



“A Q1 2026 Market Letter”

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As we approach the end of Q1, the investment landscape has already undergone a meaningful shift. The year began with optimism carried over from late 2025, supported by expectations of moderating inflation, multiple Federal Reserve rate cuts, and continued strength in artificial intelligence-driven growth. That optimism has since been tested. What has emerged is a market defined not by continuation, but by recalibration. From my perspective, this transition is both expected and constructive. Markets function most effectively when expectations are challenged and repriced. The first quarter of 2026 has done precisely that, forcing investors to reconcile narratives with reality across inflation, policy, geopolitics, and technology.

Market Performance: A Measured but Meaningful Pullback

The most immediate evidence of this recalibration is visible in equity market performance. After reaching all-time highs in January, U.S. equities have declined steadily through March.

As of late March 2026:

- The S&P 500 is down approximately 4.2 percent year-to-date
- The Dow Jones Industrial Average is down approximately 4.0 percent
- The Nasdaq Composite has declined approximately 6.4 percent
- The Russell 2000 is modestly positive at approximately +0.9 percent year-to-date

Importantly, this follows a sharp multi-week decline. Over a recent four-week stretch, the Dow fell 8.2 percent, while the S&P 500 declined 5.8 percent, marking one of the most persistent drawdowns since early 2023. The S&P 500 reached an all-time high near 7,000 in January 2026 before retracing lower into the mid-6,500–6,800 range. This context matters. The market has not collapsed; it has repriced. The distinction is critical. A collapse reflects systemic stress. A repricing reflects changing assumptions.

The nature of the pullback has also been instructive. Losses have been concentrated in large-cap growth and technology sectors, particularly those tied to artificial intelligence expectations. Market breadth has been uneven, with periods where the broader market held up better than index-level performance suggests.

In practical terms, this is a transition from multiple expansion to multiple compression.

Inflation and the Federal Reserve: A Narrow Policy Path

Inflation has moderated but remains unresolved. Recent data places headline inflation in the 2.7 to 3.1 percent range, close to but not fully aligned with the Federal Reserve’s 2 percent target.



The composition of inflation remains the challenge. Services inflation continues to run above trend, housing costs remain elevated, and wage growth, while slowing, is still inconsistent with long-term price stability.

The Federal Reserve has responded by maintaining a cautious stance. Expectations entering 2026 called for several rate cuts. Instead, the Fed has signaled a slower and more conditional approach.

At the same time, economic growth has not materially deteriorated. Forecasts for U.S. GDP growth in 2026 remain around 2.0 to 2.5 percent, suggesting continued expansion rather than contraction.

This creates a complex policy environment. The Fed is balancing three competing realities:

1. Inflation is declining but not defeated
2. Growth is slowing but not weak
3. Financial conditions are tightening but not restrictive enough to ensure disinflation

Complicating matters further, recent geopolitical developments have introduced new inflationary pressures. Rising oil prices, driven by conflict in the Middle East, have begun to filter through to broader economic indicators, contributing to slower business activity and higher input costs. The result is a policy path with limited margin for error. Markets have begun to reflect this through higher volatility and increased sensitivity to data.

The Iran Conflict and Energy Markets: Inflation Reintroduced

The escalation of conflict involving Iran has been the most significant macro development of the quarter. Its primary transmission mechanism has been energy markets.

Oil prices have surged, with Brent crude exceeding \$104 per barrel and U.S. crude approaching the low \$90s during recent spikes. This represents a material shift. Energy had largely faded as a market driver in recent years. It has now re-emerged as a central variable.

The implications are broad:

- Higher fuel costs reduce consumer purchasing power
- Input costs increase for businesses across industries
- Inflation expectations become less anchored
- Central bank policy becomes more constrained

Markets have responded accordingly. Equity declines have often coincided with oil price spikes and escalations in geopolitical tension. The key risk is not simply high oil prices, but volatile oil prices. Stability allows markets to adjust. Volatility introduces uncertainty, which raises risk premiums and reduces confidence.



Tariffs and Trade: Structural Inflation Pressures

Trade policy has quietly reasserted itself as a market driver. Tariffs and shifting trade agreements are contributing to a broader restructuring of global supply chains.

The current environment is defined less by globalization and more by regionalization. Companies are increasingly prioritizing resilience over efficiency, leading to:

- Diversified supply chains
- Increased domestic production
- Higher capital expenditures

While these changes reduce geopolitical risk, they also introduce structural cost increases. Over time, this can contribute to persistent inflation.

Markets are still in the process of incorporating these effects. Unlike interest rates or earnings, which are measured quarterly, supply chain shifts unfold over years. However, their impact on margins and pricing power is significant. Tariffs function as both economic and strategic tools. Economically, they raise costs. Strategically, they reflect a shift toward national prioritization of key industries. For investors, the implication is clear: cost structures are becoming more complex and less predictable.

Artificial Intelligence: From Narrative to Accountability

Artificial intelligence remains the most important long-term driver in markets today. Capital investment in AI infrastructure has accelerated significantly, with major firms committing tens to hundreds of billions of dollars toward data centers, semiconductors, and energy.

However, the market narrative is evolving. Earlier phases of the AI cycle were driven by discovery and enthusiasm. The current phase is increasingly focused on return on investment. Concerns have emerged around the scale of capital expenditures required to support AI growth. These investments, while necessary, are compressing margins in the near term and delaying profitability. Recent market behavior reflects this shift. Technology stocks, particularly those most closely tied to AI infrastructure, have led the market's decline. The Nasdaq's 6.4 percent year-to-date drop underscores this sensitivity.

At the same time, the long-term opportunity remains substantial. AI has the potential to drive productivity gains across industries, lower costs, and create new revenue streams. The key distinction is timing. Markets initially priced AI as an immediate earnings driver. Increasingly, it is being recognized as a multi-year investment cycle.

Market Structure and Liquidity: Beneath the Surface

While headline indices have declined modestly, underlying market conditions suggest tighter financial environments.



The Russell 2000's volatility and recent correction highlight the challenges facing smaller companies. These firms are more sensitive to borrowing costs and credit availability.

Higher interest rates have increased the cost of capital, particularly for companies with weaker balance sheets. Credit spreads have widened, and access to financing has become more selective. Liquidity is no longer abundant. This shift has important implications. Markets are moving away from a regime where capital is broadly available toward one where it is allocated more selectively. This favors companies with strong fundamentals and penalizes those reliant on external financing.

Risks and Opportunities for 2026

The remainder of 2026 will be shaped by a combination of policy, geopolitical, and structural factors.

Key risks include:

- Federal Reserve policy miscalculation
- Sustained elevation in oil prices
- Escalation of geopolitical conflict
- Valuation compression in technology and AI sectors

At the same time, several supportive factors remain:

- Continued economic growth in the 2 percent range
- Strong corporate balance sheets among large-cap firms
- Ongoing technological innovation
- Flexibility in monetary policy should conditions deteriorate

Final Thoughts

Growth remains important, but it must be supported by earnings. Innovation remains valuable, but it must translate into returns. Liquidity remains necessary, but it must be deployed strategically.

Diversification should not be viewed as passive protection, but as active positioning across a range of outcomes.

The objective is not to predict market direction with precision, but to build portfolios that can perform across varying scenarios.

The first quarter of 2026 has been defined by recalibration. Markets have adjusted to new information regarding inflation, monetary policy, geopolitical risk, and technological investment.

The transition from optimism to discipline is a necessary phase in any cycle. It creates volatility, but it also creates opportunity.



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