

Quarterly Commentary

Q3 2026

REWIND

We entered Q3 on a wave of optimism following the announcement of a potential peace deal between the U.S. and Iran, and with resurgent enthusiasm for the Artificial Intelligence (AI) trade — as well as the capital spending driving it. We leave Q3 having witnessed an all-but-complete breakdown of diplomacy between the U.S and Iran, oil trading above $100 USD per barrel, AI companies calling for regulation of their own technologies, and central banks being forced to hit the rewind button on interest rates.

Geopolitical headlines and thematic market movements have been in ample supply in 2026, yet the third quarter saw the convergence of these themes play out in a single arena — the bond market.

Collectively, long-term government bond yields in the U.S., Canada, and various markets across Europe and Asia, moved sharply higher in Q3, ultimately reaching levels not seen since before the 2008 Financial Crisis. In Japan, the move was even more notable, with yields rising to nearly thirty-year highs. While much of the focus during the quarter was on long-term bonds, short- and medium-term yields pushed higher, too, responding to myriad forces that have increasingly prompted bond investors to reassess what the appropriate level for the cost of capital really is.

Much of the increased volatility can be attributed to the ongoing conflict in the Middle East. Energy prices are a critical driver of inflation, and the disruption of supply associated with the closure of the Strait of Hormuz has pushed prices higher globally. The collapse of a potential peace deal and the return to active conflict between the U.S. and Iran during the quarter reduced the hope for an imminent normalization of supplies, forcing oil prices to trade back above $100-per-barrel. Meanwhile, rising tensions across the region added to the stress. Saudi Arabia's East-West pipeline, which has emerged as a critical workaround for Gulf oil to access markets via the Red Sea, was forced to shut-down in September following a drone attack by the Iran-backed Yemeni Houthis.

More notable from an inflationary perspective, however, were the significant moves in refined-product prices. Wholesale diesel prices and other fuels rallied much harder than oil prices during Q3, as Ukrainian attacks on Russian refining infrastructure, and reduced refining activity in China, exacerbated the already significant disruptions stemming from the onset of hostilities in the Persian Gulf. Prices of diesel moved to record levels across multiple regions, rising to nearly double pre-war levels. In the face of supply shortages, and with inventories running low, multiple nations moved to implement export controls on diesel to help safeguard supplies, further exacerbating price movements.

With diesel being the primary fuel of industry and trade, elevated prices risk inflation spilling over more readily into the prices of goods and services globally. These forms of inflation are stickier than energy prices themselves, and could therefore pose a more significant challenge to the interest rate outlook going forward.

Indeed, inflation has once again returned to the forefront of central bank policy decisions. The U.S. Federal Reserve raised interest rates for the first time in three years on September 16th, citing too-high inflation as the primary motivator. The European Central Bank and the Bank of Japan also raised rates in September, while commentary from others, including the Bank of England and the Bank of Canada, signaled rate hikes could be on the horizon if inflationary pressures don't abate.

And yet, bond yields are no longer being driven by expectations for central bank policy alone.

In the post-COVID era, the world has moved firmly into an environment dominated by fiscal policy. Shifting geopolitical dynamics and rising trade tensions have pushed countries to spend more to support social needs, reconfigure supply chains, expand defence capabilities, and seek strategic autonomy. Fiscal deficits have expanded in response, and the acceleration of debt accumulation in the 2020s has been notable. The global public debt-to-GDP ratio rose to 94% in 2025 from 84% in 2019, and is projected to reach 100% by 2029, according to data from the IMF (International Monetary Fund). Total U.S. Government debt crossed the $40 trillion mark in August. A 1% increase in the average interest rate on that debt would eventually translate into an additional ~$400 billion of annual interest expense for the U.S. Government. The U.S. is not alone on this front. The average debt carried by G7 nations is approximately 126% of GDP, with the U.S. at ~121%.

At the same time, Government bonds are facing growing competition from corporate issuers too — most significantly, AI hyperscalers (Alphabet, Amazon, Meta, Microsoft and Oracle). These large, highly credit-worthy technology companies are increasingly issuing debt to fund expanding capital programs focused on the buildout of AI infrastructure. They have also issued considerable amounts of long-term debt, encroaching on a corner of the market traditionally dominated by governments, and offering conventional buyers of 30-year government bonds an alternative option. Of the total bond issuance from the hyperscalers in 2025-2026, approximately 41% has been issued for terms exceeding fifteen years, compared to just ~16% for the broader U.S. corporate market.

Together, more bonds from both governments and corporations means higher competition for investors' capital. More spending and higher interest rates may also translate into increased risk issuers struggle to service that debt in the future. The longer the duration of the bond, the longer investors are exposed to that risk, necessitating higher yields to compensate. Add-in inflation, changing geopolitical dynamics, increasingly protectionist policy, and limited political will to balance budgets, and investors are repricing bond yields for an environment where interest rates settle at structurally higher rates.

Importantly, however, policymakers are not signaling a return to the aggressive tightening cycle of 2022 and 2023. Rather, they are adjusting rates to changing macroeconomic conditions, aiming to ensure they are appropriately restrictive for the current environment. It is also important not to view current rates in isolation. There is little doubt our perspective on interest rates has been skewed by recency bias following the very abnormal decade of near-zero rates following the Financial Crisis. At the time of writing (October 1st), the U.S. 10-year treasury yield is trading at ~5.2%. According to the St Louis Fed, the average 10-year yield, from 1953 to present, is approximately 5.8-6%.

Higher rates pose a potential headwind to household balance sheets and corporate profits, though, as the past several years illustrate, they are not the only determinant.

Energy prices remain the most critical factor driving the near-term path for inflation and interest rates. A resolution to the Middle Eastern conflict would provide welcome relief to the recent pressure on both metrics. Nonetheless, in an environment where the U.S. and global economies broadly continue to perform well, consumers remain resilient despite higher inflation, and corporate earnings remain remarkably strong, higher interest rates are likely appropriate. Being only several years past the zero-interest-rate era, markets remain in a recalibration phase. As our view of 'normal' adjusts to a very different world, so too must the cost of capital.

PICKING FRIENDS

Leading into 2026, we predicted rhetoric from the U.S. administration in the leadup to the renegotiation of the Canada-U.S.-Mexico Agreement (CUSMA) would be loud and blustery, but were hopeful the relationship between Canada and the U.S. would settle — even if not completely normalize — under a successful extension of the deal. It is safe to say things have evolved very differently. Although CUSMA continues to operate under a now-annual review process, the relationship between our two countries deteriorated significantly in Q3.

On August 22nd, President Trump imposed new 50 percent tariffs on approximately $20 billion of Canadian imports after last-minute changes by the U.S. administration caused negotiations on a revised trade agreement to collapse. The levies targeted dairy, alcohol, lumber, electronics, apparel, and building materials. President Trump later banned imports of Canadian motorcycles, alcohol, and certain dairy products — representing another $1 billion of goods. Finally, he announced existing tariffs on autos and steel would double to 50 percent on January 1st, while new tariffs would be applied to auto parts. Canada responded with tariffs of its own on approximately $20 billion of U.S. goods, which took effect September 8th.

Though $21 billion is relatively minor in terms of total Canadian exports to the U.S. (about 3% 2025's total), these developments are unfortunate and will have considerable impacts on businesses operating within these sectors. Moreover, they further underscore the erratic policy shifts common to the current U.S. administration, and the very real challenge Canada faces navigating the changing dynamics of this critically important relationship.

In stark contrast to the negative tone set by Canada-U.S. relations during the quarter, the actions taken by Prime Minister Mark Carney's government to improve Canada's business and investment landscape were highly encouraging. On September 14-15th, Canada held its first ever 'Canada Investment Summit', an event which brought together major global institutional investors, sovereign wealth funds, and business executives to showcase Canadian business and investment opportunities. During the event, Prime Minister Carney announced nearly $500 billion in new investment commitments for Canada, including nearly $100 billion from Canadian pension funds, insurers, and institutional investors, more than $325 billion in financing commitments from Canada's major banks, and billions more for infrastructure, artificial intelligence, energy, critical minerals, and other strategic industries. In a move widely applauded for its potential to improve Canada's competitiveness in attracting capital, Prime Minister Carney also announced the so-called Productivity Mega Deduction — effectively a tax incentive which allows for accelerated deduction of eligible capital costs, which could push the marginal tax rate on new business investment to as low as 6.4% from 13%; the lowest in the G7.

Both the Summit and the Mega Deduction are part of the federal government's broader goal of promoting $1 trillion of new investment in Canada, all with a focus on improving long-term economic growth, productivity, and global competitiveness.

Prime Minister Carney also sped-up efforts to diversify the country's trade relationships,

announcing Canada would become the first 'Associate Member' of the European Union (EU). Though the particulars of new membership status remain somewhat undefined, the intent is quite clear: In the face of changing trade balances and global geopolitical orders, both countries are seeking reliable partners to support future economic growth and safeguard against evolving threats. In practical terms, the membership represents a commitment to a broader partnership focused on trade, defence cooperation, improved supply chains, critical minerals, space and scientific research. Indeed, Canada has already become the only non-EU country participating in the bloc's €150 billion SAFE defence procurement program.

Though much work lies ahead – both in changing the economic trajectory of our country, and in the management of our relationship with our closest neighbour – it is refreshing to see meaningful, concerted efforts being made to promote our resources and improve the economic competitiveness of our great country.

MARKET PERFORMANCE

Global equities continued to march higher in Q3 despite an ever-challenging macroeconomic backdrop. Strong corporate earnings and continued enthusiasm surrounding AI ultimately outweighed concerns over the ongoing Middle Eastern conflict, inflationary pressures, and rising long-term interest rates.

In the U.S., economic growth remained resilient and corporate profitability exceeded expectations in Q3. Approximately 85% of S&P 500 companies beat earnings estimates during the quarter, with reported profits rising over 30%. The S&P 500 Index reached new all-time highs during the quarter, finishing up 2.5%. Though volatility continued in the face of ever-shifting momentum in the AI race, and despite questions about future returns on staggering capital investments, the tech-heavy NASDAQ posted a 3.3% return over the quarter. The improvement in earnings has helped valuations fall, as measured by the price-to-earnings (PE) ratio, with the forward PE of the S&P500 hovering around 19.4x as of August 31st, down from 22x at the start of the year.

Canadian equities remained resilient in Q3 despite escalating trade tensions with the U.S. The S&P/TSX Composite Index posted a 1.6% return over the quarter, with continued resilience in financials, industrials, materials and select information technology names. Sentiment also improved following the inaugural Canada Investment Summit and expanded ties with the EU. Energy stocks benefited from a rebound in oil prices late in the quarter amid renewed Middle East supply concerns, while financials continued to provide the foundation for market performance as Canadian banks demonstrated strong earnings, healthy credit quality, and growing wealth management revenues.

Outside of North America, International markets were mixed. The broad MSCI EAFE Index was positive on the quarter, returning 1.0%. Many international markets were supported by strong earnings growth, with beneficiaries from AI spending contributing to stronger performance in certain regions. At the same time, heavily concentrated AI markets, such as South Korea, returned to earth following a meteoric rise in the first half of the year. South Korea's KOSPI Index suffered a dramatic selloff in July as foreign investors took profits on chip stocks, SK Hynix and Samsung, which together make up over 50% of the index. The KOSPI finished down 19.1% on the quarter (though, remains up 62.3% year-to-date).

European equities proved reasonably resilient despite volatility brought on by rising yields, higher energy prices, a rate hike from the European Central Bank, and internal political unrest in the UK, France and Germany. All told, European equities, as measured by the MSCI Europe Index, finished the quarter down 0.1%.

Fixed Income headwinds ramped up in Q3 as rising energy and refined-product prices stemming from the ongoing conflict in Iran brought about renewed concerns over the path

for inflation and interest rates. Bond yields moved higher as persistent inflation pressures, a strong economic backdrop, a surge in bond issuance from tech companies, and questions around the sustainability of government debt prompted investors to demand higher returns on borrowed capital. In September, the Federal Reserve (the Fed) delivered its first-rate increase since September 2023, with Chairman Kevin Warsh emphasizing the Board's resolve to return inflation to the 2% target. Despite the 25 basis-point hike, the U.S. 10-year Treasury Yield continued to trade above the psychologically important 5% barrier, with the market pricing-in at least one additional rate hike prior to year-end. Bond yields in Europe and Asia moved notably higher too, with long-term yields in the UK, France, Germany and Japan facing pressure from internal political dynamics raising concerns around future spending. Overall, the upward movement in rates weighed on bond prices during the quarter, resulting in fixed income lagging equities considerably. Though volatility is likely to remain, higher yields are once again creating attractive income opportunities for long-term investors.

Year-to-Date Market Performance (Local Currency, Total Returns)

S&P/TSX Composite Index: 13.0%

S&P 500: 12.8%

NASDAQ: 16.1%

Euro Stoxx 50: 11.1%

Japan Nikkei 225: 34.6%

Shanghai Stock Exchange (SSE) Composite: -1.4%

Data: FactSet as of September 30, 2026

A NOTE ON Q4

The final quarter of the year can often bring volatility as investors complete portfolio rebalancing, tax-loss harvesting, and profit taking. Seasonal weakness can be even more pronounced during mid-term election years in the U.S. Historically, these years have proven to be the weakest of the four-year Presidential cycle. Market volatility has a history of peaking immediately before the election as investors prepare for uncertainty. Given the current political backdrop in the U.S., polling suggests uncertainty leading into the 2026 mid-terms may be higher than usual. However, history has also shown election-related volatility is generally short-lived, typically returning to normal levels shortly after election day.

As always, our goal at GUWM is to build durable client portfolios that perform well in a range of conditions. We remain focused on quality companies, true diversification, and continue to overweight strategies that have historically reduced volatility and provided downside protection, while also capturing upside opportunity. Though we remain active in our positioning, we will continue to look through the noise and focus on the long-term objectives of our clients.

The Griffiths Underdahl Wealth Management team would like to thank you for your business and continued trust in our team. We look forward to continuing to work with you and your family as we help navigate your financial journey with deep knowledge, diverse experience, and commitment on your side. If you have any questions or issues you would like to discuss, we would be happy to receive your call.

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