SMITH AFFILIATED CAPITAL

# September Investment Review 2026

## Competitive Yields Strengthen the Role of High-Quality Bonds

### Overview

September brought a sharp repricing of fixed income as rising energy costs, resilient economic activity, and renewed Federal Reserve tightening pushed yields higher. The pressure intensified in the second half of the month. Higher financing costs weighed on existing bonds and on parts of the equity market, while improving the income available to investors committing new capital. The central question became how much additional compensation was needed to hold longer-term assets amid persistent inflation and substantial borrowing needs.

Brent crude rose 14.41% during the month, and national average diesel prices peaked at $6.52 a gallon on September 21st. Higher diesel costs matter beyond the pump because they increase transportation and distribution expenses throughout the economy. Some energy prices subsequently eased, but Treasury yields continued rising. Strong business surveys released September 23rd reinforced expectations that growth remained firm, limiting confidence that inflation would quickly return to the Fed's 2% target.

| Macro View | MTD (%) | YTD (%) | 1Y (%) | 10Y (%) | 10Y STD (±) |
|---|---|---|---|---|---|
| DJIA | (4.12) | 7.19 | 11.50 | 13.09 | 15.24 |
| S&P 500 | (0.35) | 12.73 | 15.72 | 15.31 | 15.31 |
| NASDAQ | 1.93 | 16.09 | 19.26 | 18.65 | 18.72 |
| Equity EM Mkts. | (0.65) | 23.52 | 29.44 | 9.50 | 17.46 |
| EM Bond Mkt. | (2.91) | (1.51) | 0.86 | 2.76 | 7.27 |
| US High Yield | (2.52) | (0.00) | 1.36 | 4.93 | 7.14 |
| Commodity | 0.61 | 32.87 | 40.64 | 7.85 | 14.07 |
| COMEX Silver | (10.04) | (17.82) | 21.82 | 9.38 | 30.90 |
| COMEX Gold | (6.55) | (7.61) | 2.58 | 9.68 | 14.78 |
| BRENT OIL | 14.41 | 146.62 | 133.45 | 19.38 | 41.51 |
| Dollar Index | 2.03 | 3.18 | 3.76 | 6.27 | 6.50 |

The Fed raised its policy rate by 25 basis points (bps) in mid-September. Inflation data released at month-end offered qualified relief: August core PCE rose approximately 0.25% and stood at 3.0% year-over-year after revisions, while headline inflation was 3.4%. Methodological revisions accounted for part of the improvement. Second-quarter GDP growth was revised from 1.5% to 2.2%. These backward-looking releases did not yet capture September's energy shock, leaving the outlook dependent on its persistence.

### Taxable Markets

Bloomberg indexes recorded broad losses in September; the U.S. Aggregate Bond Index declined 2.61%, Treasuries lost 2.24%, corporates fell 2.72%, and agency mortgage-backed securities declined 3.38%. Among corporate sectors, financials fell 2.35%, industrials 2.87%, and utilities 3.11%. Their differing durations helped shape results; the utilities index carried substantially more interest-rate exposure than financials. Interest income cushioned losses but was insufficient to offset the price adjustment.

The Treasury curve shifted higher across maturities. In the month-over-month curve table, the 2-year yield rose 53 bps to 4.87%, the 5-year increased 58 bps to 5.07%, and the 10-year rose 53 bps to approximately 5.28%. The 30-year increased 39 bps to 5.63%. The 5-to-30-year spread narrowed from 75 to 56 bps: intermediate yields rose faster, reducing the extra yield earned by extending to the longest maturities.

The rise in nominal yields was accompanied by substantial real yields: the table showed approximately 2.70% at five years and 2.92% at ten years. Market-implied inflation compensation remained near 2.38% and 2.37%, respectively. This suggests that inflation expectations alone do not explain the level of Treasury yields; investors also require a meaningful return after inflation.

Shorter maturities offered greater price stability. Bloomberg's 1–3-year Treasury index lost 0.56%, compared with 1.53% for intermediate Treasuries. At month-end, these indexes yielded 4.86% and 5.00%, with durations of 1.85 and 3.49 years. The broader Aggregate yielded 5.56% with duration of 5.77 years, while corporates yielded 6.04% with duration of 6.41 years.

Credit spreads remained relatively restrained: Barclays' broad investment-grade credit index widened only two bps to 75. The selloff therefore reflected a substantial interest-rate adjustment rather than widespread corporate deterioration. Higher underlying yields strengthen the case for measured duration additions in quality bonds, while narrow spreads argue for selectivity in accepting additional credit risk.

| US Fixed Income | Price | Cpn | Total Returns (%) | | Dur | Yield |
|---|---|---|---|---|---|---|
| | (%) Rtn | (%) Rtn | Mo. | YTD | +/- | +/- |
| Agg. Bond | (2.97) | 0.34 | (2.61) | (2.91) | 5.77 | 5.56 |
| US Treasury | (2.55) | 0.3 | (2.24) | (2.77) | 5.54 | 5.13 |
| US Agency | (1.97) | 0.34 | (1.63) | (1.19) | 3.43 | 5.22 |
| Tax.Muni | (3.58) | 0.40 | (3.18) | (3.27) | 7.36 | 5.84 |
| Agency MBS | (3.79) | 0.41 | (3.38) | (3.31) | 5.90 | 5.95 |
| Gov/Credit | (2.74) | 0.34 | (2.40) | (2.85) | 5.79 | 5.44 |
| TIPs | (2.73) | 0.12 | (2.61) | (2.12) | 5.05 | 5.23 |
| Corporate | (3.13) | 0.41 | (2.72) | (3.11) | 6.41 | 6.04 |
| AAA Corp | (4.09) | 0.38 | (3.71) | (6.01) | 10.18 | 5.83 |
| AA Corp | (3.23) | 0.40 | (2.83) | (4.53) | 7.39 | 5.89 |
| A Corp | (3.14) | 0.40 | (2.74) | (3.24) | 6.36 | 5.91 |
| BBB Corp | (3.09) | 0.43 | (2.67) | (2.64) | 6.17 | 6.21 |

### Tax-Exempt Markets

Municipals faced both rising Treasury yields and heavier selling driven by issuance, fund redemptions, and tax-loss activity. Daily bid lists reached approximately $3.7 billion, among the largest recorded. The Bloomberg Municipal Aggregate Index declined 4.36% in September. General obligation bonds fell 4.22% and revenue bonds lost 4.43%. Within revenue sectors, housing declined 5.30% and

hospitals 5.12%, compared with 4.41% for transportation, 4.42% for water and sewer, and 4.12% for electric utilities. Duration and sector-specific risks both matter when interpreting these differences.

Curve positioning provided a clearer distinction. SAC's municipal benchmarks, the Bloomberg 3-year and 5-year GO indexes, declined 2.21% and 3.25%, respectively, less than the broad municipal market. The 1–2-year segment lost 1.15%, while the 15-year and 22-year-and-longer segments declined 5.00% and 5.66%. Short and intermediate positioning limited the damage, although no maturity segment was immune to September's adjustment.

| Municipal Market | Price | Cpn | Total Returns (%) | | Dur | Yield |
|---|---|---|---|---|---|---|
| | (%) Rtn | (%) Rtn | Mo. | YTD | +/- | +/- |
| Muni Agg | (4.74) | 0.38 | (4.36) | (4.18) | 7.01 | 4.78 |
| 1Y (1-2) | (1.52) | 0.37 | (1.15) | 0.54 | 1.30 | 3.89 |
| 3Y (2-4) | (2.57) | 0.37 | (2.21) | (1.00) | 2.52 | 3.87 |
| 5Y (4-6) | (3.60) | 0.36 | (3.25) | (2.84) | 3.95 | 4.02 |
| 7Y (6-8) | (4.19) | 0.37 | (3.82) | (3.87) | 5.13 | 4.37 |
| 10Y (8-12) | (4.79) | 0.36 | (4.43) | (5.04) | 6.52 | 4.64 |
| 15Y (12-17) | (5.38) | 0.37 | (5.00) | (6.15) | 8.24 | 5.04 |
| 30Y (22+) | (6.06) | 0.40 | (5.66) | (5.02) | 10.99 | 5.42 |
| AAA | (4.73) | 0.37 | (4.36) | (4.72) | 7.19 | 4.64 |
| AA | (4.66) | 0.38 | (4.28) | (4.19) | 6.92 | 4.69 |
| A | (4.85) | 0.38 | (4.47) | (3.90) | 6.94 | 4.97 |
| Gen. Oblig. | (4.59) | 0.37 | (4.22) | (4.40) | 6.81 | 4.60 |
| Revenue | (4.81) | 0.38 | (4.43) | (4.11) | 7.11 | 4.85 |

The resulting yields are highly competitive for investors in higher tax brackets. The 3-year GO benchmark yielded 3.87%, equivalent to 6.54% taxable, with duration of 2.52 years. The 5-year GO benchmark yielded 4.02%, or 6.79% taxable-equivalent, with duration of 3.95 years. These equivalents exceed the 5.33% yield on the Bloomberg 1–3-year credit index and the 5.73% yield on intermediate credit, respectively. The indexes differ in composition and duration, but the comparison demonstrates the strength of municipal income after federal taxes.

Tax-equivalent value depends on the investor's actual tax rate. At 40.8%, the 5-year GO benchmark's 4.02% yield compares favorably with the corporate index's 6.04%, even though the municipal benchmark carries considerably less duration. Individual bond selection remains essential because credit quality, call provisions and liquidity can materially change the comparison.

Further out the curve, the 10-year municipal segment yielded 4.64%, equivalent to 7.84% taxable, while the broad Municipal Aggregate offered 4.78%, or 8.07% taxable-equivalent. All equivalents use a 40.8% federal tax rate and exclude state-tax effects. They are yield comparisons, not forecasts of total return. Longer maturities provide additional income but also greater price sensitivity. We favor selective extensions within short and intermediate maturities, where attractive tax-exempt income can be secured without assuming the broad index's approximately seven-year duration.

## Equity Markets

September's equity results revealed increasingly narrow leadership. The Nasdaq gained 1.93%, while the S&P 500 declined 0.35% and the Dow lost 4.12%. Small caps reported a 5.25% decline in the Russell 2000 index. Global equities also weakened, with the MSCI World Index down 1.15%. Technology strength supported the major indexes while smaller companies and businesses sensitive to borrowing costs faced greater pressure.

Higher bond yields create more competition for equity capital and increase the earnings needed to justify stock valuations. AI investment remains an important growth driver, but the spending must ultimately translate into durable profits. October earnings will help clarify whether companies can maintain margins as energy and financing costs rise. We favor strong balance sheets, sustainable cash generation and diversification beyond the narrow group leading the market.

## Precious Metals and Digital Assets

Gold fell 6.55% and silver declined 10.04% during September, while the dollar index strengthened 2.03%. Gold ended near $4,157 an ounce. Higher longer-term yields increased the opportunity cost of holding metals that generate no income, and dollar strength added pressure. Geopolitical uncertainty continued to support gold's diversification role, but it did not prevent a substantial monthly decline.

Bitcoin ended near $83,621. The digital-market research reported an approximately 43% gain for the third quarter, supported by renewed demand through spot bitcoin funds. That quarterly result illustrates how investor flows can offset an unfavorable interest-rate backdrop. It does not establish digital assets as dependable protection against inflation or market losses. We continue to view such exposure as a modest, opportunistic allocation.

## Outlook

September's losses improved the prospective income available across high-quality fixed income. Municipal yields are particularly compelling for higher-bracket taxpayers, with the 3-year and 5-year GO benchmarks offering taxable-equivalent yields of approximately 6.5%–6.8% at moderate durations. This supports gradual reinvestment and selective extensions rather than relying entirely on cash.

The path ahead depends on energy costs, inflation and the economy's response to higher financing rates. Yields could rise further, but current income provides a stronger cushion for patient investors. Our priority is to improve compensation for risk while matching duration to cash needs, maintaining liquidity, and keeping capital preservation central to portfolio decisions.

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