MAINSTREET ADVISORS

Second Quarter 2026

Quarterly Market Insights



SPRING SENTIMENT SHIFT

EXECUTIVE SUMMARY

- S&P 500 surges 15% amid easing US-Iran tensions
- Elevated inflation but limited wage pressure
- Warsh Era likely to begin with holding period
- "Real Economy" shows momentum
- Midterms: more noise than signal

Market psychology improved in the second quarter, as war-driven anxiety in the late-winter dissipated and a wave of spring optimism emerged. The S&P 500 delivered an impressive 15.2% total return in the period, marking the benchmark's strongest quarterly showing since 2020 and completely erasing its 9% pullback in the first quarter. This relentless buying pressure culminated in the S&P 500 logging nine consecutive weekly gains from late March through the end of May, surging nearly 20% off its low to close at 7,580 on May 29—30% higher than one year ago. During this stretch, the benchmark recorded 20 new all-time closing highs. Since 1985, the index has put together a nine-week winning streak just four other times. Historically, after these hot streaks ended, the S&P 500 averaged a 3.9% return over the next six months and a 9.3% return over the following 12 months.

The primary catalyst for this risk-on surge was the emergence of credible pathways toward a resolution in the U.S.–Iran conflict in April and May, which stabilized global crude oil prices. In a classic example of the market front-running geopolitical headlines, the S&P 500 bottomed on March 30, just eight days before West Texas Intermediate (WTI) crude recorded its daily closing high during the quarter of $112.95 per barrel (see Chart 1).

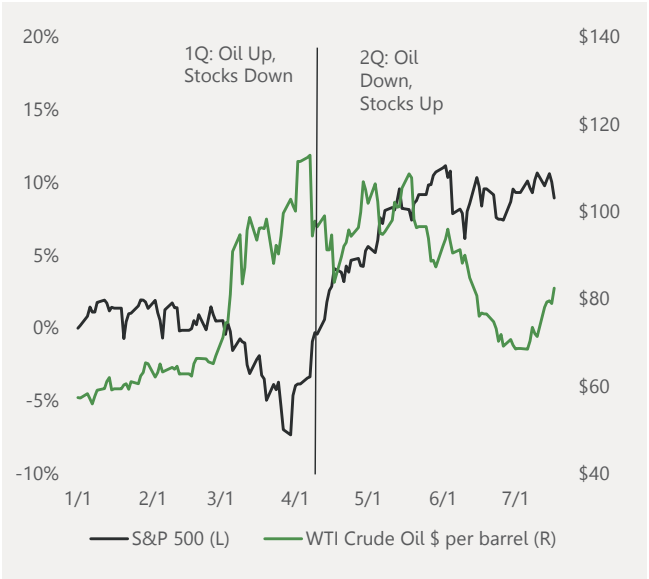
Corporate fundamentals strongly reinforced the geopolitical relief rally. The first-quarter earnings season delivered exceptional results, characterized by an S&P 500 year-over-year profit growth rate of 28%, significantly outstripping the 13%–14% expansion expected by analysts in early April. Capital markets activity also took center stage, highlighted by high-profile corporate actions and heavy investor focus on the IPO calendar. Primary equity offerings reached historic proportions, headlined by SpaceX's (SPCX) historic $86 billion launch and Alphabet's (GOOGL) massive $85 billion secondary issuance.

U.S. Large Cap Sector Leaderboard
Under the surface, U.S. equity market sector leadership underwent a complete transformation from the previous quarter. Technology (+31.8%) led all sectors, propelled by relentless demand for artificial intelligence infrastructure and robust data center capital expenditure. This massive upcycle in memory and storage stocks easily overshadowed lingering pockets of weakness in enterprise software. The semiconductor space was the crown jewel of this buildout; in April, the Philadelphia Stock Exchange Semiconductor Index recorded an extraordinary 18-day rally, marking its longest winning streak in history. Bloomberg projects that semiconductor earnings will grow nearly 60% in 2026, easily outstripping the broader technology sector. Conversely, energy (-13.5%) and utilities (-0.5%) sat on the other side of the ledger as the quarter's weakest S&P 500 groups, hindered by a sharp drop in energy commodity prices and an aggressive rotation away from defensive styles.

Widening the Lens
Across size and style categories, U.S. small-cap stocks experienced an upward re-rating as the Russell 2000 surged 21%, driven by improving earnings expectations and broader risk-on sentiment. Emerging market equities were among the strongest performers globally, with the MSCI EM index advancing 23%, led by technology-heavy markets like Taiwan and South Korea due to their central roles in the global AI semiconductor supply chain.

Fixed income markets painted a more complex picture. Yields on the benchmark 10-year U.S. Treasury note trended higher, opening the period at 4.32% and finishing at 4.46%. They touched a 17-month intraday high of 4.68% on May 19 before cooling over the final six weeks of the quarter. The U.S. Treasury yield curve experienced a bear flattening, driven by the

CHART 1
Stocks Front-Ran the Oil Price Peak



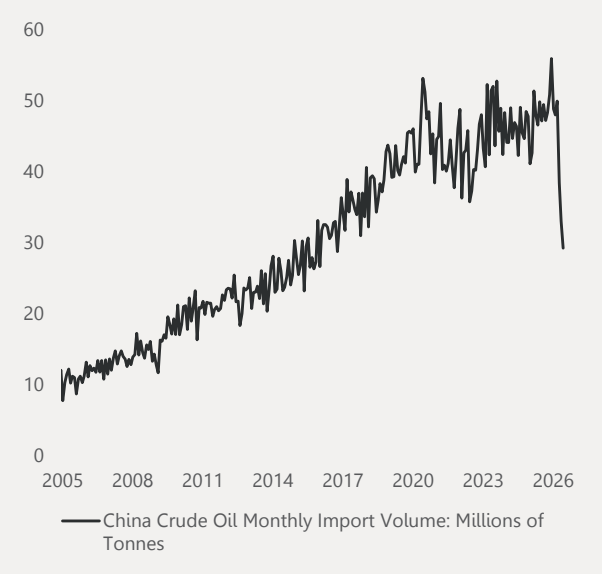
Bloomberg. Data as of 6/30/26. Past performance does not guarantee future results.

short-end as the market priced in a more restrictive monetary policy path. A significant spike in rate volatility occurred in mid-May as global bonds sold off amid elevated oil prices and a sharp rise in UK gilt yields, briefly pushing the 30-year U.S. bond yield past the 5% threshold.

Economic Data Trends
The underlying economic backdrop remained supportive of growth despite yield pressures. We would characterize the labor market as balanced, with the unemployment rate holding around 4.3%, steady continuing weekly jobless claims, and a job openings-to-unemployed persons ratio near 1. Consumer spending was once again resilient, as U.S. retail sales rose by an average of 1.1% per month from March through May, bolstered by robust tax refunds and a rebounding stock market. On the inflation front, three straight elevated monthly consumer price index (CPI) readings in March, April, and May were driven by the war-related surge in energy prices, but were followed by a highly welcomed, sharp drop-off in June.

Against this backdrop of solid economic data and volatile energy metrics, the Federal Open Market Committee kept its policy rate unchanged in the 3.50%–3.75% range. However, their communications bias shifted decisively from dovish to hawkish. In his first major quarter steering policy, new Fed Chair Kevin Warsh explicitly emphasized that policymakers are intensely focused on achieving their structural 2% inflation target.

CHART 2
China: Getting By on Their Own Supply



Bloomberg. Data as of 6/30/26. Past performance does not guarantee future results.

From Blockade to Breakthrough?
The second quarter saw U.S.–Iran hostilities pivot from violent escalation to high-level diplomacy, culminating in a signed interim agreement before deteriorating at quarter's end. The quarter opened with a fragile, two-week truce announced by President Trump on April 7–8, brokered by Pakistan. Subsequent talks in Islamabad between U.S. Vice President Vance and Iranian representatives ended without a deal, prompting the U.S. to implement a naval blockade on Iran's ports on April 13 to force concessions regarding the Strait of Hormuz. Though the initial truce expired, President Trump extended the U.S. ceasefire indefinitely to allow backchannel negotiations with Iran to develop.

By late May, diplomatic efforts facilitated by Qatar and Pakistan bore fruit. On May 29, both nations reached a preliminary 60-day ceasefire extension to protect maritime traffic in the Strait and address Iran's nuclear program, providing a major boost to global risk assets. Breakthrough momentum accelerated in June. On June 17, the U.S. and Iran signed a landmark 14-point Memorandum of Understanding (MoU) in Islamabad. The interim deal formalized a regional ceasefire, lifted the U.S. naval blockade, reopened the Strait of Hormuz, and granted Iran a 60-day oil sanctions waiver in exchange for nuclear compromises.

High-level peace talks subsequently shifted to Switzerland on June 21 to establish technical-level terms. However, during a second round of technical talks on June 28, deep disputes surfaced over policing mechanisms in the Strait and whether the truce applied to fighting in Lebanon. This foreshadowed renewed friction heading into July.

Relief Valves: How Oil Prices Were Contained
Despite fears of a catastrophic energy spike due to the Strait of Hormuz closure, crude oil prices remained remarkably contained during the second quarter. A powerful combination of non-OPEC production surges, aggressive inventory drawdowns, logistical rerouting, and structural demand rationing effectively absorbed the geopolitical shock.

Record-high domestic production in the United States, alongside expanding Atlantic Basin supply from non-OPEC producers in the Americas and West Africa, added massive physical cargoes to global markets independent of the Persian Gulf. Simultaneously, the U.S. government tapped the Strategic Petroleum Reserve (SPR) aggressively to blunt the price surge. Following a cumulative draw of over 104 million barrels since late February, the SPR fell to 311.4 million barrels by mid-July, which marked a 43-year low. This provided critical liquidity to refiners when supply chains were most fragile.

Saudi Arabia acted as a primary logistical anchor by maximizing its 1,200-kilometer East-West Pipeline. Aramco pushed operational throughput to its maximum capacity of 7 million barrels per day (bpd), surging Red Sea exports out of Yanbu to 5 million bpd and bypassing the Strait of Hormuz for 85% of its crude trade.

At the same time, China acted as a critical economic pressure valve by drastically curbing spot market purchases (See Chart 2). Beijing slashed its seaborne crude imports from a pre-war baseline of 11 million bpd down to an 8-to-10-year low of 6.4–7.8 million bpd, accounting for nearly three-quarters of the global trade contraction. China was uniquely positioned to execute this strategy due to its multiyear buildout of petroleum reserves.

The EIA estimates that China entered 2026 holding 1.4 billion barrels in total crude reserves (up 25% year-over-year), including an estimated 1 billion barrels in commercial inventories. For context, this is more than double the 411 million barrels held commercially in the U.S. By drawing down these massive stockpiles and benefiting from rapid domestic electrification China effectively temporarily starved the global spot market of demand.

Inflation and Wages: 2026 is not 2022

While built-in cushions and rerouted supply chains helped prevent a debilitating energy price spike, the temporary surge in crude oil inevitably triggered investor muscle memory of 2022. However, analyzing the macro backdrop reveals that today's economy is fundamentally different. In 2022, energy shocks arrived in an economy already plagued by severe post-COVID supply bottlenecks, depleted inventories, and an emerging wage-price spiral. Today, global supply chains have normalized, goods inventories are healthier, and the underlying labor market is far more balanced. As seen in Chart 3, average hourly earnings growth has cooled from near 7% in 2022 to a pre-pandemic trend near 3%, while the ratio of job openings to unemployed workers has fallen below one. Because wage growth (not short-lasting energy spikes) tends to drive persistent inflation, we think the risk of a 1970s-style wage-price spiral remains low. Furthermore, record domestic oil production and reduced energy intensity per dollar of U.S. GDP provide structural cushions that were absent four years ago.

These core differences have major implications for the likely paths of monetary policy and corporate health. Rather than embarking on the aggressive, profit margin-crushing rate hikes of 2022, the Federal Reserve can afford to maintain a patient, watchful stance. Corporate earnings are currently accelerating from a position of fundamental strength, unlike in 2022 when profit margins were peaking. Consequently, we think elevated oil prices are more appropriately viewed as a manageable headwind within an expansion, rather than an accelerant on an inflation fire.

Fed Policy: The Warsh Era Begins

The second quarter marked a changing of the guard for U.S. monetary policy as Kevin Warsh became the 17th chair of the Federal Reserve on May 22. The quarter began with a divided April Federal Open Market Committee (FOMC) meeting, where three regional Fed Presidents dissented against an easing bias in the group's official statement.

By late June, the FOMC seemed to be less divided with a moderately hawkish stance. At the June 16–17 FOMC meeting, officials unanimously voted to hold the benchmark rate steady at 3.50%–3.75%, while updated economic projections revealed that half the committee now anticipates at least one rate hike by the end of 2026. Fed funds futures quickly adjusted, fully pricing in a rate increase by year-end and driving short-term Treasury yields higher.

The June meeting will be remembered less for the rate hold and more for new Fed Chair Warsh placing his stamp on the institution. In his debut press conference, Warsh unveiled a stylistic break from the Powell era, stripping out traditional forward guidance, shortening the policy statement, and reiterating an uncompromising commitment to the Fed's 2% inflation target. Crucially, Warsh noted that outside of housing, it remains "hard to say policy is restrictive."

Signaling a comprehensive operational overhaul, Warsh launched five internal task forces to review policy communications (including the dot plot), the $6.6 trillion balance sheet, inflation drivers, productivity, and economic data sources. Notably, Warsh cautioned that traditional metrics might be an "echo of history," advocating for real-time data inputs instead.

While financial markets have abandoned hopes for near-term rate cuts and began pricing in a "higher-for-longer" environment, we do not see the Warsh-led Fed being in a rush to aggressively hike rates either. Instead, the "Warsh Era" opens with a data-dependent central bank determined to anchor

CHART 3

Job Market is not an Inflation Factor



Bureau of Labor Statistics. Data as of 6/30/26. Past performance does not guarantee future results.

inflation expectations, while exploring ways to reshape how monetary policy is conducted and communicated.

Real Economy Rumblings
Beyond the headlines surrounding the leadership change at the Fed, encouraging signs of organic growth are emerging from U.S. factory floors and cyclical supply chains. Following an extended slowdown in goods-producing and trade-sensitive sectors from 2022 to 2025, factory activity and cyclical hiring are showing clear signs of stabilization and renewed momentum.

The Institute for Supply Management (ISM) manufacturing gauge rose 1.3 points in May to 54, marking the fastest pace of expansion in four years. The index notched a sixth straight month with an expansionary reading above 50 in June. Importantly, this strength looks like it's being propelled by genuine end-demand rather than mere precautionary inventory building. New orders growth accelerated to a four-month high alongside gaining production steam, with broad-based growth reported across nearly every manufacturing industry—from electrical equipment to chemical products.

Hiring in transportation and warehousing, one of the clearest real-time indicators of goods movement and inventory activity, has rebounded sharply from late-2025 weakness. Retail trade hiring has also turned positive again, while couriers & messengers, another sector closely tied to e-commerce and consumer demand, has begun to show signs of life. Construction and manufacturing payrolls have shown fewer signs of picking up steam, but remain comparatively firm, suggesting underlying resilience in domestic investment activity.

Taken together, the recent improvement across these cyclical categories points to a broader firming in economic activity beyond the defensive sectors like healthcare, education, and social assistance that had dominated job growth earlier in the cycle. While gains remain modest by historical standards, the breadth of improvement suggests recession risks may be easing rather than intensifying (See Chart 4).

Is a Rotation Bubbling Under the Surface?
While cyclical employment and real-economy indicators reflect a stabilizing fundamental backdrop, financial markets are signaling a similar broadening beneath the headline indexes. A distinct market rotation gathered steam in June, as U.S. small caps, value stocks, and international equities began outperforming mega-cap technology. Year-to-date, the Russell 2000's 21.8% gain leads the S&P 500, while the "Magnificent Seven" has entered a consolidation phase. Rather than economic de-risking, this shift points toward a potential "reflation" trade resulting in a rotation into cyclical sectors positioned to benefit from accelerating global growth.

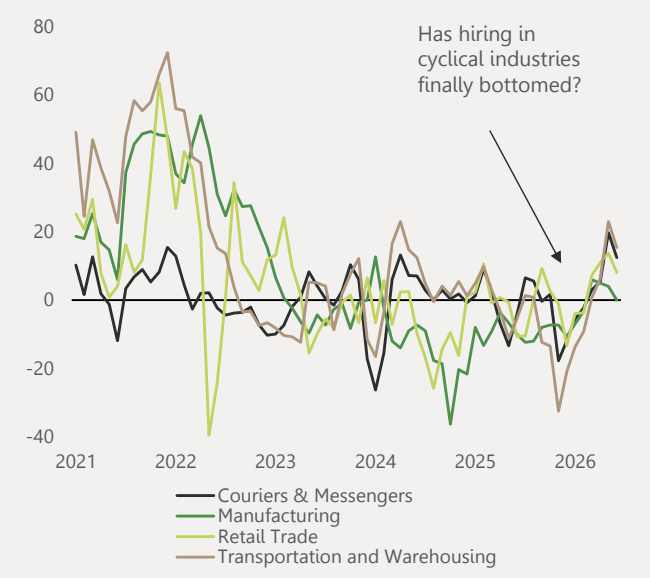
Value stocks are particularly sensitive to expanding global trade. Neuberger Berman estimates the earnings sensitivity to global trade volume across the Russell 1000 Value Index is roughly 1.2, compared to 0.8 for growth stocks. Value companies also tend to be shorter-duration assets, generating profits nearer-term and holding less sensitivity to rate fluctuations. Additionally, value stocks may disproportionately benefit from AI efficiency gains; because value firms typically carry higher debt and lower operating margins, every dollar saved via automation translates into a larger relative earnings boost.

In June, ETFs that track biotechnology companies and regional banks notably broke away from broad market performance. Historically, these two are among the most sensitive groups of stocks to interest rates and growth. The former has been fueled by a wave of biopharma M&A and IPO activity. The latter has benefited from improving credit metrics, resilient net interest margins, and industry consolidation.

For most of the last three years, we have discussed the elevated concentration of leadership within the S&P 500 Index, where 10 to 20 stocks accounted for a majority of the benchmark's returns. In our view, this nascent June-July rotation represents a healthy broadening of market participation as investors lighten up on the AI infrastructure winners and rediscover other areas of the market with differentiated catalysts.

Equity Fundraising Comes Alive
2026 has witnessed a resurgence in U.S. equity capital markets, with total issuance in the first half of the year exceeding the

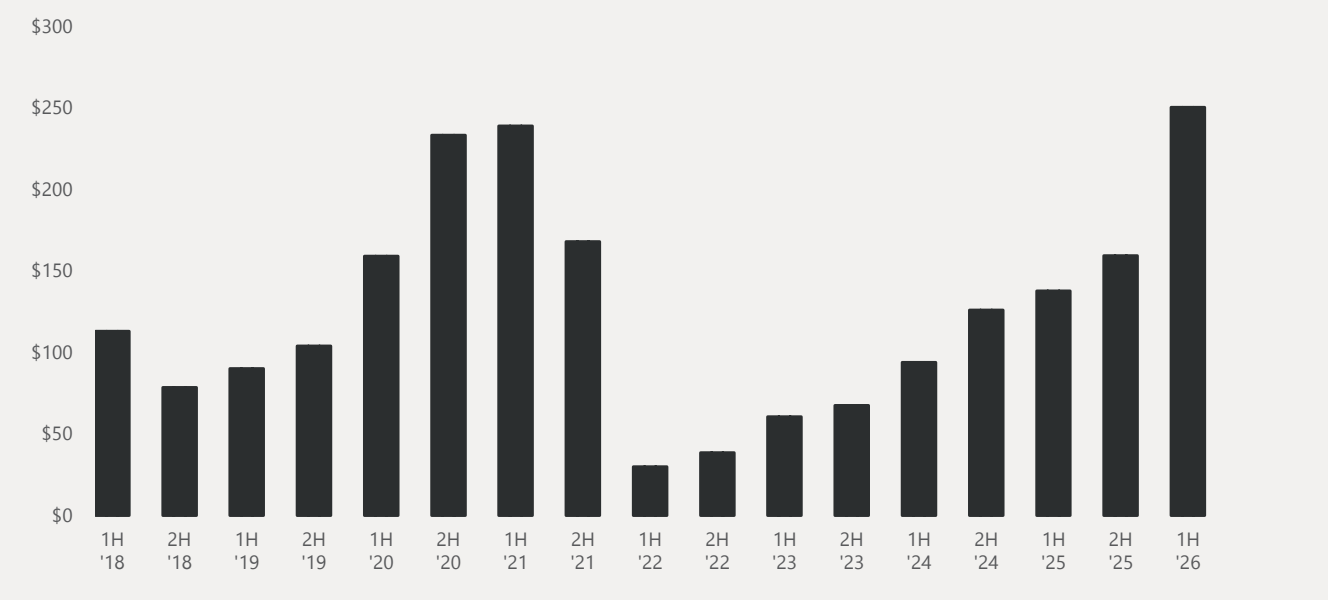
CHART 4
Signs of Life in the Real Economy?



Bureau of Labor Statistics. Data as of 6/30/26. Past performance does not guarantee future results.

CHART 5

Equity Issuance Picks up Steam



Bloomberg. Data as of 6/30/26. Past performance does not guarantee future results.

second half of 2020 and the first half of 2021. Driven by massive structural capital needs and a wave of high-profile debuts, the fundraising market is experiencing its most vibrant window in five years. As seen in Chart 5, U.S. equity issuance exceeded $250 billion in the first six months of the year.

The relentless expansion of the AI infrastructure buildout to satisfy computing demand has been the primary driver of this capital rush. Hyperscalers and technology companies are rapidly turning to the equity and convertible debt markets to fund massive projects, like Meta Platforms' (META) $50 billion data center in Lake Parish, Louisiana. Notable transactions include Alphabet's $85 billion secondary share offering, South Korean memory chip giant SK Hynix's $26 billion ADR listing, and U.S. AI semiconductor firm Cerebras Systems' (CBRS) $6 billion public debut.

Looking ahead, investment bankers are likely preparing to front-load a significant pipeline of deals into the summer months. With a Federal Reserve talking about potential rate hikes and a new Congress being elected in November, issuers are probably looking to price deals in Q3 to avoid potential market volatility in the fall.

SpaceX IPO: To Infinity and Beyond

Throughout May and June, equity market sentiment was heavily influenced by the blockbuster initial public offering of Elon Musk's SpaceX (SPCX). The company raised $75 billion in core equity—expanding to a total transaction size of $85.7 billion upon full exercise of the overallotment option—officially setting the record for the largest IPO in history.

The public debut highlighted SPCX's evolution from a pure rocket manufacturer into a deeply diversified technology conglomerate. Starlink and connectivity services remain the primary commercial profit engine, accounting for approximately 60% of FY25 revenue, while the launch infrastructure segment continues to secure long-term cost advantages through Starship reusability. The company's newest growth narrative centers on AI infrastructure and compute, spanning xAI, Grok, the Colossus data center, and orbital computing concepts.

Priced at $135 per share, SPCX raised $75 billion in core equity at an implied $1.77 trillion valuation, before secondary trading pushed its market capitalization near $2.5 trillion. Valuation debates remain sharp: bears highlight a steep trailing 12-month sales multiple of roughly 130-times against 2025 revenue of $18.67 billion and a $4.94 billion net loss amid massive capital expenditures. Conversely, bulls argue that forward compute contracts compress the operational multiple nearer to 40-times expected sales, with Starlink's cash flows acting as the primary engine to fund the capital-intensive AI buildout.

Setting valuation aside, passive capital flows will dictate much of the stock's near-term trading volume. Fast-track provisions allow index providers like FTSE Russell, MSCI, and Nasdaq

to include SpaceX within one to three weeks of the IPO. However, S&P Dow Jones maintains its requirement for one year of seasoned trading alongside strict profitability criteria. Because the initial free float represents only about 5% of total shares, SpaceX's initial index weights will remain modest between 0.25% and 1.00%. As insider lock-ups expire over the next 12 months, the stock's float will expand substantially. If the 60% of its float not owned by Musk unlocks by mid-2027, SPCX would represent roughly 2% of the S&P 500, positioning it as a top-10 holding in the benchmark.

Midterm Musings

On November 3, 2026, voters will decide all 435 House seats and 35 Senate seats, potentially reshaping the balance of power during the final two years of President Donald Trump's second term. Republicans currently hold narrow majorities in both chambers, but lack the 60-vote Senate threshold required to easily pass non-budgetary legislation. Prediction markets currently project Democrats will reclaim the House, while the Senate remains a toss-up.

Historically, midterm election years exhibit higher volatility and lower average returns prior to the polls opening. Research from U.S. Bank reveals that from 1900 through 2025, in the 12 months preceding a midterm, the U.S. stock market* has averaged a 2.9% return.This is well below the 8.9% average across all non-midterm years amid elevated policy uncertainty and shifting regulatory expectations. From November 3, 2025 through July 17, 2026, the S&P 500 is up about 9%, trending above the 2.9% average return in the 12 months preceding midterm elections.

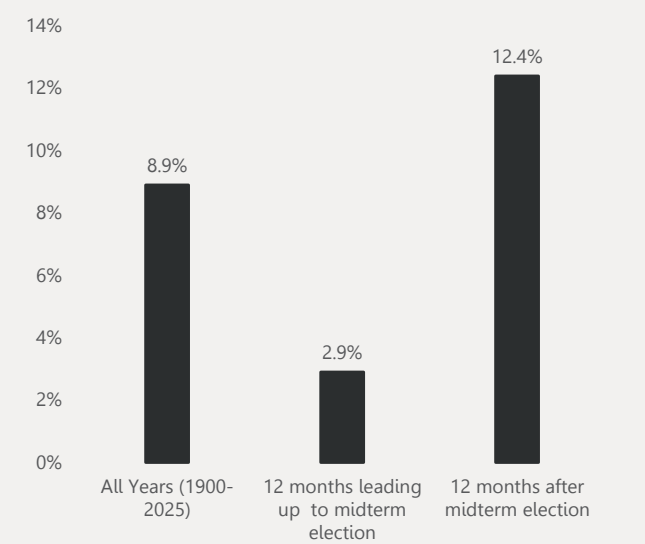
Long-term investors should probably avoid treating pre-election jitters as a signal to de-risk. Once policy clarity emerges, markets tend to experience a post-election relief rally. According to the U.S. Bank study, in the 12 months following a midterm election from 1900 through 2025, the U.S. stock market has historically rebounded to post an impressive 12.4% average return (See Chart 6).

Politics and policy debates create endless headlines, but monetary policy, inflation, interest rates, and corporate earnings exert a far greater influence on long-term portfolio performance than political control. In fact, major drawdowns in recent midterm years (such as 2002, 2018, and 2022) were triggered by tech valuations, interest rate hikes, or inflation shocks rather than election results. In previous generations, recessions and energy price spikes during midterm election years of 1930, 1970, 1974, and 1990 drove market weakness rather than congressional political reshuffling.

Furthermore, letting political preferences dictate portfolio positioning can be costly. S&P 500 annualized returns during the Obama administration (+16.3%) and the first Trump administration (+16.0%) were virtually identical, with both significantly outperforming the 30-year market

CHART 6

Midterm Volatility: Fade the Noise



U.S. Bank Asset Management Group. 12/31/25. Past performance does not guarantee future results.

average. Whether the outcome yields a split government or a unified sweep, history proves that markets adapt to any political configuration. Investors are best served by maintaining a long-term allocation grounded in risk tolerance and economic fundamentals rather than political headlines.

Footnote from Midterm Musings section
*U.S. stock market represented by the Dow Jones Industrial Average from 1900-1928, and the S&P 500 Index from 1929-2025.

Economic Outlook and Investment Policy

ECONOMIC FACTORS	CURRENT OUTLOOK
U.S. GDP Growth	We expect slightly above-trend U.S. GDP growth (2.5%) in 2H as continued AI infrastructure investment offsets the fading OBBBA boost.
Federal Funds Rate	Fed officials are talking like hawks but the FOMC will likely keep the policy rate (3.5%-3.75%) steady through the midterm elections.
Inflation	Headline inflation should moderate from 4% in the spring toward 2.5%-3% in coming months assuming energy prices stay contained.
Employment	Hiring is showing some signs of gathering steam but we still expect moderate payroll growth through the end of 2026.
Consumer Confidence	A glaring disconnect remains in place between historically-low consumer sentiment and resilient consumer spending.
Oil	An uneasy ceasefire and the need to refill depleted global inventories will make it hard for WTI crude to stay below $75/barrel in 2H26.
Housing	Housing market activity will likely be challenged until the average 30-year fixed rate mortgage drops back down closer to 6%.
International Economies	Elevated energy prices could suppress growth in India, the UK, and Germany. South Korea and Japan are benefitting from AI boom.

FIXED INCOME	MINIMUM		NEUTRAL		MAXIMUM
Core Bonds				●	
TIPS	●				
Non-Investment Grade			●		
International	●				

CURRENT OUTLOOK

Investors should continue to prioritize diversified sources of income while avoiding overextension into lower-quality credit. We favor short- to intermediate-term U.S. government and investment-grade corporate bonds, positioning we believe should benefit from the Federal Reserve on pause for the remainder of the year. We have a slight preference for Treasuries versus corporates on a relative value basis heading into 3Q.

While corporate fundamentals are supportive, tight valuations demand discipline. We emphasize issuers with resilient profiles and strong balance sheets to navigate the current environment. For tax-aware portfolios, the municipal sector is experiencing its seasonal issuance slowdown but continues to exhibit solid fundamentals.

We continue to view high-quality bonds as an important tool for dampening portfolio volatility, offering significant coupon income and capital appreciation potential as the economy navigates the current set of crosscurrents.

EQUITIES	MINIMUM		NEUTRAL		MAXIMUM
Large Cap			●		
Mid Cap				●	
Small Cap		●			
Developed International			●		
Emerging Markets		●			

CURRENT OUTLOOK

We expect periods of equity volatility in 2H26 as markets recalibrate for midterm elections and a leadership transition at the Federal Reserve. We advocate for diversified exposure with an increased focus on companies with stronger relative earnings growth and cyclical areas of the economy poised to benefit from an upshift in nominal U.S. GDP growth.

Earnings growth must perform the heavy lifting for further index-level gains given extended valuations. We expect S&P 500 earnings to grow 15%-20% in 2026, supported by a robust investment cycle in AI and energy infrastructure, alongside incremental margin expansion.

We expect follow-through from the recent broadening of leadership across U.S. stocks as earnings participation extends beyond mega-cap technology. Developed market international stocks could benefit from a rotation in favor of value given comparatively low technology sector weights. Within emerging markets, elevated oil prices could suppress growth in India and China, while Japan and South Korea continue to benefit disproportionately from the AI infrastructure boom despite their reliance on imported oil and gas.

ALTERNATIVES*	MINIMUM		NEUTRAL		MAXIMUM
	Cap Pres	IWSG	Balanced	GWSI	Growth
Gold		●	●	●	
Hedged Equity					
Arbitrage					

CURRENT OUTLOOK

Most portfolios should maintain a moderate allocation to gold despite the precious metal's correction in 2026. The desire of many global central banks to diversify their reserves, elevated geopolitical instability, and rising developed-nation government deficits are likely to create the conditions for gold to improve portfolio risk-adjusted returns. Our alternatives allocations, as seen in the table to the left, are designed to decrease the overall risk profile of our five investment objective-based portfolios. (CAP PRES, IWSG, BAL, GWSI, and GROWTH.)

The above minimum/neutral/maximum recommendations represent MainStreet Advisors' current positions relative to our Strategic Asset Allocation ranges.
Views expressed have a 6-12 month horizon and are those of the MSA Investment Committee.
*Cap Pres: Capital Preservation, IWSG: Income with some growth, GWSI: Growth with some income

IMPORTANT DISCLOSURE INFORMATION

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