

April 3, 2026

Economic Outlook:

The first quarter of 2026 is in the books. The S&P 500, which started higher in January, slumped in February and March and finished down 4.6% for the quarter. The quarter is typically a positive one for equities, as the average gain for the period has been 2.0% since 1980. Stocks historically have risen in 1Q about two-thirds (64%) of the time. But just because the first quarter was negative, it doesn't mean the full year will follow. Going back to 1980, there have been 16 negative first quarters, but in more than half of those years, stocks finished with positive annual returns. The average gain for those recovery years was 14.7%.

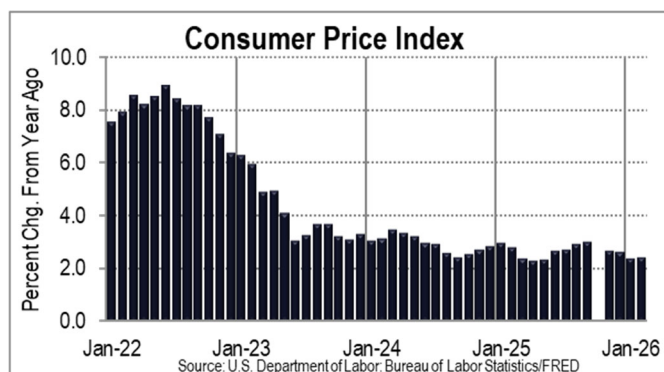
April historically is the second-best month of the year. The average gain for the S&P 500 in the month since 1980 is 1.5%. Last year in April, stocks slumped 2.2%, before the bull market returned in May. April is a busy month on Wall Street, as companies report first-quarter results. This year, 1Q earnings are expected to grow at a mid-teens rate, driven by the performance of the IT sector. The direction of interest rates also will be an important topic, as the markets process the latest oil prices and prepare for the Fed's next meeting. The wild card will be the status of the war in Iran.

As I write this letter the situation in Iran is very fluid. We are receiving very different messages from the White House and Iran and it remains uncertain if we were even negotiating with the parties in control. This will continue to be a developing story, but it does appear clear that the longer the conflict remains active, the more damage that will be done to the global economy. That doesn't necessarily mean the American economy, however.

Employment: The latest available data as of this writing is the March jobs report released on April 3rd. That report showed jobs grew by +178,000 with an unemployment rate of 4.3% (-0.1% lower than previous reports). Labor force participation and employment to population ratios remained little changed at 61.9% and 59.2% respectively. Hourly earnings increased \$0.09 to \$37.38 per hour, an increase of 3.5% over the past 12 months. The prior two months' job creation numbers were revised down by -7,000 jobs for January and February combined.



Inflation: The latest inflation figures came in lower than expected but still above the Fed's 2% target. According to last month's Bureau of Labor Statistics' (BLS) Consumer Price Index (CPI) report, prices increased 0.3% in February for "All items" and 0.2% for "Core" which strips out food and energy costs. Year-over-year prices increased 2.4% and 2.5% respectively. Unfortunately, this data was collected before major operations in Iran drove oil prices from \$60-65/barrel to over \$100/barrel for much of March. We fully expect to see prices move higher in the coming months as higher fuel prices flow into the economy. Again, the duration of the Iranian conflict will determine the level and severity of the price increases.



GDP: The second estimate of Q4 2025 GDP was released on March 13, 2026. Fourth quarter annualized GDP (Q4 2025) was reported as just +0.7%. This was a revision down from 1.4% in the initial estimate. The extended government shutdown in Q4 impacted consumer spending more than initially expected, causing the downward revision.

Equity Market Review and Outlook:

The first quarter of 2026 featured a tumultuous stock market landscape, characterized by a rotation away from 2025's mega-cap tech winners. While the S&P 500 faced volatility and a significant dip in March—due to rising geopolitical tensions in the Middle East and renewed inflation fears—it largely hung onto earlier gains driven by solid earnings. The quarter was marked by a "value rotation," where value stocks (+1.3%) outperformed growth stocks (-8.4%), and small-cap stocks showed significant strength.

Large Cap Tech stocks faced pressure as investors questioned AI capital expenditures and scrutinized software as service (SaaS) models, leading to a 23% decline in US software stocks through February. Ultimately, the broader market was challenged with balancing strong earnings with deteriorating geopolitical issues.

Interest rate expectations also played a role, with the Fed maintaining a cautious easing bias. The prospect of continued, albeit slower, rate cuts and a stable labor market sustained market optimism, preventing a deeper correction. Looking forward, the market remains focused the conflict with Iran and the potential for wider sectoral gains beyond tech leaders if the conflict can be resolved quickly. We continue to believe the certainty of a defined tax code, trade deal progress, and lower interest rates, could fuel stocks through 2026.

Fixed Income Market Review and Outlook:

Over the last two years the Fed has cut overnight rates from 5.25-5.5% to 3.5-3.75%. The Fed should be acknowledged for dramatically reducing inflation without creating a recession. This is the definition of a "soft landing" and one of the only instances that the Fed can claim the successful execution of a "soft landing".

Fed chair Powell now states rates are "on the high side of neutral". We would agree with this assessment, though events in the middle east now put that assessment in jeopardy. The closing of the Strait of Hormuz has spiked oil prices from \$65/barrel in late February to >\$110/barrel at the time of this writing. It is no secret that elevated oil prices flow into the prices of virtually every good and service. The longer the conflict drags on, the more inflationary pressure is transferred into the economy.

The current bias is still toward lower Fed Funds interest rates, but US Treasury yields have already reacted with yields higher by nearly 0.5% across much of the maturity scale. We don't anticipate much Fed action in 2026, but the next move could very well be higher rates if the Iran conflict drags out longer than promised.

Conclusion

The foundation of the economy remains strong, but the rise in oil prices related to the Iranian conflict currently dominate the market outlook. When a resolution is reached, the market will react instantly to the upside. We have made portfolio adjustments but caution against dramatic changes in asset allocation during volatile market periods.

Thank you for your continued confidence,



Warren M. Hurt
Senior Vice President/Chief Investment Officer

Stock Market Returns - Year to Date thru April 2, 2026

