Cabot
INCOME ADVISOR

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## Look Beyond AI in 2026

The market has been spectacular. Can we expect more of the same in 2026?

Predicting the future is a dicey business to say the least. No one saw the pandemic coming. Virtually no one predicted the highest inflation in more the 40 years. And precious few anticipated a resounding Trump victory in the presidential election. Nevertheless, a calendar year is a measurable bookmark in time. It's a good opportunity to step back and assess where we have been and where we might be going, like an annual market physical.

The "where we've been" part is easy. Things have been great in the market. The S&P 500 has returned over 17% in 2025 with just over a week left in the year after two straight years of 20%-plus returns in 2023 and 2024. That's the best three-year run since the go-go 1990s.

The S&P is up a staggering 95% since this bull market began in October of 2022. It's up 128% this decade, for an average annual return of about 15%, 50% higher than the historical average.

The high returns are particularly impressive considering this decade has included a global pandemic, the highest inflation in 40 years, and the highest interest rates in 20 years. If the "experts" saw those things coming, they likely would have predicted a lousy market. But returns have been stellar for one dominant reason: technology.

The artificial intelligence catalyst is driving earnings growth through the roof in the market's largest sector. The technology is real, and it provides a once-in-a-generation catalyst. Without technology, market returns for the past few years would have been rather uninspired.

But the market has gotten pricey. According to the Wall Street Journal, the current S&P 500 price/earnings ratio is 25.63. That's well above historical averages, and such lofty valuations have rarely been sustained in the past.

Of course, technology has never been such a huge part of the index. The "Magnificent 7" stocks account for more than 35% of the index. Those stocks currently trade at an average PE ratio of 31 times. **Nvidia (NVDA)** accounts for about 8% of the index all by itself. For perspective, the entire energy sector accounts for less than 3% of the index.

If you take out the overrepresentation of technology, valuations aren't that high. An equally weighted S&P 500 has a current PE ratio of just 17 times. The huge technology weighting is what makes current valuations high by historical standards, and those high technology valuations are justified by higher earnings growth.

Will the AI boom continue in 2026? There is growing investor angst regarding the sustainability of technology valuations and whether all this massive AI investment will deliver tangible payoffs. Technology stock prices could continue to fall and drag the indexes lower. I believe the AI catalyst is real and still in the early stages. But technology could still have a tougher year in 2026.

Fortunately, there are a lot of stocks that aren't technology. The rest of the market cares more about interest rates and the economy, and those things are shaping up well. The Fed is in a rate-cutting cycle, inflation is subdued, oil is cheap, and a higher level of economic growth is expected in 2026.

The rally is broadening, and 2026 may be a year for non-technology stocks to shine. Overall earnings are expected to grow 14% next year, with much of the growth over last year coming from other sectors. Many stocks in other industries sell at cheaper valuations than the market, and performance is improving as investors seek to diversify beyond technology.

Regardless of what happens with technology stocks in 2026, several other sectors could have a great year, maybe the best year of this decade so far. Notable sectors that are well positioned ahead of the new year include health care, energy, financials, and utilities.

The bull market has been lopsided toward technology so far. But 2026 is shaping up to be a year for other stocks to catch up.

## Recent Activity

November 25
**Eli Lilly and Company (LLY) – Rating change “BUY” to “HOLD”**
**Fidelity National Financial, Inc. (FNF) – Rating change “BUY” to “HOLD”**

November 26
**SOLD LLY January 16th $1060 call at $83.00 or better**

December 18
**Sold ALLY February 20th $45 call at $2.65 or better**

December 23
**Buy Expand Energy Corporation (EXE)**

## What to Do Now

Several high-performing technology stocks in the portfolio were called away last year, including **Broadcom (AVGO)**, **Constellation Energy (CEG)**, and **Oracle (ORCL)**. Other strong-performing stocks were also called, including **AbbVie (ABBV)** and **Cheniere Energy (LNG)**. That all provided great total returns but left the portfolio with several underperforming stocks in other industries.

The year ahead should be better for those stocks. A stronger economy would be great for **Ally Financial (ALLY)**, **Fidelity National Financial (FNF)**, and **Toll Brothers (TOL)**. A better economy would help with affordability issues for purchases of homes and autos.

Earnings estimates for 2026 have been rising in financials and utilities. Utilities should benefit as demand for electricity adds more growth to the defensive characteristics of utilities. Both **NextEra Energy (NEE)** and **American Electric Power (AEP)** are well positioned as AI metastasizes beyond technology stocks.

Natural gas stocks are also well positioned for the new year and worth considering. This country and the world are expected to continue to rely overwhelmingly on fossil fuels for decades to come. But fossil fuel consumption is changing. A new king is emerging: natural gas.

Natural gas is by far the fastest-growing fossil fuel. It is the number one fuel source by far for generating electricity in the U.S. and much of the rest of the world. Demand across the globe is booming and continues to increase. At the same time, the U.S. is the world’s largest producer of natural gas and the largest exporter.

After being stagnant for decades, U.S. electricity demand is growing at breakneck speed. As a result, demand for natural gas is booming right along with it. It’s also a global phenomenon. U.S. natural gas exports, in the form of natural gas liquid (NGL), are soaring. This country is already the largest exporter, and growth is staggering. U.S. NGL liquid exports over this past year have grown a whopping 67% over the prior year. And it’s just the beginning.

Natural gas was already the fastest-growing fossil fuel. The addition of soaring electricity demand and exploding U.S. exports adds far more growth to the demand. That should be a huge tailwind for companies involved with the fuel, including companies that transport, store, and process it, such as **Enterprise Product Partners (EPD)** and **The Williams Companies (WMB)**. It's also positive for companies involved in the rapidly growing natural gas export business, including **Cheniere Energy (CQP)**. Trends should also bode well for the stock highlighted below.

## Featured Actions - Buy Expand Energy Corporation (EXE)

**Yield: 2.9%**
**Expand Energy Corporation (EXE)Security type:** Common Stock
**Sector:** Energy (exploration and production)
**Price:** $109
**52-week range:** $91.01 - $126.62
**Yield:** 2.9%
**Profile:** Expand Energy is the largest natural gas producer in North America.
**Positives**

- Natural gas demand is booming because of electricity and export demand.
- Expand can grow capacity to meet demand because its properties are in the highest growth shale regions of the country.
- The company is growing production at lower cost because of cost savings and synergies.
- Growing demand is likely to keep natural gas prices high.

**Risks**

- The fortunes of EXE are tied to natural gas prices, which fluctuate unpredictably.
- A recession would crush energy demand and most likely the stock price.

Established by a 2024 merger between Chesapeake Energy and Southwest Energy, Oklahoma City-based Expand Energy is the largest producer of natural gas in North America. The company acquires and develops properties to produce natural gas, natural gas liquids (NGL), and crude oil. But more than 90 percent of production is natural gas. Expand has huge exposure to the fastest-growing natural gas-producing shale basins in the country. It operates approximately 1.83 million net acres in Haynesville shale in Louisiana, Marcellus Shale in northeastern Appalachia, and the Marcellus and Utica Shale in Ohio and West Virginia. Haynesville is a major supplier of natural gas to Gulf Coast liquefaction facilities and benefits materially from rapid LNG exports because of its proximity to the Gulf Coast. The Appalachian properties benefit from proximity to the vast population centers of the northeastern and mid-Atlantic areas.

As a company involved in exploration and production, the business model is to find gas, get it out of the ground, and sell it for a profit. Profits are determined by the spread between the cost of production and the final sales price, along with the volume of sales. The higher the price, the higher the profits, and vice versa. Natural gas is a commodity, and price swings can be unpredictable. Expand seeks to manage and increase profitability by growing production, reducing costs, and securing long-term contracts.

Prior to the merger in 2024, Chesapeake Energy had gone through bankruptcy. But the merger provided stability and remedied the problems. There was fat that was easy to cut. The new company is easily able to slash costs and create much greater efficiency. In addition, the merger created more scale and synergies, as the companies complement each other. In fact, Expand expects to generate $500 million from synergies this year and $600 million next year.

The company also mitigates the risk of price fluctuations with long-term contracts and hedging. The company also uses long-term contracts, where buyers agree to fixed prices or prices with limited fluctuation.

Expand can also increase production as demand warrants because of its dominating presence in the fastest-growing shale basins in the country. That ability is key. The more gas sold at a profit, the greater the overall profits. The ability to produce more is also crucial as demand from electricity producers and exporters is likely to skyrocket in the years ahead. Expand currently sells 2 Bcf/d (billion cubic feet per day) to LNG export facilities. In the years ahead, LNG export capacity is expected to be 32 Bcf/d.

The company expects to produce an average of 7.15 billion cubic feet of gas equivalent per day (Bcfe/d) in 2025. That will be a 177% increase over last year's average. For perspective, one Bcfe/d is enough to supply about 5 million U.S. homes. Expand also says it can grow production to 7.5 Bcfe/d in 2026. At the same time, Expand is reducing capital expenses.

Because of the synergies, cost controls, and ability to ramp up production, the company expects to spend less to produce more this year, next year, and beyond. The results so far this year are impressive.

For the first nine months of this year, Expand grew overall revenues a whopping 358% over the same period last year. The company also expects 312% earnings growth for the full year and credits the strong numbers to increased production and higher natural gas prices. Average sales of natural gas prices so far this year have increased to $2.81 per thousand cubic feet (Mcf) from $2.51 for the same period last year. And that was before the recent natural gas price surge.

Expand Energy pays dividends as well. The history is short because the company is new and dividends only started in the first quarter of this year. The payout is currently $0.575 per quarter, which translates to $2.30 per year for a yield of 2%. However, the company paid a supplemental dividend in addition to the regular payout in the August quarter, totaling $1.465. Including the high dividend, the trailing yield is 2.6%. There is a possibility of more extra dividends going forward.

Free cash flow has grown 30% this year, and the company expects growth of 20% for 2026. Debt is also being reduced at a rapid clip as capital expenditures decline, and cash flow grows. Expand has a current modest debt/capitalization ratio of 21.6%.

Sure, the stock price can bounce around along with the overall energy sector and gas prices in the short term. But being the number one producer of a commodity in skyrocketing demand should be a very good place to be over time. The stock periodically gets hot and generates high-priced call premiums. There should be several opportunities in the year ahead.


**Expand Energy Corporation (EXE)**
**Next ex-div date: February 13, 2026, est.**

## Portfolio Recap

| Open Recommendations | Ticker Symbol | Entry Date | Entry Price | Recent Price | Buy at or Under Price | Yield | Total Return |
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**AGNC Investment Corp. (AGNC)**
**Yield: 13.5%**

The mortgage REIT hit a new 52-week high last Friday. The price has been in an uptrend since April, and it doesn’t need much appreciation on top of that huge dividend to provide a good total return. While the longer-term total return has been good, this security has good times and bad times. The REIT had bad time for a few years during inflation and rising rates. But now that we are in a Fed rate-cutting cycle, AGNC could continue trending higher. Lower short-term rates will lower costs for AGNC and raise profit margins. All the REIT needs to do is appreciate a little bit in addition to that massive monthly dividend to provide a great total return. **HOLD**


**AGNC Investment Corp. (AGNC)**
**Next ex-div date: December 31, 2025**

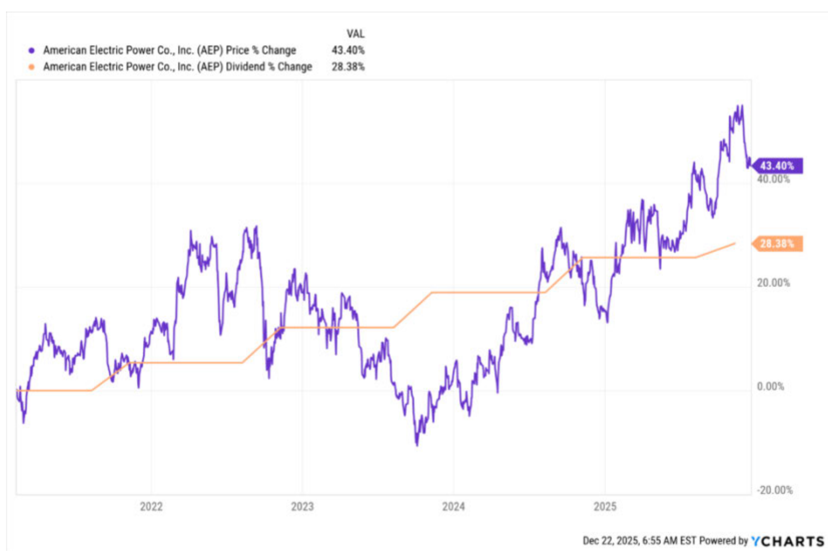
**Ally Financial Inc. (ALLY)**
**Yield: 2.6%**

The online banker stock has been bouncy. And the price has a long way to go to get back to the 2021 high. But the price hit a new 52-week high this month and is at the highest level since early 2022. The company primarily makes auto loans and had a hard time during inflation and rising interest rates. But now the stock should be poised for performance that makes up for lost time. Ally reported strong earnings that soundly beat expectations, and loan delinquencies at the company declined compared to last year’s quarter. A strengthening economy and/or falling interest rates could ignite the price in 2026. **HOLD**


**Ally Financial Inc. (ALLY)**
**Next ex-div date: January 30, 2026, est.**

**American Electric Power Company, Inc. (AEP)**
**Yield: 3.3%**

The utility company stock was near the high and having a great year but has pulled back 5% so far this month. Utilities had been hot but have been the worst-performing sector over the past month as other sectors rotated into favor. The earnings were solid, but what jazzed the market was the growth projections. The company announced a $72 billion capital investment plan over the next five years, which is a 33% increase over the last five-year plan. American Electric projects growing peak loads to 65 GW from the current 37 GW. The growth from soaring electricity demand is coming to fruition, and this utility should benefit, despite the recent pullback. **BUY**

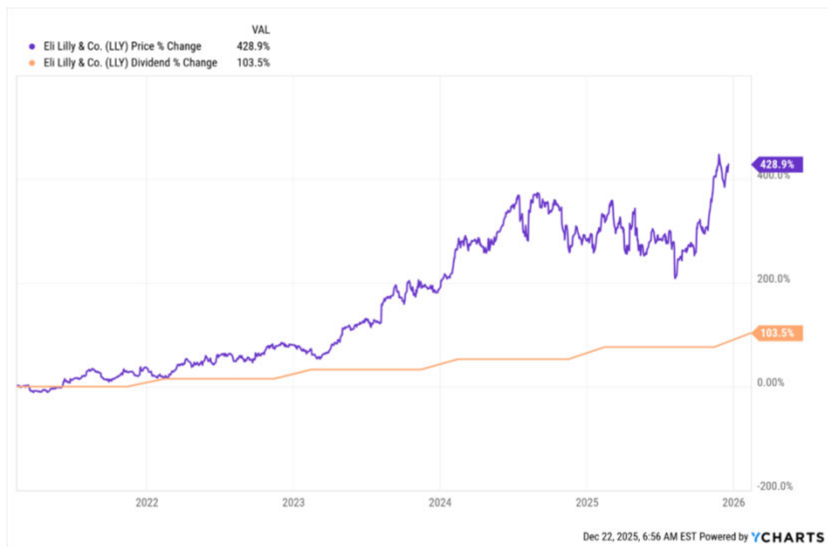


**American Electric Power Company, Inc. (AEP)**
**Next ex-div date: February 9, 2026, est.**

**Cheniere Energy Partners, L.P. (CQP)**
**Yield: 6.2%**
The LNG export business is at an unfortunate crossroad right now, and the CQP price lost most of its recent gains. U.S. natural gas prices soared because of early winter weather and rising demand from overseas and utilities, although there has been a pullback recently. Domestic gas is Cheniere's feedstock. At the same time, prices overseas have been falling because of rising supply from U.S. exports. Margins are getting squeezed. But the current juxtaposition of prices is likely temporary. The recent short-term price struggles are despite a positive longer-term prognosis for the business as global demand for American LNG is growing sharply. (*This security generates a K1 form at tax time.*) **HOLD**


**Cheniere Energy Partners, L.P. (CQP)**
**Next ex-div date: February 6, 2026, est.**

**Eli Lilly and Company (LLY)**
**Yield: 0.6%**
This pharmaceutical juggernaut is bouncing back after it pulled back from the high after the big price surge in November. It appears that good news interrupted the natural pullback. Lilly's oral weight-loss drug showed good trial results and is likely to be submitted for FDA approval in the next few weeks. The existing weight-loss drugs did $10 billion in sales last quarter, and an oral drug could be a game-changer, as it is preferable to an injection. At the same time, the health care sector is benefiting from investors' rotation from AI-related stocks into other sectors. **HOLD**



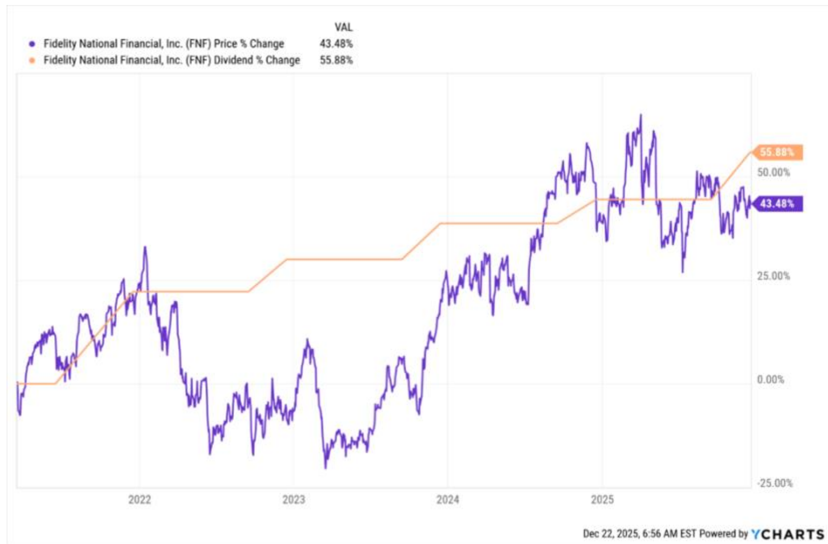

**Eli Lilly and Company (LLY)**
**Next ex-div date: February 13, 2026**

**Enterprise Product Partners L.P. (EPD)**
**Yield: 6.8%**
After two stellar years in 2023 and 2024, EPD is finishing a subpar year. But it hasn't been terrible. The stock has returned 9% YTD. Despite slightly weaker-than-expected earnings, Enterprise is about to turn the corner from a period of heavy spending to one of rising cash flow as $6 billion in new projects will come online in the quarters ahead. In addition, the trade deal with Europe should ensure high NGL volumes for years to come.

EPD has delivered as advertised with appreciation to go along with the huge yield. If it can improve in the appreciation department, it will be a phenomenal holding. And better days could be ahead. (*This security generates a K1 form at tax time.*) **BUY**


**Enterprise Product Partners L.P. (EPD)**
**Next ex-div date: January 30, 2026, est.**

**Fidelity National Financial, Inc. (FNF)**
**Yield: 3.7%**
After bouncing around en route to nowhere for most of this year, the price got a boost in November. But it has pulled back again so far in December. The company deals in title insurance and needs a strong housing market. It benefits from the Fed's lower rates. But it is pulled back amid skepticism over future Fed rate cuts. The biggest impediments right now are high mortgage rates and housing affordability. It will likely be range-bound until there is some significant improvement in the mortgage rate/housing market situation. **HOLD**




**Fidelity National Financial, Inc. (FNF)**
**Next ex-div date: March 11, 2026. Est.**

**NextEra Energy, Inc. (NEE)**
**Yield: 2.9%**
Like AEP, NEE has pulled back along with the rest of the utility sector over the past six weeks. Despite the recent downturn in sympathy with the sector, the price broke out this past fall and should rise beyond the old high when it comes back into favor. NextEra delivered solid earnings results in the third quarter. But the main event should be future growth as the demand for electricity continues to increase. NextEra is in an ideal position, as technology companies tend to prefer clean energy sources when possible. NEE is undervalued. The nation's largest electric utility has a lot going for it right now, and the future should be bright. **BUY**


**NextEra Energy, Inc. (NEE)**
**Next ex-div date: February 20, 2026, est.**

**Realty Income Corp. (O)**
**Yield: 5.7%**
The legendary income REIT should love the Fed rate cuts. Nevertheless, the price pulled back from the highs in September and October. O had a tough couple of years amidst inflation and rising rates. Although interest rates remain peskily high, the direction of longer-term rates is more likely to be lower or at least stable going forward. The table should be set going forward. Earnings were solid, and the REIT slightly raised guidance. Realty also just closed a $9.5 billion acquisition that adds 15,600 commercial properties to the portfolio. O is still attractively valued and should have some pent-up upside if interest rates fall. **HOLD**


**Realty Income Corporation (O)**
**Next ex-div date: December 31, 2025**

**Toll Brothers, Inc. (TOL)**
**Yield: 0.7%**
TOL got a price bump from the Fed rate cut speculation last month. But, like most other interest rate-sensitive stocks, it levelled off because of the increasingly negative prognosis for future cuts in the quarters ahead. TOL had shown signs of life as it trended higher from April until September. But it pulled back again before rising in November. There was optimism about the housing market as mortgage rates fell. But rates have since remained high, and there are reports of weak homebuying demand because of affordability issues. But the longer-term trend is strong as demand exceeds the supply of housing. If the economy and housing market pick up in 2026, TOL could soar. **HOLD**


**Toll Brothers, Inc. (TOL)**
**Next ex-div date: January 9, 2026**

**The Williams Companies, Inc. (WMB)**
**Yield: 3.4%**
After pulling back to the lowest level since April, the price had a strong surge in November. Natural gas got hot primarily because of early winter weather, and prices shot up. But natural gas prices have pulled back sharply this month, and the stock price fell too. The recent price action is only a temporary blip though. Even in a tougher year for midstream stocks, WMB has still delivered a respectable 12% YTD return.
Guidance for 2026 included revenue growth of 11% and strong earnings growth of 25% over 2025. The midstream natural gas company continues to have predictable and resilient revenues as well as growth projects coming online. Huge demand growth for natural gas from utilities and exporters is a growth catalyst that isn't reflected in the historical performance of the stock. **BUY**

**The Williams Companies, Inc. (WMB)**
**Next ex-div date: March 13, 2026, est.**

## Existing Covered Call Trades

**Sell NEE January 16th $85 call at $4.60 or better**
Utilities went out of favor after being red-hot for a while. NEE has taken a hit, and the price is currently more than 5 per share below the strike price. Although there is a good chance that NEE has a strong year in 2026, it might not be above the strike price at options expiration. In the meantime, we are finally getting some good income generation from this portion.

**SELL LLY January 16th $1060 call at $80.00 or better**
It looked like we timed these calls just right as the price pulled back after a big surge. But good news about its oral weight-loss drug and rotation away from tech has again boosted the price. LLY is currently trading right around the strike price. We'll see what happens, but will we get a great income no matter what and a strong total return if the shares are called at options expiration.

**Sell ALLY February 20th $45 call at $2.65 or better**
The stock price is bouncy. And we sold the calls near the high point of the last bounce. Typically, it pulls back after a big spike like it just had. We may have sold the calls near the temporary high. But if the stock gets called, it will still provide a strong total return in addition to the income.

## Income Calendar

Ex-Dividend Dates are in ***RED** and italics*. Dividend Payments Dates are in **GREEN**. Confirmed dates are in bold, all other dates are estimated. See the Guide to *Cabot Income Advisor* for an explanation of how dates are estimated.

**JANUARY 2026**

| SUNDAY | MONDAY | TUESDAY | WEDNESDAY | THURSDAY | FRIDAY | SATURDAY |
|---|---|---|---|---|---|---|
| 28 | 29 | 30 | 31 | 1 New Year's Day | 2 | 3 |
| 4 | 5 | 6 AGNC 0.12 | 7 | 8 | 9 *TOL* | 10 |
| 11 | 12 | 13 | 14 | 15 O 0.27 | 16 | 17 |
| 18 | 19 M L King Day | 20 *ALLY* | 21 | 22 | 23 | 24 |
| 25 | 26 TOL 0.25 | 27 | 28 | 29 | 30 *AGNC* *EPD* *O* | 31 |

**FEBRUARY 2026**

| SUNDAY | MONDAY | TUESDAY | WEDNESDAY | THURSDAY | FRIDAY | SATURDAY |
|---|---|---|---|---|---|---|
| 1 | 2 | 3 | 4 | 5 | 6 CQP | 7 |
| 8 | 9 AEP | 10 AGNC 0.12 | 11 | 12 *LLY* | 13 *EXE* ALLY 0.30 EPD 0.545 | 14 |
| 15 | 16 Presidents' Day | 17 O 0.27 | 18 | 19 | 20 *NEE* | 21 |
| 22 | 23 | 24 | 25 | 26 | 27 O AGNC | 28 |
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**The next *Cabot Income Advisor* issue will be published on January 27, 2026.**

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