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Monthly Insights: January Outlook

S&P 500

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Sector Price Action & Performance Review: S&P 500

The S&P 500 continued to consolidate through December though price made a marginal new all-time high on 12/26 in a lightly traded post-holiday session.

From a technical perspective, the long-term bull market trend that began in early 2023 remains in force. Evidence of "late cycle" dynamics have emerged as the Fed is now in the middle of an easing cycle while commodities prices have firmed over the intermediate-term spurring renewed concerns about inflationary pressure. Against this backdrop there has been some rotation away from speculative, long-duration themes like Crypto, Nuclear, Space and AI. However, cyclicals including semiconductors, banks, base and precious metal miners, airlines and retail stocks have caught a bounce from an easy Fed.

Economic prints have resumed with the re-opening of the Federal Government and November's inflation print came in below expectations which gives the Fed some cover to continue its dovish policy prescriptions. The base case for 2026 is continued moderating Growth with potential liquidity tailwinds from falling rates. Rates are setting up as a key pivot. Higher rates would likely complicate the Fed's policy goals and act as headwind to speculative trades.

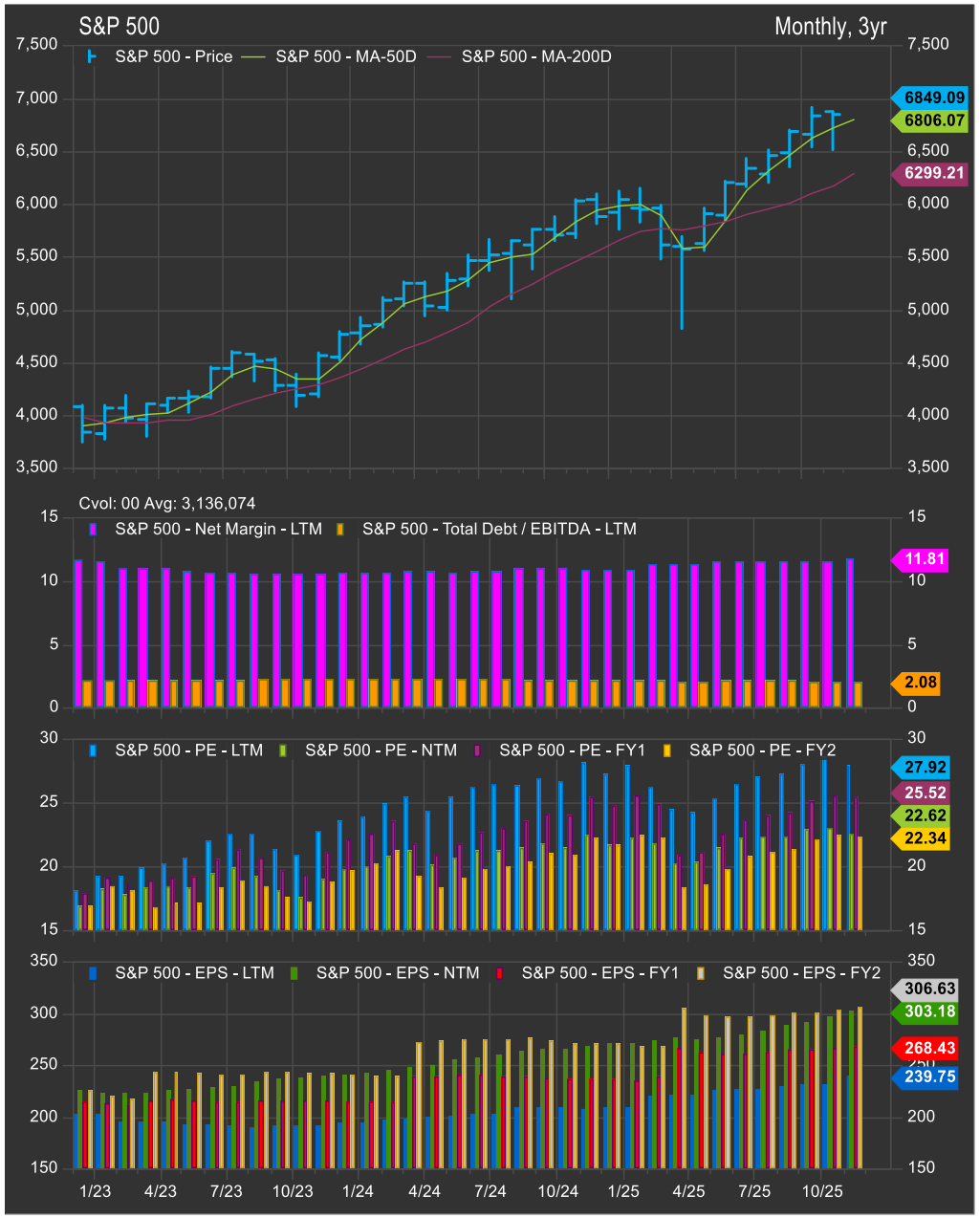
We think the current setup calls for a cautious but positive approach to equities as inflation risks have receded in the near-term, but structural risks still remain.

Our Elev8 Sector Rotation Model Portfolio starts January with the following sector allocations:

Elev8 Model Positions: January 2026

	BMK Weight	Elev8 Model	+/-
XLC	10.42%	13.51%	3.09%
XLK	34.52%	37.28%	2.77%
XLF	13.43%	15.11%	1.69%
XLI	8.16%	9.68%	1.52%
XLV	9.59%	10.99%	1.40%
XLY	10.47%	10.65%	0.18%
VNQ	1.83%	1.57%	-0.26%
XLB	1.82%	1.21%	-0.61%
XLU	2.23%	0.00%	-2.23%
XLE	2.78%	0.00%	-2.78%
XLP	4.75%	0.00%	-4.75%

Fundamentals: S&P 500



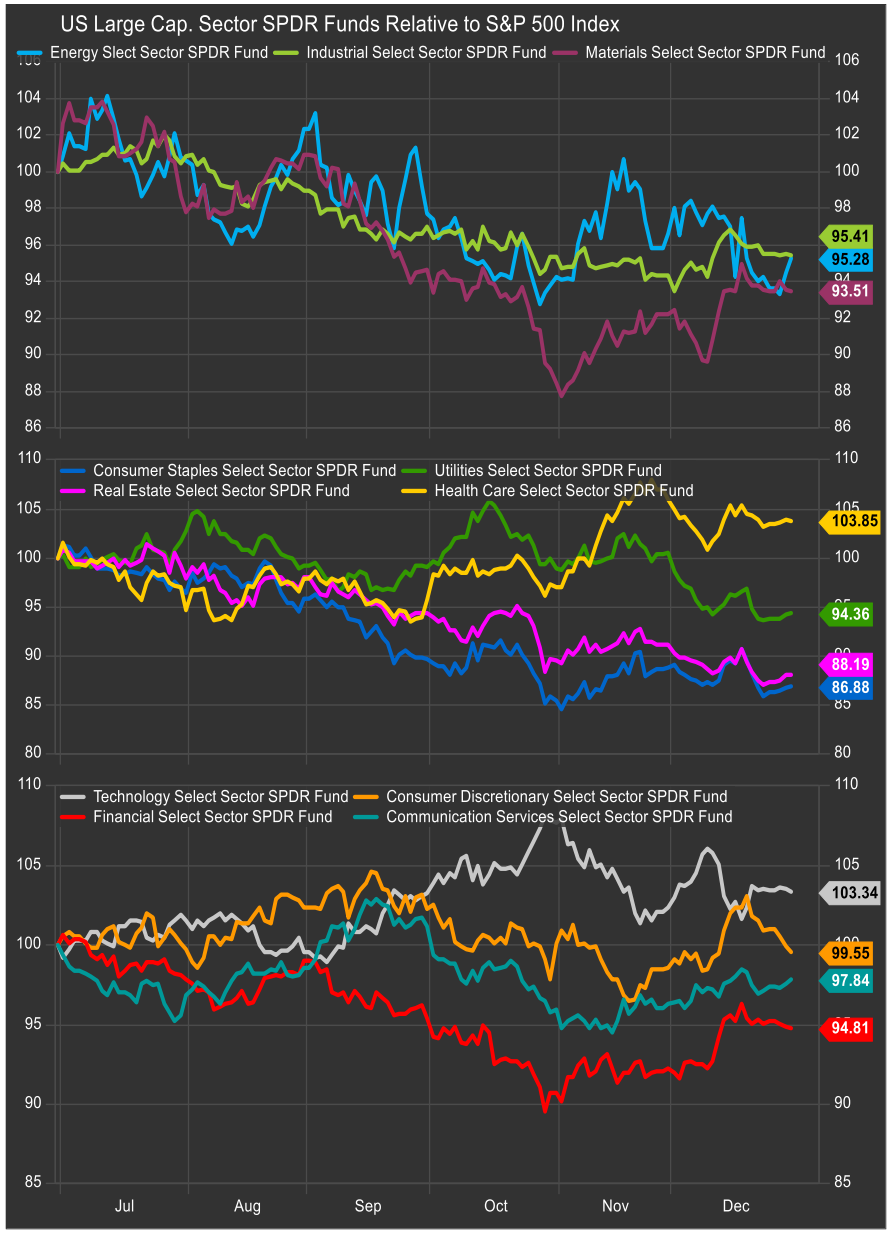
The chart (left) shows S&P 500 Margins, Debt/EBITDA, Valuation and Earnings

Net Margin for the S&P 500 ticked higher as earnings season has been better than feared. Valuations have also contracted on data points generated in November/December

While a trailing multiple of 28x is high by historical standards, we tend to be skeptical of longitudinal comparisons that measure the current environment to the past. We would be more concerned if there was a wide valuation spread between sectors, but we note that elevated valuations are fairly wide-spread

Financials and Energy sectors are the only sectors that screen as “cheap” in our work

Industry/Sub-Industry Performance and Breadth: S&P 500



S&P 500 Sectors (chart, left): Tech shares gained in December but continue to consolidate leaving the door open for a new sector leadership dynamic to emerge. Financials have held onto recent gains while Discretionary stocks have been volatile. Materials and Healthcare stocks are showing intermediate-term bullish reversal on performance

S&P 500 Internals (chart, right): As investors took profits from Tech sector outperformance the **% of stocks above their 50-day moving average** and **200-day moving average** are firming as AI trade correction has benefitted a far wider swath of Value/Cyclical exposures…the big surge came off the 11/20 breadth low as the Fed signaled an increased willingness to ease in December on that date

Top 10/Bottom 10 Stock Level Performers: S&P 500

Symbol	Name	GICS Sector Name	CHART_PATTERN	MktVal Co	Valuation Multiple Rel to Index	Momentum Score	Div Yld Multiple rel to Index	3y BETA Rel to Loc Idx	1-Month Excess Return vs. BMK
DG	Dollar General Corporation	Consumer Staples	Bullish Reversal	30,270.7	0.78	24.4	1.2	0.37	24.7
MU	Micron Technology, Inc.	Information Technology	Uptrend	331,316.2	0.35	69.8	0.1	2.03	23.6
NCLH	Norwegian Cruise Line Holdings Ltd.	Consumer Discretionary	Consolidation	10,202.3	0.34	-0.9	0.0	2.73	20.5
MCHP	Microchip Technology Incorporated	Information Technology	Consolidation	34,939.9	1.17	0.9	1.9	1.79	19.7
WBD	Warner Bros. Discovery, Inc. Series A	Communication Services	Bullish Reversal	71,353.1		58.5	0.0	2.45	19.0
MRNA	Moderna, Inc.	Health Care	Bullish Reversal	12,171.4		15.6	0.0	0.90	19.0
FCX	Freeport-McMoRan, Inc.	Materials	Bullish Reversal	73,921.7	0.93	24.4	0.8	1.26	18.8
TPR	Tapestry, Inc.	Consumer Discretionary	Uptrend	26,674.0	0.88	19.9	0.8	2.17	18.7
CCL.U	Carnival Corporation	Consumer Discretionary	Bullish Reversal	35,866.9	0.48	5.7	0.7	3.49	18.2
LUV	Southwest Airlines Co.	Industrials	Bullish Reversal	21,265.4	0.58	19.7	1.2	1.57	17.7

Symbol	Name	GICS Sector Name	CHART_PATTERN	MktVal Co	Valuation Multiple Rel to Index	Momentum Score	Div Yld Multiple rel to Index	3y BETA Rel to Loc Idx	1-Month Excess Return vs. BMK
LW	Lamb Weston Holdings, Inc.	Consumer Staples	Downtrend	5,810.7	0.59	-29.9	2.4	0.85	-30.1
LEN	Lennar Corporation Class A	Consumer Discretionary	Retracement	26,257.6	0.57	-21.1	1.3	1.55	-21.8
MPC	Marathon Petroleum Corporation	Energy	Consolidation	49,178.6	0.46	-17.8	1.5	0.98	-16.5
PSKY	Paramount Skydance Corporation Class B	Communication Services	Retracement	14,467.5	0.53	-23.0	1.0	1.66	-16.3
COIN	Coinbase Global, Inc. Class A	Financials	Retracement	53,340.8	1.37	-30.9	0.0	5.26	-15.2
DDOG	Datadog, Inc. Class A	Information Technology	Consolidation	44,891.7	2.39	-10.6	0.0	1.85	-14.7
AZO	AutoZone, Inc.	Consumer Discretionary	Retracement	56,592.5	0.86	-20.0	0.0	0.21	-14.6
BBY	Best Buy Co., Inc.	Consumer Discretionary	Retracement	14,214.9	0.41	-12.9	3.7	1.55	-14.2
AVGO	Broadcom Inc.	Information Technology	Uptrend	1,656,553.8	1.30	0.7	0.5	0.90	-14.1
NFLX	Netflix, Inc.	Communication Services	Retracement	430,218.0	1.17	-25.3	0.3	1.38	-13.4

Dovish Fed intervention was a dominant macro dynamic during December with central bank support lifting a broad mix of cyclical stocks from Miners to Airlines to out of the money consumer plays

Laggards were a mixed bag, but housing, speculative Growth plays and Mega Cap. Growth names were among the biggest decliners

Metrics:

(Formulas are in the appendix at the end of the report)

Valuation Multiple Relative to Index

Premium (or discount) to benchmark valueation

Momentum

Long higher scores, short lower scores

Dividend Yield Relative to Index

Higher scores preferred when rates and equities are moving lower

Near-term Overbought/Oversold

Price is >10% away from the 50-day moving average Above/Below

GREEN|RED

Company scores positively|negatively for Elev8 Sector Rotation Model

Economic & Policy Drivers: S&P 500

The Federal Reserve remained the dominant macro driver throughout 2025. After signaling a “hawkish cut” posture for much of the year, the final FOMC meeting delivered a 25 bp rate cut accompanied by cautious forward guidance and visible internal disagreement. While the Fed emphasized data dependence and a higher bar for further easing, the absence of a more aggressive tightening stance was interpreted as removing a key macro overhang.

Treasury bill purchases to maintain ample reserves, combined with expectations for modest additional easing, helped support risk assets despite persistent uncertainty around the longer-term neutral rate.

Inflation and Growth

Disinflation made tangible progress, with core inflation trending lower and reaching its slowest pace in several years by late 2025. However, inflation data were complicated by reporting distortions and timing issues, limiting policymakers’ confidence.

At the same time, real economic activity surprised to the upside. Strong GDP growth and resilient consumption late in the year raised questions about how much additional policy easing would ultimately be justified. This tension—cooling inflation alongside firm growth—created alternating periods of risk-on and rate-sensitive pullbacks.

Labor Market Dynamics

Labor market data showed gradual softening rather than abrupt deterioration. Hiring slowed, unemployment drifted higher, and revisions weighed on headline job growth, but broader conditions remained consistent with a “late-cycle cooling” rather than recession. This backdrop reinforced expectations that policy easing would be cautious and incremental.

Global Policy and Rates

A hawkish tilt among global central banks—most notably the Bank of Japan—contributed to upward pressure on global bond yields at times. Spillovers into U.S. rates periodically challenged equity valuations, particularly in long-duration growth segments, and reinforced rotation within the equity market.

Fiscal, Trade, and Political Factors

Fiscal policy expectations shifted toward 2026, with investors increasingly focused on prospective tax changes, spending initiatives, and potential stimulus. Trade and tariff uncertainty resurfaced intermittently, adding to inflation and margin risk considerations. Political developments, including uncertainty around future Fed leadership, contributed to episodic volatility in rates and policy-sensitive sectors.

AI and Earnings Leadership

AI investment remained the defining structural theme of 2025. Strong results from select semiconductor and software companies reinforced the earnings upside from AI demand, but scrutiny intensified around infrastructure-heavy models, funding needs, and return on invested capital. This led to growing dispersion: index-level strength often masked divergence between AI “enablers,” infrastructure providers, and non-AI cyclicals.

Flows, Liquidity, and Seasonality

Supportive technicals played an important role late in the year. Improved positioning after midyear volatility, elevated buyback activity, compressed volatility, and strong seasonal patterns helped keep drawdowns shallow and supported the S&P 500 near all-time highs despite mixed fundamentals.

2. Macro and Policy Outlook for 2026

Base Case

The most likely 2026 scenario is **moderating but positive growth**, continued **gradual disinflation**, and **measured Fed easing**. In this environment, earnings growth—rather than valuation expansion—is expected to be the primary driver of equity returns. AI-related productivity gains remain a key upside lever if monetization continues to improve.

Key Risks

Higher-for-longer rates: Strong growth or sticky inflation could limit Fed easing, pressuring long-duration assets.

Labor-market deterioration: A sharper rise in unemployment could accelerate rate cuts but raise earnings risk.

AI investment payback: Failure of AI capex to translate into sustainable margins and cash flow could drive leadership reversals.

Policy shocks: Tariffs, fiscal uncertainty, or geopolitical escalation could reprice inflation risk and the term premium.

3. Investment Implications

Equity leadership is likely to remain selective, favoring companies with visible earnings growth, strong balance sheets, and demonstrated AI monetization.

Cyclical exposure may benefit if easing proceeds alongside fiscal support, but sensitivity to rates remains high.

AI infrastructure and leveraged growth models warrant caution given funding and ROI scrutiny.

Volatility is likely to remain episodic, tied to inflation data, labor-market signals, and global rate developments.

Appendix: Metric Interpretation/Descriptions

Valuation Multiple Relative to Index

Higher scores correspond to more expensive earnings than the index, lower scores are cheaper

Valuation Multiple Relative to Index

(Company Price/NTM EPS) / (Index Price/NTM EPS)

Dividend Yield Relative to Index

Higher scores correspond to higher company dividend yield relative to the S&P 500 Index dividend Yield

Dividend Yield Relative to Index

Company FY1 Rolling Dividend Yield / Index FY1 Rolling Dividend Yield

Momentum

Long higher scores, short lower scores

Momentum (simple mean)

1-Month Excess Total Return (vs. S&P 500) * 0.2

Plus

3-Month Excess Total Return (vs. S&P 500) * 0.5

Plus

6-Month Excess Total Return (vs. S&P 500) * 0.3

Metric Interpretation/Descriptions

Price Structure

We categorize stock chart patterns into 7 categories
Uptrend—Stock exhibits sustained outperformance
Bullish Reversal—Stock has outperformed over the past 3-6 months by > 10% vs. benchmark
Consolidation—Sideways price action, generally a bearish pattern in a bull market
Retracement—A sharp move lower in a previously strong chart
Distributional—A topping pattern
Downtrend—Sustained underperformance, lagging the benchmark by >15% per year
Support—Price has reached a level where major bottom formations or basing has occurred in the past
Basing—A protracted consolidation at long-term support

Deviation from Trend

Intermediate-term: Price % Above/Below 200-day moving average
Near-term: Price % Above/Below 50-day moving average

Overbought/Oversold (We want to sell overbought charts with declining momentum)

Overbought = Stock price > 25% above 200-day m.a.
Oversold = Stock price > 20% below 200-day m.a.

Near-term Overbought/Oversold (Signals depend on trend context)

Overbought = Stock price > 15% above 50-day m.a.
Oversold = Stock price > 15% below 50-day m.a.