SECURITY
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OUTLOOKS

July 2026

ECONOMIC OUTLOOK

Summary

Kevin Warsh chaired his first Federal Open Market Committee (FOMC) meeting in June and left no doubt where his priorities lie. The Committee held rates at 3.50% to 3.75%, but the messaging carried a hawkish tilt. Warsh cut the policy statement to a third of its length, pledging the Committee "will deliver price stability" while dropping the customary reference to maximum employment. He told reporters the Committee's commitment was "strong, unanimous and unambiguous," acknowledging inflation has run above the Fed's 2% goal for more than five years. The Summary of Economic Projections reinforced the shift with the median dot now implying a rate hike by year-end, erasing the cut they had projected in March.

The inflation data drove that shift. The headline Consumer Price Index (CPI) accelerated to 4.2% year-over-year in May, up from 3.8%, driven largely by higher gasoline prices. Excluding food and energy, core CPI sits at just 2.9%, a sign the jump reflects the energy shock rather than broad-based price pressure. With gas prices already retreating, the headline should ease on its own, leaving Warsh firming policy against a number likely to fade. The bigger question is core CPI. While milder than the headline, it remains above target and has been moving in the wrong direction.

Having leaned on recent labor strength as license to set the employment mandate aside, the Fed watched that strength moderate barely two weeks later. June payrolls, released July 2, added just 57,000 jobs against expectations of 113,000, plus 74,000 in downward revisions to prior months. The three-month average slipped to 111,000 from 188,000. The unemployment rate fell to 4.2%, though potentially for the wrong reason. Labor force participation dropped to 61.5%, its lowest since March 2021. A cooler labor market weakens the case for a near-term hike, yet the data remained firm enough to keep rate cuts off the table.

For now, the broader economy gives the Fed room to be patient. First-quarter GDP was revised up to 2.1% annualized, retail sales rose 0.9% in May and ISM Manufacturing held in expansionary territory for a sixth consecutive month. Keeping rates elevated carries real costs for rate-sensitive corners like housing, where Warsh himself called policy "somewhat restrictive." But those pressures sit against a resilient backdrop, with jobless claims subdued and forward-looking gauges like ISM new orders still pointing toward expansion. We expect the economy to stay on solid footing into the second half. The wildcard is core inflation. If it keeps grinding higher, the hike the Committee put on the table could come into play.

Positives

Q1 GDP was revised higher to 2.1% annualized, above the 1.6% estimate

Retail sales rose 0.9% in May, ahead of the 0.6% consensus

ISM Manufacturing Prices Paid Index fell 9.1 points to 73.0 in June, the largest drop since July '22

Negatives

June nonfarm payrolls missed (57k vs. 113k est.), with 74k in downward revisions

Headline CPI accelerated to 4.2% year-over-year, up from 3.8%

Housing starts plunged 15.4% in May to 1,177k

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EQUITY OUTLOOK

Summary

After significant rallies over the previous two months, equity markets took a breather in June with the S&P 500 Index drifting 1.0% lower. Even with that sluggish month, the 15.2% return represented the twelvth-best quarterly performance for that index since 1950. The month of June also saw a bit of rotation out of growth and into value. The Russell 1000 Growth Index lost 2.7% while the Russell 1000 Value Index added 2.3%. International stocks were also relatively flat with the developed MSCI EAFE Index rising 0.1% and the MSCI Emerging Market Index falling 1.4%.

While the equity markets have performed well this year, investors have been focused on the war in the Middle East and elevated oil prices. The situation is far from resolved but markets appear to be less focused on the conflict and oil prices have eased near pre-strike levels. Tax refunds were supposed to boost consumer activity but many of those benefits were offset by higher gasoline prices. Now energy prices seem to be leveling which could provide lift to activity which may benefit equity markets.

The focus headed into the end of the year will likely be on Federal Reserve policy and the midterm elections. The Fed has been on pause and markets are suggesting they may continue to be, but there is a new chair and markets will be closely monitoring activity over the coming months. The election is still months away, but equity markets could respond as they anticipate potential policy changes.

The best word to describe equity markets through half of 2026 is resilient and there does not appear to be much on the horizon to stop that momentum. Corporate earnings have been strong and we do not anticipate any change to that as we move into the second-quarter reporting season. Equity markets tend to follow earnings and that is a great sign as we move into the back half of the year.

Positives

Falling crude oil prices

Easing geopolitical tensions

Corporate earnings growth and profitability

Solid economic backdrop

Negatives

Sticky inflation

Elevated equity valuations

Unknowns

Midterm election

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FIXED INCOME OUTLOOK

Summary

The U.S.-Iran war inches toward resolution as both parties signed a Memorandum of Understanding (MOU) on June 17. Importantly, the MOU states Iran should use its best efforts to ensure safe passage of commercial vessels through the Strait of Hormuz for 60 days. This increased the traffic of oil tankers passing through the strait which drove oil prices approximately 20% lower in June. Last month we wrote about the strong positive correlation between the price of oil and the yield of the 10-year Treasury note. However, this correlation broke down in June as the 10-year Treasury note's yield rose 3 basis points (bps) to 4.47% despite the dramatic fall in the price of oil. The disconnect between interest rates and the price of oil could be driven by many factors, but one culprit could be the Federal Reserve.

The Federal Open Market Committee (FOMC) held a meeting in June and Kevin Warsh, the new chair of the Federal Reserve, hosted his first press conference. Many were expecting Warsh to have a prerogative for lowering interest rates, but he did not indicate a desire to do so. In fact, he emphasized the Fed's primary objective is to meet its 2% inflation target. Additionally, members of the FOMC updated their outlooks for the overnight bank funding rate and half the committee is projecting at least one 25 bp increase to the rate by year-end. This outlook likely influenced short-term Treasury yields as the 2-year and 5-year Treasury notes finished June higher in yield by 17 bps and 9 bps, respectively. We view the front end of the curve as attractive since we do not believe the Fed will raise interest rates this year.

The investment-grade bond market broke a record for the most issuance ever in the month of June with $202 billion of supply. This was more than double the average issuance in June over the last four years. This record issuance was driven by a handful of large deals, specifically NVIDIA and SpaceX both issued $25 billion of debt. It is likely the heavy issuance will continue through the back half of this year as companies continue to issue bonds to fund the infrastructure buildout for AI. Investors are not deterred by the issuance as demand remains resilient with spreads near all-time tight levels. The Bloomberg U.S. Corporate Bond Index ended June with a spread of 74 bps, just 3 bps wide of the tightest level the past 20 years. We would not be surprised if spreads remain near historically tight levels for the remainder of the year given the strength in the economy and corporate earnings. Both Treasuries and investment-grade bonds posted marginally positive returns for the month of June.

Positives

Yields remain attractive relative to the past 20 years

Markets are now expecting a Fed rate hike which is not a guarantee

Oil prices have declined from elevated levels, relieving pressure on inflation

Negatives

Fed rate cuts are unlikely this year

GDP growth and the labor market remain resilient

Record investment-grade corporate bond issuance expected in 2026

Unknowns

Final resolution to the U.S.-Iran war