M1 CAPITAL
INVESTMENT MANAGEMENT

AI Falters – Market Commentary

July was marked by a reversal of AI's gains and this impacted global benchmarks.

Most prominent in Developed Markets was the Nasdaq which declined -6.6% while the S&P 500 ended the month only marginally down at -0.1%. The US indices in turn impacted the MSCI World Index which was marginally up +0.5% vs the MSCI World ex-US at +2.1%.

Emerging Markets were down -3.1%, under pressure from sharp declines in Korea and Taiwan which have significant concentrations in AI stocks. Korea declined -39.4% from its peak while Taiwan was down -16.8% but both regained losses to end the month -17.1% and -5.4% respectively.

It should be noted that both the Nasdaq and the MSCI Emerging Markets Index remain strongly positive for the year-to-date at +20.3% and +23.8% respectively even after July's declines.

South Africa was not impacted by the volatility in the AI sector and returned a marginally positive +0.2% in USD terms. The return masked some underlying volatility e.g. Sasol was up +20.2% while Gold shares were down -1.3% in ZAR terms.

SA is lagging EMs for the year-to-date at -1.9% vs +23.8%. This is courtesy of a lack of AI representation and a declining Gold price in SA and significant AI presence in EMs primarily through Korea and Taiwan.

The various market returns are summarised in Table 1 below.

Table 1. South African and global equity returns (USD) for June 2026*

	Jul-26	YTD 2026
FTSE/JSE ALSI (ZAR)	1.2%	-3.0%
FTSE/JSE ALSI (USD)	0.2%	-1.9%
MSCI World	0.5%	9.7%
MSCI World ex-US	2.1%	9.2%
MSCI EM	-3.1%	23.8%
MSCI Value	3.6%	10.5%
MSCI Growth	-2.5%	8.8%
S&P 500	-0.1%	10.0%
Nasdaq 100	-6.6%	20.3%

*Total return indices, Source: Factset

July's sharp reversal of the AI trade may mark an inflection point for the market. The impact was felt primarily in US semiconductors and memory stocks, down -21.2% and -31.8% respectively, as well as the prominently covered emerging markets Korea and Taiwan. As a reminder Korea is heavily concentrated in Samsung and SK Hynix, both of which account for 67.3% of the MSCI Korea index, while Taiwan is dominated by TMSC which represents 58% of the MSCI Taiwan index.

For context the top holdings for the MSCI Korea and Taiwan are presented in Table 1 below.

Table 1. MSCI Korea and Taiwan top constituents

Korea	Float Adj Mkt Cap (USD Billions)	Index Wt. (%)	Sector
SAMSUNG ELECTRONICS CO	861.13	35.44	Info Tech
SK HYNIX	665.59	27.39	Info Tech
SAMSUNG ELECTRONICS PREF	107.49	4.42	Info Tech
SK SQUARE CO	67.25	2.77	Industrials
SAMSUNG ELECTRO-MECH. CO	44.87	1.85	Info Tech
KB FINANCIAL GROUP	41.86	1.72	Financials
HYUNDAI MOTOR CO	36.22	1.49	Cons Discr
SHINHAN FINANCIAL GROUP	29.34	1.21	Financials
HANA FINANCIAL HOLDINGS	23.87	0.98	Financials
KIA CORP	21.67	0.89	Cons Discr
Total	1,899.30	78.17	

Taiwan	Float Adj Mkt Cap (USD Billions)	Index Wt. (%)	Sector
TAIWAN SEMICONDUCTOR MFG	1,848.51	58.07	Info Tech
MEDIATEK INC	158.78	4.99	Info Tech
DELTA ELECTRONICS	98.86	3.11	Info Tech
HON HAI PRECISION IND CO	94.71	2.98	Info Tech
ASE TECHNOLOGY HOLDING	57.28	1.80	Info Tech
UNITED MICROELECTRONICS	42.38	1.33	Info Tech
ELITE MATERIAL CO	42.09	1.32	Info Tech
FUBON FINANCIAL HOLDING	33.81	1.06	Financials
CTBC FINANCIAL HOLDING	33.59	1.06	Financials
ACCTON TECHNOLOGY CORP	33.20	1.04	Info Tech
Total	2,443.20	76.76	

Source: MSCI

These two markets provide some useful perspective and a point of comparison for both the US and SA markets which are perceived to be highly concentrated.

The Mag 7 accounts for 31.9% of the MSCI USA, illustrated in Table 2 below and presented instead of the S&P 500 for comparability to Korea and Taiwan above.

Table 2. MSCI USA top constituents

	Float Adj Mkt Cap (USD Billions)	Index Wt. (%)	Sector
NVIDIA	4,634.31	7.19	Info Tech
APPLE	4,535.15	7.03	Info Tech
MICROSOFT CORP	3,278.30	5.08	Info Tech
AMAZON.COM	2,628.58	4.08	Cons Discr
ALPHABET A	2,073.39	3.22	Comm Srvcs
BROADCOM	1,750.96	2.72	Info Tech
ALPHABET C	1,648.54	2.56	Comm Srvcs
META PLATFORMS A	1,222.56	1.90	Comm Srvcs
JPMORGAN CHASE & CO	943.58	1.46	Financials
MICRON TECHNOLOGY	928.16	1.44	Info Tech
Total	23,643.52	36.66	

Source: MSCI

The FTSE/JSE ALSI could also be argued to be concentrated with 35.9% in Resources (of which 27.0% in Gold and Platinum) and a further 8.6% in Naspers and Prosus.

Where to next for AI?

We do not doubt there still remains significant expected earnings growth for AI stocks (with the usual caveat for debt-funded spending by hyperscalers), however valuation and growth are two related but different ideas, and AI valuations were high by historical standards prior to July's declines.

In general we frequently hear the suggestion that the US market is richly valued and therefore ripe for a correction. We therefore discuss AI in the context of what might be prospects for the broader market next.

Is the US market expensive and is it about to fall?

On a current valuation basis following the correction in July we actually do not think so.

An often cited claim is that the Shiller Cyclically-Adjusted PE is high therefore the US market should expected to decline. We present the Shiller CAPE for the S&P 500 in Chart 1 below.

Per Chart 1 the Shiller CAPE is indeed near all time highs. There are two points of concern however in interpreting this

1. the ratio is historic i.e. backward-looking, in an environment of sharp AI-related growth, therefore a backward-looking indicator is not necessarily indicative of overvaluation

2. a broader argument is that the CAPE averages inflation-adjusted EPS over 10 years – while this is intended to adjust for cyclicality, in an environment of real earnings growth there is a case to suggest the CAPE overstates the valuation

Still, the CAPE remains high relative to its history.

Chart 1. Shiller Cape ratio



Source: multpl.com

Next we present in Chart 2 below the forward PE i.e. based on 1-year forward EPS estimates for the Nasdaq.

Chart 2. Nasdaq 12-month forward PE



Source: Factset

We regard Chart 2 above as an important chart because of the information it conveys

1. the current 12-month forward PE has declined and is in line with market valuation levels of 2017-2019 i.e. prior to the Covid period
2. there was clear overvaluation in the 2020-2021 period through the Covid stimulus which corrected in 2022 as interest rates rose

3. by historical standards the current forward is relatively high but not at an extreme, and certainly not at all close to valuation levels seen in the early 2000s
4. as an aside we also note that if one had entered the market at the dotcom peak in early 2000, it took 16 years to recover one's capital losses

The forward PE remains estimate-based and is therefore subject to economic developments. If the economic and therefore EPS growth outlook deteriorates, the estimate will prove overly-optimistic and will be adjusted downward. The market would be expected to respond even before estimates are adjusted.

What about Treasury yields?

The financial media has also been preoccupied in recent days with the rise in US Treasury yields and the US Treasury Secretary's attempts to manage these down.

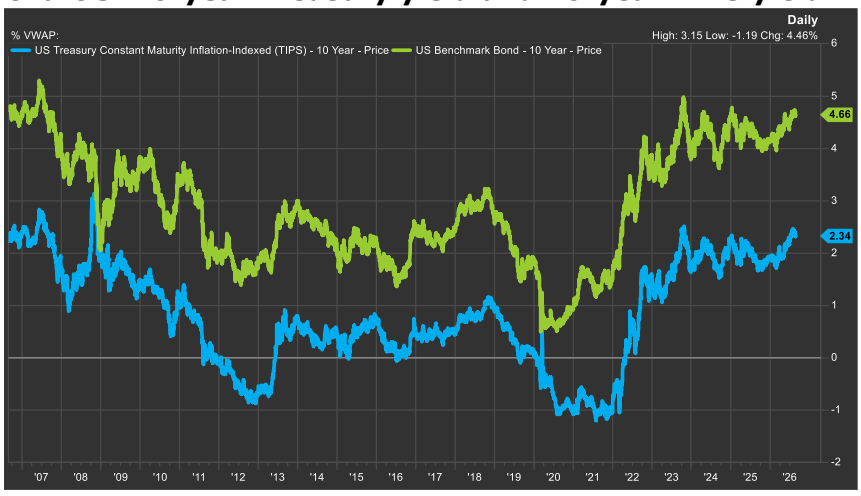
We offer several thoughts on this

1. the US Treasury's announcement represents signalling more than substance – a maximum of USD 4 billion per operation is unlikely to have impact in a Treasury market with USD 31.5 trillion of outstanding securities and USD1.2 trillion in daily trade – we think the market correctly reverted to prior levels after initially responding to the announcement

2. the episode reminds us that a central economic objective of the Clinton administration was to bring down long term Treasury yields - the goal at the time was to encourage investment, economic growth and employment. James Carville, a Clinton adviser, famously stated in 1993 in connection with this that *"I used to think that if there was reincarnation, I wanted to come back as the President or the Pope or as a .400 baseball hitter. But now I would want to come back as the bond market. You can intimidate everybody."*

3. we compare the 10-year nominal Treasury yield and the 10-year Treasury Inflation-Protected Securities ("TIPS") i.e. real yield in Chart 3 below.

Chart 3. 10-year Treasury yield and 10-year TIPS yield



Source: Factset

Per Chart 3 above, the 10-year yield has indeed risen in 2026 but remains range-bound at the upper end of its trading range from 2023.

We note that it is the real yield which is driving the nominal yield upward. Therefore, aside from being range-bound, the rising nominal yield does not reflect rising inflation expectations (breakeven inflation remains stable at +2.2%) nor rising default risk.

We have suggested in previous commentaries that the strongest determinant of real yields tends to be monetary policy. In this sense a rising real yield could rather reflect rising short rate expectations and/or stronger economic growth. Indeed it appears to be the case, considering the 2-year Treasury yield, that the market would like to see a rate hike from the Fed.