Market Update
Q3 2026

TOMPKINS Financial Advisors
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Crude Awakening: Oil, the Fed, and the Return of Tightening Monetary Policy

If 2026 has been defined by one market theme, it is the extent to which consensus expectations have been turned on their heads. Entering the year, many investors anticipated a slowing U.S. economy, additional Federal Reserve rate cuts, solid but hardly spectacular corporate profit growth, and moderating inflation.

Nine months later, the landscape is strikingly different: economic growth has remained resilient, the Federal Reserve has resumed raising interest rates, corporate earnings have materially exceeded forecasts, and oil prices have risen above $100 per barrel, renewing inflationary pressure. Ordinarily, that combination might have unsettled investors. Instead, strong corporate earnings, substantial investment in artificial intelligence, and a still-supportive fiscal backdrop helped sustain economic growth and equity-market performance.

Despite the sharp departure from many consensus expectations, financial markets have provided a masterclass in market resilience. The S&P 500 reached a record high in mid-August and ended September just below that level. One development that has unfolded largely as we anticipated at the start of the year is the highly rotational nature of the market, with leadership shifting repeatedly across sectors, investment styles, and asset classes. Substantial capital investment in artificial intelligence and the influence of fiscal policy have helped support that resilience, while continuing to shape the outlook for economic growth, corporate earnings, and market leadership.

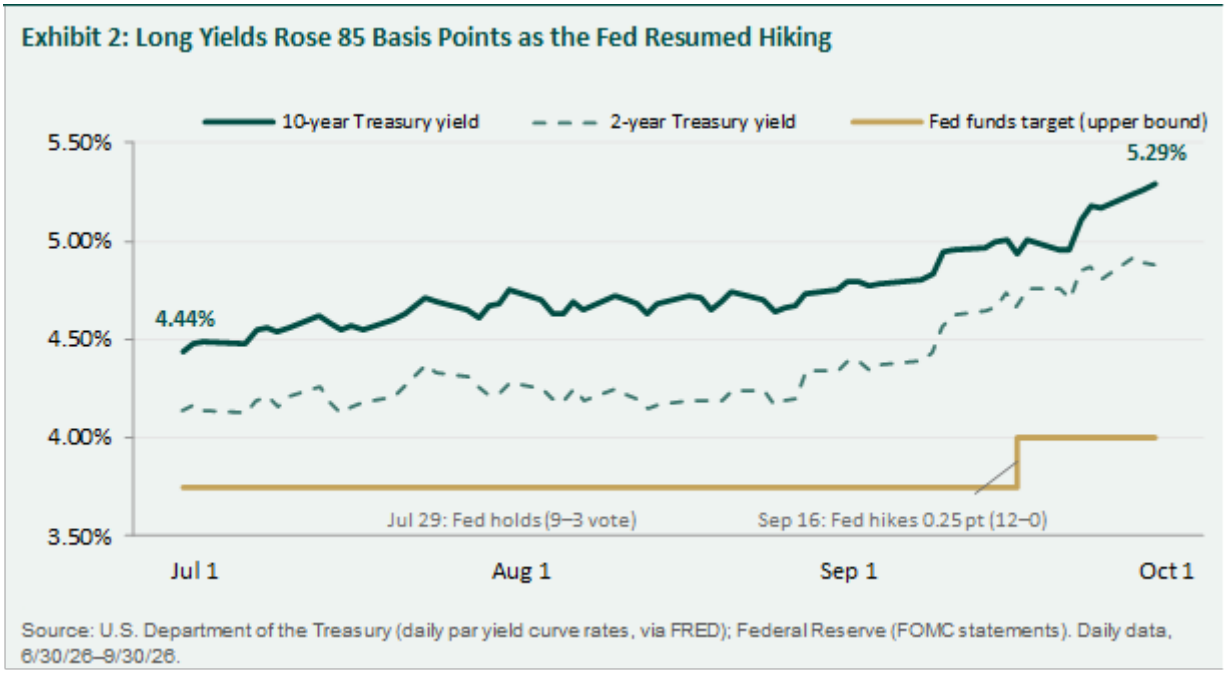
Exhibit 1: Stocks Edged Higher While Yields and Oil Surged

As of	30-Sep-26	Q3 % Chg	YTD % Chg
US Stocks (S&P 500)	$ 7,651.54	+2.3%	+12.8%
Non-US Stocks (MSCI ACWI ex US)	$ 463.30	+0.5%	+14.2%
US Bonds (Bloomberg US Agg)	$ 2,280.45	–3.5%	–2.9%
10-year Treasury yield	5.29%	+0.85%	+1.11%
2-year Treasury yield	4.88%	+0.74%	+1.41%
10-year TIPS (real) yield	2.93%	+0.73%	+1%
Brent crude ($/barrel)	$115.91	+65%	+89%
WTI crude ($/barrel)	$90.42	+30%	+58%

Source: Morningstar, Factset, U.S. Department of the Treasury

Bonds Took a Hit but Real Yields Are Up

Renewed inflation pressure prompted the Federal Reserve to raise interest rates in September for the first time since 2023. The bond market moved even faster. As Exhibit 2 shows, the 10-year Treasury yield rose 85 basis points during the quarter, from 4.44% to 5.29%, its highest close since 2002. The 2-year Treasury yield increased 74 basis points, from 4.14% to 4.88%. With longer-term yields rising more sharply, the yield curve steepened, reflecting a higher term premium on longer-dated bonds.



Rising interest rates have weighed down on fixed income returns, as bond prices move inversely to interest rates. As a result, the Bloomberg U.S. Aggregate Bond Index is down -2.9% so far this year. A potential silver lining is that much of the high-quality bond market now offer investors a yield of more than 5%, and tax-exempt municipal bond yields are near their highest levels in well over a decade. Higher income provides a cushion against some of the volatility from rising rates, and we believe this market backdrop will continue to reward investors with a balanced, high-quality approach rather than a bet on the timing of the next rate adjustment by the federal reserve.

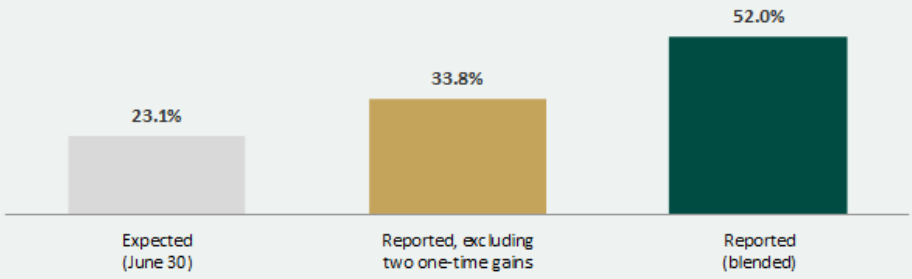
Earnings Continue to Clear an Elevated Bar

If interest rates were the quarter's principal headwind, corporate earnings remained the equity market's primary tailwind. Second-quarter S&P 500 earnings increased 52.0% from a year earlier—the fastest pace since 2021 and more than double the 23.1% growth rate analysts had expected at the start of the quarter, back on June 30th.

Although two of the index's largest companies reported unusually large investment gains, underlying earnings results were still robust. As Exhibit 3 shows, earnings growth excluding those companies was still 33.8%, and more than 86% of S&P 500 companies exceeded consensus estimates.

Strong earnings have not, however, produced equally broad market participation. The widening performance gap between the capitalization-weighted S&P 500 and its equal-weight counterpart indicates that market leadership continues to become increasingly concentrated. In September, the capitalization-weighted index declined 0.45%, compared with a 5.18% decline for the equal-weight index. That divergence underscores how heavily the broader market has depended on a relatively small group of mega-cap companies, most of which being linked to the AI investment cycle. We therefore remain constructive on equities while recognizing that narrow participation could leave the market more vulnerable if earnings expectations or capital-spending assumptions for those leaders begin to weaken.

Exhibit 3: Q2 Profits More Than Doubled Expectations. Excluding Two Windfalls from Alphabet & Amazon, S&P 500 Profit Growth Was Still 34%



Source: FactSet Earnings Insight, August 28, 2026 (97% of S&P 500 companies reporting). Year-over-year growth in S&P 500 earnings per share for Q2 2026.

Outlook: A Consistent Framework for a Higher-Rate Environment

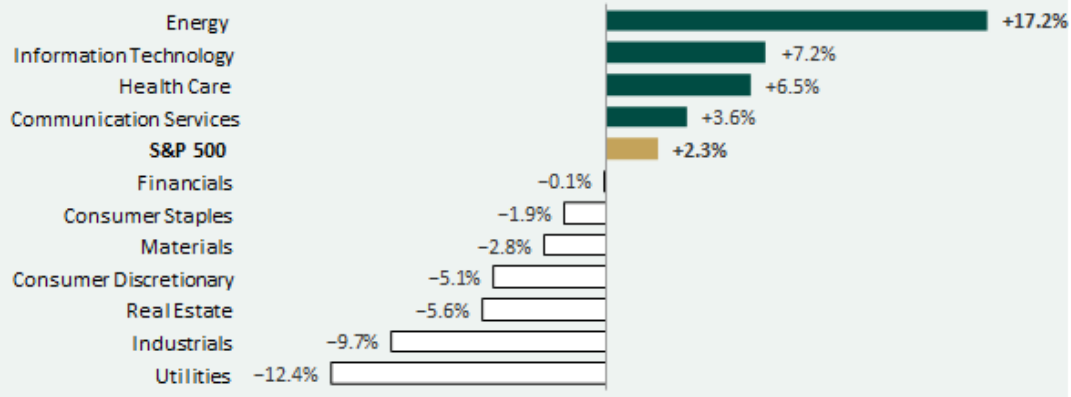
As we enter the fourth quarter, three interconnected forces remain central to our investment outlook: interest rates, corporate earnings, and inflation. Their implications vary across asset classes, reinforcing the importance of diversification, security selection, and disciplined portfolio construction.

Interest rates. The 10-year Treasury yield ended the quarter at its highest level since 2002. Higher yields can pressure equity valuations and bond prices, but they also provide fixed-income investors with some of the most attractive acquisition yields in nearly two decades.

Earnings delivery. Third-quarter results begin arriving throughout October, and expectations are elevated. Investors will be assessing whether substantial capital spending is producing durable profit growth, whether earnings strength is broadening beyond the market's largest companies, and whether management teams signal any moderation in their elevated capital investment plans.

Oil and inflation. As Exhibit 4 illustrates, higher oil prices helped make Energy the strongest-performing S&P 500 sector during the third quarter. The broader implications are less uniformly positive. Higher oil prices can strengthen energy-company cash flows while constraining household spending, pressuring margins in energy-intensive industries, and sustaining inflation that keeps interest rates higher for longer.

Exhibit 4: Energy Led the Quarter as Oil Rebounded



Source: S&P Dow Jones Indices; J.P. Morgan Asset Management, Guide to the Markets (FactSet data). S&P 500 sector total returns, Q3 2026 (6/30/26–9/30/26).

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Throughout 2026, markets have absorbed a notable combination of higher interest rates, rising oil prices, and increasingly concentrated equity market leadership. That resilience is encouraging, but it should not be mistaken for an absence of risk. We continue to emphasize diversification, quality, disciplined rebalancing, and a risk posture for client portfolios that's capable of withstanding the continued rotations in both market leadership and economic policy.

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