Biweekly Investment Insights: AI resurgence propels equities as breadth builds

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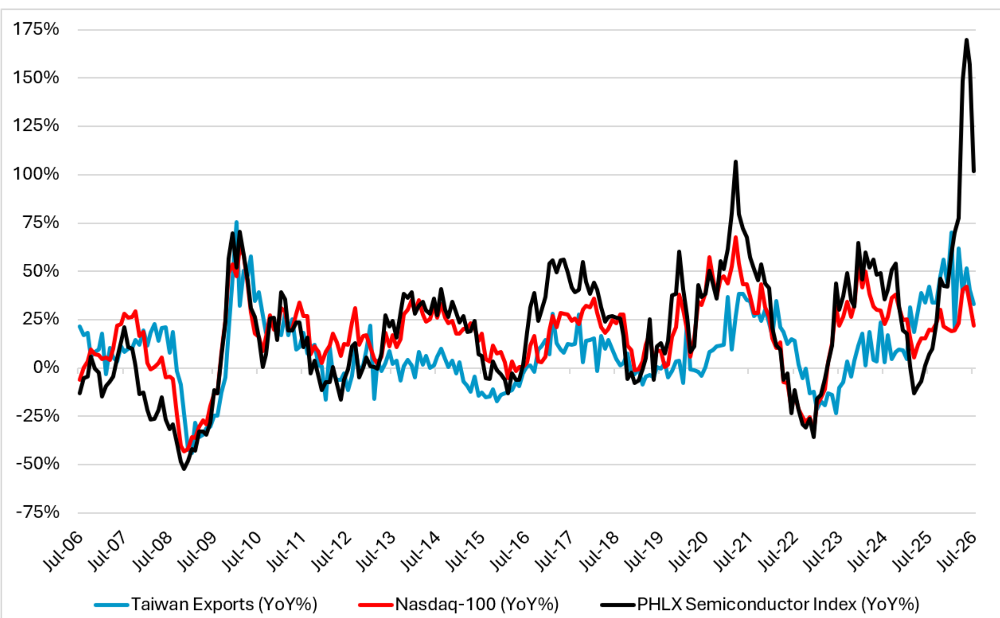
Strong earnings push equities to new highs amidst higher rates

- AI theme continues to underpin equities & earnings, broader EPS growth rates support widening market breadth
- Softening Fed rate hike expectations have also helped risk assets while global bond yields hover near multi-decade highs
- Markets historically choppy heading into U.S. November midterm elections, then advance over ensuing months

Biweekly Chart in Focus: Taiwanese exports, Nasdaq-100 Index® (Nasdaq-100®), PHLX Semiconductor™ Index YoY% have cooled but still at elevated levels



Source: Bloomberg. As of August 14, 2026.

Summary

Although the focus is the impact of AI on the U.S. economy and markets, the AI theme is, of course, a global phenomenon. Per our Biweekly Chart in Focus, if looking at Taiwanese exports as a proxy for global AI and technology demand, though annual growth has slowed it remains at a very healthy 39.2% on a YoY basis as of July. Nasdaq-100 and semiconductor YoY returns similarly remain at elevated levels despite having slowed as momentum cooled.

From a bottom-up perspective, Q2 earnings season helped allay AI spending concerns in the near-term. However, just as importantly, earnings helped to underpin a broadening of equity returns as U.S. equities hit new highs—the median Russell 3000 EPS growth rate is 15% in Q2 YoY, the highest since Q3 2021.

Also helping risk assets over the past two weeks at a macro level were softer July U.S. CPI and PPI reports which scaled back the market pricing of Federal Reserve rate hikes. As of August 17th, there is an 89% chance of a 25 basis point hike by year's end versus *at least one* 25 bp hike priced in only a week earlier. While a near-term relief for markets, investors are still contending with multi-year highs in U.S. Treasury yields as the 10-year is at 4.70% and global government bond yields also remain elevated.

As the markets move past Q2 earnings, summer winds down, and the calendar turns to September, based on history, we suspect that the market narrative will turn to the U.S. midterm elections in early November. Historically, per Goldman Sachs, market volatility ramps up heading into midterm elections. Yet, these elections tend to be more noise than anything as the S&P 500 typically averages a total return of 14.1% over the six months following midterm elections, since 1970, according to BlackRock.

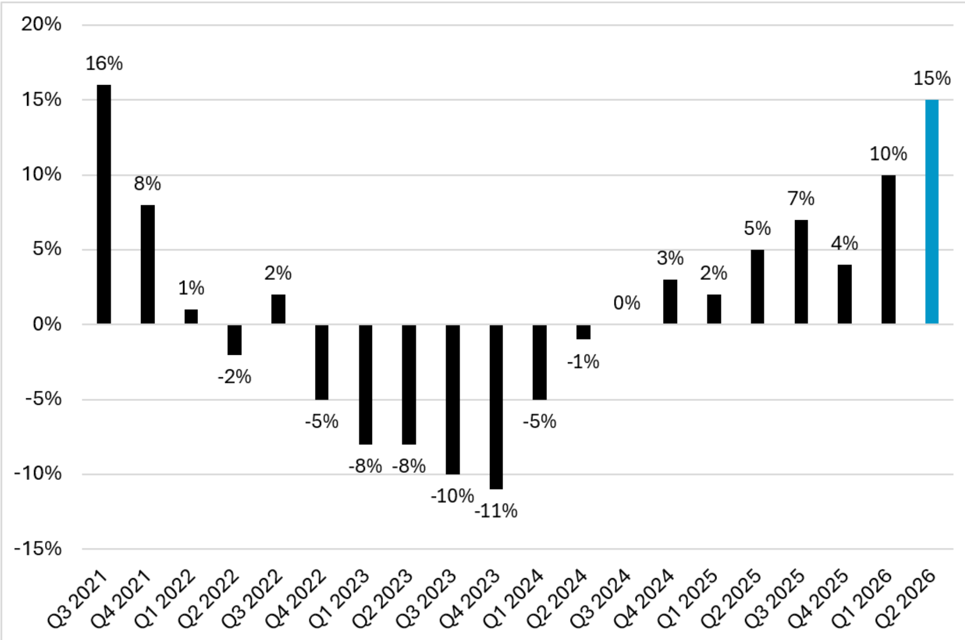
Details

A strong Q2 2026 earnings season winds down

With only about 13% of S&P 500 market cap left to report over the last two weeks of Q2 earnings season (~8% of this being NVDA), around 90% of reporting S&P 500 companies have beaten EPS estimates, per Bloomberg. Focusing on the megacap tech space, which has helped the latest rebound in U.S. equities (Nasdaq-100 is +11% from its July 29th lows), 89% of Nasdaq-100 companies that have reported as of August 14th have beaten EPS estimates. The Nasdaq-100 blended (actuals + estimates) EPS growth rate now stands at approximately 76%—significantly higher than the consensus growth forecast of 29.2%. As discussed in our prior piece, while this is skewed by significant contributions from Amazon and Google due to unrealized gains in equity stakes, these are nevertheless very strong earnings trends.

Stepping back, the growth rate of the median stock's EPS in the Russell 3000 Index is 15% YoY—its highest rate since Q3 2021 which benefited from Covid-19-time frame comparisons (Figure 1).

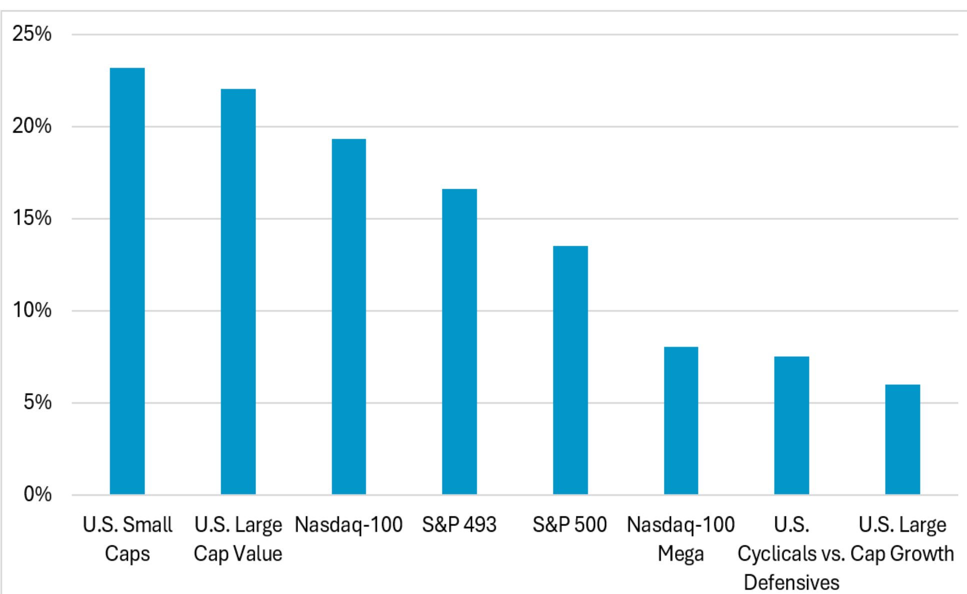
Figure 1: Russell 3000 median stock EPS YoY growth



Sources: Morgan Stanley, FactSet

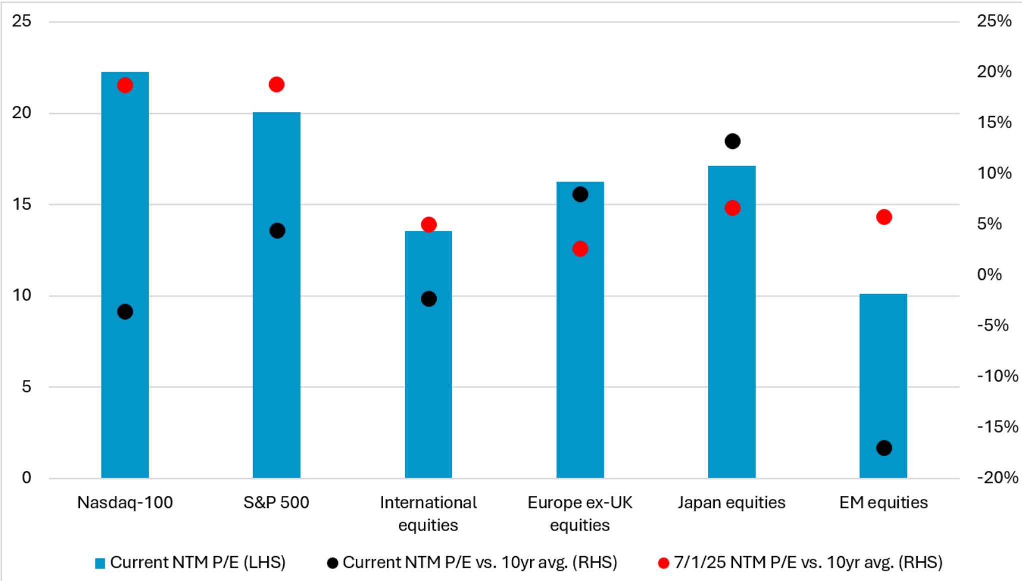
This widening of EPS growth breadth supports the broadening of U.S. equity returns on a YTD basis (Figure 2) while also keeping equity valuations in check relative to their 10-year averages compared with the middle of 2025 (Figure 3).

Figure 2: Thematic 2026 YTD U.S. equity returns



Source: Bloomberg. As of August 14, 2026.

Figure 3: Global equity next 12-month P/Es relative to 10-year averages

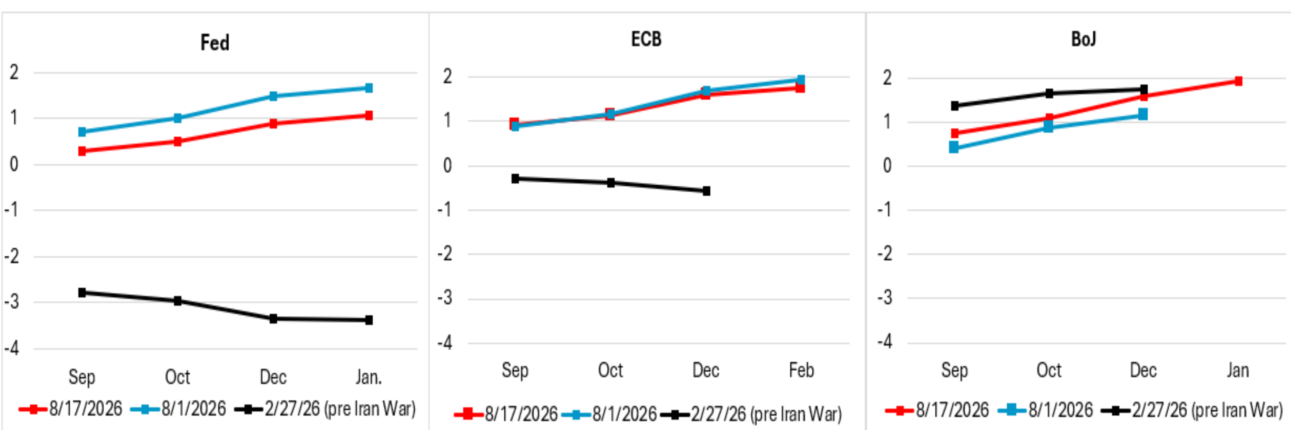


Source: Bloomberg. As of August 17, 2026.

Softer U.S. inflation trends yet central bank rate expectations and government 10-year yields remain elevated

Softer Tier 1 U.S. economic data—July NFPs and retail sales—coupled with cooler-than-expected inflation—July CPI (core inflation was up just 2.5% year-over-year in July, the slowest since 2021) and PPI—caused markets to largely price out a September Fed rate hike. The latest data also brought down expectations for the next several Fed meetings (Figure 4). In the very near-term, the markets will be parsing global central bankers' signaling at the upcoming Jackson Hole Symposium on August 27th to 29th.

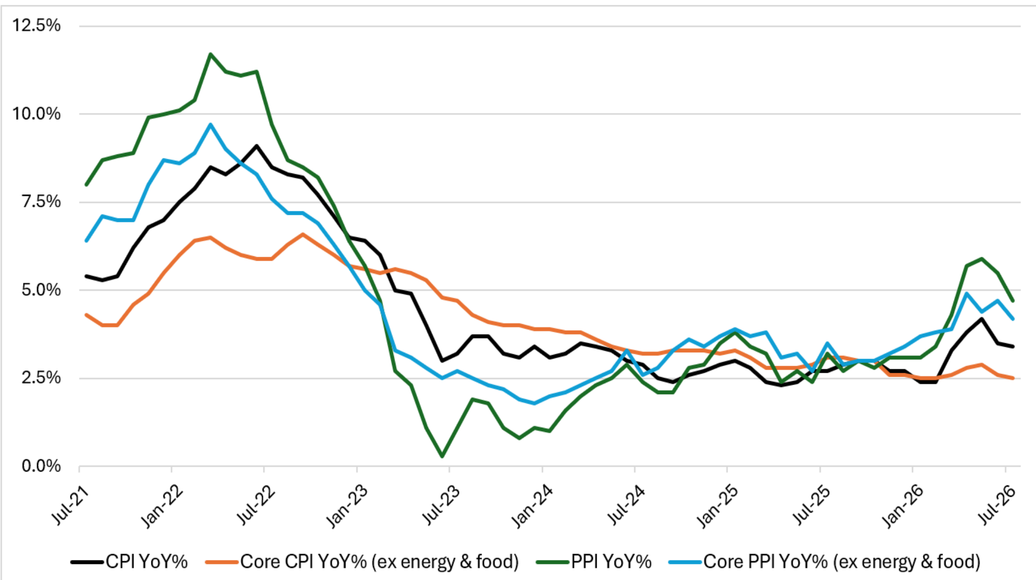
Figure 4: Number of 25 bp rate hikes or cuts priced in by market for major central banks



Source: Bloomberg

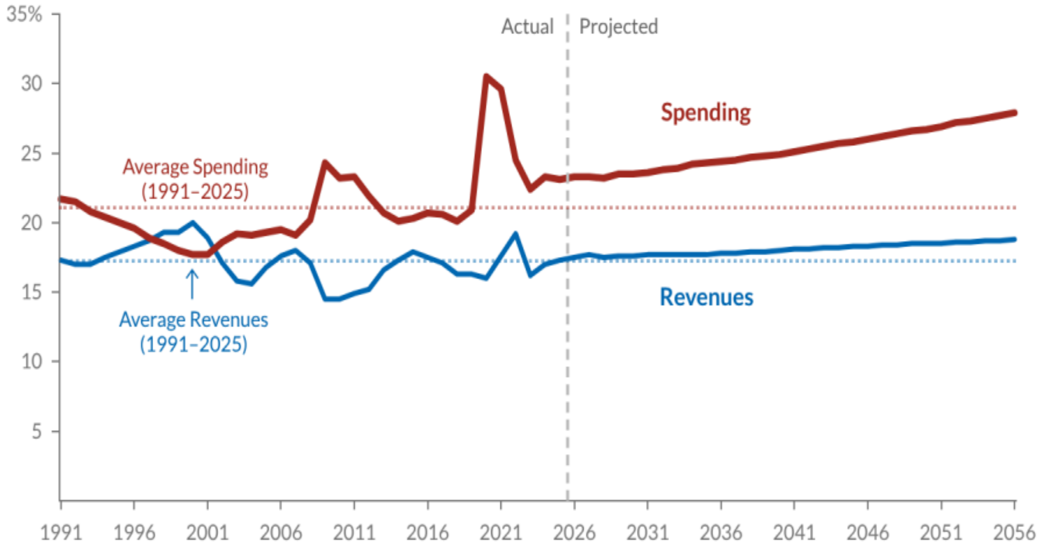
However, Treasury yields have also remained elevated as U.S. inflation remains a source of concern for the Fed (Figure 5) with oil prices hovering around $80/bbl for WTI crude since late July, Fed policy uncertainties lingering (as we showed in the decomposition of the YTD change in Treasury 10-year yields in our prior piece), and U.S. government debt levels to climb leading to widening fiscal deficits (Figure 6). This, of course, is not only a U.S. dynamic as global bond yields are at multi-year highs (Figure 7). While market pricing of Fed rate hikes has softened, as Figure 4 also shows, the market pricing of ECB and BoJ's rates trajectory is higher relative to the Fed as they battle inflation, energy supply shocks (more so than the U.S. which is an energy exporter), and fiscal concerns.

Figure 5: U.S. inflation measures have moderated, though remain sticky



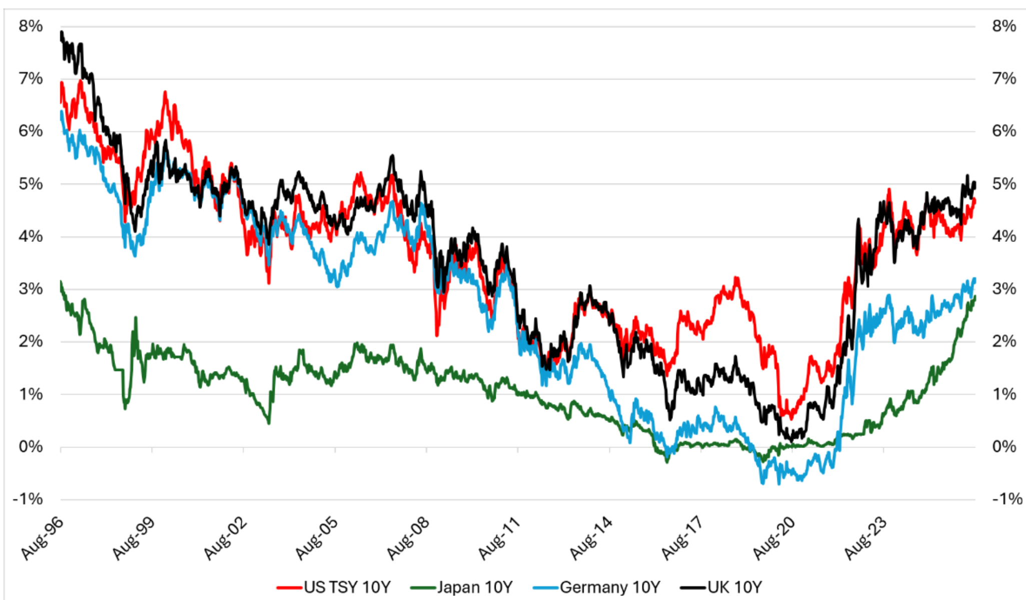
Source: Bloomberg

Figure 6: U.S. federal spending & revenues (% of nominal GDP)



Source: Office of Management and Budget, Congressional Budget Office, Peter G. Peterson Foundation

Figure 7: Global government 10-year debt yields remain elevated



Source: Bloomberg

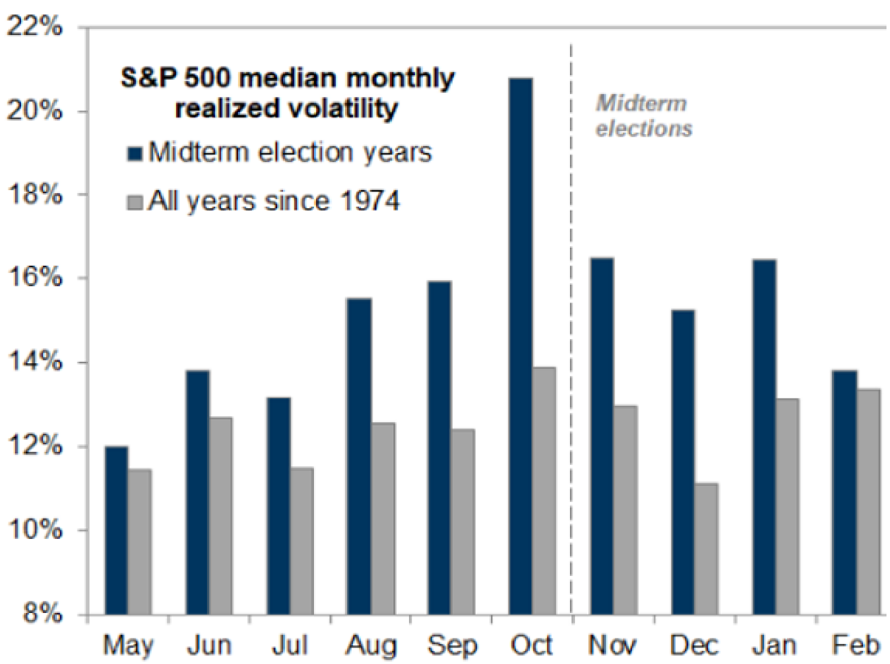
Historical U.S. midterm election trends

As recent U.S. elections cycles have shown, predicting outcomes can be very difficult and, though informative, polling can prove to be unreliable. What can be useful for investors is looking at history as a gauge of market reactions leading into and following midterm elections in early November.

While historical averages cannot be relied upon as forecasts, Figure 8 below shows that equity volatility usually increases heading into midterm elections but then tends to fade. Figure 9 shows the total return for U.S. equities before and after midterm elections since 1970. The interesting part from Figure 9 is that S&P 500 total returns were 16.1% on average over the six months following mid-term elections in which the President's party either gains or keeps control of both chambers of Congress. However, when the governing party has a "trifecta" and subsequently loses control of at least one of the chambers of Congress during the midterms, forward 6-month returns were almost 6% lower (10.4%).

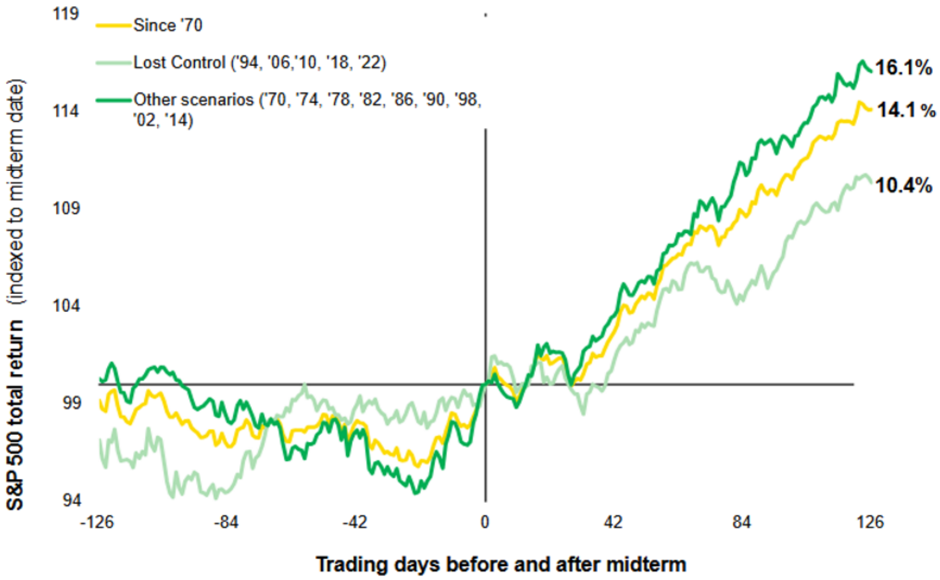
The takeaway from these charts for investors? If history is any guide, pre-midterm election volatility does not necessarily portend poor forward equity returns and timing the markets is difficult, particularly around what can be unpredictable macro-oriented events.

Figure 8: Equity volatility tends to rise headed into midterm elections



Source: Goldman Sachs

Figure 9: U.S. equities under different midterm election scenarios



Source: BlackRock. Notes: "Lost Control" defined as scenarios in which one party was controlling the presidency and both chambers of Congress heading into midterms, then lost control of at least one of them.