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Economy on Solid Footing as Negotiations Continue

The memorandum of understanding (MOU) between the U.S. and Iran has been signed, enabling a 60-day period to structure a lasting peace between the two countries, as well as Israel and Lebanon. The U.S. and Iran are simultaneously negotiating permanent peace terms and maintaining low-level hostilities, with Iran most recently declaring the Strait of Hormuz again closed due to the ongoing fighting in Lebanon. Here in the U.S., the economy is chugging along. And the U.S. mood has had an unexpected lift from the success of the U.S. Men's National Team as the World Cup plays out across North America.

Gasoline prices have come down, while remaining above prewar levels. We believe gasoline demand proved more elastic than anticipated during the height of the war, preventing worse-case scenarios of \$150- or \$200-per-barrel oil from materializing. The U.S. consumer remains resilient, with the tenacity and flexibility on display during COVID-19, the supply chain crisis, and the withering inflation that emerged in 2022 and has never fully gone away. And the economy remains on solid footing, with Argus Director of Economic Research Christopher Graja, CFA, recently raising his gross domestic product (GDP) forecasts for 2026 and 2027.

Energy and Demand Elasticity

The “prevailing wisdom” has been that gasoline demand is inelastic because consumers cannot reduce driving without putting their employment at risk. This entrenched belief led to ominous forecasts in the first weeks and months of the war, as the Strait of Hormuz remained locked down and nations began to work off their strategic reserves.

Gasoline and other derivatives such as diesel and heating oil experienced 40%-50% price appreciation in the early weeks of the war, tracking the rise in oil benchmarks

(Brent and West Texas Intermediate crude) to the \$100 level from the mid-\$60s. As traffic through the strait slowed to a trickle and remained there, economists broadly predicted that oil prices would continue rising as worldwide global reserves were exhausted. But oil prices, despite some brief and soon retraced spikes, never moved much above those shock peaks experienced right after the war started. And even before the signing of the MOU, they were moving lower.

Academic studies from the 1990s and before — by Thomas Sterner, P.B. Goodwin, and Molly Espey among others — reaffirmed the conventional wisdom that gasoline demand was inelastic. In a paper published in June 2020, economists from the Federal Reserve Bank of Dallas posited that gasoline demand was more responsive to price changes than economists once thought. Citing new modes of data collection, such as examination of gasoline tax policy and analysis of retail gasoline receipts, Dallas Fed economists argued that drivers could lever both short-term and long-term responses to significant price swings.

In the short term, consumers could reduce discretionary driving, improve vehicle maintenance, and drive more slowly to conserve fuel. They could temporarily embrace carpooling, long promoted by environmental advocates even though drivers in the U.S. never liked it. Over the longer term, they could replace gas-guzzlers with more fuel-efficient vehicles. That not only meant trading down from pickups and SUVs to midsize sedans but also shifting to hybrids such as the Toyota Prius and full electric vehicles (EVs) such as the increasingly popular Tesla.

U.S. consumers may envision European and Asian workers piling onto trains to get to work. That's not entirely true, as

(continued on next page)

ECONOMIC & MARKET COMMENTARY (CONT.)

car culture is pervasive. But overseas workers in many cases do have access to better public transportation options, and that too may have blunted the impact of less available oil for gasoline. In any event, global strategic reserves, which were first forecast to begin running dry by midsummer, are severely reduced but less depleted than anticipated in many nations. Asian nations, which are most heavily reliant on Middle Eastern oil, are also pivoting. India's imports of Russian crude oil are on track for record-high monthly levels in June, according to FuelWatch Global.

Many industry watchers are beginning to believe that the demand destruction from the war and shutdown of the Strait of Hormuz will never be fully reversed. The world's biggest oil importer, China, has responded to oil shortages by accelerating incentives for EVs. This is a win-win for China, which is weaning its own consumers off gasoline while simultaneously nurturing and expanding the world's largest EV industry.

Higher Outlook for U.S. Economic Growth

U.S. consumers have had lots of “No matter what, just keep going” moments in the past several years, and the oil and gasoline shock from the war is one more of them. Just since 2020, U.S. consumers have had to contend with the health and economic impacts of COVID-19 and business shutdowns; the supply chain crisis that first drove prices higher and the subsequent supply chain glut that caused business activity to stall; an oil price spike in 2022 related to Russia's invasion of Ukraine; the second, larger, and still unsettled round of U.S. tariffs on imported goods; and the war-related spike in energy prices that is rippling across all goods prices.

Through all this, consumers have kept going. May 2026 retail sales, released in mid-June, surprised to the upside with a 0.9% gain; economists had forecast a 0.5% monthly rise. Retail sales excluding vehicles rose 0.8%, compared with the 0.5% consensus call. Higher gasoline prices plainly goosed up the overall level of spending. Yet retail sales excluding vehicles and gasoline were up 0.5% in May, better than the 0.4% consensus forecast.

On a regional basis, the Philadelphia Fed Manufacturing Business Outlook Survey for June came in at 10.3%, at the upper end of the 5.0%-12.0% consensus range. With the jobs economy still strong and earnings growth the strongest since the immediate postpandemic period, business planners appear optimistic. The purchasing managers' reports from the Institute for Supply Management showed the industrial and services economies clearly in expansion territory in May. The Manufacturing Purchasing Managers' Index (PMI) was at 54.0%, and the Services PMI was at 54.5% — and both were comfortably above the 50% cut-off between expansion and contraction for these diffusion indexes.

Argus Director of Economic Research Graja recently raised his GDP forecasts for 2026 and 2027. He now looks for 2.3% GDP growth in 2026, raised from 2.1%, and 2.4% growth in 2027, raised from 2.0%. Chris now anticipates stronger gross domestic investment as companies seek to boost productivity and improve return on investment by spending on artificial intelligence (AI). This in turn raises spending on the equipment and intellectual property accounts in the GDP report.

Chris has not made major changes to his forecast for consumer spending, which continues to reflect a bifurcated economy. Employment growth has been stronger than expected. Tax refunds helped many consumers make it through the peak of energy price inflation in April and May. And he has raised his forecast for imports, which are subtractive to GDP, given that many if not most of the semiconductors used in AI build-outs come from Asia. All in all, Chris is being cautious in his GDP forecasts given the ongoing uncertainties created by the war with Iran, strains on consumers on the bottom leg of the K-shaped economy, and the possibility that spending on AI could periodically pause as companies assess the rapidly evolving environment.

Conclusion

Heading into the final full trading week of the first half of the year, on June 22, 2026, crude oil on the New York Mercantile Exchange (NYMEX) was trading at \$73.60 per barrel. That is well below the trend from early April 2026 to mid-May, when the price was consistently above \$100 and briefly (early in April) was above \$112. Current NYMEX oil prices are still well above the high-\$50s-to-low-\$60s level prevailing in the 12 months before the war began in March 2026.

As we went to press, Iran had again declared the Strait of Hormuz closed to traffic, while U.S. Energy Secretary Chris Wright was indicating that oil tankers continued to traverse a route across the southern part of the strait. This uncertainty could keep a floor under oil prices near current levels.

The passing of former Federal Reserve (Fed) Chairman Alan Greenspan brought a wave of nostalgia for the ritual of assessing his briefcase in advance of any Federal Open Market Committee (FOMC) meeting. According to pundits, a full briefcase packed with charts and papers was thought to signal a change in rates, while a slim briefcase signaled no change in monetary policy. Greenspan himself stated that the only thing changing the shape of his briefcase was whether or not he packed a sandwich.

Take a walk on Wall Street today and you will see a lot of backpacks and no briefcases. Recently appointed Fed Chairman Kevin Warsh has promised less transparency, and he made good on that promise with a meaningfully

ECONOMIC & MARKET COMMENTARY (CONT.)

truncated statement following the June FOMC meeting. We are not sure if the new chairman carries a briefcase or wears a backpack. But he may have more room to act on

his desire for lower rates than was anticipated just a few weeks ago, given the positive trend in energy prices and the resilience in consumer spending.

Jim Kelleher, CFA,
Argus Director of Research

KEY ECONOMIC FORECASTS

- The \$32 trillion U.S. economy remains on course for productive long term growth, powered by corporate investments in Artificial Intelligence. Nvidia CFO Colette Kress estimated, on May 20, that AI infrastructure spending is on track to reach \$3 - \$4 trillion annually by the end of this decade.
- Real Potential GDP – the sustainable speed limit of the US economy is poised to increase to 2.1%, on average, through 2030 according to the Congressional Budget Office. AI is likely to raise productivity, offsetting slower growth in the labor force from an aging population and reduced immigration.
- We recently raised our 2026 gross domestic product (GDP) growth forecast to 2.3% from 2.1%, our 2Q26 estimate to 2.5% from 2.2%, and our 2027 growth forecast to 2.4% from 2.0%. The major change is that indicators point to even stronger domestic investment. The investment dollars will boost the AI-dominated Equipment and Intellectual property categories in the GDP report.
- News of an interim peace deal between the U.S. and Iran sent gasoline below \$4.00 a gallon from a peak of more than \$4.55 (according to AAA). Lower gas prices are welcome news for consumers as we approach the important back-to-school shopping season, which starts after the July 4 weekend.
- The Misery Index, which is the Consumer Price Index (CPI) inflation rate plus the unemployment rate is below the average of 9.2% since 1949 but it rose to 8.5% in May from 6.9% in January. The May unemployment rate is low at 4.3% but the CPI rose to 4.2% in May from 2.4% in January.
- We are monitoring financial conditions and high-frequency indicators. They show ongoing economic resilience and financial system stability.
- Argus expects S&P 500 EPS to rise almost 25% to \$340 in 2026 and increase about 15% to \$390 in 2027. EPS is helped by an increase in operating margins to about 18.8% this year, well above 13.9% in pre-pandemic 2019. Growing tech giants such as MSFT and NVDA have operating margins of 47% and 64% respectively while Dow stalwarts Walmart and Caterpillar earn 4% and 17%, respectively.
- Argus Fixed Income Strategist Kevin Heal expects the Fed to maintain the funds target at 3.50% to 3.75% in 2026 and reduce the target by 25 basis points in 2027 as inflation is likely to abate. We expect the dollar to be slightly stronger in 2026 driven by foreign demand for shares of innovative U.S. companies and continuing economic growth.
- Gold is likely to remain at elevated levels amid global uncertainty. The safe-haven asset recently topped \$5,000 an ounce. With seeming progress in winding down the Iran war, gold has declined.
- What could go right? Low unemployment, spending by wealthy consumers, strong S&P earnings, capital investment in Artificial Intelligence, productivity gains, slower inflation if the price of oil has peaked, a small economic boost from the World Cup, and ongoing innovation.
- Risks: Strains on affordability from years of elevated inflation, uncertainty related to the interim peace deal with Iran, a lower 10-year Treasury yield could depend on deficit reduction, a weak housing market, low income consumers are struggling, spending by affluent may depend on stock gains.

CURRENT ECONOMIC RELEASES

Current Economic Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
18-Jun	Leading Index	May	0.2%	0.3%	NA	0.1%
24-Jun	New Home Sales	May	626K	665K	640K	580K
25-Jun	GDP Annualized QoQ	1Q "Final"	1.6%	1.6%	1.6%	NA
	GDP Price Index	1Q "Final"	3.5%	3.5%	3.5%	NA
	PCE Deflator	May	3.8%	4.0%	4.1%	NA
	PCE Core Deflator	May	3.3%	3.3%	3.4%	NA
	Personal Income	May	2.5%	2.2%	NA	NA
	Personal Spending	May	5.9%	5.9%	NA	NA
	Durable Goods Orders	May	19.2%	-4.8%	NA	NA
	30-Jun	Consumer Confidence	June	93.1	94.5	NA
1-Jul	ISM Manufacturing	June	54.0	54.4	NA	NA
	ISM New Orders	June	56.8	56.2	NA	NA
	Construction Spending	May	0.9%	1.5%	NA	NA
2-Jul	Nonfarm Payrolls	June	172K	125K	NA	NA
	Unemployment Rate	June	4.3%	4.3%	NA	NA
	Average Weekly Hours	June	34.3	34.3	NA	NA
	Average Hourly Earnings	June	3.4%	3.4%	NA	NA
	Factory Orders	May	11.7%	2.5%	NA	NA

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