

It has been an eventful start to the year for equity markets. While the major indexes are currently in modestly positive territory, investors have had to navigate meaningful factor rotations (e.g., growth vs. value), sharp sector shifts (e.g., semiconductors vs. software), a barrage of policy headlines, and rising geopolitical risk.

Just 13 trading days into the year, small-cap stocks and cyclical sectors are handily outperforming the S&P 500 and mega-cap technology—extending a trend that began last fall and has recently picked up steam, marking a departure from the mega-cap market leadership over the past several years. While the S&P 500 is up just over 1% year-to-date, cyclical sectors such as Industrials, Energy, and Materials are all up in the high single digits. Moreover, the small-cap Russell 2000 index is up roughly 10% and hit an all-time high.

We believe this broadening of market leadership has more room to run, supported by an expected pickup in earnings growth outside of technology, driven by monetary and fiscal stimulus, rising foreign direct investment, onshoring activity, and still-intact secular trends such as AI-related capital spending. Earnings for the S&P 600 small-cap index are expected to grow by roughly 15% this year—on par with the S&P 500—while earnings for the Russell 2000 are projected to jump by more than 60%. Meanwhile, valuations still look reasonable for smaller caps, with the S&P 600 trading at approximately 18x forward earnings versus nearly 23x for the S&P 500. Accordingly, we are maintaining our cyclical and smaller-cap bent.

Small Cap and Equal Weight Outperformance to Start the Year Suggests Broadening Market



Small Cap Valuations Remain Attractive Compared to Large Caps



Despite what we view as a generally positive backdrop for equities, particularly for the average stock, the chances of a policy misstep appear to be rising. Since the start of the year, the administration has announced a barrage of policies (e.g., caps on credit card interest rates, bans on stock buybacks for housing and defense companies, instructions for Fannie Mae and Freddie Mac to buy \$200 billion in mortgage bonds, etc.), which have at times rattled financial markets. At the same time, geopolitical tension has flared with the extraction of Venezuelan President Maduro and the dustup with our allies over control of Greenland, which included the threat of a new round of tariffs. Still, it appears the administration is highly sensitive to anything that could disrupt its desire to keep inflation numbers in check, bolster the housing market, and lower interest rates ahead of the mid-term elections, which is likely why it was quick to find an off-ramp for the Greenland situation. Yet, the risk remains that one of these initiatives or geopolitical maneuvers could go sideways, complicating an otherwise constructive equity backdrop. Against this risk and given the average intra-year drawdown in the NASDAQ since 1990 is roughly 15%, we will continue to monitor potential market impacts and position our portfolios accordingly.

In the meantime, we are spending additional time sifting through the recent carnage in the software sector, where the relative performance versus semiconductors looks extreme and may present some longer-term opportunities.

Software may present select longer-term opportunities especially given divergence vs. semis



Jed Glick, CFA, Portfolio Manager – U.S. Equities

Commentary as of 1/22/26. Data and charts as of 1/22/26, per Bloomberg.

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- *Diverse Perspective*
- *Impactful*
- *Authentic*

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To be an agent for change in the finance industry by demonstrating a straight line between the support we receive as a women-owned firm and the support we provide to women in the industry and in the community.

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