Constructive, Not Complacent | 08.28.2026

The market continued to grind higher in August, brushing aside a dizzying array of headlines. Iran, inflation, Federal Reserve policy, Treasury buybacks, data centers, AI spending, tariffs, and more have done little to knock stocks off course. The S&P 500 sits just below its all-time high and remains up more than 12% year to date. There is no shortage of things for investors to worry about, but the fundamentals remain solid.

Earnings continue to do most of the heavy lifting. Following a sensational second-quarter reporting season, analysts now expect S&P 500 company earnings to grow more than 33% in 2026, followed by another 13% in 2027. Both figures are well above the historical average of roughly 7.5%. If there is a concern, it is not the strength of earnings growth, but how much of it remains tied to a relatively small group of AI-related companies. Political opposition to new data centers is also emerging on both sides of the aisle, raising questions about the sustainability of the current investment boom.

So far, the actual numbers remain encouraging. Growth in business construction spending has slowed from the surge seen in 2023, but spending remains historically elevated. The pace of investment has cooled, but the broader building boom remains intact, and there is little evidence of the broad spending pullback many skeptics have been expecting. Investors may also be underestimating AI's impact beyond the companies building the infrastructure. Over time, the bigger story may be the companies using these tools to improve productivity, reduce costs, and support margins. If adoption continues to broaden, earnings growth could become less concentrated, providing a wider foundation for the market.

The risks, however, have not disappeared. Perhaps the most important tension today is the growing disconnect between the Fed's approach and the government's spending. The Federal Reserve remains focused on containing inflation pressures, even as the Treasury looks to pump more cash into the financial system by buying back twice as many of its own bonds. Put simply, one is trying to cool the economy while the other is focused on supporting financial markets. Strong earnings and a resilient economy have allowed investors to focus on the positives, but policies designed to support growth and markets can also complicate the Fed's effort to bring inflation fully back under control.

Geopolitics adds another layer of uncertainty. The situation with Iran remains unresolved, and any escalation could place renewed pressure on energy markets. Midterm elections are also approaching quickly. While the market has yet to experience the typical pre-election pullback, volatility has historically picked up during September and October as investors begin to guess how new policies might play out. These risks may not be enough to derail the broader bull market, but they are worth monitoring as we move into a seasonally more volatile period.

For now, we continue to view the backdrop as constructive. Unemployment is low, cash continues to flow freely, and earnings are strong. While policy uncertainty and geopolitical risks deserve respect, stock valuations remain reasonable relative to expected profit growth. We remain focused on high-quality businesses with durable earnings power and on identifying companies that can convert AI investment into measurable business results. As always, we will continue to adjust as the data evolves.

Thanks,
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