September 2026 Market Commentary

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Stocks Keep Climbing, but the Bond Market Is Sending a Different Message

August was another strong month for stocks, but beneath the surface, the financial markets are sending some conflicting signals.

Equity markets moved higher during the month, with the S&P 500, Dow Jones Industrial Average, Russell 2000, and equal-weight S&P 500 all reaching new all-time highs. The Nasdaq 100 also moved back toward its June record.

The breadth of those new highs is important. These indexes represent very different parts of the market, from the largest technology companies to small-cap stocks and the average company in the S&P 500. Market leadership has shifted several times this year, alternating between periods dominated by a relatively small group of companies and periods when participation broadened.

August was clearly one of the broader periods. Rather than relying exclusively on a handful of mega-cap technology companies to push the major indexes higher, investors were willing to put money to work across a much wider range of companies and industries.

The bond market; however, is telling a somewhat different story.

Interest Rates Are Becoming More Important

Treasury yields moved sharply higher during August, with the 10-year Treasury yield climbing above 4.75% and the 30-year yield approaching 5.30%. Longer-term interest rates are now near levels we have not seen since the early 2000's.

Several factors are contributing to the higher rates. First, inflation remains above the Federal Reserve's target zone. Secondly, government borrowing remains elevated. Also, higher energy prices have created another potential source of inflation. Federal Reserve Chair Kevin Warsh used his Jackson Hole speech to make it clear that the Fed's next move could be a rate increase rather than the rate cuts investors had previously hoped for.

Last week's employment report reinforced that possibility. The U.S. economy added 162,000 jobs in August, substantially more than economists expected, while unemployment remained at 4.1%. July's initially reported decline in employment was also revised to a net gain. The report provided additional evidence that the economy and labor market remain resilient.

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The employment report pushed Treasury yields higher and increased expectations that the Federal Reserve could raise rates at its September meeting. That makes the upcoming inflation reports particularly important. If inflation continues to remain higher than the Fed would like, the combination of persistent inflation and a resilient labor market could give policymakers additional justification to tighten monetary policy.

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That suggests bond investors are not particularly concerned about companies' ability to repay their debt. Instead, the concern appears to be the level and direction of interest rates themselves.

Markets Are Learning to Live with Headline Volatility

Geopolitical events continue to dominate headlines, particularly developments in the Middle East and the Strait of Hormuz.

What has changed is the market's reaction to those headlines. Earlier this year, the beginning of the conflict and disruption in the Strait of Hormuz sent oil prices sharply higher and contributed to a broad stock market selloff. Investors were immediately concerned about what higher energy prices could mean for inflation, economic growth, and Federal Reserve policy.

As we moved through 2026, markets have experienced several rounds of escalation and de-escalation. Oil prices still react quickly when developments threaten global energy supplies, yet investors appear less willing to treat every headline as the beginning of a larger economic shock. Markets increasingly seem to be waiting for evidence that an event will materially affect the supply of oil, inflation, or economic growth before reacting as dramatically as they did earlier this year.

Investors worry that higher oil prices could keep inflation elevated and force the Federal Reserve to maintain higher interest rates or raise them further.

That doesn't mean geopolitical risk has disappeared. Oil remains above $90 per barrel, and renewed escalation in the Middle East could quickly push energy prices even higher. This is important because as we mentioned above, inflation is already running above the Fed's target. Investors worry that higher oil prices could keep inflation elevated and force the Federal Reserve to maintain higher interest rates or raise them further.

The AI Debate Isn't Going Away

Artificial intelligence remains the other dominant market story. There are two main debates taking place.

The first is whether AI will ultimately transform large portions of the global economy. There appears to be less disagreement about that than there was even a year ago.

The financial markets will likely continue to debate if this spending will ultimately produce acceptable returns, but the companies making the investments are not waiting for an answer as the buildout continues.

Secondly, there are questions about the vast sums being spent on AI infrastructure, and whether these investments will generate adequate returns.

Data centers need enormous quantities of computer chips, networking equipment, electricity, cooling systems and increasingly sophisticated infrastructure. Companies continue to commit extraordinary amounts of capital to building that capacity.

The financial markets will likely continue to debate if this spending will ultimately produce acceptable returns, but the companies making the investments are not waiting for an answer as the buildout continues.

We continue to believe AI will be one of the most important investment themes of this decade. That does not mean every AI-related investment will work, or that valuations don't matter.

The market's reaction to last week's employment report captures the unusual environment we find ourselves in. We have stocks near record highs and at the same time long-term bond yields are at multi-decade highs.

This creates an unusual situation. AI companies have produced tremendous earnings growth, but expectations and valuations are also high. Strong results can therefore sometimes be met with relatively muted stock reactions because investors have already priced in substantial future growth.

We continue to believe AI will be one of the most important investment themes of this decade. That does not mean every AI-related investment will work, or that valuations don't matter. Transformational technologies almost always produce winners and losers along the way.

Good News Is Once Again Complicated News

The market's reaction to last week's employment report captures the unusual environment we find ourselves in. We have stocks near record highs and at the same time long-term bond yields are at multi-decade highs. Something eventually must resolve this tension.

Either inflation moderates to relieve pressure on interest rates, higher inflation drops economic growth enough to eventually bring rates lower, or businesses and investors demonstrate that they can continue to operate successfully with long-term rates around today's levels.

For now, the stock market appears willing to give the economy and corporate earnings the benefit of the doubt.

What We Are Watching

As we move through September, we are paying particular attention to four things.

Inflation and the Federal Reserve - The next CPI and PPI reports are important. The question is no longer when the Fed will cut rates. The more immediate question is whether inflation and economic growth will force the Fed to raise rates.

Long-term Treasury yields - The 10-year Treasury approaching 5% deserves attention. Higher long-term rates affect mortgage rates, corporate borrowing, real estate values, equity valuations, and ultimately economic activity.

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Investors should remember that the goal is not to capture every last gain in a rising market, but to participate in long-term growth while taking appropriate risk and staying prepared to act when volatility creates new opportunities.

Oil and the Middle East - Markets have become more accustomed to geopolitical headlines, but a sustained disruption in energy supplies would be different. Oil is one of the clearest transmission mechanisms between geopolitical risk, inflation, and monetary policy.

AI spending and earnings - AI infrastructure spending continues at an extraordinary pace. The next phase will focus on whether today's massive capital investments can generate sustainable earnings and productivity gains over time.

Don't Ignore What the Bond Market Is Telling Us

A 10-year Treasury yield approaching 5% and a 30-year Treasury yield above 5% are significant. These levels increase borrowing costs throughout the economy, create greater competition for investor capital, and ultimately raise the hurdle that stocks and other risk assets need to clear. When investors can earn attractive yields in high-quality fixed income, the case for buying stocks becomes less compelling.

Corporate earnings remain resilient, employment is healthy, credit conditions are stable, and stock market participation has broadened. Even so, investors should not ignore the bond market's warning: inflation, government borrowing, and interest rates may stay elevated even as stocks signal confidence in continued economic and earnings growth. Both messages can be true for a while, but the key question for the rest of 2026 is how long that balance can last.

This is precisely the type of environment where we believe discipline becomes increasingly important.

When markets are setting records, volatility is relatively low, and investors are being rewarded for taking risks, the temptation is often to become more aggressive. We believe the better approach is the opposite. This is not the time to get greedy.

Investors should remember that the goal is not to capture every last gain in a rising market, but to participate in long-term growth while taking appropriate risk and staying prepared to act when volatility creates new opportunities.

The bond market is reminding us that the cost of money has changed. With long-term Treasury yields around 5%, investors have alternatives today that simply did not exist when interest rates were near zero. That should be reflected in how we think about portfolio construction, diversification, and the amount of risk we are willing to accept.

Diversification remains important, and it is important to resist the temptation to increase risk simply because markets have been moving higher.

Investors should remain focused on their long-term objectives, not become complacent, and not get greedy. Diversification remains important, and it is important to resist the temptation to increase risk simply because markets have been moving higher.

There are times to press your advantage and there are times to protect it. With stocks at record highs and the bond market flashing a very different signal, we believe this is a time to stay disciplined.

Please contact us if you have any questions,

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Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index, which represents approximately 8% of the total market capitalization of the Russell 3000 Index.

S&P 500 Index is a capitalization-weighted index calculated on a total return basis with dividends reinvested. The index includes 500 widely held U.S. market industrial, utility, transportation and financial companies.

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