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INVESTMENT STRATEGY QUARTERLY

THE MAIN MARKET EVENT:

Strength, Surprises, and the Road Ahead

Letter from the Chief Investment Officer

The main market event: Strength, surprises, and the road ahead

As we commemorate the 250th anniversary of the United States, it's worth reflecting on institutions that feel distinctly American: innovative, resilient, and constantly reinventing themselves. One unlikely example: WWE (World Wrestling Entertainment and its predecessors). What began in the 1950s as a regional promotion has evolved into a global powerhouse, exporting a uniquely American blend of sport and storytelling around the world. That evolution offers a useful lens for markets. Like professional wrestling, investing blends structure with uncertainty. Narratives build, momentum shifts, and roles are defined – but the outcome is never fully scripted to the audience. Today's market backdrop reflects that same tension between expectations and reality. So, in this quarter's outlook, we'll take our cues from wrestling. After all, in this environment, it's not just about knowing the storyline … it's about anticipating the next plot twist.

The US economy is channelling The Rock (an actor who started his professional life as a WWE wrestler): resilient, durable, and firmly in the main event. Despite higher oil prices and plenty of geopolitical noise, growth continues to show up and deliver. And if you ask, "If you smell what the economy is cooking?" – it's steady consumer spending, a labour market finding its footing, ongoing fiscal support, and a surge in AI and infrastructure investment.

But like The Rock in the "Attitude Era" (1997 to 2002), there's also a bit of swagger – and a touch of unpredictability. One moment, the data flexes with strong payrolls and solid demand; the next, it's hit with increasing AI-driven layoffs and consumer pullbacks. That's the nature of cycles: rarely linear, often noisy, and prone to short-term twists that don't change the broader story.

At the end of the day, the fundamentals remain Rock-solid. We expect US GDP to grow 2.4% in 2026, supported by fiscal tailwinds, tax incentives, and continued investment in AI and data centres. That capex isn't just driving demand – it's improving productivity while a stabilising labour market underpins consumer spending. For now, the US economy remains the undisputed champion of the global ring.

Every era has its defining villain. Today, inflation is playing the role of Andre the Giant: powerful, imposing, and not easily brought down. Like Andre, inflation still has real presence, fuelled in large part by elevated oil prices tied to the lingering Middle East supply disruption. As long as energy remains a pressure point, inflation continues to stand tall in the ring. We expect PCE inflation to end 2026 at 3.7%, above the Federal Reserve's 2% target.

Right now, inflation still seems difficult to move. But the setup is beginning to shift, and oil is the key catalyst. With a US-Iran deal in place, supply dynamics should gradually improve. We expect the US benchmark West Texas Intermediate to end the year at ~$70 per barrel, close to its level just prior to the Iran conflict.

The reopening of the Strait of Hormuz, and changes in oil demand patterns, should all contribute to lower energy prices. This would relieve one of the most persistent sources of inflation pressure and help accelerate a broader cooling trend across all international markets.

While the build-out in AI and data centres is adding to near-term demand pressures – particularly in electricity and critical minerals – we believe the longer-term impact is disinflationary. Rising investment in AI should lift productivity, improve efficiency, and ultimately help pin inflation to the mat.

So, while inflation may still look like a heavyweight, the balance of forces is starting to turn. And if history is any guide, the shift may not be gradual. Just as Hulk Hogan stunned the crowd by ultimately lifting the 525-pound Andre the Giant, it may take a decisive move – led by easing oil prices and stronger productivity – to bring inflation back down to earth.

In WWE, the referee plays a critical – yet often underappreciated – role. They are more than rule enforcers; they are in constant communication behind the scenes, ensuring the match unfolds as intended while maintaining order amid the chaos. You may not notice them when things are running smoothly, but their presence is essential to keeping everything on track.

The Federal Reserve plays a similar role in the economy. It operates largely out of the spotlight yet remains deeply connected to the system – shaping financial conditions and helping sustain the expansion. The Fed may not drive the action, but it is instrumental in how the story ultimately unfolds, and critically, it does so with independence, regardless of external pressures or outside noise.

Now, with Kevin Warsh stepping in as chair, the Fed is navigating a complex backdrop: growth remains resilient, inflation is still elevated, and geopolitical risks persist. We expect the central bank to remain on hold through at least year-end, closely monitoring how the data evolves. But if conditions were to shift materially, senior officials stand ready to step in – ensuring the match doesn't spiral out of control.

A useful comparison for today's bond market is The Undertaker. As one of the longest-tenured performers in WWE history, with a career spanning three decades, he built a legacy around durability and consistency. Time and again, he defied defeat, rising ever stronger after setbacks. In many ways, bonds feel similar today. After years of being overlooked, rising long-term Treasury yields – now at their highest levels in over a decade – have brought fixed income back to life in investors' portfolios.

And just as every great wrestler has a signature move, the bond market has one of its own – the "Stabilizer". It may not generate headlines, but it plays a critical role: delivering income and providing diversification when portfolios need it most. From here, the opportunity set looks increasingly attractive. We expect the 10-year Treasury yield to finish the year in the 4.25%–4.50% range, leaving bonds fairly valued with compelling income potential. We continue to favour high-quality, US investment-grade securities, where risk-adjusted returns remain more attractive than in lower-quality credit. Municipal bonds may have only modest international appeal but they also stand out for US investors, offering appealing tax-equivalent yields for investors seeking income with tax efficiency.

If there's one legend who defined staying power, it's Bruno Sammartino. His seven-year championship reign is the longest in WWE history. Like Bruno, the equity market continues to prove it has endurance. Markets may get caught up in the day-to-day drama – central bank moves, geopolitics, and short-term market swings – but over time, the title is decided by the fundamentals.

That said, there are challengers stepping into the ring. From elevated inflation to rising equity supply and a less accommodative Federal Reserve, it may be harder for equities to maintain their run. Still, the market's underlying strength remains. US earnings have delivered six straight quarters of double-digit growth, and we expect that momentum to carry well into next year. While the upside may be more measured given elevated valuations, the fundamental backdrop supports our constructive view, with S&P 500 targets of 7,650 for 2026 and 8,200 over the next 12 months (June 2027).

Importantly, this is no longer a one-man show – more players are entering the ring. Technology continues to lead with the AI theme, but the rally is starting to broaden. US Industrials should benefit from defence spending and the ongoing AI buildout. And an underappreciated tag team – Consumer Discretionary and Health Care, two very different sectors that have lagged and remain less favoured by investors – could also help power the next phase of the rally, as could value investing internationally. So, despite potential distractions – from Congressional elections and a new Fed chair to geopolitics and seasonality – the underlying story remains intact: this market has the staying power to extend its run.

One of the most fascinating things about WWE is that you can step away for years, come back, and instantly pick up the story. The faces change. The rivalries evolve. The production gets bigger. But the structure? That never changes.

There are still heroes and villains. Momentum shifts. Underdogs rise. Champions fall. The long-term story keeps moving forward – as the short-term drama grabs the spotlight.

That's investing. Markets, like wrestling, operate within a framework. We analyse the data, assess the matchups, and position portfolios based on the most likely path forward. But just as in WWE, there's always a plot twist. Surprises happen. Narratives shift. Outcomes evolve. Our job is not to react to every headline – it's to stay grounded in fundamentals, remain disciplined, and adjust as the story unfolds. Because in both wrestling and investing, success comes from understanding the structure beneath the spectacle, not getting distracted by it. That's where our team and your wealth manager play a critical role, helping you tune out the noise, stay aligned with your long-term goals, and keep your portfolio positioned for what matters… not just what's happening in the moment.

Because in the end, whether it's in the ring or in the markets, the winners aren't the ones chasing every twist; they're the ones who stay disciplined, stay focused, and stick to the game plan.

Enjoy the summer!

Lawrence V. Adam, III, CFA, CIMA®, CFP®
Chief Investment Officer

*Financial forecasts should NOT be considered a guarantee of future performance or a guarantee of achieving overall financial objectives.
Expressions of opinion are as of this date and are subject to change. Past performance is not a guarantee or a predictor of future results.

In the Fed we trust?

Eugenio J. Alemán, PhD, *Chief Economist,* Raymond James
Giampiero Fuentes, CFP®, *Economist,* Raymond James

The US economy has continued to reaccelerate in 2026, and we expect growth this year to outpace that of 2025. Strong investment in AI infrastructure, along with broader industrial activity, is boosting non-residential fixed investment. Government spending has also picked up following the fourth-quarter 2025 shutdown, while defence outlays are rising as the US works to replenish armaments used overseas. Additionally, stronger demand for petroleum products and increased shipments of industrial supplies and materials are likely to boost exports.

> US growth is reaccelerating in 2026, led by AI investment, industrial activity and government spending.

At the same time, the two-speed consumer economy remains firmly in place. Headline consumer spending appears resilient, but the underlying drivers remain uneven. Higher-income households, households with equity investments and retirees that continue to benefit from higher returns in 401(k)s and IRAs (types of retirement savings vehicles), continue to account for a disproportionate share of spending – a trend that was once again evident during the latest earnings season, as higher-end companies generally outperformed lower-tier, more price-sensitive businesses.

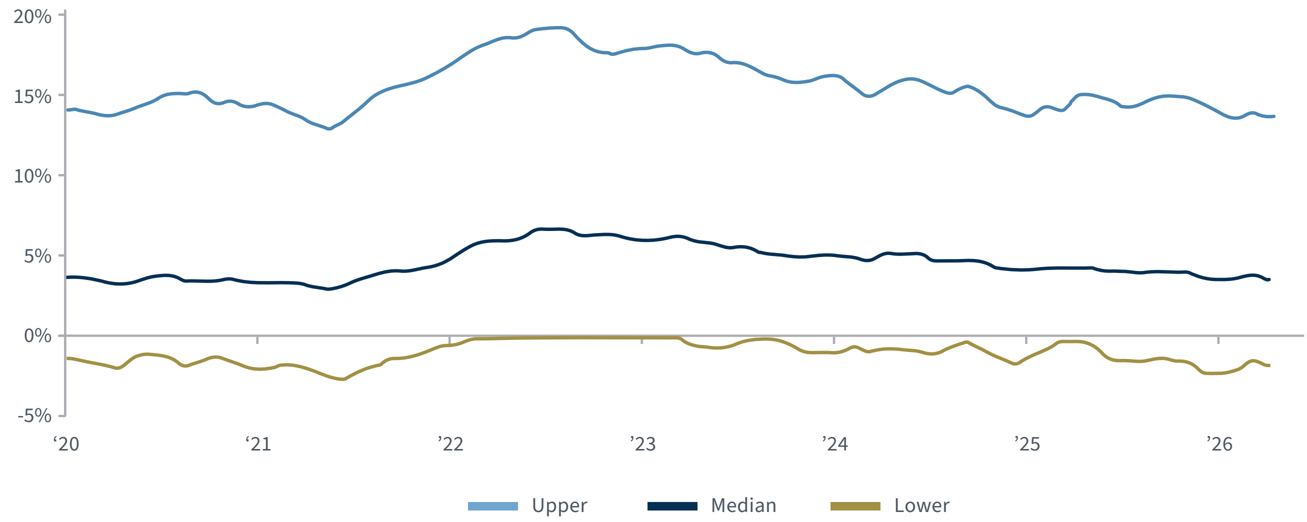
In addition to positive real wage growth, wealthier households have benefited from strong financial market performance. US equities returned roughly 10% by the end of the second quarter, while elevated fixed-income yields have provided an additional source of income and support for household balance sheets. Given our team's constructive outlook on both equities and fixed income, we believe these tailwinds are likely to remain in place throughout the remainder of the year.

KEVIN WARSH AND THE FUTURE OF THE FEDERAL RESERVE

Kevin Warsh has spent years arguing that the Federal Reserve (Fed) had become too large, too talkative and too dependent on outdated economic models. He believes the central bank lost credibility by placing excessive confidence in inflation forecasts, intervening too aggressively in financial markets, and communicating too frequently about the future path of interest

Wage tracker by household income

(YoY change, 3-month moving average)



Source: AtlantaFed, data as of 6/30/2026

> The two-speed consumer economy remains firmly in place, with higher-income households continuing to drive spending.

rates. In his view, a stronger Fed is not a louder Fed, but a more disciplined one.

The challenge is that Warsh's diagnosis was largely formed before today's environment became so complex. Inflation has not settled comfortably back at the Fed's 2% target, while pressures stemming from energy prices, tariffs and geopolitical tensions continue to complicate the case for easier monetary policy. A year ago, Warsh could argue that restoring credibility would ultimately allow the central bank to lower rates. Today, that same credibility argument may instead support keeping rates higher for longer or even tightening policy if inflationary pressures intensify.

It is also important to recognise that President Donald Trump may have sought a Fed chair more sympathetic to lower interest rates, but Warsh will not govern alone. The Federal Open Market Committee includes governors and regional Fed presidents with their own perspectives, institutional experience and policy preferences. A chair can shape the discussion and influence the agenda, but consensus remains essential.

As a result, Warsh's most important test may prove to be institutional rather than ideological.

At the June FOMC meeting, the Fed held rates steady, emphasised that inflation remains above target, and issued a shorter statement that dropped forward guidance. Warsh also announced task forces on communications, balance-sheet policy, data, productivity and jobs, and inflation frameworks. Each priority carries implementation risk: better real-time data will take time, balance-sheet changes could unsettle markets, and less guidance may make policy cleaner but less transparent.

Contrast, in passing, the difficulties faced by the Federal Reserve and those divergent forces confronting monetary policymakers elsewhere. The Bank of Japan is slowly normalising policy after decades of low and zero interest rates. In India the Reserve Bank is tackling a sharp depreciation in the rupee while in the UK and Europe central banks, despite their mandated focus on inflation (“The compass has just one needle” as the former ECB President Jean-Claude Trichet once famously said) are attempting to steer a policy course between rising inflationary pressure and weak economic activity.

Note, too, that while all the world’s systemic central banks are nominally independent (including the Federal Reserve) senior officials typically appointed on the basis of experience alone, in the US the Chair is a political appointment, ratified by the Senate. While all senior global central banking officials must explain policy and its context to lawmakers from time to time, none must balance rigorous economic analysis against a highly determined White House policy agenda.

The 12 voting members of the FOMC

Monetary policy decisions are made by the Federal Open Market Committee (FOMC).

1
FED CHAIR
A Board Governor designated by the president and confirmed by the Senate.

+

5
RESERVE BANK PRESIDENTS
Includes the New York Fed president and four rotating Reserve Bank presidents.

+

6
OTHER BOARD GOVERNORS
Appointed by the president and confirmed by the Senate.

=

12
TOTAL VOTES
Decisions are made by a majority of the 12 votes.

Each voting member has one vote.

OUR OUTLOOK FOR MONETARY POLICY

We believe Warsh was a strong choice for Fed chair because of his unique combination of experiences. As a member of the Federal Reserve Board during the Global Financial Crisis, he gained firsthand experience navigating one of the most significant economic downturns in modern history. At the same time, much of his career before and after his tenure at the Fed has been spent on Wall Street, providing him with valuable insight into how monetary policy decisions affect financial markets, businesses and investors.

Overall, while Warsh has begun to shift the Fed's communication style through a shorter statement, less forward guidance, and a broader review of the operating framework, we believe the institution will remain fundamentally data dependent. With the June FOMC statement keeping rates unchanged, citing solid activity, stable unemployment, and inflation still above target, the Fed is unlikely to pursue policy easing in 2026. Nevertheless, we continue to anticipate a single rate cut next year, reflecting our expectation that growth will slow, fiscal tailwinds will diminish, and inflationary pressures will gradually subside, absent any material economic shocks.

LABOUR MARKET STRENGTHENS

Our view is that the US labour market has remained resilient. During the first five months of the year, the economy generated nearly 114,000 jobs, with average monthly job creation exceeding 188,000 between April and May. That pace is substantially stronger than the roughly 10,000 jobs per month generated on average in 2025.

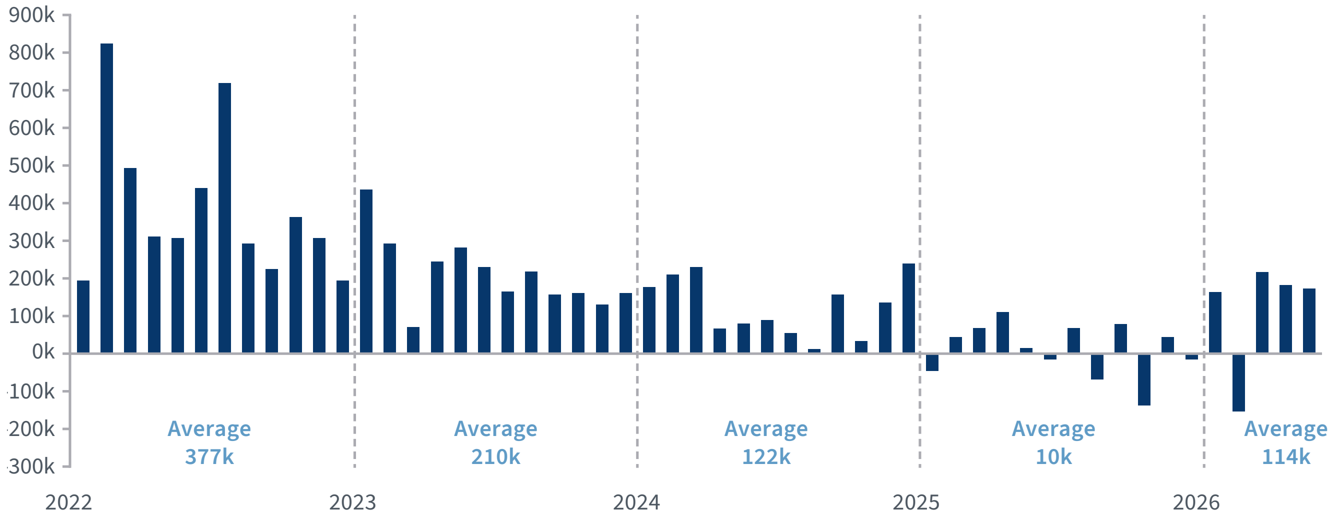
As a result, despite potential headwinds from advances in AI and the possibility of softer consumer demand later in the year, labour market conditions remain relatively healthy. Moreover, several sectors, particularly Health Care, continue to experience robust hiring demand. Consider the lengthy waiting times many patients face when trying to see a doctor or the delays homeowners often encounter when scheduling a skilled workman. These examples highlight ongoing labour shortages in key industries.

In our view, the labour market story is increasingly one of sector-specific shifts and labour reallocation rather than broad-based weakness that would justify aggressive monetary easing. While certain industries may face disruption, the overall employment backdrop remains considerably stronger than many expected at the start of the year.

INFLATION OUTLOOK AND INTEREST RATES

From an inflation perspective, the outlook has improved. With the conflict involving Iran now appearing to have reached a framework for de-escalation, oil prices have declined meaningfully. We expect energy prices to move lower as the year progresses, providing additional support for the disinflation process and helping inflation move closer to policymakers' targets.

Nonfarm payrolls - Monthly change



Source: FactSet, data as of 6/30/2026

> The Fed can afford to remain patient: labour markets are resilient, inflation is moderating and any policy easing is likely to be gradual.

Consequently, we continue to view rate hikes as unlikely during this year. In addition to the improving inflation backdrop, a single rate increase would likely do little to meaningfully restrain economic activity while potentially creating unnecessary market volatility. Historically, a meaningful tightening in financial conditions has required a sustained series of rate hikes rather than a one-off adjustment.

That said, inflation risks have not disappeared entirely. One key factor to monitor is the potential for additional fiscal expansion, which could provide further support to demand and complicate the disinflation process. Even so, absent a material reacceleration in inflation driven by stronger fiscal stimulus or other demand-side pressures, the case for renewed monetary tightening remains weak.

BOTTOM LINE:

Taken together, a resilient labour market, moderating inflation pressures and continued economic expansion suggest that the Fed can remain patient. While policy easing may eventually become appropriate, we believe any adjustment will be gradual and driven by incoming data rather than urgency. For all investors, both domestic and international, the key question is not whether rates move by 25 basis points in either direction, but whether the underlying US economic backdrop continues to support stable growth, healthy labour markets and downside progress on inflation.

KEY TAKEAWAYS

- Economic growth is broadening and strengthening in 2026, supported by accelerating AI infrastructure investment, stronger industrial activity, firmer government and defence spending, and improving demand for energy and industrial materials.
- Consumer spending remains resilient, but leadership is increasingly concentrated in higher-income cohorts.
- A Warsh-led Fed is already shaping communications and reviewing its policy framework, but decisions should remain driven by incoming data.
- The macro backdrop supports patience from the Fed, not urgency.

Q&A – Midterm elections and geopolitical risk will drive the market

Ed Mills, *Washington Policy Analyst,* Equity Research

As we move through 2026, the political and geopolitical landscapes remain key drivers of policy uncertainty. For the US Congressional midterm elections, our base case is a Democratic House and Republican Senate, a historically favourable outcome for equities. Meanwhile, the US-China relationship has stabilised modestly, and multiple Trump-Xi meetings are expected this year, creating opportunities for incremental progress, with key questions around export controls and access to advanced technology unresolved. Geopolitical risks remain elevated, particularly amid the ongoing US-Iran tensions. While markets have remained resilient to geopolitical flareups so far, a prolonged conflict or sustained pressure on energy prices could weigh on economic activity and introduce greater market volatility.

> Divided government has historically been positive for equities.

2026 MIDTERM ELECTIONS

Q. What's the base case for the 2026 midterm elections?

A. Our base case remains a Democratic House and Republican Senate. Divided government historically has provided for a market-friendly backdrop, limiting legislative surprises, but President Donald Trump's use of executive action could continue to drive uncertainty and volatility. As we have framed all year, elections ultimately remain a maths problem. Republicans enter the cycle with a 220-215 House majority. 218 seats are needed for a majority and several structural challenges against Republicans present an opportunity for Democrats to capture a majority, including an unfavourable national environment, weak presidential approval ratings, elevated voter dissatisfaction and an energised Democratic base. Redistricting efforts could add anywhere from four to eight seats to the Republican column and reduce Democratic gains. In the Senate, Democrats would need to net four seats out of the 33 Senatorial races. Midterm Senate election results tend to match the presidential results in most states. An analysis of previous midterms shows there is a 20-29% deviation between the winner of the Senate election and the state's preference in the previous presidential election. For Democrats to win the Senate they would need a 67% deviation. Not impossible, but a significant departure from recent midterm election results.

Q. What's the impact of divided government on policy?

A. Traditionally, policymaking is limited to bipartisan efforts in divided governments. Volatility occurs on must-pass legislation such as government funding bills, increasing the risk of government shutdowns. A key issue after the election will be how Democrats and Trump approach policy debates. Will Democrats and Trump work together or will they seek to define the other as the obstacle? In his second term, Trump has increasingly used executive action and emergency powers to implement policy. The unpredictable nature of these efforts – for example, the April 2025 tariff announcement – has caused significant market volatility. Markets have become more accustomed to this style, and the courts have limited some of these actions, but it may usher in a different policy environment than previous divided government scenarioss.

- **Divided government market impact?** Historically, equities perform best under this scenario, and markets experience the least overall volatility. While shutdown risks would likely increase, other policy initiatives would face substantial hurdles. Areas with bipartisan support, including potentially more hawkishness toward China, infrastructure spending, national security initiatives, supply chain resilience and permitting reform remain the most likely avenues for legislative action.

- **Sweep scenarios and market impact?** While a divided House and Senate remain our base case, investors should not ignore the possibility of sweep scenarios. Unified control of Congress by either party would increase the likelihood of increased standoffs between Congress and the president. A change in the Senate majority would limit the president's ability to win confirmation of his appointments and would likely cause the return of many of the fired Democrats at independent agencies. Increased executive action, as discussed above, would also become even more likely.

US-CHINA

Q. What is the status of the US-China relationship?

A. The US-China relationship is currently characterised by a mutual desire to reduce friction and increase stability. While fundamental tensions remain – and with that, a long-term effort to mutually de-risk – both Trump and Xi are placing emphasis on the truce struck last October. In their first meeting of 2026, this focus was demonstrated by the announcement of aerospace and agricultural purchase agreements, initial progress on the bilateral Boards of Trade and Investment, and a stated desire to continue high-level contact between the two countries. Taiwan remains one area of tension, with Xi seeking concessions from Trump on arms sales to the island and Trump potentially using their suspension as a bargaining chip.

Q. What should we expect from US-China ties this year?

A. Trump and Xi have already met once this year in Beijing and up to three more meetings are expected, the next being a September summit held in Washington, DC. Given the multiple expected meetings, few of the market-relevant deliverables were raised or finalised at the May meeting. As such, key issues such as tech controls will be watched closely in the runup to the September meeting. The Trump administration has, overall, shown a greater willingness to export leading-edge US tech to China than its predecessor or Congress, and Beijing is keen to receive access to the latest semiconductors and semiconductor capital equipment. While some initial easing has taken place, it remains to be seen whether Trump opens the spigot further given competing concerns between the US tech industry, which wants to promote the US tech stack overseas, and concerned China hawks in Congress. Further progress on the Board of Trade is another key issue, with the White House preparing to receive public comment on which goods should be eligible for a $30 billion trade initiative intended to identify and promote bilateral trade in sectors not sensitive to national security.

GEOPOLITICS

Q. With geopolitics front and centre in 2026, what are the key lessons for investors?

A. One fundamental shift we have observed between 2025 and 2026 has been the White House's preferred policy lever for securing policy outcomes overseas. While 2025 was dominated by the use of economic tools like tariffs, paired with fairly limited uses of force, 2026 has been marked by the demonstrated willingness to use military force in a more expansive matter. This shift, exemplified most by the US-Iran war, has been accompanied by a renewed focus on the Western Hemisphere and the adoption of a wartime footing on the defence spending and industrial policy front.

> Geopolitical risk is the key macro threat.

Q. What should investors expect in terms of key risks going forward?

A. While a durable resolution to the Iran war remains some away (especially as negotiations continue between the US and Iran), other geopolitical risk areas are simmering, such as Cuba, Greenland and Venezuela. If these regions were to see flareups, market expectations will likely continue to assume a short-term duration to these engagements. However, the more these incidents take place, and the longer US -Iran negotiations take to complete, the more these expectations will be challenged. Market reaction to the geopolitical flareups of recent memory has overall been relatively muted; economic stimulus and earnings optimism have played key roles here, but the longer pressures continue – such as oil pressure associated with the Iran war – the greater the economic impact and associated market risk.

"Great Burnham (sic) Wood to Dunsinane Hill shall come"

Prof Jeremy Batstone-Carr , *European Strategist, Raymond James*

UK financial markets have taken the outgoing Prime Minister Sir Keir Starmer's resignation in their stride. Sterling has lost some ground against an appreciating US dollar since local elections on 7 May but has made some modest upside against the euro. If fiscal credibility is to be assured, the new incumbent of No. 10 Downing St, a seventh Prime Minister in the 10 years since the Brexit referendum, must be mindful that whatever plans may lie in wait the gilt-edged market must be placated. Andy Burnham duly won the Makerfield by-election with an increased majority and has signalled his intention to bid for the premiership. Nominations will open on 9 July and with several potential candidates aligning behind the candidate it remains to be seen whether he will face a challenge.

A change in leadership may alter the size of the state but it will do nothing to alter fiscal realities. If public spending is to increase relative to current plans, then taxes on both capital and wealth may be increased to pay for it. Two key constraints limit room for manoeuvre; the perception of fiscal prudence in financial markets and the political cost of adding to pressure on household budgets by keeping inflation and interest rates higher than might otherwise have been the case. It remains to be seen whether Burnham's flagship proposal, to devolve some powers from London to the North of England, will deliver a lasting improvement in productivity and in so doing a sustainable improvement in economic activity over the medium term.

DEVOLOUTION DOES NOT GUARANTEE ECONOMIC GROWTH

Mr Burnham's economic credentials have improved in tandem with the increasing likelihood that he will be the UK's new Prime Minister on 17 July. Gone is the belief that a Burham-led administration should not be "in hock to the bond market", in its place the more sober assertion that the fiscal rules are inviolable and must be adhered to. Credibility has been enhanced by what financial markets view as the gathering of a high-powered team of informal advisers including Lord (Jim) O'Neil of Gatley, the former Goldman Sachs Chief Economist and coiner of the "BRICS" acronym, as well as MR Andy Haldane, a former Monetary Policy Committee (MPC) member and Bank of England Chief Economist. Both know well that devolving some of No. 10's operations to Manchester grabs headlines and more importantly costs very little. Building on the much-vaunted "Manchesterism" brand, a highly visible demonstration of change, could play out well with voters in the Midlands and the North. Furthermore, the geographical shift could deliver local solutions to local issues, improve policy coordination and by extension deliver the productivity benefits for so long the UK economy's Achilles' heel.

But there is room for doubt. Simply switching some powers from London to Manchester amounts to little if local governments in that city and elsewhere cannot meaningfully raise their own revenues and instead remain reliant on stop-start funding from the Treasury. OECD data confirms that while local government expenditure in the UK represents a broadly similar share to that achieved in other OECD countries, its share of revenue generation is towards the bottom of the international league table. Furthermore, if a Burnham-led administration does follow the OECD model it should be aware of the fact that those countries that have migrated down the devolution route have seen little discernible improvement in GDP growth as a consequence.

MIGHT THE NEW PRIME MINISTER GET LUCKY?

Everybody needs a bit of luck from time to time, and political leaders are no exception. The increasingly fragmented nature of British politics owes much to a decade thus far characterised by the difficulty associated with domestic policymaking against a backdrop of international turbulence and the transformative impact of a worldwide pandemic, the fall-out from the Ukraine war, President Trump's trade policy initiatives and another major conflict in the Middle East. The latter's impact is clearly visible in economic activity data confirming a return to stagnation after a strong start to the year. Manufacturing activity has held up, likely benefitting from precautionary stock building, but services output has borne the brunt of the war in the Persian Gulf. More encouragingly the energy price spike has proved less pronounced than that following Russia's invasion of Ukraine, meaning that while inflationary pressures are evident they will likely end up peaking at a significantly lower level than the 11% recorded in the autumn of 2022.

The combination of weak growth and a soft labour market, meaning that employees have little bargaining power when it comes to the wage growth that rate-setters at the Bank of England fear as much as anything, may encourage the MPC to "look through" prevailing price pressures. With the UK's base rate of interest holding at 3.75%, policymakers know only too well that monetary conditions are already much more restrictive now than was the case four years ago. Although the Bank's rate-setting Committee is divided, the majority may hold their nerve sufficient to leave policy rates unadjusted in the near-term and look to cut again next year, an outcome not priced in by financial markets still of the opinion that the near-term path of least resistance lies to the upside. A benign outcome could drive the benchmark 10-year gilt-edged yield down to around 4.25%, converging with the equivalent US Treasury yield (and sterling to drop to around $1.25 next year). The big risk in all this lies in a materially looser fiscal policy which could drive both borrowing costs and interest rates higher. If one believes that you make your own luck, Burnham's destiny lies in his own hands.

KEY TAKEAWAYS

- A change in political leadership may increase the size of the state but it will do nothing to alter the UK's fiscal realities and by extension little to promote lasting economic growth.
- The scope for a big fiscal policy loosening; increased investment, renationalisation of water, energy and the rail network, more social housing and higher defence spending is likely modest.
- A new Prime Minister (and perhaps Chancellor) must commit to fiscal policy discipline to keep the gilt-edged market onside and prevent borrowing costs and interest rates from rising sharply. Higher taxes on both capital and wealth are possible.
- A new Prime Minister will not want to make the hit to household incomes worse by adopting measures that might keep inflation and interest rates higher than might otherwise have been the case.
- A commitment to fiscal policy probity will encourage the Bank of England from raising interest rates. Weak economic activity and soft employment conditions will ensure that the inflation fall-out from the Middle East conflict is limited both in extent and duration, a development likely regarded favourably by the gilt-edged market.

Resilience by construction: How index evolution drives earnings strength

Matt Barry, CFA, *Senior Investment Strategist,* Investment Strategy
Mike Payne, *Investment Strategy Analyst,* Investment Strategy

Despite multiple risks that emerged over the past year – tariffs, higher energy prices, upward pressure on interest rates and evolving growth and earnings outlooks – US equities have shown remarkable resilience. The S&P 500 has gained 10% year to date (YTD) with eight of 11 sectors in positive territory for the year[1]. Notably, the move higher was driven by earnings rather than multiple expansion. In fact, while the S&P 500 has moved higher YTD, the forward 12-month price-to-earnings estimate has moderated from 22.2x to 21.4x. Contrarily, consensus estimates now point to a remarkable 24% year-over-year earnings per share (EPS) growth for the S&P 500 in 2026 – levels usually seen only during recoveries following recessions. Perhaps unsurprisingly, one of the largest questions domestic and international market participants have at this stage is: How have US corporate earnings been so resilient despite the risks that have materialised thus far?

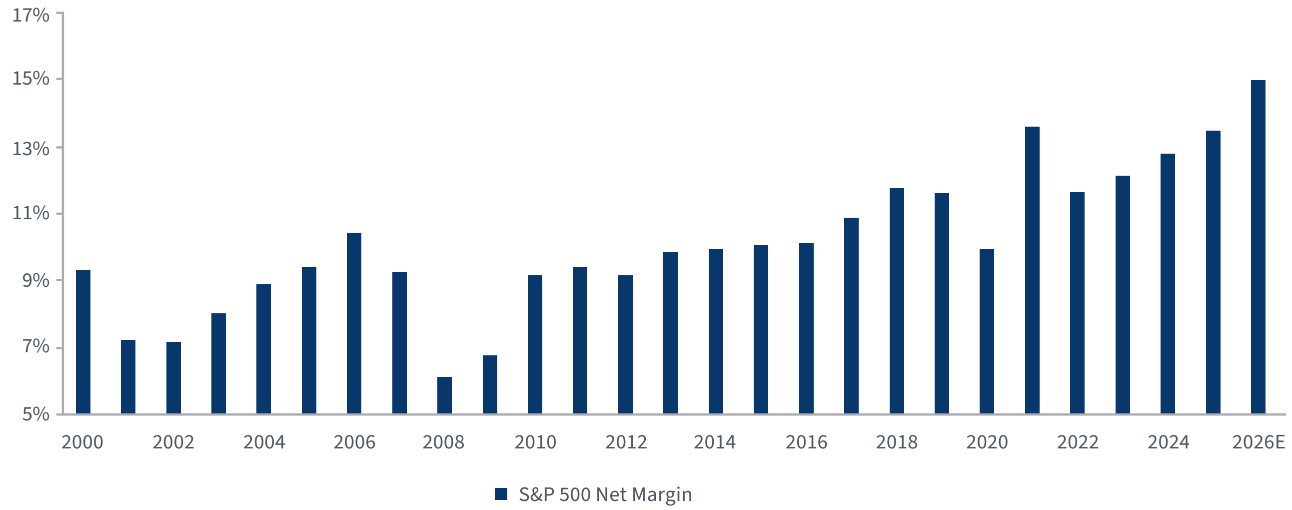
S&P 500 earnings resilience reflects a structural shift toward less energy-intensive, more asset-light and technology-driven sectors

FUNDAMENTALS: REMARKABLE STRENGTH DESPITE HIGHER ENERGY PRICES

S&P 500 earnings have shown impressive strength in 2026 despite higher energy costs, largely because the index itself looks very different than it did in prior cycles. Most importantly, it is far less energy-intensive than in the past. Over time, index earnings have become less exposed to traditional manufacturing, where higher energy costs directly pressure profitability, and to energy-sensitive areas of consumer spending, where elevated fuel prices can weigh on

[1] As of 6/19/2026

S&P 500 margins expected to reach record highs in 2026



Source: FactSet, RJ Investment Strategy, data as of 6/1/2026

demand. Today, the index composition has shifted decisively toward asset-light, service-oriented and technology-driven businesses. As a result, energy is a smaller share of total cost structures for the average S&P 500 company, dampening the direct impact of rising oil. This declining energy intensity reflects not only sectoral shifts but also operational changes within firms. Advances in energy efficiency, more flexible supply chains and the increasing digitisation of business models have all reduced the amount of energy required per unit of output. As a result, the sensitivity of corporate profitability to oil price shocks is structurally lower than in prior decades. Another important factor is the improvement in pricing power across large corporations. Following the post-pandemic inflationary period, many firms have demonstrated an increased ability to pass on higher input costs to end customers. While not universal, this has reduced the typical pressure on profitability associated with rising energy prices, particularly among firms with strong competitive positioning and differentiated value propositions.

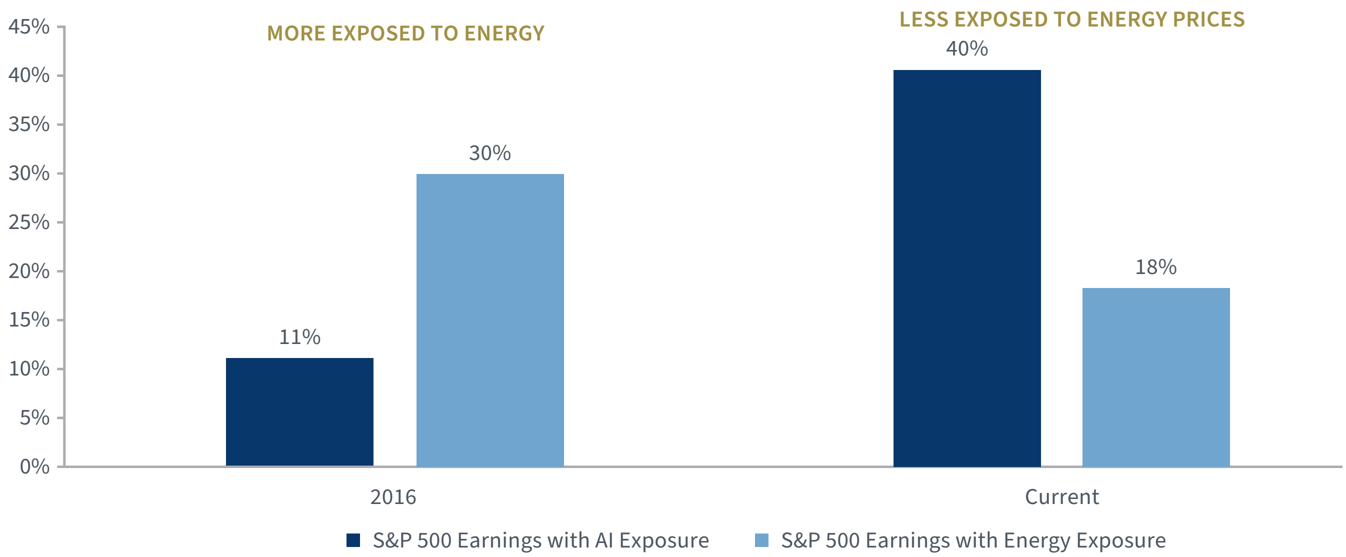
MARGIN RESILIENCE: COST DISCIPLINE AND OPERATING LEVERAGE

Another important, and often underappreciated, factor supporting earnings resilience is the shift toward greater capital and cost discipline across large companies. In the years following the pandemic, firms have become more focused on efficiency, earnings durability and return on invested capital rather than purely top-line revenue growth. This has led to leaner cost structures, tighter control over operating expenses and more scalable business models. At the same time, operating leverage has structurally shifted in favour of larger firms, particularly within asset-light and technology-enabled sectors where fixed costs are relatively high but variable costs remain low. This dynamic allows revenue growth, although uneven across the economy, to translate more efficiently into profits. As a result, many companies are better positioned to absorb input-cost volatility, including energy, without a proportional impact on profitability. Taken together, stronger cost discipline and improved operating leverage have reduced the sensitivity of earnings to external shocks, reinforcing the broader resilience seen at the index level. This evolution in corporate behaviour, far from unique to the US but very highly visible there, along with greater exposure to more insulated secular growth trends, is reflected in S&P 500 net margins projected to reach a record high of 15% in 2026, underscoring the durability of profitability even in a more challenging cost environment.

CONCENTRATION EFFECTS: THE RISING DOMINANCE OF AI-DRIVEN EARNINGS

Even more critical is the increasing concentration of earnings in a narrow set of AI-enabled industries, particularly semiconductors and cloud computing. Unlike any other major developed global equity index, the modern S&P 500 is now nearly half AI-focused when viewed through the lens of earnings contribution and index

Composition of S&P 500 earnings has evolved over time



Source: FactSet, RJ Investment Strategy, data as of 6/1/2026

*AI Exposure is defined as Cloud Computing, Electrical Equipment, Semiconductors, and Software. Energy Exposure is defined as Materials, Industrials Ex. Electrical Equipment and Professional Services, Consumer Discretionary Ex. Services and Internet, Consumer Staples, and Health Care Equipment and Supplies.

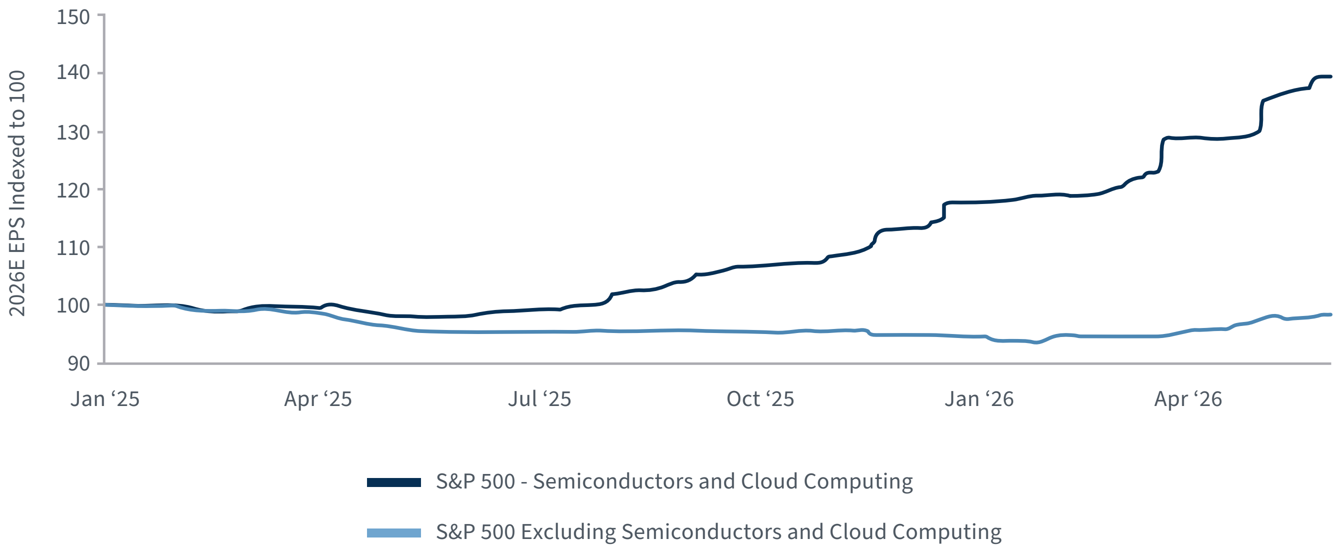
composition. These industries are benefiting from powerful secular demand tied to artificial intelligence adoption, data centre buildouts and enterprise digitisation. Unlike tradi-tional industries more prevalent in other global indices, their revenue growth is driven less by cyclical factors and more by structural trends, allowing them to offset the cost pressures apparent elsewhere in the index. In fact, 10 years ago, 30% of S&P 500 earnings were directly exposed to energy prices while only 11% were tied to today's AI beneficiaries. Today, AI-related firms are responsible for 40% of S&P 500 earnings while only 18% of index earnings are exposed to energy prices. Importantly, the AI investment cycle is also creating second-order support across the broader index. Data centre buildouts and infrastructure expansion are driving demand for industrial equipment, electrical components and power generation, benefiting sectors that would otherwise be more exposed to higher energy costs. This capital expenditure-driven demand spillover further cushions earnings in aggregate.

EARNINGS DIVERGENCE: NARROW BREADTH BENEATH STRONG HEADLINE GROWTH

This divergence between broader economic pressures and secular growth themes is clearly visible in earnings revision trends. Over the last two years, 2026 earnings estimates for semiconductors and cloud computing companies have been revised higher by roughly 39%, reflecting strong pricing power, accelerating AI demand and sustained capital investment in AI infrastructure. In contrast, the rest of the index has seen aggregate earnings estimates revised modestly lower, by about 1%. In other words, while much of the S&P 500 is experiencing pressure on profitability from higher input costs, including energy, the outsized growth of AI-linked industries is more than compensating at the index level. At the same time and unique to the US barring several stock markets in Asia, this dynamic also points to narrower earnings breadth, with a smaller group of companies driving a disproportionate share of index-level growth, leaving aggregate earnings increasingly dependent on the durability of AI-driven demand and execution.

> Lower energy sensitivity, stronger pricing power and improved cost discipline have reduced the impact of rising input costs on profitability

AI Strength masking mixed fundamentals beneath the surface



Source: FactSet, RJ Investment Strategy, data as of 6/1/2026

BOTTOM LINE: INDEX CONSTRUCTION IS LARGELY RESPONSIBLE FOR RESILIENT FUNDAMENTALS

Taken together, the resilience of US corporate earnings is less about uniform strength across all sectors and more about index composition effects. A less energy-intensive cost base, combined with the increasing dominance of high-growth, AI-driven industries, has allowed aggregate earnings to hold up even in the face of rising energy costs. This structural shift underscores why headline index earnings can remain strong even when underlying conditions are more mixed.

KEY TAKEAWAYS

- S&P 500 earnings durability reflects a structural shift toward asset-light, less energy-intensive, and technology-driven businesses rather than uniform strength across sectors.
- Reduced energy intensity, enhanced efficiency and stronger corporate pricing power have materially dampened the historical margin pressure associated with rising oil prices.
- A narrow group of AI-linked sectors – particularly semiconductors and cloud computing – is generating an outsized share of earnings growth, masking weaker trends across the broader index.

Crude awakening: The Iran conflict's aftereffects will linger long after it's over

Pavel Molchanov, *Senior Investment Strategist*, Investment Strategy

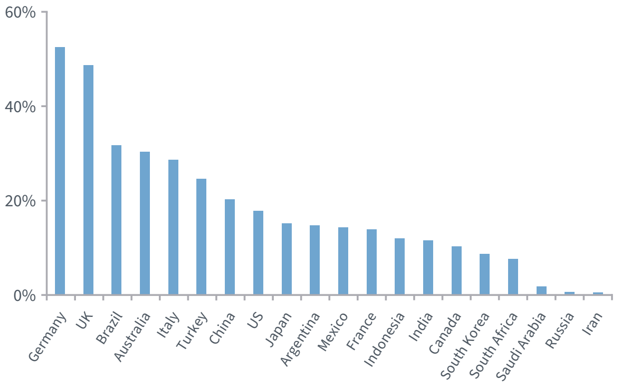
Every major geopolitical crisis has two types of effects: those that occur during the crisis itself and those that remain on a long-term basis, perhaps even permanently. The US-Iran conflict is no exception. The most severe oil supply disruption in world history – and related impacts on liquified natural gas, helium, ammonia and aluminium – has led to higher commodity prices around the world, with some countries experiencing outright shortages. While $100+/barrel oil and $4.00+/gallon petrol are already in the rearview mirror, some of the aftereffects of this unprecedented crisis are here to stay. Just as the energy shocks of the 1970s led to, among other things, the creation of emergency oil stockpiles and a shift away from gas-guzzling vehicles, the latest crisis may exert influence on policymakers, businesses and consumers for years or even decades to come.

NATURAL GAS STOCKPILING: A LONG-MISSING PIECE OF THE ENERGY SECURITY PUZZLE

When the 32 member countries of the International Energy Agency (IEA) pledged this past March to release 400 million barrels from their emergency oil stockpiles, it was by far the largest such action in the IEA's 52-year history; in fact, larger than all previous ones combined. But the IEA's remit has never been extended to include natural gas. In retrospect, that was a big oversight, dating back to the IEA's creation in 1974.

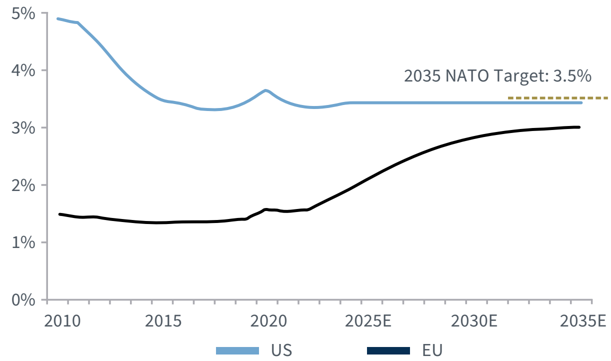
Natural gas plays a much greater role in the global energy mix today than it did half a century ago. Whereas oil is overwhelmingly used for transportation, natural gas has a wide range of use cases: electric power, heating, industrial processes (e.g., steel mills) and the chemical industry (where it has been increasingly displacing oil). And while global oil demand has been growing at less than 1% per year in the post-COVID era – even setting aside the decline in 2026 due to the price spike – global natural gas demand tends to increase two to three times faster.

Non-Hydro renewables share of electricity mix, 2025E



Source: FactSet, RJ Investment Strategy, data as of 6/1/2026

Amid conflicts, Europe ramps up defence spending



Source: FactSet, RJ Investment Strategy, data as of 6/1/2026

Europe's energy crisis in 2022 – the restriction of Russia's natural gas supply after its invasion of Ukraine – illustrated that natural gas also needs to be stockpiled. Europe has made progress in that regard over the past four years. By contrast, countries in Asia – the main importers of liquefied natural gas from Qatar, whose main facility was seriously damaged by an Iranian strike in March – have yet to follow suit. Along the same lines, there may be efforts to stockpile natural gas derivatives such as ammonia (a key input for fertilizer) and helium (playing an important role in semiconductor manufacturing).

MORE RENEWABLES AND NUCLEAR POWER: A WAKE-UP CALL FOR ASIAN ECONOMIES

Countries such as Japan and South Korea, which are virtually 100% dependent on imported oil and natural gas, cannot drill their way toward energy independence – they simply do not have the required natural resources. What they are able to do, however, is shift their electricity mix towards renewables – wind, solar, in certain cases hydro and geothermal – as well as nuclear power. Whereas power plants that burn fossil fuels require a non-stop supply of those raw materials and are thus prone to supply disruptions, energy security can be enhanced by shifting to electricity sources that face little to no geopolitical risk.

The energy crisis of 2022 provided an impetus for European countries to accelerate the buildout of renewable power generation, as well as nuclear (with the notable exception of Germany), and this latest crisis may provide a similar wake-up call for countries in Asia. As shown in the chart, Germany and the UK are among the leaders in non-hydro renewable power as a percentage of the electricity mix. China and Japan are further behind – although China is installing more solar panels and wind turbines in absolute terms than the rest of the world combined – with India and South Korea near the bottom of the international spectrum. Wind turbines, solar panels and other products for the electric grid are manufactured by companies in the Industrials sector, and bolstered demand for this equipment would support our positive stance on the sector.

FASTER EV ADOPTION: A STEP THAT CONSUMERS CAN TAKE TO PROTECT THEMSELVES

The 50% run-up in US retail petrol prices, coupled with sharp fuel price spikes internationally during the Iran conflict provided the latest illustration of the fact that when oil prices rise, they rise worldwide – even in countries such as the US that are net exporters. The global nature of the oil market means that there is no such thing as immunity from oil price increases. A similar story played out during the 2022 energy crisis, even though Russian oil exports (in contrast to natural gas) never actually experienced a significant disruption.

The good news is that consumers and businesses can protect themselves from sudden spikes in oil prices by shifting toward electric vehicles (EVs). (Electricity prices are rising over time, but because they are regulated they are not prone to abrupt changes in either direction.) With the exception of China, the price tag of EVs tends to be higher than comparable conventional vehicles, but the higher fuel prices become, the shorter the payback period. At $4.00 per gallon, we estimate that the payback for US consumers would be in the range of six to seven years, as compared to eight.

As it stands, EVs comprise more than half of new auto sales in China, roughly 30% in Europe, but only roughly 10% in the US. Interestingly, among the leaders in EV adoption are low-income countries with essentially no oil of their own – Ethiopia and Nepal are notable case studies – because it is precisely these countries that struggle the most during oil shocks. The faster EV adoption progresses, the slower global oil demand is set to grow in the future, a key reason for our underweight on the energy sector.

It is worth noting that EVs, more so than conventional vehicles, depend on critical minerals such as lithium and nickel (for batteries) and rare earths (for powertrains). The Iran conflict directly disrupted supply of only one metal – aluminium, which is refined in the UAE and Bahrain, though there are hypothetical geopolitical scenarios that could have far-reaching impacts on critical minerals. Case in point: war between China and Taiwan. But here's the essential difference between critical minerals and oil: While disruption of such exports from China would make it more difficult to manufacture new EVs, it would have no effect on existing EV drivers. By contrast, every owner of a conventional vehicle felt the impact of $100+ oil each time they pulled up to the fuel station.

MORE DEFENCE SPENDING: IN A VOLATILE WORLD, PAST ISN'T ALWAYS PROLOGUE

Never in the modern history of the Middle East has there been a war that embroiled more countries than this one. The first Gulf War in 1991 involved many countries in the region but Iran chose to stay on the sidelines. More recently, brief conflicts between Israel and Iran remained limited to just those two countries. But in March and April of this year, Iran's willingness to attack fellow Muslim countries around the Persian Gulf shocked its neighbours. While air defences in these countries were partially successful in intercepting Iranian missiles and drones, there was still widespread damage to infrastructure, including, as mentioned earlier, energy facilities. It is a good bet that governments across the region will want to be even better prepared in the future.

Looking beyond the Middle East, the conflict has had a second-order effect: It provided a hefty boost to the Russian economy. Accordingly, the Kremlin will have even more resources to continue its war in Ukraine. As NATO's European members ramp up defence spending toward the alliance's official target of 3.5% of gross domestic product by 2035, the threat from Russia is top of mind. While we doubt that Europe as a whole will average 3.5%, those countries that are geographically closer to Russia – Baltic states, Poland, to some extent Germany – have a heightened perception of risk and are therefore willing to spend more. Growth in defence spending among the US and its allies is also a driver of our overweight on Industrials.

> The good news is that consumers and businesses can protect themselves from sudden spikes in oil prices by shifting towards electric vehicles

CONCLUSION

As was the case in previous geopolitical crises, we expect the Iran conflict to have a series of long-term consequences. Given that energy was more affected by this conflict than any other sector of the global economy, these aftereffects are disproportionately energy-related: stockpiling of natural gas, a push for energy security via renewable and nuclear power, and bolstered demand for electric vehicles. Looking beyond energy, higher defence spending is also likely. The ways in which these aftereffects materialise will vary in different parts of the world. For investors, the key message is that all long-term trends carry opportunities as well as risks.

KEY TAKEAWAYS

- With emergency oil stockpiles playing a useful role during the Iran conflict, governments may pursue similar policies for natural gas, particularly in Asia.
- Energy-vulnerable economies in Asia are likely to follow Europe's lead in bolstering domestic generation of renewable and nuclear power.
- Given that oil price shocks have a worldwide scope, electric vehicle sales around the world are getting a boost, which accentuates the importance of critical minerals.
- Defence spending is likely to keep increasing in the Middle East as well as Europe, as governments prepare for potential future wars.

DISCLOSURE

All expressions of opinion reflect the judgment of the authors and are subject to change. Past performance may not be indicative of future results. There is no assurance any of the trends mentioned will continue or forecasts will occur. The performance mentioned does not include fees and charges which would reduce an investor's return. Dividends are not guaranteed and will fluctuate. Investing involves risk including the possible loss of capital. Asset allocation and diversification do not guarantee a profit nor protect against loss. Investing in certain sectors may involve additional risks and may not be appropriate for all investors.

International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic volatility. Investing in emerging and frontier markets can be riskier than investing in well-established foreign markets.

Investing in small- and mid-cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor.

There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices rise.

US government bonds and Treasury bills are guaranteed by the US government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. US government bonds are issued and guaranteed as to the timely payment of principal and interest by the federal government. Treasury bills are certificates reflecting short-term obligations of the US government.

While interest on municipal bonds is generally exempt from federal income tax, they may be subject to the federal alternative minimum tax, or state or local taxes. In addition, certain municipal bonds (such as Build America Bonds) are issued without a federal tax exemption, which subjects the related interest income to federal income tax. Municipal bonds may be subject to capital gains taxes if sold or redeemed at a profit.

If bonds are sold prior to maturity, the proceeds may be more or less than original cost. A credit rating of a security is not a recommendation to buy, sell or hold securities and may be subject to review, revisions, suspension, reduction or withdrawal at any time by the assigning rating agency.

Commodities and currencies are generally considered speculative because of the significant potential for investment loss. They are volatile investments and should only form a small part of a diversified portfolio. Markets for precious metals and other commodities are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising.

Investing in REITs can be subject to declines in the value of real estate. Economic conditions, property taxes, tax laws and interest rates all present potential risks to real estate investments.

High-yield bonds are not suitable for all investors. The risk of default may increase due to changes in the issuer's credit quality. Price changes may occur due to changes in interest rates and the liquidity of the bond. When appropriate, these bonds should only comprise a modest portion of your portfolio.

Beta compares volatility of a security with an index. Alpha is a measure of performance on a risk-adjusted basis.

The process of rebalancing may result in tax consequences

Alternative investments involve specific risks that may be greater than those associated with traditional investments and may be offered only to clients who meet specific suitability requirements, including minimum net worth tests. Investors should consider the special risks with alternative investments including limited liquidity, tax considerations, incentive fee structures, potentially speculative investment strategies, and different regulatory and reporting requirements. Investors should only invest in hedge funds, managed futures, distressed credit or other similar strategies if they do not require a liquid investment and can bear the risk of substantial losses. There can be no assurance that any investment will meet its performance objectives or that substantial losses will be avoided.

The companies engaged in business related to a specific sector are subject to fierce competition and their products and services may be subject to rapid obsolescence. Investing in the technology sector is not suitable for all investors.

The indexes are unmanaged and an investment cannot be made directly into them. The Dow Jones Industrial Average is an unmanaged index of 30 widely held securities. The NASDAQ Composite Index is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The S&P 500 is an unmanaged index of 500 widely held securities. The Shanghai Composite Index tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange.

The VIX is the Chicago Board Options Exchange (CBOE) Volatility Index, which shows the market's expectation of 30-day volatility.

The MSCI Emerging Markets Index is used to measure the financial performance of companies in fast-growing economies around the world. The MSCI China A Index measures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges. The MSCI Pacific Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in the Pacific region. The MSCI USA Index is designed to measure the performance of the large- and mid-cap segments of the US market. The MSCI Europe index is a European equity index which tracks the return of stocks within 15 European developed markets.

The Bloomberg Barclays US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

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