



JUNE 2026

QUARTERLY INVESTOR LETTER

Divergences and reversals characterized market performance in the Second Quarter. Notably, the Philadelphia Semiconductor Index posted a record quarterly gain. However, two of the sector's leaders lagged both the index and the market. This divergence was consistent with the broad market as small caps outperformed large caps and breadth improved substantially. The so-called Magnificent Seven stocks suffered a correction and ended the quarter with year-to-date losses. For the first time in years, the S&P 493 (i.e., the S&P 500 excluding the Magnificent Seven stocks) outperformed the benchmark S&P 500. Meanwhile, the Small Cap index posted one of its best quarterly returns in decades.

Gold suffered its worst quarter in a decade, and crypto assets continued a sharp correction that began last year. One factor contributing to underperformance by alternative assets was a sharp reversal in the Dollar. There were several fundamental developments that support the greenback.

First, the Yen has declined to levels last witnessed in 1986, and the Dollar has benefited from Yen weakness. Japan contends with surging inflation, and its central bank has been slow to address pressure on its currency.

Second, new Fed Chair Warsh began his term under economic conditions that could require monetary tightening. The Federal Reserve has adopted a more hawkish tone in response to strong labor market conditions and inflation that remains stubbornly above target. Consequently,

investors reversed expectations for a rate cut this year. The market has begun to price in rising probabilities for a rate hike. This reversal provides additional support for the Dollar.

Some of the inflationary pressures associated with crude oil abated as prices returned to pre-conflict levels. In addition, corporate earnings growth remains robust with an additional one-time boost from tariff refunds. These factors represent tailwinds for the second half of the year.

Breadth often indicates wide participation in a growing economy, and we were encouraged by the market's reversal of extremely narrow conditions. However, the reversals and divergences of the Second Quarter could merely reflect portfolio re-positioning. Market leadership rotates periodically as investors rebalance allocations. In other words, breadth might reverse again if rebalancing was primarily technical in nature, not fundamental. At the same time, there is a growing chorus of investors who has raised reasonable concerns about the sustainability of massive AI infrastructure spending. In that context, breadth could reflect fundamental concerns regarding the AI buildout and investor interest in diversification.

Everybody at Patten & Patten extends their wishes for an enjoyable summer and a joyous 4th of July as our nation celebrates its semiquincentennial. Please contact the office if you would like to schedule a review meeting, either in person or by Zoom.