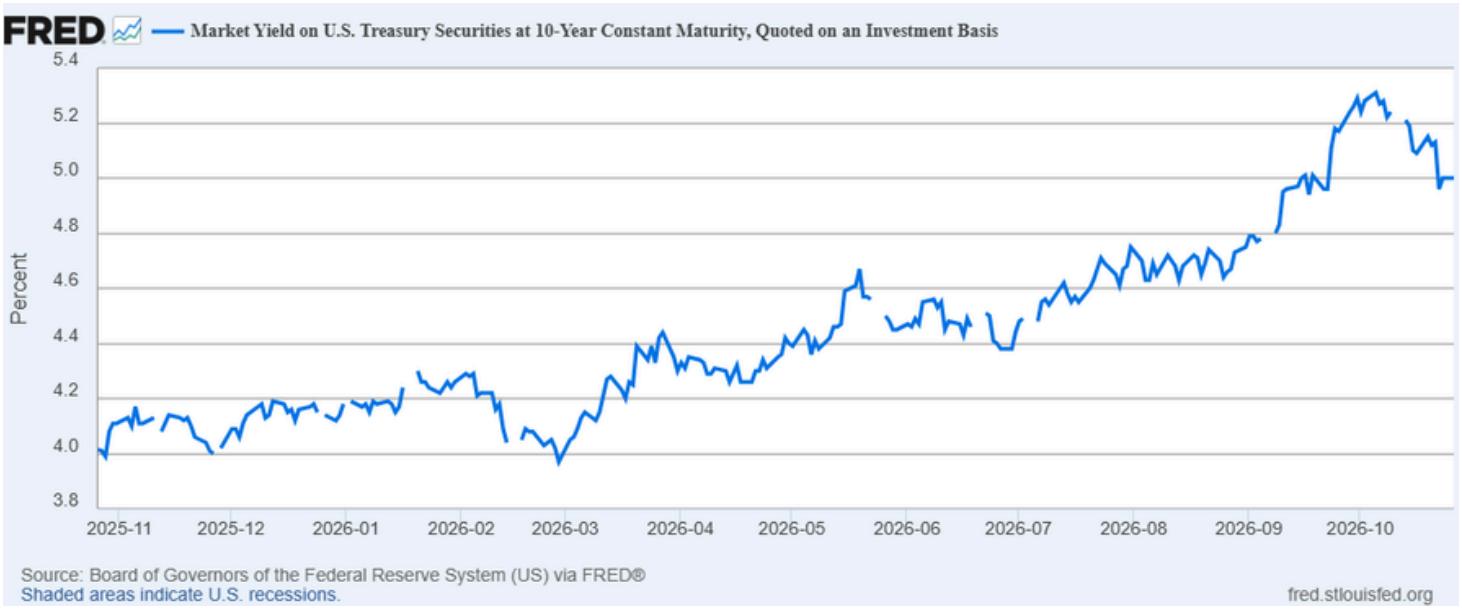
Mosaicfi *Market Insights*

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Q3 2026

WRITTEN BY JENIFER ARONSON, CFA

In the 3rd quarter of 2026, market news focused on two major questions: what was driving the sharp rise in interest rates in the bond markets, and whether we are in an AI bubble.

The rise in bond-market interest rates appeared to reflect investors' demand for a higher risk premium in response to several factors.

One was inflationary pressure from the war in Iran, which drove oil prices from $72 to $98 a barrel. That pressure increased the likelihood that the Federal Reserve will need to continue raising interest rates in the coming quarters.

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In September, the Fed raised the fed funds rate by 25 basis points—its first increase since July 2023.[1] Higher oil prices have not only made filling our gas tanks more expensive; they have also increased diesel fuel prices, affecting the cost of farming and transporting goods.

But inflation is not the only concern on investors' minds; governments around the world have been unable or unwilling to rein in spending and/or increase tax revenue and, as a result, have been issuing large amounts of debt to cover deficit spending. This problem has been exacerbated in 2026 as companies connected to the build-out of AI and data centers have been issuing enormous amounts of debt to fund their capital expenditures which, in our view, has been competing with government debt issuance.

Which brings us to the other topic on investors' minds - are we in an AI bubble? The debates and opinions expressed in the media vary widely. They range from 'maybe' to 'possibly' to 'probably'….

There has been a tremendous amount of capital spent on the buildout of the infrastructure needed to meet the anticipated level of AI demand.

Some estimate that annual spending could reach 3% of U.S. GDP over the next few years.[2] This includes building enormous data centers to house the chips required for all the AI computing power. The big question is whether the return on investment will be worth the enormous expense.

The Equity Markets

Global equity markets, as measured by the MSCI All Country World Index were up 1.08% in the 3rd quarter.[3] The developed international equity markets underperformed U.S. equity markets. International developed markets were up 0.89%[4] for the quarter vs. U.S. equity markets, which were up 1.41%.[5] Emerging markets underperformed developed markets for the quarter, down -0.37%.[6] U.S. REITs significantly underperformed the equity markets, down -5.37%.[7]

As small cap companies tend to be more sensitive to higher interest rates, the U.S. small cap market underperformed large cap stocks in the 3rd quarter. Small cap stocks were down -7.23%[8] for the quarter versus large caps, which were up 1.80%.[9] Large cap value stocks outperformed large cap growth; value stocks were up 2.61%[10] vs. growth stocks up .92%.[11]

The Fixed Income Markets

The concerns being whispered about in the 2nd quarter became a loud drumbeat in the 3rd quarter - would the Fed need to aggressively raise interest rates to stem the persistent inflation that has taken hold?

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Interest rates generally increased across the maturity spectrum. The most dramatic move was in the 'belly of the yield curve'- the yield on 5-year UST increased by 90 basis points.[12] The yield on the 10-year UST increased 85 basis points, ending the quarter at a yield of 5.29%.[13]

The U.S. bond market, as measured by the Bloomberg U.S. Aggregate bond index[14] returned -3.51% for the quarter. The municipal bond market, which typically lags the taxable markets when there is a dramatic spike in interest rates, underperformed the taxable bond markets. As measured by the Bloomberg Municipal bond index,[15] the municipal bond market ended the 3rd quarter, down -6.35%.

Corporate bonds underperformed the U.S. treasury market as spreads widened in the 3rd quarter. Intermediate corporate bonds returned -2.31%,[16] with comparable treasuries down -1.69%.[17] The high-yield market, which is less sensitive to changes in interest rates, ended the quarter down -1.82%.[18] Despite continued concerns over rising inflation, U.S. TIPS (inflation protected securities) returned -3.24% for the quarter as rising real yields drove the decline.[19]

Looking Ahead

As we look ahead, we don't expect the outcome of the mid-term elections to have a significant impact on the markets. Investors have grown accustomed to a lot of uncertainty around what comes out of Washington. It is anticipated that Democrats may sweep both the House of Representatives and the Senate.[20] This could create gridlock in getting any significant legislation passed over the next two years. For better or worse, this could provide a degree of certainty for the markets.

Despite higher inflation and interest rates, the economy remains in solid shape. The consumer has remained strong and willing to spend despite low consumer sentiment and frustration with the current inflation environment.

The strength in consumer spending appears to be due to a relatively low unemployment rate.[21] Even if people are unhappy in their current job but can't find a new one, they are still earning and spending. If we begin to see the unemployment rate tick higher and consumer spending decline, this could be a precursor to a slowing economy.

As always, we would love to hear from you, so feel free to contact us at any time.

Your paragraph text

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Sources

1 Source: Board of Governors of the Federal Reserve System, Federal Open Market Committee statement dated September 16, 2026. The Committee raised the target range for the federal funds rate by 25 basis points to 3.75%–4.00%. The prior increase occurred in July 2023.
2 Torsten Slok, Apollo Global Management, projects that U.S. AI-related capital expenditures could reach roughly 3% of GDP between 2027 and 2029 [confirm Apollo publication title and date]. Stijn Van Nieuwerburgh, "Financing the AI Buildout," NBER Working Paper 35865 (2026), estimates that a U.S. AI infrastructure buildout completed by 2032 would require nearly $9 trillion of total investment, or approximately 3.2% of GDP annually over 2025–2032. Estimates of artificial intelligence-related capital expenditures vary widely by source and methodology, are subject to change, and should not be relied upon as a prediction of future results.
3 MSCI All Country World Index (ACWI) data sourced from MSCI Inc. The index captures large- and mid-cap representation across developed and emerging market countries. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
4 MSCI EAFE Index data sourced from MSCI Inc. The index measures the equity market performance of developed markets outside the U.S. and Canada. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
5 U.S. equity market performance referenced here is measured by the Russell 3000 Index, which represents approximately 98% of the investable U.S. equity market. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
6 MSCI Emerging Markets Index data sourced from MSCI Inc. The index captures large- and mid-cap representation across emerging market countries. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
7 FTSE Nareit All Equity REITs Index data sourced from Nareit. The index measures the performance of U.S. equity real estate investment trusts. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
8 Small cap performance referenced here is measured by the Russell 2000 Index. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
9 Large cap performance referenced here is measured by the Russell 1000 Index. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
10 Large cap value performance referenced here is measured by the Russell 1000 Value Index. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
11 Large cap growth performance referenced here is measured by the Russell 1000 Growth Index. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
12 Yield data sourced from the U.S. Department of the Treasury's daily par yield curve rates; change in yield measured over the third quarter of 2026. Treasury yields are shown for reference only and are not indicative of the performance of any advisor-managed portfolio.
13 Yield data sourced from the U.S. Department of the Treasury's daily par yield curve rates. Treasury yields are shown for reference only and are not indicative of the performance of any advisor-managed portfolio.
14 Bloomberg U.S. Aggregate Bond Index data sourced from Bloomberg Index Services Limited. The index measures the investment grade, U.S. dollar-denominated, fixed-rate taxable bond market. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
15 Bloomberg Municipal Bond Index data sourced from Bloomberg Index Services Limited. The index measures the performance of the U.S. municipal bond market. This illustration is for reference only and not indicative of any client or model portfolio results.
16 Bloomberg U.S. Intermediate Corporate Bond Index data sourced from Bloomberg Index Services Limited. The index measures the investment grade, U.S. dollar-denominated, fixed-rate corporate bond market with maturities of 1 to 10 years. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.

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Sources, cont.

17 Bloomberg U.S. Intermediate Treasury Index data sourced from Bloomberg Index Services Limited. The index measures U.S. Treasury securities with maturities of 1 to 10 years. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
18 Bloomberg U.S. Corporate High-Yield Bond Index data sourced from Bloomberg Index Services Limited. The index measures the U.S. dollar-denominated, high-yield, fixed-rate corporate bond market. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
19 Bloomberg U.S. Treasury Inflation-Protected Securities (TIPS) Index data sourced from Bloomberg Index Services Limited. The index measures the performance of U.S. Treasury Inflation-Protected Securities. Index returns shown are for reference only and do not represent the performance of any advisor-managed portfolio. Investors cannot invest directly in an index.
20 Statements regarding the potential outcome of the November 3, 2026 midterm elections reflect the author's views as of the date of publication. Election outcomes are inherently uncertain. This commentary is not intended to express support for or opposition to any political party or candidate.
21 Unemployment rate data sourced from the U.S. Bureau of Labor Statistics, The Employment Situation. 4.2% as of September 2026.

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