Active equity allocation report

Q1 2026

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Key takeaways

- Our quarterly analysis reflects an increase in negative indicators for active equity performance in most global markets at the start of 2026, reversing a strong trend for these indicators for the second half of 2025.
- Monthly return dispersion, which measures how much individual stock returns differ from each other, declined from the previous quarter, pointing to potentially fewer opportunities for managers to choose stocks that can outperform the market.
- However, stock-level return correlation remained below the historical average for the major equity indices we track, suggesting opportunities for active selection, especially within the Russell Top 200 and S&P 500.
- Also, the MSCI EAFE Index generated positive active management signals vs. history for three of the four major signal categories.

The big picture for Q1

At the start of 2026, the number of negative indicators for active management increased vs. the previous quarter, reflecting narrower market leadership, complacency amid low equity market volatility (as measured by the VIX), and continued concentration among the top 10 holdings for most major large cap indices. However, several indicators pointed to specific opportunities for active managers.

Exhibit 1: Active Equity Monitor

	Russell Top 200	Russell Mid Cap	Russell 2000	S&P 500	MSCI EAFE	MSCI EM
Monthly return dispersion	**6.1%**	**7.8%**	**10.7%**	**6.7%**	**6.0%**	**8.4%**
Historical average	7.4%	9.2%	12.1%	8.0%	8.1%	10.5%
Trend vs. historical average	-1.2%	-1.5%	-1.4%	-1.2%	-2.1%	-2.0%
Trend vs. 3 months ago	-2.8%	-0.8%	-1.8%	-1.5%	-1.2%	-0.3%
Stock-level return correlation*	**0.15**	**0.20**	**0.19**	**0.18**	**0.15**	**0.11**
Historical average	0.30	0.25	0.21	0.28	0.19	0.14
Trend vs. historical average	-0.14	-0.06	-0.02	-0.10	-0.04	-0.03
Trend vs. 3 months ago	+0.04	+0.01	-0.03	+0.03	-0.01	+0.03
Volatility from stock-specific risk**	**51.3%**	**58.3%**	**64.8%**	**53.7%**	**64.0%**	**64.6%**
Historical average	46.8%	56.4%	67.1%	51.7%	56.1%	61.3%
Trend vs. historical average	+4.5%	+1.9%	-2.3%	+2.0%	+7.9%	+3.3%
Trend vs. 3 months ago	-7.6%	-5.3%	-2.8%	-9.0%	-2.4%	-7.9%
Weight in top 10 holdings	**46.9%**	**5.7%**	**5.1%**	**40.7%**	**13.1%**	**31.5%**
Historical average	27.3%	5.0%	3.0%	22.3%	13.9%	21.9%
Trend vs. historical average	+19.6%	+0.7%	+2.1%	+18.4%	-0.8%	+9.6%
Trend vs. 3 months ago	+0.4%	-0.3%	+0.1%	+0.3%	+0.6%	+0.9%
Number of positive indicators	**2**	**3**	**2**	**2**	**4**	**2**
Number of negative indicators	**6**	**5**	**6**	**6**	**4**	**6**

* Analysis using trailing 60 days of daily returns.
** Percent of total variance not attributable to the top 5 factors in a principal component analysis. Source: Bloomberg Finance LP, FactSet, and Fidelity Investments Equity Quantitative Research, as of 12/31/25.

The most significant big-picture change versus 2025 occurred in the monthly return dispersions. Return dispersion measures how much individual stock returns differ from each other. Dispersions declined broadly across major indices in the final quarter of 2025, suggesting fewer opportunities to identify mispriced stocks compared with the previous quarter.

Exhibit 2 (left) reflects the quarter-over-quarter decline in return dispersion for the major indices.

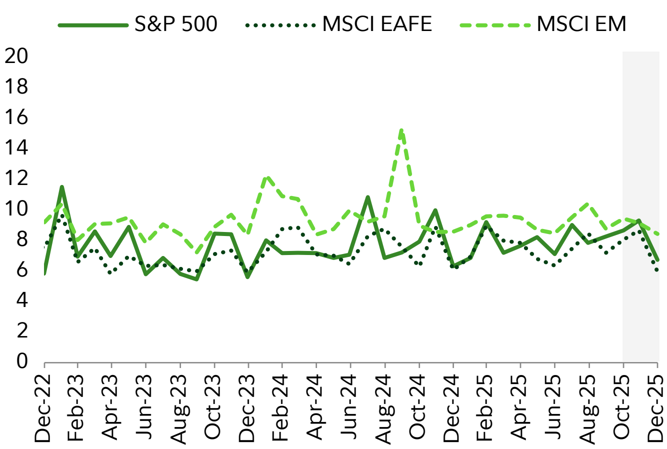
The chart at right shows the widespread nature of the dispersion decline for U.S. stocks across all capitalization ranges (large, mid, and small).

Trends to watch in future quarters include 1) whether the decline in dispersion continues to be broadly based, 2) if U.S. large cap stocks begin to lead a declining dispersion trend over consecutive quarters, and 3) whether dispersion for any of the indexes climbs back toward their respective historical averages.

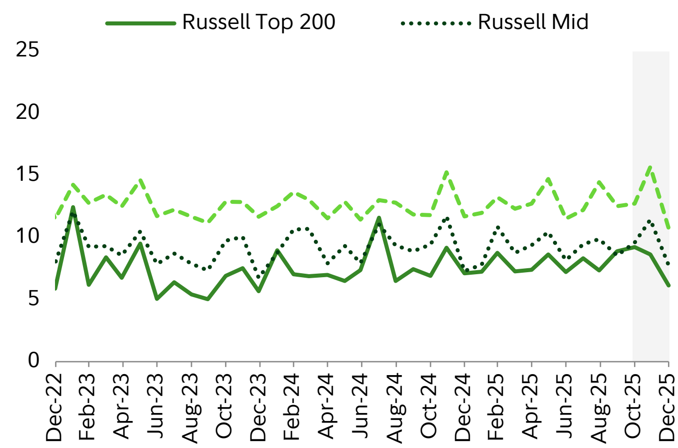
If there's good news regarding return dispersions, they remain higher than the average 15-year trend. Even though dispersions have declined recently, there may be more alpha-seeking opportunities vs. the low-rate environment following the Global Financial Crisis (the Russell Top 200's dispersion reached about 4% in mid-2011 and again in March of 2017, compared with 6.1% at the end of 2025).

Exhibit 2: Global correlations and stock-specific risk percentage

Global monthly return dispersion (%), major U.S. and international indexes



U.S. domestic monthly return dispersion % by market capitalization



Shaded areas (both left and right) highlight the quarter-over-quarter return dispersion decline. Source: Bloomberg Finance, LP, Factset, and Fidelity Investments Equity Quantitative Research, as of 12/31/25.

Where active equity selection may be working better

While the return dispersion bears watching, stock-level correlation remained below the historical average for all six major equity markets we track. This reflects that individual stocks continue to move more independently to one another versus the long-term trend. This may help create opportunities for skilled managers to generate alpha.

While the stock-level correlation increased versus the previous quarter for both the Russell Top 200 (50th percentile vs. history) and S&P 500 (64th percentile vs. history), each remained meaningfully below the long-term trend. This appears to point to continued opportunities for U.S. large caps.

Looking ahead, possible performance drivers for these stocks could include:

- Any marginal improvement for consumer sentiment, which at the start of 2026 remained at less than two-thirds its all-time average since 1978. It remained near the same levels reached in 1979 (amid 11% inflation) and late 2008 (the global financial crisis).
- Strong earnings surprises in select cyclical sectors, including industrials, which could be supported by defense and infrastructure spending.
- Better-than-expected economic data as it relates to jobs (mixed signals, but with some signs of potential stabilization) and the health of U.S. manufacturing (ISM has been in contraction for most of the past three years, making any move toward expansion a potential catalyst).
- Potential artificial intelligence-related earnings surprises driven by infrastructure build-outs.

Also on the radar

Among all major indexes, the MSCI EAFE saw the greatest number of positive quarterly signals, and healthy historical trends for three of the four major signal categories we track (all but monthly return dispersion). The volatility explained by stock-specific risk within the MSCI EAFE declined from the previous quarter, although it remains well above its historical average.

Also, the MSCI EAFE is the only equity index of the six majors in which the weight of its top 10 holdings remained below the historical average. This may point to a more balanced structure for active managers, and opportunities for alpha generated by a wider range of securities. In comparison, EM's top 10 concentration is higher, and it continued to increase above the historic average.

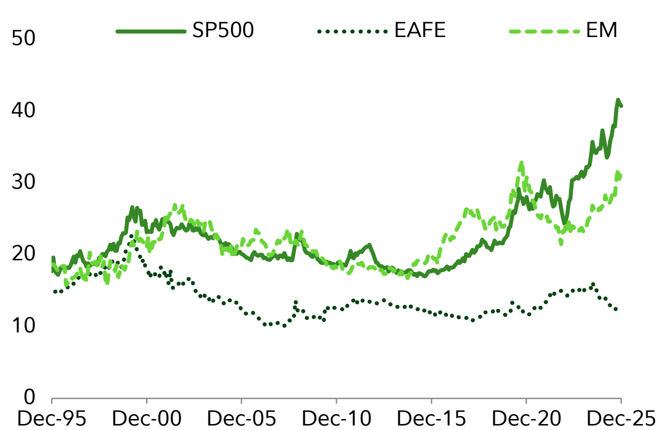
What about U.S. market concentration?

Top 10 holdings now account for 40.7% and 46.9% of the S&P 500 index and Russell Top 200, respectively, each well above their historical averages. In particular, the concentration of the S&P 500 continues to make it difficult for active managers to outperform.

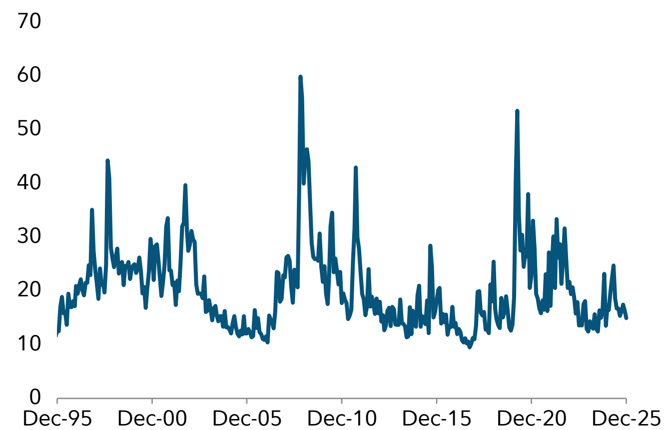
The declining volatility trend since April 2025 hasn't helped either. It is approaching the 2023/2024 lows.

Exhibit 3: Higher top 10 concentration, lower volatility in the S&P 500

Global concentration: Weight in top 10 holdings (%)



Absolute market volatility (VIX price)



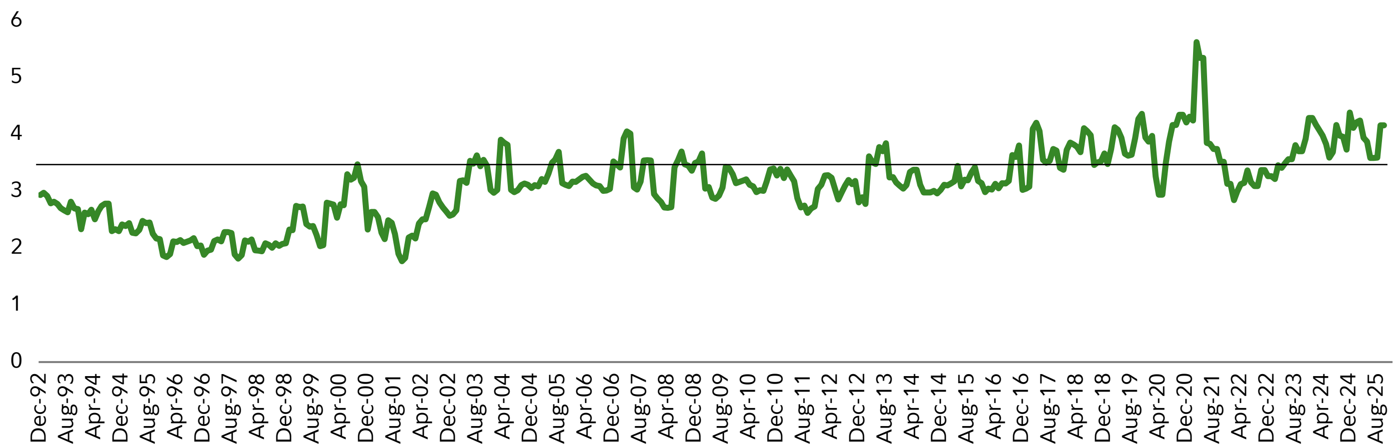
Correlation analysis above uses trailing 60 days of daily returns. Absolute market volatility reflects the historical price of the CBOE Volatility Index (VIX). Source: Bloomberg Finance LP, and Fidelity Investments Equity Quantitative Research, as of 12/31/25.

If there's any benefit of rising U.S. concentration, it's that it may create opportunities for stock selection based specifically on upside earnings surprises. Exhibit 4 shows the quarterly standardized unexpected earnings (SUE)—in other words, earnings surprises—for the top 200 stocks in the Russell Index. Higher readings on the chart show a larger gap between stocks that surprised the most versus those that surprised the least. The amount of surprise variance has risen since early 2022 and remains above its median going back to the early 1990s.

The caveat to the widening gap between stocks that surprise the most versus the least is that, historically, more expensive markets (like the one at present) have tended to punish earnings misses more than in periods of historically average valuations. Therefore, there's a potentially larger penalty for getting it wrong.

Exhibit 4: Russell Top 200

Quarterly SUE: High minus low spread (Z score)



The green line shows the spread of standardized unexpected earnings (SUE) for the top 200 stocks in the Russell Top 200 Index, calculated quarterly. The black line marks the average spread since December 1992 (3.12). Russell Top 200 is a large cap index that contains the 200 largest companies in the broader Russell 1000 index. The SUE differential is the delta between the standard deviation adjusted earnings surprises of the 90th and 10th percentiles (weighted 25%) and the 75th and 25th percentiles (weighted 75%). Source: Haver Analytics and Fidelity Investments, as of 10/31/25.

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Anna is head of equity quantitative research for Equity Quantitative Research within the Quantitative Research Investments (QRI) division at Fidelity Investments. She is responsible for a team of quantitative analysts who build quantitative stock selection models, perform risk analysis on portfolios, and assist portfolio managers with portfolio construction. Prior to her current role, she was an analyst on the team for 13 years.

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Claire builds quantitative stock selection models, performs risk analysis on portfolios, and assists portfolio managers with portfolio construction.

Definitions

Monthly return dispersion gauges the variability of individual stock returns relative to each index. High dispersion suggests divergent performance and wide market breadth. The monthly return dispersion reflects the standard deviation of 1-month trailing returns, in percentage points.

Stock-level return correlation measures how closely two stocks move together. Low correlation indicates stocks move more independently of each other. Correlation analysis above uses trailing 60 days of daily returns.

Volatility from stock-specific risk measures the percent of returns attributed to idiosyncratic stock events, rather than market-driven factors ("beta"). High stock-specific risk volatility usually points to high dispersion. It is represented by percent of total variance not attributable to the top 5 factors in a principal component analysis (PCA).

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Russell Top 200 Index is a market capitalization-weighted index designed to measure the performance of the largest cap segment of the U.S. equity market.

Russell Midcap Index is a market capitalization-weighted index designed to measure the performance of the mid cap segment of the U.S. equity market. It contains approximately 800 of the smallest securities in the Russell 1000 Index.

Russell 2000 Index is a market capitalization-weighted index designed to measure the performance of the small cap segment of the U.S. equity market. It includes approximately 2,000 of the smallest securities in the Russell 3000 Index.

S&P 500 index is a market capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation to represent U.S. equity performance.

MSCI EAFE Index is a market capitalization-weighted index that is designed to measure the investable equity market performance for global investors of developed markets, excluding the U.S. and Canada

MSCI Emerging Markets Index (MSCI EM) is a market capitalization-weighted index that is designed to measure the investable equity market performance for global investors in emerging markets.

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