

FORTITUDE CAPITAL MANAGEMENT

Independence • Integrity • Insight

800 Roosevelt Road
Bldg. B, Suite 413
Glen Ellyn, IL 60137
630.545.2800
fortitudecapitalmgmt.com

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"You can never plan the future by the past." – Edmund Burke

"Doubt is not a pleasant condition, but certainty is an absurd one." – Voltaire

"... a choice by the people themselves is not generally distinguished for its wisdom." – Thomas Jefferson

Fellow Investors:

If you are looking for conflicting signals, the economy and the markets do not disappoint. We are bombarded with data and signals, opinions by so-called experts on all of it and predictions on where things will go. Seemingly the predictions that turn out to be accurate are just as likely to be random. The world is full of moving parts and unpredictable variables. As we close out the third quarter and roll into the fourth quarter, the future continues its unpredictability as we all live in interesting times whether we like it or not.

First, let's review third quarter results. The S&P 500 moved modestly in the quarter, going up 2.0% for the three months. That does not give as accurate picture of the day-to-day volatility as the S&P 500 made daily moves either up or down by over one-half percent on 45% of the trading days. Despite the relatively flat quarter, the S&P 500 is up 11.8% year to date. Concentration remains an issue, as the top five companies in the capitalization-weighted index comprise over 30% of the index. This was driven by two companies, Nvidia and Apple, which both had extraordinary quarters.

We have been looking for a broadening of equity markets. The first half of the year did bring signs of a broadening market as the small and mid-caps outperformed but that turned around in the third quarter. So, we are still waiting. The equally-weighted S&P 500 declined 2.3% for the quarter compared to the capitalization-weighted index's modest gain. Year-to-date the equally-weighted S&P 500 was up 8.6%. The Nasdaq Composite is even more concentrated with the top five names making up nearly half of the index. It was up 2.5% for the quarter and 15.6% year-to-date. Smaller companies took it on the chin for the quarter with the Russell 2000 declining 7.5% in the quarter although still up by 12.7% for the year. Internationally, the EAFE was up 2.9% for the third quarter and 8.1% for the year.

Both the S&P 500 and Nasdaq Composite showed steady increases from the low reached at the start of the Iran war, although the Nasdaq Composite exhibited more volatility. Both of these are heavily driven by the concentration mentioned above and the enormous capital investment and resultant expectations related to AI. The Russell 2000, equal-weight S&P, and EAFE indexes peaked around mid-August before tailing off as interest rate expectations changed to anticipate a Fed hike which came to fruition in September.

The two-year treasury finished the quarter at 4.88%, showing a steady increase over the last six months before a sharp increase in September as the Fed move became imminent. The ten-year finished the quarter at 5.29% following the

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same pattern. The higher rates are a concern across the economy as it affects consumers, businesses, government budgets, and the discounting of asset values. Part of the pressure on interest rates is expected inflation, the biggest factor of which is energy costs as oil has been very volatile due to the war. At the beginning of the quarter crude oil (spot WTI) was just under \$70 a barrel, but that was short-lived as price hit a high of \$107/bbl in mid-September and finishing the quarter just under \$100/bbl. Another factor pressuring interest rates is demand for capital. Between the capital being poured into the various elements of the data center investments and the always hungry federal government, demand for capital is huge.

But are things good or bad? It depends who you ask and what their interests are. Talking one's book is endemic in the financial press. Reading between the lines is important. Revenue growth, margins, and earnings are generally strong, especially among the mega-tech giants plowing into the AI universe. Earnings for the S&P 500 have grown by double-digit rates for eight consecutive quarters. While currently concentrated at the top, the anticipation is that there will be a broadening of benefits that should move through the economy with time. Improvements in productivity and the boom in construction should benefit companies throughout the economy. The job market is generally considered tight, not necessarily strong, but tight and perhaps currently unbalanced as demand for trades skills outstrip current available skilled workers, much to the benefit of the current trades cohorts. Economic transitions are always difficult to navigate, but historically turn out just fine, or more than fine after we navigate the rapids.

Finally, what about the election in less than a month? Polls are tight and results uncertain. The track record is actually encouraging. Since 1950, the S&P 500 has gone up over the 12 months following a mid-term election 100% of the time. Fingers crossed that this record stays intact.

Rough markets are like an airplane flying through rough weather. It can be uncomfortable at times as we ride toward our destination. We rely on the pilot to steer us safely through to a safe landing. That is the role we try to play as we navigate the ever changing environment.

Sincerely,

Erik Ford

Jason Marrs

The S&P 500 Index, or the Standard & Poor's 500 Index, is a market-capitalization-weighted index of the 500 largest publicly traded companies in the U.S. It is not an exact list of the top 500 U.S. companies by market capitalization because there are other criteria to be included in the index.

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The S&P 500 Equal Weight Index (EWI) is an equal-weight version of the popular S&P 500 Index. Although both indexes are comprised of the same stocks, the different weighting schemes result in two indexes with different properties and different benefits for investors.

The term Russell 2000 Index refers to a stock market index that measures the performance of the 2,000 smaller companies included in the Russell 3000 Index. The Russell 3000 is a capitalization weighted index representing approximately 96% of the investable U.S. equity market.

The MSCI EAFE Index tracks large cap and mid-cap companies in developed countries around the world. The index primarily covers the Europe, Australasia, and the Far East regions.

The NASDAQ Composite is a stock market index of the common stocks and similar securities listed on the NASDAQ stock market. Along with the Dow Jones Average and S&P 500 it is one of the three most followed indices in US stock markets. The composition of the NASDAQ Composite is heavily weighted towards information technology companies.

Indices mentioned are unmanaged and cannot be invested in directly. Past performance is not a guarantee of future results.

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