

Look at the Markets

An in-depth analysis of U.S. and world markets focused on complexities, risks, and trends shaping the economic landscape

FOURTH QUARTER 2026

Commerce Trust
Banking | Investments | Planning®

Table of contents

3 Letter from the Chief Investment Officer

4 Real Gross Domestic Product (GDP)

5 U.S. Energy Consumption

6 Employment's Shifting Picture

7 Inflation Persistence

8 U.S. Debt, Deficits, and Higher Borrowing Costs

9 Federal Reserve Interest Rates Reverse Course

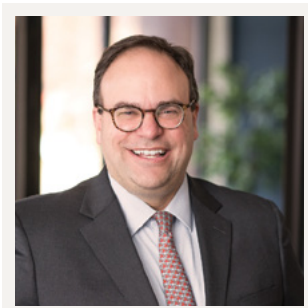
10 The Shifting Landscape of Artificial Intelligence Exposure

11 $3 Trillion of Contracted Artificial Intelligence Buildout

12 Indices Change Over Time

13 Global Earnings Momentum versus Long-term Performance

14 Liquidity Constraints Continue to Weigh on Private Markets



From the Chief Investment Officer

Throughout 2026, the U.S. economy and financial markets have endured a succession of significant distortions that have influenced interest rates, economic growth, and equity markets.

These wide-ranging influences include the artificial intelligence (AI) revolution, fiscal policy, the labor market, and inflationary pressures, which have acted as accelerators and detractors to the economy. We believe these dynamics will have a moderating effect going into 2027 and throughout the coming year.

Over the course of the third quarter in 2026, the rising tide of the AI infrastructure buildout left the equity market grappling with how much capacity is necessary and how the buildout could affect employment and productivity. That tension led to a slump in September that kept the market range-bound, as market participants deciphered rising earnings and slower consumer spending from higher prices.

In the fixed income market, inflation and the AI buildout were priced into longer-term bonds, while AI hyperscalers were on pace to issue $510 billion in debt to finance data center construction.

We remain diligent in exploring opportunities and risks inside financial markets as we construct portfolios based on individual client needs, characteristics, and goals.

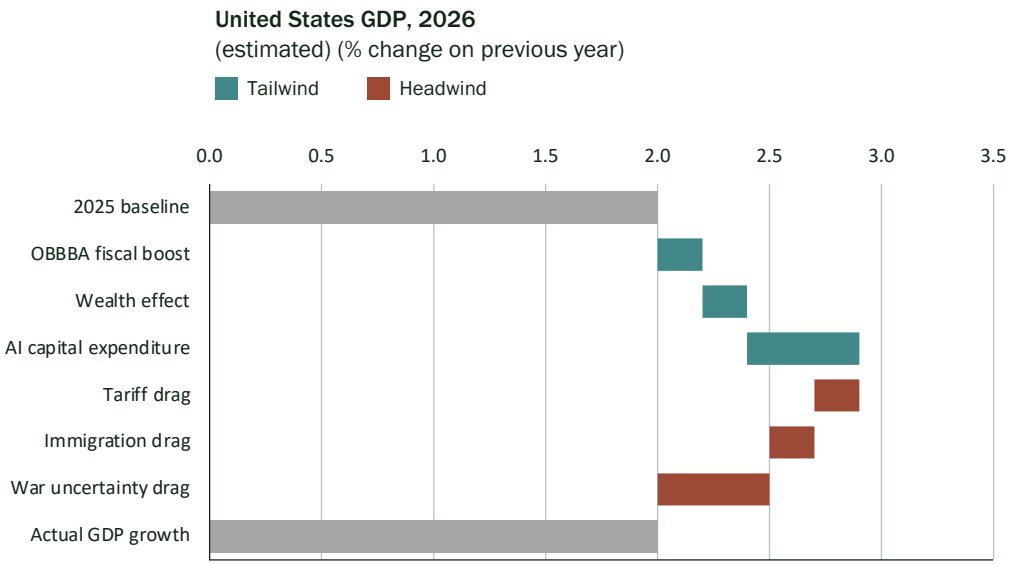
I encourage you to explore this edition of Look at the Markets and thank you for your confidence in Commerce Trust.



DAVID HAGEE
Chief Investment Officer
Commerce Trust

Real Gross Domestic Product (GDP)

Distortions have affected U.S. economic growth in 2026



Source: Bureau of Economic Analysis (real GDP year over year as of 9/30/2026), Commerce Trust.

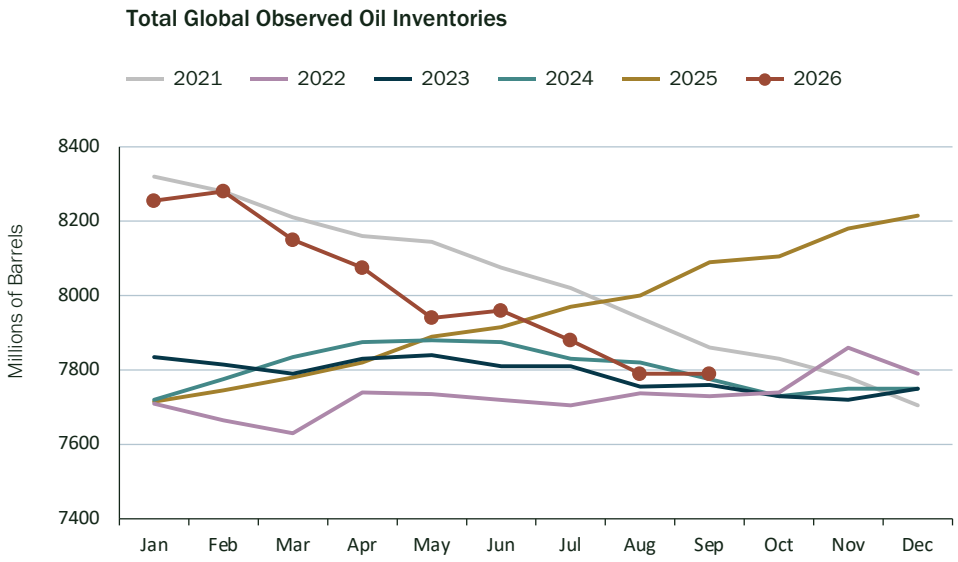
At the start of 2026, we projected the U.S. economy would grow by 2% based on fiscal tailwinds from the One Big Beautiful Bill Act (OBBBA) and tariffs being digested in 2025. The first half of 2026 saw inflation rise along with the Middle East conflict and uncertainty about how the war might hamper the U.S. economy. The Trump administration's immigration policies shifted the jobs landscape as well.

Prior to the conflict, 20% of the world's oil supply moved through the Strait of Hormuz. Since then, oil has hovered around $100 per barrel, and lower-income consumers have slowed their spending in response to higher gas prices, dampening broader consumption, which makes up about 70% of the U.S. economy. Energy-price-driven inflation, paired with shifting consumer dynamics, constrained the economy on one hand while the artificial intelligence (AI) buildout provided a lift.

As the economic expansion continues despite some additional headwinds, this environment historically favors equities while we continue to keep an eye on risk.

U.S. Energy Consumption

Oil reserves dampened the economic impacts of the oil shock



Source: Energy Information Administration (EIA), Federal Reserve Bank of Boston, Yale Lab, Commerce Trust.

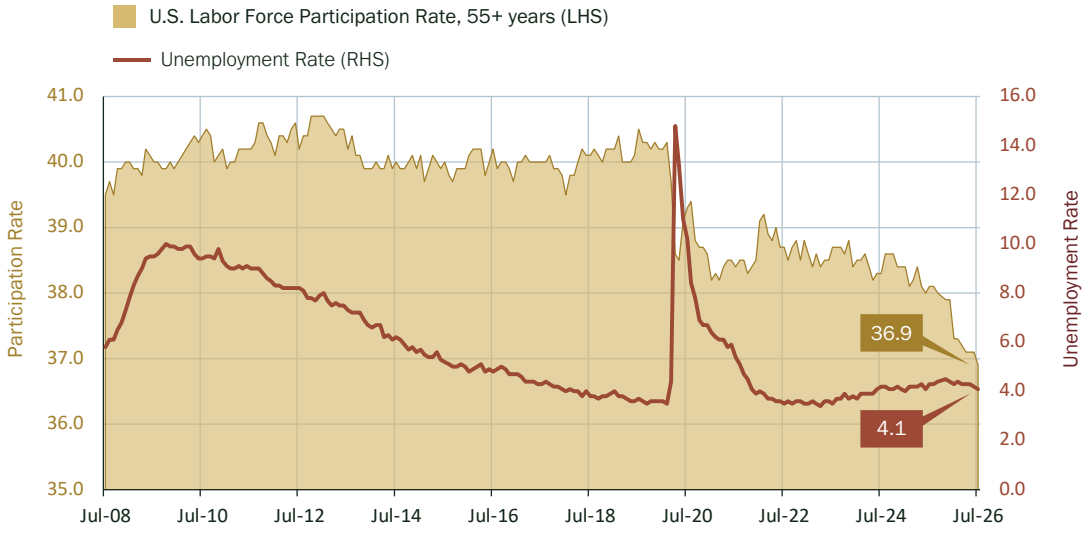
The Middle East conflict's energy shock pushed global oil prices to $144 per barrel inside the second quarter. The global economy relies on oil, with global demand around 105 million barrels per day. Historically, energy shocks have caused inflation surges and economic disruptions. The oil shocks of the 1970s reduced gross domestic product (GDP) by 1.74% and raised the consumer price index (CPI) by 2.2%. Today, the U.S. is energy independent, insulating the economy from the effects of higher energy prices but putting pressure on consumers at the pump.

In prior energy shocks, the world had fewer energy reserves to offset higher prices. With the current energy crisis, oil importers have used their reserves to make up for the lack of oil flowing through the Strait of Hormuz. As the conflict drags on, importers are becoming more reluctant to use their oil reserves to meet domestic demand.

The resilience and flexibility of energy producers and suppliers has kept the U.S. on track for economic growth. We anticipate Real GDP growth of around 2.0% for 2026. While market reactions have produced higher energy prices, putting inflation into focus, the Federal Reserve's (Fed's) reaction has been to raise interest rates twice, with a further rate hike projected in December. With higher interest rates, we expect economic growth to moderate throughout 2027.

Employment's Shifting Picture

U.S. labor force shrinks in response to economic environment



Source: Bureau of Labor Statistics, Federal Reserve Bank of St. Louis, Bloomberg (seasonally adjusted data through 07/31/2026).

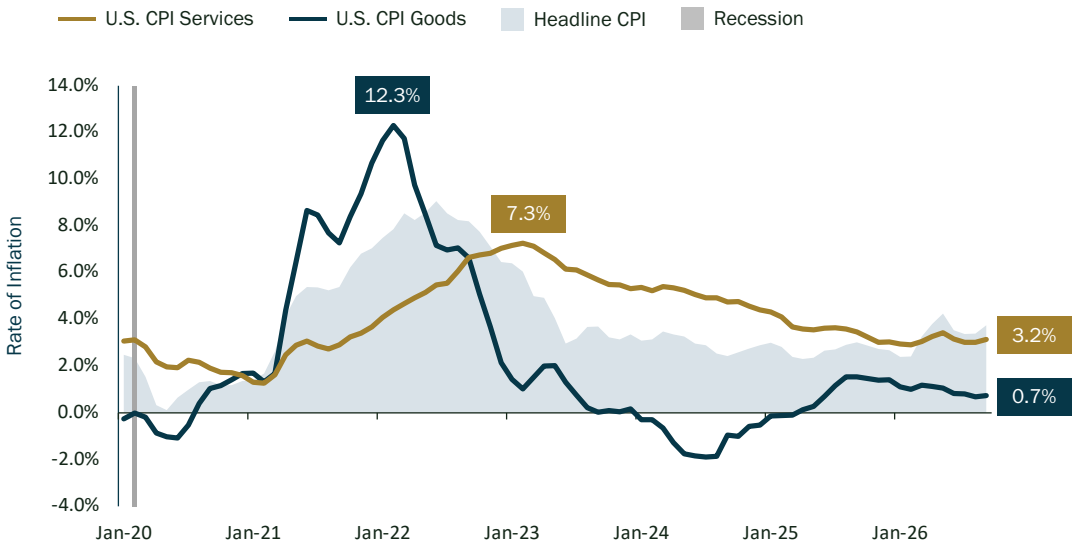
Labor force dynamics have shifted as the Trump administration's immigration policies have shrunk the labor pool, with virtually no immigration occurring and deportations removing workers. Additionally, AI and the wealth effect have removed participants from the labor pool.

Labor force participation has declined among 16– to 24-year-olds and workers ages 55 and older. For older workers, the wealth effect may be contributing to this trend, as those with assets have accumulated additional wealth due to large gains in U.S. equity markets.

The shifting labor force picture, coupled with a slower jobs market, has led to significantly fewer jobs being added to the economy each month. Unemployment has remained subdued, allowing the Federal Reserve to focus on its mandate to lower inflation. We continue to look for monthly gains of 30,000 to 80,000 jobs on average to maintain economic growth.

Inflation Persistence

Composition of inflation has changed during 2026



Source: Bloomberg, Commerce Trust (data through 9/30/2026).

With a stabilizing job market, the Federal Reserve is now focusing on its mandate to get inflation down to its 2% target. U.S. consumption is roughly two-thirds service-based and one-third goods. Goods have faced inflation challenges from tariffs, and now higher energy prices. Additionally, the AI buildout has created inflationary pressures as labor and materials shift to the data center buildout.

Although consumers feel the impact of higher prices more acutely in the short term, inflation's effects may be more moderate in the longer term. As inflation from oil, AI, and tariffs is digested by the markets and consumers adjust to higher prices, and without a new source of inflationary pressure arising, price growth could slow in 2027.

Markets are anticipating an additional interest rate hike during the Fed's December meeting. In 2027, markets are expecting additional rate hikes, but with inflation potentially fading, the Federal Open Market Committee (FOMC) may have an opportunity to pause or reverse its rate-hiking cycle.

U.S. Debt, Deficits, and Higher Borrowing Costs

Longer-term interest rates reach multi-decade highs



Sources: Board of Governors of the Federal Reserve System, Commerce Trust (data as of 10/14/2026).

Longer-term yields for U.S. government securities have hit multi-decade highs, pushing up interest rates for consumers. This is especially true for mortgage rates, limiting housing demand and slowing economic growth.

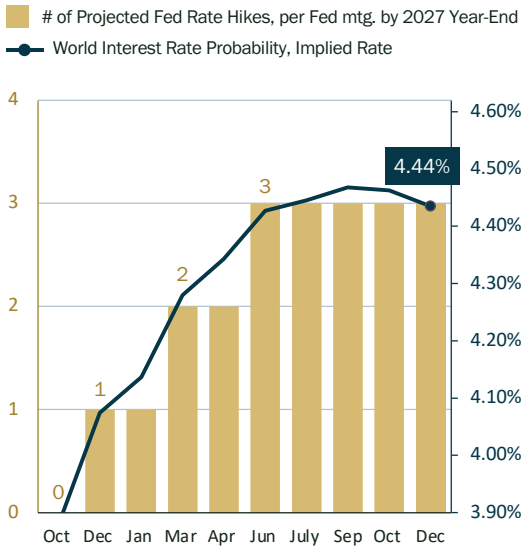
The dynamics surrounding the bond market do not appear to be abating. This should allow higher yields to persist and offer investors the opportunity to receive attractive nominal yields with lower risk profiles than those of equities.

With rates reaching multi-decade highs, investors may find substantial yields from fixed income investments not seen since the early 2000s. Portfolios may benefit from an asset allocation review to explore diversification opportunities.

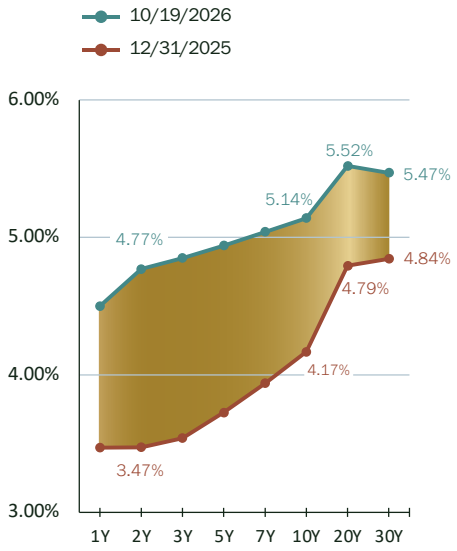
Federal Reserve Interest Rates Reverse Course

Inflation leads markets to reprice shorter-term rates

Fed Rate Cut/Hike Expectations versus Inflation



U.S. Treasury Bond Yields



Source: Bloomberg, Commerce Trust; Left chart as of 09/30/2026; Right chart as of 10/19/2026.

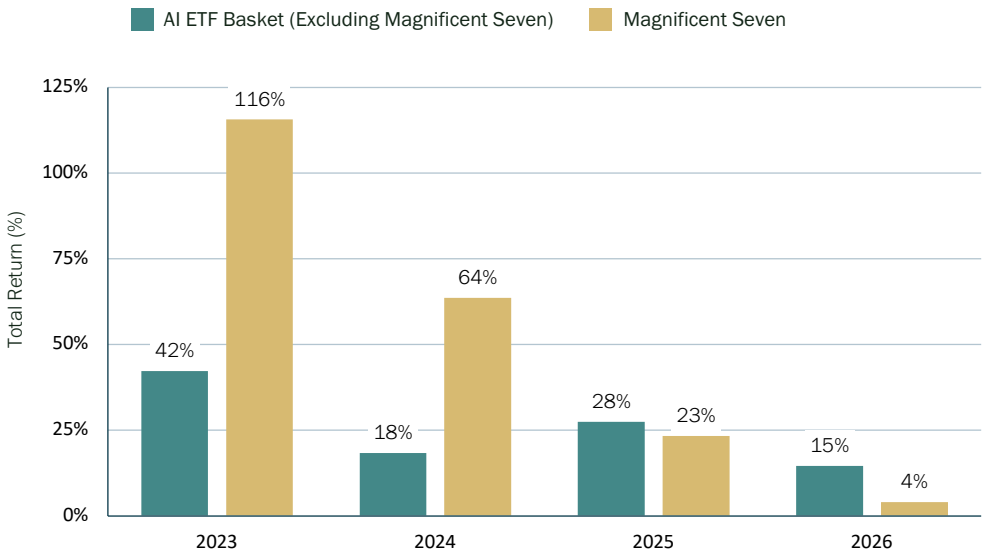
Markets entered 2026 anticipating that moderating inflation and slowing job growth would lead the Federal Reserve to lower the overnight federal funds rate. As energy prices remained around $100 per barrel, inflation remained persistently high, prompting the Fed to reverse course and begin raising rates in contrast to the rate-cutting of 2025.

Higher shorter- and longer-term rates have a moderating effect on the U.S. economy. Historically, consumer spending slows with higher interest rates. Typically, FOMC rate hikes work on a 12-month lag.

Fixed income investors have had smaller returns as rates have been rising but are now well-positioned to earn attractive yields with high-quality assets including Treasuries. Municipal bonds for qualified investors can also represent attractive yields on a forward basis.

The Shifting Landscape of Artificial Intelligence Exposure

AI exposure is becoming less concentrated in Magnificent Seven stocks



Source: Bloomberg, Commerce Trust.

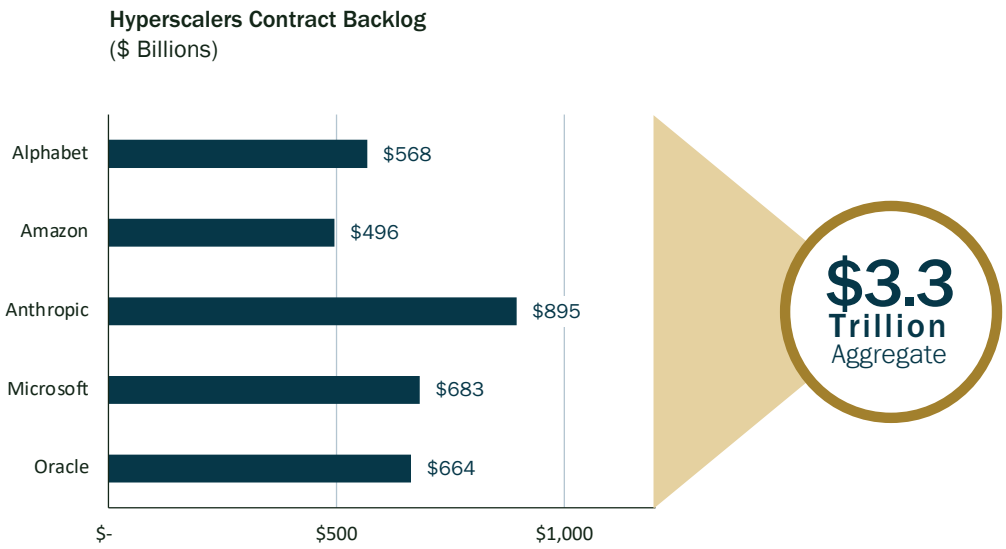
As the pace of AI investment accelerates, spending is expanding beyond chipmakers and model developers to the data centers needed to support this growth. Building AI infrastructure requires a broad network of suppliers, materials, and construction labor, extending the economic benefits of AI investment to a wider range of companies, helping to drive earnings growth and stock price appreciation.

The growth of the hyperscalers (large U.S. technology companies) has been tangible. Their valuations as measured by their price-to-earnings ratios have fallen over the course of 2026. Smaller-capitalization stocks and non-technology players have increasingly benefited from the buildout.

The broadening of the market to include smaller U.S. companies reinforces the need for diversification away from investing exclusively in large-cap growth securities. The market environment continues to be dynamic as the buildout offers opportunities to outfit the AI revolution.

$3 Trillion of Contracted Artificial Intelligence Buildout

AI infrastructure investment continues to support U.S. economic growth



Source: Bloomberg (Alphabet, Amazon, Anthropic, Microsoft backlog as of 09/30/2026; Oracle backlog as of 08/31/2026).

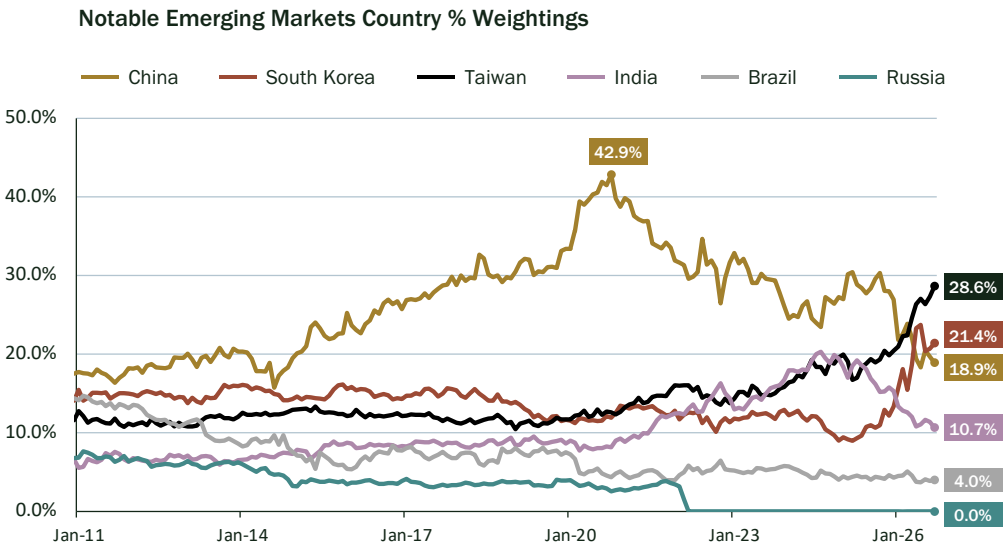
While there is some concern about increasing capital expenditures for AI hyperscalers, a backlog of $3 trillion in aggregate revenue provides assurances to investors. In 2026, the expected buildout from five hyperscalers is $510 billion, more than double the outlay in 2025 for the same companies, contributing to economic growth and inflation.

While the price of compute power, or total processing capacity, comes down, new contracts to provide power continue increasing because of strong demand. External forces such as AI demand, available materials, and a shrinking labor pool are beginning to slow data center construction.

We are watching for signs that AI demand will begin to slow. Conversely, we could see an increase in demand through lower pricing, new use cases, or higher returns on investment.

Indices Change Over Time

Economic growth and geopolitical events have affected emerging markets



Source: Commerce Trust; iShares MSCI Emerging Markets ETF (EEM) historical holdings used as a benchmark proxy for the MSCI Emerging Markets Index (data through 09/01/2026).

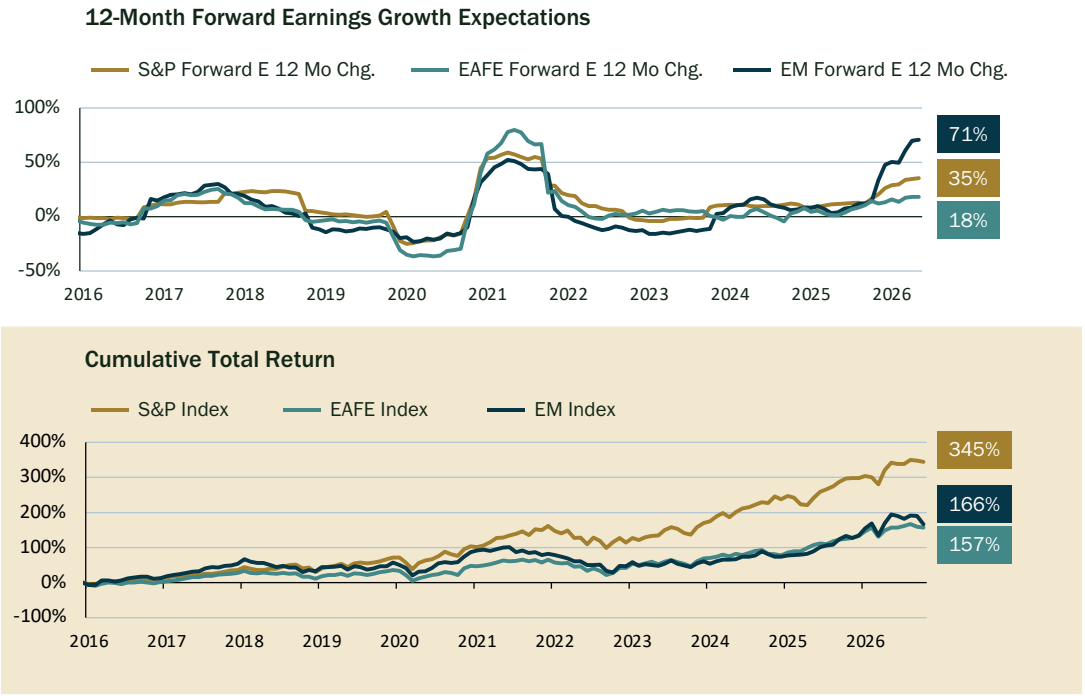
Emerging markets have outperformed U.S. equities over the trailing one- and three-year periods, highlighting the benefits of maintaining global diversification. However, the sources of return have shifted meaningfully, with technology and AI-related companies increasingly driving performance.

Taiwan and South Korea have become key beneficiaries of the global AI buildout due to their leadership in semiconductors and memory chips. At the same time, China's influence has declined, creating fewer China-centric opportunities in emerging markets.

While we see attractive long-term opportunities and diversification benefits in emerging markets, market leadership has become increasingly concentrated among a handful of AI-related companies. Given elevated concentration risk and higher volatility, investors should evaluate the risk inside these markets.

Global Earnings Momentum versus Long-term Performance

Recent strength of emerging markets has been driven largely by AI exposure



Source: Bloomberg, Commerce Trust; Top chart through 09/30/2026; Bottom chart normalized to 0 as of 12/31/2015, data through 10/30/2026.

International developed stocks have performed well over the past year, while they remain at lower valuations relative to their domestic counterparts. Meanwhile, emerging market securities have benefited from the AI buildout, reflecting continued growth in their valuations.

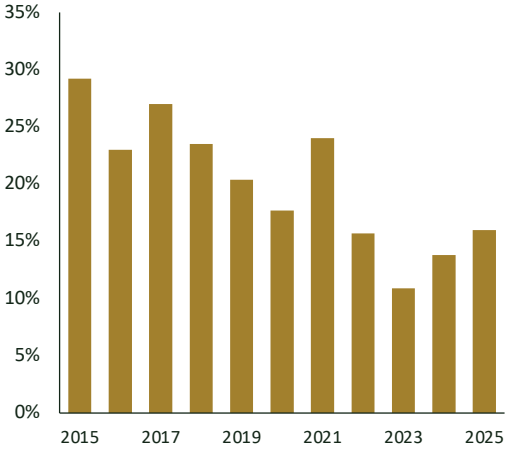
Emerging market stocks and domestic equities benefit from significantly larger technology exposure, giving a substantial lift to returns. International returns, while having lower valuations, have begun to accelerate even without notable AI companies.

Investors have benefited from diversifying away from U.S.-centric portfolios to the attractive valuations in international developed stocks and the growth opportunities in emerging markets.

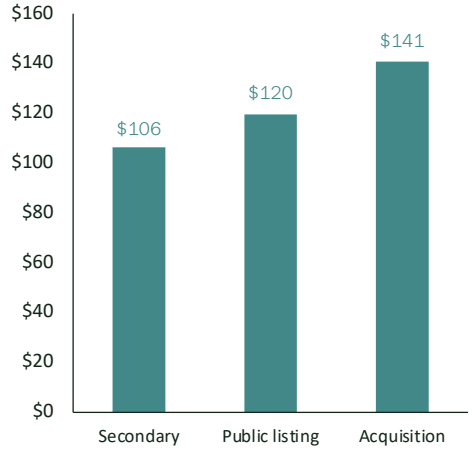
Liquidity Constraints Continue to Weigh on Private Markets

Lower distributions are creating a tighter fundraising environment

Private Market Distributions by Year
(% of Outstanding NAV)



U.S. Venture Capital – 2025 Exit Values by Type
($ Billions)



Source: PitchBook Data, Inc.

Liquidity in private markets remains constrained as exit activity is uneven, with initial public offering (IPO) markets largely stalled and distributions still below historical averages. Distributions as a percentage of outstanding net asset value (NAV) since 2025 are still well below the average over the past 10 years.

In response, limited partners (LPs) and general partners (GPs) are increasingly relying on the secondary market to generate liquidity. LPs and GPs are also adjusting fund structures. However, these mechanisms have not been sufficient to fully alleviate broader distribution pressures.

Liquidity constraints have also directly weakened fundraising by limiting distributions back to LPs, leaving capital trapped in existing funds and reducing LPs' ability to commit to new vehicles. As a result, LPs have become more selective, extending fundraising timelines and concentrating capital flows into a smaller group of established managers.

The opinions and other information in the charts and commentary are provided as of November 16, 2026 and are subject to change based on changes in the market or other conditions. Commerce Trust does not undertake to advise you of any change in its opinions or the information contained in these charts and commentary. This summary is intended to provide general information only and may be of value to the reader and audience.

The information contained herein is not directed to, designed for, or individually tailored to, any particular investor or potential investor. Different types of investments have varying degrees of risk and the asset classes and investments discussed in this commentary may not be appropriate for all investors.

Past performance is no guarantee of future results. Diversification does not guarantee a profit or protect against all risk. This material is not a recommendation of any particular investment strategy, is not based on any particular financial situation or need, and is not intended to replace the advice of a qualified attorney, tax advisor, or investment professional.

Alternative investments often carry additional risk considerations and may involve significant losses, periods of extreme volatility, and lack of liquidity. These investments, in general, are not suitable for all investors. Additionally, certain alternative investments may require investors to be accredited or qualified investors, which have defined minimum asset requirements.

Data contained herein from third-party providers is obtained from what are considered reliable sources. However, its accuracy, completeness, or reliability cannot be guaranteed.

HARNESS THE TRUE TEAM ADVANTAGE

Commerce Trust
Banking | Investments | Planning®

commercetrustcompany.com

Commerce Trust is a division of Commerce Bank
Investment Products: Not FDIC Insured | May Lose Value | No Bank Guarantee