

## The Balancing Act

**The U.S. economy continues to show considerable strength, but the forces shaping the outlook are becoming increasingly complex.** The Fed recently raised interest rates for the first time in three years. This appears to be the start of a modest rate increase cycle which is currently expected to continue gradually into next year. Inflation has moved higher, oil prices remain elevated, and the Treasury Department has begun taking a more active role in the bond market. At the same time, economic growth remains strong, and the labor market continues to provide an important source of stability.

Taken together, these developments offer a useful look at the balancing act taking place across the economy. Policymakers are attempting to support continued growth and market liquidity while keeping inflation from gaining enough momentum to threaten that progress. The individual pieces can appear contradictory. **In many ways, that is the point: measures that support one side of the economy often create pressure somewhere else.**

### A New Tailwind from the Treasury

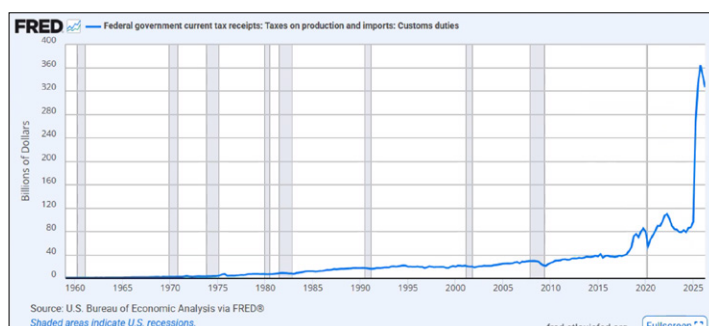
**One of the more significant recent developments is taking place in the bond market. The U.S. Treasury has increased its purchases of longer-term Treasury securities, including 10-, 20-, and 30-year bonds.**

When the federal government purchases bonds in the open market, those securities are exchanged for cash. That puts additional liquidity into the financial system. Banks and other large institutional investors that sell those bonds are then left with cash that can be lent, invested in other fixed-income securities, or deployed elsewhere in the markets.

The result can be a modest tailwind for economic activity and asset prices. Greater demand for longer-term bonds can also put downward pressure on their yields, which is relevant because the 10-year Treasury yield is closely connected to borrowing costs such as mortgage rates.

This shouldn't be confused with the large stimulus programs used during the financial crisis or the pandemic. It is better viewed as a targeted effort that can improve liquidity and ease some pressure on longer-term interest rates.

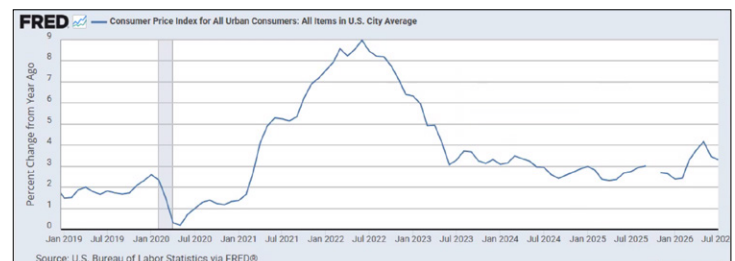
**The Treasury is also entering this period with substantial cash on hand.** Customs-duty receipts have risen sharply over the past year, providing an additional source of federal revenue and providing the Treasury greater flexibility in managing its debt and bond purchases.



### Inflation Remains the Key Risk

**If greater liquidity represents one side of the balancing act, inflation represents the other.**

Higher oil prices have contributed to renewed upward pressure on headline inflation. After falling substantially from its 2022 peak, the Consumer Price Index has turned higher again in 2026. Continued geopolitical tensions and elevated energy prices could keep that pressure in place.



Inflation itself, however, is only part of the equation. What ultimately matters to consumers is how quickly prices are rising relative to wages. When wages grow faster than prices, purchasing power can continue to improve.

However, when prices begin rising faster than wages, households have less room in their budgets and may eventually reduce spending.

**That relationship matters because consumer spending represents a significant share of U.S. economic activity.**

If inflation were to accelerate enough to materially outpace wage growth, the effects could eventually extend beyond household budgets and begin to seriously weigh on the broader economy.

*(The Balancing Act continued on next page.)*

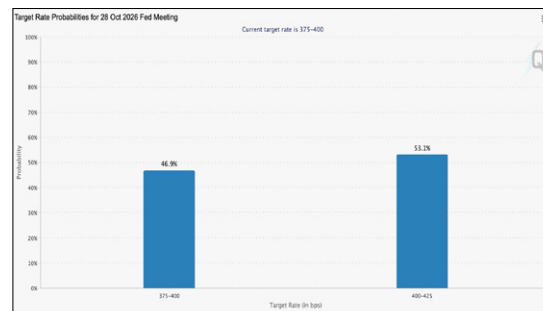
*(The Balancing Act conclusion from last page.)*

## The Federal Reserve Has a Difficult Decision Ahead

**The Federal Reserve sits directly in the middle of these competing forces.** Normally, persistent inflation would strengthen the case for higher interest rates. Raising rates makes borrowing more expensive and can slow demand, helping bring inflation under control. The tradeoff is that tighter monetary policy can also slow economic growth and weaken employment.

For now, the labor market appears strong enough to give the Fed some flexibility. Unemployment remains relatively low, job openings remain elevated and new unemployment claims continue to run at historically low levels. That resilience gives policymakers more room to focus on inflation without immediately putting the labor market at significant risk.

Markets currently reflect a divided outlook for the October Fed meeting, with approximately a 53.1% probability of a quarter-point increase and roughly a 46.9% probability that rates remain unchanged. That lack of consensus is notable this close to a policy decision and could contribute to short-term market volatility regardless of which direction the Fed ultimately takes.



## A Strong Foundation Beneath the Noise

**While these crosscurrents deserve attention, the underlying economy continues to provide an important source of support.** The Atlanta Fed's GDPNow model currently estimates 5.1% annualized real GDP growth for the third quarter of 2026. That represents a strong pace of economic activity and suggests the economy has meaningful room to absorb periods of uncertainty. The labor market reinforces that picture. Businesses continue to hire, unemployment remains relatively low and investment in areas such as technology, data centers and manufacturing continues to support economic activity.

**None of this means the economy is immune to setbacks.** Persistent inflation, higher energy prices or an escalation in geopolitical tensions could change the outlook. But the current economic foundation suggests it would likely take a more substantial shock to turn today's risks into a broader, sustained downturn.



## Keeping the Bigger Picture in Focus

The coming weeks may test investors' patience. September and October have historically been more challenging months for stocks, and uncertainty surrounding inflation, interest rates and the approaching election could create additional swings in the market.

Periods of volatility, however, should be viewed in the context of the broader economic picture. Growth remains strong, the labor market remains resilient and policymakers have multiple tools at their disposal as they work to balance inflation against continued economic expansion. There are risks on both sides of that balance, and the path forward is unlikely to be perfectly smooth. But short-term market turbulence does not necessarily signal a change in the longer-term outlook.

**As always, maintaining a disciplined investment approach and remaining focused on long-term financial objectives continues to be one of the most effective ways to navigate changing market conditions.**

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