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ASSET MANAGEMENT

Research **Viewpoints**
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Everything's AI

AI infrastructure and productivity themes permeate nearly all corners of the financial markets, masking geopolitical crosscurrents and policy limitations that may define the second half of 2026.

AI euphoria has been the primary narrative propelling U.S. equity market performance. Increasingly, however, large segments of the global economy and financial markets have become intertwined with the AI infrastructure buildout and expectations of associated productivity gains. While this has produced some apparent broadening in market leadership across sectors and regions, the perceived diversification may be underpinned by a common theme. With swaths of the economy and capital now linked to the success of AI adoption, a disappointment in the AI revolution could have global consequences.

Market performance and corporate fundamentals appear robust on the surface, yet massive AI capital expenditure has created a stark bifurcation between perceived "AI winners" and the broader market:

- **Corporate earnings growth remains heavily concentrated in AI and technology.** First-quarter S&P 500 earnings rose nearly 30% year-over-year, with analysts projecting strong growth through 2026 and 2027. A significant portion of both current and expected earnings expansion is being driven by AI-related companies.
- **The apparent broadening of equity market leadership is largely AI-driven.** While large cap value and small cap indices have shown improved performance, much of the strength has come from AI-linked segments. Semiconductor companies have fueled gains in large cap value benchmarks, while speculative areas such as neocloud computing, quantum computing, semiconductors, and nuclear power have led small cap performance, largely outperforming more established and consistent businesses.
- **International and emerging market gains also reflect AI concentration.** Much of the recent outperformance in these markets has been driven by a small group of companies involved in the AI chip manufacturing and supply chain ecosystem.
- **Technology's influence is expanding into credit markets.** The weight of the technology sector is growing within public and private credit markets, as hyperscalers tap debt markets in order to fund capex plans. Data center construction is increasingly being financed by private asset-backed loans, some of which are being held off-balance sheet.
- **Real assets are following the same trend.** Companies that build, equip, or power data centers have benefited disproportionately, while real estate, utilities, and infrastructure assets not related to the secular AI trend have generally lagged.
- **AI-related investment is becoming a meaningful contributor to economic growth.** A significant portion of recent U.S. GDP growth has been supported by AI capital spending and investment, even as consumer spending has remained subdued.
- **Labor market trends increasingly reflect AI adoption.** Businesses have moderated hiring as they balance workforce expansion against technology investments, and AI is becoming a more commonly cited factor in workforce reductions and restructuring decisions.

Despite the strong momentum, risks to the AI trade are mounting. In our April 2026 Viewpoints (***"What Can Derail the AI Train"***) we highlighted challenges around energy availability and NIMBYism (not in my backyard-ism). More recently, questions have surfaced regarding the cost of compute for enterprises deploying AI solutions. Several companies reportedly exhausted their full-year AI budgets in the first quarter alone due to rising costs, prompting major AI labs to consider price reductions to retain customers. Adding to the uncertainty, OpenAI is reportedly exploring a delay of its planned initial public offering (IPO), which raises questions about the underlying economics of the business and the broader ecosystem.

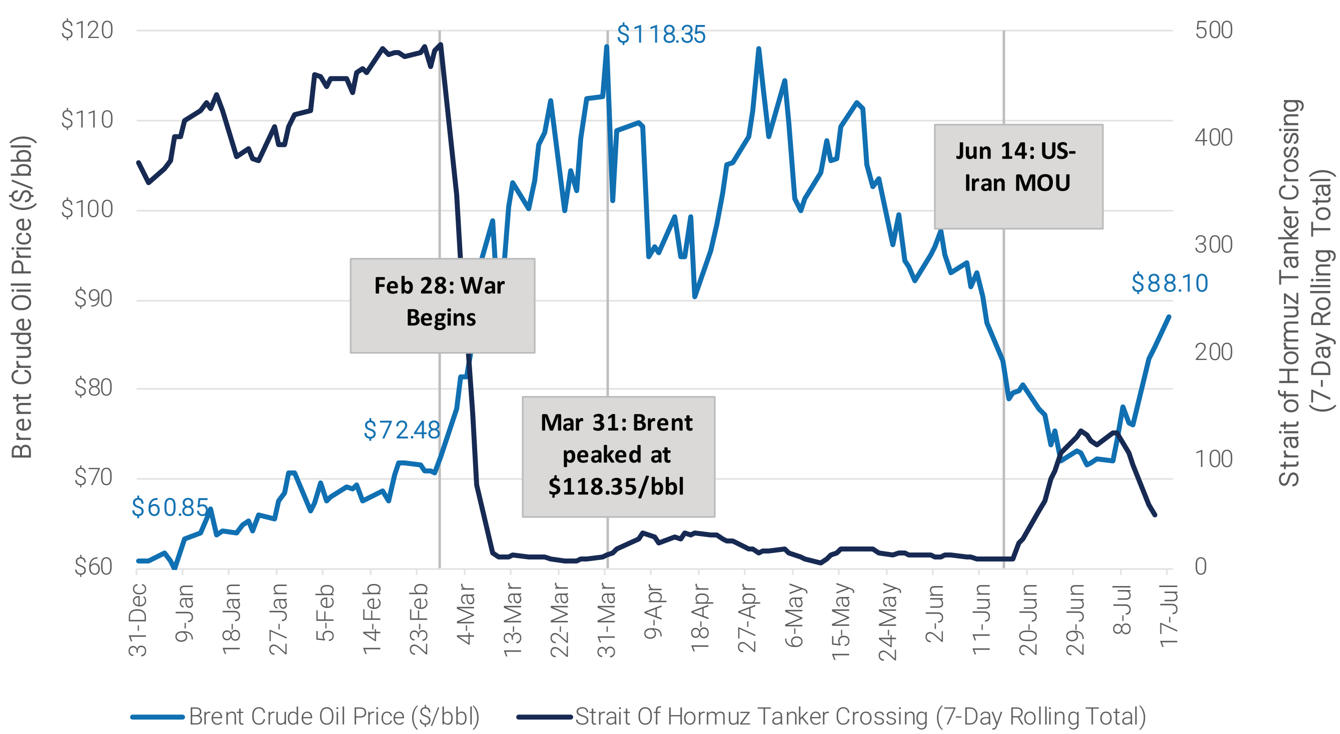
Should the AI trade stall or reverse the ripple effects could be significant across asset classes. Given the theme's pervasiveness, such a development could precipitate a meaningful market correction. In that environment, we believe active managers who avoided the epicenter of exuberance could deliver strong relative performance, though there is no assurance any strategy will outperform.

Geopolitical Risks Persist

Diplomatic efforts between the U.S. and Iran appear to be faltering after the termination of the memorandum of understanding (MOU). Negotiations are expected to continue but compromise on control over the Strait of Hormuz and Iran's nuclear program appears elusive.

Oil Prices are Rising Again

YTD Brent Crude Oil Price vs. Strait Of Hormuz Tanker Crossing



Source: Bloomberg, data as of 7/17/2026.

Oil prices retreated to pre-conflict levels during the ceasefire but are rising again and will likely remain volatile given the fluidity of the situation. Supply chains and commodity markets are still feeling secondary effects, while policymakers contend with the threat of resource hoarding. Over the longer term, we anticipate that supply chain reorientation will contribute to diminished global trade and structurally elevated inflation.

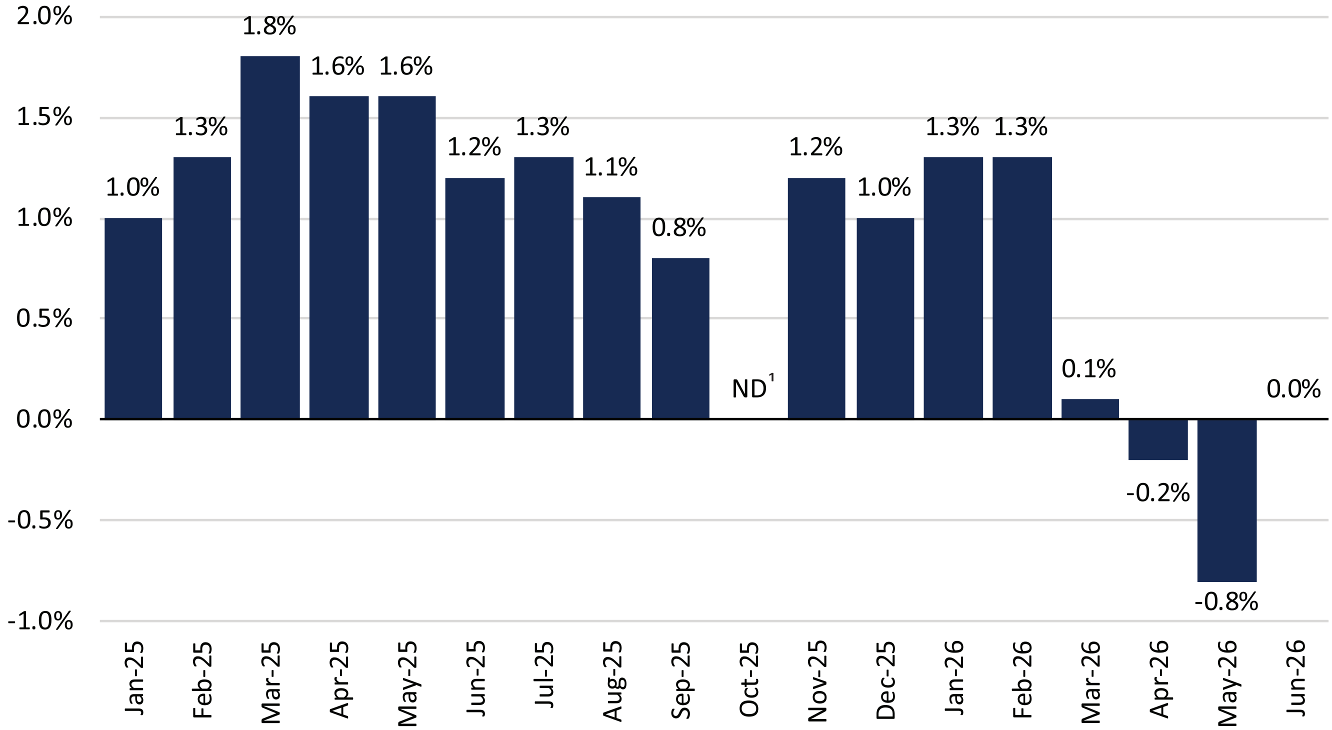
Macro/Markets Update and Policy Conundrums

U.S. Economic Backdrop Remains Uneven

The U.S. consumer has proven more resilient than expected, supported by nominal wage gains, elevated household net worth, and the stimulative effects of excess savings and tax refunds. Consumer strength remains bifurcated, with higher-income households driving discretionary spending while lower and middle-income cohorts face growing financial strain from higher prices that have begun to erode wage gains and shifting labor market dynamics.

Real Wage Growth Turned Negative in 2Q 2026

Real Wage Growth YoY (Nominal Wage Growth YoY - CPI YoY)



Source: Bloomberg, Bureau of Labor Statistics.

Inflation reaccelerated in 2026. While higher energy prices may ease if a diplomatic solution is achieved, core inflation, which removes volatile food and energy prices, remains well above the Federal Reserve's (Fed's) 2% target. The lagged effects of higher energy costs are likely to continue filtering through transportation, manufacturing, and supply chains.

The labor market appears to have stabilized following a weak second half of 2025. The June employment report disappointed and included some downward revisions, yet strong job gains were still reported in March through May and the unemployment rate remains low at 4.2%. However, much of the job growth was concentrated in the government and government-adjacent sectors and private sector hirings were more muted, raising concerns about the strength of the business environment.

Limited Policy Reactions

Monetary policy expectations have adjusted as the labor market firmed and inflationary pressures persist. Markets are now pricing in the possibility of a rate hike later in 2026 following a more hawkish shift in the Fed's projections and Chair Warsh's emphasis on restoring price stability.

Fiscal policy faces similar constraints. A large budget deficit and rising interest costs limit policymakers' capacity to provide meaningful stimulus in the event of a downturn. If elections result in a divided government, gridlock would further constrain fiscal support.

Financial Markets: A Heat Check

Major equity indices have largely looked past geopolitical uncertainties, rallying sharply from the lows of late March. This advance has been led primarily by momentum and growth stocks. While earnings growth has helped moderate valuations, they remain elevated compared to historical norms. The S&P 500's forward price-to-earnings (P/E) ratio stands at approximately 22x, above the long-term average of 16.5x, aligning with levels that historically preceded more challenging subsequent returns. The Shiller cyclically adjusted price-to-earnings (CAPE) ratio, which adjusts for earnings cycles and inflation, is near 40x, close to the Tech Bubble peak of 44x.

1. The Consumer Price Index (CPI) data for October 2025 was canceled due to a government shutdown, leaving a gap in inflation data for that month.

The Shiller CAPE Ratio Nears Tech Bubble Peak

S&P 500 Shiller CAPE Ratio (Jan 1900 - June 2026)

Source: Robert J. Shiller, schillerdata.com

A surge in equity issuance this year further illustrates the prevailing exuberance. SpaceX's landmark $75 billion IPO in June—the largest in history—helped drive U.S. equity issuance to a record $251 billion in the first half of 2026. Several other high-profile AI-related companies are expected to come to market in the second half.

Public technology companies are also tapping the equity markets at scale. Alphabet has issued $85 billion in stock, and Meta is reportedly exploring a similar move. This marks a notable shift: today's leading technology firms are increasing their share counts and deploying enormous amounts of capital into long-term corporate investments, reversing the prior pattern of aggressive share buybacks and robust free-cash-flow generation.

What We are Keeping an Eye On: Private Credit Market Dynamics

Private credit has become a staple allocation for many portfolios, but the rapid influx of capital has introduced risks. Managers of evergreen funds face pressure to deploy capital quickly, contributing to a rise in covenant-lite structures and lending to lower-quality borrowers. Recent concerns about funds' software exposure and overall credit quality have led to redemption pressure, with many funds limiting redemptions.

Funds have largely refrained from marking positions down despite pockets of stress, but managers may eventually need to realize losses to meet redemptions. Loans in current funds were originated in a highly liquid environment, and these companies may face financial stress when they need to refinance at wider credit spreads. Rising payment-in-kind (PIK) interest and other liability-management transactions also point to elevated stress, even if headline default rates remain contained.

Undisciplined private credit managers with sub-optimal fund structures are likely to continue facing withdrawal challenges. We believe losses in private credit may eventually flow through to private equity valuation if managers are forced to write down holdings. At the same time, greater market bifurcation creates opportunities for skilled credit investors to capitalize on dislocations. Asset-backed private credit may offer structural protections and lower cyclical correlation. Secondaries strategies can also benefit from discounted entry points.

Asset Class Detail

This chart outlines OAM Research & Investment Management's macroeconomic and asset class views.

Asset class views reflect a medium-term outlook by OAM Research based on macroeconomic trends, valuations, and technical indications and are intended to advise allocation tilts relative to an appropriate strategic asset allocation.

Underweight · Slightly Underweight · Neutral · Slightly Overweight · Overweight

Global Equity

U.S. Large Cap
Large cap earnings growth has been strong, but future growth is highly dependent on the AI trade. Valuations remain high compared to historical norms, though smaller large cap companies less exposed to AI risk may look more attractive. Higher-quality companies with pricing power should be more resilient, and investors may benefit from allocating to strategies focused on quality and downside protection. Value indices are expensive but pockets of opportunities remain in defensive business models with more reasonable growth expectations.

U.S. Small-Mid Cap
Small and mid-cap index valuations are extended following a significant rally in low quality momentum stocks. Higher quality small and mid-cap companies look more compelling today and should be more resilient if higher interest rates persist or the economy turns.

International Developed
Relative valuations remain attractive but some prior tailwinds from monetary policy, economic growth, and U.S. dollar weakness have faded. Longer-term risk reward in international equities still appears better than in the U.S. given more fiscal support, lower valuations, and greater dividend returns, which can provide a ballast to portfolios.

Emerging Markets
Valuations are stretched for AI-related stocks but remain reasonable for the rest of the asset class and look attractive relative to developed equities. Active managers can take advantage of bifurcated performance by allocating to countries and sectors with more promising growth prospects and more reasonable valuations.

Global Equity - Alternatives

Long/Short Equity is considered part of the strategic asset allocation for equities based on each fund's underlying investments.

Long/Short Equity
Long/short strategies can benefit from higher volatility and dispersion to add long and short alpha. Many managers benefited from the rebound in technology but may be exposed if the AI trade reverses. Nimble managers that can effectively manage exposure can potentially navigate a fast-moving, headline-driven market.

Global Fixed Income

U.S. Core Fixed Income
Treasury yields remain elevated and volatile. The Fed may be on hold or even raise interest rates given upside risks to inflation, but current yields are attractive and the asset class should provide portfolio protection if growth deteriorates. Investment-grade credit spreads are still tight, and corporate balance sheets remain healthy but rising issuance could signal future stress.

High Yield Credit
High yield credit spreads remain historically tight. Defaults remain muted and leverage is not excessive in public markets, but private credit loans have come under increased scrutiny and may signal a turning credit cycle. Private asset-backed lending and opportunistic credit strategies appear more compelling than corporate direct lending.

International Fixed Income
International bond performance was muted due to inflation concerns and U.S. dollar strengthening. Emerging market debt looks more attractive within the non-U.S. market, both from a yield perspective and as a portfolio diversifier, though the asset class may suffer if global growth slows.

Diversifying Strategies

Real Assets
Real asset strategies may outperform with continued inflationary pressures. Midstream energy infrastructure may benefit from energy supply chain reorientation, and defensive areas like Utilities and Infrastructure can protect from volatility. REITs are attractively valued but will have to contend with higher interest rates and the potential for lower growth.

Event Driven/Uncorrelated
Event-driven strategies may benefit from a rebound in M&A volumes, and deal activity is expected to continue to recover in 2026. However, prior tailwinds from declining interest rates and stable economic growth may be at risk.

Opinions expressed are current as of 07/17/2026 and are subject to change. These opinions do not guarantee future results. See pgs. 7-8 for important disclosures.

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S&P 500 Index is a market capitalization-weighted index of 500 leading publicly traded U.S. companies. It is considered to be generally representative of the U.S. large cap equity market.

Forward Price-to-Earnings ("P/E") Ratio is a valuation measure calculated by dividing a company's or index's current share price by its estimated earnings per share over the next twelve months.

Shiller Cyclically Adjusted Price-to-Earnings ("CAPE") Ratio is a valuation measure, developed by economist Robert J. Shiller, calculated by dividing a company's or index's share price by the average of ten years of inflation-adjusted earnings. It is intended to smooth out fluctuations in corporate profits caused by economic cycles. Indices are unmanaged, do not reflect the costs associated with buying and selling securities and are not available for direct investment. Investors cannot invest directly in an index.

Risk Factors
The success of an investment program may be affected by general economic and market conditions, such as interest rates, the availability of credit, inflation rates, economic uncertainty, changes in laws and national and international political circumstances. These factors may affect the level and volatility of securities prices and the liquidity of a portfolio's investments. Unexpected volatility or illiquidity could result in losses.

Investing in securities is speculative and entails risk. There can be no assurance that the investment objectives will be achieved or that an investment strategy will be successful.

Special Risks of Foreign Securities
Investments in foreign securities are affected by risk factors generally not thought to be present in the United States. The factors include, but are not limited to, the following: less public information about issuers of foreign securities and less governmental regulation and supervision over the issuance and trading of securities. International investments may involve risk of capital loss from unfavorable fluctuation in currency values, from differences in generally accepted accounting principles or from economic or political instability in other nations.

Special Risks of Small- and Mid-Capitalization Companies
Investments in companies with smaller market capitalization are generally riskier than investments in larger, well established companies. Smaller companies often are more recently formed than larger companies and may have limited product lines, distribution channels and financial and managerial resources. These companies may not be well known to the investing public, may not have significant institutional ownership and may have cyclical, static or moderate growth prospects. There is often less publicly available information about these companies than there is for larger, more established issuers, making it more difficult for the Investment Manager to analyze that value of the company.

The equity securities of small- and mid-capitalization companies are often traded over-the-counter or on regional exchanges and may not be traded in the volume typical for securities that are traded on a national securities exchange. Consequently, the investment manager may be required to sell these securities over a longer period of time (and potentially at less favorable prices) than would be the case for securities of larger companies. In addition, the prices of the securities of small- and mid- capitalization companies may be more volatile than those of larger companies.

Special Risks of Fixed Income Securities
For fixed income securities, there is a risk that the price of these securities will go down as interest rates rise. Another risk of fixed income securities is credit risk, which is the risk that an issuer of a bond will not be able to make principal and interest payments on time. Liquidity risk is the risk that you might not be able to buy or sell investments quickly for a price that is close to the true underlying value of the asset. When a bond is said to be liquid, there's generally an active market of investors buying and selling that type of bond. Fixed income securities markets are subject to many factors, including economic conditions, government regulations, market sentiment, and local and international political events. Further, the market value of fixed-income securities will fluctuate depending on changes in interest rates, currency values and the creditworthiness of the issuer.

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