Markets around the world did yeoman's work delivering strong returns during the second quarter. Emerging markets were the hands down winner posting a 24% gain. Unsurprisingly, given the craze of all things AI, growth stocks bested value stocks. Even small-cap stocks gained a thumping 21.6%. Global bonds posted a small positive return as did the dollar. Impressive results given the backdrop against which they occurred.

2Q2026: STRONG RESULTS WITH HINTS OF A POSSIBLE ROTATION

Equity Market Returns
Total Returns as of June 30, 2026

	June	Q2	YTD
MSCI All Country World Index	-0.8%	15.1%	11.5%
MSCI Europe Asia and Far East Index	0.1%	11.1%	9.9%
MSCI Emerging Markets Index	-1.4%	24.1%	24.0%
S&P 500 Index	-1.0%	15.2%	10.2%
S&P 500 Equal-Weight Index	2.4%	11.4%	12.1%
Russell 1000 Index	-0.5%	15.1%	10.3%
Russell 1000 Growth Index	-2.7%	16.7%	5.3%
Russell 1000 Value Index	2.3%	13.9%	16.2%
Russell 2000 Index	3.7%	21.6%	22.7%
BBG Magnificent 7 TR Index	-8.8%	11.7%	-1.7%

Source: Bloomberg, Brooklands Partners LLC

The world failed to fall apart after hostilities commenced between the U.S. and Iran. Despite an early market shuddering, oil prices going parabolic, and energy rationing in Asia, markets recovered their form in relatively short order as the trading of bombs turned to the trading of demands for ceasing hostilities.

Nonetheless, the volatility and inflationary pulses I warned of in the 2nd quarter note did materialize. Yet, whenever equity markets appeared on the verge of upset, promises from the White House of an imminent deal ending the conflict and opening the Strait of Hormuz ameliorated investors' concerns and market volatility. On the other hand, the inflationary pulses caused by higher energy prices continue and will likely take some time to work through the economy. Interest rates attest to this as the entire structure of the yield curve is higher at the end of the quarter compared to the day before hostilities began. The bond market remains the sentinel reminding investors that the "all clear" signal has not been sounded.

It appears there are three prevailing narratives now facing investors. First, the conflict with Iran is moving into a resolution phase. This allows investors to return to the second narrative, dealing with the transformational impacts of Artificial Intelligence. A third but subsidiary

(cont'd.)

narrative holds that economic growth remains in fine form, and the rapidly expanding government debt is not something of immediate concern.

The first narrative, while hopeful, is fanciful. The Iranians are famously tough negotiators. The U.S. is pressing for a deal ahead of mid-term elections but where is the Iranian incentive to accommodate the American timeline? Bombing has been tried without success so far. The last nuclear agreement with the Iranians took more than two years to negotiate. While there is a template for an agreement in the erstwhile Joint Comprehensive Plan of Action (JCPOA), it is reasonable to expect that negotiations will take time to be concluded, which means episodic breakdowns will occur as happens in any difficult negotiation. With these breakdowns, closures and reopenings of the Strait will likely be a feature of the future, as will periodic flares of mutual missile exchanges. This might lead to market ructions, or it might be just more background noise. It is impossible to tell at this juncture.

The second narrative concerning the transformational impact of AI is more troublesome. Promoters of all things AI claim the demands of this digital build out will be long lived and profitable. Worry not, they say, about a bubble in asset prices of companies in the space, as growth will be an enduring feature as far as the eye can see. Without a doubt, the incorporation of AI into daily workflows holds enormous promise. I have seen it at Brooklands where I use AI agents to do work that is the equivalent of a first-year analyst. These agents are helpful in smart searches, summarizing earnings and research reports, and organizing and executing the first run of complex portfolio construction studies. They are not fool proof as they require checking of work. More importantly, they are not capable of lateral thinking, which is the work of a second or third-year analyst.

The promise is obvious, but it will take time to sort. Successful commercialization of any new technology takes time to separate the wealth creating business models from the wealth destroying ones. It has always been thus, from railroads to the internet: the first entrants are often not the ultimate survivors.

The counter to the prevailing AI narrative is found in the numbers. Large Language Model companies such as OpenAI and the hyper-scalers that provide the infrastructure for the LLM providers have an insatiable appetite for capital. Global corporate investment in AI totals more than a trillion dollars from the end of 2022 through 2025. From the end of 2020, the number jumps to $1.64 trillion.[1] J.P. Morgan expects total global AI-related investment will reach $5.5 trillion through 2030.[2]

The problem is an obvious one. What types of returns will that capital investment deliver? No one knows as the future is unwritten. If past is prologue, we know that some of that investment will be very productive and a fair amount will not. There appear to be two camps of companies operating in AI World: the spenders and the profit makers. The LLM companies and hyper-scalers make the capital investment that builds AI World, while the chip designers, memory makers, data center construction companies, and investment bankers print profits. When will the profits appear for the LLM companies which are the root of all the spending? Again, no one

(cont'd.)

[1] Stanford University Human-Centered Artificial Intelligence, The 2026 AI Index Report

[2] *What bubble? JP Morgan says the $5.5 trillion AI capex explosion is profitable-for now.* Fortune.com June 25, 2026

knows. When pressed, one CEO of a prominent LLM company snapped the questioner should sell his stock when the CEO could not deliver a date when profits might be expected. If the favored AI narrative is to hold, investors will have to see a timeframe for profits.

Finally, the subsidiary narrative which suggests that concerns about the explosion of government debt are overdone since the economy is growing and employment is high is suspect. The federal government's appetite for capital puts that of any hyper-scaler or LLM company to shame. Moreover, unconstrained by the public company need to make a profit and satisfy investors, the federal government appears to be undeterred in its spending. Old hands at capital markets are reminded of the crowding out that occurs when an uneconomic player like the government competes for the same capital that the private sector does. It is hard to satisfy the financing needs of both the federal government and the private sector without a repricing of capital.

Sensing a limit may be why yields rose over the second quarter. Investors seem to be taking note as well, as the average stock, represented by the S&P 500 equal-weighted index, rose 2.37% in June while the market cap version of the index fell almost 1% and the Magnificent 7 collection of companies dropped roughly 9%. The start of a market rotation could be commencing, hence the average stock picking up, and emerging markets and developed markets showing solid returns. If this is the case, a new narrative will take hold. One for which we have positioned through exposures to international markets, broader U.S. market exposure than that afforded by the S&P 500 index, and thematic investments in defense and commodities.

As always, please reach out if you have any questions. I hope you have a wonderful summer.

Originally published July 6, 2026

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