



Tom Slefinger
Market Strategist

Weekly Relative Value

WEEK OF MAY 26, 2026

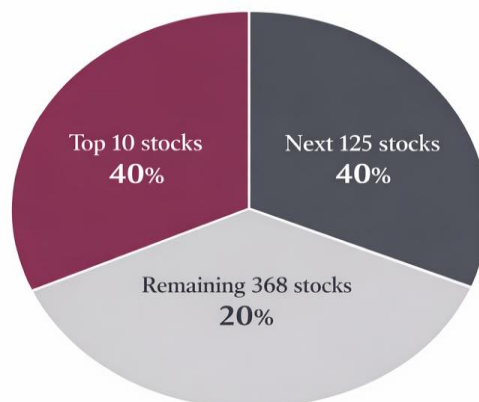
Record Highs, Rising Risks

“We will have a crash, I just can't tell you when, and I can't tell you how deep. But I can assure you, unfortunately, I wish I wasn't saying this, we will have a crash.”
— Andrew Ross Sorkin, Financial Journalist & Author of 1929

The major equity averages remain near record highs. Bank of America’s (BofA’s) latest monthly survey of global institutional investors shows a record jump in equity exposure, with respondents moving to a net 50% overweight from 13% in April — the highest level in four years. At the same time, they cut bond allocations to a net 44% underweight. Cash levels fell to 3.9%, their biggest two-year drop, while private clients reduced liquidity to a record low below 10%. These are interesting, but dangerous times.

The top ten stocks in the S&P 500 now comprise 40% of the market cap. The next 125 largest stocks comprise another 40%. Then we have the remaining 368 stocks accounting for just 20% of the index. Do retirees, in particular, realize how much concentration risk there is in their portfolios? Do they even care?

S&P 500 Market Cap Concentration



Share of total S&P 500 market capitalization

PLEASE NOTE: The views and opinions expressed herein are those of the author and do not necessarily reflect the views of Alloya Corporate Federal Credit Union, Alloya Investment Services (a division of Alloya Solutions, LLC), its affiliates, or its employees.

THIS WEEK

- FIXATED ON INFLATION
- NEARING THE DANGER ZONE
- STILL ON THE ROPES
- PENDING HOME SALES
- SINGLE FAMILY HOMES AND APRIL SHOWERS
- THE MINUTES
- THE CONSUMER
- MARKET OUTLOOK AND PORTFOLIO STRATEGY



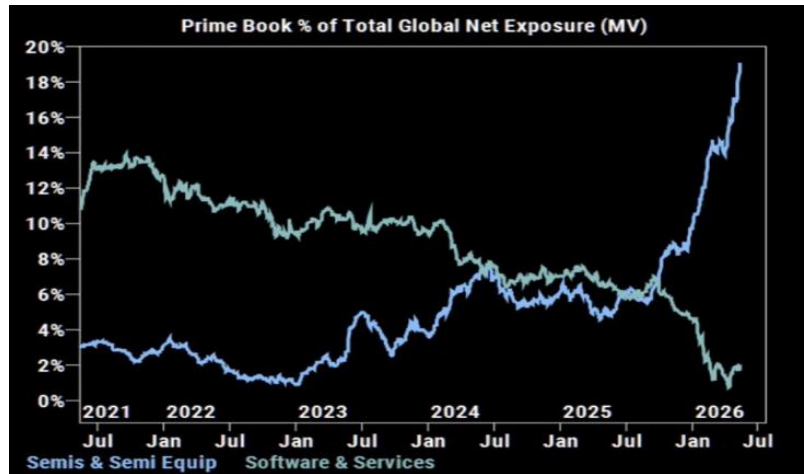
Credit Union Leadership
SYMPOSIUM
September 9-11, 2026
Nashville, TN

[REGISTER NOW](#)



SUBSCRIBE

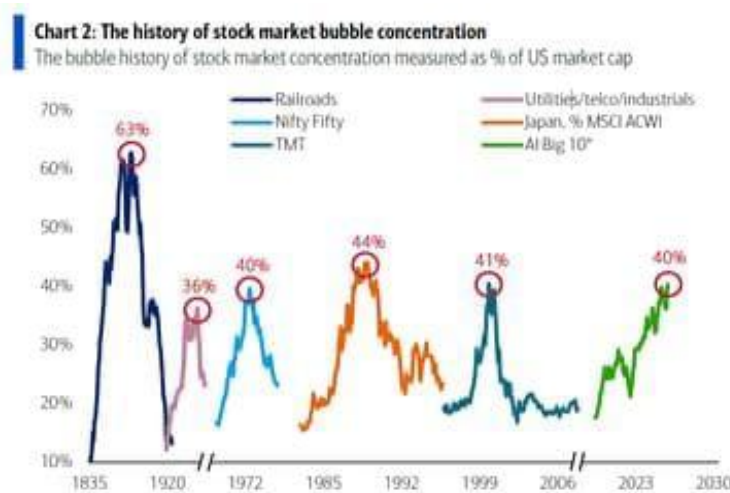
To further highlight the concentration risks, semiconductor stocks now make up almost 20% of total hedge fund net exposure. Five years ago, that number was 3%. Software and services was 14% back then. Today it sits at barely 2%. The two did not just shift; they completely swapped places.



Every major fund is in the same trade. Software has been cut to the bone on the view that artificial intelligence (AI) is disrupting it, while the market now values the semis (aka shovel makers) more than what is being built.

Maybe that is correct. Maybe semiconductors really are the trade of the decade. But with one sector at 20% of all hedge funds’ net exposure, this has never once ended in a good way.

BofA’s Michael Hartnett, Chief Investment Strategist at BofA Merrill Lynch Global Research, says this is the biggest bubble since the railroads!



And then we have extreme bullish sentiment. The Citi Panic/Euphoria Index, developed by Citigroup in 1987, is a sentiment gauge that tracks investor psychology to identify periods of extreme fear or excessive optimism. **It is used primarily as a contrarian indicator.**

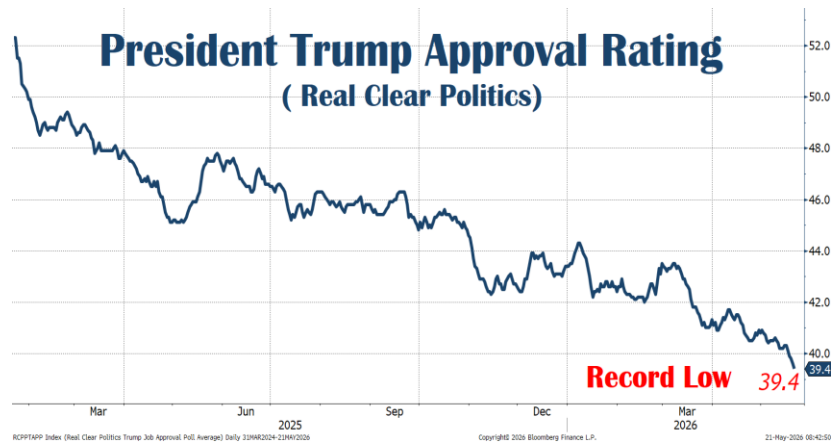
As a measure of how extreme bullish sentiment is, the Citi Panic/Euphoria Index at 91, more than double the 0.41 level where the euphoria level begins. We haven’t seen such giddiness in at least five years. Does this mean investors should

be craving wars, supply shocks and energy price spasms? It’s like rolling in the aisles with laughter at a horror flick. In any event, this all speaks to the fact that if there is a bear market out there right now, it is grounded in rational thinking.

For some perspective, historically, a reading in euphoria levels generates a better than 80% probability of stock prices being lower one year later, while panic supports a better than 95% likelihood that stock prices will be higher one year later.

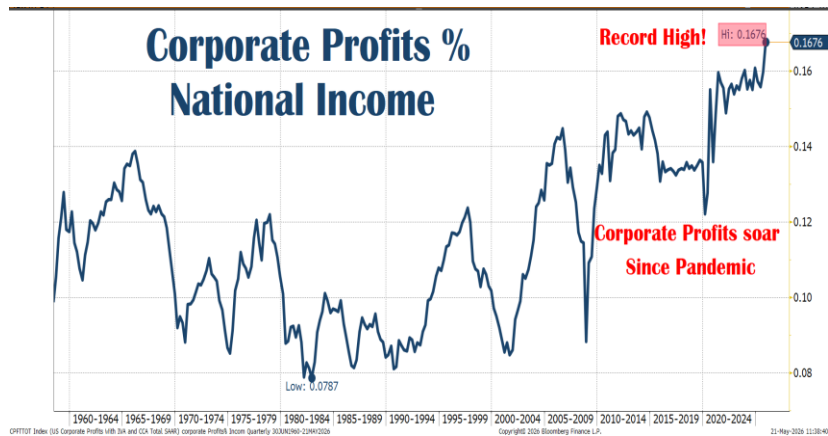


Moving on, making matters even more bizarre is that history shows us that there is typically a high correlation between presidential approval ratings and equity market performance. Not today. Donald Trump’s approval rating just sank to the lowest level of his second term — a mere 39% as per the latest Real Clear Politics poll. Fully 64% disapprove of his handling of the economy, and the share stating the country is on the right track this past month collapsed further to 32% from 37%. And it’s not just card-carrying Democrats — support has fallen dramatically among Independents and Republicans as well.



Then again, investors buy stocks for earnings. Larry Kudlow famously says profits are the stock market’s “mother’s milk.” When earnings rise, stock prices usually follow. Companies with high profit margins do extremely well because those margins let them reinvest and strengthen their advantages.

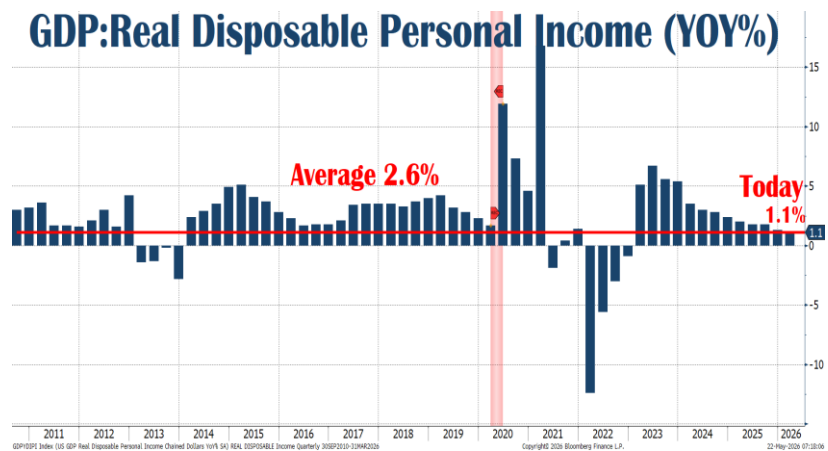
Indeed, investors have been willing to pay up for earnings, and with good reason given how strong profits have been. U.S. corporate profits have risen to near all-time highs since the start of the pandemic, both in nominal terms and as a share of national income.



Even as corporate profits continue to claim an unprecedented share of national income, beneath the surface, the more consequential economic trend is the stagnation in real after-tax personal income.

“In 1947, U.S. workers got about two-thirds of the income from their labors. Now, they’re getting something that is just a little bit over half. And so, they’re getting less of the pie.”
 — Erica Groshen, Former Head of the Bureau of Labor Statistics, now at Cornell.

U.S. labor's share of national income — the portion of gross domestic product (GDP) paid out as wages, salaries and benefits — has dropped to 53%, marking an all-time low in this highly uneven expansion. With the advent and now acceleration of AI, this trend is likely to worsen as people have less bargaining power. Let them eat cake!



Bottom line: Stocks remain near record highs, but investor positioning has become increasingly crowded and risky, with extreme concentration in a handful of large stocks and in semiconductors, while bullish sentiment has reached levels that historically have been strong contrarian warning signs.

At the same time, the market’s strength looks increasingly disconnected from broader public and economic reality, as presidential approval and consumer confidence weaken even while equities continue to rally. Although strong corporate profits have supported stock prices, the gains are not being broadly shared, with labor’s share of national income at a record low and real after-tax personal income stagnating.

FIXATED ON INFLATION

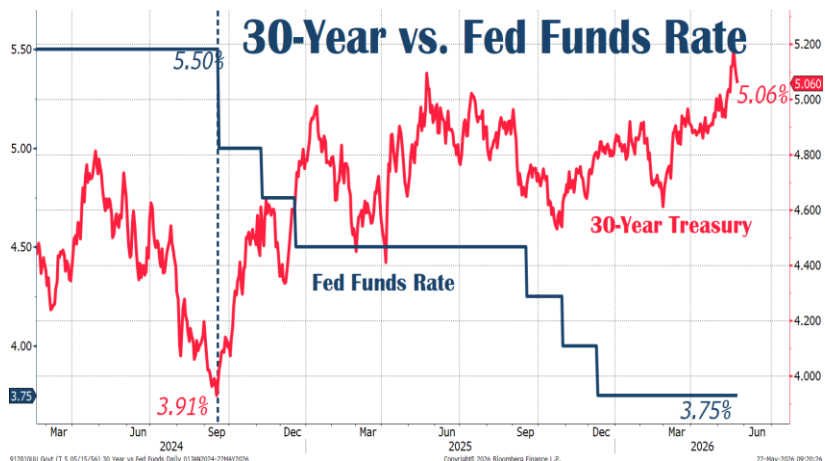
“I’m not a buyer that there’s some deep structural shift that’s going to make the economy more inflationary ...that’s largely because AI is likely to be an enormous positive supply shock....I don’t think we’re going to see it today or tomorrow, but over a several-year period it is likely to bring a reduction in inflationary pressures, as the economy’s capacity to produce inevitably expands.” — Nathan Sheets, Global Chief Economist, Citigroup, Inc.

As the stock market makes new record highs, the bond market remains fixated on inflation. Since the war with Iran started, the benchmark 10-year Treasury yield has spiked by 62 basis points to 4.55%.



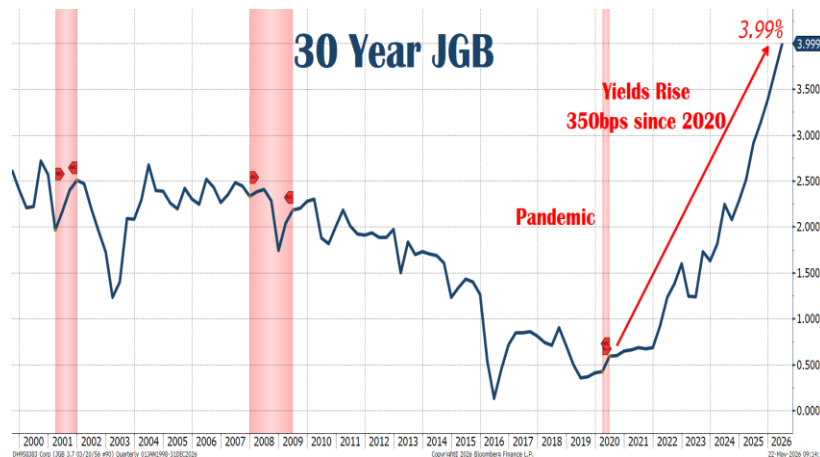
Last week, for the first time in nearly two decades, the U.S. Treasury issued a long bond with a coupon north of 5.0%. It has tested 5.2%, which is the highest since June 2007. A Bank of America survey shows 62% of global fund managers now expect the 30-year Treasury yield to reach 6%, and Citi says 5.5% is the next target.

As depicted below, the Fed has lowered the fed funds rate by 175 basis points to 3.75% September 2024. At the same time the 30-year Treasury yield soared by 115 basis points to 5.06%. Normally, there is a positive correlation between fed policy and long-term rates. Not this time. The market is pricing in higher inflation and bigger deficits no matter what the Fed says.



Consider what the bond market is saying. The Fed cut rates. The long bond rose anyway. Before the Fed began cutting in 2024, the 30-year Treasury yield was BELOW the federal funds rate. Today there is a spread of roughly 156 basis points between them. That is not what you normally see after a cutting cycle. That is not a normal relationship.

The selloff has been global. Japan's 30 year rose to 4%. U.K. long bonds are back to levels not seen since the 1990s. Germany's long bond yields are at 15-year highs even after the European Central Bank cut rates by 200 basis points. The move means investors are dumping bonds on inflation fears tied to Iran energy prices.



The bond market's instinct has been to treat the latest oil shock as a simple inflation problem: higher oil, higher Consumer Price Index, and higher rate hikes. But the Fed is not on autopilot. When inflation comes from a supply shock, policy makers must decide whether to look through the price spike or tighten enough to prevent inflation expectations from drifting higher. Here's the thing. Central bankers can't do much about the sudden stop to Persian Gulf energy, just like they had no fixes for higher commodity prices after Russia's invasion of Ukraine, or factory closures during the pandemic.

Monetary policy cannot produce more oil, reopen supply chains or fix an energy bottleneck. It can only cool demand and manage inflation expectations. Their key challenge now is to persuade everyone that once the latest storm has passed, the ocean will be calm again. As long as expectations remain anchored, policymakers have room to look through part of the oil-driven inflation impulse rather than rush into a more hawkish stance.

Bottom line: Bond investors are increasingly focused on inflation, driving long-term Treasury yields sharply higher even as the Fed has cut short-term rates — an unusual divergence that suggests markets are more worried about persistent inflation and deficits than about Fed easing. The selloff is global, with long-term yields also rising in Japan, the U.K. and Germany, largely on fears that the Iran-related oil shock could keep price pressures elevated. Still, central banks cannot fix a supply-driven energy shock directly; their real task is to keep inflation expectations anchored so they can avoid overreacting with unnecessarily aggressive tightening.

NEARING THE DANGER ZONE

"I used to think that if there was reincarnation, I wanted to come back as the President or the Pope or as a .400 baseball hitter. But now I would want to come back as the bond market. You can intimidate everybody."

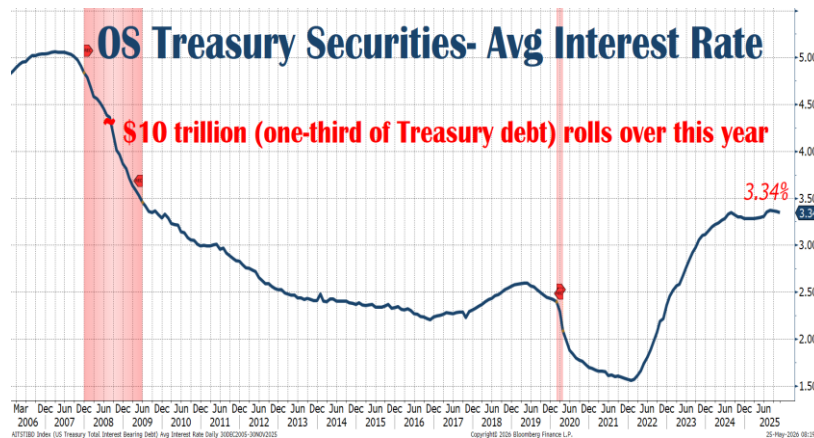
— James Carville, Political Strategist

The 10-year U.S. Treasury yield is perhaps the most important financial benchmark in the global financial system, as it drives valuations and market trends worldwide. When the 10-year yield rises, the cost of borrowing money for everything you might want to do also rises. Mortgages, car loans, business loans and credit card rates all take their cues from these Treasury yields.

At today’s debt levels, every 1 basis point increase in the government’s average borrowing cost adds roughly \$3.9 billion in annual interest expense. So, a 62-basis-point rise is not trivial — it translates to nearly \$250 billion in additional yearly interest costs, materially widening a 2025 budget deficit that was already around \$1.8 trillion.

Higher yields mean the U.S. government must pay tens or even hundreds of billions more in interest on its debt. The problem is that interest on the federal debt is already over \$1.2 trillion and is now the second largest item in the budget, exceeding defense, Medicare and Medicaid. With higher rates, interest costs would exceed Medicare spending next year, making it the second largest government program. By 2036, the federal government would spend almost as much on interest as on Social Security’s retirement program.

The U.S. government has \$31 trillion in public debt, and the average interest rate on that debt is 3.5%. They cannot refinance a single dollar of it at a lower rate than what they are currently paying. And they have \$9.7 trillion in securities maturing THIS YEAR that needs to be rolled over.



The U.S. government cannot afford yields going much higher.

According to the Committee for a Responsible Federal Budget (CRFB):

- Interest costs are projected to rise from a record 3.2% of gross domestic product (GDP) in 2025 to **5.3% of GDP** by 2036.
- By 2036, interest costs could consume about 30% of federal revenue, up from 19% today and a 50-year average of 12%.



Higher Treasury yields also raise borrowing costs for households and businesses. A 55-basis-point increase in mortgage rates would add nearly \$200 to the monthly payment on a \$500,000 30-year loan and about \$64,000 to its lifetime cost. On a \$1 million mortgage, the same increase would add roughly \$350 per month and nearly \$130,000 over the life of the loan.

Impact of a 55-Basis-Point Mortgage Rate Increase

\$500,000 30-Year Mortgage



+\$200 /month

Monthly Payment Increase

+\$64,000

Lifetime Cost Increase

\$1,000,000 30-Year Mortgage



+\$350 /month

Monthly Payment Increase

+\$130,000

Lifetime Cost Increase

Lawmakers must lower rates while preventing them from crowding out other priorities or triggering a fiscal crisis. The clearest path is deficit reduction, which can ease near-term inflation pressures, help bring down long-term rates by reducing crowding out and shrink the debt burden on which the government pays interest. With debt near record levels, time is short.

Interest rates are not that high from a historical perspective, but debt levels are dramatically higher today, financial markets are far more leveraged and political tolerance for economic pain is considerably lower.

Bottom line: Something has to give.

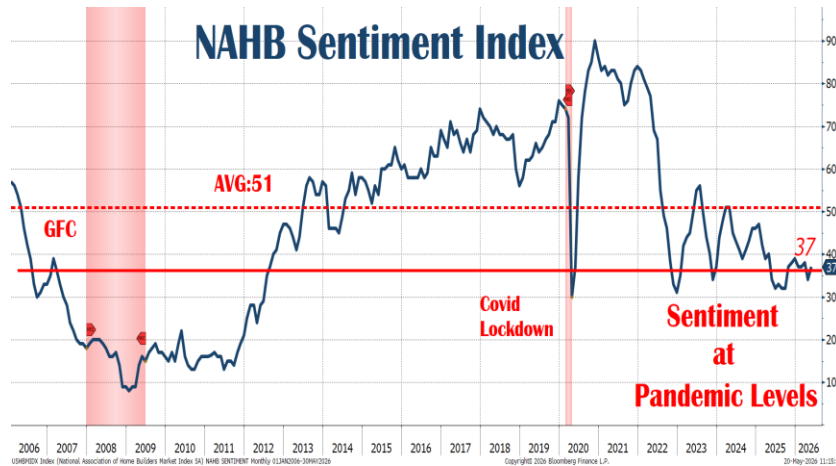
I do not see how U.S. rates can move materially higher and stay there without causing significant damage to the broader economy.

Those of us still bullish on the maligned bond market may need patience. But extreme pessimism often creates the best opportunities — much like buying the S&P 500 in August 1982, when few wanted any part of equities. At a 5.0% yield,

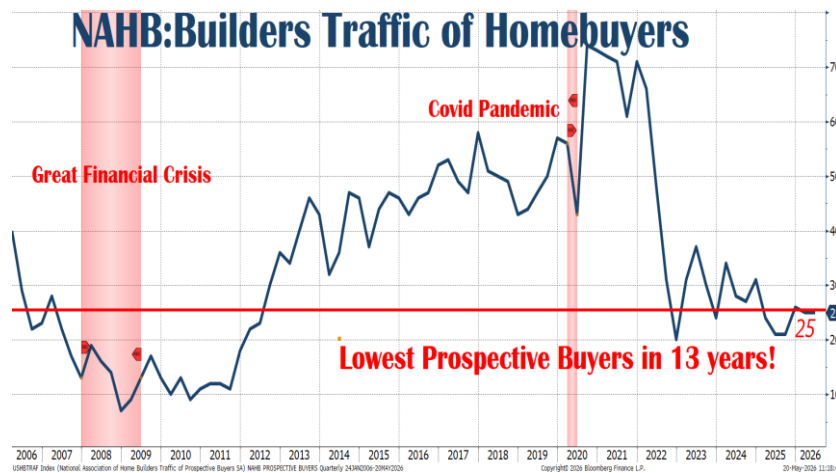
coupon income offers meaningful protection, and over the past 20 years, the odds of losing money at the long end of the Treasury curve over the following 12 months have been close to zero.

STILL ON THE ROPES

The National Association of Home Builders (NAHB) index of housing market activity increased from 34 to 37, but that’s still below March’s 38 print and the long-term average of 51.



The key leading indicator is traffic of prospective buyers, and the story was the same there — an improvement from 22 to 25, but mired at recessionary levels.



Bottom line: The triple threat of unaffordability, still-restrictive interest rates and macro uncertainty means that a meaningful recovery in housing is not likely any time soon. This looks increasingly like a structural affordability problem, not something that simply disappears if the Strait of Hormuz reopens quickly or energy prices retreat.

PENDING HOME SALES

Pending home sales for April came in stronger than expected at +1.4% month over month, although this was slower than March’s revised +1.7% month over month print. At first glance, the release looks strong overall: The year-over-year pace increased from +1.8% to +3.3%, the fastest trend since November 2024.

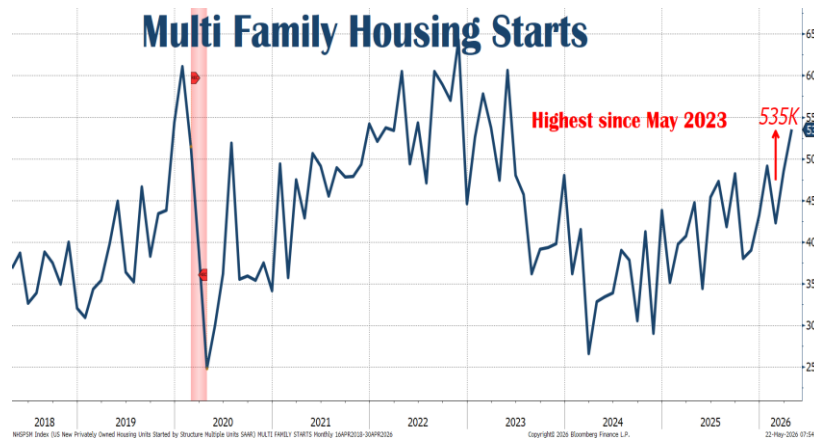
However, the data is a bit less rosy than they appear. Most of the increase in the year-over-year trend was due to base effects, because the year over year is measured against the depressed April 2025 level (the month of “Liberation Day,” when pending home sales fell off a cliff due to elevated uncertainty). Over the last six months, pending single family home sales have fallen by -1.1%.



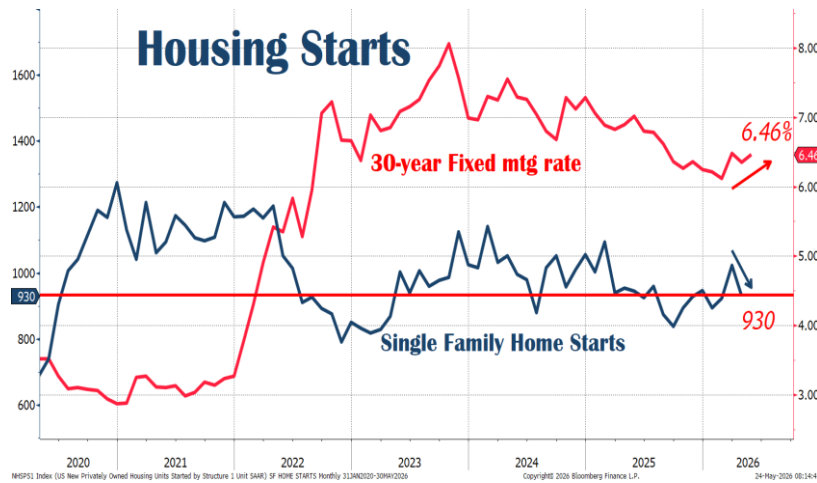
Bottom line: The key takeaway is that the level of pending home sales remains incredibly depressed. The current level is just barely above the bottom of the pandemic trough in 2020, and worse than those seen during the 2008-2010 Great Financial Crisis.

SINGLE FAMILY HOMES AND APRIL SHOWERS

Housing starts beat expectations in April, rising to a 1.465 million annualized pace versus a 1.410 million consensus. The smaller-than-expected decline was driven by a 10.3% month-over-month gain in multi-unit starts, which are up 19.7% year over year and at their highest level since May 2023.



That said, single-family starts fell by -9.0% month over month, and this is more reflective of the health of the housing sector. Here, we may be seeing some of the pain from mortgage rates starting to bite, as average rates have risen from 6.19% in February to 6.32% in March and 6.46% in April, with a further rise likely in May. Whatever remained of the hope for sub-5% mortgages is now very difficult to imagine.



Bottom line: The headline for housing starts was better than expected, but the underlying picture for owner-occupied housing remains soft, and the prospect of sub-5% mortgages looks increasingly remote.

THE MINUTES

“If I believe inflation expectations start to become unanchored, I would not hesitate to support an increase in the target range for the federal funds rate...But at this point that action is premature. It is time to simply sit and watch how the conflict and the data evolve.”

— Christopher Waller in a speech titled, “Policy Risks Have Changed”

In its April policy meeting, the Federal Open Market Committee (FOMC) elected to leave its benchmark federal funds rate unchanged in a range of 3.5% to 3.75%. But the decision prompted dissents from three policymakers who objected to the so-called “easing bias” in the post-meeting statement’s language, suggesting the Fed will eventually resume rate cuts.

The FOMC minutes from the April 29 meeting were released last week. Not surprisingly, there was a long discussion around inflation and inflation risks. There were concerns that inflation had been above +2.0% for several years, the potential for the Middle East conflict to persist for “an extended period,” even after the conflict ends, and that other commodity prices could remain elevated.



The “vast majority” of participants saw an increased risk that inflation could take longer to return to the +2.0% target. That said, this is far from a warning sign that the FOMC was setting the stage for future rate hikes. To me, if members of the FOMC were seriously concerned about inflationary outcomes, they would have dissented in favor of a tightening bias. They didn’t, because sustained upward pressure on inflation is not the base case.

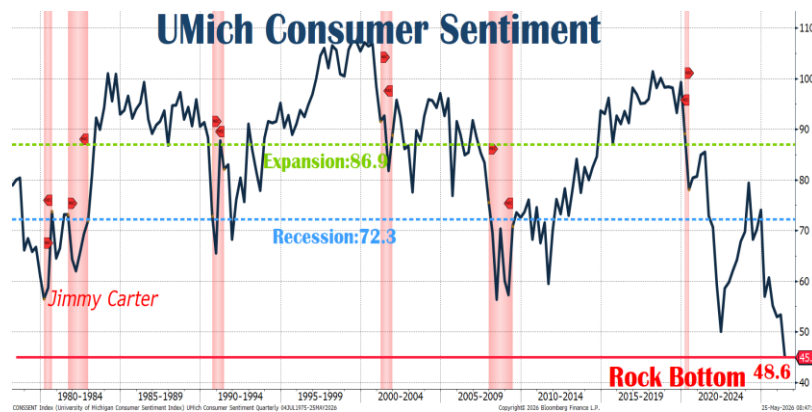
The minutes also clearly highlighted ongoing concerns about the labor market. While most FOMC participants felt labor market conditions had stabilized, those observations had qualifiers. For example, on signs of weak job growth, “a few participants” felt that this was possibly a sign of a fragile labor market, with “several participants” commenting that this was “not necessarily” the case.

Bottom line: The Fed held rates steady and the dissents were about future-cut language, NOT a push to hike even though inflation risks remain elevated.

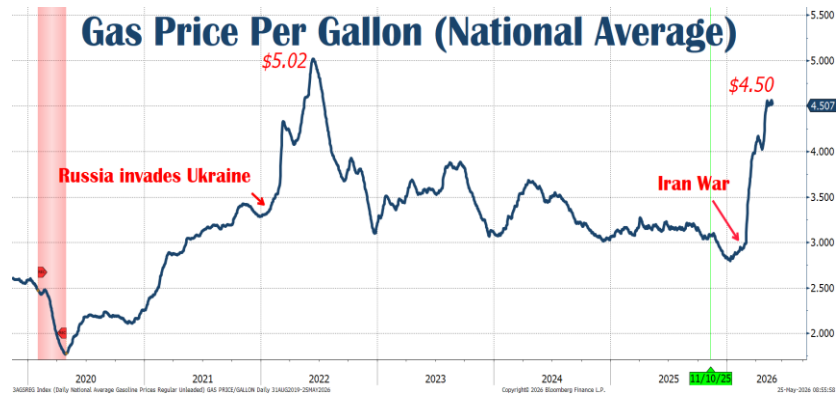
THE CONSUMER

“The cost of living continues to be a first-order concern, with 57% of consumers spontaneously mentioning that high prices were eroding their personal finances, up from 50% last month.” — Joanne Hsu, American Economist, Director of the University of Michigan Consumer Sentiment Index

With the "mini war" still ongoing (albeit with a “ceasefire” in place), expectations were for **record lows** in final May data released. And it did, with the headline sentiment — along with both current conditions and expectations — all plunging to record lows. Sentiment was down by a whopping **-10%** from April and posted **-13.5%** below the deep sub-basement reading under Jimmy Carter exactly 46 years ago this month. Americans have never been more miserable!



Gasoline prices hovering near the highest since 2022 are compounding Americans’ concerns about the cost of living and the absence of a deal to end the war. The toll of inflation on household budgets, particularly for lower-income consumers, poses a risk to the spending outlook. Critically, consumers appear worried that inflation will increase and proliferate beyond fuel prices, even in the long run.

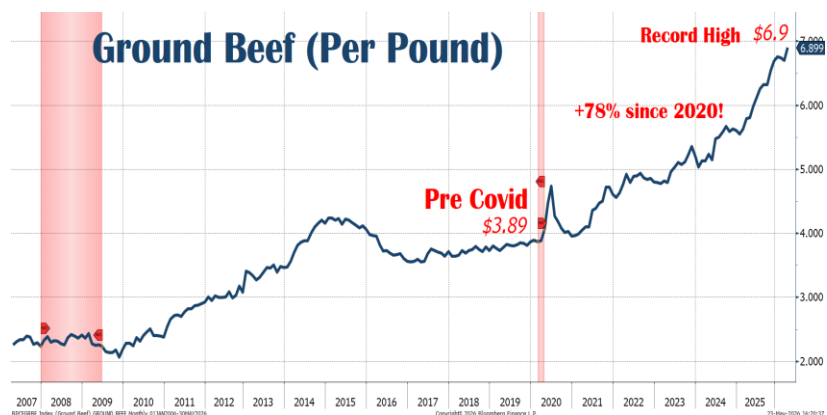


So far, consumer spending has held up primarily due to the stock-market wealth effect and higher, reduced savings and higher credit card debt. That said, the toll of inflation on household budgets, particularly for lower-income consumers, poses a risk to the spending outlook.

Have a look at a recent New York Fed article: [“Same Shock, Different Roads? A K-Shaped Pattern at the Pump.”](#) The article finds that low- and middle-income households are increasingly turning to carpooling and public transit. The pressure is mounting: The average household has seen a \$320 cash-flow drain since late February — a *de facto* tax increase of more than \$40 billion that continues to build. Credit card use is also rising sharply, with aggregate consumer delinquency rates nearing 5% for the first time since 2017 and the average FICO score falling for the first time in a decade. (See last week’s *WRV*, “Baptism of Fire,” for more on this theme.)

But inflation is not just an energy problem and is proving far stickier than many expected, and not in ways consumers can easily ignore. Since January 2020, food consumed at home is up 32%. Ground beef is up 19% year over year to a record \$6.90 per pound. Coffee is up 29%!

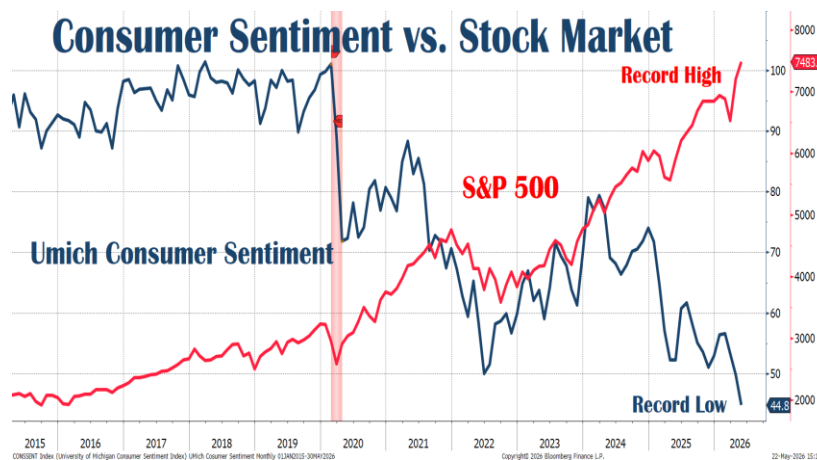
People don’t need a graph to see inflation trends. They experience inflation every week at the grocery store. And these increases are landing on top of prices that were already painfully high. We are not talking about a fresh shock. We are talking about acceleration on top of acceleration.



Making matters worse, consumers expect prices to rise an annualized 3.9% over the next five to 10 years, up from 3.5% in April and the highest in seven months. They also saw costs advancing 4.8% over the next year. This month’s increase in long-run expectations reflects sizable jumps among independents and Republicans. For the latter group, long-run inflation expectations are currently more than double their February 2025 reading on a monthly basis.



Finally, this is absolutely incredible: Over the last six years, the S&P 500 has risen +130% while consumer sentiment has collapsed by -55%, to its lowest since data began in 1952. We are witnessing the formation of the biggest wealth divide in modern history. This divergence is ultimately unsustainable.



Bottom line: Higher fuel and transportation costs, fading fiscal and tax-refund support, softer sentiment and a sluggish housing cycle all point to a consumer sector that is slowing, not collapsing. The consumer is pressured, but not out — at least not yet.

Households may feel worse about the economy, inflation and their finances, yet they remain upbeat on stocks. That split captures the psychology of this cycle: Economic pessimism is not weakening demand for equities and may even be reinforcing the view that stocks are the only real hedge against lost purchasing power.

MARKET OUTLOOK AND PORTFOLIO STRATEGY

“I want Kevin to be totally independent. I want him to be independent and just do a great job. Don’t look at me, don’t look at anybody, just do your own thing and do a great job.” — President Donald Trump

Kevin Warsh was sworn in as Fed Chair last Friday. The next FOMC meeting and first with Warsh as Fed chair is June 17. In his confirmation hearing for the job, Warsh repeatedly pledged to act independently even as he criticized the central bank for what he called mission creep and its response to the pandemic inflation surge.

Warsh takes over at a tense moment for the economy and the Federal Reserve. Price pressures have reaccelerated in recent months, driven by the impact of war in the Middle East on energy supplies. Meanwhile, the labor markets are weaker than the headline numbers suggest.

In the current economy, labor does not have enough leverage to generate the kind of wage inflation the Fed still seems worried about. Without wages chasing higher prices, inflationary spikes tend not to become self-reinforcing. At least not without wages following along.

Also, real-time housing data already show new lease rents falling, vacancy rates near cycle highs, and home prices cooling. The problem is that the Bureau of Labor Statistics' shelter calculation lags reality by 12-18 months. That means the disinflationary impulse is still slowly working its way into the official inflation data and should continue doing so for some time.

"AI is a significant disinflationary force, boosting productivity and wages." — Kevin Warsh

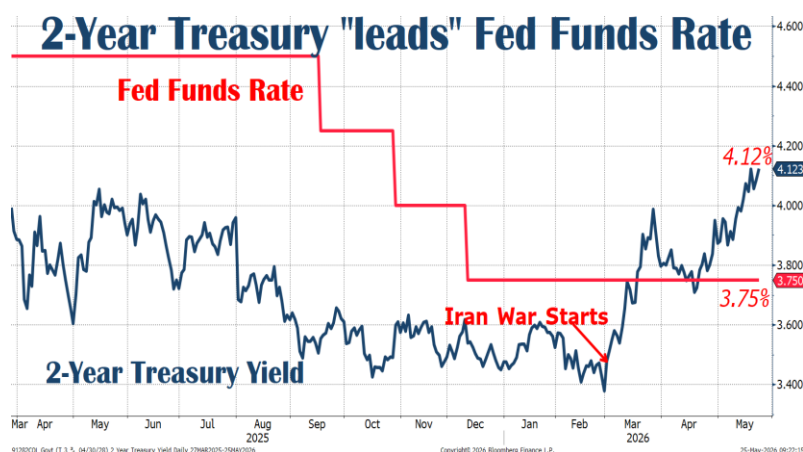
Kevin Warsh firmly believes the advent of AI will likely lead to higher level of productivity, which should lead to growth with lower inflation.

That said, this is an uncomfortable corner for any central bank to find itself in. It is a particularly uncomfortable corner for a Fed chair who has been on the job for one week.

While Trump appointed Warsh expecting a rate cut, that isn't happening soon.

According to fed fund futures, there is a near 100% chance the Fed holds pat. The market is also now pricing roughly a 50% probability of more rate hikes before year-end. Not cuts. Hikes. That is the bond market sending Warsh a message before he has even held his first press conference.

I should highlight that the 2-year Treasury yield typically leads the fed funds rate. In my view it's NOT possible to cut interest rates when the 2-year Treasury is almost 40 basis points higher than the fed funds rate.



Despite the near-term energy price shock and the potential for still higher inflation prints, my base case is that energy prices will reverse after the war ends and bonds will eventually benefit from the major disinflation in the pipeline from reduced wage pressure and a sustained slowdown in shelter costs. At the same time, the tariff impact should subside.

That said, with so much near-term uncertainty, I would continue to maintain a laddered portfolio while overweighting the front end of the curve.

WHY SUBSCRIBE TO THE WRV?

The financial world is full of opinions, often emphasizing rewards and ignoring risks. I cut through the noise and offer critical reviews of market headlines and economic realities, focusing on risk as an essential factor. This commitment makes *Weekly Relative Value (WRV)* distinct. Subscribers get timely updates on market trends and key risks. To receive future *WRV* issues in your inbox, subscribe [here](#).

MORE INFORMATION

For more information about credit union investment strategy, portfolio allocation and security selection, please contact the author at tom.slefinger@alloyacorp.org or (630) 276-2753.

As Alloya's Market Strategist, **Tom Slefinger** leverages nearly 40 years of investment strategy expertise to deliver insightful commentary on the economy and market events to optimize balance sheet performance at the credit union level. With thousands of subscribers, Tom's daily and weekly publications are widely read amongst credit union executives.

Prior to becoming the corporate's Market Strategist, Tom served as the Senior Vice President of Institutional Fixed Income Sales at Alloya Investment Services, a division of Alloya Solutions, LLC. In this role, Tom developed and managed operations associated with institutional fixed income sales in addition to developing investment portfolio strategies, identifying appropriate sectors and securities, and optimizing portfolio performance at the credit union level.

Tom holds a B.S. in business administration from the University of Maine. In addition, he holds a Series 7 and 63 through ISI.

The views and opinions expressed herein are those of the author and do not necessarily reflect the views of Alloya Corporate Federal Credit Union, Alloya Investment Services (a division of Alloya Solutions, LLC), its affiliates, or its employees. The information set forth herein has been obtained or derived from sources believed by the author to be reliable. However, the author does not make any representation or warranty, express or implied, as to the information's accuracy or completeness, nor does the author recommend that the attached information serve as the basis of any investment decision and it has been provided to you solely for informational purposes only and does not constitute an offer or solicitation of an offer, or any advice or recommendation, to purchase any securities or other financial instruments, and may not be construed as such.

*Information is prepared by ISI Registered Representatives for general circulation and is distributed for general information only. This information does not consider the specific investment objectives, financial situations or needs of any specific individual or organization that may receive this report. Neither the information nor any opinion expressed constitutes an offer, or an invitation to make an offer, to buy or sell any securities. All opinions, prices, and yields contained herein are subject to change without notice. Investors should understand that statements regarding prospects might not be realized. Please contact **Alloya Investment Services*** to discuss your specific situation and goals.*