

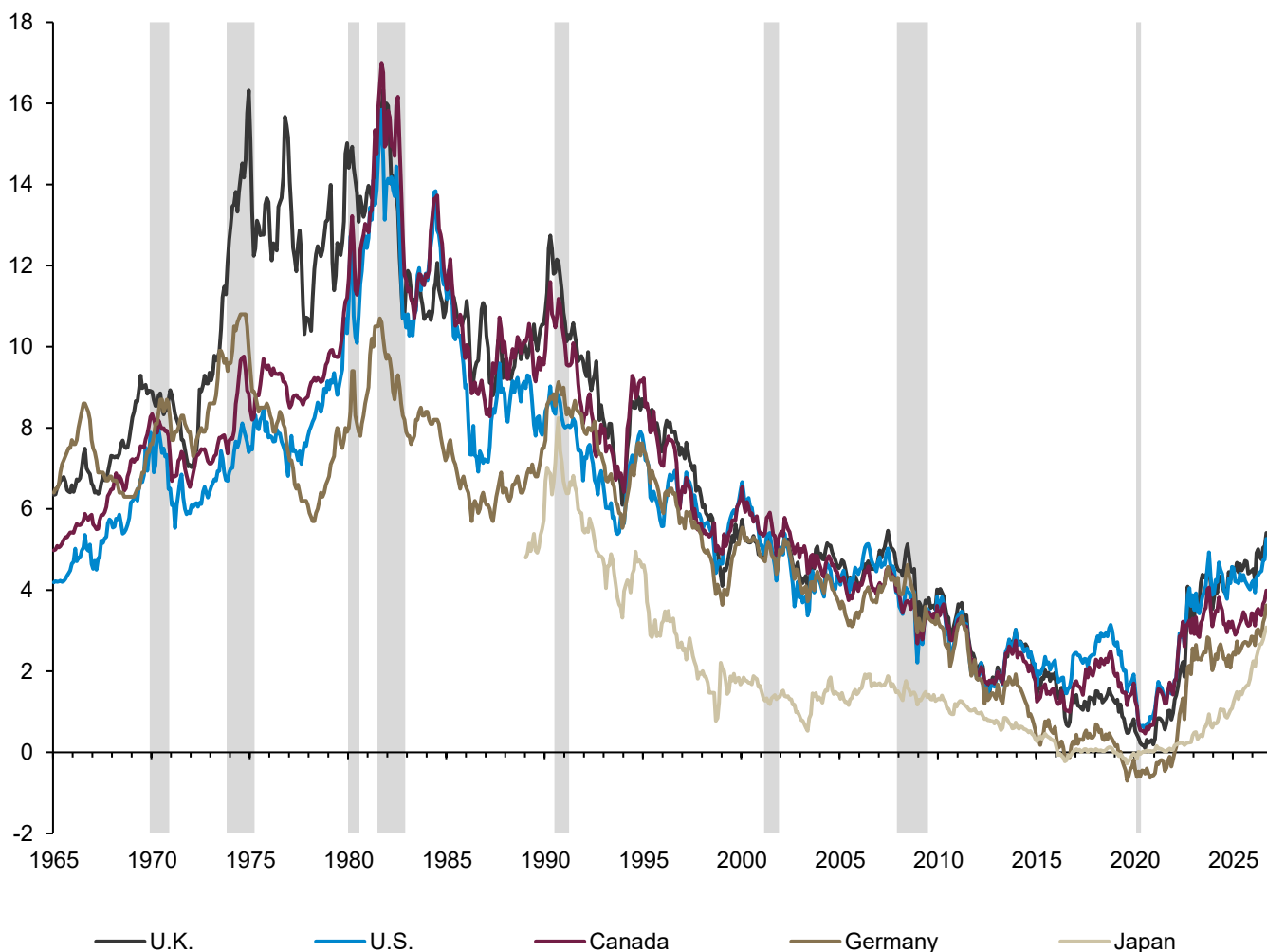


Bond Yields: We're Going Up, Up, Up, It's Our Moment...

Commentary

After declining almost uninterrupted for four decades, global interest rates have risen sharply from their pandemic era lows. Recent increases over the last few months have pushed government bond yields to their highest level in more than two decades, and in some cases, even longer.

10-year sovereign bond yields (percent, U.S. dollar basis)



Source: Guardian Capital using from Bloomberg, the Federal Reserve of St. Louis and Robert Shiller to September 29, 2026



For many investors, today's elevated interest rates represent a significant change from what they have experienced throughout most of their adult lives. Since the Global Financial Crisis in 2008/2009, policy rates have generally remained near zero, and the benchmark 10-year U.S. Treasury yield has not traded above 5% since June 2007. At that time, the median Millennial, now part of the largest demographic cohort, was just 18 years old. Accordingly, there are reasonable questions and concerns for investors regarding what higher interest rates may mean for financial markets and the broader economy.

As a starting point, it is worthwhile to explain why interest rates are where they are now.

Despite the many uncertainties that have plagued the economic outlook over the last six years, economic momentum remains on solid footing worldwide. Household net worth across Developed Markets is at all-time highs, supporting consumer spending and helping keep job markets tight, which in turn reinforces consumer demand. Concurrently, businesses have increased capital expenditures as they invest to capitalize on the opportunities presented by the ongoing technological and information revolution. These positive economic impacts are further compounded by the effects of substantial government spending and investment initiatives.

The resulting robust demand has placed upward pressure on prices. In an environment where the supply-side of the economy can grow sufficiently to keep pace with demand, these inflationary pressures would likely be contained. As it stands, however, limited inventories and capacity constraints, particularly in technology-related areas of production, have contributed to rising costs that are filtering through the broader economy.

Furthermore, the ongoing wars in Ukraine and the Middle East have disrupted the flow of key commodities and natural resources. Against a backdrop of strong underlying demand, these supply disruptions have contributed to rising commodity prices, particularly in energy markets. Higher energy costs have broad implications, affecting not only production processes, but transportation and logistics costs throughout global supply chains.

Add in the impact of increased trade barriers tied to U.S. economic policy changes and the net impact is that global inflation, the generalized increase in prices, has been persistently running above desired rates and is expected to continue to do so, eroding purchasing power and creating potential longer-term damage to economic stability.

In response, central banks have become increasingly focused on doing their part to rein in inflation, which means tightening monetary policy by raising short-term interest rates. Higher rates mean higher costs of capital which can restrain borrowing, temper demand growth and ease pressure on prices. Several major central banks have increased their policy rates, and more hikes are expected by more central banks in the months to come, which is putting upward pressure on longer-term market interest rates.



At the same time, governments are issuing significant amounts of debt to finance their hefty spending plans and ongoing fiscal deficits. The Organisation for Economic Cooperation and Development (OECD) estimates that governments will issue an additional US\$4 trillion in net new debt this year, in addition to approximately US\$14 trillion of required refinance for existing maturing liabilities. Meanwhile, “hyperscalers”, those huge cloud computing and storage companies, are increasingly tapping into debt markets to fund their massive capital spending plans. This significant increase in bond issuance, combined with uncertainty surrounding future public and private sector spending, has placed further upward pressure on market yields.

Higher interest rates are clearly less than ideal for borrowers, including households, businesses, and governments, as they make the costs of carrying new and refinanced debt more onerous. The prospect of rates remaining elevated, or moving higher still, also presents risks for economic growth, especially in interest-rate sensitive sectors such as real estate.

As such, higher rates typically serve as a headwind for equities. They increase financing costs for businesses, can weigh on economic growth and corporate revenues, and generally lead investors to lower valuation adjustments¹.

That said, the current level of interest rates and the expectation of further increases are in part a product of a global economy that has remained resilient and there is no reason to anticipate that momentum will soon be derailed. There is plenty of historic precedence for the economy and markets performing well in a world with non-zero interest rates, even if it is novel to a large swath of the population.

Further, higher rates benefit lenders, savers, and fixed income investors by increasing the income generated on their capital. Indeed, the current market environment is one in which fixed income securities are arguably the most attractive they have been in decades, particularly as a going share of the population approaches retirement and seeks reliable sources of income. This stands in sharp contrast to late 2020, when nearly one-third of the global bond market was trading at negative yields, effectively locking investors into losses if held to maturity.



Equity Commentary

The third quarter of 2026 delivered modest gains across the major developed equity markets, although the advance was narrow and the path more turbulent compared with the sharp rebound of the second quarter. In U.S. dollar terms, the MSCI EAFE Index of European and Asian markets rose 0.9% and the S&P 500 Index gained 2.3%. The Canadian market rose 1.6%, slightly behind the U.S., largely due to differences in sector composition. U.S. gains came mostly from large technology and semiconductor companies tied to artificial intelligence, an area where the Canadian market has relatively limited exposure. Meanwhile, Canadian banks, which represent the largest sector of the TSX, came under pressure late in the quarter as bond yields moved higher. A weaker Loonie widened the gap further by boosting the value of U.S. returns for Canadian investors.

With three months to go in the year, year-to-date developed-market equity returns in 2026 remain solidly positive. In Canadian dollar terms, the S&P 500 Index is up 16.8%, the MSCI EAFE Index is up 14.3% and the S&P/TSX Composite index up 13.0%. Artificial intelligence remains one of the market's dominant themes, with leadership once again concentrated this quarter in the largest technology and semiconductor companies. This follows a stronger first half of the year when market gains were more broadly distributed across sectors. The concentration was stark in September, when Information Technology and Communication Services were the only S&P 500 sectors to generate positive returns. Meanwhile, rising bond yields continued to weigh on more interest-rate-sensitive sectors such as Real Estate, Utilities, Consumer Staples, and Financials. While these sectors have been among the weaker parts of the market this year, their lower valuations may present attractive opportunities for long-term investors.

The sharp global market selloff in March, triggered by the outbreak of war with Iran, now feels increasingly distant following the subsequent recovery. Yet that resilience has come despite a difficult backdrop. Energy prices remain elevated, inflation has proven stubborn, and global bond yields have climbed to multi-decade highs, raising borrowing costs for households and businesses. Escalating trade tensions between Canada and the U.S. have added further uncertainty for a Canadian economy already struggling with growth challenges.

In response, central banks have shifted from an easing to a tightening stance. The U.S. Federal Reserve raised interest rates in September for the first time since 2023, while the Bank of Canada has signaled growing concern about upside risks to inflation, suggesting the potential for further policy tightening. While equity market performance in the coming months will reflect this confluence of factors, valuations remain reasonable across many sectors, particularly among high-quality businesses, providing a supportive backdrop for long-term investors.



Fixed Income Commentary

It was another challenging quarter for fixed income markets as solid growth momentum and persistent concerns about inflation, in no small way exacerbated by the renewed upward pressure on energy prices following the collapse of negotiations and ongoing war in the Middle East, drove notably hawkish turns from global central banks over the summer. The likes of the U.S. Federal Reserve, European Central Bank, Bank of Japan, and Reserve Bank of Australia, all raised their policy interest rates in the third quarter in response to inflationary pressures. At the same time, markets increasingly priced in additional hikes from these and other monetary policy authorities in the months ahead, including the Bank of Canada, which chose to leave rates unchanged during the period.

Upward pressure on market interest rates was further compounded by expectations for a surge in debt issuance from global governments looking to finance their sizable fiscal deficits, heightening investor concerns regarding fiscal sustainability. Concurrently, corporations, particularly the “hyperscalers”, are increasingly tapping the market to fund substantial capital expenditure plans, contributing to the global supply of securities and exerting further upward pressure on yields.

As a result, government bond yields rose significantly over the quarter and ended September at their highest levels in two decades. The sharp rise in yields drove a broad decline in fixed income markets, as bond prices move inversely with yields. The broad-based FTSE Canada Universe Bond Index dropped 3.0% in the third quarter, marking its worst quarterly performance in three years (and sixth worst quarter of the last 20 years). More rate-sensitive segments of the market underperformed, with the FTSE Canada Long-Term Bond Index falling 6.3% and the FTSE Canada Government Bond Index declining 3.2%. Short-Term and Corporate Bond Indexes fared somewhat better, declining 0.9% and 2.1%, respectively, but still finished the period in the red.

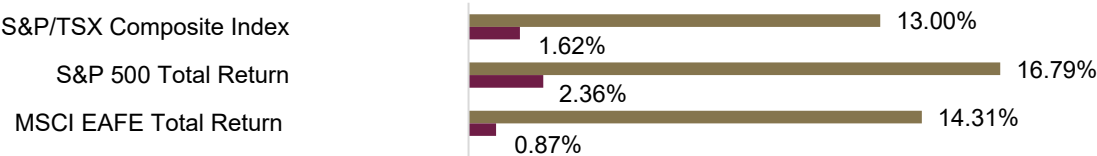
Looking ahead, in the absence of a sustained resolution to the war in Iran that sees the resumption of traffic through the Strait of Hormuz that results in a material decline in energy prices, there is little reason to anticipate a near-term turn of fortunes in the bond market. Upside risks to inflation and sustained growth momentum appear likely to keep the hawkish bias in place at central banks, which at a minimum suggests policy rates staying at their current levels for longer.

From an investor standpoint, however, while the near-term upside risks for rates and the low level of credit spreads are less than ideal, the all-in yield on offer in fixed income securities makes the asset class arguably the most attractive it has been in decades from a return and balanced portfolio diversification perspective.

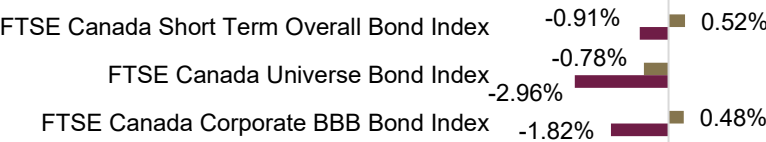


Market Indices Performance (C\$ - September 30, 2026)

Equity



Fixed Income



F/X Rate



-5.00% 0.00% 5.00% 10.00% 15.00% 20.00%

■ Year-to-Date ■ Q3 2026

Source Bloomberg: All figures stated in Canadian dollars as of September 30, 2026.

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Endnotes

¹ Higher interest rates mean higher discount rates that reduce the present value of future cash flows/earnings; assuming that valuation multiples such as price-to-earnings ratios stay constant, that implies declining prices.

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