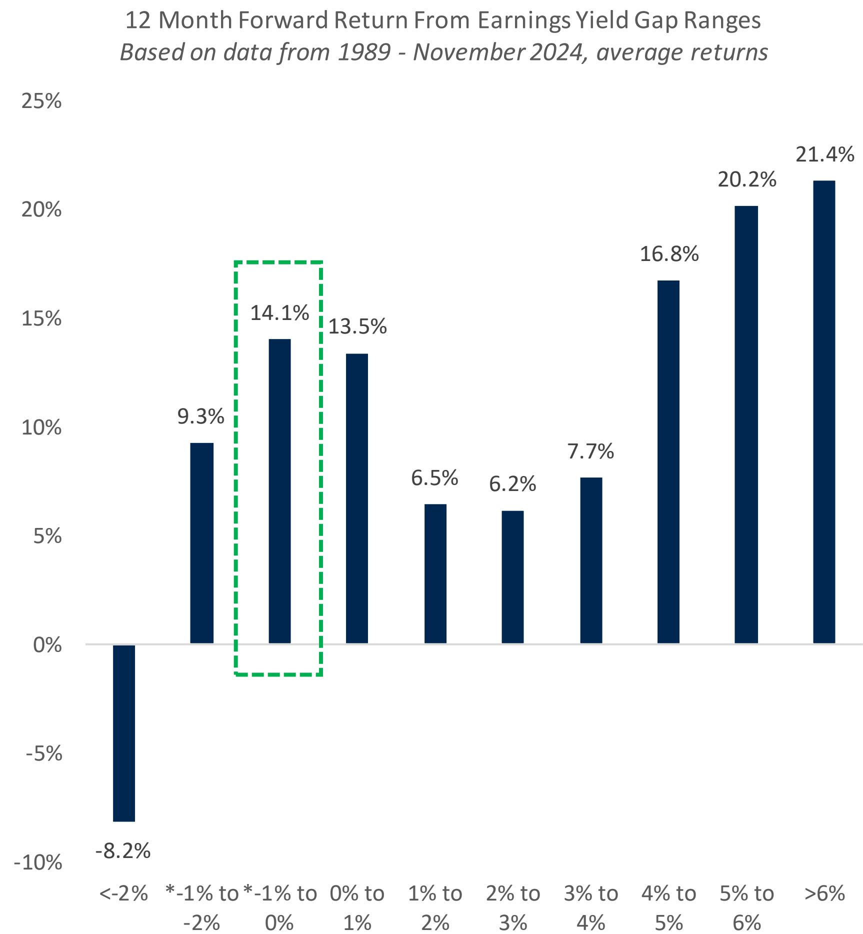
Source: RBC US Equity Strategy, Bloomberg, Haver, S&P

Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors; we do not share the excel version of this model.

Our EPS Yield Gap Analysis Points to Mid-Teens Gains for the S&P 500 in the Next 12 Months

- The gap between the next 12 months' earnings yields in the S&P 500 and the 10-year Treasury yield is now slightly negative, and within a range that has been followed by strong gains in the S&P 500 in the past.





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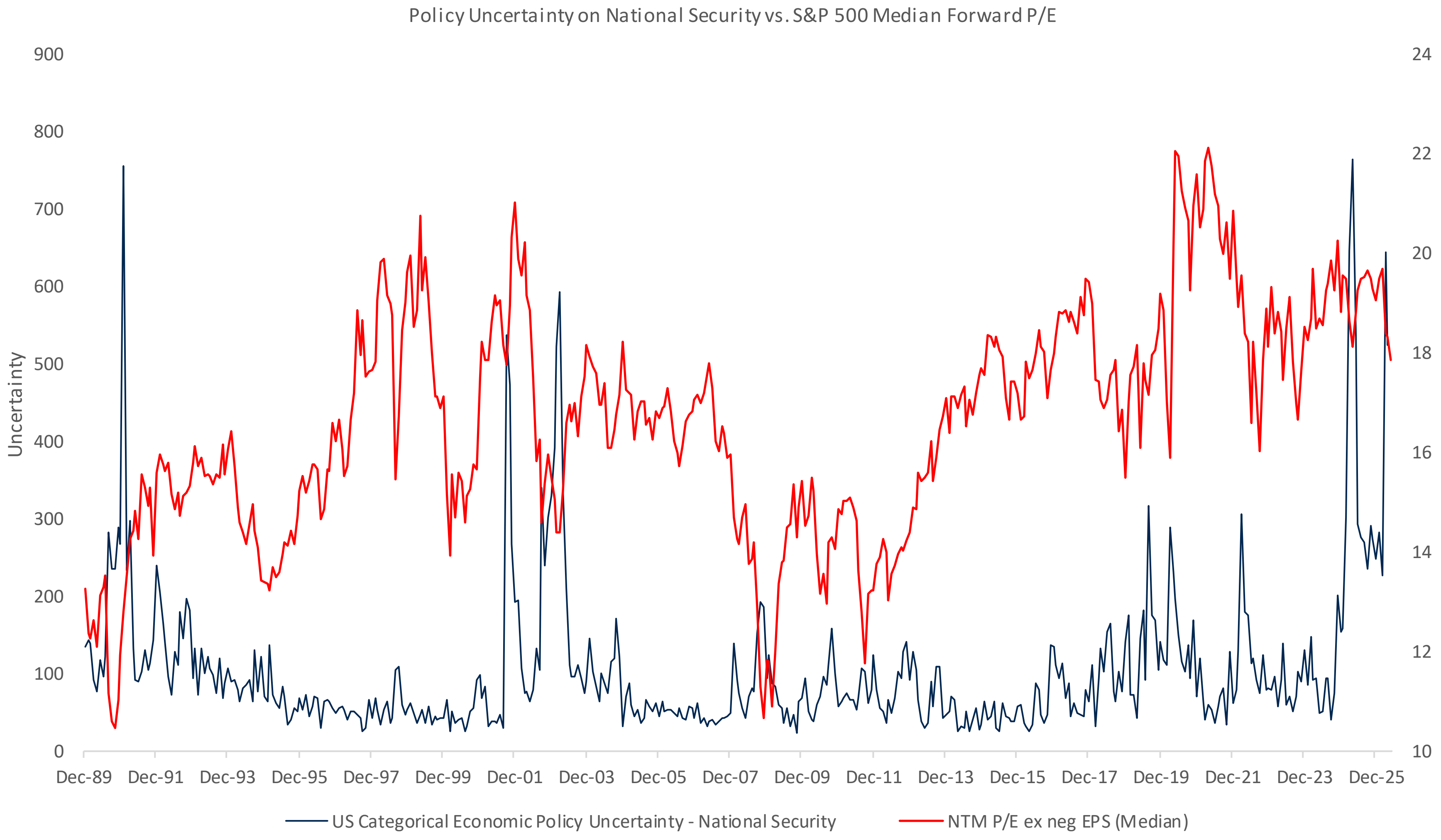
Source: RBC US Equity Strategy, Haver, Bloomberg, S&P; May 12, 2026.

Foreign Policy Uncertainty Tends to Weigh on P/Es

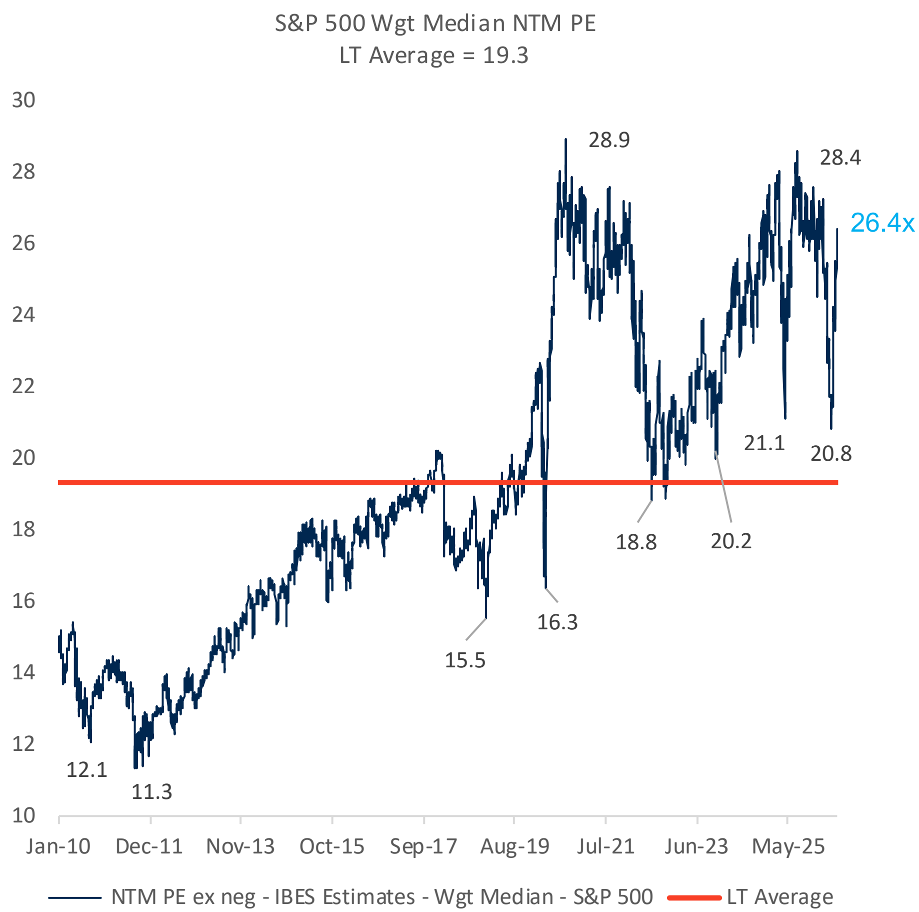
- Whenever geopolitical uncertainty spikes, the first thing that usually jumps into our mind is that forward P/E multiples tend to come under pressure for the S&P 500. This speaks to one of the transmission mechanisms of geopolitical conflicts and risks to equities.
- In recent years we've seen some deterioration in S&P 500 median P/Es when uncertainty regarding national security spiked in spring 2025 (Liberation Day tariffs), 1Q22 (Russia's invasion of Ukraine), and 1Q20 (COVID). This is something we also saw in early 2003 as the US was preparing to invade Iraq.

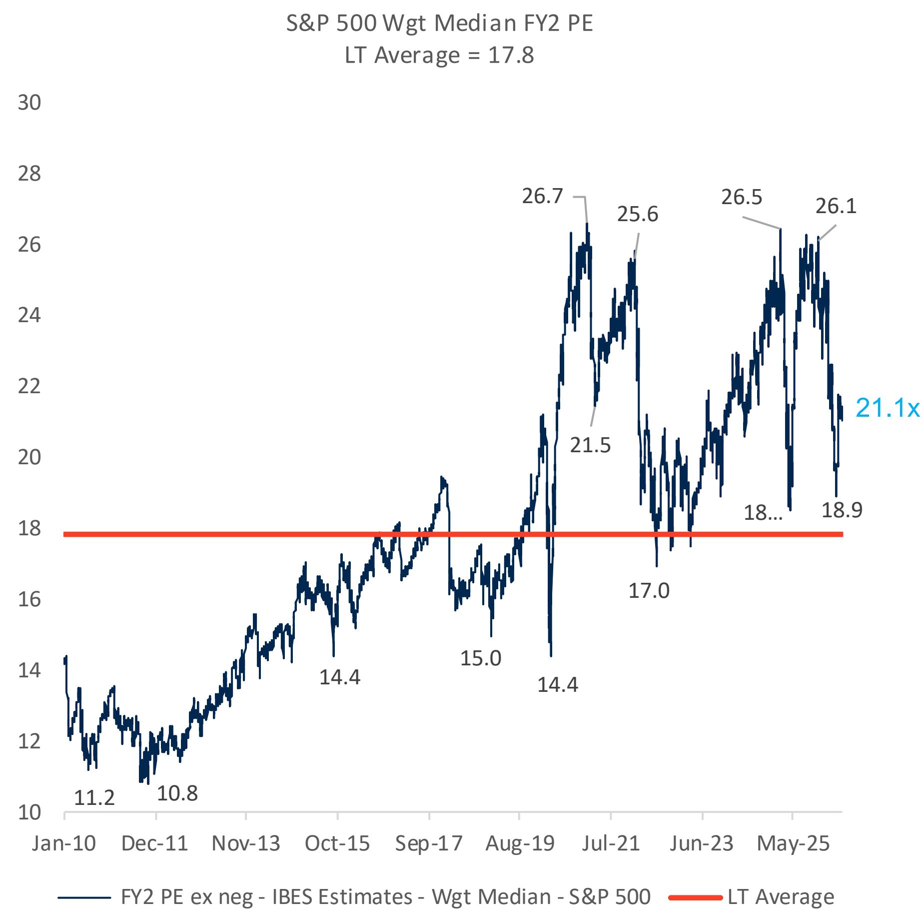


Source: Bloomberg, Baker Davis & Bloom, S&P Capital IQ Clarifi, May 12, 2026

S&P 500 Forward P/E's Are Rebounding, Closing In On Past Highs on NTM but Not FY2

- Large Cap valuations corrected earlier this year as investors worked through AI concerns, private credit stress, and geopolitical uncertainty.
- The S&P 500 avoided a full washout to 2025 lows, in our view, as both NTM and FY2 P/E multiples failed to break materially below long-term averages or reclaim the prior 2018-2023 trough range. They did hit 2025 lows.
- We believe excess froth was removed from Large Caps, creating room for multiples to recover once the macro and geopolitical backdrop got less negative. However, we disagree with those who argue that valuations became a reason to buy the market on their own. We simply didn't see washout conditions on either metric for this index.





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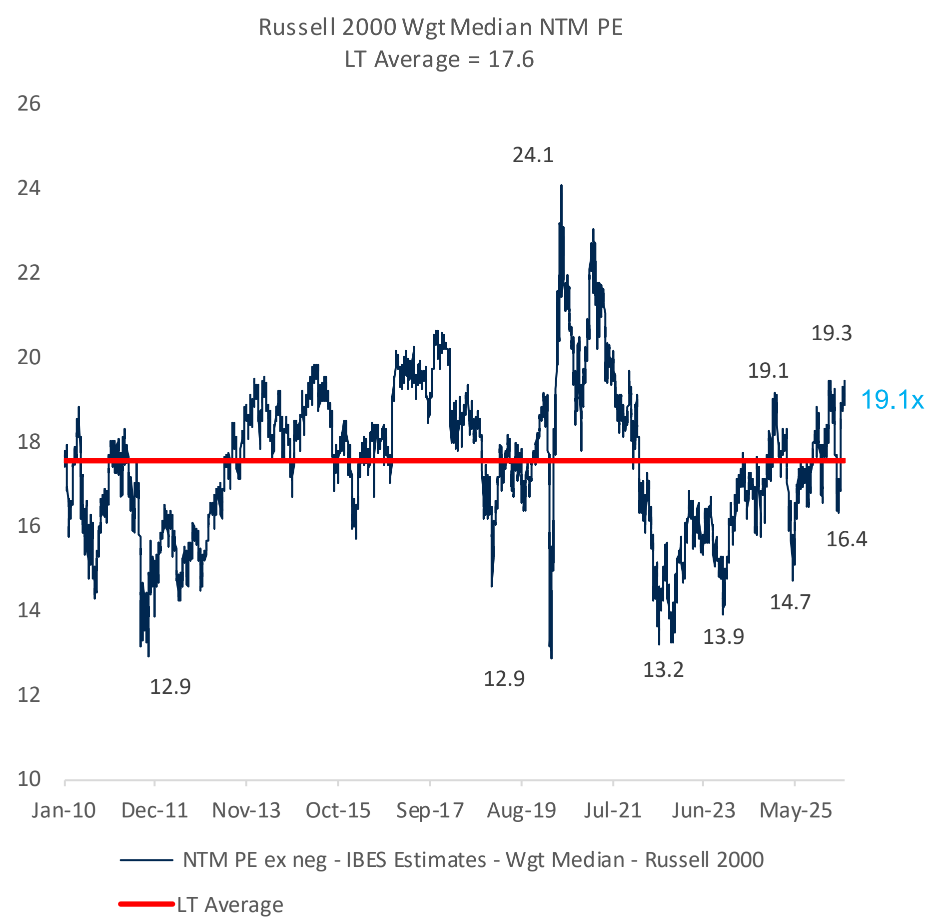
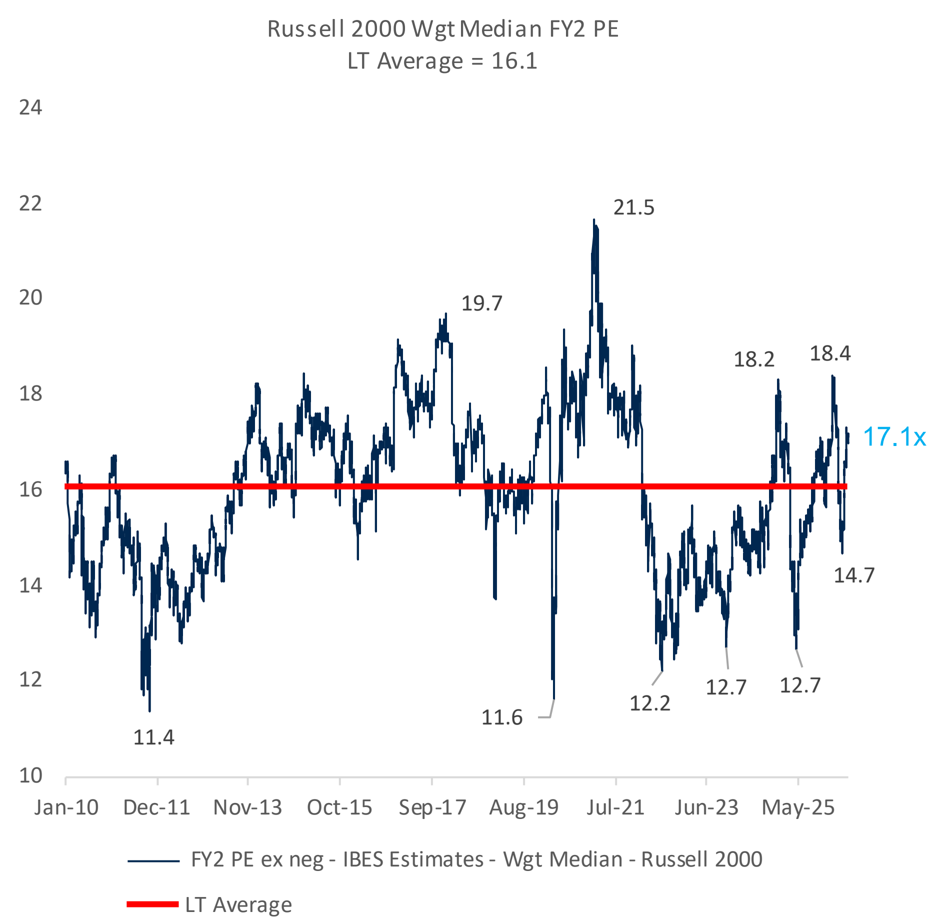
Source: RBC US Equity Strategy, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of May 12, 2026.

Russell 2000 Forward P/E's Are Rebounding, Also Closing In On Past Highs on NTM but Not FY2

- Small Cap valuations also corrected earlier this year amid AI, private credit, and geopolitical concerns.
- With Small Caps, we focus mostly on FY2 P/E. On that metric, the Russell 2000 broke slightly below its long-term average, but failed to reach the recession zone of 11-13x, which it achieved during the lows of COVID, 2022, 2023, and 2025. Note we're still trading well below the last two peaks on this metric pointing to some room for Small Caps and US equities broadly to run. Valuations are admittedly close to the most recent highs on an NTM basis, but that metric has been less helpful as a bottom indicator.
- Similar to our thinking on Large Caps, we think recent multiple compression removed the froth from Small Caps, but valuations did not reach levels that historically signaled a major washout opportunity.





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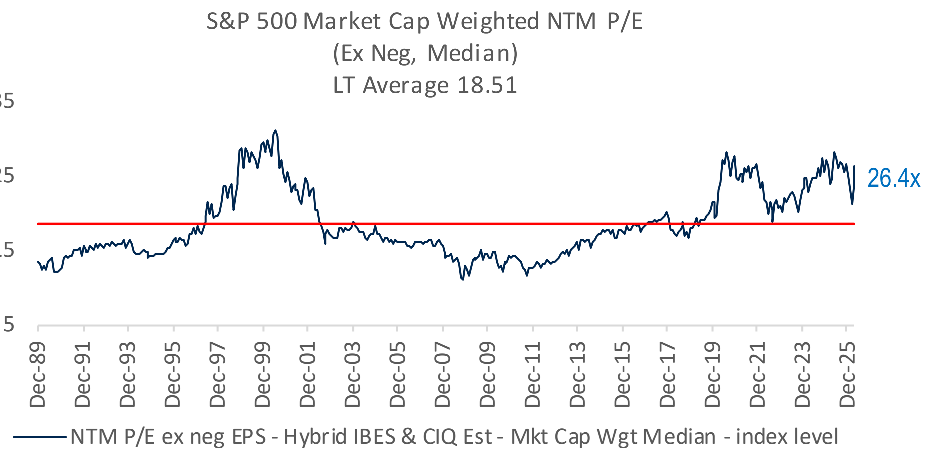
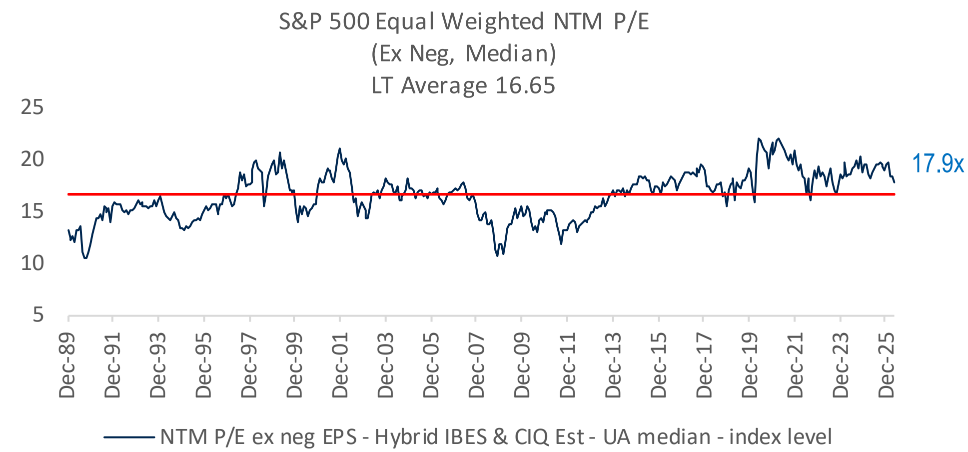
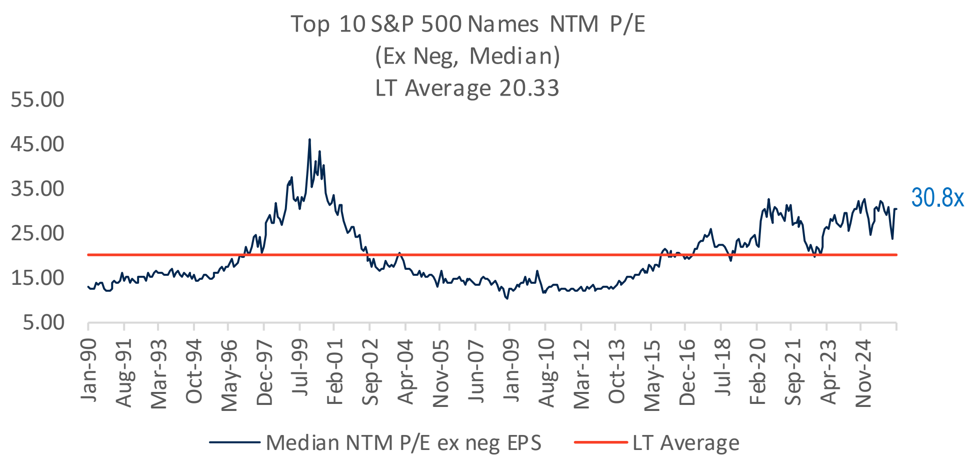
Source: RBC US Equity Strategy, Russell, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of May 12, 2026.

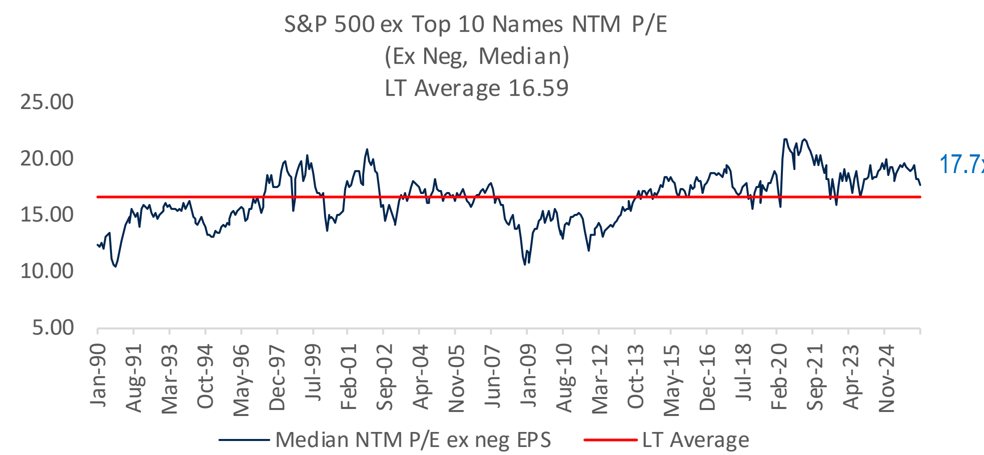
Forward P/Es Stalled Near Their Pre- and Post-COVID Era Ceilings Throughout the S&P 500

- When we look at NTM P/Es on bottom-up consensus EPS forecasts, we find that valuations were coming under pressure in the S&P 500 generally ahead of the war – whether we're focusing on the overall index, the top-10 market cap names, the index excluding those names, and looking at the data on an equal-weighted or market cap-weighted basis.
- On this methodology, the broader index on a cap-weighted basis and the top-10 names bumped up against their pre- and post-COVID ceiling last year. In the equal-weighted S&P 500 and the index excluding the top market-cap names, the NTM P/E stalled near its post-COVID high but not its pre-COVID high.
- We saw more noteworthy slippage in the market cap-weighted P/E in part due to compression in the P/Es of a handful of the biggest market cap names.









Note: Mid-week basket portfolio rebalancing applied for the Top 10 and S&P ex Top 10 baskets; as of May 12, 2026.
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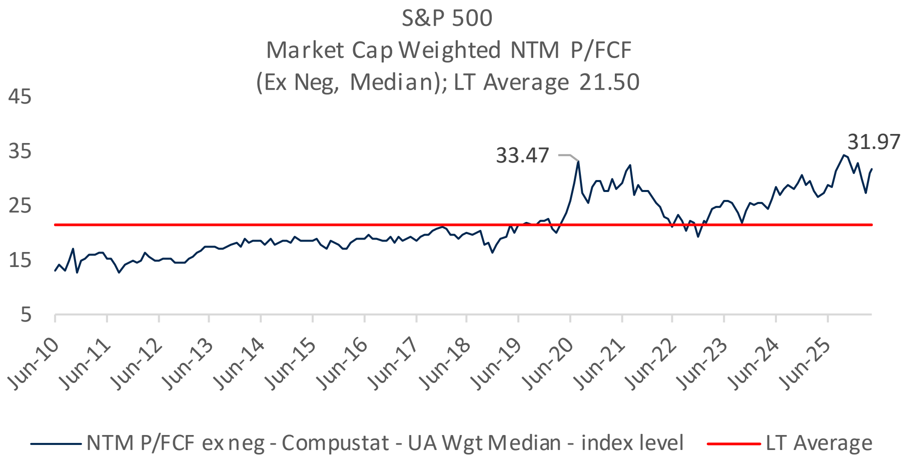
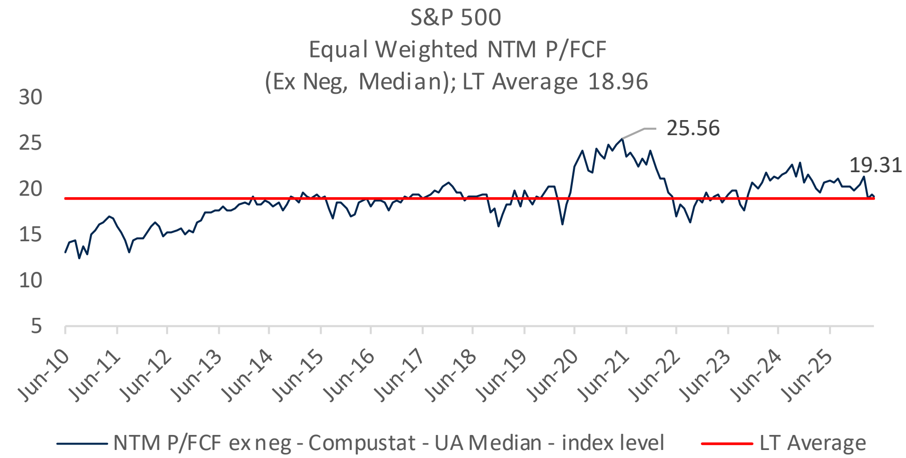
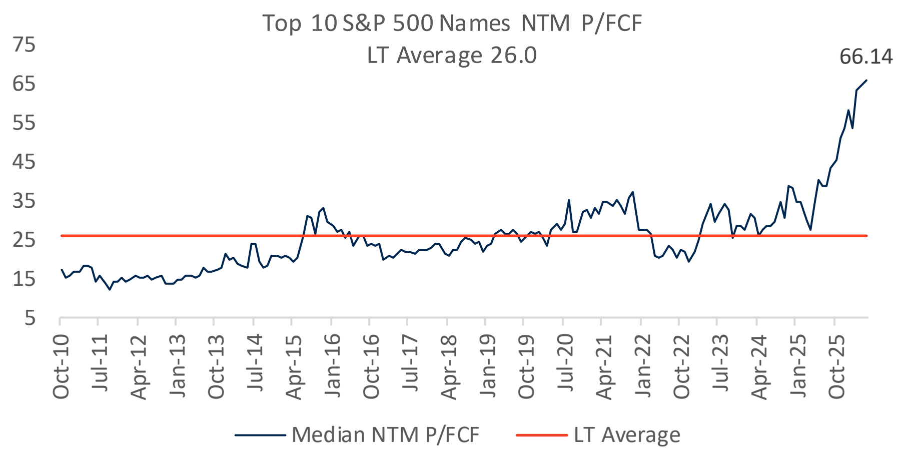
Source: RBC US Equity Strategy, S&P, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of May 12, 2026.

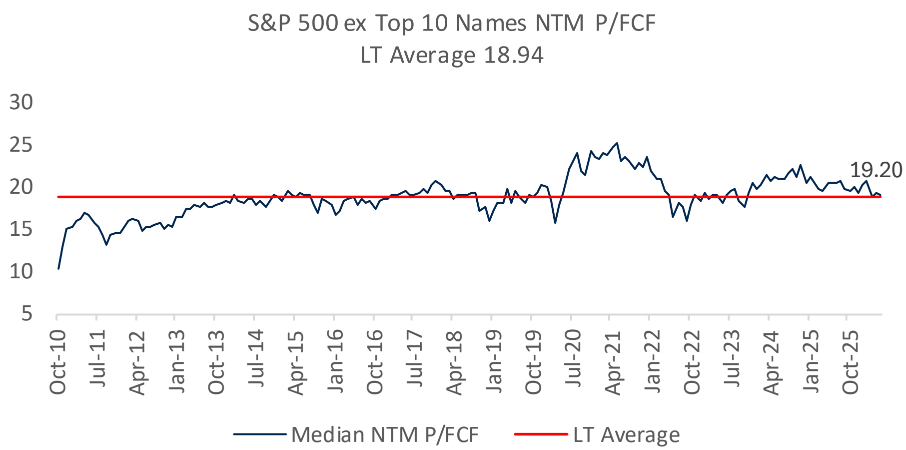
The S&P 500 Has Returned to Past Peaks on Projected Cash Flow, Driven by Mega Cap Growth Stocks

- The last major peak on this metric for the S&P 500 was achieved in mid-2021 – the index would go on to rally through the end of the year, peaking in early-January 2022.
- The problematic cash flow multiple is something that very much seems to be concentrated in the mega cap growth complex. This multiple is well below recent and prior peaks for the equal-weighted S&P 500 and the index excluding the top-10 market cap names.









Note: Mid-week basket portfolio rebalancing applied for the Top 10 and S&P ex Top 10 baskets; as of May 12, 2026.
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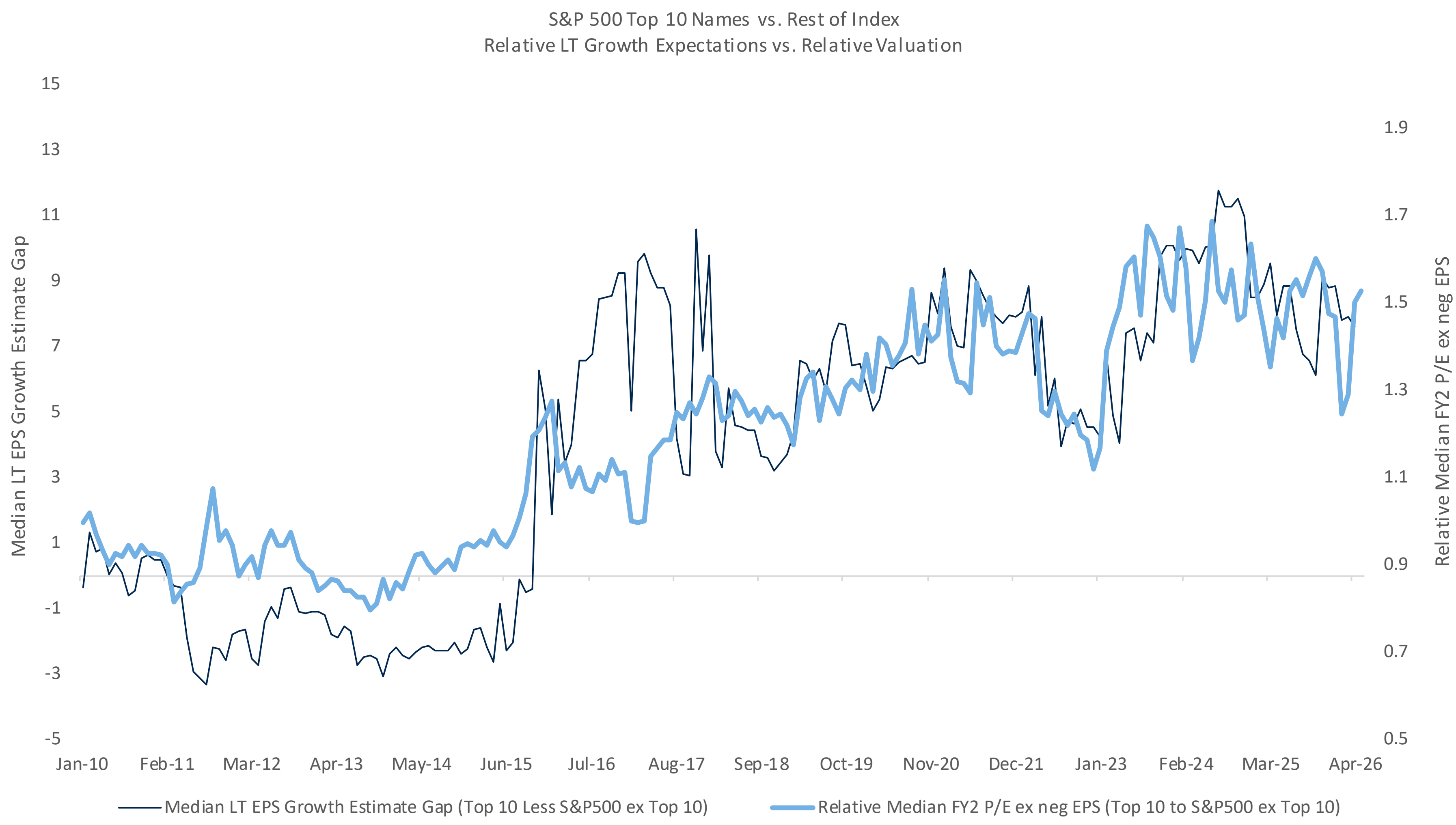
Source: RBC US Equity Strategy, S&P, S&P Capital IQ / ClariFI, Compustat, CIQ estimates, IBES estimates; as of May 12, 2026.

Relative Valuations of Top-10 S&P 500 Names Usually Track Relative LT EPS Growth

In the chart below, we look at the biggest market cap names against the rest of the S&P 500 on relative P/E and relative LT EPS growth. Generally, these two lines have been tracking one another. Last year, a gap opened up, suggesting the mega cap growth trade was a bit ahead of itself. In the most recent updates, the gap has disappeared – indicating that the mega cap growth trade does not look undervalued anymore from this perspective.



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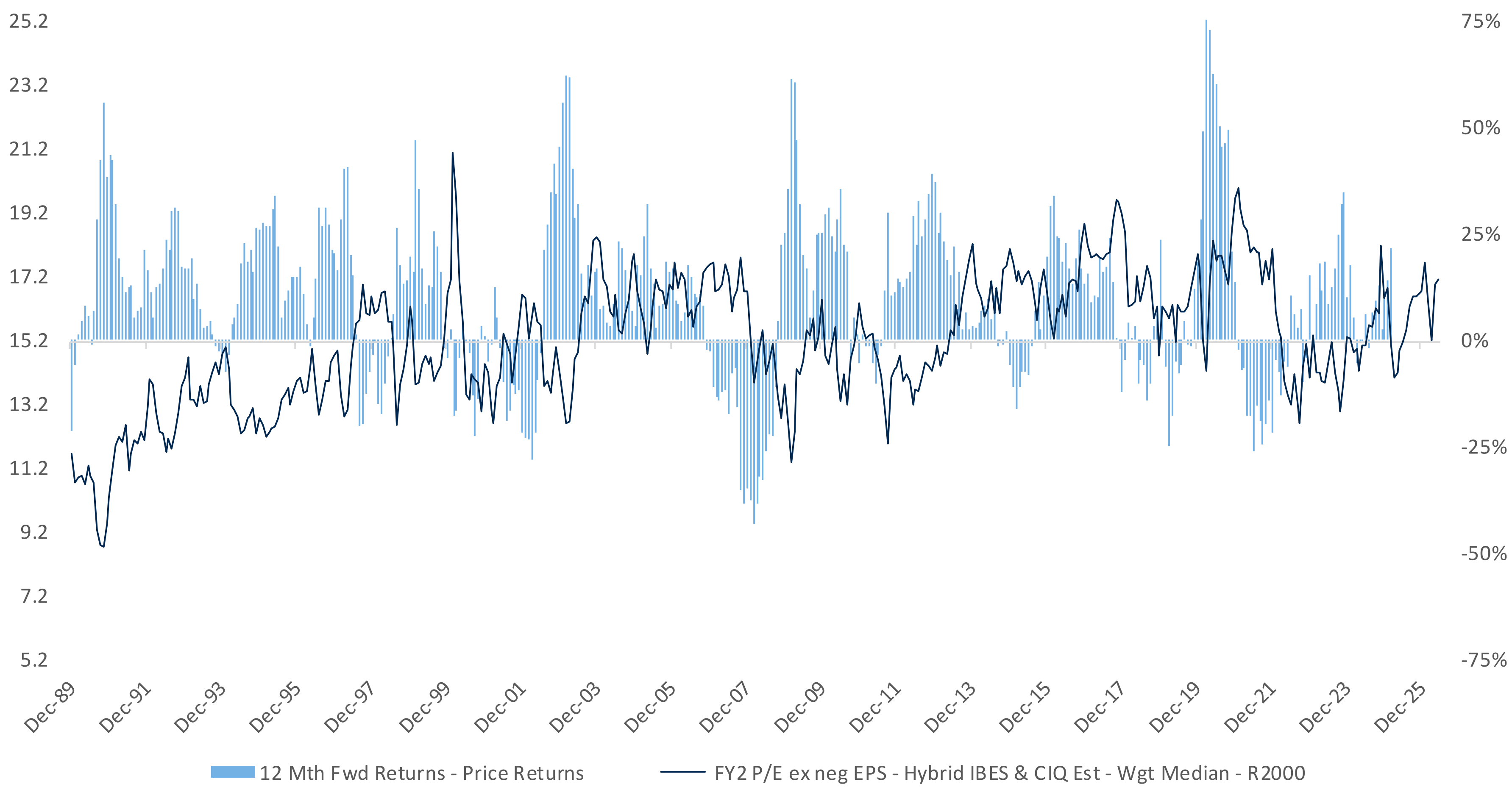
Source: RBC US Equity Strategy, S&P, S&P Capital IQ/ClariFi, CIQ estimates, IBES estimates, as of May 12, 2026. Mid-month basket portfolio rebalancing applied.

The Russell 2000 FY2 P/E Is Back Above Its Long-Term Average, but Not Yet Recent Highs

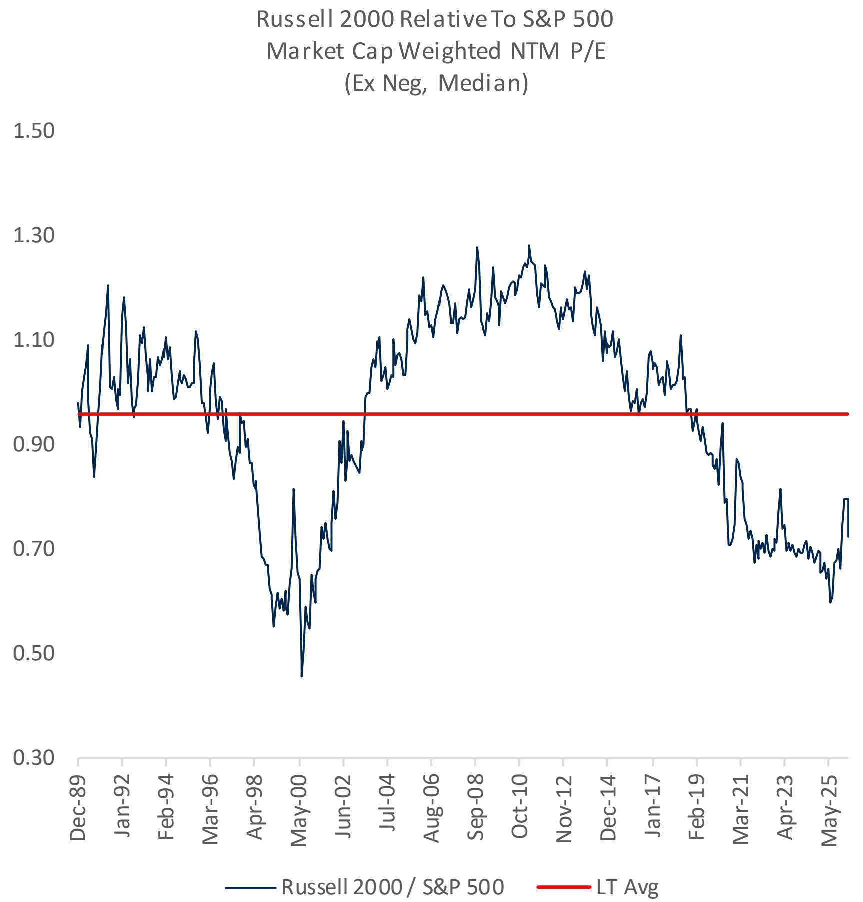
- The Russell 2000 forward P/E hit 12.65x when the stock market hit its YTD low in early April. That was a significant milestone, as this indicator often bottoms in the 11-13x range. That level was also in line with its 2022 and 2023 lows.
- At January month-end, this stat was 17.5x, close to the November-2024 high of 18.1x. On an intramonth basis, this metric got even closer to the November-2024 level.
- As of mid-May 2026, this metric is 17.11x – above its long-term average of 15.18x (it briefly dipped below it in March). A return to the November-2024 and January-2026 highs will be an important test for the market. A return to even higher levels is possible based on history, but it's worth noting that the index failed to break out earlier this year.

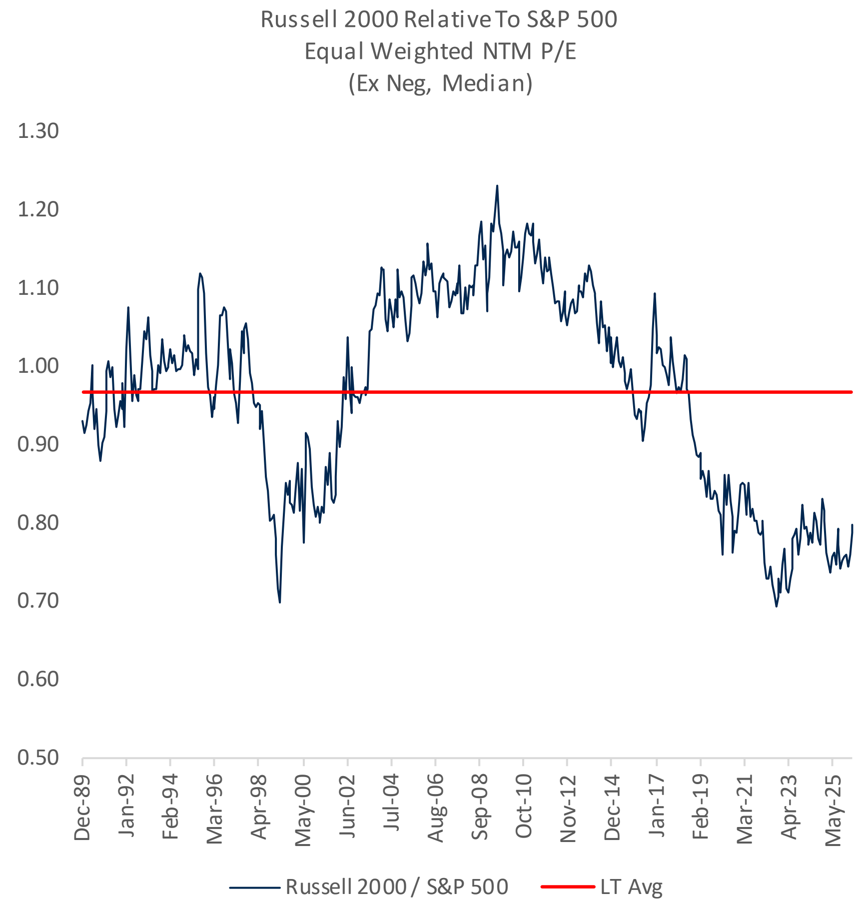
R2000 FY2 P/E ex neg EPS (Wgt Median) vs. 12 Month Fwd Russell 2000 Performance



Source: RBC US Equity Strategy, Russell, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of May 12, 2026

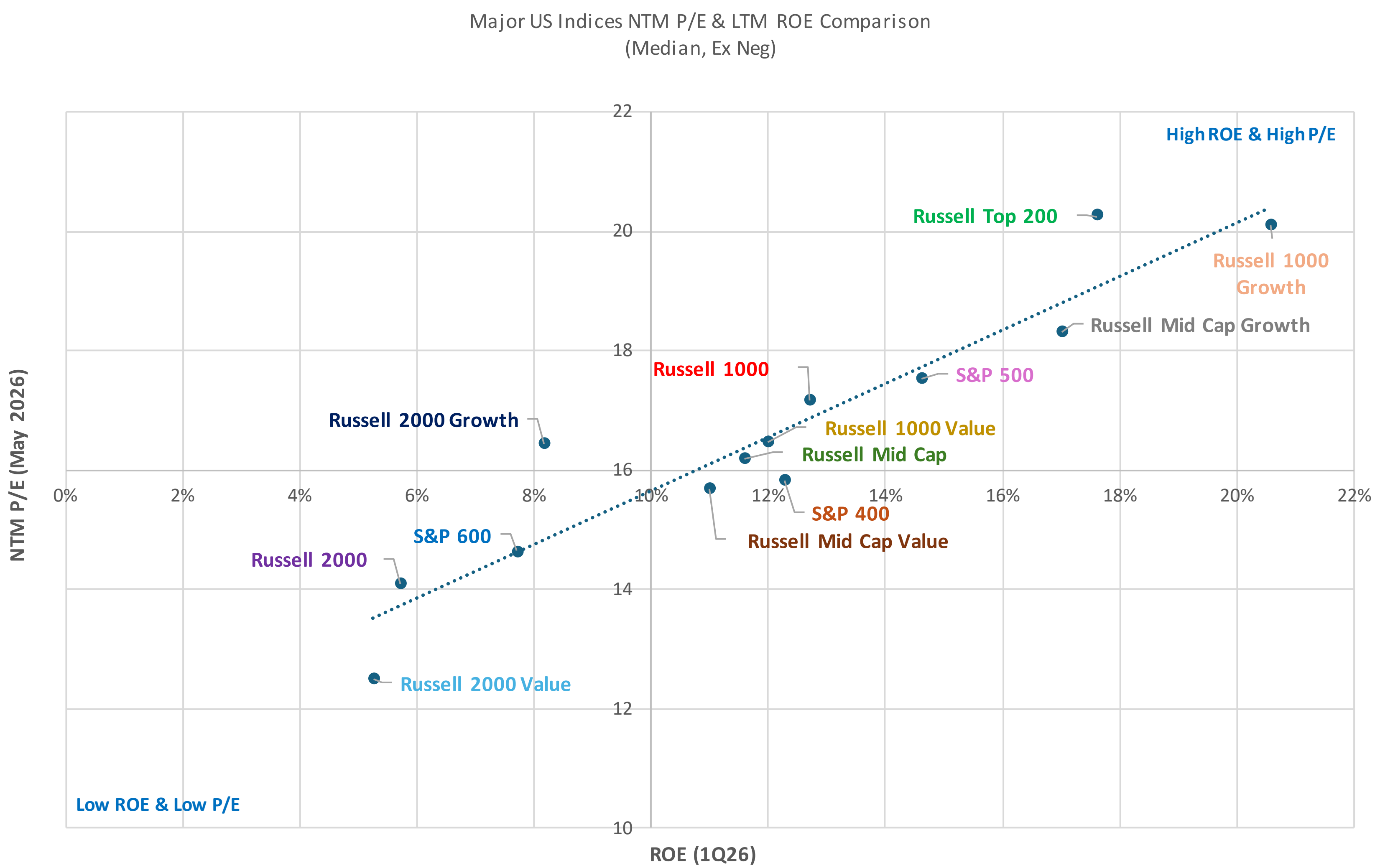
Russell 2000 Remains Undervalued vs. S&P 500 on NTM P/E





Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P, Russell, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of May 12, 2026.

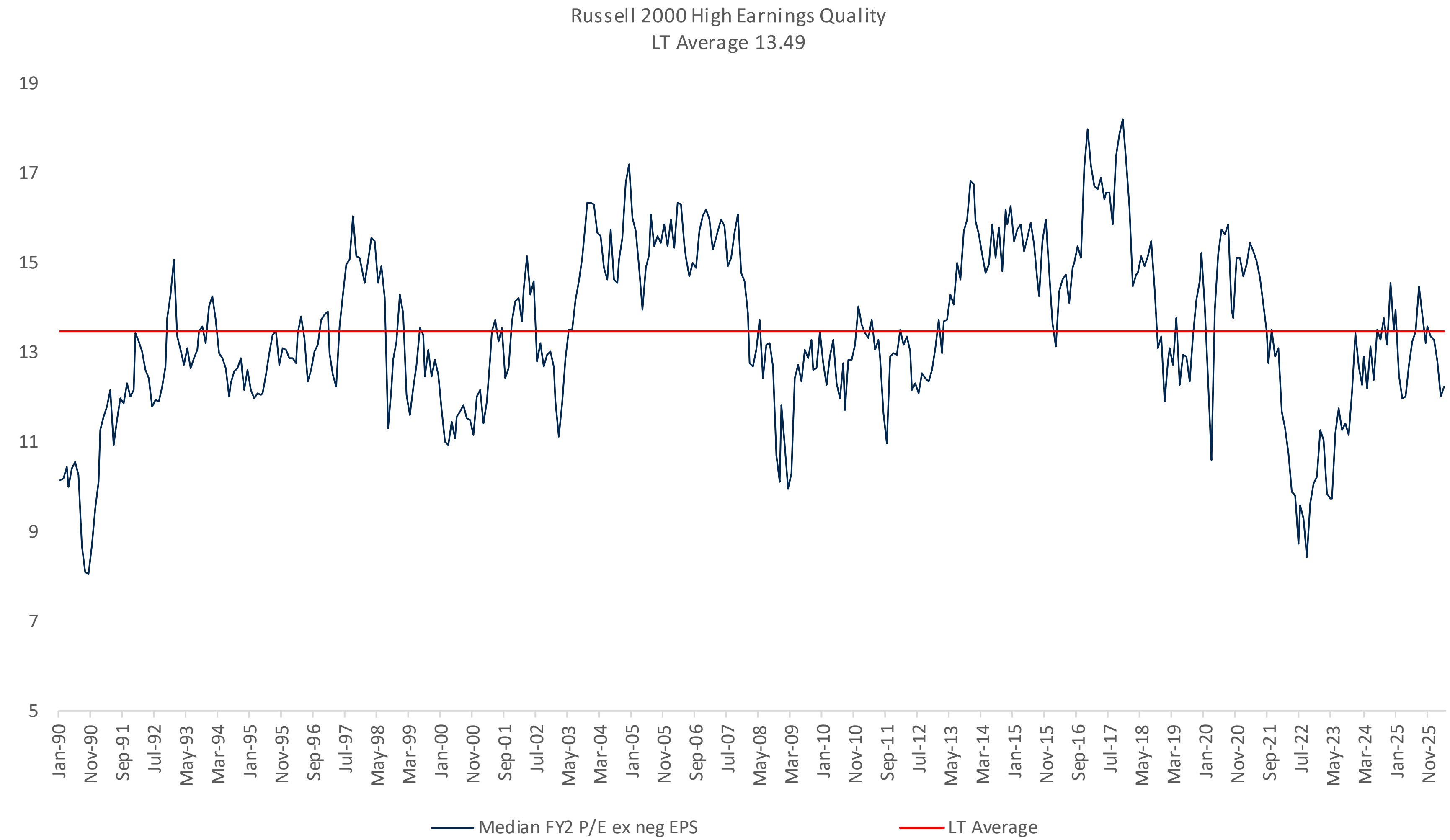
The Russell 2000's Lower P/E vs. the S&P 500 Reflects Its Lower ROE



Source: RBC US Equity Strategy, Russell, S&P Capital IQ / ClariFI, CIQ estimates, IBES estimates; as of 5/13/2026
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.

High Earnings Quality Trades at a Discount Within Small Cap on Forward P/E

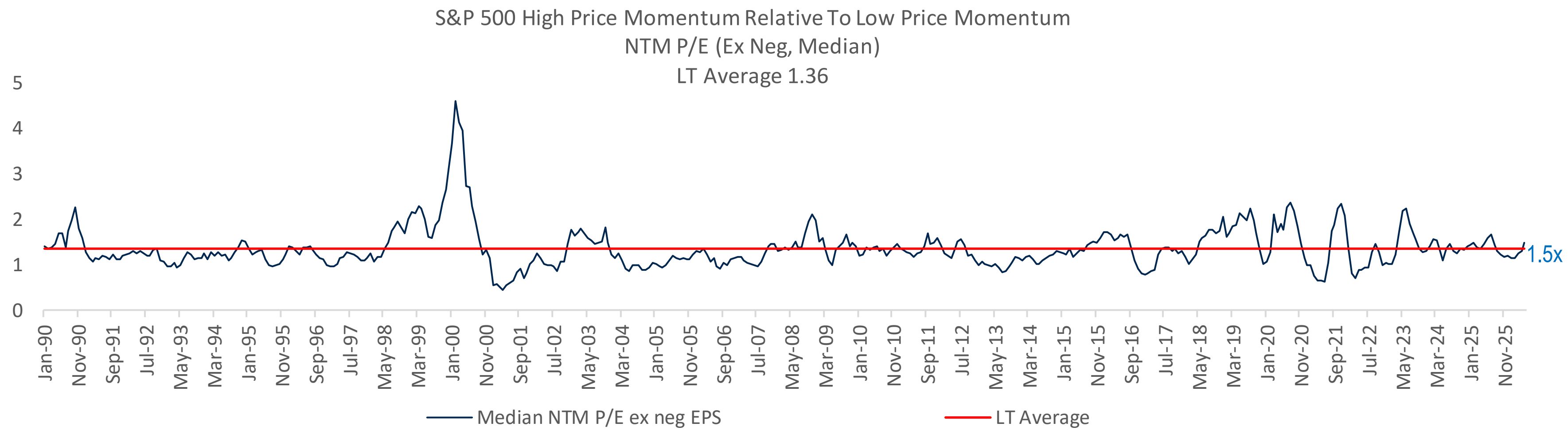
- We examined median valuation multiples for the high-EPS-quality baskets within the Russell 2000. We found that the high-EPS-quality basket's forward P/E is below its historical average, suggesting to us that valuation opportunities do exist within this cohort.

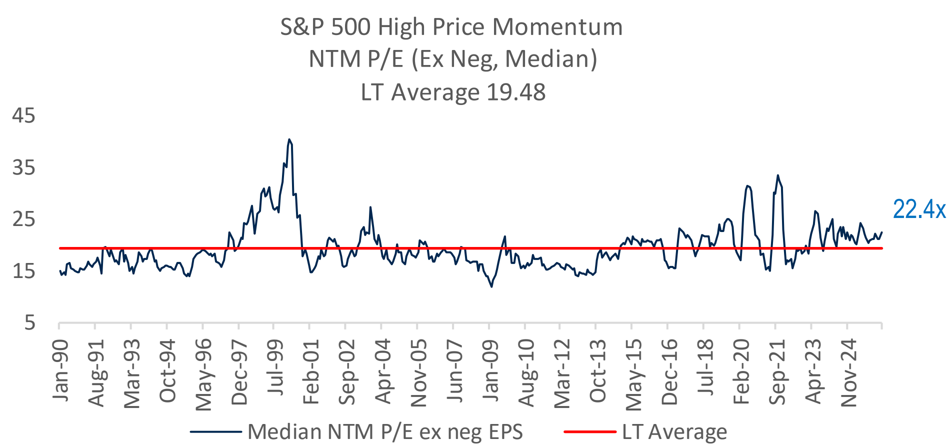


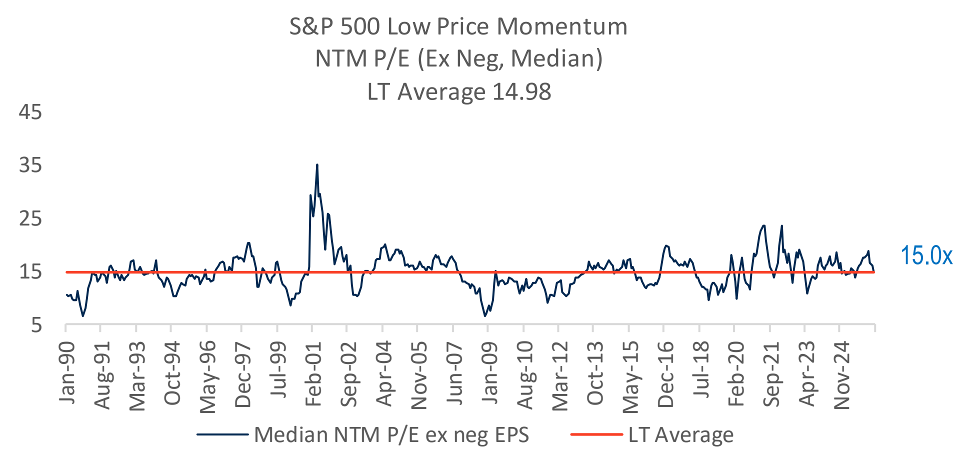
Note: The earnings quality factor is a sector-neutral, equal-weighted multifactor based on historical constituents that combines the trailing 12-month return on equity, earnings stability (measured as the ratio of the one-year change in EPS to the standard deviation of the one-year change in EPS across eight prior periods), and the distinction between positive and negative earnings based on whether EPS is above or below zero.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of May 12, 2026.

High Price Momentum Stocks Look Slightly Overvalued vs. Low Price Momentum Stocks

- High momentum stocks continue to trade at a premium to low momentum peers, with the relative valuation spread sitting slightly above its long-term average. It's worth noting that the relative multiple is well below most prior peaks.
- The high momentum cohort currently trades at 22.4x NTM P/E versus 15.0x for low momentum stocks. While momentum premiums have moderated from prior peaks, leadership valuations are still somewhat elevated versus historical averages. Low momentum valuations remain close to its long-term average, suggesting multiple expansion continues to be concentrated in high price momentum leadership area of the market.



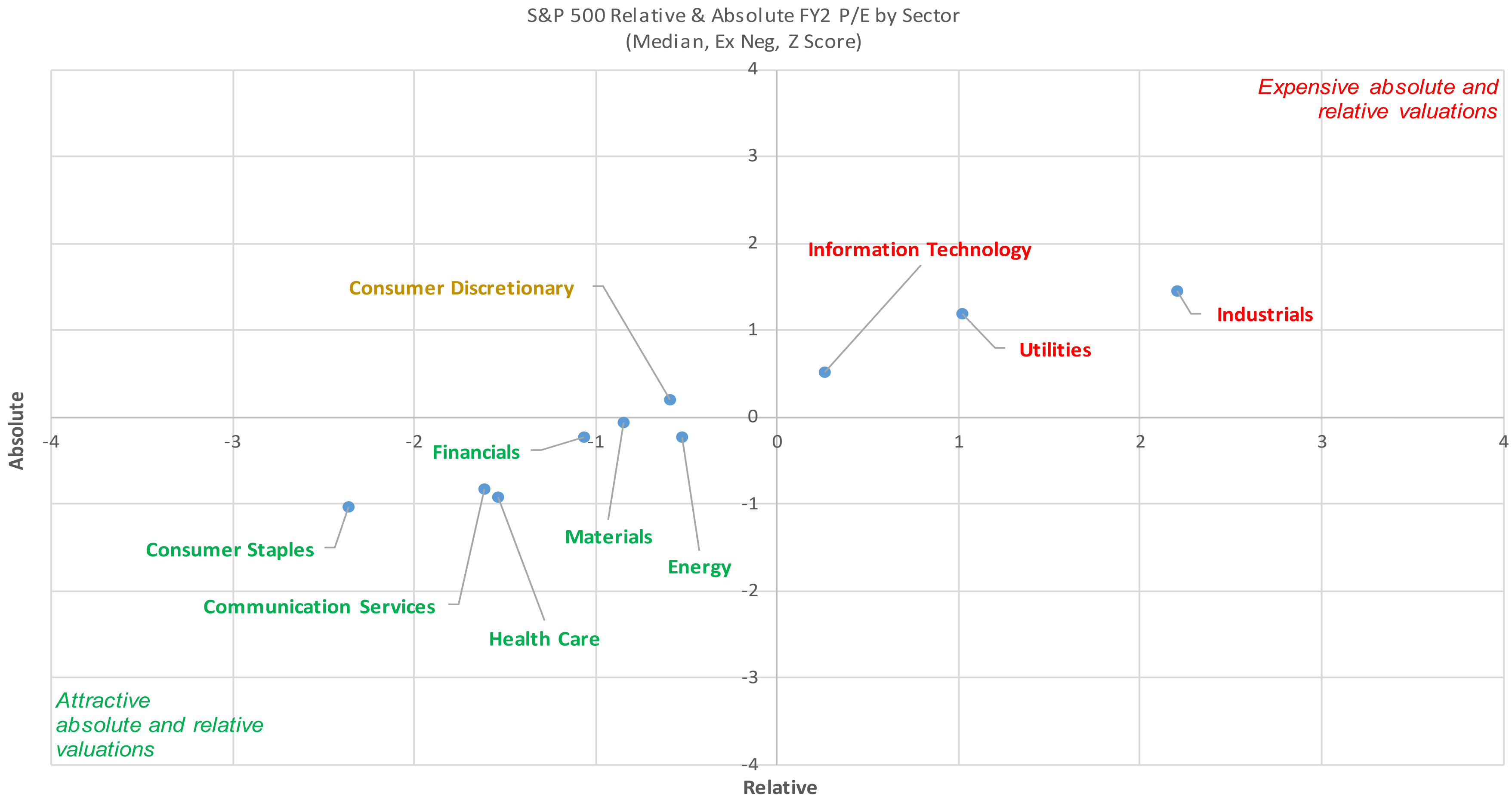




Note: The price momentum factor is a sector-neutral, equal-weighted factor based on historical constituents that measures the strength and the direction of a price movement depending on the direction of the 50-day moving average relative to the 200-day moving average.
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, S&P Capital IQ/ClariFi; Russell, S&P, as of 5/12/2026

Industrials, Utilities, and Tech Look Most Expensive Within Large Cap

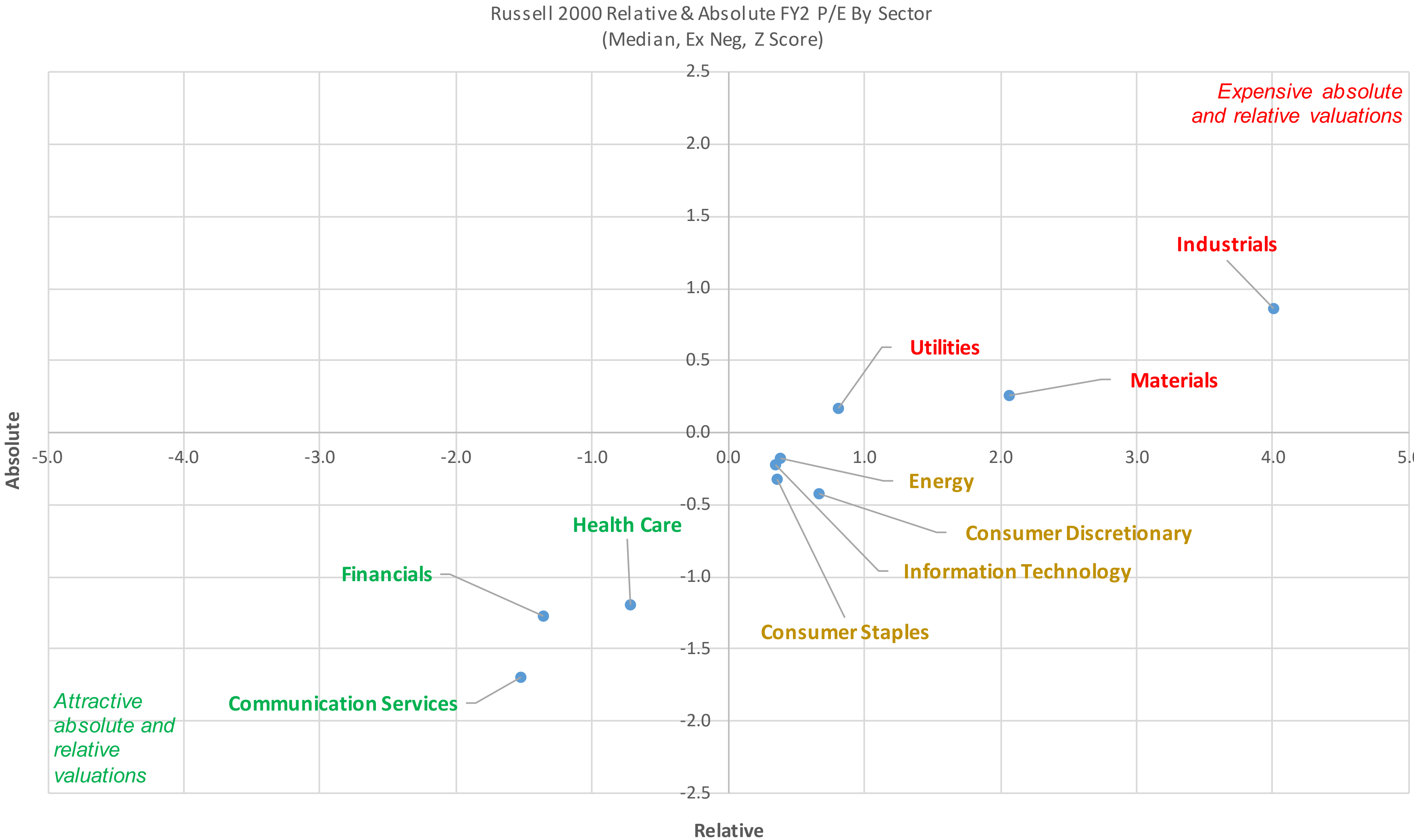
- Consumer Discretionary is slightly above their long-term averages on an absolute P/E, but slightly attractive/close to average on a relative P/E basis.
- Tech is now expensive on both an absolute P/E and relative P/E basis.
- Meanwhile, Energy, Materials, Health Care, Communication Services, Financials, and Consumer Staples look attractively valued on both absolute and relative P/E – more so on relative than absolute.



Note: Excludes REITs; data since December 1989 for all sectors ex REITs; as of May 12, 2026.
Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, S&P

Valuations Look Most Attractive in Comm Svcs, Financials & Health Care Within Small Cap

- The Utilities sector screens expensive on a relative P/E basis and somewhat neutral on an absolute P/E basis. The Industrials sector in the Russell 2000 stands out as the most expensive, especially on a relative P/E basis. Materials is now screening negative on both an absolute and relative P/E basis. Consumer Discretionary, Consumer Staples, Energy, and Info Tech screen attractive on an absolute P/E basis, but expensive on a relative P/E basis. This is a recent development for Energy and Info Tech.

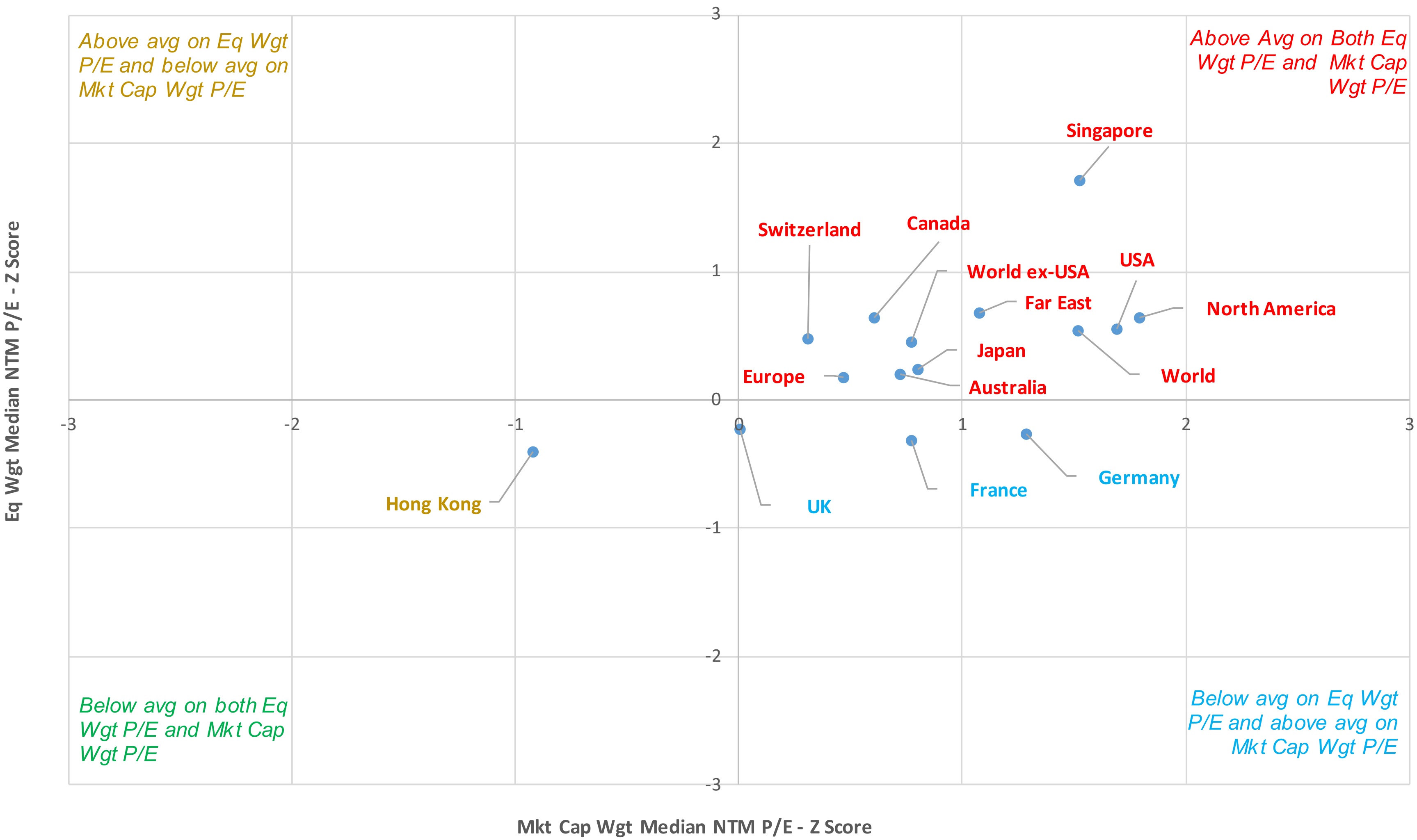


Notes: Excludes REITs; data since December 1989 for all sectors ex REITs; as of May 12, 2026.
Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell

North America Has Been Driving Up Global Developed Market Equity Valuations

- It is no surprise that the US doesn't look cheap. More interesting to us is that Australia and Singapore look similarly or more overvalued than other major developed market countries. That was also true for Canada until recently.
- While World ex USA and Europe don't look cheap, valuations look more reasonable than what we see in North America and the commodity-driven countries. Note within Europe, Germany and France look expensive on a market cap-weighted basis.

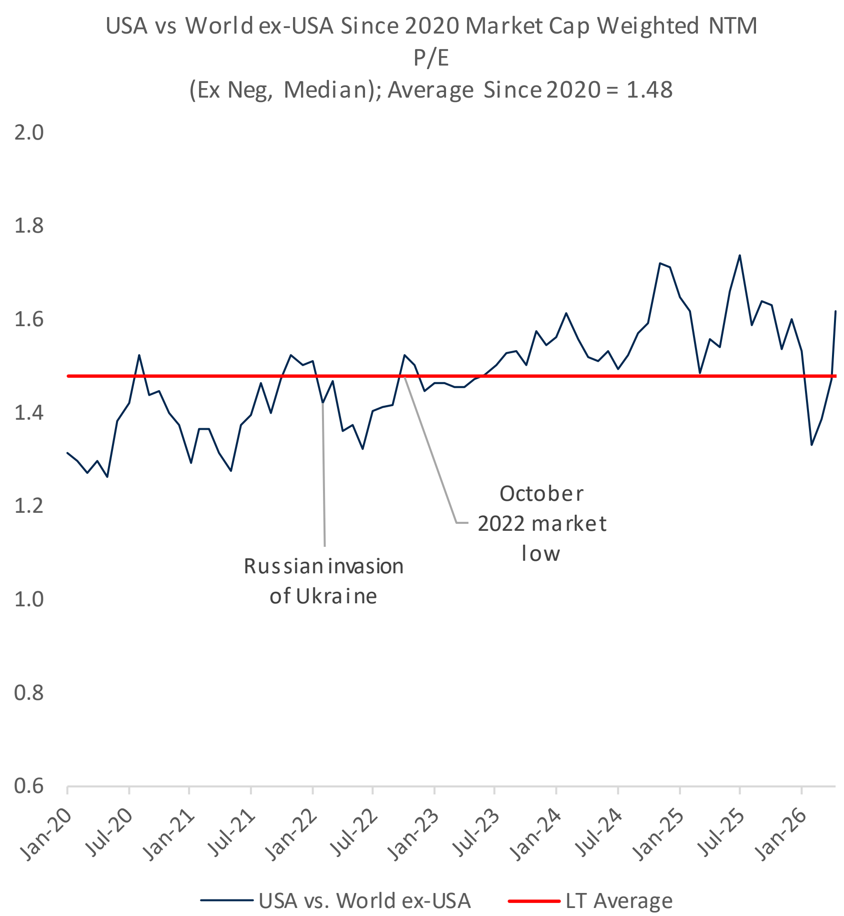
Valuation Comparison of Global Developed Markets Regions & Major Countries

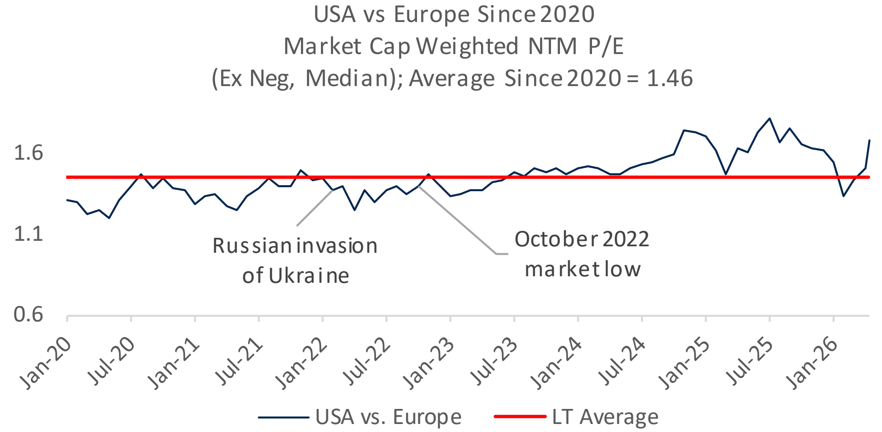


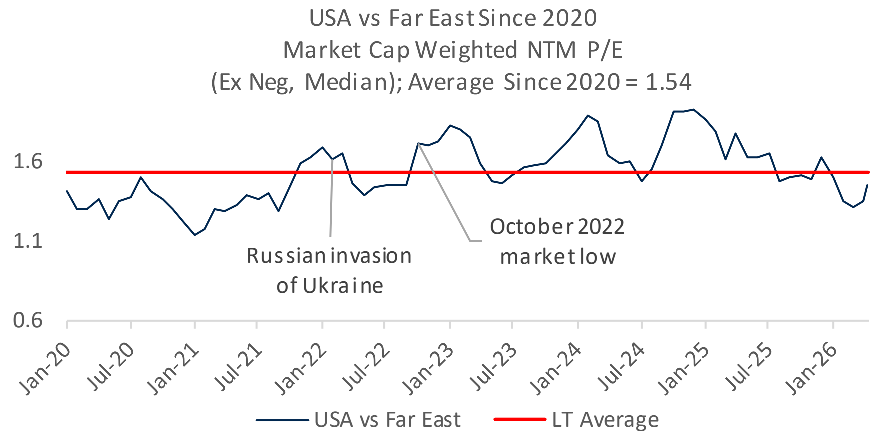
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, MSCI, S&P Capital IQ Clarifi; as of May 12, 2026; please see the MSCI disclaimer at the end of this report; regions/countries based on MSCI constituents with negative earners excluded.

US P/E Is Now Back Above Its Five-Year Average Relative to Non-US and Europe

- In late 2025/early 2026, we saw the US P/E compress relative to Non-US, Europe, and the Far East. Those declines took the US below its post-COVID average relative to non-US, Europe, and the Far East. We think AI fears were largely responsible for the relative P/E compression seen late last year, setting up for a defensive trade back into the US after the US strikes on Iran occurred.
- Since the low in the broader market in late March, US valuations have been climbing relative to non-US valuations again. They are back at average but don't look extreme yet.







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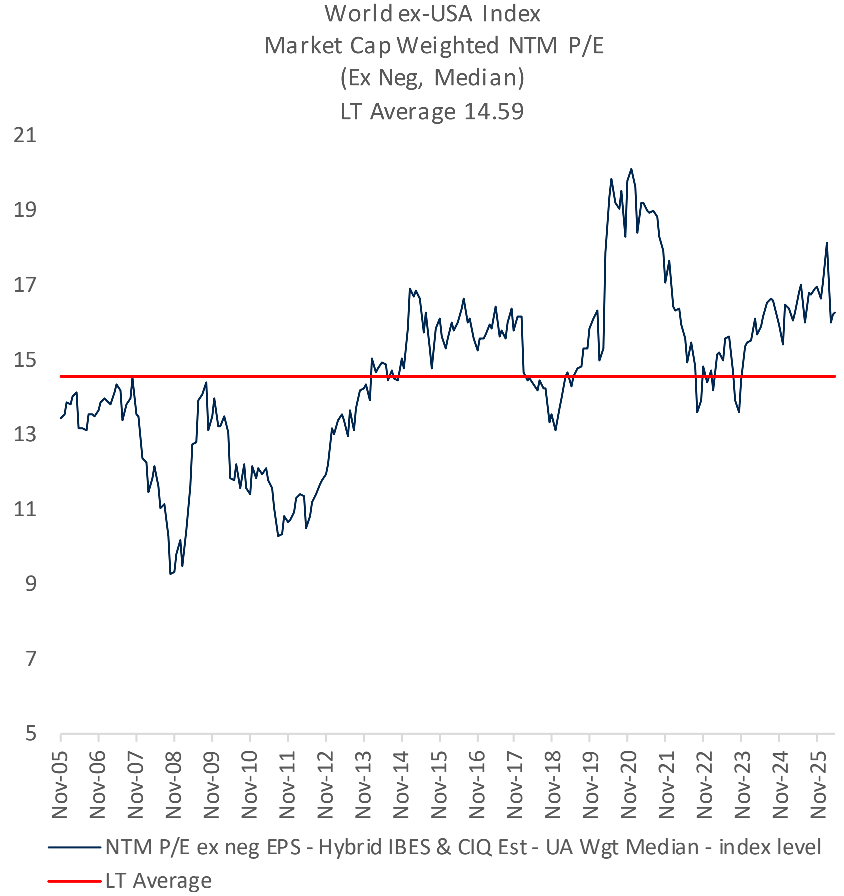
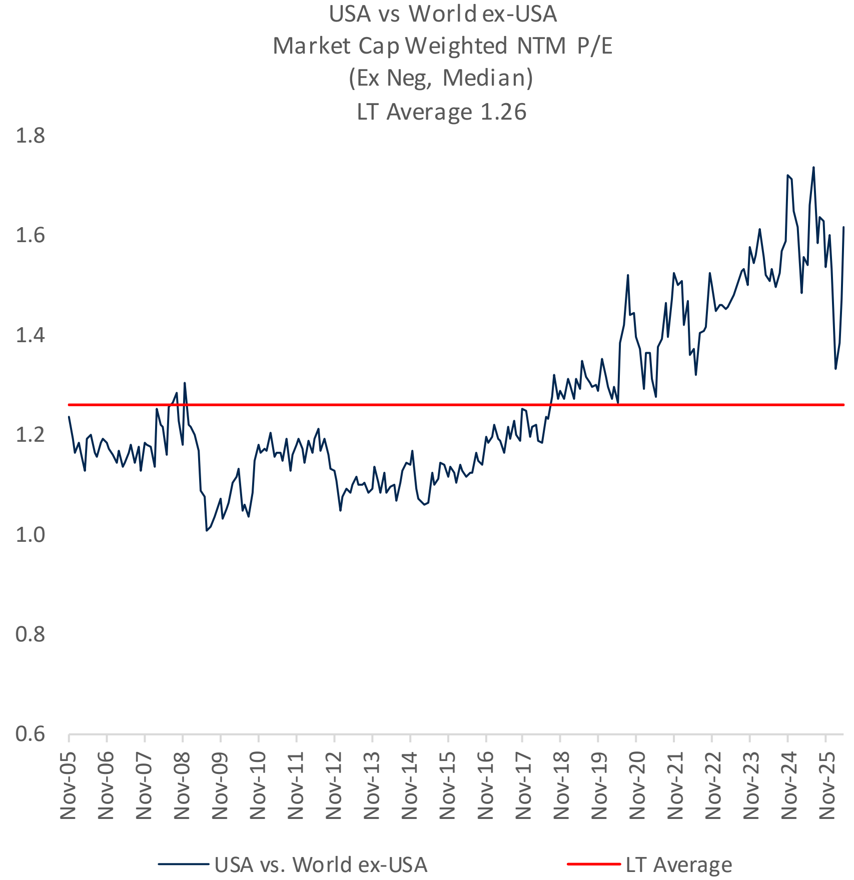
US Premium Relative to Non-US Dropped Sharply Ahead of the War, Is Returning Again

- The US valuation premium over the rest of the world fell last fall and in early 2026, and got close to its long-term average in February ahead of the Iran war. The US has begun to rebuild its premium in recent updates, but is not yet back to past highs.





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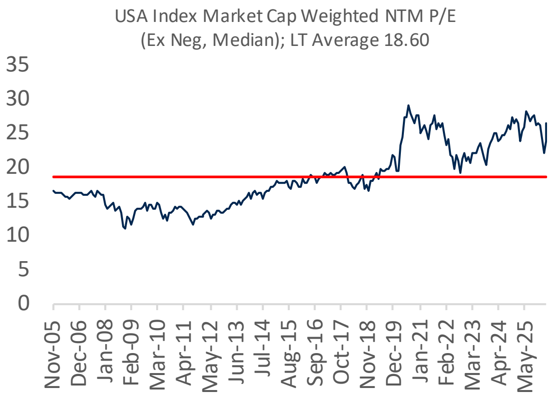
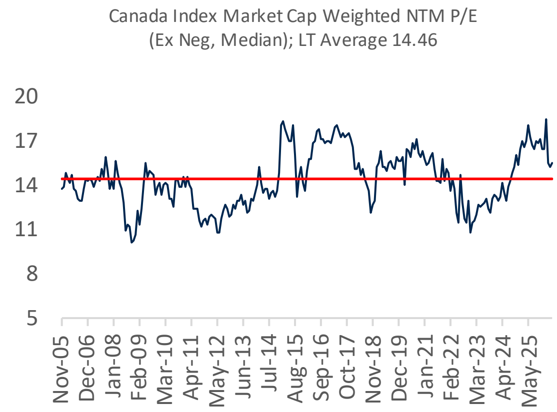
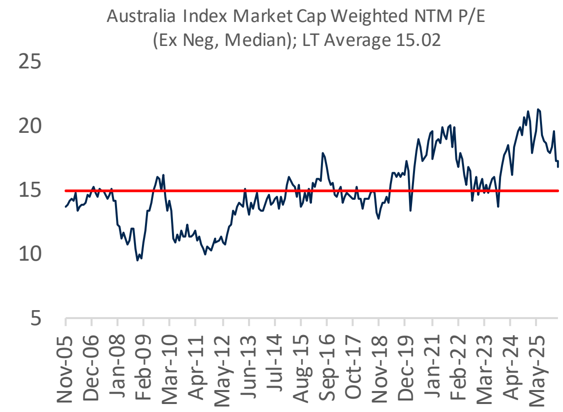
Source: RBC US Equity Strategy, MSCI, S&P Capital IQ Clarifi; as of May 12, 2026; please see the MSCI disclaimer at the end of this report; regions/countries based on MSCI constituents with negative earners excluded.

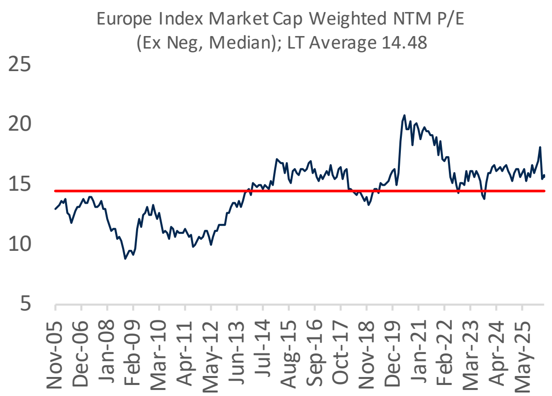
Key Major Non-US Developed Markets Countries Have Seen Their P/Es Move Down

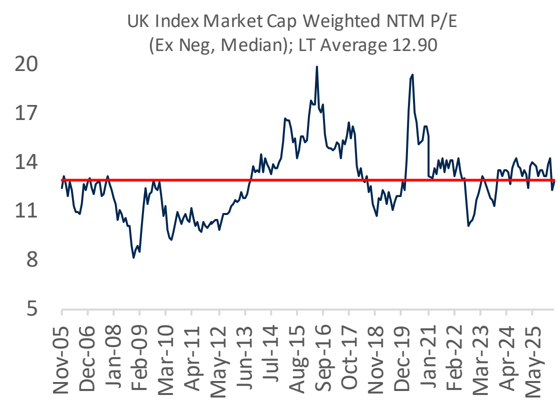
- The US P/E has started to rebound. The P/Es for Canada, Australia, Europe, and UK have moved down in the latest updates.
- In the case of Canada and Australia, early-2026 levels were close to past highs (more so for Canada).

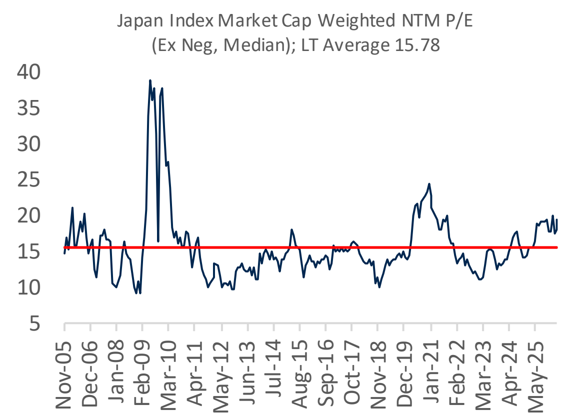








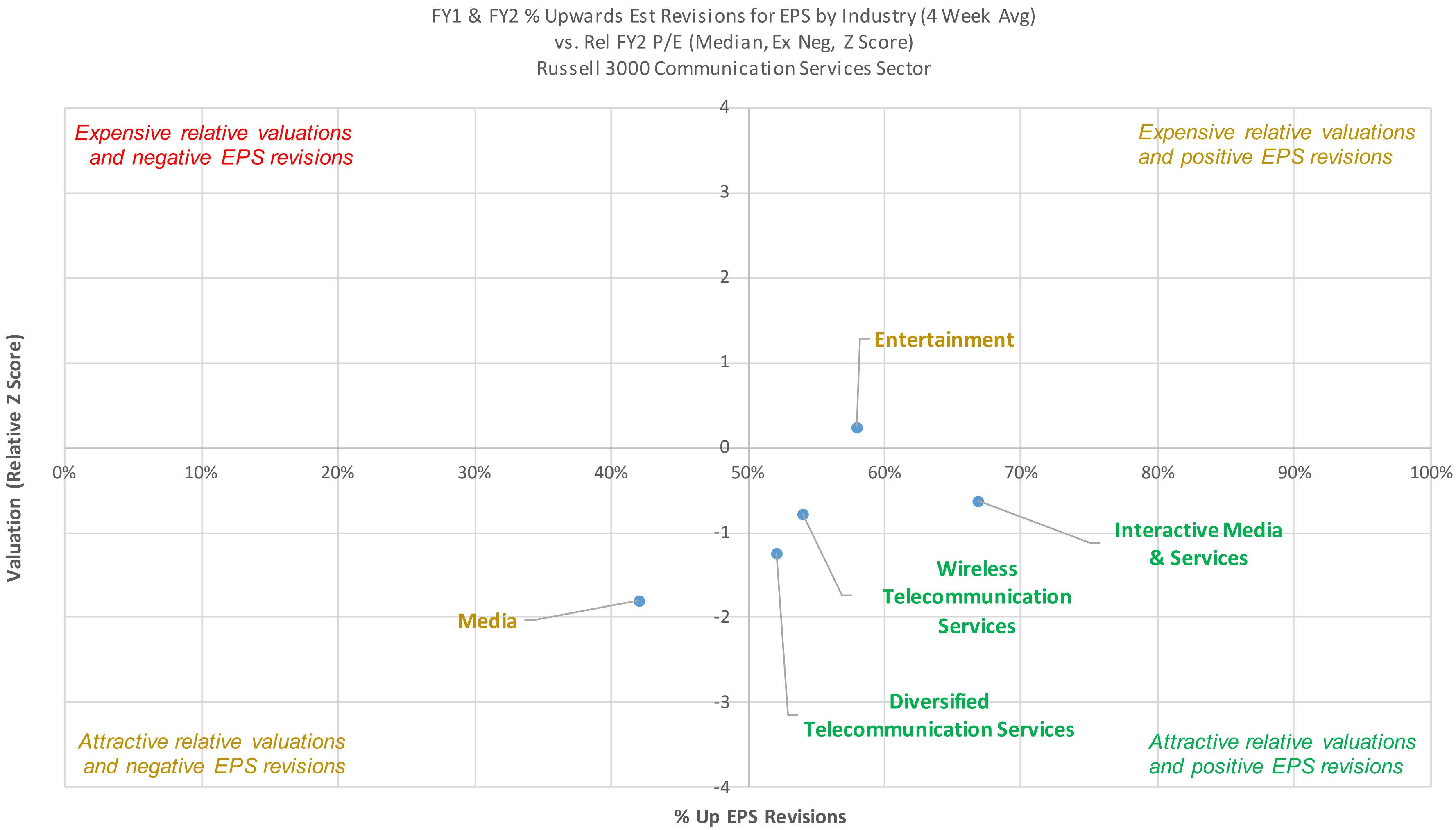




Note: The red line represents the long-term average of the time series.
Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, MSCI, S&P Capital IQ Clarifi; as of May 12, 2026; please see the MSCI disclaimer at the end of this report; countries based on MSCI constituents with negative earners excluded.

Within Comm Svcs, All Industries Look Attractively Valued Except for Entertainment

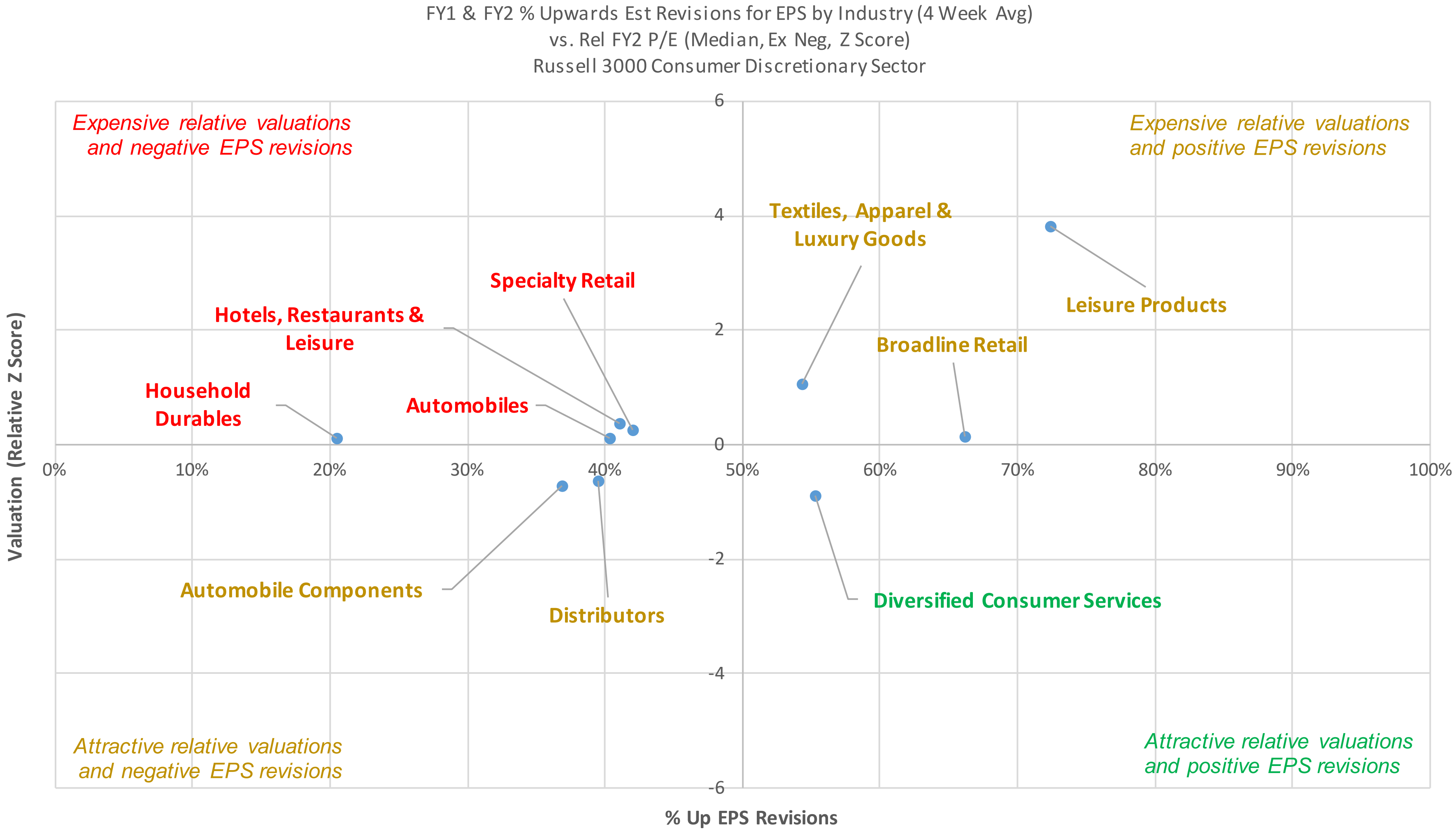
- Interactive Media & Services, Diversified Telecommunication Services, and Wireless Telecom Services have attractive valuations and positive revisions.
- Media has negative EPS revisions, but attractive valuations.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell, as of May 12, 2026

Within CD, Diversified Consumer Services Industry Stands Out as Most Attractive

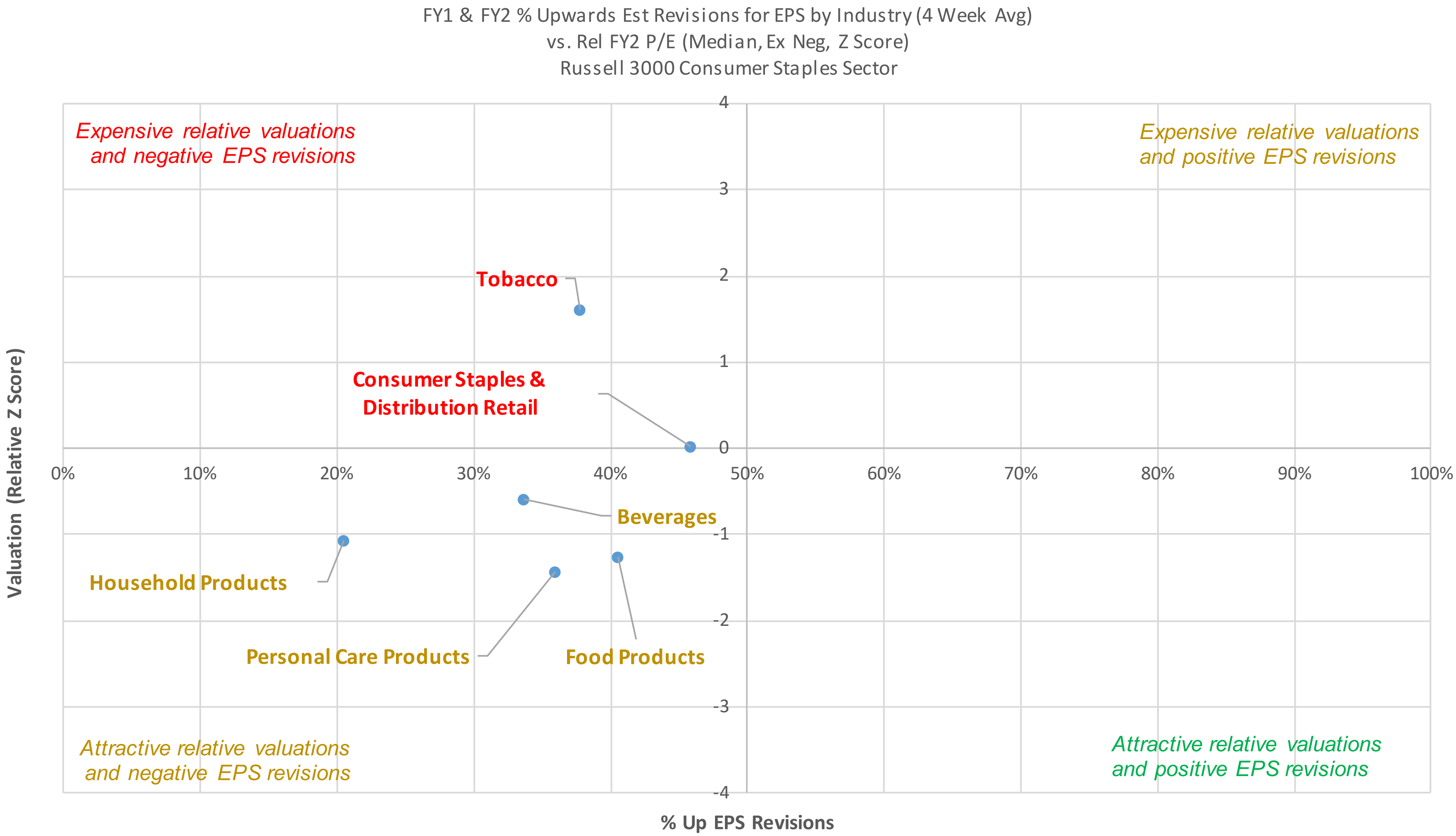
- Household Durables, Hotels, Restaurants & Leisure, Specialty Retail, and Autos look pricey and have weak EPS revisions. Textiles, Apparel & Luxury Goods, Leisure Products, and Broadline Retail have positive revisions but expensive valuations. These are all areas that may be more vulnerable to the impacts of higher energy costs going forward given the lack of valuation appeal.
- Automobile Components and Distributors have weaker revisions. Valuations look reasonable (in line with the average) but not cheap.
- Diversified Consumer Services are the only bright spots with slightly attractive valuations and positive earnings revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Staples, No Industry Has Positive Earnings Revisions

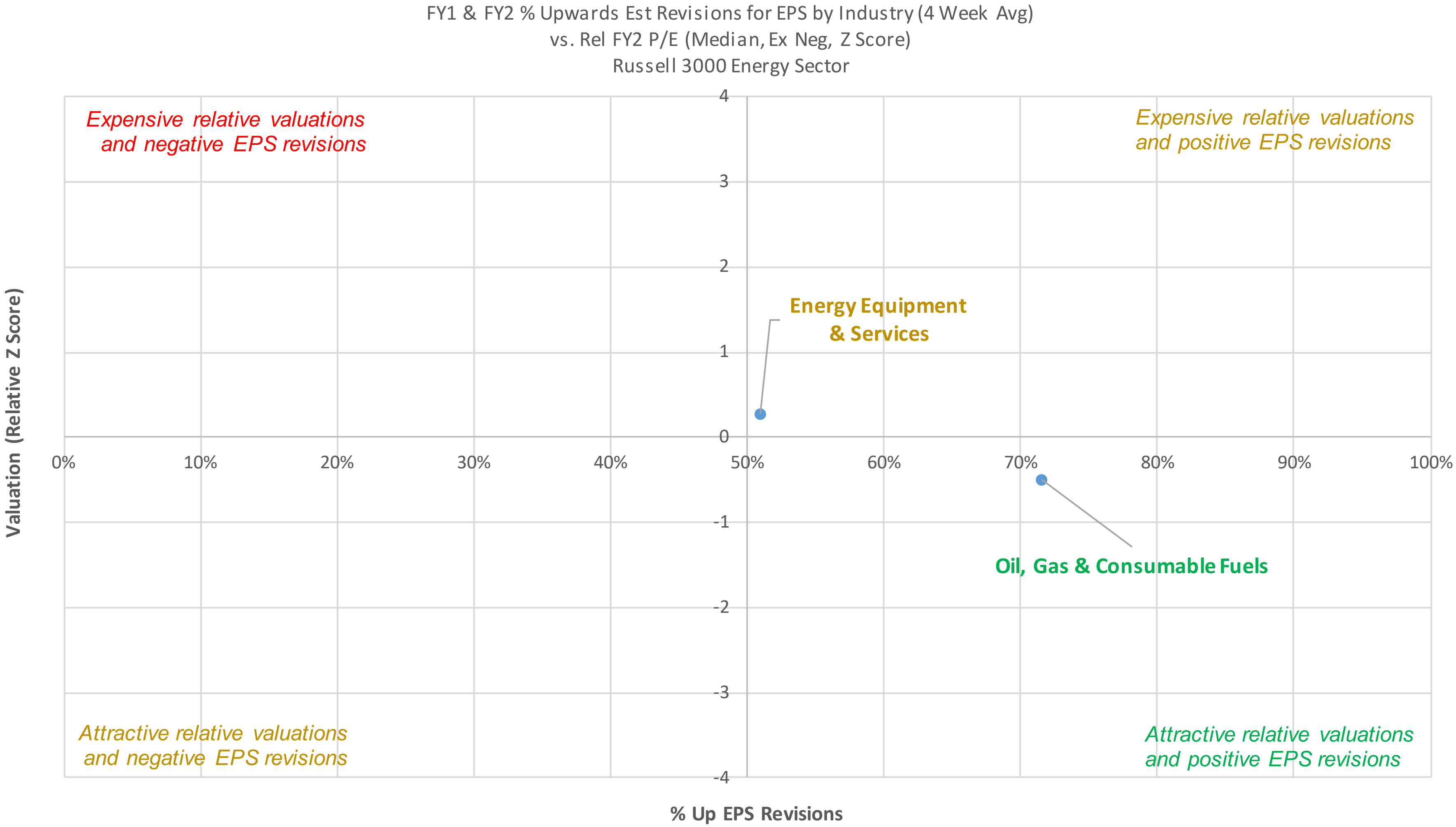
- Food Products, Beverages, Household Products, and Personal Care Products look attractively valued but EPS revisions are weak.
- Tobacco and less so Consumer Staples & Distribution Retail have expensive valuations with negative EPS revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Energy, Valuations Are Close to Average for Both Industries

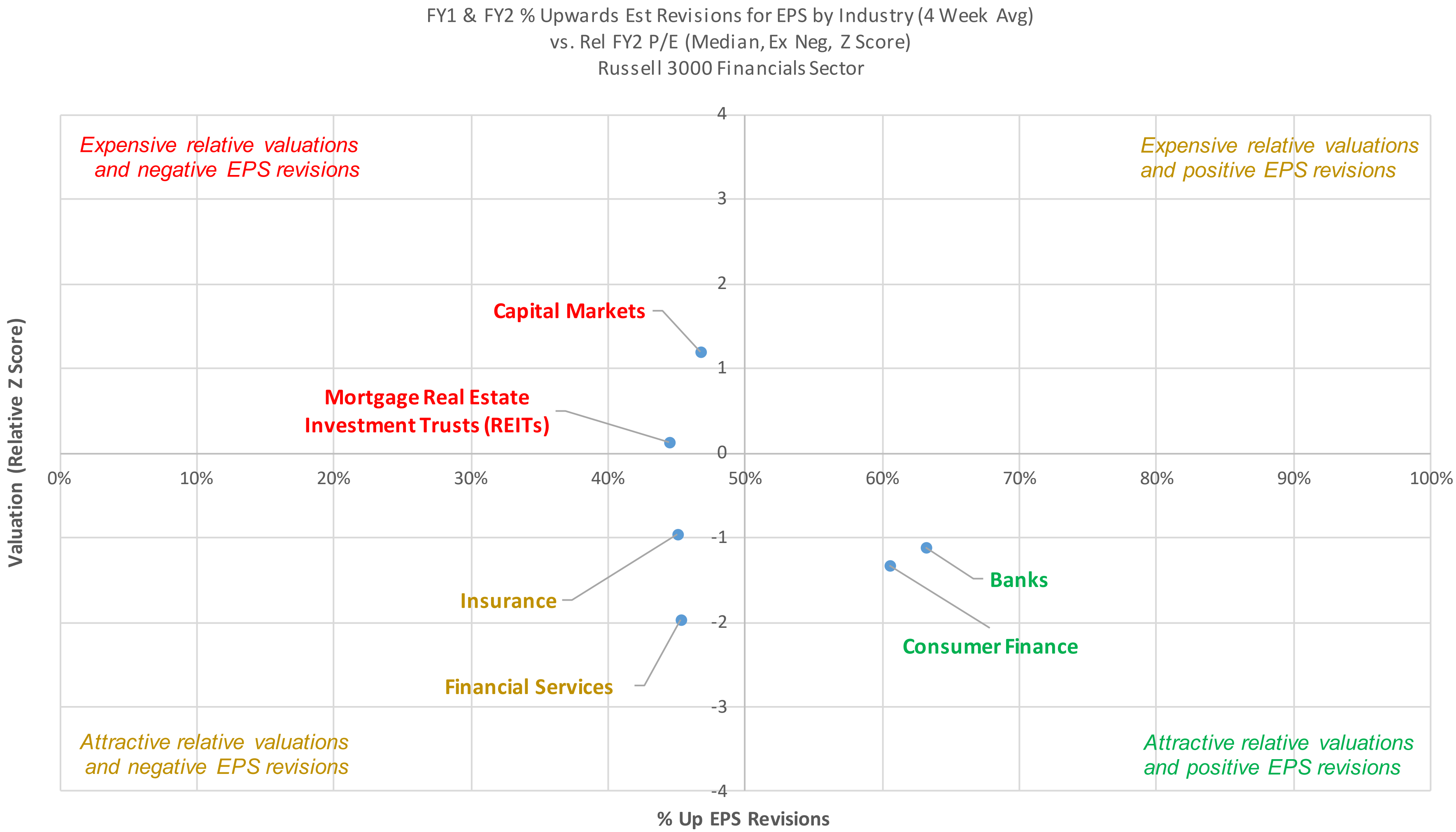
- We see a little more valuation appeal in the oil and gas names.
- Both industries have positive EPS revisions, but those for Oil, Gas & Consumable are much stronger than those for Energy Equipment & Services.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Financials, Capital Markets Are Still Screening Slightly Expensive With Negative EPS Revisions

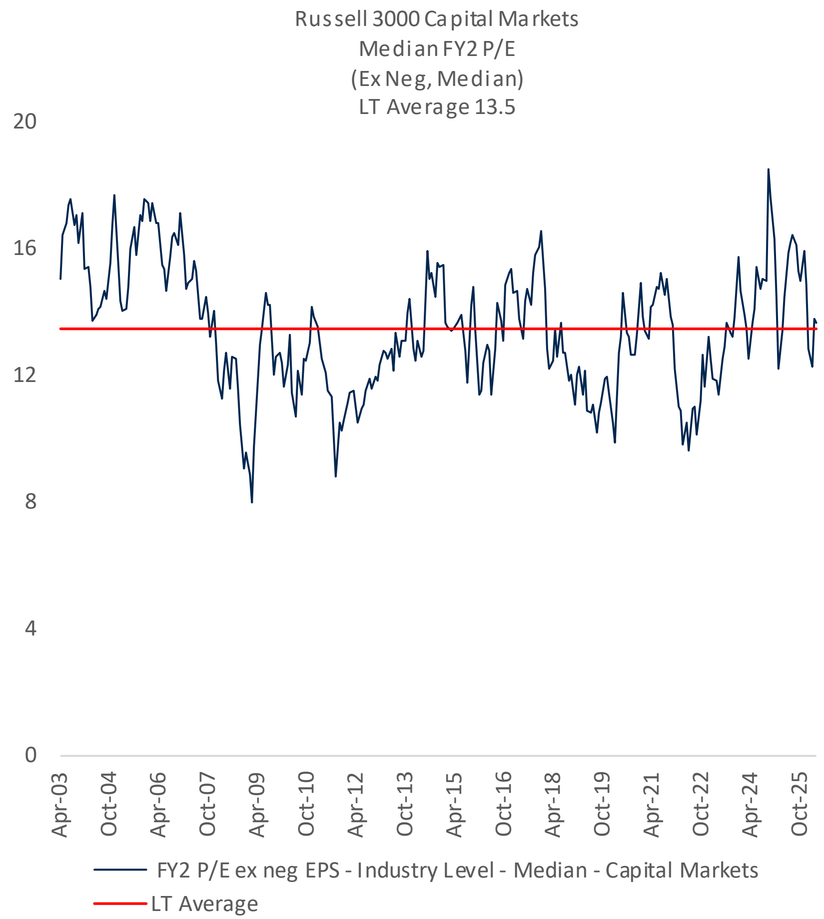
- Capital Markets was expensive to start the year. Valuations had improved to average levels but have turned slightly expensive again. Note that the industry used to have positive earnings revisions, but those have turned negative now. Mortgage REITs also screen expensive with negative earnings revisions.
- Banks and Consumer Finance have attractive valuations and screen positive on their EPS revisions.
- Insurance and Financial Services have attractive valuations too but screen negative on their EPS revisions.

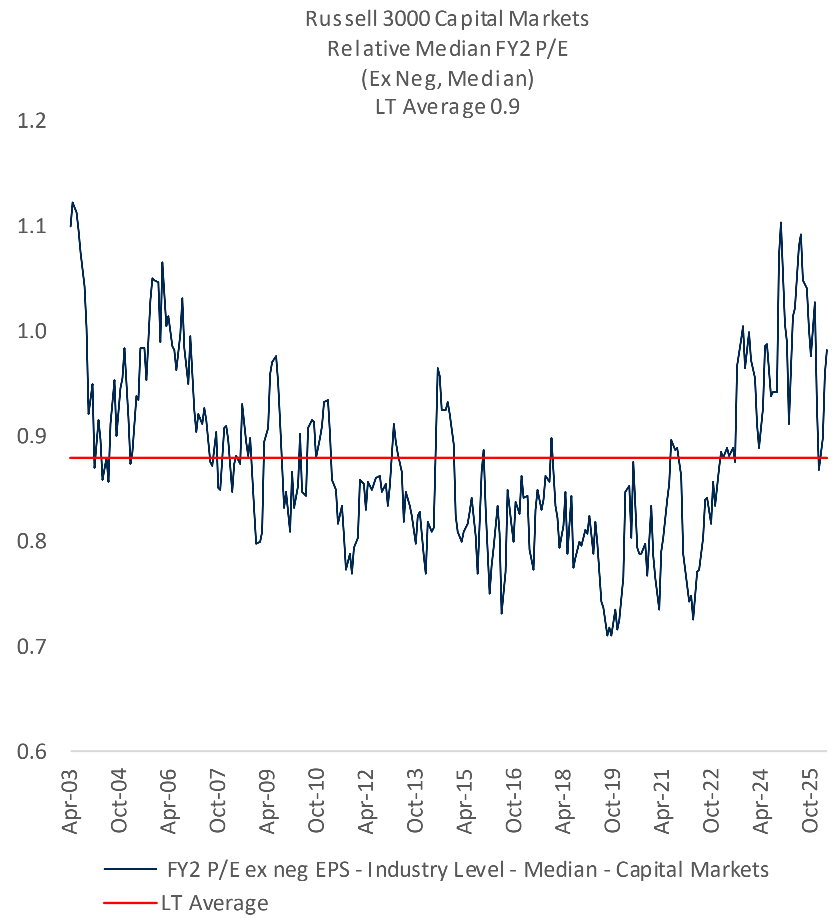


Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Financials, Capital Markets Valuations Are Rebounding Again, Remain Well Below Past Peaks

- Absolute valuation and relative valuation vs. the Russell 3000 recently fell back down to levels slightly below the long-term average, but remained well above past troughs. Similar to our thinking on the broader market indices, we think the froth was removed from this group but don't think valuations got washed out.

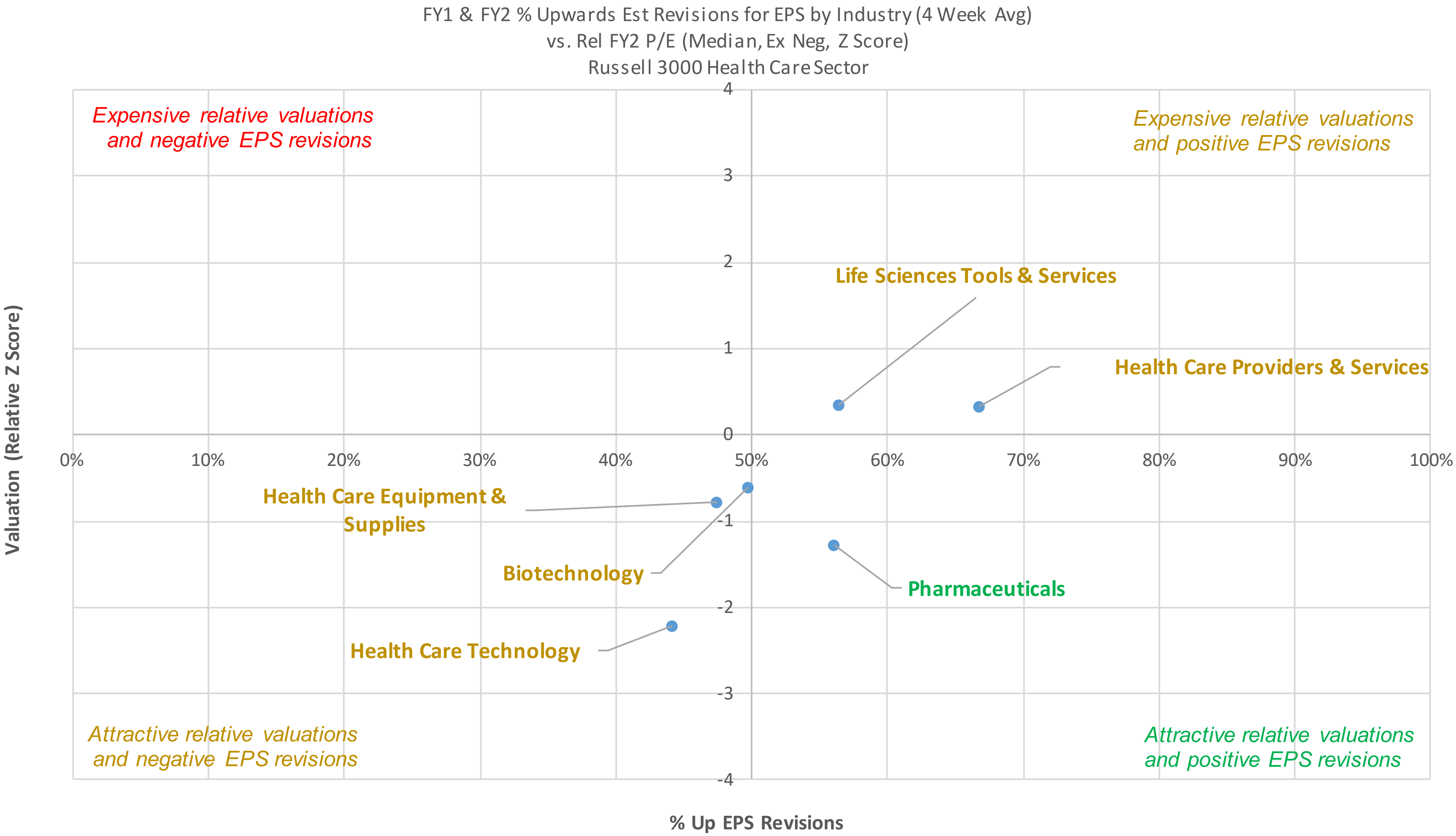




Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within HC, Pharma Stands Out as the Most Interesting Industry

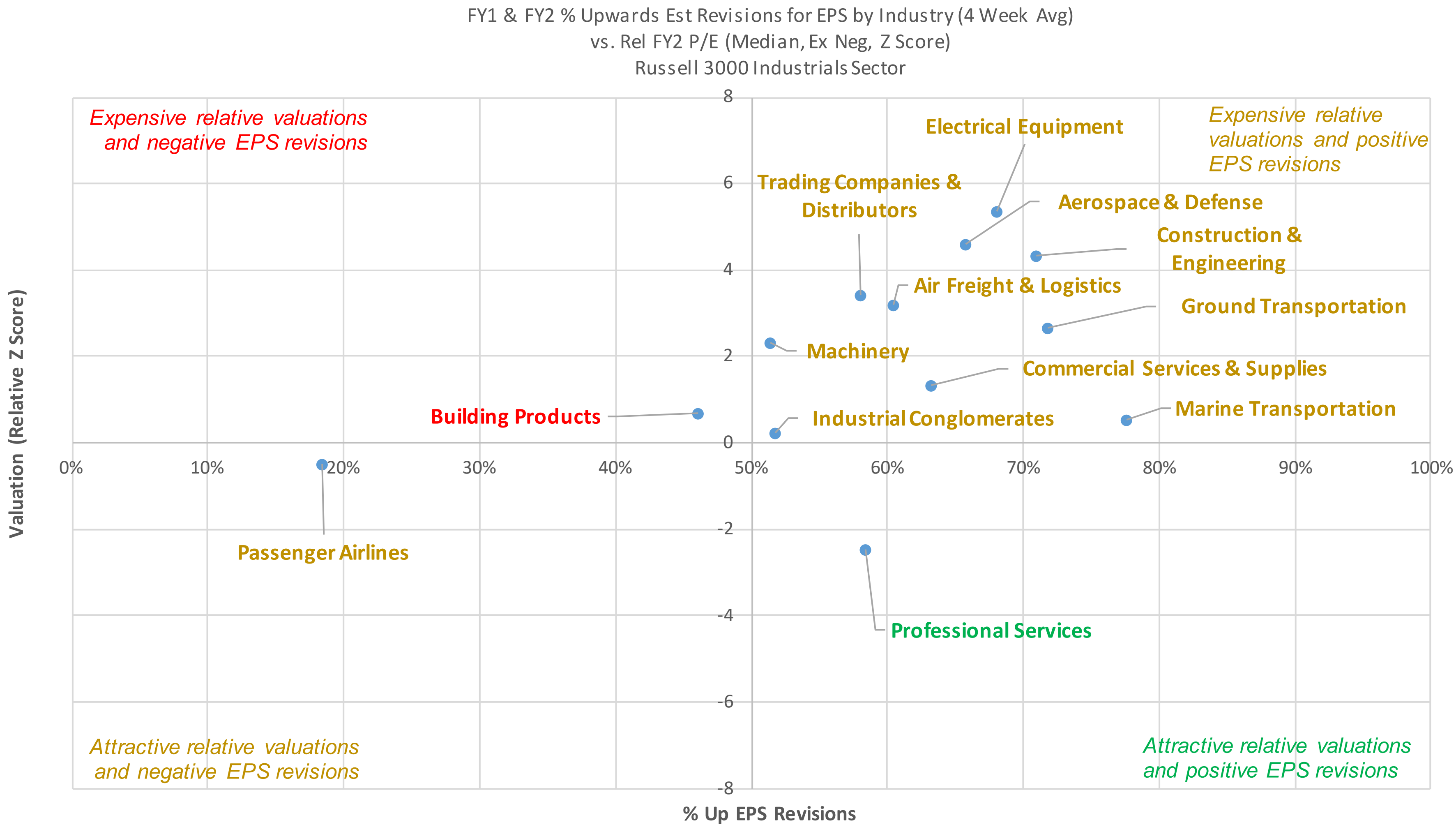
- Health Care Equipment & Supplies, Health Care Tech, and Biotech have attractive valuations but negative EPS revisions. On the flip side, Health Care Providers & Services and Life Sciences Tools & Services are pricey with positive revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell, as of May 12, 2026

Within Industrials, Few Groups Look Attractively Valued

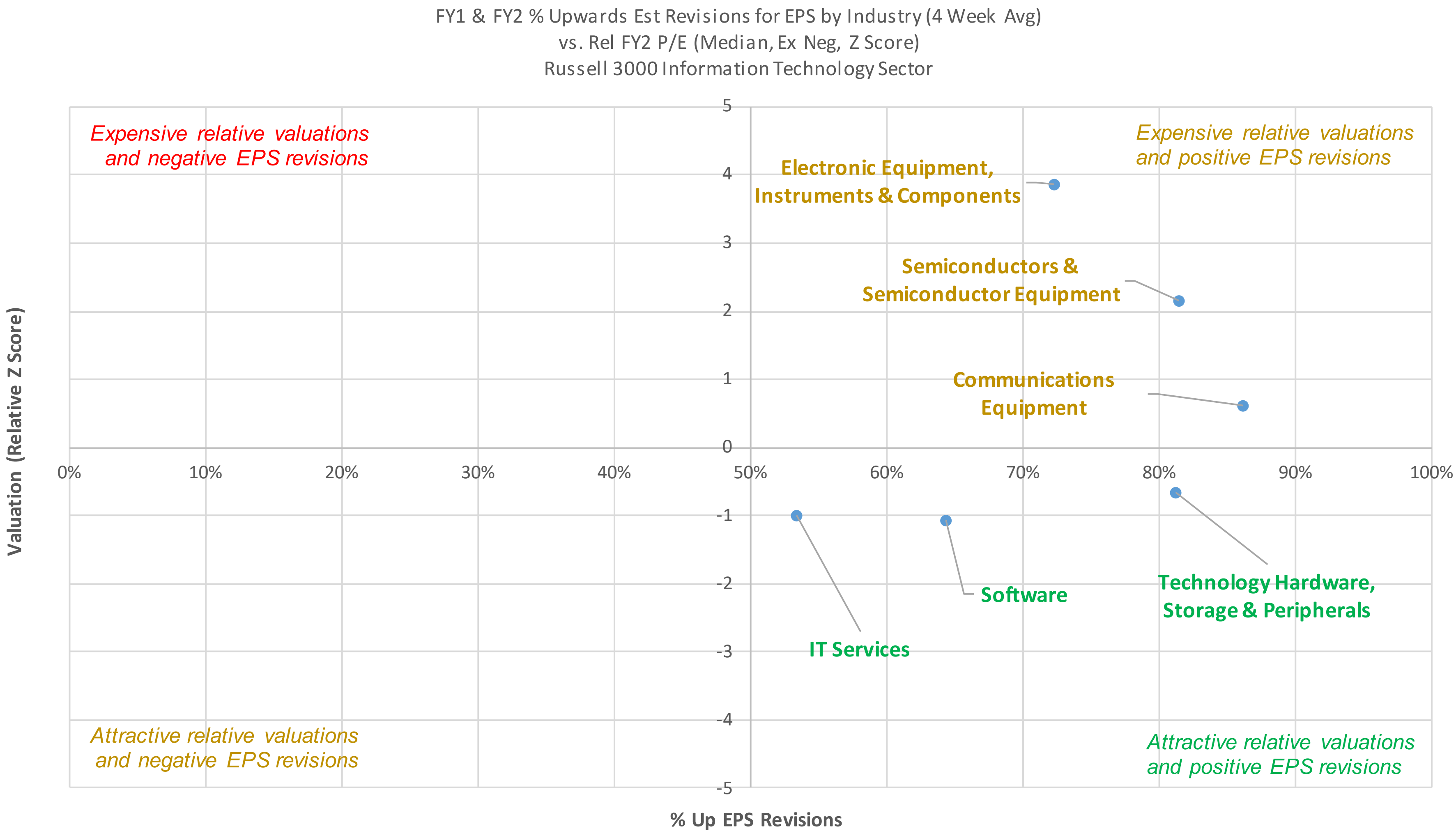
- Only Professional Services industry looks attractively valued and has positive EPS revisions. Electrical Equipment, Aerospace & Defense, and Construction & Engineering now screen extremely expensive per our model with relative valuations between four and six standard deviations above the long-term average.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Tech, All Industries Have Positive EPS Revisions

- Software, Tech Hardware, and IT Services all have attractive valuations.
- Semis/Semi Equipment and Electronic Equipment Instruments & Components lack valuation appeal.

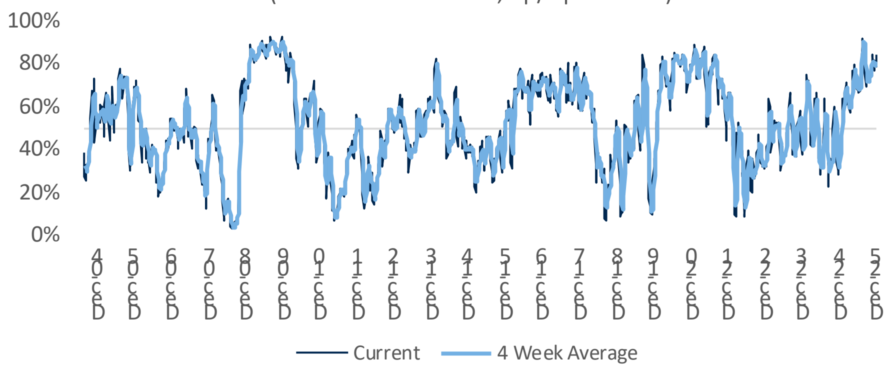


Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

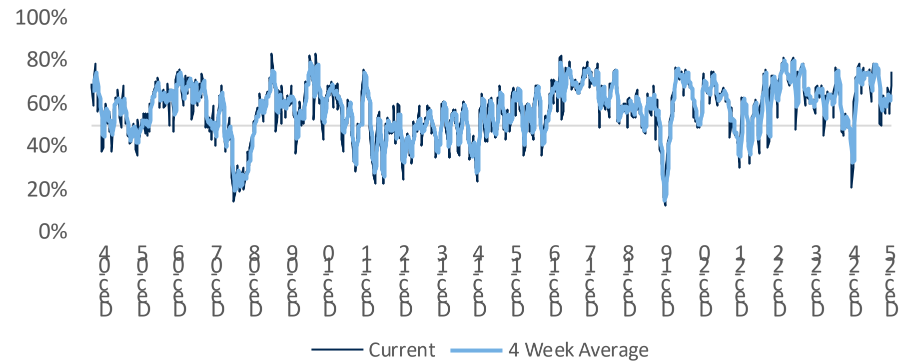
Semis EPS Estimate Revisions Have Been Near Peak, While Software Revisions Have Fallen Sharply

- One thing we've been pointing out in recent client meetings is that Software revisions have stabilized around the 50% mark, but haven't yet entered negative revisions territory. While valuations for this industry are close to past lows, we are not seeing the same thing on Software EPS revisions and normally like to see extreme negative EPS revisions and depressed valuations before considering an industry to be washed out. Meanwhile, Semis revisions are in line with past peaks, which keeps us vigilant for a deceleration in the rate of upward revisions which we think would be a negative signal for performance. It's worth noting that past peaks for this industry have sometimes been extended.

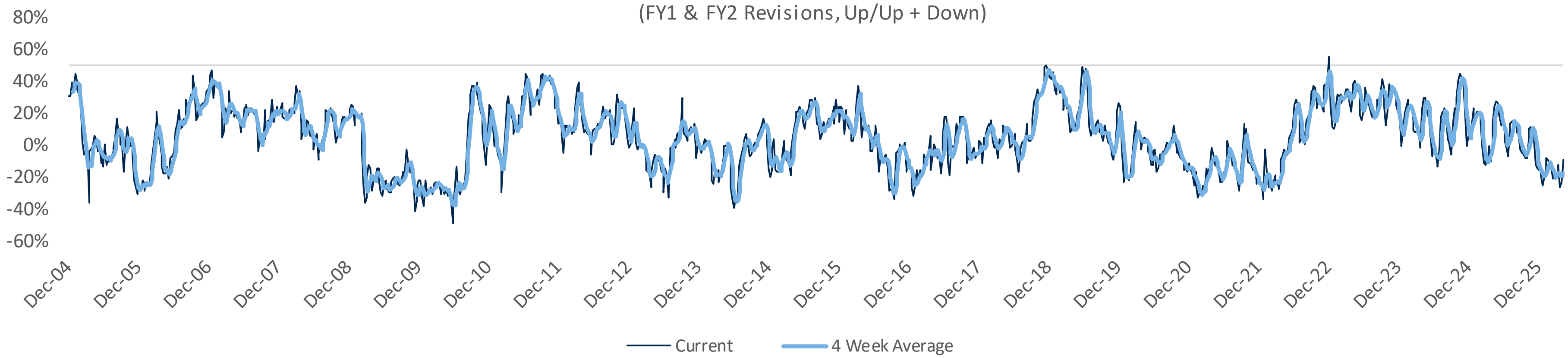
R3000 Semiconductors & Semiconductor Equipment: % Upward EPS Revisions
(FY1 & FY2 Revisions, Up/Up + Down)



R3000 Software: % Upward EPS Revisions
(FY1 & FY2 Revisions, Up/Up + Down)



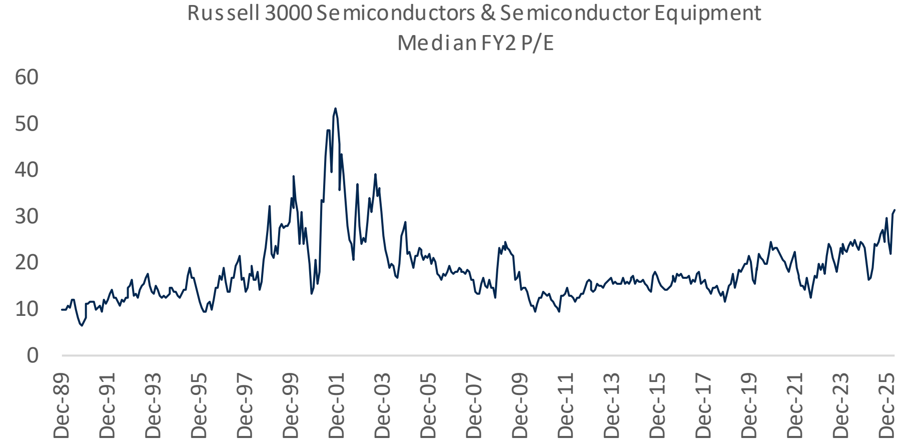
R3000 Software Less Semiconductors & Semiconductor Equipment
% Upward EPS Revisions
(FY1 & FY2 Revisions, Up/Up + Down)

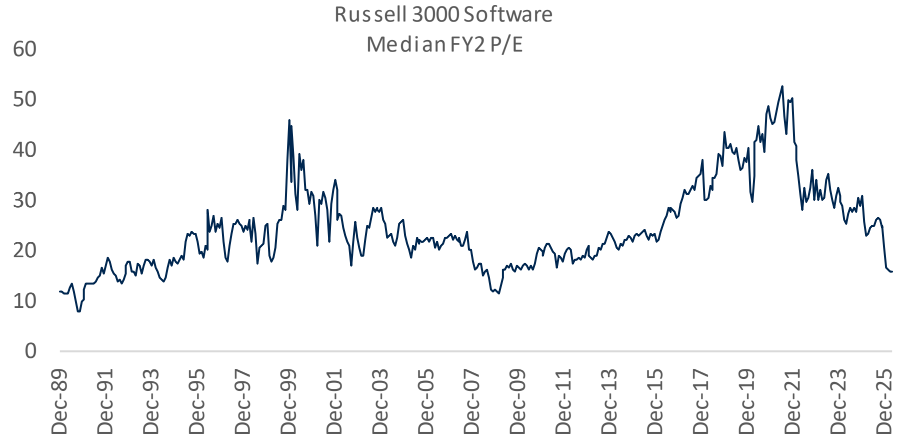


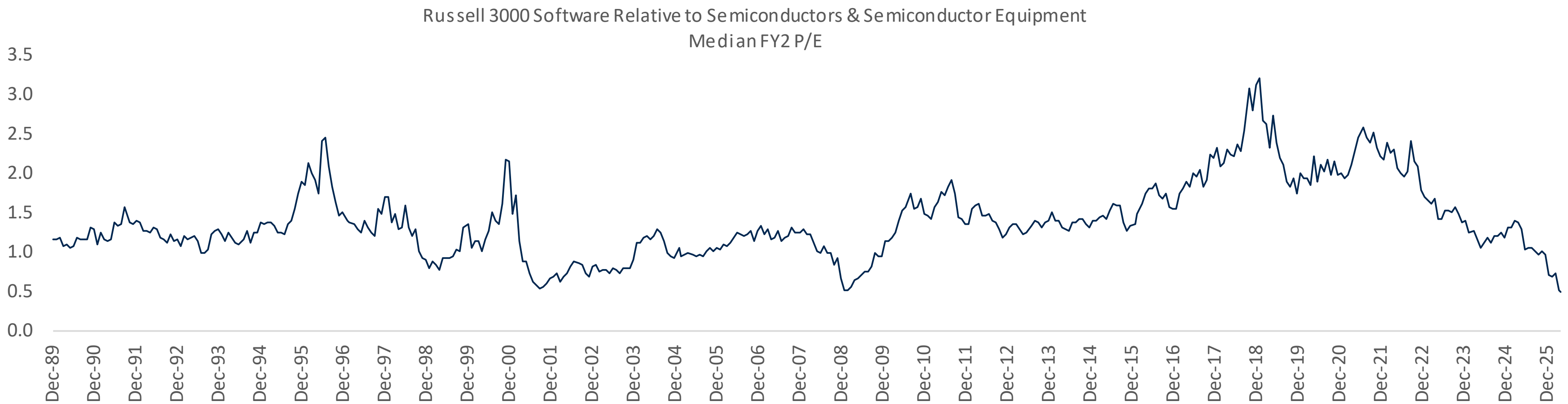
Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Semis Valuations Have Returned to Post-GFC Highs, Software FY2 P/Es Approaching Past Lows

- We had seen some slight contraction in Semis P/E, but it's popped back up again to levels above recent highs. Tech bubble highs remain far off, however.
- The relative P/E of Software relative to Semis has gotten close to Tech bubble and GFC lows. Some investors have recently raised the idea to us of Software potentially going up in the Russell value indices in the upcoming reconstitution, which could prompt buying by Value PMs.



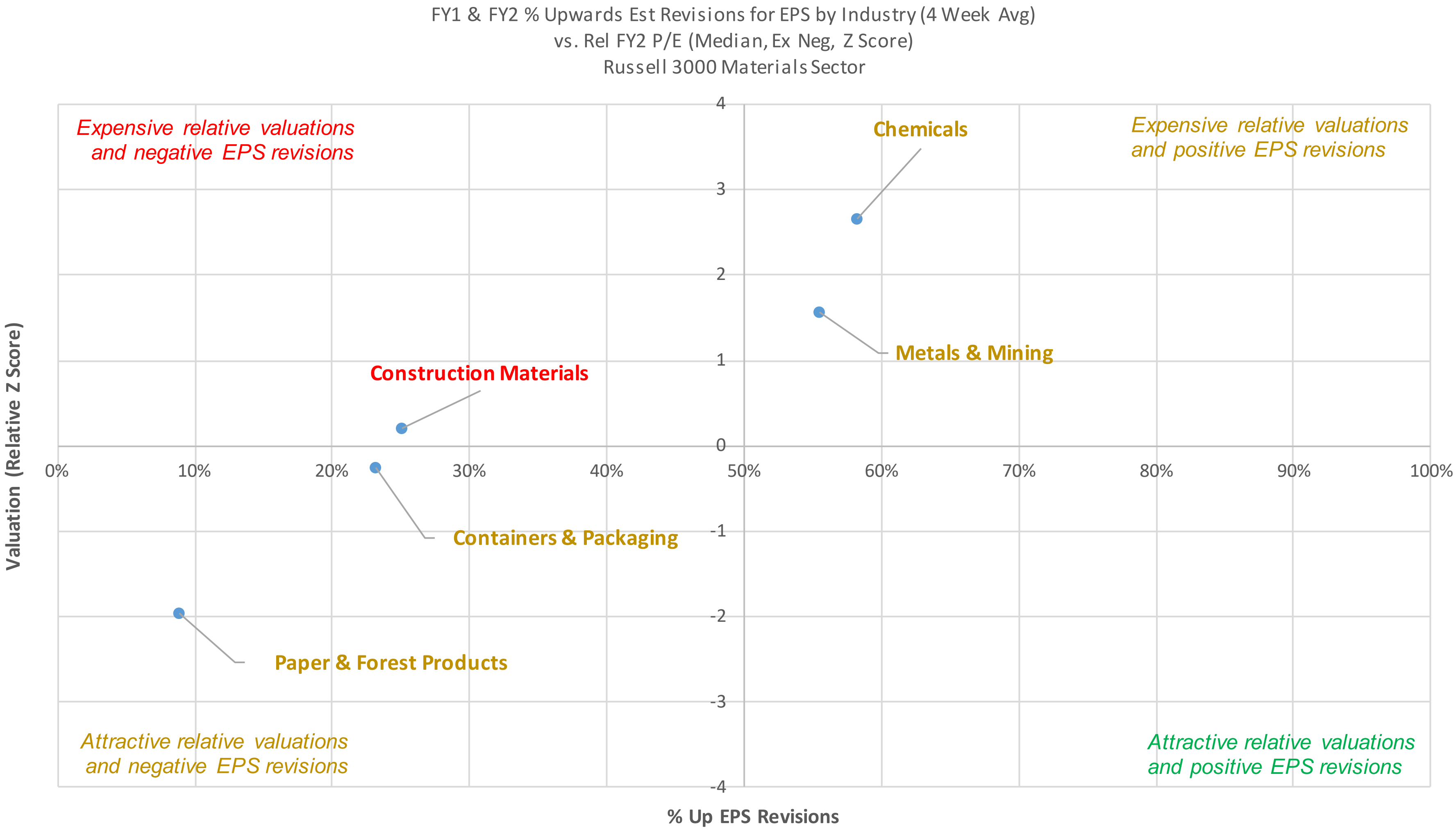




Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Within Materials, Construction Materials Stands Out With Negative EPS Revisions & Pricey Valuations

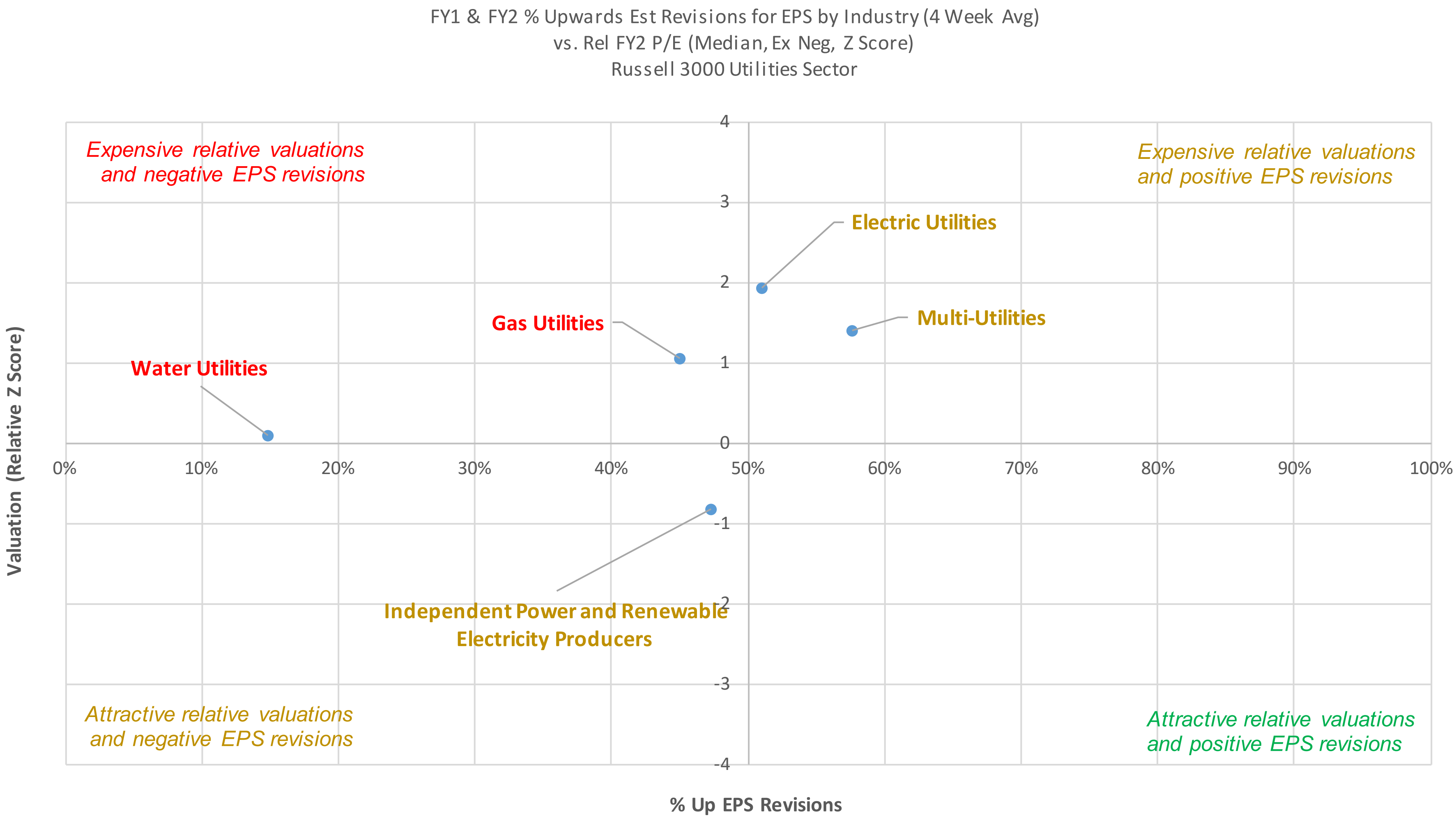
- Metals and Mining and Chemicals have positive EPS revisions. Valuations have fluctuated recently and are currently sitting a bit above their long-term average.
- Paper & Forest Products and Containers & Packaging appear to have attractive valuations but have negative earnings revisions.



Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell, as of May 12, 2026

Within Utilities, No Industry Stands Out With Attractive Valuations and Positive EPS Revisions

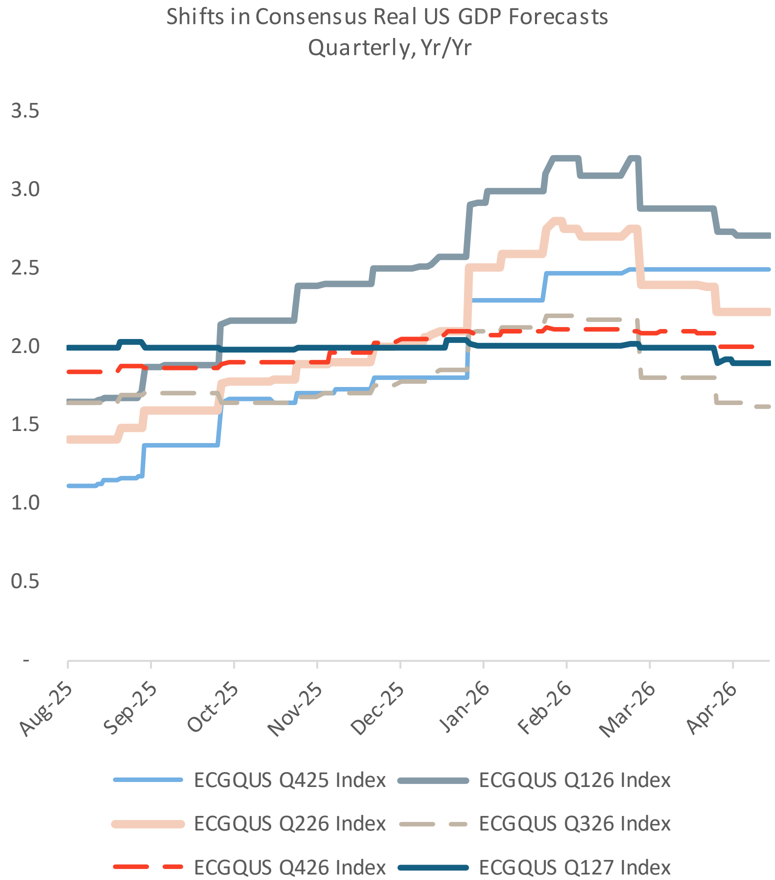
- Multi Utilities and Electric have positive EPS revisions but expensive valuations.
- Water Utilities and Gas Utilities screen expensive with negative EPS revisions.
- Meanwhile, Independent Power and Renewable Producers have negative EPS revisions but is the only industry with attractive valuations.

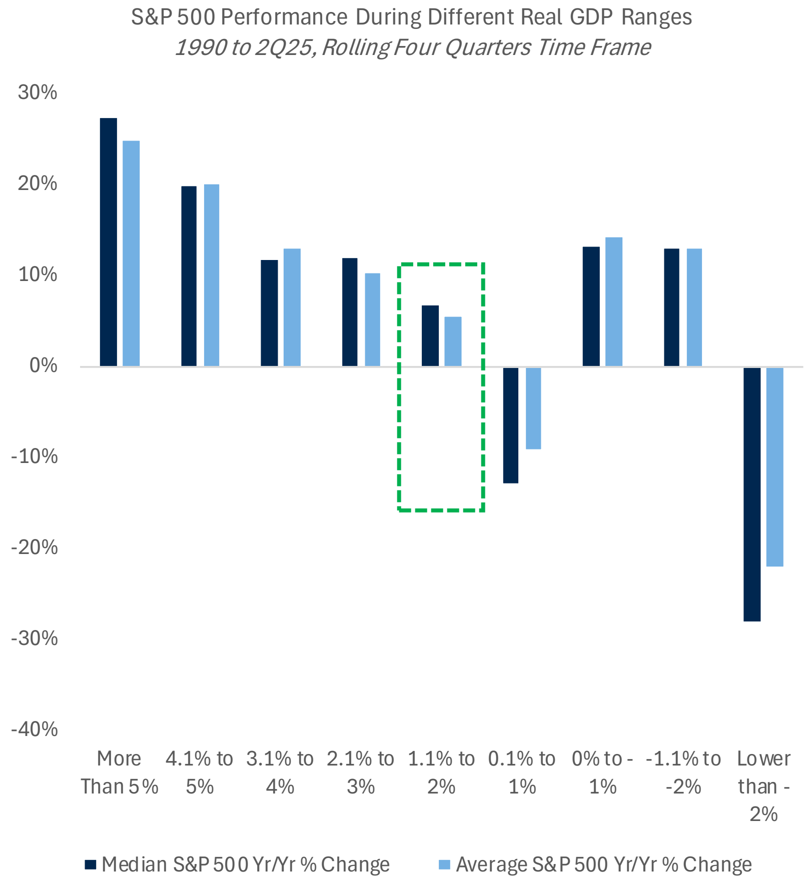


Source: RBC Equity Strategy, S&P Capital IQ / ClariFI, Russell; as of May 12, 2026

Expectations for the Real GDP Backdrop Have Remained Solid from a Stock Market Perspective

- We have seen some modest downward revisions to quarterly GDP forecasts recently, but are still in a range that points to decent stock market returns.
- RBC Economics is anticipating 1.7% for 1Q27 while the street consensus is tracking at 1.9% per Bloomberg.
- Given the fact that RBC and consensus are in the upper end of the 1.1–2% range for 1Q27, we are using an anticipated return of 5.7% in our price target modeling.
- Note if the 1Q27 real GDP forecast slips into the 0.1–1% range, that poses a downside risk to our price target as stocks tend to fall in that range.

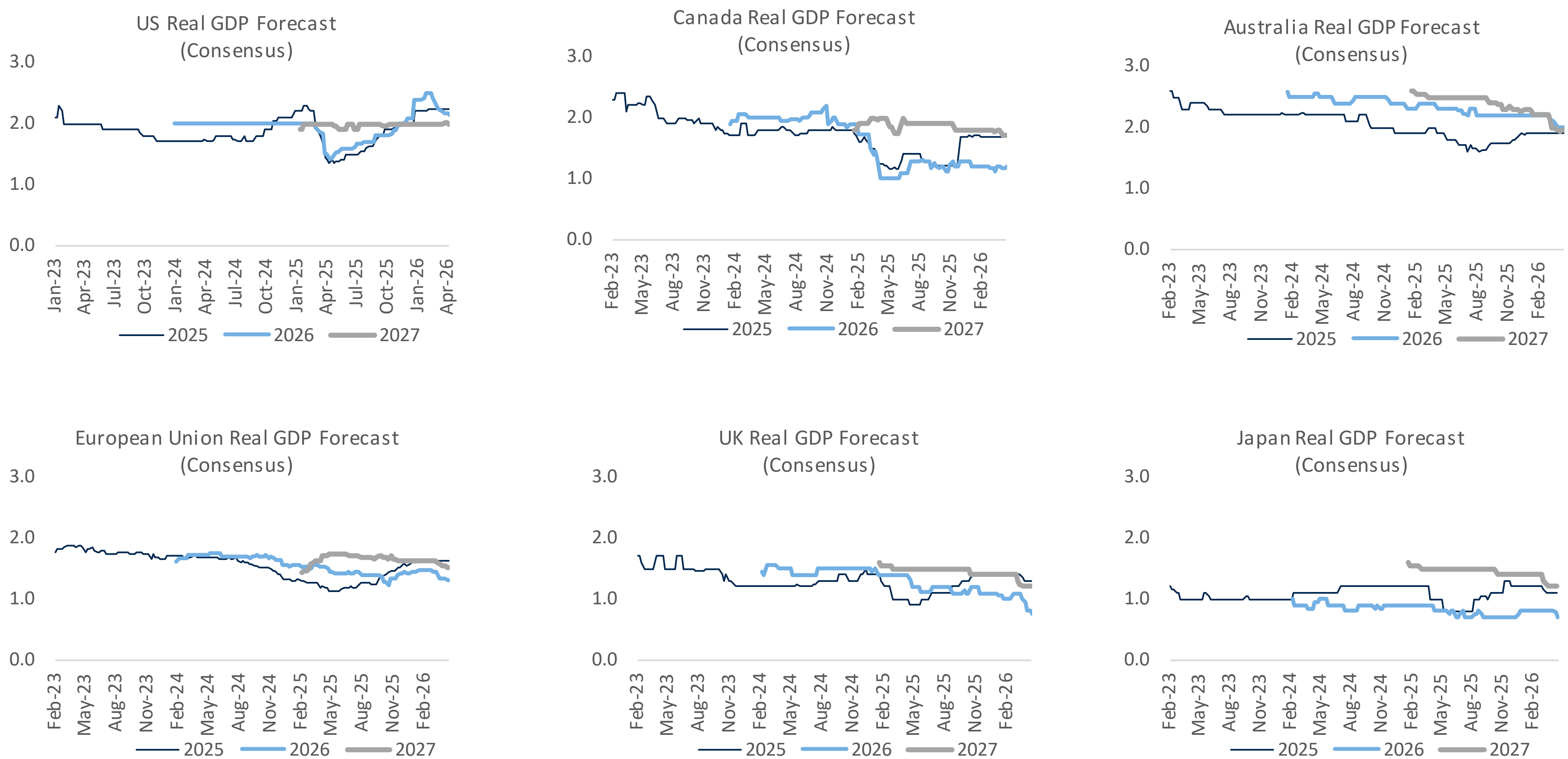




Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg, S&P; as of 5/13/26

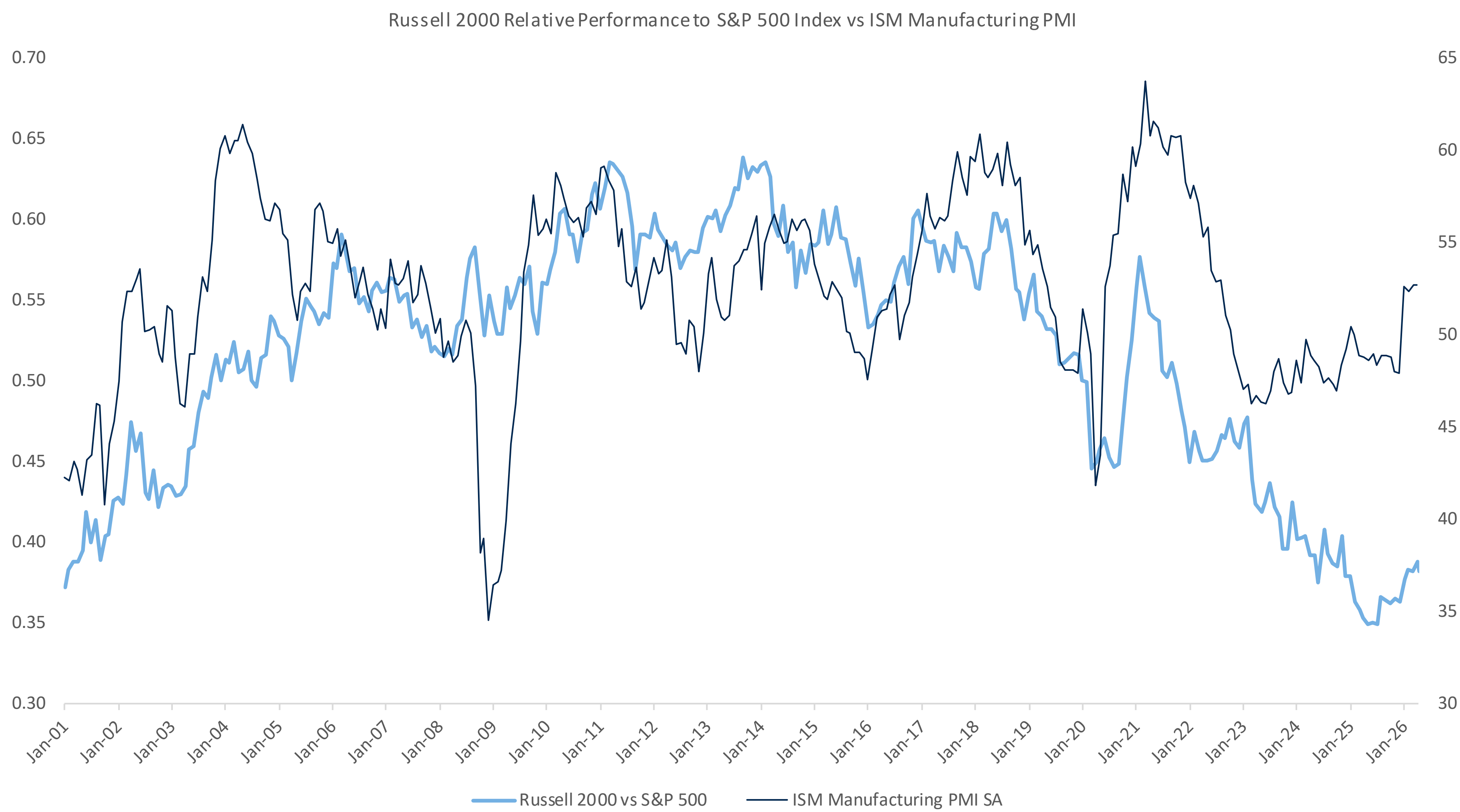
Trends in Consensus US GDP Forecasts Had Been a Bright Spot Among Global Developed Markets

- US GDP forecasts for full-year 2026 have softened lately but remain on par with 2025's levels, which ended on strong footing. Meanwhile, 2027 expectations have been firm.
- Outside the US, we've also seen some slippage in consensus GDP forecasts for 2026 for all of the major countries we've been tracking plus the EU. 2027 consensus forecasts have been coming down in most major non-US countries that we track as well.



Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg; as of 5/8/2026; forecasts are the consensus tracked by Bloomberg

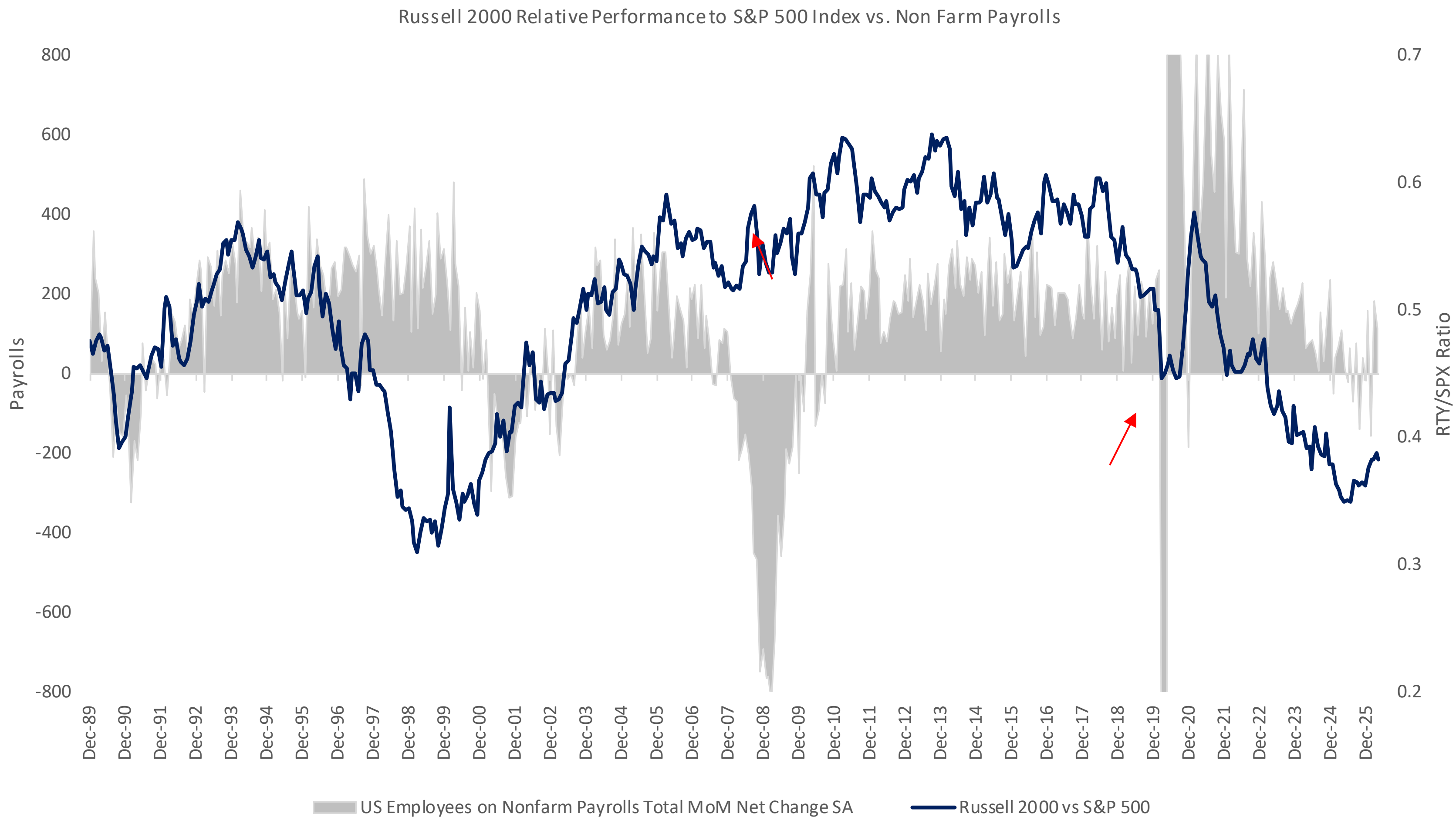
Recent Improvement in ISM Manufacturing Is Supportive of Small Caps



Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy, Bloomberg. Russell, S&P, latest available data as of 5/13/26

Small Caps Usually Lag When Jobs Growth Is Weak, and Outperform When It Is Strengthening

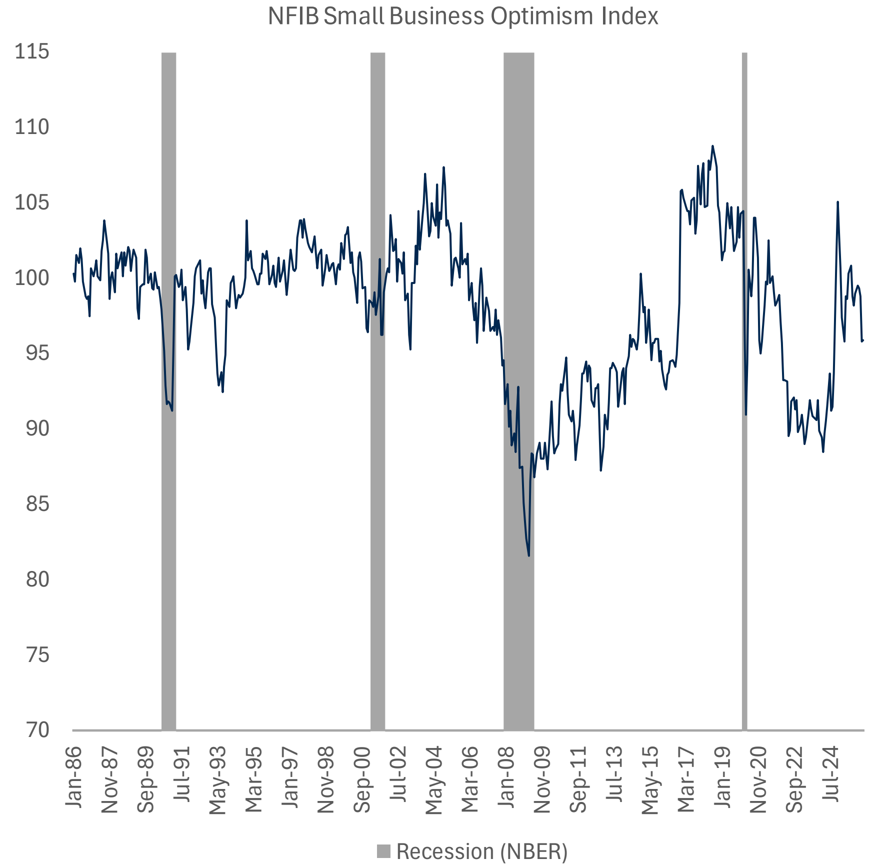
- We had been starting to see some signs of a positive jobs growth environment in the January NFP release, but this shifted abruptly in the update for February, which came out in early March. That downtick was a challenge to the positive fundamental story for Small Caps that had been unfolding. The good news for Small Caps is that trends improved again in the March and April NFP releases.
- Generally, neither stalling nor deteriorating jobs growth tends to be good for Small Cap performance relative to Large Caps. Usually, Small Caps need to see accelerating jobs growth to outperform. There is a wrinkle to that idea, however. In the last two cycles, Small/Large relative performance has tended to bottom right around when deep and sustained jobs losses emerge.
- Looking ahead to the next NFP report for May, in the very short term, we think a bad print would be bad for Small Caps, unless it results in increased expectations around Fed cuts in the year ahead. Conversely, a good print would be good for Small Caps unless it results in increased concerns that hikes are coming.

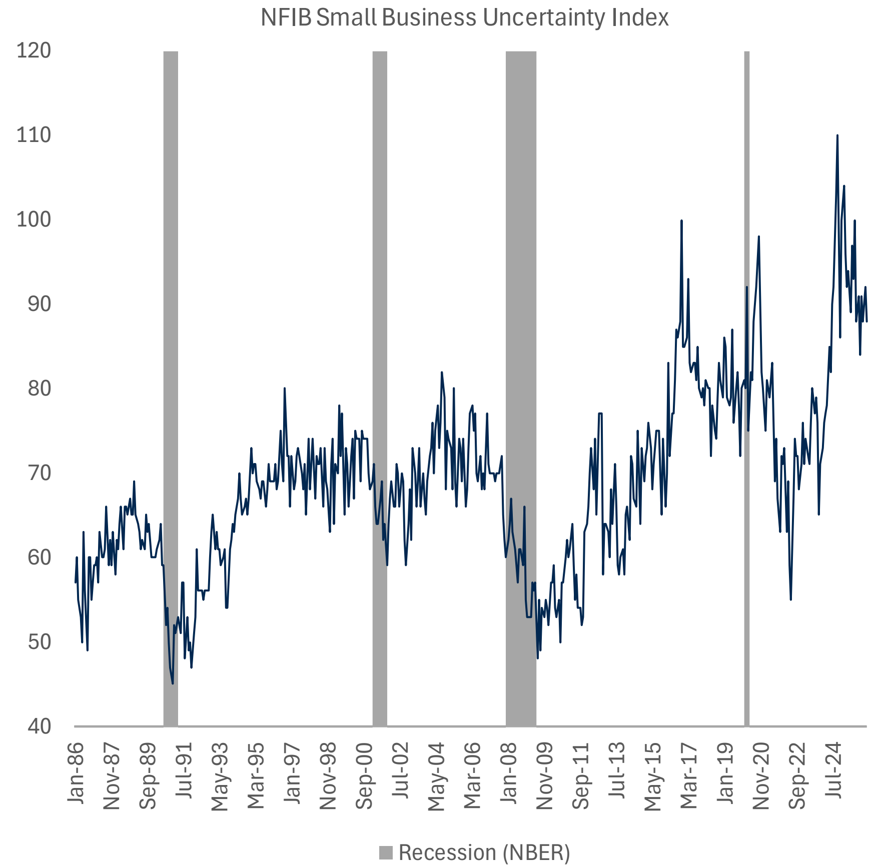


Source: RBC US Equity Strategy, Bloomberg. Russell, S&P. As of 5/13/2026.

Small Business Optimism Flat While Uncertainty Ticked Down a Little in the Latest NFIB Update

Optimism and uncertainty are both below their latest highs, but have not collapsed.

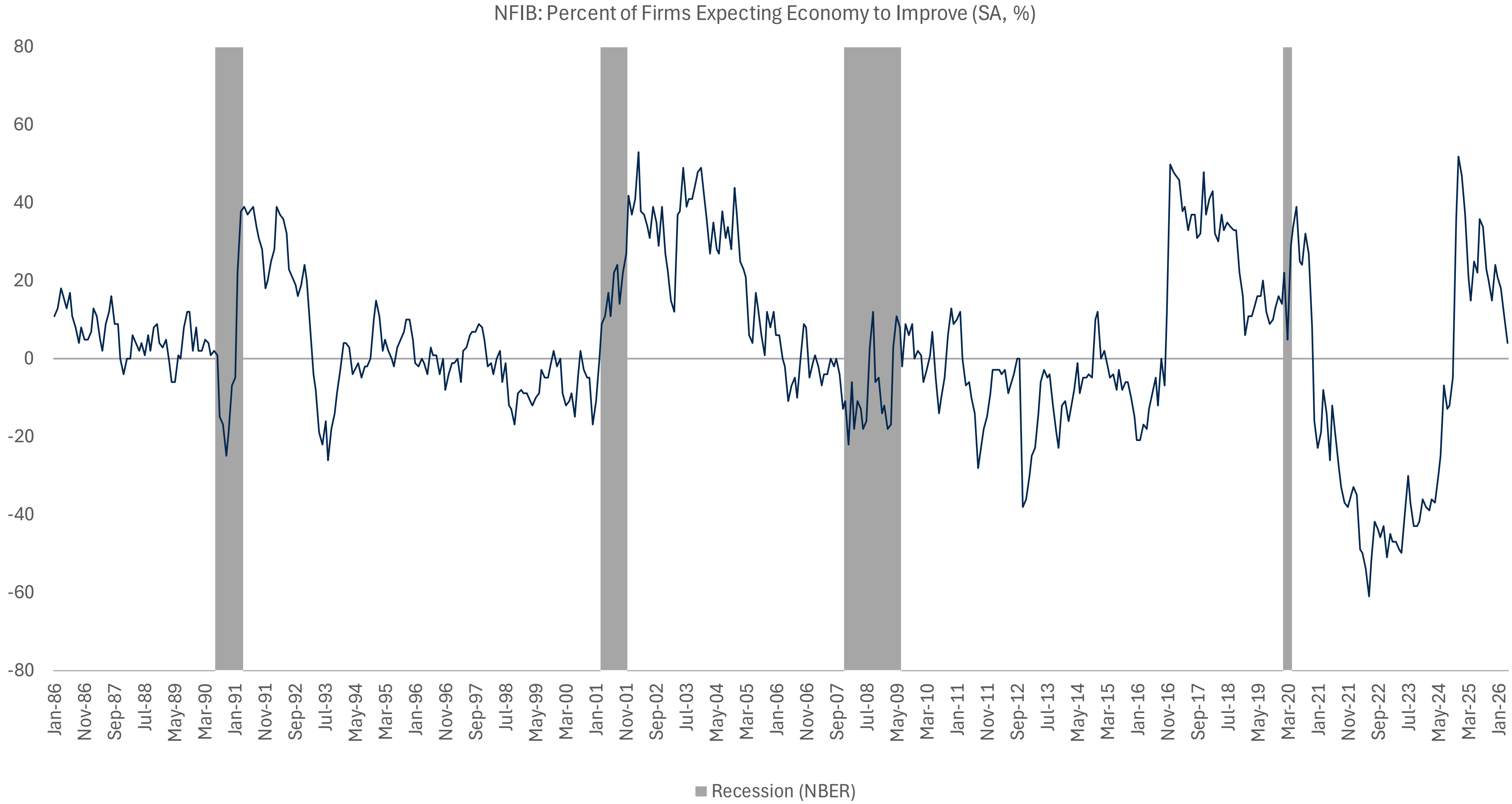




Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

Economic Outlooks By Small Businesses Deteriorating Again in the Latest Update

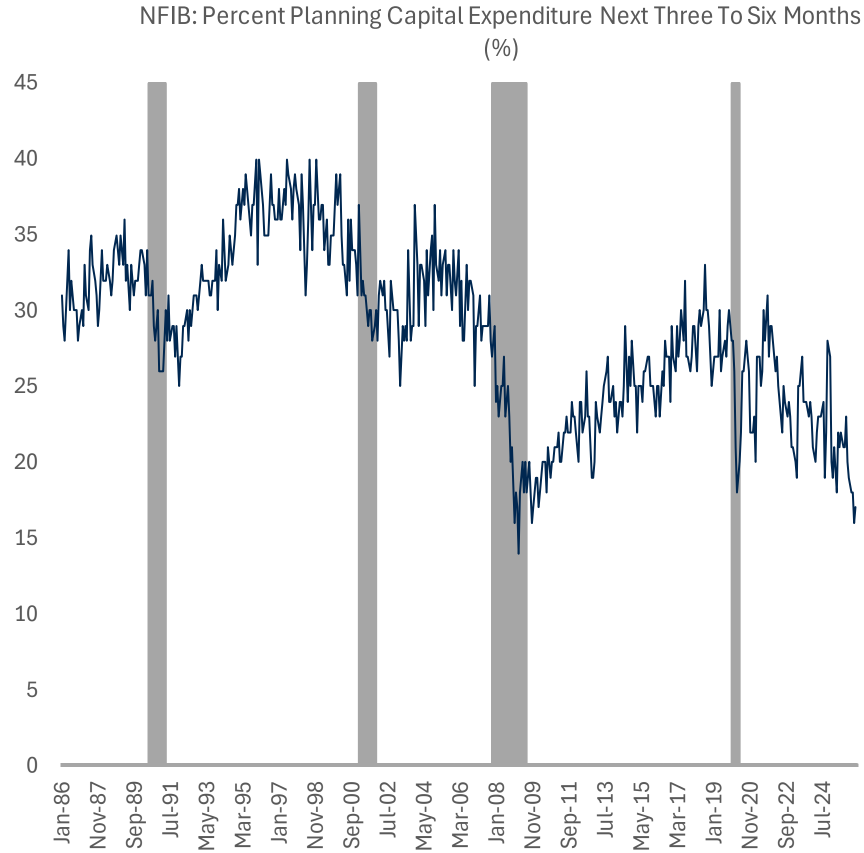
Those expecting the economy to improve are below recent peaks, which were consistent with the peaks in past cycles.

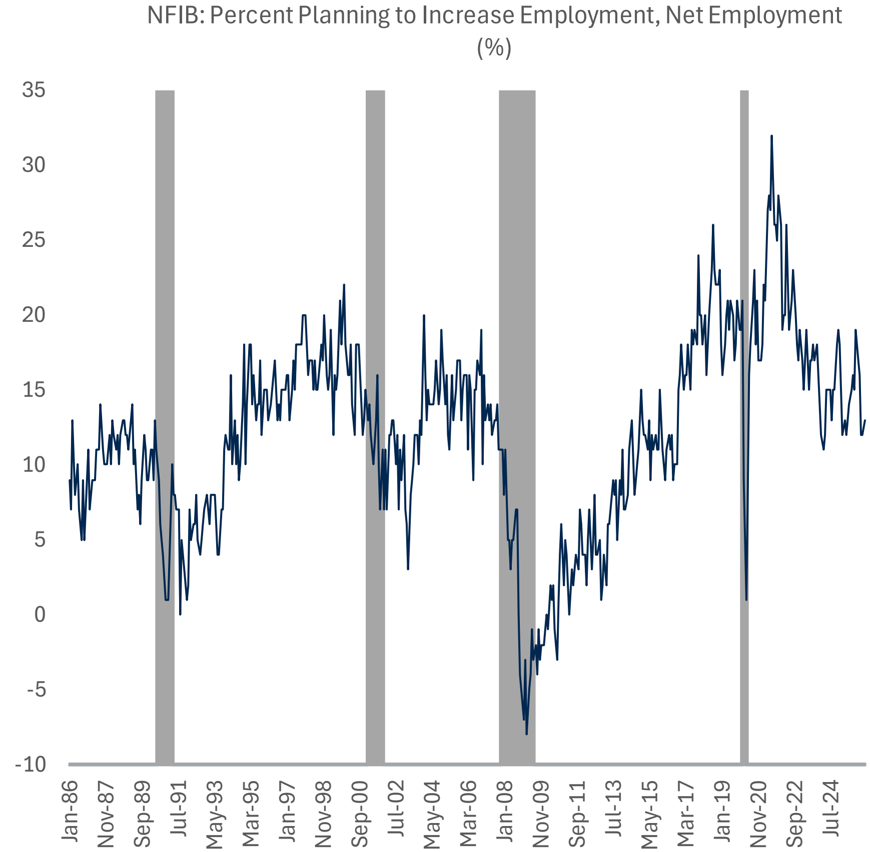


Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

Small Business Capex Expectations Ticked Up Very Little After Several Months of Weakness

Small business employment expectations also ticked up in the latest update but remained relatively weak.

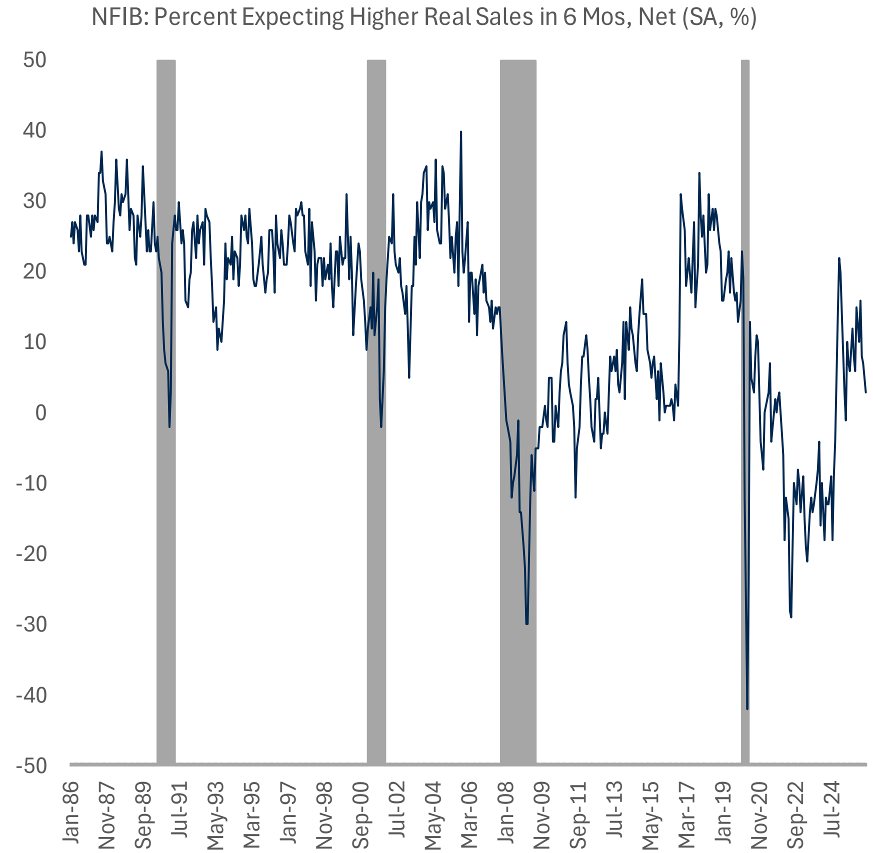


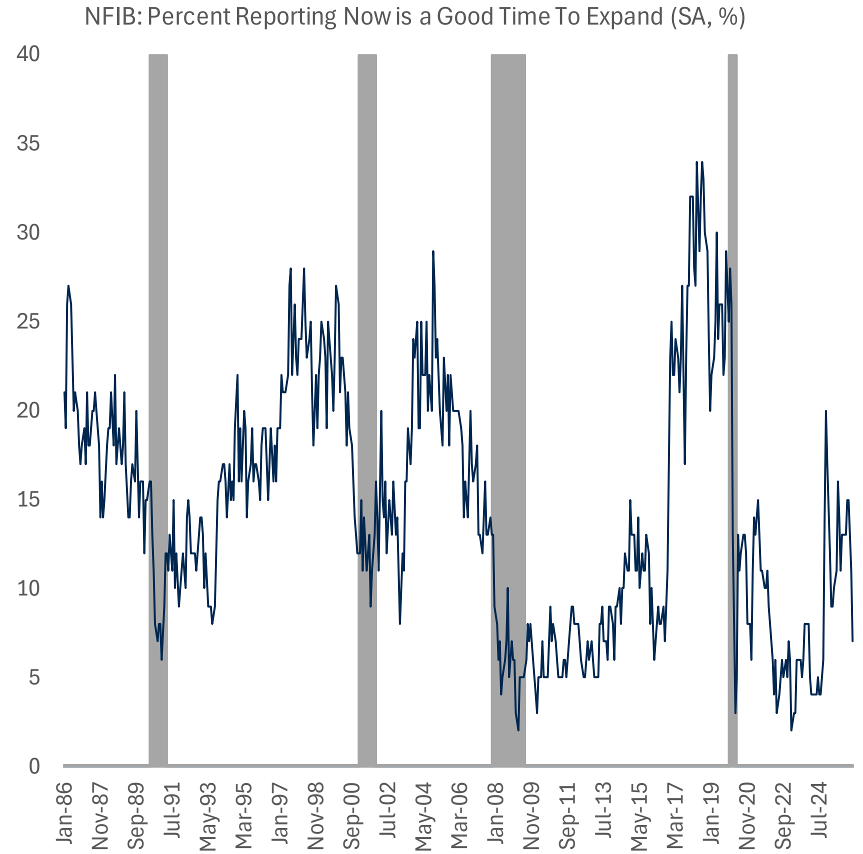


Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

The Percent of Small Businesses Expecting Higher Sales in Six Months Ticked Down

Small business optimism regarding expansion plans also declined.

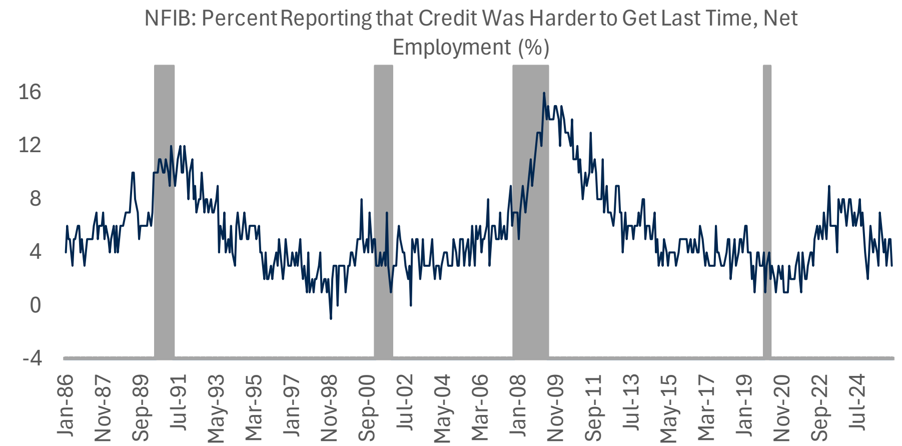


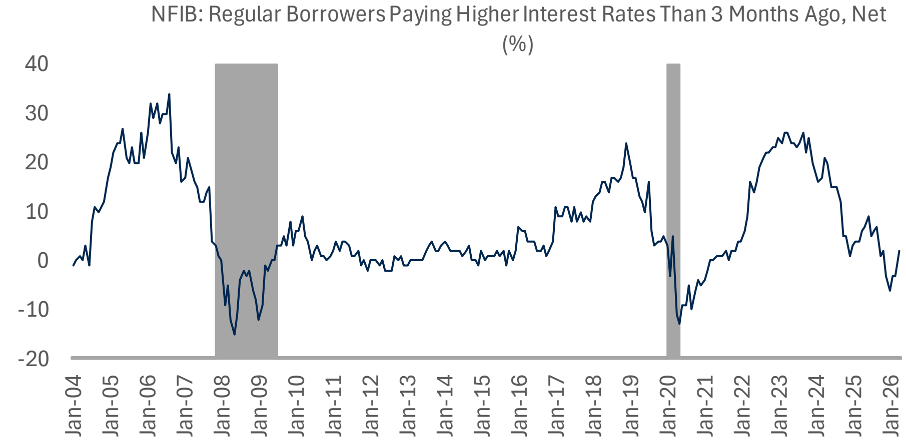


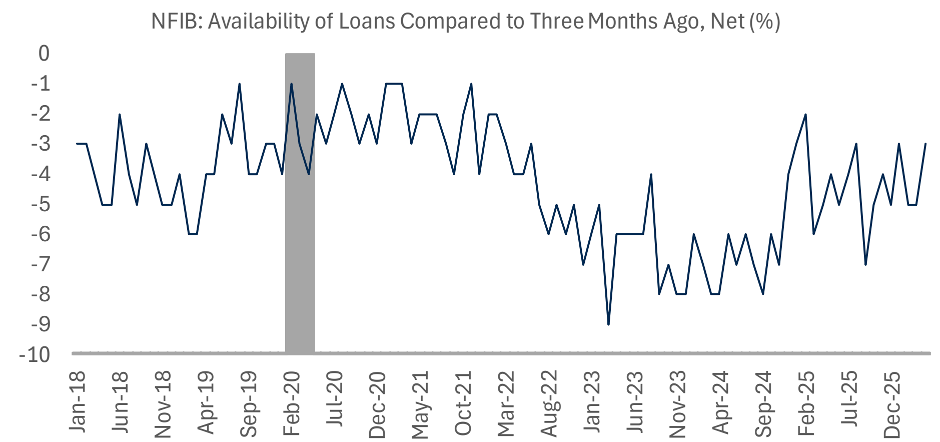
Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

Small Businesses Say Lending Conditions Are Slightly Better

Those saying credit has been harder to get ticked down a little. The number of borrowers paying higher interest rates than three months ago also ticked up. The availability of loans has increased for small businesses.



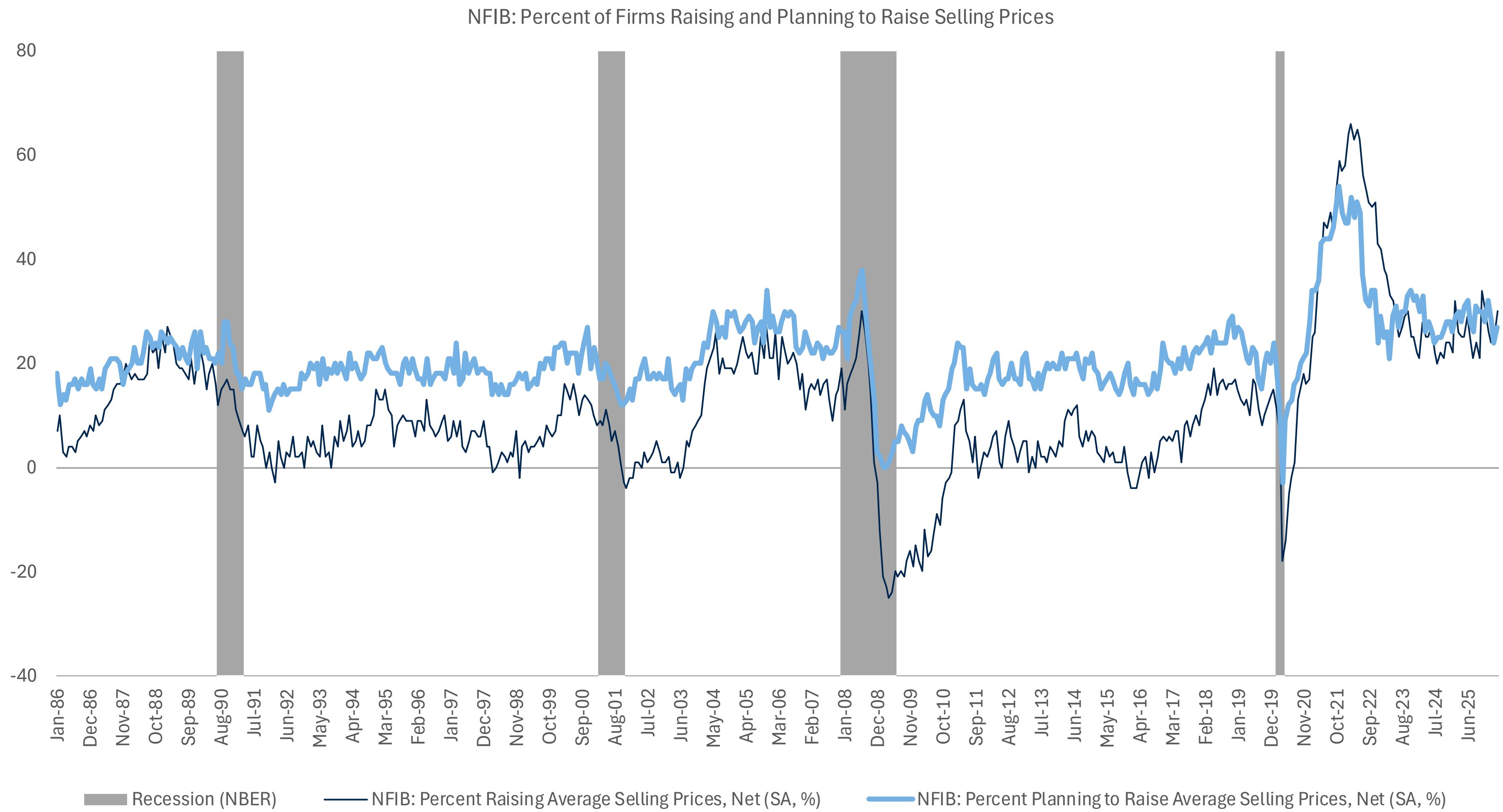




Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

Uptick Seen in Percent of Small Businesses Currently Raising Selling Prices

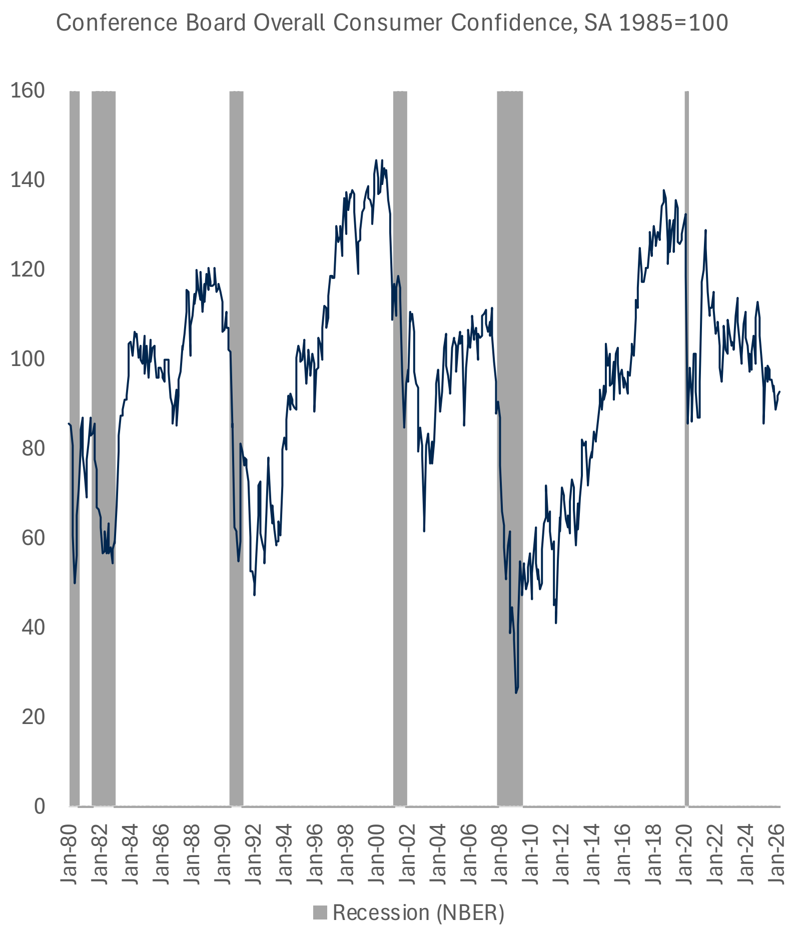
The percent of small businesses planning on raising selling prices also ticked up. Both remain elevated vs. pre-COVID levels.

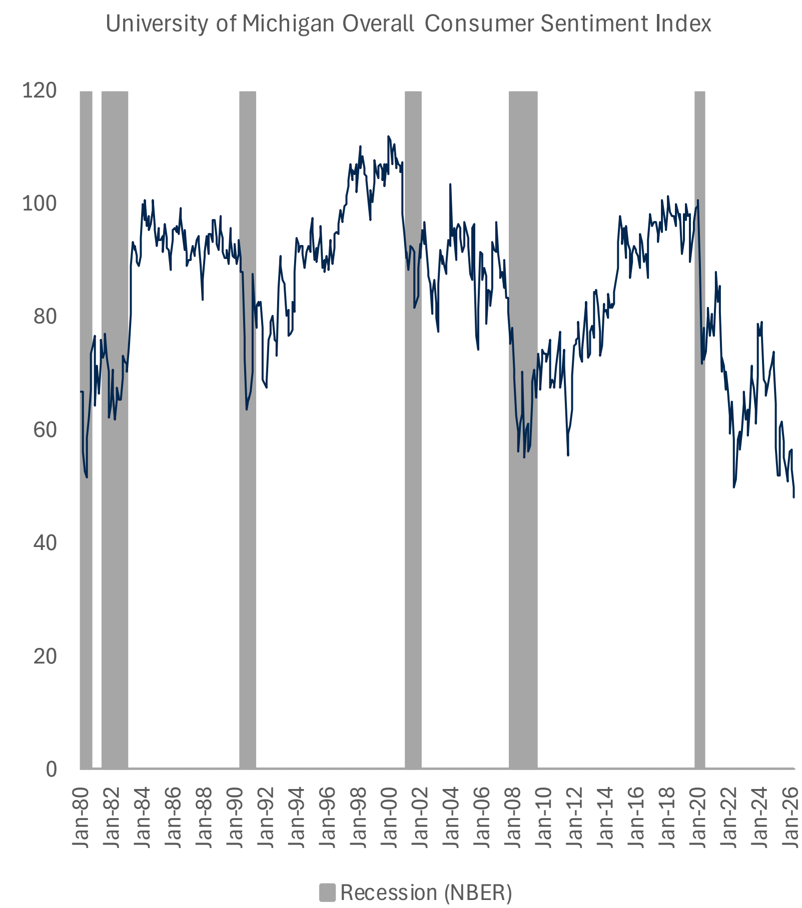


Source: RBC US Equity Strategy, Haver Analytics; data through April 2026

Consumer Confidence / Sentiment Has Been Weak, and Is Not Showing Signs of Recovery

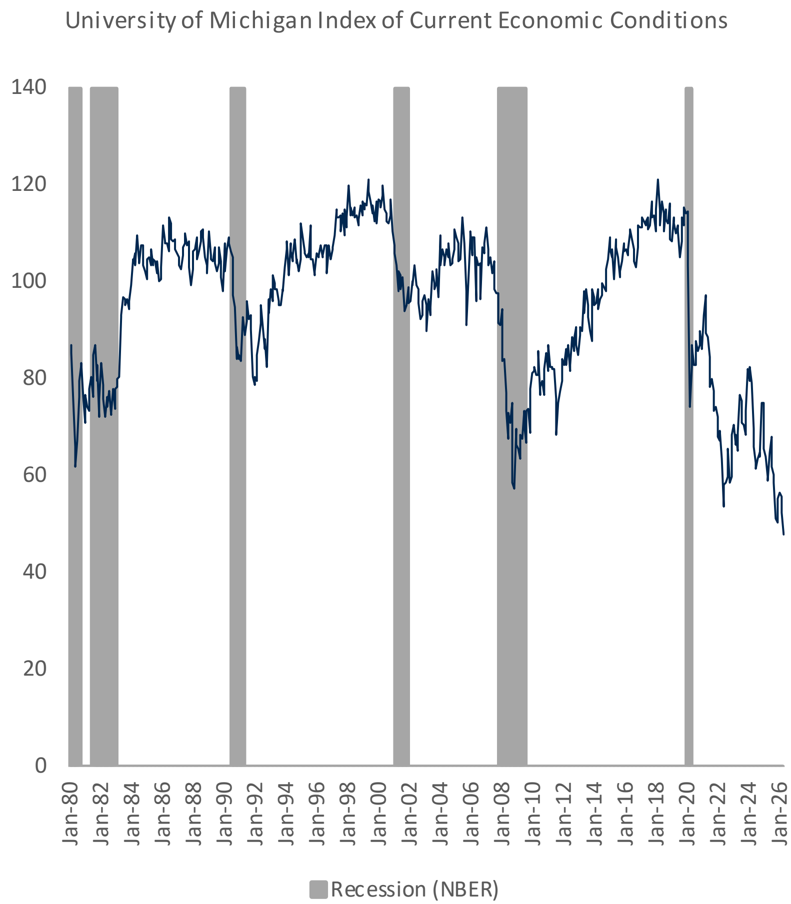
- Consumer sentiment on the University of Michigan survey broke slightly below prior 2025 and 2022 lows in the November update. After a period of attempted stabilization, May preliminary data showed renewed signs of weakness, with sentiment at 48.2, a new post-COVID low.
- Conference Board consumer confidence – which is only through April – has shown more signs of stabilization, but this could change in the next update. For the month of April, overall confidence came in at 92.8.

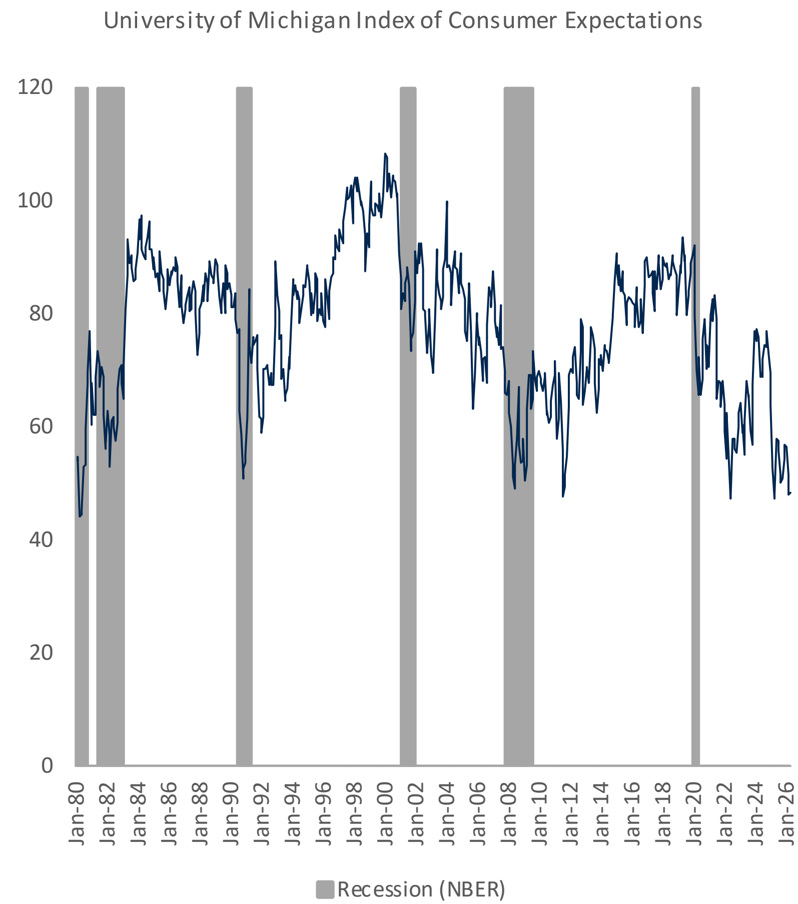




Source: RBC US Equity Strategy, Haver Analytics, Bloomberg. UMich data as of May 8, 2026; Conference Board data through April 2026.

Current Economic Conditions Stalled and Expectations Weakened in the Latest U Mich Survey

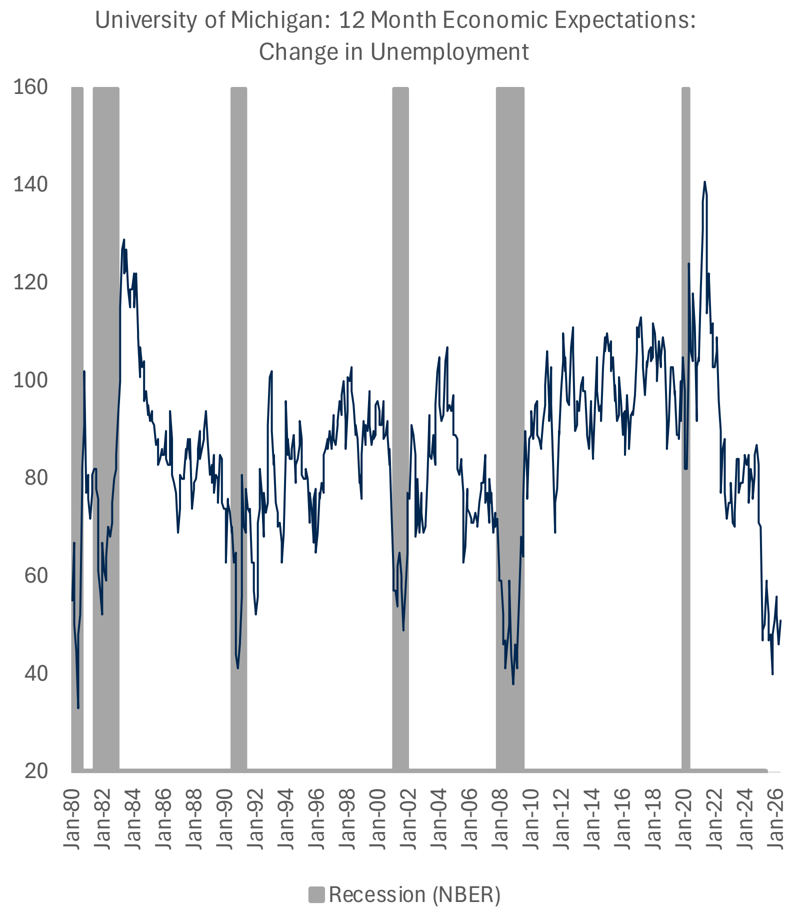


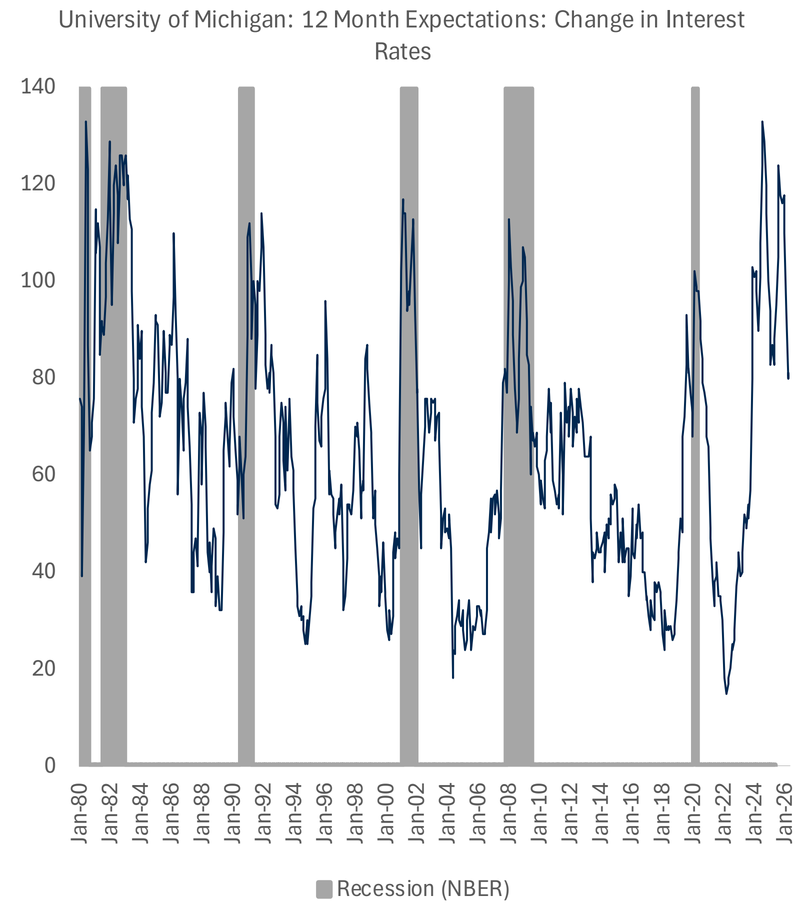


Source: RBC US Equity Strategy, Haver Analytics; latest available data as of May 8, 2026.

Consumer Views on Employment Have Deteriorated, Expectations for Lower Rates Have Come Down

- Employment views on this survey are near recession/GFC lows.



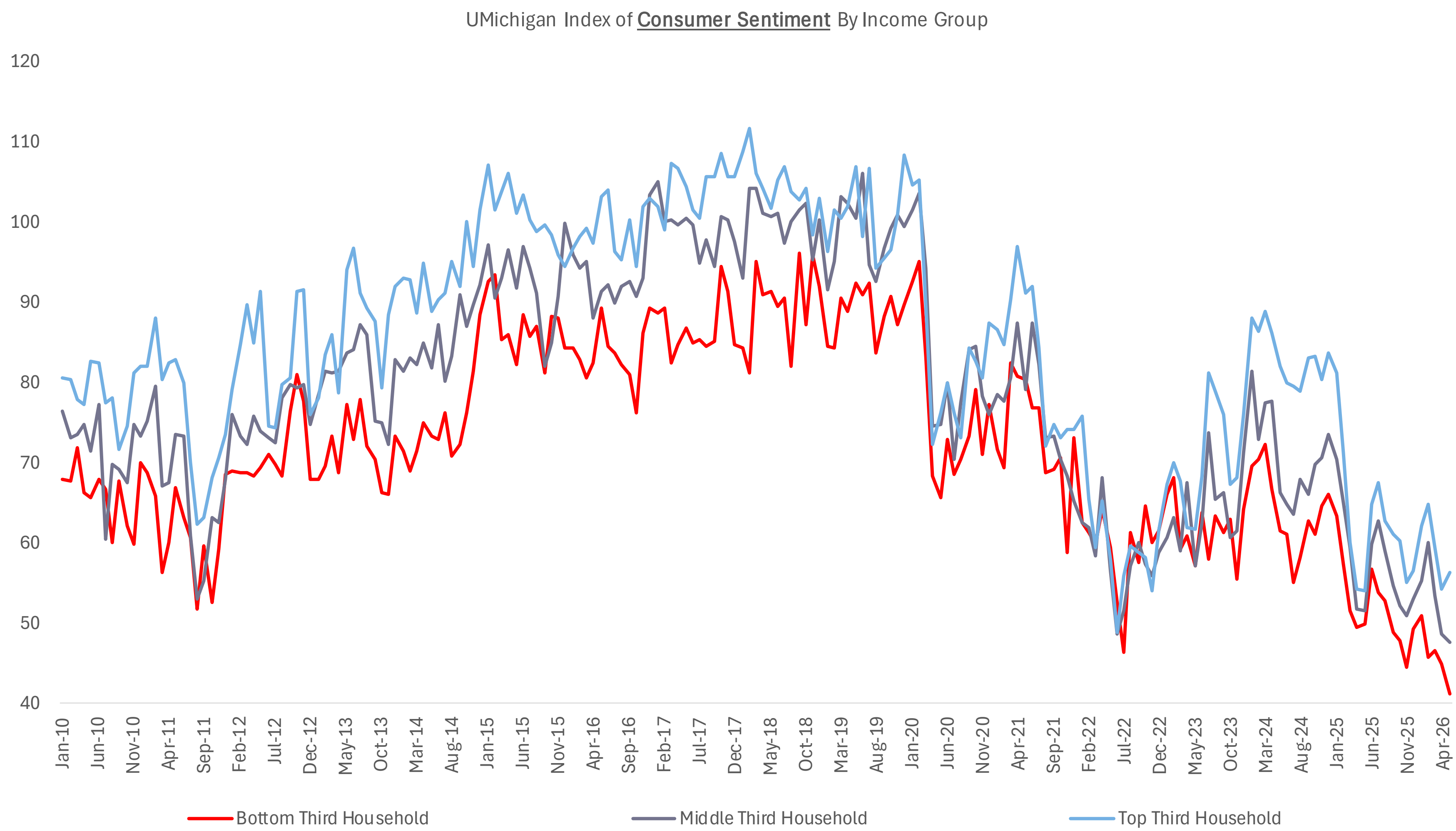


When this time series is moving up, it represents a pick-up in those expecting lower interest rates.

Source: RBC US Equity Strategy, Haver Analytics; latest available data as of May 8, 2026.

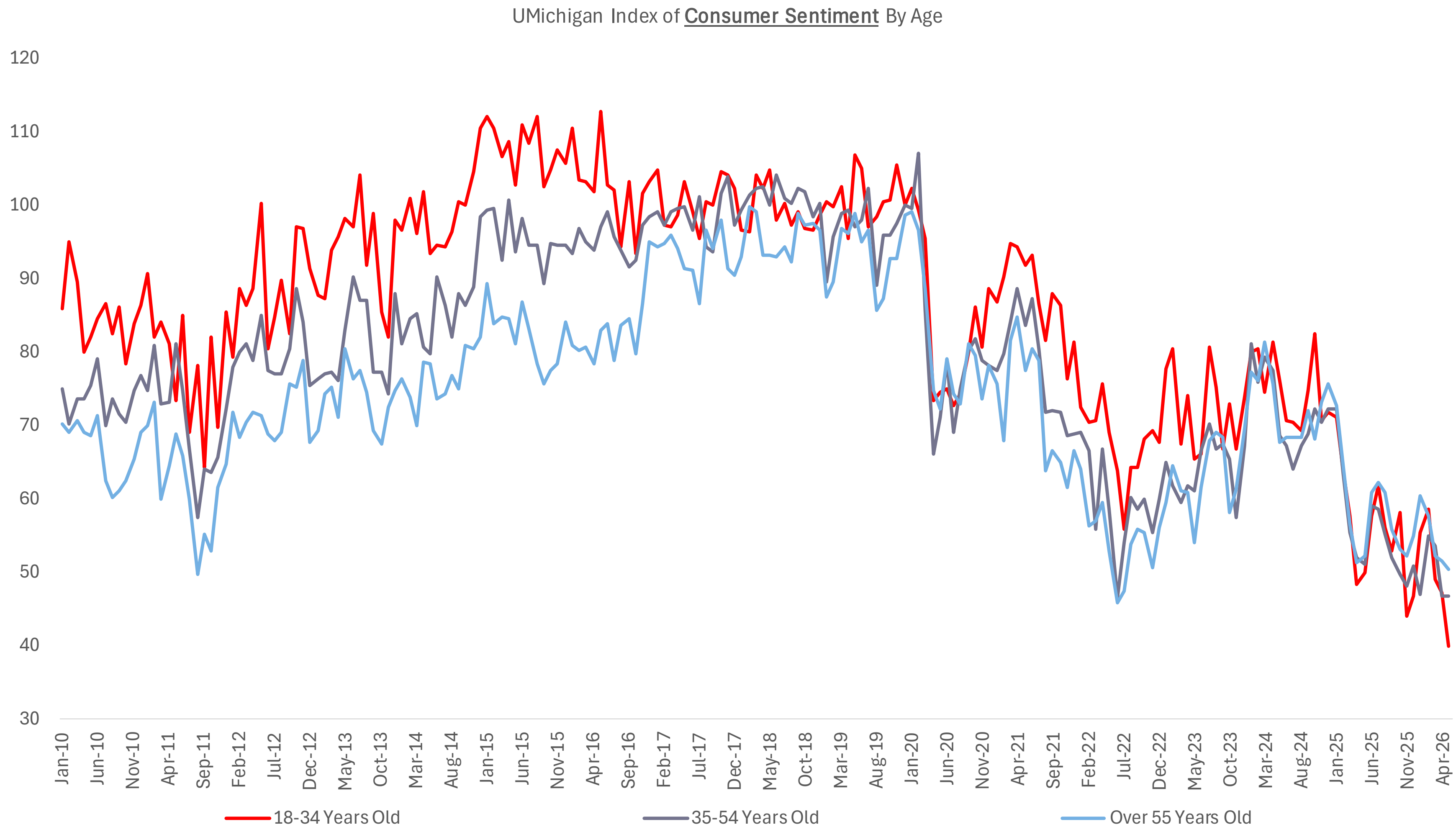
Consumer Sentiment Fell for the Bottom and Middle-Income Cohorts in May's Update

The top third income group was the only one that saw a small uptick, while the bottom third is below its 2022 lows.



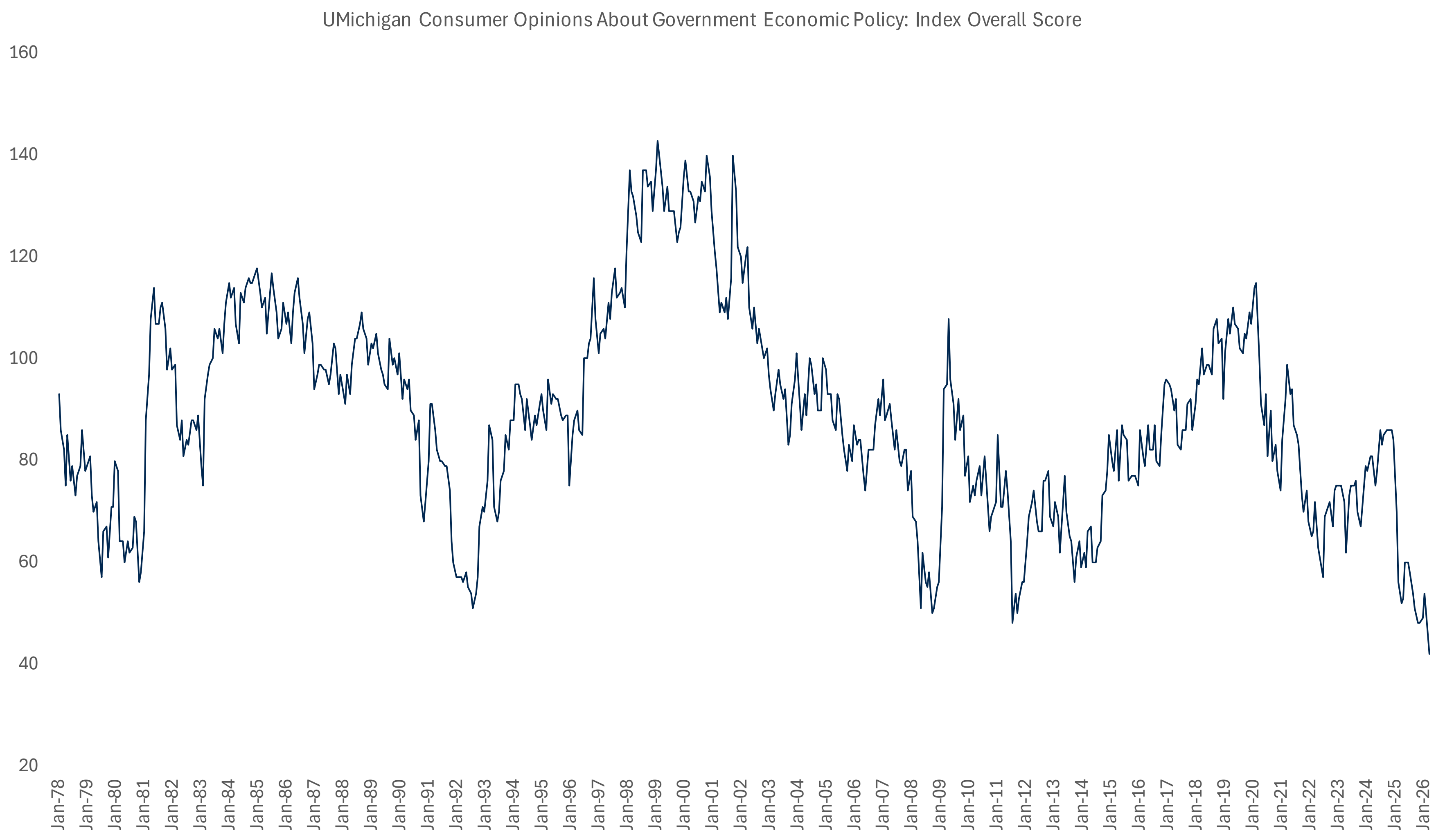
Source: RBC US Equity Strategy, Haver Analytics; latest available data as of May 8, 2026.

Consumer Sentiment Declined For All Age Cohorts



Source: RBC US Equity Strategy, Haver Analytics; latest available data as of May 8, 2026.

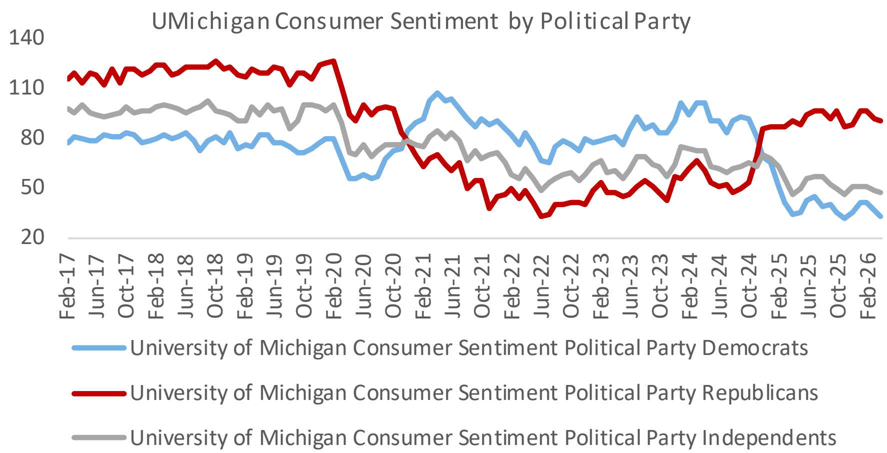
Consumer Opinions on Government Policy Near Historical Lows, Ticked Down in Latest Update

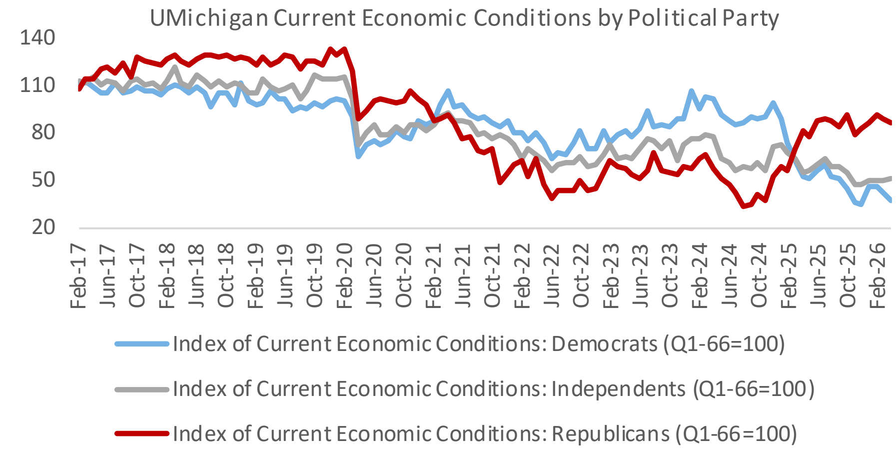


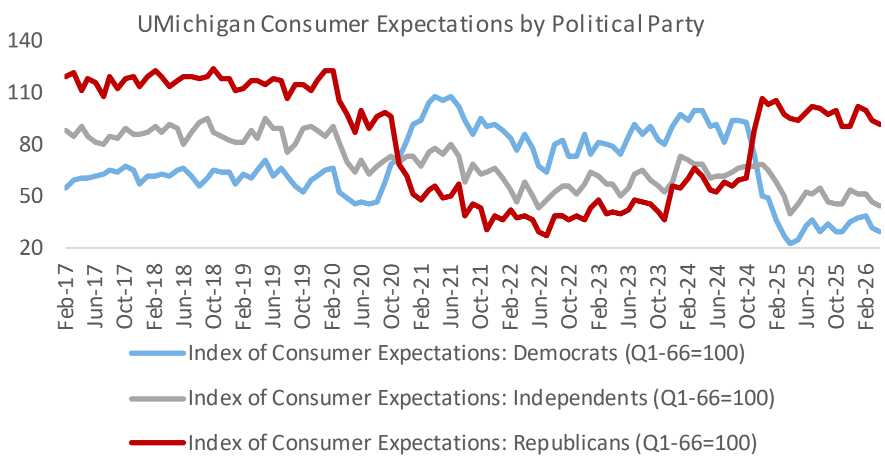
Source: RBC US Equity Strategy, Haver Analytics; as of May 8, 2026

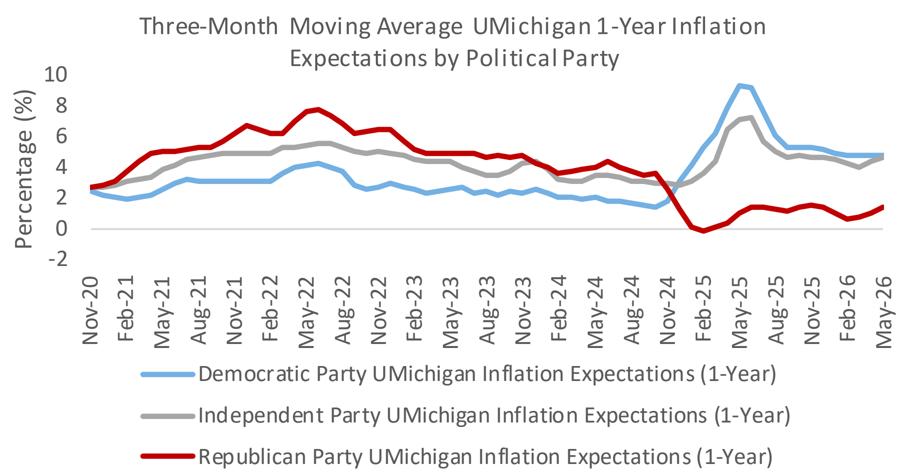
Trends by Political Cohort in the U Mich Consumer Sentiment Survey

- All three partisan cohorts have fallen in terms of overall sentiment and expectations.
- On current conditions, Independents have stabilized but both Democrats and Republicans have fallen.
- Inflation expectations appear to be easing for Democrats but ticking up slightly for the Republican and Independents cohorts.









Source: RBC US Equity Strategy, Bloomberg; as of May 8, 2026

Small Caps Had Benefited from Improving Enthusiasm on the US Economy

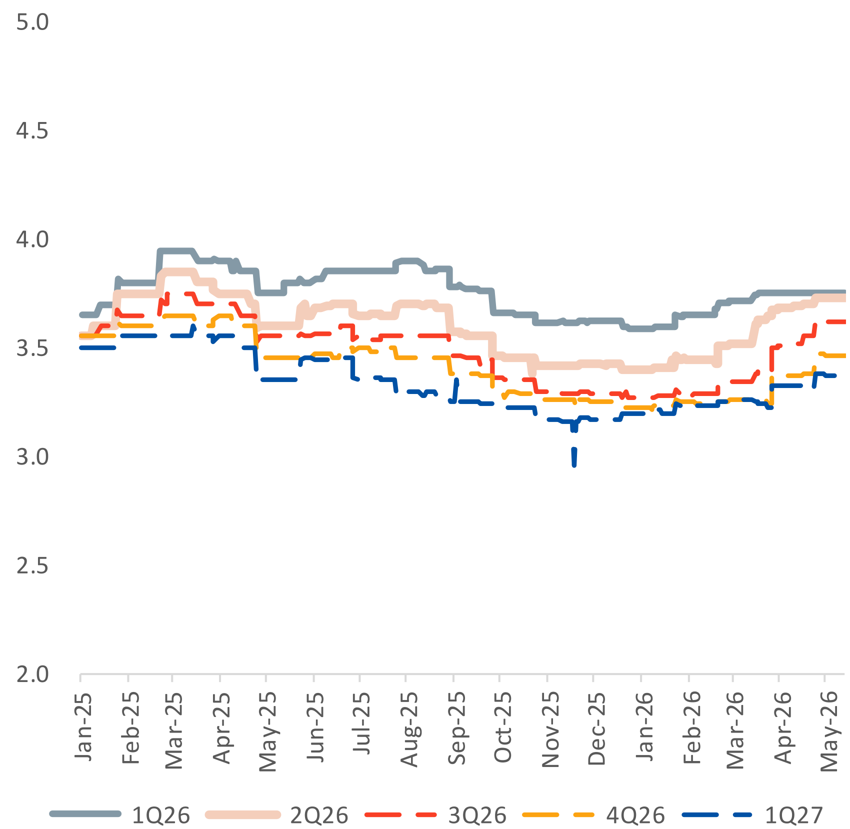
- In recent years, Russell 2000 performance relative to S&P 500 performance – our preferred way to gauge Small/Large relative performance – has been linked to shifts in GDP expectations in the US for 2025 and more recently 2026. Small has lagged as economic growth expectations cooled off.
- Late-2025 strength in Small Cap leadership occurred alongside a sharp pickup in domestic economic expectations. 2026 expectations have come down, while we have seen some momentum in Small Cap leadership of late. It's worth noting that 2027 GDP expectations have been relatively flat.
- Note that 2026 full-year GDP forecasts have been trimmed in recent updates as Middle East peace talks continue.

Note: The RBC US Equity Strategy team does not authorize the reproduction of its published charts and is not able to share their underlying data due to license restrictions with our vendors.
Source: RBC US Equity Strategy; Bloomberg, S&P, Russell, as of 5/13/26

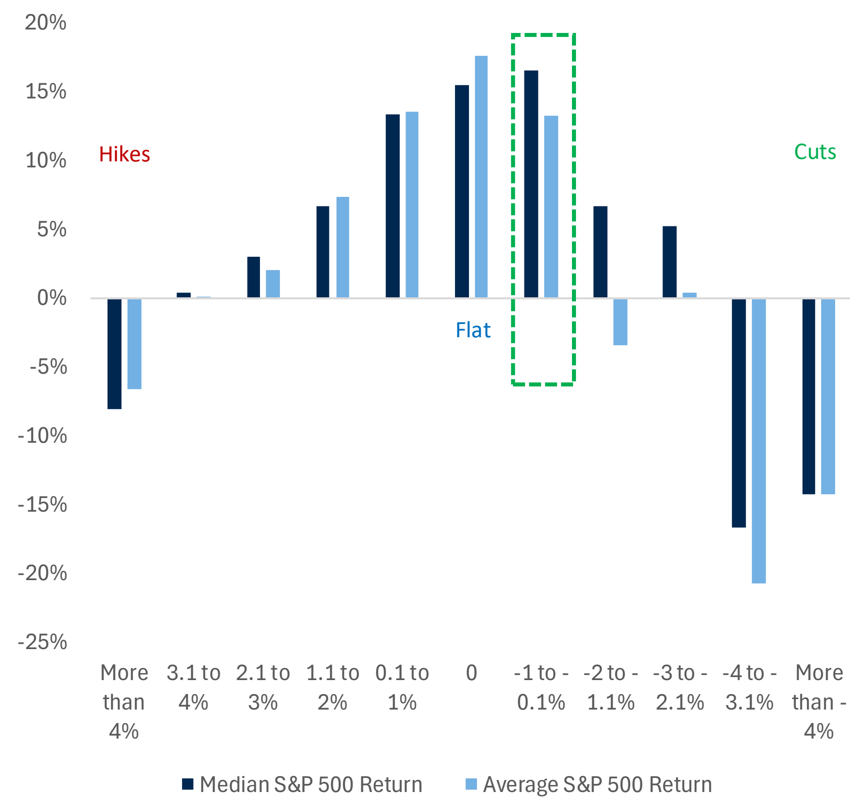
How We Think About Fed Moves in the Context of Longer-Term US Equity Market Moves

- Historically, when the Fed has made modest cuts in a 12-month period (that amount to 1% or less), the S&P 500 has gone up by 13.3% on average. When the Fed does nothing or hikes modestly, returns tend to be similar. Deeper cuts during a 12-month window tend to be accompanied by weaker equity market returns or declines.
- The published consensus per the ECFC function on Bloomberg currently points to between one and two cuts through 1Q27. With this in mind, we are keeping in place the assumption in our 12-month S&P 500 price target process that Fed expectations are signaling a 13.3% return in the index, the same core assumption that has been in place in our process over the past few months. It's worth noting, however, that RBCCM's US Rates Strategy team is no longer expecting any cuts in either 2026 or 2027 per their mid May forecast update. Previously, they had been looking for one cut in early 2027.
- Note that if the Fed does not cut over the next 12 months, this would have a minimal impact on our S&P 500 outlook, as S&P 500 moves tend to be slightly stronger (17.7%) when the Fed does nothing in a 12-month time frame. A few hikes, while likely to upset markets in the short term, would also not be onerous to our forecast from the perspective of this model, though we do acknowledge the removal of cuts tends to generate some downside in the US equity market in the short term.

Shifts in Consensus Fed Funds Forecasts
Quarter End, Upper Bound



S&P 500 During Different Fed Backdrops
Based on Returns & Total Fed Moves On a Past 12 Months Time Frame From Jan 1990 to Oct 2025



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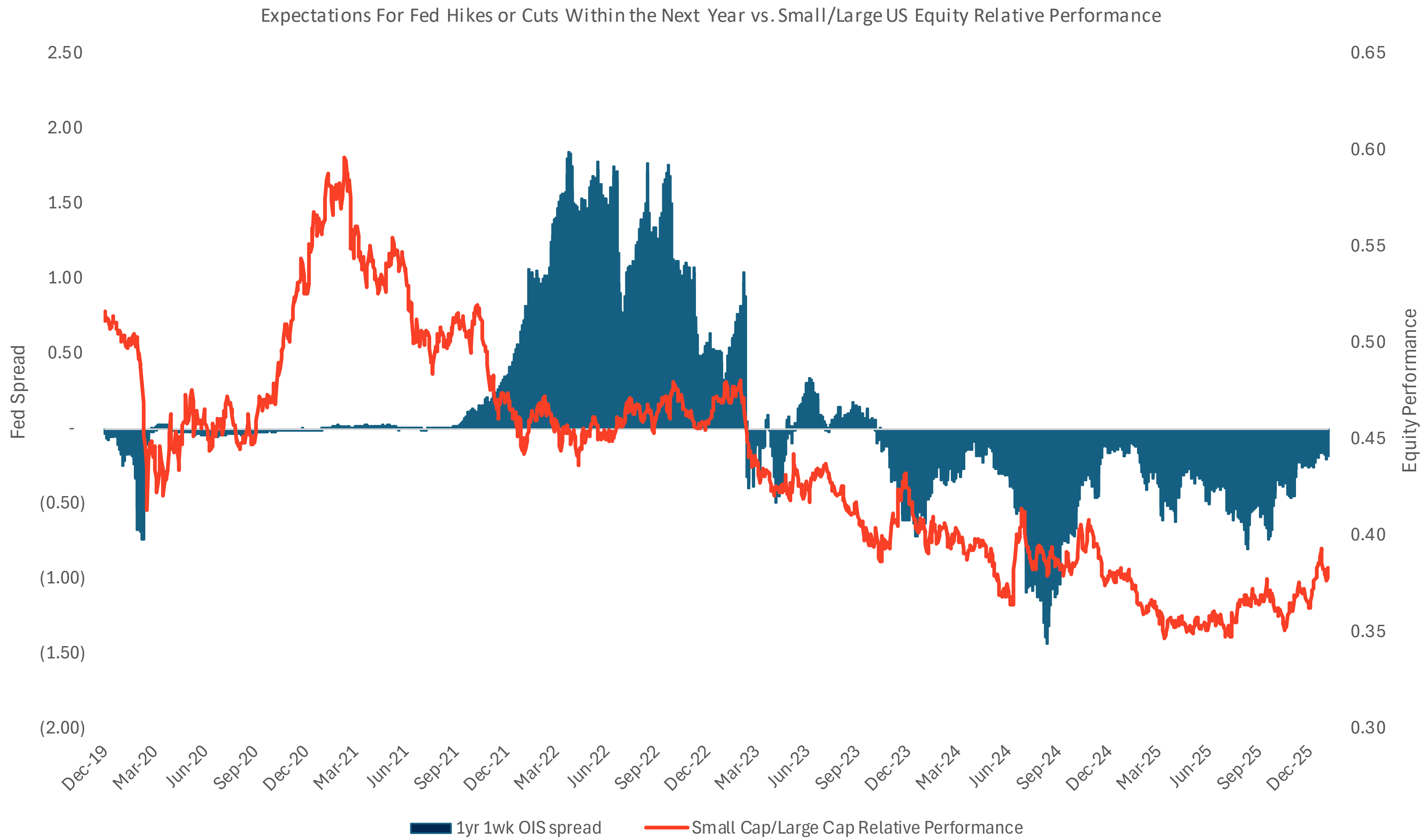
Source: RBC US Equity Strategy, Bloomberg, S&P; as of 5/13/26

The Dialing Up & Dialing Down of Fed Rate-Cut Expectations Have Driven Small Cap Relative Performance

- In recent years, Small Caps tend to outperform Large Caps when Fed-cut expectations have increased, and have underperformed when Fed-cut expectations have eased back or when hikes have gotten priced in. To the extent the situation in Iran results in increased expectations for Fed hikes (which is not the view of RBC's Rates Strategy team), it would be a problem for Small Caps in the short term from this perspective.



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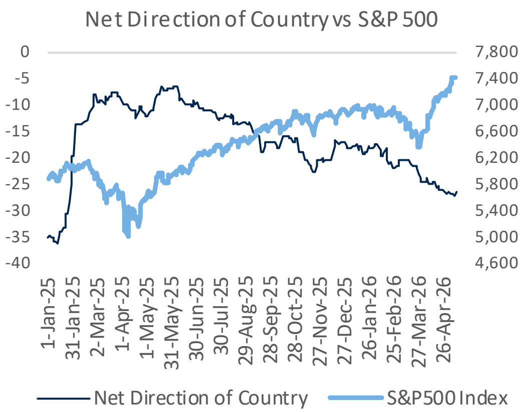
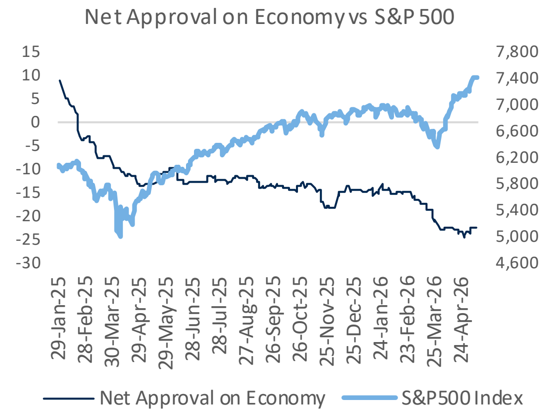
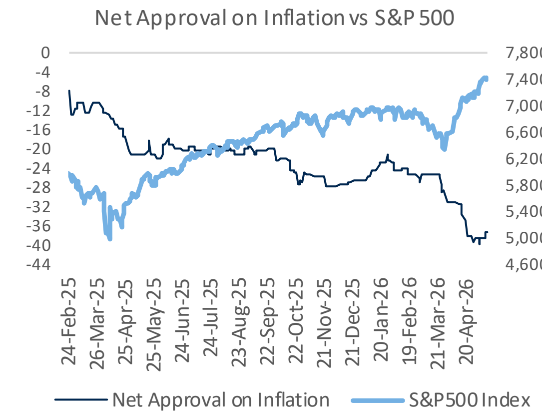
Source: RBC US Equity Strategy, Bloomberg, S&P; through May 13, 2026.

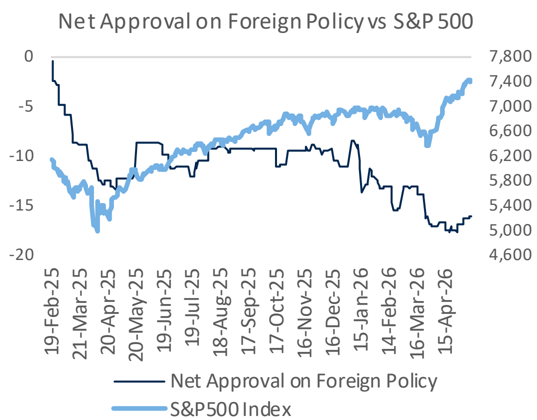
Net Approval Is Improving on a Few Key Policy Issues

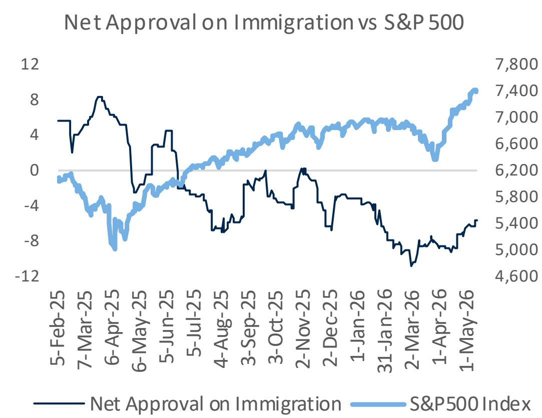
We're seeing net approval move up on the economy, inflation, foreign policy, and immigration in recent updates. Views on crime have edged lower but remain net favorable.

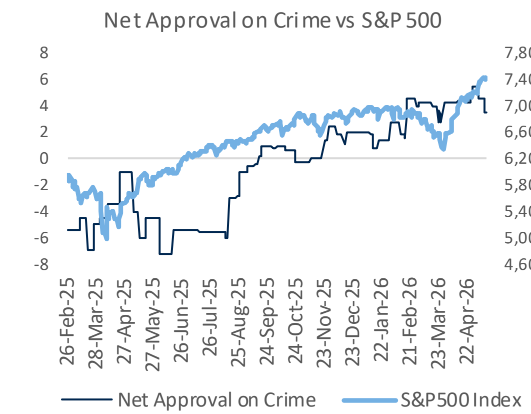












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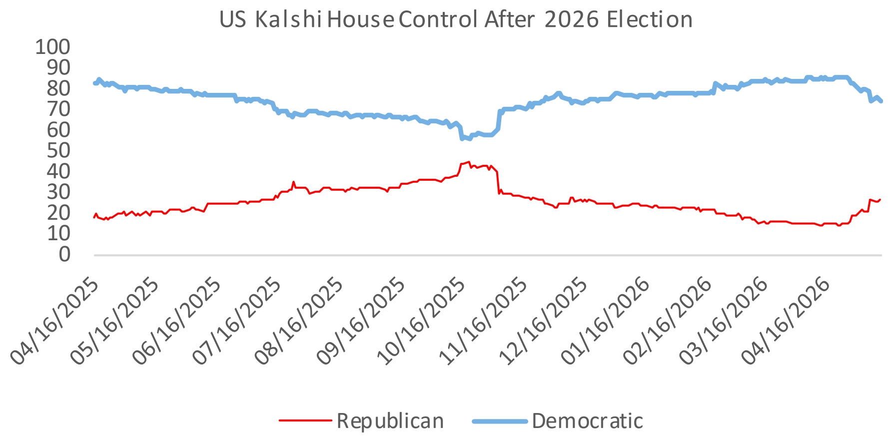
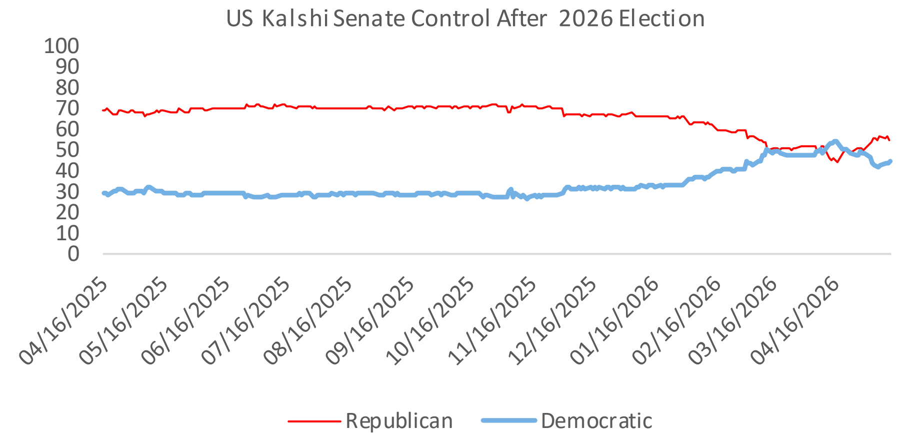
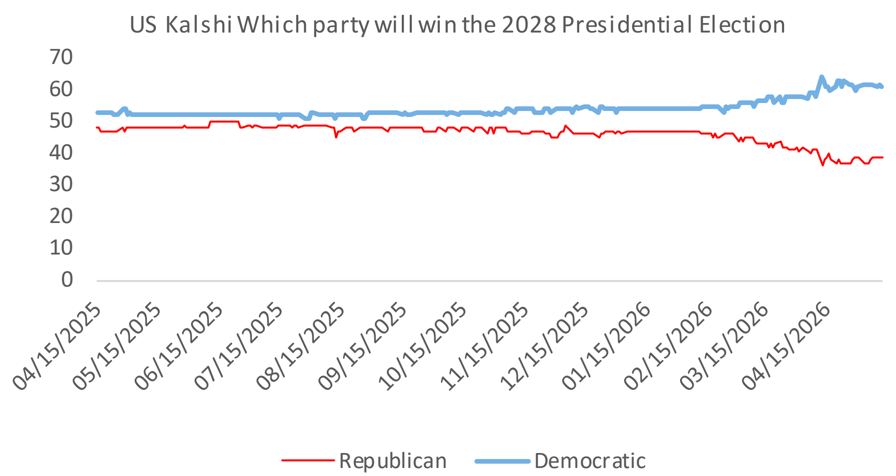
Source: RBC US Equity Strategy; Bloomberg, S&P, as of May 13, 2026

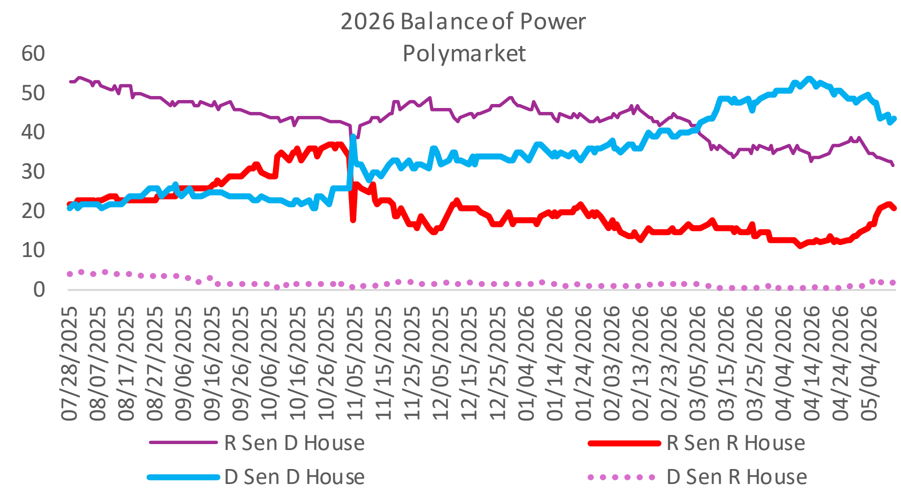
Betting Markets Are Starting to Move Back Toward Republicans for the Midterms

- Currently, betting markets anticipate Democrats will take back the House in 2026 and the White House in 2028, but we have seen expectations for Democratic control of the House erode in recent updates. Views on the Senate had been tied between the two parties, but have recently shifted back in Republicans' favor.
- In Polymarket's balance-of-power scenarios, a blue sweep in the midterms has been in place since the Iran war began, and that remains the case today. It's followed by a Republican Senate/Democratic House scenario, and then the Republican sweep scenario. In recent updates, expectations around the Democratic sweep scenario have fallen, while expectations around a Republican sweep had been moving up. There has been some ebb and flow in the split Congress scenario of late.









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Source: RBC US Equity Strategy; Bloomberg, as of May 13, 2026

Sentiment on Stocks and Trump/Congressional Republicans Have Been Linked

- In 2024, the S&P 500 and Trump net favorability moved in tandem. After Trump took office, S&P 500 performance and Trump's net job approval trended together until the summer of 2025. Then, the S&P 500 became more aligned with betting market expectations for a Republican sweep in the midterms.
- The November-2025 dip in the S&P 500 saw the stock market become aligned with all three of these gauges of political sentiment again.
- The 1Q26 weakness in the S&P 500 coincided with low Trump approval/favorability levels and lowered expectations for a Republican sweep in the midterms. The recent bounce-back in the S&P 500 has come with some improvement in those metrics.
- What we've noticed though, is that there's also been an improvement in anticipation of a Republican sweep scenario, making us wonder if increased expectations for that scenario may be contributing to recent strength in the US equity market.

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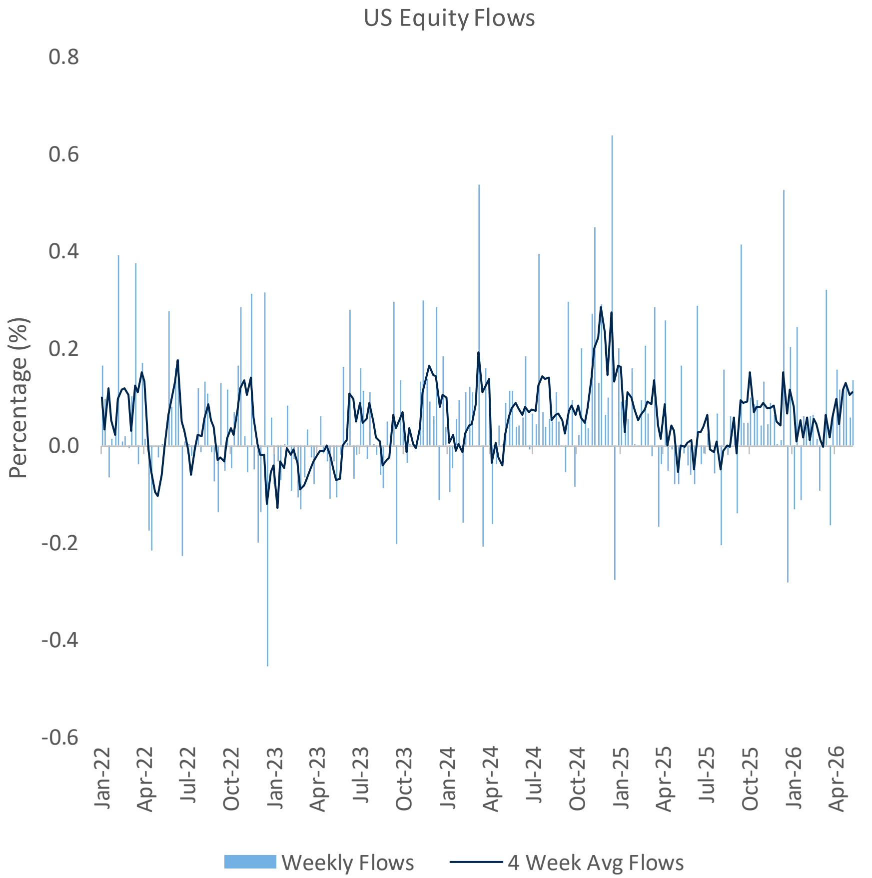
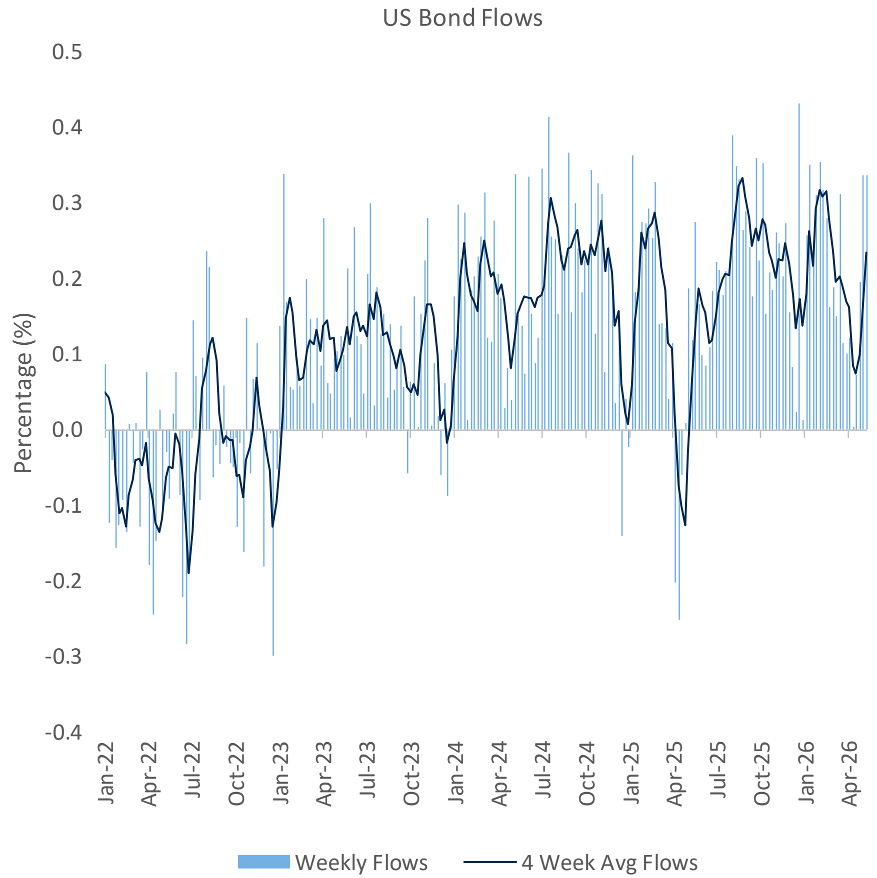
Source: RBC US Equity Strategy, S&P, Bloomberg; as of May 14, 2026 (SPX) and May 14, 2026 (polling/betting market)

US Equity Fund Inflows Are Improving, and Firmly in Positive Territory Again

- US equity funds saw inflows return on the weekly EPFR data in 2H25, but well below the levels in place in late 2024 and early 2025. We saw modest outflows on a weekly basis in early 2026, but in recent weeks we are seeing some inflows return and gathering steam.
- Meanwhile, US bond flows have been strong this year. They recently have picked up some momentum again after a brief period of deceleration.





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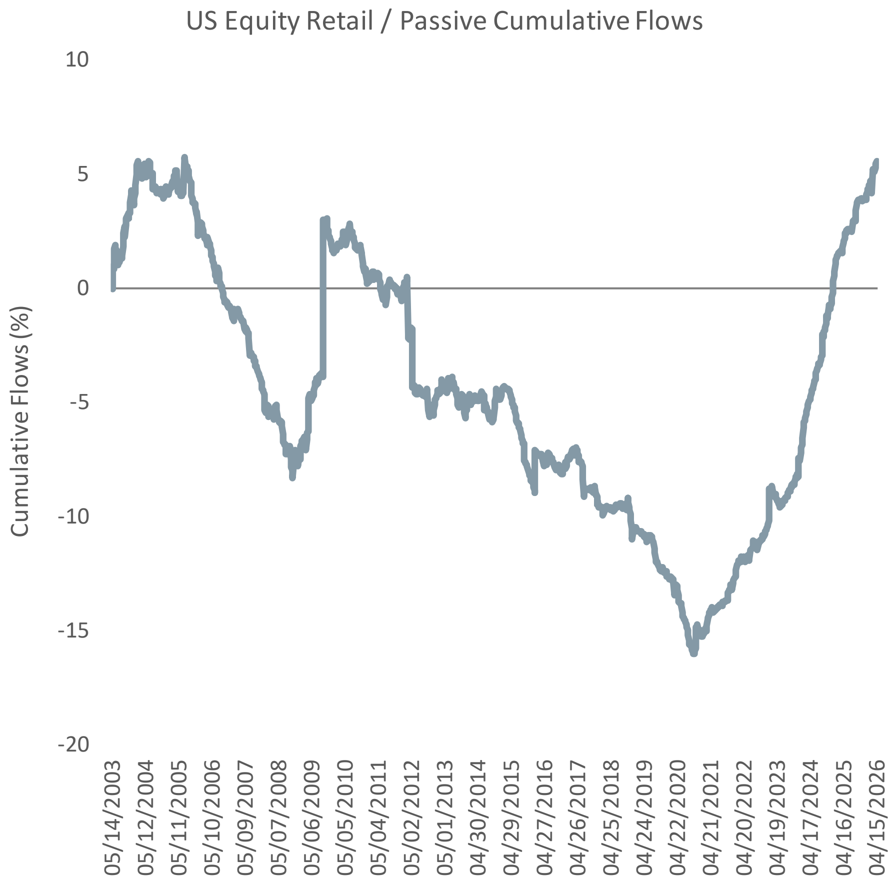
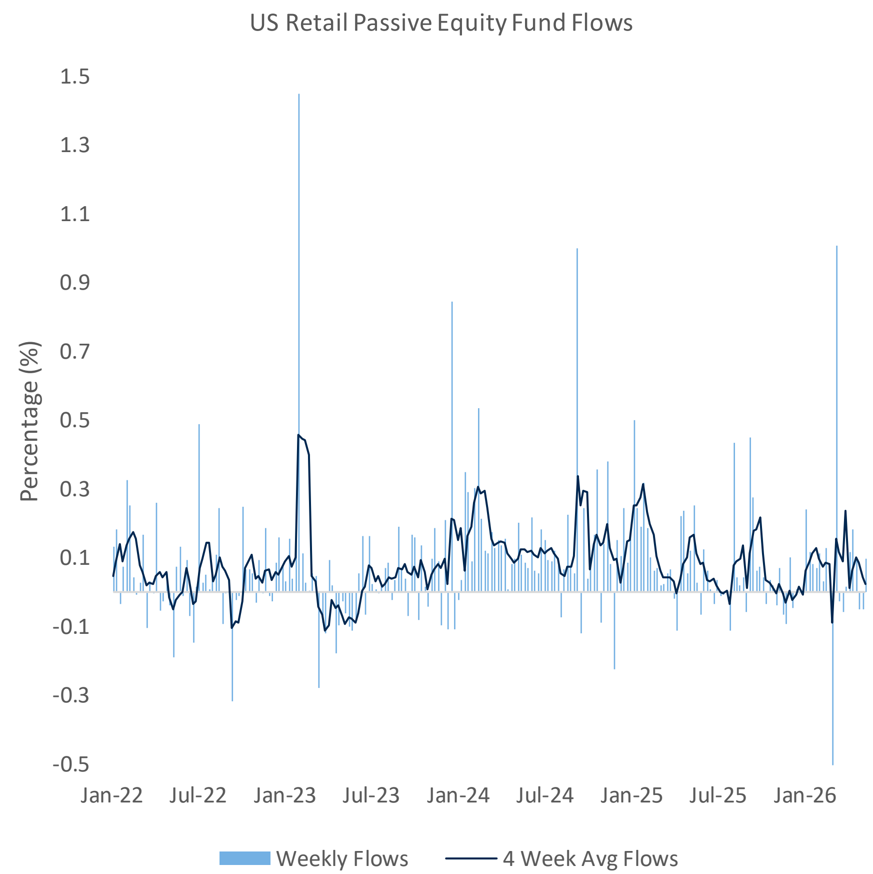
Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

Passive Retail Flows Have Been Choppy in Recent Updates

- Flows to passive retail funds have ebbed and flowed since the start of this year. In the latest weekly updates, small inflows were seen, which followed a few weeks of modest outflows.





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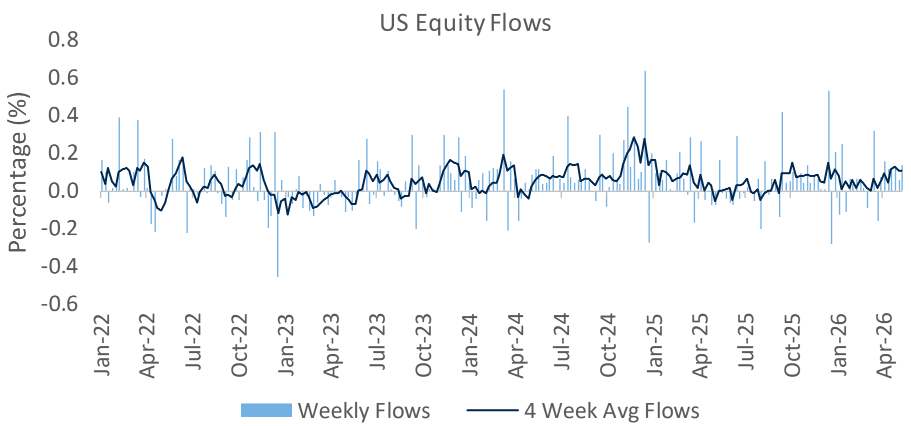
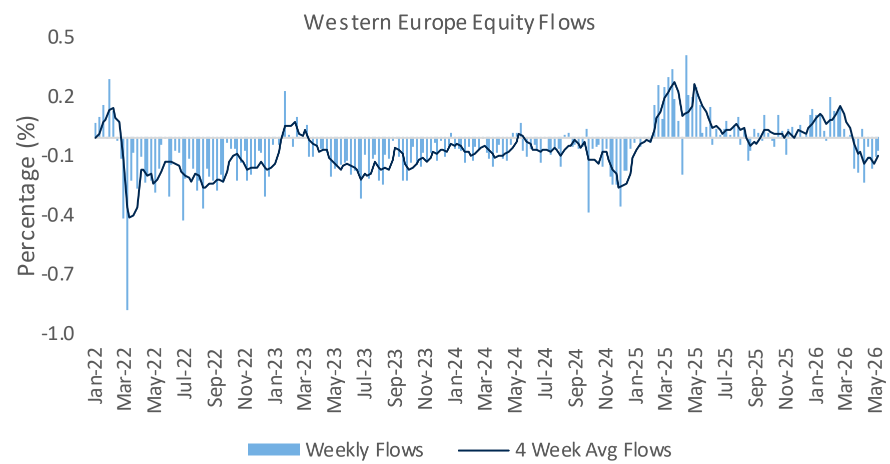
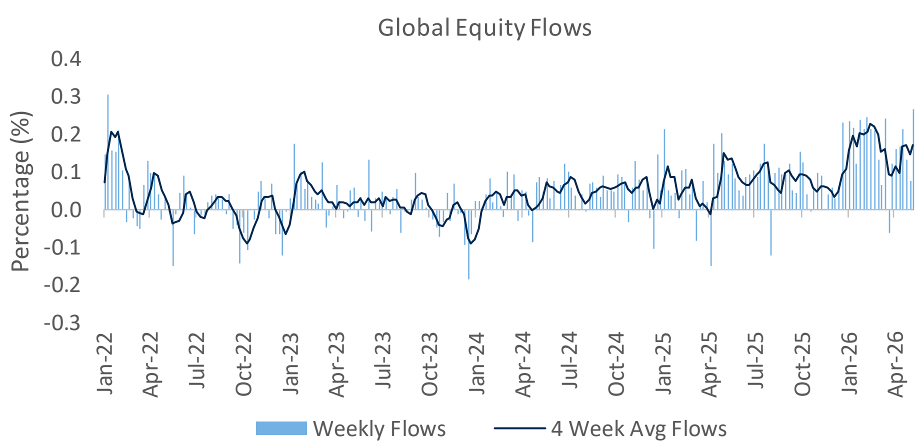
Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

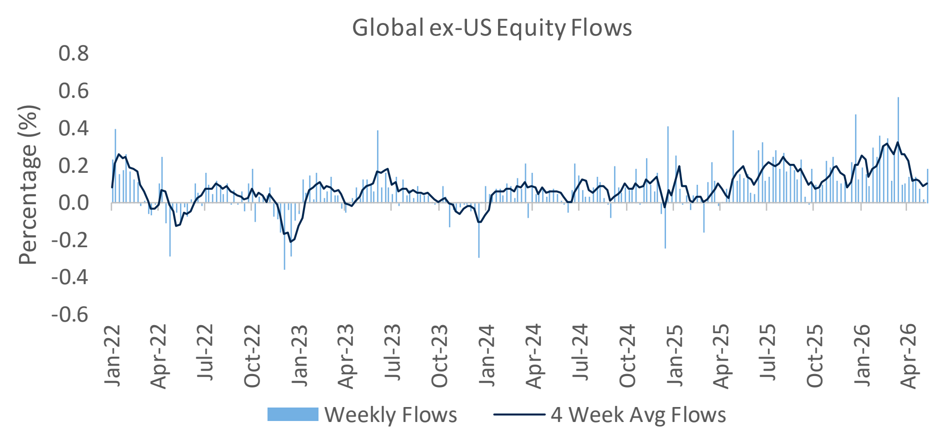
Improving US and Global Equity Flows Seen Alongside Weaker European & Global ex-US Flows

- Western Europe flows got off to a good start in 2026 as part of the rotation in leadership that occurred within US equities, but we are seeing clear outflows over the past few months as a "buy the USA" trade took hold as the war in Iran broke out. Western European flows have not shown any sign of improvement in recent updates.
- Flows to global equity funds are showing strength again. Flows to global ex US equity funds are weaker and are off their highs, but unlike Western Europe are still positive.









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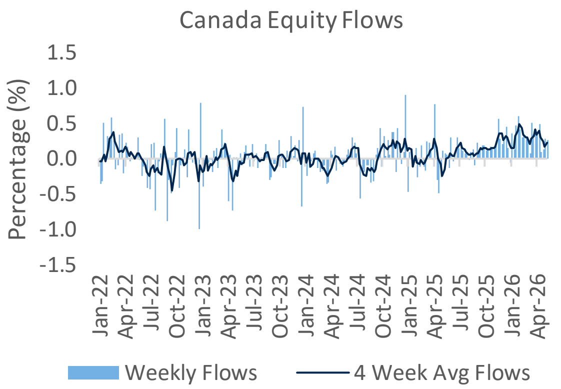
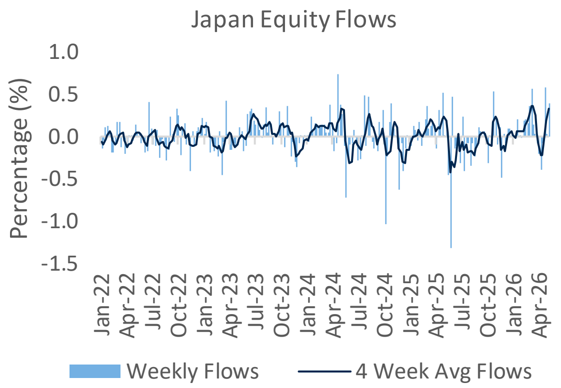
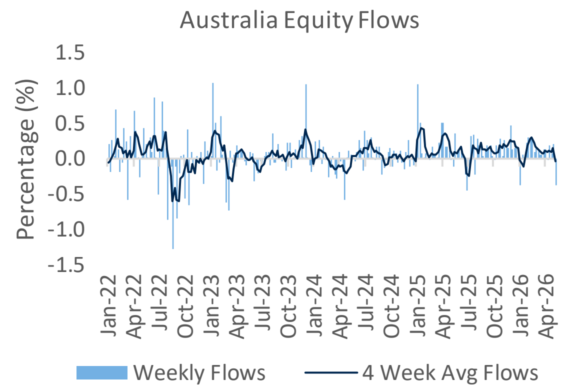
Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

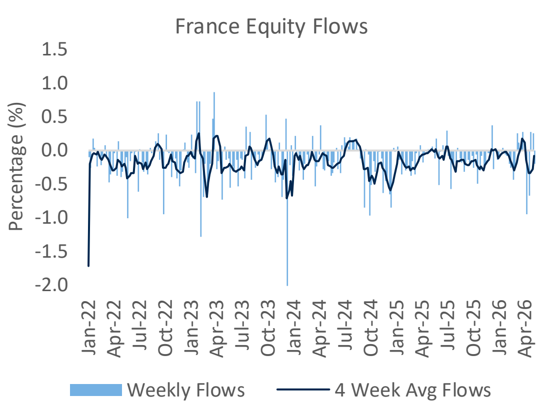
Mixed Trends for Key Developed Market Country Equity Fund Flows

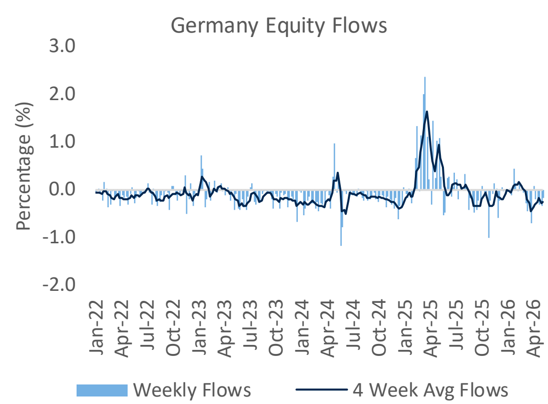
- We are seeing stable inflows for Canada, strengthening inflows to Japan, and weaker flows for Australia.
- France and the UK are seeing improving trends lately, and German flows are getting less negative.

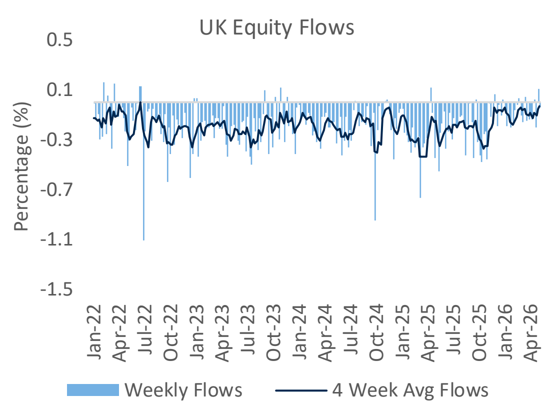












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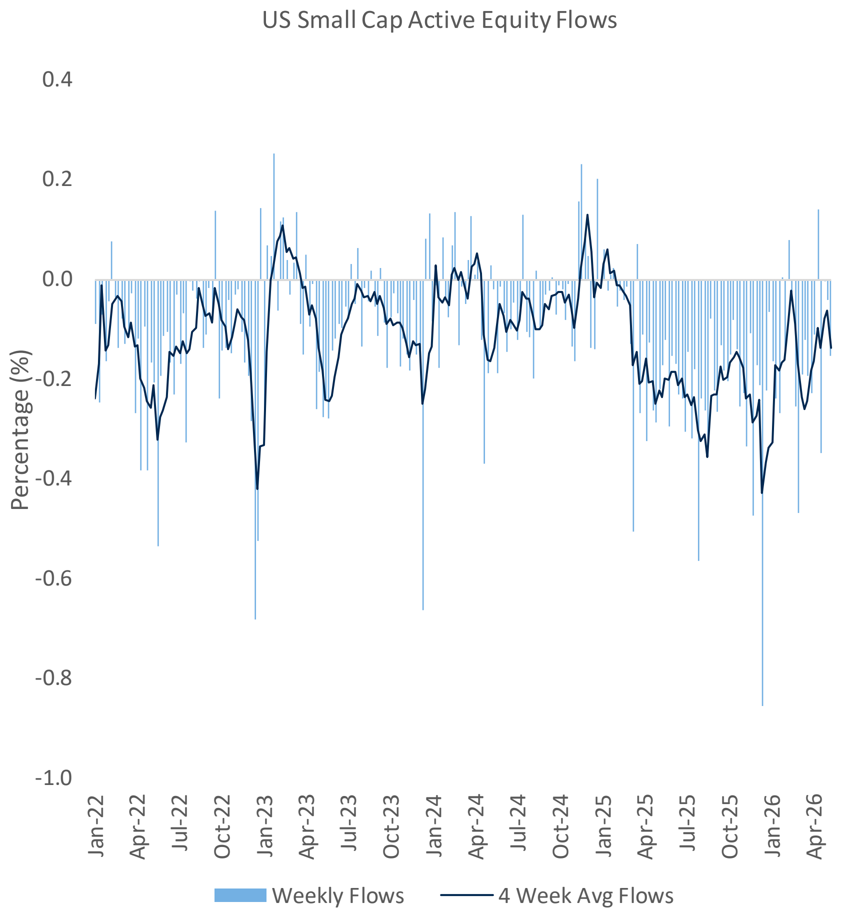
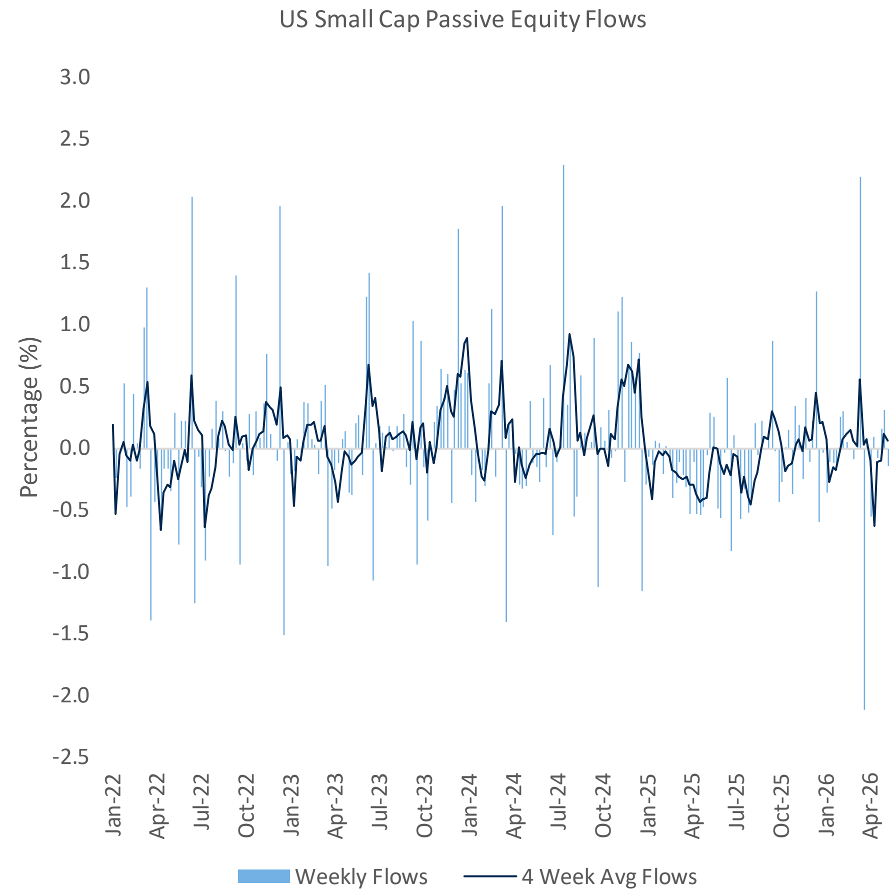
Within Small Cap, Active Funds Just Registered an Outflow, Passive Flows Have Improved Recently





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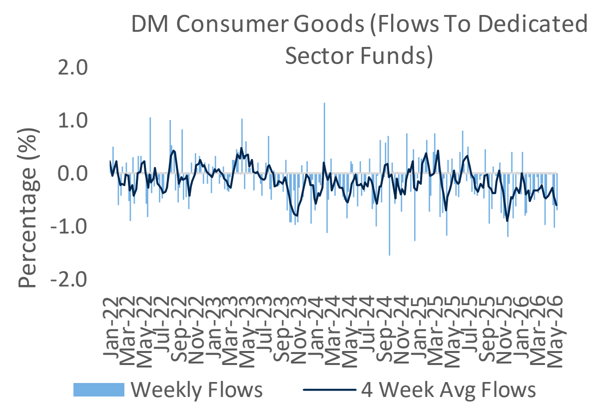
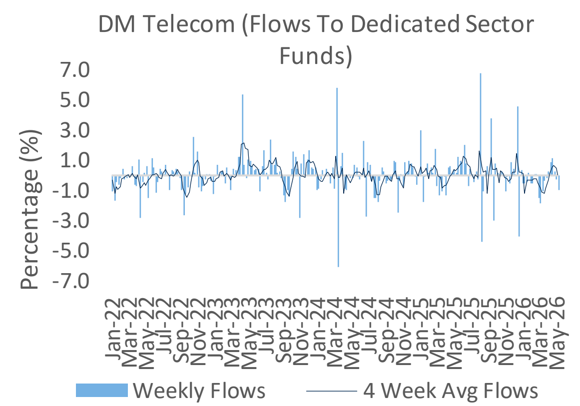
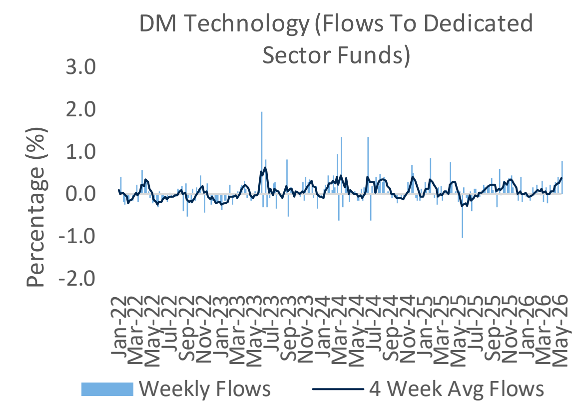
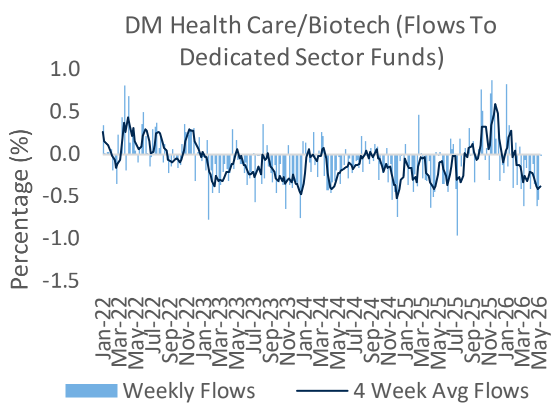
Global Developed Markets Sector Flows (Growth and Defensive)

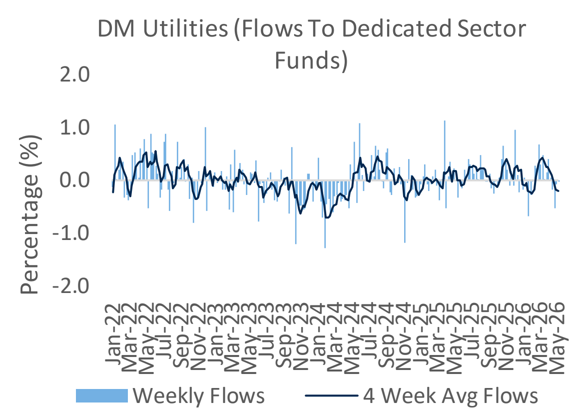
- These charts capture inflows / outflows to funds dedicated to specific sectors.
- On the growth side, Consumer flows have generally been negative. Telecom flows have stalled. Tech flows are still holding up and keep improving.
- On the defensive side, Health Care continues to see deep outflows in the latest updates. Utilities flows are deteriorating and have turned negative, while REITs appears to have turned a corner and are starting to see inflows now.

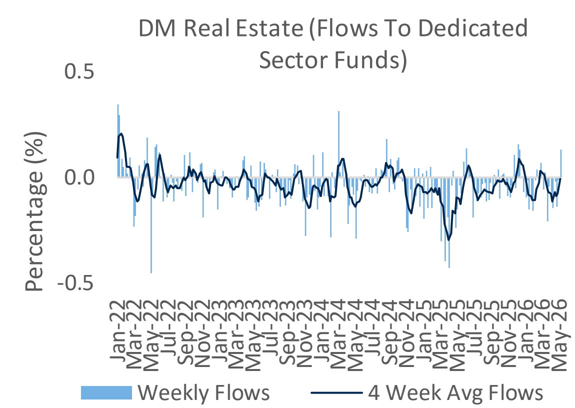








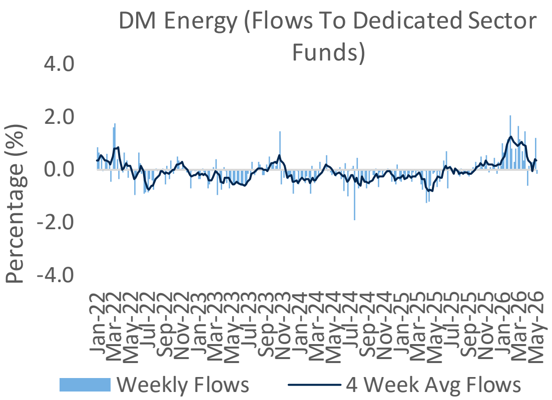


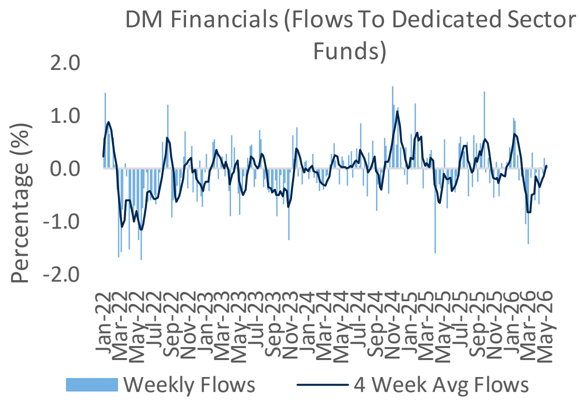


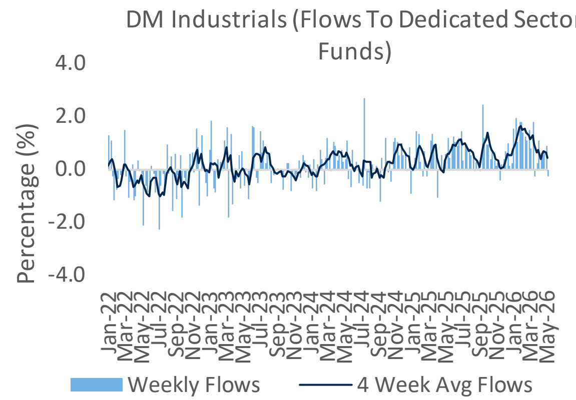
Note: Global Developed Markets includes all developed market funds dedicated to Asia-Pacific, North America, Western Europe, and Global as their regional mandate.
Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

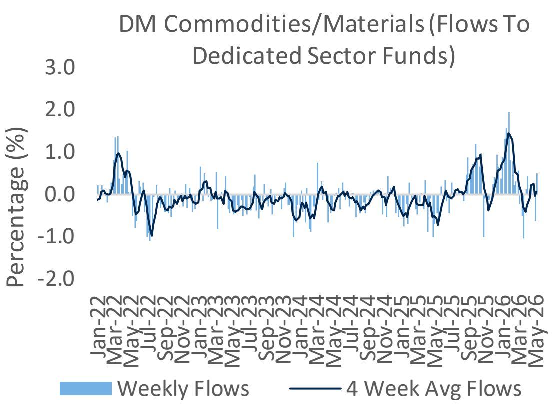
Global Developed Markets Sector Flows (Cyclical and Value)

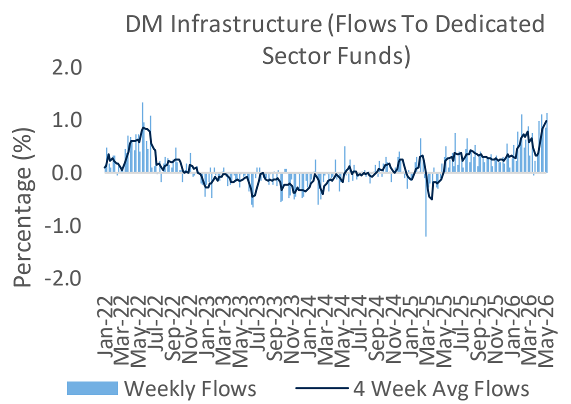
- These charts capture inflows / outflows to funds dedicated to specific sectors.
- On the commodity side, Energy flows went through a period of brief weakness but just saw a large inflow.
- Materials flows have turned back to positive and are starting to stabilize after a period of weakness earlier this year.
- On the cyclical side, Industrials flows have been strong but are weakening. Financials flows have been weak but are getting less negative.
- Infrastructure flows have been positive and continue to be strong.







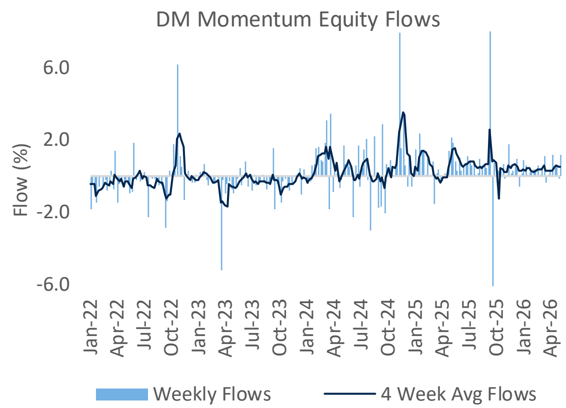


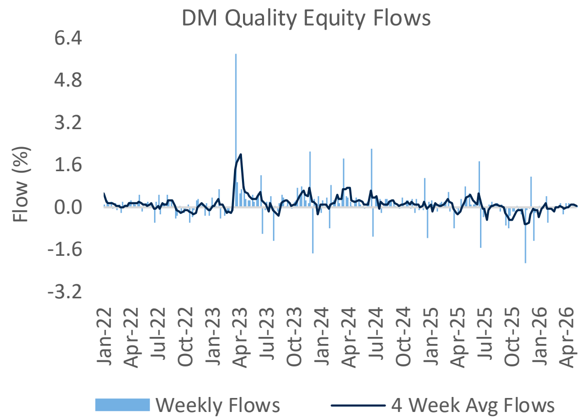


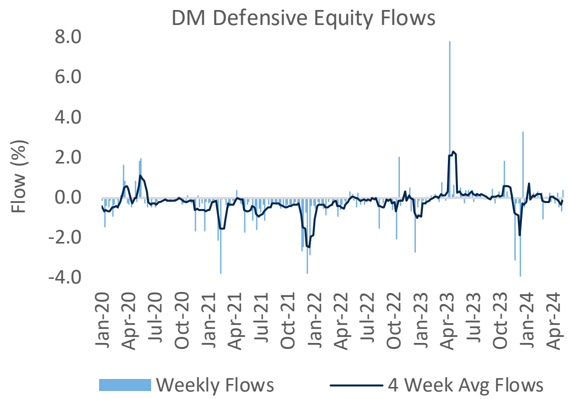
Note: Global Developed Markets includes all developed market funds dedicated to Asia-Pacific, North America, Western Europe, and Global as their regional mandate.
Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

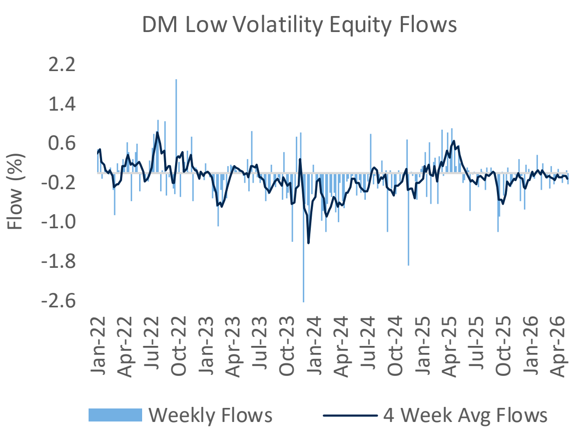
Global Developed Markets Factors Flows

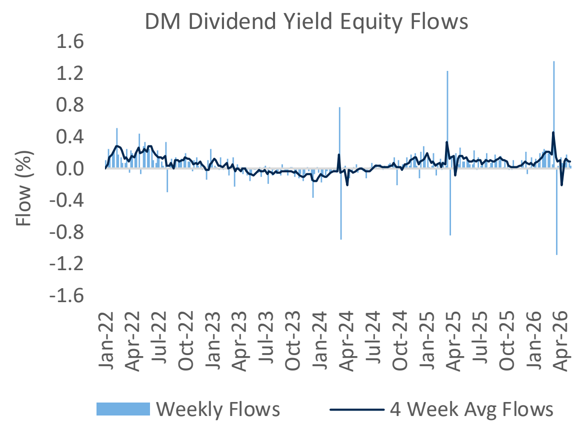
- These charts capture inflows / outflows to funds dedicated to specific factors.
- Flows for momentum funds have been positive and stable lately.
- Flows for low vol and for quality funds have been muted.
- Flows to defensive funds have been choppy recently.
- Dividend funds recently registered their largest weekly inflow and outflow since 2022.











Source: RBC US Equity Strategy, EPFR; as of May 13, 2026

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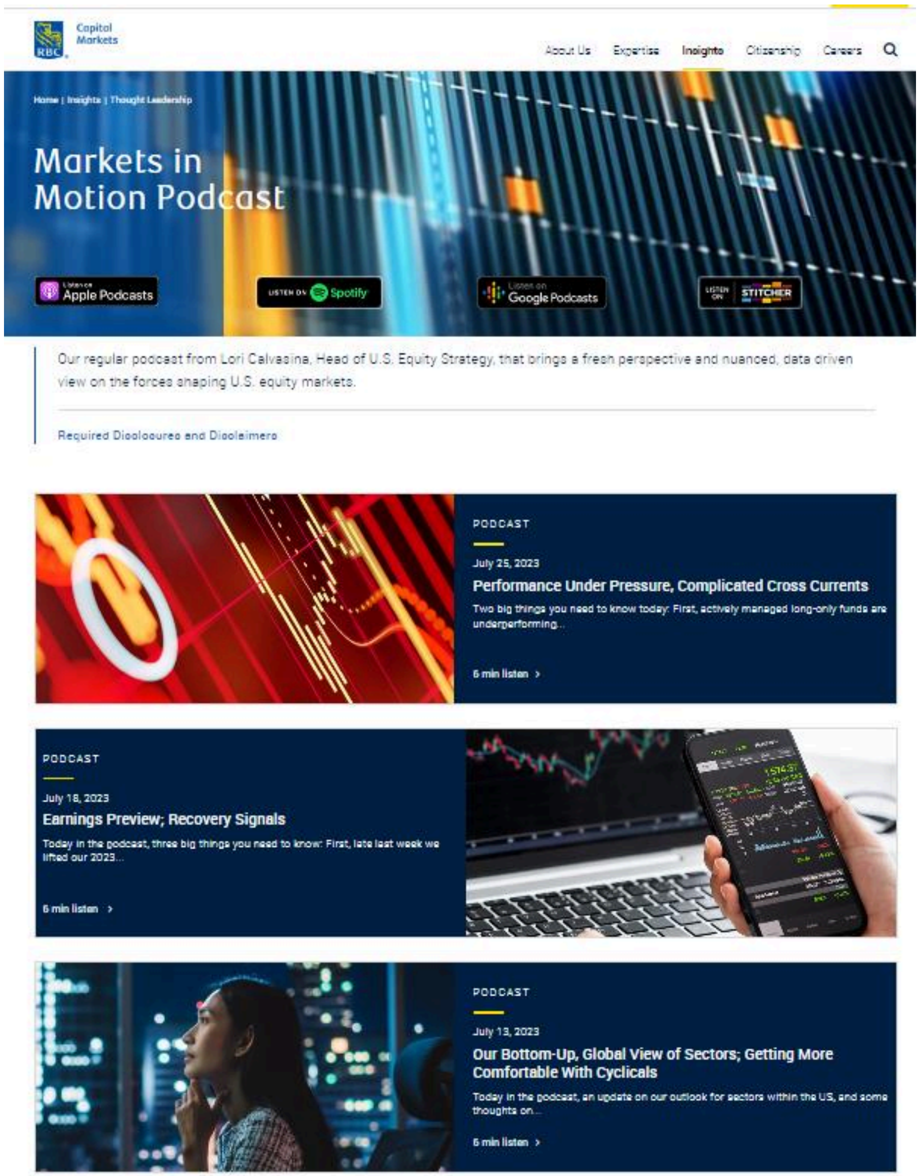

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