

## Q1 2026 Commentary

In the first two months of the new year, financial markets gave investors good returns, building upon the gains seen in 2025, but volatility followed in the latter part of the first quarter. This volatility resulted from the US/Israeli attacks on Iran and subsequent escalation in hostilities in the wider Middle East as Iran responded with attacks that included some on their neighbouring countries.

With Iran controlling and closing the Straits of Hormuz, deep concerns resulted from the supply of oil. Before the US strikes on Iran, approximately 20% of the world's oil and liquified natural gas from the Gulf would pass through the Straits. The price of oil rose sharply at the start of the conflict but has recently retreated on news of a two-week ceasefire.

The extension to the temporary pause in hostilities is very welcome, and, above all, the respite it offers people in a region that has endured prolonged conflict. Any break in fighting brings much-needed relief to local communities, allows humanitarian assistance to flow more freely, and creates at least the possibility of further de-escalation. It is important, however, to stress that the ceasefire remains fragile. There have already been reports of strikes on Lebanon and retaliatory attacks by Hezbollah on Israel, underlining how quickly tensions can resurface. These incidents highlight the limited trust between the parties and the narrow margins for error on both sides.

The broader political picture also remains challenging. The opposing sides are still far apart in their negotiating positions, and there is little evidence so far of meaningful progress towards a more durable settlement. In that context, it is too early to conclude that the ceasefire will hold or that the underlying risks to regional stability have materially diminished. From an economic and market perspective, the key relief will come from energy-related transport routes opening and returning to pre-war levels, and that still appears to be a hope at this stage. Nevertheless, we hope that the ceasefire proves durable and can serve as a foundation for further diplomatic engagement.

We believe the most likely scenario outcome will be that the Strait of Hormuz remains open for limited transit, but repeated interference disrupts shipping for several weeks, reducing traffic and raising costs. This results in a modest supply loss that can be largely offset through storage drawdowns and alternative transport channels.

The failure to reach agreement over the first weekend of discussions was not unexpected although undoubtedly there is a global desire to reach some form of compromise as soon as possible, and until then we anticipate markets will remain volatile; the recent change in leadership in Hungary is, however, a positive change for European cohesion.

In further news, at the end of February, the US Supreme Court ruled that the new tariff regime put in place by President Trump's government is illegal. The US administration will likely consider using other legal authority to impose tariffs. Trump's new 15% global tariff is allowed under a 1974 act designed to address trade deficits and has to be agreed by Congress after 150 days.

The US economy expanded at an annualized rate of 0.5% in the fourth quarter of 2025, below the earlier estimates, due to the government shutdown which cut spending and saw consumer demand weaken. The unemployment rate remains fairly steady at 4.3%, but the number of new and lost jobs has seen some swings in the past few months.

Government bond yields and borrowing rates have risen since the start of the Middle East conflict as inflation is now expected to increase. Expectations for interest rate cuts over the year have now moderated.

Further commitments have been announced by tech companies for AI-driven capital expenditure (principally building data storage facilities) and could exceed \$750bn, up from \$425bn last year. There is, however, little evidence yet that these investments will boost both productivity and corporate earnings sufficiently to justify those company valuations.

Diversification, including asset allocation towards global equities and different styles (growth and value), should, we believe, increase the chance of earning resilient portfolio returns.

Although there are many uncertainties, especially concerning resolution to the Russian invasion of Ukraine, the situation in the Middle East, the ongoing concerns about the effect of trade tariffs, and the US government's recent involvement in Venezuela, risk assets offer attractive opportunities for the longer-term investor, as do certain fixed income assets which provide useful diversification to investor portfolios particularly at times of volatility.

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