THE SHORT AND LONG

Weekly Bulletin

The De-rating Investors Should Welcome

JULY 28, 2026

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TAKEAWAYS

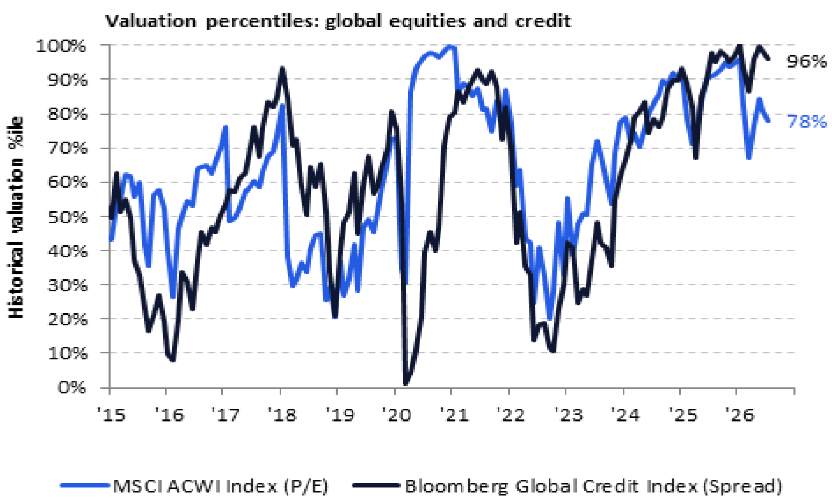
Global equity markets have priced in more uncertainty than the macro backdrop currently warrants. The macro data tells a more constructive story than investor sentiment does, and when fundamentals improve faster than sentiment, long-term investors can seek a more attractive opportunity set.

U.S. Q2 earnings growth continues to impress, with reported companies surprising by 17%[1] in aggregate. Under the hood, markets are rewarding companies based on capital intensity and macro sensitivity. We prefer companies with strong fundamentals and earnings drivers.

AI is expanding data vulnerabilities and security requirements, potentially making cybersecurity one of the most durable areas of enterprise spending. With 88% of companies increasing cybersecurity budgets, cybersecurity may offer exposure to a reliable source of earnings growth[2].

This week in charts

FIGURE 1: Equities are repricing from peak valuation levels



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Looking closer

Macroeconomic data continues to surpass expectations while risk asset valuations have moderated in recent months. This is a result of stronger earnings growth but also flatlining investor sentiment. We believe markets have priced in more uncertainty than the macro backdrop currently warrants.

[1] EPS surprise is using non-GAAP adjusted EPS for the S&P 500 firms that have reported earnings through July 27, 2026.
[2] Bloomberg as of July 23, 2026.

Growth holds up while equity valuations come in

Markets have cycled through the same concerns all year: valuation fears, AI skepticism, geopolitical shocks, and questions about inflation and central bank policy. Few of these worries have left a lasting mark on markets, yet the debate resets every few weeks. Equity markets have traded in a range since mid-May, leaving us focused on two questions for the rest of the year: what creates the next leg higher, and where can investors find themes that transcend the worry cycle?

The data keeps answering the first question. The Citigroup Global Economic Surprise Index (CESI) measures whether macro data beats or misses consensus forecasts, remains firmly positive at 21.9, indicating economic data improvement. That momentum has held through periods of elevated geopolitical tension, including the ongoing Middle East conflict. The economic story remains strong in the U.S. and solid across other regions.

Historically, positive economic surprise momentum supports cyclical assets, corporate earnings expectations, and broader risk sentiment. That has not fully played out recently. Investor attention remains fixed on a familiar set of risks, creating a disconnect between improving fundamentals and cautious positioning.

Equity valuations tell the same story. Credit still sits near the top of its 15-year historical range at the 96th percentile, but global equity multiples have contracted to roughly the 78th percentile (Figure 1). That happened in part because company earnings grew faster than their stock prices. We view this as a healthy development. After years of multiple expansion driving parts of the global equity market higher, earnings now lead. The market has addressed valuation concerns not through falling prices, but through stronger earnings momentum.

Bottom line: Equity markets have priced in more uncertainty than the macro backdrop currently warrants. When fundamentals improve faster than sentiment, long-term investors may find attractive entry points into solid fundamental stories.

Earnings beat expectations, but investors reward companies selectively

This is the biggest week of the second quarter U.S. equities reporting season, with about a third of S&P 500 market cap reporting. Combined with 31% already in the books, roughly two-thirds of U.S. large cap market value will have reported by Friday. Expectations were high entering the quarter, and results have thus far exceeded them, with earnings surprising by +17% in aggregate.

Q2 S&P 500 EPS growth has jumped to 36% year over year, driven primarily by one-time investment market-ups at a single mega-cap Tech company. Excluding that one-time gain, growth is tracking 24% year over year, up 2% since the start of the month. Earnings surprises remain strong, with companies beating by 17% in aggregate[3].

Investors continue to question whether AI spending is sustainable and whether it converts into revenue growth. The companies writing the checks offer some reassurance. One of the largest hyperscalers raised its 2026 capital expenditure (capex) forecast last week, indicating spending could rise significantly again in 2027, and tied the increase to accelerating demand. Our read is that the AI build-out is broadening rather than slowing.

Focus now shifts to the remaining hyperscalers reporting this week. Following that capex guidance increase, hyperscaler stocks have underperformed, implying lowered expectations for this round of reports. The bar may now sit lower than it did a few weeks ago, and that raises the importance of guidance and management commentary echoing the same confidence in persistent demand.

Price reactions to earnings have been uneven so far this season. Healthcare stands out, with higher prices on weaker EPS. Meanwhile, pockets of the market with strong EPS trends, including IT and communications services, have seen lower prices.

Beyond earnings, central bank policy takes center stage this week. The Federal Open Market Committee (FOMC) rate decision comes on Wednesday, with the Bank of England (BoE) and Bank of Japan (BoJ) also meeting. In U.S. economic data, we will get June Personal Consumption Expenditure (PCE), second quarter GDP, and the University of Michigan consumer sentiment survey. We do not expect the Fed to raise rates despite somewhat elevated inflation, and we expect policymakers to keep watching the data. We also want to hear more from consumer-facing companies reporting later, which matters for re-underwriting the positive macro view.

[3] Bloomberg as of July 23, 2026.

Bottom line: Investors continue to worry about AI spending, while companies continue to report AI-fueled earnings growth. So far, fundamentals are winning the debate by surprising positively. We continue to prefer companies with strong fundamentals and clear earnings drivers.

Cybersecurity emerges as one of the clearest AI investment beneficiaries

Against a backdrop of cautious sentiment, we look for themes less correlated to the market's worry cycle. Cybersecurity and data security stand out. Companies cannot afford to cut security spending when operational resilience is at stake, when reputation depends on how well they protect data, and when the right protection is critical to continued growth.

The budget data supports this view. 88% of companies plan to increase cybersecurity budgets over the next 12 months, and nearly half are growing budgets by double digits, with 37% increasing spend by 10% to 25% and another 8% by more than 25%. Only 2% of companies expect to cut security spending at all[4].

This quarter's earnings calls reinforce the theme. A major hyperscaler reported strong interest in its AI-powered security platform, with a more than 45% quarter-over-quarter increase in AI workloads scanned and protected. A large enterprise technology firm noted that increasingly capable AI models are accelerating the discovery of security vulnerabilities for clients, creating a multi-billion-dollar total addressable market. A financial infrastructure provider said anti-financial crime clients want to adopt agentic security workers as fast as possible.

That is the core of the investment case. AI expands the vulnerability and the security requirement at the same time, which makes cybersecurity spending unusually durable across market cycles.

Bottom line: AI is expanding both vulnerabilities and security requirements, making cybersecurity one of the most durable areas of enterprise spending. With 88% of companies increasing security budgets, we think cybersecurity spending will be resilient to the market's recurring cycle of worries.

[4] Bloomberg as of July 23, 2026.

	What happened	What's ahead
ECONOMIC DATA	**U.S.** Composite PMI of 53.6 up from 51.9 highest since November, with manufacturing PMI at 53.8 and service PMI at 53.6. June Leading Economic Index declined 0.2% to 99.1 with H1 2026 down 0.3%, with yield spread as the top positive contributor, but couldn't offset weak consumer expectations.	**U.S.** PCE for June Q2 GDP University of Michigan consumer sentiment survey
	Global Taiwan's exports rose 40.3% year-over-year, to $74.8B, third highest monthly total, driven by AI-related demand. UK CPI +2.6%; Eurozone composite PMI of 51.9, best est. 50.3.	**Global** China's NBS PMIs for July Eurozone CPI for July Taiwan and Eurozone Q2 GDP
POLICY	**U.S.** Iran rejected cease-fire proposal, Trump is increasingly frustrated with Tehran and has shifted into a hardline stance. Trump administration announced new import duties ranging from 10-12.5% on 60 economies, citing prevention of forced labor in supply chains to the detriment of American workers.	**U.S.** FOMC decision Silicon Valley firms urge Trump not to restrict Chinese open-source AI models, arguing it would ban innovation, as Washington investigates Moonshot AI.
	Global PBOC left loan prime rate to be unchanged for 14th straight month, with one-year at 3% and five-year at 3.5%. ECB kept interest rate steady, closely watching energy shock.	**Global** Fed, BoJ, and BoE meetings ECB said to be considering options to mitigate financial losses, with debate expected to peak in fall.
MARKETS	**U.S.** Alphabet revenue $119.8B (+24% y/y), boosted by 82% cloud growth; shares fell on first-ever negative FCF and raised FY26 capex guidance to $200B. IBM missed estimates with revenue of $17.2B, lowered guidance. Intel posts fastest revenue growth in 15 years (+25% y/y) and raises AI-chip-driven capex by $2B.	**U.S.** 33% of S&P 500 market cap reporting this week
	Global Mag 7 lost $797B in market value as AI spending doubts and macro uncertainty hit Tech.	**Global** Notable Tech earnings set to report

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RELATED READING

July 21, 2026 | Broad Growth, Cooler Sentiment, and Long-Term Themes

In last week's Bulletin, we looked at how economic expansion continues to broaden, while U.S. inflation breadth eased. We see a high-growth, high but moderating inflation backdrop that remains fundamentally supportive.

July 20, 2026 | The Short and Long Podcast

In the third episode, "AI, Quantum, and Cybersecurity; From Breach to Resilience," host and Chief Investment Officer of Citi Wealth Kate Moore speaks with Fatima Boolani, Co-Head of U.S. Software Equity Research, Citi Research, and Anneka Gupta, Chief Product Officer at Rubrik, on how today's cybersecurity threats require continuous adaptation in prevention and resilience and covers questions every investors should be asking right now around cybersecurity in the age of AI. Watch on **YouTube, Apple**, or **Spotify** and subscribe for future episodes.

July 14, 2026 | The Short and Long: Q3 Macro Investment View

Citi Wealth's quarterly report is designed to offer global, data-driven guidance to help investors navigate increasingly complex markets with confidence and clarity. The latest report delivers a breakdown of forces shaping global markets, how they impact potential investment opportunities, and provide guidance across asset classes.

April 2, 2026 | Global Investment Council

The Citi Wealth Global Investment Council met April 2, 2026, and reallocated equity exposure from Europe to the U.S. The move maintains equity allocation while shifting risk toward more resilient markets. European fundamentals were already weakening prior to the Middle East conflict, and the U.S. offers more durable earnings with less geopolitical vulnerability.

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Upper medium grade (Strong)	A	A	A
Medium grade	Baa	BBB	BBB
Not Investment Grade			
Lower medium grade (somewhat speculative)	Ba	BB	BB
Low grade (speculative)	B	B	B
Poor quality (may default)	Caa	CCC	CCC
Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	C	D	C
In default	C	D	D

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- potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized;
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