
INVESTMENT OUTLOOK

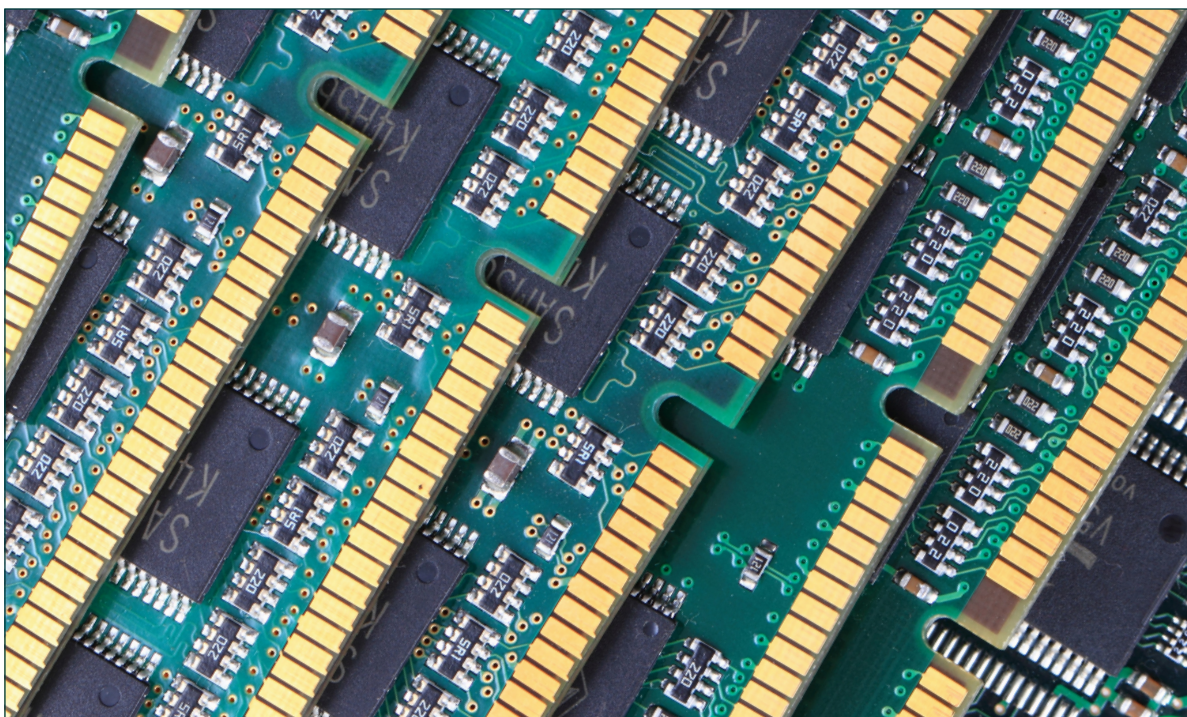
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SECOND QUARTER 2026 INVESTMENT OUTLOOK: CHIPS AHOY!

Thanks for the memory.

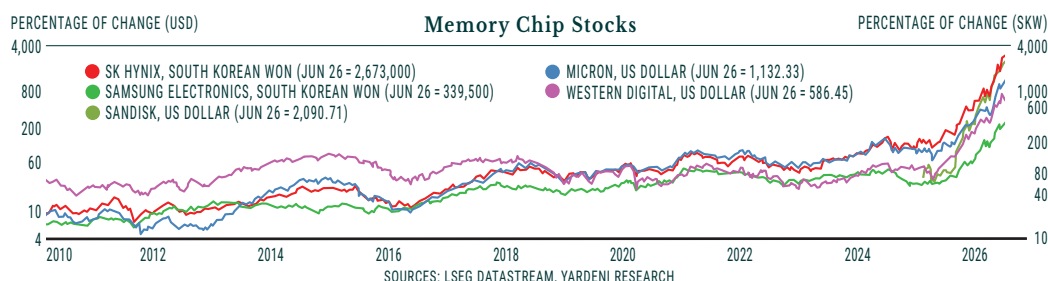
–Bob Hope

Semiconductor memory chips were first developed in the 1960s. They revolutionized computing by transitioning it from bulky vacuum tubes and magnetic-core memory to lightning-fast, microscopic solid-state silicon circuits. Computing, of course, has traveled a long distance since then, and for many years memory chips were viewed as commodity products—cheap, standardized, and interchangeable. They are durable—a high-quality memory card can last five to ten years under normal conditions—and are widely used in a variety of devices such as smartphones, USB drives, and solid-state drives. Their ability to retain data without a power supply is a key feature supporting broad adoption.

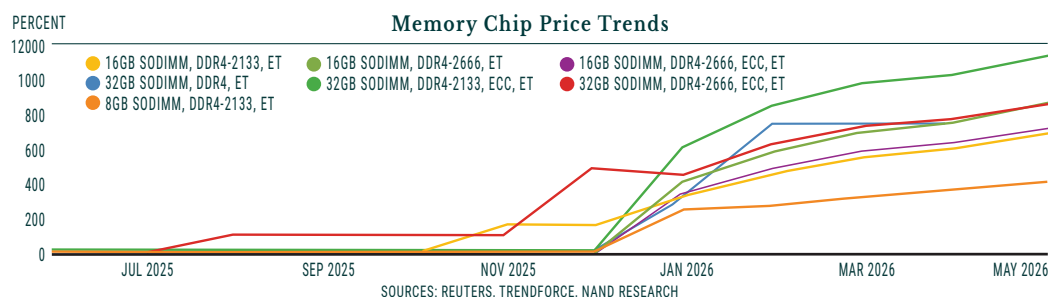


Today, memory chips are crucial components for temporary fast data-processing, for permanent data storage, and for increasing capacity without increasing the physical size of the chip. The explosive growth of generative artificial intelligence (AI) services has triggered unprecedented demand for specialized memory chips, especially High Bandwidth Memory used in AI accelerators and data center GPUs (graphics processing units).

As a result of skyrocketing demand for memory chips and the extended timeframe required to build new chip fabrication plants to increase supply, prices for these chips have risen enormously. And, with higher prices, the leading memory chip suppliers have seen their stock prices soar. Since March 31st only, the top memory chip producers—Micron Technology, SK Hynix, and Samsung Electronics—have seen their stocks appreciate 242%, 226%, and 99%, driven by remarkably robust fundamentals. Other memory chip makers also notched dramatic gains.



Driving those fundamentals? Lofty price increases producers can charge, given surging demand and an inability to lift production in the short term—as the chart below of selective memory chip price increases shows.



There is another chip story whose origins also date back to the early 1960s, when the American snack food company Nabisco introduced Chips Ahoy!, a chocolate chip cookie brand. The name, of course, is a wordplay on 'ship ahoy'—a traditional nautical greeting or lookout cry used to spot and call out to another ship in the distance. Chips Ahoy! is the third best-selling cookie in America, and promises chocolate chips are baked into every bite.

The cookie is one of Mondelez International's fastest-growing brands and dominates the US chocolate chip cookie market with over a 50% share. Recently, it has added over 2 million households to its customer base.

Of course, in our brave new GLP-1 world, growth in chocolate chips pales in comparison to memory chips. In the past year, the cookies posted a rather tame compound annual growth rate of 2.3%. Perhaps unsurprisingly, Mondelez International posted a mere 0.4% return in the second quarter.

FEELING CHIPPER: MARKETS TAKE OFF

*Mem'ry
 All alone in the moonlight
 I can dream of the old days
 Life was beautiful then.
 —Andrew Lloyd Webber*

Global markets rallied beautifully in the second quarter, as investors came to believe that some form of resolution would be found for the conflict in the Middle East, allowing the Strait of Hormuz to re-open and for energy and other resources to flow to export markets around the world. Overseas, developed markets appreciated more than 10% and emerging markets by better than 24%. In US markets, large cap stocks, propelled by technology-heavy NASDAQ, rose by double digits. Smaller US stocks did even better, up 20% for the quarter. Real estate returns were also strong. Bonds and cash generated moderate returns. Only commodities turned down, with crude oil trading down more than 23% on the US-Iran ceasefire. Gold was off better than 12% on the quarter, copper 10%, and soybeans 14%.

Asset Class	Index	2nd Quarter Returns	Year to Date Returns
US Large Cap Stocks	S&P 500 Total Return	15.2%	10.2%
US Large Cap Stocks	S&P 500 Equal Weight	11.4%	12.1%
US Large Cap Stocks	NASDAQ Composite	21.6%	13.1%
US Small-Mid Cap Stocks	Russell 2500	20.3%	22.7%
International Developed Markets Stocks	MSCI EAFE	10.8%	9.4%
Emerging Markets Stocks	MSCI EM	24.1%	23.9%
Real Estate Securities	MSCI US REIT	12.2%	17.6%
Commodities	Bloomberg Commodities Futures	-8.1%	14.4%
Bonds	Bloomberg Barclays US Aggregate	0.7%	0.6%
Cash	ICE BofA 0-3 Month US Treasury Bill	0.9%	1.8%

SOURCES: THE WALL STREET JOURNAL, STANDARDANDPOORS.COM, FTSE, MSCI, BLOOMBERG

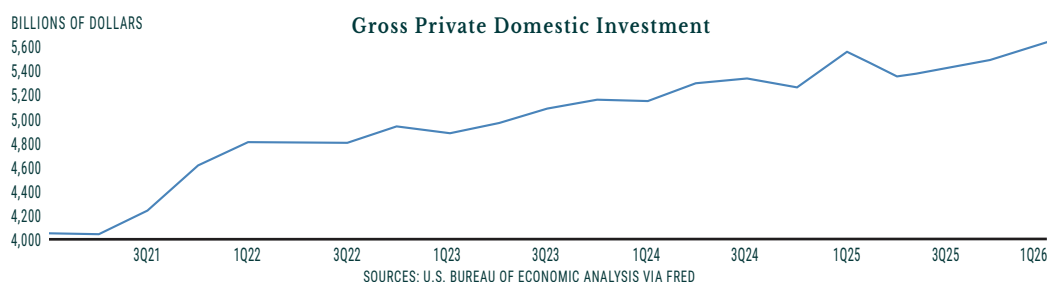
Within US large cap stocks, the technology sector once again reigned supreme, returning 31.8%. Nine of the ten best-performing stocks in the second quarter were technology stocks. The Magnificent Seven, however, were laggards, returning 11%. Investors rotated away from companies spending heavily on AI infrastructure and toward companies selling the components—particularly memory, storage, and semiconductor equipment—that benefited directly from the spending boom.

For the year thus far, the standouts have been emerging markets and US Small-Mid Cap stocks, notching gains greater than 20%. Particularly noteworthy: the South Korean KOSPI Index rose by 101% in the first half of the year. The index is dominated by global chip makers SK Hynix and Samsung Electronics—these two stocks constitute 60% of the index. The former surged over 300% while the latter jumped 169% during the period.

CHIPPING IN: AI IS DRIVING THE ECONOMY

*It's so easy to leave me
All alone with the memory
Of my days in the sun
—Andrew Lloyd Webber*

The US economy grew at a 2.1% annual rate in the first quarter, in line with its long term growth trend. The biggest contributors were private domestic investment (primarily AI spending for equipment—chips and more chips—and intellectual property) and government spending (rebounding from the longest federal government shutdown in last year's fourth quarter). Personal consumption expenditures, the largest component of GDP, were comparatively weak, advancing 0.5%—likely due to household caution in the face of higher inflation, high interest rates, and the war with Iran. Put another way, this is a business investment driven capital expenditure expansion, not a consumer driven cycle.

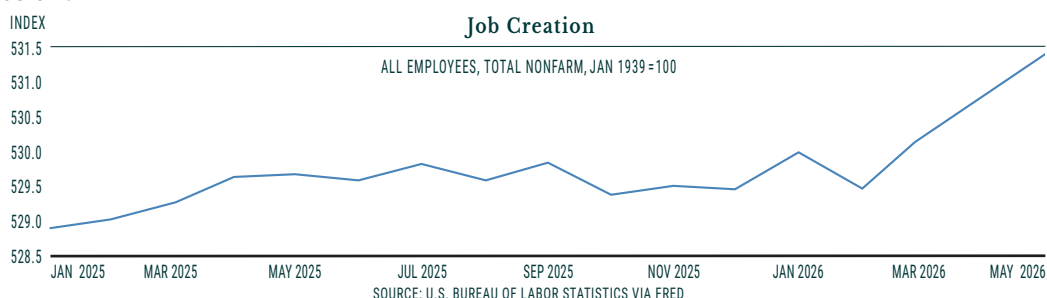


The Atlanta Fed's GDPNow estimates that growth picked up in the second quarter to a 2.5% annual run rate, fueled once again by strength in technology spending for business equipment and intellectual property. Business investment likely accounted for 60% of the growth in the economy, and is growing at an 8.5-10% annualized rate.

Consumer spending appears to have picked up in the second quarter, supported by higher tax refunds (due to the One Big Beautiful Bill Act), rising personal income, and a lower savings rate. Consumer spending growth is advancing at a 2.5 -3.0% annualized rate.

Underlying better retail sales, the labor market showed signs of recovery during the period from sluggish trends in the prior 12 months. The unemployment rate has remained steady at 4.3% for most of the year, shaking off for now fears that AI would prove to be a job-destructive force.

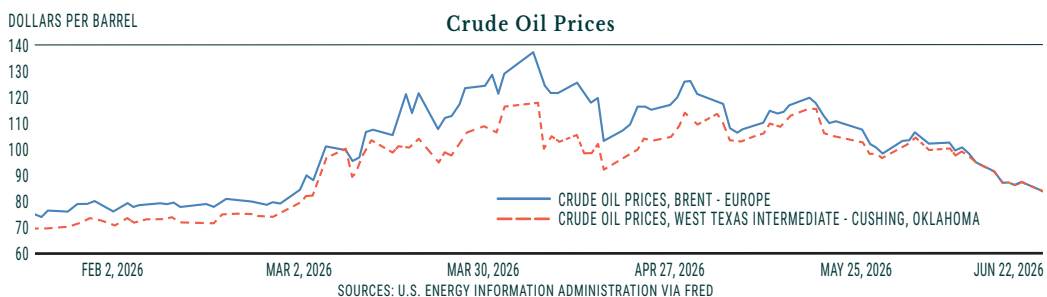
The American economy has seen a pick-up in job creation in the last three months, as can be seen in the chart below:



In last three months, employers added 565,000 workers to their payrolls. For context, in 2025 the US averaged only 10,000 new jobs per month. Further confirming this trend, May data from the Bureau of Labor Statistics indicates there were 7.6 million unfilled jobs, well above consensus expectations.

Perhaps the most challenging issue facing the economy is uncertainty about the direction of future inflation. Inflation has been running at a rate well above the Fed's 2% target for several years now, with recent acceleration as a result of Mideast conflict-driven energy price increases. The May 'core' PCE (excluding food and energy) rose to 3.4%, its highest reading since October 2023. While outsized tax refunds helped consumers meet the challenge of higher energy costs earlier this year, that source of relief has run its course.

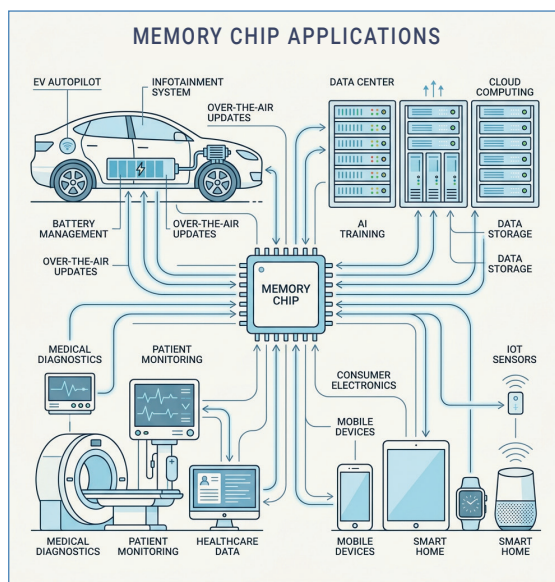
With the signing of a Memorandum of Understanding bringing a shaky ceasefire and an awkward re-opening of the Strait of Hormuz, crude oil prices have turned sharply lower. Energy prices are now modestly below pre-Iran war levels. In other words, the geopolitical risk premium has largely disappeared.



Retail gasoline prices at the pump should follow suit—they have fallen about 70 cents per gallon so far and, with a lag, should return to pre-Iran war levels.

In addition to the improved outlook for energy prices, tariff rates too are well below last year's levels, further easing inflation worries—Strategas estimates that the US has collected a mere \$10 billion in new tariff revenues this year. And there is little inflation pressure from wages. The Atlanta Fed's Wage Growth Tracker suggests that wage growth is now 3.4%, down from 4.3% a year ago—the slowest pace in several years and in line with a normal, non-inflationary rate.

Many economists believe that AI, like previous technological advances, will ultimately prove to be a disinflationary force as well. So, is the inflation genie back in the bottle?



Perhaps it's at best premature to draw that conclusion. Why? We return to our theme of memory chips. As noted above, memory chip prices have been on a tear, due to demand from AI and the re-direction of capacity toward high-bandwidth memory (creating shortages in dynamic random access memory). Technology data company Gartner reports that DRAM prices are up about 125% year over year in 2026, and forecasts that NAND memory prices will rise 234% over the same period. In other words, memory chips may be one of the most inflationary components in the global supply chain. Most industry forecasts do not expect a significant decline in memory prices over the next year. The more likely path is continued increases at a slower pace, followed by eventual stabilization once new capacity arrives in 2027–2028.

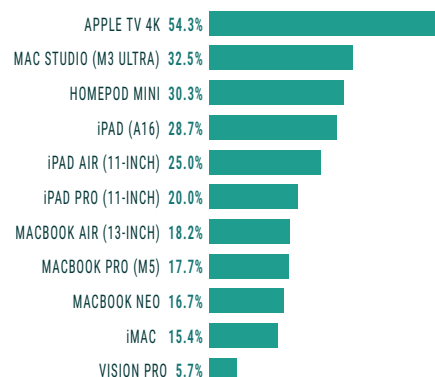
Memory chips are among the most widely used products in the global economy, embedded in billions of devices and much of the world's digital infrastructure. Virtually every modern electronic device contains memory. Memory chips are used in consumer electronics, data centers, industrial and automotive applications (factory automation, telecommunications infrastructure, driver assistance systems, electric vehicles), and medical equipment. Memory revenue is approximately \$295 billion, 30% of total semiconductor revenue approaching \$975 billion.

In June, Apple announced price increases on MacBooks and other devices of several hundred dollars. It cited higher memory chip prices as a justification.

Other device makers are sure to follow suit. And if memory inflation is affecting hardware prices, will it also ultimately force automobile manufacturers, diagnostic and medical imaging makers, factories, and others to raise prices?

The Federal Open Market Committee (FOMC) does not have a compelling case to lower interest rates to protect the labor market, full employment being one of its mandates. Energy prices and tariff reductions may help it avoid the need to raise rates to meet its price stability mandate, but if elevated chip prices are passed along to end users, the FOMC may remain on the sidelines a bit longer.

Apple Raises Prices in June 2026



SOURCES: APPLE VIA BUSINESS MODEL ANALYST

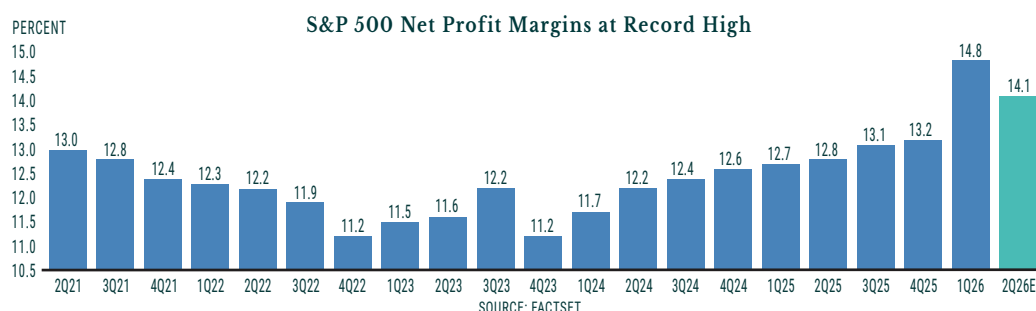
CHIPPING IN? HIGHER MARGINS

Tonight will be a memory too

And a new day will begin

—Andrew Lloyd Webber

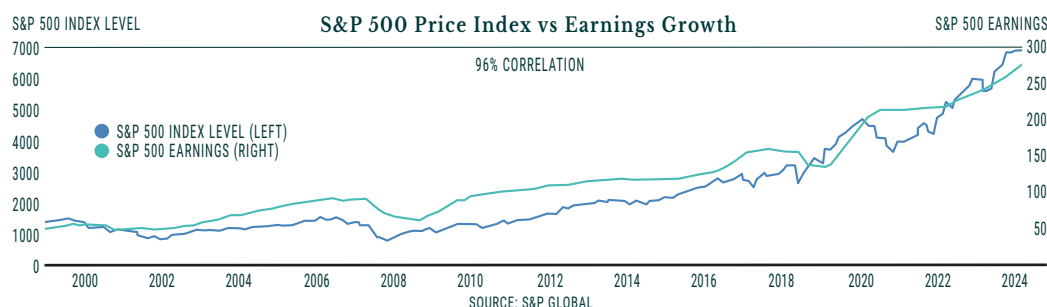
The euphoria over memory chips helped propel equity markets higher this past quarter. What drove investor enthusiasm for chipmakers and other technology companies? Higher profit margins, and higher profits. FactSet reports that the blended net profit margin for the S&P 500 in the first quarter was 14.8%, the highest ever recorded.



High margins translate, of course, to higher earnings, with first quarter earnings growth of 28.8% in the period. Revenue for the period was robust at 11.1%—but with profits growing 2 ½ times as fast, margin expansion, not sales growth, was the dominant driver of such outstanding profit growth.

Notably, profit growth for the technology sector specifically was a whopping 50.7%. Focusing on the leading US memory chip maker Micron: it recorded revenue of \$41.5 billion, up a staggering 346% over the prior year, and net profit of \$28.2 billion. Its gross margin was an astonishing 84.9%, and its net profit margin was 68.1%—about 5 times the average S&P 500 profit margin. This reflects the extraordinary pricing power created by the memory chip shortage and AI-driven demand.

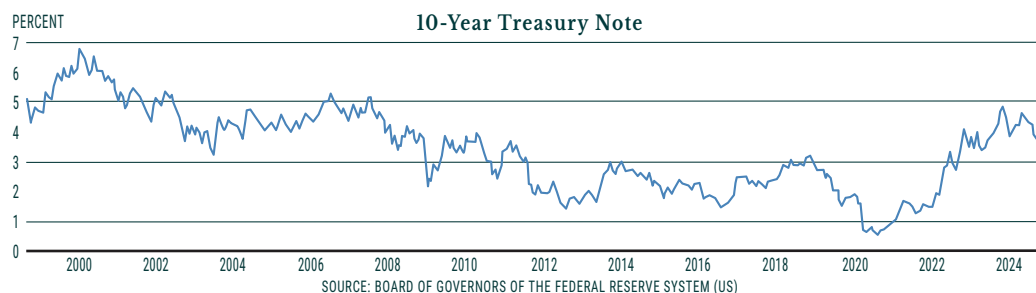
US corporate profits reached an all-time high of \$4.42 trillion in the first quarter of 2026, according to the US Department of Commerce. It should be unsurprising that stocks are at record highs when corporate profits are at record highs. There's no better reason for stock prices to rise than rapidly growing underlying corporate profits. As the chart below indicates, stock prices rarely depart, and not for long, from earnings trends.



Have stock valuations outrun fundamentals? In other words, are stocks in general expensive? Selling for approximately 20.5 times next 12 months profits, the stock market is only marginally above its five year average valuation. But by a number of other valuation metrics—price/book, price/sales, Shiller CAPE, EV/EBITDA—equities are in the 99th percentile.

These traditional measures suggest caution, but it is also noteworthy that companies' exceptional operating performance has few historical precedents. Analysts expect revenues to rise 7.2% this year. They see profits rising 24% in the just completed second quarter and for 2026 overall. Profit margins are expected to climb higher, to 14.6% in the third and fourth quarters. Looking further into the future, analysts see incremental sales and earnings growth of 7% and 17%, respectively, for 2027. This is truly extraordinary growth.

Many investors are concerned, understandably, about tariffs and geopolitical risks as macro issues and valuations as a market issue. That said, there are powerful structural forces supporting both the economy and financial markets—particularly equities. As outlined, profit growth is remarkably resilient. Capital spending is booming. Many companies are exhibiting pricing power without seeing demand destruction. Earnings growth appears to be broadening out from technology companies to industrials and financials, among others. Productivity improvements from AI and automation bring the prospect of faster, noninflationary economic growth. Corporate balance sheets are healthy. Consumer spending is supported by low unemployment, moderate debt levels, and wage growth. With strong support from fiscal policy, the good times appear ready to roll.



This remarkably constructive environment is equally true for the bond market. Absolute yields—10 year Treasuries at 4.46%—are attractive, particularly in the context of the rate repression fixed income investors endured for 15 years following the Global Financial Crisis. Bond investors' inflation expectations appear to be well anchored—they remained so even during the oil price spike at the start of the Iran war. Credit quality is generally healthy, and credit spreads are tight—an indication that bond investors do not foresee a near term recession or widespread defaults. While borrowers are increasing their debt issuance, demand from institutional investors remains strong. Bond rating agencies' upgrades exceed downgrades. Investment grade bond investors are presented with the opportunity to receive meaningful income at moderate risk, and yields at these levels will likely provide some portfolio diversification benefit when equities decline.

CASHING IN ONE'S CHIPS?

Has the moon lost her memory?

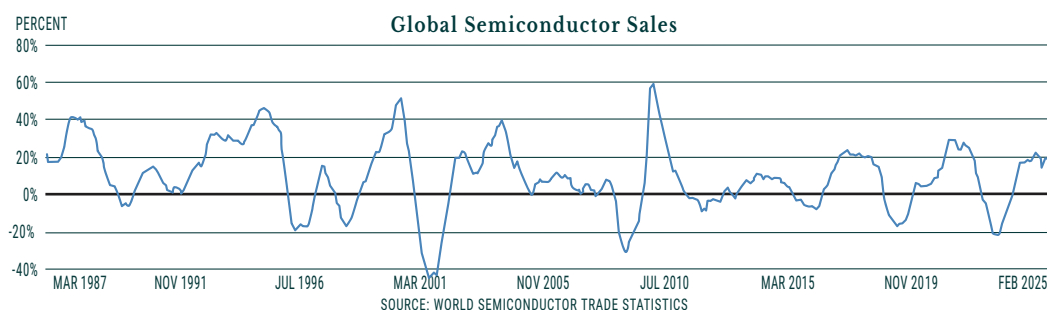
She is smiling alone.

—Andrew Lloyd Webber

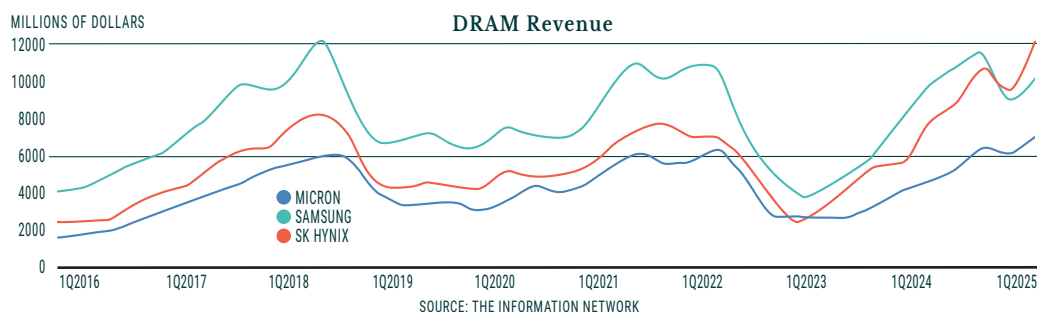
The AI story generally, and the memory chip story specifically, are compelling. Gartner estimates that direct spending on AI—covering hardware, infrastructure, software, and services—will total \$2.6 trillion this year. That's a 47% increase over 2025. Their forecast for 2027 is \$3.5 trillion.

The AI driven memory scarcity has provided an extraordinary opportunity for players in the space to make extraordinary amounts of money. Investors, too.

Semiconductors generally have exhibited a great deal of volatility in demand. As the chart below indicates, the industry enters a new cycle every three or four years, on average.



Memory chips in particular have historically been amongst the most cyclical of products, subject to booms and busts with high highs and low lows. After all, memory chips are an undifferentiated commodity product. The chart below illustrates the fluctuations in demand for dynamic random access memory chips.



So will the current growth phenomenon continue? Is AI demand structurally different and more durable than past memory cycles?

Perhaps a lesson from another chip maker may be instructive. The Chips Ahoy! brand achieved rapid growth in its early years, but momentum stalled in the years 2017-2019.

To revive growth, Mondelēz increased marketing and advertising, modernized the Chip mascot and packaging, improved distribution, renovated the core recipe, rebuilt emotional connections with consumers, collaborated with Hershey on co-branded flavors, and invested in innovation.

The company credits these moves with driving sustained growth through the pandemic and afterward. By 2023, Chips Ahoy! had become one of Mondelēz's fastest growing brands in North America. It's the number one chocolate chip cookie brand, as noted earlier enjoying a 50% US market share, and grew at a double digit rate.

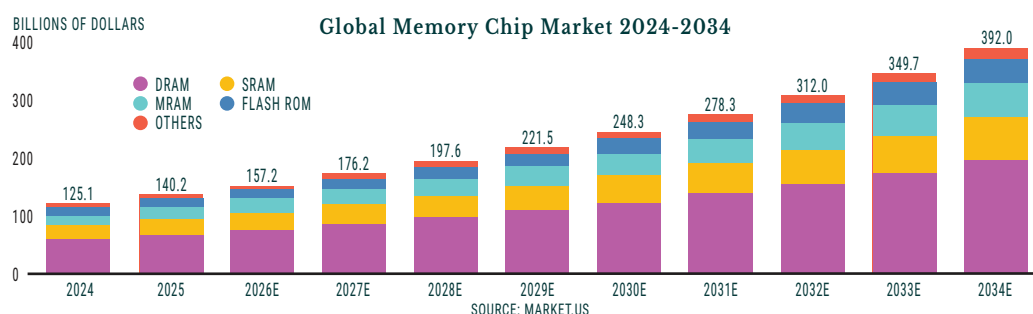
The takeaway? Innovation became the growth engine.

What lessons about sustainable growth can a consumer packaged good product have for a technology product? Chips Ahoy! grew by creating and increasing consumer demand. Its growth is relatively durable, as it controls levers to continuously refresh and innovate its distribution, marketing, product extensions, relevance to younger consumers, and leverage of a powerful brand.



By contrast, growth for Micron and other memory chip makers stems from AI-driven demand and supply constraints—customers competing for scarce product. The extraordinary financial results—tripling and quadrupling revenue, unheard-of gross and net profit margins—are the result of an economics of scarcity. That’s an inherently less durable growth model, for several reasons. One is that chip makers don’t create or control demand. A second is that capacity can be increased, in time, reducing scarcity—resulting in sharply lower pricing power and declining profit margins. A third is that high growth attracts capital and competition, with similar results.

The lesson from Chips Ahoy! is not that growth can persist forever. The lesson is that durable growth comes from sustained demand, not constrained supply. Applying that lesson to memory chips, the question to ask is whether the AI revolution may have changed the demand curve. Memory chips, as noted, have always been a cyclical business, with demand waxing and waning. Is it possible that demand will now be sustained, driven by potential years-long AI requirements? If so, memory could look less like a commodity and more like critical infrastructure.



Memory chip makers are going all out to increase production capacity. The largest players have capital spending budgets of \$25-30B each for 2026. But chip fabrication plants are time consuming as well as expensive to construct. Additional capacity is expected to begin ramping up in 2027, and add more substantially to supply in 2028 and beyond. That suggests manufacturers will continue to exercise considerable pricing power in the near term—but that pricing power could erode over the next couple of years. Increased capacity will ease supply constraints and reduce margins, and may, in time, return the industry to its prior pattern of rapid growth and dramatic collapse.

LET THE CHIPS FALL WHERE THEY MAY

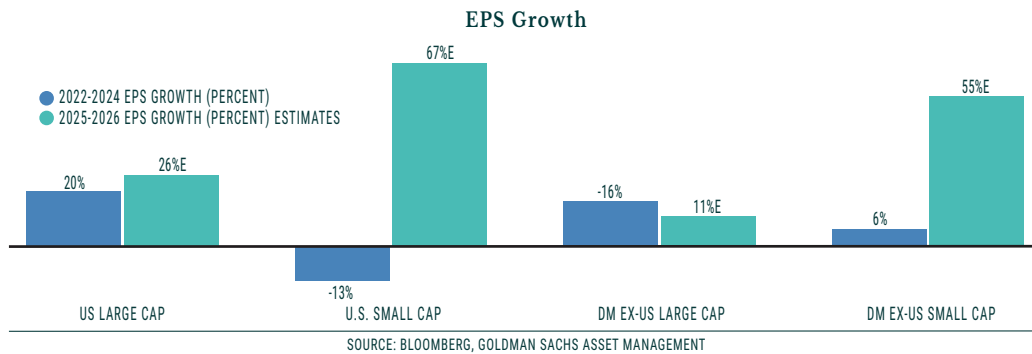
*When the dawn comes
Tonight will be a memory too
And a new day will begin
—Andrew Lloyd Webber*

How should investors be positioned in such an environment?

Equity investors should hold their course. There will likely be an ongoing dialectic between advocates of the brave new world of AI with all its glittering possibilities and naysayers who see profligate and ultimately unprofitable over-investment in a dangerous technology. Policy support, exceptional profit growth, and a productivity wave argue for maintaining exposures—granted, markets have recognized many of these strengths already and baked them into current valuations.

Within equities, small and mid-cap US stocks screen attractively. They sport more modest valuations than US large cap companies and, after years of relative under-performance, have begun to out-perform. They are

generally less exposed to geopolitical risks, and are beneficiaries of lower interest rates that may follow an easing of inflationary pressures.



Emerging markets stocks have dramatically out-performed, and while appreciation could persist, they may be increasingly viewed as AI plays. Technology represents 37% of emerging markets indices, a level similar to the dominance of technology in the S&P 500. And, more specifically, semiconductor manufacturers comprise the lion's share of emerging markets technology companies.

In fixed income, intermediate-term high quality bonds offer an attractive risk-reward profile: they provide meaningful income, retain the potential to appreciate if the economy slows, and are less subject to price fluctuations if longer term rates rise in the face of fiscal and structural forces.

Portfolio management is a long game. Investors need good memories, to recall past cycles and always be wary of siren songs that 'this time is different.' Memory chip exposure has been good for portfolios, but laws of economics hold: supply rises to meet demand, and price is driven by their intersection. The memory chip tsunami is a wild fun ride but could turn dangerous when it nears shore. Periodically trimming exposure is prudent. And when the chips are down, have a cookie or two. Chips Ahoy! anyone?



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