

WEEK ENDED MAY 22, 2026

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Great (Inflation) Expectations – Part I

“Inflation is as violent as a mugger, as frightening as an armed robber and as deadly as a hit man.”

– Ronald Reagan

The Through Line: Last week’s toasty reads on U.S. consumer and business inflation nudged both bond yields and investor anxiety higher. Many market watchers were surprised it hadn’t happened sooner, given the ongoing energy shock of the past few months on top of persistent cost stickiness created by last year’s shifts in tariffs, trade, and immigration policy. Inflation and interest rates (bond yields) are closely related. However, there are important nuances in what influences each – and how they interact with each other. This week, we do a deep dive into inflation. Next week, we will delve more thoroughly into fixed income markets and how they are absorbing increased supply and shifting fundamentals.

Inflation: transitory or tenacious?

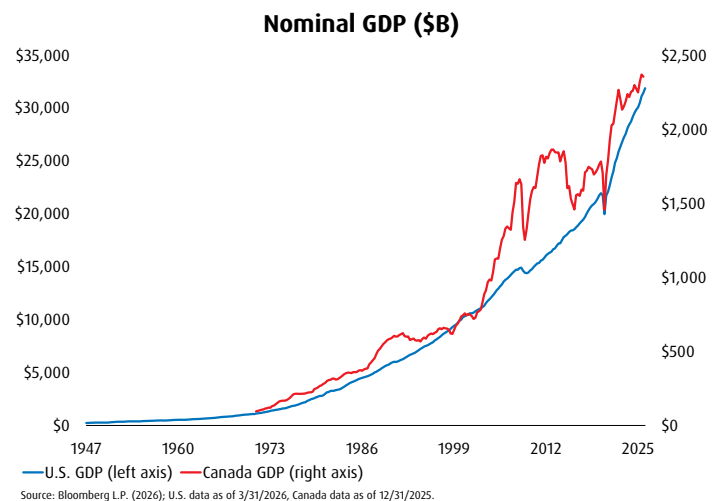
What a difference a few trading days make. Just last week, stocks were hitting new highs, buoyed by Q1 earnings growth that was much stronger than initially anticipated ([WSP - Q1 Earnings Update](#)) plus optimism over the generationally transformative nature of the AI revolution. This week, attention has turned to anxiety over rapidly rising bond yields and whatever policy response they may provoke from global central banks.

Most strategists entered the year presuming the U.S. Federal Reserve’s Federal Open Market Committee (FOMC) could resume interest rate cuts by year’s end in light of steady progress for the economy and inflation. War in the Middle East – and concomitant damage to energy prices – marred the picture, however. Strategists struggled to determine whether the conflict would see a spike and then a relatively quick retreat for energy prices – or embed cost increases more perniciously into a broader range of goods and services. (Then, too, there was some question whether it truly even mattered for North America, a net-energy exporter, relative to Europe and Southeast Asia, which are more dependent on energy imports.)

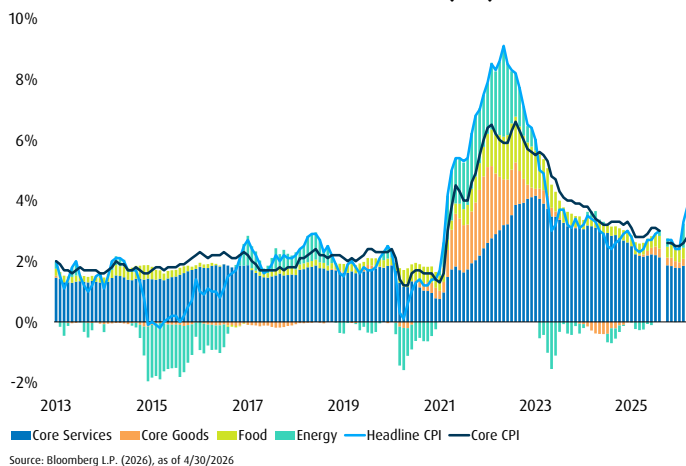
For investors and policy makers, trying to ascertain whether a particular economic event would produce temporary or lasting inflation has been a repeated challenge. **Five out of the last seven springs have featured a seemingly one-off shock that could have easily hardwired sustained higher inflation** (COVID in 2020, Ukraine/Russia in 2022, Silicon Valley Bank in 2023, Liberation Day in 2025, and this year’s U.S.-Israel-Iran war). Inflation did spike to multi-decade highs in the pandemic’s wake

before eventually settling into the lowish single digits of the past few years. For consumers, slowing inflation doesn’t change the irritation that it’s a slower increase from a much higher absolute level of prices – a factor exacerbated by the recent substantial increase in prices at the pump.

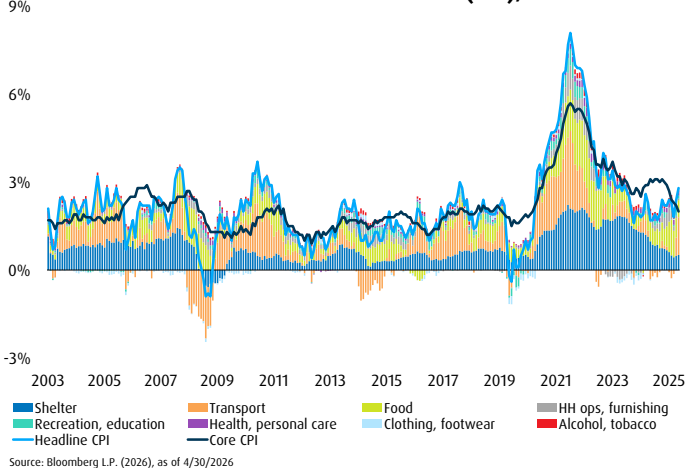
For investors, though, GDP has climbed despite repeated disruptive events and price increases have slowed in both the U.S. and Canada (albeit settling at levels more akin to very long-term averages than the abnormally low levels we saw during COVID). Fixed income bond yields (illustrated here via the 10-Year U.S. Treasury) have remained in a relatively tight band – even after last week’s upmove.



U.S. Consumer Price Index (CPI), YoY



Canada Consumer Price Index (CPI), YoY



U.S. 10-Year Treasury Yield (%)



Inflation gets a bad rap

Investors are trained to fear the mere mention of inflation. Yet a moderate amount of it can be constructive for an economic system because it provides pricing power for companies and the ability to raise worker wages over time.

Stock and bond markets look at inflation somewhat differently. Equity investors care about growth and margins (*return on capital*). Higher selling prices featuring steady margins can lead to faster growth in earnings. Bond investors, on the other hand, care about credit worthiness and maintaining their purchasing power (*return of capital*). Bond buyers are also concerned with why rates are moving. Is it strong organic growth, for example, or slack demand for issuance needing a higher yield to entice buyers? They also understand the toxic nature of inflation, which eats away at purchasing power minute by minute (e.g., this year's dollar buys \$0.97 of next year's goods). Thus, they are more nervous about whiffs of inflation running hotter – or for longer – than current yields support.

Inflation's influence on prices and interest rates

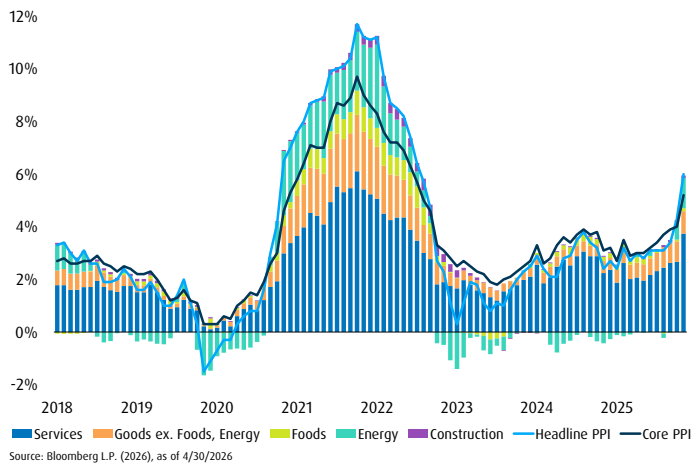
The bleed-through of inflation into prices is not typically straightforward. Considerations like market position, customer loyalty (or understanding of their exhaustion over previous price increases), ability to offset costs by achieving efficiencies elsewhere, and/or a desire to take market share all factor into the decision of how much to pass along to customers/consumers. Companies impacted by tariffs last year had a number of options: absorb the levies; negotiate with suppliers; raise prices; or some combination of all of the above. They also had a choice whether to do it all at once or gradually over time. When tariffs were rolled back, those same businesses could then decide to revert to pre-tariff price levels – or not. Each of those individual decisions influences the aggregate reported inflation level and trend.

Similarly, inflation's impact on interest rates is seldom 1:1. Interest rates in shorter maturities are typically reflective of expectations for central bank policy (hold, cut, raise rates). This, in turn, can be influenced by unexpected strength or weakness (or a change in trend) in reported inflation numbers.

Inflation in the present tense

This week's stock and bond price volatility hints that investors are becoming more uncomfortable with recent inflation reports that, at least in the U.S., have shown upticks in price levels (Canada's inflation showed an unexpected softening in the rate of increase when the report was released on Tuesday). A variety of components are to blame, including higher global energy prices. The results are evident, especially at the producer level (chart). These are the business-to-business prices in the pipeline that may, or may not, eventually trickle down to consumers. Case in point: how to manage an increase in the cost of aluminum (from tariffs) and shipping (higher diesel) that a soft drink manufacturer pays for each can of soda.

U.S. Producer Price Index (PPI), YoY



Aside from energy, tariffs and rearranged supply-chain costs, the frenetic pace of the AI buildout are pressuring margins. Expenses are rising thanks to limited supplies of construction materials, skilled workers, energy infrastructure and semiconductor chips relative to nearly three-quarters of a trillion dollars in intended expenditure. Manufacturers of memory chips are increasingly diverting significant portions of their production toward data centers and away from the phones, tablets, PCs and thousands of other uses they normally serve.¹ This is parallel to the way chip manufacturers diverted production intended for auto companies toward PC and gamers during the pandemic. (Remember those empty auto lots but used car prices that were higher than prices for new cars?). **These imbalances may put pressure on prices and constrain activity in the short run, prompting investor heartburn. But we expect them to support disinflation over the long term as capacity is brought online, corporate processes are redesigned and the benefits of technological transformation take hold.**

WWKD? What will Kevin (Warsh, the new Fed chair) do?

Investors have become increasingly nervous about how the U.S. Federal Reserve, Bank of Canada and other central banks will respond to higher prices. Non-North American countries are likely to face greater challenges from the oil and derivatives disruptions, plus supply-chain problems tied to the closure of the Strait of Hormuz. Correspondingly, rate hikes are being actively discussed within the halls of many central banks. **While energy prices are one factor for Canada and the U.S., we maintain that bottlenecks in the growth story will ultimately be the bigger challenge.**

Running parallel to inflation concerns, fixed income investors are also increasingly wary of rising borrowing needs and leverage ratios of sovereign countries like the U.S., Japan and the U.K. During recent bond auctions there, bond vigilantes have demanded higher yields for holding longer-dated instruments.

In the U.S., new Fed Chair Kevin Warsh was confirmed this week but has yet to conduct his first FOMC meeting or press conference. **Investors will watch, listen and draw careful conclusions in the early days as he navigates an FOMC that has voiced increasing discontent over the notion of near-term rate cuts and a White House intent on pressuring the body into making significant cuts.** Former Chair Jerome Powell will remain an FOMC voting member, further complicating Wall Street's ability to read the tea leaves.

During the nomination process, Mr. Warsh outlined his beliefs: less forward guidance; a smaller Fed balance sheet; the procurement of revised data sets; and fewer board members commenting publicly. We are not sure the markets will take kindly to reduced information – especially if the various data inputs and decision methodology may be changing.

Implications for Investors

Markets could easily be buffeted in the short run by unexpected headlines or social media posts now that earnings season is almost complete, Congress is leaving town for the campaign trail, and the long (hopefully) sunny days of summer are drawing nigh. Investors will be closely observing the new Fed Chair for signs revealing how he will lead the new team while orchestrating and communicating interest rate policy. **Watchers have recently begun pricing in the potential for rate hikes even though the new Fed Chair will be under close scrutiny from a White House that wants rate cuts. We don't believe there will be a rate hike, but we do expect the central bank will remain static for an extended period** while the picture on inflation and the constructs of a new Chair become clearer.

We anticipate that investors will vacillate between fundamental optimism re AI and equities and fretfulness about the usual laundry list of concerns, including inflation that looks to be stuck higher for longer. We would not be surprised to see rates and volatility push higher in the short run and would not be extending duration (aka holding the bulk of fixed income holdings in instruments that have longer time to maturity). Equities – particularly small and mid-cap – have historically been a good hedge against inflation that was hotter than hoped, given their ability to move more nimbly by substituting inputs and streamlining processes.

In focus in North America

Jon Borchardt, Sr. Analyst

George Trapkov, CFA, VP and Portfolio Manager

This week

Consumer prices up less than expected in Canada – In April, Canadian consumer prices rose 0.4%, lifting the headline inflation rate to 2.8% from 2.4% the prior month. CPI excluding gasoline was up precisely 2.0% from a year ago, so any high-side miss in inflation can be tied exclusively to what's going on at the pumps. A small bit of good news: grocery prices receded a touch in April, trimming the annual rise to 3.8% from 4.4% and a recent high of 5.0%. In a similar vein, annual rent increases pulled back to 3.6% year over year from 4.2%, the slowest increase in more than four years, and more relief incoming. There is a risk that increasing energy prices could keep inflation high in the near term, but Canada's overall economic growth remains soft. *According to BMO Economics, a Bank of Canada rate hike is unwarranted.*

Canada's tepid housing situation remains – Canadian existing home sales nudged up 0.7% in April from the prior month in seasonally adjusted terms, but no one is going to mistake this for a sign of spring in the chilly housing market. Sales remain 4% below last year's anemic levels and about 10% below normal April levels. Now that new listings are edging up, the sales balance turned further against sellers and prices receded a bit further. Some additional softness in prices may be precisely what's needed to more fully return the Canadian housing market to normal affordability. Much of Ontario and B.C. are still seeing price declines, while much of the rest of the country is edging higher.

Green shoots in U.S. manufacturing – After more than two years in technical recession, the U.S. manufacturing sector has reemerged. ISM Manufacturing PMI composite readings were above 50 during the first four months of the year. The most recent ISM and Empire State Manufacturing reports showed continued strength in new orders, which has boosted utilization rates and improved sentiment within the sector. During Q1 earnings calls, trucking companies spoke of an improved outlook that was solid though not necessarily overtly robust. The theme of companies moving forward on smaller-scale projects while delaying plans for larger capital spending was repeated on numerous earnings calls. Rising costs have been a feature of recent manufacturing sector surveys, so an argument can be made that orders have picked up due to fears over inflation tied to the Middle East conflict and ahead of new tariffs from the Trump administration when inventories among manufacturers were considered "too low" by ISM. AI-related spending has provided support for the manufacturing sector. Within the trucking sector, flatbed freight has been a hotspot led by deliveries to new data-center sites. For now, greater certainty on trade and geopolitics is likely needed before today's green shoots evolve into a broad-based manufacturing recovery.

Next week

We'll see a sprinkling of important economic insights culminating in GDP reports in the U.S. (Thursday) and Canada (Friday). Expect the Fed's (at least the Powell Fed's) favorite inflation measure, the Personal Consumption Expenditures surveys, to be unveiled on Thursday.

Monday 5/25 – U.S. None scheduled, markets closed for Memorial Day | Canada – none scheduled

Tuesday 5/26 – U.S. Case-Shiller home price index, Consumer confidence | Canada Manufacturing sales

Wednesday 5/27 – U.S. None scheduled | Canada Wholesale sales

Thursday 5/28 – U.S. Initial jobless claims, Durable goods orders, New home sales, GDP, Personal income/spending, PCE | Canada BoC Financial statement report

Friday 5/29 – U.S. Retail inventories, and Trade balances | Canada GDP

Data scorecard as of May 20, 2026

Equity Market Total Returns						
	5/20/2026 Level	WTD	YTD	2025	2024	5-Year*
S&P 500	7,433	0.3%	9.1%	17.9%	25.0%	14.4%
NASDAQ	26,270	0.2%	13.3%	21.2%	29.6%	13.4%
DOW	50,009	1.0%	4.7%	14.9%	15.0%	11.6%
Russell 2500	4,919	0.9%	14.4%	11.9%	12.0%	7.3%
S&P/TSX	34,162	1.0%	8.6%	31.7%	21.7%	16.1%
MSCI EAFE	11,334	0.9%	6.9%	31.2%	3.8%	8.9%
MSCI EM	899	-1.8%	17.3%	33.6%	7.5%	4.2%
Bond Market Total Returns						
		WTD	YTD	2025	2024	5-Year*
Bloomberg U.S. Aggregate		0.2%	-0.5%	7.3%	1.3%	-0.4%
Bloomberg U.S. Treasury		0.2%	-0.8%	6.3%	0.6%	-1.0%
Bloomberg U.S. Corporate		0.2%	-0.4%	7.8%	2.1%	-0.1%
Bloomberg U.S. High Yield		0.1%	1.0%	8.6%	8.2%	4.5%
Bloomberg 1-10 Year Munis		-0.3%	-0.2%	5.1%	0.9%	1.2%
Bloomberg Canada Aggregate		0.8%	0.4%	2.4%	4.0%	-0.4%
Bloomberg Canada Treasury		0.7%	0.2%	1.4%	2.9%	-0.8%
Bloomberg Canada Corporate		0.6%	0.7%	4.4%	6.9%	1.5%
Government Bond Yields						
	5/20/2026	Last Month End	Last Quarter End	2025	2024	5-Year Average
U.S. 10-Year Treasury	4.59%	4.37%	4.32%	4.17%	4.57%	3.37%
Canada 10-Year Government	3.59%	3.54%	3.47%	3.43%	3.23%	2.81%
U.K. 10-Year Gilt	4.99%	5.01%	4.91%	4.48%	4.56%	3.16%
German 10-Year Bund	3.10%	3.04%	3.00%	2.85%	2.36%	1.66%
Japan 10-Year Government	2.77%	2.52%	2.35%	2.06%	1.09%	0.65%
Currencies & Real Assets						
	5/20/2026 Level	WTD	YTD	2025	2024	5-Year*
USD Index	99.09	-0.2%	0.8%	-9.4%	7.1%	1.8%
CAD:USD	\$0.73	0.0%	-0.2%	4.8%	-7.9%	-1.5%
Bitcoin	\$77,661.43	-1.8%	-11.4%	-6.5%	120.5%	24.8%
Gold	\$4,544.19	0.1%	5.2%	64.6%	27.2%	17.9%
Oil (WTI)	\$98.26	-6.8%	71.1%	-19.9%	0.1%	3.4%

*Annualized

5-Year data as of December 31, 2025. Benchmark data does not reflect actual investment performance but reflects benchmark results of the underlying indices referenced. You cannot invest directly in an index. Index definitions can be found at the end of this publication.

Index Definitions

Equity indices

S&P 500® Index is an index of large-cap U.S. equities. The index includes 500 leading companies and covers approximately 80% of available market capitalization.

NASDAQ Composite Index is a market-cap weighted index of the more than 3,000 common equities listed on the Nasdaq stock exchange.

Dow Jones Industrial Average (“DOW”) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange and the Nasdaq.

Russell 2000® Index (Russell 2000®) is an unmanaged index that measures the performance of the smallest 2000 U.S. companies in the Russell 3000® Index.

S&P/TSX Index is a capitalization-weighted equity index that tracks the performance of the largest companies listed on Canada’s primary stock exchange, the Toronto Stock Exchange (TSX).

MSCI EAFE Index (Developed Markets —Europe, Australasia, and Far East Index) is a standard unmanaged foreign securities index representing major non-U.S. stock markets, as monitored by Morgan Stanley Capital International. The index captures large and mid-cap representation across 21 developed markets countries around the world, excluding the U.S. and Canada.

MSCI Emerging Markets Index is a market capitalization weighted index representative of the market structure of the emerging markets countries in Europe, Latin America, Africa, Middle East and Asia. Prior to January 1, 2002, the returns of the MSCI Emerging Markets Index were presented before application of withholding taxes.

Fixed income indices

Bloomberg U.S. Aggregate Bond Index is an unmanaged index that covers the U.S. investment-grade fixed-rate bond market, including government and credit securities, agency mortgage pass-through securities, asset-backed securities and commercial mortgage-based securities.

Bloomberg U.S. Treasury Index is an unmanaged index that includes a broad range of U.S. Treasury obligations and is considered representative of U.S. Treasury bond performance overall.

Bloomberg U.S. Corporate Bond Index measures the investment grade, fixed-rate, taxable corporate bond market. It includes USD denominated securities publicly issued by U.S. and non-U.S. industrial, utility and financial issuers.

Bloomberg U.S. Corporate High Yield Index is an unmanaged index that covers the USD-denominated, non-investment-grade, fixed-rate, taxable corporate bond market. Securities are classified as high yield if the middle rating of Moody’s, Fitch and S&P is Ba1/BB+ or below.

Bloomberg 1-10 Year Blend Municipal Bond Index is a market value-weighted index which covers the short and intermediate components of the Bloomberg Capital Municipal Bond Index — an unmanaged, market value-weighted index which covers the U.S. investment-grade tax-exempt bond market.

Bloomberg Canada Aggregate Bond Index measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market. It includes treasuries, government-related, and corporate issuers.

Bloomberg Canada Aggregate Bond Index - Treasury is the treasury sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.

Bloomberg Canada Aggregate Bond Index - Corporate is the Corporate sub-component of the Bloomberg Canada Aggregate Bond Index, which measures the investment grade, Canadian dollar-denominated, fixed-rate, taxable bond market.



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¹ AI data center boom squeezes consumer tech’s chip supply - Fast Company