WEALTH MANAGEMENT 360
FARMERS TRUST COMPANY

MARKET UPDATE & OUTLOOK | Q2 2026

COMPANY PROFILE

Farmers Trust Company is licensed by the Ohio Division of Financial Institutions as a bank, authorized to conduct trust business and exercise full fiduciary powers. Our efforts are focused on the administration and management of trust assets. As an independent trust company, Farmers Trust Company offers several investment management options. We are committed to providing the highest level of service in the areas of investment management, estate settlement, living trusts, testamentary trusts, charitable trusts, charitable endowments and employee benefit plans. Tax and estate planning services are available to our clients as well. Farmers Trust Company has the unique ability to integrate investment, trust and estate management at a local level. Our clients appreciate the fact that their financial affairs are handled personally and confidentially. They also value our ability to work closely with their attorneys, accountants and insurance professionals to achieve a comprehensive financial strategy.

MARKET RECAP

In the first quarter of '26, the US Equity market recorded its first negative return in a calendar quarter going back to the first quarter of '25. That was only the second quarterly decline in the last ten. The important distinction this time was that the US equities did not get help from other assets classes. International equities also had a down quarter. Even the hedge fund index had a negative return for the period. Bonds were flat as well. The only asset class that rose meaningfully was commodities, specifically the energy complex. It remains to be seen to what degree this foreshadows the outlook for the rest of the year. Nonetheless, the US equity market is seeing increasing headwinds for the first time in a while.

Despite the weakness at the index level, several S&P sectors actually posted positive returns for the quarter. Energy was the best performing sector in the S&P 500 Index in Q1, up 38.2%. Materials were a distant second, up 9.7%. Utilities and Consumer Staples also rose better than 7.5%. Information Technology, Consumer Discretionary, and Financials were down the most, each down more than 9%. Large-cap Value outperformed Large-cap Growth by 8% during the quarter just by staying flat. Small-cap stocks, represented by the Russell 2000 Index, were up 0.9% in Q1.

International equities were down for the quarter but outperformed the US equity market. The MSCI EAFE Index of developed markets was down 1.1%. Similarly, the MSCI Emerging Markets Index was down just 0.1%. This relative outperformance occurred despite strength in the US dollar, which was up almost 2% during the quarter.

Benchmark GSCI Commodity Index, which has a 50% weight in energy, was up 39.6% in Q1. Crude oil, as measured by the WTI futures contract, rose 76.6%, with gasoline futures up 94.2%. Precious metals prices were up 3.6% in Q1 as per the Bloomberg Precious Metals Index. Agricultural commodities also had a good quarter, up 7.1% as per the Bloomberg Agriculture Index. Natural Gas and soft commodities (e.g., cotton, coffee) were down for the quarter.

The US bond market had a snooze of a quarter as bond volatility continued to come down. The Bloomberg US Aggregate Index was flat on the quarter, as was the Bloomberg US Treasury Index. The Mortgage-Backed Securities Index recorded a gain of 0.4%, outperforming both Investment-Grade Corporates (-0.5%) and High-Yield (-0.5%) benchmarks. International bonds were down the most (-1.9%) as per the Bloomberg Global ex-USD Aggregate Index. The Treasury bond yield curve moved up during the quarter as inflation expectations rose and dissipated expectations for Fed rate cuts early in the year. The interest rate spread between the 2-year yield and the 10-year Treasury bonds moved down from 69 basis points to 51 basis points during the quarter.

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MARKET SCORECARD as of 3/31/2026	TOTAL RETURN IN USD	
	Q1	2026 TR
DOW JONES IND AVG	-3.2%	-3.2%
S&P 500	-4.4%	-4.4%
NASDAQ	-7.0%	-7.0%
RUSSELL 2000 INDEX	0.9%	0.9%
MSCI EAFE EQUITY (GROSS)	-1.1%	-1.1%
MSCI EMERGING MARKET EQUITY (GROSS)	-0.1%	-0.1%
BLOOMBERG GLOBAL AGG BOND INDEX	-1.1%	-1.1%
BLOOMBERG INTERM. TREASURY	0.1%	0.1%
BLOOMBERG INTERM. GOVT/CREDIT	0.0%	0.0%
BLOOMBERG 5 YEAR MUNI INDEX	0.0%	0.0%
BLOOMBERG HIGH YIELD CORP INDEX	-0.5%	-0.5%
ishares S&P GSCI COMMODITY TR INDEX	39.6%	39.6%
HFRX ABSOLUTE RETURN INDEX	-0.2%	-0.2%

Note: All returns include invested cash flows expressed in U.S. dollar terms.

KEY POINTS

- The US economy slowed in Q4 of last year and sent mixed signals in Q1. Consumer spending has weakened while the employment picture has been neutral.
- Pockets of economic strength, such as acceleration in the manufacturing sector, have not been able to create broad-based sustainable economic momentum. They have, however, spurred an improvement in corporate profits, which is one bright spot for investors.
- The oil price shock from Q1 has pushed inflation expectations higher. The Fed is unlikely to meaningfully lower short-term rates until those pressures subside.
- We remain underweight US Large-cap Equities relative to our benchmark. We like Energy, Materials, Consumer Staples, and Utilities at the expense of Information Technology sector. Alternatives, like commodities and REITs, appeal to us for their diversification benefits.

GLOBAL MACROECONOMIC REVIEW & OUTLOOK

The outlook on the US economy has grown foggier entering the second quarter. The job market has continued to soften and economic growth has slowed. Various pockets of economic strength have not created enough momentum for re-acceleration. At the same time, inflationary expectations have risen, obfuscating the future path of the Fed's monetary policy. This uncertainty has weighed on the market and has been amplified by the ongoing geopolitical tensions in the Middle East.

Having grown 4.3% in Q3, the US economy slowed to just 0.5% growth in Q4 as per the official GDP measurement. The US consumer continued to spend in the first quarter, albeit at a lower rate as higher oil prices sapped consumer confidence. Retail sales grew 3.2% in January and 3.6% in February, both at a pace that was well below last year's 5.5% growth. Purchasing Managers Index (PMI) of economic activity paints a mixed picture as well. While the Manufacturing PMI readings bounced into expansionary territory during the quarter, Services PMI declined in March for the first time in six months.

The job market has been a neutral factor for economic growth, with job openings continuing to decline but unemployment claims still not increasing meaningfully. Non-Farm Payrolls, which have gone through a significant downward adjustment upon each release, continue to send a mixed signal. The economy created 160k jobs in the month of January only to lose 133k jobs in the month of February. While March reading surprised to the upside (177k vs. 60k expected), it is likely that subsequent adjustments will see that number move lower as well. The economy is not seeing enough job creation in the manufacturing sector to generate sustainable economic momentum. It remains stop-and-go for now.

Investors came into the year expecting at least two quarter-point cuts to the Fed's interest rate target this year as inflationary expectations had been on a downward path. Given that oil prices have more than doubled since the beginning of the year, the potential for upward pressure on inflation going forward has significantly complicated the Fed's monetary policy outlook. Breakeven 2-year inflationary expectations have risen from 2.3% at the beginning of the year to 3.2% in April. The Producer Price Index (PPI), which is a leading indicator for consumer prices, jumped from 2.9% in January to 3.4% in February. PMI pricing surveys from March also point to a buildup of inflationary pressures. That has effectively shackled the Fed, such that investors now only see a 50% chance for one quarter-point rate cut this year

INVESTMENT OUTLOOK

Our cautionary tone from the beginning of this year has firmed up as prospects for a stagflationary economic scenario have risen. Weakening economic growth and rising inflationary expectations do not allow the Fed to stimulate the economy more aggressively with its interest rate policy. Policymakers understand this and that is why their rhetoric has stiffened up as well. This jawboning has occurred despite an upcoming change at the Fed, which should see President Trump's appointee, Kevin Warsh, take over for Jerome Powell this summer. With Warsh as the Chairman, the potential for lower rates is there, but the key question will be at what pace. As investors recalibrate the timing and the degree of potential cuts, the equity market's valuation starts to look more challenging to sustain.

On the positive side, corporate earnings estimates have actually been rising, and there is an ongoing policy stimulus that has come in the form of larger tax rebates from the Big Beautiful Bill. Investors have also been searching beyond the usual suspects for a new batch of winners. While the Mega-Cap Tech stocks' underperformance has weighed on the overall index performance so far this year, relative breadth of positive performers in the market has been increasing.

We continue to track key signposts to help us determine the trajectory for the market and the economy this year. One of those is the level and the shape of the US Treasury yield curve, which now points to a buildout of inflationary pressures in the system. Simultaneously, the ongoing conflict in the Middle East has exerted additional pressure on the US Federal Budget. The timing of these two developments will eventually put pressure on the US dollar, which has been holding up relatively well for now. Higher inflation and a potentially weakening currency would both be positive for corporate profits. However, if those were to be accompanied by higher nominal long-term interest rates, the earnings multiple that investors would be willing to ascribe to the market would likely be lower than it is today.

We remain underweight Equities relative to our benchmark. Our key underweights are specifically in the US Large-Cap area of the market and the Technology sector, where we see excessive valuation as the key risk. Our overweight positions include Materials, Energy, and defensive non-cyclical sectors like Consumer Staples and Utilities. We also like the prospects for Small-Caps, as they are likely to benefit from a less onerous regulatory agenda of the Trump administration. Our weight in international stocks is neutral relative to the benchmark. Commodities and alternatives (e.g., REITs) continue to appeal to us from the standpoint of portfolio diversification in times when most other asset classes have continued to be increasingly correlated.

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