

Summary

Stocks struggled in September, but most indexes remain near highs. We continue to view the last months as a period of consolidation following exceptional performance in Q2. This is generally healthy and although most concerns remain unresolved (wars, high oil prices, rising interest rates, looming mid-term election...) investors have shown resilience and **positive trends remain intact**. September itself was interesting as leadership was exceptionally narrow (see chart and thoughts on page 4).

Bonds fared worse as yields rose. The silver lining in bonds is that yields are now relatively attractive and provide a cushion against portfolio volatility. The downside is higher borrowing costs and increased debt service costs for variable loans or debt (including sovereign debt) that needs to be refinanced. **Our tactical portfolio maintains benchmark equity exposure**, underweight bonds, with limited exposure to REITs and gold miners– uneven performance amongst stocks, sectors and regions has prompted incremental, opportunistic adjustments.

Key Market and Economic Drivers in Q3 2026

- The S&P 500 returned +2.3% in the third quarter with dividends and the Nasdaq Composite gained +2.6%, while the Dow Jones Industrial Average declined -2.3%. Year-to-date, the three indices have earned +12.7%, +16.1%, and +7.2%, respectively.
- Developed market international stocks (MSCI EAFE) gained +0.9%, while emerging market stocks (MSCI EM) declined -0.4% over the quarter, both in U.S. dollar terms.
- The Bloomberg U.S. Aggregate Bond Index fell -3.5% in the third quarter for a year-to-date decline of -2.9%, with longer-dated bonds struggling. The 10-year Treasury yield climbed to 5.29%, a two-decade high.
- Brent crude ended the quarter at \$103 per barrel while WTI finished at \$90.
- August headline CPI rose +3.4% year-over-year, while core CPI, which excludes volatile food and energy prices, increased only +2.4%. The core PCE price index, the Fed's preferred measure of underlying inflation, rose +3.0% year-over-year in August.
- The Federal Reserve raised its key policy rate to a range of 3.75% to 4.00% in September.

Source: Cleonomics, Investors FastTrack and Ned Davis Research

1. What to Expect in Portfolios

Last month we said, "The setup going into September appears tenuous. Seasonality suggests correction risks remain elevated. On a brighter note, consolidations tend to be healthy and lead to a resumption of the prior trend..."

October may be scary at times, this year with Fed risks and looming mid-term elections. That said, we are cautiously optimistic in terms of our Q4 outlook and expect potential volatility to be short lived and benign.

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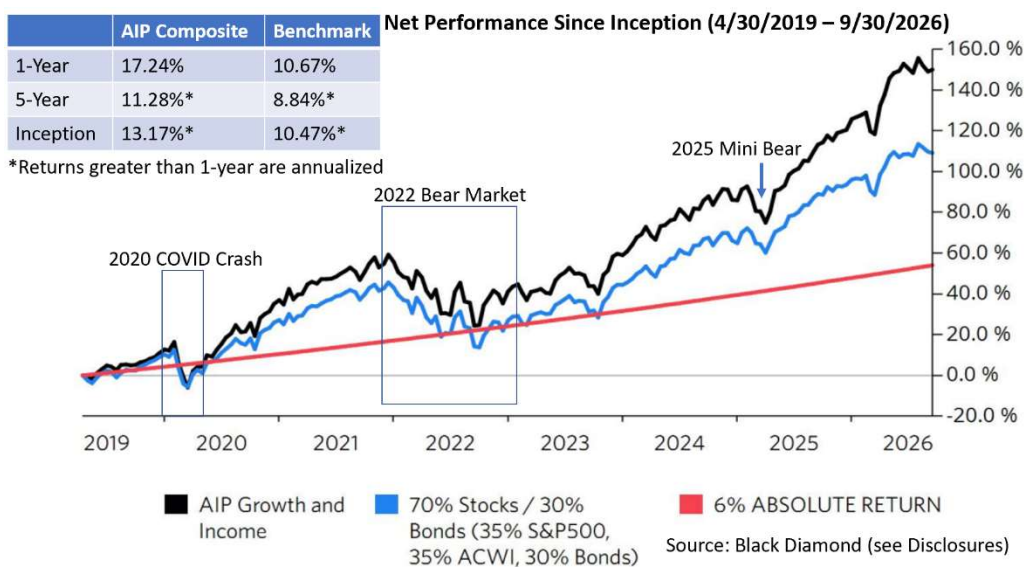
2. Current Conditions and Composite Performance

September was rough for most stocks as evidenced by the significantly worse performance from the equal-weight S&P500 index (RSP) compared to the cap-weighted version of the same index (SPY), which is concentrated in the Mag-7 leaders. The tech-heavy Nasdaq (QQQ) was a standout leader and the only gainer last month.

Year-to-date performance remains robust and most indexes are near all-time highs. The notable exception is bonds (AGG) that have struggled as yields rose to multi-decade highs. At this point, bond yields are attractive (10-year Treasury 5.2%, corporate bonds more than 6%). Higher yields dampen volatility for balanced accounts and may serve as an alternative to stocks should growth slow.



The chart below shows the net performance of our most popular composite since inception (120 accounts – see disclosures on page 4). The 7+ years shown have been volatile including COVID and the 2022 Bear market. Our strategy and discipline led to greater participation in gains than declines, allowing us to add value through this volatile time.



3. Indicators and Analysis

Investing can be an emotional roller coaster, leading to costly mistakes. To navigate effectively as we seek greater participation in advances than declines, we have found it helpful to monitor a series of indicators and models based on 3 key tenets — **Don't Fight the Fed, Don't Fight the Trend, Follow Sentiment Except at Extremes**. The tiles below summarize current conditions:



We evaluate market risk and return potential from a broad perspective, including a range of indicators, because markets are complex. Investors bid up stocks when they see legitimate reasons for long-term upside. Just as bull markets are born out of despair, bear markets develop on euphoria — and most are not event-driven.

Trend & Sentiment

Our indicators improved as markets churned over the last months. We continue to characterize our view as **cautiously optimistic** and although we see potential for further near-term volatility, we also see a rising probability of a year-end rally.

Trend strength remains bullish, but breadth deteriorated in September (more details on page 4). Earnings growth is impressive, and consolidation following a strong rally like we saw in Q2 tends to be healthy.

The breadth issue may be an early sign of a topping process, especially if the bull market reasserts itself while breadth remains weak. This would be especially **discouraging if we saw signs of a consumer slowdown and peak earnings growth**. For now, these are things to monitor, not worry about.

Despite August strength, **the stock market “wall of worry” remains intact**. The AAll sentiment survey (below) shows relatively few bulls relative to bears as investors ponder the prospects for the next 6 months. **Investor skepticism tends to limit drawdowns due to sidelined cash**.

Valuations, Seasonality & the Fed

Seasonality improves this month (especially late-October) but remains a headwind leading into the mid-terms. So far, seasonal weakness has impacted many stocks and sectors but has been more rotational than problematic for broad trends. This type of resilience is healthy.

Valuations remain a headwind for long-term investors. Earnings growth is impressive, but stocks are priced based on strong growth continuing for many years – a feat that would be unprecedented. This is unlikely to change for the foreseeable future. When valuations reflect strong expectations, **stocks can slide rather sharply on news that is less good than hoped**.

Rising interest rates and tighter monetary conditions are a risk. We think it was a mistake for the Fed to raise rates but we expect that they may tighten policy further in the coming months. **We think inflation may be peaking** – but will remain above 2% regardless of Fed actions. **Fed policy errors have a nasty tendency to lead to recessions**. We hope the Fed will proceed with caution, and we will watch closely and adapt our portfolio if needed.

What Direction Do AAll Members Feel The Stock Market Will Be In The Next 6 Months?

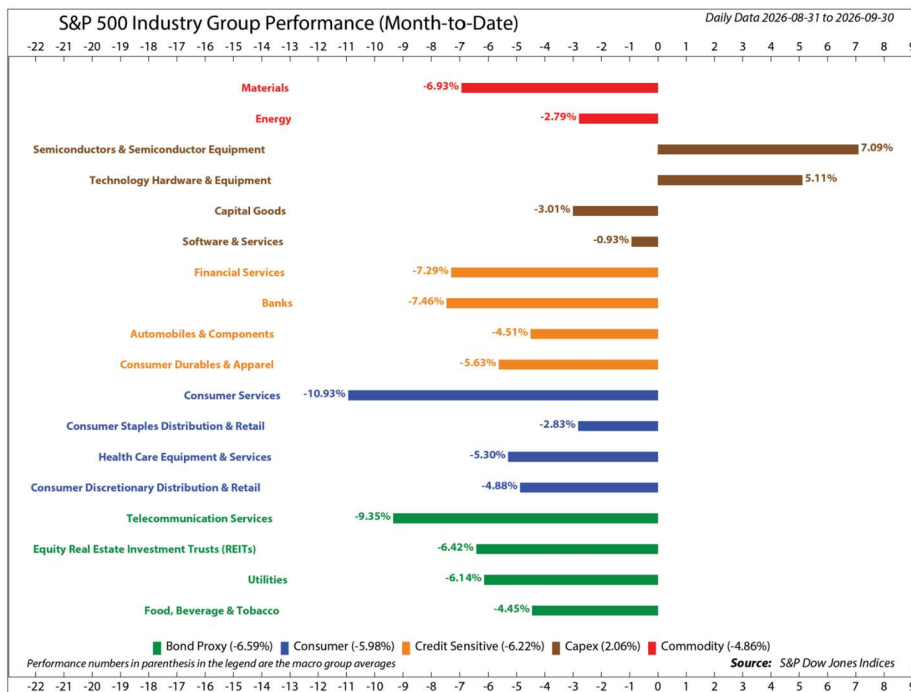


Source: AAll.com

4. Observations and Outlook

Our **Market Pulse** shows stocks in a **Bull (rising) market**. In a bull market, pullbacks and corrections tend to be relatively short-lived.

The chart below shows **most stocks/sectors struggled in September**, with the notable exceptions of semiconductors and tech hardware. Some of this reflects a rebound as tech leaders fell hard in the prior months as leadership “broadened” and value stocks surged. This rotation may have gotten extended and “corrected” itself in September. That’s the “bullish” interpretation. Some fear narrow leadership, but market indexes have tended to follow semiconductors over the past year (from a risk-on / risk-off perspective) so this could be a pre-cursor to broader gains – we’ll see.



Looking forward, **we expect the Q3 2026 consolidation will lead to a resumption of the bull market in the form of a year-end rally**. We don’t know the catalyst for this – it could be continued strong earnings or a resolution of the Iran war – or it could simply be relief after we clear the mid-term election and October Fed meeting.

We want to see more stocks gain should a year-end rally materialize. Market indexes are currently near highs, yet many stocks and sectors have entered downtrends. In a healthy bull market, a rising tide lifts all boats (or at least, most boats). At present, we’re not too concerned – but narrow leadership has historically preceded significant market tops so we will want to stay alert to that potential.

We look forward to your feedback, questions, and concerns.



Market Pulse

We try to avoid jargon, but a few terms are helpful when describing financial conditions.

Bull Market: markets trending up (higher highs on rallies, higher lows in declines). Expect periodic pullbacks and corrections – usually short and shallow – followed by resumption of the up-trend.

Consolidation: after strong gains or steep declines, markets sometimes become range-bound, moving up and down 3–5% over several weeks before the prior trend resumes.

Pullback: a decline of 3–5% that happens at least twice a year, typically resolving within a few weeks.

Correction: a decline of 5–10% that typically happens once a year, usually recovering within 3–6 months.

Bear Market: a decline of 20% or more. Most recover within 18–24 months, though severe ones (2000–03, 2007–09) can take 5–7 years or longer.

Bottoming Process: after a correction or bear market, stocks often bounce and re-test lows multiple times before recovering.

Quick Note — Required Minimum Distributions (RMDs) and other year-end considerations

Clients who need to pull RMDs will need to process these by year-end, and we encourage taking action in October or November. Many of our clients choose to reinvest the proceeds in a taxable account. Most direct some of their RMD direct tax payments. Some take advantage of Qualified Charitable Donations to reduce the taxable component of their RMD. If you have questions about any of these, please let us know. If you need to take an RMD this year and we don't hear from you by early November, we will reach out proactively. If we are unable to connect before mid-December, we will instruct your custodian to process the RMD by check to ensure that you don't miss the deadline. Q4 is a busy time for brokerages. If you have cash flow or other paperwork-intensive needs before year-end we encourage you to make requests early. Early communication also allows more time to consider alternatives that might offer tax savings or other advantages.

5. Closing Comments

Several clients have recently been speaking with friends who are looking to make a change, either because they are nearing a life transition or have been unhappy with their current advisor.

We appreciate your referrals and are pleased that our company continues to enjoy steady growth. Our focus is always on providing exceptional service and performance, and we are very grateful for your confidence and support!

Please call and/or email us personally for most of your account servicing needs — and especially when you have questions or concerns.



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Disclosures

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