Level Set - The Biggest Questions, Pushback and Consensus Views on our 2026 Outlook

Last week we published our 2026 year-ahead outlook, and in today's Level Set we address the questions we received, and areas of push back and our updated assessment of the most consensus views.

QUESTIONS

We discussed in our year-ahead outlook that we believe the 2026 bottom-up consensus S&P500 earnings estimates are likely too optimistic. Below we show the bottom-up consensus EPS estimates and Trivariate's top-down EPS estimates for the S&P500 through 2027. We forecast $300 in 2026 EPS and $324 in 2027 EPS vs. the consensus of $313 and $345, respectively. The consensus outlook embeds 15.3% EPS growth for 2026, followed by another year of double-digit growth in 2027. We forecast a 10% EPS growth in 2026 and 8% in 2027.

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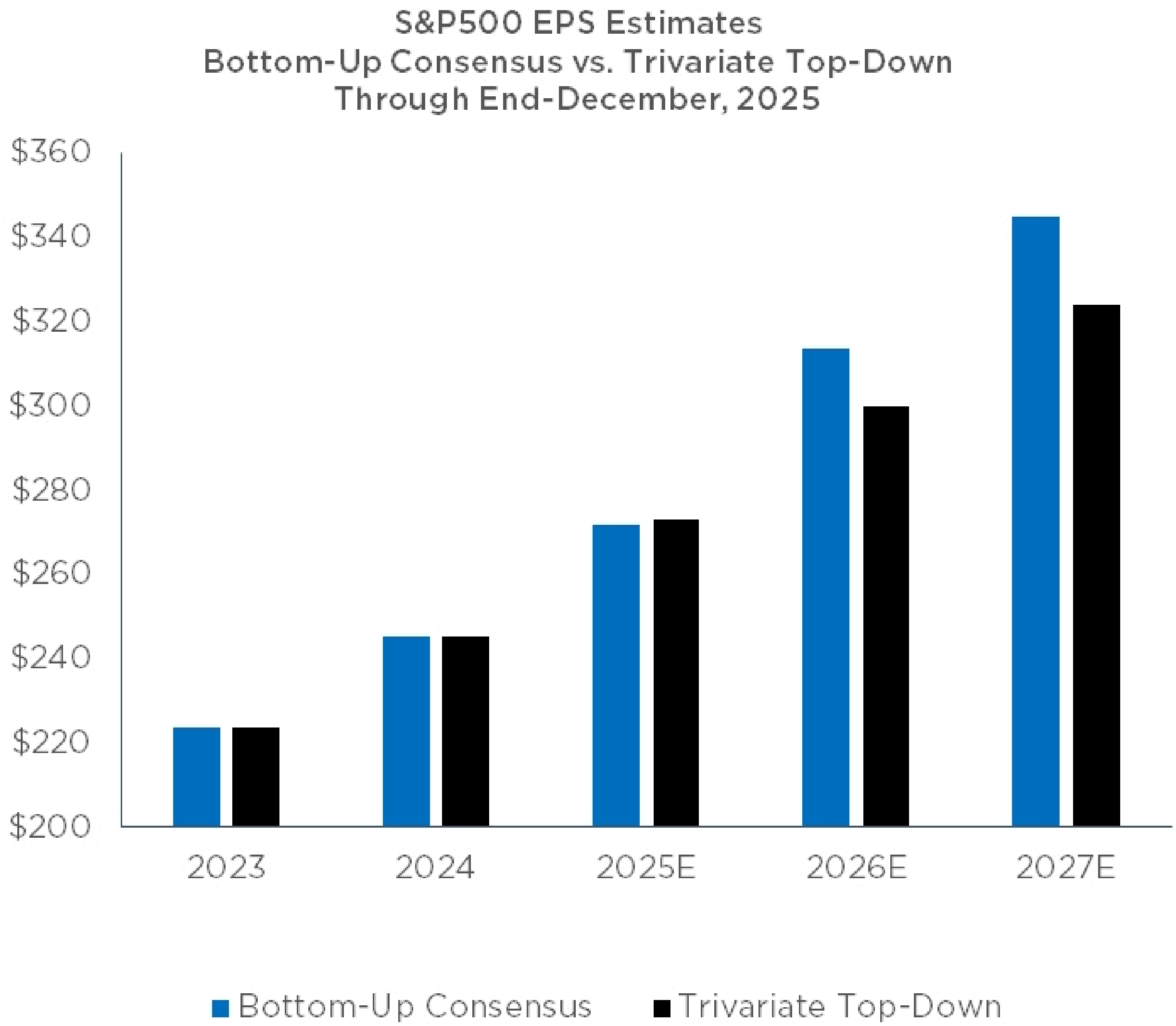
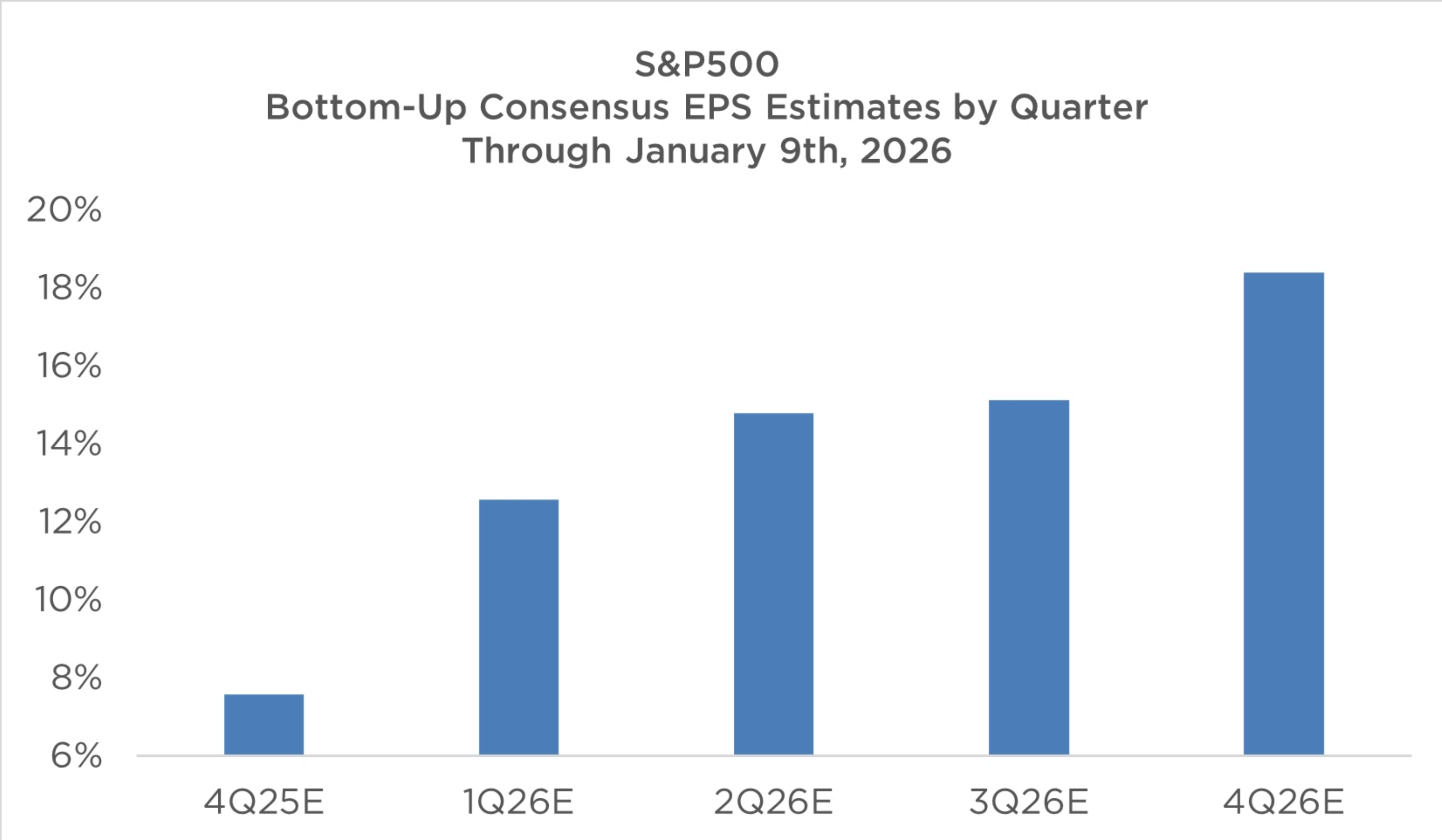


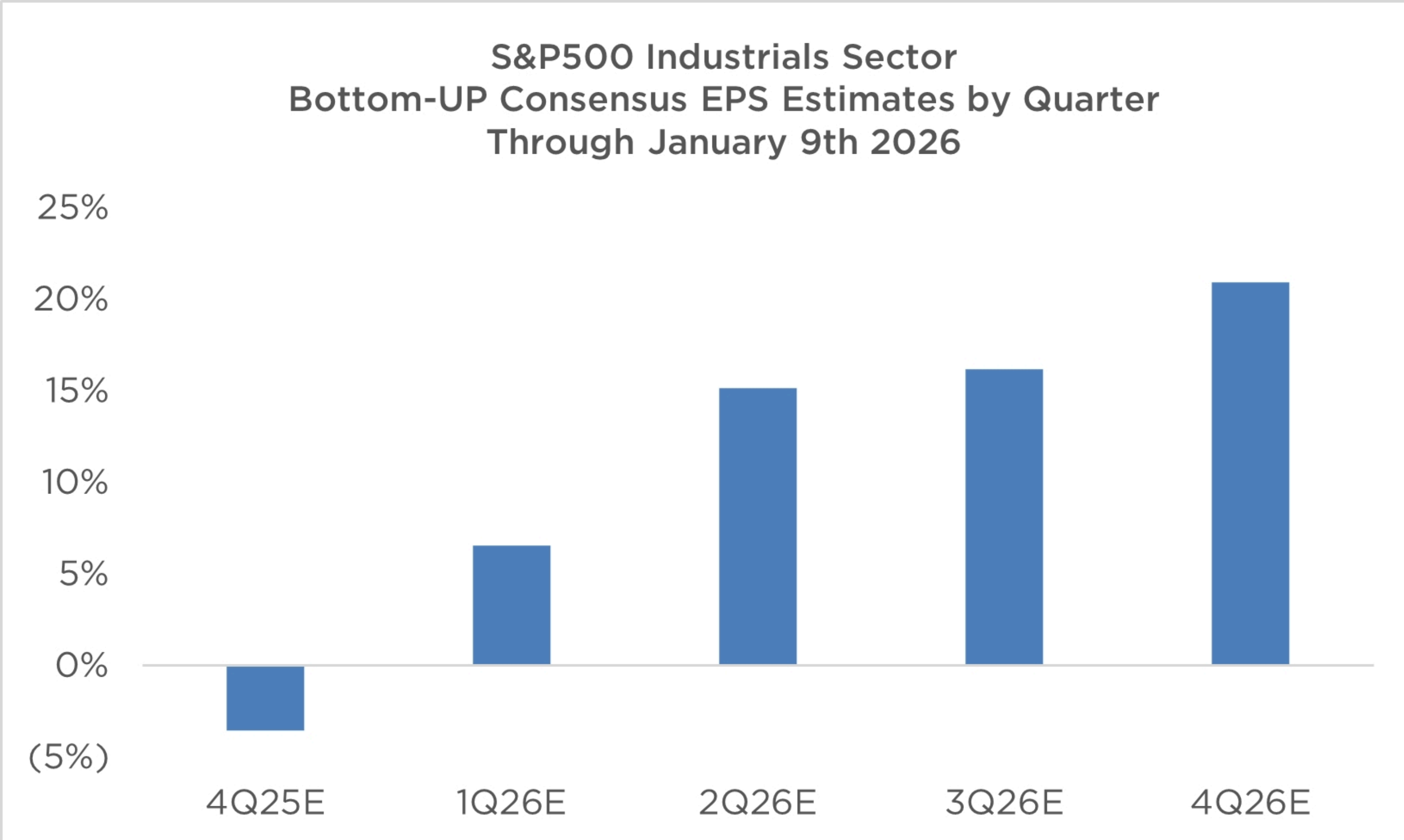
Source: Trivariate Research, LP

We consistently received questions about our forecasts relative to consensus on the S&P500 earnings and **when** we suspect we will see downward revisions. Below we show the bottom-up estimates on a sequential basis. The consensus embeds 12.6% EPS growth in Q1, 14.8% in Q2, 15.1% in Q3 and 18.4% in Q4. Our sense is the imminent earnings season, reported Q4 2025 results and guidance for 2026 will be reasonably strong, so we don't suspect imminent misses. We currently suspect conditions will remain robust enough that April earnings are achievable. If we had to guess, it is Q1 results and Q2 guidance (likely May or June) where we start to see the risk-reward of estimate achievability start to skew to the negative.



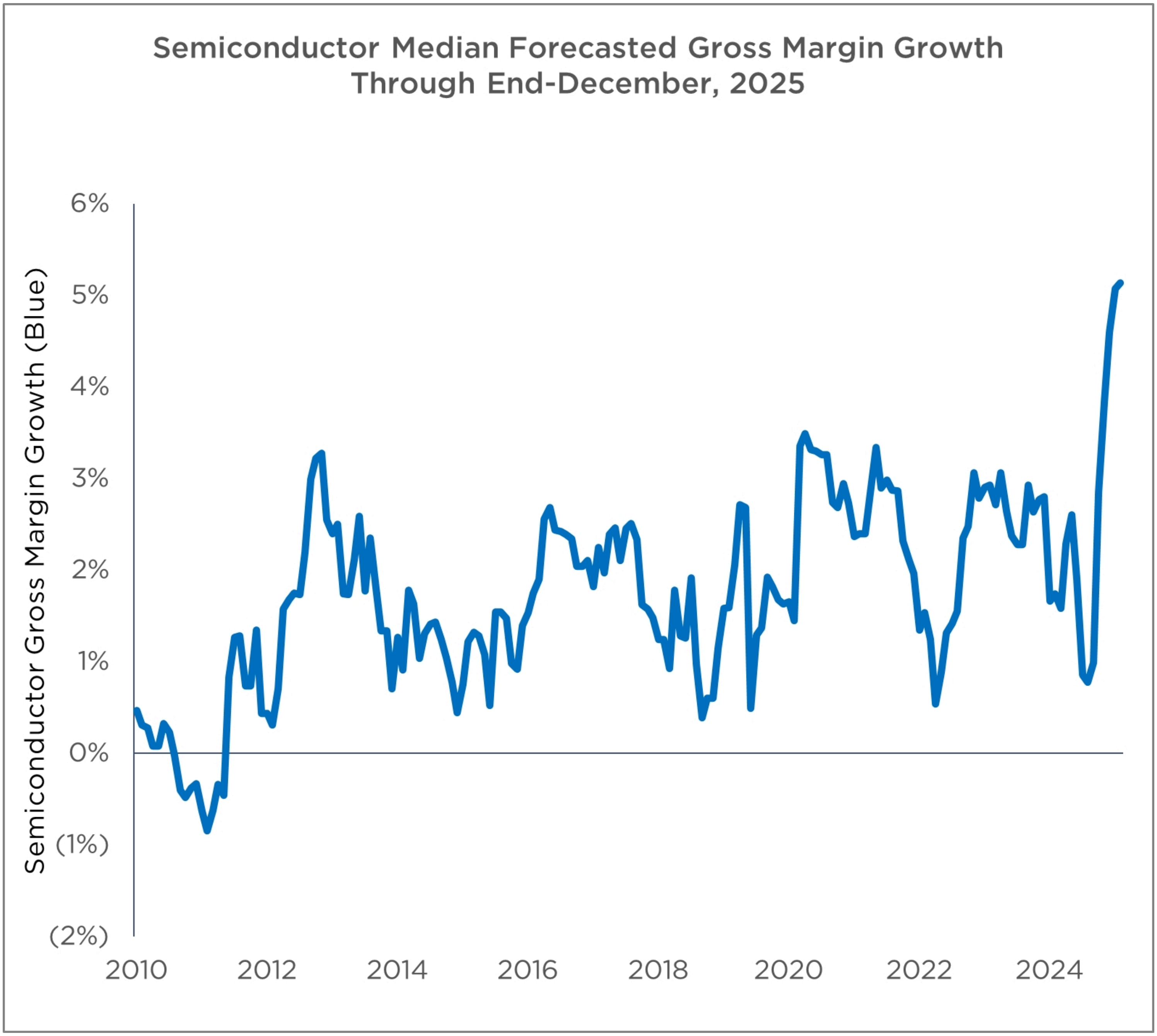
Source: Trivariate Research, LP

<u>We were also asked several times about which sectors we thought had the least achievable estimates</u>. We think the estimates in Industrials, Technology, and Consumer Discretionary are particularly vulnerable. Industrials' estimates, even against easier comps, embed acceleration that seems challenging given current conditions. Trivariate's Proprietary Industrial Activity gauge leveled off in Q4 after slightly increasing in Q3. North American Carloads are lower now than at the end of Q3, though they made a V-shaped recovery in the second half of December. US manufacturing utilization modestly weakened. The ISM declined modestly, ending November below September levels and still below the important "50" threshold. The Baker Hughes Rig Count remained relatively stable during Q4, though well below levels in the first half of the year. The US Auto SAAR is slightly lower at the end of Q4 than end of Q3, though the end November data of 15.6 million was a touch above the 15.32 million from the end of October. Overall, it is not obvious why there would be a huge acceleration in earnings for most exposed companies, outside Aerospace & Defense, where government spending tends to help over the long-term, but not immediately.



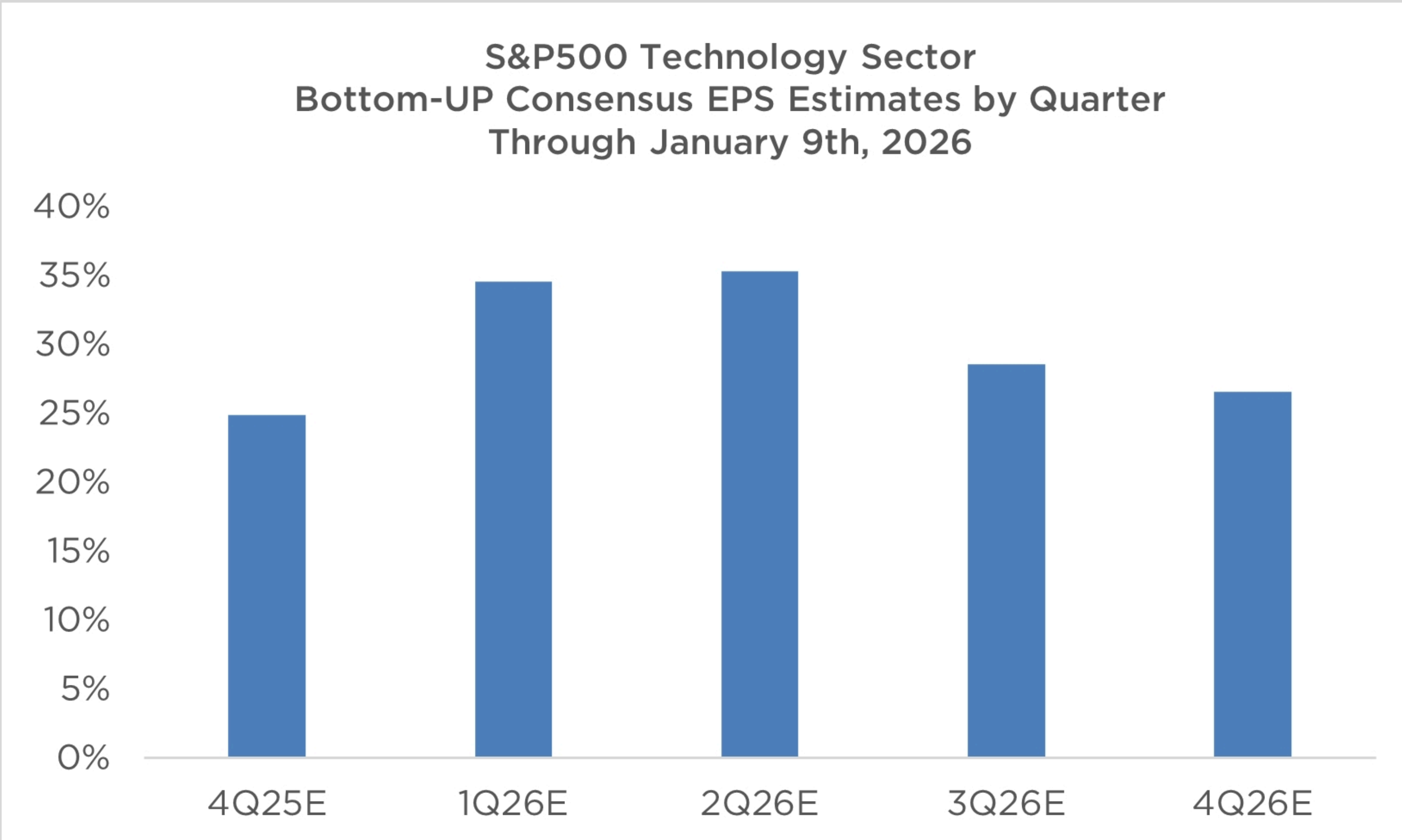
Source: Trivariate Research, LP

Technology sector estimates also seem particularly high. Microchip (MCHP) pre-released positively last week, and we got several questions about memory pricing and the sustainability of strength of Sandisk (SNDK), Micron (MU) and the rest of the storage complex (Western Dig. and Seagate). We feel confident Q4 results and Q1 guidance will be strong. But, estimates certainly embed those expectations. The median Semiconductor company is expected to have over 500bps of gross margin growth this year, the highest percentage in years (see below) and well above the “normal” 200bps of expected growth.



Source: Trivariate Research, LP

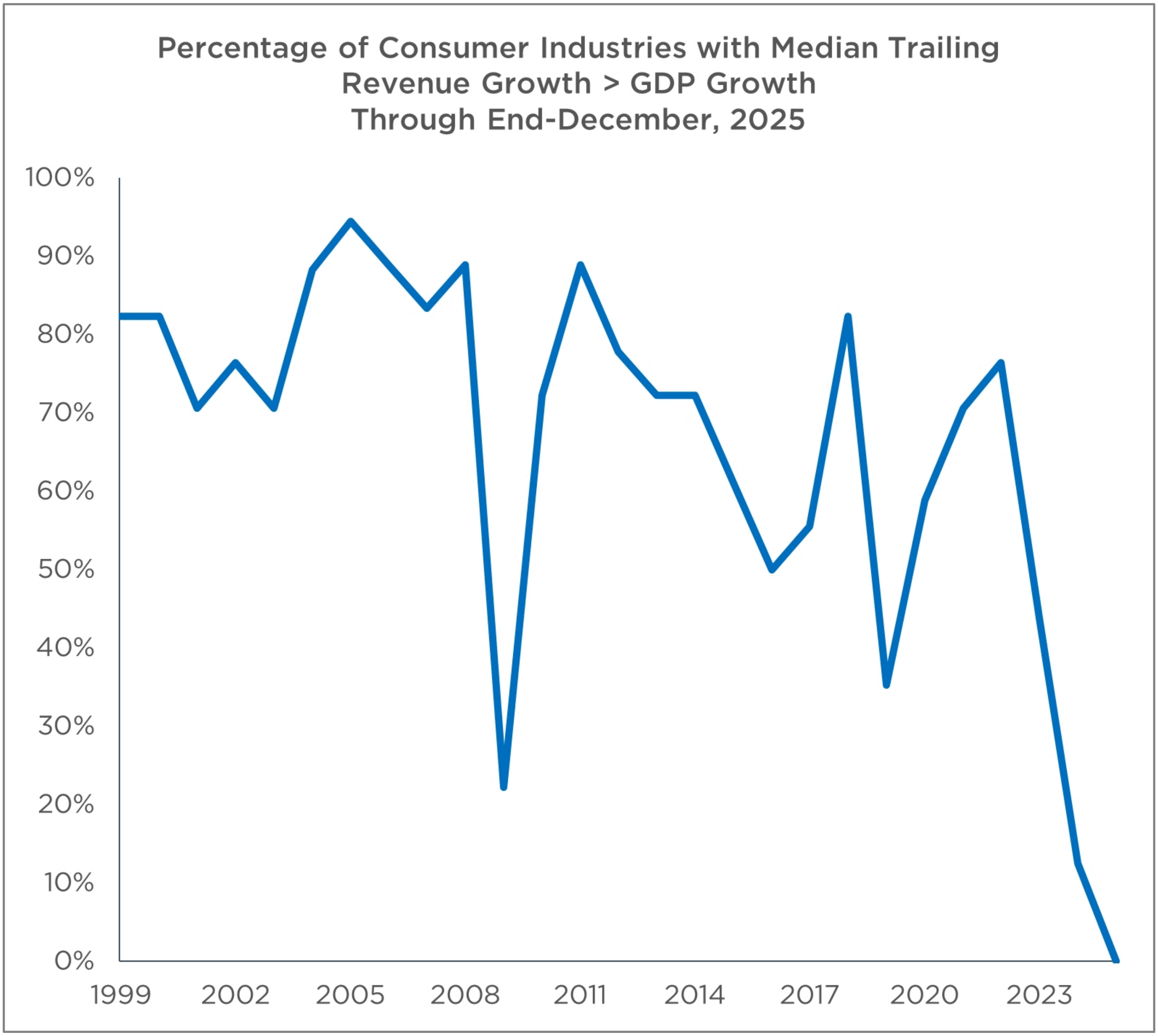
This is a large reason why the Technology sector expectations are high and accelerating through the middle of 2026. We expect Q2 numbers to be at risk. Q2 estimates of 35% year-over-year growth are likely going to be missed. The Morgan Stanley Technology Conference in early March 2026 is likely an interesting time to see how numbers are trending vs. consensus expectations. It is also worth noting that the Technology sector estimates decelerate in the second half of 2026. High expectations that decelerate can be interpreted as a negative as first some companies might miss expectations, and second the collective group of companies have decelerating trends. We shall see.



Source: Trivariate Research, LP

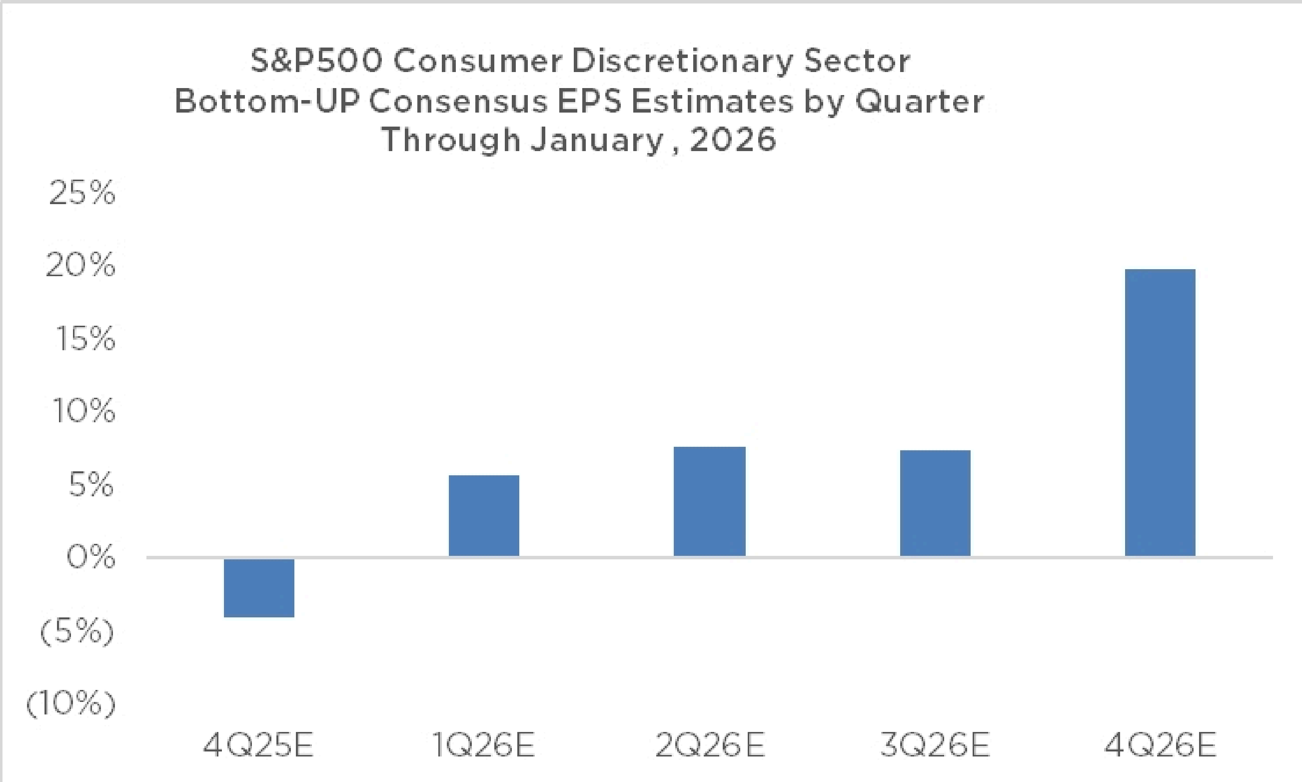
While the One Big Beautiful Bill is widely known—and a potential housing stimulus now appears possible, with Government-Sponsored Enterprises potentially purchasing mortgage-backed securities—current consumer spending forecasts still appear to require such stimulus to be realistic/achievable.

We think it makes sense to own Homebuilders which have suppressed expectations, but in aggregate Consumer Discretionary stocks are forecasted to have accelerating revenue that likely isn't achievable. We analyzed the revenue growth of the 16 different sub-industries within the Consumer Staples and Consumer Discretionary sectors. Last year, for the first time in at least 25 years, NONE of these industries had revenue growth above nominal GDP growth.



Source: Trivariate Research, LP

While in aggregate the Consumer is considered to be in solid -but slightly eroding shape - the estimates embed a huge amount of fiscal stimulus positively impacting their earnings. After a decline in year-over-year growth, estimates accelerate all year. Our sense is that it is far too early to bank on the kind of second half rebound in Consumer Discretionary earnings currently in the consensus numbers - 20% growth!



Source: Trivariate Research, LP

PUSHBACK

The primary area of pushback we have received so far is on our view that the Fed might not have as much impact on multiples going forward as they had in the past. **So** far, we look wrong - though the news has evolved some this past week. The Polymarket and the WIRP function in Bloomberg indicated that, when we wrote our year-ahead outlook, investors expected no more cuts from the Fed until June 2026, and two total this year. Since then, however, the policy backdrop has become more fluid. President Trump indicated that he will announce the new Fed Chairperson before the Davos conference. Separately, **Federal Reserve Governor Stephen Miran** publicly said he's looking for much deeper interest rate cuts—about **150 basis points over the course of this year**—to help boost the labor market and because he believes underlying inflation is close to the Fed's target. He made these remarks in a **Bloomberg TV interview** and reiterated them in subsequent media coverage. In addition, some commentators noted that **U.S. Treasury Secretary Scott Bessent** has also pushed for significant rate cuts (on the order of 150 bps or more) in broader discussions on monetary policy, though his comments were from earlier and tied to broader economic growth arguments. Moreover, **President Trump announced that he's directing Fannie Mae and Freddie Mac to buy up to** $200 billion in mortgage-backed securities (MBS) as part of a housing-market intervention. He posted on Truth Social that he is instructing "his representatives" to buy $200 billion in mortgage bonds, and that this action is intended to **lower mortgage rates and monthly payments** for homeowners. This past week, **mortgage rates fell**, with 30-year rates dipping near *6%*, their lowest in years, on expectations these purchases could support the secondary mortgage market. Housing stocks and mortgage-related equities rallied on the news as well. Which makes sense to us, given they have low expectations.

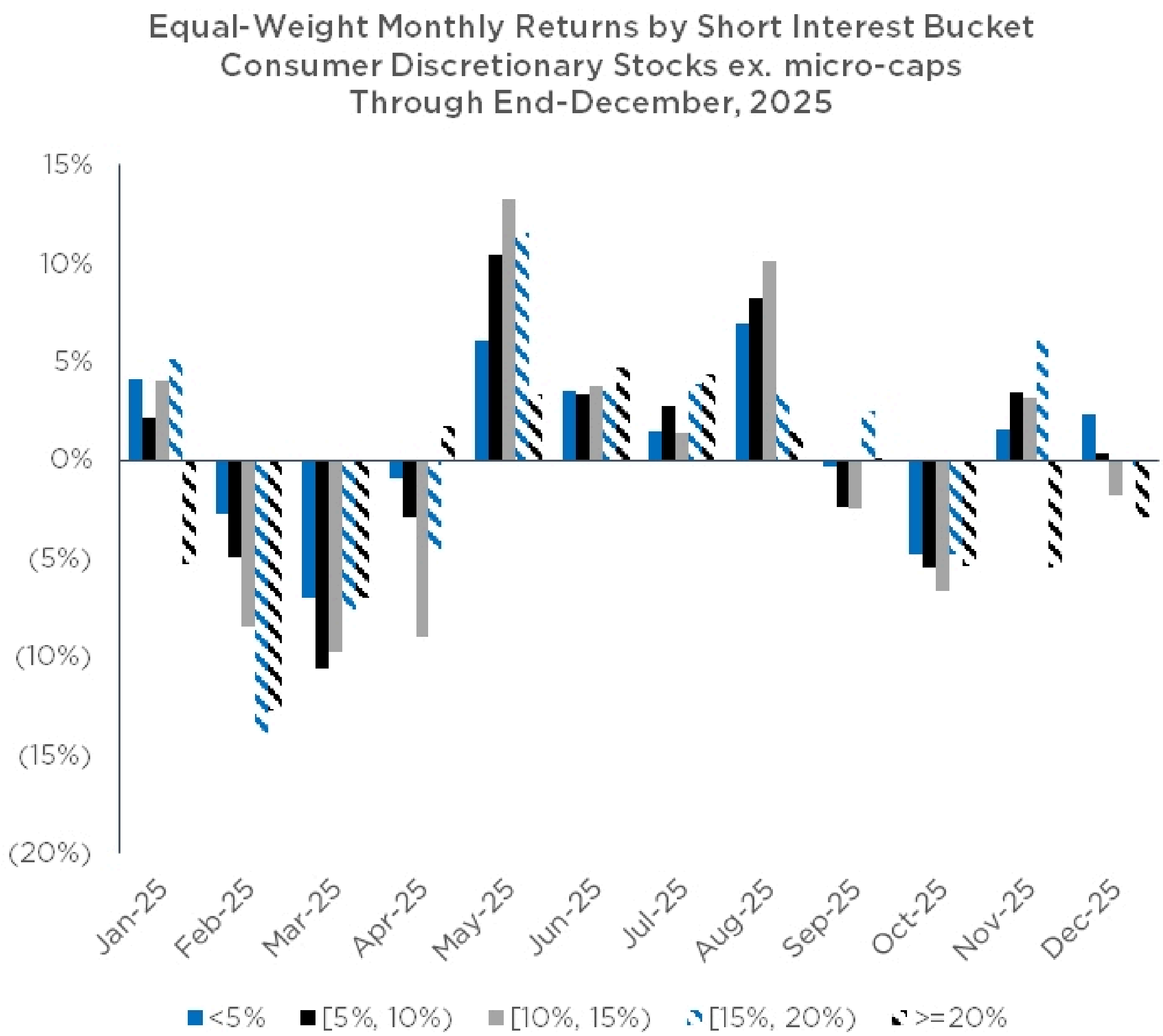
We indicated in our bull case scenario in our outlook that INCREMENTAL Fed accommodations would be bullish, and to some extent the market is moving in that direction already this year. If you take the consensus 2027 EPS estimates (assume we are wrong and these numbers are achievable) and then apply the all-time high price-to-forward earnings for the market to that multiple, that would be $8450 on the S&P500, or 21% upside from here. We don't think this is likely.

CONSENSUS VIEWS

What is the consensus view? There is no question that the consensus view of US equities is bullish. We laid out an argument that multiple contraction is more likely than expansion, that EPS estimates are likely too high, that the median company is struggling to show margin expansion, and that the consensus was quite bullish as part of our outlook. **The price action so far**

has only reinforced the bullish narrative. investors like small caps, Technology, and Financials. We think our overweight in Healthcare, despite the fact it was the best performing sector in Q4, is still contrarian.

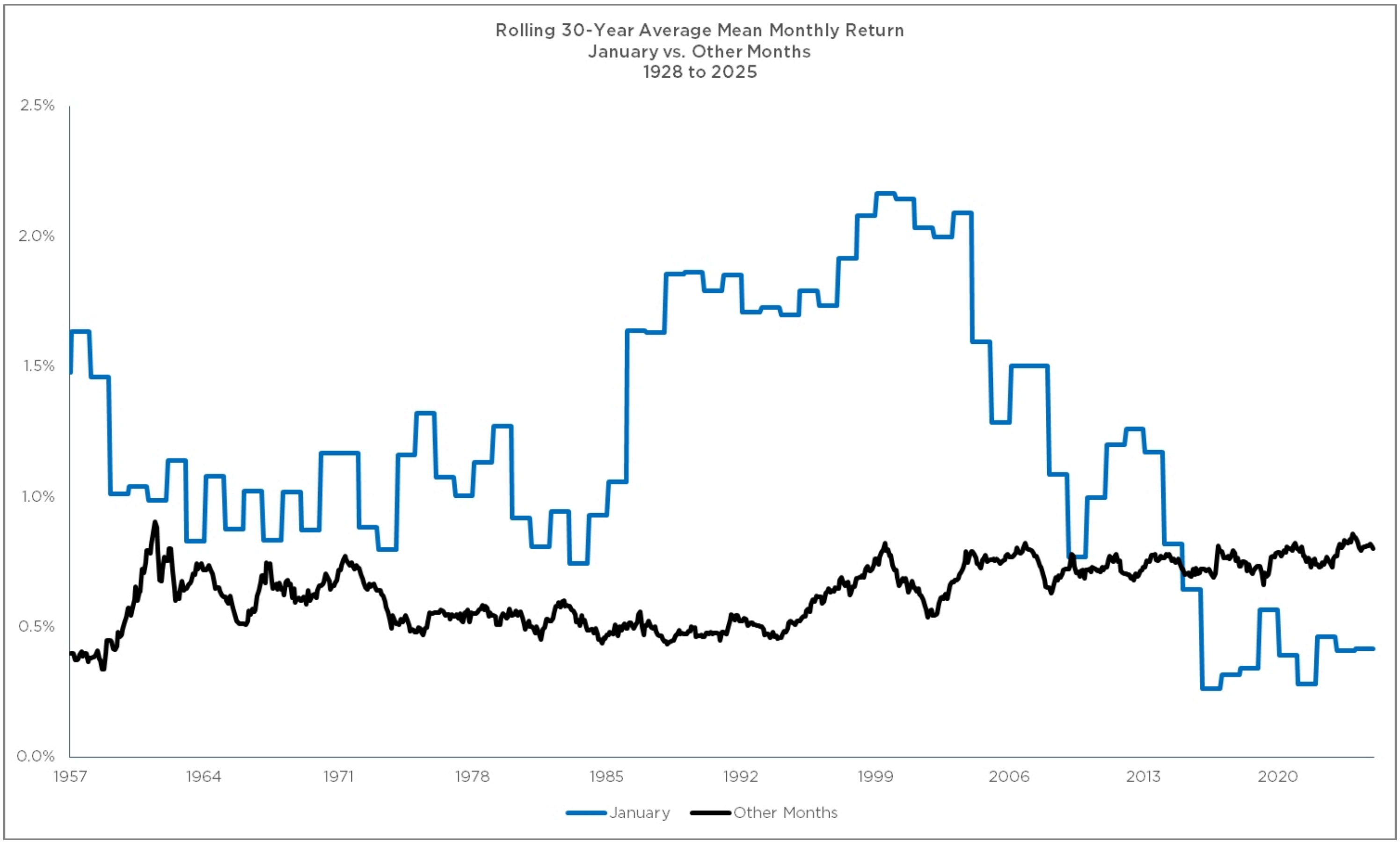
Shorting stocks has been extremely challenging out of the gate this year, with profitless baskets already up double-digits in some cases this year. As we highlighted in our outlook, we think investors have to be very cautious shorting high short interest stocks, and only short those where they are confident January estimates or April guidance will be negatively impacted. The month-to-month volatility of high short-interest stocks has been astounding. Below we show that 6 of the last 8 months of last year, stocks with 15-20% short interest OUTPERFORMED. That has been the case so far month-to-date as well. We don't think the consensus view is that the junk will still run, but our best guess is it is correlated to the incremental dovish view from the Fed and a typical January risk-on mentality.



Source: Trivariate Research, LP

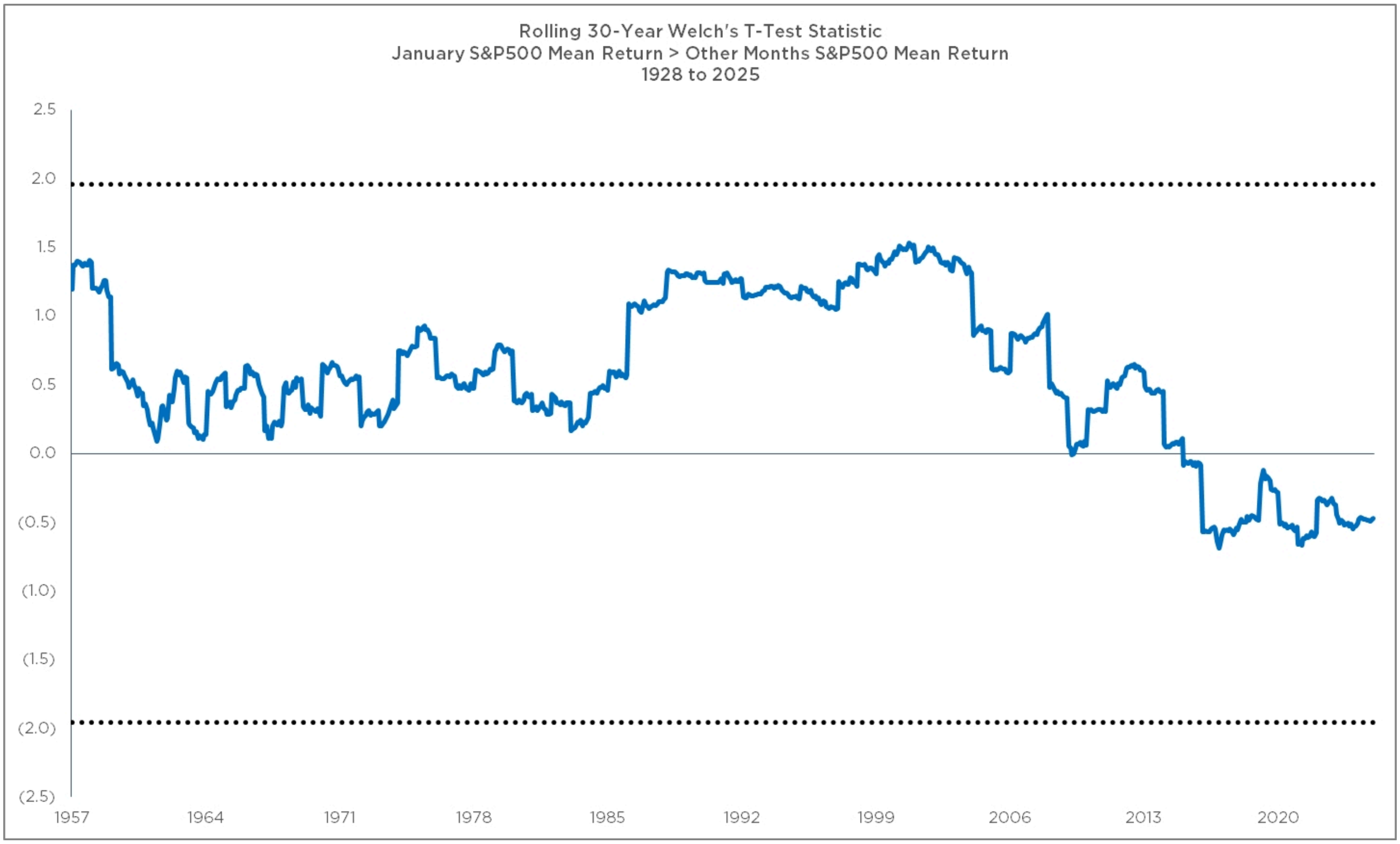
There is no January effect

We are asked last week about the risk-on nature of the month of January - i.e, is there a demonstrable "January bullish effect." The answer is - there isn't one anymore. We looked at the rolling 30-year average mean monthly returns of January vs. other months. Over the last decade the average has been WORSE for January, though there was some effect from 1958 through 2000.



Source: Trivariate Research, LP

We then looked for statistical significance between the rolling 3 Welch's T-Test for the difference of mean between January returns and all other months. The test statistic has never been statistically significant in any 30-year window since 1928 (see below).



Source: Trivariate Research, LP

CONCLUSION

We are more neutral than bullish on US equities for the following five reasons:

1. The earnings expectations appear too high, particularly in Technology and Industrials, and the penalty for missing estimates has been harsh.
2. Margin expansion has become increasingly challenging for the median stock, and multiple expansion is correlated to margin expansion.
3. We don't think that if the Fed cuts interest rates it will drive the price-to-forward earnings expansion as has been the case for the last three years.
4. The historical precedent for continued double-digit returns is low, though there have been three prior examples in the past 100 years.
5. The bottom-up and top-down consensus are bullish, so investors can't romanticize they are contrarian bulls. The top-down consensus has been consistently wrong over the past few years.

Non-Technology Compounders

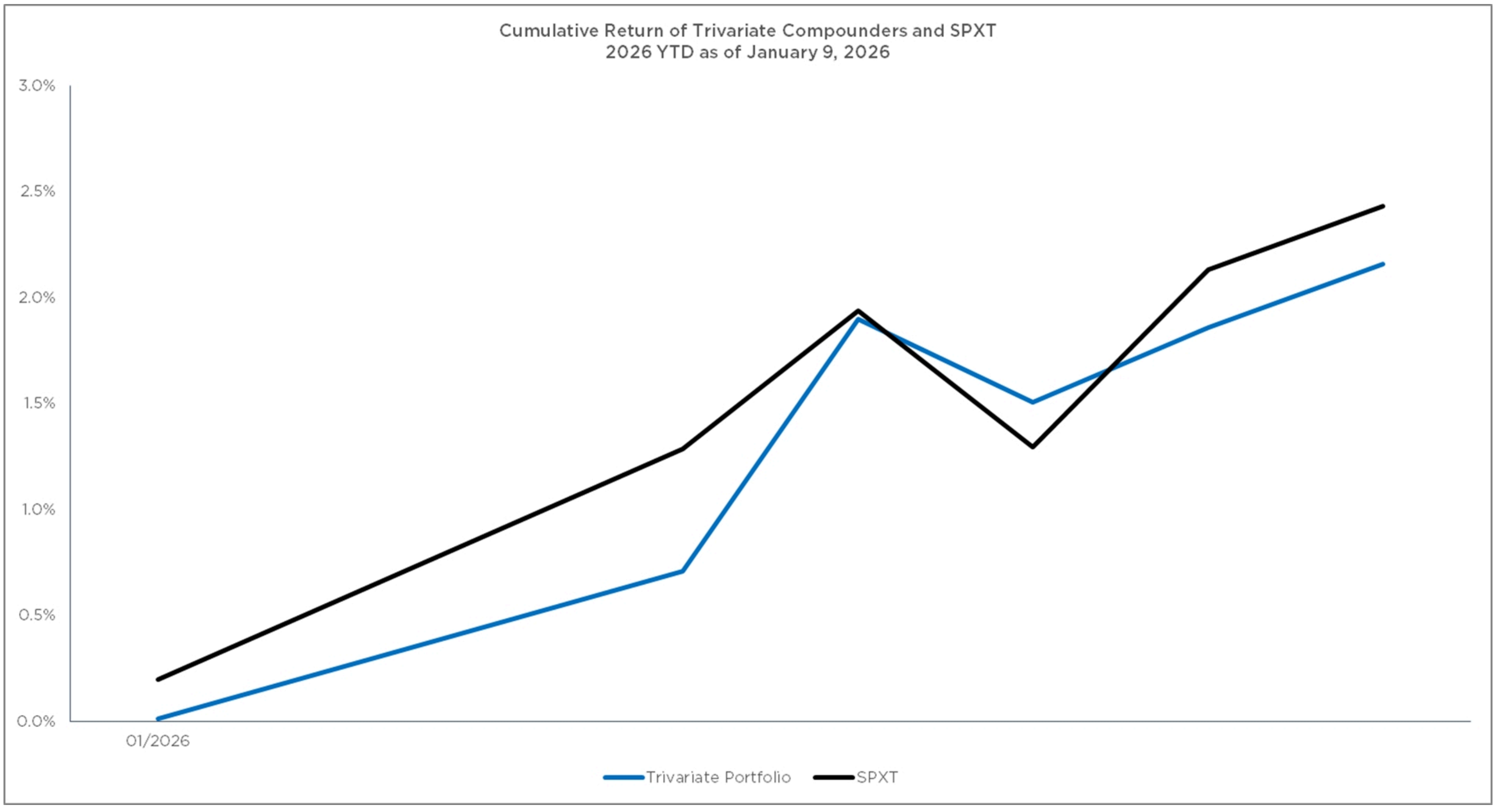
We launched a new ideas basket this year, which is 20 Non-Technology Compounders. Ideas below.

Trivariate Compounders Portfolio
As of End-December, 2025

Ticker	Company Name	Industry	Market Cap.	Beta	CSR
AMZN	Amazon.com, Inc.	Broadline Retail	2,467.52	1.53	53%
BRK.B	Berkshire Hathaway	Financial Services	1,084.82	0.28	65%
V	Visa Inc.	Financial Services	670.64	0.68	66%
PM	Philip Morris	Tobacco	249.68	(0.17)	73%
TMUS	T-Mobile US, Inc.	Wireless Telecom. Serv.	227.10	0.02	84%
TMO	Thermo Fisher Sci.	Life Sciences Tools & Serv.	217.70	0.79	54%
LIN	Linde plc	Chemicals	199.10	0.42	63%
SCHW	Charles Schwab	Capital Markets	177.53	0.77	65%
BKNG	Booking Holdings	Hotels, Rest. & Leisure	172.62	0.92	74%
UBER	Uber Technologies	Ground Transportation	169.78	1.15	75%
NEE	NextEra Energy	Electric Utilities	167.19	0.34	90%
GILD	Gilead Sciences	Biotechnology	152.28	0.33	82%
SYK	Stryker Corporation	Health Care Equip. & Supp.	134.41	0.57	61%
WELL	Welltower Inc.	Health Care REITs	127.39	0.25	75%
WMB	The Williams Comp.	Oil, Gas & Consumable Fuels	73.41	0.50	81%
CTVA	Corteva, Inc.	Chemicals	45.29	0.52	76%
CPNG	Coupang, Inc.	Broadline Retail	43.09	1.03	78%
VMC	Vulcan Materials	Construction Materials	37.69	0.70	59%
XYL	Xylem Inc.	Machinery	33.16	0.80	55%
LZ	LegalZoom.com, Inc.	Professional Services	1.76	1.09	77%

Source: Trivariate Research, LP

The portolio is up 2.2% YTD, vs. its comparable index of 2.4%.



Source: Trivariate Research, LP

Important Disclosures

Analyst Certification

The analysts, Adam Parker, Maxwell Arnold, Chang Ge, Jesse Goodman, Colin Cooney 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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