

Economic Commentary Q2 2026

The second quarter of 2026 began with markets still processing the outlook of the Iran conflict and the energy shock that defined the end of Q1 with a sharp selloff in equity markets. Brent crude opened April above \$100 per barrel, and uncertainty surrounding the Strait of Hormuz remained a significant concern. However, as the quarter progressed, a ceasefire evolved into a broader peace agreement, helping oil prices reverse sharply. Brent crude closed the quarter at \$72.92 per barrel, down nearly 28% from April 1. Falling energy prices became the dominant market theme, supporting improving equity prices, credit conditions and easing inflation concerns. Despite that improvement, inflation remained stubbornly elevated, leading to a noticeably more hawkish tone from the Federal Reserve.

Domestic Fixed Income Markets

U.S. fixed income markets generated modest positive returns during the quarter with the Bloomberg U.S. Aggregate Bond Index returning 0.67%. Treasury yields moved higher across the curve as inflation remained elevated and investors adjusted expectations for monetary policy. The 2-year Treasury yield rose to the largest degree from 3.80% to 4.18% while the 10-year Treasury yield increased from 4.32% to 4.47%. Credit markets were a bright spot, as investment-grade and high-yield spreads narrowed amid falling oil prices, reduced recession concerns, and improving corporate earnings expectations. The combination of higher Treasury yields and tighter credit spreads reflected growing confidence in the economy even as investors look towards a more restrictive Federal Reserve policy stance.

Domestic Equity Market

Domestic equities posted their strongest quarterly gains in several years, with the S&P 500 advancing 15.20% as improving geopolitical conditions and lower energy prices supported investor sentiment. The technology sector led the market higher, with the tech-heavy Nasdaq 100 rising 27.73% as enthusiasm surrounding artificial intelligence continued to benefit large-cap growth stocks. Market leadership shifted back toward growth after value outperformed in Q1, with the Russell 1000 Growth Index gaining 16.74% compared to 13.87% for the Russell 1000 Value Index, while the Russell 2000 rose 21.57%. International developed markets lagged US markets with a return of 11.08% but emerging market equities returned 24.14%. Energy was the only major sector to post negative returns as oil prices retreated from elevated levels, highlighting how quickly market leadership can change as macroeconomic conditions evolve.

Federal Reserve

The Federal Reserve maintained the federal funds target range at 3.50% to 3.75% during both its April and June meetings, but policy communication became increasingly hawkish throughout the quarter as officials expressed concern that inflation remained too high. The

June meeting, chaired by newly appointed Fed Chair Kevin Warsh, reinforced this message, with updated projections showing a growing number of policymakers expecting higher rates by year-end and several officials emphasizing their commitment to restoring price stability. Inflation remained well above the Fed's 2% target with a 4.2% CPI reading in May, while labor market conditions softened as payroll growth slowed noticeably and the unemployment rate held at 4.2%, creating a more challenging policy backdrop heading into the second half of the year. Fed Funds futures were pricing in the expectation of at least 1 interest rate hike by year-end, with a Fed Funds effective rate target of 4%.

Summary

The second quarter demonstrated how quickly market narratives can shift, as falling oil prices, improving geopolitical conditions, and stronger risk appetite helped drive gains across equity and credit markets. At the same time, inflation remained well above target, prompting the Federal Reserve to adopt a more hawkish tone despite signs of slowing labor market growth. Looking ahead, investors will remain focused on the durability of the Iran peace agreement, the trajectory of inflation as energy-related pressures fade, and the Federal Reserve's response to the competing forces of persistent inflation and a cooling labor market. While equity markets have recovered sharply, high-quality fixed income continues to offer attractive yields and diversification benefits should volatility return.