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Third Quarter 2026

One of the more well-known market adages reminds investors that fundamentals matter most in the long run, while fear and greed can drive short-term swings. This year has illustrated that contrast. In the chart of index returns below, the longer-run returns on the right show substantial equity gains over the past 3-, 5- and 10-year periods, while bond returns have been more restrained. The shorter periods in 2026 show the see-saw behavior of a market responding to changing expectations. For investors, the challenge is to distinguish those short-term swings from changes in the longer-term investment outlook. It has been an environment that could be characterized as an alternating battle between fear and greed.

Market Performance	1Q-26	2Q-26	3Q-26	Jul	Aug	Sep	YTD-26	1 Yr	3 Yrs	5 Yrs	10 Yrs
S&P 500	-4.4%	15.2%	2.3%	-0.1%	2.7%	-0.3%	12.7%	15.7%	22.8%	13.8%	15.3%
Russell 2000	0.9%	21.6%	-7.2%	-3.0%	1.0%	-5.3%	13.9%	16.4%	17.7%	6.3%	9.8%
MSCI ACWI	-3.2%	14.9%	1.6%	0.1%	2.7%	-1.1%	13.0%	16.8%	21.7%	11.6%	12.4%
MSCI EAFE	-1.2%	10.8%	0.8%	2.0%	2.0%	-3.1%	10.3%	15.7%	18.4%	9.3%	9.1%
MSCI EM	-0.2%	24.1%	-0.4%	-3.1%	3.4%	-0.6%	23.4%	29.2%	24.1%	8.9%	9.1%
BBG U.S. High Yld.	-0.5%	2.5%	-1.8%	-0.2%	1.0%	-2.5%	0.1%	1.4%	8.0%	3.6%	5.0%
BBG U.S. Agg Bd	-0.0%	0.7%	-3.5%	-1.3%	0.4%	-2.6%	-2.9%	-1.8%	4.1%	-0.6%	1.1%
BBG U.S. TIPS	0.3%	0.9%	-3.2%	-0.7%	0.0%	-2.6%	-2.1%	-2.0%	3.8%	0.0%	2.1%

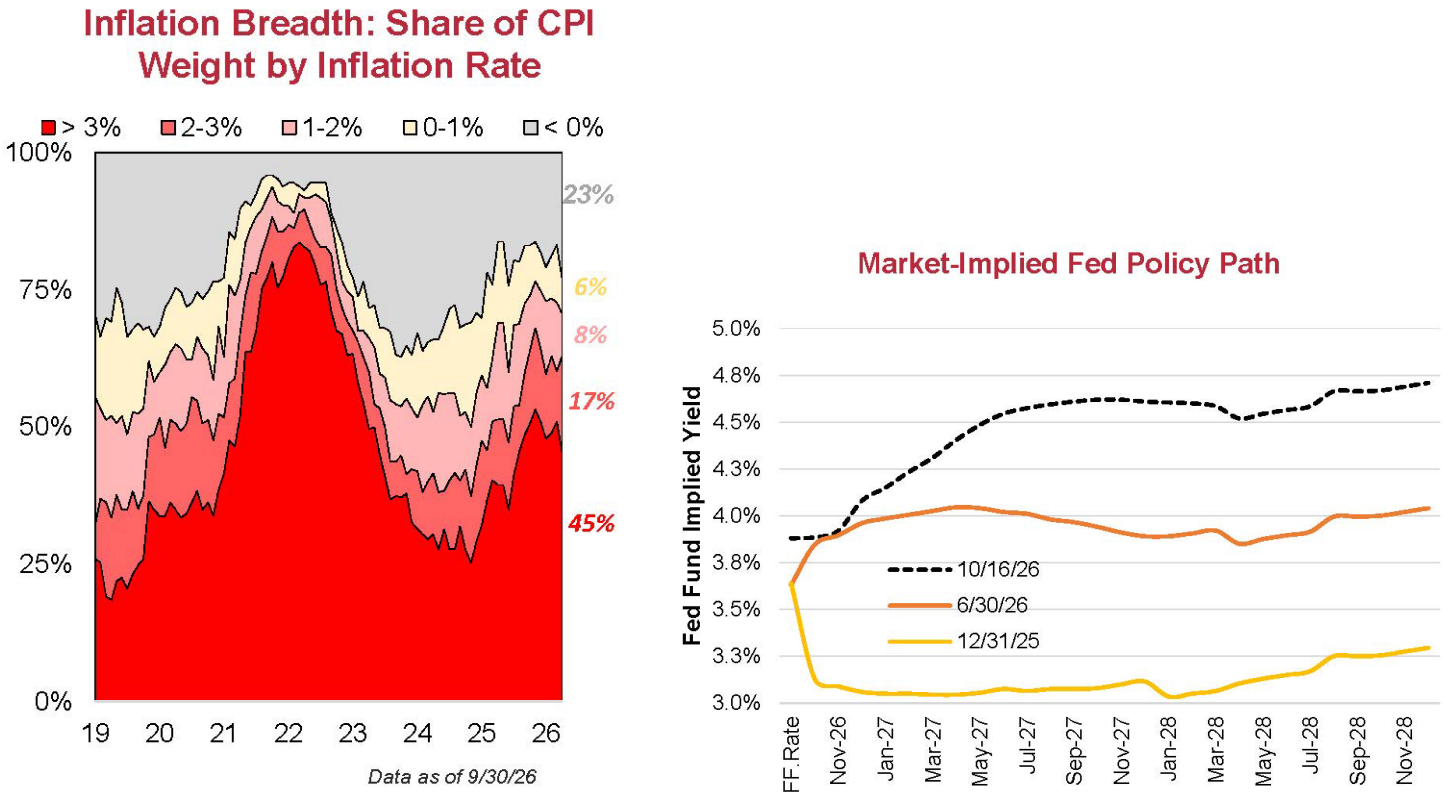
Source: Bloomberg and Monticello Associates

The fear showed up in Q1 as the Iran war commenced. The second quarter rebound reflected relief at the short-lived truce announced in April. The third quarter alternated month by month as investors reassessed the massive artificial intelligence (AI) investment cycle now under way. Semiconductor stocks, in particular, have had large swings as expectations for demand and pricing ebbed and flowed. South Korea's stock market, where Samsung and SK Hynix carry large index weights, has been particularly volatile. It's been quite the ride.

It is a good thing that investors are asking whether the vast sums being committed to AI will generate the future cash flow needed to earn an attractive return. And when we say AI, we include chips, data center construction, electrical infrastructure and power generation. So far, the optimists have had good reasons for confidence: the AI investment boom is supporting economic activity, and strong demand is driving earnings growth across much of its supply chain. It is a remarkable period. However, the speed at which technology is evolving creates its own challenges. Improvements in hardware use and in the efficiency of AI models are changing assumptions about equipment life and computing needs. These advances can lower costs and encourage wider adoption, but they also make long-term spending and profit forecasts more difficult. For investors, rapid growth is only part of the equation; the price paid and the eventual return on capital matters as well.

Amid this back and forth on AI investment, investors have also contended with a significant move in interest rates. The 10-year Treasury note yield rose by 80 basis points, or 0.80 percentage point, in Q3. That is a substantial move. The Federal Reserve raised its short-term policy rate by one-quarter percentage point in September, and analysts are debating whether further increases will follow. Inflation has now remained above the Fed's two percent target for over sixty consecutive months, continuing to put pressure on household purchasing power.

The two charts below provide insight into the interest rate and inflation debate. The chart on the left shows the proportion of items in the Consumer Price Index (CPI) rising at various rates. The darker red at the bottom shows that 45% of the items are rising at rates greater than 3%. To achieve its formal 2% target rate of inflation, this implies the Fed has lots more work to do. The chart on the right shows that markets have raised their expected path for the Fed's policy rate. Those expectations can change as inflation and economic conditions evolve.

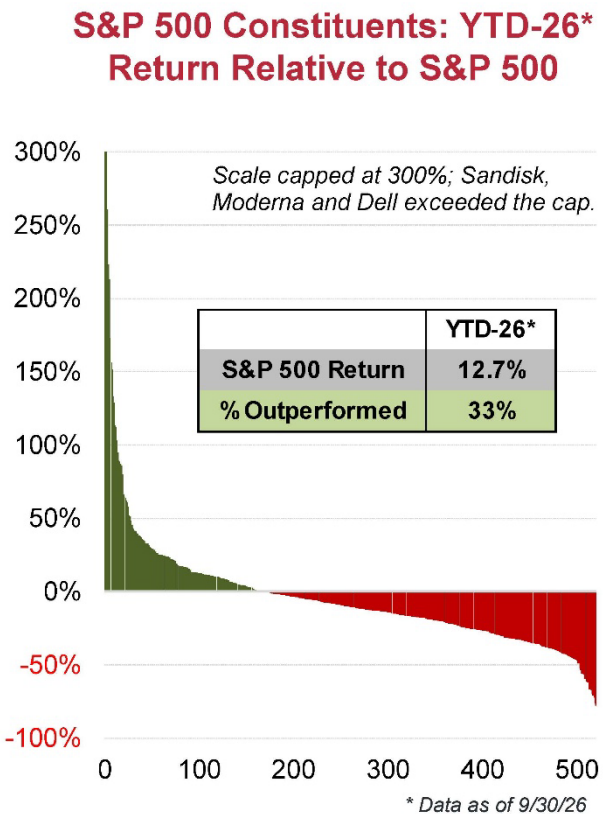


Source: Bloomberg and Monticello Associates

Higher rates affect households, businesses and government finances. Higher borrowing costs continue to challenge homebuyers and keep housing affordability under pressure. For financial markets, higher rates tend to weigh on the value assigned to future cash flows, although continued earnings growth can help offset this effect. They also raise the cost of new borrowing and refinancing for companies funding the AI buildout in public and private markets. Existing fixed-rate debt does not immediately become more expensive, but costs can rise when it matures and is refinanced. The same pressure applies to more than $30 trillion of publicly held federal debt, alongside large ongoing budget deficits. At the same time, higher starting yields improve the income available on new bond investments. We continue to weigh these pressures against the opportunities created by business investment and earnings growth.

Portfolio Positioning

We are maintaining our broad asset allocation while continuing to refine manager selection and portfolio construction. Our portfolios are diversified across global markets, growth and value investing, and sectors such as energy and technology. The S&P 500 Index continues to be highly concentrated in large companies linked to the AI theme (almost 50% at this point). Although the index includes many businesses, a relatively small group can dominate its returns, leaving investors more exposed to a shared set of expectations than they may realize. The chart below illustrates the narrow leadership: only 33% of the stocks in the index have outperformed it year to date. The large gains among companies on the far left of the chart have helped drive the index's advance.



Source: Bloomberg and Monticello Associates

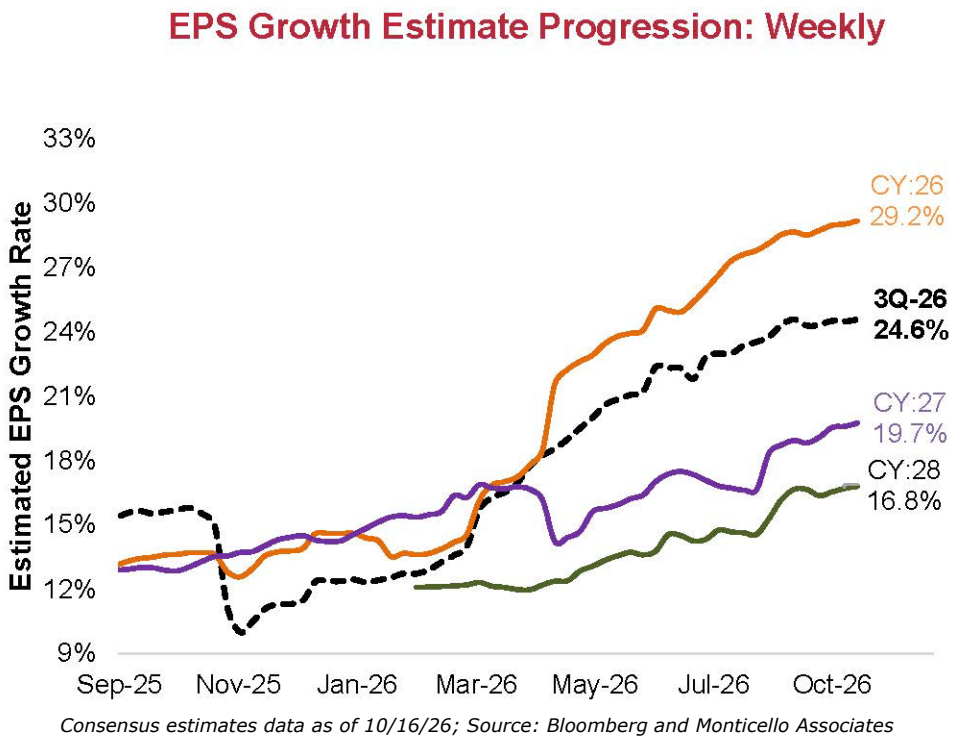
We do have passive index exposure in the U.S. and developed international markets. It provides efficient participation in market gains, including further advances in AI-related businesses. We balance that exposure with active managers whose portfolios include other sectors that could benefit if market leadership broadens. Active management does not automatically remove concentration risk, however; some managers also invest in AI-related businesses. The goal is a mix of exposures that can participate in continued growth while remaining attentive to the risks that several holdings may share.

We have long advocated for portfolio allocations to managers we call "diversifiers." These managers seek returns from sources beyond simply owning stocks that rise with the market or bonds tied to interest rates and credit spreads. Traditionally, allocations to high-quality fixed income have served as a ballast for investors facing equity market volatility. However, with the

low returns offered by fixed income over the last 15 years, we have found that over time, diversifiers can help to provide that lower volatility profile without sacrificing as much return. Some of these strategies combine "long" positions, which benefit when prices rise, with "short" positions, which benefit when prices fall. Others pursue opportunities less related to stock market indexes, focusing on currencies, commodities, credit, or other differentiated strategies. We hold these strategies because they can provide different sources of return and help manage overall portfolio risk. Their intended role is to add resilience through a range of market conditions.

Market Environment and Outlook

Earnings remain a central driver of stock prices over the long run. You may have heard us say that before. The encouraging feature today is the impressive earnings growth being reported by many of the same AI-related companies leading the market. Analysts forecast that strong growth will continue over the next two years. The chart below shows how estimates have risen over time, with projected earnings growth for 2027 and 2028 approaching 20%. This is almost without precedent in market history and sets a high bar for companies to meet.



Consensus estimates data as of 10/16/26; Source: Bloomberg and Monticello Associates

The important caveat is that those earnings still have to materialize. Higher earnings forecasts have made valuations look somewhat lower when prices are measured against expected profits. Valuations remain elevated versus long-term averages, however, leaving less room for disappointment. A broader contribution to earnings growth across sectors and countries would provide a firmer foundation for the market. The chart below shows earnings growth expectations across S&P 500 sectors. The two purple rows at the bottom separate the "AI Theme" companies from the rest of the index. The gap highlights both the strength of the AI cycle and the market's dependence on it.

S&P 500 Sector Earnings Growth Expectations

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	1Q-26¹	2Q-26¹	3Q-26*	4Q-26*	CY 26*	CY 27*	CY 28*
Energy	4%	149%	132%	137%	106%	-7%	-13%
Info. Tech.	57%	77%	66%	55%	63%	41%	26%
Materials	45%	42%	26%	42%	32%	11%	8%
S&P 500	**30%**	**34%**	**25%**	**29%**	**29%**	**20%**	**17%**
Industrials	12%	13%	17%	16%	16%	17%	16%
Utilities	13%	17%	9%	14%	13%	9%	10%
Financials	23%	25%	4%	8%	15%	7%	11%
Comm. Svc.	54%	13%	3%	11%	20%	8%	16%
Real Estate	9%	10%	3%	5%	6%	5%	7%
C. Discr.	39%	13%	2%	15%	16%	15%	27%
C. Staples	7%	14%	2%	6%	8%	7%	8%
Health Care	-3%	-6%	-2%	14%	0%	22%	10%
Mag 7	**64%**	**36%**	**20%**	**23%**	**34%**	**27%**	**27%**
Remng. 493	**19%**	**33%**	**26%**	**31%**	**28%**	**17%**	**13%**
Theme: AI	**73%**	**60%**	**47%**	**50%**	**57%**	**37%**	**29%**
Theme: ex AI	**15%**	**26%**	**17%**	**21%**	**20%**	**12%**	**10%**

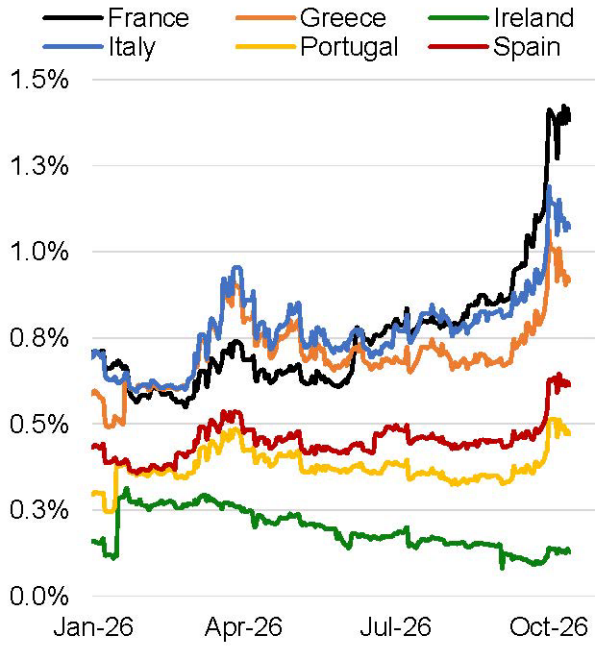
*1: Actual Growth; *Consensus estimates data as of 10/16/26; Source: Bloomberg and Monticello Associates*

The analyst community's outlook is optimistic. If earnings arrive as expected, they should provide support for markets, although inflation, interest rates and geopolitical conflict can still affect the prices investors are willing to pay. Strong earnings growth is already part of current expectations. For investors with long horizons, our emphasis remains on ***time in the market***, supported by appropriate diversification and liquidity, rather than market timing and trying to predict every short-term turn.

One final risk to watch is the global rise in sovereign bond yields, particularly in Europe. German government bonds serve as a benchmark for the euro area's borrowing costs. Countries in the euro area share the European Central Bank's monetary policy but retain responsibility for their own budgets and debt issuance. The chart below shows how much other countries' bond yields have risen relative to Germany's. The pressure is especially acute in France: The French yield spread shown here is above levels seen during the 2011–2012 European debt crisis. That comparison highlights investor concern about public finances, although a similar spread does not necessarily imply the same economic outcome.

10-Year Sovereign Yield Spreads vs. German Bund

YTD-2026*



**Data as of 10/15/26; Source: Bloomberg and Monticello Associates*

We continue to consider these country-specific pressures alongside global investment opportunities.

Conclusion

As always, our focus remains on positioning client portfolios for the future by asking hard questions of our managers and ourselves about our allocations. We remain confident in our disciplined process and prepared to adjust as conditions change. Our aim is to help each client progress toward their long-term portfolio objectives. Thank you for the opportunity to work on your behalf.

Daniel F. Smith John M. Simms, Jr.

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