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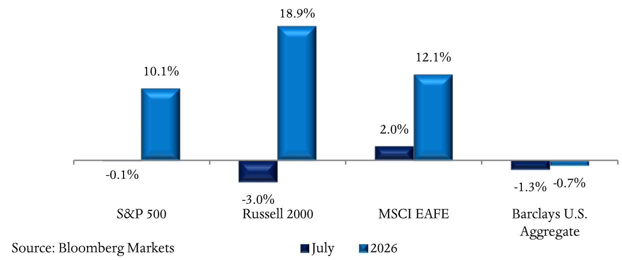
Markets

Following the strongest quarter of the century, the S&P 500 index ended July essentially flat (-0.1%; +10.1% ytd). However, beneath the calm surface a historic rotation unfolded, with AI-related stock momentum reversing. The Philadelphia Semiconductor index, fresh off its record +88% second quarter, fell -20.6% for the month, dragging the Nasdaq composite down -3.2% (+9.5% ytd). Meanwhile, the S&P 500 Equal Weight index rose +0.9%, outperforming by 4.1%, an event that hasn't occurred since the dot-com bubble burst over 25 years ago. The style shift was striking, large-cap value (+3.8%) outperformed growth (-5.9%) by 9.7 points, a 99th-percentile event, as investors heavily unwound concentrated mega-cap tech positions and rotated into defensive sectors such as financials, utilities, and industrials. This left value ahead of growth over the trailing three-, six-, twelve- and twenty-four-month periods, a fact that may surprise many. Sector leadership confirmed this trend, with energy (+12.6% in July; +34.7% ytd, more than double any other sector) and financials (+6.2%, their best month since January 2025) leading. Meanwhile, small-caps in the Russell 2000 consolidated (-3.0% in July; +18.9% ytd) after an unusually strong first half.

Foreign stocks, as measured by the MSCI EAFE index, rose +2.0% in July (+12.1% ytd) aided by a weak dollar and low technology exposure. Europe's Stoxx 600 added +1.3% (+12.4% ytd) on strong earnings. Following global trends, Japan's chip-heavy Nikkei 225 fell -8.1% (+29.0% ytd) while the broader TOPIX held flat. Emerging markets dropped -3.0% as a forced unwind of borrowed tech stocks slammed the quarter's biggest winners: SK Hynix sank -35% and Samsung Electronics -21%, dragging down Korea and Taiwan. Finally, Chinese equities decoupled completely. Offshore shares rallied +9.0% in Hong Kong (-1.7% ytd), while the



mainland Shanghai Composite fell -5.9% (-2.0% ytd) as traders hunted for bargains across jurisdictions.

Fixed income markets delivered a consequential signal. The Federal Reserve held rates steady in a 9-3 vote, but Chairman Warsh's press conference raised central bank credibility questions. Specifically, he reiterated the FOMC's 2% inflation target, but withdrew forward guidance and asserted that the bond market should price risk on its own. In the ensuing days the 30-year US Treasury Bond yield broke above its post-Covid high of 5.18% to close at 5.27%, the highest level since June 2007. As a result, the Bloomberg US Aggregate index fell -1.3% for the month (-0.7% ytd). In currencies, the dollar weakened (-1.3%), and Japan's Ministry of Finance, joined by US authorities, conducted the first coordinated yen-buying intervention since June 1998.

Commodities rebounded +7.2% (+23.0% ytd) as geopolitics returned. WTI crude oil surged +21.8% to $84.67 per barrel, with Brent briefly above $100, as Middle East skirmishes reignited. Gold edged higher (+0.8%) to $4,041/oz, holding the psychologically important $4,000 level, while silver slipped -1.7%.

Geopolitics

June's memorandum of understanding collapsed in a dispute over shipping routes through the Strait of Hormuz, and fighting between the US and Iran resumed. By month-end, however, diplomacy had regained the upper hand. President Trump announced that planned

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strikes would be held off, conditioned on rapidly concluding a deal that would include the complete reopening of the Strait, while Tehran reported that negotiations with Oman over a new maritime route were in their "final stages." Complications have nonetheless multiplied. Houthi activity in the Red Sea, and deepening damage to Russian refineries, by ever more sophisticated Ukrainian drones, is pressuring energy markets.

US

The latest readings of US macroeconomic data have been mixed but point to a durable economy. Inflation surprised meaningfully to the downside, with June consumer prices falling -0.4% month-over-month, aided by a sharp -5.7% drop in energy, relief that July's oil rebound may partially reverse. Activity indicators firmed, with the composite PMI rising to 53.6% and the manufacturing PMI improving to 55.6% from 53.3%, the highest level since May of 2022. Meanwhile the labor market appears to be cooling at the margin and consumer confidence eased to 90.8, a level not seen since March of last year. Second-quarter GDP decelerated to a 1.5% annualized rate, reflecting solid private domestic demand offset by trade and inventory drags. At its July meeting, the FOMC held rates for a fifth consecutive meeting, though with three hawkish dissents. Chairman Warsh's dismissal of forward guidance as a "crisis-era tool" left markets pricing a hike by December, possibly earlier, should inflation run hot.

Europe

European economies recovered from their geopolitically-driven soft patch. The eurozone flash composite PMI rebounded to 51.9%, reaching pre-war levels, while economic sentiment improved, and unemployment held at 6.3%, near cycle lows. Meanwhile second-quarter GDP rose at a 1.8% annualized pace, above expectations. With headline inflation firming to 2.9%, the European Central Bank is widely expected to hike again in September, with roughly 40 basis points of tightening priced by year-end.

July 2026 Economic Statistics

	Jul-26	Dec-25	Dec-24
Federal Funds Target Rate	*3.50 - 3.75%*	*3.50 - 3.75%*	*4.25 - 4.50%*
Consumer Confidence Index	*90.8*	*91.8*	*104.7*
Manufacturing PMI Index	*55.6%*	*52.7%*	*49.3%*
Unemployment Rate	*4.2% (est.)*	*4.3%*	*4.2%*
JPY/USD	*157.57*	*158.71*	*157.18*
USD/EUR	*1.1527*	*1.1552*	*1.0353*
Gold/oz.	*$4,040.95*	*$4,669.56*	*$2,623.81*
Oil (WTI)/bbl	*$84.67*	*$101.38*	*$71.72*

Sources: see disclosure *

In the United Kingdom, inflation again undershot at 2.6%, and the Bank of England's July 'hold' was read as dovish despite a 6-3 vote split. Andy Burnham was confirmed as PM, naming John Healey chancellor.

Asia

The Bank of Japan also held interest rates steady and adopted a more hawkish tone, with an October hike the base case, possibly sooner due to concern over a weakening yen. Indeed, the currency dominated the month. The Ministry of Finance intervened to buy yen in late July, joined by US authorities in the first coordinated effort since 1998, an unexpected degree of cooperation typically reserved for crises.

China's second-quarter GDP slowed to 4.3% year-over-year from 5.0%, though first-half growth of 4.7% remained within Beijing's 4.5-5.0% annual target. The economy's bifurcation deepened. June exports surged +27%, the fastest pace since 2021, driving a near-record $125.6 billion trade surplus, and high-tech manufacturing output expanded +14.1%, while retail sales, fixed investment and property remained weak. The Politburo emphasized fiscal execution and counter-cyclical support, targeting measures aligned with strategic-technology priorities rather than broad reflation.

Outlook

Corporate earnings, the most important anchor for equities, continue to accelerate. Second quarter estimated earnings growth for the S&P 500 index surged to 47.4% year-over-year from the 23.2% expected on

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June 30. When adjusted for non-operating gains, the growth rate drops to a still remarkable 28.8%, with associated revenue growth of 14.1%, the strongest top line since 2021, with ten of eleven sectors posting profit growth. This marks the index's second consecutive quarter of year-over-year earnings growth above 20% and its seventh consecutive quarter of double-digit expansion. Drivers include the estimated $765 billion dollar annual capital expenditure boom in Artificial Intelligence infrastructure (expected to grow to $1.1 trillion in 2027), which translates into immediate profits for semiconductor and hardware providers. This spending has also had a knock on effect on the associated physical industrial and infrastructure sectors. Another notable effect has been the energy sector's structural supply squeeze which has led constituents to post triple-digit year-over-year earnings growth. In the Financial sector, a resurgence in investment banking, dealmaking, and rebounding initial public offering (IPO) pipelines is powering strong capital market results. Overall, corporate America has shown high efficiency and margin leverage, levitating net profit margins to a historic high of 15.7%.

Investors have begun demanding evidence that the unprecedented AI-related capital spending will generate an attractive return, marking a decisive shift in focus from AI demand to AI monetization. With the information technology and communication services sectors accounting for roughly three-quarters of aggregate S&P 500 earnings growth, headline index results overstate the breadth of underlying profit momentum, and any disappointment within this narrow cohort would carry outsized consequences for the market overall. That said, July's correction in technology-related equities appeared driven more by technical selling than by deterioration in fundamentals. Extreme bullish positioning was unwound through hedge fund de-grossing and forced liquidations of leveraged vehicles, particularly in Korea, underscoring how much speculative excess had accumulated. Meanwhile, the risks we flagged last month (pull-forward of demand, debt-funded capex and compressed AI economics) are now being actively repriced. On the latter point, the commoditization of AI models is accelerating. Capable open-source alternatives, many originating in China, are now offered at discounts of 90+% to frontier systems, calling into question whether model-makers can earn returns commensurate with the infrastructure being built on their behalf.

In fixed income, the long-end has spoken. The 30-year Treasury Bond's breakout to its highest yield since 2007 validates our short-duration bias, where income does the heavy lifting while price risk stays contained. The rate path remains bifurcated. Core inflation is falling even as July's energy rebound clouds the headline. A new element warrants attention, some of the long bond's rise reflects a credibility premium, as markets test a Fed that talks tough, withdraws guidance, yet declines to act. In our estimation, higher yielding credit, especially floating rate securities, offer acceptable risk-adjusted income. We remain cautious on investment-grade credit, where tight spreads and heavy hyperscaler issuance offer little cushion.

Given the twin risks now confronting markets, inflation driven by energy and the technology capex boom on one side, and the sustainability of AI-related earnings on the other, we reiterate the case for diversification. The traditional 60% stock 40% bond asset allocation model has shown cracks of late. We continue to recommend owning high-quality globally-oriented equities for the long run. In addition, a combination of Treasury bills, alternative hedged strategies and precious metals should provide better resilience and inflation protection than intermediate duration bonds. Gold stabilized above $4,000/oz despite the headwinds of rising yields, higher oil and a firmer dollar, while central bank purchases rebounded 62% year-over-year in the second quarter and speculative futures positioning washed out to thirteen-year lows. Gold mining equities, meanwhile, trade at their lowest historical valuations. For longer-duration investments we are finding compelling private-market opportunities in cybersecurity, water infrastructure and battery storage. Lastly, our proprietary efforts to source direct investments continue to gain traction, with several interesting small and middle-market prospects.

*Sources: Reuters, Bloomberg, Bureau of Labor Statistics, Conference Board, Federal Reserve, Institute for Supply Management, MSCI, Russell, Standard & Poor's, Financial Times and the Wall Street Journal.