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Investment Institute

Market Commentary

Weekly perspective on current market sentiment **September 4, 2025**

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Last week's S&P 500 Index: -0.1%

The waiting is the hardest part

Key takeaways

- The decision to cut rates this month will likely come down to what two reports, the August employment report and Consumer Price Index (CPI), show.
- But financial markets have more to be concerned about than just the Federal Reserve (Fed) decision.

We know the financial media has been talking about the upcoming September (16-17) Federal Open Market Committee (FOMC) meeting ever since the Fed held its last meeting in July and the target rate did not change. We were reminded of this month's meeting again when Fed Chair Jay Powell spoke a couple of weeks ago at the Kansas City Fed's annual Jackson Hole Symposium. Note that the market is convinced the Fed is going to cut as the federal fund futures are pricing in a 92% probability of a 25 basis point (100 basis points equal 1.00%) reduction at the time of this writing.

But there are several factors at play that markets are thinking about. To begin, between now and the next Fed meeting, we will see the August employment report (tomorrow) and then next week's inflation reports, including last month's CPI and Producer Price Index (PPI) data. Chair Powell and other Fed members have been reminding us that they are "data dependent."

What that ultimately means is the decision to either cut rates this month or hold pat will likely come down to what these reports, particularly the employment report and CPI, show. A weaker labor market would likely trigger a cut. The Fed has been very focused on the labor market, even with what many would consider to be a low unemployment rate, at least by historical standards. As far as CPI, readings in recent months have been trending higher and remain above the Fed's longer term average target of 2%. Market participants appear to believe the Fed would cut, even with higher than desired inflation, if the labor market slips further.

But financial markets have more to be concerned about than just the Fed decision. The U.S. Congress needs to have next year's budget approved or pass a continuing resolution to extend current spending levels before the new fiscal year starts on October 1. In addition, a number of other countries, including the United Kingdom and France, are facing deficit concerns as their budgets have been proposed and then analyzed by investors. Deficit concerns have created political stress and pushed longer term bond yields to multi-year highs in these countries, as well as a number of other developed economies including Germany. In the U.S., deficit funding concerns have helped push the yield on the 30-year Treasury bond up over the last month to nearly 5% but the U.S. 10-year note yield has remained in a relatively tight range over the past four weeks. We believe bond investors are focusing on the long-term sustainability of current deficit growth rates. Meanwhile, the U.S. economy is slowing, which puts some downward pressure on yields.

The market is waiting for more data to resolve the cross-currents on yields. For now, we expect volatility in yields and prefer intermediate fixed income (3-7 year maturity range), whose returns are less rate sensitive compared to longer dated securities. More broadly, as the cross-currents spill over into profit, taking in equity markets, our equity focus is on quality large- and mid-cap equities, and we are trimming from small caps, as well as the Communication Services sector, as we see these areas fully valued after the robust rally since the early April lows. Moreover, as short-term rates fall and long-term rates rise, we have downgraded the Energy sector to reallocate to Financials.

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Definitions

Consumer Price Index (CPI) produces monthly data on changes in the prices paid by urban consumers for a representative basket of goods and services.

Producer Price Index (PPI) is a family of indexes that measures the average change in selling prices received by domestic producers of goods and services over time.

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