



**Overview**

Financial markets navigated a dynamic and evolving environment throughout the second quarter, balancing strong underlying fundamentals with increasing pressure from inflation and shifting monetary policy expectations. Equity markets rebounded sharply in April and extended gains through much of May, supported by resilient earnings, a stable labor market, and continued enthusiasm surrounding artificial intelligence. As the quarter progressed, however, rising interest rate expectations, persistent inflation pressures, and geopolitical uncertainty contributed to increased volatility and a moderation in market momentum.

**Capital Markets**

Equity markets advanced during much of the quarter, with major indices reaching new highs as improving sentiment and strong earnings growth supported performance. April marked a clear turning point following first-quarter weakness, while May extended the rally, driven by robust corporate fundamentals and structural growth themes.

By June, however, market leadership began to shift, with increased volatility and a more mixed performance across asset classes. A rotation away from large-cap technology and AI-driven equities emerged late in the quarter, reflecting valuation considerations, AI cap-ex spending concerns, and heightened sensitivity to potential higher interest rates. As a result, equities finished the quarter near highs but with a more uneven and volatile pattern relative to earlier strength.

**Table 1 – Equity Total Returns – June 30, 2026**

Equity	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year
S&P 600	7.29	19.70	23.90	37.50	16.05	7.37	11.52
MSCI Emerging	-1.41	24.05	23.85	43.51	23.03	7.20	10.07
Russell 2000	3.74	21.49	22.57	40.78	18.60	6.98	11.62
S&P 400	3.59	14.47	17.34	25.89	15.41	9.07	11.65
NASDAQ	-2.75	21.60	13.13	29.48	24.74	13.40	19.44
S&P 500	-0.95	15.20	10.21	22.32	20.61	13.41	15.51
Dow Jones Industrial	2.71	13.38	9.76	20.65	17.10	10.78	13.68
MSCI Developed	0.07	10.82	9.44	20.23	16.44	9.05	9.66

Similar to last year, diversification is playing an important role in controlling the risk and return profile of portfolios as small-caps, mid-caps, and emerging markets have out-performed large-cap stocks on year-to-date and one year basis.

In fixed income markets, yields moved higher over the course of the quarter, with more pronounced increases occurring in May through mid-June as robust inflation data and strong economic reports prompted a recalibration of interest rate expectations. Bond prices



strengthened a bit late in the quarter as yields moved modestly lower, though the broader trend remained one of elevated rate levels.

The rise in yields, coupled with a flattening yield curve, underscored growing sensitivity to both inflation and policy uncertainty.

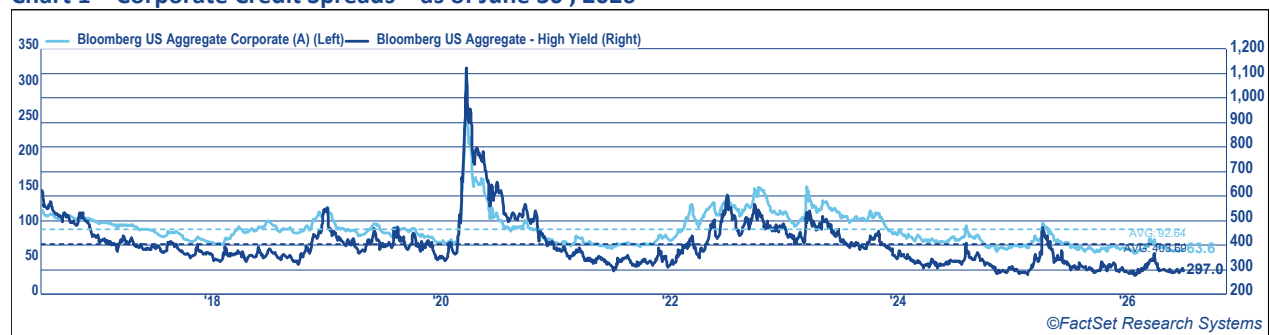
The 2-year Treasury yield rose 36 basis points, from 3.79% to 4.15%, while the 10-year Treasury yield increased 12 basis points, from 4.32% to 4.44%. During the quarter, closing yield highs reached 4.23% for the 2-year on June 22 and 4.66% for the 10-year on May 19.

**Table 2 – Fixed Income Total Returns – June 30, 2026**

Commodity	1-Month	3-Month	YTD	1-Year	3-Year	5-Year	10-Year
Bloomberg Michigan Muni	0.99	2.61	2.49	7.25	3.98	1.10	4.66
Bloomberg Municipal	0.96	2.50	2.32	7.03	3.76	1.05	2.15
Bloomberg High Yield	0.27	2.47	1.96	5.91	8.86	4.17	5.81
Bloomberg Municipal 5-Year	0.45	1.07	1.08	3.81	3.45	1.23	1.80
Bloomberg Aggregate	0.24	0.67	0.62	3.79	4.16	0.08	1.54
Bloomberg Inter Gov't/Credit	0.10	0.43	0.40	3.14	4.68	1.22	1.92

The tightening of corporate credit spreads more than offset the rise in yields, which helped taxable bonds eke out small gains for the quarter. Like stocks, corporate bond prices were under pressure due to credit spreads substantially widening at the onset of the Iran war but have since moved sharply lower ending the quarter well below historical averages. Corporate debt trades at a spread to treasury bonds and is how investors are compensated for assuming the risk of a company’s ability to timely pay interest and ultimate repayment of principle.

**Chart 1 – Corporate Credit Spreads – as of June 30 , 2026**



Credit spreads are an important indicator of corporate health and economic resilience. Tight spreads signal investor confidence that companies can service debt, manage higher input costs, and sustain profitability. They also support broader financial conditions by encouraging corporate borrowing for research, capital investment, and merger and acquisition activity.



Private credit markets, however, showed signs of stress as continued withdrawal activity pointed to tighter financial conditions beneath the surface. Liquidity mismatches and elevated redemption requests highlighted risks not fully reflected in public market performance. Many private funds continue to limit withdrawals because investor demand for liquidity exceeds the ability to raise cash from illiquid assets.

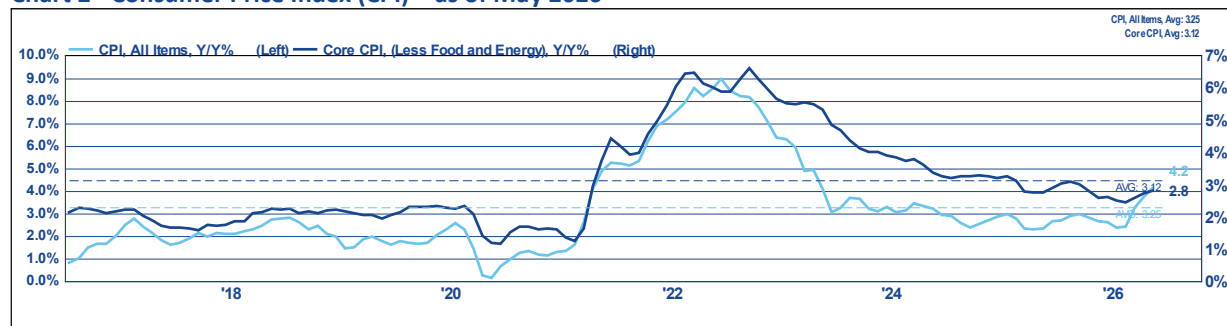
**Economy**

The economic backdrop remained resilient throughout the quarter. Labor market conditions continued to demonstrate stability with April and May nonfarm payrolls exceeding expectations and unemployment remaining steady. Broader economic data—including manufacturing and services activity—pointed to continued expansion.

Growth conditions also improved modestly, with upward revisions to first quarter GDP reinforcing the view of a stable economic foundation. The final estimate of first quarter GDP was revised upward to 2.1% from 1.6%. At the same time, measures of recession risk declined as incoming data continued to exceed expectations along with positive Iran conflict resolution developments.

Inflation emerged as a central theme during the quarter. Elevated CPI and PPI readings in April and May reinforce the view that price pressures remain persistent. This dynamic has become a key factor influencing market behavior, particularly as inflation trends increasingly shape expectations for monetary policy.

**Chart 2 - Consumer Price Index (CPI) – as of May 2026**



While core inflation measures, which exclude food and energy, showed signs of stabilization later in the quarter, headline inflation remained elevated due mostly to energy-related influences tied to geopolitical developments. This divergence between core and headline inflation contributed to ongoing uncertainty in the macroeconomic outlook.

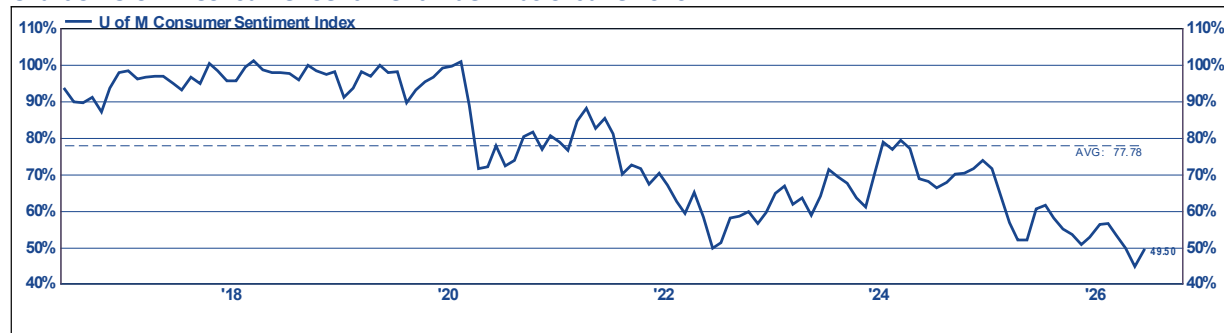
Consumer activity remained firm as April and May retail sales readings handily bested consensus, though underlying concerns regarding the durability of consumer spending are building, driven by elevated price levels, high borrowing costs, and softer sentiment readings.



Forward-looking survey components increasingly reflected concerns around rising input costs, inflation, and supply chain disruptions, suggesting that economic strength may be accompanied by mounting cost pressures.

In fact, the U of M Consumer Sentiment Index posted its lowest reading on record (44.8) in May as persistent high gas prices and inflation intensified household cost-of-living concerns and weighed further on consumer sentiment. This index started monthly reporting in November 1952.

Chart 3 - U of M Consumer Sentiment Index – as of June 2026



### Federal Reserve

Monetary policy expectations shifted meaningfully over the course of the quarter. Entering April, markets broadly anticipated a more accommodative Federal Reserve stance; however, as inflation persisted and economic indicators remained firm, expectations evolved toward a more cautious and increasingly hawkish rate policy outlook. By late June, market expectations for potential rate increases later in the year had risen significantly, reflecting both resilient economic data and persistent inflation concerns. The bond market is currently pricing in two rate hikes by the end of the year.

A notable development during the quarter was the transition in Federal Reserve leadership, with the new Chair Kevin Warsh introducing a framework built around five key task forces aimed at addressing evolving economic conditions. These Fed initiatives are focused on communications and transparency, size of balance sheet, data sources used, productivity, and inflation frameworks. Refreshingly, these task forces will draw on internal Fed resources and external experts.

While the full implications of these efforts will develop over time, the structure reflects a Federal Reserve that is operating in an increasingly complex environment, where traditional policy tools must incorporate a broader set of structural considerations.

Early messaging has emphasized a data-dependent approach, acknowledging that inflation risks remain elevated and may require a more measured and flexible policy response. As a result,



markets have increasingly focused not only on near-term rate decisions, but also on the broader policy framework guiding those decisions.

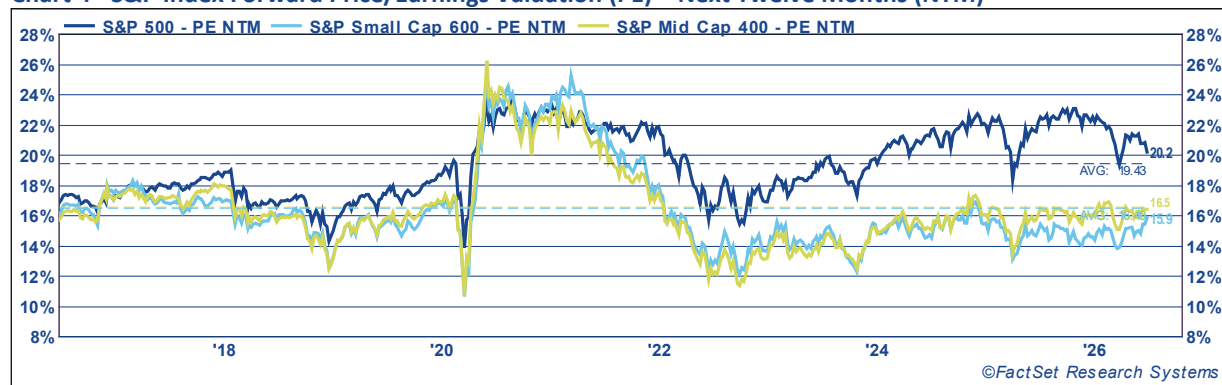
**Market Dynamics**

A defining characteristic of the quarter was the market's ability to reconcile rising uncertainty with improving fundamentals. Throughout April and much of May, investors consistently rewarded strong earnings, resilient economic growth, and the productivity benefits associated with artificial intelligence, while largely discounting geopolitical risks and higher interest rates. Even periods of heightened volatility surrounding the Iran conflict proved temporary, as markets repeatedly recovered on signs of de-escalation and continued confidence in corporate profitability.

Strong corporate earnings remained the primary support for equity valuations throughout the quarter. First quarter results substantially exceeded expectations and drove meaningful upward revisions to full-year earnings estimates. Early April forecasts called for S&P 500 earnings growth of 13.3% in the first quarter and 14.8% for full-year 2026. By quarter-end, those estimates had increased to 28.6% and 24.0%, respectively, with 9 of 11 sectors reporting earnings above expectations.

The significance of these revisions should not be understated. Earnings growth expanded rapidly enough to offset much of the market's price appreciation during the quarter and played a critical role in keeping valuations in check and helped to maintain investor confidence despite rising interest rates and inflation concerns.

**Chart 4 - S&P Index Forward Price/Earnings Valuation (PE) – Next Twelve Months (NTM)**



Market leadership, however, began to broaden as the quarter progressed. After leading much of the advance, AI-related and large-cap technology stocks experienced periodic bouts of weakness as investors rotated into more cyclical areas of the market. At the same time, rising bond yields and shifting expectations for Federal Reserve policy increased sensitivity to



economic data releases, reinforcing the notion that market performance is becoming increasingly dependent on the balance between earnings growth, inflation, and interest rates.

### Closing Perspective

The second quarter reflects a market transitioning from one driven primarily by earnings strength and growth optimism to one increasingly influenced by inflation and monetary policy considerations. While underlying economic conditions remain stable and corporate fundamentals continue to support valuations, rising rate expectations, shifting market leadership, and geopolitical uncertainty have introduced greater complexity into the investment landscape.

Encouragingly, strong earnings growth has largely justified the market's advance, while eased recession concerns and continued economic resilience have provided an important foundation for investor confidence. At the same time, persistent inflation pressures, prolonged conflict resolution uncertainty, and growing sensitivity to monetary policy expectations suggest that future returns may become increasingly dependent on earnings execution rather than multiple expansion.

As a result, we believe the environment that justified an overweight position in equities has become more balanced. With both opportunities and risks appearing more evenly distributed, a return to a more neutral allocation posture is appropriate. Maintaining diversification and discipline continues to be the most prudent approach as investors navigate an environment defined by strong fundamentals, evolving policy expectations, and ongoing geopolitical uncertainty.

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Sources: FactSet, Federal Reserve, FactSet Earnings Insight, U.S. Bureau of Economic Analysis, University of Michigan, U.S. Census Bureau, U.S. Bureau of Labor Statistics.

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