WEEKLY STRATEGY

Perspectives

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Great Expectations: What to Watch for This Earnings Season

"It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of light, it was the season of darkness, it was the spring of hope, it was the winter of despair."

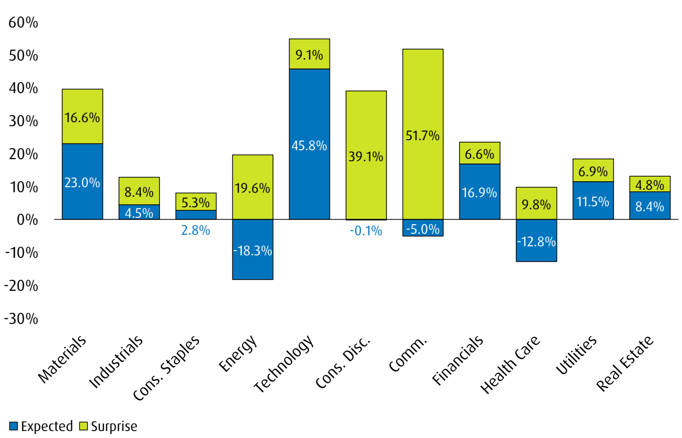
\- Charles Dickens, *A Tale of Two Cities*

The Through Line: Investors are entering the Q2 reporting season buoyed by lofty expectations rooted in unexpectedly robust Q1 results. Economic statistics from the last three months suggest the strength can continue thanks to resilient consumers, strict attention to business operational efficiency and record levels of corporate transactions. Most global bourses are within an eyelash of all-time highs, so trading trigger fingers are nervous. We outline the themes to watch as results continue to roll in.

Q2 expectations: the bar moves up

Aggregate first quarter earnings topped even the most optimistic estimates. The S&P 500, for example, grew earnings at a 28% clip versus the 13% that consensus had projected when the period started. And it wasn't just AI or AI-adjacent companies: eight of 11 sectors produced double-digit earnings growth. Materials, consumer discretionary, tech and communication services boasted bottom-line upturns of better than 40%. All 11 sectors generated better than projected results.

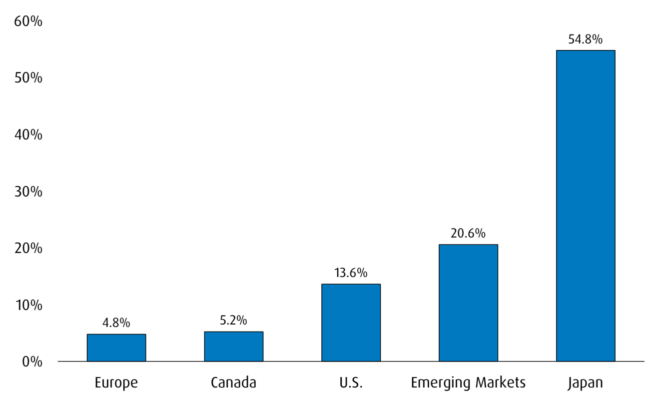
S&P 500 Sector Q1 2026 EPS Growth: Expected & Surprise



Source: Bloomberg L.P. (2026)

Such stellar numbers prompted analysts to nudge *second quarter* estimates noticeably higher in the U.S., Canada and particularly in Southeast Asian markets (chart).

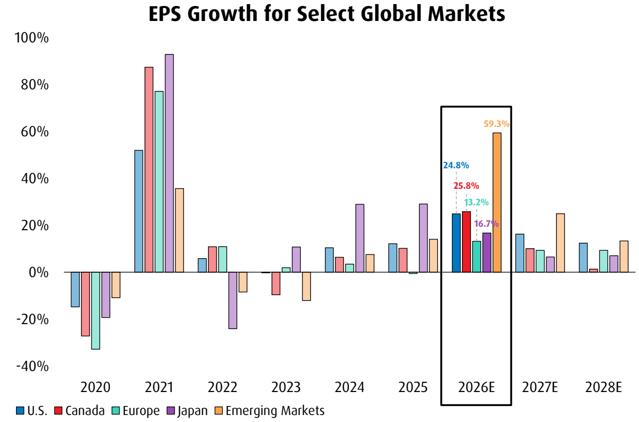
Change in Q1 2026 Earnings Estimates (12/31/2025-6/30/2026)



Source: Bloomberg L.P. (2026)
U.S.: S&P 500; Canada: S&P/TSX Composite; Europe: Stoxx Europe 600; Japan: Nikkei 225; Emerging Markets: MSCI Emerging Markets

This tees up a second quarter report period with loftier expectations than previous quarters. Bloomberg reports that consensus is now looking for combined Q2 S&P 500 earnings growth of 25%; TSX earnings are projected to rise 26%.

EPS Growth for Select Global Markets



Source: Bloomberg L.P. (2026), as of 7/21/2026
U.S.: S&P 500; Canada: S&P/TSX Composite; Europe: Stoxx Europe 600; Japan: Nikkei 225; Emerging Markets: MSCI Emerging Markets

So far so good – but a lot to live up to

The U.S. season kicked off in fine fashion last week with some of the largest money center banks and select other financials reporting. The industry didn't disappoint: total earnings for those that have reported advanced more than 30% (well above analysts' expectations), benefiting from volatile markets (lots of trading revenue), record-setting Mergers & Acquisition (M&A) activity and substantial fees from record-breaking stock and bond issuance.

On the flip side, IBM shares were pummeled – down nearly 30% in a single day (the worst decline in over half a century) when the company pre-announced a 4% revenue miss. It exacerbated the concern by noting that it had misread a sudden shift in customer activity when they prioritized AI spending over purchasing IBM hardware and services. The fact that the U.S. government awarded a $2 billion quantum computing contract to Big Blue (prompting the biggest one-day stock price *jump* since 1968) was clearly forgotten as investors hummed that familiar tune "what have you done for me lately?"

The through line: Hopes are high – but so are stock prices, expectations and the perception of valuations. This makes trigger fingers itchy. It's likely that even beat and raise reports (a.k.a. highly positive corporate earnings announcements when a company handily beats financial targets and increases its future guidance) will be greeted by a sigh of relief (if not an outright yawn). On the other hand, misses or perceived disappointments may well be taken to the woodshed. Management teams will need to tread carefully during post-release conference calls to convey an in-depth picture of how they are handling the constantly evolving setting.

AI: under the microscope

AI will undoubtedly be first on the list of issues, including progress on data center builds. By some estimates, barely half of the more than $700 billion in announced projects have been started[i] and investors will want to get a read on what's stalled, moving and newly planned. They will also want to know about any bottlenecks in powering the data centers – either hooking to an existing grid or plans for sourcing off the grid (so called behind-the-meter arrangements).

Analysts will probe financing. To date, a mix of corporate cash flow plus stock and bond issuance has been used to fund capital expenditures (CapEx). The additional shares and debt offerings were readily absorbed. However, softening demand for the most recent rounds of hyperscaler debt (and after-market price drops in longer-maturity paper) hint that bond investors are sending an important message to issuers: **show us fundamental progress in order to receive our continued support**. *When key hyperscalers release next week (Apple, Amazon, Meta and Microsoft) individual stocks (or entire sectors) could see outsized price moves depending upon how the narrative is perceived.*

Margins will also be scrutinized. The graphic programming and memory chips needed to outfit data centers are being accumulated even if the buildings aren't yet operational. In some cases, warehouse space near data centers is being marshaled to house materials and components until permitting and groundbreaking are complete. Storage and insurance costs pick away at margins, and delays expose purchases to other costs (e.g., the risk of new tariffs). **Investors have quickly learned that one company's excess margin is another company's increased cost.** That's a delicate tug of war for investors to navigate while assessing how best to participate in the most significant infrastructure reboot of our time.

For companies not directly involved in data center buildouts, the AI questions will (again/still) revolve around progress on implementation and use cases, cost/budget for token use, and the increasing preponderance of efficient routing techniques designed to ensure that requests are sent to the most cost-effective resource. Anecdotal evidence suggests rollouts are moving quickly as AI and other advanced technologies push everyone into a mode of "figure it out to stay competitively viable." Ready or not here it comes; inquiring investor minds want to know how companies are responding.

Consumers: crabby but consistent

Last week's bank results gave us an early read on consumers – and the news is constructive. Balance sheets in aggregate are healthy and total household net worth remains at all time high levels. A low 4%ish unemployment rate means most of the populace is in the labor force – and employed individuals spend. A record percentage of citizens own stocks; stocks at record highs produce additional psychological comfort around spending (the "wealth effect"). Aggregate spending further underpins a constructively growing economy.

Although consumers' economic profile is solid overall, their psychological profile remains dour. This general dissatisfaction has been present and worsening since the pandemic. While policymakers and strategists obsess about inflation (a.k.a. the rate of change in prices), **consumers care about absolute price levels. And the simple fact is that average prices (proxied in the U.S. as the Consumer Price Index) are up 29% since the start of the pandemic**.[ii] No amount of moderating inflation is going to bring those levels back down. The elevated gas prices of the last few months don't help, nor does the growing fear in some quadrants re potential job losses due to AI.

Still, even crabby consumers consume. We've seen that trend over and over through household expenditure numbers and last week's bank and credit card company reports. Sometimes they spend precisely *because* they're crabby. Actions speak louder than words. Investors care that consumers keep their wallets open. Investors don't care what mood consumers express to pollsters, who will be closely parsing earnings releases for hints of slowing or significant shifting in services versus goods.

M&A and CapEx: bull market in process

M&A has been running at record levels in the first six months of 2026, even though the aggregate number of transactions has dropped slightly relative to last year. According to a recent Bloomberg article, only 24% of the deals have emanated from venture portfolios versus 34% that came from that source last year.[iii] **This suggests that large companies are deploying strategic repositioning to gear up for a resilient future. Companies are shedding non-core businesses while simultaneously buying others to supplement key endeavors.**

Capital spending is also running at a rapid clip, which Fed Chair Kevin Warsh addressed during last week's congressional testimony. He noted: "*The most striking feature of the economy right now is business investment. The rapid pace – which appears to be accelerating – reflects, in large part, the construction of data centers and the immense demand for the AI-related equipment and software that fill them. Investment in equipment overall increased about 8% for the year ending in the first quarter. Within that category, high-tech spending logged an especially impressive growth rate of nearly 25% on a four-quarter basis.*" **While the data-center spend gets the attention, non-data spending growth of upper single digits is praise worthy.** Multiple projects such as roads, bridges, ports, factory automation, reshoring and manufacturing expansion are rolling out at an increasingly rapid clip thanks to funding from several Biden-era infrastructure programs and the important tax benefits woven into last summer's new tax law (e.g., accelerated R&D and construction expensing).

Costs: tariffs plus energy boon and bane

Corporate margins in both Canada and the U.S. remain near record highs – proof of the increasing resilience that has been fire-forged in the many tests of the past decade. Still, during this earnings season investors will be closely watching for signs of cracking. Higher energy prices, for example, have the potential to touch virtually every industry. Because they only spiked for the last month of the first quarter, we won't get a full-bodied picture of how companies are being impacted – or how they plan to respond – until more companies have reported this period.

Tariffs are another conundrum. The IEEPA (country-wide) levies initiated in April of last year were ruled unlawful by the Supreme Court and some companies applied for and received refunds. To date, refunds of nearly $90 billion have been returned to U.S. companies.[iv] The Trump administration has pulled many levers trying to replace those revenues, including this week's surprise announcement of 50% tariffs on a broad variety of Canadian goods (incorporating for the first time those that fall under CUSMA/USMCA protections) to be implemented on August 19. The president invoked a never before used section of law giving him authority to impose tariffs on countries perceived to be discriminating against U.S. goods. Interestingly, markets largely remained calm despite the surprising news. This suggests they regard the move as a typical Trump negotiation tactic: "escalate to deescalate." By the end of Tuesday, Canadian Prime Minister Mark Carney and the Trump administration were noting an intention to accelerate trade talks before the August deadline. Additional tariffs on other countries and goods are also rumored to be in the works for announcement this week. Not coincidentally, the 10% blanket tariffs President Donald Trump issued when his IEEPA tariffs were overruled last spring expire on Friday, July 24.

We expect analysts to vigorously dig into potential tariff/trade disruption issues during reporting season. While they may have only partial or no impact on this quarter's numbers, analysts will be looking for indications of corporate contingency plans to handle any new levies. They will also need to understand how companies that received refunds deployed them so models are not distorted relative to future periods.

Analysts will also be watching for downstream price pressures from AI knock-on impacts. As prices for memory chips go up by double or even triple digits, for example, we'll be watching to see who pays, who doesn't and who has the pricing power in their own products to pass on. Can offsets be found elsewhere? We've noted many times that the rollout of transformational technology is bound to be bumpy. Yet, history tells us infrastructure investment boosts long-term productivity.

The bottom line

Over the next few weeks, earnings season will gear up and trading may well be volatile against a backdrop of double-digit market performance to date and buoyant expectations for outsized earnings progress. Healthy earnings prospects are broad based despite the perception that a handful of hyperscalers are driving the bus. Thus, those names may have undue influence on short-term markets on report days if results don't meet (or more likely excessively beat) consensus expectations. However, any pullbacks represent repositioning opportunities. We would not view them as an indication of a bubble bursting nor disruption of the solid long-term trends currently in motion.

Next week in North America

A newsworthy week: the U.S. central bank rates decision and presser on Wednesday; earnings reports from hyperscaler heavyweights Meta, Apple, Microsoft and Amazon. University of Michigan and Conference Board readings will also be on the docket, offering a glimpse into consumer confidence levels. In Canada on Wednesday, we'll get a peek at minutes from the last Bank of Canada rate-setting meeting and on Friday a GDP measure.

Monday 7/27:	**U.S.** Durable-goods orders | **Canada** none scheduled
Tuesday 7/28:	**U.S.** Advance U.S. trade balances, Retail and Wholesale trade inventories, Consumer confidence | **Canada** none scheduled
Wednesday 7/29:	**U.S.** U.S. Federal Reserve FOMC rates decision and press conference | **Canada** BoC Summary of deliberations
Thursday 7/30:	**U.S.** Initial jobless claims, Personal income and spending, PCE | **Canada** Average weekly earnings
Friday 7/31:	**U.S.** Employment cost index, Chicago PMI, Consumer sentiment | **Canada** GDP, Budget balance

Index Definitions

Equity indices

S&P 500® Index is an index of large-cap U.S. equities. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

NASDAQ Composite Index is a market-cap weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange.

Dow Jones Industrial Average ("DOW") is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq.

Russell 2000® Index (Russell 2000®) is an unmanaged index that measures the performance of the smallest 2000 U.S. companies in the Russell 3000® Index.

S&P/TSX Index is a capitalization-weighted equity index that tracks the performance of the largest companies listed on Canada's primary stock exchange, the Toronto Stock Exchange (TSX).

MSCI EAFE Index (Developed Markets —Europe, Australasia, and Far East Index) is a standard unmanaged foreign securities index representing major non-U.S. stock markets, as monitored by Morgan Stanley Capital International. The index captures large and mid-cap representation across 21 developed markets countries around the world, excluding the U.S. and Canada.

MSCI Emerging Markets Index is a market capitalization weighted index representative of the market structure of the emerging markets countries in Europe, Latin America, Africa, Middle East and Asia. Prior to January 1, 2002, the returns of the MSCI Emerging Markets Index were presented before application of withholding taxes.

Fixed income indices

Bloomberg U.S. Aggregate Bond Index is an unmanaged index that covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities.

Bloomberg U.S. Treasury Index is an unmanaged index that includes a broad range of U.S. Treasury obligations and is considered representative of U.S. Treasury bond performance overall.

Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

Bloomberg U.S. Corporate High Yield Index is an unmanaged index that covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody's, Fitch and S&P is Ba1/BB+ or below.

Bloomberg 1-10 Year Blend Municipal Bond Index is a market value-weighted index which covers the short and intermediate components of the Bloomberg Capital Municipal Bond Index — an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market.

Bloomberg Canada Aggregate Bond Index measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market. It includes treasuries, government-related, and corporate issuers.

Bloomberg Canada Aggregate Bond Index - Treasury is the treasury sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.

Bloomberg Canada Aggregate Bond Index - Corporate is the Corporate sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.

Precious metal investing involves greater fluctuation and potential for losses.

[i] US Data Center Boom Relies on Hard-to-Find Electrical Equipment - Bloomberg

[ii] Inflation Calculator | Federal Reserve Bank of Minneapolis

[iii] Global M&A Tops $2.5 Trillion After First-Half Deals Surge - Bloomberg

[iv] Tariff Refund Update July 2026: $86B Paid, $49B in June