From the US Market Desk: Now…We Wait…

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Macro

Our real gross domestic product (GDP) forecast for 2026 is 2.5% (based on our Global Investment Management Survey) versus the Federal Reserve's (Fed's) forecast of 2.2% and the Wall Street consensus of around 2%. The economy remains resilient and the consumer is strong. The only thing that could throw us a curveball would be a policy mistake by the Fed. We do not anticipate that. I hesitate to even mention this because the data whips around so fast I don't glean much from it, but the latest Atlanta Fed GDPNow forecast is now up to 4.6%.

The core Personal Consumption Expenditures (PCE) price index was one of the big data points this week and came in at 3.3% as expected for July, which was also in line with our year-end forecasted range of 3.0% - 3.5%. This gauge of core inflation is the Fed's preferred measure; however, the Fed won't ignore the 3.7% increase in headline inflation, as the continued US conflict with Iran has caused energy prices to remain elevated (and volatile).

Given our central bank's dual mandate, the somewhat unexpected 4,000 fall in this week's initial jobless claims numbers is also noteworthy. Unemployment ticked lower in July, to 4.1%.

Fed policymakers met in Jackson Hole, Wyoming this week for their policy symposium, and new Fed Chair Kevin Warsh used most of his time at the podium on Friday morning to reinforce what he's been communicating to the market the past couple of months. Specifically, his belief that our economy is doing well and our labor market is healthy, but that the central bank is serious about achieving the Fed's 2% core inflation goal and that short-term rates are the primary tool to do it. He also said that a quieter Fed which provides less forward guidance is probably better and gives them more flexibility in making monetary policy decisions.

The US two-year Treasury note yield ticked up a couple basis points this week and currently sits at 4.22%, still about 40 basis points (bps) over the federal funds rate but off the boil. Remember, the bond market leads the Fed, not the other way around.

Treasury Secretary Scott Bessent seems to have brought back "Operation Twist" last week. He announced that the Treasury will double the size of its monthly purchases of long bonds for at least a few months beginning in September, from $2 billion to $4 billion, to "improve liquidity." The additional nominal dollar amount of $2 billion is not significant, but this could be a signaling event for markets. As our Head of Research Larry Hathaway noted to us, the risk is that the peashooter becomes a bazooka. Markets reacted modestly on the news.

Meanwhile, the fed funds futures market is indicating there is now only a 35% chance of a 25-bps hike in September and a hike fully priced in by the last policy Fed policy meeting of the year in December. This data moves very fast, so this picture can and will change quickly depending on incoming data.

On the currency front, we are expecting the US dollar to be essentially flat for the year despite the recent volatility. The US Dollar Index is trading at 99.11, slightly higher over the past week but still slightly lower than following the “Operation Twist” announcement on August 19. We expect the relative strength of the US dollar will continue to be rangebound, as it has been for the last year and a half.

Equities

We are constructive on US equities and have established a year-end target range of 7400-7800 for the S&P 500, driven by 15+% year-over-year (Y/Y) earnings-per-share (EPS) growth. Second-quarter (Q2) earnings season is now over.

NVIDIA reported quarterly results this week, and they were eye-opening. The company not only posted another record quarter which easily beat expectations, but its forward guidance was incredibly strong as revenues are expected to grow 70% in fiscal year 2028.

All in, earnings power has been very strong in the first six months of the year. Consensus expectations for 2026 are now about 25% Y/Y and for 2027, the consensus earnings estimates show growth of nearly 15% versus 2026.

Bloomberg reports that in Q2, 25 firms in the S&P 500 Index have quantified the use of artificial intelligence (AI) on their income statements, saying that on average they have seen 180 bps of margin growth. This is the first inning of hearing about AI impact, I suspect. Meaning, going forward I’d expect we hear more companies quantify the impact of AI on their businesses. Accretive to margins is bullish.

If we assume the consensus earnings estimates are reasonably correct, that puts the tape at 21x this year’s earnings and 19x 2027 estimates. The long-term historical forward multiple is about 17x. Portfolio managers are now focusing their efforts on corporate earnings power for calendar year 2027. I can’t make a strong argument that the tape is “cheap” here, but I also can’t make the argument that a 19x forward multiple is crazy rich either. If bond yields move significantly higher, that could change and be a risk. It’s unclear how Bessent might react if this happens.

Here’s the next thing I’m thinking about: The concept of peak rate of change in earnings growth. Not peak earnings power in dollars, but peak rate of change Y/Y. Just looking at consensus estimates for the S&P 500 out to 2028, the data says 2026 is the peak Y/Y rate of change. If this is accurate, I’d expect a higher level of volatility going forward.

Speaking of rising volatility, please take five minutes to read our latest white paper on what to expect from equities. Our Market Strategists Chis Galipeau and Lukasz Kalwak provide a look at seasonal volatility, midterm election years, liquidity, fundamentals, and what we historically see in the third year of the presidential cycle. Don’t miss this piece: “Broadening Delivered. Now Prepare for Volatility.”

The tape is recognizing broad fundamental strength. Consider this: The cap-weighted S&P 500 Index is up 12.95% year-to-date (YTD) through August 26, and the S&P 500 Equal Weight Index is up 17.04%. The S&P 400 MidCap Index is up 16.60% and its equal-weighted version is up 15.61%. The Russell 2000 Index is up 22.13% and its equal-weighted version is up 20.99%. No single name is dominating. Everything is participating.

Bottom line: We think it’s prudent to have a diversified equity playbook that includes US large-, mid- and small-cap exposure with a balance of growth and value. The same can be said for ex-US equity exposure; emerging markets and Japanese stocks look attractive. That involves reducing concentration and spreading one’s bets. We favor buying on pullbacks.

Fixed Income

We expect the 10-year US Treasury bond to yield in the range of 4.25%–4.75% for the year. As of this writing, the last trade was 4.66%. We think adding duration risk makes sense around 4.75% or so. Core and core plus strategies should get closer looks, should rates remain elevated. Our Senior Analyst Lukasz Labedzki just came out with a piece that reinforces this view and provides some color on not just US Treasuries, but also the state of corporate and mortgage credit. “Core Bond (Plus): What’s Under the Hood and When to Consider It” is another piece worth your time.

The US yield curve had another week of modest flattening. The two-year/10-year spread is now 44 bps, 6 bps tighter versus last week.

We expect short duration fixed income mandates and corporate credit to outperform cash again this year. Considering our views on US 10-year yields, we do not expect duration to be a significant driver of total return this year. Rather, all-in yield capture seems to be the play, although recent spread widening might create an opportunity for additional total return. Clipping coupons looks attractive.

Credit spreads remain well behaved in the face of higher yields. Investment-grade spreads, as proxied by the Bloomberg US Corporate 1-3 Year Option-Adjusted Spread (OAS), are now 45 bps over comparable Treasuries. Investment-grade spreads are still only a few basis points from five-year tights. High-yield spreads, as proxied by the Bloomberg US Corporate HY OAS, are now 265 bps over. These are both relatively tight levels from a historical perspective, reflecting a strong fundamental backdrop with corporate profitability being the main driver.

We are bullish on municipal bonds and find taxable equivalent yields to be attractive, along with robust fundamentals. Importantly, municipal bonds can offer potential diversification benefits in the form of low correlations to various equity markets, relative to most taxable fixed income mandates. The market is on pace for another year of record supply; however, tight spreads in taxable bonds have helped the markets absorb these high supply levels

Sentiment

The percentage of bullish investors in the latest AAII survey (the week ending August 26) is 33%, a low reading. The percentage of bearish investors in the AAII survey is 44%. The wall of worry is still in place.

Bull markets peak on euphoria. I don’t think we are there yet.

We will continue to analyze the markets and will offer insights again next week.

Source of data (except where noted) is Bloomberg and Franklin Templeton Institute, as of August 27, 2026. Important data provider notices and terms are available at www.franklintempletondatasources.com.

The Franklin Templeton Institute Global Investment Management Survey is a biannual outlook survey designed to give a view across our investment teams. The Franklin Templeton Institute identifies the median across the survey answers and develops the outlook. The survey received responses from around 200 portfolio managers, directors of research and chief investment officers, representing participation across equity, private equity, fixed income, private debt, real estate, digital assets, hedge funds and secondary private markets. Each of our investment teams is independent and has its own views.

The AAII (American Association of Individual Investors) Sentiment Survey: This survey offers insight into the opinions of individual investors by asking them their thoughts on where the market is heading in the next six months.

Breakeven rates: The difference between yields of Treasury bonds and TIPS for issues of the same tenor/maturity, calculated by subtracting TIPS yields from Treasuries; a measure of inflation.

Capital expenditure (capex): Funds that companies spend to acquire, upgrade or maintain physical assets, such as buildings, technology or equipment, with the purpose of maintaining or growing future operations.

Duration: A measure of how much a bond's price changes relative to changes in interest rates.

Earnings per share (EPS): The portion of a company's profit allocated to each outstanding share of common stock. An index EPS is an aggregation of the EPS of its component companies.

EBIT: Earnings before interest and taxes.

Fed funds (FF) rate: The interest rate that depository institutions such as banks charge other institutions for holding overnight reserves.

Option-adjusted spread (OAS): Measures the spread between a bond's interest rate and the risk-free rate, while adjusting for any embedded options like callable or mortgage-backed securities.

Tape: A reference to broad market performance, based on the ticker tape that transmitted stock prices during the 19th and 20th centuries.

Taxable-equivalent yield: The yield of a municipal bond investment calculated to reflect the benefits of income tax exemption and to be comparable to the yield of a taxable bond.

Yield spreads/tights: Spreads are the difference between yields on differing debt instruments of varying maturities, credit ratings, issuers or risk levels. "Tights" in reference to spreads indicates small differences in yields.

Indexes are unmanaged and one cannot directly invest in them. They do not include fees, expenses or sales charges. Past performance is not an indicator of future results.

Bloomberg US Corporate High Yield Index: Tracks the performance of the USD-denominated, high-yield, fixed-rate corporate bond market.

Russell 2000® Index: A market capitalization-weighted index that measures the performance of the 2,000 smallest companies in the Russell 3000 Index.

S&P 500® Index: A market capitalization-weighted index of 500 stocks, a measure of broad US equity market performance.

S&P 500 Equal Weight Index: The equal-weight version of the S&P 500 Index. The index includes the same constituents as the capitalization weighted S&P 500, but each company is allocated a fixed weight, or 0.2% of the index total, at each quarterly rebalance.

S&P MidCap 400® Index: A market capitalization-weighted index of 400 stocks of mid-size companies, distinct from the large-cap S&P 500.

US Dollar Index: A basket of six foreign currencies (euro, Japanese yen, UK pound sterling, Canadian dollar, Swedish krona and Swiss franc) used to track the relative strength of the US dollar, with a higher index value representing US dollar strength.

All investments involve risks, including possible loss of principal.

The allocation of assets among different strategies, asset classes and investments may not prove beneficial or produce desired results.

Diversification does not guarantee a profit or protect against a loss.

Equity securities are subject to price fluctuation and possible loss of principal.

Fixed income securities involve interest rate, credit, inflation and reinvestment risks, and possible loss of principal. As interest rates rise, the value of fixed income securities falls. Low-rated, high-yield bonds are subject to greater price volatility, illiquidity and possibility of default.

International investments are subject to special risks, including currency fluctuations and social, economic and political uncertainties, which could increase volatility. These risks are magnified in emerging markets.

The investment style may become out of favor, which may have a negative impact on performance.

Large-capitalization companies may fall out of favor with investors based on market and economic conditions.

Small- and mid-cap stocks involve greater risks and volatility than large-cap stocks.

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