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INVESTMENT STRATEGY QUARTERLY

STATE of PLAY

DISCIPLINE OVER EMOTION

Letter from the Chief Investment Officer

State of Play: Discipline Over Emotion

Soccer legend Pelé famously called soccer "the beautiful game"—a tribute to its universal accessibility, elegant simplicity, and strategic depth. All it takes is a ball, yet at its best, soccer becomes a shared global language, connecting players and fans across cultures and generations. That spirit will be on full display this summer as the US, Mexico, and Canada co-host the World Cup, with an estimated six billion viewers watching teams adapt to unfamiliar opponents, conditions, and tactics. The best players know talent alone doesn't win tournaments—preparation, flexibility, and calm under pressure determine who advances.

The past year has demanded many of those same traits from investors. Rapid advances in artificial intelligence, persistent geopolitical tensions—particularly Iran—and ongoing trade uncertainty have kept headlines loud and emotions elevated. In that kind of environment, the biggest mistakes come from reacting to noise rather than fundamentals. Like a well-organized team that keeps its composure over the full tournament—not just one match—investors who stay focused on long-term objectives and respond thoughtfully instead of emotionally are best positioned to succeed over time.

In the near term, developments in Iran will shape the economic outlook. Energy prices have reached multiyear highs, pressuring consumers. While the situation remains fluid, our base case is that the conflict will end shortly. Limited public support, rising gasoline prices, and shifting political momentum ahead of the midterm elections are likely to constrain its duration. Importantly, the impact on oil has been more about shipping disruptions than a significant loss of production. As conditions normalize, we expect oil prices to retreat toward $60 per barrel, reducing spillovers to economic growth, monetary policy, and asset markets.

Coming into the year, the US economy took the field in strong form. Still, as any soccer fan knows, matches can turn on a single moment—a deflection, a missed clearance, or a sudden counterattack. The recent spike in oil prices prompted a fresh review—our own Video Assistant Referee (VAR) moment—but the call stands: we still expect 2.4% economic growth in 2026.

Historically, oil shocks have been most damaging to weaker, energy dependent economies. Today, however, the US is on firmer footing: more energy efficient, less energy intensive, and a net exporter of oil, providing a stronger defensive line against supply disruptions. Given our expectation of a brief conflict in Iran, higher oil prices appear to be a temporary headwind rather than a match-altering 'red card.'

Consumer spending should remain supported by healthy tax refunds this season and improving hiring conditions, while business investment continues to benefit from record AI-related capital expenditures that are delivering the strongest productivity gains in two decades. While a prolonged rise in energy prices would raise recession risk, we see no reason to abandon our broader, more optimistic outlook based on a single contested play.

The Federal Reserve (Fed) is navigating this stretch with potential new leadership on the horizon, as Kevin Warsh sits a Senate confirmation vote away from becoming the next Fed chair. He appears well-suited for the coach's role, bringing a rare blend of experience—firsthand knowledge of the locker room from his time as a Fed governor (2006–2011) and a clear understanding of how the crowd and markets react from his years on Wall Street. That perspective matters. Still, once policy debates begin, the ultimate tempo of play is set by the full Federal Open Market Committee—the eleven other 'players' alongside the chair—and, as with any new leader, markets and fellow policymakers will quickly test his discipline, credibility, and consistency.

At present, the Fed faces a delicate tactical dilemma. Inflation remains stubbornly above the 2% target, constraining the Fed's ability to ease, even as a softening labor market increasingly argues for eventual support. Geopolitical tensions and higher

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oil prices add near-term complexity and reinforce that restraint, but as those pressures fade later in the year, we expect the Fed to place greater weight on labor market conditions and deliver one rate cut before year-end.

In fixed income, bonds continue to play the role of the goalkeeper—steady and dependable when conditions get choppy. While inflation remains a risk, we do not expect elevated energy prices to persist, and with growth holding up, the 10-year Treasury yield should finish the year within our 4.25%–4.50% forecast range. Like a goalkeeper who favors control over power—calmly distributing the ball to reset play rather than forcing a booming kick—today's starting yields are attractive, especially when compared to the historically low COVID-era levels. With monetary policy still mildly restrictive but gradually tilting toward easing, we continue to favor higher-quality bonds such as investment-grade bonds over riskier high-yield credit.

While the World Cup will capture global attention, many Americans dismiss soccer as "too boring." But seasoned fans know the game isn't just about goals; it's about spacing, positioning, pace, and movement off the ball. Markets have looked similar this year: while the S&P 500's pullback has been modest and its top-line trading range narrow by historical standards, a great deal of game-changing action has been unfolding beneath the surface.

Sector rotation has been meaningful. Energy surged early, while Financials lagged. We expect rotation to remain a defining feature of the equity market. Against geopolitical uncertainty and elevated energy prices, sectors with durable tailwinds and strong margins should prove most resilient. Technology remains the market's captain, with Industrials, Consumer Discretionary, and Health Care as our other star players. Technology benefits from sustained AI investment; Industrials from infrastructure, reshoring, and defense spending; Consumer Discretionary from moderating energy prices; and Health Care offers something akin to home-field advantage given its more domestic orientation and support from durable demographic trends. While Energy has been an early standout, we do not believe now is the time to increase exposure. As supply disruptions ease, recent outperformance may prove temporary—more like a breakaway run steadily closed down by disciplined defenders.

Volatility is likely to remain elevated in the near term, but investors should resist reacting to every whistle. The US economy remains on solid footing, and equities are entering this stretch from a position of strength. With valuations now more reasonable, we expect earnings growth of ~10% to carry the S&P 500 toward our year-end target of 7,250. Importantly, that target is built on a conservative $300 earnings assumption—providing a meaningful cushion relative to the consensus forecast of $316.

Long-term success comes from balance and preparation, not reacting to short-term headline noise.

Internationally, non-US equities were winners last year, aided by improving growth and a weaker dollar. Recently, however, a few 'yellow cards' have appeared. While the odds of winning the World Cup may favor teams like Spain, England, and France, we continue to prefer US equities over other developed international markets due to stronger GDP growth, more resilient earnings, and lower sensitivity to Middle East-related costs. In Asia, near-term volatility may persist, but we view these pressures as temporary setbacks. We remain constructive—though selective—on Asian emerging markets, where improving earnings momentum and solid longer term fundamentals, including exposure to the Technology sector, remain intact.

In soccer, the most reliable penalty kick isn't the spectacular corner strike—it's the calm kick straight down the middle as the goalkeeper commits one way or the other. Investing works much the same way. Long-term success comes from balance and preparation, not reacting to short-term headline noise. Over a full tournament—or a full market cycle—results are shaped by positioning and discipline. That's where your advisor and our work help complete your team, maintaining perspective and increasing the likelihood of achieving your goals. In markets, as in soccer, championships are won by those who keep their composure, trust the process, and keep their eyes on the trophy.

Wishing you an enjoyable World Cup. Go USA!

Larry Adam

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Chief Investment Officer

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Understanding the Complexity of the Affordability Crisis

Eugenio J. Alemán, PhD, *Chief Economist,* Raymond James
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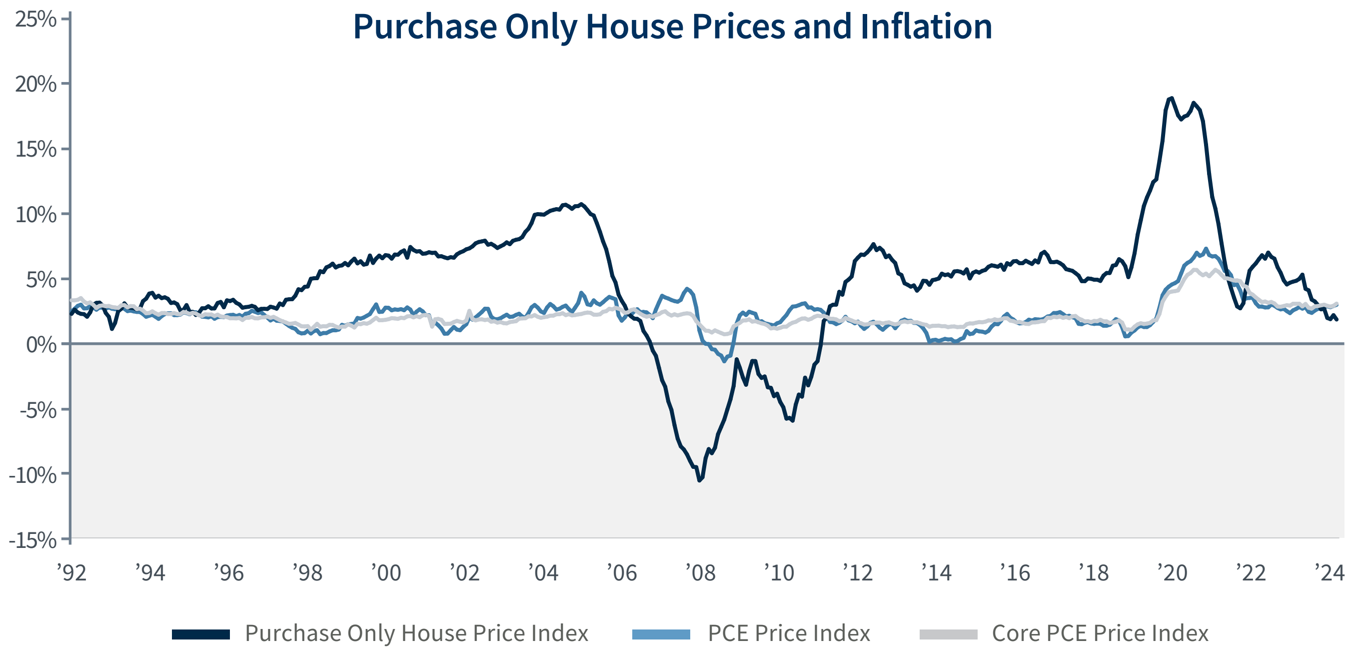
Politicians love low interest rates, or 'easy money,' because, among other benefits, it helps economic growth by expanding the number of individuals who have access to credit. Easier access to credit increases the ability of those individuals to buy goods and services as well as get a loan for purchasing a home. All of this increases consumption and pushes economic growth higher. But lower interest rates are not always good for the economy as a whole. Low interest rates may also have negative consequences, especially for those who are typically at a disadvantage—those at the middle to lower income levels and who have low levels of wealth.

> Lower interest rates are not always good for the economy as a whole.

Why? Because low interest rates have the potential to increase asset prices at a faster pace than consumer prices are increasing. What is an asset? An asset is typically a financial instrument like stocks or bonds, or real estate like homes or commercial properties. This means that asset price inflation affects the components of wealth, such as equities, bonds, housing, commercial real estate, commodities, and even collectibles, which include art and precious metals, etc.

On the other hand, consumer price inflation, measured by the consumer price index (CPI) or the personal consumption expenditures price index (PCE price index), measures the price of goods and services that consumers typically consume. Although these measures of consumer prices also include the price of homes, the prices of homes are not measured directly in these indices. Rather, they are measured indirectly, for the services they provide—what is called 'owners equivalent rent.'

Since the early part of this century, the Federal Reserve (Fed) has pursued an expansive monetary policy, i.e., a policy of low interest



Source: FactSet, data as of 3/17/2026

rates, because inflation remained below the Fed's target for years, and the Fed had been trying to bring inflation back to the 2.0% target. During that period, very low interest rates as well as lack of regulations helped to produce a home price asset bubble that ended with the Great Financial Crisis (GFC) or Great Recession. Prior to that crisis home prices surged well above the overall price level, but the increase in the price of homes did little to affect the rate of inflation as other disinflationary effects overwhelmed the effects of home price appreciation (see graph above).

However, that environment changed after the COVID pandemic recession when the underlying disinflationary trend that existed since the start of the century ended and both goods as well as services prices, which include housing prices, started to move higher simultaneously.

THE FEDERAL RESERVE TODAY: BETWEEN A ROCK AND A HARD PLACE

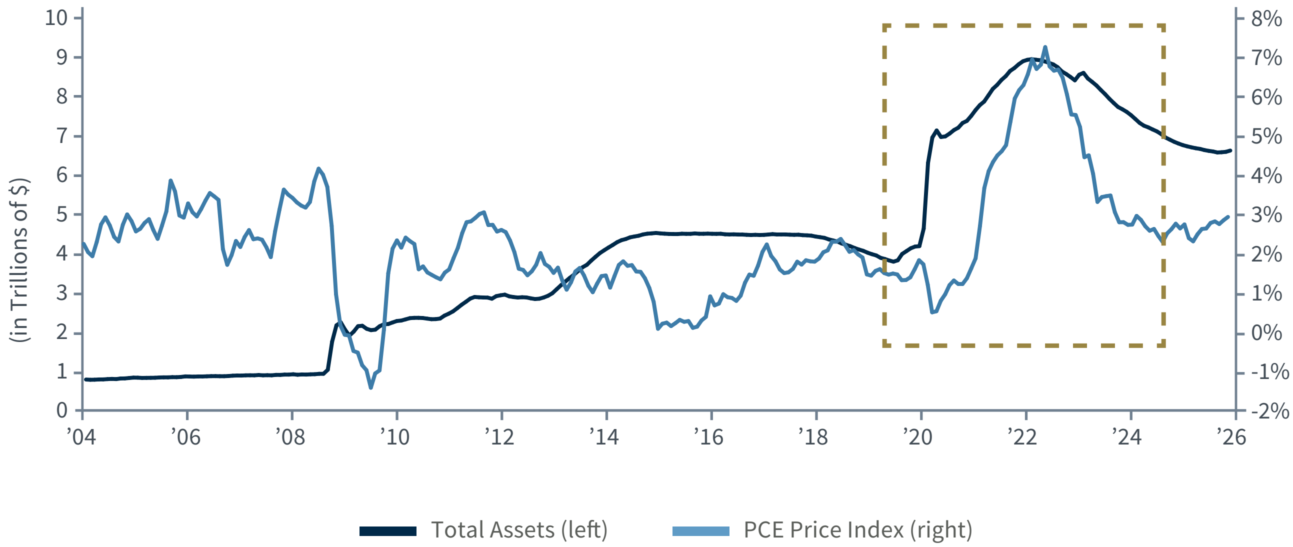
The job of the Fed since the beginning of the century was to increase inflation, getting closer to 2%. Today’s job, however, is just the opposite: to bring inflation down to 2.0%. An expansionary monetary policy was what was called for in order to increase the rate of inflation, which included the introduction of quantitative easing (QE) during the worst of the financial crisis. However, today’s policy cannot be expansionary because it would only make the Fed’s job of bringing inflation back to 2.0% more difficult. Thus, today, the Fed needs to conduct monetary policy that is tighter than what it has been for the past two decades.

Enter Kevin Warsh as President Trump’s nominee for Fed Chairman. During his tenure as a Governor of the Board of the Federal Reserve (2006-2011), Kevin Warsh was, as some have indicated, very close to Fed Chairman Ben Bernanke when he introduced quantitative easing (QE) and other programs to stabilize the financial system. But he resigned from the Board in disagreement with a second phase of QE that started in 2010, which he argued was going to increase inflation. However, inflation did not increase during that period even as the Fed continued to expand QE.

QE was used again during the COVID recession, and in this case, inflation increased. However, QE was not to blame for the increase in inflation. Inflation was more of a byproduct of supply chain issues created by the COVID pandemic, as well as very expansive

> It is important to note that the increase in inflation was a worldwide phenomenon and not just a US phenomenon.

The Impact of QE on Inflation Post-Pandemic



Source: FactSet, data as of 3/17/2026

fiscal policies conducted across the global economy as well as by successive Republican and Democratic administrations. It is important to note that the increase in inflation was a worldwide phenomenon and not just a US phenomenon, while there are very few countries that have used or have the ability to use QE.

At the end of his tenure as a Board member of the Fed, Kevin Warsh was considered a ‘hawkish’ member of the Board. That is, he was more concerned about the inflationary effects of monetary policy while being against the continuous expansion of the Fed’s balance sheet (see graph above). Recently, he has transitioned from having hawkish views to having more ‘dovish’ views on monetary policy, arguing that the current increase in productivity generated by AI would allow the Fed to lower interest rates without pushing inflation higher.

The problem for the Fed today is how to bring down interest rates without generating an asset price cycle that continues to push the price of these assets higher. This is particularly the case with the housing market. If the Fed lowers interest rates further and that pushes home lending higher, it could continue to push home prices even higher and worsen housing affordability even more.

Furthermore, the fundamentals of the US housing market are not related to the level of mortgage rates but, fundamentally, to a lack of supply of homes; that is, a lack of homebuilding, something that lower interest rates will probably not solve.

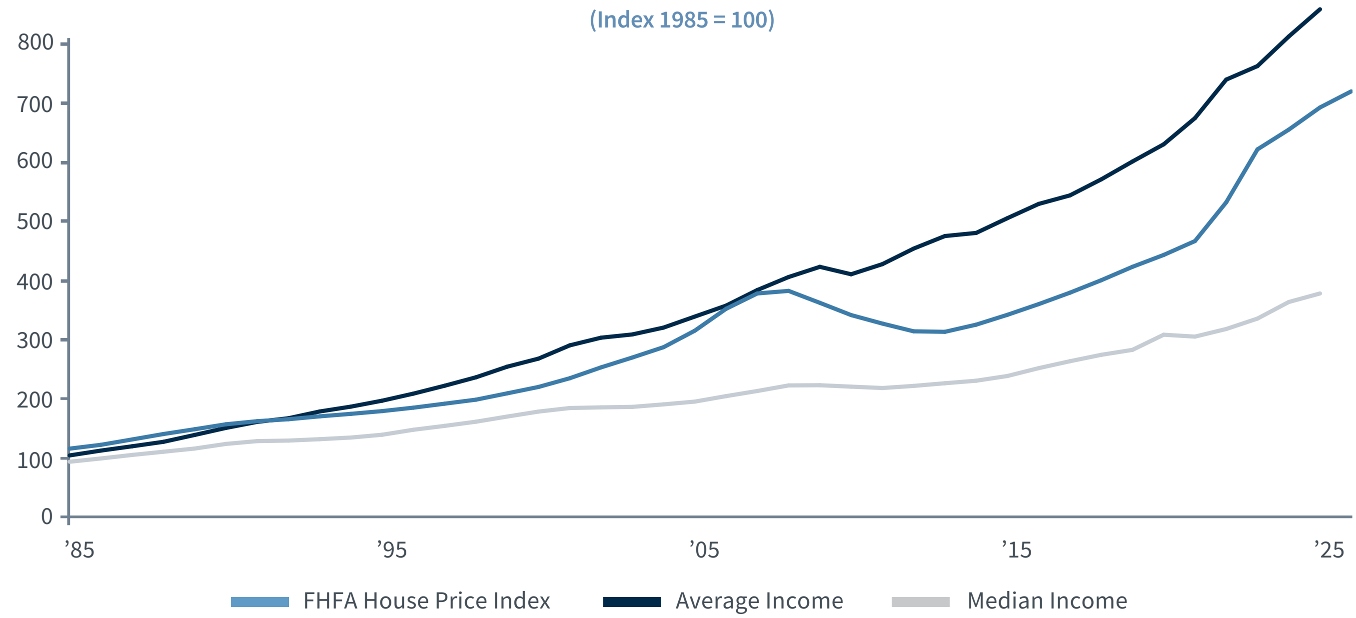
MEDIAN INCOME AND MEDIAN HOME PRICE

Home affordability has become a daily headline, and for many households, it is not an abstract policy debate but something real. Those who did not purchase or refinance a home more than three years ago, when home prices were lower, and mortgage rates were near historic lows, are facing a fundamentally different market today. Prices surged during the pandemic-era housing boom, and although mortgage rates have come down from their recent peaks, they are still hovering around 6%, more than double the ultra-low levels many existing homeowners locked in.

At first glance, affordability may not appear to be a systemic issue. Average disposable personal income has increased over time and, on paper, has broadly kept pace with home price growth over the last four decades. But averages can be misleading. When we shift from average income to median household income, the picture changes significantly. The median better reflects what a typical household earns, whereas the average is pulled higher by top-income households. Since the GFC, there was a period when housing became unusually affordable, supported by low prices and low interest rates. For

House Prices vs. Average and Median Income

(Index 1985 = 100)



Source: FactSet, data as of 3/17/2026

many middle-income households, homeownership required disciplined but achievable savings.

In the post-pandemic environment, however, that dynamic has reversed. Rapid home price appreciation combined with higher borrowing costs has pushed monthly payments beyond what the median household can reasonably afford. The discrepancy between average and median income highlights a broader structural issue: gains at the top of the income distribution disproportionately lift averages, masking the affordability pressures faced by typical households.

This also helps explain why simply lowering interest rates may not resolve the problem. While lower rates reduce borrowing costs, they also tend to stimulate asset prices. Higher-income households, who already hold significant assets, are positioned to benefit disproportionately from further appreciation, as seen in the years following the GFC. Meanwhile, lower- and middle-income households, constrained by limited savings and rising entry costs, risk falling further behind.

In that sense, the affordability challenge is not just about interest rates or home prices in isolation. It is about distribution, about average versus median income, and how policy responses can unintentionally widen the gap between households that already own appreciating assets and those still trying to enter the market.

KEY TAKEAWAYS

- Lower interest rates are not always good for the economy and don’t solve all problems.
- Easy money inflates asset prices—especially housing—faster than consumer prices, disproportionately benefiting higher-wealth households while leaving middle and lower-income families further behind.
- Instead of fighting too low inflation, the Fed must now cool inflation without reigniting another asset boom—particularly in housing—should rates fall too quickly.
- Lower mortgage rates won’t fix affordability because the primary issue is a chronic shortage of homes, not just the cost of borrowing.
- While average incomes appear to keep up with home prices, median incomes have not—showing that typical households face worsening affordability even as wealthier households benefit from rising asset values.

Q&A: A Pivotal Time for the Fed

Tracey Manzi, CFA, *Senior Investment Strategist,* Investment Strategy

New Fed chairs don't come along often. Since 1980, only five individuals have led the Federal Reserve (Fed): Jerome Powell is currently in his second term; Janet Yellen served one term, and Alan Greenspan famously held the role for more than eighteen years. With such infrequent turnover in the Fed's top spot, markets naturally pay close attention to a new nominee—especially when the nominee brings different views than the sitting Fed chair. Kevin Warsh's nomination comes at a pivotal time. Questions about the Fed's independence have intensified, the administration is openly pressuring the central bank to lower interest rates, and the economy is undergoing meaningful structural shifts—from evolving trade policy to AI's growing influence on productivity and the labor market. Against this backdrop, understanding Warsh's policy leanings and potential impact on the Fed is critically important.

Q. What are the next steps for Warsh to become Fed chair?

A. Several procedural steps remain. The process began on March 4, when the president submitted the nomination to the Senate. The next step is a series of public hearings before the Senate Banking Committee. After the hearings, the committee will vote on whether to advance Warsh's nomination to the full Senate, where confirmation requires a simple majority. Historically, first-term Fed chair confirmations take about 44 days on average. While Warsh should be confirmed, obstacles remain. Senator Thom Tillis (R-NC) has indicated he will block Warsh's nomination until the criminal investigation involving Chair Powell is dropped. With Republicans holding a narrow 13-11 majority on the Senate Banking Committee, Tillis' stance poses a meaningful risk. Betting markets currently assign ~50% probability that Warsh is confirmed before Powell's term expires on May 15. Powell has noted he will remain as chair pro tempore if his successor is not confirmed, though that interpretation could be challenged.

Q. What do we know about Kevin Warsh's views?

A. During his tenure as a Fed Governor from 2006 to 2011, Warsh developed a reputation as an inflation hawk, often placing more weight on inflation risks than on employment concerns. Although he supported the Fed's crisis-era tools during the Great Financial Crisis, including large-scale asset purchases (quantitative easing), he later became increasingly critical of the prolonged balance sheet expansion. He has also criticized the Fed's extensive use of forward guidance, its broader communication tools, and its slow response to changing economic conditions. More recently, however, Warsh has adopted a more dovish tone. He now believes that the economy may be experiencing an AI-driven productivity boom, allowing for faster growth without triggering inflation. Some observers worry that this shift reflects political alignment with the administration. However, we believe these concerns are overstated. Warsh has long been a strong defender of Federal Reserve independence and understands the importance of maintaining public trust in the institution.

Q. What could the Fed look like under Warsh's leadership?

A. Although Warsh was a vocal critic at times during his previous Fed tenure, he never dissented—underscoring his willingness to work collaboratively. In theory, Warsh may favor a combination of lower policy rates, a smaller Fed footprint in the financial markets and a higher bar for future intervention. However, none of these changes would occur quickly in practice. Even if he leans more dovish than some of his colleagues, elevated inflation and a still solid economic backdrop make near-term rate cuts difficult to justify, especially within a committee that is more divided today than at any point in modern history. One of Warsh's more ambitious goals is reducing the Fed's balance sheet. But shifting away from the Fed's current ample-reserves framework would require significant operational adjustments that are unlikely to happen quickly. The area most likely to see quicker movement is the Fed's communication strategy. Warsh has argued for scaling back forward guidance, including the widely followed dot plot, which he views as unnecessary and occasionally counterproductive in normal economic times.

BOTTOM LINE

Kevin Warsh's nomination comes at a consequential moment for monetary policy and the financial markets. While Warsh may desire meaningful regime change at the Fed, structural constraints and a divided committee argue for gradual adjustments, rather than abrupt shifts. We expect Warsh to uphold the Fed's independence in the face of political pressure.

The Great Rotation of 2026: Broad-Based Shifts Reshape Equity Market Leadership

Matt Barry, CFA, *Senior Investment Strategist,* Investment Strategy
Mike Payne, *Investment Strategy Analyst,* Investment Strategy

The defining feature of equity markets in 2026 has been a dramatic and broad-based rotation, marking a clear departure from the narrow leadership that characterized much of the prior two years. Investors have actively repositioned portfolios in response to improving macro conditions, moderating interest rates early in the year, evolving expectations around Federal Reserve policy, and heightened geopolitical tensions. As a result, leadership has rotated away from last year's Artificial Intelligence (AI) driven winners (e.g., Technology, Communication Services) toward more defensive and cyclical segments, as areas like Consumer Staples, Energy, Materials, and small-capitalization stocks have all experienced meaningful relative strength. This rotation reflects not only a reassessment of valuation and earnings durability across sectors, but also a recalibration of investor sentiment as markets digest the implications of AI adoption, geopolitical uncertainty, and the path of monetary policy in the year ahead. Against this backdrop, sector dispersion has widened significantly, creating both pockets of opportunity and areas of caution as the market continues to rebalance across styles, factors, and market caps.

AI EUPHORIA MEETS LONGER-TERM SKEPTICISM

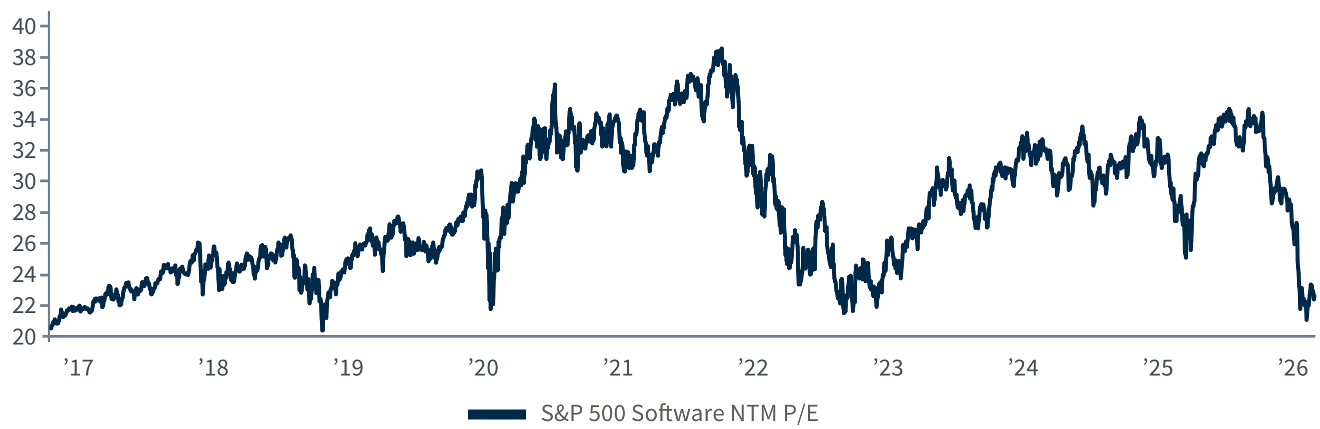
Perhaps one of the most remarkable observations from this rotation has been the stark shift in investor sentiment toward AI. Despite the fundamental supremacy story remaining in place with the Technology sector expecting 34% year-over-year earnings per share (EPS) growth in 2026 compared to only 14% for the S&P 500, the sector has underperformed the index by over 2% year-to-date.

> What the market has largely ignored, however, is AI's potential to meaningfully improve operating efficiency, expand margins, and enhance product delivery for incumbent software vendors.

Underperformance has been driven by recent declines in software stock prices that are largely tied to investor fears that rapidly advancing AI tools could erode traditional software business models, compress pricing, and reduce long-term growth prospects. New AI agents from companies such as Anthropic have triggered broad sell-offs by demonstrating the ability to replicate or automate workflows that many software providers rely on for revenue, raising concerns that demand for seat-based Software as a Service (SaaS) products may shrink or become commoditized. However, we have not seen these risks materialize thus far. What the market has largely ignored, however, is AI's potential to meaningfully improve operating efficiency, expand margins, and enhance product delivery for incumbent software vendors. Many companies are already deploying AI internally to streamline development cycles, automate support functions, and scale customer-facing capabilities at far lower incremental cost—all of which could strengthen competitive positioning rather than weaken it. This disconnect between perceived risk and the realized benefits creates an opportunity: as AI-driven productivity gains begin to show up in financial results, sentiment may recalibrate, presenting upside for investors willing to look beyond the current fear-driven narrative.

We believe recent declines across the software ecosystem are overdone at this point with the software industry trading at only 22x forward earnings estimates—the lowest level since 2018. Therefore, we remain comfortable with our overweight position in the Technology sector.

Software Trading at Lowest P/E Since 2018

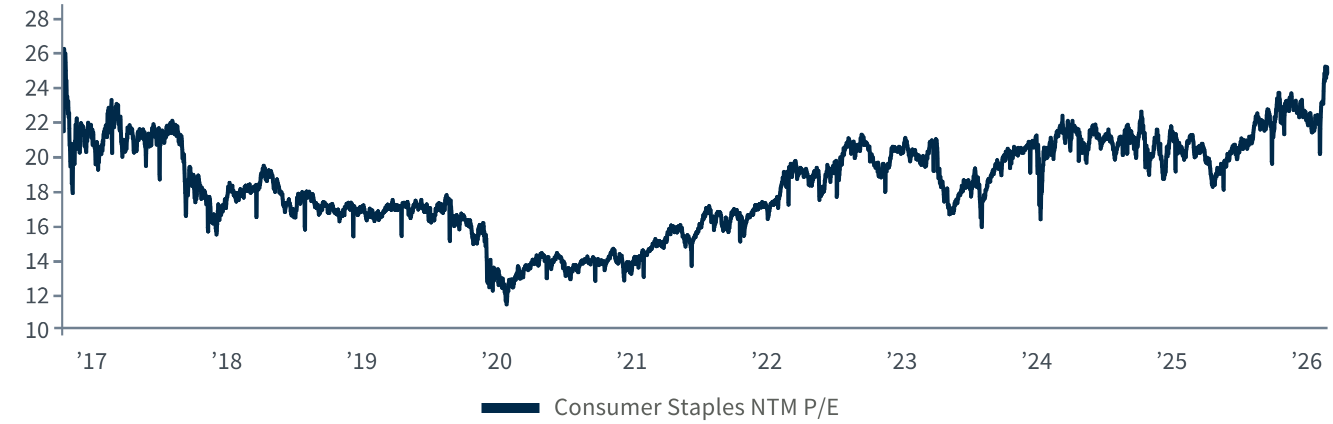


Source: FactSet, data as of 3/17/2026

THE STAPLES COMEBACK: FROM OVERLOOKED TO OVERCROWDED

The rotation has benefited formerly unloved areas of the market. In fact, the Consumer Staples sector has gained 10% year-to-date, marking the strongest start to a year for the sector over the last 30 years. A mix of weaker labor market signals combined with geopolitical uncertainty has heightened risk aversion. In response, investors have shifted into areas with predictable demand. This rotation reflects a classic de-risking pattern that historically benefits staples during periods of volatility. However, with Consumer Staples' earnings growth expected to lag the S&P 500 in both 2026 and 2027, while valuations are at the highest level since 2000, we are downgrading Consumer Staples from neutral to underweight.

Defensive Rotation Leads Staples P/E to Highest Level Since 2000



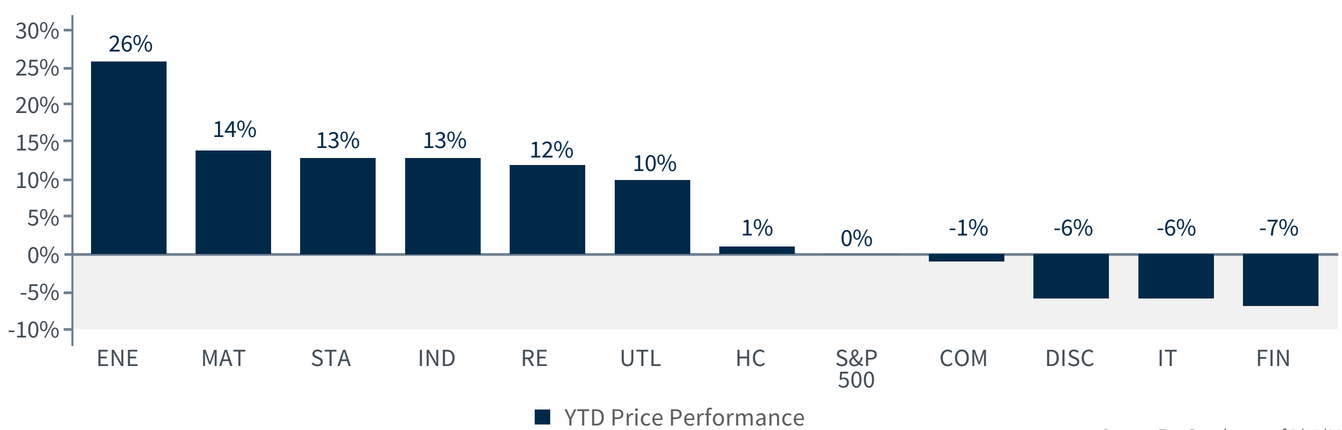
Source: FactSet, data as of 3/17/2026

ENERGY & MATERIALS OUTPERFORM ON GEOPOLITICAL PREMIUMS—BUT SUSTAINABILITY IS LIMITED

The Energy sector has been the top performer year-to-date, driven by geopolitical tensions that have pushed oil prices higher and kept them elevated (thus far).

Escalating instability in key producing regions—most notably Venezuela and Iran—has added a meaningful geopolitical risk premium to crude markets, driving energy equities higher in the early part of the year. At the same time, the Materials sector has also posted strong year-to-date gains, supported by a rebound in industrial commodity prices and tightening supply conditions. Industrial metals such as copper, aluminum, and nickel have benefited from supply deficits, infrastructure-driven demand, and a supportive macro backdrop in 2026, contributing to broad-based strength across materials stocks. However, despite this near-term performance, we remain underweight both sectors. In Energy, we believe the rally is likely to be short-lived as oil prices are expected to reset lower toward our target of $55-$60/bbl once geopolitical risk premiums fade, with structural oversupply and long-term electrification trends continuing to work against the sector’s earnings power. Similarly, in Materials, while commodity prices have firmed, the underlying drivers appear cyclical rather than durable, and the sector remains exposed to slowing global growth, and policy uncertainty. As a result, we view the recent strength in both groups as an opportunity to maintain our underweight positioning rather than chase late cycle gains.

Commodity Related Sectors Outperforming YTD



Source: FactSet, data as of 3/17/2026

> "What matters for long-term investors is ... maintaining a disciplined framework anchored in fundamentals, earnings durability, and strategic asset allocation."

SMALL CAPS OUTPERFORM, BUT RISK-REWARD APPEARS BALANCED LOOKING FORWARD

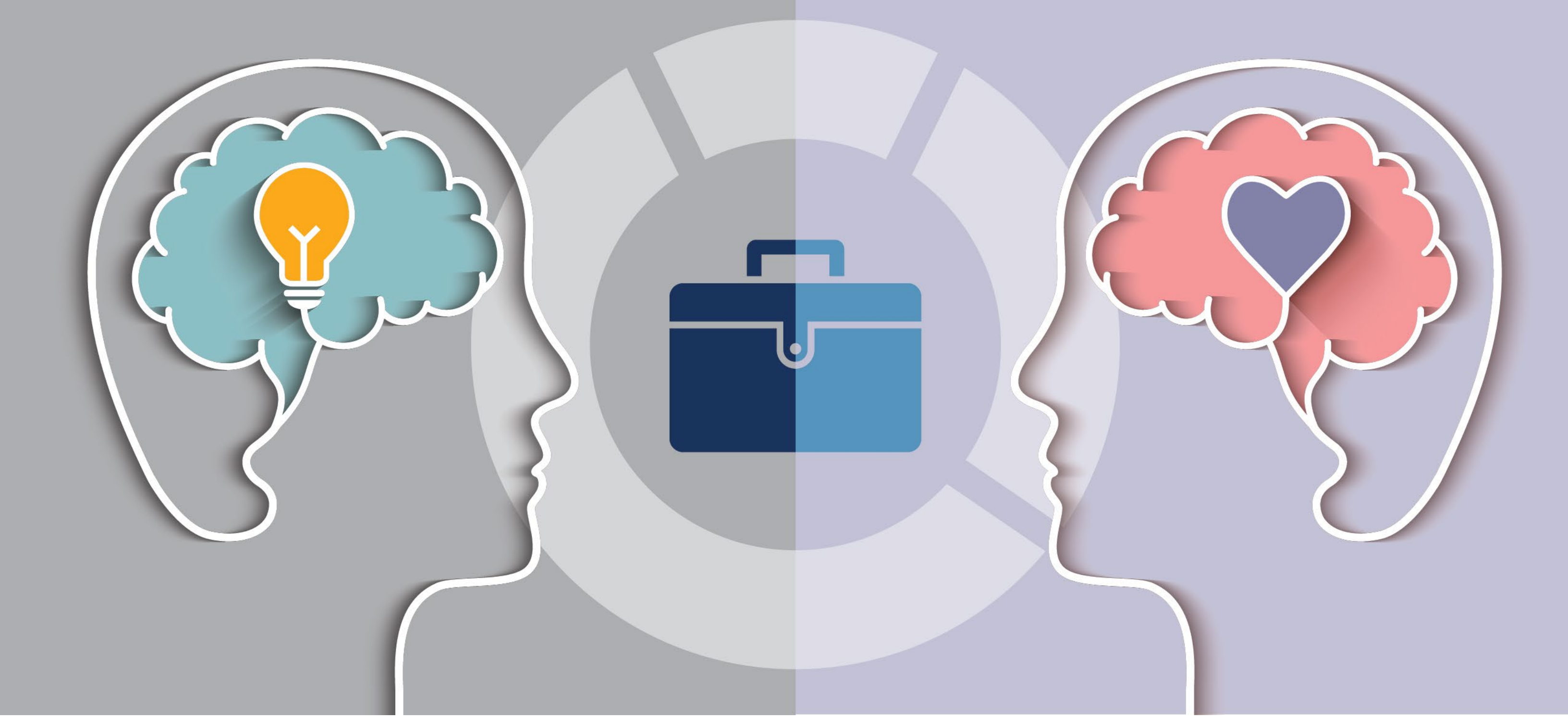
Small caps have outperformed large caps year-to-date as earnings momentum has begun to inflect higher and lower interest rates have provided a disproportionate tailwind to smaller companies, which typically carry more variable rate debt and therefore benefit more immediately from easing financial conditions. Additionally, estimates for 2027 earnings growth now favor smaller companies due to their more domestic revenue exposure and sensitivity to cyclical improvements in the US economy, further supporting recent outperformance. Despite these near-term tailwinds, we remain neutral on small caps as we believe market expectations are too optimistic on additional rate cuts throughout 2026 which could reverse some of the rate-cut-driven benefits currently supporting the group. Additionally, consensus expects only 7% net margins for small caps this year compared to nearly 15% for large caps which leaves small caps particularly vulnerable to the risk of rising input costs in the year ahead.

STAYING THE COURSE THROUGH SHIFTING LEADERSHIP

While the sharp sector rotations that have characterized 2026 may feel dramatic, they are far from unusual—equity markets routinely undergo periods where leadership shifts abruptly in response to changing macro conditions, sentiment swings, or short-term dislocations. What matters for long-term investors is not chasing these rotations after they've already played out, but maintaining a disciplined framework anchored in fundamentals, earnings durability, and strategic asset allocation. This year's movements—from the downturn in Technology to the surge in Staples, Energy, Materials, and small companies—underscore how quickly narratives can change, often before underlying fundamentals do. Staying grounded in a long-term plan allows investors to benefit from volatility rather than be whipsawed by it, ensuring that portfolio decisions reflect enduring opportunities rather than fleeting momentum. In our view, maintaining discipline—rather than reacting to every rotation—remains the clearest path to compounding wealth over time.

KEY TAKEAWAYS

- Equity leadership in 2026 has dramatically broadened. Markets have shifted away from the narrow, AI-driven leadership of the past two years toward more defensive and cyclical areas.
- AI sentiment has swung from euphoria to skepticism—creating opportunity. AI-driven efficiency gains are being overlooked, and concerns over software have not materialized.
- Defensive sectors have rallied—but may not be sustainable. Earnings fundamentals and valuation concerns lead to our underweight views on Staples, Energy, and Materials despite recent strength.
- Small-cap companies have outperformed but face a more balanced outlook ahead. Expectations for additional rate cuts appear overly optimistic, and lower margin profiles make them vulnerable, prompting a neutral stance going forward.



How Happy Is Your Portfolio? Differentiating Between Fundamentals and Investor Sentiment

Pavel Molchanov, *Senior Investment Strategist*, Investment Strategy

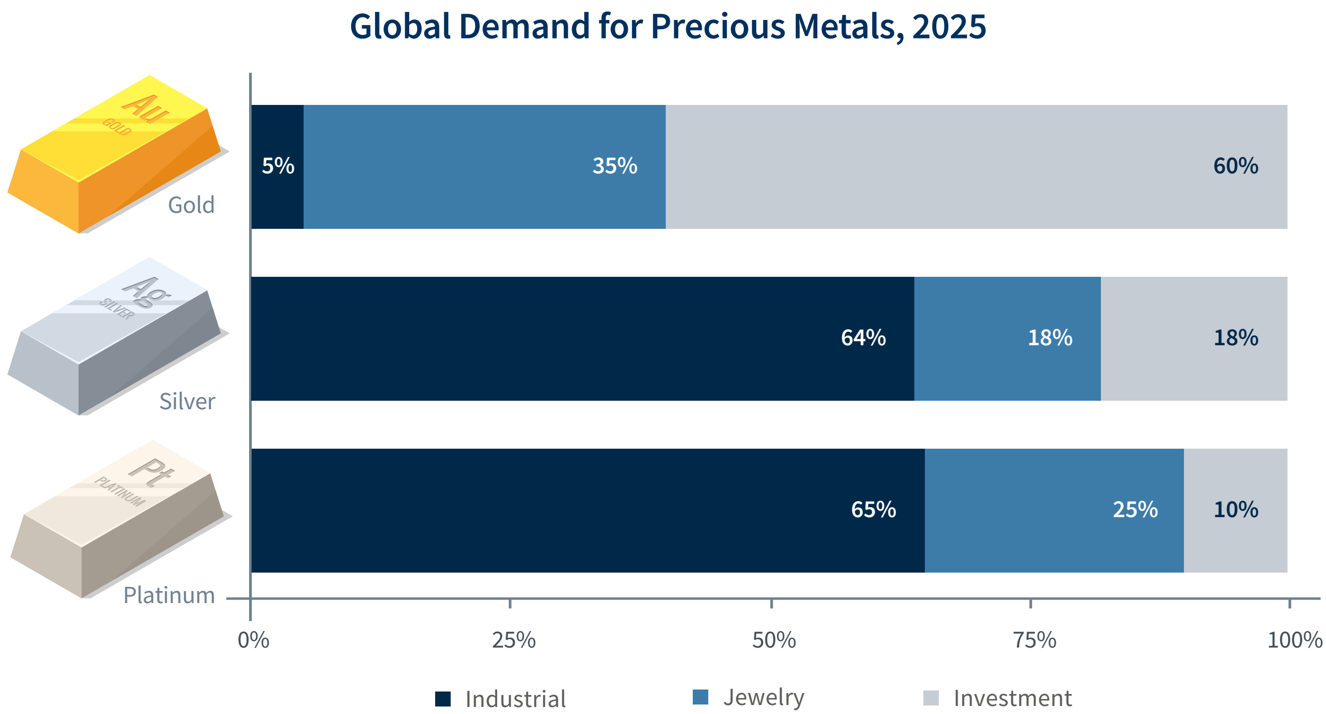
The famed economist John Maynard Keynes said almost a century ago that "markets can remain irrational longer than you can remain solvent." He was referring to the unpredictable nature of investor sentiment: an amorphous, hard-to-define concept that nonetheless plays a major role across various asset classes. As investment strategists, our approach is grounded in fundamentals, such as interest rates and corporate earnings. But at the same time, it's important to be aware that sentiment—that is to say, the market's emotional state—also influences how investments perform, especially over relatively short timeframes. As vital as fundamental analysis is, an understanding of sentiment is also useful.

MEME STOCKS: WHERE SENTIMENT SUPERSEDES FUNDAMENTALS IN THE EQUITY MARKET

Fundamental analysis of stocks centers on earnings. The standard method of valuing a stock is a price-to-earnings (P/E) ratio. When the P/E multiple is high, a stock is typically referred to as 'expensive' or 'richly valued.' This does not mean that it's necessarily a bad investment, but we typically want to see some justification for the lofty multiple, i.e., an expectation of high earnings growth in the future. For companies that have negative earnings, we can apply a revenue multiple instead. In certain sectors, other multiples are sometimes used, such as free cash flow yield in Real Estate and price-to-book value in Financials.

> Meme stocks resemble lottery tickets—it's a matter of luck rather than skill.

But what if a company has no revenue? In other words, the firm is an early-stage business that has yet to begin selling a product or service. Traditional valuation analysis isn't practical in these cases. It's possible to create estimates for many years into the future, but these are prone to error. Share prices of such companies move from day to day based in large part on how the market perceives the company. Corporate announcements (R&D milestones, M&A



Source: FactSet, data as of 3/17/2026

activity, management changes) can influence sentiment, but even when there are no headlines whatsoever, sentiment is still subject to change.

You may have come across the term meme stocks. While there is no 'official' list, the term refers to companies that, in general, 1) are on the smaller side; 2) have little to no earnings, and sometimes no revenue; and 3) are popular with day traders or momentum-oriented funds. Meme stocks are very sensitive to changes in sentiment, with share prices routinely swinging by double-digit percentages on a daily basis. A single social media post can be enough to move meme stocks. While these stocks can be found in any industry, they tend to cluster around certain innovative or high-growth themes, such as quantum computing, nuclear technology, electric vehicles, and cryptocurrencies (more on that last one later).

For our readers who may be tempted to invest in meme stocks, our message is: be careful. It's certainly possible to ride a meme stock to hefty gains—but it's also possible that any given meme stock will turn into a penny stock, or perhaps go out of business altogether. Precisely because they don't lend themselves to fundamental analysis, meme stocks resemble lottery tickets—it's a matter of luck rather than skill.

PRECIOUS METALS: ALL THAT GLITTERS CAN BE VOLATILE

Gold, silver, and platinum all posted hefty gains over the past year, but—as with all commodities—they also exhibited intense volatility. Gold is the most sentiment-driven, while silver and platinum tend to be influenced more by 'physical' supply/demand fundamentals.

Gold has a centuries-long history of being regarded as a one-of-a-kind metal, but why is that? The short answer is because that's just how society looks at it. Gold's special status in culture and the economy is ultimately a matter of sentiment rather than chemistry. Industrial applications account for a mere 5% of global gold demand, whereas 60% represents gold as an investment (e.g., stockpiles in central bank vaults). The remaining portion is jewelry. The amount of gold mined around the world barely changes from year to year, so price volatility is largely a function of the level of investor appetite for owning gold. This appetite tends to increase in times of geopolitical turbulence and/or high inflation, but it is subject to abrupt reversals, sometimes for no apparent reason.

With silver and platinum, sentiment also plays a role, but physical demand is more important. Nearly two-thirds of global silver demand is attributable to industrial end markets, including 20%

> “Gold is the most sentiment-driven, while silver and platinum tend to be influenced more by ‘physical’ supply/demand fundamentals.”

in solar panel manufacturing. In high-volume / low-margin products such as these, rapid escalation in input costs can create serious margin pressure. We are already seeing evidence of solar manufacturers starting to redesign their hardware to use copper in place of silver. Platinum is also vulnerable to commodity substitution, though to a lesser extent than silver. A key application for platinum is catalytic converters in auto engines, but because these are more highly engineered products than solar panels, redesign efforts are likely to take longer.

CRYPTOCURRENCIES: SENTIMENT ON STEROIDS

In thinking about which asset class is the most sentiment-driven, cryptocurrencies provide the prime case study. There is no fundamental underpinning to the value of Bitcoin, Ethereum, or other cryptocurrencies, with the exception of stablecoins. Trading dynamics from day to day can be extremely volatile, even more so than meme stocks or precious metals. Among the reasons for this is the fact that cryptocurrencies are typically subject to less regulation than other asset classes. Cryptocurrencies have no governing authority, such as a central bank, and various trading platforms operate under a wide range of rules.

What makes stablecoins different from other cryptocurrencies is the emphasis on maintaining a stable value, typically $1.00/unit. Stablecoins must be backed by assets—such as Treasury bills—that are low-risk and highly liquid. That said, stablecoins are not insured by the FDIC, so they should not be looked at through the same lens as a bank account. If the company that issued any given stablecoin ends up going bankrupt, it's possible to conceive a scenario where the stablecoin's value could fall below par.

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Entire mini-cultures have developed around some of the cryptocurrencies, with numerous blogs, podcasts, and conferences. Celebrities and politicians occasionally endorse certain cryptocurrencies, which can result in gains that are rapid but also fleeting. Along the same lines, a critical news story can lead to sudden selling pressure. All of this means that cryptocurrency investors need to be ready for intense volatility, at any time. Given that sentiment plays such a central role, we are unable to provide price targets or even offer directional guidance for cryptocurrencies. Remember, they are ultimately just strings of digital code.

CONCLUSION

As much as we might wish for markets to always behave rationally, the reality is very different. Investors are human beings, who can be swayed by greed, fear, and every other emotion. While no asset class is entirely immune from sentiment-fueled volatility, some types of investments are more sentiment-driven than others. In the equity market, it's meme stocks. In the commodity market, it's precious metals, especially gold. Finally, cryptocurrencies across the board are particularly susceptible to abrupt shifts in sentiment.

KEY TAKEAWAYS

- In contrast to well-established companies, meme stocks cannot be valued using traditional metrics.
- Whereas gold is heavily sentiment-driven, silver and platinum trade more on supply/demand fundamentals.
- Cryptocurrencies lack any fundamental underpinnings, making this the most sentiment-driven asset class.

Economic Snapshot

EUGENIO J. ALEMÁN, PhD
Chief Economist

Coming into 2026, the economy was supported by several key tailwinds: tax cuts and retroactive accelerated depreciation expected to boost consumer and business spending, moderating inflation, improving productivity, rising foreign direct investment, and the economic lift associated with major national events such as hosting the World Cup and celebrating America's 250th anniversary. As the year progresses, however, the pace of economic activity is likely to moderate. We expect growth to accelerate compared to 4Q25, but remain just over potential output, as the labor market has continued to cool even as unemployment remains relatively low, and policy uncertainty around tariffs has caused some businesses to delay investment decisions. Similarly, residential investment remains under pressure as high mortgage rates and rising construction costs continue to constrain housing activity. At the same time, tariff measures and higher oil prices are expected to put some upward pressure on inflation, although still-restrictive monetary policy should limit the magnitude of that increase. On the fiscal side, little progress has been made in reducing federal deficits. The ongoing geopolitical tensions have contributed to a somewhat stronger but still range-bound US dollar. Overall, policy uncertainty will continue to push firms to invest in capital to support higher growth in productivity while using less labor.

	ECONOMIC INDICATOR	COMMENTARY
FAVORABLE	BUSINESS INVESTMENT	Policy uncertainty around tariffs and global trade continues to weigh on some investment decisions. However, structural investment tied to industrial policy, reshoring, and technology remains supportive of overall capital spending.
	MANUFACTURING	The manufacturing sector is on a favorable trajectory, and with continued investment in advanced manufacturing, it is expected to support a continued gradual improvement through the year.
NEUTRAL	GROWTH	Economic growth should reaccelerate after a weak 4Q25, with growth showing the economy settling closer to its long-term trend rather than moving toward recession.
	EMPLOYMENT	The labor market has been cooling down, but we expect it to stabilize and for the unemployment rate to remain relatively stable.
	CONSUMER SPENDING	Consumer spending remains positive but continues to decelerate from the strong pace seen in most of 2025. Lower-income households are facing greater financial strain from rising prices, while higher-income consumers continue to support overall spending.
	MONETARY POLICY	The Federal Reserve has a challenging year ahead, with inflation on the way up again while the administration calls for much lower interest rates. Expect the dual mandate between inflation and employment to become unbalanced once again.
	LONG-TERM INTEREST RATES	The acceleration in inflation and the strong fiscal expansion during this year has the potential to keep interest rates high during the rest of the year.
	THE DOLLAR	Economic weakness and fiscal deficit fears have pushed the US dollar to an almost three-year low, but current global instability is supporting a recovery in the US dollar.
	REST OF THE WORLD	We continue to believe the US economy will grow faster than other developed countries, especially given its minimal exposure to the Middle East energy supply disruption.
UNFAVORABLE	HOUSING AND RESIDENTIAL CONSTRUCTION	High mortgage rates, rising construction costs, and tariffs will keep this sector of the economy in the red. Meanwhile, the low supply of homes will keep upward pressure on prices and reduce the number of potential home buyers.
	INFLATION	Inflation is expected to accelerate during the quarter as tariffs and higher oil prices unsettle an otherwise disinflationary trend. This is expected to create a very difficult tradeoff for policymakers.
	FISCAL POLICY	With an expected increase in the fiscal deficit due to higher spending, high interest rates, lower taxes and tax collections, the fiscal deficit debate will continue to keep the markets on edge.

Sector Snapshot

MIKE PAYNE
Investment Strategy Analyst

This report is intended to highlight the dynamics underlying the 11 S&P 500 sectors, with a goal of providing a timely assessment to be used in developing your personal portfolio strategy. Our time horizon for the sector weightings is not meant to be short-term oriented. Our goal is to look for trends that can be sustainable for several quarters; yet given the dynamic nature of financial markets, our opinion could change as market conditions dictate.

Most investors should seek diversity to balance risk versus reward. For this reason, even the least-favored sectors may be appropriate for portfolios seeking a more balanced equity allocation. Those investors seeking a more aggressive investment style may choose to overweight the preferred sectors and entirely avoid the least favored sectors. Investors should consult their financial advisors to formulate a strategy customized to their preferences, needs, and goals.

These recommendations will be displayed as such:

Overweight: favored areas to look for ideas, as we expect relative outperformance

Equal Weight: expect in line relative performance

Underweight: unattractive expectations relative to the other sectors; exposure might be needed for diversification

For a complete discussion of the sectors, please ask your financial advisor for a copy of *US Equity Strategy.*

	SECTOR	S&P WEIGHT	COMMENTARY
OVERWEIGHT	INFORMATION TECHNOLOGY	32%	The AI megatrend remains the preeminent driver of Technology earnings. Alongside strong demand for advanced chips, the theme is broadening into cloud computing and specialized use cases. Consensus estimates point to Technology once again having the S&P 500's fastest EPS growth in 2026, and estimate revisions continue to have an upward bias. We view the recent multiple compression as an opportunity to add exposure.
OVERWEIGHT	CONSUMER DISCRETIONARY	10%	Investor expectations for this sector in 2026 are muted, and any signs of improving fundamentals should catalyze outperformance. While the oil price spike may pressure near-term spending on large-ticket items and leisure travel, we believe this headwind will subside in 2H26.
OVERWEIGHT	HEALTH CARE	10%	Health Care is benefiting from secular trends, including an aging population and biotech innovation. While there are lingering investor concerns about federal regulatory changes, thus far those changes have been more bark than bite. Valuations are moderate by historical standards, and the sector is full of stocks with enticing dividend yields.
OVERWEIGHT	INDUSTRIALS	9%	The buildout of AI data centers and associated modernization of the electric grid are potent demand drivers for the sector. Other themes are supportive as well: tariff-fueled reshoring of supply chains, robust defense spending on both sides of the Atlantic, and benefits from the new tax law (e.g., immediate expensing). The sector's EPS growth is poised to accelerate in 2026.
EQUAL WEIGHT	FINANCIALS	13%	This is the worst-performing sector YTD, amid concerns about AI disruption and private credit. More encouragingly, there are signs that investment banking and capital markets activity will continue to strengthen in 2026. With valuations having moderated to 2x NTM price/book—down from recent highs of 2.5x—our neutral stance reflects the balanced risk/reward profile.
EQUAL WEIGHT	COMMUNICATION SERVICES	11%	While some investors look at Communication Services as an AI derivative, we prefer Technology and Industrials to play AI. Although this sector's largest companies are Big Techs that benefit from robust digital ad spend, it also includes telecom and traditional media firms, which have weaker growth profiles. For example, the traditional media space faces structural headwinds from shrinking TV audiences.
EQUAL WEIGHT	UTILITIES	2%	Amid the data center buildout, US power demand is poised to grow as much between 2025 and 2030 as in the previous 25 years. While balance sheets in the sector are highly leveraged—resulting in hefty interest-rate sensitivity—most companies in the sector have a predictable revenue model, which translates into mild credit risk. Meanwhile, as rising electric bills lead to political pushback, the sector may face even stricter regulatory scrutiny.

Continued on next page

Sector Snapshot (cont.)

	SECTOR	S&P WEIGHT	COMMENTARY
UNDERWEIGHT	CONSUMER STAPLES	5%	Despite persistent input cost risk resulting from volatile prices for a wide range of commodities, sector valuations are at the highest levels since 2000. And yet, consensus expects single-digit EPS growth in both 2026 and 2027—significantly slower than the broader market—amid sluggish demand as consumers balk at high prices on store shelves. **Accordingly, we are downgrading the sector to Underweight.**
	ENERGY	4%	Amid the US-Iran conflict and resulting Persian Gulf supply disruption, oil prices have soared to four-year highs. We would use the resulting share price gains as an opportunity to take profits. The supply disruption is transitory, whereas the longer-term outlook is for sluggish growth in global oil demand, alongside plentiful supply (both OPEC and non-OPEC). We expect WTI to fall to $55-$60/barrel by year-end.
	REAL ESTATE	2%	A mild EPS acceleration is on deck in 2026, including the benefit of lower interest rates. Commercial office space is facing structural headwinds, partially offsetting the growth from data centers, healthcare facilities, and logistics. The sector's lofty dividend yield is not enough to get us enthused.
	MATERIALS	2%	After record-setting rallies in precious metals, we look at these markets as stretched—sentiment could move them in either direction. We are more positive on industrial metals such as copper and lithium, though investor expectations are also lofty. Meanwhile, the spike in oil and international natural gas prices may pressure near-term margins for producers of plastics and chemicals.

Disclosure

All expressions of opinion reflect the judgment of the authors and are subject to change. Past performance may not be indicative of future results. There is no assurance any of the trends mentioned will continue or forecasts will occur. The performance mentioned does not include fees and charges which would reduce an investor's return. Dividends are not guaranteed and will fluctuate. Investing involves risk including the possible loss of capital. Asset allocation and diversification do not guarantee a profit nor protect against loss. Investing in certain sectors may involve additional risks and may not be appropriate for all investors.

International investing involves special risks, including currency fluctuations, different financial accounting standards, and possible political and economic volatility. Investing in emerging and frontier markets can be riskier than investing in well-established foreign markets.

Investing in small- and mid-cap stocks generally involves greater risks, and therefore, may not be appropriate for every investor.

There is an inverse relationship between interest rate movements and fixed income prices. Generally, when interest rates rise, fixed income prices fall and when interest rates fall, fixed income prices rise.

US government bonds and Treasury bills are guaranteed by the US government and, if held to maturity, offer a fixed rate of return and guaranteed principal value. US government bonds are issued and guaranteed as to the timely payment of principal and interest by the federal government. Treasury bills are certificates reflecting short-term obligations of the US government.

While interest on municipal bonds is generally exempt from federal income tax, they may be subject to the federal alternative minimum tax, or state or local taxes. In addition, certain municipal bonds (such as Build America Bonds) are issued without a federal tax exemption, which subjects the related interest income to federal income tax. Municipal bonds may be subject to capital gains taxes if sold or redeemed at a profit.

If bonds are sold prior to maturity, the proceeds may be more or less than original cost. A credit rating of a security is not a recommendation to buy, sell or hold securities and may be subject to review, revisions, suspension, reduction or withdrawal at any time by the assigning rating agency.

Commodities and currencies are generally considered speculative because of the significant potential for investment loss. They are volatile investments and should only form a small part of a diversified portfolio. Markets for precious metals and other commodities are likely to be volatile and there may be sharp price fluctuations even during periods when prices overall are rising.

Investing in REITs can be subject to declines in the value of real estate. Economic conditions, property taxes, tax laws and interest rates all present potential risks to real estate investments.

High-yield bonds are not suitable for all investors. The risk of default may increase due to changes in the issuer's credit quality. Price changes may occur due to changes in interest rates and the liquidity of the bond. When appropriate, these bonds should only comprise a modest portion of your portfolio.

Beta compares volatility of a security with an index. Alpha is a measure of performance on a risk-adjusted basis.

The process of rebalancing may result in tax consequences.

Alternative investments involve specific risks that may be greater than those associated with traditional investments and may be offered only to clients who meet specific suitability requirements, including minimum net worth

Disclosure (cont.)

tests. Investors should consider the special risks with alternative investments including limited liquidity, tax considerations, incentive fee structures, potentially speculative investment strategies, and different regulatory and reporting requirements. Investors should only invest in hedge funds, managed futures, distressed credit or other similar strategies if they do not require a liquid investment and can bear the risk of substantial losses. There can be no assurance that any investment will meet its performance objectives or that substantial losses will be avoided.

The companies engaged in business related to a specific sector are subject to fierce competition and their products and services may be subject to rapid obsolescence. Investing in the technology sector is not suitable for all investors.

The indexes mentioned are unmanaged and an investment cannot be made directly into them. The Dow Jones Industrial Average is an unmanaged index of 30 widely held securities. The NASDAQ Composite Index is an unmanaged index of all stocks traded on the NASDAQ over-the-counter market. The S&P 500 is an unmanaged index of 500 widely held securities. The Shanghai Composite Index tracks the daily price performance of all A-shares and B-shares listed on the Shanghai Stock Exchange.

The VIX is the Chicago Board Options Exchange (CBOE) Volatility Index, which shows the market's expectation of 30-day volatility.

The MSCI Emerging Markets Index is used to measure the financial performance of companies in fast-growing economies around the world. The MSCI China A Index measures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges. The MSCI Pacific Index is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of the developed markets in the Pacific region. The MSCI USA Index is designed to measure the performance of the large- and mid-cap segments of the US market. The MSCI Europe index is a European equity index which tracks the return of stocks within 15 European developed markets.

The Bloomberg US Aggregate Bond Index is a broad-based flagship benchmark that measures the investment grade, US dollar-denominated, fixed-rate taxable bond market.

The Bloomberg US Treasury Index measures the performance of fixed-rate, nominal debt issued by the US Treasury and denominated in US dollars. It is a benchmark for the US Treasury market, excluding Treasury bills (which are covered by a separate index) and certain special issues according to Bloomberg.

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