QUARTER 3

MARKET OUTLOOK

AT A GLANCE

A more fragmented world is reshaping how markets price risk. AI remains the dominant growth engine, driving equity leadership and new bond issuance, while higher yields are restoring opportunity in fixed income. Across regions and asset classes, the message is the same: selectivity, discipline, and active management matter more.

ECONOMY

Global trade is being rewired as countries prioritize resilience, security, and strategic alignment over efficiency.

EQUITY

S&P 500: +10.19%
Mag 7: -1.74%
S&P 493: +15.53%

*as of 6/30/2026

FIXED INCOME

Bloomberg Agg: +0.62%
10-Year Yield: 4.55%
30-Year Yield: 4.95%

*as of 6/30/2026

"THE STRENGTH OF OUR WEALTH MANAGEMENT PROCESS COMES FROM BRINGING THE RIGHT EXPERTISE TOGETHER. INVESTMENTS, PLANNING, TRUST, BANKING, AND ADVISORY PROFESSIONALS WORK AS ONE TEAM TO HELP CLIENTS ADDRESS COMPLEXITY AND MOVE FORWARD WITH CONFIDENCE."

Dan L. Stevenson, CFA
EVP - President Wealth Management

GEOPOLITICS, FRAGMENTATION & THE NEED FOR SELECTIVITY

SUMMARY:

Geopolitical conflict and supply chain reorganization are reinforcing a less integrated global economy. The result is not the end of globalization, but a more fragmented version of it, one where country-level fundamentals, resource security, policy alignment, and supply chain resilience should play a larger role in determining risk premia, or the additional compensation investors demand for accepting uncertainty, volatility, or potential loss beyond what they could earn from a safer asset.

OUR PERSPECTIVE:

The world is moving from frictionless integration toward selective interdependence. Trade remains global, but governments and corporations are increasingly reassessing where critical production occurs, who controls essential inputs, and how much geopolitical risk is embedded in cross-border exposure. For investors, this argues for greater selectivity across regions, countries, sectors, currencies, and asset classes.

REORGANIZATION: A RETHINKING OF GLOBAL SUPPLY CHAINS

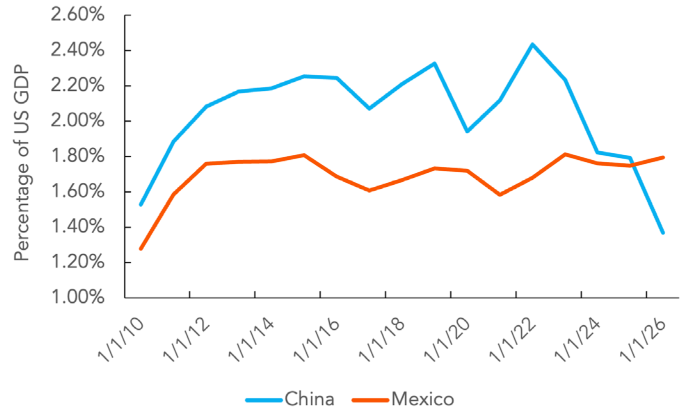
The immediate geopolitical focus remains the Strait of Hormuz, but the waterway is best understood as one part of a broader shift taking place across the global economy. The Iran War has disrupted energy logistics and trade routes while reminding investors that supply chains, transportation corridors, and funding markets remain vulnerable to geopolitical stress.

At the same time, the U.S. economy is less exposed to traditional oil shocks than it was in prior decades. Domestic energy production has improved materially, and oil-related spending now represents a smaller share of overall economic activity than during prior periods of energy stress. That does not mean energy no longer matters. It does. Higher energy prices can still affect inflation expectations, consumer sentiment, corporate margins, and monetary policy. But the transmission mechanism is different. The market impact may show up less through an immediate growth shock and more through inflation sensitivity, term premia, and country-level dispersion.

Put simply, the conflict highlights a world that is becoming less integrated and more fragmented.

Countries are reassessing their interdependence and increasingly organizing around political, economic, and strategic alliances. The processes of on-shoring, near-shoring, and friend-shoring have moved from corporate talking points to policy priorities. In the U.S., this shift has already produced a meaningful change in trade patterns. Previously dominated by China, U.S. imports have increasingly shifted toward Mexico, with the southern neighbor becoming America's largest trading partner earlier this year.

Composition of US Trade: China vs. Mexico



Source: Bloomberg

This is not solely a U.S. phenomenon. At the most recent G7 conference, the conversation also centered on reorganizing European trade away from China. The rationale is straightforward: as competition for critical minerals intensifies, China's control over key inputs has given the country significant pricing power and supply-chain influence. These concerns will continue to reshape trade relationships, capital flows, and the way countries think about economic security.

Technology may be the clearest example of how far this reordering has moved beyond traditional goods trade. The artificial intelligence infrastructure buildout depends on semiconductors, high-bandwidth memory, advanced networking equipment, data-center capacity, power availability, and critical minerals. These inputs are global, but not evenly distributed. As a result, the beneficiaries of this cycle are not confined to the United States, nor are the risks.

Supply chains have become a key macroeconomic and geopolitical consideration. Countries with access to critical resources, reliable trade partnerships, credible policy frameworks, and strategic relevance to AI and energy infrastructure may command lower risk premia over time. Countries more exposed to chokepoints, import dependency, fiscal instability, or policy uncertainty may require greater compensation from investors.

Fragmentation can redirect opportunity toward countries and sectors positioned to benefit from new trade routes, resource needs, and capital spending priorities. Select emerging markets, commodity exporters, and semiconductor-linked economies may benefit as production, capital spending, and trade relationships diversify. But the broader investment implication is that country-level dispersion should rise.

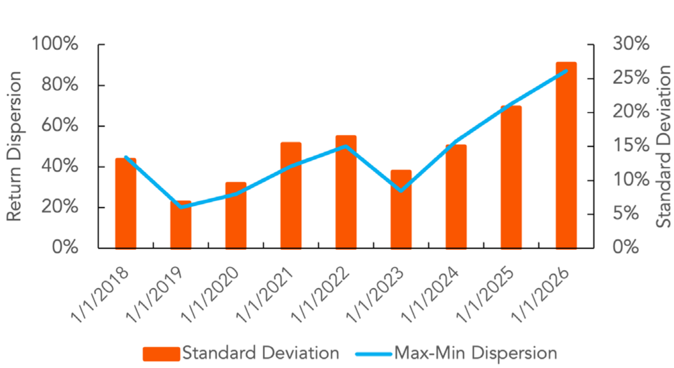
In a more fragmented world, it will matter less whether an investor owns "international" exposure in broad terms and more which countries, currencies, sectors, and supply chains they own specifically.

SELECTIVE INTERDEPENDENCE: THE NEW GLOBALIZATION

The next phase of globalization is unlikely to resemble the last one. The prior cycle was defined by low friction, expanding trade, and globally synchronized supply chains. The coming cycle appears more likely to favor redundancy, resilience, and regional alignment.

This implies that global trade will become more strategic. Governments will likely continue to protect industries that are sensitive to national security, secure access to critical resources, and prioritize supply-chain reliability over lowest-cost production. Corporations, in turn, will likely place greater value on certainty, proximity, and political alignment when making long-term capital decisions.

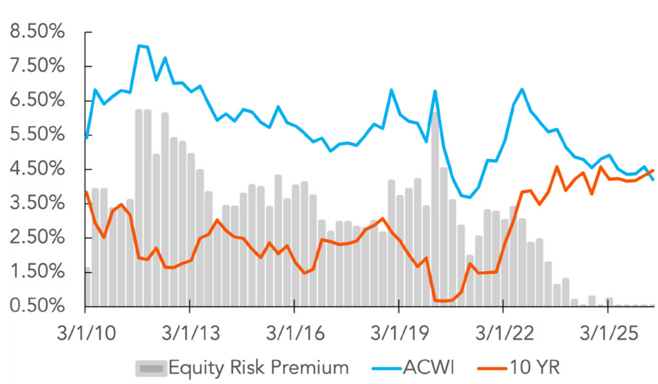
International Return Dispersion & Standard Deviation



Source: Bloomberg

For investors, this means risk premia should become more differentiated. Policy credibility, fiscal position, energy security, resource access, labor availability, currency stability, and geopolitical alignment are likely to matter more than they did in the prior era. That does not mean global diversification is less important. In fact, the opposite may be true. But diversification must become more intentional.

The Decline of the Equity Risk Premium



Source: Bloomberg

The same fragmentation that is changing trade flows is also changing the way investors price capital. Less reliable supply chains, greater energy uncertainty, larger fiscal deficits, and more capital-intensive technology investment all argue for a higher hurdle rate. In fixed income, that shows up through term premium, credit selection, and the need to be more conscious of duration and liquidity risk. In equities, it shows up through concentration risk, valuation discipline, and the need to distinguish between companies benefiting from the AI buildout and those merely attached to the narrative.

This is where selectivity becomes the common thread across asset classes. The AI infrastructure buildout may continue to support earnings growth and capital spending, but the winners are unlikely to be evenly distributed. Similarly, higher long-term yields may improve the return profile for fixed income investors, but only where compensation is adequate for the risks being taken.

CONCLUDING THOUGHTS

Taken together, fragmentation and compressed risk premia suggest the next phase of the cycle should reward discernment over indexing. Global exposure certainly has a role, but the benefit is likely to come less from owning everything and more from understanding where supply chains, policy choices, currencies, and capital costs are creating durable advantages, or exposing investors to underappreciated fragility.

In a world where risk premia are compressed and outcomes are becoming more differentiated, prudence is not about avoiding risk altogether. It is about being more deliberate about where risk is taken.

By Ryan Lange, CFA, CAIA, Chief Investment Officer, and Aakaash Raja, Intern

EQUITY

AI HOLDS CENTER STAGE AS MACRO RISKS TAKE A BACK SEAT

SUMMARY:

Despite macro and geopolitical headwinds, markets advance as AI infrastructure broadens beyond mega-cap tech.

OUR PERSPECTIVE:

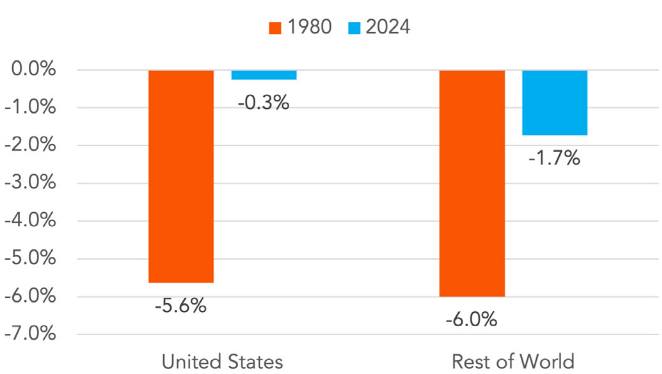
We remain constructive on AI's long-term opportunity, but after a historic run, execution matters more. Selectivity, valuation discipline, and concentration management are increasingly important.

MARKETS LOOK PAST THE NOISE

Despite a complicated economic and geopolitical backdrop, U.S. equity markets have continued to post double-digit returns in 2026. Sticky inflation, elevated rates, bond-market volatility, and renewed geopolitical conflict all have the potential to weigh on investor sentiment. Yet the S&P 500 is up about 10.2% year to date, while the Nasdaq 100 and Russell 2000 have delivered stronger gains. Rather than being derailed by macro uncertainty, markets have remained focused on one dominant theme: the buildout of artificial intelligence infrastructure.

One reason investors have been able to look past geopolitical stress is that oil shocks no longer transmit through the U.S. economy with the same force as in prior decades. In the 1970s and 1980s, the U.S. was far more dependent on foreign oil imports, making supply disruptions a direct threat to growth, inflation, and consumer spending. Today, the U.S. is in a much stronger energy position, producing significantly more of its own oil and exporting more energy than in past cycles. At the same time, oil and petroleum-related spending represents a smaller share of GDP than it did during prior energy shocks. Oil still matters, particularly for inflation expectations and market sentiment. Still, the U.S. economy is less exposed to a sustained growth shock than it was during earlier periods of geopolitical conflict.

Impact Effect of a 15% Oil Supply Disruption on Real GDP Growth



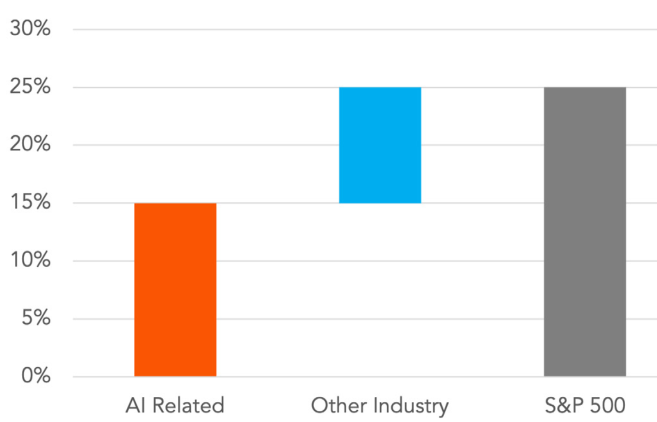
Source: Federal Reserve Bank of Dallas

AI REMAINS THE MARKET ENGINE

That structural resilience has allowed investors to focus on the more powerful market story: the AI infrastructure and semiconductor supercycle. The Philadelphia Semiconductor Index has been the clearest expression of this theme, rising roughly 80% year to date, compared with an approximately 10% gain for the S&P 500. The rally has been fueled by extraordinary demand for AI compute, high-bandwidth memory, advanced networking, semiconductor equipment, power infrastructure, and data-center capacity. In many ways, the market has shifted from rewarding the companies that first popularized AI to those that physically build it.

That shift is now showing directly in earnings as AI-related companies contributed 15 percentage points of the S&P 500's 25% EPS growth in 1Q2026, or about 60% of the total. Semiconductors and equipment remain the largest direct contributors. Still, the breadth of the contribution across hyperscalers, tech hardware, power, and data-center-related industries underscores that the AI trade has evolved from a narrow narrative into a broader earnings engine for the index.

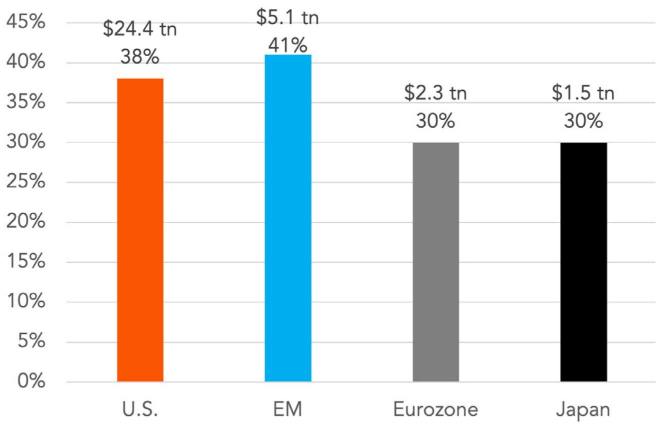
AI-Related Stocks Contribution to S&P 500 EPS Growth



Source: KKR GMAA

This leadership has also become less U.S.-centric. Emerging markets have benefited significantly from their exposure to the global semiconductor supply chain, particularly in Taiwan and South Korea. The MSCI Emerging Markets Index is up 21% year to date; nearly 70% of that return has been driven by just three semiconductor companies: Taiwan Semiconductor Manufacturing, Samsung Electronics, and SK Hynix. As a result, the U.S. is now sharing the AI stage with key foreign suppliers. However, that does not necessarily mean leadership has become more diversified. In fact, concentration within emerging markets now looks eerily similar to the concentration investors have wrestled with in the S&P 500 over the last several years.

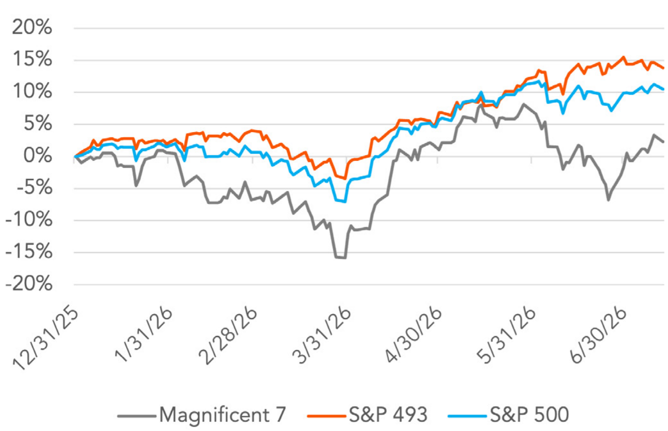
Top 10 Companies in Regional Indices



Source: JPMorgan Chase

Within the U.S. market, the leadership profile has also changed. The Magnificent Seven, which dominated the early and mid-2020s, have been essentially flat year to date. Meanwhile, the S&P 493 has outpaced the headline S&P 500, and small caps have nearly doubled the S&P 500's return. This is a meaningful shift. The downstream effects of the AI buildout are beginning to permeate through the broader market, benefiting memory providers, equipment manufacturers, networking companies, data-center infrastructure firms, utilities, industrials, and other companies tied to the physical expansion of AI capacity.

S&P 500 Decomposed Returns



Source: Bloomberg

BALANCING OPPORTUNITY AND RISK

Other macro tailwinds are supporting the broadening. Expectations for eventual rate cuts, fiscal and tax policy support, improving earnings growth, and renewed capital markets activity have helped lift sentiment beyond the largest technology names. But the core driver remains the same theme we have discussed over the last several quarters: AI is broadening from a narrow mega-cap growth story into a wider infrastructure and capital-spending cycle.

The reopening of the IPO market reinforces that point. After several years in which many high-growth companies were forced behind the private-market curtain, public market demand has returned for businesses tied to AI, compute, and innovation. Cerebras gave the public a direct way to access AI chip architecture, while SpaceX's public debut reflected a broader appetite for large, capital-intensive innovation platforms. These IPOs are not the primary driver of index performance, but they are important signals. Strong demand for these offerings suggests that investors are once again willing to fund long-duration growth stories, particularly those tied to AI infrastructure, compute scarcity, or next-generation technology platforms.

Still, the AI narrative is not without risk. As highlighted in our opening commentary, global economic segregation and increasing consolidation among leading companies in the AI ecosystem have significantly narrowed equity risk premia worldwide. The semiconductor rally has, of late, shown some signs of fatigue. Chip stocks sold off sharply in early July as investors questioned whether valuations had run too far ahead of fundamentals. Momentum strategies also experienced a meaningful reversal, a reminder that crowded trades can unwind quickly even when the underlying theme remains intact.

The next phase of the AI cycle will likely be more selective. Companies will need to prove that today's capital spending can translate into durable revenue growth, attractive margins, and real returns on invested capital.

The key risks are clear: elevated valuations, power constraints, data center capacity limitations, supply chain bottlenecks, export controls, customer concentration, and uncertainty around the ultimate monetization of AI. The buildout is real, but not every company tied to the theme will be a long-term winner.

The bottom line is that AI infrastructure has delivered earnings and revenue surprises large enough to overwhelm macro and geopolitical noise. The question now is whether that fundamental support can sustain valuations after a historic run. We remain constructive on the long-term AI opportunity, but the market is moving from pricing in promise to pricing in execution. That argues for staying invested, but with greater selectivity, discipline, and attention to concentration risk.

By Jake Stapleton, MBA, Team Lead–Research, and
Hunter Bukowy, Portfolio Implementation Analyst

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LONG-TERM YIELDS, AI DEBT ISSUANCE & THE CASE FOR ACTIVE MANAGEMENT

SUMMARY:

Higher long-term yields and hyperscalers' bond issuance are reshaping fixed income, creating volatility and opportunity. Active management is critical in balancing duration, credit selectivity, and diversification.

OUR PERSPECTIVE:

Two themes have stood out in fixed income markets over the past quarter. First, long-term Treasury yields moved sharply higher as markets reassessed inflation risk following the energy shock tied to the Iran War and a Federal Reserve that has sounded more hawkish than investors initially expected under Chair Kevin Warsh. Second, the corporate bond market has been absorbing significant new issuance from large technology companies and hyperscalers to fund the buildout of artificial intelligence infrastructure.

These developments fit within the broader framework discussed earlier in this outlook. A more fragmented global economy, less synchronized policy environment, and greater geopolitical uncertainty should result in higher risk premia across markets. For fixed income investors, that means the opportunity set may be improving, but so too is the need to be selective about where to take duration, credit, liquidity, and currency risks.

Together, these themes reinforce why we believe investors should remain active, selective, and nimble.

THE LONG END HAS REPRICED

The most visible sign of recent volatility has been the move in long-term Treasury yields. The 30-year Treasury yield reached 5.18% on May 19, 2026, its highest level since the Global Financial Crisis. Long-duration bonds are more sensitive to changes in interest rates, which can be painful when yields rise, but that same sensitivity can create opportunity when yields appear to have moved too far, too fast.

10- & 30-Year Treasury Yields

Source: Bloomberg

The move toward 5.2% on the 30-year Treasury reflected several concerns. Markets were pricing the possibility that inflation may prove more persistent if the Iran War remains unresolved, that fiscal deficits may keep Treasury supply elevated, and that investors may demand a higher term premium—the extra compensation investors require to hold longer-duration Treasuries. The CBO projects a federal deficit of $1.9 trillion in fiscal 2026 and federal debt rising to 120% of GDP by 2036, which helps explain why markets remain focused on long-term Treasury supply and fiscal sustainability.

Federal Reserve communication has also mattered. At the June FOMC meeting, the Committee kept the target range for the federal funds rate at 3.50% to 3.75%. It noted that inflation remained elevated relative to its 2% objective, partly due to supply shocks including energy. The statement also emphasized that the Committee "will deliver price stability," language that contributed to the perception that Warsh may be more hawkish than some investors initially expected. The June projections also showed the median 2026 federal funds rate rising to 3.8%, up from 3.4% in the March projection, suggesting the possibility of a higher policy-rate path than markets previously anticipated.

This is where active fixed income management matters. We viewed the move in the 30-year Treasury yield toward 5.2% as a tactical opportunity to add long-duration Treasury exposure within portfolio strategies. If yields mean-revert lower, long-duration Treasury exposure should benefit. That said, risk must be controlled through position sizing, as long-duration Treasuries can remain volatile and depreciate meaningfully if yields continue to rise. Still, today's higher long-term yields create a more attractive total return setup than existed when yields were much lower. Investors are being paid more in income while also gaining potential price appreciation if yields decline.

HYPERSCALER BOND ISSUANCE IS CHANGING CORPORATE BOND MARKETS

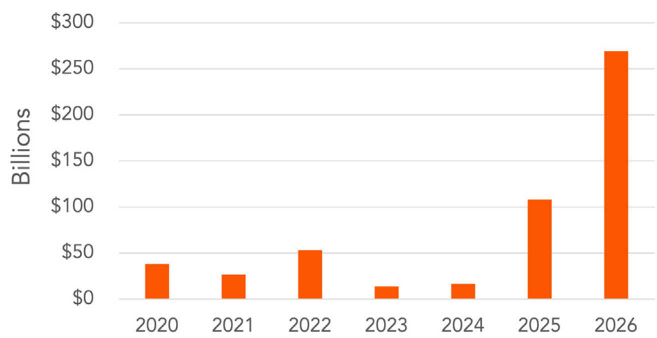
The second major development has been the surge in debt issuance from technology companies and hyperscalers to fund AI-related capital investment. The AI buildout is capital-intensive. Data centers, chips, servers, networking equipment, and energy infrastructure require enormous investment.

Global equity indices have become increasingly concentrated in a relatively small group of firms that are leading the AI infrastructure buildout. What is now becoming clearer is that this concentration is no longer confined to equity markets.

Many hyperscalers, including Alphabet, Amazon, Meta, Nvidia, Oracle, and SpaceX, initially funded this buildout using existing cash flow. Increasingly, however, that investment is being financed through the bond market. As these companies increasingly fund capital expenditures through debt issuance, AI exposure is becoming more visible inside fixed income benchmarks.

Hyperscalers have issued nearly $270 billion in bonds so far in 2026, already more than double their 2025 gross issuance of just under $110 billion. Much of that issuance has been long-term, which brings more duration sensitivity and potential price volatility. Large issuance can also pressure valuations. When the market has to absorb a significant amount of new supply, issuers may need to offer higher yields or wider spreads to attract buyers. Credit spreads—the additional yield investors receive over Treasuries—have widened for hyperscalers as markets digest the supply and weigh uncertainty around project payoffs.

Hyperscaler Bond Issuance

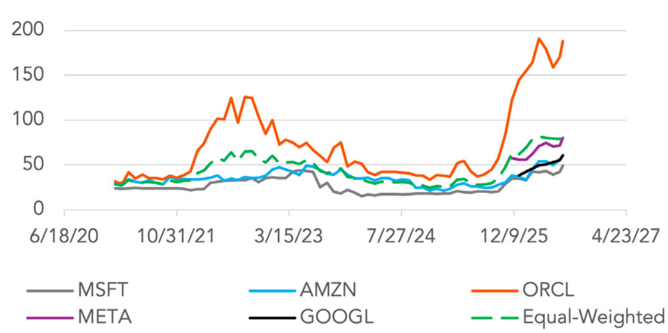


Source: Bloomberg

This matters because the more debt an issuer has outstanding, the larger its presence can become in bond indexes. As large technology companies and hyperscalers borrow more, the composition of investment-grade benchmarks may gradually change. Investors may find themselves exposed to AI not only through their equity portfolios but also through their fixed income allocations.

That can create price pressure for existing bonds, but it can also create opportunity. If high-quality companies with strong balance sheets come to market at more attractive spread levels, investors may be better compensated for taking credit risk.

CDS Spreads for Hyperscalers (bps)



Source: Bloomberg

The key is selectivity. Large issuance and uncertainty around AI monetization can pressure hyperscaler bonds and fixed income indexes, but dislocation can also create opportunities. In our view, the goal is not simply to own the benchmark exposure as it changes, but to evaluate where investors are being appropriately compensated for the risks being taken.

WHY ACTIVE MANAGEMENT MATTERS

This environment favors a more active approach to fixed income. The opportunity set is shifting across duration, credit quality, sectors, and maturity ranges. Short-term rates still provide income, while long-duration bonds may offer appreciation potential if yields decline. Corporate credit may also become more attractive on a relative basis if heightened issuance creates better valuations. Each opportunity carries a different risk profile, which makes discipline and flexibility important.

For accounts invested in our strategies, nimbleness remains central to how we manage fixed income. Strategies can adjust as conditions change, whether that means emphasizing short duration, adding long duration when yields move too far, or selectively adding corporate credit when valuations become more attractive, or looking beyond traditional markets to alternative assets like infrastructure and insurance-linked notes. This dynamic approach is difficult to replicate with a static portfolio or individual bonds.

We continue to evaluate the fixed income market through the same disciplined lens we have always used. As a team, we are focused on where investors are being paid appropriately, where risks are attractive, and where we can improve portfolio outcomes. In a more fragmented world, that means being willing to invest beyond traditional markets, particularly where correlations between asset classes and regions remain lower, and diversification can still provide meaningful portfolio benefits. It also means remaining prepared to become more defensive if risk premia fail to compensate investors for the uncertainty ahead adequately. In today's fixed income market, being dynamic is not merely useful; it is necessary.

By Nicholas Hinkebein, CFA, CFP®
Senior Portfolio Manager

WELCOME TO MIDLAND!

Please join us in welcoming:

Laura Palmisano Graham – Senior Trust Officer

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QUARTER 3

MARKET OUTLOOK

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