PLAINSCAPITAL BANK

ECONOMIC HIGHLIGHTS

STRENGTH ★ MOMENTUM

Economic Commentary
August 2026

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Executive Summary

- The U.S. economy keeps expanding, but growth is now more investment-driven than consumer-driven. Business investment, technology spending, data center construction, and AI-related capital expenditures are key drivers.
- Corporate capital spending remains a strong economic sector, with nonresidential fixed investment, capital goods orders, technology infrastructure, and data center projects trending higher despite uncertainty.
- The labor market has cooled but remains healthy. July payrolls declined slightly, unemployment dropped to 4.1%, claims are low, and demographic trends imply fewer jobs are needed to sustain stability than in previous cycles.
- Inflation remains the main challenge for policymakers. Despite softer June inflation and contained wage pressures, energy prices, tariffs, and supply disruptions pose ongoing inflation risks.
- Federal Reserve officials seem more focused on inflation than employment. Labor market conditions are stable, and markets debate whether the next move will be a rate hike or cut.
- Earnings growth remains strong with second-quarter S&P 500 earnings surpassing expectations, driven by healthy profit margins, productivity gains, and tech-sector leadership.
- AI investment remains a key driver of economic growth and profits, with data center construction, semiconductor demand, cloud infrastructure, and tech spending accelerating globally.
- Market leadership expands beyond a few mega-cap tech stocks. Financials, industrials, value sectors, and small-cap equities show increased participation, supporting a healthier market.
- International growth is mixed but generally positive. Taiwan, South Korea, Japan, and other tech economies benefit from strong demand for semiconductors and AI, while China shows relative weakness.
- Credit conditions remain favorable, not indicating recession stress. Lending standards are improving, commercial lending is expanding, and investment-grade credit markets stay stable despite rising geopolitical uncertainty.
- Key risks include persistent inflation, energy shocks, Middle East tensions, high market expectations, and potential profit peak after a strong earnings cycle.

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US Economic Cycle Drivers:

Growth	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Citi Economic Surprise - United States	23.0	40.5	↓	↑
Bloomberg Economics US GDP Nowcast	3.0	2.6	↑	↑
Concensus USA Growth Forecast Survey	-8.6	-33.7	↑	↑

Inflation	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Citi Inflation Surprise Index - United States	-9.4	-13.9	↑	↑
Bloomberg Economics US CPI Nowcast	3.3	4.3	↓	↑
Concensus USA Inflation Forecast Survey	15.0	79.5	↓	↓

Employment	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Unemployment Rate	4.1	4.3	↓	↓
Conference Board Employment Trend	107.7	107.6	↑	↑

Consumer Spending	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Johnson Redbook Retail Sales y/y	8.3	7.3	↑	↑
Adjusted Retail & Food Service Sales	6.7	4.2	↑	↑
Conference Board Consumer Confidence	90.8	93.8	↓	↓

Corporate Profitability	NTM (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
S&P 500 Est. Sales Growth Rate	7.8	8.5	↑	↑
S&P 500 Est. EPS Growth Rate	11.9	9.4	↑	↑
NFIB Small Business Optimism	97.4	95.9	↑	↓

Government Policy	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
Budget/ GDP	-5.7	-5.4	↓	↑
USD Real Effective Exchange Rate	107.8	108.1	↓	↓

Central Bank Policy Rate	Latest Value (%)	Value 3mo Ago (%)	Trend q/q	Trend y/y
U.S. Federal Funds Rate Upper Bound	3.8	3.8	→	↓
U.S. Market Implied Policy Rate 1Y Fwd	4.0	3.9	↑	↑

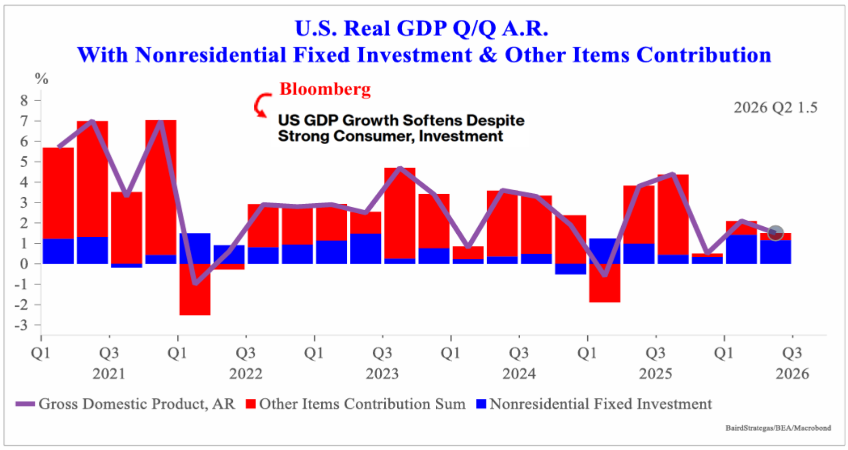
Liquidity	3mo Δ (%)	12mo Δ (%)	Trend q/q	Trend y/y
U.S. Domestic Liquidity	-0.6	-0.8	↓	↓
Global Liquidity Index	-1.8	7.8	↓	↑

Data source: Bloomberg

US & Global Economic Highlights

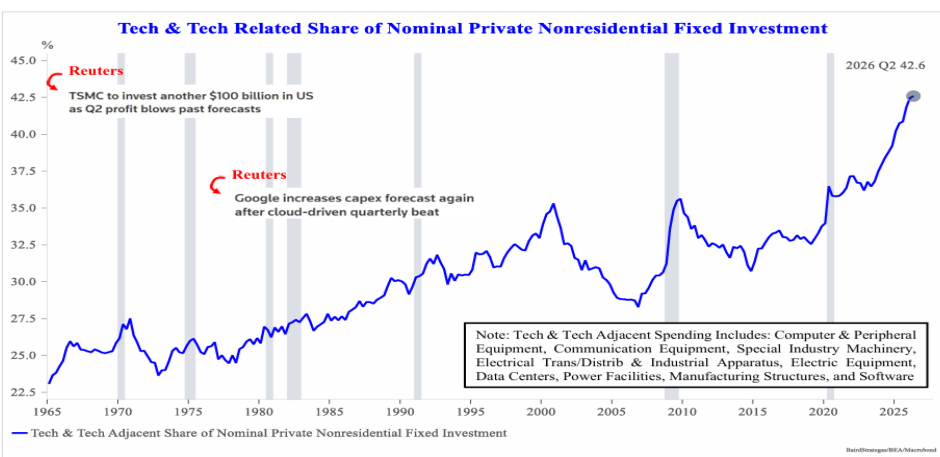
U.S. Economic Activity Continues to Expand: Consumer spending remains the primary driver of economic growth. Real GDP growth slowed to 1.5% SAAR in the second quarter, while real consumer spending grew at 3.2%. Capital spending on technology infrastructure, artificial intelligence, data centers, automation, and manufacturing capacity remained a notable positive theme, with nonresidential fixed investment providing meaningful support even as the consumer continues to lead this expansion.

NONRESIDENTIAL FIXED INVESTMENT CONTRIBUTION TO U.S. REAL GDP GROWTH REMAINS ELEVATED



AI Investment Remains a Powerful Economic Tailwind: Technology spending continues to accelerate across the global economy. Data center construction spending has now surpassed traditional office construction. Technology-related investment has historically accounted for a large share of overall business investment, and major technology companies continue to raise Cap-Ex plans to support AI infrastructure. This investment cycle remains one of the critical drivers of economic growth and corporate profitability.

TECH-RELATED INVESTMENT HAS BEEN GROWING FOR MANY DECADES



Labor Market Cooling Without Meaningful Deterioration: July's employment report showed payroll declines of 23,000 jobs, but the unemployment rate improved to 4.1%. Jobless claims have remained broadly contained, though the most recent reading of 209k (week of August 8) moved back above 200,000 after several weeks below that threshold. Importantly, declining labor-force participation means fewer monthly jobs

Critical points for the economy

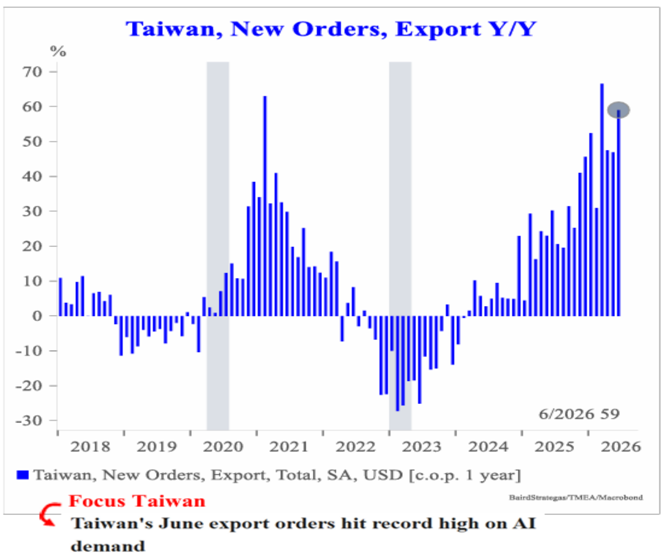
- Business investment remains the primary engine of economic growth.
- AI-related capital spending continues to support U.S. and global expansion.
- Corporate investment remains significantly stronger than consumer-led growth.
- The labor market has cooled but remains broadly healthy.
- Fewer jobs are needed to maintain employment stability due to demographic trends and lower labor-force participation.
- Manufacturing activity has strengthened meaningfully in recent months.
- Technology infrastructure spending continues to accelerate.
- Consumer spending remains resilient despite weak confidence surveys.
- Inflation pressures have moderated but remain elevated relative to central bank targets.
- Housing remains one of the weakest segments of the economy.
- Taiwan, South Korea, and Japan continue to benefit from strong semiconductor and AI demand.
- China remains a notable area of relative economic weakness.
- Productivity gains are helping offset higher labor and input costs.
- Base case remains continued economic expansion rather than recession.

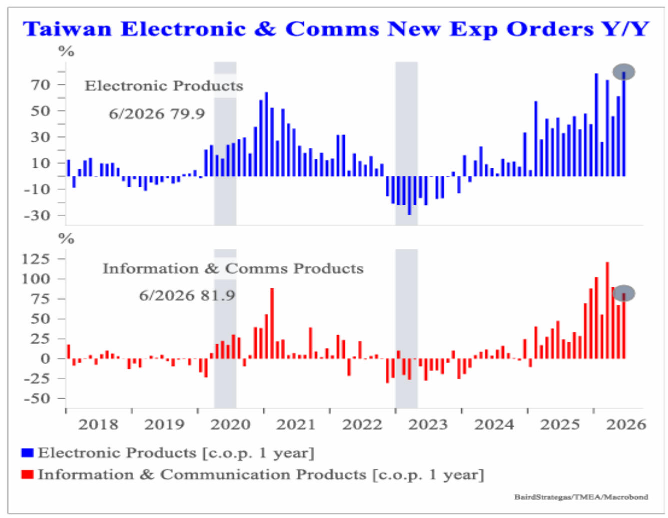
are required to maintain labor-market stability than in previous decades. Healthcare employment, demographic trends, and ongoing labor shortages continue to provide support even as hiring activity moderates. Current conditions appear more consistent with normalization than recession.

Consumer Spending Remains Resilient: Despite weak confidence readings, actual spending activity continues to exceed expectations. Real consumer spending remains near trend, supported by healthy household balance sheets, low unemployment, and continued income growth. Survey measures remain depressed due to concerns surrounding inflation and affordability, but spending behavior has remained considerably stronger than sentiment surveys would suggest.

Manufacturing Activity is Improving: Manufacturing has become one of the more encouraging developments within the economy. ISM Manufacturing improved to 55.6 in July, capital goods orders remain firm, and industrial activity continues benefiting from technology investment, reshoring initiatives, and infrastructure spending. Areas that had previously lagged the broader economy are beginning to participate more meaningfully in growth.

Global Growth Remains Increasingly Driven by Technology Demand: International growth remains uneven, but technology-oriented economies continue to perform exceptionally well. Taiwan's economy grew 12.9% year-over-year in the second quarter, South Korean exports and GDP remain robust, and Japanese semiconductor equipment orders continue to rise. Strong global demand for semiconductors, cloud computing infrastructure, and AI-related technologies remains one of the most important sources of global growth.





China Remains the Most Notable Area of Weakness: China continues to lag most major economies. While inflation has stabilized, consumer demand remains subdued, business confidence remains weak, and economic activity continues to underperform developed-market peers. China continues to face headwinds from subdued consumer demand and weak business confidence, with 2026 GDP growth consensus at approximately 4.6% — below its historical trend. While China is investing heavily in AI infrastructure domestically (a reported $295 billion five-year data center buildout), its participation in the global AI investment cycle has been more insular and less integrated with the broader technology supply chains driving growth in Taiwan, South Korea, and Japan.

Bottom Line: Economic conditions remain consistent with continued expansion. Business investment, technology spending, manufacturing improvement, and resilient consumer activity continue to support growth despite moderating labor conditions and elevated geopolitical uncertainty. The global economy is increasingly being driven by AI-related capital spending, while inflation and energy markets remain the primary variables that could alter the outlook.

Monetary Policy & Fed Outlook Highlights

Fed Focus Shifts Back to Inflation: The Federal Reserve's policy debate has decisively returned to inflation. While the July employment report was soft, Fed officials continue to view the labor market as broadly consistent with maximum employment. Several hawkish Fed officials have explicitly argued that stable unemployment allows the central bank to prioritize inflation risks. The key issue is that the economy no longer requires the same level of monthly job creation to keep unemployment stable. The Atlanta Fed jobs calculator suggests roughly 40,000 jobs per month may be sufficient to maintain a steady unemployment rate, assuming labor-force participation continues to drift lower.

Labor Market Softness Is Not Yet Enough to Change Policy: July payrolls declined by 23,000, but the unemployment rate fell to 4.1%, participation declined, and initial jobless claims have remained broadly contained, though the most recent reading of 209k (week of August 8) moved back above 200,000. This combination creates a difficult message for policymakers: hiring has slowed, but broader labor market stress remains limited. Strategas' view is that the Fed's employment mandate is still effectively satisfied. As long as unemployment remains near 4% and jobless claims stay low, policymakers are likely to focus more on inflation than on weaker payroll growth.

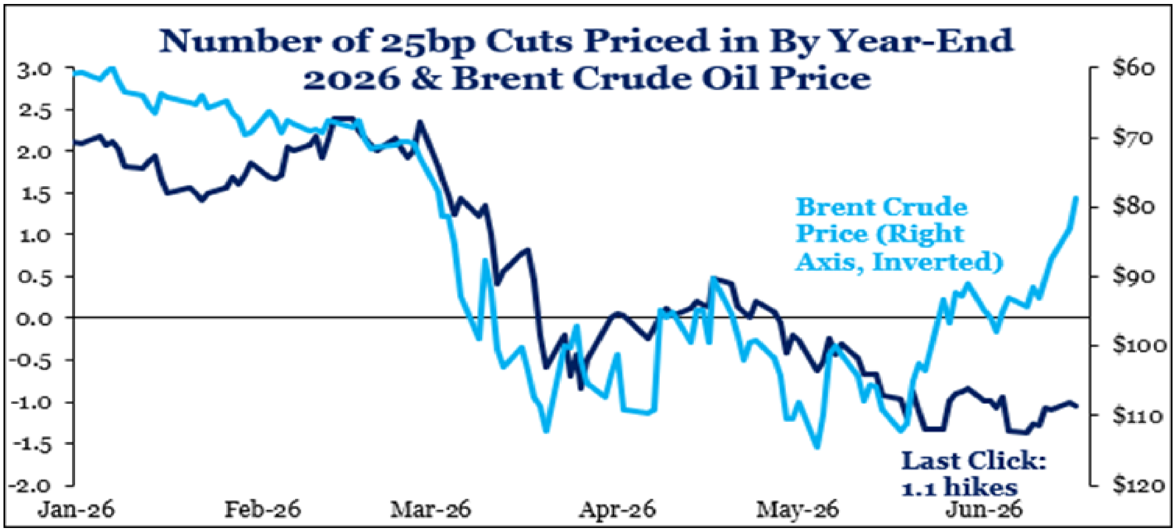
Source: Department of Labor, Baird Strategas, Data updated as of 8/7/26

Inflation Risks Remain Unresolved: Inflation pressures have moderated from earlier peaks, but the Fed is not yet in a position to declare victory. Energy prices remain sensitive to developments in the Strait of Hormuz, tariffs remain a potential source of goods inflation, and global supply disruptions continue to complicate the inflation outlook. Strategas' central point is that shocks need to end, not merely pause, to be considered transitory. Oil, tariffs, and geopolitical risk have each eased at times, but none have been fully resolved. That keeps the Fed cautious even when individual inflation reports look more benign.

Fed Pause Remains Likely, But Hike Risk Has Increased: The near-term base case remains a Fed pause, particularly at the September meeting. However, the policy path has become more asymmetric as inflation risks linger and several Fed officials appear more willing to consider additional tightening. Futures markets now assign roughly a one-in-three probability of a rate hike by December, rising to approximately 40% by March 2027 — a meaningful shift, but not yet a base-case expectation. The policy path has become more asymmetric, and markets should not assume the next move is automatically a cut.

Critical points for policy

- Inflation remains the primary focus for the Federal Reserve, as labor market conditions are still viewed as broadly stable despite slower payroll growth.
- The July payroll decline does not appear severe enough to shift the Fed away from its inflation focus, especially with unemployment declining to 4.1% and jobless claims remaining low.
- Demographic trends and lower labor-force participation mean the economy needs fewer monthly jobs to keep unemployment stable than in prior cycles.
- Markets continue to debate whether the next Fed move will eventually be another rate hike rather than a rate cut.
- It's looking more like the Fed remains on hold at the September meeting, but a rate hike in December and another in early 2027 are still in play if inflation risks remain unresolved.
- Energy prices, tariffs, currency volatility, and geopolitical tensions remain the most important inflation risks facing policymakers.
- The Fed's reduced forward guidance may itself function as a form of tightening by increasing policy uncertainty and making each meeting more data-dependent.
- Balance sheet policy has become an increasingly important potential tightening tool, especially as policymakers consider how to remove liquidity without immediately raising the fed funds rate.
- Treasury market volatility reflects more than Fed policy alone, with oil prices, Iran-related geopolitical risk, fiscal concerns, and yen intervention also influencing long-term yields.
- The base case remains an extended near-term pause, but the range of possible Fed outcomes has widened.



Less Forward Guidance May Be a Form of Tightening: Chair Warsh's communications approach appears to be intentionally less dependent on forward guidance. One could make the case that less guidance may itself tighten financial conditions by shifting more uncertainty onto markets and making each Fed meeting more "live." This approach forces investors to rely more heavily on incoming data rather than policy promises. In practice, reduced guidance can increase rate volatility and keep short-term yields from falling as quickly as they otherwise might when inflation data soften.

Balance Sheet Policy Becomes More Important: It is increasingly important to the Fed's outlook. The Fed's reserve management T-bill purchase program provided some accommodation earlier in 2026. Still, that program has now been wound down — the Fed announced it will conduct no reserve management purchases through mid-September. Chair Warsh has formed a task force to review the $6.7 trillion balance sheet, and Wall Street expects outright shrinkage to begin as early as Q1 2027. The key issue remains whether policymakers can begin removing liquidity without destabilizing funding markets.

Long-Term Yields Reflect More Than Fed Policy: The rise in long-term Treasury yields should not be viewed solely as a referendum on Fed credibility. Strategas notes that long bond yields are also being affected by Iran-related risks, oil prices, fiscal concerns, Treasury supply, and currency market volatility. Japan's yen weakness and related intervention are also important because severe yen pressure could increase the risk of Japanese investors selling Treasuries. US support through the FIMA repo facility has been proposed as a mechanism to reduce Treasury selling risk — Treasury Secretary Bessent has urged the Fed to expand the facility — but Japan has not yet utilized it. Japan reportedly has alternative liquidity tools available that would not require outright Treasury sales.

Bottom Line: The Fed is likely to remain on hold in the near term, but the policy backdrop has become more complicated. The labor market has cooled, yet not enough to force a policy pivot. Inflation risks tied to energy, tariffs, currency volatility, and supply shocks remain unresolved, keeping the Fed tilted toward caution. The most likely outcome remains a September pause, but markets should continue to take seriously the possibility of renewed tightening later this year or in early 2027 if inflation pressures persist.

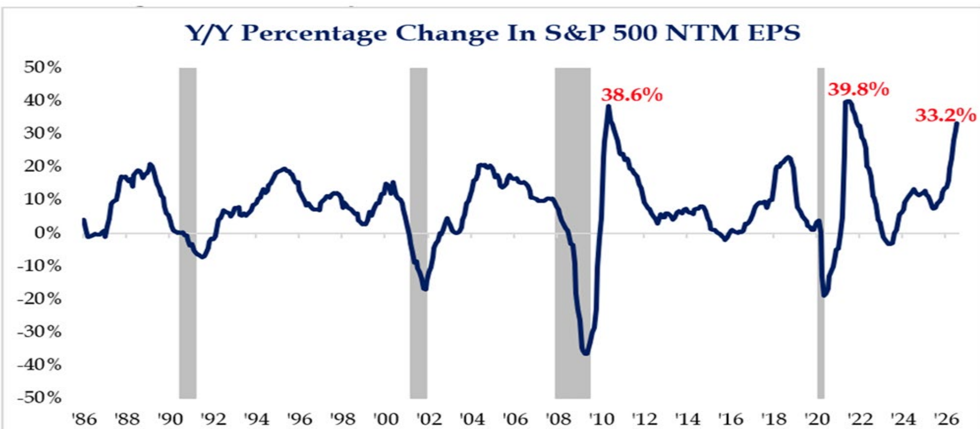
Corporate Profitability Highlights

Earnings Growth Has Exceeded Expectations: Second quarter earnings season has been considerably stronger than expected. S&P 500 earnings growth has reached nearly 50%, more than double the initial estimate of roughly 24%. However, the 47-50% headline figure includes a large one-time mark-to-market gain at Alphabet; on an ex-item basis, growth is closer to 26-33%, still well ahead of the 24-26% initial estimate. Revenue growth has also improved materially, rising to approximately 11-14% from an initial estimate near 10-12%. The communication services contribution to headline EPS is driven more by the magnitude of Alphabet's one-time gain than by broad sector strength, and the beat rate was less than 50%. In contrast, Consumer Discretionary had a stronger beat rate of ~60%. 85% of companies beat consensus estimates, and all 11 GICS sectors are on track for positive growth, with 8 in double digits.

S&P 500 2nd Quarter Earnings Scorecard

	Sales Growth (Y/Y%)			Earnings Growth (Y/Y%)			# Reported
	Jan. 1	Jul. 1	Today	Jan. 1	Jul. 1	Today	
S&P 500	6.9%	11.7%	15.1%	15.2%	24.4%	49.6%	385/500
Discretionary	5.9%	7.2%	8.8%	8.8%	5.5%	89.2%	33/47
Staples	5.7%	7.4%	8.0%	7.0%	5.6%	8.3%	20/34
Energy	-1.3%	23.8%	41.8%	11.6%	116.0%	138.5%	16/21
Financials	5.5%	6.9%	11.9%	7.7%	8.1%	22.8%	66/76
Health Care	4.9%	4.6%	7.4%	7.8%	-9.3%	-7.2%	46/59
Industrials	5.5%	8.2%	11.7%	15.1%	10.3%	17.9%	73/83
Materials	3.4%	7.9%	8.7%	18.6%	32.7%	40.0%	22/25
Real Estate	7.0%	9.7%	11.4%	6.3%	6.2%	9.6%	28/31
Technology	19.2%	33.8%	35.4%	35.5%	65.5%	72.2%	43/73
Communications	8.8%	11.9%	12.8%	6.0%	8.0%	107.7%	14/20
Utilities	7.4%	8.5%	6.7%	11.8%	11.3%	10.5%	24/31

Earnings Estimates Remain Elevated: The usual downward progression in forward earnings estimates has not materialized this year. Consensus expectations for 2026 and 2027 remain elevated, with 2026 earnings growth still projected at an unusually strong pace and 2027 estimates also remaining constructive. This reflects a favorable profit backdrop, but it also raises the hurdle for future upside surprises. If expectations have already outpaced fundamentals in parts of the market, even strong results may not be sufficient to support further price gains.



Source: Baird Strategas, FactSet, Data as of 8/07/26

Profit Margins Remain Strong, But Breadth Matters: Corporate profit margins remain one of the most important supports for the current expansion. Market-cap-weighted margins

Critical points for Corporate Profitability:

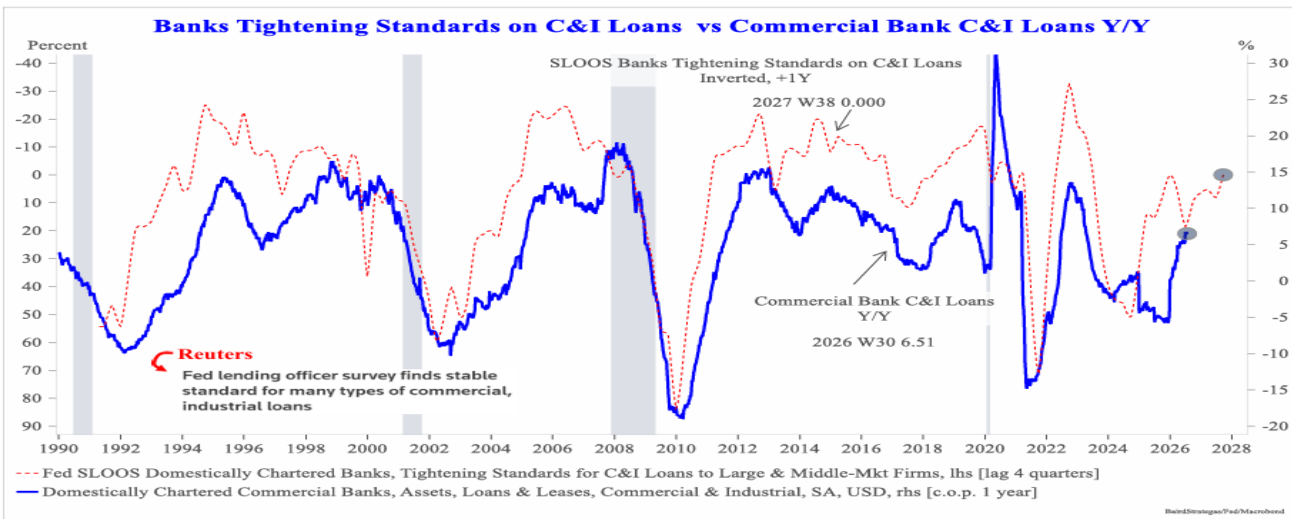
- Second-quarter earnings growth has significantly exceeded initial expectations.
- Revenue growth has also surprised to the upside, reinforcing a still-healthy demand backdrop.
- Earnings strength has been broad-based across sectors, though communications and consumer discretionary have contributed meaningfully to the upside.
- Consensus earnings estimates for 2026 and 2027 remain elevated, with less downward revision than is typical at this point in the cycle.
- Profit margins remain near record levels, but margin expansion is increasingly concentrated in mega-cap companies.
- Equal-weighted margins have begun to show signs of fatigue, creating greater need to monitor breadth of profitability.
- AI-related investment continues to support revenues, earnings, and productivity, but investors are demanding clearer evidence of returns on capital.
- Productivity gains are helping offset wage and input-cost pressures.
- Capital spending remains a key support for profit growth but may face more scrutiny if earnings growth begins to peak.
- Credit conditions remain broadly supportive and are not signaling recessionary stress.
- Input-cost risks remain elevated due to energy prices, tariffs, transportation costs, and AI-related supply-chain constraints.
- Corporate profitability remains supportive of expansion, but future gains are likely to depend more on earnings delivery than valuation expansion.

continue to rise, aided by mega-cap technology and communication services companies. Margin beats in Q2 2026 were broad, with 80% of companies beating on margins and the median company beating by 54 basis points. Elevated margins remain a critical cushion against tariffs, energy costs, labor expenses, and other input-cost pressures.

AI Investment Continues to Support Results: Artificial intelligence remains a major driver of revenue growth, capital spending, and earnings. Semiconductor demand, cloud infrastructure, software integration, data center construction, and power infrastructure continue to support corporate activity. At the same time, investors have become more selective. Companies linked directly to AI infrastructure continue to attract capital. Still, markets are increasingly focused on whether AI-related spending produces measurable returns rather than simply rewarding the scale of spending.

Productivity Gains Are Helping Offset Cost Pressures: Productivity has improved as the AI investment cycle continues, and rising productivity can help offset wage and input-cost pressures. Trend productivity remains well below prior productivity booms, but recent improvement is important because stronger output per hour can limit unit labor cost growth and support margins. This is particularly important in an environment where wage growth, energy costs, tariffs, and transportation costs remain potential risks to profitability.

Credit Conditions Remain Supportive: Corporate credit markets continue to signal confidence in fundamentals. Credit spreads remain historically tight, lending standards have eased, and commercial lending growth remains positive. While issuer differentiation is emerging and higher financing costs bear watching, current credit conditions are not consistent with broad recessionary stress. Stable credit markets remain an important source of support for capital investment, refinancing, and shareholder returns.



Peak Profit Risk Bears Watching: The central risk is not that corporate profitability is weak, but that profit growth may be approaching a cyclical peak after an exceptionally strong period. High earnings expectations, record-level margins, elevated input costs, and increased scrutiny of capital spending create a narrower margin for error. Corporate profitability remains highly supportive of economic expansion, but future market gains may require continued earnings delivery rather than additional valuation expansion.

Bottom Line: Corporate profitability remains a major pillar of support for the economy and markets. Earnings growth has exceeded expectations, margins remain elevated, AI investment continues to support revenues and productivity, and credit conditions remain constructive. The key question is whether profit growth can continue to exceed already high expectations as input costs, capital-spending scrutiny, and peak-margin concerns become more important.