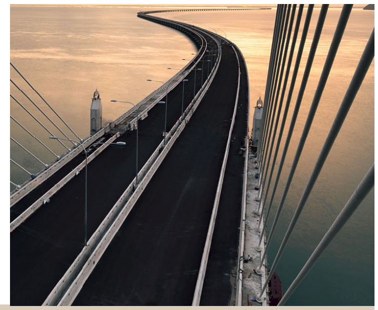
Investment Strategy



Weekly guidance from our Investment Strategy Committee — September 21, 2026

- U.S. Treasury yields have risen, but in an orderly manner consistent with income-oriented investors simply seeking more yield to compensate for risks.
- We remain unfavorable on U.S. Long-Term Taxable Fixed Income and, instead, prefer short-term maturities for their attractive yields and limited exposure to rising rates.

- Declining artificial intelligence (AI) costs are fueling adoption, not eroding demand. As with past technology cycles, cheaper inference is expanding AI's addressable market—while rising usage and agentic workflows sustain demand for compute, networking, and power even as token prices decline.
- As AI models become commoditized, durable value is shifting to data and workflow ownership. Competitive advantage increasingly favors platforms that control mission-critical workflows, governance, and orchestration rather than the underlying model itself.

- Escalations in the Middle East have pushed West Texas Intermediate (WTI) crude above $100 per barrel, while ongoing global refining constraints drove diesel prices to record highs.
- We believe commodities may provide investors with a potential hedge against renewed inflation risks as prices for refined products continue to rise.

- Despite geopolitical uncertainty, higher oil prices, and potential interest-rate pressures, merger and acquisition (M&A) dealmaking activity continued to strengthen and exceed prior cycle highs.
- We continue to favor merger arbitrage sub-strategies while monitoring interest rates and financing conditions for signs of slowing activity.

Fixed Income Spotlight

Tony Miano, CFA, CAIA
Global Fixed Income Analyst

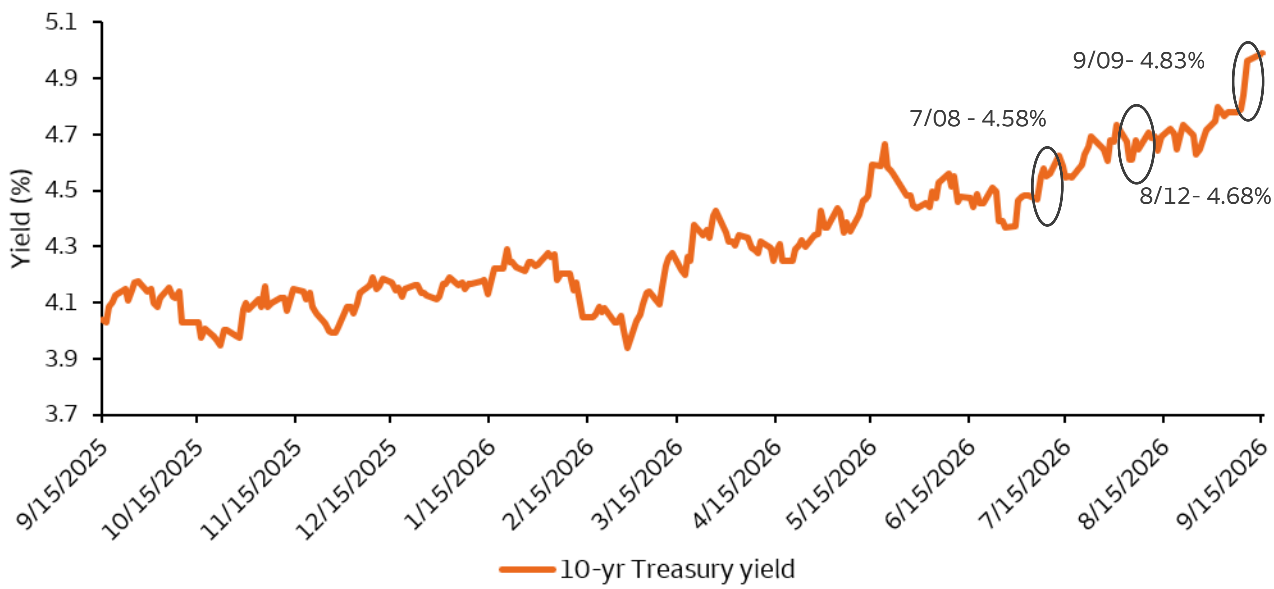
U.S. Treasury yields are rising to keep buyers interested

One of the factors that affects the price of Treasury securities is the price of other securities that also generate income. The large increase in corporate bonds issued by AI-related issuers since 2025 suggests a negative impact on prices for Treasury securities, driving yields higher. The key question is whether there will be enough buyers for all those new bonds, and what compensation (in the form of yield) investors will require to purchase them.

Are rising yields a warning sign?

Rising U.S. Treasury yields suggest that one factor weakening Treasuries is the rising supply of corporate-issued bonds. The chart below shows how yields have risen ahead of recent Treasury auctions. The September 9 auction of 10-year Treasuries produced a yield of 4.834%, the highest auction yield for this maturity since late 2007.

Chart 1. Rising yields for the last three 10-year Treasury auctions



Sources: Bloomberg and U.S. Treasury. Data as of September 15, 2026. Treasury auctions for the 10-year are generally held monthly. Yr = year. Yields represent past performance and fluctuate with market conditions. Current yields may be higher or lower than those quoted above. **Past performance is no guarantee of future results.**

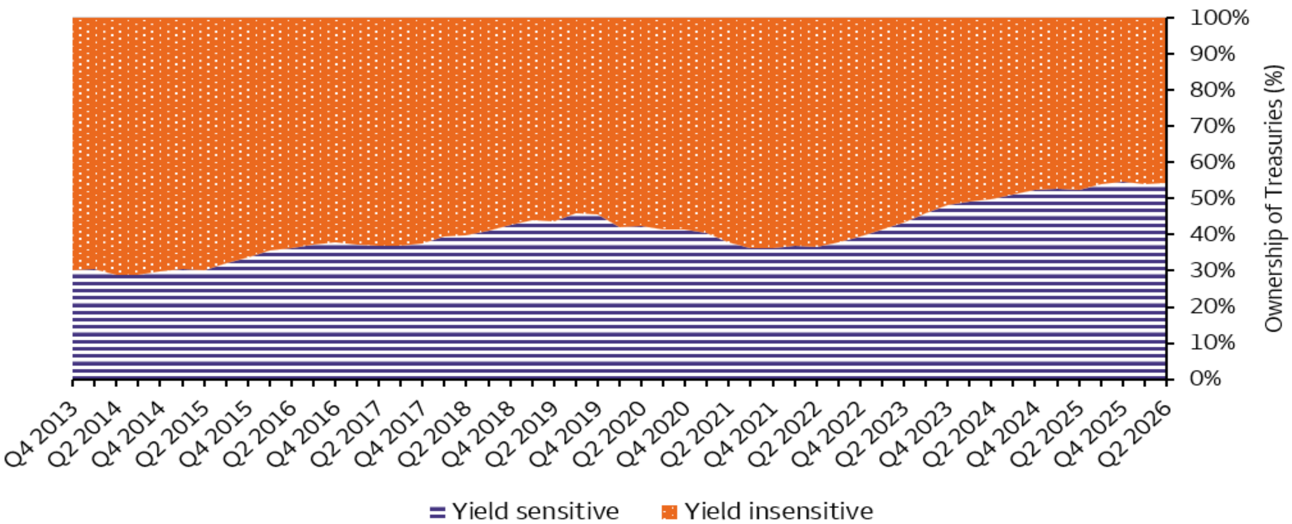
However, even as yields have been rising, demand at recent long-term treasury auctions has remained robust. The increase in yields has been orderly, without broad market disruption or significant volatility spikes. This suggests the market is adjusting rather than breaking down. Investors are seeking higher yields to compensate for new supply, as well as increased Treasury borrowing and rising inflation. Buyers may not be disappearing; they just require higher yields.

Who is buying Treasuries?

Strong demand at one auction does not mean the buyer base has stayed the same. Investors still purchase Treasuries, but the mix of buyers has evolved. Historically, many large holders of long-term U.S. Treasuries were long-term buyers, including central banks and sovereign wealth funds. Institutional rules often limit their investment choices, and they generally do not behave like short-term traders. These institutions often hold Treasuries to maintain ready access to cash (liquidity) or manage financial reserves, usually making investment income a secondary consideration.

Although central banks and sovereign wealth funds have not broadly abandoned the Treasury market, the majority of the additional issuance in recent years has been absorbed by a different type of buyer (see Chart 2). Investment funds, households, and other private investors generally place greater emphasis on the income a bond provides. These investors are more yield-sensitive, buying when yields are attractive and stepping back when income appears too low for the risks involved. When rising debt supply or persistent inflation creates additional risk, these investors demand higher yields.

Chart 2. Yield-sensitive investors now hold a majority of Treasuries



Sources: Treasury International Capital. Data as of June 30, 2026. Yield sensitive investors include Households, Funds (investment and money market), and foreign unofficial investors. Yield insensitive investors include banks, the Federal Reserve, state and local governments, and official foreign investors (including central banks). Q1 = first quarter. Q2 = second quarter. Q3 = third quarter. Q4 = fourth quarter. Yields represent past performance and fluctuate with market conditions. Current yields may be higher or lower than those quoted above.

How does this impact Treasuries in investor portfolios?

We expect continued demand for U.S. Treasuries, supported by their central role in global financial markets.[1] Although headlines have stated the risk that major foreign Treasury bond holders would sell large amounts of U.S. Treasuries, we believe the concerns of a disorderly withdrawal by major foreign investors is overblown and that a significant loss of confidence in U.S. government debt is unlikely.

More likely, we believe yields will need to remain attractive enough for price-sensitive investors to absorb additional Treasury supply. This environment could remain a headwind for long-term bonds, which have a larger risk of price declines if interest rates increase. In our view, investors who already own long-term Treasuries and do not need near-term liquidity may want to consider holding them to maturity rather than selling and locking in a loss after rising rates in recent years. Investors should still be aware that these bonds may remain volatile. Higher yields can create both a risk and a potential opportunity: They can pressure the prices of existing bonds while providing more attractive income on new bonds. For new investments, we prefer short-term bonds that can potentially offer attractive yields with less sensitivity to further increases in rates.

1. For more discussion of the future of U.S. Treasuries, see our May 2026 reports, "Paying America's Bills" and "Q&A: Addressing concerns about rising U.S. federal debt."

Equities

Thomas Christopher
Equity Sector Analyst, Communication Services and Information Technology

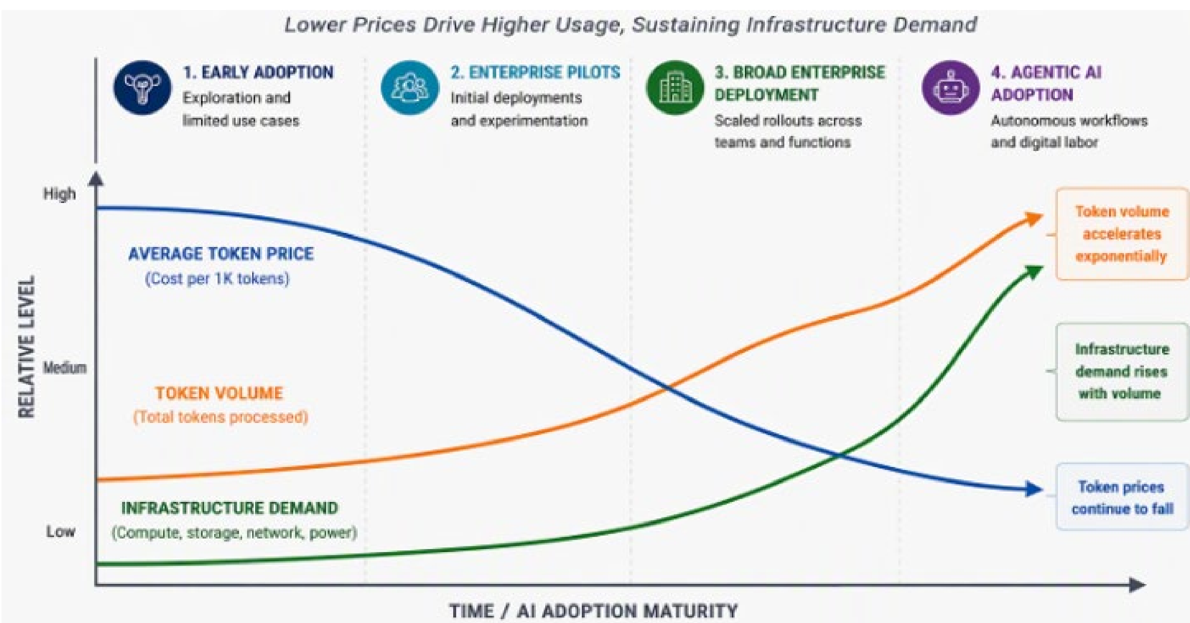
The AI opportunity continues to expand

The AI investment debate has evolved from whether demand exists to whether sufficient capacity can be built to meet that demand profitably. While declining AI costs and increased model competition have raised concerns about economics, we believe lower costs are more likely to accelerate adoption than reduce demand. History suggests lower technology costs often drive broader usage, and AI increasingly appears to be following a similar path. As enterprises move from experimentation to production across coding, search optimization, customer support, cybersecurity, and business workflows, token growth, infrastructure utilization, and enterprise adoption may become more important metrics than model pricing. While AI costs continue to fall, usage is growing even faster, driving higher overall spending and expanding opportunities across both AI infrastructure and software.

The next phase of AI is increasingly being defined by inference rather than training. Inference scales with usage and occurs every time an AI application is used, while agentic workflows can require multiple model calls, validation steps, and tool interactions. As a result, rising consumption may offset falling prices and support continued demand for computing power, networking, cloud infrastructure, data centers, and energy. We believe power availability is emerging as one of the most important constraints in the AI ecosystem, supporting continued investment across the infrastructure stack.

While infrastructure remains essential, we believe the next stage of value creation may increasingly shift toward software platforms that own proprietary data, control mission-critical workflows, and serve as AI control towers for governance, security, and model orchestration. As foundation models become more accessible, durable competitive advantages may increasingly come from data, workflow ownership, enterprise relationships, and the ability to deliver measurable business outcomes. In our view, we favor maintaining exposure across AI infrastructure, software and data platforms, and cybersecurity.

Chart 3. The metric that matters: Token volume growth



Sources: Wells Fargo Investment Institute; image created using Microsoft Copilot as of September 8, 2026. AI = artificial intelligence. K = thousand.

Real Assets

Mason Mendez
Global Real Assets Analyst

Oil is making headlines, but diesel is the real story

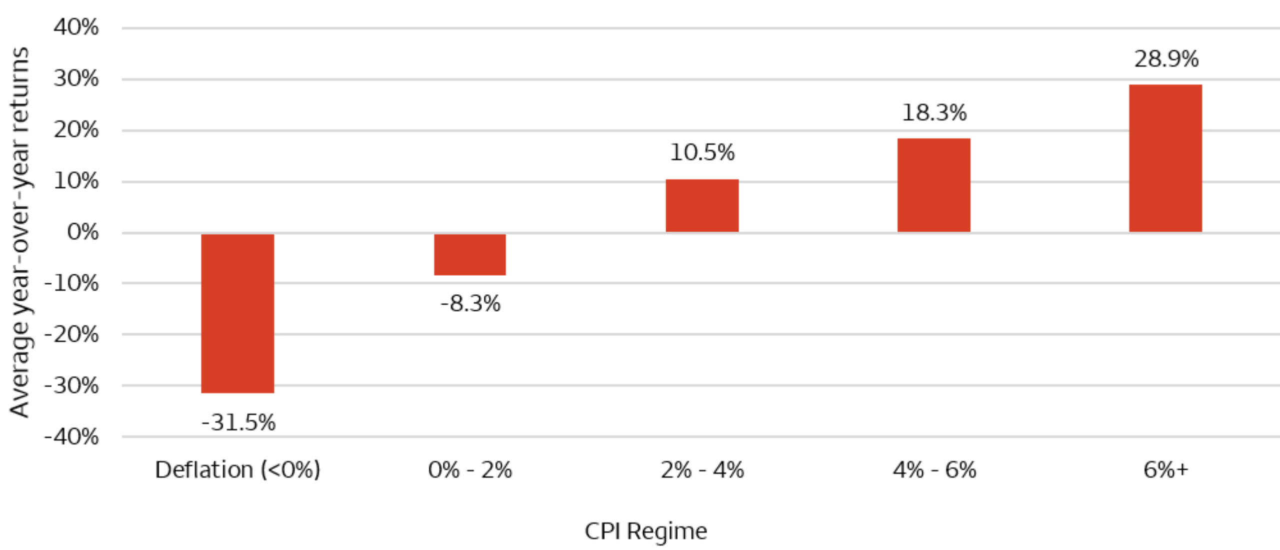
Energy prices have recently climbed as escalations in the Middle East conflict has raised the risk for prolonged supply disruptions. As a result, the front month WTI crude futures jumped above $100 per barrel on September 10 for the first time since May. Yet the bigger story may be diesel, which has surged to record highs[2] and is putting upward pressure on everything from transportation costs to food prices. For investors, we believe commodities may offer a potential hedge against these renewed inflation risks.

Despite WTI sitting roughly 10% below its 2026 peak, diesel prices continue to rise to record highs and are up 74% year-to-date, as of September 14. This divergence reflects the growing constraints in global refining capacity and dwindling inventories. While U.S. refiners are operating near full capacity, refining activity elsewhere has been significantly impaired. Disruptions to energy exports through the Strait of Hormuz and attacks on Russia's energy infrastructure have hindered the world's ability to produce and export fuels needed to keep up with demand. Meanwhile, exporters like China have prioritized its fuel supplies to be used domestically rather than exporting, further reducing the supply available to global markets.

This matters because refined products, not crude oil, are directly used for many crucial areas of the economy such as transportation, agriculture, construction, and manufacturing. As prices for fuels rise, costs can increase across supply chains and contribute to higher inflation.

For investors, we remain favorable on Commodities and believe they may offer a potential hedge against these renewed inflation risks. Since 1971, the Bloomberg Commodity Total Return Index has performed best during periods of elevated inflation, generating average year-over-year returns of 10.5% when inflation ranged between 2% and 4%, and even stronger returns with inflation above 4% (see Chart 4). Constrained energy supply and refining bottlenecks may continue to pressure inflation higher. Therefore, we believe commodities may offer a potential hedge against rising prices.

Chart 4. Commodities may offer a potential hedge against inflation



Sources: Bloomberg and Wells Fargo Investment Institute. Monthly data is from January 1970 – August 2026. The Bloomberg Commodity Total Return Index was used to measure commodity performance. Inflation is measured by the year over year change in the Consumer Price Index (CPI). Deflationary periods are marked when the CPI turns negative. An index is unmanaged and not available for direct investment. **Past performance is no guarantee of future results.**

2. AAA U.S. National Average Diesel.

Alternatives

Mark Steffen, CFA, CAIA
Global Alternative Investment Strategist

M&A strength persists despite headwinds

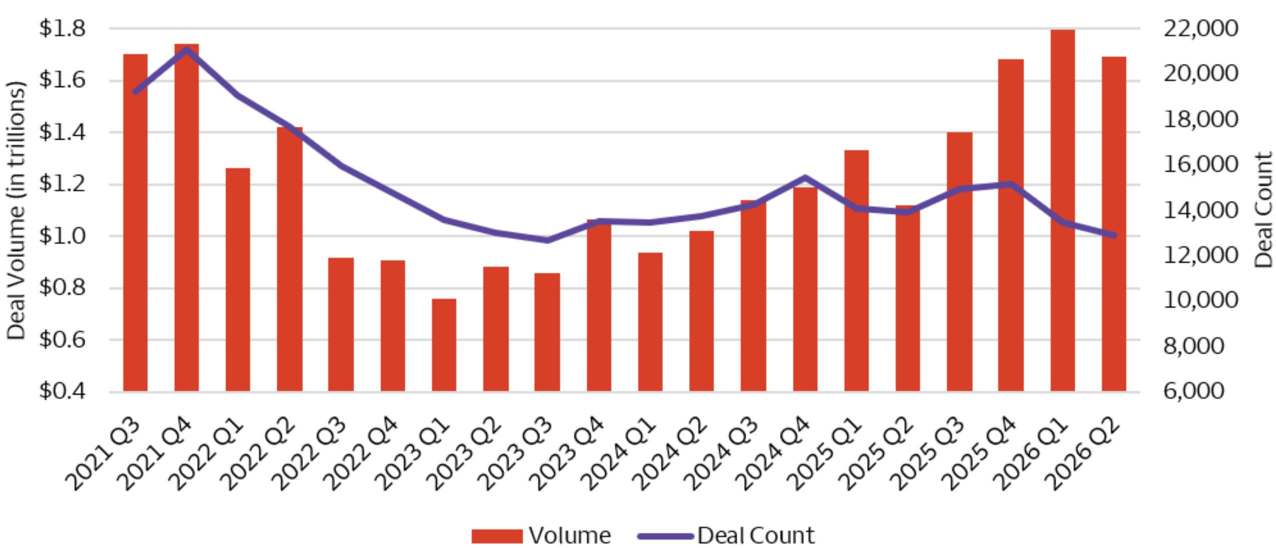
Despite ongoing geopolitical tensions, elevated oil prices, and expectations for potentially higher short-term interest rates on the horizon, M&A activity continued to strengthen through the first half of 2026. Building on the momentum that began in late 2025, overall deal volume has remained near record levels.

M&A activity reached a cycle low of $757 billion in the first quarter of 2023 (see Chart 5). Since then, deal volume has steadily recovered, reaching a record $1.8 trillion in the first quarter of 2026 and surpassing the elevated levels seen during the peak activity of 2021. While total deal volume has increased significantly, the number of completed transactions has trended lower, declining to approximately 13,000 deals in the second quarter of 2026. This suggests that larger transactions are playing an increasingly important role in driving overall activity. Much of this growth has been concentrated in the Information Technology, Industrials, and Health Care sectors, which together accounted for approximately 57% of North American deal volume. [3] Strong equity market performance and investments in AI-related themes have provided meaningful support for dealmaking activity.[3]

Although geopolitical conflicts and higher energy prices have created uncertainty, they have not materially slowed M&A transaction activity to date. Looking ahead, investors will be closely monitoring the Federal Reserve's renewed focus on maintaining price stability, as the prospect of higher short-term interest rates could influence financing costs and the pace of future M&A activity.

While we continue to monitor for signs that the recovery may lose momentum, we remain constructive on merger arbitrage strategies. In our view, the sustained strength in M&A activity continues to provide a favorable backdrop for deal completion and supports our expectation that merger arbitrage strategies may potentially benefit from this backdrop in the periods ahead.

Chart 5. M&A volumes and deal count on quarterly basis (last 5 years ending June 30, 2026)



Sources: Bloomberg. Data as of June 30, 2026. Q1 = first quarter. Q2 = second quarter. Q3 = third quarter. Q4 = fourth quarter.

Alternative investments, such as hedge funds, private equity, private debt and private real estate funds are not appropriate for all investors and are only open to "accredited" or "qualified" investors within the meaning of U.S. securities laws.

3. Citi, Executive M&A Summary, First Half 2026 Edition.

Tactical guidance*

Cash Alternatives and Fixed Income

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
	Developed Market Ex-U.S. Fixed Income U.S. Long Term Taxable Fixed Income	Cash Alternatives Emerging Market Fixed Income High Yield Taxable Fixed Income U.S. Intermediate Term Taxable Fixed Income	U.S. Short Term Taxable Fixed Income	

Equities

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
	U.S. Small Cap Equities	Developed Market Ex-U.S. Equities Emerging Market Equities U.S. Mid Cap Equities	U.S. Large Cap Equities	

Real Assets

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Digital Assets Private Real Estate	Commodities Private Infrastructure	

Alternative Investments**

Most Unfavorable	Unfavorable	Neutral	Favorable	Most Favorable
		Hedge Funds—Equity Hedge Hedge Funds—Macro Hedge Funds—Relative Value Private Equity Private Debt	Hedge Funds—Event Driven	

Source: Wells Fargo Investment Institute, September 21, 2026. Please see Wells Fargo Investment Institute's Asset Allocation Strategy Report for more detailed, investable ideas in each asset group.

*Tactical horizon is 6-18 months

**Alternative investments are not appropriate for all investors. They are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. Please see end of report for important definitions and disclosures.

Risk considerations

Each asset class has its own risk and return characteristics. The level of risk associated with a particular investment or asset class generally correlates with the level of return the investment or asset class might achieve. **Stock markets**, especially foreign markets, are volatile. Stock values may fluctuate in response to general economic and market conditions, the prospects of individual companies, and industry sectors. **Foreign investing** has additional risks including those associated with currency fluctuation, political and economic instability, and different accounting standards. These risks are heightened in emerging markets. **Small- and mid-cap stocks** are generally more volatile, subject to greater risks and are less liquid than large company stocks. **Bonds** are subject to market, interest rate, price, credit/default, liquidity, inflation and other risks. Prices tend to be inversely affected by changes in interest rates. **High yield (junk) bonds** have lower credit ratings and are subject to greater risk of default and greater principal risk. Although **Treasuries** are considered free from credit risk they are subject to other types of risks. These risks include interest rate risk, which may cause the underlying value of the bond to fluctuate. The **commodities** markets are considered speculative, carry substantial risks, and have experienced periods of extreme volatility. Investing in a volatile and uncertain commodities market may cause a portfolio to rapidly increase or decrease in value which may result in greater share price volatility. **Real estate** has special risks including the possible illiquidity of underlying properties, credit risk, interest rate fluctuations and the impact of varied economic conditions.

Alternative investments, such as hedge funds, private equity/private debt and private real estate funds, are speculative and involve a high degree of risk that is appropriate only for those investors who have the financial sophistication and expertise to evaluate the merits and risks of an investment in a fund and for which the fund does not represent a complete investment program. They entail significant risks that can include losses due to leveraging or other speculative investment practices, lack of liquidity, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification, absence and/or delay of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than mutual funds. Hedge fund, private equity, private debt and private real estate fund investing involves other material risks including capital loss and the loss of the entire amount invested. A fund's offering documents should be carefully reviewed prior to investing.

Hedge fund strategies, such as Equity Hedge, Event Driven, Macro and Relative Value, may expose investors to the risks associated with the use of short selling, leverage, derivatives and arbitrage methodologies. Short sales involve leverage and theoretically unlimited loss potential since the market price of securities sold short may continuously increase. The use of leverage in a portfolio varies by strategy. Leverage can significantly increase return potential but create greater risk of loss. Derivatives generally have implied leverage which can magnify volatility and may entail other risks such as market, interest rate, credit, counterparty and management risks. Arbitrage strategies expose a fund to the risk that the anticipated arbitrage opportunities will not develop as anticipated, resulting in potentially reduced returns or losses to the fund.

Definitions

Bloomberg Commodity Total Return Index reflects the returns that are potentially available through an unleveraged investment in the futures contracts on 19 physical commodities comprising the Index plus the rate of interest that could be earned on cash collateral invested in specified Treasury Bills. The Index is a rolling index rebalancing annually.

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

An index is unmanaged and not available for direct investment.

General disclosures

Unless otherwise noted, market data, index data, economic statistics, earnings data, and related analytical information referenced throughout this report are sourced from Bloomberg and Wells Fargo Investment Institute, as of September 15, 2026.

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