The Weekly Market Update – 5/18/26: Interest Rates Surge to 2026 Highs

Major Indices (Price Returns)	Close	Last Week	Quarter-to-Date	Year-to-Date	Trailing 12-Months	All-Time High	% to High
S&P 500	7,408.50	0.13%	13.48%	8.22%	33.03%	7,501.24	1.3%
Dow Jones Industrial Average	49,526.17	-0.17%	6.87%	3.04%	21.78%	50,188.14	1.3%
NASDAQ Composite	26,225.15	-0.08%	21.47%	12.84%	50.32%	26,635.22	1.6%
Russell 2000	2,793.30	-2.37%	11.89%	12.55%	42.22%	2,886.77	3.3%
MSCI EAFE (USD)	3,024.90	-1.67%	6.56%	4.57%	20.95%	3,179.91	5.1%
MSCI Emerging Markets (USD)	1,668.17	-2.52%	19.39%	18.78%	49.90%	1,723.92	3.3%
Bloomberg Commodity Index	140.91	1.82%	4.19%	28.46%	39.62%	237.95	68.9%
Barclays U.S. Aggregate Bond	92.17	-1.22%	-1.16%	-2.03%	-0.28%	112.07	21.6%

Source: FactSet

U.S. Treasury yields surged to multi-month highs in mid-May as inflation pressures build from sustained oil market disruptions. U.S. Treasury bonds serve as a reliable proxy for both short-term (2-year Treasury yield, TY) and long-term (10-year TY) U.S. interest rates. In addition, the U.S. Federal Reserve Bank (Fed) manages overnight bank lending interest rates by setting a target fed funds range. As of 5/15/26, compared to year-end 2025 (12/31/25), the 2-year TY was 4.08% vs. 3.48%, the 10-year TY was 4.59%, up from 4.17%, and the fed funds target range was unchanged at 3.50% to 3.75%. We attribute the higher U.S. Treasury yields to elevated inflation data as the April consumer price index (CPI), the most widely-followed measure of consumer inflation, surged to +3.8% year-over-year (Y/Y), the highest level in nearly three years (since May 2023), and is now up +140 basis points since the start of military action in Iran (the February CPI was +2.4%). Despite recent reports of a limited number of ships navigating the Strait of Hormuz, the global oil supply remains severely disrupted. West Texas Intermediate (WTI) oil was trading at $103 per barrel on 5/18/26, still elevated following a brief dip below $100 in early May, and well above $67 per barrel at the end of February. The U.S. national average price of unleaded gasoline was $4.52 per gallon on 5/18/26, up +52% from $2.98 per gallon on 2/28/26. This was the largest component of the April surge in CPI, but prices also lurched higher for food (both at grocery stores and restaurants), apparel, shelter (higher rents), and transportation services (mostly airline fares). With oil market disruptions nearing three full months at the end of May, we are increasingly concerned that oil-driven price hikes could impact a wider swath of the economy, especially if higher interest rates act as a brake on economic growth. While the Fed has left its fed funds target unchanged this year, the fed funds futures market (which serves as a point-in-time market estimate of future Fed policy) has effectively priced out any fed funds rate reductions this year, and reflects a 50% chance of a +25 bp increase in the fed funds target by year-end 2026. We also believe the 2-year TY is a fairly accurate predictor (with a several months lag) of the fed funds trajectory, and it also points to potential rate hikes ahead. This creates challenges for incoming Federal Reserve Chair Keven Warsh (set to be sworn in on 5/22/26) as his long-term Fed plan is to drive lower rates.

The U.S.-China meetings were largely uneventful. As the two-day summit concluded on 5/15/26, there were no specific large-scale agreements, although the themes of improving economic cooperation and market access were generally supported by both sides. Friday's U.S. equity market weakness, higher interest rates, and higher oil prices could reflect investor disappointment that the talks yielded no progress on the Strait of Hormuz (some had hoped that China would agree to pressure Iran to negotiate). There was undefined discussion about China purchasing more aircraft and agriculture, but other key issues such as AI and semiconductors, rare earth minerals, and oil purchases were unresolved. This does not mean that potential trade deals and other China discussions are concluded, but near-term catalysts from last week's meeting did not materialize.

With a full week ahead of the Memorial Day holiday on 5/25/26, we are watching several key earnings reports as the first quarter reporting season winds down. Although 91% of the S&P 500 had reported 1Q26 financial results through Monday morning, many market leaders (with April fiscal quarters) in the retail and technology industries will report this week. This includes semiconductor bellwether Nvidia, which is the largest company (by market capitalization) in the S&P 500. Reported earnings growth of the S&P 500 so far was +25.3%, coming in above the +12.9% consensus estimate.

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The Global Industry Classification Standard (GICS) is a four-tiered, hierarchical industry classification system. Companies are classified quantitatively and qualitatively. Each company is assigned a single GICS classification at the Sub-Industry level according to its principal business activity. MSCI and S&P Dow Jones Indices use revenues as a key factor in determining a firm's principal business activity. The 11 sectors are: Communication Services, Consumer Discretionary, Consumer Staples, Energy, Financials, Health Care, Industrials, Information Technology, Materials, Real Estate, and Utilities. Growth sectors are those that generally drive expected annual sales and earnings growth that exceed market and sector average. Value stocks will typically trade at valuation levels below peer group averages. Cyclical sectors tend to be more economically sensitive, with more volatility in sales and earnings growth when the economy is either decelerating or accelerating. Defensive sectors (which often include Consumer Staples, Health Care and Utilities) tend to outperform during periods of economic uncertainty or slow down, as many of the products and services in these sectors are essential in daily life and less impacted by economic swings.

FactSet is a data aggregation software utilized by D.A. Davidson's Wealth Management Research. The FactSet consensus refers to the aggregate of all analysts' estimates from firms that submit estimates to FactSet for a given financial metric. Calculations on the percentage price change on indices are provided by FactSet.

Gross domestic product (GDP) is a measure of economic growth and refers to the monetary measure of the market value of all final goods and services produced within a country's borders within a specific time period. Real GDP is adjusted for the impact of inflation. GDP numbers are compiled by the Bureau of Economic Analysis (BEA), a division within the U.S. Department of Commerce. Quarterly GDP is reported as a percentage change from the prior quarter, annualized. The BEA also reports data as a year-over-year percentage change from the same period one year prior. The most recent GDP report can be found at www.bea.gov. Major components of GDP include personal consumption expenditures, non-residential fixed investment, residential investment, government expenditures and adjustments for inventories and net exports (imports). Non-Residential Fixed Investment includes several subcategories including software and information processing equipment that measure investment in technology. Imports of goods and services are subtracted from GDP data (products are not produced or performed in the U.S) while exports are added to GDP. The first estimate of 1Q26 U.S. GDP was released on 4/30/26 and can be found at www.bea.gov.

On 2/28/26, the U.S. and Israel launched an air attack on Iran designed to eliminate weapons capabilities and critical infrastructure. On 3/1/26, the White House published a release detailing the operation. On 3/6/26, President Trump issued a 10-day deadline for Iran to open the Strait of Hormuz to shipping traffic. The deadline was set to end the evening of 4/6/26. On 4/8/26, the U.S. and Iran agreed to a two-week ceasefire that was set to expire (unless extended or replaced with a peace agreement) on 4/22/26 but has since been extended indefinitely.

The Strait of Hormuz is located in the gulf between Oman and Iran. According to the U.S. Energy Information Administration, an estimated 20 million barrels per day are transported on ships through the Strait on a daily basis. This includes liquefied natural gas (LNG) as well and is an essential waterway for Gulf energy exports. As of 5/18/26, some ships were travelling through the Strait, but activity remained severely disrupted.

The International Energy Agency (IEA) has monitored shipping and supply disruptions through the Strait of Hormuz. They have published key facts on the disruption with links to other reports as well. The Middle East and Global Energy Markets.

The consumer price index (CPI) is a measure of average change, over time, in the prices paid by urban consumers for a market basket of goods and services. It is reported monthly by the U.S. Bureau of Labor Statistics. The U.S. Personal Consumption Expenditures (PCE) Price Index is an indicator of the growth in consumer spending and measures the value of goods and services purchased by persons who reside in the U.S. It is reported monthly by the Bureau of Economic Analysis. PCE inflation is the percentage rate of change in the price index for personal consumption expenditures (PCE).

Generative Artificial Intelligence (GenAI): We think of artificial intelligence as using advanced computers to process large amounts of data to ultimately approach human problem solving and decision making. While still predictive models, generative AI can give detailed responses, much better than a search engine, which does a good job of telling the user where to go to find additional information. As generative AI systems access more data, they become larger and learn to make better decisions. At each iteration, the system gains knowledge, enhancing its predictive (reliable) capabilities and ability to produce original content. Generative AI systems become more robust as they are used as all new data can be trained into the system, creating new challenges and opportunities.

The U.S. Census Bureau conducts the Advance Monthly Retail Trade and Food Services Survey to provide an early estimate of monthly sales by kind of business for retail and food service firms located in the United States. Each month, letters are mailed to a probability sample of approximately 4,800 employer firms selected from the larger Monthly Retail Trade Survey (MRTS). Advance sales estimates are computed using a link relative estimator.

S&P 500 earnings growth reflects the year-over-year change in operating earnings on a per share basis. Earnings data are aggregated for all S&P 500 constituents and are measured according to the relative market capitalization weights for each company. Estimated earnings are the combined FactSet estimates of analysts covering each company included in the index.

The Treasury yield curve displays the market interest rate across different contract lengths for U.S. Treasury securities, indicating the relationship between the interest rate and the time ("term") to maturity. The yields of the 2-year and 10-year U.S. Treasury notes are widely followed barometers of the current U.S. interest rate environment. Treasury security data used in calculating interest rate spreads is obtained directly from the U.S. Treasury Department, through FactSet.

The Federal Reserve Bank's Open Market Committee (FOMC) consists of twelve members – the seven members of the Board of Governors of the Federal Reserve System, the president of the Federal Reserve Bank of New York, and four of the remaining eleven Federal Reserve Bank presidents, who serve one-year terms on a rotating basis. The FOMC holds eight regularly scheduled meetings per year. At these meetings, the Committee reviews economic and financial conditions, determines the appropriate stance of monetary policy, and assesses the risks to its long-run goals of price stability and sustainable economic growth.

The term "monetary policy" refers to the actions undertaken by a central bank, such as the Federal Reserve, to influence the availability and cost of money and credit to help promote national economic goals. The Board of Governors of the Federal Reserve System is responsible for the discount rate and reserve requirements, and the Federal Open Market Committee is responsible for open market operations. The Federal Reserve influences the demand for, and supply of, balances that depository institutions hold at Federal Reserve Banks and, in this way, alters the federal funds rate. The federal funds rate is the interest rate at which depository institutions lend balances at the Federal Reserve to other depository institutions overnight.

Data on the economics of oil price changes on the retail price of gasoline can be found from the Federal Reserve Bank of St. Louis and the U.S. Energy Information Administration (EIA). The Automobile Club (AAA) monitors daily fuel prices in the U.S., which can be tracked at: gasprices.aaa.com. The EIA provides comprehensive data on the U.S. and global energy markets through its eia.gov home page.

The CME Group "Countdown to FOMC" FedWatch Tool is based on futures pricing in the 30-Day Federal Funds futures market and reflects market-implied probabilities of potential Federal Reserve interest rate outcomes at upcoming FOMC meetings. These probabilities are derived from trading activity and do not represent the views, forecasts, or predictions of CME Group, the Federal Reserve, or any other institution. They can be used to assess current market probabilities of future fed interest rate action.

Presidents Trump (U.S.) and Xi (China) met in Beijing, China for two days (5/14/26 & 5/15/26) billed by the state as aiming for stabilizing U.S.–China relations after elevated tensions in 2025. Talks concluded with limited break-throughs, but talks continue and President Xi is expected to visit the U.S. in September 2026.

Kevin Warsh became the new Chair of the Federal Reserve after being confirmed by the U.S. Senate on May 13, 2026, in a 54–45 vote, replacing Jerome Powell. He is a former Federal Reserve Governor (2006–2011) and a macro-focused policymaker viewed as an inflation hawk, taking leadership at a time of elevated inflation and policy uncertainty.