NATIXIS INVESTMENT MANAGERS | SOLUTIONS

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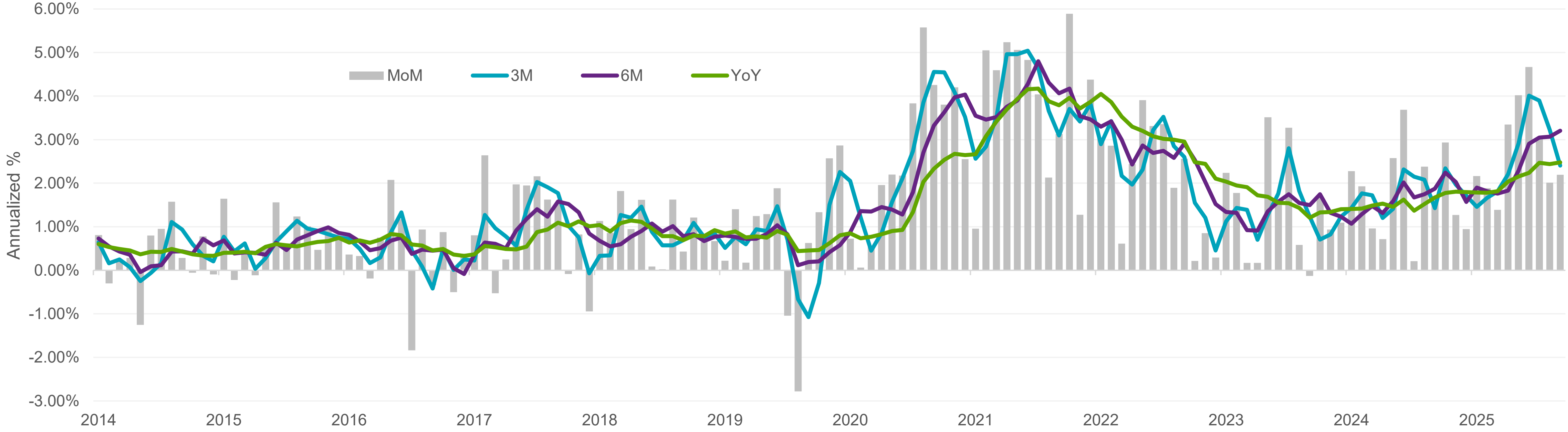
Charts and Smarts®

Jack Janasiewicz, CFA®
Multi-Asset Portfolio Manager and Lead Portfolio Strategist

Garrett Melson, CFA®
Portfolio Strategist

Up Around the Bend

Market-based core PCE less shelter (9/30/14–5/31/26)

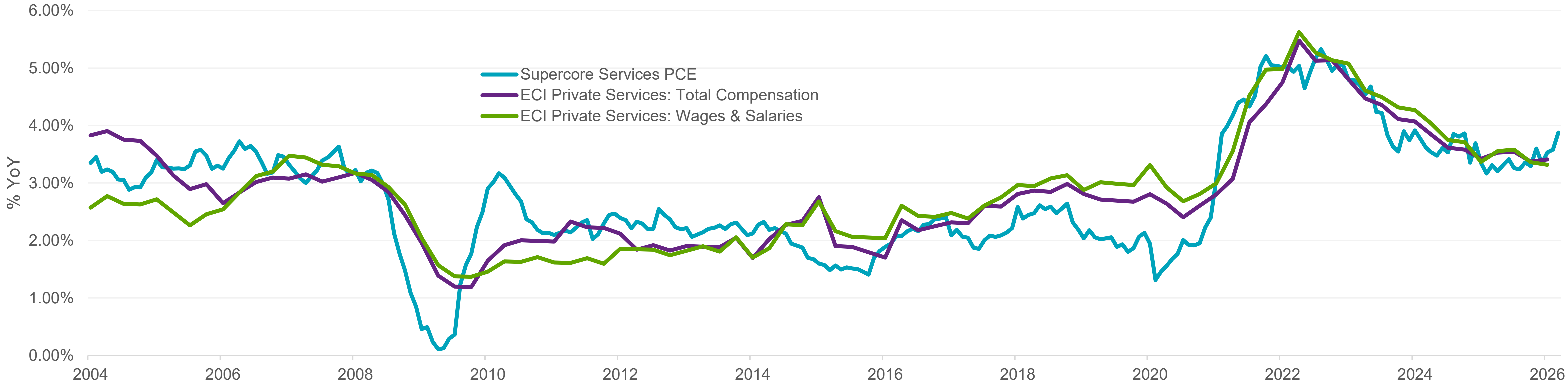


The hawks are back in town and they're now fully in control of the FOMC. While much of the inflation focus has been centered squarely on the surge in headline inflation on the back of the energy price shock, the true fly in the ointment has been the firming and stickiness in core prices that saw core PCE less shelter rise at a 4.2% annualized clip over the six months ending in May. The inflation backdrop has undoubtedly taken a turn in the wrong direction, but under the surface, there's evidence to suggest that the data hasn't deteriorated to the degree the narrative surrounding it has. The Fed focuses on core PCE to strip out volatile components that can mask the underlying trends within inflation. But empirically market-based core PCE, which excludes imputed prices, such as financial services, and focuses exclusively on measured prices, has been a more reliable indicator of underlying inflation. To that end, while market-based core PCE has indeed firmed as well, rising 3.2% annualized over the past six months, the trends have been more encouraging as monthly prints have settled back into a 2% annualized pace after the four-month surge around the start of the year. Put that together with the pipeline of shelter disinflation reasserting itself as the shutdown distortions fade and tariff effects continuing to roll off from core goods prints and the window is wide open for improving inflation trends to once again take hold just as the hawks seemed to have hikes within their grasp. While it will take a few months worth of good news for the doves to wrest control back from an increasingly hawkish committee, the path to an extended pause appears to be widening.

Source: Portfolio Analysis & Consulting; Bloomberg. Core PCE is personal consumption expenditures price index less food and energy. FOMC is the Federal Open Market Committee.

Bad Moon Rising

Supercore services inflation vs. services labor costs (3/31/04–5/31/26)

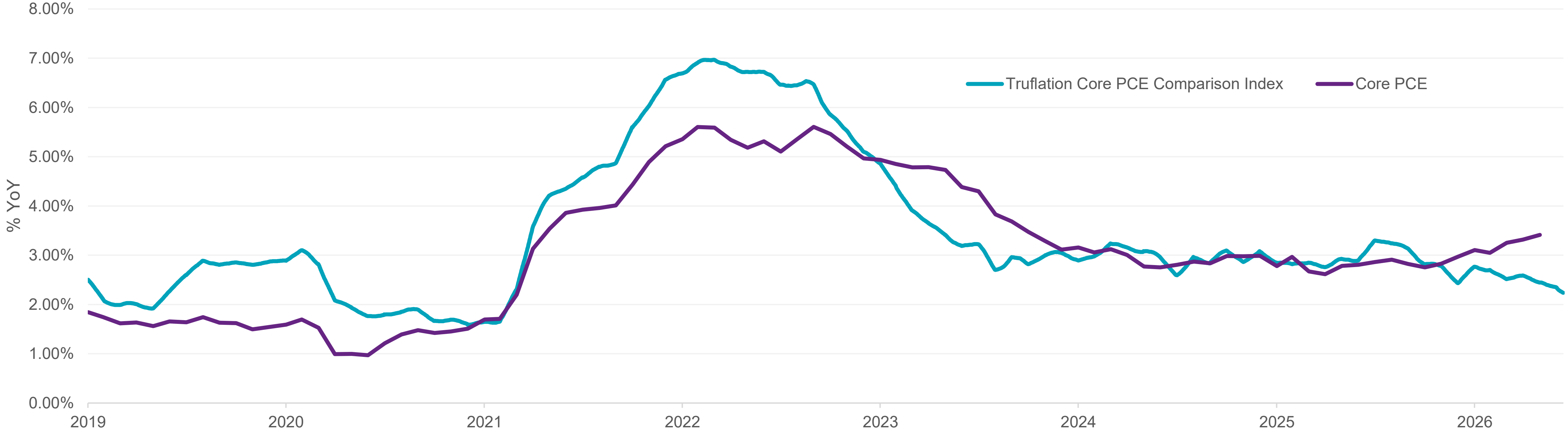


For the hawks on the FOMC, the issue has never really been about oil prices, but rather the reacceleration in supercore services. Throughout the disinflationary process, supercore services has been the most frustratingly sticky component, falling from meaningfully from the 2022 highs, but settling into a range still well above the pre-pandemic pace. While the softening in shelter has been able to offset some of the supercore services stickiness, the reacceleration since late 2025 has been concerning for the hawks. Nonhousing core services prices tend to be largely a function of labor market conditions and, as such, track closely with broad measures of wage growth, such as the Fed's preferred gauge, the Employment Cost Index (ECI). As we've highlighted all year, despite the optimism around the labor market reacceleration, nearly every measure of wage growth has continued to cool. The key question to ask is which way the causality runs. Historically, it has been wage growth that has tended to follow prices, and not wages leading to demand, driven inflation. And to that end, it seems unlikely the recent divergence will persist. With the labor market remaining on soft, albeit stable footing, and the balance of power firmly in the hands of employers, it's hard to see how wage growth accelerates materially from here, which would portend a compression in real wages stemming from supercore services ultimately limiting further upside in supercore service prices. And with nearly half of the contribution to the uptick in supercore services over the past six months driven by healthcare and financial services, it's worth asking whether tighter monetary policy is the correct tool to combat the increase in these acyclical and imputed prices. With the labor market providing little in the way of an inflationary impulse, it seems more likely that supercore services converge back down toward the softening trends in wage growth in the coming months, thereby removing the strongest pillar of support for the hawkish bias.

Source: Portfolio Analysis & Consulting; Bloomberg. Supercore Services PCE is services personal consumption expenditures price index less food, energy, and housing. ECI is employment cost index.

Lookin' Out My Back Door

Truflation vs core PCE (1/31/19–7/13/26)

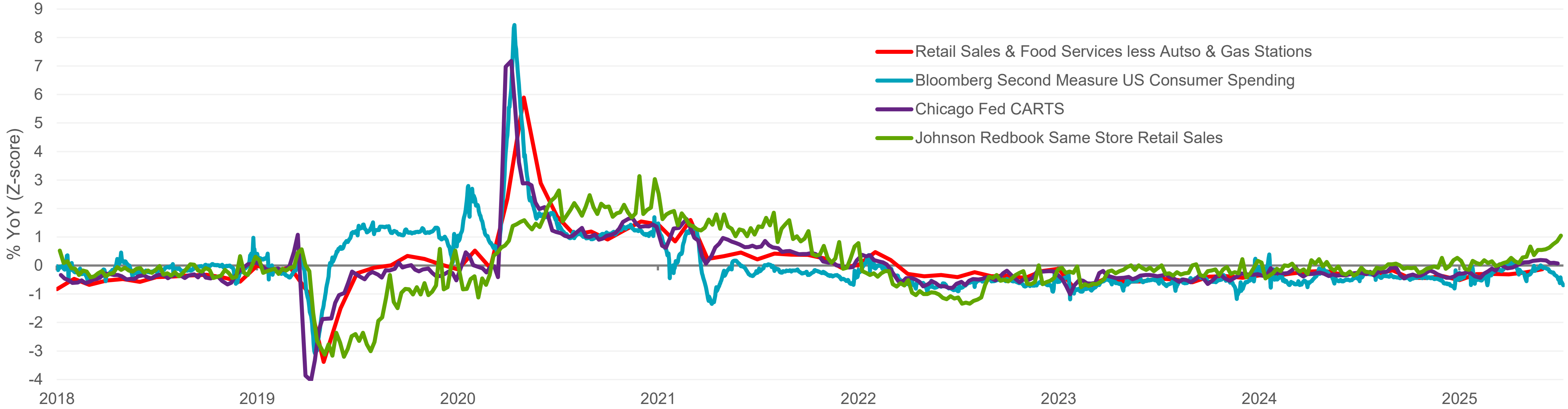


While oil prices have indeed perked up on the collapse of the memorandum of understanding, as we've laid out, the real debate around the inflation outlook revolves around the trends within core prices. Stickier oil prices may eventually bleed further into core prices, but under the surface, real-time price measures continue to move in the right direction as the disinflationary process continues. Truflation aggregates the prices of over 15 million goods and services to provide a real-time look at price trends throughout the economy. While the index has been maligned in recent years as the year-over-year-rate has tended to print much lower than official statistics, the utility isn't in the level but rather the direction of travel. Over the pandemic era, Truflation has been a remarkably reliable and consistent indicator to identify the trend and turning points in price pressures ahead of the official measures. The recent message from the Truflation data is clear: After stabilizing for much of the past two years, core prices as measured by their Core PCE Comparison Index appear to be drifting lower once more. Indeed, the hawks retain control of the FOMC for the moment as even views from the doves have evolved in a materially more hawkish direction, but that hawkishness appears to be growing ever more divorced from underlying inflation trends. Akin to what we've seen on numerous occasions over the past few years, the consensus and the Fed appear to have turned most hawkish at exactly the point that the underlying inflation impulse appears to be rolling over. Should that disinflationary impulse reassert itself in official statistics over the coming months, we have very likely passed peak hawkishness, and markets will be forced to walk back expectations for further tightening.

Source: Portfolio Analysis & Consulting; Bloomberg. Core PCE is personal consumption expenditures price index less food and energy.

Down on the Corner

Retail sales vs. consumer spending indicators (12/31/18–7/8/26)

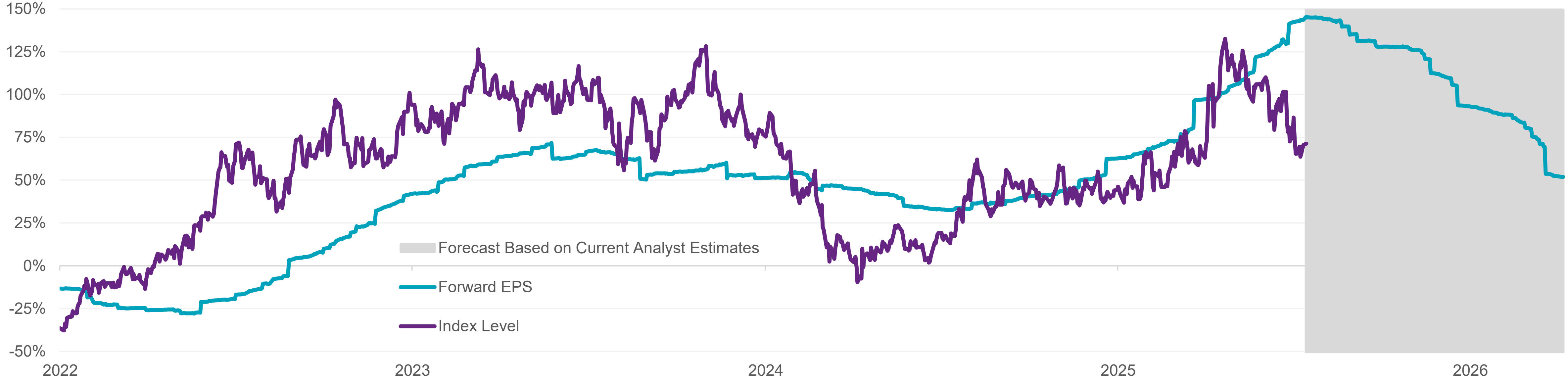


For all the optimism around a resurgence in consumption on the back of a meaningful fiscal boost it's certainly been a disappointing first half of the year. Real consumption has grown just 1.3% over the first five months of 2026 as the energy shock offset any lift from tax cuts and real consumption cooled on the back of firming inflation and softening wage growth. But as oil and gas prices have fallen well off their highs, optimism is high around a recovery in consumption as the real income squeeze fades. As is tradition in the economics field there are a multitude of indicators constructed to measure trends within consumption. And while these indicators tend to move in fairly coordinated fashion, a notable divergence has emerged over the past few months amongst a number of the top consumption indicators. It's plain to see that one of these is not like the others. While the Johnson Redbook Same - Store Retail Sales Index has been powering to levels last seen in 2022, the Bloomberg Second Measure US Consumer Spending Index and Chicago Fed Advanced Retail Trade Summary, or CARTS model, both of which have tended to track actual retail sales more closely thanks to their reliance on credit and debit card transaction data as opposed to merchant-reported estimates from brick-and-mortar stores, have been much more muted and weakening of late. With consumers relying on tapping savings through the energy price shock to smooth out consumption, it seems more likely that the decline in energy prices will be pocketed to refill savings buffers than to fuel a renewed jump in consumption. Indeed, should we see continued cooling in inflation in the coming months, real consumption should benefit from the disinflationary impulse. But with labor market conditions remaining soft and wage growth continuing to cool, consumption looks set to remain somewhat soft in the coming months.

Source: Portfolio Analysis & Consulting; Bloomberg. The Chicago Fed Advance Retail Trade Summary (CARTS) tracks the U.S. Census Bureau's Monthly Retail Trade Survey on a weekly basis providing an early snapshot of national retail spending.

Who'll Stop the Rain

S&P 1500® semiconductors and semiconductor equipment (12/30/22–4/5/27E)



As we enter the second - quarter confessionals, all eyes will be on semiconductors and the broader AI complex as the technical unwind of the crowded momentum trade has taken the wind out of the sails of the year-to-date leaders. While we continue to view this unwind as more technical in nature, with renewed AI skepticism serving as a simple and appealing narrative to backfill the price action, the earnings outlook certainly appears to fit in nicely with that narrative. Earnings estimates have surged across the market this year, with the largest gains predictably located within semiconductor and memory names, which have seen forward earnings estimates explode higher by over 70% since the start of the year. Yet despite the fundamental support for the trade, year-over-year performance for the semis space has been compressing over the past few months. Indeed, part of this slowdown is simply the result of rolling off performance from the post-Liberation Day lows last year. But for an industry that has historically been highly cyclical, it's beginning to feel like the market is front-running an anticipated peak in earnings, a peak that is currently reflected in the forward quarterly earnings estimates. While investors are understandably on edge for a potential cyclical peak, particularly as fears of the market forcing the hyperscalers to find religion with respect to their capital expenditures are running rampant, the risk to current pricing and the growing consensus are that this cycle has much further to run as compute looks likely to remain acutely constrained well into the future. If that's the case, we may not be on the precipice of a cyclical peak, but rather a moderation in the growth rate that stabilizes at a much higher plateau than currently discounted. With semiconductors reaching oversold levels as the momentum unwind has taken its toll, we could be primed for a meaningful bounce in both price and forward earnings estimates, particularly if the current and coming earnings season confirm the durability of this cycle.

Source: Portfolio Analysis & Consulting; FactSet. As of 7/13/26. Forward EPS is consensus estimate for earnings per share over the next 12 months.

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Natixis Advisors, LLC are located at 888 Boylston Street, Suite 800, Boston, MA 02199-8197. 800-862-4863. im.natixis.com.

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