Schrödinger's Market

Energy scarcity, tech euphoria, and opportunity amid the market's contradictions

27 Jul 2026 CIO Perspectives

> "If a man never contradicts himself, the reason must be that he virtually never says anything at all."
>
> -Erwin Schrödinger

Key Takeaways

- Markets are pricing in a split reality: oil markets remained constrained despite energy underperformance, while momentum and leverage continues to fuel a powerful rally in some of the most cyclical parts of the market, in our view
- Energy's tight inventories, record refining margins, and persistent transportation disruptions supported durable cash returns for producers
- Select hyperscalers and semiconductors now offer more compelling AI exposure after valuation resets, in our view, while closed-source model providers face growing sustainability and competitive risks

We do not often write about quantum mechanics, and we will not spend a ton of time on it, but often analogies can be quite helpful in making a point.

Erwin Schrödinger created his famous "Schrödinger's Cat" thought experiment to illustrate the absurdities of applying quantum mechanics to everyday objects. The idea is that until you look into the box, the cat is suspended across two simultaneously opposed states: one alive and one not so.

Similarly, we think today's markets are suspended in two similar states: one of simultaneous belief and disbelief. A belief that some trends can go on forever, say a rise in the price of some of the most cyclical parts of semiconductors, or that some trends simply do not matter, say damaged energy infrastructure and their subsequent bottlenecks.

THE MARKET'S SUPERPOSITION

If we compare and contrast 1Q 2026 with 2Q 2026, those states could not be more diametrically opposed. Most sectors declined in 1Q, with energy being one of the few positive standouts. However, during 2Q, we saw the inverse. In fact, despite what is arguably the largest energy supply shock of our lifetimes, the energy complex—and by extension, energy producers—all underperformed. It seems very difficult that both of these things can be true simultaneously. Yet here we are.

ENERGY'S UNEXPECTED PRICE DROP

Over the last 90 days or so, we have been surprised by the magnitude of the overall price declines across the energy sector. Part of this has been due to the decline in Chinese imports[1] and part of this has been due to the US reducing its Strategic Petroleum Reserves (SPR) down to early 1980s levels.[2] Regardless, we are running into a situation where inventories are declining across the board on a global basis. To us, these things cannot go on forever.

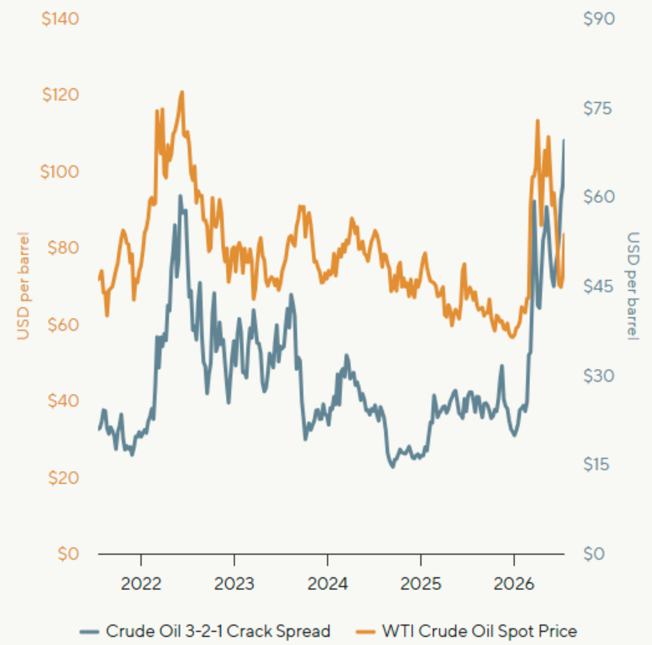
Our views were never predicated on a massive increase in the price of oil. Instead, our energy exposure has consistently been based on Brent crude trading between $65 and $80 per barrel, a range we view as ideal for oil producers. It stays out of the crosshairs of political backlash, while simultaneously staying below levels where shale producers would likely meaningfully ratchet up production.

But one area where we are seeing an incredible rise is in crack spreads, which are basically a proxy for overall refining profitability. Crack spreads measure how profitable it is to take three barrels of oil and break them down into a usable product, such as two barrels of gasoline equivalent and one barrel of distillate.

If we look at a chart of the standard 3-2-1 crack spread, it recently surpassed the 2022 highs and is now sitting at nearly $70 per barrel, an all-time high. All of this is happening despite the fact that crude oil benchmarks Brent and WTI are in the $80s per barrel as of July 2026. Rising spreads tend to be a net positive to the underlying price of oil.

On Tight Supply, Refining Margins Flying High

Crack spreads at an all-time high



Source: GQG Partners LLC (chart). LSEG Datastream (data). Data for the time period from 16 July 2021 through 17 July 2026.

Therefore, with this type of backdrop, we believe a company like Exxon can generate attractive mid- to high-teens returns, supported by dividends, buybacks, and organic EPS growth.[3]

Further, we continue to question how quickly the normalization of the Strait of Hormuz will occur, especially in light of refiner Valero noting on their most recent earnings call that it takes roughly three days for every one day the strait is closed. At this rate (July 2026) that puts us about a year out. Not only that, but we are continuing to see tanker rates elevated while also having little clarity on how many ships will re-enter the strait after being stranded in the strait for so long.

EVOLVING VIEWS ON HYPERSCALERS

To continue our contradiction, it made little sense to us that a massive energy supply shock could be net positive for the broader technology complex. Yet these companies continued to exhibit upward price action. We see several risks in the tech space despite the price rise, but we have also recently identified a few potential opportunities.

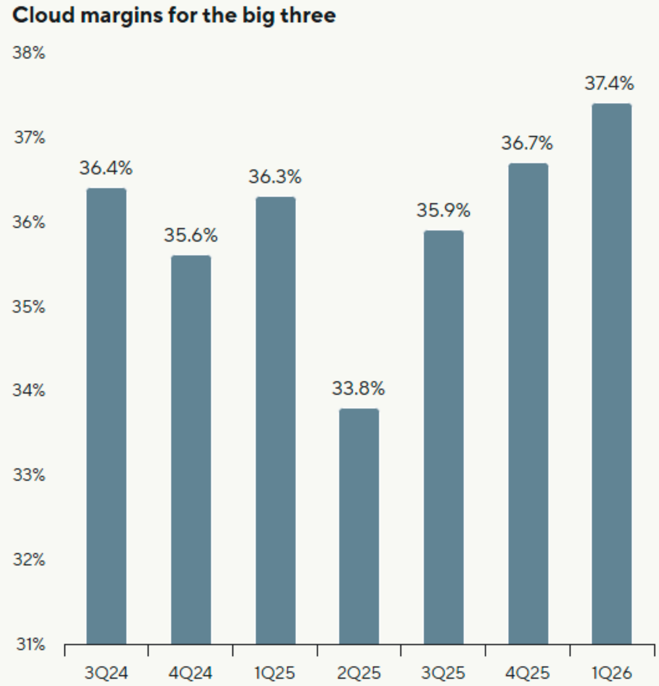
On the risk side, we continue to monitor the memory complex, with particular attention to emerging markets. Because of their meteoric rise, maybe it is not that surprising that many South Koreans reportedly cashed out their life insurance policies[4] while borrowing the most money on margin in the country's history to ride this wave.[5]

On the flip side of things, the hyperscaler complex appears more attractive to us.

Over the past six to 12 months, many high-quality technology companies, notably, hyperscalers and select semiconductor companies have derated on fears that these businesses are exhibiting higher capital intensity going forward (a characteristic markets have generally penalized). However, as our view on enterprise AI spending as a driver of more sustainable demand has improved, we now believe valuations of select companies have become more compelling and now reflect some of our broader views and concerns about AI.

The key change, for us, is not that AI risks have disappeared within these businesses but that margins have remained better than we expected, while valuations have meaningfully reset. In some cases, such as with Amazon, Nvidia, and Microsoft, valuations are now lower than before AI took off in early 2023. To us, this is equivalent to investing in the core businesses we like at a reasonable price, with AI now becoming an interesting call option, in our opinion.

Hyperscaler Margins Have Been Better than Expected

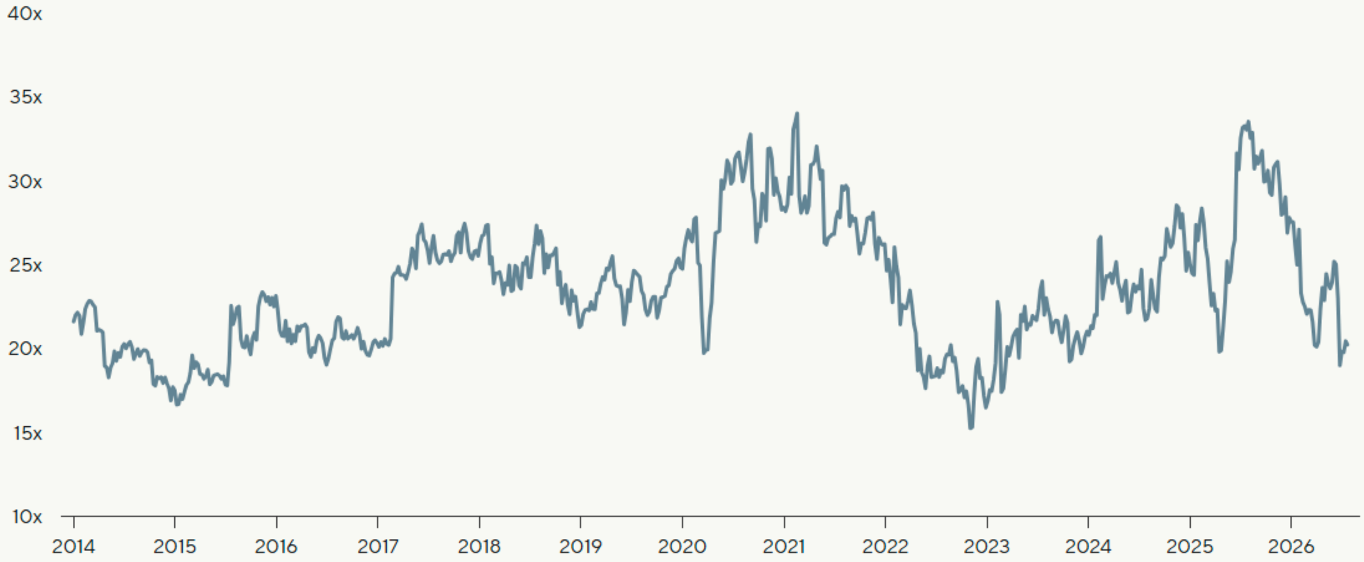


Source: GQG Partners LLC (chart). Wells Fargo Securities (data). Data as of 20 May 2026. Big 3 hyperscalers include AMZN, MSFT, and GOOGL. Content does not constitute investment advice and no investment decision should be made based on it. The stocks illustrated above may or may not be held in GQG client portfolios.

At a time when growth is strong and margins are generally improving, we think the normalizing valuations and subsequent stock underperformance, specifically across the hyperscalers, make the current setup quite compelling. Memory stocks are more likely to be overearning while semiconductor names like Nvidia are less likely, in our view. As always, we keep an open mind and do not shy away from revisiting names we have owned previously.

Valuations May Now Reflect Prior Concerns

Average forward 12-month earnings multiple on hyperscalers



Source: GQG Partners LLC (chart). BNP Paribas (data). Data as of 21 July 2026. Hyperscalers include AMZN, GOOGL, META, MSFT, ORCL. Content does not constitute investment advice and no investment decision should be made based on it. The stocks illustrated above may or may not be held in GQG client portfolios.

With more and more competition from open-source models, particularly those coming from China, we think the closed-source models could be in a very unenviable position going forward. We see the possibility for closed-source models losing market share and pricing power, while the overall system grows due to enterprise adoption. While this may seem like a net negative because many market participants associate OpenAI and Anthropic with everything "AI", this may be a net positive for the environment as businesses gravitate toward cheaper models while increasing their overall usage.

When we roll these things up, it may seem like a contradiction that we are holding two incompatible things simultaneously: energy versus technology, select semiconductors and hyperscalers versus memory, etc. But at the end of the day, we must grapple with and react to the markets and data that we are presented with, not the ones we want. And in our minds, it is better to seem like a contradiction than do nothing at all.

As always, thank you for your support.

Rajiv Jain
Chairman & Chief Investment Officer
GQG Partners LLC

END NOTES

[1]"China's Collapsing Crude Oil Imports to Fall Further in June." Bloomberg News. 25 June 2026.

[2]"Oil stocks in US Strategic Petroleum Reserve fall by 5.5 million to lowest level since 1983." Reuters. 29 June 2026.

[3]"Investor Presentation. ExxonMobil Company overview and investment case." ExxonMobil. 20 February 2026.

[4]Ji-Won, Choi. "Policy surrender payouts rise as savings-bank deposits hit 4-year low." Korea Herald. 11 May 2026.

[5]Rimmer, Jules. "Debt-fueled bets are turbocharging the South Korean stock market as Kospi jumps 8%." Morningstar. 21 May 2026.

DEFINITIONS

Closed-source model: A proprietary artificial intelligence (AI) system whose model weights, source code, training data, or other core technical components are controlled and kept private by its owner. Access typically occurs through an API, application, or licensed product.

Earnings Per Share (EPS): A company's net income attributable to common shareholders divided by its weighted-average number of common shares outstanding during a reporting period. It measures the profit attributable to each common share. Rising EPS can indicate improving profitability, though investors also assess the source and sustainability of that growth.

Enterprise adoption: The process through which an organization evaluates, procures, integrates, governs, and scales a new technology, software product, standard, or business practice across its operations.

Hyperscaler: A company that operates cloud infrastructure at enormous global scale, including extensive data centers, computing capacity, storage, and networking. Hyperscalers can rapidly provision and scale resources to support large, variable workloads. Examples include Amazon Web Services, Microsoft Azure, and Google Cloud.

Market participant: Any individual, company, institution, or government entity that participates in a market by buying, selling, lending, borrowing, investing, trading, or facilitating transactions.

Market share: The proportion of a defined market accounted for by a company, product, or brand during a given period. It is commonly calculated as a company's sales revenue or unit sales divided by total market sales over the same period.

Open-source model: An artificial intelligence (AI) or machine-learning model released under a license that permits public access, use, study, modification, and redistribution of specified components, often including model weights and source code. The availability of training data, training code, and architecture details varies by model and license.

Pricing power: A company's ability to raise prices while maintaining demand, customer retention, and profitability. It commonly arises from differentiated products, strong brands, switching costs, market position, intellectual property, or essential offerings.

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