



AOR Update: Mailbag Edition

May 4, 2026

Key Takeaways

- ▶ Although we saw a geopolitical dip in March, it once again proved to be a good opportunity to deploy capital with the S&P 500 rallying back to all-time highs in a matter of weeks.
- ▶ The ClearBridge U.S. Recession Dashboard continues to show an overall green signal. The housing permits indicator is now again available following a lapse due to the government shutdown and has improved to a green signal.
- ▶ We continue to believe the economic impacts of the Middle East conflict remain manageable and further pullbacks are likely to represent buying opportunities; we modestly favor the positive earnings revisions and less demanding valuations of non-U.S. equities.

A Fast and Furious Rebound

U.S. equities have roared back to all-time highs, rising 13.6% from their late-March lows. April alone accounted for 10.4% of the rally, marking the best month for the market since 2020 and the 12th best monthly gain in over 75 years. Although we saw a [geopolitical dip](#) emerge in March, it once again proved to be a good opportunity for investors to deploy capital. A key reason we continue to believe markets can [climb the wall of worry](#) is the green overall signal emanating from the ClearBridge U.S. Recession Dashboard.

We are pleased to welcome back Housing Permits, the final dashboard indicator that has been unavailable due to data delays from the government shutdowns. The new data shows that housing permits have stabilized, and the indicator has turned green from the yellow reading that existed when the data disruptions began (Exhibit 1).

The market rally in April came on fast and furious; so have the AOR team's travels been over the past several weeks, sending us across the U.S. and to five countries across two continents. We met with a wide array of investors, and the overwhelming majority of our conversations focused on five key questions. We thought it would be helpful to succinctly outline our thinking on these issues.

1. **How worried should we be about the labor market?**

The labor market has alternated between positive and negative prints for the past 11 months, with net job creation modestly positive on balance. More broadly, the labor market has cooled over the past few years primarily due to drags from changes in immigration policy and the aging population demographics. It still does not appear that artificial intelligence (AI) is driving [widespread layoffs](#), although there are pockets of softer hiring.

We are encouraged by initial jobless claims — our economic [canary in the coalmine](#) — notching its lowest total since 1969 last week alongside other recent signs of labor market stabilization. Looking ahead, we remain on watch for AI-driven job losses, but we are also eyeing AI job creation as previously unimaginable jobs emerge on the back of this technological advancement.

Exhibit 1: U.S. Recession Dashboard

	April 30, 2026	Dec. 31, 2025	Sept. 30, 2025
Consumer	Housing Permits	↑	●
	Job Sentiment	×	×
	Jobless Claims	↑	↑
	Retail Sales	↑	↑
	Wage Growth	↑	↑
Business Activity	Commodities	↑	↑
	ISM New Orders	↑	×
	Profit Margins	●	●
	Truck Shipments	↑	↑
Financial	Credit Spreads	↑	↑
	Money Supply	↑	↑
	Yield Curve	↑	●
Overall Signal	↑	↑	↑

↑ Expansion ● Caution × Recession

Data as of April 30, 2026. Source: ClearBridge Investments.

2. How could the Fed evolve under Kevin Warsh?

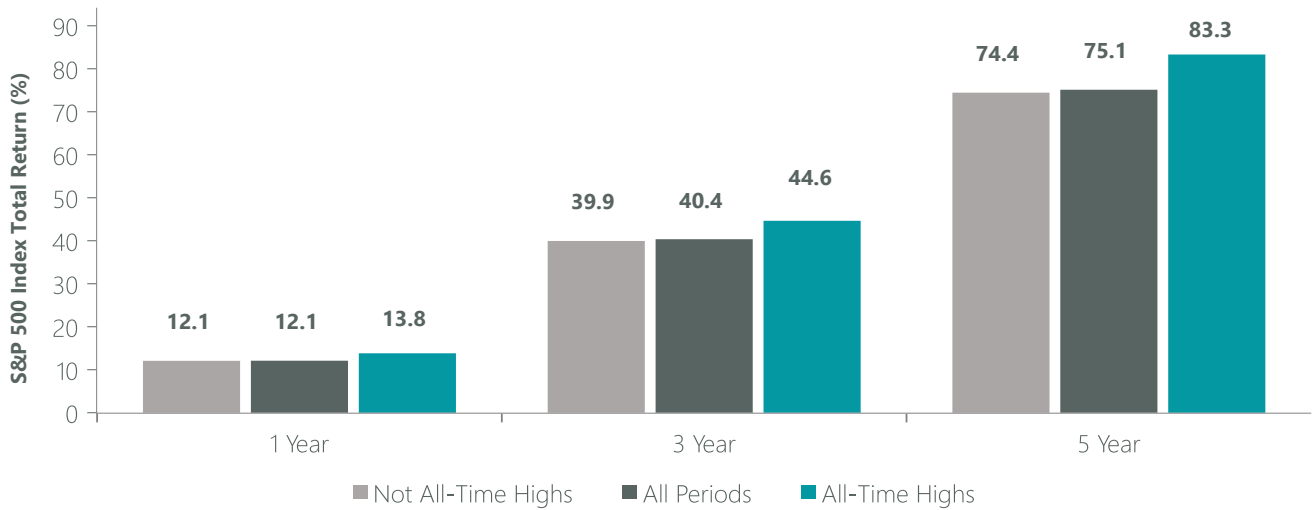
It is important to remember that monetary policy decisions are made by a majority count of the 12 voting members of the Federal Open Market Committee (FOMC) rather than just the Fed Chair. While Kevin Warsh is on the record as favoring lower interest rates, his views appear out of sync with the rest of the FOMC at the moment. The FOMC’s meeting in late April produced no change in interest rates, but four dissents — the most since 1992 — with three of them opposing the “inclusion of an easing bias in the statement at this time.” Upside risks to inflation emanating from higher energy prices are likely to keep FOMC members wary of lowering rates until greater clarity emerges regarding the conflict in the Middle East.

3. The Middle East remains fragile despite the ceasefire and markets are back to all-time highs. Are equities getting ahead of themselves?

The equity rally does appear to be vulnerable to a re-escalation of the conflict in the Middle East, particularly if disruption to trade in the Strait of Hormuz lasts longer than is currently expected (reopening around mid-year). Given that the bulk of the April rally occurred in conjunction with the de-escalation of tensions in the Middle East, we believe the risk of a prolonged supply bottleneck is real.

We continue to believe that the economic impacts should remain manageable and not result in a meaningful economic slowdown: further pullbacks would likely represent buying opportunities, in our view. At the same time, we do not believe investors should be scared off by the markets being back at all-time highs. Our work (counterintuitively) shows that investing at new highs has historically outperformed deploying capital when the benchmark is below peak.

Exhibit 2: Don't Be Afraid of All-Time Highs



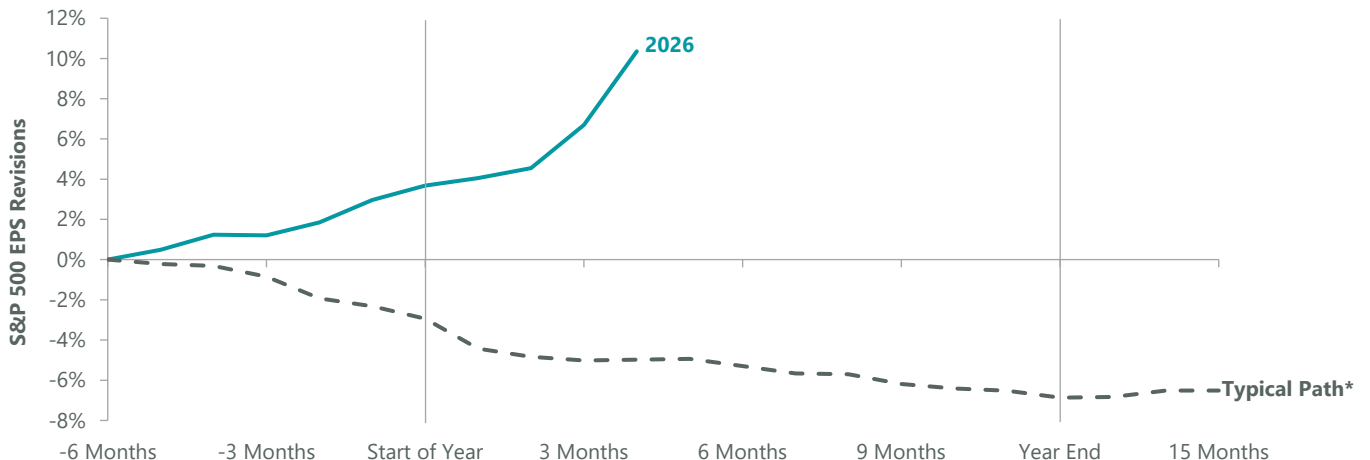
Data from Sept. 1989 – April 30, 2026. Sources: S&P Global, Macrobond.

4. How concerning are high valuations and lofty earnings expectations?

Valuations are elevated, with the S&P 500 Index trading back above 20x on forward (next-12-month) P/E basis. However, U.S. equities have been trading at rich multiples since the pandemic, with the benchmark remaining above 20x most of the time (63%) since first crossing that threshold in April 2020. Importantly, lofty valuations have not been a headwind to returns; the S&P 500 has risen 147.5% over the past six years, or 16.3% annualized, which is roughly double the long-term average.

Much of this strength has been underpinned by robust earnings, with next-12-month earnings expectations rising 137% cumulatively over the past six years. Sell-side consensus expectations for mid-teens earnings growth may seem lofty at first blush. However, these expectations have been moving steadily higher, bucking the historical pattern and providing a fundamental support to the market rally. Information technology, energy and materials sectors are showing notable strength. With the first-quarter earnings season now past the two-thirds mark (by market cap), results so far have been solid, with strong delivery and upside surprises across sectors. This is an encouraging start to the year.

Exhibit 3: EPS Revisions Resilient

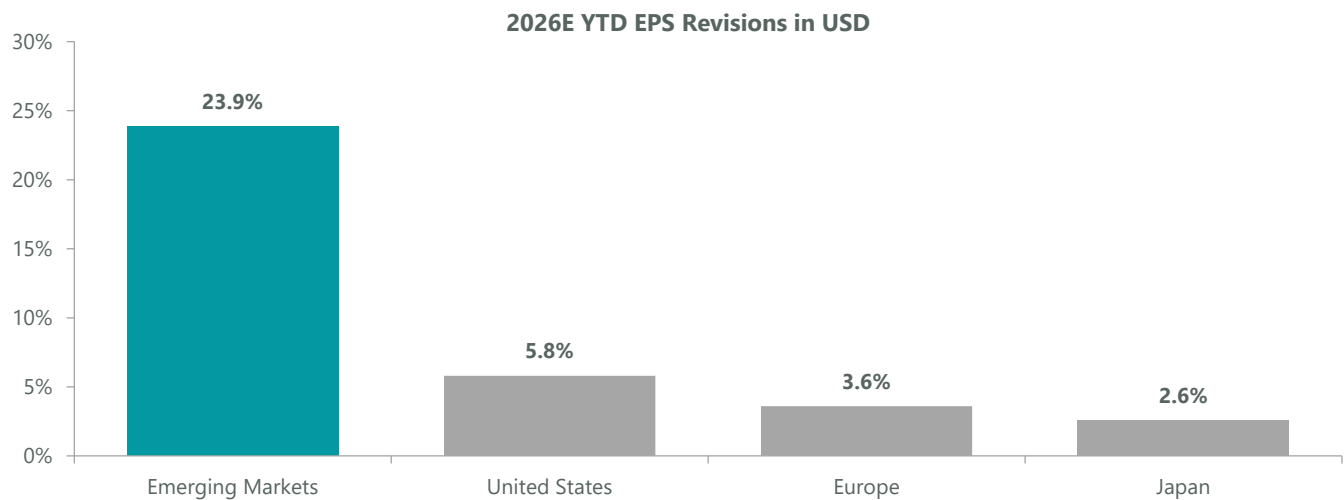


*Typical Path is 2012-2017, 2019, and 2022-2024; 2018 is excluded due to TCJA (Tax Cuts and Jobs Act) distortion; 2020-2021 is excluded due to COVID-19 pandemic distortion; Percent change in \$EPS expectations. Data as of April 30, 2026. Sources: FactSet, S&P.

5. What opportunities do you see in the market at present?

We continue to believe non-U.S. equities present an attractive opportunity relative to domestic stocks. Emerging markets (EM) look particularly compelling despite their recent strength, with robust revisions to earnings expectations powering their returns and supporting a continued constructive fundamental outlook. Valuations also remain less challenging than in the U.S., and although some EM economies are significant oil importers, the adage that the stock market is not the economy rings even more true in the case of many EM countries. Developed non-U.S. equities should also benefit from positive earnings revisions and attractive valuations, although to a lesser degree.

Exhibit 4: Earnings Revisions Favor Emerging Markets



Japan represented by the MSCI Japan index, Europe represented by the MSCI Europe index, Emerging Markets represented by the MSCI Emerging Markets index, and United States represented by the MSCI USA index. Data as of April 30, 2026. Sources: FactSet, MSCI.

In sum, markets have quickly reclaimed new highs, yet the underlying backdrop still appears supportive: the ClearBridge U.S. Recession Dashboard remains green, the labor market continues to stabilize and we believe the economic fallout from Middle East tensions will remain manageable. Elevated valuations warrant selectivity, but history suggests investors needn't shy away from new highs, particularly when earnings expectations are holding up. We would stay disciplined, using volatility as an opportunity to deploy capital, while modestly favoring the stronger earnings revisions and more reasonable valuations available in non-U.S. equities.

About the Authors



Jeffrey Schulze, CFA

Managing Director, Head of Economic and Market Strategy

- 21 years of investment industry experience
- Joined ClearBridge Investments in 2014
- BS in Finance from Rutgers University



Josh Jamner, CFA

Director, Senior Investment Strategy Analyst

- 17 years of investment industry experience
- Joined ClearBridge Investments in 2017
- BA in Government from Colby College

ClearBridge Investments
ClearBridgeInvestments.com.au

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