

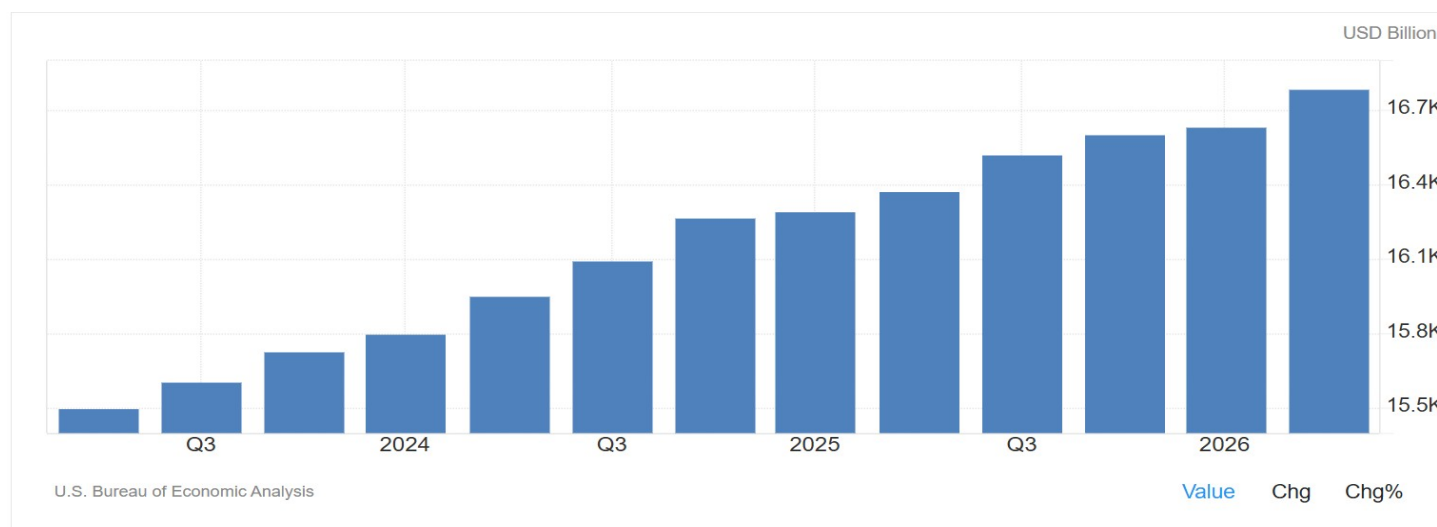
ECONOMIC AND INVESTMENT OUTLOOK

Fall 2026

The Economy – The U.S. economy in the first half of 2026 is still demonstrating surprising resilience, driven by AI-related capital investments and strong corporate earnings. The economy is projected to maintain resilient real GDP growth above 2% for the remainder of 2026. This should be sustained by robust artificial capital expenditures and steady consumer spending, even as persistent energy inflation and elevated interest rates keep the Federal Reserve cautious. Housing is experiencing deeply sluggish activity with high mortgage rates hovering above 7% which have severely suppressed existing home sales. On the commercial front, we see standard commercial office real estate remaining weak, whereas industrial real estate tied to data center infrastructure is heavily outperforming.

Sales and Spending –The expected August rebound in retail sales turned out to be unexpectedly strong. Sales excluding motor vehicles and gasoline rose slightly, with all categories showing good growth. Notable rises were gains by e-commerce, a jump at miscellaneous stores, a gain at electronics and appliance stores, and a gain in sporting goods and hobby stores. Restaurant sales have been climbing strongly for five months in a row, rising nicely in August. The fly in the ointment: Rising gasoline prices may be a drag on retail sales this fall. Savings rates are low, and households may need to rebuild their bank accounts by curbing their discretionary spending. The Federal Reserve's decision to start raising short-term rates will also have some effect since it raises rates for borrowing from home equity lines of credit. However, consumers keep surprising analysis with their willingness to spend, despite consumer sentiment measures that keep trending down. Perhaps the lingering effects of past stock market gains are enabling higher-income households to power through this period of uncertainty. (see chart below)

Consumer Spending over 3 years



Sourced from: *tradingeconomics.com United States Consumer Spending*

Inflation – Inflation in August returned to an uncomfortably high rate from the prior month. Higher gasoline and fuel costs added to the pickup as well as the cost of groceries. Another category is airfares that saw an increase of around 3.0% because of the climb in jet fuel costs. We are seeing a rise in most consumer goods. One area that we did see a decline is medical care, which actually declined slightly. The price of energy is likely to remain high with the situation in the Middle East unresolved. With the average price of diesel now above \$6 per gallon, and higher still in some states, this cost will begin to filter into goods prices, giving a small boost to overall inflation. Food prices may come under new pressure at some point in the future, as one-third of the world's fertilizer is produced in the Persian Gulf region. The Federal Reserve will likely not cut interest rates at its policy meeting in October.

Monetary Policy comprises the Federal Reserve's actions and communications to promote maximum employment, stable prices and moderate long-term interest rates. The Federal Reserve has eight meetings a year starting in January. The next couple of meetings are scheduled for October 28 and December 9. The current U.S. monetary policy stance is restrictive but aimed at balancing economic stability, targeting a fed funds rate in the range of 3.75%-4.00%. The FOMC raised the benchmark interest rate by 25 basis points at its most recent meeting on September 16. This action marked the first rate hike since 2023 and was implemented by the committee to curb persistent inflation pressures and steer it back down toward the Fed's 2% long term target. Another hike may be needed before year-end to combat persistent inflation.

Fiscal Policy As of mid-October 2026, US fiscal policy looks like this: deficits are large, the government is running on a stopgap, and the big decisions are waiting until after the November midterms. Gross national debt recently passed \$40 trillion, the government now spends more on annual interest than on defense, debt held by the public exceeds the size of the economy, and major trust funds face insolvency in under a decade. What we are watching: Congressional Budget Office's fuller FY2026 analysis next month, the Dec. 11 funding deadline, and whether the midterms change who controls the FY2027 spending and tax fights.

The Dollar In the short-term we expect to see the dollar stay firm at roughly current levels partly due to our expectation of no cuts until 2028. Furthermore, other major central banks have announced tightening schemes, which will provide market forces competing against the US dollar.

Corporate Profits are currently booming at historic highs, reaching an annualized record of \$4.83 trillion in the second quarter of 2026, according to recent data from the U.S. Bureau of Economic Analysis (BEA). This milestone marks a surge year over year, driven by resilient consumer spending, corporate windfalls from tariff refunds, and an aggressive AI infrastructure buildout.

MARKETS

Uncertainties U.S. economic uncertainty remains elevated in 2026, driven by a persistent inflation pressure, evolving monetary policy from the Federal Reserve, cooling job market, and questions regarding whether high stock valuations and AI investments are sustainable.

Positives The US economy in the third quarter of 2026 shows resilient mid-cycle growth, supported by steady consumer spending, robust capital expenditures in AI, and broadening equity market gains alongside a lowering perceived risk of an immediate downturn.

Negatives As of the third quarter of 2026, the economy has been characterized by persistent inflation above target, higher borrowing costs weighing on housing, and a cooling labor market characterized by cautious hiring and demand uncertainty represents key negative headwinds facing the US economy. The immediate negative is the conflict in the Middle East specifically with Iran which has triggered much volatility.

Interest Rates The Federal Reserve on September 16 raised its short-term interest rate by a quarter-point for the first time in three years, while Chairman Kevin Warsh's tough inflation talk at his press conference boosted long rates above 5.0%. Bond investors likely interpreted his words as a promise to raise rates more than they had expected over the next year. They will probably look to hike rates at its December meeting and are unlikely to rise at its October meeting since its around the midterm elections. The current 30-year home mortgage rate is hovering around 7.49%.

Common Stocks Wall Street YTD finished the first three quarters of 2026 with gains over 11.75%. During the quarter the stock market managed to finish with overall gains despite facing waves of volatility driven by rising crude oil prices, surging bond yields and ongoing geopolitical tensions in the Middle East. Indexes such as the S&P 500 and Nasdaq held up well as investors balanced concerns over sticky inflation with solid corporate earnings and steady economic growth. Even though higher treasury yields created pressures at times, resilient business profits and strong enthusiasm around technology infrastructure kept global equities close to their record highs by the end of September. We expect more volatility for stocks in the months ahead but remain optimistic. As always, we will remain patient and stick to the long-term plan as we navigate this ever-changing market.

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