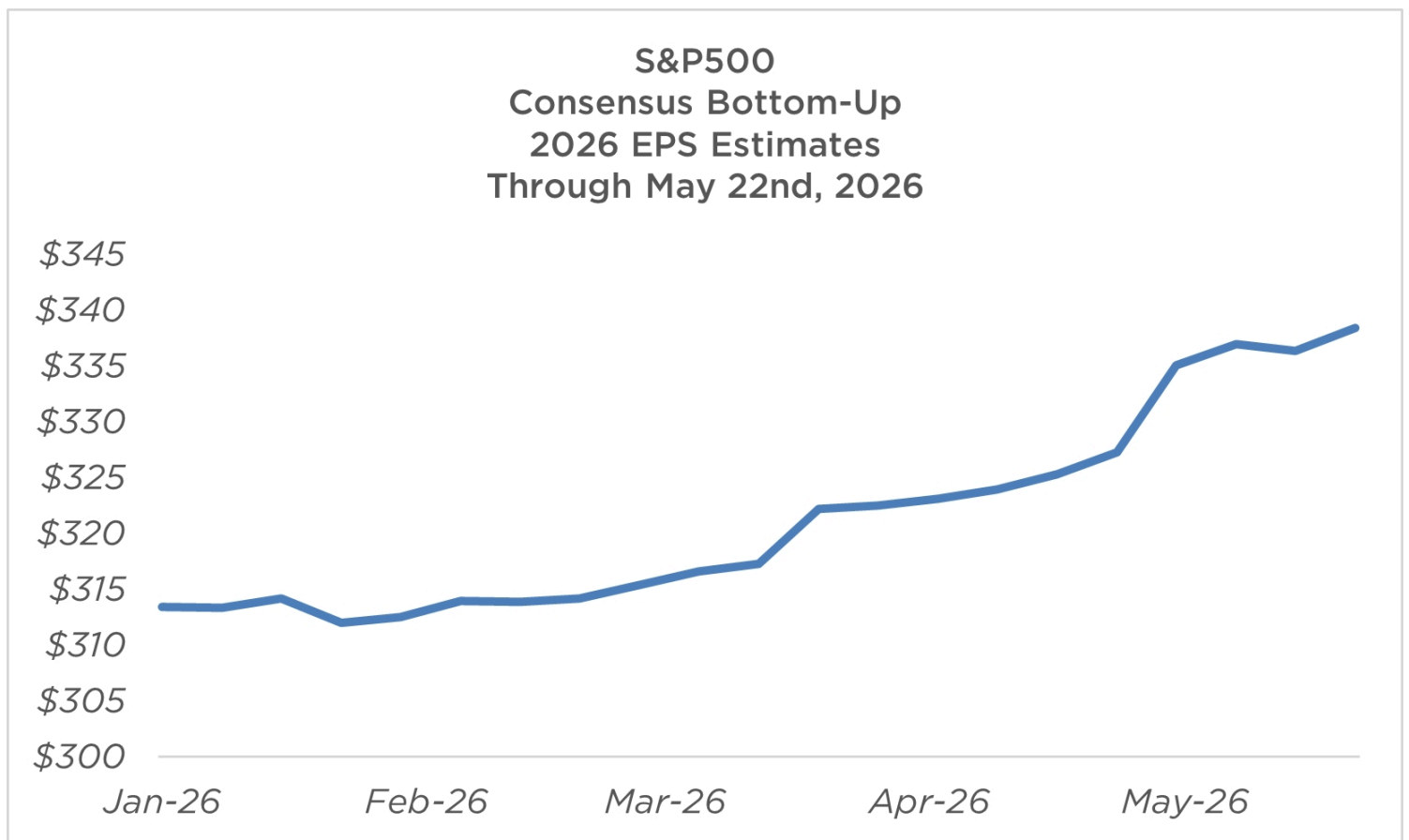


## Level Set: The Market Is Trading on Fundamentals

After another solid week in the S&P500, back within a few points of all-time highs established last Thursday, May 14th, we have been challenged by a number of our clients to put forth a credible narrative that could derail the AI story and the broader market, as opposed to what could continue to make it last. While we loathe bubble talk, and don't think we have the skill to time the exact top of the AI Semiconductor trade, there is no doubt that fundamentals are at least partially responsible for the market rally. The consensus bottom-up S&P500 estimates for 2026 have continued to rise this year (see below), and are in aggregate 8% higher than they were on January 1<sup>st</sup>. The S&P500 is up 9.2% year-to-date, so about in-line. With earnings projected to grow 23% this year, and 16% next year, there's a credible argument to make that despite the increasing projections for earnings, and strong earnings growth, the price-to-forward earnings has been modestly contracting.



Source: Trivariate Research, LP

**Adam Parker**

Founder  
646-734-7070  
[adam@trivariateresearch.com](mailto:adam@trivariateresearch.com)

**Maxwell Arnold**

Analyst  
347-514-1234  
[maxwell@trivariateresearch.com](mailto:maxwell@trivariateresearch.com)

**Colin Cooney**

Head of Sales  
617-910-7934  
[colin@trivariateresearch.com](mailto:colin@trivariateresearch.com)

**Chang Ge**

Analyst  
614-397-0038  
[chang@trivariateresearch.com](mailto:chang@trivariateresearch.com)

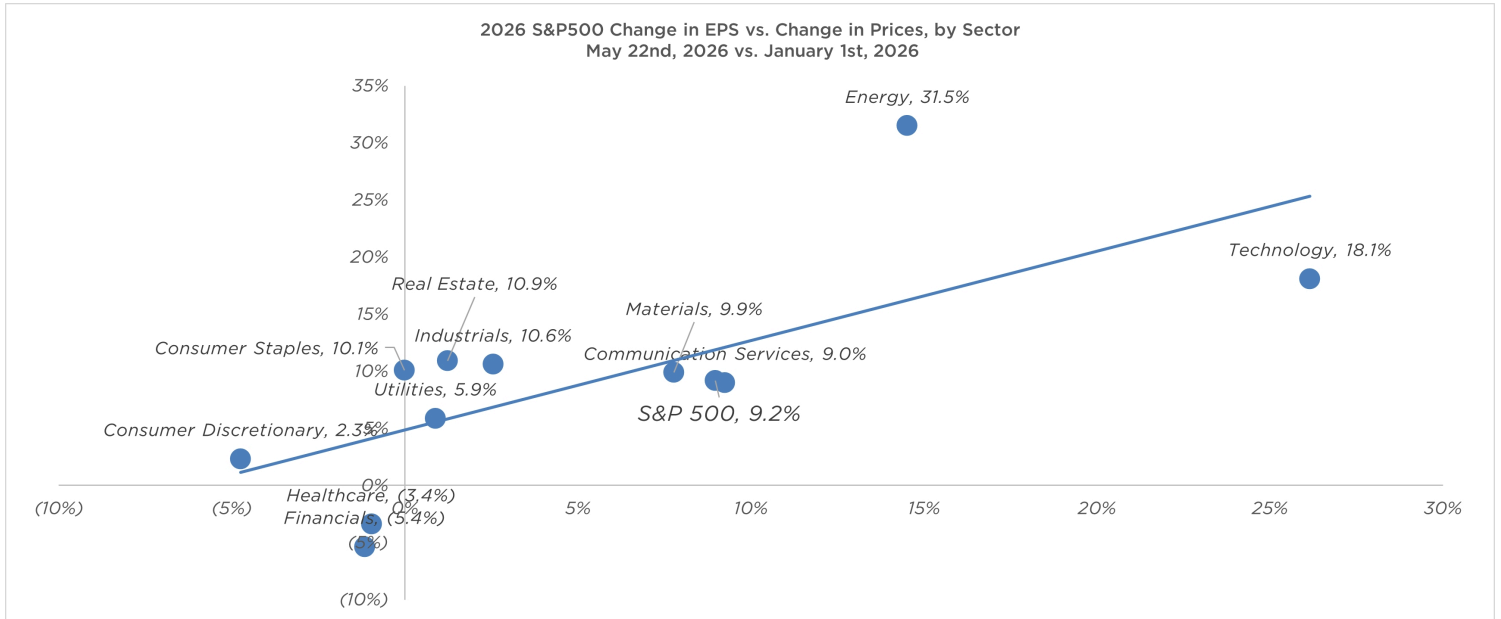
**Jesse Goodman**

Analyst  
917-741-5744  
[jesse@trivariateresearch.com](mailto:jesse@trivariateresearch.com)

**Ryan McGovern**

Director of Research Sales  
973-271-8017  
[ryan@trivariateresearch.com](mailto:ryan@trivariateresearch.com)

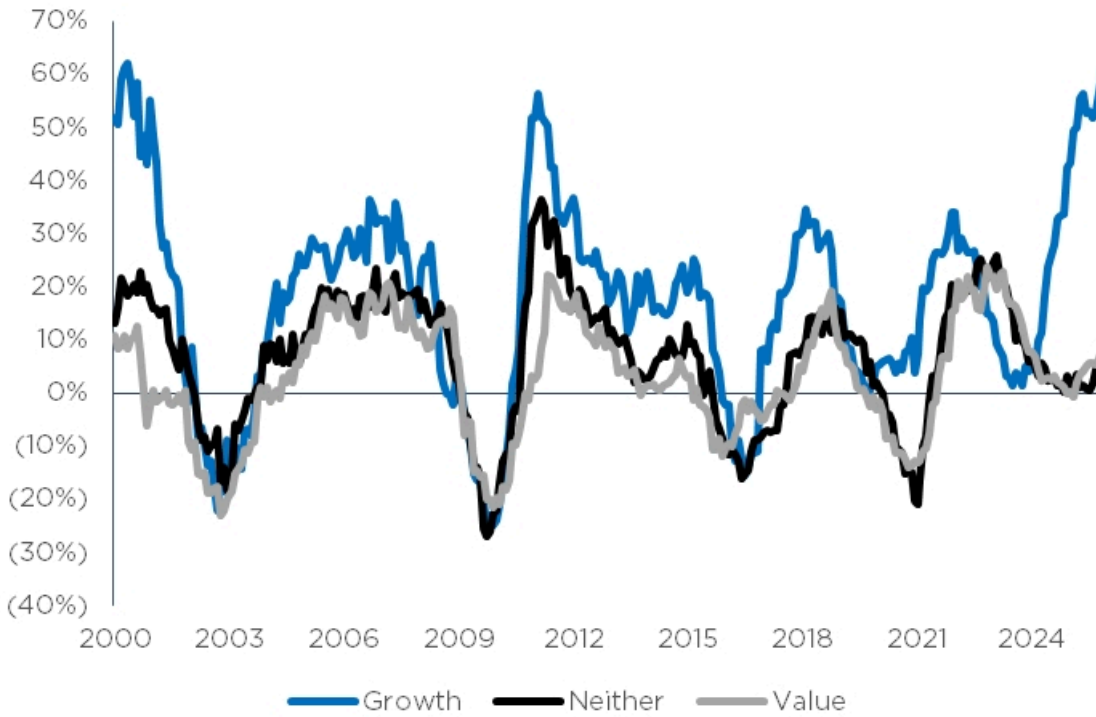
Year-to-date, there has been a significant relationship between the change in sector performance and the change in analyst estimates at the sector level (see below). The sectors with the worst aggregate change in consensus bottom-up earnings estimates are Consumer Discretionary, Financials, and Healthcare-the three worst performing sectors. The sectors with the biggest increases in 2026 earnings estimates year-to-date are Technology, Energy, and Communication Services. Energy, Technology, and Real Estate are the three best performing sectors so far this year. **While there are modest exceptions, so far it isn't wrong to say fundamentals and performance have been highly correlated, both at the market and sector level. Many investors have said to us that the market isn't trading on fundamentals. But maybe it is?**



Source: Trivariate Research, LP

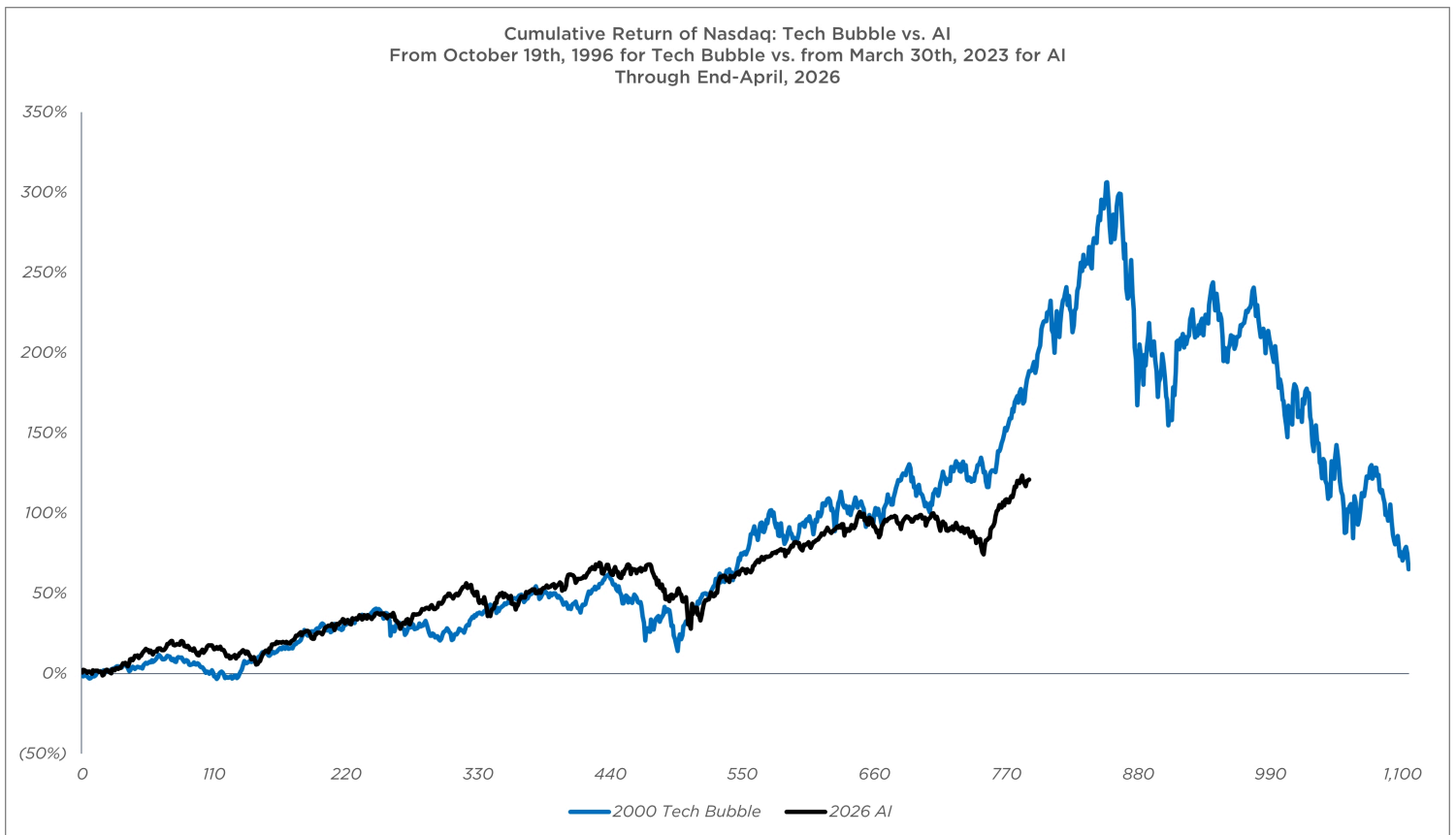
That being said, we do believe and agree with the consensus narrative that stock prices are ahead of the fundamentals when it comes to the Data Center build out and AI-related stocks. Last week published ([see here](#)) our detailed analysis that shows that just less 9% of the top 3000 US equities are currently generating any meaningful AI revenue. With experts and hyper-scalers generally projecting as much as 3x more spending on Data Centers over the next three years than we have so far witnessed, the absolute growth rate of the exposed businesses is likely to remain high. That may not create upward revisions or multiple expansion, but the level of growth might continue to be enough to drive further appreciation for the stocks. Investors and customers are searching for cheaper DRAM to combat the parabolic move in Memory stocks. It came up twice last week in our meetings and once on Friday during our CNBC appearance about how the current trading environment compares to the final phases of the TMT bubble that peaked in March 2000. We were asked - is this 1995 or 1999? Our answer is - neither. In some ways there are similarities to the end of the bubble - the one area that seems most consistent is the capital spending dollar growth from the growth stocks (see below) - otherwise known as the hyperscaler capital spending. There are also the imminent giga-cap IPOs, which certainly ring "toppy" at some level.

### Trailing Capital Spending Dollar Growth By Style Through End-April, 2026



Source: Trivariate Research, LP

But in many other ways, there are differences, at least for now, in terms of leverage, valuation, and price action. We compared the run-up into the TMT bubble and the recent AI price action. The huge move from October 1999 through March 2000 is still NOT in the price (see below).



Source: Trivariate Research, LP

**What is a non-consensus worry?** One risk to the continued AI rally we don't think is being talked about very much is any potential AI deployment hiccup. To the extent a major company indicates they have to run systems in parallel before large AI deployments, or there is less headcount savings, that might dampen the enthusiasm some investors have for long-term earnings productivity. There seems to be a universal consensus that AI will eliminate white collar jobs, and cause massive unemployment. Many investors have commented to us in recent months that they are worried not only about their own careers, but also that their children won't be able to find jobs. Recent college graduate data certainly hasn't been directionally confidence-inducing. But, recently we have started to think that perhaps this is yet another consensus view that could turn out to be wrong - and in fact - the opposite view - is more likely.

Every major Technology cycle obsoletes old jobs and creates new ones. This has been happening for decades, and the new job creation in different fields has offset the jobs that are rendered vestigial by the new Technology. In some ways, history indicates this should be the default economic assumption for AI, not the opposite. What are examples? A hedge fund client mentioned to us last week they need an Agentic AI Safety officer. A quick prompt on Gemini suggested these below are some of the possibilities. Another friend of ours said he wants to short any company that overly focuses on labor productivity, implying they should have other focal points. Perhaps the tide is going out a bit.

**Finance (Banking, Investing, Consulting)** - AI is becoming increasingly embedded in areas like:

1. AI Risk: Monitoring model errors, bias, financial risk
2. Quant and AI: Using AI models alongside statistical finance tools, like we do at Trivariate Research
3. AI Compliance Officers: Trading, lending, regulatory compliance
4. Investment strategist: Using AI to spot trends, signals, opportunities. Analytical skills aren't investment skills.
5. Client AI Advisor: Explaining AI-generated insights to clients.
6. Agentic supervisor to quality control and monitor AI agents.

**Law:** Legal work is being augmented fast—but not replaced:

1. AI Legal Analyst: Review contracts or case law produced by AI
2. Legal AI Prompt Specialist: Design prompts for legal research tools

3. AI Compliance Policy Advisor: Interprets regulations around AI use and misuse
4. eDiscovery AI Manager: Oversees AI scanning documents for litigation

**Healthcare:** Sector might need AI jobs without replacing as many human jobs Might need more people

1. Clinical AI Reviewer: Verifies AI-generated diagnoses or patient recommendations
2. Healthcare AI Implementation: Deploy AI tools in hospitals
3. Medical Data Curators: Structures and cleans patient datasets for AI modeling and analysis
4. Patient Experience: Designing and improving AI chatbots for patient interaction

**Technology / start-ups:** This is where most new roles originate.

1. AI Product Manager
2. AI Solutions Architect
3. Prompt Engineer / LLM Specialist
4. AI App Builder (no-code / low-code)
5. AI Startup Founder / Operator

**Marketing, Media & Creative:** AI is transforming content creation.

1. AI Content Director: Oversees AI-driven content pipelines
2. Brand Voice AI Trainer: Ensures outputs match tone and style
3. Synthetic Media Producer: Creates AI video, images, voice
4. AI SEO Strategist : Optimizes for AI-driven search

**Corporate / Operations (Across All Industries):** Every company needs these roles.

- AI Transformation Lead: Drives company-wide adoption
- Business Process Automation Specialist: Replaces manual workflows with AI
- Internal AI Consultant: Helps different teams use AI effectively
- Knowledge

**What's our take?** AI will not gut as many jobs as the doomsayers believe, and will likely create a host of new jobs. Smaller companies will be able to compete on a more level playing field, and if you want to get really bullish, we think spin-cos and more focused companies could result in a wave of transactions by the end of the decade. **We see the benefits of AI to likely outweigh the negatives, both economically and for US corporations for now - and frankly, are surprised that isn't the universal consensus.**

There was a lot of press commentary about the new Fed Chair Kevin Warsh being sworn in on Friday. However, we got zero investor questions or commentary on this last week. The consensus view has shifted dramatically on the Fed Funds rate. It was universally thought at the beginning of the year that the Fed would cut interest rates twice this year, and now, pundits are saying "there is now no way they can cut for several months." Given there isn't a collection of strategists, in our view, more consistently wrong than Interest Rate strategists, maybe the pendulum has swung a shade too far on what and when the Fed's next move will be. The perception of the 12-month forward Fed Funds rate (see below) is now nearly 100bps different from where it was at the beginning of the year. While inflation in Oil and Commodities is certainly part of the issue, this just highlights how quickly sentiment can change. **We aren't sure if the market will like EITHER Fed cutting or Fed HIKING, but we do know that when a consensus forms on the path of interest rates, it is more likely to be wrong than right, based on the last 15 years of observation.**

## 12-Month Fed Fund Futures End-2025 to May 22nd, 2026



Source: Trivariate Research, LP

## CONCLUSIONS

We have all learned that pre-positioning for geopolitical risk isn't prudent. But we are less convicted that pre-positioning for the mid-term elections won't become a hot topic of debate as we move through the summer. Perhaps the year-to-date weakness in some Financials, and Bitcoin is in part emblematic of positioning already underway? And, since we are recommending Healthcare, we will ask, is any political regime good for Healthcare Services stocks?

Our view is that the earnings trajectory is strong enough in this data vacuum to keep the risk-reward skewed to the positive. We think the market is likely to sell-off hard at some point, maybe even after all the giga-cap IPOs. But if we continue to ride the performance, and then experience some sell-off, we are likely better off losing "house money" than not participating. Playing the "downside" capture game in an up tape just hasn't worked.

Our last three research notes have reinforced these three investment conclusions:

1. **Run more diversified than usual.** If your portfolio has historically consisted of 25-30 stocks, the odds of success on a volatility-adjusted basis vs. a 50-stock portfolio are low.
2. **It is harder to get defensive, so use non-traditional methods.** It is not just low beta, but upward revisions are required. Continue to look for fundamental strength but where returns are NOT correlated to our AI Semis basket.
3. **Within AI, parse the AI-revenue exposure,** so look for multiple expanders, which are more likely to beat estimates.

We have written detailed notes on all of these points in the last few weeks, so don't hesitate to reach out if you want longer explanations.

## Important Disclosures

### Analyst Certification

The analysts, Adam Parker, Maxwell Arnold, Colin Cooney, Chang Ge, Jesse Goodman and Ryan McGovern, responsible for the preparation of this research report certifies that: all the views expressed in this research report accurately reflect the research analyst's personal views.

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