

Newsletter: October 2026

Market Update

The most interesting market right now is the bond market. By the end of September yields on both the 30-year Treasury bond and 10-year Treasury note had reached their highest levels since 2002. Elevated energy prices have contributed to faster inflation, and in response the Federal Reserve recently raised short-term interest rates, which are expected to increase further in the months ahead. However, long-term inflation expectations have not risen by nearly as much as long-term bond yields, which suggests that other factors are at play.¹

30-Year Treasury Bond Yield:

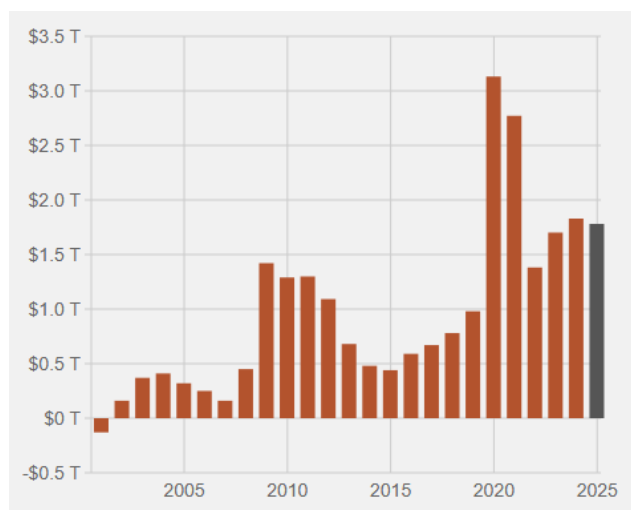


Whenever long-term bond yields rapidly rise, it is natural to revisit the chronic fiscal deficits of the US federal government, a topic that we discussed in our October 2024 letter.² 2001 was the last fiscal year in which the US federal government ran a budget surplus, and since then the ratio of federal government debt outstanding to Gross Domestic Product (GDP) has increased from approximately 55% to more than 120%, which is higher than the prior peak at the end of World War II. Reducing the federal budget deficit would require some combination of spending reductions and tax increases, which are politically unpopular, and thus the path of least resistance has been to allow the debt/GDP ratio to expand while hoping that there remain enough buyers to absorb the continuous stream of net new Treasury issuance.

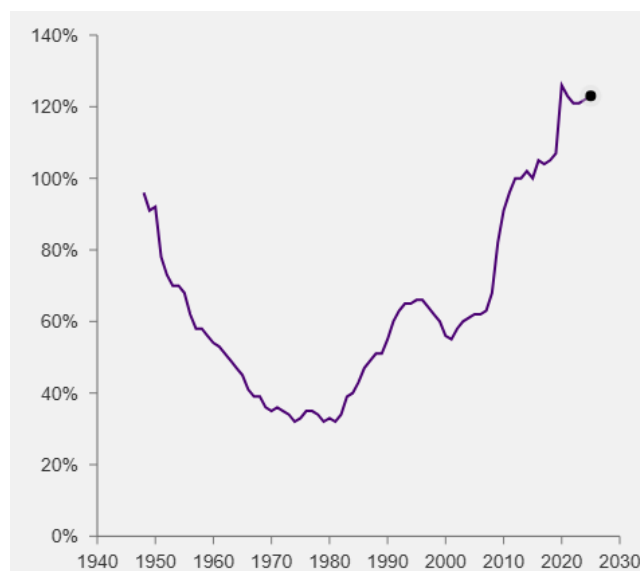
¹ "Expectations," in the context of interest rates and inflation, are derived from prices observed in markets such as those for fed funds futures, Treasury Inflation-Protected Securities, and inflation swaps.

² For prior newsletters, please see our website: <https://www.beckmack.com/>.

Federal Budget Deficit:



Federal Debt Outstanding as a Percentage of GDP:



The recent rise in long-term bond yields aggravates this underlying fiscal imbalance, as more economic resources are required merely to service the debt outstanding due to rising coupon rates. At the same time, the ownership base of Treasury debt continues to shift away from foreign central banks towards hedge funds, which tend to be significantly more price-sensitive. This has made the Treasury market more volatile and more fragile.

These fiscal dynamics, if not course-corrected, will place upward pressure on both bond yields and inflation, but in our view they do not fully account for the rapid rise in long-term bond yields this year. This is because inflation expectations are the primary mechanism by which fiscal dynamics influence bond yields, and, as noted above, long-term inflation expectations have not moved by nearly as much as yields themselves.³ Consider the market changes between the end of February and the end of September:

	February	September	Change
Nominal 30-Year Treasury Bond Yield	4.61%	5.63%	+1.02%
30-Year Inflation Expectations	2.19%	2.31%	+0.11%
Real 30-Year Treasury Bond Yield	2.42%	3.32%	+0.91%

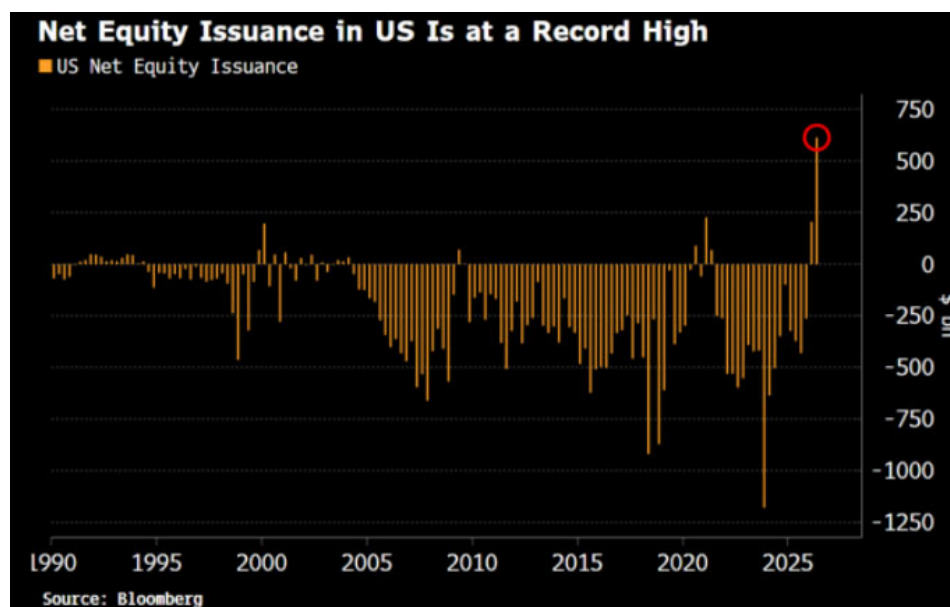
Thus, notwithstanding the renewed topicality of US fiscal imbalances, long-term inflation expectations have only moderately increased this year, while a large majority of the increase in nominal bond yields represents an increase in “real” yields—i.e., yields after deducting expected inflation. **We believe that this phenomenon**

³ A way to conceptualize this mechanism is to observe that fiscal surpluses—i.e., tax revenues less government expenditures—are the ultimate source of capital with which to pay down federal debt. If fiscal surpluses are insufficient, then the government must create new dollars with which to pay down debt (“monetization”), and those newly created dollars lead to faster price inflation. (When the government pays off maturing debt with the proceeds of newly issued debt, it is not paying *down* debt.) If the market believes that the government will monetize the debt in the future, then that belief will be priced into bond yields in the present.

reflects events taking place in the corporate bond and equity markets related to the ongoing buildout of artificial intelligence (AI) infrastructure.

There are today many unresolved debates about AI, but one incontrovertible fact is that several of the companies involved in the infrastructure buildout are not generating enough cash flow to fund their investment plans. AI “labs,” such as OpenAI and Anthropic, require enormous fleets of semiconductor chips running in data centers in order to train and operate their models. Although the labs are generating revenue, they remain heavily reliant on external sources of funding to acquire the computing capacity to run their businesses. Many companies involved in the construction of data centers and the provision of related equipment are similarly forced to borrow and raise capital because they too lack sufficient cash flow. One of the central unresolved debates about AI is whether it will give rise to sustainable business models on the other side of this massive investment cycle, but in the meantime those investment needs are being funded by corporate bond issuance, other forms of debt financing, and the issuance of new equity.

The sheer quantity of all this new capital is staggering. Through the end of August, there have been nearly \$1.9 trillion of corporate bonds issued in the US year-to-date. This is already close to the \$2.2 trillion issued during the entirety of 2025, which set a new annual record. The large “hyperscalers”—companies that provide computing capacity, such as Google, Amazon, Microsoft, Meta, Oracle, and SpaceX—have collectively issued nearly \$250 billion of corporate bonds thus far this year, which is more than they had issued in the prior 10 years combined. As The Economist recently observed, “In the past year American markets have digested the largest-ever initial public offering (SpaceX), equity raise by a public company (Google) or a foreign firm (SK Hynix), private-funding round (OpenAI) and private-debt deal (Broadcom), as well as most of the biggest bond issue in history (Amazon).”⁴ SoftBank Group recently set a record for the largest ever junk bond issuance at more than \$11 billion. Shortly thereafter, Paramount Skydance issued more than \$12 billion of junk bonds. And due to the issuance of new equity and lower levels of share repurchases, net equity issuance has increased dramatically.



The Economist’s digestion metaphor is apt, but we believe the market is in fact on the cusp of indigestion. Signs of indigestion include the growing list of delayed initial public offerings, widening corporate bond spreads, bonds and shares trading poorly after issuance, and companies resorting to increasingly creative and opaque

⁴ <https://www.economist.com/business/2026/09/30/the-era-of-speedball-capitalism-has-dawned>.

off-balance sheet financing. The essential function of capital markets is to allocate capital from savers to businesses that can invest that capital and earn a return. The US economy is currently making a highly consequential bet that the massive investment in AI will generate a sufficient return in the form of sustainable productivity enhancements and economic growth. We have our doubts about that, but even if all this capital turns out in the end to be money well spent, there is a practical limit to how much net new issuance the market can absorb over any given period of time without disruption, and we are approaching that limit. **Rapidly rising Treasury bond yields are the result of competition between the federal government and companies involved in the AI buildout for capital, of which there is only so much to go around.** As that competition for capital intensifies, so too does the risk of market disruption, and with the S&P 500 close to its all-time high, that risk is not appropriately priced into the equity market.

Portfolio Update

In general this year, we have been (i) pleased with the financial and operational performance of our portfolio companies; (ii) disappointed in their absolute or relative share price performance; and (iii) able to identify a number of new investment ideas that we either have already initiated or are prepared to initiate at somewhat lower prices.

As we noted in our most recent letter, it is an axiom of public equity markets that share prices tend to move up and down to a far greater extent than changes in underlying business values, and this year has provided an excess of examples of this tendency. Microsoft, for instance, lost almost \$1 trillion of market cap between the beginning of the year and late June, which it then regained and then some during the third quarter. Apollo's share price declined by 30% to start the year, rallied by 44% over the next five months, and then subsequently declined by nearly 20%. We recognize that in the short run share prices are pushed around by greed, fear, and all the rest. But we are certain that the values of Microsoft and Apollo, *as businesses*, did not change anywhere nearly as much as did their respective share prices. Indeed, our view is that these companies are worth intrinsically more today than at the beginning of the year, and, most importantly, we remain confident that they will be worth substantially more in the years ahead.

While we may look askance at the share price volatility of our portfolio companies, especially during a period when their financial and operational performance has met or exceeded our expectations, that same share price volatility creates opportunities to deploy capital into businesses at attractive valuations. In our last letter we discussed new investments in Alcon and Sotera, and we look forward to discussing our research efforts in greater detail in our next letter.

Partners of Beck Mack + Oliver

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