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ASSET MANAGEMENT

Harmony Insights

INSTITUTIONAL INVESTMENT PERSPECTIVES
FOR NONPROFIT ORGANIZATIONS

Q2 2026

EMPOWERING NONPROFITS | ELEVATING IMPACT

HARMONY NONPROFIT

HARMONY ASSET MANAGEMENT

Executive Summary

Market Performance

Index	YTD
S&P 500	+9.6%
MSCI ACWI IMI	+10.9%
Bloomberg US Aggregate	+0.6%

Key Themes

- Strong economic backdrop
- Elevated speculation
- Sticky inflation
- Higher interest rates
- Remain modestly defensive while emphasizing long-term opportunities

Market Review

After a volatile first quarter driven by the conflict in Iran, global markets rebounded sharply during the second quarter (see Chart 1). Last quarter, we suggested the market reaction would likely prove temporary rather than a lasting shift in economic fundamentals. While the conflict persisted longer than initially anticipated, in short order the markets resumed their upward trajectory.

The markets' upward trend masks the conflicting crosscurrents happening inside the indexes. On the one hand, the economy continues to demonstrate remarkable strength. On the other hand, an ever-dwindling part of the economy accounts for this growth.

Meanwhile, interest rates continued to trend higher in both the United States and abroad. Strong economic growth has contributed to this move, but so too have growing concerns that inflation may remain more persistent than many had anticipated (see Chart 2). While inflation has moderated from its peak, it continues to exceed the Federal Reserve's long-term target, reinforcing expectations that interest rates may remain elevated for longer.

Chart 1: Indexes – 12/31-25 to 6/30/26

Chart data provided by Bloomberg LP

Chart 1:

While the indexes show some volatility from 12/31/25 until 6/30/26, individual securities were dramatically more volatile. Note the quick correction between the start and end of the conflict. While the markets continued higher for a few weeks, the leaders rolled over.

Chart 2: US Treasury Curve

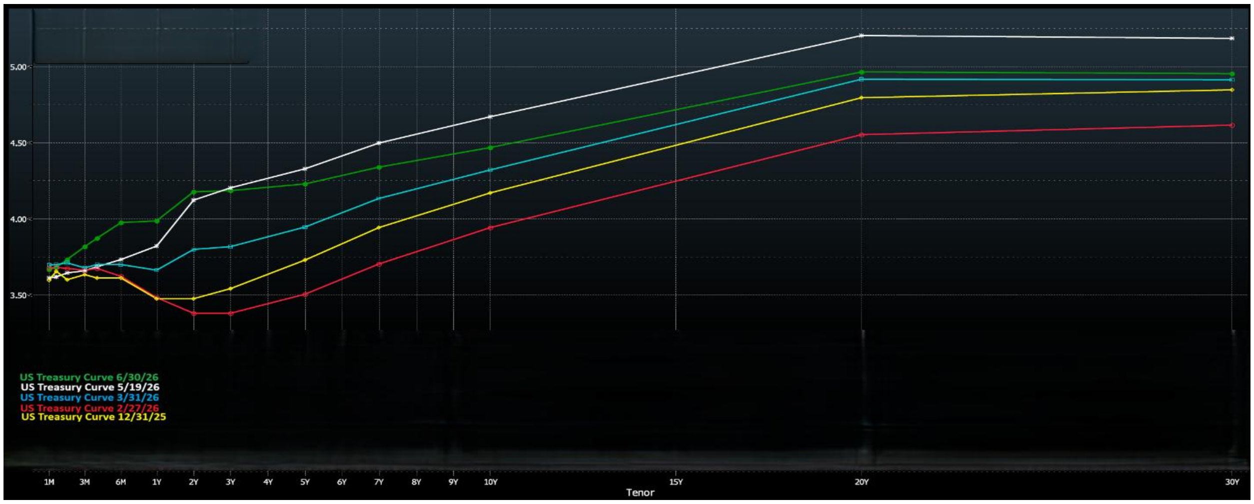


Chart 2:

Notice the change in the shape of each curve. The curve represents interest rates of Treasuries for a given length of maturity starting with 1 month on the left side of the x-axis and ending with the 30yr treasury on the right. The curve in red is as of 12/31/2025, you can see the key in the lower left-hand corner of the chart for the different time series.

Note how rates have risen all year, peaked on 5/19/26 (white line) and then have come off those peaks by the end of June 2026 (green line). Notice how the shorter end of the curve, out to 3 years have moved the most. Also notice that the difference in the yields for 30 years of risk is not appreciably higher than one gets for two years.

Crosscurrents

First Quarter Earnings

S&P 500 average revenues increased 11.6%; earnings rose an astonishing 27.7%, however, removing the tech sector, earnings growth averaged only 5.5%.

Operating Margins

Margins (company profits) were squeezed in many industries; while revenues were up, costs were up even more, putting pressure on profits. This pressure was a result of the war where certain commodities were, and will be, impacted for some time and higher interest rates.

Employment & Wages

Low unemployment persists while wage growth remains subdued (peaking almost 4 years ago). This suggests that productivity has been strong, which is good, but typically, this comes at a cost to employment and wage growth.

Sector Economic Growth

AI-related sectors were the primary source of growth. This went beyond the hyperscalers (Google, Microsoft, Amazon, etc.) and included the memory companies and the semiconductors companies. But it also impacted any industry associated tangentially, including utilities, construction or anything tied to building data centers, powering them or providing platforms for artificial intelligence.

The AI industry has invested hundreds of billions of dollars into infrastructure, with long-term estimates of investments in the trillions. All of this is in anticipation of future profitability based on the belief of overwhelming compute demand. However, Meta recently announced plans to monetize excess computing capacity, just as analysts are predicting a shortage of compute power and thus highlighting just how much guesswork is involved.

Outside of AI-related industries, earnings growth has been considerably more modest, although still generally positive. At the same time, consumers are increasingly relying on debt and the world's largest cash-generating companies have shifted from repurchasing shares with excess cash flow to raising billions of dollars in both debt and equity to finance continued investment. This reversal removes a meaningful source of demand that has supported equity markets for much of the past decade and may become a headwind going forward.

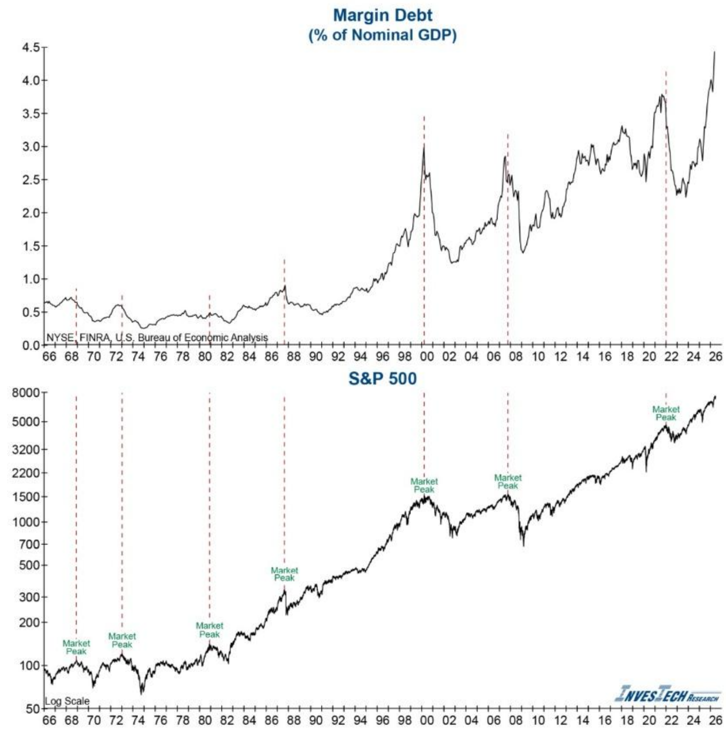
Sticky Inflation

The Fed’s target for inflation has been 2% for six years. However, the latest CPI numbers confirm that the Fed has been unable to bring inflation down to less than about 3%. Weak wage growth will help keep a lid on inflation, but the massive federal spending and pressure on corporate profits are likely to keep inflation from dropping significantly towards the Fed’s goal unless there is a recession.

Margin Debt

Margin debt is at all-time highs (Chart 3), a sign that speculation is very high. The most active assets currently are single-stock leveraged ETFs, and option trading are at all-time highs (the latest expiration at the end of the second quarter was the largest expiration in history), both signs of intense speculation.

Chart 3: Margin Leverage



Margin Debt is the amount of money borrowed by investors to buy stocks on margin. It is an important measure of the public's appetite for risk and the degree of speculation in the equity market. It also represents "hot money" – or the funds that will head for the exit quickly at the earliest sign of trouble or when margin calls are triggered and leveraged positions must be sold.

What We Are Watching

While the economic backdrop remains constructive, the speculative nature of today's markets is our greatest concern. Moderate inflation, when well contained, has historically been compatible with healthy equity market returns. However, today's combination of elevated valuations, increased leverage, and heightened speculation creates an environment where market volatility can accelerate quickly if investor sentiment shifts.

Leverage deserves particular attention because it can amplify both gains and losses. During periods of market stress, leveraged investors may be forced to sell assets to meet liquidity needs, often intensifying market declines. Although elevated leverage alone does not signal an imminent correction, it increases the market's sensitivity to unexpected events.

Within fixed income markets, the landscape has also become more nuanced. Higher interest rates have improved income opportunities but have also increased borrowing costs, making leverage more expensive throughout the financial system. In addition, inflation decreases real returns, which can create a feedback loop which forces rates higher.

While we do not currently view a recession as the most likely outcome, an economic slowdown would likely lead to lower interest rates, benefiting high-quality Treasury securities. Corporate bonds and higher-yield sectors, however, fall as credit conditions deteriorate and spreads widen. Given the significant federal deficits and continued fiscal spending, a recession does not guarantee lower inflation, which would exacerbate real returns even further.

The Bottom Line…

The economy is strong and providing a tailwind. Government spending remains strong, providing a tailwind. Inflation will continue to be sticky, but not out of control at this point, a neutral wind (eye of the storm?), but puts pressure on margins and profits and create questions about valuations. Leverage is elevated and only becomes a problem when something breaks – then it becomes a serious headwind. Speculation remains very high, leading to volatility as traders run from one theme to the next. We have seen examples of this with the Mag 7 which has underperformed the S&P 500 this year. They ran from the Mag 7 to semiconductor stocks and now appear to be rotating out of them (see Chart 1).

All this suggests that we should continue to expect volatility. We intentionally have been underweight our targets by ~5% (70/30 portfolios are running at 65/35) since the beginning of the year. While slightly underperforming our benchmarks, we have been able to capture most of the returns with less risk and hold conviction this is still the best approach given the issues discussed.

We still believe for long-term investors stock offer much better opportunities than fixed income, but the volatility and valuations keep us on the cautious side for now. Utilizing fixed income funds that focus on investment grade and short-intermediate maturities will over a good balance to the crosscurrents we have discussed until such time that a significant pullback provides the opportunity to rebalance back to our more typical weightings.

Regards,

Alan

Alan E. Rosenfield, President

July 7, 2026