TRUST INVESTMENT SOLUTIONS

OUTLOOKS

September 2026

ECONOMIC OUTLOOK

Summary

Inflation as measured by the Consumer Price Index (CPI) eased from the energy-fueled spike earlier this summer, but the Federal Reserve is not treating that as much of a victory. Headline CPI rose 3.4% year-over-year through July, down from a 4.2% peak in May. Meanwhile, core CPI, which strips out food and energy, fell to 2.5%, matching its lowest reading since early 2021. At the Jackson Hole Economic Policy Symposium in late August, Fed Chair Kevin Warsh said that although the "… readings were better than expected, they do not tell me that underlying trends have meaningfully improved." With that, market participants went from largely dismissing a September rate hike to pricing in the possibility of one.

Part of what Warsh is seeing comes down to which inflation measure the Fed uses. It does not target CPI, but rather the Personal Consumption Expenditures Price Index (PCE), which tracks many of the same prices, just with different weightings. For example, housing carries roughly half as much weight in PCE as it does in CPI, so cooling rents have pulled CPI down more than PCE. By the Fed's preferred measure, inflation is still running at 3.7% year-over-year, or 3.3% excluding food and energy. At Jackson Hole, Warsh left no doubt that PCE is still the measure governing policy, and by that standard, inflation has been stuck above 3% all year long.

The labor side of the dual mandate is less of a concern for the Fed. Hiring rebounded in August after slowing the few months prior, and through both stretches, companies have held onto their workers. With weekly unemployment claims still near historic lows, we remain in a "low-hire, low-fire" employment environment.

Elsewhere the economy remains solid. ISM Manufacturing registered 54.6 in August, an eighth consecutive month of expansion. However, the survey's Prices Paid Index held at 71.1, a 23rd consecutive month of rising input costs, which ISM attributes to petroleum costs from the war in Iran, along with tariffs.

That leaves the question of what higher rates would accomplish. A rate hike would do little to relieve those pressures, since they come from the supply side rather than overheated consumer demand, but it would weigh on the parts of the economy that depend on borrowing. Additionally, a single quarter-point move would likely change little on its own. The Fed's counterargument is that inflation has run above target for more than five years and a central bank that keeps explaining away misses eventually loses credibility. For now, the economy is entering the fall in solid shape, with manufacturing expanding and layoffs scarce. The question doesn't appear to be whether growth holds up, but how long it takes prices to come down.

Positives

Durable goods orders rose 1.1% in July, double the 0.5% estimate

Import prices decelerated to 5.9% year-over-year, down from 7.1%

NFIB Small Business Optimism Index rose 2.4 points to 99.8, above the 97.5 estimate

Negatives

Retail sales fell 0.6% in July against a 0.1% gain expected

Real Average Hourly Earnings turned negative at -0.2% year-over-year

UofMich Consumer Sentiment Index fell to 51.7 in August from 55.2

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EQUITY OUTLOOK

Summary

The S&P 500 Index rose 2.7% in August and less than 2% below the all-time closing high achieved earlier in the month. Market strength for the month was fairly broad with most major global equity indexes advancing regardless of style, size or geography. The biggest directional drivers of the market have largely remained the same for many months. Bullish drivers are innovation and the artificial intelligence boom, reaccelerating earnings growth and generally healthy economic conditions. Bears typically focus on uncertainty around the war with Iran, tariffs and other geopolitical noise, and lofty equity valuations.

With midterm elections now just a few months away, capital markets are likely to experience some sort of reaction to the potential outcome. Volatility could be higher than usual as the balance of power appears to be shifting. Seasonality could also play a part as September has historically been a weaker month for equity markets.

The war in Iran continues to linger on and recent escalation has resulted in higher oil prices that have taxed the consumer. Prolonged consumer pressure may start to have a greater impact on earnings and the stock market. U.S. sanctions and blockades on Iran are inflicting a greater toll on their economy yet those pressures have so far failed to force the hand of Iranian leadership at the negotiating table. It is nearly impossible to predict how and when this conflict will end but it's highly likely to be impactful on equity markets.

Yet, with all this uncertainty, the stock market continues to make new highs. No, not every day but the S&P 500 closed at record highs 29 times in 2026. The momentum is clearly strong for equity markets. Second-quarter earnings season has all but wrapped up and it is hard to ignore the impressive results. Markets should continue to focus on fundamentals and ignore the noise, which should bode well for equity investors as we turn toward the final quarter of 2026.

Positives

Corporate earnings growth

Healthy labor markets

Negatives

Sticky inflation and uncertain oil prices

Elevated equity valuations

Unknowns

Midterm election

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OUTLOOKS

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FIXED INCOME OUTLOOK

Summary

The outlook for fixed income markets remained largely unchanged during August. The ongoing Iran-U.S. war continues to exert pressure on energy prices and therefore inflation, while the broader U.S. economy and labor market are healthy. Inflation is still higher than the Federal Reserve's 2% target, importuning the Fed to increase rates. The last time the Fed's preferred inflation measure of core Personal Consumption Expenditures Price Index (PCE) was at or below its 2% target was in March 2021. Although inflation is meaningfully lower today than its 2022 peak, some members of the Federal Open Market Committee (FOMC) are becoming increasingly perturbed that its 2% target has not been accomplished.

The FOMC did not have a meeting in August, but the Federal Reserve Bank of Kanas City hosted dozens of central bankers and policymakers at its annual Jackson Hole Economic Policy Symposium. It is tradition that the Federal Reserve Chair give the keynote speech and Kevin Warsh obliged, giving a 30-minute speech detailing his views on the economy and inflation. He explicitly stated the Fed has "work to do" if above target inflation persists. He also said, "I would be hard pressed to describe financial conditions as restrictive." Market participants reacted to Warsh's hawkish speech with Treasury yields moving sharply higher on the day. We believed it was unlikely the Fed would increase rates this year as elevated inflation is primarily being driven by an oil supply shock from the war. However, given the Fed's recent communication and tone shift, we believe the odds of a rate hike this year have increased meaningfully.

The investment-grade bond market broke another monthly record for the most issuance ever in the month of August with $163 billion of supply. This is the fourth month in which new issuance in the investment-grade market broke a monthly supply record. Issuance through August was $1.5 trillion and we forecast annual issuance will reach $2 trillion for the first time ever in 2026. Investment-grade bonds performed well during the month, and we anticipate credit spreads will remain tight throughout the rest of the year as strong corporate earnings more than offset the heavy bond issuance.

We continue to maintain a neutral duration policy and see a favorable risk/reward dynamic at the front of the yield curve.

Positives

Yields remain attractive relative to the past 20 years

Markets expect a Fed rate hike by year end, which may not occur

Robust second-quarter corporate earnings justify tight credit spreads

Negatives

GDP growth and the labor market remain resilient, keeping the Fed from lowering rates

Oil prices remain elevated as the U.S.-Iran war continues

Record investment-grade corporate bond issuance expected in 2026

Unknowns

Final resolution to the U.S.-Iran war