SECURITY
Trust & Investments
5901 College Boulevard, Suite 100
Overland Park, KS 66211
913-319-0350

OUTLOOKS

August 2026

ECONOMIC OUTLOOK

Summary

The initial data for second quarter GDP shows 1.5% annualized growth and that is the number on which most people will focus. It came in below expectations and marked a slowdown from the first quarter's 2.1% pace. Behind the headline, though, real final sales to private domestic purchasers accelerated to 3.9%, the fastest pace in more than three years. That measure strips out trade, inventories and government spending to capture genuine private consumer and business demand. For the quarter, consumer spending rose 3.2% and business investment grew 8.4%. What held the top line number down was a surge in imports and an inventory drawdown, but the consumer was stronger than the headline number would indicate.

Real consumer spending rose 0.4% again in June, matching its strong May reading. And while aggregate retail sales looked soft at 0.2%, cheaper energy prices during the month distorted the math. The retail sales control group, which feeds directly into GDP, rose 0.5% and has been solid in every month of 2026. The quarter ended with spending momentum intact, not fading.

Manufacturers may finally be responding to a strong consumer. The ISM Manufacturing Index jumped to 55.6 in July from 53.3, its highest reading since May 2022. Production now sits at a nearly five-year high and the survey's employment index swung back into expansion for the first time since 2023. After roughly three years below the expansion line, broken only briefly in early 2025, the goods economy is scrambling to catch up. Customers' inventories came in at 40.7, low enough to suggest restocking should begin to add to growth in the second half.

It is not all good news, considering how that spending appears to be funded. The personal saving rate fell to 2.7% in June, a near four-year low, down from 4.4% in January. Households are still saving, just less of each paycheck, with spending growing faster than income. That makes the second half less a question of whether households want to keep spending and more a question of income, specifically whether wage growth reaccelerates to meet the pace at which they are already spending. The manufacturing recovery suggests businesses are betting it will. If they are right, firm demand and restocking should carry the economy into the fall in good shape. If not, spending settles gradually back toward what incomes will support, a slower growing economy, not a deteriorating one.

Positives

CPI fell 0.4% in June, the largest monthly decline since April 2020

Core capital goods shipments jumped 2.0% in June, the strongest since Dec '21

NFIB Small Business Optimism Index rose 2.1 points to 97.4 in June

Negatives

Core PCE held at 3.3% in June, the fourth straight month at or above that level

ISM Prices Paid for both Services and Manufacturing are above 70.0

Existing home sales fell 2.4%, with pending sales down 5.4% during June

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EQUITY OUTLOOK

Summary

The Iran war and situation with the Strait of Hormuz remains very fluid and Brent crude oil prices rose 23.6% over the month of July. This comes after oil prices had receded with hopes of some sort of agreement to end the fighting. Equity markets have largely downplayed the conflict but on-again, off-again negotiating and yo-yoing crude prices have elevated near-term uncertainty. Equity markets paused in July with the S&P 500 Index drifting 0.1% lower and unsurprisingly led by the energy sector, which climbed 12.6%.

With geopolitical noise continuing, the market's other primary focus has been on corporate earnings. Approximately three quarters of the S&P 500 has reported for the period and approximately 87% of companies surpassed expectations. This far exceeds recent and historic "beat rates" and has generally been well received by markets and investors. Earnings and profitability, which have been the true drivers of equity market performance for the last several years, continue to impress.

Equity markets are likely to begin paying more and more attention to the upcoming midterm elections. Decentralized prediction markets currently have the most probable outcome split between a Democratic sweep and a congressional split. Either of these scenarios likely result in gridlock in Washington, which should be familiar territory for capital markets. That being said, polling accuracy has been questioned in recent elections and several outcomes have been a surprise to market participants. There is also enough time between now and election day for unforeseen events to swing voter allegiance.

While near-term events have caused temporary distractions for equity markets, the prevailing force has been corporate productivity and earnings growth. The stock market will have pauses, pullbacks and periods of consolidation but the positive momentum still seems clear over the long term. The overall backdrop remains accommodative for equity investors.

Positives

Corporate earnings growth

Healthy labor markets

Negatives

Sticky inflation and uncertain oil prices

Elevated equity valuations

Unknowns

Midterm election

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OUTLOOKS

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FIXED INCOME OUTLOOK

Summary

At the late July meeting of the Federal Reserve's Federal Open Market Committee (FOMC) the decision to keep the overnight rate unchanged came with three dissents favoring a 25 basis point (bp) hike. In his second appearance as Fed Chairman, Kevin Warsh attempted to ease concerns about the hawkish bias, but the bond market took little solace. For the month, the 2-year Treasury note increased by 12 bps to 4.29%, which is more than 65 bps higher than the effective Fed Funds rate. This was the fifth consecutive month yields on the front end of the curve increased bringing the total to nearly 80 bps since the war with Iran began. The rise in short- maturity yields reflects investor expectations the FOMC will soon raise rates to combat the effect of higher oil prices on overall inflation. The yield curve steepened as the 10-year Treasury note increased by 27 bps to end July at 4.74%, the highest yield since January 2025. The overall U.S. Treasury market delivered a return of -1.11% which brought the year-to-date return to -0.84%.

Led by the tech sector, issuance of new investment-grade corporate bonds reached a record for the month of July at $141 billion. This level was 44% higher than in the past four years. January and June were also record-setting months, which brings this year's total issuance to $1.33 trillion, according to JP Morgan research. 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 build out for artificial intelligence (AI). Even with issuance now expected to reach $2 trillion for 2026, investors are not deterred as demand remains resilient. The Bloomberg U.S. Corporate Bond Index ended July with a spread of 78 bps, just 4 bps wider for the month and 6 bps from the tightest level over the past 20 years. Corporate bonds also delivered negative returns for the month and trailed the returns from Treasury notes. At the blended index level, the Bloomberg Intermediate Government/Credit Index returned -0.43% during July placing it in the bottom 20% of monthly returns over the past 52 years.

Looking forward, we still believe it is unlikely the Fed will increase the overnight rate three or four times in the next year. It is more likely that before making strategic moves in either direction, Chairman Warsh waits to receive results from his task forces. He is then likely to proceed cautiously. In the meantime, he is allowing the market to do the work for the Fed and tighten "implicit" monetary policy by increasing rates across the curve. We still expect the short-maturity spectrum to offer extremely attractive yields with longer rates becoming more interesting, albeit with more uncertainty. We recommend maintaining a neutral duration policy. Additionally, while we remain selective, the modest spread widening and resilient demand lead us to maintain our higher allocation to investment-grade corporate bonds.

Positives

Yields remain attractive relative to the past twenty years

Markets are now expecting a Fed rate hike, which may not occur

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

Negatives

Dissents on the FOMC could outweigh the Chair's influence and lead to a rate increase

GDP growth and the labor market remain resilient, show little risk to a rate increase

Record investment-grade corporate bond issuance expected in 2026

Unknowns

Final resolution to the U.S.-Iran war

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