Q1 Earnings Season: AI Capex, Productivity and the Broadening of Growth

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Vittorio Treichler
Partner & Strategist

YTD performance

World Equity Indices

	YTD % TR USD	YTD % TR Local
MSCI World	8.7%	8.7%
S&P 500	9.3%	9.3%
S&P 500 Equal Weighted	7.4%	7.4%
Mag 7 Index	6.0%	6.0%
Russell 2000	15.2%	15.2%
Euro Stoxx 50	4.9%	6.1%
CSI 300 Index	8.1%	5.1%
Hang Seng Index	0.0%	0.7%
Nikkei 225	24.6%	26.8%
MSCI EM	20.2%	20.2%

S&P 500 Sectors

	YTD% TR USD
S&P 500 Info Tech	17.8%
S&P 500 Comm. Serv	10.1%
S&P 500 Health Care	-3.9%
S&P 500 Financials	-5.1%
S&P 500 Cons Discr.	2.4%
S&P 500 Energy	32.7%
S&P 500 Real Estate	12.0%
S&P 500 Materials	10.1%
S&P 500 Industrials	10.3%
S&P 500 Cons Staples	11.2%
S&P 500 Utilities	6.2%

Key Thematic Indices

	YTD % TR USD	YTD % TR Local
ARK Innovation ETF	-0.4%	-0.4%
Software ETF	-12.5%	-12.5%
GS Uranium	7.8%	7.8%
GS Cyclicals	6.1%	6.1%
BBG Defensive Sectors	9.07%	9.07%

Fixed Income

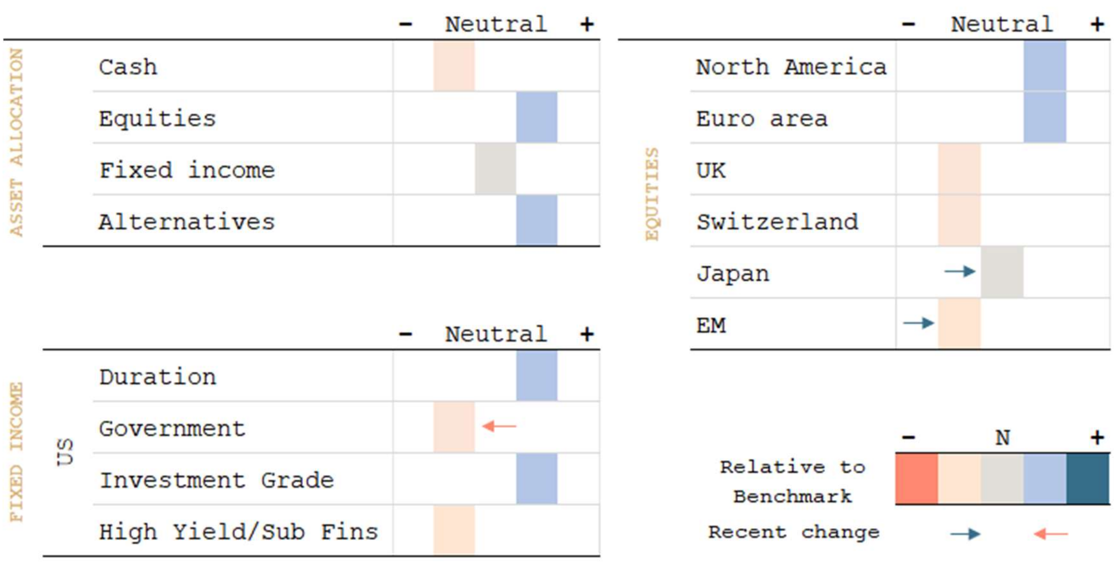
	YTD% TR USD
LQD (High Grade)	-0.3%
HYG (High Yield)	1.1%
US Treasuries Index	-0.7%
TSY 2 year (bps)	60
TSY 10 year (bps)	38
Bund 10 year (bps)	18
SOFR March 27 rate (bps)	87

FX & Commodities

	YTD % TR USD
US Dollar Index	1.0%
Bitcoin	-11.7%
BBG Precious Metals	4.9%
BBG Energy	91.1%

Data as of 22 May

Novum's "Investment Mosaic"



Novum Partners SA
Rue des Alpes 7 ▪ 1201 Geneva - Switzerland
T + 41 (0) 22 715 18 00 ▪ www.novumpartners.com

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Executive Summary

- Q1 2026 earnings have come in dramatically above an already elevated bar, with S&P 500 EPS growth on track to accelerate from 14.4% in Q4 to roughly 25.5% YoY, the strongest pace in four years and, stripping out base effects and tax cuts, arguably the strongest in two decades.
- Earnings strength is genuinely broadening: all 11 S&P 500 sectors are tracking positive YoY growth for the first time in four years, median company EPS growth has spiked to 12.2% (from 8.7% in Q4), and the size of the average beat (8.6%) is well above the 4.9% historical norm.
- Margins have made a new record high (15.7%), with the structural uptrend in Mag 7 now joined by a sharp break from the three-year downtrend in the rest of the index. Sales growth (10.1%) has reached a pace previously seen only in post-recession recoveries.
- A supportive domestic macro backdrop is allowing the earnings recovery to broaden beyond technology: while tech continues to lead profit growth, the broader market - as reflected by the S&P 500 Equal Weight Index - is also improving, with earnings growth expected to accelerate from 6.2% in 2025 to 10.2% in 2026.
- Unlike Q4, the market is rewarding the results: the S&P 500 is up roughly 5% since the start of reporting, ahead of the historical median (+2%).
- The caveats are macro, not micro. The Iran-related oil shock, a renewed bond sell-off and the highest G7 sovereign yields since 2001 raise the bar for valuations even as fundamentals improve. Corporate guidance is constructive but visibly more cautious in tone, and the dispersion between the largest contributors and the median stock is wide - a backdrop where stock-picking and risk discipline matter more.

The quarter in the data: a sharp acceleration

Heading into Q1 reporting season, the bottom-up analyst consensus was already exceptionally strong, and we wrote at the time of the Q4 review that earnings momentum was likely to broaden rather than fade. The data have delivered more than that. With about 90% of S&P 500 market cap reported, S&P 500 earnings are on track to grow roughly 25.5% YoY in Q1, up from 14.4% in Q4 and the highest reading in four years. Excluding 2021 (pandemic base effects), 2018 (corporate tax cuts) and 2010 (post-GFC rebound), the last time underlying earnings growth was this strong was 2004.

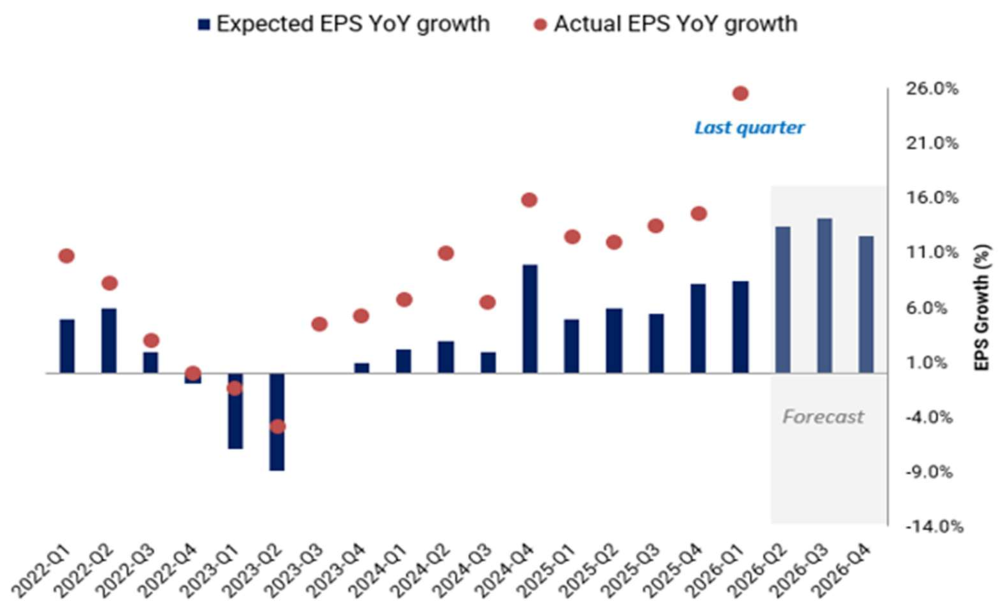


Chart 1 – S&P 500 EPS growth and surprises

Aggregate S&P 500 margins printed 15.7% in Q1, a new record high, up from 14.9% in Q4. The familiar story of Mag 7 marching their margins higher continues, but Q1 marked the first material break from the three-year downtrend in margins for the rest of the index. Sales growth of 10.1% YoY is, outside post-recession rebounds, without precedent in the past 15 years.

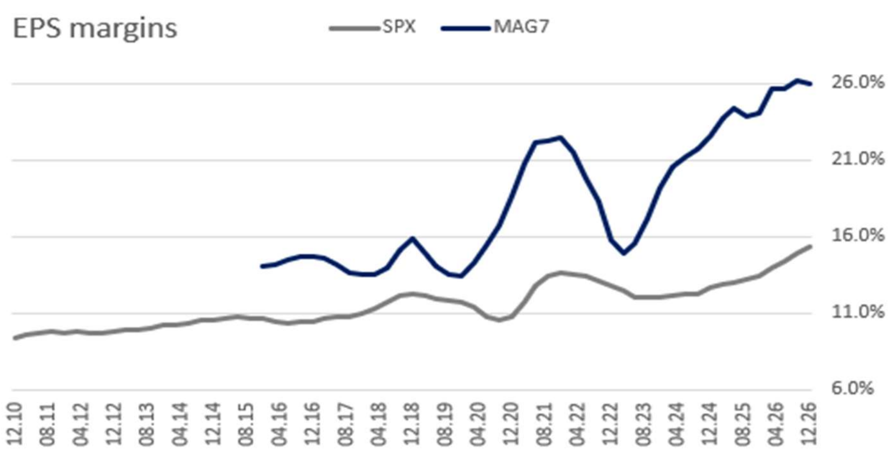
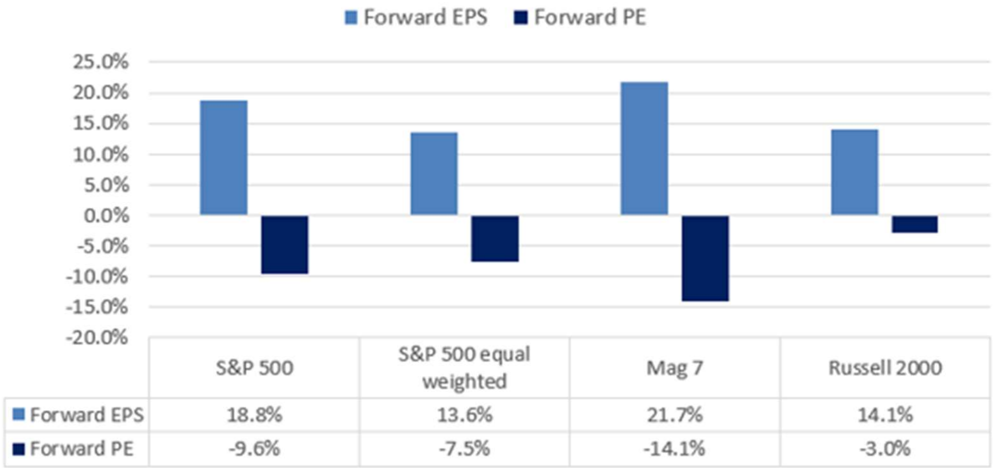


Chart 2 – S&P 500 and Mag 7 EPS margins

A genuine broadening across sectors and the paradox of cheaper stocks

Our Q4 review flagged a meaningful but incomplete broadening. Q1 closes the gap. All 11 S&P 500 sectors are tracking positive YoY earnings growth - the first time that has happened in four years.

The defining paradox of the Q1 2026 earnings season is that even as every sector begins to show solid price performance, equities are simultaneously becoming cheaper. The next two charts capture this dynamic with unusual clarity, revealing a deep and consistent divergence between earnings expectations and valuation multiples.

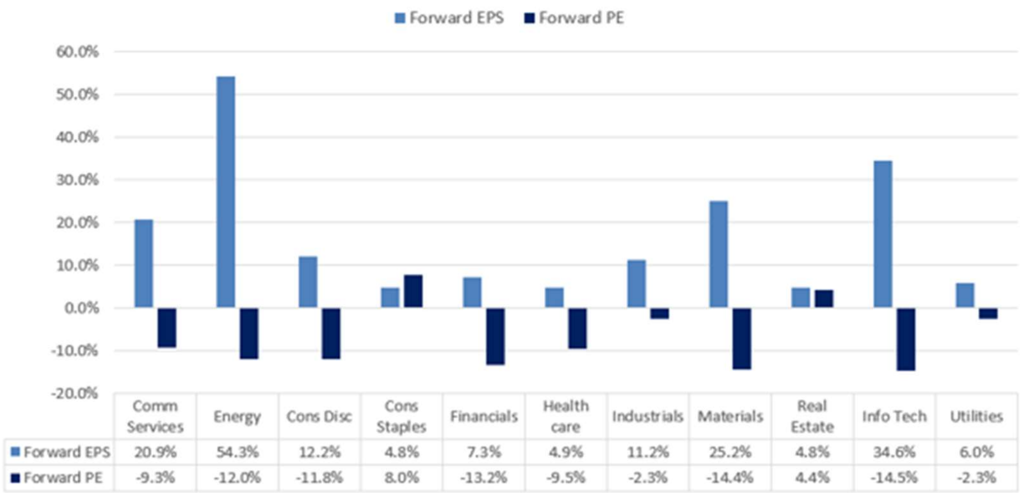


PE levels

	S&P 500	S&P 500 ew	Mag 7	Russell 2000
End 2025	22.8	17.4	32.1	24.8
Today	20.7	16.1	27.5	24.1

Chart 3: % change since the beginning of the year in Forward EPS and PE – major US indices. Below, table of forward PE levels.

Since the start of the year, the next-twelve-month earnings outlook has been revised materially higher - and crucially, not just for Technology. The improvement is genuinely broad-based across the sector spectrum. Energy leads with a striking +54.3% upward revision to forward EPS, followed by Information Technology at +34.6% and Materials at +25.2%. But the upgrade reaches well beyond the obvious AI and commodity-supply winners: Communication Services has seen forward EPS revised up +20.9%, Consumer Discretionary +12.2%, Industrials +11.2%, Health Care +4.9%, Financials +7.3%, Consumer Staples +4.8%, Real Estate +4.8% and Utilities +6.0%. There is not a single sector in negative territory.



	Comm Services	Energy	Cons Disc	Cons Staples	Financials	Health care	Industrials	Materials	Real Estate	Info Tech	Utilities
Forward EPS	20.9%	54.3%	12.2%	4.8%	7.3%	4.9%	11.2%	25.2%	4.8%	34.6%	6.0%
Forward PE	-9.3%	-12.0%	-11.8%	8.0%	-13.2%	-9.5%	-2.3%	-14.4%	4.4%	-14.5%	-2.3%

Chart 4: % change since the beginning of the year in Forward EPS and PE – major US sectors

The second leg of the divergence is the forward P/E ratio, which has moved in precisely the opposite direction. Every sector save one has seen its forward multiple contract since the start of the year. The de-rating has been most pronounced in Information Technology (-14.5%), Materials (-14.4%), Financials (-13.2%), Energy (-12.0%) and Consumer Discretionary (-11.8%), with Communication Services (-9.3%), Health Care (-9.5%), Industrials (-2.3%) and Utilities (-2.3%) also lower. The lone exception is Consumer Staples, whose forward P/E has actually expanded (+8.0%), consistent with the defensive re-rating we have flagged elsewhere in this publication. At the index level, the S&P 500 forward multiple has compressed -9.6%, the equal-weighted index -7.5%, the Mag 7 -14.1% and the Russell 2000 -3.0%. In absolute terms, the S&P 500 forward P/E has moved from 22.8x at end-2025 to 20.7x today; the equal-weighted index from 17.4x to 16.1x; the Mag 7 from 32.1x to 27.5x; and the Russell 2000 from 24.8x to 24.1x.

A rational market, not a complacent one

Read together, these two charts suggest the market is behaving rationally rather than complacently. On one side, price performance has been positive, justified by the genuine and sizable earnings surprises documented throughout this season. On the other side, investors are clearly applying more caution than they were at the start of the year, and they are doing so by paying a lower multiple for each dollar of (rising) earnings. That caution is well founded: geopolitical risk has escalated, and interest rates have moved higher across the entire yield curve. It is worth recalling that the market has priced out nearly 100bp of Fed cuts over the next twelve months, and no longer rules out the possibility of an outright hike before year-end.

In our view, this de-rating represents a reasonable and proportionate adjustment rather than a warning sign. The discount being applied looks broadly adequate and in line with comparable past episodes: the market is funding higher earnings power at a lower multiple, which is the textbook response to a higher discount rate and elevated macro uncertainty. The earnings upgrade and the multiple compression are, in effect, partially offsetting - leaving price action positive but valuations healthier than they were six months ago.

We would, however, flag one risk for prudence. The de-rating to date reflects a market that has priced out cuts; it has not priced in a genuine tightening cycle. Were the Fed forced into actual rate hikes, the impact could be negative on two fronts simultaneously - compressing multiples further and eroding earnings, the latter through weaker demand and a heightened probability of recession. We regard such a scenario as difficult to forecast at this stage: it would require a further deterioration on the geopolitical and military front and, critically, the energy shock turning from a transitory disruption into a permanent feature of the cost base. That is not our base case. But it is the tail outcome against which the current, otherwise reassuring, valuation adjustment offers the least protection.

Market reaction and rotation

In contrast to Q4, when strong fundamentals were met with a flattish index and a sharp internal rotation toward HALO ("Heavy Assets, Low Obsolescence"), Q1 results have been rewarded. The S&P 500 is up roughly 5% since the start of the earnings season, well above the historical median of +2%, and median stock performance on beats has been broadly in line with history.

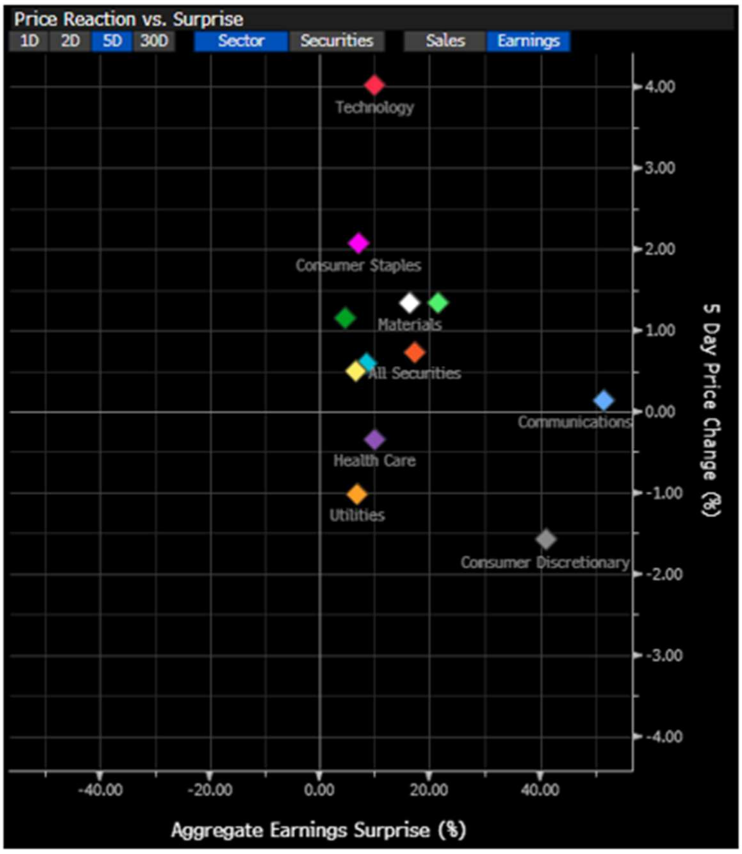


Chart 5: price reaction to earnings publication across major sectors

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Hyperscaler capex: bigger again, but better digested

In our Q4 review the dominant near-term concern was "sticker shock" from the upward revision in hyperscaler capex plans (the five largest spenders moving toward roughly $660bn in 2026 after a $120bn upgrade since the start of the Q4 season). Q1 has, if anything, extended that trajectory: the AI infrastructure buildout is widening, with semis revenue, electrical equipment, data-center construction and power providers all confirming demand running ahead of supply.

What has changed is the market's framing. With AI beneficiaries delivering ~50% earnings growth, and management teams now articulating concrete monetization paths in cloud, advertising and adjacent productivity tools, the absolute capex number is being judged against a tangible revenue and margin response.

The right question is no longer whether capex is too high, but where in the value chain the marginal dollar is best paid: it is increasingly being captured by infrastructure providers - semis, electrical equipment, construction & engineering, data-center REITs and select utilities - while the hyperscalers themselves digest the cash-flow impact.

AI capex and the limits of the GDP tailwind

The broader conclusion to draw from this quarter is that the AI investment theme has become powerful enough to register at the macroeconomic level: it is now actively supporting the growth of US GDP. The economy expanded at a real rate of around 2% in the first quarter, and the contribution from investment was a meaningful part of that figure. Technology equipment investment grew roughly 19% year-on-year, adding close to a full percentage point to GDP - on the order of $250bn. An earnings theme has, in effect, become a national-accounts theme.

The two charts below, however, add an important nuance to that story. Chart number 6 plots technology investment both as a share of GDP (right axis) and as a share of total investment (left axis). On both measures the line is rising steeply, and the move is not subtle: tech investment as a percentage of GDP has climbed toward 5%, while its share of total investment has pushed up toward 28%. Crucially, both series have now exceeded their previous peaks: the dot-com high of 2001 and the 2008 peak.

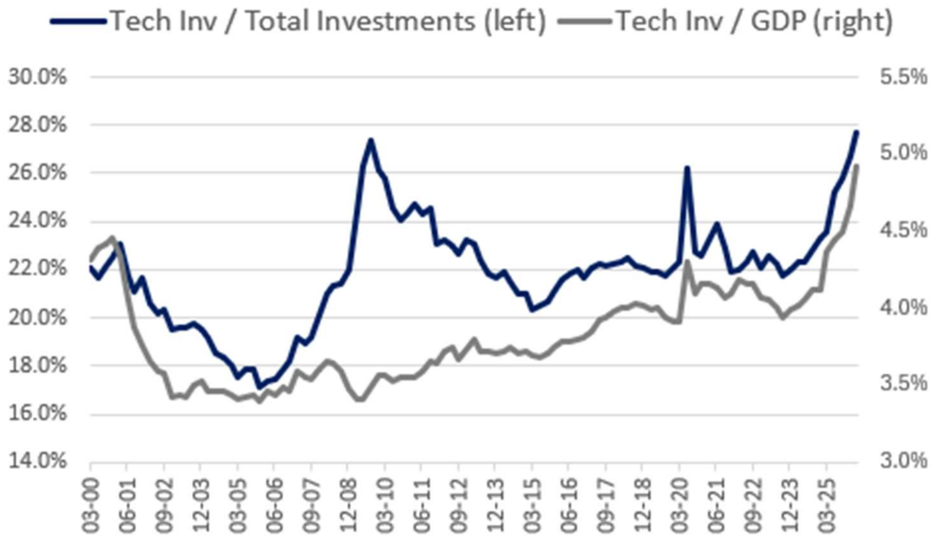

Chart 6: Investments in Tech Equipments as a share of total investments and US GDP

Chart 7 supplies the counterpoint: total investment as a share of GDP is not rising at all. It has been broadly stable at around 18%, well within its long-run historical range.

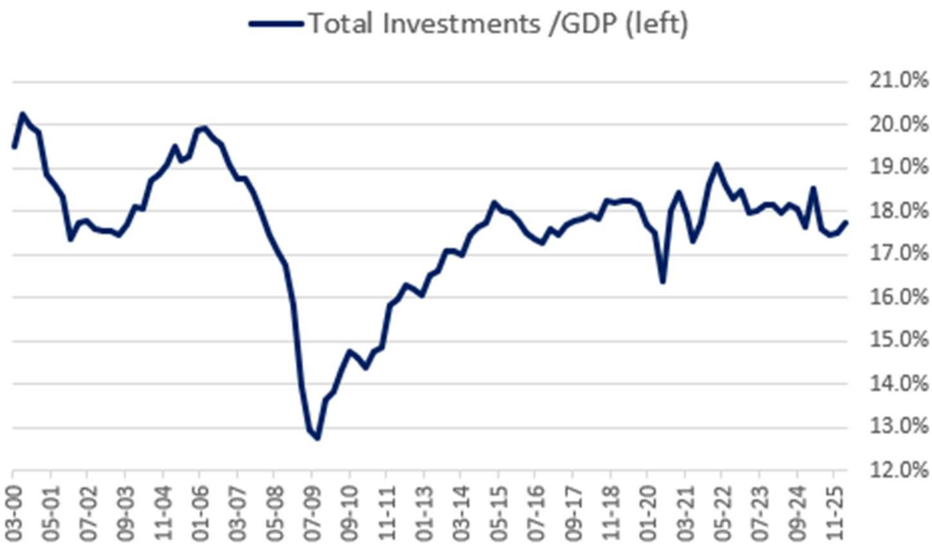

Chart 7: Total Nonresidential Investments as a share of GDP

Read together, the two charts deliver a clear and slightly sobering message. For the moment, technology investment is not expanding the overall investment pie - it is taking a larger slice of a pie that is roughly fixed in size. AI capex is, in other words, partly crowding out other forms of investment rather than being purely additive to them. That distinction matters for the durability of the growth contribution.

Because the top chart shows tech investment has already surpassed both the 2001 and 2008 cyclical peaks, it is difficult to argue that this ratio can keep climbing at the same pace in the coming quarters. There is a natural ceiling to how large a share of GDP, and of total investment, a single category can credibly occupy. The implication is that the direct, capex-driven contribution to GDP growth is likely closer to its high-water mark than to its starting point.

That does not mean the macro tailwind from AI is exhausted; rather, it means the source of the tailwind has to rotate. If the spending itself can no longer accelerate as a share of the economy, then economic growth will need to find other points of support, and the most plausible candidate is the productivity that this investment is designed to generate. Encouragingly, that hand-off is already visible: the AI-related investment cycle began roughly two years ago, and the productivity dividend from that earlier spending is starting to come through now. The market's task over the coming quarters will be to watch the baton pass from capex as a growth input to productivity as a growth output - the second being far more valuable, and far more durable, than the first.

Novum's Trade History

From 31.12.2023 to 22.05.2026