

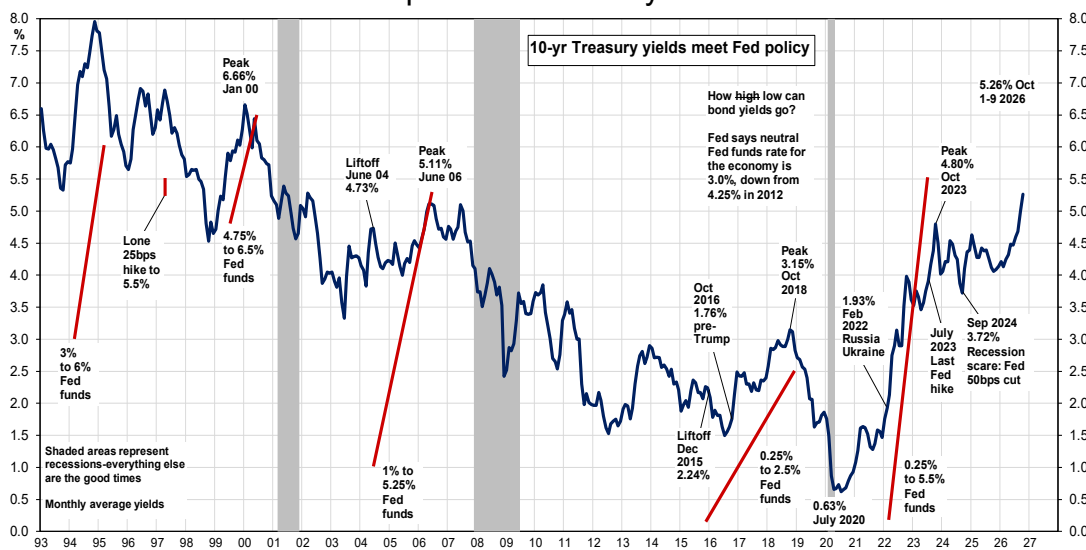
Financial Markets This Week

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BOND MARKET ROUT

There was volatility with some wide-daily trading ranges during the payroll jobs week. The headlines of bond yields hitting levels not seen in over two decades sound scarier than necessary. There has been a tendency for 10-yr Treasury yields to peak in an interest rate cycle at the final destination of the Fed policy rate. Bernanke's tightening to 5.25% before the 2007-09 recession saw 10-yr yields peak at 5.11% on a monthly average basis in June 2006 and hit 5.25% on the day of June 28. Finding value in 10-yr Treasury purchases can also be measured against inflation. Headline inflation comes and goes, but core consumer inflation seems good enough for an historical valuation that can never be done with rocket-science precision unless you hold a CFA.

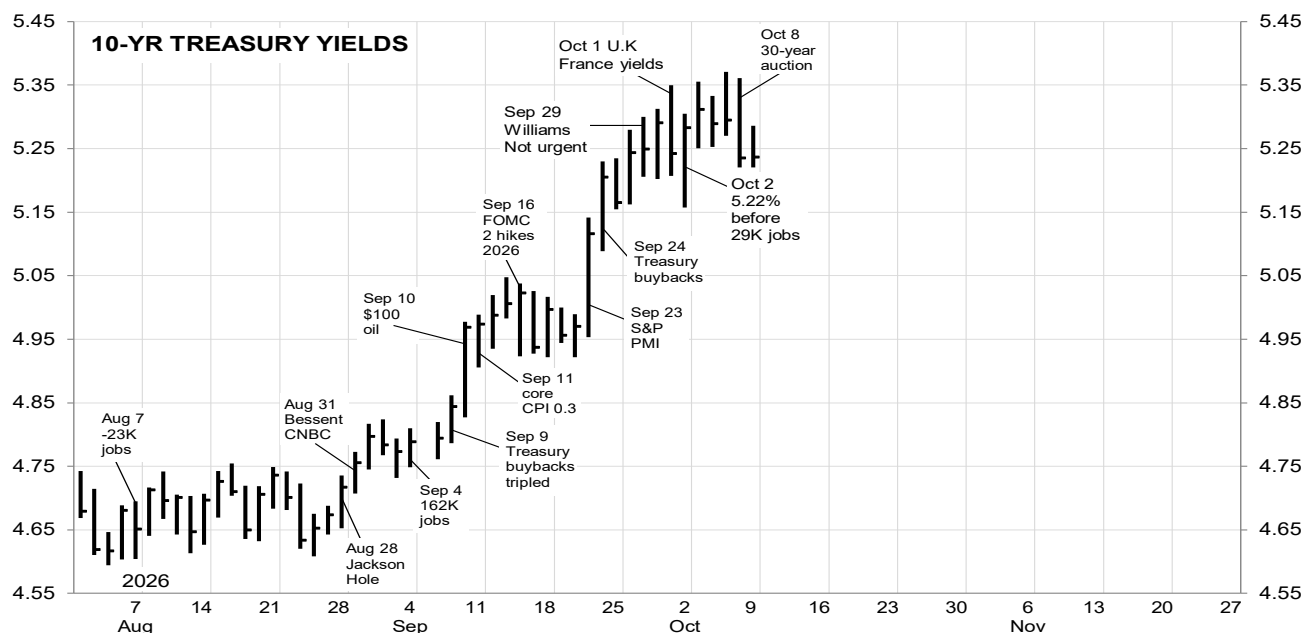


August year-year inflation changes for core PCE is 3.0% and core CPI is 2.4%. Pick your choice of poison before [Warsh's book-club study group](#) makes its recommendations. But not for anything, there is real yield pickup for long-term bond investors over core inflation buying 10-yr yields above 5%. There are fiscal spending and debt worries around the world, but the failure of Trump 2.0 to rein in spending so far is not enough to justify a greater yield cushion for US Treasuries at this point, with the final FY 2026 Federal budget deficit results (with September data) just hours away. The inflation fight has some credibility issues as the definition is haywire with CPI inflation below PCE inflation so far in 2026. There's still too much of it for policymakers and don't ask the public. To conclude, there is value for long-term holders as 10-yr yields return to the 5.5% Fed peak of July 2023. Once the geopolitical risks moderate and energy prices fall, speculators may find value in bonds at current yield levels.

%	Core CPI	Core PCE	Diff
1992	3.7	3.0	0.7
1993	3.3	2.7	0.6
1994	2.8	2.2	0.6
1995	3.0	2.2	0.8
1996	2.7	1.9	0.8
1997	2.4	1.8	0.6
1998	2.3	1.3	1.0
1999	2.1	1.3	0.8
2000	2.4	1.8	0.6
2001	2.6	1.9	0.7
2002	2.4	1.7	0.7
2003	1.4	1.6	-0.2
2004	1.8	2.0	-0.2
2005	2.2	2.2	0.0
2006	2.5	2.4	0.1
2007	2.3	2.2	0.1
2008	2.3	2.0	0.3
2009	1.7	0.9	0.8
2010	1.0	1.4	-0.4
2011	1.7	1.6	0.1
2012	2.1	1.9	0.2
2013	1.8	1.5	0.3
2014	1.7	1.5	0.2
2015	1.8	1.2	0.6
2016	2.2	1.6	0.6
2017	1.8	1.6	0.2
2018	2.1	1.9	0.2
2019	2.2	1.6	0.6
2020	1.7	1.4	0.3
2021	3.6	3.5	0.1
2022	6.2	5.4	0.8
2023	4.8	4.2	0.6
2024	3.4	2.9	0.5
2025	2.8	2.8	0.0
2026	2.6	3.0	-0.4

2026-to August

INTEREST RATES

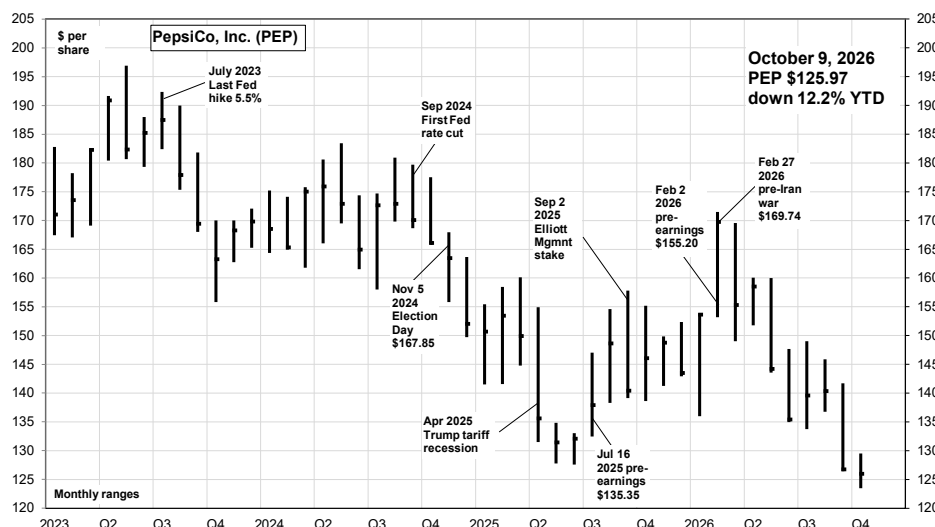


Fiscal concerns in Europe, France and UK mostly, keeps the push on 10-yr US Treasury yields again this week. The debt time bomb worries of \$40 trillion in US debt outstanding (just \$28.9 trillion for marketable T-bills, notes and Government bonds) did not stop investors from buying 10-yr notes auctioned Wednesday, and 30-yr bonds on Thursday. The Treasury did do \$6 billion of buybacks of 20Y to 30Y long debt Thursday, purchasing mostly 30-yr bonds, one issued in 2019 and another in 2021 in an operation done between 140pm and 200pm, after the strong 30-yr auction results were known. For stocks it was Tech or at least Nvidia new record highs early in the week moving the [S&P 500 to a new closing record](#) Tuesday up 14.2% YTD. The previous high was way back on August 13, closing up 13.9% YTD. CPI is back, September core expected at 0.2% Wednesday, October 14.

PepsiCo, Inc. (PEP) down 12.2 YTD

Pepsi rallied 3.7% to \$128.34 Thursday after earnings in the morning, rallied from the 2026 low. It could have been worse perhaps with the company cutting full-year guidance. The stock closed under \$150 back on May 11 with the rest of consumer staples (XLP) selling off. The war restart and higher gas prices have sent PEP and XLP lower since a relatively recent August 24 high. There are cost cuts coming but the company says it is experiencing higher input costs, and even said GLP-1 weight-loss drugs could affect demand for its snacks and beverages. Dividend is 4.7%.

S&P 500 Weights	
Top 7: 35% of S&P	
8.34	NVIDIA
7.43	AAPL
5.80	MSFT
3.73	AMZN
3.06	GOOGL
2.56	Broadcom
2.45	GOOG
2.38	Meta

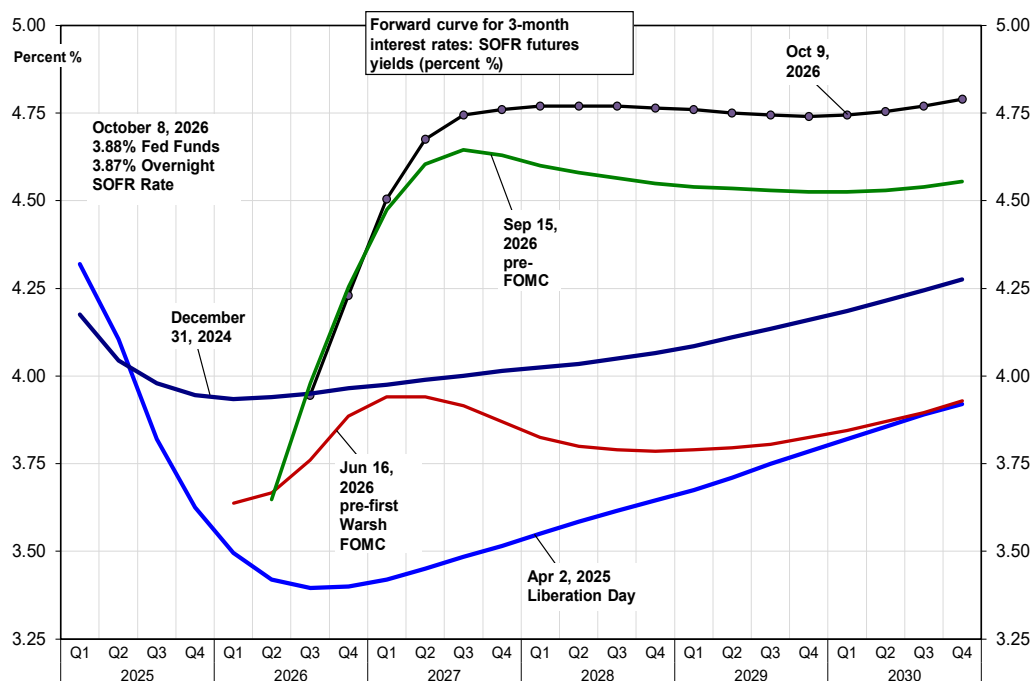


FEDERAL RESERVE POLICY

The Fed meets October 27-28, 2026 to consider its monetary policy. [Fed governor Waller](#) gave the market some guidance Thursday about more rate hikes being needed to bring inflation down more quickly to target, and he seems to be flexible on a date, and perhaps the two more hikes that are needed are consistent with the 8 out of 18 Fed participants forecasting a 4.5% Fed funds rate at the end of 2027. He almost made it sound like rates could go even higher next year before changing into rate cuts by year end. We are not sure what happened with the long-held Warsh belief that Fed officials talk too much. Waller gave his own view on “communications” which sounds little different than the good old pre-Wash days. He does not think policymakers should be locked into any specific guidance on the path of rates or forecasts that they give. Well, then just change the forecast would be our thought if circumstances change. Come to think of it, Waller’s speech on “The Signaling Value of the Summary of Economic Projections” in Turkey this week could have been an attempt to [stop its elimination](#) under the new Warsh Administration.

Selected Fed assets and liabilities						Change from 3/11/20 to Oct 7
Fed H.4.1 statistical release	7-Oct	30-Sep	23-Sep	16-Sep	3/11/20*	
billions, Wednesday data						
Factors adding reserves						
U.S. Treasury securities	4566.384	4564.161	4558.332	4554.450	2523.031	2043.353
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	1898.089	1898.089	1910.409	1913.523	1371.846	526.243
Repurchase agreements	0.002	1.200	0.001	0.255	242.375	-242.373
Primary credit (Discount Window)	9.965	8.738	6.235	6.879	0.011	9.954
Bank Term Funding Program	0.000	0.000	0.000	0.000		
FDIC Loans to banks via Fed	0.000	0.000	0.000	0.000		
Paycheck Protection Facility	0.007	0.007	0.015	0.016		
Main Street Lending Program	0.873	0.872	0.872	0.871		
Term Asset-Backed Facility (TALF II)	0.000	0.000	0.000	0.000		
Gold stock	11.041	11.041	11.041	11.041	11.041	0.000
Central bank liquidity swaps	0.207	0.207	0.072	0.094	0.058	0.149
Federal Reserve Total Assets	6799.4	6794.9	6795.5	6798.3	4360.0	2439.364
3-month Libor-% SOFR %	3.88	3.90	3.87	3.62	1.15	2.730
Factors draining reserves						
Currency in circulation	2486.120	2482.756	2482.383	2483.040	1818.957	667.163
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	885.783	984.046	947.317	991.708	372.337	513.446
Treasury credit facilities contribution	0.000	0.000	0.000	0.000		
Reverse repurchases w/others	2.338	11.539	0.461	5.375	1.325	1.013
Federal Reserve Liabilities	3777.324	3913.200	3829.614	3876.772	2580.036	1197.288
Reserve Balances (Net Liquidity)	3022.066	2881.686	2969.922	2921.536	1779.990	1242.076
Treasuries within 15 days	102.162	107.411	131.913	140.626	21.427	80.735
Treasuries 16 to 90 days	394.160	372.603	368.918	360.938	221.961	172.199
Treasuries 91 days to 1 year	526.600	540.933	531.946	527.324	378.403	148.197
Treasuries over 1-yr to 5 years	1436.121	1436.000	1426.912	1426.916	915.101	521.020
Treasuries over 5-yr to 10 years	482.130	482.108	473.532	473.533	327.906	154.224
Treasuries over 10-years	1625.211	1625.107	1625.110	1625.114	658.232	966.979
Note: QT starts June 1, 2022	Change	10/7/2026	6/1/2022			
U.S. Treasury securities	-1204.395	4566.384	5770.779			
Mortgage-backed securities (MBS)	-809.357	1898.089	2707.446			
**March 11, 2020 start of coronavirus lockdown of country						

Fed Policy-key variables					Long Term
	2026	2027	2028	2029	
Fed funds	4.1	4.1	3.9	3.6	3.2
PCE inflation	3.7	2.3	2.1	2.0	2.0
Core inflation	3.4	2.5	2.2	2.0	
Unemployed	4.1	4.1	4.1	4.1	4.2
GDP	2.3	2.4	2.2	2.1	2.0
September 2026 median Fed forecasts					



Just 4.5 bps of a 25 bps rate hike is discounted at the October meeting.

Fed funds futures call Fed policy

Current target: Oct 9 -- 4.00%

Rate+0.12 Contract	Fed decision dates
4.045 Nov 2026	Oct 28
4.260 Jan 2027	Adds Dec 9*
4.350 Feb 2027	Adds Jan 27
4.530 Apr 2027	Adds Mar 17*
*Jan 2027 could be 4 days at a new rate	
*Apr 2027 could be 2 days at a new rate	

Next up: September CPI inflation Wednesday, October 14 830am ET

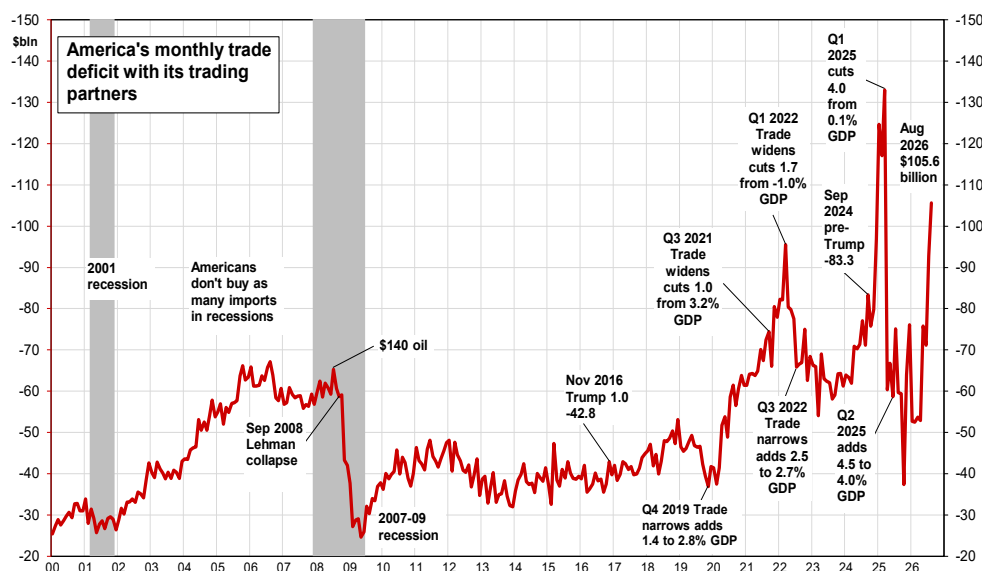
Monthly % Changes	2026				2025											
	Aug	Jul	Jun	May	Apr	Mar	Feb	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun	
Core CPI inflation	0.3	0.2	0.0	0.2	0.4	0.2	0.2	0.3	0.2	na	na	0.2	0.3	0.3	0.2	
Core PCE inflation	0.2	0.1	0.1	0.3	0.3	0.3	0.3	0.4	0.3	0.2	0.2	0.2	0.2	0.2	0.3	
Core PCE YOY	3.0	3.0	3.0	3.2	3.1	3.1	3.0	2.9	2.9	2.7	2.7	2.8	2.9	2.8	2.8	
Core CPI YOY	2.4	2.5	2.6	2.8	2.7	2.6	2.5	2.5	2.6	2.6	na	3.0	3.1	3.1	2.9	

OTHER ECONOMIC NEWS

More trade deficit red ink (Tuesday)

Breaking economy news. The trade deficit jumped to \$105.6 billion in August and the July data were revised sharply higher as well to \$92.8 billion from the \$88.6 billion preliminary figure. The increase in the trade deficit will be a drag on real GDP growth in Q3 2026, but it is likely to end up in inventories which adds to real GDP. It is notable that the imports from

China have shrunk over time with imports from Taiwan and Vietnam of similar magnitude this year. China imports peaked at \$538.5 billion in 2018.



Net, net, the international trade deficit literally exploded this month back to worrisome triple digit levels which will take a toll on economic growth this quarter as the goods are not being produced here domestically. Despite the Administration's economic policies which have jacked up the tariff-related costs of many imported goods, America is just as dependent as ever on foreign produced goods as there is no good alternative. Despite all the campaign rhetoric, the trade deficit was \$79.8 billion when the President was elected in November 2024 and it is \$105.6 billion in August 2026 which means the Administration's trade policies have largely been a failure, there can be no other conclusion, trade tariffs have done nothing to reduce America's reliance on the import of foreign-produced goods. The cost of American labor is simply too high to produce goods here cheap enough for consumers to even think about purchasing. Even if US manufacturers were willing, the factories could not be built here fast enough to produce the goods that US consumers depend on. At the moment the only major manufacturing plant construction is in data centers and in a few scattered auto production facilities trying to evade the Trump 2.0 tariffs. Stay tuned.

Top US Trade Partners for Goods 2026 August YTD			
\$ billions	Exports	Imports	X-M
Mexico	263.5	419.3	-155.8
Canada	236.0	269.6	-33.6
China	73.9	183.5	-109.6
Taiwan	39.3	186.9	-147.6
Vietnam	12.2	176.1	-163.9
S. Korea	55.0	110.1	-55.1
Japan	66.7	96.5	-29.8
Germany	57.9	100.6	-42.7
Total	1,641.3	2,415.2	-773.9

\$mIn	Trade balance			Exports			Imports		
	Total	Goods	Services	Total	Goods	Services	Total	Goods	Services
Jul 2026	-92,826	-123,809	30,982	310,723	201,245	109,479	403,550	325,053	78,497
Aug 2026	-105,572	-136,572	31,000	315,182	205,660	109,522	420,754	342,232	78,522
Change	-12,746	-12,763	18	4,459	4,415	43	17,204	17,179	25

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