

Weekly Market Commentary

Keep Calm and Clip Coupons

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Client Summary

The first half of 2026 brought several challenges for bond markets, including a change in Federal Reserve (Fed) leadership, rising geopolitical tensions, and a surge in borrowing tied to artificial intelligence (AI) infrastructure investments. Despite these events, bond markets have remained resilient, and LPL Research believes income opportunities continue to be attractive for investors seeking stability and diversification.

Positive Factors

- **Bond Yields Remain Attractive:** Starting bond yields are still well above their long-term averages, providing investors with meaningful income opportunities even if bond prices do not rise significantly.
- **Economic Growth Has Stayed Resilient:** The U.S. economy has remained stronger than expected, helping support financial markets and reducing concerns about an immediate economic slowdown.
- **Bond Markets Have Absorbed Major Shocks:** Markets have successfully navigated changes in Fed leadership, geopolitical unrest, and record levels of corporate borrowing without losing stability.
- **Corporate Financial Health Remains Strong:** Large technology companies investing heavily in AI generally maintain strong balance sheets, helping support confidence in the corporate bond market.

Concerning Factors

- **Inflation Remains Too High:** Inflation has improved from prior peaks but remains above the Fed's 2% goal, particularly in service-related areas such as healthcare and transportation.
- **Interest Rates May Stay Elevated:** Because inflation remains persistent, the Fed may keep interest rates higher for longer than investors had expected at the start of the year.
- **Geopolitical Risks Could Add Pressure:** Ongoing conflict involving Iran has contributed to higher energy prices, which can increase inflation and create additional uncertainty for markets.
- **Heavy AI-Related Borrowing Bears Watching:** Significant borrowing by major technology companies to fund AI infrastructure could place modest pressure on corporate bond markets, even though fundamentals remain solid.

LPL Research's Perspective

- **Income Is Likely to Drive Returns:** LPL Research believes investors should expect most bond returns to come from interest payments rather than large price gains.
- **Treasury Yields May Remain Range-Bound:** LPL Research expects the 10-year U.S. Treasury yield to finish the year in a range of approximately 4.00% to 4.50%, limiting the potential for major bond price appreciation.
- **Quality Fixed Income Remains Attractive:** LPL Research favors high-quality bond sectors and believes select mortgage-backed and asset-backed securities may provide attractive risk-adjusted opportunities.
- **Stay Disciplined and Diversified:** LPL Research believes investors should focus on long-term goals, maintain diversified portfolios, and continue emphasizing quality investments rather than attempting to time short-term market moves.

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