

THE SHORT AND LONG

Weekly Bulletin

Following the earnings: where we are adding equity risk

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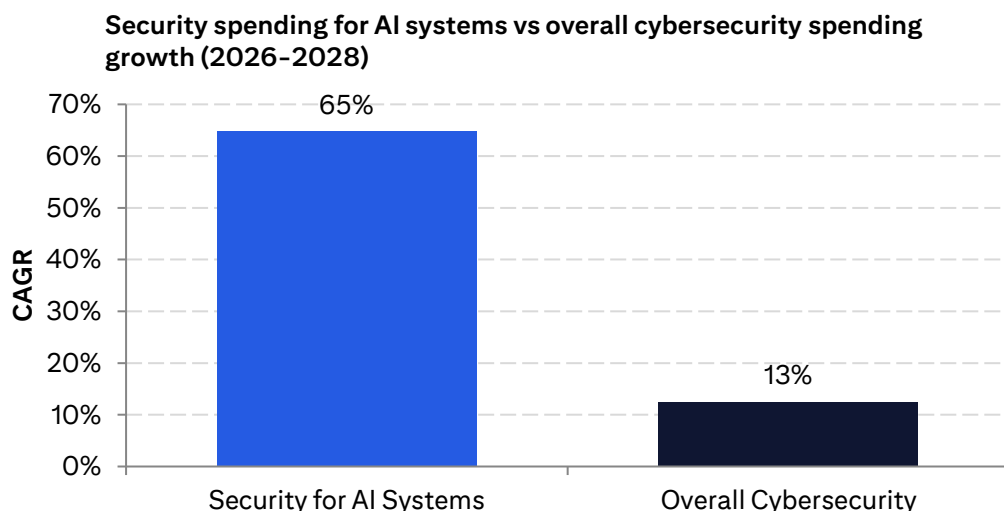
Cybersecurity seeks exposure to AI adoption without picking the ultimate model or platform winner. As AI agents multiply across enterprises, we believe security spending could become an unavoidable cost of doing business.

Japan combines firm growth, accelerating earnings revisions, and record corporate profitability, while investor positioning remains far from euphoric. We moved Japanese equities to a modest overweight to help capture this setup.

U.S. large caps remain our quality anchor, and valuation compression has created a better entry point. We fund these additions from securitized fixed income, where tight spreads offer limited compensation amidst rate volatility.

THIS WEEK IN CHARTS

FIGURE 1: Security spending for AI systems is expected to grow 5x faster



Source: Gartner as of September 25, 2026.

LOOKING CLOSER

We believe cybersecurity spending is poised to become one of AI's largest second-order beneficiaries. As AI adoption expands enterprise data access, identities, endpoints, and application connections, security risks are rising rapidly. AI security spending is expected to grow roughly five times faster than overall cybersecurity, creating a durable investment opportunity without betting on a single AI model or platform.

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CYBERSECURITY: AI'S
INSURANCE POLICY
AS THE ATTACK
SURFACE EXPANDS

JAPAN: FIRM
GROWTH,
ACCELERATING
EARNINGS, AND
RECORD
PROFITABILITY

Last week, our [Global Investment Council](#) selectively increased equity exposure where earnings and secular demand look strongest. We added to cybersecurity, Japan, and U.S. large caps, and we used securitized fixed income as the funding source in our multi-asset class portfolios.

We start with cybersecurity because AI adoption expands the enterprise security perimeter. Every new AI agent brings more users, identities, data access points, and connections across enterprise systems. Each connection creates another endpoint that companies must authenticate, monitor, and protect, and the data flowing into AI workflows often ranks among a firm's most sensitive.

Industry data shows how quickly this surface is growing. 40% of enterprise users have installed AI-powered browser extensions, and 64% of those extensions can access sensitive internal data. AI bot traffic grew 300% year over year in 2025, while daily API attacks rose 113%.

Spending could follow. Projections show security spending for AI systems growing at a roughly 65% compound annual rate from 2026 through 2028, about five times the 13% pace expected for overall cybersecurity spending (Figure 1). In our view, markets still underappreciate this spending wave.

For portfolios, cybersecurity offers exposure to AI adoption without requiring a view on which model or platform ultimately wins. We see it as AI's insurance policy, since few executives will leave their systems unprotected as adoption broadens.

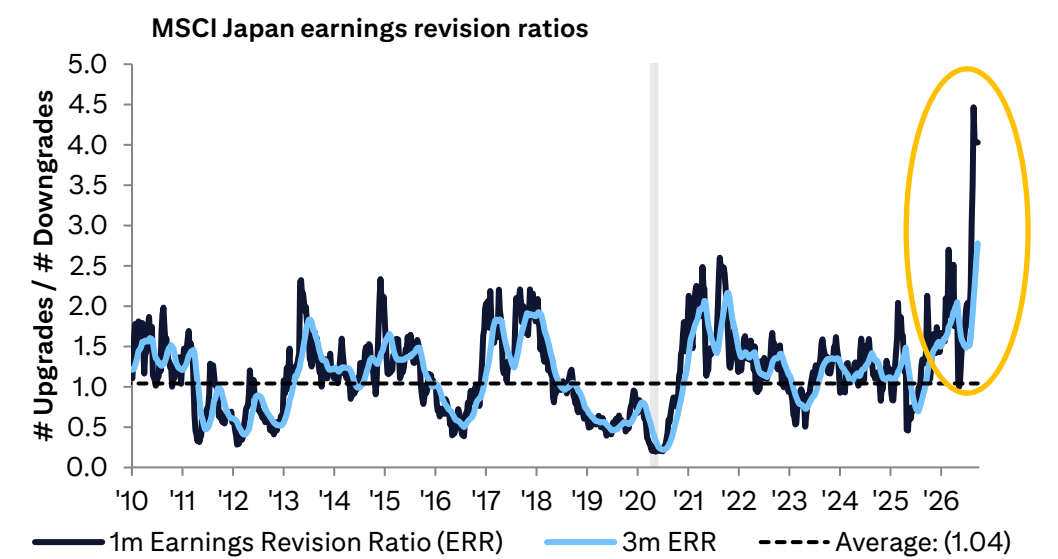
Bottom line: Cybersecurity is becoming an unavoidable cost of enterprise AI, and we believe the spending cycle has only begun. It offers investors a durable way to participate in AI adoption without betting on a single model or platform.

Japan combines a cyclical improvement in growth with a structural improvement in corporate profitability. The macro and earnings signals are pointing in the same direction, which gives us the conviction to move Japanese equities from a slight underweight to a modest overweight.

Japan's growth backdrop remains firmly expansionary. Both its three-month and six-month average PMI readings are expansionary and rising, placing Japan alongside the U.S. with respect to macroeconomic momentum. Outside the U.S., Japan shows some of the strongest growth momentum among developed markets.

Earnings revisions send an even stronger signal. Across MSCI Japan, upgrades now outnumber downgrades by 2.6 to 1 on a three-month rolling basis, well above the long-term average of roughly 1.0 (Figure 2). The one-month revision ratio has accelerated sharply, and the three-month trend confirms that the improvement extends beyond a single set of recent estimate upgrades.

FIGURE 2: Earnings upgrades outnumber downgrades by 2.6 to 1



Source: Datastream as of September 25, 2026. Yellow circle indicates recent positive equity revision surge in Japanese equities. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

U.S. LARGE CAPS ANCHOR PORTFOLIOS, FUNDED FROM TIGHT SECURITIZED SPREADS

Companies are converting this backdrop into realized profits. Japanese corporate profits have climbed to 22% of output, a multi-decade high in data going back to 1970. We treat profitability as our north star for the U.S. cycle, and it carries similar weight for us in other markets, since recessions have historically coincided with declining corporate profits.

Positioning completes the picture. Rolling 65-day ETF flows into Japan remain near flat as a share of assets under management, well below prior peaks in investor enthusiasm, leaving ample room for further participation. Structural tailwinds reinforce the opportunity. Since taking office last fall, the Takaichi government has advanced a pro-growth fiscal agenda, while Japanese industrial companies supply critical materials used in the production of high bandwidth memory, a key component of the AI supply chain.

Bottom line: Japan offers growth momentum, accelerating earnings revisions, and record profitability without euphoric positioning. We believe this combination supports a larger allocation to Japanese equities as a source of improving momentum outside the U.S.

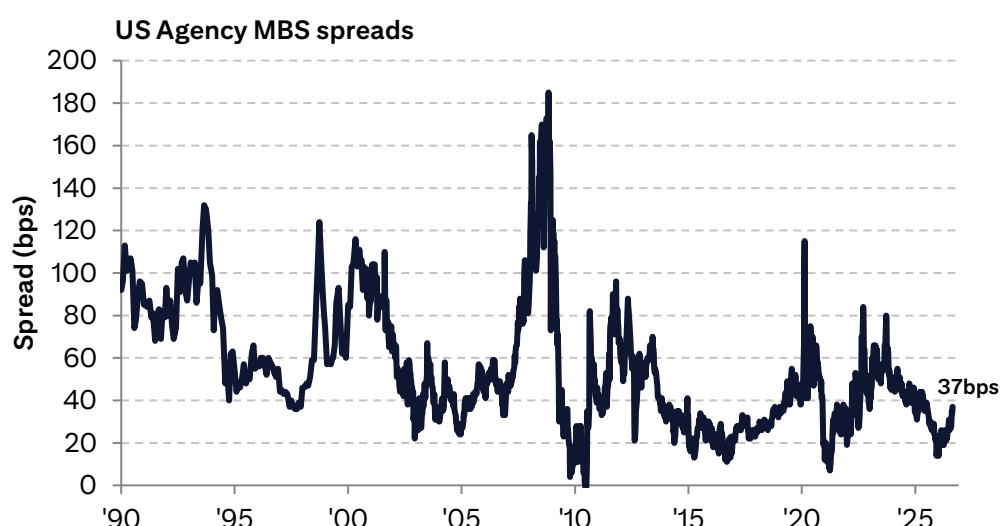
U.S. large caps remain the quality anchor of our equity allocation. The S&P 500 leads major regions in year-to-date revisions to next-12-month earnings at 29.2%, and it posts the highest interest coverage ratio at 9.4x. These fundamentals offer resilience against a complicated geopolitical backdrop.

The entry point has also improved. As real yields have risen, valuations have compressed, leaving the S&P 500's price-to-earnings multiple in the 29th percentile since 2020, while earnings growth sits in the 89th percentile. Valuation forms only one piece of our process, but superior fundamentals at a better price strengthen the case.

We continue to favor large caps over small caps, and our conviction has strengthened as the Fed has raised rates and tightened financial conditions. Over the past month, large caps outperformed small caps by more than 6.5%. Year to date, large caps now trail by just 0.9%, narrowing the gap from 14% in June.

We fund these additions from securitized fixed income, and the decision reflects relative opportunity rather than a negative view on credit quality. In our view, agency mortgage-backed securities (MBS), which comprise the bulk of securitized assets, remain high-quality holdings with a role in diversified portfolios. However, agency MBS spreads stand at 37 basis points, near the tight end of their range since 1990, which we believe limits the potential for further price appreciation (Figure 3).

FIGURE 3: Tight MBS spreads offer limited compensation for incremental risk



Source: Bloomberg as of September 25, 2026. Bloomberg U.S. MBS Index used as proxy. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

Rate volatility adds to the concern. Rising readings on the MOVE Index, which tracks interest rate volatility, have historically coincided with weaker MBS returns. MBS also carry extension risk: when rates rise, prepayments slow and effective duration lengthens, increasing sensitivity to further rate increases. Given our underweight view on duration, we reduced securitized exposure to benchmark weight.

Bottom line: U.S. large caps combine superior fundamentals with a better entry point following valuation compression. We believe tight spreads and sensitivity to rate volatility make securitized fixed income a logical funding source for these higher-conviction equity opportunities.

ECONOMIC DATA

WHAT HAPPENED

U.S.

U.S. PMIs jumped up to 58.4 from 56 with both manufacturing and services contributing to the strongest reading since July 2021.

Global

Eurozone PMIs for September rose to 53.1 to reach its highest level in over three years as France activity expanded for the first time in ten months; inflation signal worrying.

Germany's IFO business outlook survey recovered to the highest level since 2025, and growth forecasts for 2026 were raised to 1.3% from previous 0.6% estimate.

WHAT'S AHEAD

U.S.

Employment report for August

Personal Consumption Expenditures (PCE) for August

Manufacturing Institute for Supply Management (ISM) for September

Global

China PMIs for September

Eurozone CPI for September

POLICY

U.S.

President Trump/Xi summit largely as expected following two-month extension of trade truce. Both gave no inclination to curb AI competition, no news or purchase agreements.

Trump administration mulls diesel export ban but investors are mixed on efficacy and long-term supply effects.

Global

BoE deputy chief signaled rate hikes are increasingly likely if energy prices remain elevated. Lombardelli was among the six officials that voted to leave rates unchanged this month.

Japan PM Takaichi signaled caution about committing to a defense spending target of 3.5% of GDP.

U.S.

U.S. and Iran discussing a phased deal to reopen the Strait of Hormuz with the first stage seeing Iran allowing Hormuz flows while U.S. lifts economic blockade.

Fedspeak leaned hawkish with Barkin (nonvoter), Hammack (voter), Paulson (voter), and Williams (voter) all agreeing inflation pressures are mounting and it could be more challenging to bring back down.

Global

Red Sea loadings well below estimates with the East-West pipeline restart yet to resume Red Sea exports as Houthi attacks intensify.

MARKETS

U.S.

Yields hitting multi-decade highs after hotter growth signals (PMIs) and a weak five-year note auction added to angst. Big move in real yields while breakevens remain relatively contained.

Global

U.S.

Early Q3 reporters beating on top and bottom lines more than average. There is a strong relationship between early reporters and full quarter results, suggesting we may see further upside surprises in coming weeks.

Global

September is historically the weakest month for equities with an average return of -0.8% for the S&P 500.

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RELATED READING

[September 24, 2026 | Global Investment Council](#)

The Citi Wealth Global Investment Council met September 24, 2026, and increased allocations to U.S. equities, Japanese equities, and the cybersecurity theme, funded by a reduction in the overweight to U.S. securitized fixed income. The Council also reviewed and endorsed the portfolio's drift, remaining comfortable with the market-driven increase in equity exposure relative to fixed income.

[September 24, 2026 | The Short and Long Podcast](#)

In the fourth episode, "Semiconductors: Navigating the AI Supercycle," host and Chief Investment Officer of Citi Wealth Kate Moore speaks with Adam Parker, Founder of Trivariate Research, and Ankur Crawford, Portfolio Manager at Alger, on why we may be only three-to-four years into a ten-year AI investment cycle, how "AI touch" is reshaping the way investors think about sector exposure and key risks that could slow the buildout. Watch on [YouTube](#), [Apple](#), or [Spotify](#) and subscribe for future episodes.

[September 22, 2026 | Higher Rates Are Here to Stay, and Earnings Keep Pace](#)

In last week's Bulletin, we looked at how strong global growth gives central banks room to lean against inflation with higher policy rates. We also looked at why higher rates have yet to dent corporate fundamentals and what this could mean for the macro outlook.

[September 18, 2026 | Fed Hikes in Response to High Inflation](#)

In our latest CIO Update, we look at the U.S. Federal Reserve's decision to raise its benchmark rate by 25 basis points, its first increase since 2023. We review what this means for investors and look at why persistent inflation raises the bar every portfolio, even as higher policy rates lift nominal yields on cash.

[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.

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Highest quality	Aaa	AAA	AAA
High quality (very strong)	Aa	AA	AA
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

1 The ratings from Aa to Ca by Moody's may be modified by the addition of a 1, 2, or 3, to show relative standing within the category.

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- potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized;
- absence of information regarding valuations and pricing;
- complex tax structures and delays in tax reporting;
- less regulation and higher fees than mutual funds; and
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