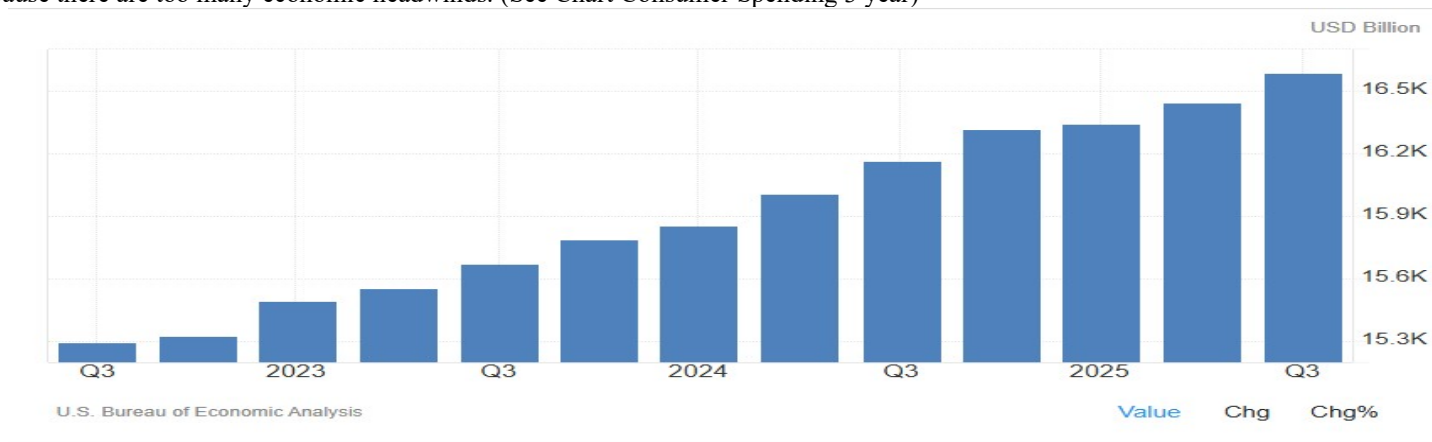


ECONOMIC AND INVESTMENT OUTLOOK Winter 2026

The Economy The U.S. economy in the fourth quarter of 2025 has shown mixed signals, resilient but slowing growth, with strong consumer spending on services and AI-related tech investment, but headwinds from higher costs, cooling labor markets, and policy uncertainty. While GDP growth was positive, inflation remained above the Fed's target and analysts noted concerns over wealth impacts from tech stock dips, with some anticipating slower spending in 2026 despite overall stability. This strength is primarily driven by continued strong consumer spending and strong stock market returns. However, concerns remain for the future, as elevated tariffs and a crackdown on immigration could slow growth in going into 2026, potentially leading to a recession by late 2026.

Sales and Spending Retail sales (excluding motor vehicles and gasoline) did well in October, rising 0.5%. Strong online sales growth of 1.8% accounted for most of that gain, though in-store sales rose a solid 0.3%, as well. Rebounds from September's decline took place in furniture and home furnishings, clothing and sporting goods. Motor vehicle sales were the only fly in the ointment, falling 1.6%, but much of that was related to the expiration of EV tax credits at the end of September. Holiday sales should grow nicely from a year ago, with informal reports from Black Friday and Cyber Monday showing a strong increase from 2024. Restaurant and fast-food sales saw an unusual decline in October. But spending on services excluding dining rose a healthy 0.4% in September. (September is the latest month for which data is available.) Consumer spending growth is likely to be weaker going into next year because there are too many economic headwinds. (See Chart Consumer Spending 3 year)



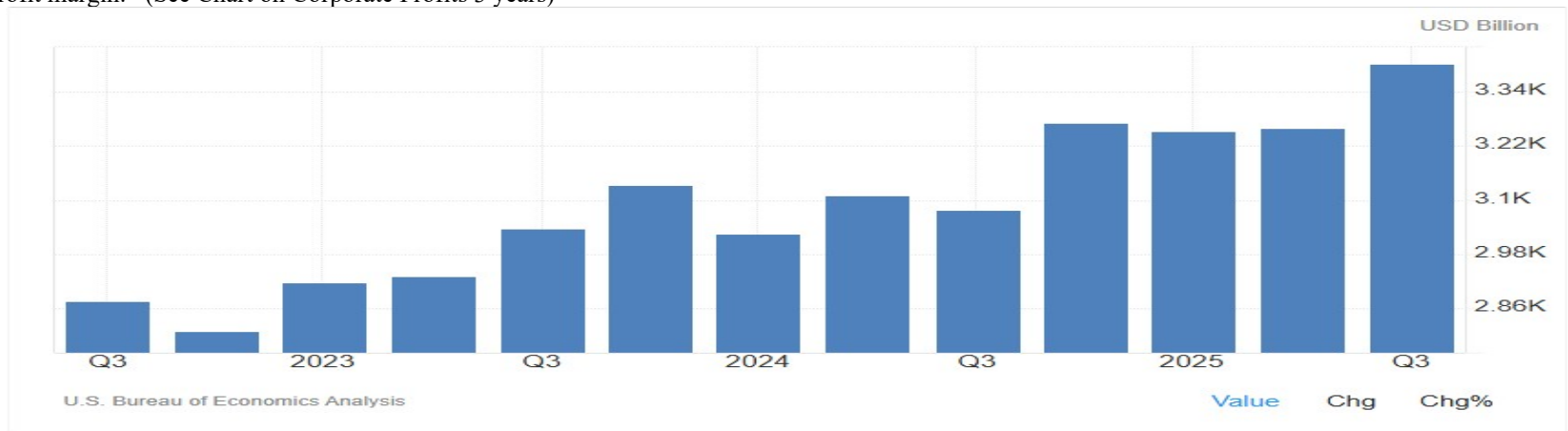
Inflation in November was lower than expected at 2.7%, dropping from 3.0% in September (October data wasn't collected because of the Federal government shutdown). Price increase for the October -November period for food, shelter and other goods came in less than half of what was expected. The only key prices that showed a normal increase were energy and new and used vehicles. Electricity prices continued their upward march, which may be related to the surge in data center construction and their energy demands. There is a good chance that the inflation rate will tick up again in December, though it is expected to stay below 3.0%. The Federal Reserve won't have to trust the November data, since the December price data will be released on January 13, well ahead of the Fed's January 28 policy meeting. If labor market weakness continues, the Fed is likely to cut rates twice more in early 2026 followed by an extended pause.

Monetary Policy The Federal Reserve (Fed), in December, reduced its target by 0.25%, setting a new range to between 3.50-3.75% after its scheduled Federal Open Market Committee (FOMC). While investors widely anticipated this move, three of the twelve FOMC voters dissented, one preferred a larger cut while two favored no change. Investors expect at least two additional cuts next year, reflecting ongoing uncertainty in the economic outlook. Inflation remains elevated, but it has not accelerated as much as feared following new tariff policies.

Fiscal Policy U.S. fiscal policy in late 2025/early 2026 is characterized by a shift from stimulus, with recent government shutdowns impacting growth, while new Trump era tax cuts provide relief, alongside ongoing debates over tariffs and deficit reduction. In the fourth quarter of 2025, U.S. fiscal policy was characterized by a combination of significant recently enacted tax cuts and increased spending measures from the OBBA, which overall is expected to be stimulative in the near term.

The Dollar The U.S. dollar generally weakened in the fourth quarter of 2025, pressured by Federal Reserve interest rate cuts, ongoing trade tensions, and stronger relative global earnings, despite some initial resilience due to safe-haven demand and sticky inflation concerns. While the dollar fell significantly throughout 2025, we look towards 2026 and the outlook for the USD remains subdued and should continue at a more moderate pace, provided that global economic growth holds steady and the Federal Reserve does not raise rates.

Corporate Profits are in a very strong position going into 2026, with profits increasing and remaining near historically high levels both in absolute terms and as a percentage of GDP. This trend is supported by resilient consumer spending, technological investments (particularly AI), and a robust profit margin. (See Chart on Corporate Profits 3 years)



MARKETS

Uncertainties revolve around persistent inflation (despite some easing). A cooler yet tight labor market with rising unemployment, ongoing policy shifts (tariffs, government spending). Questions about consumer spending resilience amid these pressures.

Positives in the current economy include resilient GDP growth, strong personal income and consumer spending, cooling inflation, robust labor markets and significant investments in infrastructure. Also, we have the stock markets trading at all-time highs.

Negatives We still see the high cost of living as a concern, persistent inflation worries impacting household budgets, rising consumer debt, a cooler labor market with falling job confidence and the weakening labor market as well as the lingering effects of high interest rates.

Interest Rates the Federal Reserve cut short-term interest rates by a quarter point, to between 3.5% and 3.7%, on December 10, but will likely pause its cuts at the next meeting, on January 28. Chair Powell feels the Fed is getting close to what he calls “the neutral rate”, which is neither expansionary nor contractionary for the economy. As a result, Powell apparently wants to stop cutting now and let economic trends determine the Fed’s next move. Part of that is waiting for pending government reports on the economy, which have been delayed by the recent shutdown, to provide some guidance. The current 10-year Treasury trades close to 4.13% and the fixed rate mortgage is approximately 6.20% on 30 years.

Common Stocks Wall Street finished 2025 with solid gains of approximately 16.5% on the S&P 500. The stock market had a very strong year with major indexes reaching new highs. Most of the robust growth came from the AI-related sectors, particularly memory/storage, strong earnings from major tech companies, supportive central bank rate cuts, and a rotation into infrastructure/cyclical stocks, despite some volatility from tariffs and inflation fears. The demand for high-bandwidth memory (HBM) for AI training was a major catalyst, alongside broader optimism about AI’s future and solid economic growth. All the major markets showed positive returns for the year, such as the Dow Jones advancing approximately 13% and the technology heavy Nasdaq jumped a nice 20.5%. Many analysts on the street believe stocks could continue to climb higher, provided fundamentals remain strong and the earnings season delivers solid results. Equity markets in 2026 should remain resilient but vulnerable to volatility as we remain constructive on the S&P 500 with a target price of 7,600. As always, we will remain patient and stick to the long-term plan as we navigate this ever-changing.

January 16, 2026

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