

Hughes Investment Advisory Service LLC

July 1, 2026

Dear Clients and Investors,

Happy 4th of July and I hope this update finds you well.

The Big Picture

Every quarter I try to step back from the daily market headlines and ask myself a simple question: *What is the one issue most likely to influence investment returns over the next several years?* While attention in financial markets shifts regularly between inflation, earnings, monetary policy, and geopolitics, my answer has remained remarkably consistent in recent years.

I continue to believe that the extraordinary growth of U.S. government debt, and the policy choices that will eventually be required to manage it, will be one of the defining investment themes of this decade. Although Wall Street tends to focus on short-term developments such as quarterly earnings and Federal Reserve policy shifts, I believe the nation's fiscal position will increasingly shape the long-term investment landscape.

For several years I have written about the growing likelihood of what economists refer to as **financial repression**. Simply put, financial repression occurs when governments maintain interest rates below the rate of inflation for extended periods in an effort to gradually reduce the real burden of outstanding debt. It is not a crisis, nor is it a conspiracy. It is a policy framework that has been used repeatedly throughout history when debt burdens become exceptionally large.

If that continues to be the path the U.S. ultimately follows, it will have important implications for investors. Traditional savings and many fixed-income investments may continue their struggle to preserve purchasing power, while ownership of productive businesses, selected real assets, and other inflation-sensitive investments may become increasingly important. Much of our portfolio positioning reflects that long-term view.

With that broader backdrop in mind, let's turn to what happened in the second quarter.

Major Asset Class Performance

Asset Class	Q2	YTD
Fidelity Balanced Fund Index (Stock/Bond Mix)	+10.1%	+8.7%
IVV – S&P 500 Equity Index	+13.4%	+9.6%
RSP – S&P 500 Equal Weight Index	+9.8%	+9.8%
EFA – Europe, Australasia & Far East Equity Markets	+4.40%	+6.0%

Asset Class	Q2	YTD
AGG – iShares U.S. Investment Grade Bond Index	+1.1%	-1.1%
GLD – Gold	-16.0%	-670%
FBTC – Fidelity Bitcoin ETF	-7.0%	-31.0%

Updated 2026 Outlook

Forecast	Original	Revised
GDP Growth	3.5%	2.8%
S&P 500 Earnings	\$310	\$330
Core PCE Inflation	3.2%	3.6%
S&P 500 Return	12%	12%
Federal Funds Rate	2.5%	2.5%

The First Half of 2026

Equities posted another solid quarter, but beneath the surface the rally was anything but broad. Semiconductor manufacturers, memory companies, and businesses directly tied to artificial intelligence infrastructure accounted for a disproportionate share of market gains. Strong earnings growth from these companies surprised even optimistic analysts and drove much of the advance.

The bottom line is straightforward: if your portfolio held semiconductor and AI-related companies, results were very strong. If not, returns were considerably more modest.

Our portfolios participated less in this rally because several of our long-held positions, particularly in defense and commodity-related companies, experienced temporary weakness. While that is never comfortable in the short run, maintaining valuation discipline is, in my view, preferable to chasing the strongest performers late in a cycle. Our responsibility is not to own whatever is working at the moment, but to build portfolios capable of producing attractive long-term returns while preserving capital across changing environments. The current trend chasing environment resembles gambling rather than investing.

So where do we stand as we enter the second half of 2026?

The first “mini” Black Swan event of the year—the conflict involving Iran—has occurred, although I do not believe it has fully resolved. While active hostilities have subsided, underlying geopolitical tensions remain, and the possibility of renewed conflict cannot be dismissed.

One of the biggest surprises was not the conflict itself, but the behavior of oil prices. I had expected that a more severe disruption could push crude oil toward the \$150–\$200 per barrel range. Instead, prices quickly retreated toward pre-conflict levels. It now appears that China maintained a substantially larger Strategic Petroleum Reserve than Western analysts had

assumed. Combined with slowing domestic demand and continued expansion of alternative energy sources, those reserves appear to have played a meaningful role in stabilizing global energy markets. I too believe energy prices are likely to settle at levels modestly above current levels.

Looking Ahead

Another major development during the quarter was the appointment of Kevin Warsh as Chairman of the Federal Reserve.

When he was first nominated, many investors assumed he would favor easier monetary policy and be less independent than his predecessor. His initial Federal Reserve meeting, however, surprised markets. His comments emphasized price stability and reaffirmed the Fed's commitment to returning inflation toward its 2% objective. As a result, many investors interpreted his stance as more hawkish than expected.

I interpret this differently.

In my view, Chairman Warsh is establishing anti-inflation credibility early, which may ultimately give him greater flexibility to support the economy later if conditions warrant. I continue to believe the odds favor a more accommodative monetary policy over time, particularly as fiscal realities become increasingly difficult to ignore.

The U.S. now carries approximately \$40 trillion of federal debt, and the cost of servicing that debt continues to rise. Lower interest rates would not only support employment, investment, and economic growth, but would also significantly reduce government financing costs. For several years I have written that this environment makes financial repression increasingly likely, and I continue to believe that assessment is correct.

Governments tend to favor this approach because it is generally viewed as less disruptive than large tax increases or significant spending cuts.

This brings us to the Federal Reserve's central challenge. Inflation remains near 4%, while the Fed's target is 2%. Under normal circumstances, the response would be straightforward: raise interest rates. Today, however, aggressively higher rates would significantly increase government borrowing costs and place additional strain on the broader economy.

In my opinion, one of the few realistic paths toward lower inflation without a meaningful economic slowdown lies in productivity growth. Advances in artificial intelligence, automation, and related technologies have the potential to materially improve productivity over the coming years. Treasury Secretary Bessent and Chairman Warsh also embrace this view. However, that transition is unlikely to be smooth, and portfolio positioning must account for that reality.

Wall Street's attention will soon shift back to Corporate America, where expectations remain constructive. Consensus forecasts currently call for approximately 22% second-quarter earnings growth for S&P 500 companies (Yardeni Research, 2026). If achieved, this would represent the second consecutive quarter of earnings growth above 20%, driven by continued strength in technology, energy, materials, and industrial companies.

There are several reasons I remain cautiously optimistic as we move into the second half of 2026:

1. Corporate earnings continue to exceed expectations
2. The labor market remains resilient
3. Unemployment remains historically low
4. Geopolitical conditions in the Middle East have stabilized relative to earlier concerns
5. The long-term trend toward reshoring U.S. manufacturing continues

At the same time, we remain attentive to several key risks, including persistent inflation, renewed geopolitical instability, and elevated valuations in parts of the artificial intelligence sector.

Portfolio Positioning

Our investment philosophy has not changed.

We continue to favor high-quality, large-cap, dividend-paying U.S.-based multinational companies with durable competitive advantages, strong balance sheets, consistent free cash flow, globally recognized brands, and long histories of increasing dividends.

We continue to believe that over the long run, the risk/reward profile favors equities over traditional fixed income. Gold and selected commodities remain important portfolio diversifiers. Treasury bills, MLPs, selected real estate investments, and specialized income strategies continue to offer attractive opportunities for income-oriented investors.

One point I would like every client to remember is that our objective has never been to outperform every quarter. Markets periodically become concentrated in a small number of companies or themes, and disciplined investing will inevitably involve periods of relative underperformance. Our objective is to compound wealth over full market cycles while assuming less risk than a traditional balanced portfolio whenever possible. In my experience, patience, valuation discipline, and prudent risk management remain among the most reliable drivers of long-term wealth creation.

We believe our portfolios remain well positioned for the years ahead. We will continue to remain disciplined, stay flexible, and invest with a long-term perspective grounded in the principles that have guided us through multiple market cycles.

As always, thank you for your continued confidence and trust. It is a privilege to manage your investments. Please do not hesitate to call if you would like to discuss your portfolio or any of the ideas in this letter.

Sincerely,
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