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SUMMARY

- A 5% 10-year rate is not a dealbreaker for stocks.
- Strong earnings growth can overcome rising rates.
- With the Fed now engaged, we think long rates are close to peaking.

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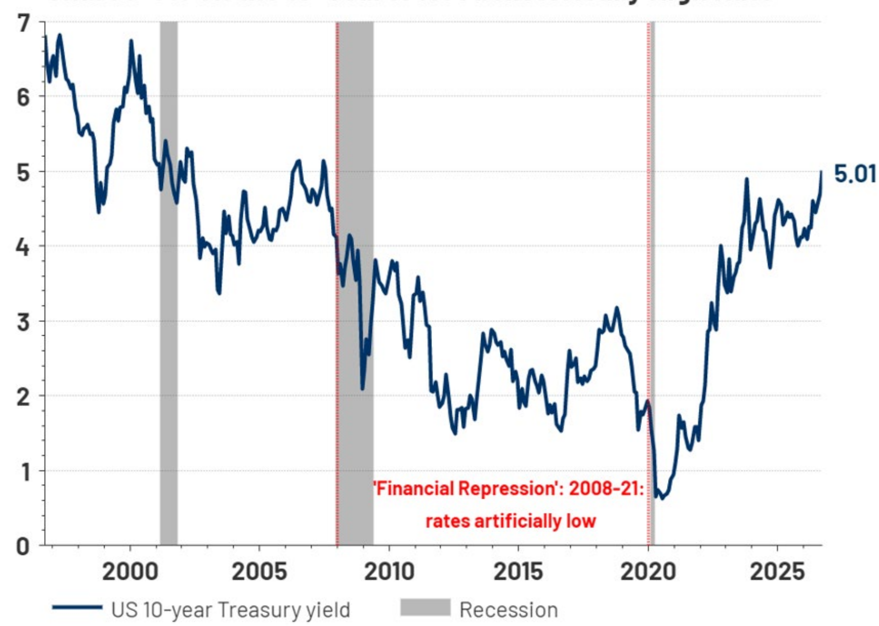
Rising Rates Not a Dealbreaker for Stocks

It Depends on the Reason for the Risin'

This week the 10-year Treasury yield crossed 5% for the first time since July 2007, while the Federal Reserve hiked the Fed funds rate by +25 basis points. For investors who began their careers after the 2008 financial crisis, when rates were incredibly low, a 5% risk-free rate must feel like a watershed moment. However, the chart below argues for perspective: across more than two decades, 5% is on the high end of the distribution. Instead, the sub-2% decade-plus of 'financial repression' after 2008 was actually the historical anomaly. **In short, a 5% Treasury does *not* have to be the harbinger of the end of the equity bull market.**

Chart 1: 5% on the 10-Year Is Not a Historically High Rate



Source: LSEG Datastream, RiverFront; data daily, as of 09.18.2026. Chart shown for illustrative purposes only. Past performance is no indication of future results.

To be clear: rising rates *are* potentially a headwind to equity valuations — because a higher discount rate tends to compress the multiple an investor will pay for a dollar of future earnings. However, it's worth noting that this headwind has already come to pass to a certain extent: the S&P 500's forward price-to-earnings ratio now sits near 19x, below its five-year average of 19.8x. Despite this, stocks are still up around 12% this year; this is possible because corporate earnings have done the heavy lifting, more than offsetting valuation compression. Consensus analyst estimates have calendar-2026 earnings growing more than +33%, with another 17% growth expected in 2027.

Two Very Different Reasons Rates Rise

Rates can climb for very different reasons, at opposite ends of the risk spectrum. The more dangerous version is inflation dramatic enough to choke

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off business activity. This forces the Fed to tighten hard into an economy already slowing, causing multiples and earnings to fall together. Historical examples of these periods include 1973, 1981 and 2022 – difficult times for investors. The more benign version is hiking into 'reflation': growth strong enough to pull inflation up with it, where the earnings cycle is typically robust enough to absorb the valuation hit. Historical analogs include 1957, 1994, 2004, and 2015; all meaningful rate hike cycles where the economy and earnings stayed resilient. In these instances, stocks fared much better over the succeeding years.

Today's economic data more resembles the second, more benign version to us. The Atlanta Fed's GDPNow tracker has third-quarter real growth running at 5.1%, though there is six weeks of data left before the books close on Q3. The S&P Global US composite PMI held at 56.0 in August. Payrolls added 162,000 jobs in August with unemployment steady at 4.1%. Most important to us, earnings revisions are still moving up. Rates rising into that backdrop is a fundamentally different animal from rates rising into a big economic or earnings slowdown. **History suggests that every rate hike cycle in which corporate earnings kept growing produced strong outcomes for stocks, despite rates moving higher.**

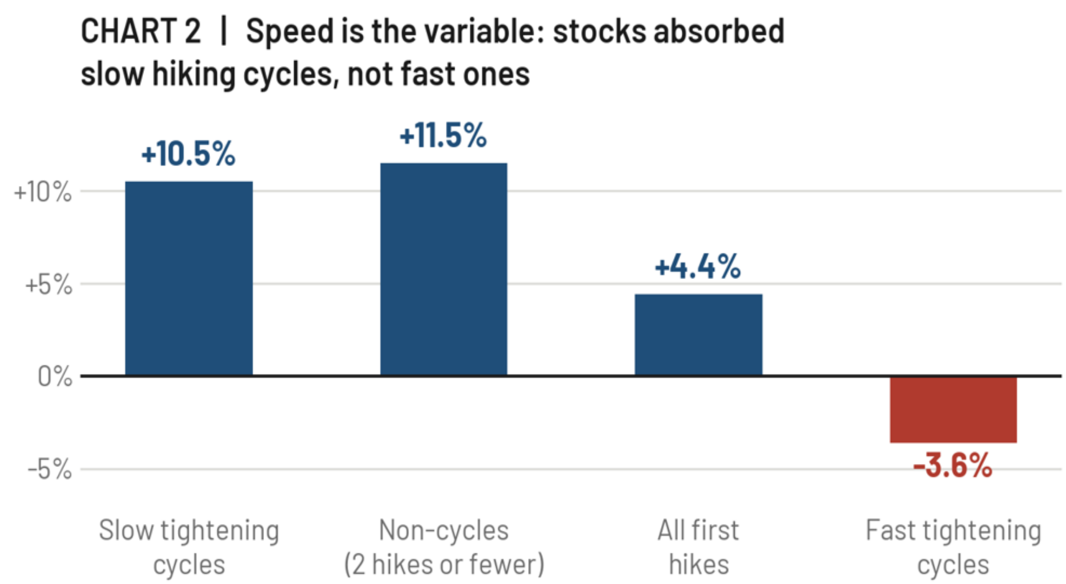
'Slow' Hike Cycles vs. Fast Ones

Historical analysis from Ned Davis Research adds some validity to these points. Sorting every first rate hike since 1946 by the pace of hikes that followed, NDR finds stocks gained +10.5% on average in the first year of 'slow' cycles — those in which the Fed waited at least a meeting between moves on average — but lost -3.6% in the first year of 'fast' ones, where it hiked at 3 meetings in a row. In 'non-cycles', defined by two or fewer hikes before a rate cut, stocks were up an average of +11.5%.

An interesting case study is 1999; the Fed hiked into a booming economy with rising oil-driven inflation and contained core prices — not far from today — and the S&P still fell nearly 40% over the following three years. However, we think the major difference to today is where the market started from a valuation perspective in '99. The S&P's trailing multiple was roughly 33x entering 1999, 60% higher than today. Speed matters, growth matters, and so does the price you pay going in. **The market's problem has never been that the Fed tightened; it has been when the Fed tightened in a hurry.**

Stocks Can Fare Well in Higher-Than-Average Rate Environments

We asked a related question of our own data. Sorting all 106 quarters since late 1999 by the fed funds rate's level relative to its full-period average and by its direction produces Chart 3, next page — not the answer most investors would guess. The best environment for the S&P 500 was not an easing cycle. Rather, it was a high and stable rate, which returned 5.4% per quarter and was positive 90% of the time. Above-average-and-rising — arguably where we sit today — still produced a positive 1.8% per quarter. Both negative buckets were falling-rate regimes, for the simple reason that the Fed usually cuts because something has broken. **High rates are not the enemy of equities. Cuts into economic weakness are.**



Average S&P 500 price gain in the first year after a cycle's first rate hike, by cycle speed, 1946- present. A "fast" cycle hiked at almost every meeting on average; a "slow" cycle waited at least one meeting between hikes; a "non-cycle" is two or fewer hikes before a cut. Source: RiverFront, from Ned Davis Research chart S859 (copyright 2026 NDR, Inc.). Chart shown for illustrative purposes only. Past performance is no indication of future results.

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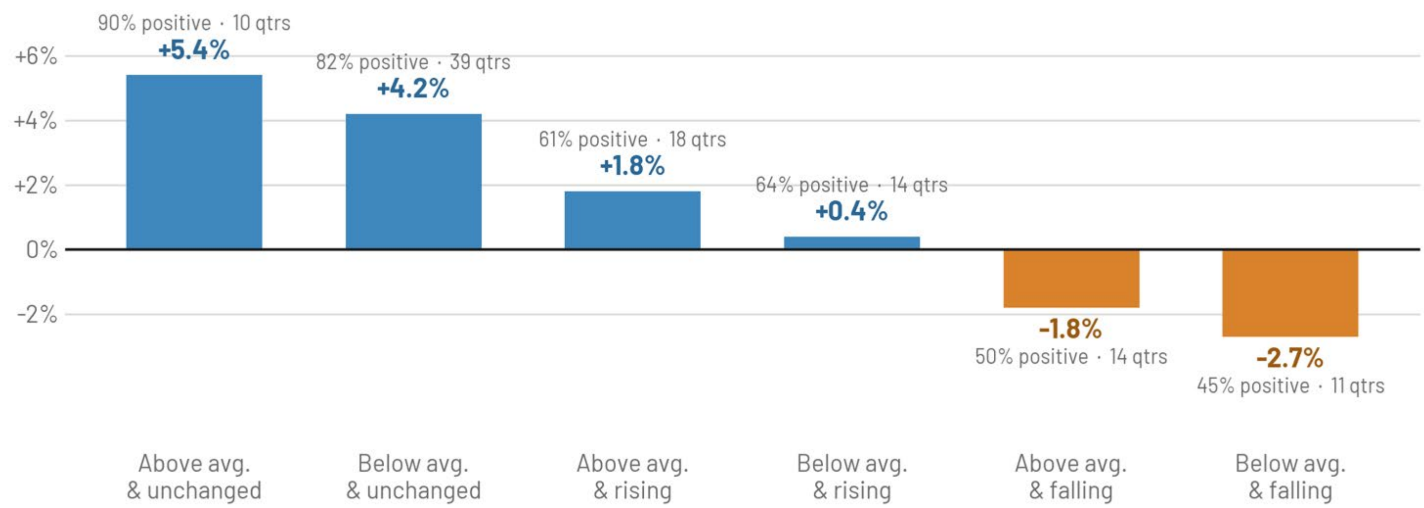
Conclusion: Higher Rates Alone Should Not Break the Stock Bull Market; Earnings Are the Key

How much further Chair Warsh goes is genuinely unclear; he has been explicit that he wants the market to show the way. We would note that the bond market has already done much of the tightening itself**.** For instance, the 2-year, the tenor most sensitive to fed funds, has risen from 3.4% at the end of February to 4.7%...the equivalent of five 25 bps hikes. Furthermore, inflation, while higher than the Fed's 2% target, looks nothing like the double digit 'Stagflation' of the 1970s. **We see about two more rate hikes in this cycle because we expect core inflation to be lower a year from now. Importantly, if we are right and the Fed continues to hike, then mid-to-long term rates may be close to peaking.**

We are not treating 5% as an automatic sell signal for stocks, as we remain constructive on corporate fundamentals for US stocks in general. What would change our mind is not the level of the 10-year, per se; rather, it would be a fast-hiking cycle concurrent with a meaningful deterioration in earnings. This is not our current view, so we remain overweight stocks in our balanced portfolios, watching earnings trends more closely than yield levels as a signal for equities.

Chart 3: Direction Beats Level on the Fed Funds Rate; Worst Quarters Came When Fed was Cutting, Not Hiking



S&P 500 average quarterly total return by fed funds regime, 106 quarters, 1999 Q4 – 2026 Q2. Each quarter is sorted by whether the average fed funds rate sat above or below the full-period average (2.07%) and whether it rose, fell or held flat (+/- 5bps) versus the prior quarter. Source: RiverFront, fed funds via FRED, returns via sector SPDR ETFs. Chart shown for illustrative purposes only. Past performance is no indication of future results.

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Standard & Poor's (S&P) 500 Index measures the performance of 500 large cap stocks, which together represent about 80% of the total US equities market.

Definitions:
Treasury bond yields (or rates) are tracked by investors for many reasons. The yields are paid by the U.S. government as interest for borrowing money via selling the bond. The 10-year Treasury yield is closely watched as an indicator of broader investor confidence. Because Treasury bonds (along with bills and notes) carry the full backing of the U.S. government, they are viewed as one of the safest investments.

Inflation is a gradual loss of purchasing power, reflected in a broad rise in prices for goods and services over time.

Stagflation is an economic condition characterized by slowing economic growth, high unemployment, and rising prices (inflation) simultaneously.

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