



May 2026
2Q2026

The *Gas* Menagerie

*“Now if I tell you that you suffer from delusions
You pay your analysts to draw the same conclusions
You live your life like a canary in a coalmine”*

~ “Canary In a Coalmine,” The Police

On the cold wet morning of January 27, 1896, there was a deadly mining explosion in the small village of Tylorstown, Wales. Fifty-seven men were killed. The obvious culprit was the blast itself. But an Oxford University professor, John Scott Haldane, had his doubts. He discovered four victims trapped in a chamber. After autopsies were performed on the miners, it was determined they were not killed by the blast, but rather, they met their untimely deaths due to carbon monoxide (CO) poisoning. Despite plenty of access to oxygen, the men had suffocated.

Haldane rushed back to Oxford and began experimenting using himself as the guinea pig. He spent the next few months locking himself in a gas-filled chamber, testing the effects of carbon monoxide on himself and various animals. Either he or the animals might pass out. His own children stood watch, ready to rescue him. Finally, he concluded that a small canary was twenty times more sensitive to CO than humans. Thus the 100-plus year tradition of miners bringing canaries down into the mines began.



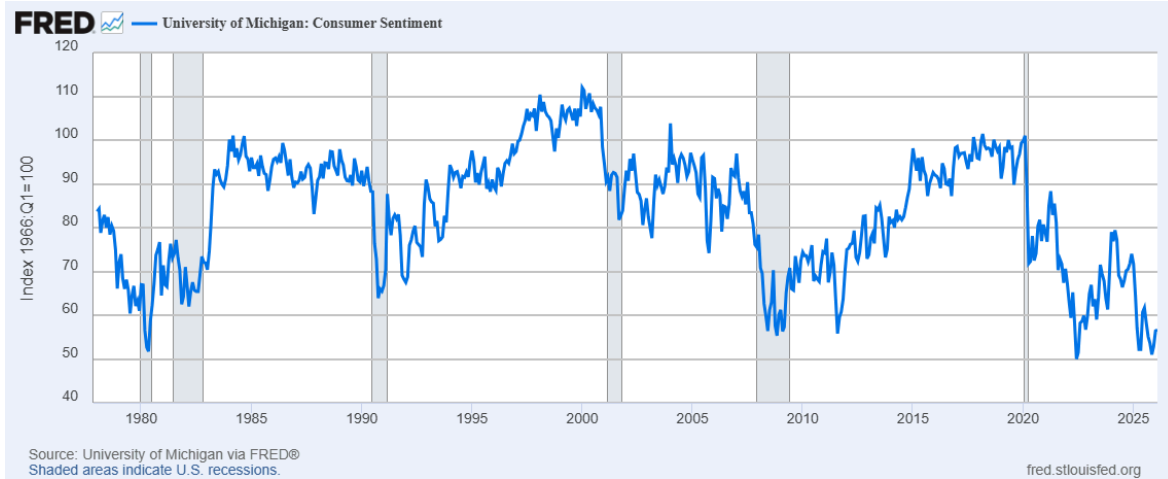
Eventually the phrase “canary in a coal mine” escaped the mines and entered the Wall Street lexicon as shorthand for an early warning sign of coming distress. Today, economists, marketeers, and bankers alike are reaching for the entire menagerie to describe risks surfacing in the economy. The recent “raging bull market” in oil prices is expected to have an outsized impact on consumer spending, sentiment and future inflation. JP Morgan CEO, Jamie Dimon claims two recent defaults on syndicated loans suggest there will be more than one “cockroach” surfacing from the dark crevices of the opaque private credit market in the near future. Also, the narrow breadth of S&P 500 earnings and the associated tempering of future market optimism is described by at least one money manager as “a dog chasing just a few birds.” Are these alarm bells a precursor to something bigger for financial markets, or simply false alarms? Is the canary alive?

Consumer Sentiment Swan Dives

One of the most high-profile “canaries in a coal mine” to hit the financial wires is the recent swan dive in consumer optimism. The Consumer Sentiment Index is a leading indicator of future economic activity that attempts to measure how likely it is that households will spend their hard-earned dollars in the near future. The reading is currently near its lowest level since the University of Michigan began publishing the Index back in 1978. This is important since almost 70% of the US economy is driven by consumption. When consumers are optimistic, they will generally feel more comfortable spending and investing. When consumers are pessimistic, they tend to spend and invest less which could adversely impact the economy and

the stock market. The Index dropped by a whopping 6.6% in the month of March followed by an equally volatile performance in April (Chart 1). Concurrently, the Economic Conditions Index, which gives a real-time snapshot of the economy's overall health, also hit a record low in March. This too may be an early warning sign of a potential downturn in economic growth and the market.

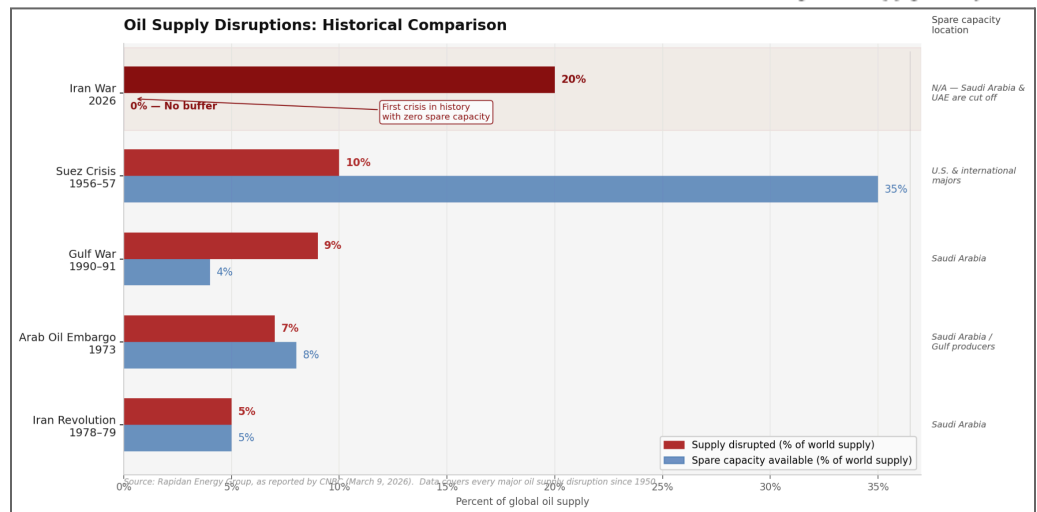
Chart 1: March Consumer Sentiment Lowest in 50 Years



Raging Bull in Oil

The crash in these consumer-oriented economic measures has been brought on by one of our menagerie, a “raging bull” in the oil market following the largest disruption in the flow of oil in history. An estimated 20% of the world’s oil supply flowed through the Strait of Hormuz before the Iran conflict started. Now it is a trickle.

Chart 2: Major Oil Supply Disruptions



Just as Covid helped precipitate an oil shock in April, 2020 that drove demand down by an estimated 29 million barrels a day and prices below zero for a time, the current oil supply shock has driven prices to over \$100 a barrel. The current oil supply shock will likely be exacerbated by the fact that the spare capacity in supplies worldwide was already at alarmingly low levels before the Iran War began (see Chart 2). Gas prices surged 21.2% in the month of March. This increase helped drive core CPI in the US up 0.9% to an estimated 3.26% in headline inflation, the largest one-month jump since the post-Covid surge that peaked in June 2022. According to the US Bureau of Labor Statistics (BLS), oil only represents 6.4% of the consumer price index or what is referred

Chart 3-Headline Inflation Highest Since Covid

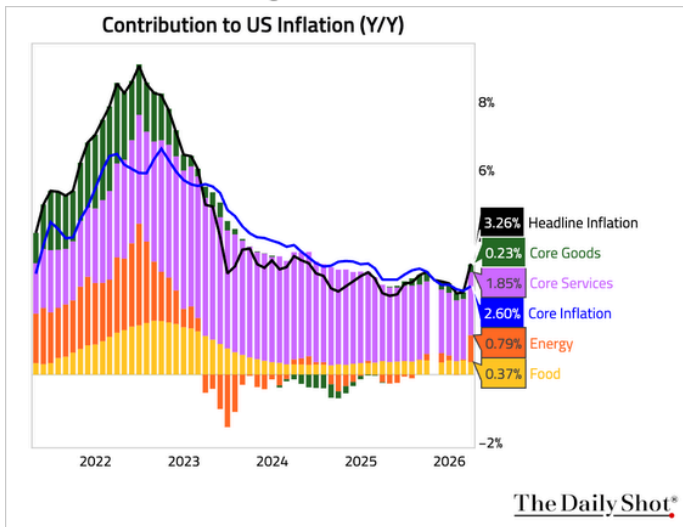
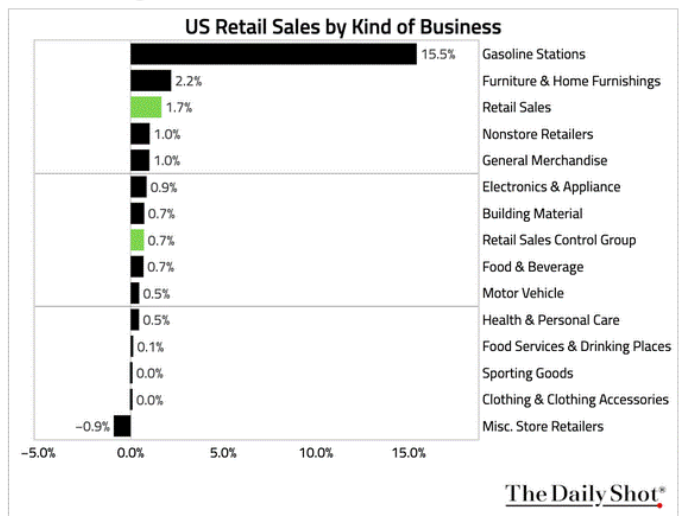


Chart 4: Rising Retail Sales



to as “headline” inflation and food is about 13.7% of the total inflation pie (see Chart 3). But when the BLS backed out those pesky energy and food costs, “core” inflation was only up a more modest 2.6%.

One might have expected the combination of war, a spike in gas prices and the lowest Consumer Sentiment reading on record to mute consumer spending, but that was not quite the case. Credit card purchases by Bank of America customers in March actually showed an *increase* of 3.9% versus a year ago. Further, as evidenced by Chart 4, most categories of retail sales realized relatively flat to modest increases in the same month. However, March gasoline station sales rose a whopping 15.5%.

Kockroaches in a K-Shaped Economy

What was already profoundly evident before the Iran War was that credit from lower end consumers and marginal corporate credits were deteriorating in the current K-shaped economy. Lower-income consumers have been losing ground to higher-income consumers for the past couple of years (see Chart 5). In a recent Bank of America report, they noted the NY Fed’s Q4 2025 Household Debt and Credit Report showed total household debt had risen to a record \$18.8 trillion. But what is truly troubling is 4.8% of outstanding debt was in some stage of delinquency and credit card loans in serious delinquency skyrocketed to a GFC-high of 7.13%.

Jamie Dimon warned of a similar trend occurring with lower rated commercial borrowers. On a JP Morgan conference call last October, Dimon

Chart 5: Lower Income Households Losing Ground

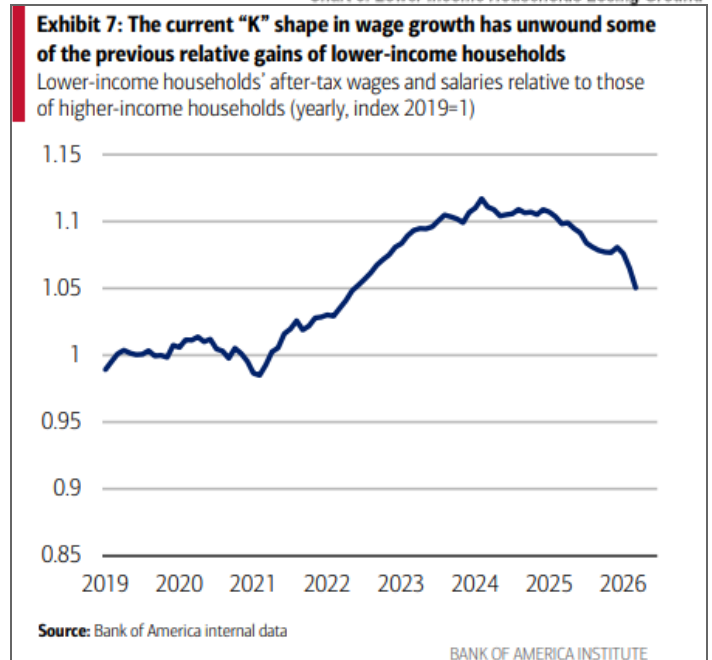
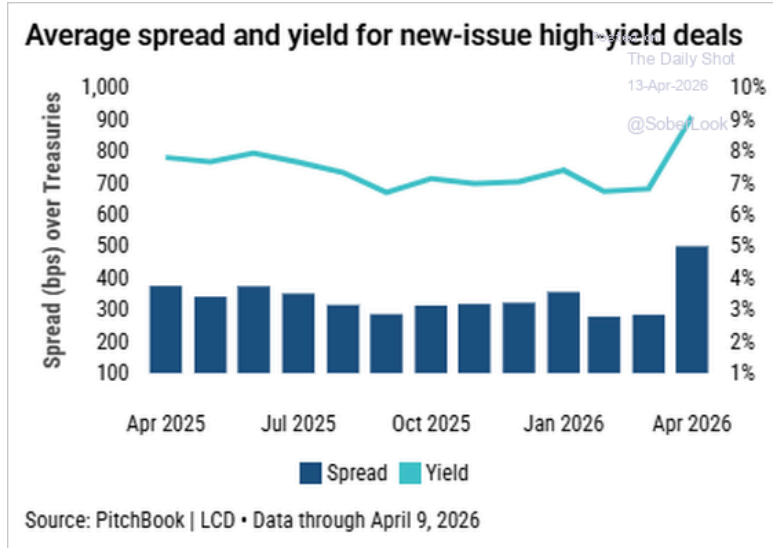


Chart 6: Credit Spreads Widening



commented on the high-profile bankruptcies of subprime auto lender Tricolor Holdings and auto parts maker First Brands. It is important to note that those collapses were as much the result of fraud and bad underwriting as they were bad business models. But Dimon stated, “When you see one cockroach, there’s probably more. Everyone should be forewarned on this one.”

Comments from Dimon and headlines about troubles in the private debt market are beginning to have a negative impact on credit markets. For years, credit spreads, the yield differential between Treasuries and corporate bonds, have been narrow because of investor

optimism, but recently these spreads have widened (Chart 6) on the heels of the Iran War and flashing yellow signs from the economy.

Dog Chasing A Few Expensive Birds

So far, these economic and financial canaries and cockroaches have not found their way into the overall market as the Indexes have recently hit record levels. The Shiller P/E is back near 40, a level that has historically been a warning sign that the margin for error in investing has narrowed significantly (Chart 7).

Chart 7: Shiller P/E Index

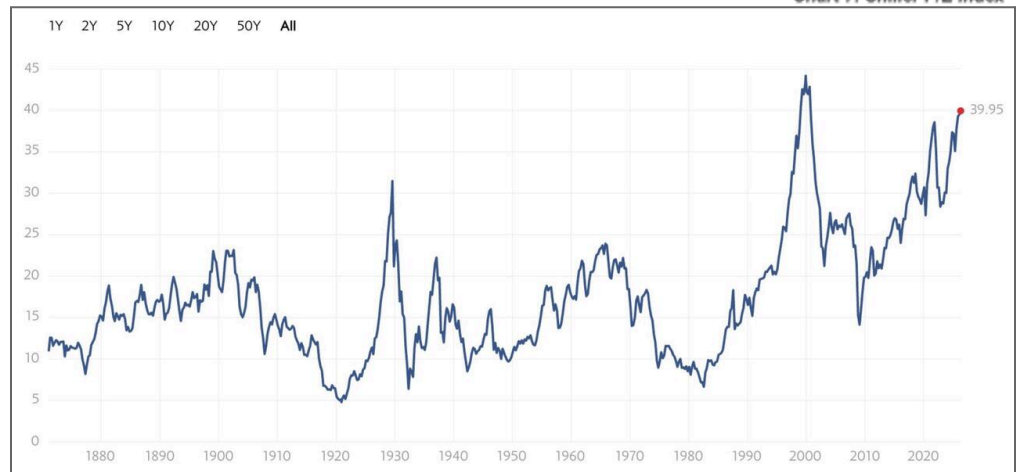


Chart 8: 2026 Expected EPS Growth Contribution

Company	Consensus year/year EPS growth		Full year 2026	
	Q1 2026	Contribution to S&P 500 growth	EPS growth	Contribution to S&P 500 growth
NVIDIA Corporation	118 %	35 %	75 %	21 %
Micron Technology, Inc.	682	18	589	19
Microsoft Corporation	17	6	14	4
Broadcom Inc.	51	6	82	7
Amazon.com, Inc.	2	1	7	1
Meta Platforms Inc	3	1	26	3
Alphabet Inc.	(7)	(4)	6	1
Total	36 %	63 %	45 %	57 %
S&P 500	12 %	100 %	17 %	100 %

Source: FactSet, Goldman Sachs Global Investment Research

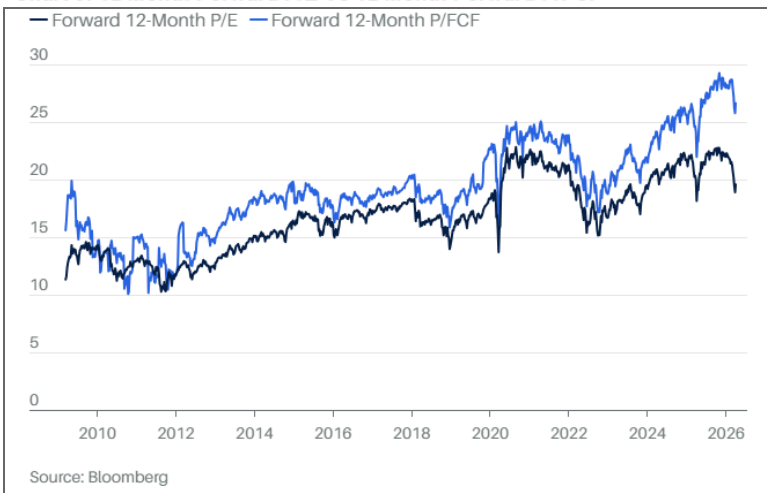
While stock prices may be near historic highs from both a valuation and price standpoint, a recent survey of Wall Street analysts shows S&P 500 earnings are expected to be up 17% in 2026 (Chart 8). Yet, a report published by Goldman Sachs points out that an estimated 57% of the earnings contribution to the S&P 500 in 2026 will come from just a handful of technology stocks.

AI, which represents the largest cap-ex event in history, is an enormous concentration in a single

investment theme. Anthropic CEO Dario Amodei warned that AI could “wipe out half of all entry-level white collar jobs” within the next one to five years. Goldman Sachs added that AI “could perform up to a quarter of all work tasks, potentially replacing a similar percentage of jobs in the US and Europe.” All of this begs the question: are investors paying for growth at this point or a very optimistic version of the future where almost nothing goes wrong? And if AI is as successful as predicted, who will be left to consume products and services?

Veteran *Barron's Magazine* editor Jack Hough suggested in a recent article “the stock market is more expensive than it looks.” (Barrons 4/3/26) While S&P 500 earnings are expected to rise by 17% this year, Hough points out that the forward P/E multiple of 20 is still 20% higher than the historical average over the past 20 years. He suggests the numbers look even more expensive when one considers how much *free cash flow* (FCF) these same companies are producing. Perhaps the best way to look at FCF is it simply measures cash in and cash out for a company over a given period of time.

Chart 9: 12 Month Forward P/E Vs 12 Month Forward P/FCF



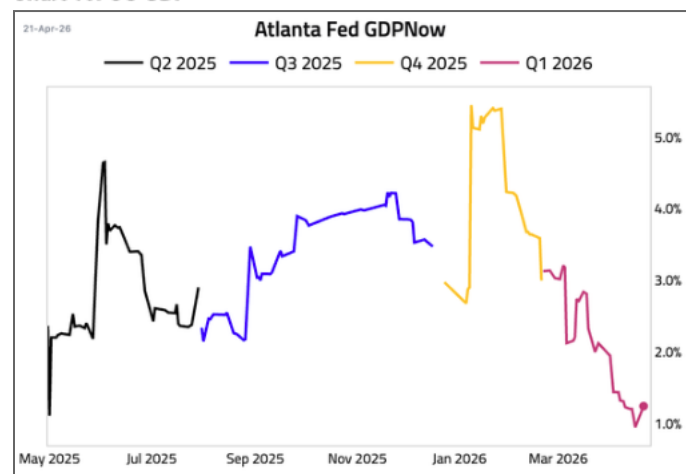
The forward price to FCF of 27.2 times is a whopping 37% above the average for the past 20 years. Companies are expected to earn \$2.8 trillion in 2026, but they are only expected to generate \$1.9 trillion in FCF.

Earnings accounting allows companies to spread cap-ex spending over multiple years, but immediately realize any income immediately from these same investments. However, all cap-ex expenses are realized in the year they occur when it comes to FCF. Hough claims this large spread in how accounting treats spending is giving these tech companies a free pass in the market.

Canary Still Singing...For Now

As the market hits new highs in real time, the Atlanta Fed's *GDP Now* clearly shows the economy is going the other way, as evidenced by Chart 10. Numbers from *Barron's* show that the chasm between the real economy and the market is certainly widening. But if the largest energy disruption in history continues, the oil bull will maintain strength and the consumer will be negatively impacted. If this impact continues, it is likely that the current pattern of the market resembling “a dog chasing a few birds” will continue. For now, multiple alarm bells are going off across the globe making it harder for the canary to sing its merry song.

Chart 10: US GDP



Sincerely,

Chris L. Duvet

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