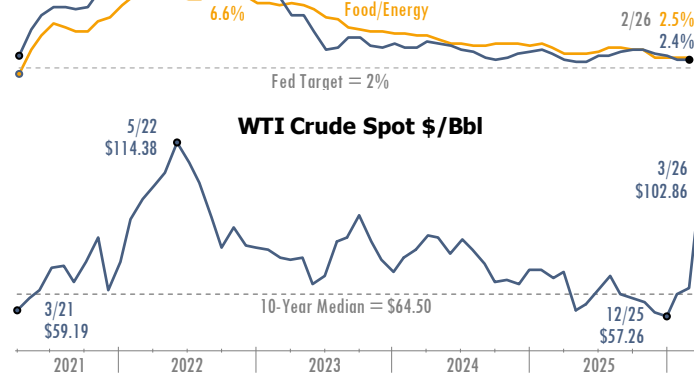


# MARKET Recap

## The US Economy: “The Price of War”

The US economy slowed more sharply than expected in Q4 due to the protracted US government shutdown, the longest on record. Decelerations in government and consumer spending, and exports of services drove the decline in growth. Net exports remained sluggish for Q1 so far, and residential investment has turned negative on stubbornly high long-term interest rates (keeping mortgage rates elevated).

Prior to the outbreak of war between the US/Israel and Iran, there was already considerable uncertainty regarding the timing of the Federal Reserve’s next interest rate cut. By the March Open Markets Committee meeting, it was clear that this easing cycle would at the least be slowed in anticipation of war-related inflation. At the March 18<sup>th</sup> meeting the Fed held rates steady and released updated economic projections showing slightly higher consumer price inflation for the next 2 years, and a slightly higher long-run Fed Funds rate.



Since then, the price of oil has continued to climb, topping \$100/barrel for West Texas Intermediate at quarter-end. This is nearly the same level reached following Russia’s invasion of Ukraine. Although oil prices quickly recovered after that event and were not the primary driver of the 2022 inflation spike, crude prices did buoy headline inflation and slowed the impact of the Fed’s rate hikes.

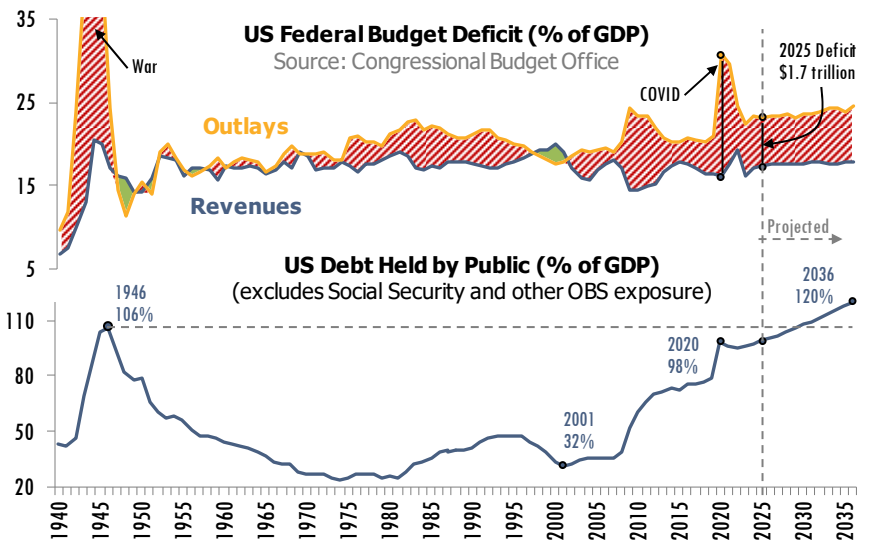
To say that war is unpredictable would be a huge understatement. We have no idea how soon or how quickly oil prices will decline. The more important question is, what will they decline to? It is hard to imagine any post-conflict scenario where Iran does not try to monetize their control over the

Strait of Hormuz; their economy was already in shambles prior to the war, and they face hefty reconstruction costs. If prices settle down to only modestly elevated levels for the next few years, that would be a big win.

Of greater long-term concern is the impact of this conflict on the US fiscal situation. Tax cuts and spending increases post-COVID remain ingrained. However, the CBO’s deficit projections do not account for a proposed increase in defense spending to \$1.5 trillion due to the war. The budget also relies heavily on \$4.4 trillion in customs duties through 2036, which seems dubious given recent court rulings and the creative ability of market participants to maneuver around them.

Finally, Congress has become adept at time-shifting revenues and expenses to clean up the 10-year budget window. One example is the SECURE 2.0 Act requirement that older, highly compensated 401(k) participants make their catch-up contributions using Roth treatment.

War, and its aftermath, is one more inflationary headwind that the economy must struggle against. Fiscal restraint in line with the post-war 1950’s environment seems like the only reasonable, and least likely, policy course forward.



## The US Bond Market

Outbreak of the US/Israel war with Iran erased expectation for rate cuts later this year. Intermediate Treasury yields rose roughly 25 basis points during the first quarter. Overnight and long-term yields were little changed. Fed Chair Powell espoused a “wait and see” response regarding the impact of commodities supply shocks on economic growth and inflation.

Investor sentiment over the AI boom continued to swell into the new year before peaking at the end of January. Credit spreads contracted moderately from already low levels. Then spreads reversed into a gradual widening as the market focus shifted to assess the impairment and disruption a new AI era may level.

Corporate bond issuance surged during the quarter and is on track to outpace all previous years. Data center hyper-scalers feature prominently among issuers. Yet, even excluding a projected \$175 billion in hyper-scaler issuance, investment grade debt raising is set to top \$2 trillion this year. Broader activity was driven by companies looking to refinance existing debt profiles or build war chests for mergers and acquisitions, which have been on the rise but may be derailed by war in Iran.

US Bond Index Returns	
Bloomberg Idx	1Q26
Aggregate	-0.05%
Short Gov't	0.56%
Interm. Gov't	0.05%
Long Gov't	-0.40%
TIPS	0.26%
Municipal	-0.18%
Interm. Credit	-0.17%
Long Credit	-1.16%
High Yield	-0.50%
Leveraged Loan	-0.56%
MBS	0.40%

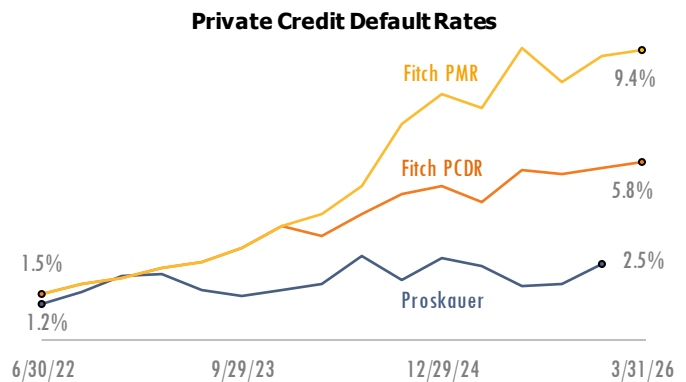
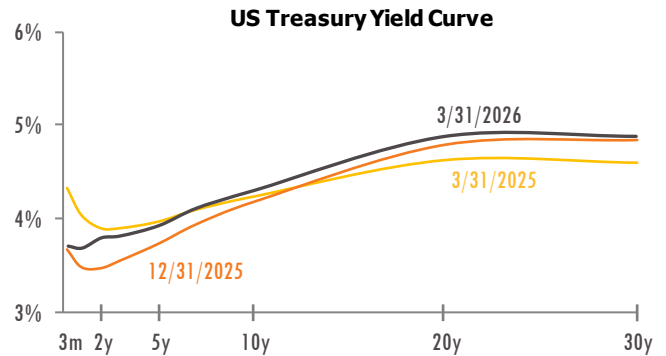
Bond sector returns were muted with long duration credit lagging and short-term high-quality debt eking out gains. Following the pandemic, bonds have often failed to fulfill their once-reliable role of ballast in a balanced portfolio. During zero-interest rate policy, yields had little room to go lower. So, when Russia invaded Ukraine in early 2022, short-term Treasury yields did not change. The 5-year key rate led the way 30 bps lower, but within 2 weeks yields broke out on inflation fears – grinding higher for months thereafter. At the February 28th onset to Operation Epic Fury, the 10-year Treasury commanded a 3.96% yield. Within the first week of fighting, it climbed 30 bps. By March 20 it had risen 43 bps in total, adding to investor losses.

Continuing from last quarter’s discussion of private credit and the rise of “Bad PIKs,” investor outflows are adding pressure to some private credit funds. In February, Blue Owl liquidated \$1.4 billion of its loans across three of its private credit funds at an average 99.7% of par value. While such a small discount from par could signal strong fundamentals, skeptical investors point out that the secondary sale may have included only the best performing loans.

In addition to rising Bad PIKs, borrowers are deferring maturities rather than refinancing as usual, a practice referred to as “amend and extend.” This combination allows borrowers to completely defer cash payments while their outstanding loan inflates. These patches can only conceal the eventual toll of poor underwriting standards and weak covenants. Data from Proskauer and Fitch illustrates the potential divergence in default rates for portfolios plagued with patches.

Fitch’s Private Credit Default Rate (PCDR) is a composite index of Privately Monitored Ratings (PMR) and Model-based Credit Opinions (MCO). PMR tracks unrated, lower middle-market loans and MCO uses point-in-time models to assess broader private debt. In contrast, Proskauer tracks a senior direct lending universe and focuses on point-in-time active payment defaults. Unlike Proskauer, Fitch counts maturity extensions and payment-in-kind (PIK) toggles as distressed debt exchanges. In addition, part of the divergence is due to higher default rates of smaller (< \$25mn EBITDA) companies captured in PMR. Fitch cites a default rate of 15.8% for this cohort vs. 4% for those above \$100mn EBITDA. Fitch also notes low loss rates for senior loans.

While public BDCs and term funds are insulated from investor cash redemptions, non-traded perpetual BDCs typically must satisfy up to 5% in redemptions per quarter. With enough sustained redemptions, they are forced to prematurely sell assets. In a healthy market, this exposes gaps between book and market values. In a panicked market, secondary buyers for assets can demand exorbitant discounts. Perpetual BDCs have been successful fund raisers, but perhaps more for fast money than good money. Emerging in 2021, they have grown in excess of \$200 billion in AUM. The confluence of PIK-inflated marks, deferred refinancing, and redemption-driven forced selling amplifies what is seen as the greatest risk in private credit today (which otherwise may not have threatened conservative and diversified portfolios): “asset-light” loan exposure.



# The US Stock Market

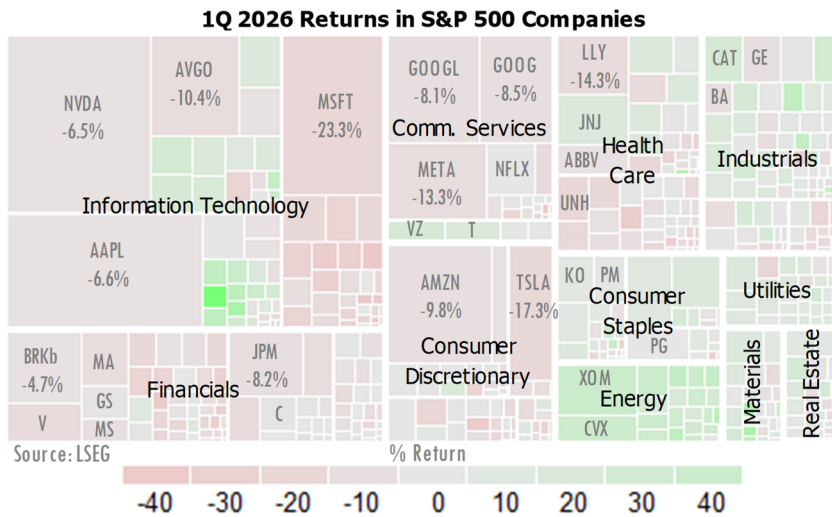
Along with a war and a record surge in oil prices, US markets battled uncertainty from heightened inflation fears, a Supreme Court ruling against President Trump’s tariffs, and broadening AI disruption. Market volatility climbed at the commencement of combat operations, pushing the VIX past 20 and underscoring growing investor angst. By the end of March, the Nasdaq and the Dow had fallen into correction territory. The S&P 500 had its worst quarter in nearly four years.

Value outperformed growth across all market caps, although the gap narrowed over the quarter. Ultimately, the Russell 3000 Value Index bested its growth counterpart by over 11% for Q1, its largest margin of outperformance since the dot-com bubble burst. Although they comprise just 4% of the S&P 500, the run-up in energy stocks helped boost value. Underperformance in tech, representing about one-third of the S&P 500, dragged down growth. The Fed pausing rate cuts was another headwind for growth names, which are more attractive in a falling rate environment when the present value of their future earnings increases.

Sector	1Q26	Sector	1Q26
Energy	38.25%	Health Care	-4.88%
Materials	9.73%	Comm Services	-6.94%
Utilities	8.26%	Info Tech	-9.13%
Consumer Stpls	7.68%	Consumer Discr	-9.19%
Industrials	4.61%	Financials	-9.35%
Real Estate	2.76%		

Category	1Q26	Category	1Q26
<b>Largecaps</b>		<b>Midcaps</b>	
S&P 500	-4.33%	S&P Midcap 400	2.50%
Russell 1000	-4.18%	Russell Midcap	1.29%
Growth	-9.78%	Growth	-6.35%
Value	2.10%	Value	3.68%
<b>Broad Markets</b>		<b>Smallcaps</b>	
S&P 1500	-3.81%	S&P Smallcap 600	3.51%
Russell 3000	-3.96%	Russell 2000	0.89%
Growth	-9.54%	Growth	-2.81%
Value	2.23%	Value	4.96%

Mag 7 returns were negative across the board, ranging from -6.5% for NVIDIA to -23.3% for Microsoft. Investor sensitivity to stretched valuations increased as did skepticism around the ultimate profitability of out-sized AI investments. Q1 also saw a rout in software-as-a-service companies on fears that AI will reduce the demand for traditional seats and licenses, negatively impacting subscription models.



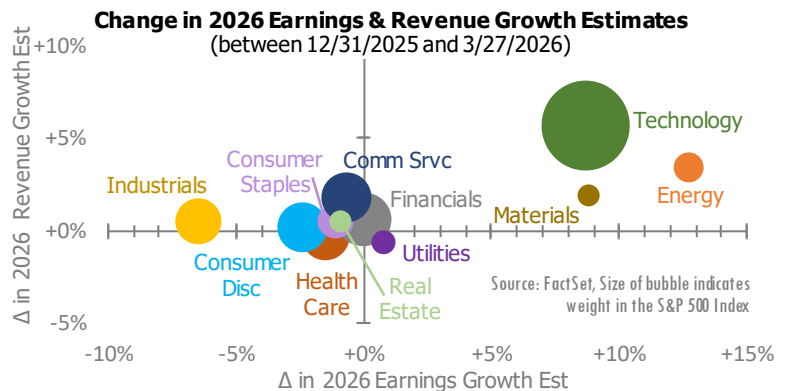
Financials were the quarter’s worst performer. All parts of the sector were beset by macroeconomic and industry-specific events. Troubles ranged from rising consumer loan defaults in banking, to a liquidity crisis amid soaring redemption requests in private credit, to retail trading volumes dampened by market volatility in fintech.

With oil closing the quarter over \$100/barrel, it is no surprise that energy posted the best return. Oil giants Exxon Mobil, ConocoPhillips and Chevron returned 41.8%, 41.9% and 36.9%, respectively. However, the sector was already a top performer prior to the onset of the war, profiting from severe winter weather earlier in the quarter.

While only a fraction of those in the energy sector, returns in materials and utilities were solid.

Materials companies have been advancing on surging commodities prices, with the price spike in oil just the latest in the series. In addition, US fertilizer companies got a leg up as the closure in the Strait of Hormuz disrupted production for their Middle Eastern and European competitors. CF Holdings, a nitrogen fertilizer manufacturer, returned 68.5%. Traditionally a beneficiary in a risk-off rotation, utilities companies were also helped by a shift in investor focus from well-known AI names to firms providing the energy infrastructure keeping the AI revolution rolling. Utilities-adjacent Bloom Energy, a fuel cell provider, returned 55.9%.

Despite the headlines, full-year 2026 revenue and earnings growth estimates for most S&P 500 sectors showed a surprisingly small change over Q1. Perhaps most counterintuitive given its performance, both revenue and earnings growth estimates for the tech sector actually increased. Industry-wide layoffs and AI-driven efficiencies must be paying off.



## International Markets

After a strong finish to 2025, developed markets erased most gains as the US and Israel attacked Iran in Q1. A sharp volatility increase wiped out over \$11.5 trillion in market capitalization, triggering a major energy shock as Iran closed the Strait of Hormuz. Few markets were untouched by spiking oil prices, equity declines, and increased inflation. While developed markets bore the brunt, emerging markets in Asia and Latin America posted gains as resource-rich economies benefited from a commodity rally.

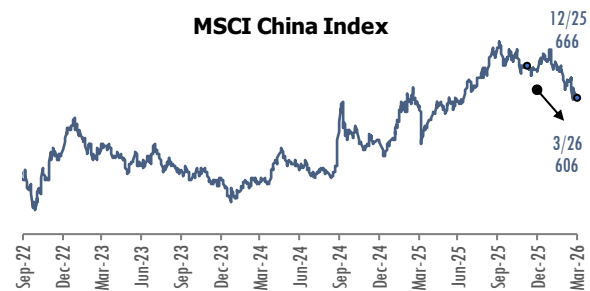
The US dollar navigated a volatile Q1. Early weakness was amplified by the so-called Greenland crisis, Trump's repeated calls to devalue the dollar, Fed rate cut signals and capital outflows from US assets. The combination dragged the US Dollar Index (DXY) to five-year lows near 95.5 in late January and stirred talk of "deglobalization" and moving away from the dollar as a reserve currency. The dollar stabilized in February after the hawkish nomination of Kevin Warsh as the next Fed Chair. A sharp March reversal pushed the DXY to a close of 100.22, fueled by safe-haven flows amid the Iran war, while strong US labor market and PPI data reinforced expectations of the Fed holding rates steady. Major currencies including the euro, Swiss franc and Australian dollar gave back ground against the greenback.

Pre-war, the IMF projected 3.3% global growth in 2026. By late March, the IMF warned the war created an "asymmetric shock" leading to slower growth and higher prices, with new growth projections slated for April. OECD global growth projections were lowered to 2.9%.

### Asia

The MSCI China Index exhibited mixed performance in the first quarter of 2026, characterized by high volatility, as investors balanced strong industrial output against ongoing property sector problems. While early-year sentiment was optimistic, with forecasts for 15% earnings growth driven by internet giants, the index experienced significant pressure in late March, ending the quarter with a -8.9% return.

Economic data for January-February 2026 showed a firm start, with key indicators exceeding expectations. Industrial production grew 6.3% YoY, up from 5.2% in December 2025, and retail sales increased 2.8%, suggesting a moderate recovery. Additionally, export growth was remarkably strong at 21.8% in the first two months, driving some early optimism.



However, weak fundamentals prevented a sustained rally. The manufacturing PMI fell to 49.0, and the non-manufacturing PMI slightly improved to 49.5, staying below the 50-point expansion threshold. The property sector faced a steep downturn; new home prices fell 3.2% in February, the sharpest drop since June 2025. The real estate drag, combined with an urban unemployment rate that ticked up to 5.3% in February, capped gains. This performance suggests a broader market turnaround requires improved consumption and stabilization of property prices.

External risks, specifically the widening Middle East conflict, compound these weaknesses. Though China built a 1.2-billion-barrel crude stockpile, a prolonged energy crisis could trigger demand shocks. Higher energy costs and supply chain disruptions threaten the export-reliant economy and spending power of key trading partners.

Japanese markets experienced elevated volatility but saw strong safe-haven demand. Energy, financials, and AI sectors performed well, while automotive faced heavy late-quarter selling. Q1 GDP growth is expected at 1.3%, with exports recovering as a resilient US economy supports consumption. Real wages are turning positive, and Japan's manufacturing expanded in March, though the Iran war pushed input costs up at the fastest rate in nearly 2 years.

### Europe

European markets fell in lockstep with other developed markets due to the impact of the war in Iran. Short-term indicators suggested positive growth dynamics early this year, but the war lowered the growth outlook as energy price shocks and increased uncertainty are expected to lead to lower consumption and investment.

ECB baseline forecasts on March 11 projected oil peaking around \$90 per barrel in Q2 2026, with increased inflation dampening purchasing power and short-term GDP. Brent crude clearly overshot these estimates, settling around \$118 per barrel. While the ultimate global impact on oil prices, inflation and growth remains uncertain, the euro area's medium-term outlook

Unhedged Foreign Markets Indices - Total Returns			
Stocks	1Q26	Bonds	1Q26
MSCI ACWI ex-US	-0.71%	Global Aggregate	-1.07%
EAFE (Developed)	-1.24%	Pan-Euro	-2.72%
Emerging Markets	-0.17%	Asian-Pacific	-0.81%
Europe	-2.82%	Eurodollar	-0.29%
Japan	1.37%	Other Currencies	-0.49%
China	-8.94%		
Latin America	14.58%		

remains optimistic, driven by domestic demand, a resilient labor market, and infrastructure spending. The ECB projects 2026 real GDP growth at 0.9%, down 0.3% due to the escalating war. Surging energy prices are projected to increase Q2 inflation sharply to 3.1%, and full-year inflation was revised upward 0.7%.

Following a late-2025 recovery, economic development in Germany lost steam in early 2026 with industrial production, new orders and retail turnover notably decreasing. Germany's ZEW indicator of economic sentiment collapsed from 58.3 in February to -0.5 in March, well-below analyst estimates of 39. The MSCI Germany Index was down 8.7%. A protracted Middle East war threatens a fragile recovery. Retail sales fell 0.9% in February and new car registrations declined 11% over the quarter. German equities experienced significant volatility, starting strong before declining sharply in March due to Middle East geopolitics. The German Dax 40 reached a record high in January, but a bruising March sell-off of 7% driven by automakers (Volkswagen, BMW) and energy-exposed firms (Siemens Energy) cast a pall on the quarter.

There were early signs of resilience in France. The Banque de France's March survey showed GDP growth between 0.2-0.3%, a slight increase over late 2025. Annual inflation jumped to 1.7% in March, up from 0.9% in February, driven by a 7.3% spike in energy prices linked to Middle East tensions. The MSCI France Index was down 5.5%. French equities were down 7.5% in March, marking the worst month since June 2022, with luxury (LVMH, Kering), consumer discretionary (Stellantis) and hospitality and leisure (Accor) dropping significantly. Basic resources, telecom, utilities, and defense names (Airbus, Safran, Thales) performed well. Despite rising inflationary pressures and geopolitical uncertainty, growth prospects remain positive for 2026.

European government debt yields rose following the Middle East conflict in late February. Investors demanded higher yields as confidence in the global economy faltered due to the severe impact on energy markets, supply chains and Middle East infrastructure. 2-year notes, sensitive to near-term expectations, have risen faster than their 10-year peers in a bear-flattening move where longer-dated yields reflect worries over the economic drag caused by more expensive energy. German 10-year Bund yields increased from 2.7% to over 3%, nearing 15-year highs, while the 2-year note climbed from 2.1% to 2.6%. Italian 10-year yields rose from 3.3% to over 3.9% and 2-year notes rose from 2.2% to 2.9%. The signal from bond markets is consistent: the Middle East conflict has recast the near-term outlook for inflation, monetary policy and borrowing costs.

European Government Bond Yield Changes (3/2 - 3/31)		
Region	2-Year	10-Year
Euro	+0.50%	+0.18%
France	+0.62%	+0.42%
Germany	+0.53%	+0.29%
Italy	+0.69%	+0.55%
Spain	+0.54%	+0.37%
UK	+0.77%	+0.56%

Source: ECB

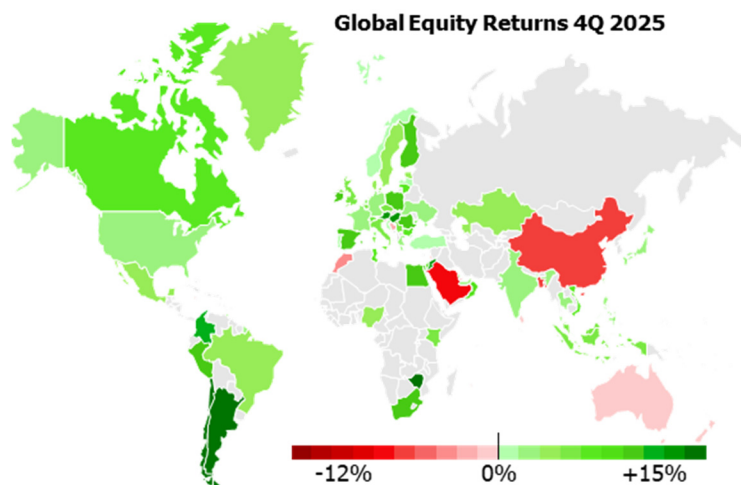
### Americas

The MSCI Canada Index returned 6.83% in Q1, fueled by an "energy renaissance" and supportive global commodity trends. While real GDP growth is projected at a modest 1.3% for the year, the market was bolstered by easing inflation and the Bank of Canada's steady interest rate stance. Investors are currently prioritizing quality and diversification as US-Mexico-Canada Agreement (USMCA) renewal discussions approach.

The MSCI Brazil Index surged roughly 15.00%, propelled by high global commodity prices and an improved political environment. As a net oil exporter, Brazil benefited from favorable terms of trade and an expanded oil-trade surplus. The Central Bank's decision to begin an easing cycle with an initial 25-basis-point rate cut supported equity valuations as headline inflation slowed to 3.81% in February.

MSCI Mexico rose 5.74%, driven by structural nearshoring momentum and more integrated regional supply chains. However, uncertainty regarding fiscal governance ahead of the 2026 USMCA review tempered growth to a forecasted 1.5%. Meanwhile, MSCI Argentina gained 1.31%, reflecting cautious optimism as the government achieved a sustained fiscal surplus and continued its macroeconomic stabilization program.

Maduro's ousting has not improved the Venezuelan economy. Prices continue climbing, with inflation around 600% and the bolivar losing nearly 20% of its value. Since 2022, the currency has devalued over 9,000% and growth has been dismal. However, double-digit growth is expected in 2026 as oil production and exporting returns. Estimates are for GDP growth of 12.1% with energy, manufacturing, trade and construction as the drivers.



## Focus On: American Exceptionalism – Cracks in the Foundation

Openness to trade, stable currency, fiscal discipline, rule of law, predictable policies, respect for property rights... These are prerequisites for the exceptionalism which has buoyed the global economy and generated enviable returns for US investors. Even during the stagflation of the 1970s or the systemic tremors of 2008, the dollar was supported by a rare alignment of structural advantages. US savers benefited from a multi-decade collapse in interest rates, a massive global trade boom, and an ever-growing, ever-more-productive working class. Contrast this with a Japanese yen saved over the same period. While the US retirement savings account basked in secular growth, the yen sailed into a perpetual storm of disinflation, stagnating businesses, and a dearth of youth. For the Japanese fiduciary, the last half century was an exercise in managing headwinds that the rest of the world seldom heeded.

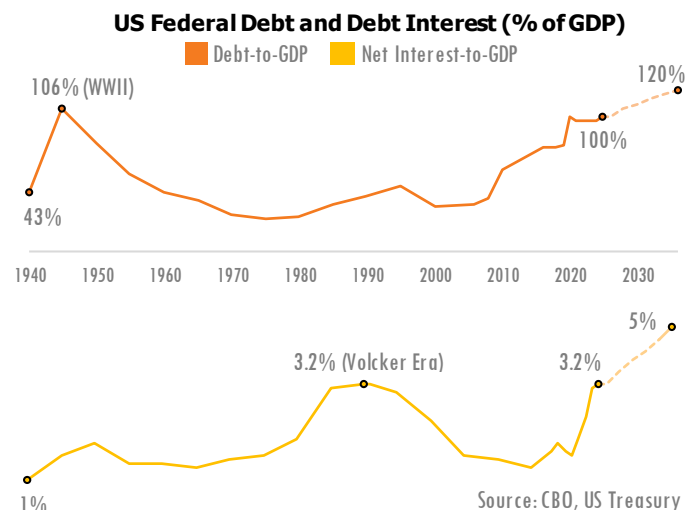
A dollar saved for retirement today enters a world fundamentally different from the one that shaped current American retirees' financial outcomes. National debt, inflationary fiscal policy, and an ongoing energy shock are forming a dreary backdrop. The launch of Operation Epic Fury was never going to be a welcome event for equity markets, but it is the most glaring sign yet that US policymaking has shifted away from the prerequisites to exceptionalism. Discarding these principles threatens the sovereign stability that has centered our economy and attracted both human and investment capital.

### The Compounding Weight of Sovereign Debt

The future of US economic growth is anchored by the federal balance sheet. The US currently owes \$38.4 trillion, a figure growing by \$6 billion every day. Federal debt held by the public has reached 100% of GDP. This is a threshold the nation last crossed in the immediate aftermath of World War II, but the context is radically different. In 1945, the country was poised for a massive demobilization and an unprecedented industrial boom. Today, the trajectory points toward a permanent expansion of obligations funded by borrowing against a future we have already spent.

Over decades, federal debt has swelled from an abstract accounting figure into a direct, competing cost within the federal budget. In 2025, the government spent \$970 billion on net interest payments alone, nearly triple the amount spent just five years ago. Interest has overtaken national defense as a line item, trailing only Social Security and Medicare. Should yields on US Treasury debt continue to rise, interest expense could quickly top the budget line items.

While this echoes Japan's path, the US has an advantage, at least for now. The dollar serves as the world's reserve currency; our domestic inflationary pressures and debt levels eventually become a global export. However, the dollar's reserve currency status depends heavily on its acceptance by global markets. To the extent the US dollar is either devalued through excess supply or weaponized to support political aims, the world will increasingly seek alternatives.



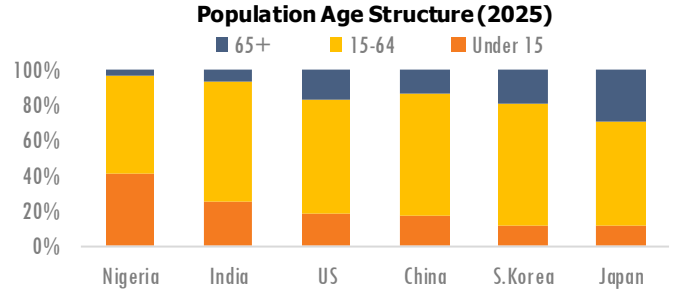
### Demographic Destiny

While interest payments are the most immediate symptom of our fiscal condition, our economic fate is equally driven by demographics. In 1950, the American system was supported by 16.5 workers for every Social Security beneficiary. Today, that ratio has narrowed to approximately 2.8, and it is on track to hit 2.1 by 2040. Declining birth rates are universal across developed and affluent countries. With zero net migration, a low birth rate becomes a dominant economic headwind.

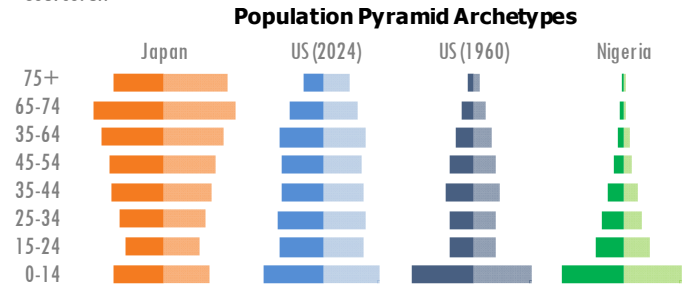
Constructive immigration policies paired with strong incentives for skilled, productive workers to come to the US has, in the past, more than offset this potential drag. The US economy has attracted skilled labor from across the world, without having to fund their formative years. It is also subsidized at its foundation by migrant labor, including undocumented workers from Central and South America who fill difficult, low-pay jobs that US citizens are unwilling or unable to perform.

Demographic maps offer a glimpse of future economic growth. While much of the developed world faces a "graying" of its capital, India is poised to contribute nearly a quarter of the global incremental workforce over the coming decade. Nigeria provides an extreme example, where childcare and education consume a high proportion of manhours. Once birth rates come down in Nigeria, the productive capacity of the workforce may increase dramatically.

The shape of the US population appears cylindrical. Nigeria’s forms a pyramid, and Japan’s shape is aptly described as a “coffin.” With nearly a third of its population over 65, Japan has spent 30 years navigating the headwinds of persistent deflation, debt-to-GDP ratio exceeding 250%, and decades of depressed equity returns. South Korea is traveling an even more extreme path, with a fertility rate of 0.74 suggesting a future where the population halving is a certainty.



Source: UN



Even China, once the world’s primary engine of growth, is facing a transition without precedent as its working-age population begins a sharp contraction. Decades-long enforcement of its One-Child Policy yielded a temporary “demographic dividend” that accelerated its industrial rise, but warped the nation’s age structure into a “coffin-shaped” profile. The engineered shortage of young people is hitting the economy now, as a rapidly aging population finds itself without new workers to replace the retiring labor force. This underscores the need to design social programs to be responsive to natural changes in demography.

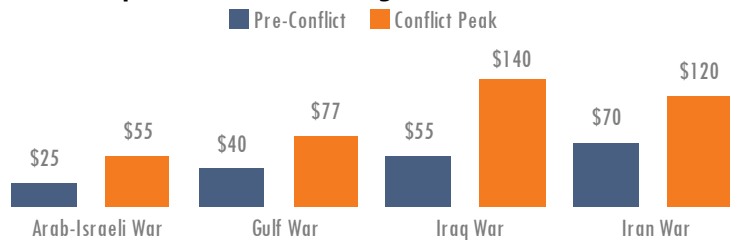
**Geopolitical Shock and Awe**

Debt and demographics serve as plodding structural supports for the economy. In contrast, geopolitics delivers dynamic change but heavily interacts with debt and demographics. For decades, American foreign policy has operated on a “buy now, pay later” model that mirrored our domestic fiscal choices. We have developed a habit of drifting into “forever wars” (Iraq, Afghanistan, and now the February 2026 launch of Operation Epic Fury in Iran) without a clear exit strategy or a plan to pay for them. It is the ultimate quagmire of short-term policymaking. We choose the immediate path of least political resistance, only to find ourselves stuck in a high-stakes entanglement that is difficult to extricate ourselves from.

Operation Epic Fury demonstrates the staggering cost of modern conflict. The Penn Wharton Budget Model projects a conservative military cost for a two-month campaign at \$95 billion; other estimates top \$200 billion. Mr. Trump has asked for a 2027 defense budget of \$1.5 trillion vs. \$1.05 trillion in 2026. The global economic supply chain shocks, damage to gulf infrastructure, and uncertainty could push total realized and opportunity costs over \$1 trillion without further escalation.

The US has a unique, perhaps enviable, habit of sharing the pain of its policy blunders with the rest of the world. Because the dollar serves as the world’s reserve currency, our domestic inflationary pressures and debt levels eventually become a global export. We saw this clearly during the 2008 Global Financial Crisis. While the crisis originated in the American housing market, the resulting economic contraction was often more severe for our trading partners in Europe and Asia than it was for us. The current conflict is following a similar script. By effectively closing the Strait of Hormuz, we have triggered a global energy shock. Brent crude has spiked past \$126 per barrel. While American drivers are feeling the sting of \$5 gas, the real damage is being felt by energy-dependent economies in Asia and Europe that lack our domestic production buffer.

**Oil prices Before and During Middle East Conflicts**



Source: Bloomberg, Axios

This is the new gravity of the 2020s. We are no longer financing wars with the ghost budgets of the post-9/11 era, where low interest rates and a manageable debt-to-GDP ratio allowed us to borrow with impunity. Today, every dollar spent on a missile is a dollar borrowed at 4% or 5% interest. This drives upward a national debt that has already crossed 100% of GDP. We no longer operate in a range of safety margin because spending has increased in both times of feast and famine.

**A Different Kind of Regime Change**

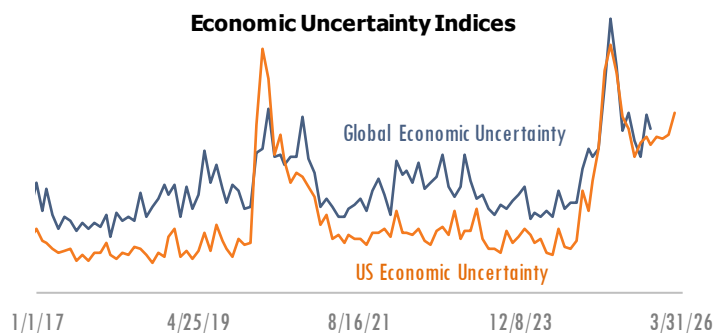
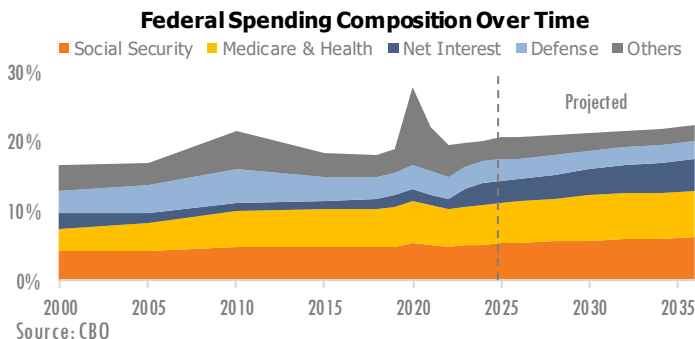
For almost two decades, investors could rely on a strong Fed put: zero-interest-rate policy. That era may be ending. A February 2026 Federal Reserve research note confirmed that recent increases in far-forward rates reflect deep-seated concerns about future federal deficits rather than temporary cyclical shifts [Fed]. With the steepening of the yield curve, Treasury bonds once again command an inflation-risk-premium. However, investors expecting higher yields to serve as defensive ballast met disappointment in March as inflation concerns outpaced recession concerns.

Fiduciaries must confront the reality that inflation is becoming a structural fixture rather than a transitory annoyance. The combination of deficit spending, energy disruptions from the conflict in Iran, and demographically constrained labor markets creates a persistent upward pressure on prices. Short-term policymaking threatens to derail the latest equity bull market promised by productivity gains and capex from large language models and other artificial intelligence advances.

### The Tipping Point

Political will shrinks at the mention of tax increases but coalesces around any guarantee of voter approval. Democrats and Republicans cannot seem to agree on much anymore, except to spend more and tax less. Political expediency is perhaps the biggest threat to long-term economic prosperity. Interest payments on federal debt were easily absorbed when the balance was modest and rates were low. Today, these payments threaten to crowd out other critical federal investments. On our current path, the Social Security Trust Fund faces a looming depletion projected between 2033 and 2035.

Recent executive efforts to trim federal spending (e.g., DOGE) have struggled to generate meaningful savings but have hollowed out institutional expertise. The broad dismantling of federal departments threatens to erode the deep institutional knowledge that underpins the country's economic competitiveness. For example, aggressive cuts to scientific research grants may yield incremental budgetary relief, but they degrade our scientific standing and reputation. Chaos and instability are not big selling points; they dissuade productive experts and talent from relocating to the US.



Historically, the US maintained a stability premium, with domestic uncertainty consistently tracking well below the global average. However, recent data shows the US economic uncertainty running at global levels, reflecting the compounding pressures of geopolitical entanglements and an increasingly strained federal balance sheet. Economic policy uncertainty can "...foreshadow declines in investment, output, and employment in the United States" [Baker et al]. The 2020 spike was caused by the pandemic, while Mr. Trump's tariffs and his war with Iran are responsible for the latest elevated levels.

### Implications for Fiduciaries

If it is no longer clear that the US is going to maintain exceptionalism over the rest of the world, fiduciaries need to adjust. Many investors have become very comfortable with a home country bias, and tend to underestimate the impact of inflation and heightened market volatility. While the picture may be daunting, fiduciaries have practical tools at their disposal:

- Diversify all asset classes globally where you control allocations (e.g., pensions, endowments, insurance, etc.).
- Stress-test portfolios for interest rate and credit risk.
- Ensure 401(k) menus offer diversified choices without undue weight to US investments.
- Consider real assets (not just TIPS) as hedges against inflation and dollar weakness.
- Avoid excess home country bias in target-date and other allocation funds.
- Emphasize the risk of inflation and avoid characterizing US assets as "safe havens" in participant communications.
- Incorporate Social Security realism into retirement planning tools.

The era of relying on US equities and bonds to perpetually outperform may be over, necessitating a departure from familiar home biases. As the macroeconomic backdrop shifts, foreign countries with favorable demographic profiles and sovereign stability may capture some of the economic premium enjoyed by the US.

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