

Q1 2026 Market Commentary

When we said at the end of our last report that in 2026 markets may well have to suffer bouts of politically inspired disruption, we didn't quite have in mind that it might transpire so soon and in such a dramatic way. Nonetheless, the quarter just ended was, yet again, a tale of (almost) two halves.

January began confidently as investors envisaged a year supported by resilient economic fundamentals and a generally benign interest rate outlook. President Trump's mini coup in Venezuela in January didn't seem to be taken as having much significance whereas the Supreme Court's rejection of the means by which he had justified his so-called "Liberation-Day" tariffs was cheered. Moreover, corporate earnings globally seemed set for another good year, aided by the enormous amount of spending on artificial intelligence (AI) related data centre investment.

However, in February, investors began to reappraise who would be the winners and losers in the great AI boom. Software companies came under particular scrutiny as some analysts began to argue that AI would destroy the Software as a Service (SaaS) model that had supported much of their expansion over recent years. This view also had an impact in fixed income markets as many SaaS-type companies had raised capital via the private credit (PC) market based on their attractive steady cash-flow characteristics.

The concern rose about whether such attractive characteristics would endure once AI began to provide a simpler, more cost-effective alternative and whether that would undermine the credit worthiness of many of the illiquid bonds that had been issued by software companies to private credit investment vehicles. The bankruptcy of a couple of PC investments led to the gating of funds that had invested in them and rising fears of contagion to public markets.

As a result, the share prices of many software companies fell sharply. Though they were not as badly hit, many of the other large technology names in the US were sold off as investors queried the extent to which their enormous capital expenditure plans would actually generate attractive long-term returns.

And then came March. President Trump, emboldened by his quick success in Venezuela and encouraged by the Israeli government, decided that his attempts to force Iran to bow to his will were going nowhere and that he needed to pursue a much more aggressive approach. Thus, in collaboration with Israel he launched massive military strikes on Iran, immediately killing many of the Islamic Republic's key leaders. Oil and other energy prices surged but, encouraged by the belief that the conflict would be short-lived, equity and bond markets remained relatively calm. However, as the days wore on and Iran responded by attacking the energy infrastructure of several regional allies of the US, the perception that this conflict may have longer-term inflationary implications grew. The investment world became preoccupied with the Strait of Hormuz, the narrow waterway through which a large proportion of the world's oil, LNG and, indeed grain, is transported.

With the falls seen in March, the result for the quarter was a modestly negative one for most equity markets. Growth stocks underperformed value, largely due to the setback for software companies and other technology stocks in the US. The best performing large equity market was Japan, helped by the election victory of the LDP led by pro-growth prime minister, Sanae Takaichi.

Not surprisingly, energy stocks were the star performers, accompanied by defensive stocks such as those in the Healthcare sector. Interest-rate sensitive stocks such as financials suffered as perceptions of the likely path of interest rates changed.

Fixed interest markets also produced negative returns with UK gilts being the laggards as the outlook for inflation and interest rates changed due to the conflict in the Gulf. US Treasuries fared better than many others, partly due to the US's lower dependence on imported energy.

Crude Oil Prices - Year-to-Date



Source: U.S. Energy Information Administration via FRED®



In currencies, the US Dollar recovered some of the ground which it had lost earlier in the period. Elsewhere, oil led the way in a strong commodities performance with the main exceptions were precious metals such as gold and silver which gave up a significant portion of their earlier gains. For those folks invested in cryptocurrencies, there was no real respite from the downward pressure that they have been under for the past six months, despite some potentially significant progress on the regulatory front in the US.

As events unfolded during March, we took the view that the conflict in the Gulf was not something that we could usefully analyse on a short-term basis.

Instead, we have focussed on the extent to which it was likely to disrupt the relatively benign investment background that we had talked about in our last report (i.e. broadening earnings growth, corporate and fiscal spending, positive global growth and an easing monetary backdrop). In the meantime, we remained comfortable with the cash buffer we have had in portfolios, though we did take the opportunity to deploy new money on days when markets were weak. However, in our Balanced and Growth portfolios we used the spike in the price of oil to sell our position in the Brent ETC, which we have held for some time and which has been a strong contributor from both a profit and diversification point of view.

Outlook

The immediate outlook for markets is, clearly, going to be driven by events in the Gulf. As we write this, the US and Iran are trying to re-establish talks before the two-week ceasefire they had agreed expires. The key for markets is how long the conflict lasts. An ongoing effect on oil supplies around the globe will increase concerns that inflationary pressures will build, leaving central banks to decide whether to defer previously hoped-for rate cuts or even raise them. Of course, a significant, sustained, rise in the cost of fuel at the pumps will also have an effect on consumer confidence and reduce disposable income, which would act to constrain growth. Thus, it is possible that central banks will seek to avoid a tightening of policy unless they are sure that there will be an ongoing rise in inflationary pressure.

However, though both sides of the conflict are talking and acting tough, there are reasons to believe that both sides have incentives to come to some sort of deal. The Iranians know that militarily they have no real chance of winning a sustained war so, for them, staying in power domestically is probably the main objective.

Indeed, if they are made to believe that this is not possible, it would seem likely that they might be prepared to take more a more destructive course. Their key allies, China, also have an incentive to ensure that the conflict does not last too long, not least because China is the destination for the largest single share of oil exiting the Straits of Hormuz. Despite all his bluster, President Trump is aware that a prolonged conflict will lead to further pain for the US consumer, particularly at the start of the summer driving season. This would be difficult for him at any point, but the US is just over six months away from crucial mid-term elections, in which Trump's Republican Party risks the loss of the House of Representatives. Affordability has become a key factor in US politics and with Trump's popularity at low levels, he is under pressure from many sides to explain why he has embroiled the US in another foreign war with the consequence being felt by US voters.

The consequence of a poor showing in the Mid-terms would mean that the President would face a much tougher time trying to fulfil the remaining policy actions he has set his heart on. Therefore, it is widely expected that Trump will seek to find an "off-ramp", while continuing to claim that he has brought the Iranian Regime to an end. He will, no doubt claim all the credit and seek to deflect criticism of his actions by criticising others (e.g. the UK and NATO) for not supporting his war.

Though there remains a risk that Israel's objectives do not align with those of Mr Trump, it seems likely that pressure will be put on them not to put any resolution to the conflict at risk. A resolution would then allow markets to re-focus on the fundamentals. Initially at least, this would most likely result in a rally. Even though there has been some significant damage to energy infrastructure in the region, it seems likely that as part of any deal, the Iranians would be able to sell some oil into international markets in order to help offset some of the production lost during the conflict. Though there has also been damage to LNG facilities, suggesting that energy prices may not fall back to their lowest pre-conflict level, a fall back to the \$70 per barrel level for Brent Crude might be enough to calm some of the inflation fears and allow investors to focus on other things.

Included in those other things will be the outlook for private credit and the risks involved. Several funds have recently announced that they will "gate" redemptions, however, there have also been new funds announced who are allowing an amount of money to be withdrawn (albeit that this is effectively pre-planned gating!) as they argue there is value emerging in the space.



One important event which was subsumed by geopolitics was the announcement of Kevin Warsh as Trump's nominee to take over as Chair of the Federal Reserve when Jerome Powell steps down in May. Warsh has strong credentials as an inflation hawk but his views on the way the Fed should manage its balance sheet may be the strongest clue as to how he might like to see US monetary policy develop. His confirmation hearings are due to take place soon and we will, no doubt, see more focus on the new Fed head in the second half of the year.

On a different political front, it is worth noting the result (post quarter-end) of the Hungarian election which saw Viktor Orbán defeated, bringing an end to his 16-year, pro Putin (and Trump) reign. Aside from the benefit to democracy and government integrity in Hungary, this has the potential to be a very significant influence on the way that the European Union operates versus Russia and also makes NATO's support for Ukraine stronger.

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Strategy

In summary, we are hopeful that the Iran conflict will move into a diplomatic phase, allowing markets to settle. If that happens, we believe that interest rate expectations will revert to anticipating cuts in the US and UK, and that interest rate curves will once again steepen. This will give a more encouraging outlook for growth and for company profits. Aside from the risks relating to domestic politics and e.g. private credit, there is, of course the possibility that the disruption to economies and the inflation outlook from the conflict linger for longer and act as a headwind for markets for the remainder of the year. Nonetheless, while recognising those risks, we feel comfortable with our generally positive stance and believe that there is more value on show now than at the end of 2025. We have well-diversified portfolios, with cash available to deploy when we see opportunities.

Commentary as of 13 April 2026



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