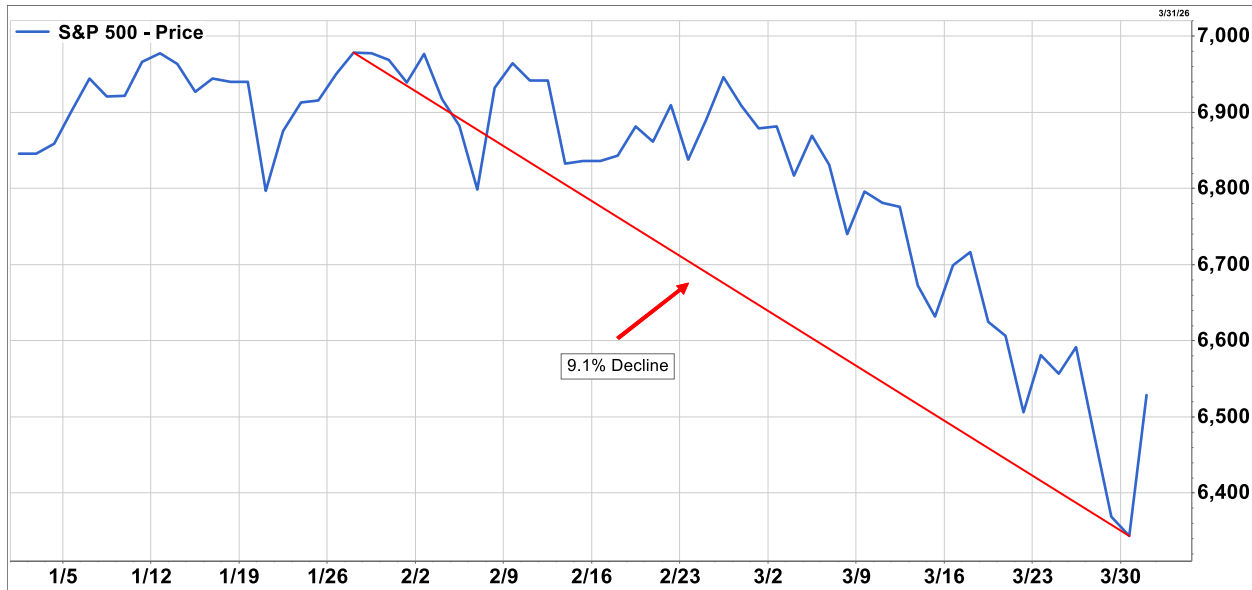


2026 Second Quarter
Investment Outlook

Equity Market Commentary

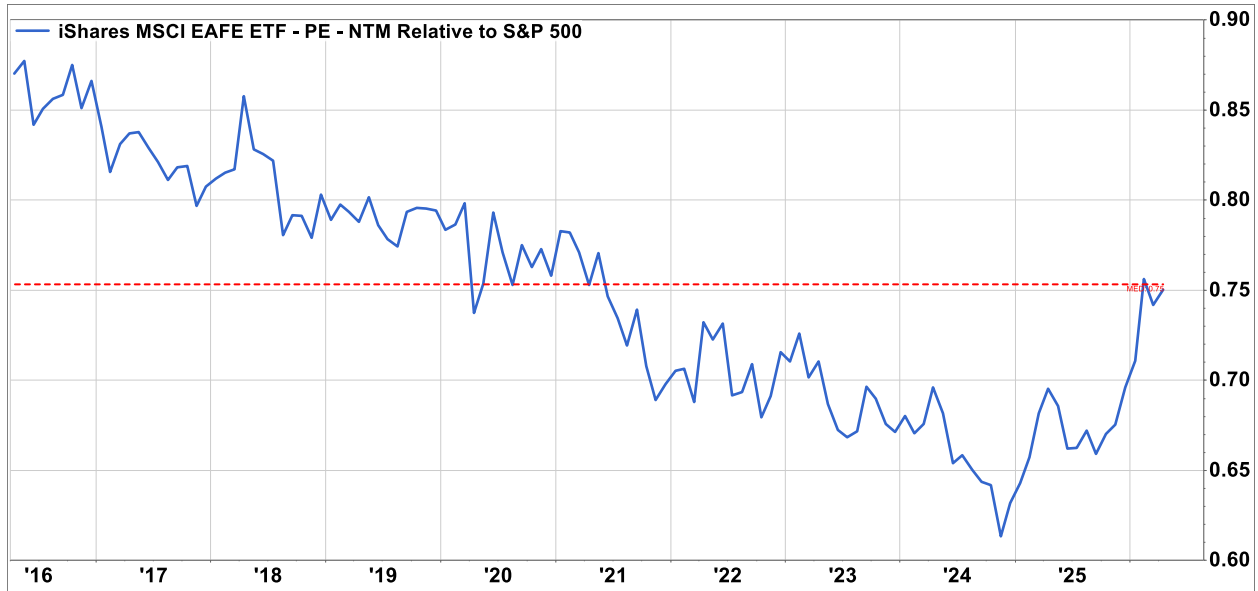
For the second year in a row, the S&P 500 posted a negative quarter to start off the new year. The Index declined by 4.33%, with the bulk of the losses occurring in March following the military strikes on Iran. Measuring from the January 27th peak, the S&P 500 narrowly avoided an “official” correction, with a 9.1% loss through the March 30th market low.



The more volatile and technology-heavy Nasdaq 100 Index did enter official correction territory with an almost 12% loss from its January high. In a continuation from the previous quarter, the Magnificent 7 Stocks (GOOGL, META, AMZN, TSLA, AAPL, MSFT, and NVDA) did not aid the Index’s performance. In fact, those stocks accounted for the majority of the losses. On a market-capitalization weighted basis, those seven stocks returned -11% and contributed 83% of the S&P 500’s quarterly loss. Not a single stock in the Magnificent 7 group outperformed the Index. Nvidia was the “best” performer with a loss of 6.5%, while Microsoft fell the most, with a 23.5% loss. The other 493 names in the S&P 500, on a market-cap weighted basis, only experienced a modest 1% decline. If the 500 names in the S&P 500 were equal-weighted, the market was essentially flat for the quarter with a 0.2% price-only gain. Just as the Magnificent 7 stocks contributed most of the market’s historic gains over the last three years, they are now accounting for almost all of the losses incurred during this market downturn.

Outside of the United States, equity market returns were slightly more encouraging. The MSCI EAFE Index, of developed economies, posted a 1% loss during the first quarter. Emerging market stocks fared the best, essentially breaking even for the quarter. This is a continuation of the trend experienced in 2025, when international stocks handily outperformed domestic equities. Despite their recent gains, international equities still exhibit attractive valuation levels relative to the S&P 500. The MSCI EAFE Index trades at a 25% discount to the S&P 500, which

is effectively back to its long-term median discount experienced over the last 10 years. Notably, emerging markets stocks have a 40% valuation discount relative to the S&P 500 and are still below the historical norm.



On the other hand, the S&P 500 has still not returned to a valuation level that would be considered consistent with its long-term average, despite its current decline. The S&P 500 trades at 19.5 times its forward earnings estimate, which is still about 20% higher than its long-term average of 16 times earnings.



While this is a substantial improvement from the 22 times earnings figure experienced at the end of last year, this valuation multiple is still one standard deviation above the 20-year average. When measured using sales, instead of earnings, the S&P 500 appears even more richly valued.

The Index trades at 3.0 times its forward sales estimate, a level that is essentially even with the peak experienced during the Dot-Com bubble at the beginning of the century.



As previously referenced, the S&P 500's current earnings-based valuation is nowhere near the peak levels of the Dot-Com bubble. This is an indication that companies are far more profitable today, compared to the early 2000's. Either way, this recent market sell-off has not returned large-cap equities to levels that represent an obvious buying opportunity yet.

Fixed Income Commentary

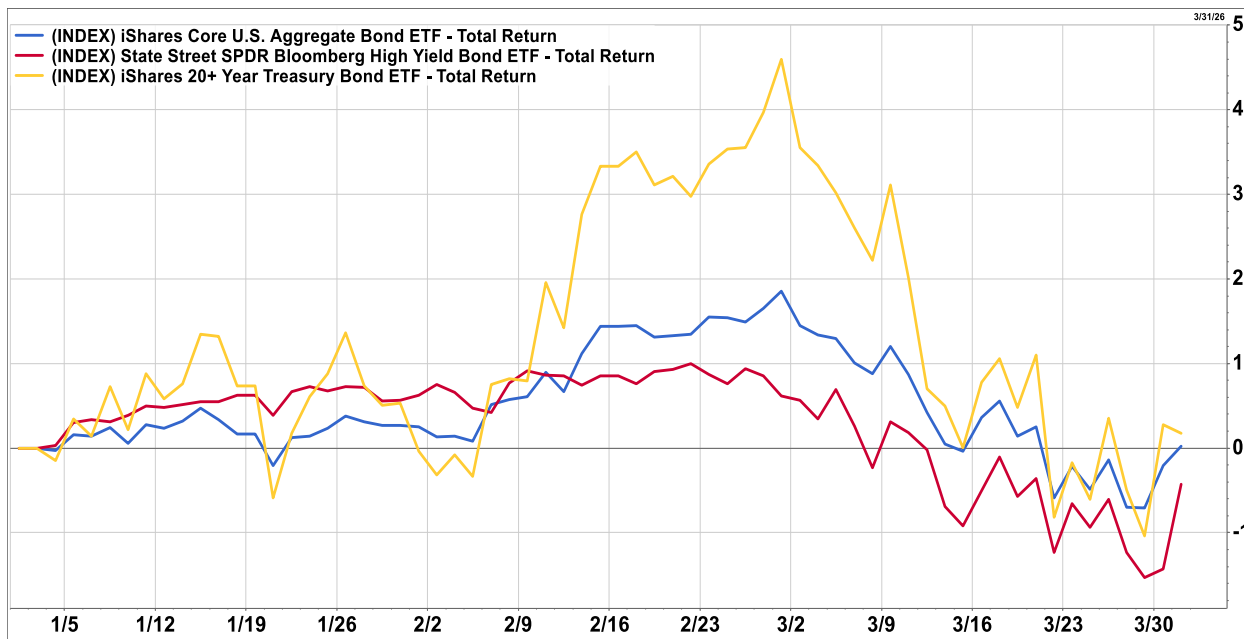
The bond market did not provide investors with much of a sense of stability to start the year. Yields moved quite violently as financial markets attempted to digest the war and the resulting economic implications. The two-year U.S. Treasury yield, which is very sensitive to monetary policy decisions, soared to 4.0% as the war progressed, before falling back to 3.8%. Prior to the war's outbreak, the two-year yield had settled into a narrow range of 3.4% to 3.6%.



Across the board, yields moved higher during the first quarter, but the most significant increases were undoubtedly at the shorter maturity points. The 10-year U.S. Treasury, which is influenced

by expectations for economic growth and inflation, increased by almost 0.2%. In this case, the increase was likely associated with increased inflation estimates as oil prices rose.

While it was a volatile quarter, bonds ended the month of March relatively flat when measured on a total return basis. Long-term Treasuries and core bonds were barely positive, and the riskier high yield bonds generated a modest loss. High yield bonds have a positive correlation with stocks, so it is not surprising to see that they were the lower returning fixed income segment during the quarter. Bonds were on track to deliver solid performance, but the spike in yields following the strikes on Iran quickly reversed that trend.

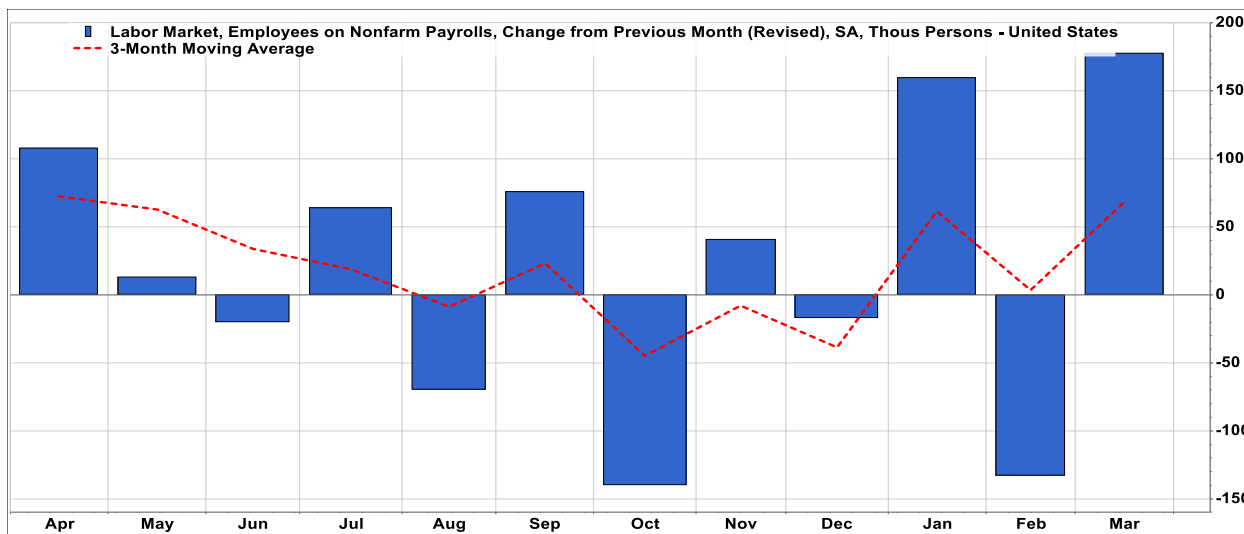


Credit Concerns

High yield bonds also felt some of the jitters that were present in private credit markets. In some respects, high yield bonds and private credit markets are similar. Both represent lending to companies that are deemed less credit worthy and riskier relative to investment-grade bonds. Estimates vary, but most data suggests that the private credit market is slightly larger than the high yield market in the United States, with each market representing about \$1.5-\$1.8 trillion in assets. One of the primary differences between the two markets is that high yield bonds are generally liquid investments while private credit offers little or no liquidity, depending on the particular investment vehicle. In private credit interval funds, where there is a degree of liquidity, investors submitted redemption requests during the first quarter that far exceeded the liquidity provisions of the funds. Some of the largest fund providers, like Blue Owl Capital and Cliffwater, saw redemption requests that represented between 15-20% of the funds' asset value. Ultimately, many redemption requests were not fulfilled, at least not to the degree that investors expected. It is a timely reminder that even though these funds offer relatively high returns, liquidity reigns supreme during periods of market turmoil.

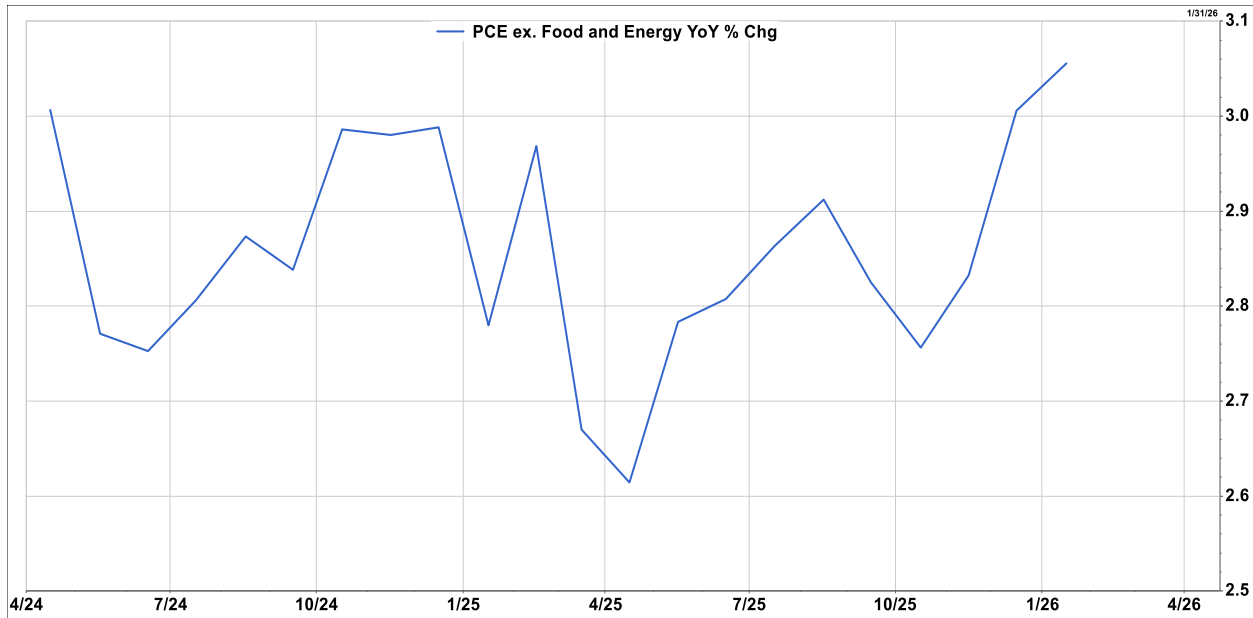
Economic Review

The U.S. economy experienced job growth during the first quarter, after ending last year with a negative three-month moving average on nonfarm payroll growth. Both January and March saw additions in excess of 150,000 jobs. On the other hand, the labor market experienced a decline of 133,000 payrolls in February. In previous *Outlooks*, we have issued caution when viewing monthly payrolls figures. They are volatile and subject to large revisions; and even the revised figures have often been determined to be somewhat inaccurate. It’s encouraging to see a pickup in the labor market compared with the tepid results in the second half of 2025, but these figures need to be viewed with a healthy degree of skepticism.



The unemployment rate has continued to hover between 4.3% and 4.4%. Even though this represents a 1% increase from the cycle low experienced in April of 2023, the unemployment rate still remains low on a historical basis. Most economists would argue that a 4.3% unemployment rate represents full employment for the U.S. economy. Initial jobless claims, a reliable leading economic indicator, remained low during the quarter and have been trending downward over the last six months. Continuing unemployment insurance claims, an indication of how long it takes to find a new job, had been rising over the last several years. These have now materially decreased over the past few months. This provides a glimmer of hope that the labor market may be exiting the “low hire, low fire” condition that has existed over the past few years.

To balance out some of the improving labor market data, inflation is giving mixed signals. The Core Consumer Price Index (CPI) has continued to decline despite the slight uptick following the imposition of tariffs in April of 2025. Core CPI, which excludes the more volatile food and energy components, rose 2.5% in February on a year-over-year basis. While the decline here is welcomed, it is important to remember that the Federal Reserve uses the Core Personal Consumption Expenditures (PCE) Index as their benchmark for measuring inflation. CPI only includes urban prices in its calculation and has a disproportionately large weighting to housing costs. The PCE data series addresses both of these shortcomings of CPI.



Core PCE has been moving higher over recent months and continues to trend further away from the Federal Reserve’s 2% inflation target. Even though the “core” measure excludes energy prices, the war in Iran will certainly put upward pressure on inflation. Energy prices will act as a second order effect on core inflation. It will not directly increase core PCE, but it will act to increase the prices of the underlying components of the index. Higher energy prices will increase transportation and production costs, which will ultimately increase the price of consumer goods and thus increase core inflation readings.

As the labor market and economic growth remain resilient in the face of stubborn inflation, market participants have made clear that they do not expect any further monetary easing in 2026. Entering the year, the consensus estimate was that the Federal Reserve would lower their policy rate, with two 0.25% rate reductions. As if the Fed’s current position wasn’t challenging enough with regards to inflation, they will now have to contend with the inflationary impact of the war.

Tariffs Become More Complicated

In a major blow to the Trump Administration, the U.S. Supreme Court ruled that the tariffs enacted under the International Emergency Economic Powers Act (IEEPA) were unlawful. The decision was founded on the principal that the President can “regulate” international trade during periods of economic emergency. The term “regulate” does not, however, include the ability to impose taxes, and the court deemed tariffs to be a clear form of taxation. It is important to note that the court’s decision did not impact all tariffs that have currently been levied. The court found that only the tariffs on Mexico, Canada, and China in relation to drug-trafficking and immigration, and the reciprocal tariffs on trading partners were illegal. Following the repeal of the IEEPA tariffs, the average tariff rate imposed on imports fell from almost 16% to 12%.



President Trump and his economic advisors had developed a contingency plan in the event that the tariffs were deemed unlawful. Immediately following the Supreme Court’s decision, the President enacted tariffs that were allowable under Section 122 of the Trade Act of 1974. Section 122 allows the President to enact *short-term* tariffs in an attempt to mitigate large balance-of-payment (BOP) account deficits. Essentially, these tariffs are meant to deter imports if the United States has a serious trade imbalance. These Section 122 tariffs may be imposed for up to 150 days and at a maximum rate of 15%. Given that the IEEPA tariffs were deemed illegal, the Section 122 tariffs are serving as a temporary solution while the Trump administration pursues other options to influence trade. In the more than 50 years that Section 122 tariffs were available for use, they had never been invoked until now.

From a longer-term perspective, there are several tariff-related avenues that President Trump will be pursuing. While more difficult to enact, Section 232 tariffs from the Trade Expansion Act of 1962 will likely be used in an increasing manner. These tariffs are placed on goods that pose a national security risk and are meant to encourage domestic production of critical goods. Currently, the United States has placed Section 232 tariffs on a variety of goods from other countries. Notably, steel, aluminum, and copper products are subject to a 50% tariff rate. The difficult nature of levying Section 232 tariffs is that they are imposed on an individual product basis, as opposed to broad tariffs on imports from a particular trading partner. There is an added difficulty in proving that a particular good actually poses a true national security threat. It’s fairly easy to conclude that the term “national security” may be used somewhat loosely when justifying these tariffs in the future.

Another option, which the Trump administration previously enacted during the 2016 presidential term, is Section 301 tariffs. As is the case with the current short-term Section 122 tariffs, Section 301 tariffs also stem from the Trade Act of 1974. These tariffs are meant as punitive measures towards countries who have unfair trading practices. Unfair trading practices are generally

defined as unreasonable, discriminatory, or those practices that burden U.S. trade. An investigation will be launched into a country's trading policies to determine whether a Section 301 tariff is truly justifiable. The term "unfair" trading practice is broad, but historically, Section 301 investigations have targeted issues such as forced labor, unfair subsidies, and intellectual property theft. Section 301 tariffs were placed on China in 2018 following an investigation surrounding China's forced transfer of technologies and intellectual property theft. As with Section 232, there is a far higher threshold for enacting Section 301 tariffs compared to the current short-term tariffs and the repealed IEEPA tariffs. Ultimately, following the February Supreme Court ruling, tariffs will not be going away anytime soon, but the path forward for President Trump's trade policy is unarguably more difficult.

War in Iran & Oil

A little more than eight months after the United States struck Iranian nuclear facilities, the U.S. and Israel launched targeted attacks on Iran. Within hours of the initial attacks, Ayatollah Ali Khamenei, who was in power for almost 37 years, was killed. The conflict continues, with no concrete timeline relating to the end of our military operations, although an additional three-to-four-week timeline has been frequently suggested.

Besides the obvious turmoil and devastation caused by the United States being involved in a war, the most significant shock has been within the energy markets. Iran and the broader Middle East region account for a significant portion of global oil and natural gas production. Following the initial strikes, Brent crude oil rose from \$70 per barrel to a high of \$122 per barrel, an increase of 74%. This was the highest price that the benchmark has reached in almost four years.



Despite the 4.3% quarterly decline in the S&P 500 Index, the stocks in the energy sector of the S&P rose by almost 38% over the same time period.

Oil and energy commodity shocks are not anything that are new for the United States. There have been several in our history, some which have been accompanied by broader economic declines, and many which were brief and without lasting consequences.

The problem with the current conflict is that one of the world’s most important energy shipping passages, the Strait of Hormuz, is squarely within the war zone. To put numbers to this, approximately 20 million barrels of oil pass through the Strait of Hormuz each day. This is approximately 20% of the world’s crude oil consumption and 25% of the world’s seaborne oil trade!

Location	2025 H1 volume (mb/d)	% of World Maritime Oil Trade
Strait of Malacca	23.2	29.1%
Strait of Hormuz	20.9	26.2%
Cape of Good Hope	9.1	11.4%
Danish Straits	4.9	6.1%
Suez Canal & SUMED Pipeline	4.9	6.1%
Bab el-Mandeb	4.2	5.3%
Turkish Straits (Dardanelles)	3.7	4.6%
Panama Canal	2.3	2.9%

Similarly, about 20% of the global supply of liquified natural gas (LNG) is shipped through the strait, primarily from Qatar and the United Arab Emirates (UAE). While the Strait of Malacca sees more of the world’s oil volume, when oil and LNG are combined, the Strait of Hormuz is the most important energy chokepoint on the globe.

The headlines, understandably, tend to focus on the increase in the price of retail gasoline. From the start of the war, the average price of a gallon of gas has increased by one dollar, which represents about a 33% increase in the last month. About half of the price of a gallon of gas is derived from the price of a barrel of crude oil. The other 50% is related to refining costs, transportation, and taxes.

The reality of the current situation is that oil price spikes tend to cause a wide degree of demand destruction throughout the economy. The old rule-of-thumb is that a \$10 increase in the price of oil tends to reduce Gross Domestic Product (GDP) by 0.1% to 0.3%. Likewise, a \$10 increase in oil also increases headline inflation by about 0.2%. An increase in prices and a decline in growth brings about one of the most sinister economic conditions possible, stagflation. Besides the obvious strain that stagflation places on consumers, it is a condition that is particularly impervious to monetary policy actions. While the U.S. economy is nowhere near stagflation at the moment, an oil price shock certainly increases the likelihood of entering into a slower growth, higher inflation environment. The U.S. does possess one advantage in the current situation relative to other industrialized countries, in that it is a net energy exporter, and it has been since 2019. Simply put, the United States still imports crude oil and other energy products, but overall, exports more than it imports. This provides a small degree of insulation from energy price shocks compared to other countries that are heavy energy importers. While the United States has a degree of energy independence, there is no country in the world that has *price* independence from the cost of oil and gas.

Conclusion

At the risk of making a painfully obvious statement, the near-term direction of the economy and financial markets is highly dependent on the length of the ongoing war in Iran. While the U.S. economy still appears to be on solid footing, the recession odds rise with the length of time that energy-related commodity prices remain elevated. High energy prices will eventually erode demand and consumption, as rising prices infiltrate the global economy. Consumers at the lower end of the income spectrum, who are already feeling their budgets strained, will struggle to bear the additional costs associated with oil and gasoline prices. Although estimates vary widely, if oil prices remain around \$100 per barrel, analysts model out that this will cost American households about \$1,000 more per year, relative to where oil prices were prior to the start of the war. It does not take a stretch of the imagination to game out a scenario where this situation ends with a recession. To be clear, a recession is not the base case expectation for most analysts and market participants at the present time. If the fighting ceases and energy transportation resumes, this oil spike and market turmoil could very well end up as a fleeting memory.

We would be remiss not to remind readers that equity market volatility and corrections are indeed normal occurrences within a typical market cycle. Since 1980, there were only three years where the S&P 500 did not experience at least a 5% decline. In slightly less than half of the years during that same period, the S&P 500 experienced a decline of 10% or more. Even though about half of the years experienced a correction, the average S&P 500 calendar year return was a positive 13.3%. The vast majority of past market corrections did not foretell a coming recession, or a true bear market. We need only look back to 2025 for a reminder of this. The S&P 500 fell 19% from its high and then rallied almost 40% to end the year. Despite the rightful angst that this war is causing, the American economy and financial markets have weathered similar situations in the past. Ultimately, it is not wars, political discourse, or news headlines that determine long-term financial success or failure. That power continues to reside with corporate profitability and innovation, and we have no reason to believe that this time will be different.