

Market Commentary

The second quarter of 2026 delivered one of the most powerful risk-on reversals in modern market history. After the U.S.-Iran conflict drove a sharp first-quarter selloff, markets staged a violent recovery beginning in early April as fears of a prolonged energy crisis gave way to de-escalation, resilient corporate earnings, and renewed enthusiasm for the AI investment cycle. The S&P 500 gained 15.2% for the quarter — its best quarterly performance since the post-pandemic rebound of 2020 — erasing the first quarter's losses and lifting the index to a gain of roughly 10.2% for the first half of the year.

The rally began from a place of deep pessimism — in early April, the Russell 2000 sat marginally below its November 2021 highs, oil hovered near \$100 per barrel, and rate cut expectations had been fully priced out. From there, both the market and the macro backdrop improved dramatically. A June U.S.-Iran Memorandum of Understanding reopened the Strait of Hormuz, and Brent crude fell from its quarterly peak near \$118 per barrel to roughly \$73 by quarter-end, back below pre-conflict levels. The inflationary damage, however, was already done: core PCE inflation reached 3.4% year-over-year in May, its highest reading since 2023. The Federal Reserve — now led by new Chair Kevin Warsh — held its policy rate steady at 3.50%–3.75%, but the June dot plot revealed a decidedly hawkish shift, with the median official now projecting a rate hike in 2026. Markets ended the quarter pricing in two hikes by year-end, a full one-percentage-point swing in expectations from January, when the consensus called for two cuts.

Performance across asset classes reflected the risk-on tone. The advance in equities, initially led by large-cap growth and the hyperscalers, broadened dramatically by quarter-end, with small cap, equal-weight, and value benchmarks all reaching new record highs, while semiconductors stood out on robust AI capital spending. Fixed income produced modest positive returns despite the hawkish repricing: the Bloomberg U.S. Aggregate Bond Index returned +0.7% as Treasury yields across the curve rose modestly. Corporate fundamentals remained the market's foundation, with the S&P 500 expected to report year-over-year earnings growth above 20% — a seventh consecutive quarter of double-digit growth — alongside revenue growth of roughly 12%, the fastest pace since mid-2022.

Looking Ahead to Q3 2026

The setup for the third quarter is constructive but not without risks. Inflation remains well above the Federal Reserve's 2% target, and the possibility of rate hikes — something few investors contemplated at the start of the

Q2 2026

year — is now a live debate. The U.S.-Iran de-escalation, while encouraging, remains fragile. Beneath the surface, June brought a notable leadership rotation toward industrials, financials, and health care, with the equal-weight S&P 500 breaking out to new highs even as the cap-weighted index consolidated — a signal of healthy, broadening participation. With analysts projecting earnings growth above 20% for the remainder of the year and the AI buildout showing no signs of slowing, we believe the fundamental backdrop remains supportive. Active risk management remains an important focus for navigating what could be a volatile path ahead.

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