



THE SHORT AND LONG

Weekly Bulletin

Rate-of-Change Season: Digesting Peak Growth in a Volatile Stretch

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AUTHOR

Jeff Puckette
Macro Portfolio Strategist

CONTRIBUTORS

Kate Moore
Chief Investment Officer

JP Coviello
Head of Portfolio Strategy

Olaolu Aganga
Head of Portfolio Construction & Analytics

Conrad DeQuadros
Head of Economics

TAKEAWAYS

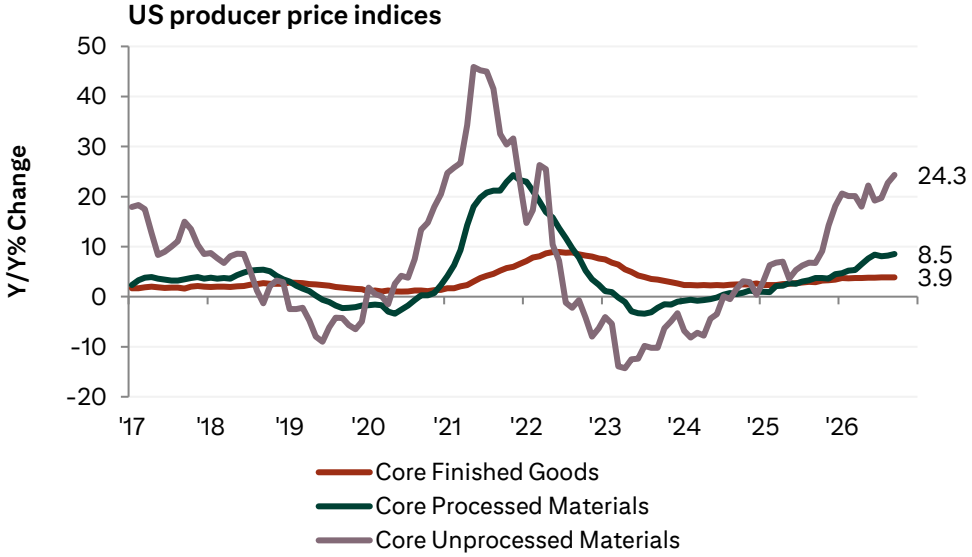
The U.S. Federal Reserve kept rates unchanged despite building pipeline inflation and still loose financial conditions. We expect the Fed to stay behind the curve, which supports strong nominal growth but raises the risk of higher inflation for the medium-term.

Nearly half of major central banks are now hiking as earnings growth may be peaking. We believe policy is catching up rather than becoming restrictive, and peak earnings growth does not have to mean peak prices.

AI capex is positioned to continue growing (at a slower pace), pressuring parts of the AI supply chain reliant on that spend. In our view, slower capital expenditures and issuance growth may support hyperscaler cash flow and profitability at these more attractive valuations.

THIS WEEK IN CHARTS

FIGURE 1: Upstream price pressures signal inflation risks ahead



Source: Haver Analytics as of October 30, 2026. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

LOOKING CLOSER

Producer prices show a clear inflation pipeline, with unprocessed materials leading processed goods and finished goods. Historically, these upstream pressures flow through to downstream inflation, suggesting consumer price measures could face renewed upward pressure in coming quarters.

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THE FED PAUSES AS INFLATION PRESSURE BUILDS IN THE PIPELINE

The Federal Reserve held rates steady last week, even as two key rate-of-change signals point the other way. Inflation pressure is building in the pipeline, and financial conditions have not tightened enough to offset it.

On inflation, Chair Warsh characterized market-based inflation expectations as moving in the right direction. We cannot find the data to support that view as inflation breakevens and inflation swaps have both been rising. Market pricing also lags consumer inflation, which lags producer inflation. Core unprocessed materials prices in the Producer Price Index (PPI) are rising nearly 25% year over year, which leads processed goods at 8.5%, which in turn leads finished goods at nearly 4%. The latter leads and may pressure higher what consumers pay in Consumer Price Index (CPI) and Personal Consumption Expenditures (PCE) from these inputs.

Second, Warsh described overall financial conditions as tighter - a stark contrast to his depiction of unrestrictive financial conditions at the last Fed meeting that resulted in a rate hike. Today, conditions still remain very loose on a level basis and have barely changed over the past year on a rate-of-change basis. We think this shift in message risks a credibility problem at future meetings if the Fed's statements continue to diverge from the data.

As a result, we now expect the Fed to remain behind the curve, all else equal. That stance supports an expansionary nominal growth environment similar to the past 12 months, at least until financial conditions tighten more quickly. If the Fed will not adjust policy rates, markets may do more of that tightening on their own. Our inflation view now differs from both the Fed and Blue Chip consensus, which expects inflation to decline from here.

Bottom line: We expect the Fed to remain reactive, which supports a strong nominal growth environment. At the same time, we see building inflation pressure that the market and Fed may underestimate.

GLOBAL TIGHTENING MEETS PEAK EARNINGS GROWTH

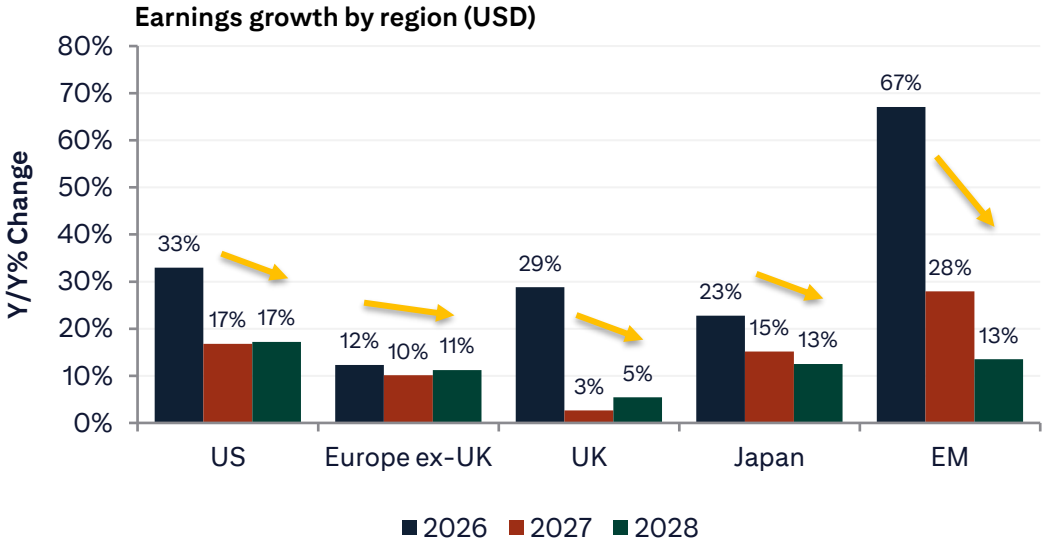
As we've previously highlighted, September and October historically rank as the most volatile months of the year, and this season lived up to its reputation. October typically brings the highest average volatility and the most fear readings in an S&P 500 sentiment and positioning indicator we reference, which recorded two in the past couple of weeks alone. Since 2010, three of the four other times we saw two fear readings in October also fell in U.S. midterm election years.

Beneath the surface, markets held up well. The S&P 500 finished October down nearly 1% while nine of 11 sectors rose and nearly two-thirds of index members gained at least 2%. Outside of recent Technology performance, stocks have been resilient despite the volatility.

Policy rates continue to tighten globally, even with the Fed on hold. Among more than 30 major central banks, the share hiking over the past six months rose from about less than 10% at the end of last year to nearly half today. Emerging and frontier markets led the way as they fought inflation and defended their currencies, and major developed market central banks, including the Fed, the Bank of Japan (BoJ), and several across Europe, have followed suit. Tightening typically slows growth, but U.S. nominal growth sits near its top decile of the past 30 years, and global nominal growth ranks in its top quartile and exceeds the U.S. by level. In our view, policy rates are catching up rather than becoming restrictive.

Tightening becomes a concern when it squeezes corporate margins, which can lead to layoffs, rising unemployment, and weaker consumption. Macro profits remain at record levels relative to GDP, so we believe that risk remains a ways off. Still, most major regions face what consensus expects to be a peak earnings growth period, with U.S. earnings growth projected to slow from 33% in 2026 to 17% in 2027 (Figure 2). Peak earnings growth usually brings narrower multiples, which has weighed on index valuations as rates have risen. We will watch how earnings reports into year-end shape forward estimates, with clarity likely helping valuations stabilize.

FIGURE 2: Peak earnings growth does not mean peak prices



Source: Factset as of October 30, 2026. Indices are unmanaged. An investor cannot invest directly in an index. They are shown for illustrative purposes only and do not represent the performance of any specific investment. Index returns do not include any expenses, fees, or sales charges, which would lower performance. Past performance is no guarantee of future results. Real results may vary.

Bottom line: We believe global policy rates are not yet restrictive given the strong nominal growth backdrop. Peak earnings growth may pressure valuations, but earnings could still grow, and prices can rise again once valuations adjust to a higher rate environment.

AI CAPEX: SLOWER GROWTH MAY BE WELL RECEIVED

This year delivered record earnings surprises that almost no one expected a year ago. Even so, many investors call a 33% earnings growth quarter disappointing and keep waiting for the other shoe to drop. Forecasters underestimated 2026, so 2027 estimates will likely miss in one direction or another. As long as the growth environment stays intact, U.S. companies have shown a remarkable ability to defend margins and beat expectations outside of a recession, and we see no signs of widespread weakness yet.

Earnings commentary by theme remains encouraging. AI demand remains exceptionally strong. AI adoption and company-level ROI are harder to measure, but executives increasingly cite efficiency gains, and some companies are clearly doing more with similar staffing. Reports on financing and the consumer have also stayed positive, despite higher rates, slightly wider spreads, and affordability concerns. We think markets need to reset expectations: earnings cannot grow 50% every quarter, but 10-15% growth works well too.

AI capex sits at the center of the growth, earnings, and debt issuance story, and its rate of change is shifting. Hyperscaler capex and issuance should keep rising for years but expected spending growth has slowed. That slowdown has compressed multiples for semiconductors, high bandwidth memory, and other high-momentum parts of the AI supply chain, many of which remain up about 100% this year after reaching gains of roughly 150%.

What hurts some parts of the market may help others - particularly for the capex spenders themselves. Hyperscalers financed about one-third of more than $1 trillion in capex this year, and we expect a similar ratio next year as spending levels rise. As capex growth slows, issuance growth slows too, which gives credit markets a better chance to digest new supply with an end in sight. Most hyperscalers are betting on owning the compute rather than the best model, which we believe can drive future revenue and profit once spending slows, and AI adoption accelerates. Free cash flow growth shows early signs of bottoming in conjunction with the capex expectations rate-of-change. Given that these are among the most profitable companies in history, we believe current valuations may offer an attractive entry point.

Bottom line: Slowing capex growth weighs on some legs of the AI supply chain but may support hyperscaler profitability, the anchor of the U.S. market. With no recession or sustained contraction in sight, we expect relief and gains into year-end after the midterms, though likely not at the 20% annual pace of the past four years that investors have gotten used to.

	WHAT HAPPENED	WHAT'S AHEAD
ECONOMIC DATA	**U.S.** U.S. GDP data showed economy expanded at an annualized 3.4% in Q3, the fastest pace in a year. Personal consumption was the dominant driver. Headline PCE rose 3.65% Y/Y in September, the most since May. Core PCE rose by 3.12%. The Conference Board's consumer confidence index rose for the first time in four months in October.	**U.S.** October nonfarm payrolls October unemployment rate ISM Services for October
	Global Eurozone advance Q3 GDP increased 1.3% Y/Y, climbing from 1.2% in the prior period. Tokyo CPI for October rose 2.8% Y/Y, keeping alive expectations for BoJ policy normalization.	**Global** Global Services PMI for October Canadian jobs report for October
POLICY	**U.S.** The FOMC left the Federal Funds target rate unchanged at 3.75%-4%. Governor Lisa Cook and Cleveland Fed president Beth Hammack dissented in favor of a 25bp hike.	**U.S.** U.S. midterm elections U.S. Treasury quarterly refunding documents
	Global ECB left its key policy rate unchanged after hikes in June and September; ECB President Lagarde announced that she would be stepping down in early 2027. BoJ left interest rates unchanged with the central bank noting that inflation is back to the 2% target but not yet in a "sustainable and stable manner." EU countries dropped the idea of offering Canada associate member status, instead promising closer association.	**Global** Bank of England interest rate decision Brazilian central bank rate decision Israeli government formation
MARKETS	**U.S.** An S&P 500 sentiment and positioning indicator registered "fear" for a second consecutive week on 10/23. Analysis shows that average and median returns for the S&P 500 exceed normal outcomes across every horizon.	**U.S.** This week sees ~20% of the S&P 500 market cap reporting Q3 earnings.
	Global	**Global** Global bond issuance has climbed to a record $6.6 trillion YTD, up 15% from one year prior.

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RELATED READING

RSVP: CIO U.S. Midterm Election Webcast | November 5, 2026

Join the Chief Investment Office (CIO) for a conversation on how the U.S. midterm elections could shape the economy and markets. Head of Government Affairs **Candi Wolff** will join our team at 11:00 a.m. ET on November 5 to discuss what comes next.

Click here to register.

October 29, 2026 | The Short and Long Podcast

In episode five of Citi Wealth's The Short and Long, Chief Investment Officer Kate Moore takes a comprehensive look at the rapidly shifting global energy landscape. Her guests, Patrick Pouyanné, Chairman and CEO of TotalEnergies, and Alastair Syme, Head of Global Energy Research at Citi Research provide an assessment of rising global power demand, the structural costs of the energy transition, and the geopolitical forces redefining market risk. Watch now on YouTube, Apple, or Spotify and subscribe for future episodes.

October 27, 2026 | Volatility Amid Strong Fundamentals Creates a Potential Entry Point

In last week's Bulletin, we looked at why recent economic data paints a picture of solid global growth. Meanwhile, forecasts of slower price growth and less policy tightening than markets price in appear to rest on hope rather than data.

October 7, 2026 | The Short and Long: Q4 Macro Investment View

Citi Wealth's quarterly report is designed to offer global, data-driven guidance to help investors navigate increasingly complex markets with confidence and clarity. The latest report delivers a breakdown of inflation, AI investment cycle, role of gold, natural resources, and portfolio resilience, and lessons from our key investment calls throughout 2026.

September 24, 2026 | Global Investment Council

The Citi Wealth Global Investment Council met September 24, 2026, and increased allocations to U.S. equities, Japanese equities, and the cybersecurity theme, funded by a reduction in the overweight to U.S. securitized fixed income. The Council also reviewed and endorsed the portfolio's drift, remaining comfortable with the market-driven increase in equity exposure relative to fixed income.

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Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	C	D	C
In default	C	D	D

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Weekly Bulletin