July 31, 2026

2Q26 Market Commentary

Sentiment is noticeably bullish—and as a contrarian signal, that's a red flag. On the other hand, market internals are encouraging, with indexes representing several different segments of the market reaching new highs.

Overview

Easing geopolitical tensions and excellent earnings growth propelled the S&P 500[1] to its best quarterly return (+15%) in six years. The S&P 500 Technology[1] sector exceeded the index's gain by more than double, while the other ten sectors all underperformed. Multiplying the index's hugely disproportionate weight in IT stocks (36%) with the almost grotesque returns of semiconductor equities resulted in the S&P 500's second quarter surge being primarily powered by its Tech stock exposure.

Small caps (Russell 2000[2]) and the tech-heavy NASDAQ[3] outshone the S&P 500, each locking in gains of over 21%. Improving economic data, hot inflation figures, and rising concerns about the U.S. fiscal situation drove interest rates higher and put Federal Reserve rate hikes back on the table.

Leuthold Equity Portfolios

During the second quarter, the firm's domestic equity strategy, Leuthold Select Industries (SI), performed slightly better than the S&P 500, profiting from the powerful upward momentum in the stock market. Not surprisingly, positions connected to the AI mania were the best performers; the most favorable group concentrations were Semiconductors, Electronic Manufacturing, and Communication Services. Outside the Info Tech space, stocks from Diversified Banks, Auto Parts & Equipment, and Investment Banking also boosted results. Small detractors to second-quarter return were holdings in the Health Care and Materials sectors.

Using the methodology of the SI portfolio, Leuthold Global Industries (GI) applies the same approach across a universe of globally traded equities. GI beat the MSCI All-Country World Index[4] (ACWI) by over 3% in the second quarter. Like the domestic equity performance, this global portfolio profited from Semiconductor-related names, as well as Airlines, Banks, and Auto Components. Alternatively, an overweight position in Integrated Oil & Gas was a drag, as the ongoing Iran conflict triggered a sharp selloff in these stocks.

Tactical Asset Allocation Portfolios

Our disciplined assessment of stock market health, which guides the level of stock market exposure in our TAA portfolios, hasn't triggered a decisive signal since early March 2025, when it deteriorated to "negative" in advance of the tariff-tantrum market meltdown. This quantitative analysis, which includes a wide range of factors segmented under the categories of Valuation, Cyclical, Sentiment, and Technical, improved back to the "neutral" zone three months later (June 2025), where it has remained ever since.

With our quant-driven outlook for stocks stuck in neutral, net equity exposure in Leuthold TAA portfolios was likewise contained in a middle-of-the-road stance around 55% over the last three months. We'd prefer less "fence-sitting" guidance from our stock market analysis, but we're mindful to let the evidence lead the way and keep emotions in check.

In the fixed income markets, the 10-year Treasury yield closed June at 4.44% compared to 4.32% at the end of March. This small change indicates that duration[5] was not a particularly important return generator in the second quarter. Credit spreads[6] narrowed slightly for investment-grade corporate bonds, and high-yield corporates saw spreads contract nearly 50 basis-points.[7] This favorable move meant that owning corporates was an advantage over Treasuries. Performance among the allocations in Leuthold portfolios was mostly flat to marginally positive. The one standout based on absolute return was the emerging market sovereign debt holding (+2%); however, due to the small size of the position, it had negligible effect on results. Other components in the fixed-income sleeve are quality corporate bonds, mortgage-backed securities (MBS), developed market sovereign debt, and treasury inflation-protected securities (TIPS).

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Outlook

While still advocating ample exposure to Info Tech and growth stocks, our equity group analysis has also steered us to several attractive market segments that are flourishing outside the fame and fortune of the AI and IT space. In fact, Leuthold equity portfolios have about ***10% lower concentrations*** in Technology stocks than the S&P 500 and MSCI ACWI. Among the non-IT opportunities, relative to the S&P 500, Leuthold Select Industries has notably heavier exposure to Health Care, Energy, and Materials stocks. Leuthold Global Industries' overweight equity segments compared to the MSCI ACWI include Financials, Industrials, and Energy. These allocations not only offer diversification and lower correlation to the major market benchmarks, but they should also benefit when investors' attention rotates away from the latest tech boom.

Although the composite score of our equity market assessment is stuck in a "neutral zone" holding pattern, its agnostic posture camouflages conflicting messages from the four factor categories. Valuations are stretched for large caps, with seemingly limited room for additional expansion. Sentiment is noticeably bullish—and as a contrarian signal, that's a red flag. On the other hand, market internals are encouraging, with indexes representing several different segments of the market reaching new highs. Breadth in terms of stock participation is a positive sign, suggesting that the market is "in gear" and well supported.

Thanks to the gargantuan sums being invested in data centers, corporate earnings are growing at a rate of more than 20%, which is a positive for equities. Nonetheless, the trillions of dollars being spent on the AI buildout are, in a sense, artificially boosting earnings, and when that slows, the impact may have a surprisingly depressing effect on future earnings. For now, with most market bellwether[8] indexes we monitor for internal fracturing having moved to new all-time highs in early July, the technical picture is compelling. We don't anticipate that a traditional, narrow market top is in the cards this summer.

Thank you for your ongoing support!

Scott Opsal, CFA | Chun Wang, CFA, PRM | Greg Swenson, CFA | Phil Segner, CFA

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[1] S&P 500 is a capitalization-weighted index of 500 stocks measuring performance of the broad domestic economy. S&P 500 Information Technology comprises those companies included in the S&P 500 that are classified as members of the GICS information technology sector

[2] Russell 2000 is a small-cap U.S. stock index that is made up of the smallest 2,000 stocks in the Russell 3000 Index.

[3] NASDAQ Composite is a stock market index that includes almost all stocks listed on the Nasdaq stock exchange.

[4] A stock market index that tracks large- and mid-cap equities across 23 developed markets and 24 emerging markets.

[5] A measure of a bond's sensitivity to interest rate changes, typically expressed in years.

[6] The extra yield a corporate or risky bond pays over a U.S. Treasury bond of the same maturity to compensate for default risk

[7] 100 basis points = 1%

[8] Dow Jones 65 (a price-weighted average of 65 stocks—30 industrial, 20 transportation, and 15 utility companies); Dow Jones Transports (includes major airlines, rail carriers, delivery services, trucking, and car rental companies); Dow Jones Utilities (water, electric, and renewable power producers); Russell 2000 (the smallest 2,000 stocks in the Russell Index); S&P 500 Financials (companies classified in the Financials sector); S&P 500 Cyclical Index (Consumer Discretionary, Industrials, and Materials stocks); S&P 500 Equal-Weighted Index (equally weighted version of the S&P 500); NYSE Daily Advance/Decline Line (a technical market breadth indicator tracking the cumulative total of daily advancing minus declining stocks on the New York Stock Exchange).

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