



The Tatton Weekly

Back to narrowing market breadth

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This week's topics:

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Do markets care about the US midterm elections?

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Laudable reform initiatives – for the next parliament, Morton Morland, 30 September 2026

Bonds cast shadow over equities

Global equities struggled somewhat this week. US tech stocks are roughly where they were last Friday – but many others took a hit. Markets see AI-fuelled growth as *too* strong, raising interest rate pressures for the rest of the economy. But this week, those pressures came back to bite the AI leaders themselves. Today's lower-than-expected US employment figure eased concerns about an overheating economy, at least. As such, strong earnings growth should still be enough to buoy markets over the coming weeks.

UK finance commentators were disappointed by the lack of growth initiatives laid out in the Chancellor and Prime Minister's conference speeches this week. But while they are sceptical about longer term fiscal discipline, markets are not overly worried about that discipline in the shorter term. That helped sterling keep pace with a stronger US dollar – even as the euro came under pressure.

Valuations hampered by a bit of credit stress

Datacentre firm Oracle saw its borrowing costs spike, after sending a 'force majeure' notice for its Project Jupiter lease obligations. Investors took this as a sign of credit stress, perhaps a little unfairly; Oracle was basically just saying it should not have to pay rent for an unfinished site. Its beleaguered bonds sold off regardless, with knock-on effects for broader tech credit spreads (the premium of corporate bond yields over government-issued bonds).

Rising debt costs usually hit companies with weaker credit ratings first but, this week, the AI winners bore the brunt. That could just be a side effect of all their recent debt issuance. Rather

than a sign of AI firms' credit stress, markets might just be struggling to digest this many new bonds at once. Still, rising debt costs make AI companies less likely to borrow more.

The problem for tech stocks is not so much what high credit spreads say about their debt, but what they imply for share prices. On the face of it, price-to-earnings valuations have cheapened this year, as earnings growth has outpaced share price gains. But to better understand relative valuations, you should factor in both real (inflation-adjusted) government bond yields and corporate credit spreads, as they are competing investments.

S&P 500 price-to-earnings

Current PE ratio using analyst estimates, and Tatton model using bond yields



Adjusting for the recently higher real yields and credit spreads, it can be argued that from that angle, stocks should be cheaper or earnings stronger. We expect that the third quarter earnings reporting season, starting next week, will deliver strong profits – which generally ensures robust stock markets. But the attractiveness of real yields and credit spreads increases the pressure on companies to deliver those profits.

Good news is bad news; bad news may not be good news

Last week, bond yields were pushed up by strong economic data (government yields should theoretically reflect growth and inflation). So, you would think that this week's lower-than-expected US core inflation data would pull yields back down. Not so: real yields initially rose sharply again, before falling back.

Rising long-term real yields normally signify stronger growth expectations. Current US growth has moved back up to an annualised rate of 2.4%, after a summer soft patch. If consumer confidence rises in line with business confidence, the US economy would have too much demand for its supply and the Federal Reserve would have to slow things down. However, inflation itself is less concerning, and today's weaker-than-expected jobs report suggests consumers will remain reticent.

Meanwhile, the rest of the world is lagging. High energy prices are curtailing Europe's growth, more than raising its inflation. Real money supply has started contracting, which may even force the European Central Bank to turn dovish (preferring lower interest rates).

The mixed global growth outlook suggests bond yields are high for other reasons. Renowned market strategist Ed Yardeni wrote this week that the Bank of Japan's recent interest rate rises have had a profound effect on global bond markets. The so-called 'yen carry trade' – borrowing cheaply in yen to fund higher yielding US bonds – provided a backstop of global bond demand for years, but the BoJ's rate hikes have now made the trade less profitable.

Yardeni has a point, but the yen carry unwind is likely one of many factors, along with intense AI capital demand, increased fiscal risks and years of bond price volatility.

In any case, markets are in the strange situation where strong growth is seen as bad for bonds and, consequently, stocks – but weak growth is not good either. Right now, markets would probably only consider mediocre growth to be good news. That is why today's soft US employment gain lowered yields and buoyed stocks.

Geopolitics hurt but earnings could come to the rescue

What would be unequivocally good news for markets is lower oil prices. Rumours of possible US-Iran talks pulled oil below \$100 per barrel this week – reinforced by Middle Eastern oil exports reaching their highest point since the war began.

Unfortunately, oil rose back up after President Trump's dismissive response to Tehran's olive branch. It seems that 'Art of the Deal' tactics are preventing both sides from meaningful negotiation: any sign that Tehran is willing to compromise is seen by Washington as a weakness to be exploited rather than a window of negotiation, and vice versa. If a resolution on oil flow does come, it will most likely be quick and unexpected.

Other geopolitical tensions could also arise at the meeting of G20 trade ministers this weekend in Milwaukee – a prelude to the G20 leaders' summit in December. Russia's trade minister is there and Vladimir Putin will attend later this year, on Trump's invite. Given Putin's recent threats against Europe, this weekend's summit could be about more than trade. European leaders are considering releasing diesel reserves. These reserves are for international emergencies – not to buffer price movements. Given Putin's actions have raised the likelihood of war, leaders will want to persuade Trump not to bar US diesel exports in the coming days.

Corporate profits should at least bring good news. Judging by strong economic data over the last three months, the Q3 earnings season should be a good one for investors. Early results from chipmaker Micron back up that bullishness. As usual, strong company profits keep drowning out the worries elsewhere, particularly around valuations.

September asset returns review

September was a decent month for stocks in aggregate, with global equities gaining 0.9% in sterling terms. That aggregate figure hides significant disparities, however, as the table below shows. Oil prices rose sharply, and global bonds lost 1.7%. Stock market returns were lopsided too. Many major indices lost ground, but tech stock gains were enough to offset other losses for globally diversified portfolios. Even then, into the end of the month, investors began to wonder how long big tech could go it alone.

Asset Class	Index	Sep	YTD	12 months	2025	3-yr	5-yr	10-yr
						rolling annualised	rolling annualised	rolling annualised
Equities	UK Large Cap	-2.0	9.6	17.1	25.8	15.6	12.3	8.4
	UK Ethical Large Cap	-2.2	4.9	13.3	18.8	10.8	8.1	4.6
	Europe ex-UK	-2.8	6.7	13.2	26.2	13.9	8.9	9.2
	US Large Cap	1.7	14.2	17.3	9.8	19.5	14.1	15.1
	US Technology Large Cap	4.0	17.5	20.8	12.8	24.0	14.4	18.3
	Japan	3.6	24.2	28.3	16.0	18.1	10.1	9.3
	Global Stocks	0.9	14.4	18.3	13.9	18.3	11.9	12.1
	Emerging Markets	1.5	24.9	31.0	24.4	20.6	9.3	8.8
	China	-2.6	-9.3	-15.4	22.6	6.9	-1.3	3.6
Bonds	UK Gilts All Stocks	-1.2	-2.4	0.6	5.0	2.3	-4.3	-1.6
	£-Sterling Corporate Bond Index	-1.3	-1.0	1.7	7.3	5.5	-0.5	1.3
	Global Aggregate Bond Index	-1.7	-1.4	-0.7	4.8	4.0	-0.1	0.8
Commodities	Commodity Index	6.9	57.2	58.8	-0.3	14.2	17.7	10.0
	Brent Crude Oil Price	10.6	63.1	50.5	-24.1	-0.8	4.9	6.7
	Spot Gold Price	-7.1	-1.6	11.5	53.6	27.2	19.7	11.9
	Spot Silver Price	-11.8	-14.6	33.3	131.9	34.2	23.4	11.9
Inflation	UK Consumer Price Index (% Chg for period) *	0.5	2.5	3.1	3.4	3.4	5.1	3.6
Cash rates	SONIA 3-Month	0.3	2.8	3.9	4.5	4.7	3.6	2.1
Property	Global REITs	-3.5	6.2	5.4	0.3	7.2	2.0	2.9
Alternatives	Multi-Strategy Liquid Alternatives	2.9	8.9	11.2	0.3	4.7	4.5	3.2
	Bitcoin	8.1	-3.1	-25.8	-13.5	10.2	7.2	61.6

Source: Morningstar Direct as at 30/09/2026. * to end of previous month (31/08/2026). All returns in GBP.

September tends to be a difficult month for investors. Investment professionals come back from their holidays and often reposition their portfolios, leading to choppy market conditions. Historically,

it is the worst month for returns – so perhaps it is unsurprising that individual company share price moves were volatile.

Bond prices also fell significantly, as government bond yields (the inverse of prices) rose to multi-decade highs. This was led mainly by the US, whose 10-year treasury yield finished the month at 5.3%. A sell-off in the world's largest bond market naturally had knock-on effects for other markets.

Interestingly, the gap between UK and US government bond yields narrowed substantially through the month – with the UK (gilts) now only marginally higher. Usually, gilt yields rise faster than other markets, due to structural imbalances, so you could interpret gilts' slower rise as improving perceptions of UK fiscal policy *relative to* the US. Unfortunately, it is a hollow victory as long as gilt yields keep rising in absolute terms.

By now, investors are used to blaming higher yields on higher energy prices. Certainly, oil prices did not help. Brent crude oil rose to \$108 per barrel at one point, amid escalation in the Red Sea and continued disruption in the Strait of Hormuz. It fell back below \$100pb on the last day of the month, following Iran's new ceasefire proposal (since dismissed by President Trump). Oil prices finished September 10.6% higher in sterling terms, thanks partly to a rising dollar.

Even so, bond yields were driven more by growth expectations than energy. Business sentiment surveys were surprisingly strong in almost every major economy – but exceptionally strong in the US. The latest data are evidence of stronger economic growth, driven by AI-related investment. AI companies' desire to borrow and spend is seemingly unaffected by high energy prices and interest rates.

They are helped by persistently strong earnings growth and rising share prices. US tech stocks gained 4% in sterling terms last month, while other tech-heavy regions like Japan (+3.6%) and emerging markets (+1.5%) were also positive.

AI-driven growth in spite of high inflation is a concern for central banks. It suggests that further growth will spur further inflation. That is why the US Federal Reserve raised rates in its September meeting, and markets expect another hike in October. The European Central Bank and Bank of Japan raised rates too, while the Bank of England signalled a hike at its next meeting.

AI stocks might be resistant to rate hikes, but other assets are not. Tech firms' immense demand for capital raised the overall cost of borrowing, hurting non-tech companies everywhere. Small and mid-cap US stocks were hit, while UK and European markets finished 2% and 2.8% lower respectively.

AI's thirst for capital also hurt government bonds, compounding growth, inflation and fiscal fears. This is a mirror image of the 'crowding out' effect that people warn governments about, where excessive government borrowing stymies private sector investment. Now, it is the largest tech companies sapping up that investment.

Chinese stocks lost 2.6% in sterling terms, thanks to China's persistently weak economy. Beijing hinted at more economic stimulus, and delivered an interest rate cut of sorts, but consumption remains weak. Unlike the US, China has little business investment to make up for the shortfall in consumption.

At least China will not face extra US tariffs – for now. September's Trump-Xi summit delivered warm words but little of substance, though the sense of détente is a relief. It is also a slight positive for Trump ahead of November's midterm elections, but oil prices are still his main liability.

The fact broader emerging market (EM) stocks still managed a 1.5% gain shows how distorted the EM index is by just three semiconductor manufacturers: TSMC, Samsung and SK Hynix. Outside of tech, EMs are struggling. Their exposure to higher oil prices, and dependence on Chinese demand, is a troubling combination.

If markets get narrower but keep going up, how much should investors care? The answer depends on how long you think AI spending can go it alone. And, towards the end of the month, we saw signs that the big AI spend might be losing momentum after all: credit spreads (the difference between government and corporate bond yields) rose sharply for the so-called 'hyperscalers' (large cloud computing companies that build and operate data centres).

Given that hyperscalers have raised so much capital already, you would expect that credit spread increase to result in slower borrowing going forward. If that is right, the growth and inflation outlook could look less worrisome as we head into the end of the year.

Do markets care about the US midterm elections?

Donald Trump's Republican party is in a tough spot. The US midterm elections are a little over a month away, and the president's unpopular war with Iran is seriously hurting Republican chances of winning. On current polling, opposition Democrats are set to win the House of Representatives and stand a strong chance of wresting control of the Senate.

How might the outcome affect markets? The short answer is not too much, but there are some subtle risks and potential benefits.

Democrats likely to win both houses

The Democrats have always looked likely to win the House of Representatives in November's elections. Republicans achieved a wafer-thin majority in the lower chamber of US Congress in 2024, and the president's unpopularity has hurt them since. Republicans have some advantages: the so-called 'redistricting wars' (Republican-controlled states redrawing electoral maps for partisan advantage, and Democrat states attempting to follow suit but facing legal challenges)

somewhat tipped the scales in Republicans' favour, and the Supreme Court recently ruled in favour of unlimited campaign spending. But these advantages alone are not enough to overcome the sizeable Democrat polling lead.

The Senate is tougher for Democrats. Before this year, overturning Republicans' 53-47 advantage seemed impossible, given the seats up for grabs (Senators are elected on six-year cycles, with roughly a third of the Senate elected every two years). That has changed dramatically in the last few months.

Most forecasters now give Democrats a slightly-better-than 50/50 chance of winning enough Senate races to control the upper chamber. Betting markets, however, imply a higher chance of Democrat control (above 60%), while renowned forecaster Nate Silver puts their chances at more than 70%. That does not mean they will achieve substantially more seats (the current forecast is for a 52-48 Democrat-Republican split), but just a higher chance of gaining those seats.

It is not hard to see why Republicans are struggling. After his war on Iran sent oil prices flying, Trump has reached his lowest ever net approval rating. The once unwavering MAGA support base is splintering. High-profile allies have turned against the president, and the percentage of voters who "strongly approve" of Trump (i.e. the MAGA faithful) is dwindling.

In his blog, Nate Silver points out that rural, energy-producing states have been hit worst by fuel prices, due to their heavier reliance on diesel. That is a bad sign for Trump, as those states are typically skewed Republican.

Trump's agenda will be constrained, not curtailed

Midterm losses for the president of the day's party are common. Historically, these have severely limited the White House's ability to enact policies – but Trump tried to circumvent that block in his previous term, by the frequent use of executive orders. His second term has seen even greater reliance on executive orders, so it might seem like a Democrat Congress would barely be able to challenge Trump's agenda.

There are limits to what can be achieved through executive order, however. The Supreme Court's ruling against Trump's unilateral "Liberation Day" tariffs is testament to that. Given that the White House quickly moved to replace the struck-down tariffs, it is easy to be cynical about how much these rulings really limit presidential power. But the new 'Section 301' tariffs require a lengthy investigation from the US Trade Representative before they can be implemented. The White House might have the final say on tariff policy – but they can no longer be imposed at the president's whim.

The more Trump tries to achieve through executive order, the more likely he will be constrained by the Supreme Court. At first, the conservative-dominated court was reluctant to rein in the president but, as the administration has tested legal limits, even conservative judges have started knocking him back.

That means we are likely to see a more restrained White House, if Democrats win both houses. The impacts will be marginal but meaningful for markets. On tariffs, for example, we should not expect any repeat of last year's Liberation Day mayhem.

Could the Democrats curtail the president even more? The talk of impeachment is unrealistic, as successful removal of a president requires a two-thirds Senate majority. They could perhaps pass legislation forcing the White House to end its war on Iran (similar bills have been rejected by Republican lawmakers) but the president could veto it in the extreme. More likely is that Trump negotiates a deal with Tehran before new Congress members take their seats in January – as he has already suggested.

A midterm loss could kickstart the post-Trump future

The likely Democrat victory means little change for markets, while an unlikely Republican victory would mean no change. But what about an extreme scenario – like Trump attempting to nullify or overturn election results? Some of the administration's election policies and rhetoric have suggested Trump might make such an attempt. If so, US government bonds and the dollar would probably take a hit – even if the attempt failed. However, we suspect that the odds of White House election interference have decreased in the last few months.

The main reason for that is that the more aggressive sects of the MAGA movement – the likes of adviser Stephen Miller – have seen their influence fade with Trump's popularity. Republican politicians are now openly disagreeing with their president on multiple policies, especially Iran. Granted, that rhetoric tends not to match up with politicians' voting records, but it shows the Republican party shifting away from the president that has dominated it for over a decade.

Secretary of State Marco Rubio clearly wants to distance himself from Trump, ahead of a widely expected 2028 presidential campaign. Even Vice President Vance has hinted at distance between himself and Trump. After the midterms, we expect to see more of this positioning.

For markets, one of the key factors here is what this Republican positioning will mean for fiscal policy. Trump has been very willing to let the US fiscal position deteriorate, to the point where it is becoming an increasing concern for bond investors. Given that the Democrats have also been lax on fiscal discipline, many fear that there is no natural end to the expansion of US debt. But depending on how the midterms go, that political wind could change.

If Republican leaders renewed their pre-Trump desire for balanced budgets, that would at least signal to investors that there is some political pressure pushing Washington towards fiscal discipline. That could be a calming force for bonds. So, even if the midterms themselves do not impact markets much, what comes after might.

Global Equity Markets			02-Oct		Technical	Valuations			
Market	Level	% 1 Week	% 1 Week (GBP)	Short Medium		Div YLD %	LTM PE	NTM PE	10Y AVG NTM PE
UK FTSE 100	10493	-1.7	-1.7	→	→	3.3	13.6	13.3	12.6
UK FTSE 250	24285	+0.2	+0.2	↗	↗	3.4	8.2	14.3	13.0
UK FTSE All-Share	5668	-1.5	-1.5	→	→	3.3	13.0	13.3	12.6
FTSE Small x Inv_Tsts	6765	+0.3	+0.3	↗	↗	4.0	15.1	11.0	9.8
EU STOXX ex UK	806	-0.9	-1.9	→	↗	3.0	16.8	17.2	15.1
France CAC 40	7912	-1.9	-2.8	↘	→	3.3	15.4	15.1	14.1
Germany DAX 40	25276	-0.3	-1.3	→	↗	2.5	17.2	17.2	13.4
US S&P 500	7742	+0.6	+0.6	→	↗	1.1	23.4	21.6	19.1
US NASDAQ comp	27318	+1.5	+1.5	→	↗	0.5	31.6	27.9	26.2
Japan Nikkei 225	68309	+2.9	+2.8	↘	↗	1.3	22.1	25.3	18.8
World Bloomberg	2642	-0.2	-0.1	→	↗	1.5	20.3	18.8	16.7
China Bloomberg	1221	-2.0	-2.1	↘	→	2.4	13.4	14.0	12.5
Emerging Bloomberg	1807	-1.5	-1.5	→	↗	2.1	15.1	11.8	12.4
FTSE100 Top 6		S&P Global Top 6		(GBP terms)		Global Sectors			(GBP terms)
Company	%	Company	%		Sector	%	Sector	%	
Airtel Africa	+4.2	Resonac	+16.9		Tech	+1.8	Staples	-2.1	
Convatec	+3.8	Furukawa Electric	+15.6		Financials	-2.8	Energy	-0.8	
Barratt Redrow	+3.4	Carnival	+15.3		Health	-2.6	Materials	-1.5	
JD Sports Fashion	+3.0	Synopsys	+14.6		Discretionary	-0.3	Utilities	+0.4	
Polar Capital Technology IT	+2.9	Royal Caribbean Cruises	+14.5		Industrials	-0.5	Real_Estate	-1.4	
Halma	+2.9	Accenture	+14.4		Communications	-1.3			
FTSE 100 Bottom 6		S&P Global Bottom 6		(GBP terms)		Fixed Income			
Company	%	Company (GBP terms)		%		Govt bond		%Yield	1 wk chg
IG	-23.3	NIDEC CORP		-25.6		UK 5yr Gilt		4.86	-0.06
Lion Finance	-9.3	Fair Isaac		-23.2		UK 10yr Gilt		5.33	-0.03
Standard Chartered	-5.6	Cochlear		-12.6		UK 15yr Gilt		5.64	-0.02
Babcock Int'l	-5.6	Chocoladefabriken Lindt Sprueng		-12.3		US 10yr Treasury		5.21	+0.03
Fresnillo	-5.3	First Quantum Minerals		-12.3		France 10yr OAT		4.85	+0.16
Lloyds Banking	-5.1	Bayer		-11.4		Germany 10yr Bund		3.45	-0.15
						Japan 10yr JGB		3.08	+0.01
Currencies			Commodities			UK Mortgage Rate Estimates			
Pair	last	%1W	Cmdty	last	%1W	Rates (LTV c.75%, no fee)		02-Oct	02-Sep
USD per GBP	1.324	-0.0	Oil Brent \$:bl	98.82	-6.3	UK BoE base rate		3.75	3.75
GBP per EUR	0.852	-1.0	Gold \$:oz	4189	-1.8	2yr fixed		5.27	4.92
USD per EUR	1.128	-1.1	Silver \$:oz	61.52	-3.6	3yr fixed		5.29	4.77
JPY per USD	157.54	+0.2	Copper \$:lb	660.8	-1.9	5yr fixed		5.20	4.78
CNY per USD	6.702	-0.3	Alumnm \$:mt	3108	-4.5	10yr fixed		5.45	5.25
USD per Bitcoin	86,354	+3.4	Agriculture BBG	61.74	-0.4	Standard variable		6.58	6.58

Where possible, prices taken levels at 02 October 3:00 PM and 25 September 3:00 PM. Mortgage rates from moneyfacts.co.uk
LTM PE is the index price as a ratio of last 12 months earnings.

NTM PE is next 12 months earnings, adjusted for historic analyst overoptimism.

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