



# The ADVISOR

*Focus on Community Banking Issues*

Second Quarter 2026

## ECONOMIC ENVIRONMENT

### *Uncertainty May Be The Only Certain Thing Right Now*

About seven weeks into the war in Iran, the economy is largely driven by the constantly changing narrative, combined with the increase in the price of oil that wreaks havoc on consumers' ability to afford daily life. This creates significant uncertainty, as the Strait of Hormuz swings from open to shut on a daily basis while the cease fire seems to be in a continuous on-again, off-again mode. It is likely that this will change multiple times even before people will have the opportunity to see this article.

### *What Does The Actual Data Tell Us?*

In short, the answer is mixed, but we need to do a deeper dive to understand what it says about the underlying economy, and how much the recent data points have been impacted by the war.

#### Inflation

This is likely the 'easiest' to diagnose, as we need to only view the recent increase in the Consumer Price Index. On a year-over-year basis, in the last reading before the inclusion of the impact of the war, prices rose 2.4%. However, that figure jumped to 3.3% as the price of oil shot upward. The implication here is straightforward- as oil drove inflation higher, the opposite should also be true, but the timing will likely be quite different.

While oil prices rose very quickly, taking the price of gas at the pump with it, they are unlikely to decline at the same speed, leaving us with a longer path back to lower costs. This data point is the one that is most likely to keep the Fed on the sidelines, but more about that later.

#### The Job Market

Job growth has been up and down over the last six months, with the average of 15,000 new jobs created over that time (per the NonFarm Payrolls report) hiding the actual volatility within the data. In two of the six months the U.S. economy gained more than 150,000 jobs, while also

## EPG RATE OUTLOOK

April 2026

MARKET RATE	Actual (%) 3/31/2026	Projected (%) 3/31/2027	Yr1 Δ	Projected (%) 3/31/2028	Yr2 Δ
FedFunds	3.75	3.50	-0.25	3.50	0.00
Prime	6.75	6.50	-0.25	6.50	0.00
3mthTsy	3.67	3.55	-0.12	3.70	0.15
6mthTsy	3.69	3.60	-0.09	3.80	0.20
1yrTsy	3.66	3.65	-0.01	3.90	0.25
2yrTsy	3.79	3.70	-0.09	3.95	0.25
3yrTsy	3.82	3.75	-0.07	4.00	0.25
5yrTsy	3.94	3.80	-0.14	4.05	0.25
10yrTsy	4.32	3.90	-0.42	4.15	0.25
30yrTsy	4.91	4.25	-0.66	4.50	0.25

#### RATE OUTLOOK DESCRIPTION:

This represents EPG's current view of interest rates.  
Depending on the actual timing of the ALM meeting, the outlook may be altered and/or updated.  
For the most accurate current rate outlook, please call EPG, Inc. at (781) 235-2666.

### *Features*

#### *Economic Environment:*

- Uncertainty Driven By the War.

#### *Fixed Income Strategy:*

- War Brings Increased Volatility.

#### *Equity Strategy:*

- Markets Look Past Current Challenges.

#### *ALM Strategy:*

- Utilizing ALM Modeling for Strategy.

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# ECONOMIC ENVIRONMENT

losing more than 130,000 in two other months. This weakness started well before the war, so it would not be fair to pin these results on events in the Middle East. We continue to argue that the job market is undergoing a longer-term transition based on AI as companies eliminate positions and become more efficient, producing more but with fewer employees. In just the last few years, seemingly ‘safe’ positions, such as coding, have been negatively impacted by automation.

Consider just a few of the recent job cuts as a result of AI, while also extrapolating out what will

likely happen as more companies adopt a similar strategy:

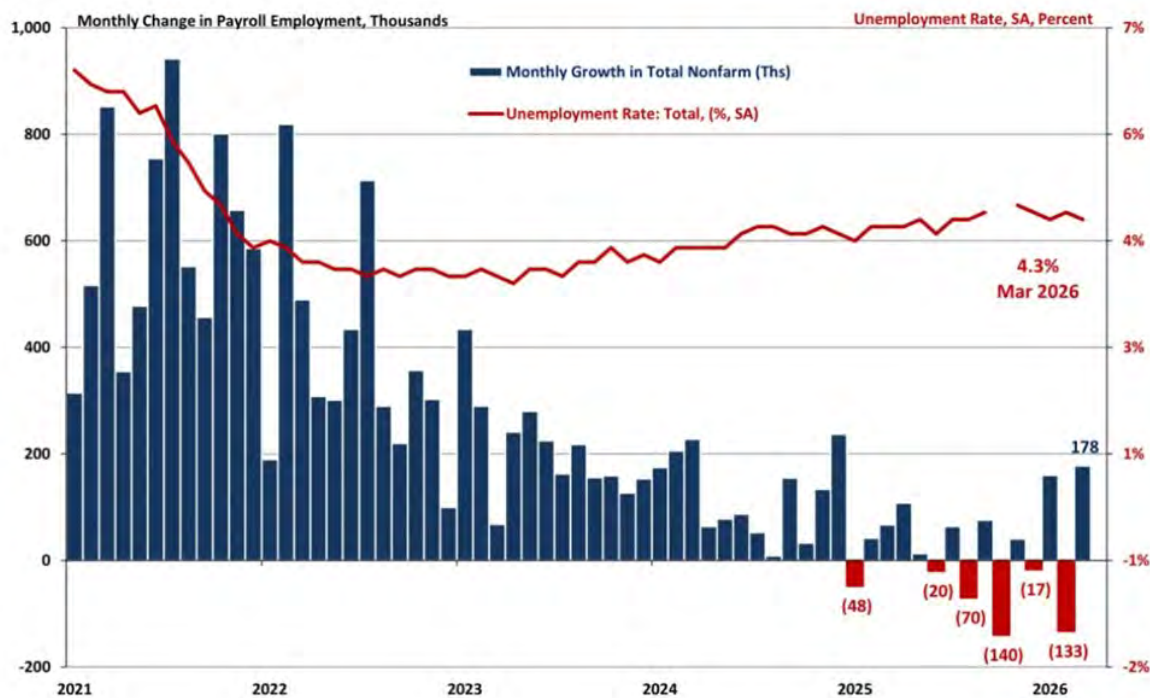
- Amazon: 16,000 earlier in 2026
- Block: nearly 40% of its workforce, about 4,000 positions
- Snap: 16% of its workforce, about 1,000 positions
- Pinterest: almost 15% of its 4,500-person workforce

Although the total cuts at Block, Snap and Pinterest were relatively small, the percentage was high, so when larger companies do the same, the cuts should be far worse. As reported by Reuters, Goldman Sachs stated earlier this year that “AI was responsible for 5,000 to 10,000 monthly net job losses last year.” This pace is only moving in one direction; however, it may be too early to sound the alarm with the Unemployment Rate still at on-

ly 4.3%. Per the chart below from the National Association of Home Builders, although job growth has trended lower, unemployment remains well below the higher levels of a few years ago, although remembering that was pandemic induced.

## Economic Growth

Although GDP growth is a lagging indicator, it still provides useful data. While full year 2025 growth of 2% sounds decent, it masks the underlying volatility from quarter to quarter (not so dissimilar to NonFarm Payrolls). Last year started off slowly, with Q1 growth of -0.6%, but jumped to 3.8% in Q2, 4.4% in Q3 before falling back to 0.5% in Q4. This data also precedes the war, so the slowdown near the end of 2025 happened independently of activi-



Source: Bureau of Labor Statistics.



## ECONOMIC ENVIRONMENT



ty in the Middle East, which is not a good sign if you are looking to blame the recent downtrend solely on the war.

With GDP comprised of about 2/3 consumer spending, what happens longer-term if companies continue to automate with AI? If taken to an extreme, the outcome can turn ugly very quickly, with corporate profits rising due to lower payroll costs, but hitting an inflection point where there are eventually too few people working, causing a demand collapse. Although this may be a bit down the road, it is not too early to consider the implications of this potential scenario.

### *What Does This Mean, Bottom Line?*

From an economic standpoint, one of the most significant short-term effects of the war is the impact on the Fed, as the sharp jump in inflation has forced the Fed to pause. In all likelihood, the Fed was already near the end of its easing cycle, so there was probably not much more to go, but that ended abruptly once oil rose. With the Fed's dual mandate, their focus bounces back and forth between their 2% inflation target and full employment, but they seem content to focus on inflation at this point.

In EPG's rate outlook, we are forecasting one additional Fed cut of 25 basis points in September this year, lowering the Funds rate to 3.50%. For the Fed to act sooner, we would likely need to see a significant decline in the health of

the labor market, which is more likely to happen slowly over time (as per discussion above) than on an imminent basis.

The unknown for the Fed is the timing of Kevin Warsh's confirmation as new Chair. He should appeal to both sides of the aisle, given his past experience in both public (he was a member of the Fed's Board of Governors for 5 years) and private capacities. He has historically been considered an inflation hawk but has recently argued that higher levels of productivity can allow for lower interest rates without causing inflation. This could be taken as an indication that he favors lower rates, but he also wants to decrease the size of the balance sheet, which is a form of tightening. In theory, as he supports both accommodative and restrictive measures, if done simultaneously could offset each other to a degree. We may know more in the near future. ♦



# FIXED INCOME STRATEGY

## FIXED INCOME STRATEGY

### *Geopolitical Uncertainty Brings Increased Volatility*

Entering 2026, it was a near foregone conclusion to investors that policy makers would be easing monetary policy. The bigger question at the time was more about the timing and magnitude of the rate cuts this year to stimulate a likely weakening economy with sluggish job growth. In January there was a strong consensus that there would be one rate cut by mid-year, followed by a second during the latter part of the year. To help easing conditions, President Trump announced Kevin Warsh as the next Federal Reserve Chair to succeed Jerome Powell,

whose term runs until May. It was also implied that Warsh has a dovish view towards the U.S. economy, and although there has been political pressure on the current Fed to deliver rate cuts, they have disappointed thus far.

On February 28<sup>th</sup>, the Middle East tension escalated, increasing volatility across the broader capital market spectrum. Equity valuations weakened, and as somewhat of a surprise, long-term bond yields rose. Typically, geopolitical conflicts would create a safe haven flight to quality in U.S. Treasuries, but that was not the case this time. By early April crude oil had surged by more than 60% since the end of February, pushing gasoline prices above \$4 a gallon, only to settle down as near-term resolution became likely. With inflation already running above the longer-term target rate, the spike in oil prices has raised concerns among bond investors.

Higher energy costs could push inflation even further upward, squeezing consumer spending habits and complicating efforts to bring inflation closer to the desired target level. Businesses are also under increasing pressure as costs for labor, insurance, energy, and materials continue to rise. The strain is already showing up in inflation data and has become a concern for the Federal Reserve, as higher operating costs will likely flow through to the consumer later this year.

Recent developments in the global economy have encouraged economists and investors to reassess their outlook and its implications for consumers. Elevated oil prices are expected to weigh directly on household spending and will be a growing headwind to discretionary consumption. As a result, the Fed funds futures market was quick to reprice expectations for any rate cuts in the near term. Labor market

**Year to Date Price Changes of Crude Oil and 10 Year Treasury Yield (oil in white, 10 Yr. Tsy. in orange)**



Source: Bloomberg

## FIXED INCOME STRATEGY

data has sent mixed signals over the last year. February's 133,000 decline in NonFarm payrolls suggested potential softening in employment, but this was quickly offset by a stronger-than-expected gain of 178,000 jobs in March, accompanied by another decline in the unemployment rate. At 4.3%, unemployment remains low by historical standards, indicating that underlying labor market conditions are still relatively strong despite recent volatility.

Given this backdrop, the EPG Investment Committee expects Fed officials will be reluctant to lower the funds target rate, as elevated inflation and escalating oil prices hinder their flexibility to ease policy. As a result, policy makers are likely to hold rates steady, unless we register significantly weaker employment results in coming months. The newly appointed (dovish) Fed Chair may have to disappoint political pressure and stay the course until the volatility subsides.

### *Investment Margins Have Expanded with Higher Yields and Wider Spreads*

Geopolitical volatility initially led to underperformance across fixed income sectors, causing wider spreads and increasing balance sheet margin possibilities. Despite this environment, there was no flight to quality into U.S. Treasuries. Instead, dislocations created more attractive yield curve opportunities across subsectors in the Agency Mortgage market and Callable Agency sectors. Even President Trump's directive in January for FNMA and Freddie Mac to purchase \$200 billion of Agency securities was insufficient to keep mortgage rates below 6.0% for an extended period.

Mortgages continue to present relative value compared to other high-quality sectors, supported by more stable credit spreads. Looking ahead, additional stimulus measures may be introduced to further enhance housing affordability and help drive mortgage rates lower.



While Corporate and Municipal bonds also experienced price volatility, spreads still remain near the lower end of historical ranges. At the same time, corporate issuance has remained elevated, as issuers capitalize on favorable spread conditions. With the long end of the yield curve holding near 4.25%, incremental investments at these levels should be accretive to balance sheets and support improved earnings potential. ♦

**Yield Curve 12/31/25-3/31/26**



Source: Bloomberg

**Yield Curve Changes Year to Date**

Term	12/31/2025	3/31/2026	Change
2 Year	3.47	3.79	0.32
3 Year	3.54	3.82	0.28
5 Year	3.73	3.94	0.22
7 Year	3.94	4.13	0.19
10 Year	4.17	4.32	0.15
20 Year	4.79	4.91	0.12
30 Year	4.84	4.91	0.07



# EQUITY STRATEGY

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### *The More Things Change, the More They Stay the Same*

Amid a stream of macro uncertainty over the past two years, equity markets continue to push higher following brief periods of volatility. This year has been no different, where the S&P 500 is once again reaching all-time highs after a choppy March. Whether a contracting labor market, tariffs, inflation, shifting monetary policy expectations, or Middle East tensions are the prevailing issue of the day, equity investors have looked ahead to greener pastures.

Despite the murky outlook, we maintain a cautiously optimistic long-term view of U.S. equities. Massive investment into data centers and AI infrastructure, combined with a still-healthy consumer, continues to support earnings growth across sectors, while the longer-term benefits of productivity gains and expanding AI use cases should favor companies with innovative and disciplined management teams.

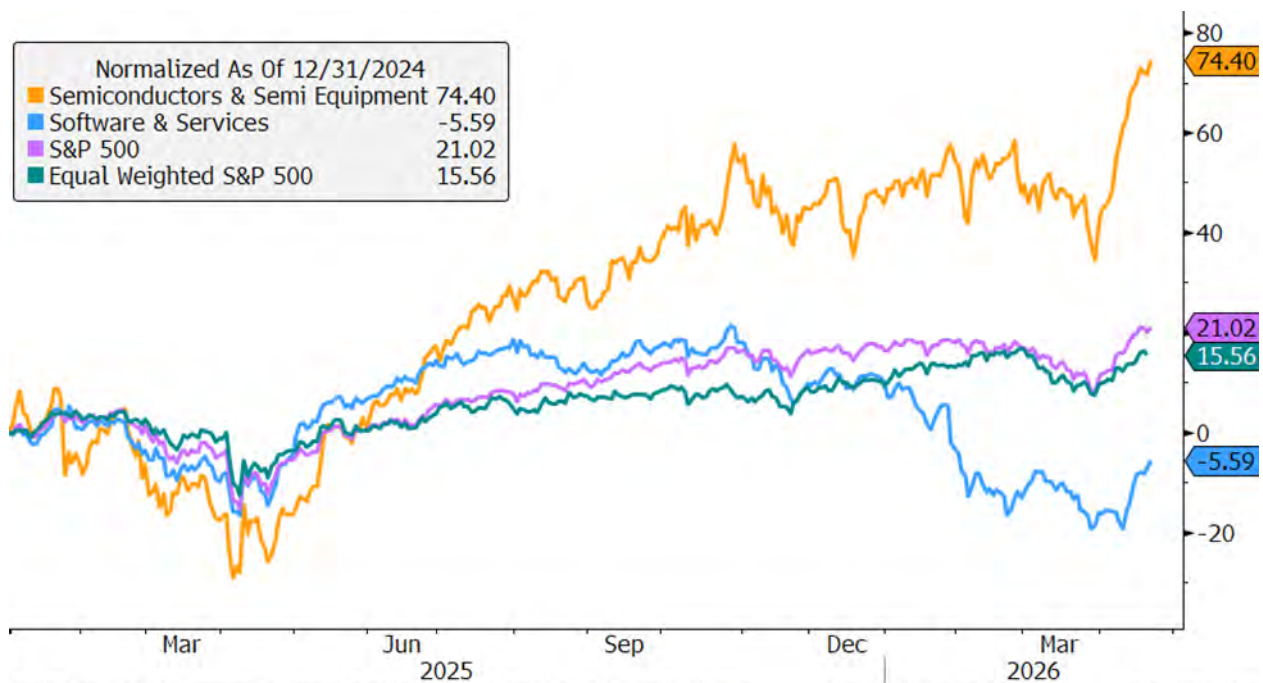
### *Divergence Within the Tech Sector*

A clear divide is emerging within the Tech sector between AI infrastructure winners and segments of software that are lagging. While software broadly participated early in the AI rally, companies are now facing slower enterprise spending as corporate

customers look to cut costs. At the same time, increased investment in AI capabilities is pressuring margins. In contrast, names related to semiconductors and data center buildout are seeing more direct demand, leading investors to favor the companies benefitting now from the spending boom.

### *Software Company Performance Lags Benchmarks Since 2024*

This dynamic reflects a shift in how markets are valuing the AI opportunity. Investors are increasingly focused on companies with revenue visibility, scalable platforms, and a direct link to the buildout of AI capabilities. We still believe the Tech sector offers meaningful opportunities, but being selective will be more im-



SSSEQX Index (S&P 500 Semiconductors & Semiconductor Equipment Industry Group GICS 2 Index) Daily 31DEC2024-22APR2026

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Source: Bloomberg



## EQUITY STRATEGY

portant than in earlier phases of the cycle.

### *Return of the “Other 493”*

Despite the continued dominance of mega-cap Tech, market breadth has expanded beyond this segment. This does not suggest a shift away from Tech leadership, but rather an expansion of participation that we view as a signal of a healthier, more durable cycle. While analysts expect the Magnificent 7 to grow earnings meaningfully in 2026 (24.6% per FactSet estimates), the other 493 companies in the S&P have strong growth prospects as well (15.9%). A key driver is the evolving nature of the AI investment cycle. What markets initially viewed as a digital transformation is increasingly becoming a physical one, with Industrials, Utilities, and Energy seeing major benefits. Data center construction, grid investment, and power generation are all emerging as necessary components, linking sectors that have historically operated more independently. The result is a market that appears less dependent on a narrow group of companies than in prior years, supporting the broader trajectory of earnings growth.

### *How Sustainable is the AI Spending Boom?*

The scale of this corporate investment is the defining feature of the

current market. However, it is fair to question whether this pace of spending can continue. We believe it is currently sustainable out of competitive necessity, where hyperscalers must invest to maintain market position in an accelerating AI arms race. This appears increasingly supported by fundamentals, as demand for compute is rapidly outpacing available capacity while revenue streams are beginning to scale.

However, the path forward is unlikely to be linear. These levels of investment are pressuring margins and free cash flow in the near term, particularly as companies balance growth initiatives with profitability expectations. Additionally, more capital-intensive areas of the broader buildout such as energy and infrastructure are more sensitive to interest rates and funding conditions. This sensitivity is particularly relevant today, where elevated oil prices have the potential to keep inflation stickier.

We believe these dynamics are more likely to create periods of volatility than signal a structural shift. Market reactions to incremental spending announcements have created buying opportunities among individual names, as high-quality companies experience short-term pressure despite strong long-term positioning. As such, the sustainability of the AI cycle may be less about the level of investment and more

about how markets digest it over time.

### *Can Consumers Keep Supporting Corporate Earnings?*

As important drivers of earnings growth, the consumer and labor market are showing signs of pressure, yet conditions remain relatively stable. The labor market has transitioned into a slower-growth phase with reduced hiring but limited layoffs, supporting income growth without signaling significant deterioration yet. Consumer behavior reflects a similar pattern. Aggregate spending is sturdy, though increasingly uneven beneath the surface. Higher-income households continue to support discretionary spending within the economy, while lower-income consumers are more sensitive to cumulative inflation and borrowing costs.

Energy prices remain an important variable. Fluctuations tied to the Iran conflict have the potential to influence sentiment and spending patterns. This dynamic has also contributed to a more uncertain policy backdrop, where inflationary risks complicate expectations for rate cuts this year. However, the consumer has thus far demonstrated an ability to absorb these pressures, helping to sustain corporate



## EQUITY STRATEGY

earnings even as overall growth moderates.

### *Risks to the Outlook*

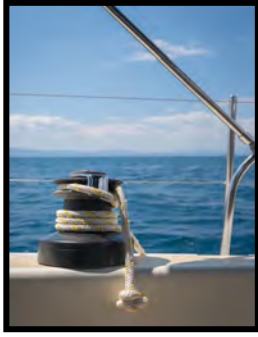
While the overall backdrop is supportive, risks are evolving. Geopolitical uncertainty remains at the forefront; an extended closure of the Strait of Hormuz is clearly reigniting inflation fears. At the same time, the scale of AI-related investment introduces the potential for a disconnect between spending and returns, which could weigh on margins if expectations are not met quickly enough.

The consumer also represents an area of focus, particularly if layoffs accelerate, which would likely erode spending power and expand the existing weakness into middle and upper-income households. Stress within private credit markets also warrants attention, as tighter liquidity or credit events could spill over into broader financial conditions. Finally, equity valuation levels remain above historical norms, suggesting that markets may be more sensitive to changes in earnings expectations or interest rate dynamics than in prior years.

### *Implications for the Community Bank Equity Portfolio*

For Community Bank portfolios, we believe the current environment reinforces the value of a disciplined

and conservative investment approach. While we see a positive long-term outlook for equities, we must be mindful of potential near-term volatility that can have an immediate impact on capital through mark-to-market movements. Thus, positioning should emphasize high quality, industry leading companies with diversified earnings exposure and experienced management teams, while ensuring appropriate sizing of the portfolio relative to capital levels. The broadening market participation and improving earnings trends are encouraging, but we believe selective active management among individual names will be critical as winners and losers emerge from the uncertainty. ♦



## ALM STRATEGY

### *ALM STRATEGY*

#### *Utilizing ALM Modeling as a Strategic Framework*

ALM in 2026 is defined by a series of strategic choices. While some institutions are taking a defensive stance, prioritizing liquidity, capital preservation, and risk reduction, others are adopting a more offensive approach, selectively extending duration, pursuing asset growth, and positioning for predicted future rate movements.

For decades, from a risk management perspective, ALM has relied heavily on static scenario analysis. Standard rate shocks, typically parallel shifts of +300bps to -300bps, but now frequently with +/-400bps shocks, have served as the foundation for measuring interest rate risk, and have done an admirable job. However, the reality of Q2 2026 is far more complex than the assumptions embedded in traditional static models. Interest rates and deposit behavior feel more challenging than normal, and liquidity concerns can emerge rapidly. The limitation of static modeling becomes especially evident in strategic planning. At EPG, we view static scenarios primarily serving a regulatory purpose, while the business plan is the tool financial managers rely on to make critical decisions that shape the institution's future. At times,

though, even dynamic, business plan modeling may not be enough, and for those instances, more granular scenarios can be created to address a specific need.

The business plan serves as the foundation for any strategic initiative, but we then refine key assumptions to generate a deeper analysis. Whether an institution is opening a new branch, launching a new deposit product, or evaluating a potential acquisition, we run targeted scenarios specifically designed to provide key information about the viability of the project. We then assess the results and extract key insights to inform strategic discussions—for example, identifying the earnings breakeven point or the inflection point at which capital, after initially declining due to asset growth, begins to recover. This type of detailed analysis is critical before the start of a project and provides vital information as analyses are updated as you move forward through the life of the initiative. While the ALCO report is typically prepared on a quarterly basis, we believe the process should be supported by ongoing communication, and include not only the base business plan, but also other longer-term or one-off projects.

#### *The End of “Sticky” Deposit Balances*

One of the most significant changes in the ALM landscape has been the transformation of

deposit behavior. The long-held assumption that non-maturity deposits are stable, low-cost, and rate insensitive has been fundamentally challenged.

As a result of rates increasing since the pandemic lows, depositors have become more active with their rate searches. Deposit balances have steadily migrated from low interest-bearing accounts into higher-yielding alternatives, including money market funds, CD specials, and online savings platforms. This shift has forced banks to confront a difficult tradeoff: whether to raise deposit rates to retain balances or preserve margins at the risk of deposit outflows.

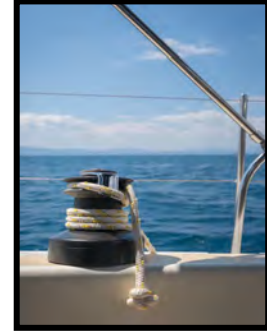
Institutions are increasingly distinguishing between operational deposits, relationship-driven balances, and rate-sensitive funds. This segmentation is not just analytical, it is strategic, informing pricing decisions, liquidity planning, and even tweaking product design.

#### *Shared Trends Looking Forward*

Most of the business plans we model lean more heavily on customized, in-house assumptions rather than purely interest rate forecasts. The growth percentages generally skew conservatively, particularly in competitive lending segments such as commercial real estate (CRE) and construction, while continuing to assume runoff in residential portfolios.

Earlier in 2026, when the 10-year Treasury yield hovered in the low

## ALM STRATEGY



4% range, residential mortgage rates followed suit, with fixed rates in the low 6% range and adjustable-rate mortgages in the mid-5s. By the end of March, however, Bankrate reported that the national average for a 30-year fixed mortgage had risen to 6.48%, up from 6.12% the prior month.

Despite these rate movements, residential lending activity continues to be constrained more by a combination of limited housing inventory and low-yielding pandemic era mortgages and MBS clogging up their balance sheets. For banks, the more favorable dynamic lies in CRE and construction lending, where pricing remains attractive relative to funding costs. As a result, these segments are driving the bulk of loan growth for many institutions, aligning with where most clients are currently seeing the strongest opportunities.

On the funding side, deposit costs have proven to be stickier than many

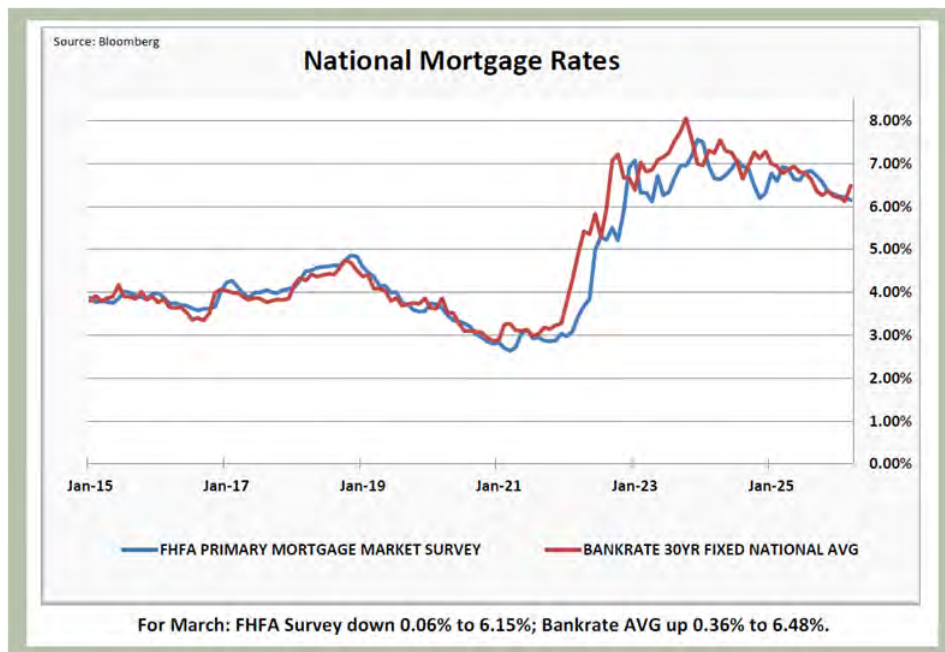
institutions anticipated. Despite shifts in the rate environment, banks continue to offer certificate of deposit (CD) rates in the range of 3.65% to 3.80% to retain balances, with even more competitive pricing often required to attract new money. We have recently seen new money specials approaching 3.90%, and in some markets, trending back toward 4%.

High yield savings accounts and tiered money market deposit accounts (MMDAs) offer a compelling alternative to CDs for customers who prioritize liquidity alongside yield. As CD rates decline closer to MMDA levels, deposit mix trends may shift back toward NMDs, reflecting a renewed preference for flexibility.

On the wholesale funding side, the curve offers little incentive to extend duration, with one-month borrowing rates around 3.87%

compared to approximately 3.83% for one-year terms. As a result, shorter-term funding strategies appear more attractive in the current environment.

CD structures themselves also reflect this preference for flexibility. Promotional terms remain concentrated on the short end, typically under six months. This persistence has contributed to limited term extension, with less than 10% of new or renewed CDs extending beyond one year, reinforcing the market's bias toward short-duration funding. ♦





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