

Quarterly Market Wrap | Q1 2026

Navigating Crosscurrents: Resilience Amid Uncertainty

FTWA[®]



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Markets entered 2026 with constructive fundamentals — solid earnings growth, participation beyond mega-cap tech leaders, accommodative monetary policy and anticipated fiscal support. At the same time, navigating the crosscurrents of geopolitical uncertainty, inflation, and elevated levels of valuations and market concentration warranted caution.

As the conflict in the Middle East escalated, markets experienced a difficult and volatile March. Despite these challenges, U.S. equities have remained relatively resilient as they've navigated the turbulence. Large-cap stocks are only modestly lower year to date, with drawdowns reaching 6.5%, well within historical norms, reflecting continued strength in corporate balance sheets and earnings power — for now.

- 1. Geopolitical trifecta:** Investors weighed the risks and potential fallout from three distinct geopolitical shocks in the first quarter:
 - **Venezuela regime change:** The United States carried out a military incursion into Venezuela, securing oil reserves and resulting in the extrajudicial capture of Venezuelan President Nicolás Maduro and first lady Cilia Flores.
 - **Tariff reversal:** A U.S. Supreme Court decision voided key Trump-era tariffs, briefly reducing trade friction and inflation pressures while reintroducing policy uncertainty as the administration pursues alternative authorities.
 - **Iran conflict:** The U.S. and Israel initiated attacks on Iran, prompting Iran to close the crucial Strait of Hormuz. With the conflict continuing for more than a month and up to 20% of global oil supply potentially impacted, markets are reacting to what global agencies describe as the largest oil supply disruption on record.
- 2. “SaaSpocalypse” — Artificial intelligence-driven software disruption raising equity and credit dispersion:** Recent AI tool announcements triggered a sharp derating across software-as-a-service (SaaS), data and workflow companies. S&P 500 software firms are collectively experiencing nearly a 30% drawdown — with spillover effects extending to alternative-asset managers exposed to software-related equities and debt. While the selloff represents a meaningful repricing event tied to AI-driven competition, shifting sentiment and potential software obsolescence, multiple counterpoints suggest investors should attempt to distinguish between near-term valuation resets in SaaS and longer-term macroeconomic outcomes.
- 3. Private credit risks take center stage:** Fueled by concerns over AI-funded debt, software concentration and the risk of public-market SaaS contagion, investors ran toward the exit from their private credit funds. The shift in investor sentiment forced prominent private-credit managers such as Blue Owl and Blackstone to restrict investors' access to liquidity.
- 4. The Federal Reserve might get backed into a corner** as a cooling labor market and moderating economic growth — conditions that typically support rate cuts — take hold. However, inflation remains stuck above the Fed's 2% target and has recently shown renewed upward pressure, risks that could be exacerbated by a prolonged conflict involving Iran. Perhaps the most difficult scenario for policymakers is stagflation, marked by slowing growth, weakening employment and elevated inflation, a backdrop in which policy tools force difficult trade-offs between supporting economic growth and the labor market and controlling prices.

Chart of the quarter: With the war, could the Fed's next move be higher rates?

Could this spell rate trouble?
2Y note yield pokes above fed funds on war, oil, deficit fears

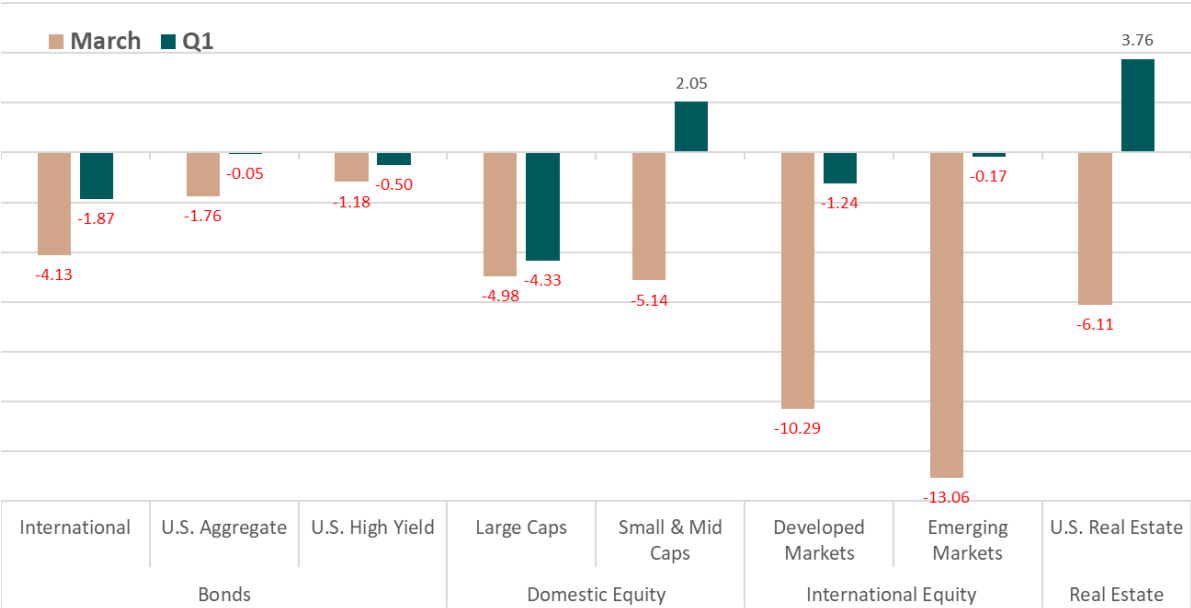


With the two-year U.S. Treasury yield now above the effective federal funds rate, investors are indicating that the Fed's next policy move is more likely to be a rate hike than a cut, reflecting rising inflation expectations and limited room for policy cuts.

The primary driver is the largest oil supply shock in modern history, stemming from escalating conflict involving Iran and the blockage of the Strait of Hormuz. Disruptions across oil, natural gas, fertilizers and related resources are pushing costs higher globally, with pressures mounting as the conflict persists.

Consumers are increasingly feeling the impact, with average gasoline prices exceeding \$4 per gallon, straining household budgets. Elevated energy costs act as a regressive tax, disproportionately affecting lower- and middle-income households, widening the wealth gap and increasing the risk of slower consumer spending and more moderate economic growth in 2026.

Asset class performance – March & Q1



Source: Bloomberg, as of March 31, 2026. Asset-class performance is presented by using total returns for an index proxy that best represents the respective broad asset class. U.S. Bonds (Bloomberg U.S. Aggregate Bond TR), U.S. High Yield (Bloomberg U.S. HY 2% Issuer-Capped TR), International Bonds (Bloomberg Global Aggregate ex USD TR), Large Caps (S&P 500 TR), Small & Mid Caps (Russell 2500 TR), Developed Markets (MSCI EAFE NR USD), Emerging Markets (MSCI EM NR USD), Real Estate (FTSE NAREIT All Equity REITS TR). Indices are not available for direct investment. Investment in a security or strategy designed to replicate the performance of an index will incur expenses, such as management fees and transaction costs that will reduce returns.

FTWA outlook & implications

Fifth Third Wealth Advisors believes several of the themes that fueled optimism in January still exist today. However, considering the rapid developments and broader implications of the conflict involving Iran, our expectations have moderated. The longer the war drags on, risks to the downside grow, as the global effects become more widespread and acute. This raises the possibility of a shift from an economic regime of rising growth and inflation to one characterized by falling growth and rising inflation.

Optimism:

- 1. U.S. equities** saw valuations decline during the first quarter of 2026 as market prices softened, and earnings growth remained strong. Fourth-quarter 2025 earnings rose 13.9%, with growth expected to continue into early 2026 and accelerate throughout the year. Notably, earnings and performance broadened beyond the “Magnificent Seven,” which declined 10.6% in the first quarter. The remaining 493 stocks in the S&P 500 were relatively resilient, down just 0.82% over the period. This widening participation reduces reliance on a small group of companies and helps lower overall concentration risk, supporting a constructive long-term outlook. That said, we remain anchored in the near term given ongoing uncertainty around the scope, duration and global impact of the conflict abroad.
- 2. International equities** are positioned for improvement as conditions evolve. While recent performance reflected short-term pressures from energy exposure and a stronger U.S. dollar, longer-term fundamentals are becoming more supportive. Attractive valuations, ongoing supply-chain realignment and increased domestic investment across regions provide a constructive backdrop. Looking ahead, progress toward a resolution in the Middle East could act as a meaningful catalyst — not only improving investor sentiment but also potentially weakening the U.S. dollar, which has historically provided an additional tailwind for international equity returns.
- 3. Fixed income** continues to offer attractive income opportunities, particularly as persistent inflation concerns and a growing fiscal deficit keep upward pressure on longer-term interest rates. At the same time, slowing growth tied to geopolitical developments could provide periods of support for longer-dated bond prices. On the short end of the market, as expectations for monetary policy stabilize, yields are likely to remain relatively steady, reinforcing fixed income’s role as both a source of yield and portfolio balance.
- 4. Alternatives** stand to benefit from several macroeconomic drivers while providing diversification benefits to portfolios. With inflation expectations rising, real assets such as infrastructure, industrial and precious metals, and certain types of real estate could benefit, helping hedge against increased pricing pressures while enhancing overall portfolio diversification.

Risks:

- 1. A prolonged conflict involving Iran** represents the most immediate and impactful risk to the global macroeconomic landscape. The largest energy supply shock on record is expected to further disrupt global supply chains, push inflation higher and slow economic growth, though the magnitude remains uncertain. As gasoline prices rise, consumers are already feeling pressure, and prolonged constraints on energy and fertilizer supplies could drive costs higher across sectors such as travel and food. These pressures raise the risk of slower consumer spending and weaker overall growth.
- 2. Inflation is likely to surprise to the upside**, regardless of developments in the Middle East. Producer prices, a leading indicator of inflation trends, continue to rise faster than consumer prices — echoing conditions seen during the 2021–22 supply-chain disruptions. This suggests ongoing pressure on corporate margins as firms struggle to fully pass higher costs on to consumers, a dynamic that has historically weighed on earnings growth and equity market expectations — further complicating the monetary policy outlook.
- 3. Monetary policy risks** may move to center stage. Rising inflation expectations, combined with a moderating labor market and slowing economic growth, are reviving concerns around stagflation — a backdrop in which the Fed’s policy tools work against its dual mandate. As a result, we expect heightened market volatility around key economic data releases as policymakers attempt to walk the proverbial tight rope. Meanwhile, the Fed Chair succession and questions around central bank independence are likely to remain in focus in the months ahead.
- 4. Midterm election years** have historically been among the weakest periods in the presidential cycle, often marked by early-year volatility followed by improving momentum later in the year. While every cycle is different and outcomes vary, the ongoing conflict involving Iran is likely to add another layer of uncertainty as the elections draw closer.

While meaningful risks remain, we believe the long-term outlook for the economy and markets remains constructive, supported by improving earnings growth, expanding profitability and market breadth, supportive fiscal trends, and longer-term industrial and infrastructure tailwinds. However, expectations have moderated, and uncertainty — particularly related to developments in the Middle East — remains elevated, leaving the outlook on fragile ground.

In this environment, our focus remains on quality, diversification and discipline. A broad-based approach aligned with long-term objectives rather than short-term headlines is best positioned to navigate evolving market dynamics. Periodic rebalancing and selective upgrades to quality can help portfolios remain resilient as conditions change. As always, your advisory team remains committed to keeping your portfolio balanced and aligned with your goals, and we appreciate your continued trust and confidence.

DEFINITIONS:

Bloomberg U.S. Aggregate Bond TR: Measures the performance of the total U.S. investment-grade bond market, including U.S. Treasuries, agency debt, mortgage-backed securities, asset-backed securities, and corporate bonds.

Bloomberg U.S. HY 2% Issuer-Capped TR: Tracks the performance of fixed rate dollar denominated debt securities. The debt instruments are non-investment grade. There's a limit of 2% maximum exposure to any one issuer.

Bloomberg Global Aggregate ex USD Total Return: Tracks the performance of investment-grade, fixed-rate bonds issued in currencies other than the U.S. dollar, including treasury, government-related, corporate, and securitized bonds from both developed and emerging markets.

FTSE NAREIT All Equity REITS TR: Measures the performance of U.S. publicly traded equity REITs, including both price changes and dividend income.

MSCI EAFE NR USD: Captures large- and mid-cap representation across 21 developed markets countries around the world, excluding the U.S.

MSCI EM NR USD: Captures large- and mid-cap representation across 24 emerging markets countries.

Magnificent Seven stocks are a group of companies in the U.S. stock market: Alphabet, Amazon, Apple, Tesla, Meta Platforms, Microsoft and Nvidia.

Russell 2500 TR: Measures the performance of the smallest 2,500 companies in the Russell 3000 Index. This index is constructed to give a comprehensive and unbiased barometer for the small- and mid-cap segment of the U.S. equity universe.

S&P 500 Total Return: Includes a representative sample of 500 leading companies in leading industries of the U.S. economy, calculated on a total return basis.

RISK CONSIDERATIONS:

Investing involves risks and you may incur a profit or a loss. Past performance does not guarantee future results.

Different types of investments involve varying degrees of risk and there can be no assurance that the future performance of any specific investment vehicle, strategy or product referenced in the material will be profitable or suitable for your particular investment situation.

Equity securities are subject to frequent changes in valuation and are often more volatile than other asset classes. Equity valuation is subject in part to the associated fluctuations in the market confidence of its issuers.

Fixed income securities are subject to credit risk, liquidity risk, call risk and interest rate risk. As interest rates rise, bond prices generally fall.

International securities risks include fluctuations in the exchange rates of foreign currencies that may affect the U.S. dollar value of the investment, the possibility of substantial price volatility as a result of political and economic instability in the foreign country, less public information about issuers of securities, different securities regulation, different accounting, auditing and financial reporting standards and less liquidity than in the U.S. markets. Historically, these risks have tended to be more pronounced in emerging market countries than in more developed foreign countries.

Alts and non-traditional assets such as real estate, commodities, currencies and private companies, are subject to risks that are different from, and in some instances, greater than, other assets like stocks and bonds. Some non-traditional assets are less transparent and more sensitive to domestic and foreign political and economic conditions than more traditional investments. Non-traditional assets are also generally more difficult to value, and less liquid than traditional assets.

Indices are not available for direct investment. Investment in a security or strategy designed to replicate the performance of an index will incur expenses, such as management fees and transaction costs that will reduce returns.

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Appropriate investment strategies depend upon the investor's investment objectives. The portfolio risk management process and the process of building efficient portfolios includes an effort to monitor and manage risk but should not be confused with and does not imply low or no risk. Some strategies may be subject to a higher degree of market risk than others. An investor should understand the costs, cash flows and risks inherent in a strategy prior to making any investment decision. There are no guarantees that a strategy will perform as intended. The value of investments and the income derived from investments can go down as well as up. Future returns are not guaranteed, and a loss of principal may occur. Investing for short periods may make losses more likely.

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