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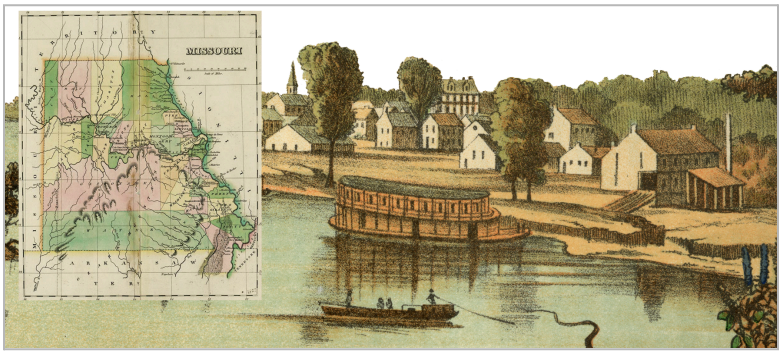
Quarterly Newsletter

October 2026
4Q2026

Fault in Financial Markets:
Temporary Tremors or Fluvial Foreshocks?

I feel the earth move under my feet
I feel the sky tumblin' down, a-tumblin' down
-- Carole King

In the early morning of December 16, 1811, the citizens of New Madrid, Missouri awoke to the violent shaking of an earthquake. Shocks caused chimneys to fall in St. Louis, bells to ring in Boston, and even 900 miles away in the Capital City, the First Lady, Dolly Madison, claimed she was awakened "by the tremors as doors slammed, furniture rattled, and dishes shook inside the White House."



This would prove to be only the beginning, with major earthquakes following in January and February of 1812. The final temblor was the most powerful of them all. And it did more than just shake the ground; it *altered* the course of the Mississippi River. A fault beneath the river bed ruptured and a 15-foot high natural dam formed downstream, causing the river to temporarily reverse direction. The resulting "fluvial tsunami" impacted geography as far south as New Orleans. The flow of water was so powerful that millions of tons of silt from the West Bank of New Orleans settled on the East Bank, building hundreds of acres of new land over the next two decades known as "battures."

Today's markets may be experiencing a similar upheaval. The financial ground itself seems to be shifting, causing some foundations to fracture and new battures to form. Bond yields have climbed to 24-year highs. A flood of government debt and significant AI infrastructure financing coupled with the diminishing currents of traditional buyers and stubborn inflation are converging and applying severe tension to the interest rate fault line.

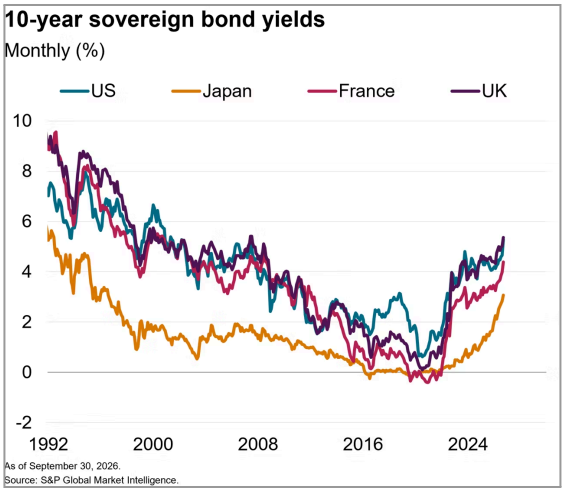
Ripple Effects

The Federal Reserve responded by raising short-term rates for the first time in three years. The Treasury announced a 1961-style Operation Twist, borrowing on the short end of the curve and buying bonds back on the long end. At the same time, the Consumer Confidence Index recently hit its all-time low while the major

stock indexes continue climbing to new peaks. Yet, 75% of S&P 500 stocks are firmly in correction territory and AI, the market's great engine, emanates rumblings of its own.

AI-centered earnings keep pushing up the summit, but continued market tremors have caused angst in the minds of even the most seasoned economists and money managers. Some rate relief is in the offing as shorts cover and capital flows into fixed income investments. However, investors are asking whether yields can stabilize and if AI data center spending can maintain its explosive pace. Or are these the rumbles of a Big One still to come?

Chart 1: Sovereign Bond Yields

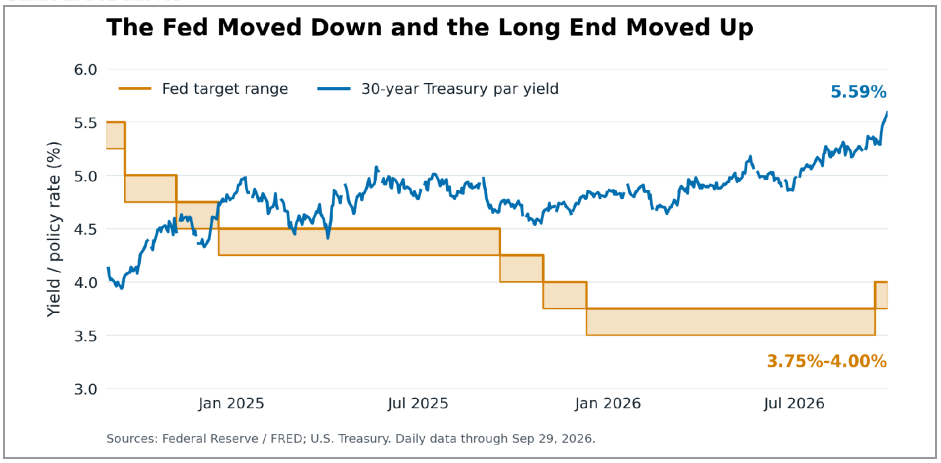


The Fault Line Beneath the Market

Interest rates have been the epicenter of the recent shocks to the market and economy. Long-term sovereign bond yields across the globe have climbed to levels not seen in decades (see Chart 1). The era of cheap money, once considered a permanent fixture across the financial landscape, has given way to higher rates, heralding a return given way to higher rates, which are more consistent with historic norms.

Investors entered 2026 expecting the Federal Reserve to lower interest rates before year-end. Instead, rising inflation forced the Fed to reverse course. The Fed raised rates by 25 basis points at their recent September meeting, representing its first rate hike in three years. This is a noticeable change in policy after a long stretch of calm where the Fed lowered its target rate by 175 basis points between October 2024 and December 2025.

Chart 2: Fed Moves



The Fed, in its limited role, can only impact short-term interest rates. It cannot dictate long-term borrowing costs. Historically, however, when the Fed cuts, rates follow. In the first 13 easing cycles since 1966, this was the case. But in the most recent easing cycle, long rates actually rose by 76 basis points, from 4.04% to 4.8%, and continue to rise today as evidenced by Chart 2.

The obvious explanations for this new higher rate environment are well known: enormous government debt burdens, chronic deficits, and persistent inflation. But there are at least three other forces impacting bond

prices: competition for capital from artificial intelligence, the decline of foreign central bank buyers, and the rise of the discretionary buyer.

Will the AI Levee Break?

The construction of AI infrastructure has become the largest capital investment program, in terms of GDP, in history (See chart 3). AI debt issuance is so large that it is forcing rates up across the board in all fixed income classes. According to the New York Times, companies have borrowed at least $3 trillion for all facets of AI infrastructure buildout.

Chart 3: AI Investment Boom

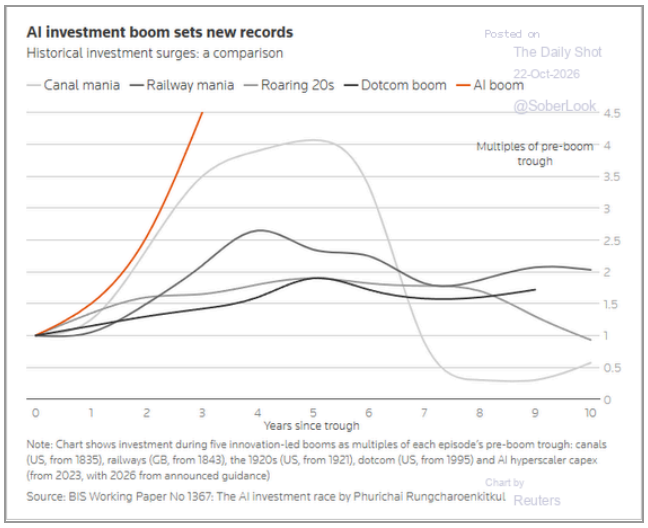
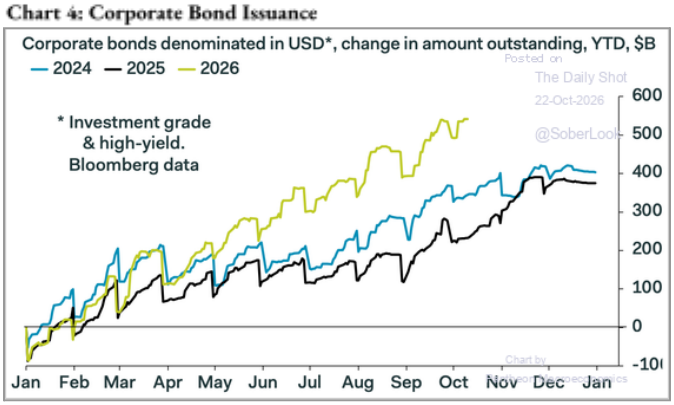


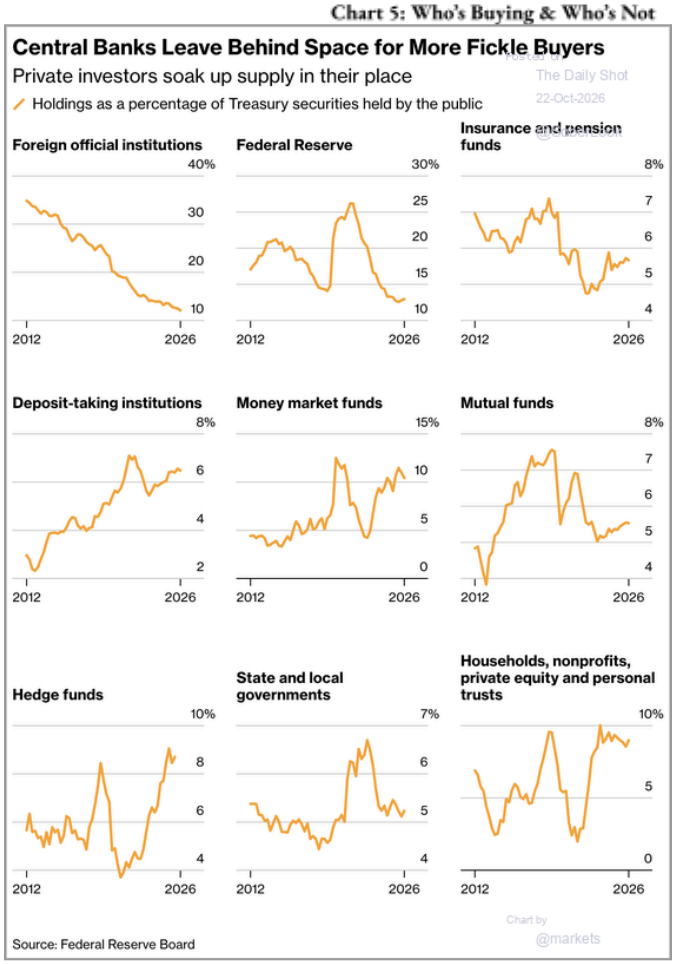
Chart 4: Corporate Bond Issuance



Further, Goldman Sachs research stated, "[In 2026] global AI-related companies have issued roughly $489 billion alone, up from $322 billion in 2025." Chart 4 illustrates how much larger the number actually is if one considers high yield debt issued by AI.

AI data centers and sovereigns are at peak borrowing, while historical buyers of the U.S. Treasuries have been absent. Central banks have been offloading Treasuries. At the same time, discretionary buyers, who require a much higher return on investment, have been left to soak up the ever-growing mountain of supply (see Chart 5).

Chart 5: Who's Buying & Who's Not



Secretary of the Treasury Bessent reacted to the rise in long-term rates by up-sizing an old approach to bringing down long interest rates, commonly referred to in bond parlance as "Operation Twist." The idea involves the Treasury issuing short term Treasuries and using the proceeds to attempt to bring down yields on

the longer end of the curve by buying long-maturity bonds. The Treasury used the scheme in 1961 and again in 2011 with limited success.

Confidence Erodes & Indexes Build?

The rise in rates has also influenced consumer confidence. According to the University of Michigan Consumer Sentiment Index, the reading recently hit 46.3, the second lowest since its inception in 1952. This number is eclipsed only by its lowest reading of 44.8 in May (see Chart 6).

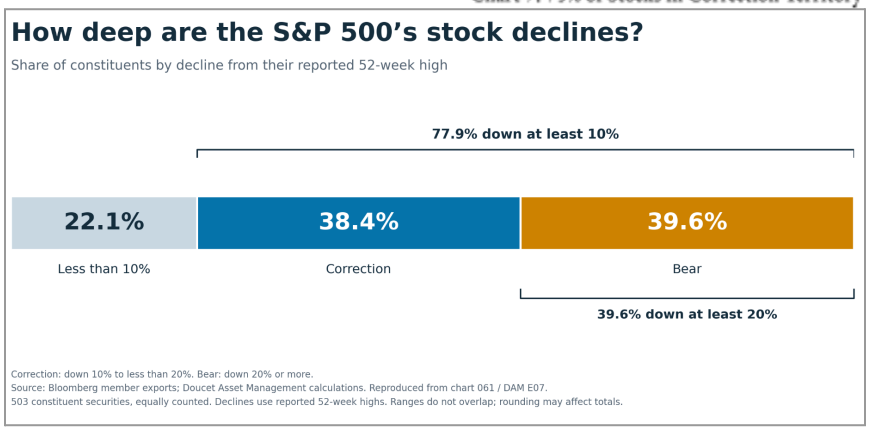
Chart 6: Consumer Confidence Low



While consumer sentiment has plummeted, consumer spending has remained strong. Overall spending numbers are dominated by the top 20% of households who are benefitting from the wealth effect. The stark contrast between Consumer Confidence and Consumer Spending Indexes match the equally stark divide in the stock market.

The indexes seem to hit new all-time highs almost daily, but over 75% of the stocks in the S&P 500 are in correction territory (see chart 7). Additionally, according to Bloomberg, 36% of all stocks in the Index are negative for the year.

Chart 7: 75% of Stocks in Correction Territory



So then how can the stock market continue to hit new highs? The answer: over 40% of the Index is composed of 10 stocks, whose futures rest firmly on the back of ever-increasing AI spending. As

evidenced by Chart 8, over 75% of earnings growth in the S&P 500 can be attributed to tech stocks. This has created a stock market and economy with one narrow theme supporting it.

Chart 8: AI Earnings Growth

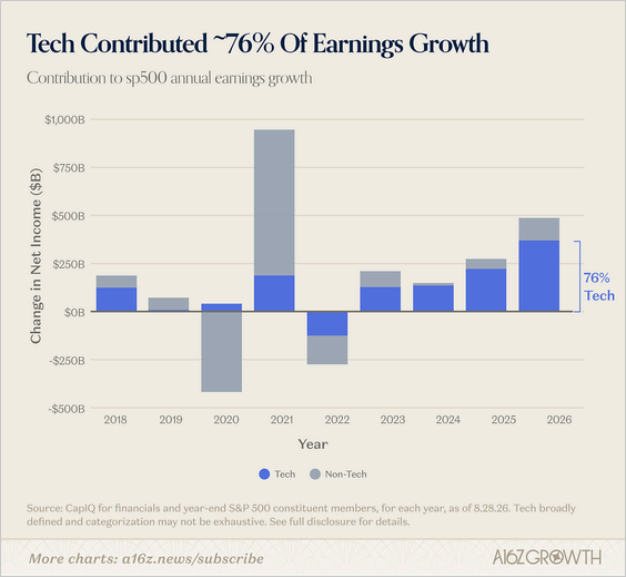
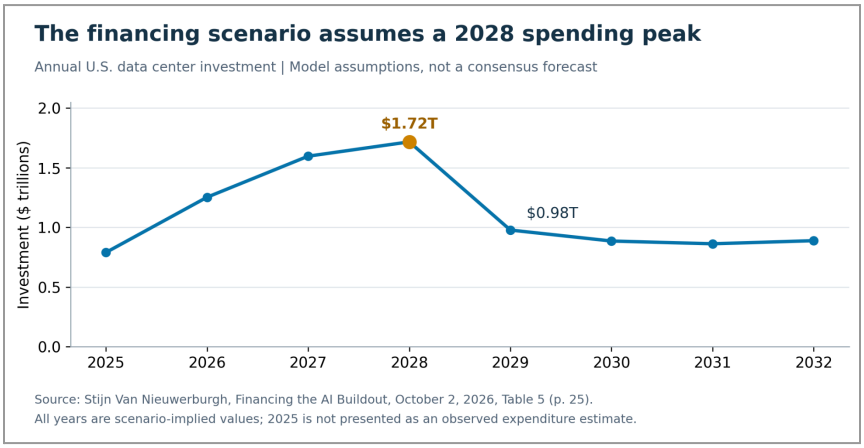


Chart 9: AI Infrastructure Buildout Peak



Changing Market Currents

Even the most hopeful forecasts for AI data center spending sketch a single luminous arc, rising toward its crest around 2028 (see chart 9) before descending into a long and steady fall. In that decline lies the promise of a seismic rupture in earnings, a fracture that will open in some distant hour, once the great build-out has reached its peak. The S&P 500 drinks in record earnings and crowns itself with new highs, almost daily, even as almost half of the Index is negative on the year.

But far below the shimmering surface, the strain gathers like a held breath along the fault line. Should these pressures endure, and should the great AI current turn and run backward in its bed, the rich silt it once laid down along the riverbank may loosen and drift downstream. There it would settle and new battures would rise from the shallows.

Sincerely,

Chris L. Probst

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