

Why higher yields are hurting everything except AI

Saxo Bank · 2026-10-05 · English original

Key points:

- The S&P 500 is hiding the damage. Technology and communication services are keeping the index afloat, while most other sectors are falling.
- Higher yields are hitting rate-sensitive sectors first. Utilities and real estate face higher refinancing costs and stronger competition from bonds, while financials are starting to feel tighter credit conditions.
- AI remains the market's shelter — for now. Strong earnings and balance sheets are helping mega-cap tech withstand higher yields, but that leaves the broader market increasingly dependent on a narrow group of winners.

The S&P 500 is still holding up. But look beneath the headline index and the picture is much weaker.

Over the past month, the S&P 500 is up around 0.7%. Yet only two sectors are positive: technology, up 7.1%, and communication services, up 3.3%.

Every other sector is down. Financials have fallen around 7%, materials 6.6%, utilities 6.2% and real estate 6.1%.

That tells us something important: higher bond yields are already hurting equities. The pain is simply being masked by the strength of AI and mega-cap technology.

Why do higher bond yields matter for stocks?

There are two simple ways higher yields can hurt equities.

First, bonds become more attractive. If investors can earn more than 5% from US government debt, stocks need to offer a more compelling return to justify the additional risk.

Second, borrowing becomes more expensive. Companies refinancing debt, households taking mortgages and businesses funding new investment all face a higher cost of money.

But the impact is not equal across the market. Some sectors feel it much more quickly than others.

1. Financials: higher rates aren't always good for banks

Banks are often thought of as beneficiaries of higher rates. But that only works up to a point.

If yields rise too far or too quickly, the story changes.

Banks may earn more from lending, but they can also face higher funding costs. Their bond portfolios can fall in value. More importantly, high borrowing costs can slow demand for mortgages, business loans and other credit.

And if rates stay high long enough, investors start worrying about loan losses.

So the issue shifts from higher interest margins to weaker credit growth and potentially weaker borrowers.

That helps explain why financials are currently one of the weakest S&P 500 sectors, down around 7% over the past month.

2. Small companies and weaker balance sheets: the refinancing problem

Higher yields can be especially painful for smaller companies.

Many large companies locked in cheap long-term borrowing when interest rates were low. Smaller businesses tend to have shorter-dated debt, more floating-rate loans and less access to capital markets.

As that debt gets refinanced, interest bills rise.

The pressure is even greater for companies that are not generating enough cash to fund themselves. When money was cheap, investors were willing to finance companies based on future growth. With bond yields above 5%, that hurdle is much higher.

In this environment, balance-sheet strength matters more.

3. Utilities: hit from both sides

Utilities are among the clearest casualties of higher yields.

These businesses typically require large amounts of capital to build and maintain power plants, electricity grids and other infrastructure. That means they often carry substantial debt.

When interest rates rise, new borrowing and refinancing become more expensive, potentially squeezing profits and cash flow.

There is another problem. Utilities are often owned for their relatively stable dividends. But a utility dividend becomes less attractive when investors can get a high yield from government bonds without taking equity risk.

So utilities face a double hit: higher financing costs and stronger competition from bonds.

That helps explain why the S&P 500 utilities sector is down more than 6% over the past month.

4. Real estate: refinancing gets painful

Real estate faces many of the same pressures, potentially even more directly.

Property companies and REITs tend to use significant amounts of debt. When that debt needs refinancing, today's higher rates can mean a sharp increase in interest costs.

Higher bond yields can also put upward pressure on property yields, which can weigh on property valuations.

At the same time, REITs compete with bonds for income-focused investors. A 4–5% dividend yield may look less compelling when government bonds offer similar income with much less risk.

The S&P 500 real estate sector is down around 6.1% over the past month.

For investors, the key question is therefore not simply how much debt a property company has, but when that debt needs refinancing and at what cost.

5. Consumer and cyclical stocks: the economic impact comes next

Higher yields also start to affect sectors that may not look obviously rate-sensitive.

Consumer discretionary stocks, industrials and materials are all lower over the past month.

Here, the transmission mechanism is the economy.

Higher mortgage rates can slow housing activity. Expensive car loans and credit-card debt can weigh on household spending. Higher corporate borrowing costs can cause companies to delay factories, equipment purchases or other investments.

A company does not have to be highly indebted itself to suffer from high rates. Its customers may be.

This is when higher yields stop being just a valuation problem for markets and begin becoming an earnings problem.

So why is technology still rising?

This is the most interesting part of the market.

Historically, technology and other growth stocks were often among the biggest losers when bond yields rose. Their valuations depend heavily on profits expected far into the future, and higher discount rates make those future earnings worth less today.

But technology is up more than 7% over the past month.

For now, investors believe that earnings growth from AI infrastructure, chips, cloud computing and related investment can outweigh the drag from higher interest rates.

The strongest technology companies also have something that highly leveraged companies do not: large cash flows and strong balance sheets.

They are much less dependent on refinancing markets to fund growth.

That means today's market divide is not simply growth versus value.

It is increasingly becoming companies that can fund their own growth versus companies dependent on expensive capital.

The S&P 500 is hiding a much weaker market

This is why looking only at the S&P 500 can give investors a false sense of comfort.

The index remains resilient because technology and communication-services giants carry such large weights.

But underneath, utilities, real estate, financials, materials and many cyclical companies are already feeling the impact of higher yields.

The bond sell-off has not broken the S&P 500. It has broken much of the market underneath it.

As long as AI-related earnings remain strong, technology may continue to offset weakness elsewhere.

But it also means the market is becoming increasingly dependent on a relatively narrow group of companies continuing to deliver exceptional growth.

What investors should watch

First, refinancing risk. Investors may want to pay closer attention to debt levels, interest costs and upcoming debt maturities, particularly in real estate, utilities and smaller companies.

Second, market breadth. If the S&P 500 keeps rising while most sectors and stocks fall, the headline index becomes increasingly dependent on a small number of winners.

Third, AI earnings. Technology has so far been the shelter from higher yields. If earnings expectations there start to weaken while bond yields remain high, the broader index could become much more vulnerable.

The key message is that high yields do not hurt every stock in the same way.

For some companies, the problem is valuation. For utilities and real estate, it is the cost of financing and competition from bonds. For banks, it is weaker credit conditions. For cyclical companies, it is slower economic activity.

The bigger test for markets will come if high yields stay around long enough that even exceptional earnings growth can no longer fully offset the rising cost of capital.

Source: <https://www.home.saxo/content/articles/equities/why-higher-yields-are-hurting-everything-except-ai-05102026>