

Rate noise, solid fundamentals

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The rise in long-term yields, driven by Fed policy, oil prices and debt issuance to finance AI infrastructure, has deprived portfolios of their traditional bond cushion.

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Growth remains robust, but persistent inflation is ruling out any near-term easing of policy rates.

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Earnings growth is broadening beyond large technology stocks and should help markets absorb the volatility surrounding the US midterm elections.

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September: tech and oil, the only exceptions

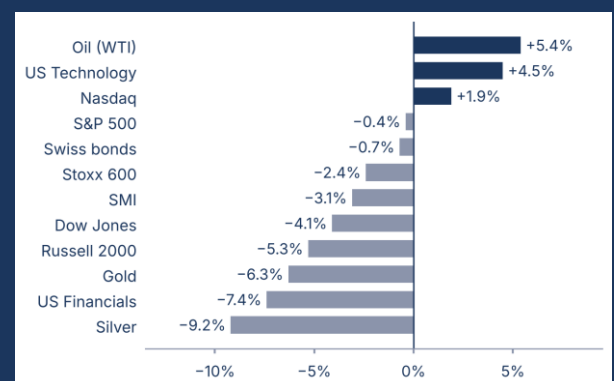
September lived up to its reputation as a volatile month, with two notable features this year: a strong downside correlation across asset classes, and extreme dispersion within equity markets. In the United States, the S&P 500 ended almost flat (-0.4%), supported by a handful of large technology stocks. Since the end of July, nearly 93% of its gains can be attributed to just five stocks, underscoring how concentrated performance has become. The Nasdaq gained 1.9% over the month, while the Dow Jones fell 4.1% and the Russell 2000 5.3%. Europe came under greater pressure, with the Stoxx 600 down 2.4%, the DAX -4.0%, the CAC 40 -4.2% and the SMI -3.1%. Year to date, however, the picture remains solid, with the S&P 500 up 12.7% and the Stoxx 600 up 10.2%.

Sector dispersion was extreme. In the United States, only technology (+4.5%) and communication services (+4.3%) posted gains, still driven by the artificial intelligence investment theme. By contrast, financials (-7.4%), materials (-6.8%) and real estate (-6.2%) fell sharply. Unsurprisingly, value lagged: the MSCI US Value index lost 2.0% while the MSCI US Growth index gained 1.3%. In Europe, where technology (+5.7%) and energy (+4.9%) were the only sectors in positive territory, value and growth declined in tandem.

The real shock, however, came from the bond market. The 10-year US Treasury yield jumped to 5.27%, up from 4.17% at the end of 2025, while the German Bund yield reached 3.58% (2.85% at end-2025). Three factors explain the move: the Federal Reserve, which raised rates and signalled further hikes; inflation concerns linked to oil; and the sheer scale of debt issuance to finance AI infrastructure. As a result, sovereign bonds in both the US and Europe, as well as credit, sold off. Only Swiss bonds held up relatively well (-0.7% for the Swiss Bond Index). For diversified portfolios, the month was therefore a difficult one: equities and bonds fell at the same time, depriving investors of their traditional cushion.

September: almost everything fell at the same time

Monthly performance, in %. Technology and oil were the only gainers.



Sources: Market data, Banque Heritage. Performance in local currency as at 30 September 2026.

Nor did gold play its safe-haven role: it fell 6.3% over the month to \$4,157 an ounce, weighed down by rising real yields and a firmer dollar, which gained 3.4% against the Swiss franc. Silver (-9.2%) and palladium (-11.5%) were hit even harder. Among commodities, only energy advanced: WTI crude rose 5.4% to \$90, and is up nearly 55% since January, against the backdrop of stalled talks between the United States and Iran. In a month when almost every asset class declined, technology and oil therefore stood out as the exceptions.

02

Robust growth, a headache for rates

The contrast with markets is quite stark. Despite the tightening of financial conditions recently initiated in the United States, economic data continue to point to robust activity. In the US, second-quarter growth was revised up to 2.2%, from a previous estimate of 1.5%. Consumption also remains on a solid footing, as illustrated by the 1.2% rise in retail sales in August, ahead of expectations. Business surveys confirm this momentum. In September, the US manufacturing PMI stood at 55.9 and the services PMI at 58.8, both well above the 50 threshold that separates expansion from contraction. According to S&P Global, these surveys are consistent with growth of around 4% in the third quarter, a trend also confirmed by the Atlanta Fed's GDPNow model, which currently estimates growth at 3.7%.

Europe is also showing signs of improvement. The eurozone manufacturing PMI stood at 52.9 in September, its highest level since May 2022, and the services PMI at 53.0, confirming a more broad-based expansion in activity. Germany is also showing signs of stabilisation, with the IFO index rising to 89.9 and the manufacturing PMI at 53.8. After several quarters of hesitant growth, European momentum therefore appears to be gradually recovering. The only cloud on the horizon is France, which is falling behind: its manufacturing PMI dropped to 50.3 in September, and it is expected to be the only major European economy to see its unemployment rate rise in 2026, to 8.6% by year-end.

In the US labour market, the slowdown continues, but it looks more like a normalisation than a deterioration. Monthly figures are volatile: after

rebounding to 162,000 new jobs in August, September added only 29,000, and successive revisions cloud the picture. The unemployment rate, which is more stable, has remained within a narrow range of 4.1% to 4.3% since March. The labour market is gradually returning to a more sustainable pace, without any abrupt break, while consumption and business surveys remain strong enough to absorb this moderation.

Finally, inflation remains the main area of concern. US consumer prices rose 3.4% year on year in August, while core inflation as measured by the PCE remains close to 3%, above the Fed's 2% target. PMI surveys also show that price pressures are intensifying in both the United States and Europe. It is precisely this combination of still-solid growth and inflation that is slow to converge towards central bank targets that keeps long-term rates under pressure. The macroeconomic scenario therefore remains supportive of activity, but considerably less comfortable for fixed income markets, in an environment where financing needs are becoming ever larger.

03

Fourth quarter: look through the noise, stay focused on fundamentals

Our year-end scenario remains constructive. Rates are high, but nominal growth is higher still: with nominal GDP growing at an annualised rate of more than 6.5% and the 10-year US Treasury yield at around 5.3%, the economy continues to generate income faster than its financing costs are rising. The rise in rates should also be put into perspective. Despite their increase since January, from 4.18% to 5.3% for the 10-year US yield and from 3.47% to 4.7% for the 2-year, they remain below their long-term averages (5.8% and 4.95% respectively). Above all, the situation bears no resemblance to the last episode in 2022. Back then, 10-year US Treasuries entered the rate-hiking cycle yielding just 1.75% and lost 13%, their worst year on record. Today, a starting yield of 4.2% provides a far better cushion against the shock. Carry has once again become a genuine buffer for portfolios.

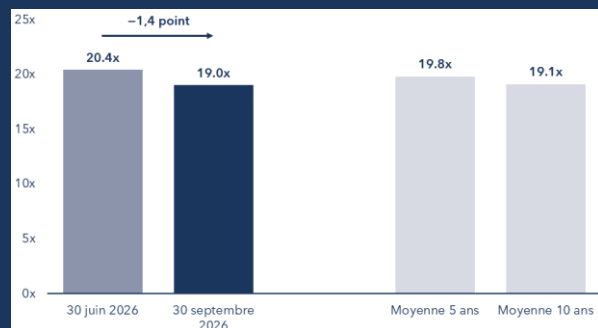
Corporate earnings remain our main source of support. According to FactSet, S&P 500 companies could report earnings growth of 29.5% for the third quarter, compared with 26.7% expected at the end of June: analysts raised their estimates during the quarter, which is unusual. Another encouraging sign is that earnings growth no longer rests solely on the large technology stocks: for the fourth quarter, analysts expect more growth from the other 493 companies in the index than from the "Magnificent Seven". Expected growth reaches 27.6% for the fourth quarter and 32.4% for 2026 as a whole. As long as earnings grow at this pace, they should be able to absorb higher financing costs. Third-quarter results, which begin in mid-October, will be a first test. We will remain attentive to dispersion: rate-sensitive sectors and the most heavily indebted companies remain the most exposed. Valuations, at around 20 times forward earnings for the S&P 500, also leave less margin for error, even though the index's gains this year have been driven entirely by earnings growth.

In the short term, the main cloud is political. The midterm elections on 3 November look set to be close, and markets dislike uncertainty: the weeks leading up to such votes are often turbulent, and a rise in volatility would not surprise us. History nevertheless counsels calm. These elections almost always have the same outcome: the president's party loses ground in Congress, as has been the case in the House of Representatives in nearly nine out of ten elections since 1914. The result is generally a more divided government and slower legislative activity. Paradoxically, this is good news for markets, which see it as reducing the risk of abrupt policy changes. Once the election is over, equities have almost always risen: the S&P 500 has gained after 23 of the last 25 midterm elections, with an average return of close to 20% over the following three quarters.

Past performance is of course no guarantee of future results, and every election has its own context. But history shows that political uncertainty tends to dissipate as quickly as it appears, with markets then refocusing on what really drives prices: earnings, growth and monetary policy. We therefore remain invested and vigilant. Should election-related volatility materialise, we would see it as an opportunity to add to quality positions rather than a reason to change our scenario.

Valuations back towards their average

12-month forward P/E ratio of the S&P 500. Expected earnings have grown faster than share prices.



Source: FactSet, Earnings Insight, 2 October 2026. Banque Heritage.