

Q3: A positive quarter for stocks, bond yields rise

The third quarter of 2026 was positive for investors, as both the S&P/TSX Composite Index and S&P Index touched record highs as they eked out slight gains over the three-month period.

In the United States, equities continued to benefit from healthy growth and exceptional earnings, with the latter doing much of the heavy lifting as valuations have moderated since the beginning of the year. A key question is whether AI spending will ultimately generate the necessary returns to justify increasingly high earnings expectations.

Canadian stocks were driven by a different earnings mix, with higher oil prices lifting energy companies and stronger earnings from financials and materials providing broader support.

Europe and Japan continued to demonstrate the value of looking beyond the United States by providing different business exposures and return drivers than technology-heavy U.S. benchmarks.

We remain constructive on equities and see room for a modest overweight in balanced portfolios. Strong earnings and economic growth remain supportive, but concentrated AI exposure, geopolitical risks and tighter financial conditions reinforce the need for broad diversification across companies, sectors and sources of risk.

Bond yields surge

U.S. and Canada long-term government bond yields continued to rise during the quarter and are now at levels not seen since before the global financial crisis. This has weighed on bond prices, but higher yields may provide a more attractive starting point for investors, though future returns aren't guaranteed.

Several forces may keep long-term yields elevated, including sticky inflation, government deficit spending and debt issuances from AI-related companies to fund capital spending. Governments and corporations are effectively competing for the same pool of global capital, and investors may require higher yields to absorb the additional supply.

However, government bonds shouldn't automatically be the first choice simply because their yields have moved higher. North American and European investment-grade corporate bonds can offer similar or better yields, with additional compensation for credit risk. Corporate balance sheets and cash flows remain healthy, and the quality of the high-yield market has improved.

From resilience to expansion

The global economy continued to move from resilience toward expansion during the quarter. This shift has been fueled by a combination of large fiscal deficits, rising defence spending, investment in the energy transition and, most importantly, the AI infrastructure buildout. The

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result isn't a traditional boom, but an environment in which growth remains reasonably solid, inflation settles above central bank targets and interest rates creep higher.

U.S. growth has been good rather than merely resilient, supported by fiscal policy, consumer spending and a powerful capital expenditure cycle. The “no hire, no fire” labour market backdrop suggests the economy is neither overheating nor approaching recession.

Canada began the year in a fragile, low-growth environment, but activity has improved, supported by manufacturing, energy, government spending and early data-centre investment. Despite this progress, weak productivity, cautious consumers and uncertainty around the Canada-U.S.-Mexico trade agreement are likely to temper the recovery. Canada is improving, but considerable work remains.

AI investment, meanwhile, has become an important engine of global growth. Spending on data centres, semiconductors, networking equipment, power generation and cloud infrastructure is benefiting industrials, utilities, construction and manufacturing. While these investments could sustain activity for years, their growing reliance on debt and equity financing warrants monitoring

Inflation remains a key risk in this environment. Disinflation is visible in areas such as shelter, but recurring shocks from tariffs, energy and AI-related demand have interrupted the path back to target. Central banks, therefore, have less room to ease than investors expected heading into the year.

Vigilance and opportunism

Overall, the third-quarter message is to stay vigilant but opportunistic. Economic growth remains supportive of earnings, but inflation, interest rates and geopolitical risks are likely to keep volatility elevated. Investors should avoid becoming overly defensive while maintaining a portfolio built for both resilience and opportunity.

A well-built portfolio should retain meaningful equity exposure, use fixed income as both a source of income and a potential ballast, and diversify across underlying business risks rather than relying on asset-class labels alone. The goal isn't to predict every change in the weather, it's to make sure the portfolio has an umbrella while remaining positioned to benefit when the sun is shining.

If you'd like to discuss recent market movements or your portfolio, please reach out.

Sincerely,

Scott Gravesande
Senior Financial Advisor

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