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COLONIAL TRUST COMPANY

3RD QUARTER | 2026

COLONIAL TRUST *Quarterly*

Quarterly Performance

All AI All the Time

Welcome Madeline Hollon

QUARTERLY PERFORMANCE

AFTER A DIFFICULT FIRST QUARTER DUE TO THE IRAN CONFLICT, THE MARKET POSTED AN IMPRESSIVE RALLY BEGINNING MARCH 30TH.

For the quarter, the S&P 500 returned 15.2%, marking the best quarter in six years. Technology stocks continue to provide market leadership, with the Nasdaq index returning 21.6%. Small cap stocks, as measured by the Russell 2000, outperformed large cap stocks, with a 21.7% return. International markets moved into the green for the year, with the MSCI EAFA developed market index returning 10.3%, and the MSCI Emerging Markets index returning 23.0%. Bonds provided positive returns for the quarter, with the Bloomberg Aggregate Bond index returning 1.1%.

Index	2Q26	YTD
S&P 500	15.17%	10.16%
DJIA	13.37%	9.75%
Nasdaq	21.60%	13.14%
Russell 2000	21.72%	22.84%
MSCI EAFE	10.29%	9.12%
MSCI Emerging Markets	22.96%	22.82%
Bloomberg Agg Bond Index	1.08%	1.03%

Source: Bloomberg, LP

The leadership throughout the market was artificial intelligence (AI) related; though, in a different way than we saw in 2025. The beneficiaries are no longer the hyperscalers spending the capex, but rather the companies receiving these dollars to build out data centers. No place is this more evident than in semiconductors. The Philadelphia Stock Exchange Semiconductor index (SOXX) returned 88.0% for the quarter. This spending also benefited industrial companies supplying equipment for the data center, with companies producing electrical components, HVAC, and turbines for power all seeing strong returns. Within emerging markets, the leadership has been semiconductor foundries in Taiwan and South Korea that resulted in robust returns.

US public sentiment on AI is negative. There is strong local public pushback against new data center construction. While the perception is negative, the impact at the enterprise has been mixed. A McKinsey study finds 39% of companies reporting a profitability impact from AI utilization; however, the gains are below 5%. Adoption across enterprises is growing but remains relatively low in many industries, with the notable exception of coding. This has some investors questioning the return of the enormous investment in the AI buildout. The market has ignored questions about long-term implications of AI and is focused on the impact the capital spending is having on the economy and companies today.

ALL AI ALL THE TIME

THE AI BUILDOUT IS HAVING EFFECTS ACROSS THE ECONOMY, THE LABOR MARKETS, POWER DEMAND, INFLATION, CREDIT MARKETS, AND EQUITY MARKETS.

It is the single biggest driver of economic activity since the railroads of 1840. Goldman Sachs estimates the global capital expenditure on AI to be $7.6 trillion between 2026 and 2031.

On June 25th, the BEA released revisions to first quarter GDP, which grew by 2.1%. The largest contributor to economic activity, consumer spending, grew by only 0.5%. Fixed investment, which represents 17.7% of GDP, grew at a much faster 6.5%. The BEA segments fixed investment into residential and nonresidential investment. The nonresidential investment is further divided into IP products, equipment, and structures. This table highlights that growth in fixed investment for IP and nonresidential equipment has outpaced the growth rates for the entire economy and that of consumer spending. These two categories represent roughly 11% of the economy, but they are driving a significant amount of economic growth. Over the last twelve months, the five hyperscalers spent $489 billion in capital expenditures and are projected to spend $726 billion in 2026. The spending from these five companies, and others, is making a meaningful contribution to GDP growth.

	2Q25	3Q25	4Q25	1Q26	Weight
GDP	3.8%	4.4%	0.5%	2.1%	
PCE (consumer spending)	2.5%	3.5%	1.9%	0.5%	68.0%
Fixed Investment	**4.4%**	**0.8%**	**1.5%**	**6.5%**	**17.7%**
Residential	-1.2%	-1.6%	-0.4%	-1.7%	3.8%
IP Products	15.0%	5.6%	5.4%	13.8%	5.7%
Nonresidential Equipment	8.5%	5.2%	4.3%	15.8%	5.4%
Nonresidential Structures	-7.5%	-5.0%	-6.5%	-4.7%	2.8%

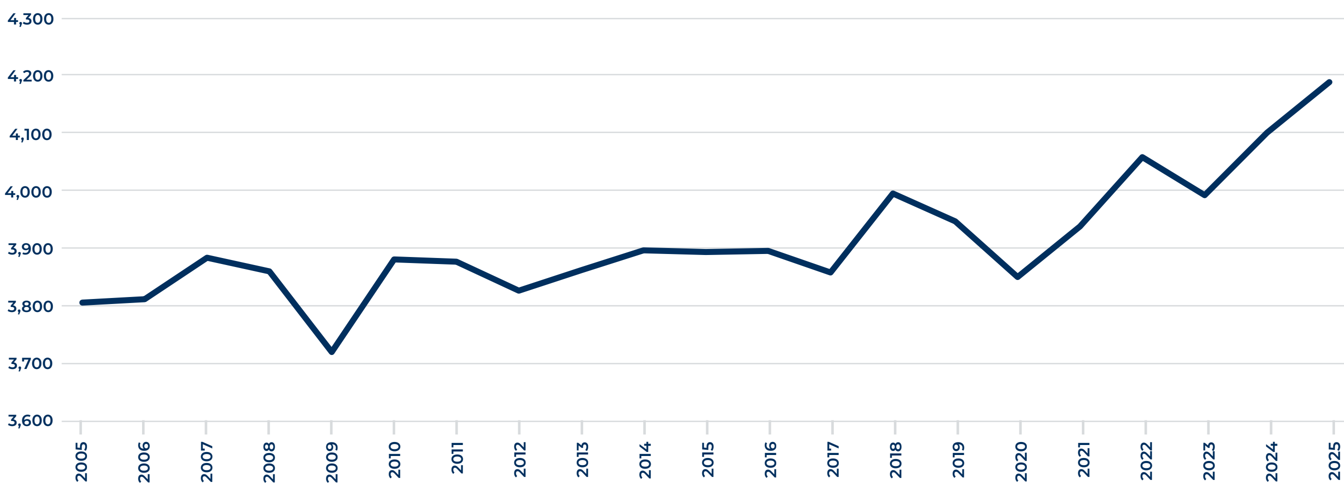
Source: Bloomberg, LP

GIVEN THAT ADOPTION OF AI REMAINS MODEST AT THE ENTERPRISE LEVEL, IT IS DIFFICULT TO SEE CONCRETE IMPACTS FROM AI ON THE LABOR MARKET.

The moribund labor market in 2025 was blamed on slow hiring due to AI and tariff uncertainty. Last year the BLS reported only 116,000 jobs were created, or 9,666 jobs per month. The labor market has rebounded in 2026, with 552,000 jobs created in the first six months, or 92,000 jobs per month. AI does appear to be changing the nature of the job market and is acting as a white-collar productivity shock. AI is increasing demand for the trades to bring data centers online, with 101,500 jobs created in nonresidential construction in the last year. White-collar workers are seeing mixed impacts. Lower skill jobs in data entry, simple coding, and low-complexity customer support are vulnerable to obsolescence from AI. AI is making higher skill jobs more productive, by augmenting human judgment in many cases. To date, the impacts on the labor market are positive, but uneven.

The growth in the US power load has been low over the last two decades, but AI is changing this dynamic. Estimates from the EIA and Wall Street point to rapid demand growth over the next decade. Demand is driving power prices higher for data centers nationally and for residential customers in some geographies. Newer data centers are increasingly "bringing their own power" to minimize the impact on the grid and other power users. These factors are driving investment in capacity and the grid from utilities. Additionally, we are seeing companies investing in shuttered nuclear reactors, battery technology, small cell reactors, and other technologies to bring reliable capacity online. In South Carolina, Santee Cooper has selected Brookfield to restart and potentially acquire the two unfinished reactors at V.C. Summer. We are seeing governments, regulated utilities, and the private sector scramble to bring power online to meet rising demand.

CONSUMPTION KWH



Source: EIA Monthly Energy Review

INFLATION IS TYPICALLY CAUSED BY TOO MUCH MONEY CHASING TOO FEW GOODS.

This capital investment cycle is driving certain prices higher. As mentioned, we are seeing power prices increase due to rising demand. This is also increasing wages for specialty trades. In data center hotspots, like Virginia, data center electrical work commands a 75% premium to typical housing construction jobs. Data center equipment is also seeing inflation. Reuters reports power transformer prices are up 80% in the last five years. Switchgear is up 12.4% over the last year and commercial HVAC prices set a record in May according to the BLS. TrendForce reported that contract prices for dynamic random-access memory (DRAM chips) rose 98% in 1Q26. This is causing the cost of new data centers to increase rapidly, driving prices higher in other areas of the economy that rely on data and chips. Apple recently announced price hikes of 15%-18% across all products due to higher memory cost. AI is projected to be deflationary when fully implemented across the economy by driving productivity, but for now prices are rising.

AI is having an impact on the credit market as well. When ChatGPT was introduced in 2022, the hyperscalers funded their capital expenditures with cash flow from operations. They have increasingly turned to the credit markets to fund these ambitious capital expenditures. The combined debt of Alphabet, Microsoft, Meta, Amazon, and Oracle in 2022 was $373 billion. In the most recent quarter this number swelled to $702 billion. These companies have become the dominant issuers in the investment grade market. BofA forecasts 2026 issuance of these companies to reach $175 billion. In addition to the bond market, these companies are turning to special purpose vehicles (SPVs) to fund construction of new data centers, which are leased back to the hyperscalers. Bloomberg estimates future data center lease commitments from the hyperscalers now exceed $850 billion. This number will not appear as capital expenditure and will not show up on the balance sheet until lease payments begin. To date, the bond market has been able to digest this debt issuance; though, these borrowers have seen their credit cost rise by around 0.3% compared to Treasuries. Assuming there is not an infinite amount of money in the bond market, the record issuance by these companies (not to mention the US government) could raise borrowing costs for other issuers competing for this capital.

LASTLY, AI IS HAVING A PRONOUNCED EFFECT ON THE EQUITY MARKET.

The AI trade began in 2022 with Nvidia as its poster child. It quickly broadened out to the hyperscalers, many of which are the Magnificent 7. The market sniffed out the inputs for the data center, from the high tech to the mundane, and bid those stocks higher – with commercial HVAC, electronic components, engineering and construction companies seeing their shares rise. In 2026, the bottleneck has been CPU and DRAM, thus the chip makers have seen their stocks skyrocket. The SOXX index is up 101.5% for the year. While the market anticipates the next bottleneck in the data center buildout, it has turned negative on the spenders of this capital. Once AI darlings, the hyperscalers have seen their stocks sold as the market worries about the long-term return on these AI investments. Meta and Microsoft have seen their stocks fall 14.7% and 23.8% year-to-date. Markets are concerned AI may make software-as-a-service obsolete or at least less profitable. For that reason, software stocks have been weak in 2026. The iShares Expanded Software ETF is down 11.7% for the year. The same belief has hurt the alternative asset managers who have private credit funds, many of which have loans to smaller software companies. The large, publicly traded alternative asset managers have seen their stocks fall between 19% and 43% this year. Few software companies have seen noticeable changes in their business, but the expectation is enough for fast money to sell these stocks.

The market sentiment on AI's impact on individual stocks shifts daily, causing swings in share prices of both the AI winners and losers. The combined market value of AI-related companies (hyperscalers, semiconductors, hardware, power, and software) represents 51.5% of the S&P 500's value, according to JP Morgan. Year-to-date, the market is hyper-focused on this half of the market and less interested in the other half. Outside of daily volatility, the market favors the beneficiaries of this enormous capital investment and shies away from companies it fears may see AI have deleterious impacts on the business in the future.

WHERE DO WE GO FROM HERE?

WE AGREE WITH WALL STREET'S CONSENSUS THAT ECONOMIC GROWTH WILL BE ABOVE TREND FOR THE REMAINDER OF THE YEAR.

Bloomberg's economic survey projects 2.1% GDP growth for the year, and quarterly estimates have been increasing. The growth in private investment will continue to be the driver. We expect consumer spending to rebound from 1Q26's low levels in 2H26 as gasoline prices have fallen from $4.56 per gallon to $3.83 nationally as traffic has increased in the Strait of Hormuz. We expect the labor market to continue to show healthy job growth, around 50k-100k per month.

Headline consumer price inflation, currently 4.2%, should fall thanks to lower oil prices. However, core services inflation has been above 3% and increased over the last three months. We don't expect inflation to fall quickly to the Fed's 2.0% target, which will prevent the Fed from reducing interest rates in 2026. Inflationary pressures, coupled with heavy government borrowing, should keep interest rates in their current range – with the 10yr Treasury trading between 4.25% to 4.75%. This offers bond investors positive real yield above inflation.

After first quarter earnings, Wall Street firms raised their year-end price targets for the S&P 500 index due to strong earnings growth. For the first quarter, FactSet reports index earnings grew 27.7%, compared to the 13.1% growth expected. The strong results have caused analysts to rachet growth expectations higher for the remaining quarters of 2026. At the beginning of April, Wall Street expected full year earnings growth of 17.4% and that number now stands at 24%. Revenue estimates have also increased from 9.5% to 12.3%. The AI buildout is the largest contributor to growth, with the technology sector projected to see earnings growth of 40% and many chip companies expected to see earnings growth north of 100%. The bullish expectations of Wall Street are grounded in earnings growth and not valuation expansion. In fact, valuations for the equity market have fallen on a forward-earnings basis as earnings estimates have risen faster than stock prices.

WE CONTEND WE ARE IN THE MIDDLE INNINGS OF THIS AI INVESTMENT CYCLE BUT BELIEVE WE ARE EARLY IN IMPLEMENTATION ACROSS THE ECONOMY.

The read about where it goes and who the winners are changes quickly. There are questions about token usage and the cost to the enterprise for the newest frontier models. A UBS report stated 60% of enterprise companies are throttling AI spending and are routing work to older AI models with lower costs. There is a growing debate about whether open source or closed source AI models are best for enterprise users. The closed source models are dominated by OpenAI, Anthropic, and Google, where users access the model on these companies' servers, where the reasoning of the model, the model weights, is a black box to the user. In open-source models, the user can download the model. They can customize the model and self-host the application. The debate is over who controls the AI stack and therefore the proprietary data that is input into the model. As enterprise adoption ramps, companies want to safeguard their data for competitive and regulatory reasons.

We don't know exactly how AI will change our economy or lives in the future, but we are confident it will. For the next few years, we are going to see continuing investment in the computing capacity for this future to manifest. Over time, the economy and enterprises will determine how to leverage AI in ways that increase productivity, while safeguarding their trade secrets and competitive moats. This will be both exciting and tumultuous as change comes rapidly. We believe the world will see more positives than negatives from this new technology and we are attempting to invest our clients' capital prudently in companies that can benefit from the investment cycle and its eventual implementation.

The market has largely been focused on AI, but not at the exclusion of Fed policy, the Iranian Conflict, or other news. We did see Kevin Warsh assume the Fed Chairman's seat during the quarter. The quick take is that he wants to remake the Fed, particularly around mission creep and communication. But his first test as Chair showed independence from the executive branch. The markets are pricing in cessation of hostilities in the Persian Gulf and oil prices closed the quarter back to late February levels. And on the last day of the quarter, SCOTUS confirmed the Fed's unique position in our government and limited the executive branch's influence without due process. These are all import stories with market and economic impacts, but the market is more focused on the AI investment cycle than other stories.

As we settle into the dog days of summer, we want to celebrate our country's founding 250 years ago and are grateful for the government that has created this wonderful country of ours.

WELCOME
MADELINE A. HOLLON

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Client Service Representative

Madeline Hollon joined Colonial Trust in November 2025, bringing more than a decade of experience in client service and financial administration. Prior to joining Colonial, she spent over six years with Synovus Securities, Inc. as an Administrative Associate, where she supported a team of investment advisors and ensured efficient operational workflows across multiple client portfolios.

Before her time at Synovus, Madeline spent 5 years with Sadler & Company, Inc. in the Sports & Recreation Division as a licensed property and casualty insurance agent. She also served as Assistant Manager and Fitness Facilities Account Manager developing strong relationships with a national client base.

A graduate of the University of South Carolina, Madeline earned her Bachelor of Science degree in 2012. Outside of work, she enjoys spending time with her husband, Brad, their yellow Labrador, Timber, and their spirited cat, Sierra “Feral”. She is also an active member of the Junior League of Columbia.

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