Commerce Trust
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Look at the Markets

An in-depth analysis of U.S. and world markets focused on complexities, risks, and trends shaping the economic landscape

FIRST QUARTER 2026

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FROM THE CHIEF INVESTMENT OFFICER

Commerce Bank kicked off 2026 by completing a merger with FineMark Bank and Trust, a division of Commerce Bank, a bank and wealth management firm with offices in Florida, South Carolina, and Arizona. We are excited for an experienced and well-rounded team of investment professionals to join us.

In 2025, equity markets delivered a third consecutive year of double-digit returns with technology stocks still in the lead. International equities not only provided diversification for stock portfolios but also outperformed their domestic peers as the declining value of the dollar lifted returns. Fixed income portfolios produced strong returns buoyed by three Federal Reserve (Fed) rate cuts in the second half of 2025.

Looking into 2026, the economic environment is presenting challenges for businesses and consumers, but both are adapting. In the near term, we anticipate that the One Big Beautiful Bill Act (OBBBA) will provide stimulus to consumers through tax changes and to businesses through accelerated depreciation. The stimulus builds on an already-resilient economy that is weathering tariffs, a weakening job market, and a shifting regulatory environment.

Our focus remains on the labor market. A lack of immigration, technology impacts, and Department of Government Efficiency (DOGE) reductions to the federal workforce are all contributing to volatility.

Equities have been trading above historical valuations for some time. However, earnings over the course of 2025 still exceeded expectations as artificial intelligence (AI) investment powered growth. AI is slated to continue to receive massive investment as businesses embrace the technology.

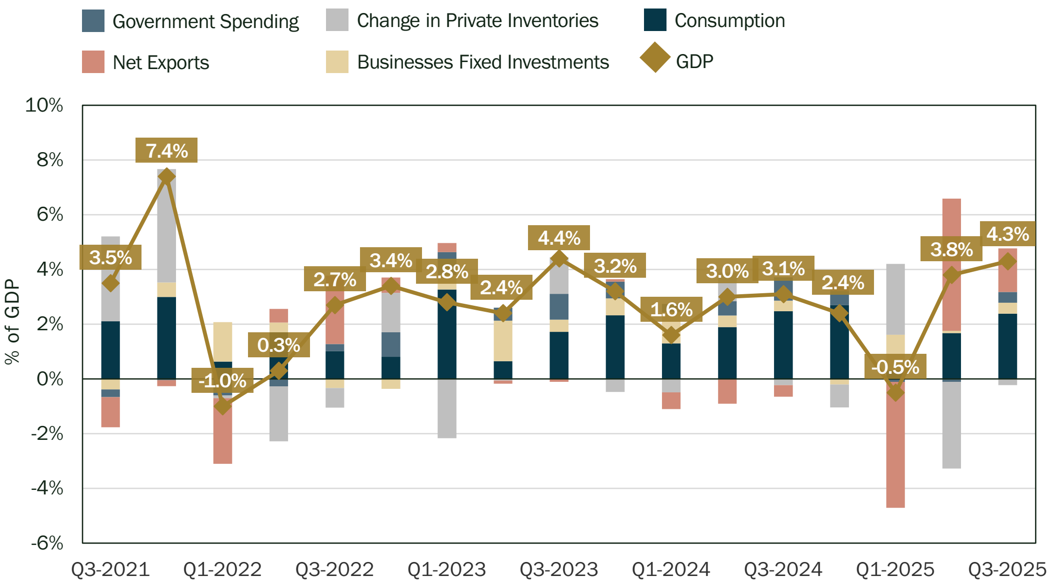
We remain diligent in exploring opportunities and evaluating risks inside financial markets and have portfolios positioned with a balanced, neutral posture.

I encourage you to explore this edition of Look at the Markets and thank you for your continued confidence in Commerce Trust.

DAVID HAGEE
Chief Investment Officer
Commerce Trust

Gross Domestic Product (GDP)

Consumption contributes to real GDP as consumers acclimate to tariffs



Source: Bureau of Economic Analysis, Commerce Trust.

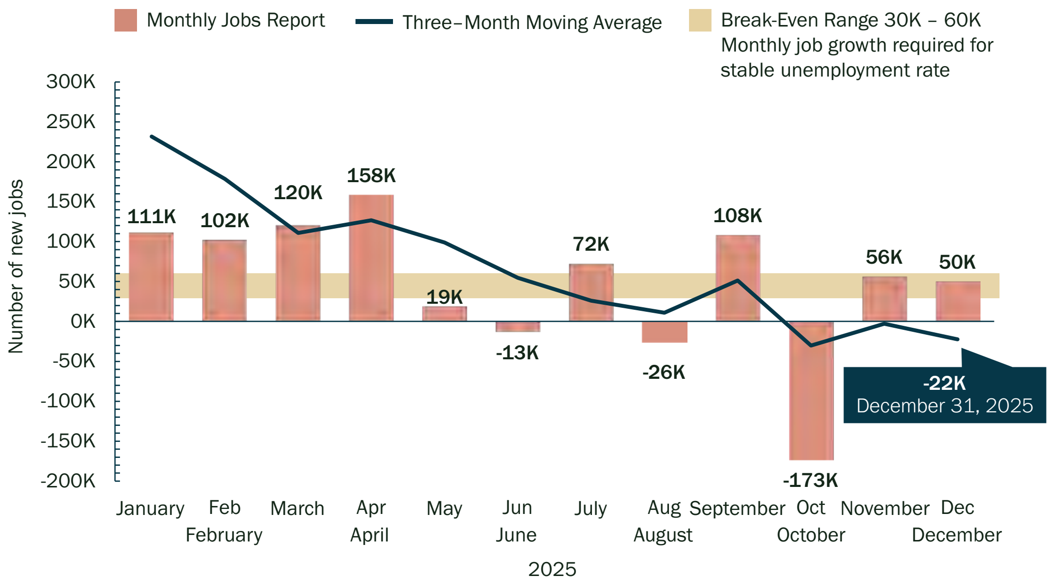
While data has remained backlogged from the government shutdown, we estimate the U.S. economy expanded around 2% in 2025 amid significant volatility, including a contraction in the first quarter driven by businesses ramping up imports ahead of the April 2, 2025 Liberation Day announcement.

Consumption drove gross domestic product (GDP) in the third quarter, as consumers acclimated to the administration's tariffs and trade policy. We continue to see muted impacts from tariffs as businesses appear to have largely adapted to the new environment.

We project full-year 2025 growth near 2%, with 2026 continuing at a similar pace. The first half of the year should benefit from stimulus measures in the OBBBA, including higher tax refunds and accelerated depreciation rules for businesses.

Average Monthly Job Growth with Three–Month Moving Average

Hiring slows, dipping into break-even range



Source: Bureau of Labor Statistics.

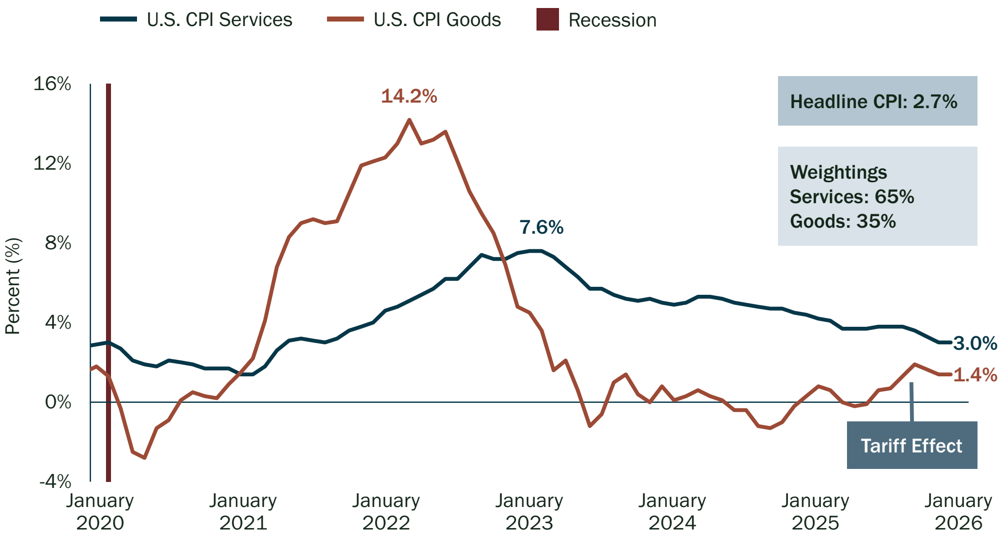
Employment remains a critical focus for markets and the Fed. After several years of robust job growth, hiring in the U.S. is cooling significantly. Historically, sustained job losses often signal the onset of a recession.

The jobs picture has become clouded with the DOGE reductions and lack of immigration. Given the constrained supply of job seekers, the unemployment rate has held steady. However if monthly job gains consistently remain below 30,000, the odds of a recession historically increase.

The employment situation has become the primary focus for the Fed as it weighs its dual mandate of full employment and stable inflation. While tariff-driven inflation has been relatively subdued, the marked slowdown in job growth was the catalyst for the three recent Fed interest rate cuts. In 2026, we continue to see jobs as the focus of policymakers, with markets pricing in two additional rate cuts by year-end.

U.S. Consumer Price Index (CPI) Goods versus Services

Inflation is slowing and tariff impacts are muted



Source: Bureau of Labor Statistics; Bloomberg.

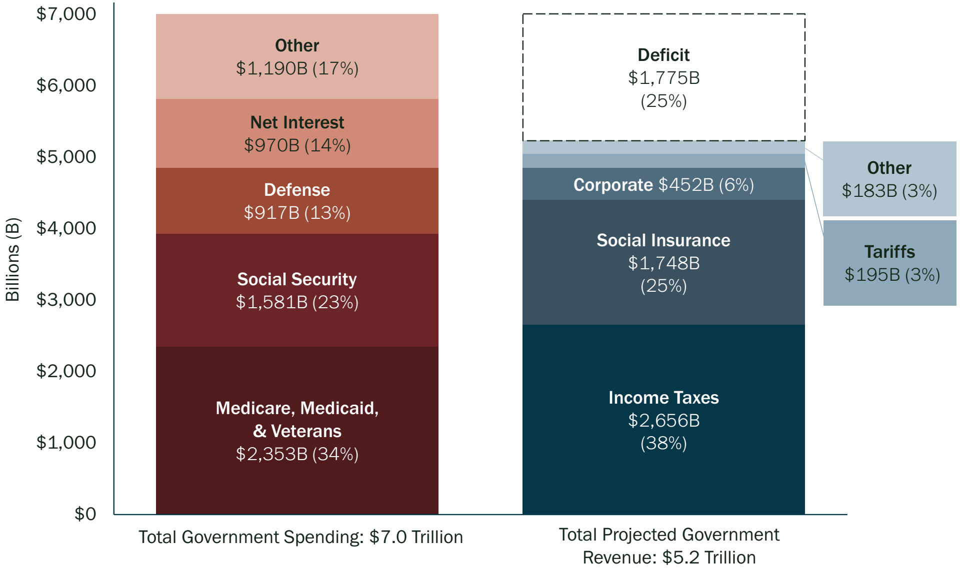
The CPI is one of the primary measures of U.S. inflation. The two components for the CPI are goods and services, with services accounting for roughly two-thirds and goods the remaining one-third. Price movements in goods tend to be much more volatile.

Inflation has been a central focus since 2022, when COVID-era stimulus drove the CPI to a peak of 9.1% in June 2022. While inflation has come down, tariff-driven goods inflation has given policymakers and market participants some concern. So far tariff implementation has been uneven, yet effective tariff rates across all imports now exceed 10%. Nonetheless, the overall impact on the CPI has been muted.

The lack of an inflation boost from tariffs afforded the Fed room to cut interest rates three times in 2025. Currently, markets are anticipating two additional rate cuts in 2026. Lower short-term rates are generally positive for fixed income and equity returns.

2025 U.S. Budget Deficit at 5.9% of Gross Domestic Product (GDP)

Tax revenues rising, but the deficit still exceeds GDP growth rate



Source: JP Morgan; Congressional Budget Office.

The budgetary position and cumulative deficit are key measures of the U.S. economy's fiscal health. While politicians talk of balanced budgets, to achieve this would require both materially higher tax revenues and reduced entitlement spending.

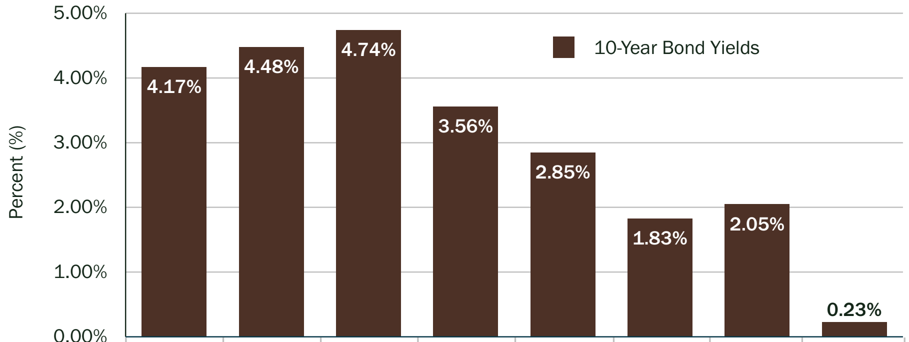
Tax revenues in fiscal year 2025 rose faster than the increase in government spending, reducing the deficit as a share of GDP on a year-over-year basis.

Last year's budget deficit of 5.9% of GDP still exceeded the country's nominal GDP growth rate of 4.5%, pushing the total deficit relative to the size of the economy to a record level.

While tariffs are being adjudicated, we expect the OBBBA to accelerate growth, helping to offset the impact of lower marginal tax rates and expanded business incentives. Even so, the 2026 deficit is projected to outpace nominal growth, adding further to the nation's fiscal imbalance.

Global 10-Year Bond Yields

U.S. Treasury yields comparatively high for the developed world



	United States	United Kingdom	Australia	France	Germany	China	Japan	Switzerland
Central Bank Overnight Rate (%)	3.75%	3.75%	3.60%	2.15%	2.15%	1.40%	0.75%	0.00%
Inflation (Y-O-Y)	2.7%	3.2%	3.4%	0.8%	1.8%	0.7%	2.9%	0.1%
Real GDP Growth (Y-O-Y)	2.3%	1.3%	2.1%	0.9%	0.3%	4.8%	0.6%	0.5%
Budget Deficit/Surplus (% of GDP)	-5.3%	-5.3%	-2.5%	-5.8%	-2.7%	-4.8%	-0.7%	-0.1%
Credit Ratings (Moody's/S&P)	Aa1/AA+	Aa3/AA	Aaa/AAA	Aa3/A+	Aaa/AAA	A1/A+	A1/A+	Aaa/AAA

Source: Bloomberg, as of 12/31/25.

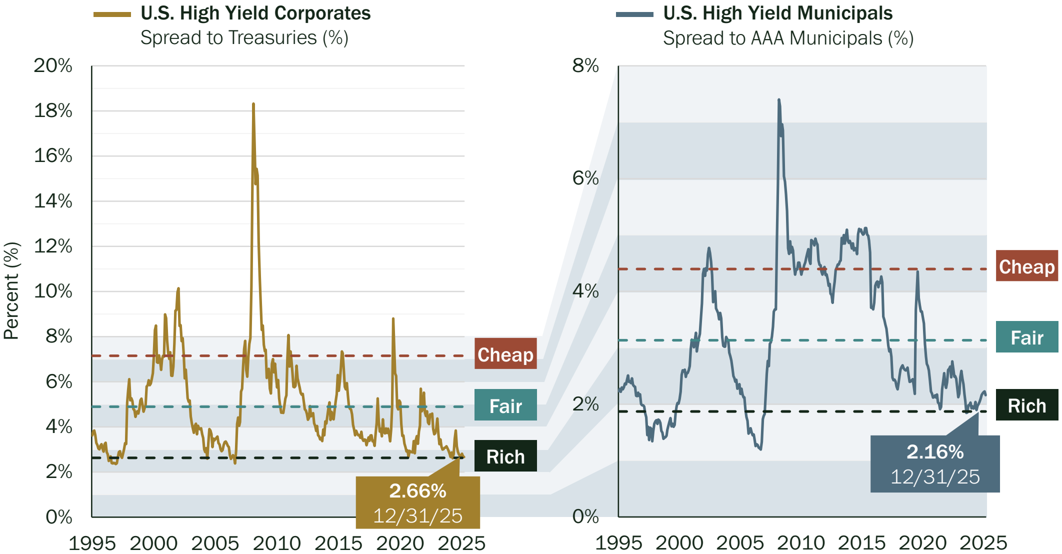
Despite drifting lower over much of 2025, U.S. Treasury yields remain relatively high compared to other major sovereign bonds. A combination of market, macroeconomic, and fiscal factors account for the attractive Treasury yields available to global bond investors.

Generally, the higher a country's central bank overnight rate, inflation, GDP growth, and fiscal deficit, the higher the yield investors will demand from longer-term bonds to compensate for interest rate risk, purchasing power erosion, and fiscal uncertainty. Conversely, stronger credit ratings tend to translate into lower borrowing rates, reflecting lower perceived default risk and greater fiscal discipline.

Fiscal dynamics play a key role. Although the U.S. is the world's largest economy and maintains a strong credit rating, the U.S. also has one of the deepest fiscal deficits at over 5% of GDP. Treasury yields reflect investor concerns over rising interest costs and long-term fiscal sustainability. At the other end of the spectrum, Switzerland remains a global safe haven with a 10- year bond yield of nearly zero.

High Yield Credit Spreads

Historically low reward for taking on higher risk



"Fair" represents the average spread over the time period, with "Cheap" and "Rich" representing +1/-1 standard deviations.

Source: Bloomberg, Commerce Trust. Benchmarks for above spreads: Bloomberg US Corporate High Yield Bond Index, Bloomberg Municipal Bond: High Yield vs. Bloomberg Municipal AAA Index.

Spreads are the extra yield investors earn over a benchmark bond of similar maturity. In U.S. taxable bond markets, Treasury bonds typically serve as the benchmark. In the U.S. tax-exempt bond market, AAA rated municipal bonds serve that role.

High yield corporate bonds have been in high demand in recent years, pushing spreads to levels we would consider overvalued or rich. High yield corporates are also much more volatile than their investment grade counterparts, exhibiting strong correlations with stock market returns on a relative basis.

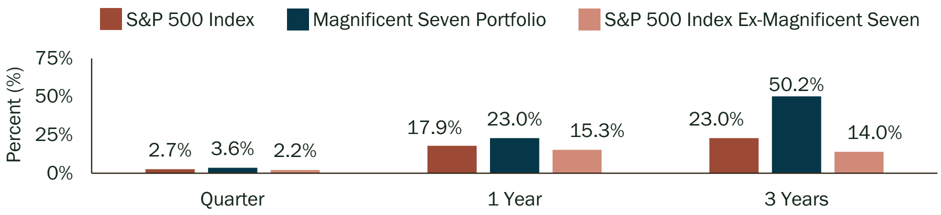
High yield municipal bonds have also been in favor as the tailwinds of a growing economy and heavy fiscal stimulus have been constructive for municipal creditworthiness. As with corporate credits on the taxable side, high yield municipal credit spreads have ratcheted steadily tighter to rich levels.

Given these valuations at this point in the economic cycle, we would caution against reaching too far down the credit spectrum in a search for yield among lower-grade bonds. We favor limited exposure to these lower-rated securities.

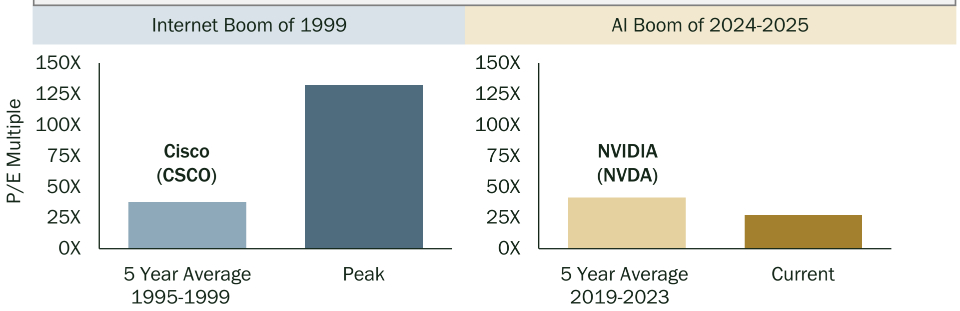
Artificial Intelligence (AI) and Technology Lead with Strong Earnings

AI boom not a replay of the internet boom

S&P 500 Index Annualized Returns



Price to Earnings Growth Comparison



Source: FactSet (SPX Annualized Returns, through 12/31/2025); Coatue, Bloomberg (Price to Earnings Growth Comparison), Cisco peak March 2000, Nvidia current through 10/31/2025.

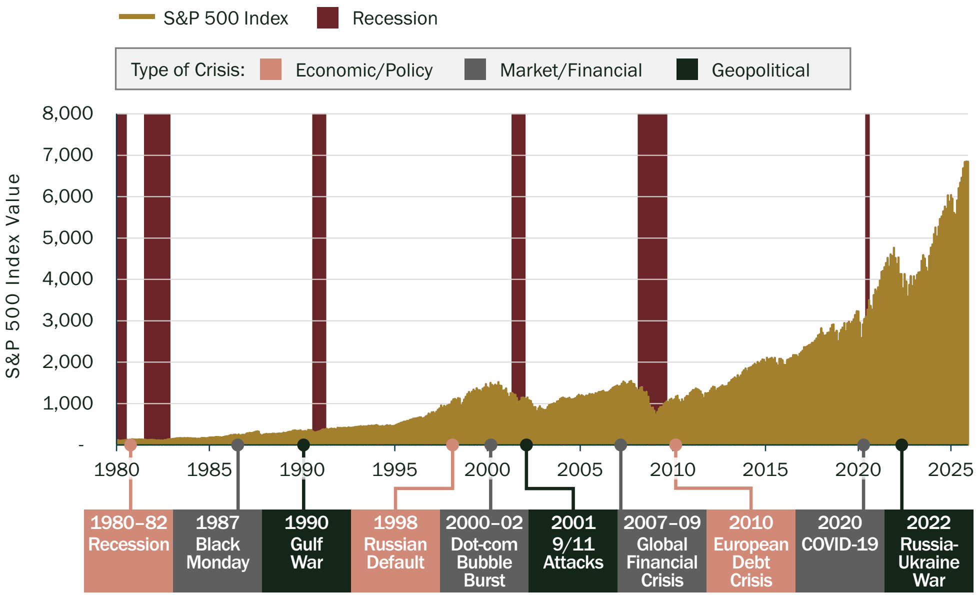
Comparing recent market leadership and valuation dynamics highlights the return dispersion between the S&P 500, the Magnificent Seven, and the broader market. A historical valuation comparison between Cisco during the internet boom and NVIDIA today shows a different story for the AI boom.

The AI boom is often viewed as a replay of the 1990's tech bubble. While both periods feature transformative innovation and heightened investor interest, today's AI leaders are generating meaningful revenues, exhibit broad enterprise adoption, and deliver measurable earnings growth. Valuations, particularly when compared with historical extremes, remain more disciplined.

While AI leadership concentration and return dispersion warrant attention, the current AI cycle is supported by stronger fundamentals than the dot-com era. Selectivity remains critical, but reasonable valuations and earnings growth point to a market driven more by actual monetization than speculation.

Impact of Geopolitical Influence on the S&P 500 Index

Equity market resilience during geopolitical uncertainty



Source: Federal Reserve Bank of St. Louis (FRED), Commerce Trust.

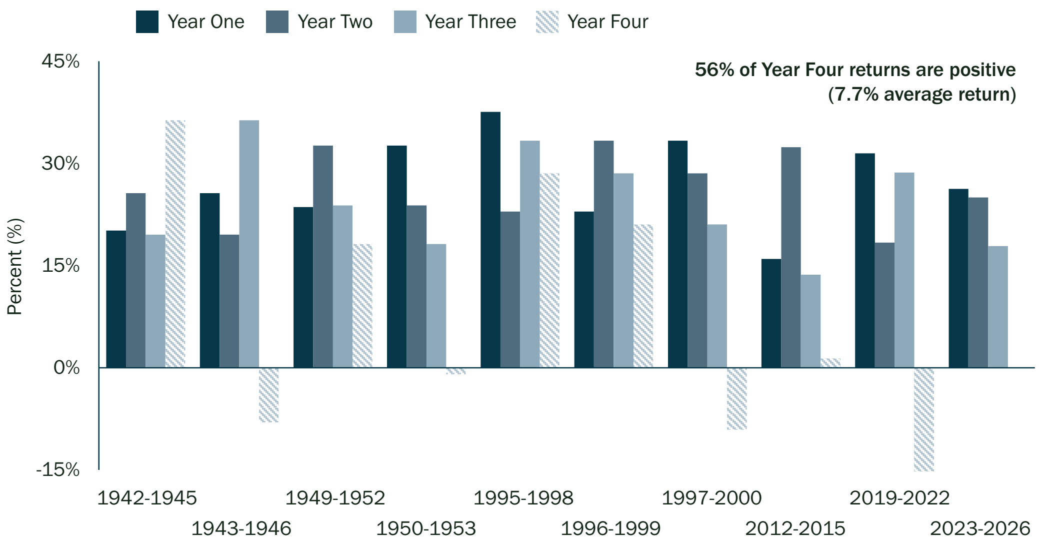
Geopolitical tensions often trigger short-term volatility in the financial markets. However, history tells us that markets are resilient and eventually post solid gains even as conflicts remain. Consistent with history, while geopolitical events have increased over the last several years, their influence over the global, and specifically the U.S., economy remains muted. The markets have looked past current events.

The Russia-Ukraine war is approaching year four and the Israel-Hamas conflict has been going on for over two years. Nevertheless, markets remained focused on the fundamentals supporting securities, especially earnings growth. Analyst's corporate earnings growth estimates for 2026 are currently in the 12 to 14% range.

While tensions remain elevated, we view the U.S. equity market as strong, well-capitalized, and resilient. We continue to favor a neutrally positioned portfolio, with balance between stocks, bonds, cash, and alternatives.

Three Consecutive Years of 10+% Returns for the S&P 500 Index

A fourth year of positive returns expected for 2026



Source: Bloomberg.

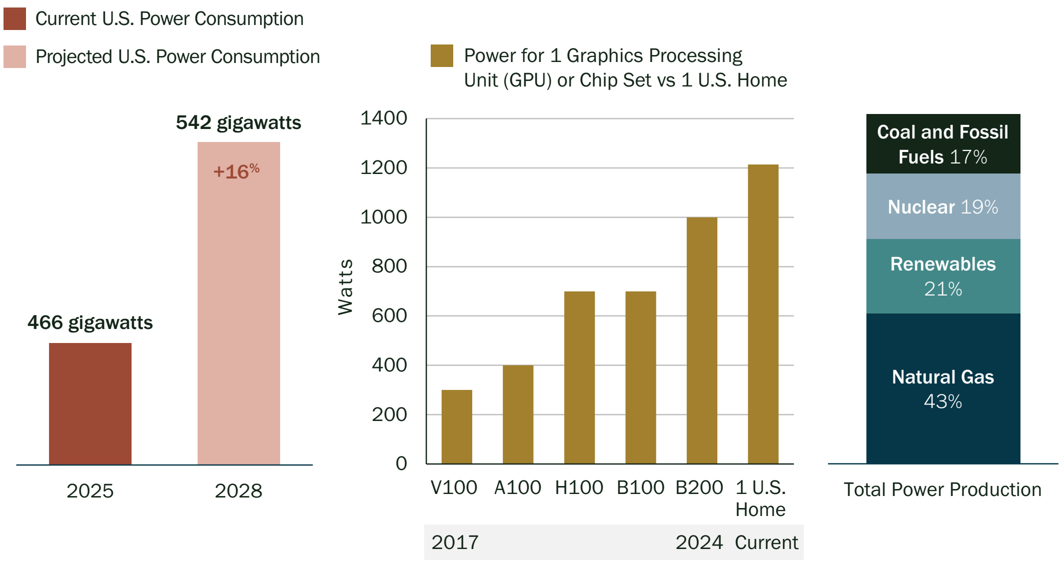
As we enter 2026, the S&P 500 delivered three consecutive years of double-digit returns. Since 1945, there have been nine previous periods where the market posted three consecutive years of returns at this level.

In the fourth year following these three-year periods, returns were positive in five of those nine instances, with an average gain of 7.7%. This is below long-term averages, but not necessarily concerning unless accompanied by a recession.

We expect 2026 to produce another year of positive returns, supported by S&P 500 earnings growth of 12 to 14%, stimulus from OBBBA, lower interest rates, and accelerating GDP growth.

U.S. Projected Power Consumption Supporting AI

Data center buildouts require substantial energy to meet expected AI needs



Source: Source: NVDA, U.S. Energy Information Administration.

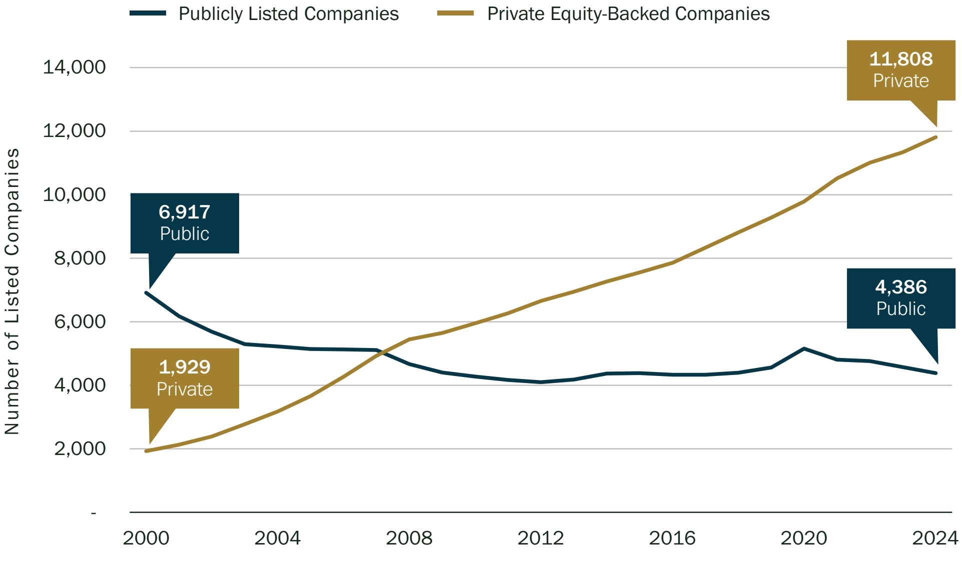
Average U.S. daily power consumption is expected to rise by 76 gigawatts (GW), or 16% for the scheduled buildout of the data centers needed to power AI technology.

The current U.S. power system can produce enough power to cover peak daily usage. Typically, peak usage can reach 760 GW on a hot day in July. Peak grid capacity would need to grow by about 10% to accommodate the additional AI data centers.

In comparison, a large coal plant or nuclear power plant produces about 1 GW per day. Adding an additional 76 GW capacity to the system will require massive infrastructure investment across the U.S.

The Shifting Equity Landscape

Publicly listed companies versus private equity-backed companies



Source: PitchBook.

The composition of the equity universe has shifted over the past two-and-a-half decades. Since 2000, the number of publicly listed companies has steadily declined, while private equity-baked companies have continued to grow. Equity creation has increasingly migrated outside of public markets.

Companies are staying private longer, accessing capital through private channels rather than public listings, and reaching greater scale before any potential IPO. As a result, a growing share of innovation, growth, and value creation now occurs in private markets rather than in a shrinking public equity universe.

While private equity is not suitable for all investors and requires meeting certain qualifications, it can offer eligible long-term investors access to differentiated return potential and distinct risk and volatility characteristics, making it a meaningful component of a diversified portfolio. For those investors, limiting equity exposure to public markets alone risks overlooking a significant and expanding segment of opportunity.

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