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Stocks outside the mainstream

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Abstract

Experience shows that a boom in a limited number of shares tends to overshadow positive business developments in other companies and in other sectors. Is this currently the case?

Zusammenfassung

Erfahrungsgemäß überstrahlt ein Boom bei einer überschaubaren Anzahl an Aktien positive Geschäftsentwicklungen bei anderen Unternehmen und Sektoren. Ist das auch aktuell der Fall?



A schematic analysis of S&P 500 companies based on current and near-future valuation metrics shows that sectors outside the mainstream sometimes exhibit moderate valuations. Within each sector, there are companies that might be worth a second look.

Experience shows that a boom in a limited number of shares tends to overshadow positive business developments at other companies and in other sectors (Pástor, Veronesi 2009). However, neglected shares may have positive future return effects on a portfolio (Arbel, Carvell, Strebel 1983). Whether this might also be the case at present will be examined below.

The analysis covers the eleven sectors into which the S&P 500 is divided.¹ How have profits and cash inflows developed here over the past ten years, and what is the current and future valuation in light of the earnings analysts expect for the next four quarters? The aim is to provide an overview of the sectors' attractiveness, as well as a breakdown of individual shares that, on closer inspection, might warrant more in-depth analysis. Should the semiconductor boom come to an end, there could be rotation into other sectors less dependent on it. Positioning oneself early on can do no harm.

High concentration in the S&P 500

The analysis yields a clear result: [45 per cent of the market capitalization in the S&P 500 is directly linked to the artificial intelligence boom. Semiconductor shares account for a record 18 per cent of the S&P 500, the world's most important share index.](#) In terms of value growth, they have recently overtaken the previous boom of the 'Magnificent Seven' ('Mag7': Apple, Nvidia, Alphabet, Meta, Amazon, Tesla and Microsoft). By the final week of June 2026, semiconductor shares had roughly doubled in value compared with the start of the year, whilst the Magnificent 7 were down slightly – even though Nvidia, the original leader of the chip rally, is one of them. Nevertheless, the Mag7 currently account for just under a third of the total weight of the S&P 500.

Such a high concentration – where a few shares from a limited universe account for the bulk of a broad index – is not unusual. In March 2000, [no fewer than five telecoms' stocks featured among the top ten global shares.](#) This is not a problem for an index as long as this dominance does not lead to valuations rising far beyond the usual level. However, this could currently be the case. [According to calculations by Landesbank Baden-Württemberg,](#) corporate profits in the S&P 500 have risen only half as much as the index since the start of the current bull market.

¹ Communication Services, Consumer Discretionary, Consumer Staples, Energy, Financials, Health Care, Industrials, Information Technology, Materials, Real Estate, Utilities



The rush for semiconductor stocks is not limited to the US stock market. In June 2026, SK Hynix overtook Samsung Electronics as the most valuable listed South Korean company. At the end of June, the two companies dominated the Seoul Stock Exchange's benchmark KOSPI index, accounting for more than half of its total value.

Historically high valuations

The prolonged rise of the Mag7 and the boom in chip shares – which, as measured by the US semiconductor index SOX, have more than quadrupled in price since a temporary low in spring 2025 – are having an impact on the overall market valuation. The so-called Buffett indicator, which shows the market capitalization of the US stock market relative to US gross domestic product, is signaling a record high (Figure 1).

Figure 1: Market capitalization of the US stock market relative to US gross domestic product



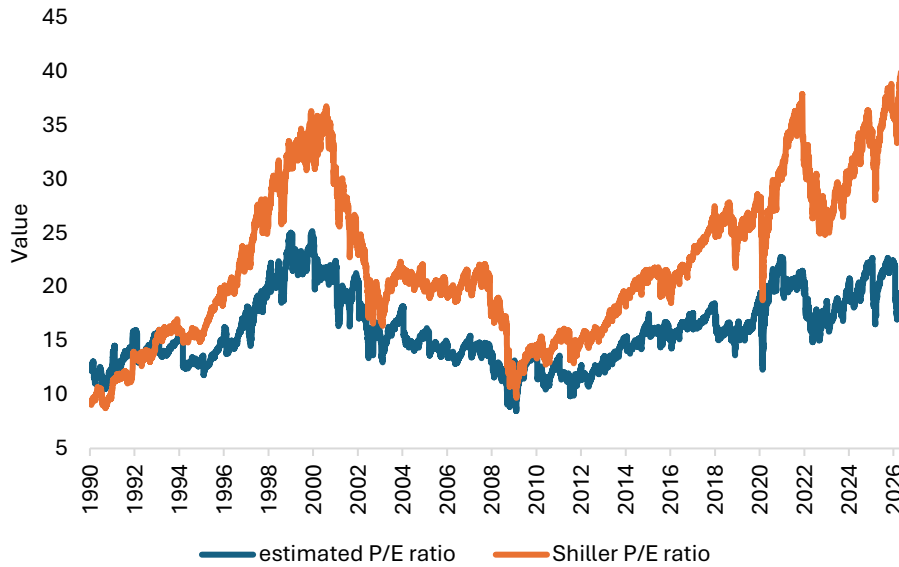
'Buffett Indicator', Source: Bloomberg, Flossbach von Storch Research Institute. As at June 2026. **Past performance is not a reliable indicator of future results.**

However, this record level does not in itself carry any particular significance. What matters are valuation metrics such as the price-to-earnings ratio (P/E ratio). Measured against long-term, price-adjusted corporate earnings relative to share prices (the 'Shiller P/E'²), valuations on the US stock market are also at a record high. By contrast, the expected P/E ratio for 2027, based on analysts' profit forecasts, is at a comparatively moderate, albeit not low, level (Figure 2).

² The Shiller P/E ratio (also known as the 'Shiller PE ratio' or 'Cyclically Adjusted Price-to-Earnings (CAPE) ratio') evaluates a share or an index by comparing the current share price to the average, inflation-adjusted corporate earnings over the past ten years



Figure 2: Price-adjusted, long-term price-to-earnings ratio and expected price-to-earnings ratio in the S&P 500

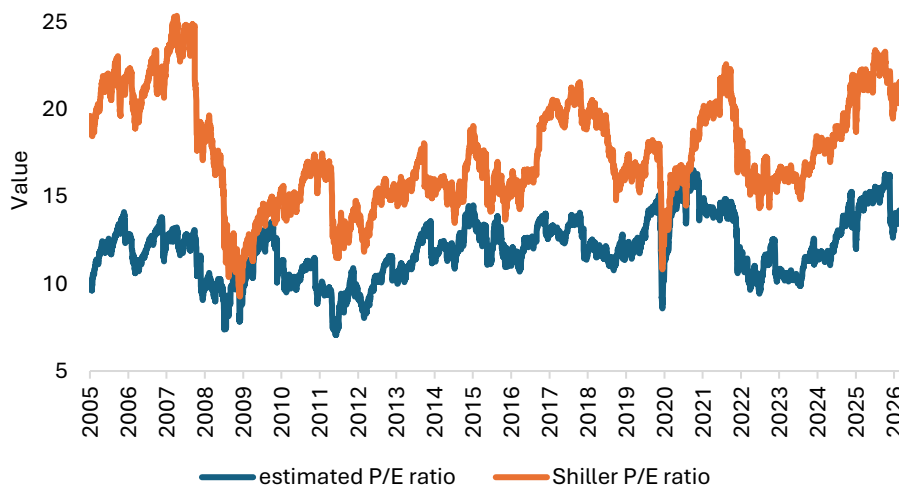


Estimated P/E ratio = next year, Shiller P/E ratio = long-term price-to-earnings ratio, Source: Bloomberg, Flossbach von Storch Research Institute, as at June 2026. **Past performance is not a reliable indicator of future results.**

The Shiller P/E ratio is usually higher than expected earnings, as it is inflation-adjusted and future earnings tend to be higher than past earnings, which pushes down the estimated P/E ratio. Furthermore, Wall Street forecasts are traditionally optimistic.

Compared with US shares, the German share index (DAX) is more cheaply valued in terms of both the Shiller P/E ratio and the estimated P/E ratio (Figure 3).

Figure 3: Price-adjusted, long-term price-to-earnings ratio and expected price-to-earnings ratio in the DAX



Estimated P/E ratio = next year, Shiller P/E ratio = long-term price-to-earnings ratio, Source: Bloomberg, Flossbach von Storch Research Institute, as at June 2026. **Past performance is not a reliable indicator of future results.**



Where price and value still align

Amid the artificial intelligence (AI) boom, the gap between US shares and German blue chips has widened, as Wall Street analysts expect significantly higher profits than in the past, particularly for the heavyweights in the technology sector.³ The tailwind for German companies is considerably weaker, as the potential beneficiaries of AI represented on the DAX carry too little weight overall, or the advantages are not apparent. This disadvantage would then become an advantage if AI were to lead to – or has already led to – a massive overvaluation.

The extent to which an AI bubble has formed that will burst sooner or later is a much-debated question. The estimated P/E ratio in the S&P 500 is well below the levels seen during the telecoms, media and internet stock bubble at the turn of the millennium (the dot-com bubble). And the record-high Shiller P/E ratio will fall should analysts' profit forecasts prove accurate. A risk arises if companies fail to meet expectations and/or investments are cut back. The fall would then be steep – at least that is what the experience of share price crashes in the last and this century suggests (Greenwood, Shleifer, You 2019). Following the bursting of the dot-com bubble (Ofek, Richardson 2001), the financial crisis and the Covid crash, the Shiller P/E ratio plummeted in tandem with falling share prices. Smaller episodes of price setbacks of around one-fifth in recent years confirm this clear pattern (see Figures 2 and 3).

It should also be noted that, within the technology sector, it is primarily producers of AI hardware that generate exorbitant cash inflows from their operations. For buyers – for example, those in the software sector – these represent capital expenditure (CAPEX)⁴, which reduces free cash flows or even exceeds them: in such cases, debt is required for financing. In aggregate, cash flow (or cash flow plus cash from additional borrowing) shifts from software to hardware companies; at the cash level, this remains a zero-sum game until the buyers of AI hardware generate additional revenue from their customers beyond their existing business. In addition to looking at profits, investors should therefore pay close attention to the development of free cash flow (FCF).

³ Bloomberg data currently indicates that year-on-year earnings growth of 24.8 per cent/16.8 per cent is expected for the S&P 500 in 2026/2027, and 12.4 per cent/15.1 per cent for the DAX (GAAP in each case, retrieved on 7 July 2026)

⁴ CAPEX (Capital Expenditure) refers to a company's investment expenditure on long-term fixed assets. Such expenditure – for example, on IT or machinery – does not usually have an immediate impact on profit (i.e. it reduces profit). Companies capitalise CAPEX on their balance sheet and depreciate it on a straight-line basis over its useful life. Depreciation charges then reduce profit; however, they are added back in the same amount in the cash flow statement, meaning that, on balance, they are cash-neutral over the depreciation period



Differing trends across sectors

This is also reflected across the various sectors. For instance, profit growth in the ‘Communication Services’ sector has been very positive for years. On average, net earnings have roughly quadrupled over the ten-year period from 31 March 2016 to 31 March 2026⁵. Recently, however, free cash flows have been declining – a trend that is likely to continue, according to analysts’ estimates. The sector includes, amongst others, Alphabet and Meta – two of the hyperscalers that each aim to invest hundreds of billions of dollars in AI – per company, per year, up to 2030.⁶ Even the sector’s current valuation is high, measured by the current price-to-free-cash-flow ratio and the P/E ratio as at 31 March 2027. Six of the 20 companies in the sector are worth further analysis due to valuation metrics that appear sound at first glance. It could be worthwhile to take a closer look here. Earnings growth, cash flows and share valuations collectively paint a positive picture for these companies (Table).⁷

Table: Assessment of individual sectors

<i>S&P 500 Sector</i>	Earnings growth	Free Cashflow trend	P/E ratio four quarters ahead
<i>Communication Services</i>	very positive	still positive (declining)	25.0
<i>Consumer Discretionary</i>	very positive	highly volatile	22.3
<i>Consumer Staples</i>	positive and stable	positive and stable	18.5
<i>Energy</i>	highly volatile	highly volatile	18.6
<i>Financials</i>	Trending positively, but volatile	N/A	14.3
<i>Healthcare</i>	Trending upwards, subject to fluctuations	Trending upwards with fluctuations	17.8
<i>Industrials</i>	positive, consistently high for the past four years	positive, consistently high for the past four years	25.1
<i>Information Technology</i>	rising sharply	rising sharply	26.0
<i>Materials</i>	highly volatile	highly volatile	28.4
<i>Property</i>	fluctuating, slightly positive	continuously rising*	N/A
<i>Utilities</i>	positive	weak, negative FCFs	18.7
	Current P/E ratio	Assessment: Profit/FCF valuation	Selection (number)
<i>Communication Services</i>	28.0	High valuation	6 out of 20
<i>Consumer Discretionary</i>	27.4	High valuation	9 out of 48
<i>Consumer Staples</i>	21.5	moderate valuation	9 out of 36
<i>Energy</i>	25.0	High rating	3 out of 21
<i>Financials</i>	N/A	Moderate valuation	18 out of 76
<i>Healthcare</i>	24.4	Moderate rating	14 out of 59
<i>Industrials</i>	28.8	High rating	17 out of 81
<i>Information Technology</i>	41.3	Very high rating	25 out of 72
<i>Materials</i>	32.2	Very high rating	3 out of 26
<i>Property</i>	N/A	N/A	7 out of 31
<i>Utilities</i>	302.3**	Unattractive valuation	1 out of 32

Selection = companies worth further analysis, current P/FCF = price-to-free-cash-flow ratio, *Funds from Operations (FFO), **Basis: 20 out of 26 companies, data equally weighted per company, not weighted by market capitalization or sector index, adjusted for outliers, Source: Bloomberg, Flossbach von Storch Research Institute, as at June 2026. **This does not constitute an investment recommendation.**

⁵ 31 March is the most common quarterly reporting date for S&P 500 companies; however, other reporting dates, such as 28 February, are also included and recorded accordingly

⁶ The companies named in this paper are provided as examples for illustrative purposes only. None of them constitutes an investment recommendation

⁷ The approach is schematic and quantitative. Consequently, lucrative business models may be overlooked



A total of 112 companies from the S&P 500 have made it onto the shortlist of companies recommended for further analysis. Most of these, both in absolute and relative terms, come from the IT sector: as many as 25 out of 72 could prove to be shares trading at interesting price levels. The sector includes, amongst others, both software companies that have recently been under pressure and high-flying semiconductor firms. However, the sector's overall valuation is very high, meaning that caution and due diligence are warranted from a fundamental perspective. Only three sectors are currently considered to be moderately valued: Health Care, Consumer Staples and Financials. The financial sector has long encompassed not only banks, but also data providers such as FactSet, rating agencies such as S&P Global, the credit card group Visa and the holding company Berkshire Hathaway. The healthcare sector includes the traditional pharmaceutical and biotech industries (Pfizer, Amgen) as well as, amongst others, medical technology firms such as Medtronic. In healthcare, it may be that generally decent to good business performance has not been sufficiently reflected in share prices recently. At least, that is what the valuation metrics suggest. 14 out of 59 companies in the sector are recommended for individual analysis.

The Consumer Staples sector includes, amongst others, consumer staples such as Coca-Cola and Procter & Gamble. Here, the long-term data and current key figures primarily indicate predictable stability rather than high-flying earnings prospects. One of the four of the 36 companies listed here warrants further analysis at first glance.

The second consumer sector, Consumer Discretionary, is a diverse mix of companies. It includes Amazon, car manufacturers Ford and General Motors, and Domino's Pizza; valuations are considered high; whilst profit trends are positive overall, free cash flows at sector level are volatile.

The utilities sector is characterized by negative free cash flows and is therefore rather unattractive. 'Materials' are considered to be very highly valued at sector level. In the energy sector, high valuations could be a deterrent; at first glance, only 3 out of 26 companies appear to be potentially attractive.

In the financial sector, by contrast, 18 of the 72 companies listed there warrant further analysis. Specialist knowledge and analysis are particularly necessary in this sector, especially for banks, and likewise for property shares (Real Estate). Seven out of 31 companies listed there show a positive trend in 'Funds from Operations' (FFO). FFO is a key metric for assessing the cash flow and operational performance of property companies.⁸

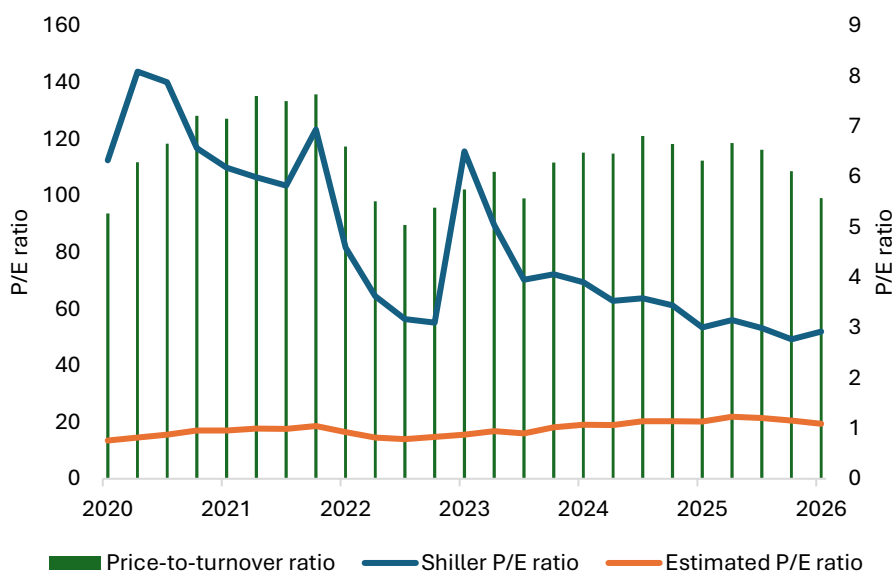
⁸ FFO adjusts net profit by adding back depreciation and amortisation whilst deducting gains from property sales and interest income, in order to reflect the actual operating result



Based on the free cash flow generated over the past twelve financial months, the 112 companies selected show an average return on market capitalization of 4.6 per cent⁹ at the time of the survey. This is 0.4 percentage points higher than the S&P 500 shares, which did not meet the selection criteria.

The Shiller P/E ratio of the selection is higher than that of the S&P 500 as a whole, but within the selection group it is close to its lowest level in six years. The estimated P/E ratio is one-tenth higher than the average over the past six years and slightly higher than the estimated P/E ratio for the S&P 500 as a whole. The price-to-sales ratio, another valuation metric – albeit not of paramount importance – averages 5.6 (past six years: 6.4/Figure 4).

Figure 4: Price-to-sales ratio, Shiller P/E ratio and estimated P/E ratio of the 112 selected S&P 500 companies



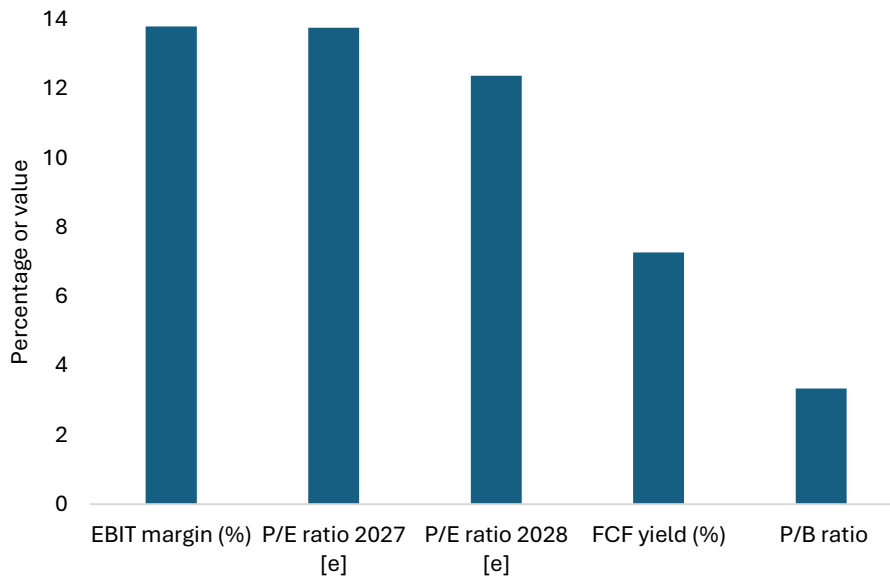
adjusted for outliers; some financial stocks, such as banks and property shares, were excluded from this calculation; source: Bloomberg, Flossbach von Storch Research Institute, as at June 2026.

The group of 112 candidates can be further narrowed down quantitatively prior to a more in-depth analysis. For example: provided that earnings before interest and taxes (Earnings before interest and taxes, EBIT) must have been at least twelve per cent, the estimated price-to-earnings ratios for 2027 and 2028 should not exceed 18, and the free cash flow yield (FCF yield) must have most recently reached at least four per cent, this results in a basket of 23 shares. These stocks exhibit relatively low price-to-sales ratios, with a median of 3.3 (Figure 5).

⁹ Some financial stocks, such as banks and property shares, were not taken into account



Figure 5: EBIT margin, estimated P/E ratios, FCF yield and P/S ratios for 23 of the 112 S&P 500 companies from the shortlist



median in each case, [e] = expected (estimated), Source: Bloomberg, Flossbach von Storch Research Institute, as at June 2026.

It is worth noting that the selection of 23 out of 112 shares also includes companies whose valuations are significantly depressed due to AI-related concerns. AI is still a relatively new factor that should be taken into account from a risk-reward perspective during in-depth analysis. Experience suggests that there is likely to be too much euphoria surrounding the (potential) AI winners, whilst a whole host of supposed AI losers may be trading at excessively low levels.

Conclusion

A schematic analysis of S&P 500 companies based on current and near-future valuation metrics shows that sectors outside the mainstream sometimes exhibit moderate valuations. Within each sector, there are companies that might be worth a second look. The approach chosen here cannot capture companies whose potential business success lies far in the future. In any case, the question arises as to what extent it is realistic to estimate revenue and earnings that lie so far in the future. A shorter-term perspective certainly offers greater certainty. The approach has not taken into account the additional need for a balance sheet analysis of the respective companies. For example, the structure of financing on the liabilities side (equity/debt) and the risks or opportunities that assets may entail require individual analysis. [For instance, a high proportion of acquisition premiums \('goodwill'\) relative to equity always increases the risk profile of a long-term equity investment](#) (Schürmann 2022). The risk premium at which future earnings should be discounted also varies from company to company. It is quite possible that companies from sectors currently valued at moderate levels may then offer better prospects than those in the IT sector. However, the opposite may also be true.



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