

Doll's Deliberations®

Weekly Investment Commentary



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Summary

Equities were mixed last week (S&P 500 -0.46%). The equal-weighted S&P outperformed by 160 basis points (bps). Big tech was mostly lower, with funding and capex concerns remaining the problem. Best performers were energy (+1.55%) and health care (+1.47%); worst performers were communication services (-6.21%) and industrials (-1.87%).

Key takeaways

1. In September, housing starts slid for the third straight month (falling 5.2%). Single-family starts dropped to the lowest level since September 2025.
2. Upcoming Fed moves should be monetary policy tweaks, not the start of an aggressive hike cycle.
3. The Fed sees core inflation cooling to 2.5%. This feels more like an optimistic best case than a reasonable base case. (Language courtesy of RENMAC.) The probability is high that the FOMC will revise their inflation estimates higher.
4. The recent decline in Treasury yields suggests that the worrisome inflation news was overshadowed by concerns about weaker economic growth. That fits with the Fed's collection of anecdotes in its Beige Book, which showed some evidence of weaker activity (particularly capex).
5. It is not difficult to see why there would be some slowdown in economic growth, even beyond the anxieties about a tech bubble teetering. Higher oil prices, aging demographics, tariffs, central bank tightening, an uptrend in mortgage rates, the U.S. fiscal impulse turning negative and debt fears abroad (e.g., France) all matter. These factors, while well-known, may be starting to bite.
6. The 3Q26 reporting season is off to a slightly soft start with company commentary generally still highlighting resilience in the economy and consumer and tailwinds from AI, with some caveats, while giving investors plenty to think about in terms of risks that may lie ahead.
7. After nearly two weeks of earnings season, expectations for S&P 500 companies have remained relatively unchanged, with revenue growth projected at approximately 12% and earnings growth at 30%.
8. With all the macro crosscurrents the market faces, a necessary condition for a continued bull market is the avoidance of earnings disappointments.
9. MarketWatch calculated that 80% of S&P 500 companies were at least 10% below their 52-week highs at the start of October, while 39% had fallen at least 20%. In other words, much of the index was already experiencing a correction or bear-sized market declines even though the benchmark itself remained close to a record.
10. According to JP Morgan, 60% of S&P 500 stocks are down 20% or more from their all-time highs despite the market being close to all-time highs. (Only 30% of stocks are outperforming the S&P 500, one of the lowest figures in more than 25 years.)

Equity markets (Index total return %)	Last week	Year-to-date
DJIA	0.42	9.99
S&P 500	-0.46	12.40
NASDAQ	-0.71	12.19
Russell 1000	0.13	12.67
Russell 1000 Growth	-1.52	1.55
Russell 1000 Value	0.67	23.90
Russell 2000	2.31	13.22

S&P equity sectors (Index total return %)	Last week	Year-to-date
Communication services	-6.21	-3.08
Consumer discretionary	0.52	-3.07
Consumer staples	0.57	16.40
Energy	1.55	58.32
Financials	0.72	3.40
Health care	1.47	17.32
Industrials	-1.87	7.05
Information technology	-0.25	21.79
Materials	-0.08	13.67
Real estate	0.87	9.16
Utilities	0.83	1.87

AI Takes a Breather

The cracks in the AI boom continue to accumulate, although they are not yet sufficient to undermine overall risk-taking. So far, equity market losses are modest, except in many parts of technology. The silver lining is that oversold government bonds have rallied. Yields seem on track to overshoot but have calmed in the past two weeks.

The economic/inflation/policy fundamentals remain bond-bearish, although valuations had improved and conditions were oversold and conducive for a pause, as we have suggested. Any consolidation should prove temporary unless the cracks in AI widen to the point where a broad risk-off phase develops and capex plans start to get pruned. The latter would generate at least an economic growth scare, especially in the U.S.

It is challenging to determine the fate of AI plays, but expectations and financing are significant and investors are finally starting to balk at even more risk in this space. Although the future will be heavily influenced by AI developments, it does not mean that the exponential rise in AI-related spending and borrowing will continue unabated. Past investment stampedes related to major technological breakthroughs have eventually witnessed busts. Thus, there will be no surprise when a replay occurs for AI. When, and how big a bust, are harder to pinpoint, but the amount of froth in this space warrants being cautious.

Many markets/indexes/sectors are not much below their peak for the cycle. This indicates that most investors are still willing to rotate, rather than reduce their overall equity holdings in the face of relentless negative AI and overall tech headlines. Broader credit warnings and/or negative economic news could finally shake investors' positive bias. So far neither has occurred, but these risks are on our radar.

One threat to the outlook continues to linger, namely prospects for an even larger energy shock. Crude oil and especially product prices remain elevated versus levels at the start of the year. Moreover, it is possible that supplies could worsen, or at least not improve, since durable agreements on the conflicts in the Middle East and in Russia/Ukraine remain elusive. For now, energy prices/supplies represent an economic headwind, but are not strong enough to undermine global growth. Economic growth has improved in recent months, underscoring that global monetary and fiscal policies have been accommodative.

While there are daily reports on the mounting woes in AI-related debt, overall credit spreads have not widened very much and remain historically narrow. This is not too surprising since the corporate profit backdrop is quite supportive, and default risks remain low outside some AI datacenter issues.

With just over one week to go, the U.S. mid-term elections do not seem to have had much impact on U.S. asset markets or the dollar. Polling has steadily deteriorated for the Republicans, including for the President. As it stands, it appears that the House will flip to the Democrats and even the Senate might as well. If so, then investors should expect a noisy next two years on the political front, with no meaningful policy initiatives.

Conclusion

Increased cracks in various AI plays and intensifying strains in the French bond market have helped to cap government bond yields. The consolidation should prove temporary, given the still-robust economic and inflation outlooks. However, the AI investment and financing boom is unsustainable and a bust is eventually inevitable. So far, broader credit issues have not developed, but stay tuned.

Source: Bloomberg as of 10/23/26

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International equity markets (Index total return %)	Last week	Year-to-date
MSCI ACWI	-0.54	11.90
MSCI ACWI EX U.S.	-1.62	10.82
MSCI EAFE	-1.29	8.83
MSCI EM	-2.76	14.10

Fixed income markets (Index total return %)	Last week	Year-to-date
Bloomberg U.S. Aggregate Bond	0.73	-0.91
Bloomberg U.S. Corp. High Yield	-0.04	-0.03
Bloomberg U.S. Gov/Credit	0.69	-0.93
Bloomberg U.S. T-Bill 1-3 Month	0.04	3.00

Alternatives (Index total return %)	Last week	Year-to-date
Real estate (FTSE NAREIT)	0.87	10.13
Commodities (DJ)	-0.43	34.99
Global listed private equity (Red Rocks)	1.92	-12.09
Currencies (DB Currency Future Harvest)	0.82	12.85