The Weekly Market Update – 8/17/26: Recent Budget Trends Pressure Interest Rates

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	7,785.76	0.36%	3.82%	13.74%	22.82%	7,798.99	0.2%
Dow Jones Industrial Average	53,732.41	-0.56%	2.70%	11.80%	21.76%	54,349.12	1.1%
NASDAQ Composite	26,729.16	0.14%	1.97%	15.00%	26.54%	27,093.90	1.4%
Russell 2000	3,068.42	1.12%	1.46%	23.63%	38.74%	3,068.42	0.0%
MSCI EAFE (USD)	3,262.58	0.51%	4.68%	12.79%	24.71%	3,262.58	0.0%
MSCI Emerging Markets (USD)	1,701.17	2.61%	-1.26%	21.13%	36.84%	1,802.77	6.0%
Bloomberg Commodity Index	135.39	2.78%	9.91%	23.43%	33.80%	237.95	75.8%
Barclays U.S. Aggregate Bond	91.83	-0.19%	-1.32%	-2.38%	-0.41%	112.07	22.0%

Source: FactSet

U.S. interest rates remain elevated as markets assess inflation trends, but a negative reversal in U.S. budget deficit data has added upward pressure to long-term yields. On 8/17/26, the yield on the U.S. 10-year Treasury bond (which we view as a proxy for long-term interest rates in the U.S.) was 4.71%, near a multi-year high and up from 4.17% on 12/31/25. At the same time, the U.S. 2-year Treasury yield (TY, a proxy for short-term rates) moved to 4.17% from 3.48%. While both 2-year and 10-year yields surged higher in 2026 year-to-date (YTD), the 2-year TY peaked above 4.35% in late July and has since retreated. We attribute this to improving inflation data in June and July. July consumer inflation, as measured by the consumer price index (CPI), increased +3.4% year-over-year (Y/Y), meeting estimates and down from +4.2% Y/Y two months earlier. Improvement was attributed to lower and more stable gasoline prices in June and July. Excluding food and energy prices, "core CPI," increased +2.5% Y/Y, its lowest level since February (pre-Iran conflict). More stable inflation data (although above optimal levels) reduces the potential for a Federal Reserve Bank (Fed) interest rate hike (to its fed funds target) at the next Fed meeting in September. This helped to drive the 2-year TY lower. But 10-year yields were higher despite improving inflation data, and we attribute this to higher budget deficits in recent months, especially in July. The Treasury department reported a July budget deficit of -$432 billion as revenue (mostly taxes and tariffs) declined -1%, while spending increased +22% (after adjusting for timing differences that pushed expenses into July, the increase was +6%). With two months remaining in the federal fiscal year 2026 (ends 9/30/26), the YTD budget deficit was -$1.80 trillion (T) through July. This reflected an increase of +11% over the same period of FY25 (-$1.63T through July 2025). The full-year FY26 budget deficit could exceed -$2.0T and represent 6.2% of nominal gross domestic product (GDP), which was $32.5T annualized as of 6/30/26. We believe that bond investors have expected the deficit as a percentage of GDP to decline and that elevated long-term Treasury yields reflect concern that the ratio has moved higher in 2026.

The 2026 budget deficit increase is attributed to a reversal in net tariff collections following the Supreme Court ruling but should turn positive again as tariff refunds wind down. For the 12 months ended February 2026, the U.S. Treasury collected $304B in trade tariffs, representing a $222B increase from the 12 months ended February 2025. Tariffs comprised 44% of a rolling 12-month budget deficit that had dropped -24% in February 2026 (rolling deficit was -$1.63T in Feb 2026 vs. -$2.14T in February 2025). On 2/20/26, the Supreme Court ruled that tariffs could not be imposed under the International Emergency Economic Powers Act (IEEPA) and opened the door for refunds. Over the three months through July 2026, net tariff collections were payments of -$34B, compared to collections of +$76B in the three months ended July 2025, a -$111B three-month Y/Y reversal. But the Administration has started new tariffs under the Trade Act of 1974, with collections already underway. Other budget considerations are under scrutiny, however, especially costs to fund the military and Iran conflict and ongoing interest expense. Long-term rates are likely to remain higher if the deficit remains higher.

July retail sales disappointed but consumer activity was better than the headline suggested. July retail sales (Census Bureau) decreased -0.6% from June, missing the consensus estimate for a +0.1% increase. Excluding cars and gasoline, sales still declined -0.2%, but a good chunk of that was due to a timing shift from Amazon's Prime Day, which accelerated June data. Several store categories showed monthly growth in July, including restaurants, store retailers, clothing, health, and building supplies. On a Y/Y basis, retail sales increased +5.0%.

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The Russell 1000 index includes the largest 1000 companies (by market capitalization in the Russell 3000 index. The Russell 1000® Growth Index is a market cap weighted index that measures the performance of the large-cap growth segment of the U.S. equity market. It includes those Russell 1000 companies with relatively higher price-to-book ratios and higher expected earnings growth rates. The Russell 1000® Value Index includes those Russell 1000 companies with relatively lower price-to-book ratios and lower expected earnings growth rates.

The Global Industry Classification Standard (GICS) is a four-tiered, hierarchical industry classification system. Companies are classified quantitatively and qualitatively. Each company is assigned a single GICS classification at the Sub-Industry level according to its principal business activity. MSCI and S&P Dow Jones Indices use revenues as a key factor in determining a firm's principal business activity. The 11 sectors are: Communication Services, Consumer Discretionary, Consumer Staples, Energy, Financials, Health Care, Industrials, Information Technology, Materials, Real Estate, and Utilities.

FactSet is a data aggregation software utilized by D.A. Davidson's Wealth Management Research. The FactSet consensus refers to the aggregate of all analysts estimates from firms that submit estimates to FactSet for a given financial metric.

Volatility looks at to what degree and how quickly prices move over a given span of time. In the stock market, increased volatility, in the form of rapidly falling prices, is often a sign of rising uncertainty.

Gross domestic product (GDP) refers to the monetary measure of the market value of all final goods and services produced within a country's borders within a specific time period. Real GDP is adjusted for the impact of inflation. GDP numbers are compiled by the Bureau of Economic Analysis (BEA), a division within the U.S. Department of Commerce. Quarterly GDP is reported as a percentage change from the prior quarter, annualized. The BEA also reports data as a year-over-year percentage change from the same period one year prior. The most recent GDP report can be found at www.bea.gov. Major components of GDP include personal consumption expenditures, non-residential fixed investment, residential investment, government expenditures and adjustments for inventories and net exports (imports). Non-Residential Fixed Investment includes several subcategories including software and information processing equipment that measure investment in technology. Imports of goods and services are subtracted from GDP data (products are not produced or performed in the U.S) while exports are added to GDP.

The Federal Reserve Bank's Open Market Committee (FOMC) consists of twelve members – the seven members of the Board of Governors of the Federal Reserve System, the president of the Federal Reserve Bank of New York, and four of the remaining eleven Federal Reserve Bank presidents, who serve one-year terms on a rotating basis. The FOMC holds eight regularly scheduled meetings per year. At these meetings, the Committee reviews economic and financial conditions, determines the appropriate stance of monetary policy, and assesses the risks to its long-run goals of price stability and sustainable economic growth. The next scheduled FOMC meeting is over two days 9/15/26 and 9/16/26.

The term "monetary policy" refers to the actions undertaken by a central bank, such as the Federal Reserve, to influence the availability and cost of money and credit to help promote national economic goals. The Board of Governors of the Federal Reserve System is responsible for the discount rate and reserve requirements, and the Federal Open Market Committee is responsible for open market operations. The Federal Reserve influences the demand for, and supply of, balances that depository institutions hold at Federal Reserve Banks and, in this way, alters the federal funds rate. The federal funds rate is the interest rate at which depository institutions lend balances at the Federal Reserve to other depository institutions overnight. The Summary of Economic Projections (SEP) represent individual projections from Federal Reserve Board members and Fed bank presidents and rely upon individual assumptions.

The Treasury yield curve displays the market interest rate across different contract lengths for U.S. Treasury securities, indicating the relationship between the interest rate and the time ("term") to maturity. The yields of the 2-year and 10-year U.S. Treasury notes are widely followed barometers of the current U.S. interest rate environment. Treasury security data used in calculating interest rate spreads is obtained directly from the U.S. Treasury Department, through FactSet.

The consumer price index (CPI) is a measure of average change, over time, in the prices paid by urban consumers for a market basket of goods and services. It is reported monthly by the U.S. Bureau of Labor Statistics. The U.S. Personal Consumption Expenditures (PCE) Price Index is an indicator of the growth in consumer spending and measures the value of goods and services purchased by persons who reside in the U.S. It is reported monthly by the Bureau of Economic Analysis. PCE inflation is the percentage rate of change in the price index for personal consumption expenditures (PCE).

U.S. monthly receipts, outlays, deficit, or surplus are reported by the U.S. Treasury at fiscal.treasury.gov. Supporting data is also available from the Congressional Budget Office (CBO). The U.S. Treasury reports monthly budget details in its Monthly Treasury Statement, and prior to that monthly numbers are estimated by the CBO in its Monthly Budget Review. The CBO provides monthly data on payments for Medicare, Medicaid, Social Security, and Interest Expense. Tax receipts are also reported.

On 2/28/26, the U.S. and Israel launched an air attack on Iran designed to eliminate weapons capabilities and critical infrastructure. On 3/1/26, the White House published a release detailing the operation. Iran and the U.S. announced a ceasefire on 4/8/26 and a Memorandum of Understanding (MOU) on 6/17/26. The MOU is presented as a framework of a peace agreement to end the war that will be negotiated over a 60-day period. As of early July, fighting resumed and the ceasefire was effectively ended. Widespread attacks have been minimal since 7/24/26.

U.S. oil prices are often described using the price per barrel of West Texas Intermediate (WTI). This is a high-quality low density crude oil grade sourced primarily from the Permian basin. Futures contracts and spot prices are traded on the New York Mercantile Exchange (NYMEX). Brent crude reflects pricing for oil from the Atlantic basin. Many believe that Brent crude represents 66% to 80% of the global trade in oil. Brent contracts are trade on the Intercontinental Exchange.

On 2/12/25, The Trump Administration announced a framework for its Reciprocal Tariffs, with a link to the memorandum, "Fair and Reciprocal Plan." On 3/26/25, the White House announced tariffs on imported automobiles and certain automobile parts. Here is a link to a Fact Sheet from the president that outlines the action. The president referred to 4/2/25 as "Liberation Day" and released a Reciprocal Tariff Memorandum. Then, on 4/9/25, the White House delayed most reciprocal tariffs, and released a memo, Modifying Reciprocal Tariff Rates. This was considered a policy change (or pivot), and since then has led to negotiated trade deals (U.K., China, and Vietnam) while many of the other tariff pauses are scheduled to be implemented on 8/1/25 if additional trade deals are not signed. Many of the administration's reciprocal tariffs were levied using the International Emergency Economic Powers Act (IEEPA). On 2/20/26, the U.S. Supreme Court ruled that tariffs could not be used under the IEEPA statute. Many tariffs have been reimposed, often set at a lower rate than before, using section 122 and section 301 of the Trade Act of 1974.

Retail sales are reported by the U.S. Census Bureau in its monthly Advance Monthly Sales for Retail and Food Services report. The report provides an early estimate of monthly sales for retail and food service firms located in the U.S. The advance report utilizes a stratified survey from approximately 4,800 retail and food services firms. Data is reported month-over-month, year-over-year, seasonally adjusted and not seasonally adjusted.