August 2026

Where is the year going! I can't believe it's August and NFL football camps are in progress.

The second half of the year has started off dominated by the same headlines - news around the Iran War and AI (artificial-intelligence). Over the past 2 weeks, we have seen a rotation out of some of the chip and semiconductor names and into the broader market. The biggest reason is investors are looking at free cash flow and the capital spending these companies are dedicating to technology and wondering how that will translate into returns (Source: Invesco). One example of this is with Googles earnings announcement; they announced record earnings along with massive AI spending and the stock fell 10 % as a result (source: Morgan Stanley). They also saw their free cash flow drop. Remember, companies like Google create products and sell subscriptions and services. In most cases, once the product is developed it takes minimal expense to upgrade. This created tremendous amounts of free cash flow. So, these large tech companies with their commitment to the data centers, supporting services, and the build out of AI are adding overhead that did not exist before and reducing their free cash flow.

Overall, Morgan Stanley remains positive on the markets long term and view this as more of a healthy correction, especially given the recent gains across those sectors. One of the biggest risks we see currently is the conflict in the Middle East and if that translates into higher energy costs and raising inflation long term. This was also reflected in the most recent Federal Reserve comments. While they left the benchmark rate unchanged at 3.50-3.75%, they described economic activity as "expanding at a solid pace despite elevated uncertainty that, in part, is due to the conflict in the Middle East" (Source: Reuters). Morgan Stanley's current view is that the Federal Reserve will remain on hold with regard to interest rates through the end of 2026.

The Commerce Department reported that US economic growth slowed to 1.5% in the second quarter. Some of the slowdown could be attributed to rising imports to fuel the AI boom along with decreased spending. As a reminder, imports count against US growth calculations because the products are not made in the US (source: WSJ). However, in the same report they showed that consumer spending rose at a 3.2% rate which was up from 0.5% in the first quarter. The consumer also got a little bit of price relief in June due to the drop in energy costs. According to the Labor Department, consumer prices were up 3.5% in June from a year earlier, this was less than the 4.2% rate we saw in May which had been lifted by gasoline prices.

Enjoy the rest of your summer and let us know if you need anything.

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