

# Quality vs. Value in a Late-Cycle Soft Landing

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February 5, 2026

Quality has the structural edge late-cycle as growth cools and inflation normalizes. Balance-sheet strength, pricing power, and earnings durability typically outperform when breadth is narrow and credit conditions tighten. Value can work tactically around rate-cut and curve-steepening episodes, but sustained leadership requires broader earnings participation.

## Forward P/E Multiples: Quality vs Value (2026)



Source: J.P. Morgan Guide to the Markets (Jan 27, 2026)

## Executive Summary

Quality retains a strategic edge in a soft-landing late-cycle setup. The factor benefits from stable margins, lower leverage, and earnings durability, while value is more sensitive to the slope of the curve and breadth of earnings upgrades. The current valuation gap is meaningful, but the catalyst set determines whether value can lead beyond short tactical windows.

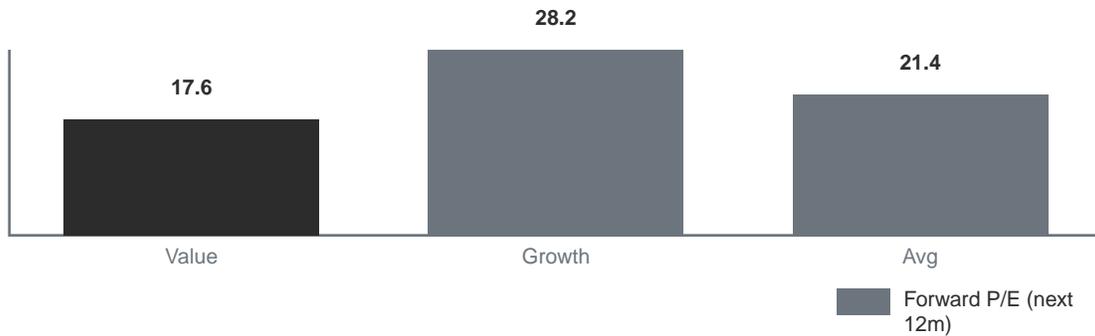
Key Takeaways:

- **Value trades at a meaningful discount:** Russell 1000 Value vs Growth P/E discount is about -37% versus a long-term average near -30% (Jan 27, 2026).
- The S&P 500 forward P/E stands at 22.2x versus a 30-year average of 17.1x, while dividend yield is 1.4% versus a 30-year average of 2.0%.
- Quality tends to outperform in fragile markets; value needs broader earnings participation and curve steepening for sustained leadership.
- **Catalysts:** easing inflation, rate cuts, and improving earnings breadth beyond mega-cap leaders.

## Valuation Gap and Quality Screens

The valuation case for value is strongest when paired with quality screens. The Russell 1000 Value discount to Growth is roughly -37% versus a long-term average near -30%. However, dividend yield on the S&P 500 remains only 1.4% versus a 30-year average of 2.0%, underscoring that the valuation buffer is thinner than in prior cycles. The implication is to emphasize quality value rather than broad, low-quality exposure.

## Value vs Growth P/E Discount (Jan 2026)



Source: J.P. Morgan Guide to the Markets (Jan 27, 2026)

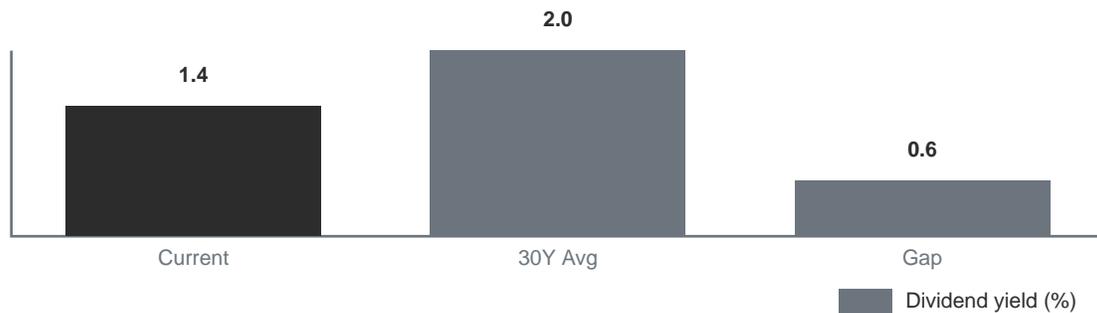
## Rate Sensitivity and Funding Mix

Quality portfolios generally carry lower leverage and longer-dated funding structures, while value baskets are more rate sensitive and cyclically exposed. As rate cuts begin, the relief can be meaningful for value, but only if credit spreads remain stable and earnings breadth improves. This is why the rate path and curve shape are central to factor rotation.

## Credit Conditions and Refinancing Calendar

Credit conditions are the gating factor for value leadership. If spreads widen or refinancing windows close, quality balance sheets typically outperform. Conversely, a stable or narrowing spread environment supports value, especially in rate-sensitive financials and cyclicals.

### Dividend Yield: Current vs 30-Year Average



Source: J.P. Morgan Guide to the Markets (Jan 27, 2026)

## Earnings Breadth and Sector Mix

Narrow earnings leadership has supported quality in recent years. Sustained value leadership requires broader upgrades across industrials, financials, and consumer cyclicals. When breadth expands, the value factor tends to capture the upside via higher operating leverage.

## **Policy Tailwinds and Domestic Exposure**

A soft-landing policy path favors factors tied to domestic demand. If fiscal spending remains supportive and wage growth holds up, value sectors with domestic exposure can benefit. However, the rotation remains conditional on inflation stability and the pace of rate cuts.

## **Investment Implications**

The trade is not simply value vs quality; it is quality core with tactical value overlays. Investors should prioritize strong balance sheets, stable margins, and pricing power while selectively adding exposure to value segments that benefit from curve steepening and easing credit.

## **Portfolio Allocation Considerations**

Maintain a quality core for downside resilience, and add selective value exposure where earnings revisions are improving. Quality and profitability screens reduce exposure to weak balance sheets, while a barbell approach balances durability with tactical cyclicalty.

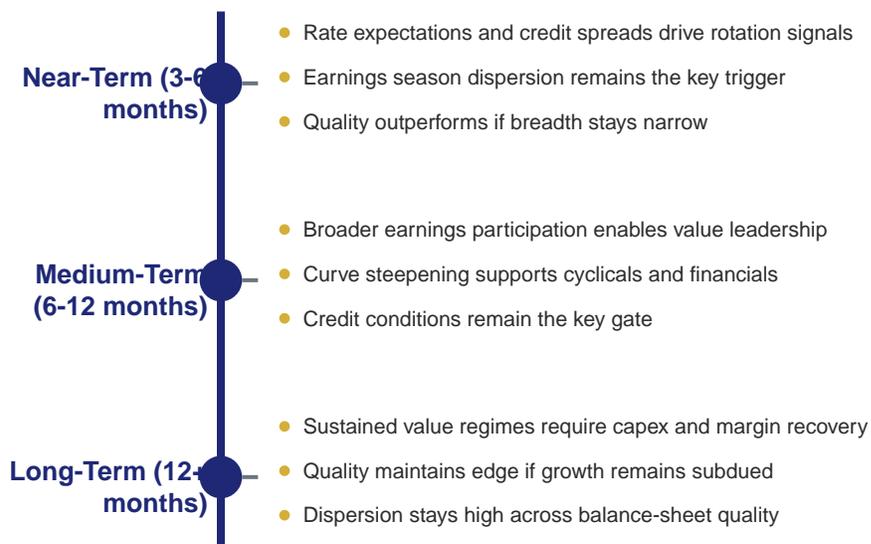
## Timeline and Outlook

**Near-Term Outlook (3-6 months):** Rate expectations and credit spreads drive rotation signals.

**Medium-Term Outlook (6-12 months):** Broader earnings participation would favor value leadership.

**Long-Term Outlook (12+ months):** Sustained value regimes require capex and margin re-acceleration.

### Timeline Overview



*Source: AVANTAS Research Analysis*

## Risk Factors

**Inflation Persistence Risk:** Inflation persistence could delay cuts and pressure rate-sensitive value sectors.

**Credit Risk:** Credit spread widening would favor quality and reduce value upside.

**Earnings Concentration Risk:** Continued mega-cap earnings dominance would limit breadth expansion.

**Geopolitical Risk:** Geopolitical shocks could increase risk aversion and rotate flows into quality defensives.

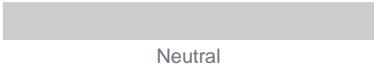
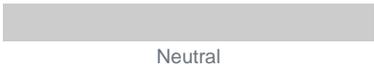
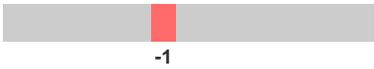
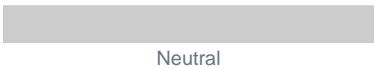
## Conclusion

Quality holds the strategic edge in a late-cycle soft-landing setup. Value can outperform tactically around policy shifts and curve steepening, but sustained leadership depends on broader earnings participation and stable credit conditions.

## Asset Class Impact

A quality tilt supports downside resilience, while selective value exposure captures upside if macro conditions broaden. Credit conditions remain the key swing factor for sustained factor rotation.

## Asset Class Impact

Asset	View	Commentary
US Quality	 +1	Overweight. Defensive characteristics and earnings durability.
US Value	 +1	Overweight. Tactical upside if curve steepens and breadth improves.
US Growth	 Neutral	Neutral. Rich valuations and concentration risks.
Investment-Grade Credit	 Neutral	Neutral. Quality balance sheets offset duration risk.
High Yield / Bank Loans	 -1	Underweight. Refinancing risk if rates stay higher.
Rates Duration	 Neutral	Neutral. Rate path remains the key swing factor.

Source: AVANTAS Research Analysis