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WEALTH MANAGEMENT

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The 2nd quarter 2026 delivered a sharp rally in stocks around the world, but beneath the surface, the rebound after a turbulent start to the year looked less like a permanent resolution of risk than a temporary reprieve from it. Stock gains during the quarter were built substantially on the easing of the US-Iranian conflict. A ceasefire in early April and a formal Memorandum of Understanding (i.e., MoU) in mid-June allowed oil prices to retreat from their peak with shipping traffic resuming through the Strait of Hormuz. While the price of oil fell, it never fully returned to its level at the start of the year as both sides of the conflict claimed the MoU had been promptly violated by the other. For much of the quarter, global stocks moved with the oil headlines rather than any durable improvement in the fundamentals. Interestingly, stock markets would rejoice and rally each time a resolution was proclaimed, only to be modestly disappointed a few days later when it became apparent the "victory" was more of a mirage than reality. This cycle of euphoria to mild disappointment back to euphoria seemed to happen every few days – a reminder of how fragile the rally's foundations really are.

Stocks in the US posted one of the strongest quarters in a long time, but the rally's internal dynamics raised more questions than answers as the quarter went on. Early gains were concentrated in large-cap technology and AI stocks, while participation only slowly broadened out to other parts of the market. The month of June brought a troubling reversal: the "Magnificent 7" mega-cap tech stocks, which had powered a significantly disproportionate amount of gains over the past few years, lost ground. Semiconductor stocks surged instead, helping to keep the broad market afloat, but the enthusiasm shifted away from the AI leaders themselves towards the memory-chip and infrastructure suppliers. Investors apparently have gotten bored with stocks that can swing +100% over a year and have now moved onto ones that can swing +100% in a month. This rotation could reflect maturing conviction of the AI thesis, or could just as easily signal cracks forming in the speculative trade that has propped up the market for years.

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The lower inflation narrative that markets had counted on over the past few years started to break down over the course of the 2nd quarter as well. Progress towards the Fed's target rate stalled, headline inflation reaccelerated, and core inflation stopped improving – all while the Federal Reserve held rates in restrictive territory with no indication that relief is coming. Economists, meanwhile, widely expect growth to slow in the second of the year. The economy, in other words, is being asked to keep supporting elevated stock prices and valuations without the benefit of lower rates.

Speaking of the Federal Reserve, leadership of the Fed had its first change since 2018 as Kevin Warsh was confirmed and sworn in as chairman on May 22nd, succeeding Jerome Powell. As a former White House economic aide, member of the Federal Reserve Board of Governors, and Wall Street banker (coincidentally, at Morgan Stanley), Warsh became the 11th Fed Chair in the last 90 years. He has quickly signaled that he wants to be tough on the stubbornly-elevated inflation that has plagued consumers the past few years. In the eyes of some, this means an increased chance of interest rate hikes moving forward. Higher interest rates to combat inflation, however, would go against the lower rates that President Trump made clear is his desire for the economy. So going forward, the big question is whether the "regime change" rhetoric translates into concrete action by the Fed, such as formally revisiting the 2020 average-inflation-targeting framework, or whether it remains mostly rhetorical while the FOMC continues its steady-as-she-goes approach on rates. That, along with how markets and the US dollar value respond to perceptions of White House influence over the Fed, is certainly an open story worth watching.

Taken as a whole, the quarter looked more like a relief rally than a genuine turning point. A stock market that climbed a wall of worry built on an unresolved US-Iran conflict, threats of higher inflation, a central bank in no hurry to help, decelerating growth expectations, and an AI trade that may be staring to fracture beneath its own hype. Our team thinks investors would do well to treat the 2nd quarter's gains with caution rather than confidence.

From a performance standpoint, the 2nd quarter turned out to be the best quarter for major US stock indexes since 2020, reversing losses from the beginning of the year. With the momentum behind the AI and technology themes, it was the S&P 500 and Nasdaq Composite indexes that led the charge higher. The S&P gained +15.2% while the Nasdaq jumped +21.6%, bringing their year-to-date (YTD) gains to +10.2% and +13.1%, respectively. The Dow Jones Industrial Average gained +13.4% during the quarter, resulting in a YTD return through the first six months of the year of +9.8%[i]. The Dow's comparatively modest gain relative to the two other indexes largely comes down to its composition: it's price-weighted rather than market-cap-weighted, holds only 30 companies, and skews more toward industrial, financials, consumer staples and healthcare stocks – sectors that simply haven't ridden the same AI and semiconductor wave the way tech has.

International stock markets were roughly in line with the S&P 500's quarterly gain but modestly behind it for the full first half. The MSCI EAFE Index (the benchmark for stocks in countries with more mature and developed economies) gained +10.8% for the quarter and is now +9.4% YTD. Emerging markets were the real standout during the quarter. The MSCI Emerging Markets Index (measuring stocks in countries with smaller and still-developing economies) was up +24.1% for Q2 and is now up +23.9% YTD[ii], the best performance among major stock indexes, building on strong 2025 gains and benefiting from Asia's central role in the AI hardware supply chain.

Core US bonds had solid but unexciting results during the 2nd quarter. The Bloomberg US Aggregate Index (the broad measurement for taxable bonds) returned +0.7% for the quarter and stands at +0.6% YTD[iii]. The relatively muted move in core bonds mask a fair amount of volatility (as least for bonds) underneath the hood. The 10-year maturity US Treasury bond ended the quarter close to where it started (near 4.4%) but climbed to nearly 4.6%[iv] by mid-May amid inflation concerns before retreating as oil prices fell back. Fed Chair newcomer Warsh's more hawkish tone and projections of several other Fed officials favoring rate hikes added to the interest rate volatility in June.

Outside of traditional stock and bond markets, broad commodities were mixed but mostly positive for the first half. The Bloomberg Commodity Index, a broad measurement of a diversified basket of commodity prices, posted one of its strongest first-half performances on record, driven largely by energy[v]. Oil roughly doubled early in the year after the outbreak between US and Iran, but then gave most of that back on news of ceasefire and the MoU. The price of oil ended Q2 down roughly -30% near $70/bbl[vi], but still modestly above where it started the year.

The story for precious metals was that of a sharp reversal after a historic first quarter. Gold and silver were unfairly punished and had their worst quarter since 2013. The price of gold fell -14% closing at $4018/oz. Silver fared worse, as it typically does in corrections, dropping -22% to about $59/oz after touching a quarterly high above $88/oz in mid-May[vii]. The driver was almost entirely macro: rising inflation expectations, a more hawkish Fed, and renewed US dollar strength all worked against the metals after rate-cut-hopes helped fuel the rally earlier in the year. Despite the quarter's declines, the longer-term picture still looks impressive: gold and silver are still up +52% and +103%, respectively, over the past 18 months through the end of June[viii]. And analysts remain optimistic further out with price targets for gold ranging from $5100/oz to $6300/oz – ranging from +25% to +50% from today's prices[ix].

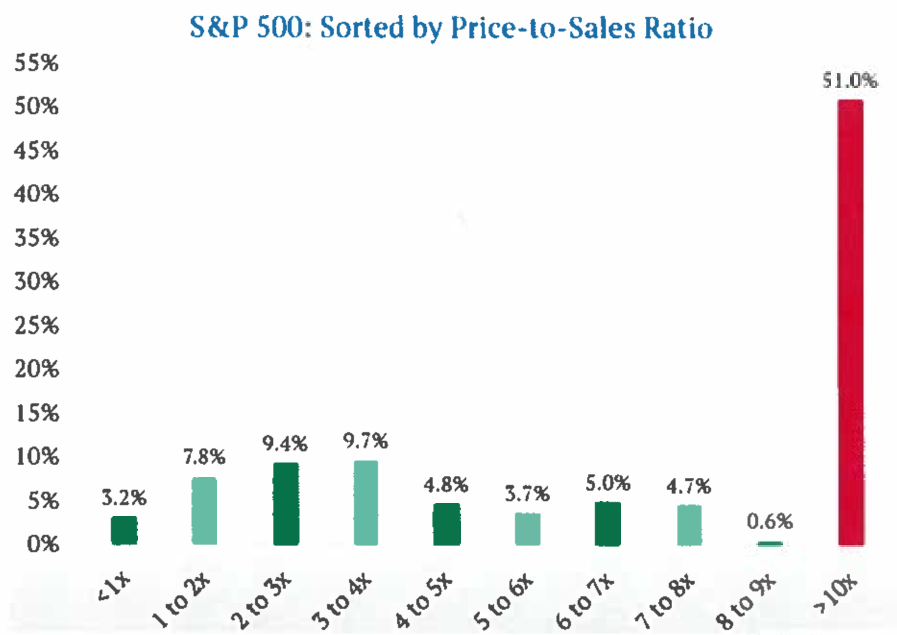
With the recent declines, some have argued the precious metals trade might be over. Our team, however, believes it is only just the beginning. Such misunderstandings have been around for a long time, as the difference between precious meals ***trading*** and precious metals ***investing*** is nothing new. Short-term traders, both skilled and unskilled, tend to track signals for short-term results while long-term investors typically watch history, debt cycles and currency erosion with patient detachment and a steady eye toward wealth preservation. The US continues an unsustainable reliance on debt with total national debt recently crossing $39.5 trillion for the first time in history, an amount up more than 40x from four decades ago[x], with no curbs in spending or budget surpluses in sight. Such patience has served long-term and independent-thinking investors with greater returns (and calm) through periods of headline flux and geopolitical gyrations because they understand the greater direction of the precious metal ball in a debt-saturated and, hence, currency-debasement playing field. Long-term investors see the bigger picture and trend.

On the other hand, our team remains highly skeptical of the stock market's ability to levitate higher on such extreme valuations, largely here in the US. Every so often, usually following a period of a long bull market, the broad investor population can become from the economic realities of the real world. A combination of greed and FOMO can drive an investing mob to chase stock prices to ever higher and more unsustainable levels. In their craze, they drop all caution and fully subscribe to all the exciting narratives about the glorious future ahead. The current casino-like environment of the US stock market is displayed by many unprecedented signs, including the highest ever margin debt, enormous trading in options that expire in a single day, huge amounts of trading in leveraged ETFs, and many stocks moving tens- and even hundreds-of-billions of dollars in market value in just a matter of hours. Warren Buffett recently stated, *"It's tough to find values when everybody is preferring gambling"* during a recent interview[xi]. The Berkshire Hathaway chairman criticized modern market behavior, pointing out that speculative trading has overtaken long-term investing. We have seemingly reached that point again in this long-running bull market that has now smashed previous overvaluation records.

The S&P 500 price-to-sales ratio is one example of that speculation. Today, 51% of the S&P 500's market capitalization is in stocks trading above 10x sales[xii]. 51%...half the index. In 2002, in the aftermath of the dot-com bubble bursting, CEO Scott McNealy of Sun Microsystems, who saw his company's stock price once sky-rocket on the heels of the internet craze, famously said this about his own stock at 10x sales:

> *"At 10x revenues, to give you a 10-year payback, I have to pay you 100% of revenues for 10 straight years in dividends. That assumes I can get that by my shareholders. That assumes I have zero cost of goods sold, which is very hard for a computer company. That assumes zero expenses, which is really hard with 39,000 employees. That assumes I pay no taxes, which is very hard. And that assume you pay no taxes on your dividends, which is kind of illegal. And that assumes with zero R&D for the next 10 years, I can maintain the current revenue run rate. Now, having done that, would any of you like to buy my stock? Do you realize how ridiculous those basic assumptions are? You don't need transparency. You don't need any footnotes. What were you thinking?[xiii]"*

Scott McNealy was explaining why investors had been insane to buy his company's stock at such extreme overvalued levels, after Sun Microsystems stock price crashed -90%. Today, half the S&P 500 trades at the same level. It might be different decade, but it's the same math. And the funny (but not funny) aspect of it is investors will likely, instead of investing in the scary stock market, want to invest in something "safe" like index funds. Well, index funds are the stock market, and the stock market is not safe with half at 10x sales.



Source: Refinitiv, as of 6/5/2026, using % of total S&P 500 market capitalization

We know volatile markets can spark a lot of emotion and concern, so please do not hesitate to reach out to us with any questions. As always, our entire team is appreciative of our relationship, and we thank you for the opportunity to be of service. We stand ready to help address any questions that may be on your mind. Feel free to reach out to us any time.

All the best,

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i All domestic equity returns courtesy of Morgan Stanley Capital Markets Research
ii All international equity returns courtesy of Morgan Stanley Capital Markets Research
iii All fixed income index returns courtesy of Morgan Stanley Capital Markets Research
iv JP Morgan Guide to the Markets 3Q 2026
v "Mid-year commodity review 2026" by Jim Wiederhold of Bloomberg.com, July 10, 2026
vi JP Morgan Guide to the Markets 3Q 2026
vii "Silver Miners Post Record Q2 Output Despite Volatility" by Giann Liguid of investingnews.com, July 23, 2026
viii "LBMA Precious Metals Market Report: Q2 2026" by lbma.org.uk, July 15, 2026
ix "Precious Metals Marekt Recap Q2 2026" by texmetals.com, July 1, 2026
x "National Debt Reaches Unprecedented $39.5 Trillion Mark" by Jackson Moreland of briefs.co, July 17, 2026
xi "Warren Buffett on the market today: by Sarah Min of CNBC.com, July 15, 2026
xii "What Were You Thinking? – The Arithmetic Behind 10x Sales" by arvy.ch, June 18, 2026
xiii "Sun Microsystems, The Greatest Quote & The Rise of the Reckless" by kailashconcepts.com, March 5, 2021

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A basis point is defined as one hundredth of one percent (1%), used chiefly in expressing differences of interest rates.

An investment cannot be made directly in a market index. For index and indicator definitions referenced in this report please visit the following: https://www.morganstanley.com/wealth-investmentsolutions/wmir-defnitions

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Because of their narrow focus, sector investments tend to be more volatile than investments that diversify across many sectors and companies.

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