

A photograph of a large warehouse interior. The scene is filled with tall, blue metal shelving units (pallet racks) that stretch into the distance. The racks are filled with wooden pallets, many of which are stacked with cardboard boxes. In the foreground, two workers wearing yellow hard hats and light-colored shirts are in motion, pushing a wooden pallet loaded with boxes. The floor is a smooth, light-colored concrete with yellow safety lines. The lighting is bright and even, typical of a modern industrial facility. A semi-transparent dark blue rectangular overlay is centered on the image, containing white text and a logo.

INVESTMENT STRATEGY GROUP

# OUTLOOK 2026

## MID-YEAR UPDATE

JANNEY MONTGOMERY SCOTT LLC

Published: June 2026



# OUTLOOK 2026: MID-YEAR UPDATE

## OVERVIEW

The *Mid-Year Update* offers the Janney Investment Strategy Group's baseline prognostications for the economy, the equity and fixed-income markets, their evolution, and investment implications for the remainder of 2026.

### Economy & Equity Markets ..... Page: 3

- The economic expansion is well-footed with prospects for a bump should the OBBBA continue to induce companies to expend capital on new plant, equipment, and technology.
- Job creation is sufficient to maintain a low level of unemployment, and wage growth is keeping pace, providing the impulse for consumers to spend despite low confidence readings.
- Trade uncertainty has dissipated, but high oil prices have introduced a new variable for businesses to overcome. Improving productivity using AI is a tool to defend or expand margins.
- The rapid pace of corporate profit growth is projected to continue. Cooling inflation and declining oil prices, inducing a monetary policy tailwind, would inject an upward bias for stocks.
- Price pressure relief would impart an impetus for yields to drift lower and may prompt investors to broaden their allocation to sectors and companies beyond the technology industry.
- Commodity prices stand to benefit from the massive construction taking place in data centers, on- and reshoring manufacturing, and the ongoing development of various energy sources.

### Fixed Income & Interest Rates ..... Page: 8

- Heading into 2026, we held a moderately constructive view of the interest rate markets and were anticipating late-year rate cuts anchored by continuing disinflation, fragile labor markets, and a new Federal Reserve chair.
- The Iran conflict shifted that view as energy prices pushed disinflation into the future without any obvious demand destruction in the U.S.
- Instead, we now anticipate a market with no Fed rate cuts, no Fed rate hikes, and rangebound interest rates through the back half of 2026, though that would still be enough to generate solid full-year Aggregate Bond Market returns in the 4.5%–5.5% range.
- Though it is not our base case, tail risks now skew toward higher, not lower, interest rates from inflation, strong job markets, and, importantly, heavier issuance across government and private sector financing needs.
- Valuations in most fixed income sectors, including IG credit and T/E municipals, are on the expensive side of history, but healthy credit metrics and continued real money demand can keep those valuations high.

# ECONOMY & EQUITY MARKETS



**MARK LUSCHINI, CMT**  
Chief Investment Strategist

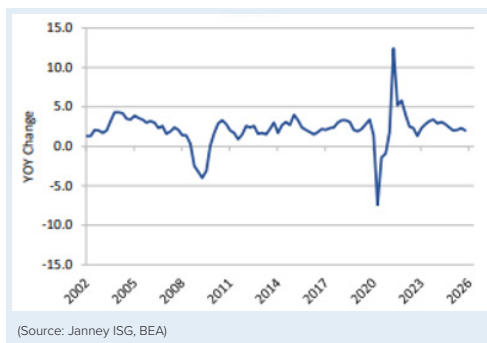
President and Chief Investment Officer, Janney Capital Management

Mark Luschini serves as Janney's Chief Investment Strategist and leads the Investment Strategy Group, which sets the firm's view on macroeconomics, as well as the equity and fixed income markets. In addition, Mark is the President and Chief Investment Officer of Janney Capital Management (JCM), the asset management subsidiary of Janney Montgomery Scott. Under his leadership, JCM has delivered competitive results across its suite of investment strategies and grown its assets under management to more than \$3.8 billion.

Mark has spent more than thirty years in the investment industry. He draws on that experience to speak on topics related to macroeconomics and the financial markets at seminars, client events and conferences. He is frequently quoted in publications ranging from the Wall Street Journal and Barron's to the New York Times and USA Today. In addition, he regularly appears in various media outlets including CNBC, Fox Business News, and Bloomberg Television and Radio. He has an undergraduate degree in Psychology and an MBA in Finance from Gannon University and holds the Chartered Market Technician (CMT) designation from the CMT Association.

The domestic economy continues to expand and has the momentum to continue for the foreseeable future. Gross Domestic Product (GDP) is a measure of the total value of goods and services produced. Its growth rate is driven in large part by consumer consumption patterns. To be sure, business spending chips in as well, as does the government, plus there are factors associated with trade and inventory adjustments. Importantly, its pace has quickened since the fourth quarter of last year, and current estimates from two notable institutions, the Atlanta and New York Federal Reserve Banks, indicate it will be sustained throughout the second quarter of this year. Inside the GDP report is a component known as Final Sales to Private Domestic Purchasers, which strips away government spending and the volatile measures of trade and inventory balancing, giving a cleaner picture of household and business spending. That figure has also firmed since the end of last year and, like the GDP estimate, looks to remain stout going into the year's second half.

Chart 1: US GDP

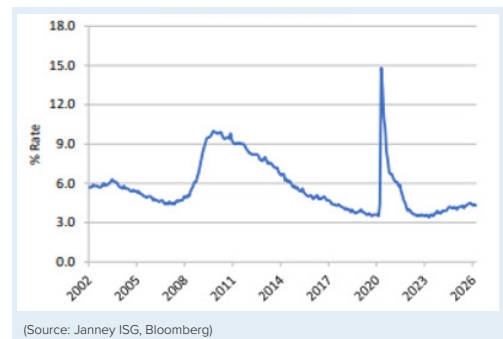


The state of the labor market is key when forecasting the likely path forward for the economy. The good news is that the pace of job growth has markedly improved compared with last year. So far this year, the monthly average of 113,800 tops last year's 9,700/month average by a wide margin. Though it lacks the much larger numbers seen in the past when the economy was expanding, the reduced level of immigration and abundance of early retirements creates less need for massive job creation to sustain

a low unemployment rate. At 4.3% today, it is off the more than half-century low of 3.4% reached in 2023, but its exceedingly gradual climb is unusual and indicative of companies holding on to and still hiring workers even while challenged by geopolitical and trade uncertainty, a spike in oil prices, and elevated inflation. Furthermore, the level is still well below average and, as such, offers a positive signal to households, thereby elevating confidence in their job security.

Last year, most of the jobs created were in the health care and social services industries. The interpretation was negatively biased because not only was it concentrated in just a few areas, but the wages associated with employment in them are commonly below the national average. In addition, they are counter-cyclical and have more to do with demographics and government-supported programming. More recently, not only has the breadth of hiring expanded, but it also includes industries that are economically sensitive, and unlikely to expand payrolls unless the traditional drivers of consumer and business activity warrant. Also, the jobs associated with them generally offer higher wages.

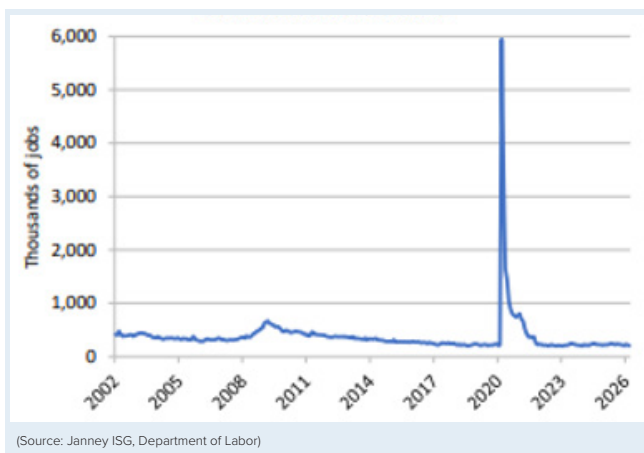
Chart 2: US Unemployment Rate



In the meantime, there is no evidence that companies are broadly shedding employees. Weekly jobless claims, cited as a leading indicator for the labor market, have remained near the low end of a range they have occupied for almost five years. Indeed, not only is the number of new filings near a historic low, but it is also true that, as a percentage of the total labor force,

claims are very close to the lowest since the series was tracked by the Department of Labor in 1967. Until claims begin to move much higher and dwarf the jobs available, the unemployment rate should remain pinned well below trend and support the spending behavior of consumers that is unequivocally necessary to propel the economy in a positive fashion. The soft data captured by surveys of small businesses and the larger manufacturing and services industries point to generally stable or improving confidence in the employment outlook. Similarly, in recent months, households have indicated that jobs are easier to get, resulting in an advance over those saying they are harder to get. With wages growing and the job market firming, the foundation for consumption appears stable.

Chart 3: US Initial Jobless Claims

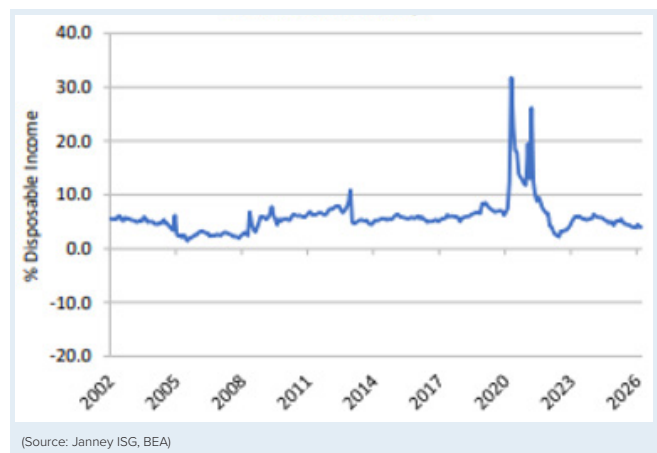


Overall, household finances are in fine shape. Net worth is at an all-time high as stock prices and home values have continued to climb. The wealth effect from that is powerful. It is estimated that for every \$1 lift in net worth, \$0.04 is likely to be spent. With more than \$10 trillion being added to it last year alone, and likely more on top of that so far this year, consumers in the aggregate are well fortified.

Apart from the moratorium placed on student loans and other credit facilities that artificially reduced debt payments in the immediate aftermath of the pandemic, service levels today are near their lowest in more than half a century. In addition, the delinquency rates on all lines of credit, including auto, revolving, and mortgage, are stable or declining but otherwise non-threatening. Of some concern is the precipitous drop in the savings rate. Through the rounds of stimulus checks the government provided to many households intended to support those who may have needed help as the economy recovered from the COVID-induced lockdown, excess savings accumulated to a record amount, allowing households to spend more than would have happened otherwise, incrementally stimulating economic activity. In contrast, not only has that been drawn down, but savings as a percentage of disposable income have fallen to just 2.6%. That rate has only been seen twice in the last 25 years; the housing bubble period in 2008,

when home equity lines were used to fund purchases, and the post-COVID “revenge spending” many undertook when we were once again “free to move about the cabin.” Such a low rate provides little cushion for spending and meeting financial obligations if something causes a slump in the economy and job losses occur. To be sure, it can be rebuilt if wages rise or inflation falls, boosting real wages, so it provides merely a warning to monitor at this juncture. Should delinquency rates creep higher together with a low savings rate, it would flag an increasingly dire prospective development, especially if it scales up the income spectrum.

Chart 4: US Personal Savings



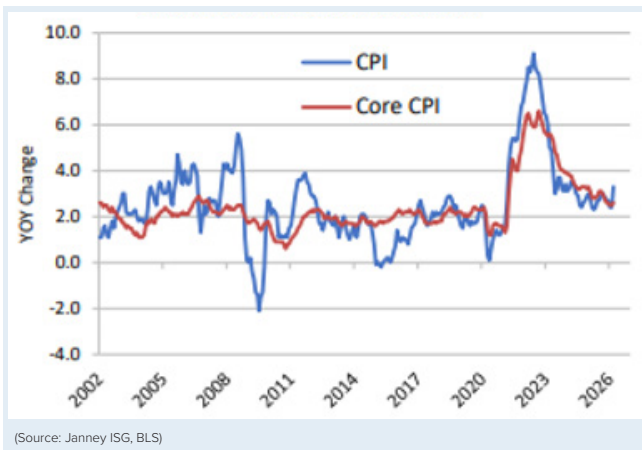
What might the variable be that could undermine the economy by crimping consumption? Inflation. Prices (commonly proxied by the Consumer Price Index or CPI, which is calculated by the Bureau of Labor Statistics) have been running well above the Federal Reserve’s target of 2% since early 2021. Granted, they have fallen meaningfully from the peak of 9.1% in June 2022, but this remains a concern for households and monetary officials alike. Until recently, wages were growing faster than inflation, enabling lower-income cohorts to combat the ill effects of rising prices. Now, with wages teetering on falling below the inflation rate and the primary contributing factor to the surge in CPI over the last two months being energy costs that remain elevated, it appears unlikely prices are about to recede unless there is an imminent resolution to the conflict in Iran, which restores oil supplies through the Strait of Hormuz.

The risk is the second-order effect on prices for things extending beyond energy costs. Headline CPI ripped higher over the last three months to 4.2%, but a measure of core inflation, which strips away food and energy prices (a gauge the Federal Reserve prefers), climbed more modestly to 2.9%. Should core prices begin to reflect the effects of higher transit costs on imports and shipping domestically produced goods, increased fertilizer costs on farm products, and higher prices for items oil or its derivative is feedstock, consumer spending may be negatively impacted likely impairing economic activity.

The average price of a gallon of regular unleaded has risen by over 50% since the conflict broke out, which, according to Brown University's Iran War Energy Cost Tracker, has cost American households an aggregate of \$26 billion (\$47 billion if diesel is included). Fortunately, the drag at the pump has been mitigated by the incremental increase in individual tax refunds, which total approximately \$45 billion more than was distributed last tax season. Therefore, the windfall has cushioned the blow and allowed most households to manage reasonably well so far. The next few months, however, will produce a clearer picture of whether the impact of high energy costs, which takes root with a lag, is filtering through the economy in a more deleterious way.

The bottom line is that the longer the closure of the Strait persists, the more global oil inventories will be drawn down to the point where deliverable oil supply becomes increasingly scarce, driving higher prices. There is a host of uncertainties around the calculus of that scenario, but it's a non-trivial risk. At this point, that outcome is neither imminent nor inevitable, and our view holds that enough ships will begin to transit the Strait before the lack of Gulf-exposed exports triggers an economic setback or worse, a recession.

Chart 5: Consumer Price Index vs Core CPI



The business sector presents an increasingly uniform picture. Similar to reports from the regional Federal Reserve Banks and S&P Global, recent readings from the Institute for Supply Management (ISM) on manufacturing have rebounded, while activity in new orders and capital expenditure plans has improved. Although the services side has been more mixed of late, perhaps reflecting an indication that higher energy prices are beginning to take a toll, it remains deeply in expansionary territory (readings above 50 in the charts below are expansionary as they reflect more than half of the survey respondents indicating activity is improving). Putting the ISM surveys together, the picture points to broad inertia underpinning the economy.

The booming technology sector is playing a major role in lifting and extending the capital expenditure cycle currently underway, which was sparked last year by the One Big Beautiful Bill Act's (OBBBA) juicy incentive for companies to spend.

Chart 6: ISM Manufacturing Index



Chart 7: ISM Non-Manufacturing Index



It is no secret that the basket of companies commonly referred to as hyperscalers (Microsoft, Amazon, Google, Meta, and Oracle) are the poster children for the "hyperspending" that is most certainly driving the copious level of tech spending, but it's also a good portion of overall capital-intensive expenditures by businesses. That group of companies alone is expected to spend more than \$700 billion this year and even more over the next two years on everything from semiconductor chips to hardware and all the equipment needed to establish the massive facilities required for the computational power necessary to generate these large language models, such as OpenAI's ChatGPT, Anthropic's Claude, Google's Gemini, and xAI's Grok.

Along with all that supports the AI ecosystem, the large cloud companies used by businesses that wish to outsource their computing and storage needs continue to grow at a rapid pace, requiring even more data centers and tech equipment. If the past is prologue, a technology-driven capital expenditure cycle increases productivity, leading to faster economic growth, which in turn raises living standards. While some job dislocation will be a byproduct of AI adoption, other positions will likely be

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created within and beyond it, some of which may not even be imagined at this juncture. History serves as a useful guide, showing that innovation disrupts but ultimately leads to more jobs and higher incomes. Let's hope if it doesn't repeat, it at least rhymes.

## CONCLUSION

The economy is growing, supported by solid conditions in the labor market and businesses that are spending capital on plants, equipment, and technology, particularly AI infrastructure. Inflation will likely subside as the base effect from last year's pronounced jump in tariffs works lower, and oil supplies will eventually be replenished, and in our opinion, in time to ward off a supply-side disaster. That should eventually allow the Federal Reserve to renew its campaign of reducing interest rates, even should it not be this year, which adds another potential tailwind helping to extend the current expansion.

## RISKS TO MONITOR

- Job creation is positive, and the number of new jobs necessary to keep the unemployment rate from rising is far fewer than most historical precedents. However, with companies aggressively seeking ways to improve productivity, particularly by way of employing AI, a larger-than-expected displacement of workers cannot be ruled out. Fewer workers with limited wage leverage would restrain spending and dim the prospects for economic expansion.
- Inflation could continue to run at a level well above the Federal Reserve's stated target, generating increased hawkishness among members of the policy-setting committee. A sharp pivot from reducing rates by 1.75% over the past two years, with expectations of more to come, to hiking rates could spike uncertainty and yields, thwart spending, and undermine the upward trajectory of stock prices. The shift would serve to challenge the new Fed Chair, Kevin Warsh, to express soothing rationale and engineer a market-friendly policy solution.
- Exogenously, the war in Eastern Europe is unresolved and may invite Russian President Putin to take more drastic measures to end it, including testing the will and cohesion of the NATO alliance. For markets, the conflict in Iran boils down to oil supply. The longer it is restrained, the more it increases the probability that prices will move materially higher, raising the risk of a global recession as so many countries rely on imports from the Gulf region to fuel their economies.

## INVESTMENT IMPLICATIONS

The positive economic backdrop we forecast underscores our constructive stance on risk assets. Below, we highlight areas of interest and opportunity to express our views in a portfolio.

- **Global Equity Markets** — U.S. stocks should continue to perform well, advancing on positive economic growth and a bright outlook for corporate profits. The dominance of technology companies in the capitalization-weighted S&P 500 index demands that their results continue to deliver on heightened expectations exacerbated by the breathless outlook for compute fed by the AI ecosystem narrative. Cyclical areas within Consumer Discretionary could pick up if rates decline, and Industrials stand to benefit from AI adoption and infrastructure capex.

While we still advocate for exposure to foreign equities, it is a more mixed picture for this year as the rise in energy prices is exerting an uneven impact on global bourses. For instance, a hydrocarbon-dependent area like Europe has been a laggard, but Japan has performed remarkably well due to profligate fiscal measures taken by its new Prime Minister. Taiwan and South Korea have concentrated exposure to companies that are technological leaders competing in the AI arms race and are well-positioned to remain so.

- **Sectors** — Technology companies are in the sweet spot for innovation, cloud computing, and the AI buildout that still seems to have much farther to go. Both Industrials and Utilities are areas adjacent to the tech industry, as they serve the infrastructure and energy needs to support enormous data centers and electrification. Favored secular themes include defense companies, cybersecurity, genomics, robotics, space, rare earth, nuclear, and quantum.
- **Commodities** — Industrial metals, such as copper, lithium, and uranium, and the precious metal silver, should benefit from expenditures on infrastructure, decarbonization, and electrification, both here and abroad. Rare earth metals have been identified as strategically important for national security purposes, and the development of reliable sources for oil and natural gas will keep an interest in energy-related stocks. The stocks of publicly traded commodity companies are an accessible means to gain selective exposure.

## VARIOUS ECONOMIC SCENARIOS AND PROBABLE OUTCOMES

Our prognostication for the U.S. stock market's path forward includes three potential outcomes emanating from various economic scenarios that could unfold. We assign a probability to each, with the highest score given to the scenario representing our base case. In preview, we remain quite bullish overall given the solid economic landscape and favorable corporate conditions. However, with the conflict in Iran still simmering, and the yet-to-be fully restored traffic through the Strait of Hormuz exerting a geopolitical risk premium in oil prices, a less sanguine view could evolve. In this report, we recognize it as a lower probability but real risk that bears monitoring.

### Scenario 1: Optimistic

Economic growth accelerates as personal spending stays well supported by solid labor conditions, while business capital expenditures increase for tech buildouts and other infrastructure boosted by on- and reshoring manufacturing migration. Meanwhile, receding tariff/trade uncertainty and de-escalation in the Iran conflict, leading to lower oil prices, tempers inflationary conditions. Residential borrowing costs fall which spawns an uptick in home projects and sales awakening the slumbering housing market. Interest rate spreads on credit remain tight, showing little sign of stress, and Federal Reserve officials foster an implicit intent to reduce rates. Corporate profits rise to meet or exceed the ambitious current estimates, which compresses the stock market's risk premium. Although led by gains in tech and tech-adjacent stocks, other lagging cyclical sectors perform well, driving the S&P 500 index to 8,200.

**Probability: 20%**

### Scenario 2: Central Case

Corporate profits remain stout, and the economic data continues to provide sufficient visibility to infer that growth will persist well into the future. Consumer spending slows somewhat but continues to demonstrate a startling level of resilience, and household finances across the income spectrum show few signs of duress. The "tax increase" from the tariffs imposed more than a year ago fades, and oil prices begin to drift lower, helping to cool the inflation thermometer. Price relief at the pump and elsewhere boosts consumer and business confidence. Monetary officials hold rates steady, but investors don't view them as overly restrictive, and bond yields trend lower. The AI-themed driver of technology stock performance maintains its momentum and drives the stock market higher, especially given its disproportionate representation in the index by both weighting and earnings. The S&P 500 reaches 7,900.

**Probability: 70%**

### Scenario 3: Pessimistic

The lack of meaningful job growth and the ongoing push to employ AI to improve productivity lead to slower wage growth and less robust spending. Although vessel traffic through the Strait of Hormuz increases and helps to restore global oil supply deficiencies, prices remain elevated. The residual benefits of sizeable tax refunds and lower withholding taxes for many households due to provisions within the One Big Beautiful Bill Act are offset by the rise in energy costs consumers must endure. Spending, the primary propellant of economic activity, slides, and although tech company capital expenditures continue unabated, growth withers. While that gives cause for the Federal Reserve to lean into an accommodative policy setting, stocks are still de-rated since lofty earnings estimates fail to be realized. The S&P 500 experiences a double-digit but not recessionary-sized drawdown to 6,800.

**Probability: 10%**

## BOTTOM LINE: ENSEMBLE FORECAST

Our weightings project a favorable view. As was the case in the initial Outlook 2026, we once again assign a 90% probability to the S&P 500 advancing to new all-time highs from current levels. However, we acknowledge that labor market developments, and now the path oil prices take over the balance of the year, could alter conditions in such a way that the low but non-trivial possibility of a less desirable outcome is delivered.

# FIXED INCOME & INTEREST RATES



**GUY LEBAS, CFA®**  
 Chief Fixed Income Strategist  
 Director of Custom Fixed Income Solutions, Janney Capital Management

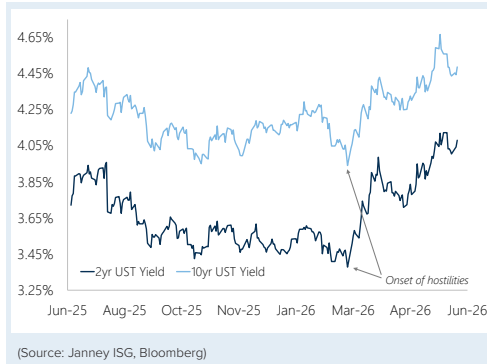
Guy LeBas is responsible for providing direction to the firm's clients on the macroeconomic, interest rate, and bond market investing climate.

Guy authors bond market periodicals which provide relative value recommendations across the fixed income spectrum. Bloomberg named him the most-accurate forecaster of the Treasuries market in 2015 and previously recognized him as a "Bloomberg Best" for his work in bond market forecasting.

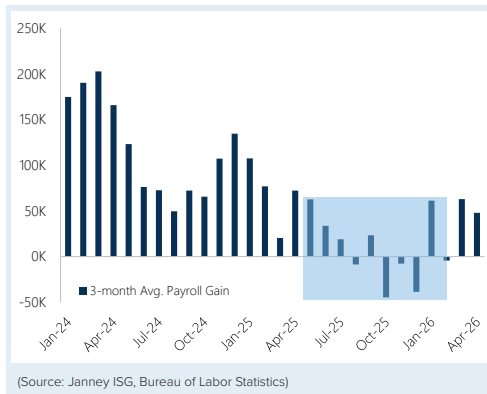
Prior to joining Janney in 2006, Guy served as Interest Rate Risk Manager for U.S. Trust's bank asset and liability portfolios, a role in which he oversaw risk and return on an \$11 billion balance sheet. He received his education from Swarthmore College and is a CFA Charterholder.

In our 2026 Outlook, we argued that interest rates would remain within a range for much of the trading year, with a bias toward modestly lower rates, largely due to late-year rate cuts by the Federal Reserve (Fed). The reasons for this outlook were several. First, the labor market looked fragile with flagging job growth. Second, the disinflation trend following the post-COVID price spike was continuing apace. Third, the Federal Reserve was facing new leadership with a probable dovish bias.

**Chart 8: Interest Rates Rose as the Iran Conflict Shook Market & Fed Faith in Gradual Disinflation**



**Chart 9: US Appears to Have Pushed Through Period of Labor Market Fragility**

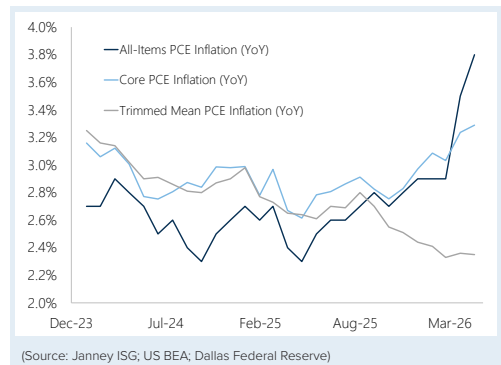


Two of these three things changed this past spring. First, labor market data firmed up after several months of weak job growth. While it is not immediately clear what led to this firming, the rollback of tariffs aided retail-related hiring, sizable tax refunds supported consumer-related hiring, and data center capex encouraged construction-related hiring. Regardless of why, the upshot is that monthly

payroll growth shifted from a three-month rolling average of about -40K in late-2025 to +188K as of May 2026. Our conclusion from this upshift is that labor markets are no longer particularly fragile, and therefore, the Fed is less likely to cut rates to support them.

Second, the Iran conflict led to a global spike in energy prices. Normally, interest rates are not highly sensitive to energy prices, as large swings tend to be mean-reverting and act more like a tax than a source of inflation. The current situation is arguably different in that the memory of the post-COVID inflation environment is so fresh that any increase in prices might reignite consumers' and firms' inflation concerns, risking a self-fulfilling cycle of price hikes. Moreover, U.S. consumer incomes are growing healthily, which increases businesses' ability to pass along higher energy costs to more "core" goods and services. In light of these risks, economic participants have grown defensive about core inflation in 2026. The history of energy price spikes suggests this inflationary view will give way to demand destruction; that is certainly the case in emerging markets, but not obviously so in the U.S. economy.

**Chart 10: Spring 2026's Energy Price Spike Risks Pulling Core Inflation Higher**



The final fundamental rate factor behind our 2026 rate outlook—a dovish tilt at the FOMC—remains partially in place. President Trump nominated Kevin Warsh as Fed Chair; Warsh recently took his seat and will preside over the first FOMC meeting shortly after this note's publication. While Warsh has been

circumspect in public on interest rates, he has suggested that productivity from AI technologies would allow the Fed to maintain lower interest rates at any given level of economic activity. He has also proposed narrowing the Fed's inflation mandate in a way that would skew the analysis to goods and services with lower inflation readings.

But Warsh's vote is only one of 12 on the Fed's rate-setting committee, and the majority on that committee are clearly opposed to cuts for now. Moreover, a new Fed Chair calling for cuts in the face of warm monthly inflation data would impair that same Chair's credibility to push through more reasonable policy actions in the future. In other words, the economic climate has limited the ability of even the most dovish Fed official to act. The hurdle for outright Fed rate hikes remains quite high, however.

In consideration of the unforeseen Iran conflict and mostly related economic developments, we are tempering expectations for interest rates in the back half of the year. Whereas our most likely scenario for overnight interest rates was 2-3x rate cuts, we are moving to an expectation of no activity. Similarly, our forecast for both 2-year and 10-year interest rates was for a small decline in yields, but we now anticipate a modest increase for the full year. For a no-cut/no-hike environment with stable growth, macroeconomic factors suggest trading should be relatively rangebound, with 10-year yields in the low-to-mid-4% range.

Table 1: Rate Outlook

	2Q26 (Act)	4Q26 (Proj)		4Q27 (Proj)	
		Most Likely	Alternate	Most Likely	Alternate
Federal Reserve	3.63%	0x Cuts	1x Cuts	3x Cuts	6x Cuts
2yr UST	4.13%	3.95%	3.70%	3.15%	2.70%
10yr UST	4.52%	4.25%	4.00%	3.80%	3.25%
IG Spreads	73bps	78bps	90bps	80bps	100bps

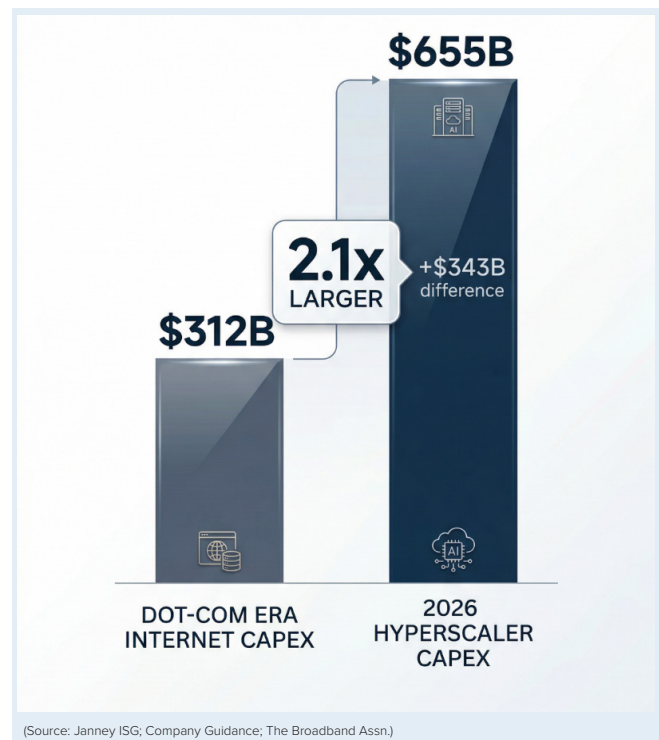
(Source: Janney ISG, Bloomberg, Federal Reserve Board)

Even with range-bound trading and small increases in yields now likely for 2026, we still anticipate solid returns from the fixed income markets. Using the US Aggregate Bond Market Index as a benchmark, YTD returns at the time of publication measured a scant (though still positive) +0.1%. One tool we use to evaluate return prospects is our Janney ISG Real Yields Model. That model projects a 12-month return range for the Agg Index of 7.8% – 9.3%, the highest such projection since late 2023 when interest rates peaked. That return potential is driven first and foremost by income generation (currently just shy of 5% for the index) and secondarily from changes in interest rates.

Admittedly, the risks to this forecast are for higher rates, and the risk to returns is to the downside, a downgrade from the balance we shared at the beginning of the year. However, these risks are more about issuance volumes

than economic fundamentals and are therefore difficult to judge. The U.S. is running a large budget deficit forecast to be -6.3% of GDP in 2026, a -1.0% deepening from the prior year. In addition, there is a mammoth financing need from the Technology sector. In 2026 alone, the five largest data center builders initially guided for \$655 billion in capital spending and have been moving up from there. More than half of this total will require financing, and we estimate a midpoint of \$225 billion of new money issuance in the public bond markets. Government issuance and the tech-sector issuance are essentially competing for dollars, and while demand is plentiful at the moment, there is no easy way to estimate whether this supply will become a more dominant force on interest rates. That supply is the main source of upside risk for interest rates and downside risk for bond market returns through the balance of 2026 and into 2027—though again, high starting yields should be sufficient to power attractive returns.

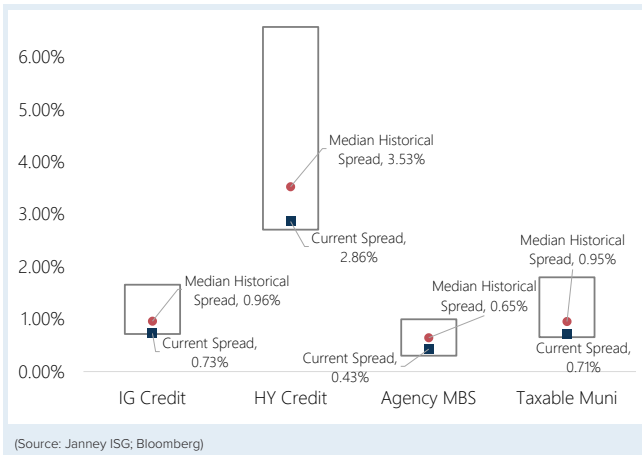
Graphic 1: AI Data Center Spending



(Source: Janney ISG, Company Guidance; The Broadband Assn.)

Absolute valuation metrics within the bond markets look reasonable, but relative valuation metrics across individual sectors of the broader U.S. fixed-income markets look stretched. Investment-grade credit spreads at +0.73% above Treasuries are in the bottom decile of all history. High-yield credit spreads at +2.60% are similarly in the bottom decile. Agency mortgage-backed security (MBS) nominal spreads at +0.62% are a bit less stretched at the second-lowest decile, but they are certainly not cheap on an historical basis. Finally, taxable Muni spreads are at or near their lowest point post-2008, when the sector first grew to a meaningful size.

Chart 11: Spreads in Almost All Fixed Income Sectors Are On Narrow Side of 5yr Range



Relatively expensive spread markets in some ways echo relatively high valuations in the stock markets in the sense that they reflect both good underlying fundamentals and strong demand for riskier securities over safe-haven assets. Valuation is not an effective timing tool for markets, but for the moment, we would encourage taking less, not more, credit risk, given the low compensation for said risk. Part of these narrow spreads is arguably from heavy Treasury issuance, which has added a phantom credit risk component to Treasury yields. We can (imperfectly) estimate this credit component by comparing Treasury and interest rate swap markets, which gives a spread of about +0.26% wider than the long-term average. Financial markets have not done a good job of internalizing this credit component, but one conclusion is that IG credit, HY credit, MBS, taxable municipals, and other sectors that trade on a spread over and above Treasuries are at least slightly less expensive than they appear on the surface.

Tax-exempt municipals occupy a small share of the overall fixed income markets at less than 7% of all outstanding debt but cast a large shadow in individual investors' portfolios owing to the nature of the tax exemption. Similar to other sectors, municipals look somewhat expensive relative to Treasuries in an historical context. Unlike other sectors, valuation is highly curve dependent. Munis in 2-5-year maturities are slightly below their normal valuation range, Munis in 10-year maturities are significantly below their normal valuation range, and Munis in 30-year maturities are roughly in line with the normal valuation range.

Demand from high-net-worth investors has been concentrated in shorter maturities, and this is reflected in terms of valuations. We tend to like the 12-15-year maturity range at present, which strikes a balance between avoiding the areas of high demand and not taking aggressive levels of interest rate risk on the long end of the curve. That said, Muni markets have become

increasingly seasonal with prices cheapening (relatively) into spring, then bouncing back into the summer before becoming expensive again (again, relative to Treasuries) into the fall. Thus far in 2026, that seasonal pattern is playing out perfectly.

The upshot is that U.S. fixed income markets are no longer operating with the same clean tailwind we expected at the start of the year, but they are also not facing a particularly hostile environment. The Fed is unlikely to deliver the rate cuts we previously expected, but absent a more obvious inflation spiral or a materially hotter labor market, the bar for tightening remains very high. That combination should leave the front end of the curve broadly anchored, with the long end trading in a range, albeit a range that is somewhat higher than we previously forecast. Fixed income markets entered 2026 with an important advantage: high starting yields. Even after tempering our rate outlook, the income component of returns remains substantial and, in our view, should be sufficient to generate positive full-year performance in a wide range of scenarios.

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**Overweight:** Janney ISG expects the target asset class or sector to outperform the comparable benchmark (below) in its asset class in terms of total return.

**Marketweight:** Janney ISG expects the target asset class or sector to perform in line with the comparable benchmark (below) in its asset class in terms of total return.

**Underweight:** Janney ISG expects the target asset class or sector to underperform the comparable benchmark (below) in its asset class in terms of total return.

## Benchmarks

**Asset Classes:** Janney ISG ratings for domestic fixed income asset classes including Treasuries, Agencies, Mortgages, Investment Grade Credit, High Yield Credit, and Municipals employ the "Barclays U.S. Aggregate Bond Market Index" as a benchmark.

**Treasuries:** Janney ISG ratings employ the "Barclays U.S. Treasury Index" as a benchmark.

**Agencies:** Janney ISG ratings employ the "Barclays U.S. Agency Index" as a benchmark.

**Mortgages:** Janney ISG ratings employ the "Barclays U.S. MBS Index" as a benchmark.

**Investment Grade Credit:** Janney ISG ratings employ the "Barclays U.S. Credit Index" as a benchmark.

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