



Third Quarter 2026

KEEPING VIGIL

The market spent the third quarter watching the horizon for the appearance of bond vigilantes. Since a bond vigilante has not been sighted for over twenty years, investors don't really know what one looks like. Most are not even certain whether the, so far, mythical creatures are friend or foe. Still, nostalgia is in vogue and everyone loves a legend.

To recruit you to the quest, some definition might be useful. Pre-millennial-period bond vigilantes scared politicians into having fiscal discipline. The vigilantes would raid the bond market, driving up interest rates until either government spending or money supply growth relented. The heroes wore bespoke suits and rode the dusty trail in the equivalent of today's G-wagons.

Have they returned?

Ten-year Treasury rates rose over ninety basis points in the third quarter. Some would call that movement a twenty percent increase in interest rates. If the celebrated vigilantes organized such devastation, however, it proved to be of little consequence to the government (or the equity markets for that matter). The three-headed monster of inflation, debt, and M2 money supply kept growing under the dog-year-old promise of transience.

While still losing the war, the suspected bond vigilantes might have regained some fighting form. Proof of life comes from the failed long bond intervention by Treasury Secretary Scott Bessent. He proposed a two-billion-dollar purchase. When that didn't work, he upped the ante to six billion. The market ran over that measly sum, gapping interest rates increasingly upward. The sword play left the market yearning to know the identities of the masked men and women involved. To date, the specters remain nameless.

Back in the day before their own disappearance (increasing snark alert), economists used to observe relationships between interest rates and equity prices. That relationship was inverse: higher interest rates necessitated lower equity prices. They even had formulas, one of which calculated a three percent equity market decline for every one quarter of one percent increase in interest rates. Current financial systems don't seem to care much for truant economists.

The Fed model, another economic relic named after the central bank once in control of the money supply, compares ten-year Treasury rates to S&P 500 earnings yields. With Treasury rates now gapping above earnings yields for the first time in a decade, bonds,

though under presumed attack, might actually be more attractive investments than stocks. The "might" depends on the government's willingness to engage in enough fiscal discipline to stem inflation.

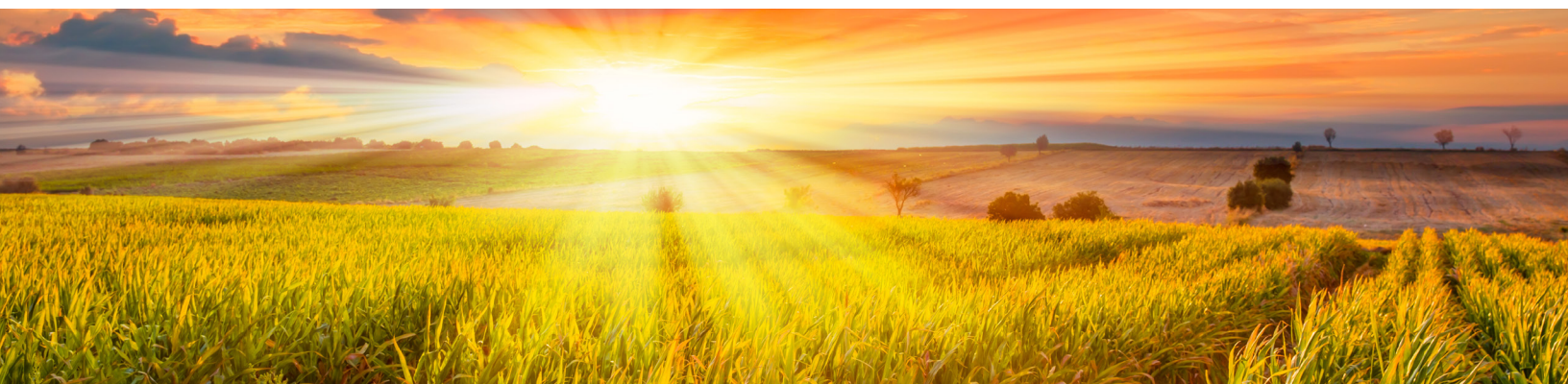
In the olden days, the bond vigilantes would continue to levitate interest rates until something that mattered broke. If they mount another charge, it might be AI, or the economy, or the stock market in the crosshairs. We'll see the extent to which the band of suspected vigilantes is large and motivated.

The successful track record of the bond vigilantes is Madonna-era ancient history. Moreover, the heretofore mentioned three-headed monster is a colossus the size of which no vigilante has ever seen. If vigilantes walk among us, and they can make interest rates matter to investment decisions for the first time in decades, the bond vigilantes may just make a viable investment vehicle out of their namesake.



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