

Q2 2026 Outlook

April 1st, 2026

Economy: Economic growth appeared to be moderating, but still healthy, in Q1 before geopolitical turmoil towards the end of the quarter raised serious questions about the economy's ability to overcome the supply shock created by surging oil prices.

- Projections from the Atlanta Fed GDPNow model currently call for Q1 real GDP growth of 1.9%, with the estimate steadily declining as a result of economic data released over the past six weeks. These tempered growth expectations come on the heels of a weak Q4 report showing 0.7% growth after the prior two quarters came in at 3.7% and 4.4%. This data shows the growth trend weakening even before the US invaded Iran, upending the flow of oil from the Middle East to the rest of the world and drastically increasing global input costs. We share concerns that these inflationary impacts will drive up prices generally, and pain at the pump and more expensive essentials could crowd out other spending and further slow the economy. However, the reality is that this situation could resolve quickly and disinflation and moderate growth could resume immediately, making longer term economic impacts nearly impossible to predict. The uncertainty and lack of predictability increase risk premiums and shake the confidence of both consumers and business leaders alike.
- Unfortunately, these inflationary impacts do nothing but exacerbate issues related to the "K-shaped" nature of the US economy that we discussed last quarter. Higher priced essential items degrade the quality of life and impact discretionary spending far more for those that live paycheck to paycheck and don't have the luxury of inflating assets that can offset the decline in spending power. This is a dynamic to watch closely as more and more of the workforce end up in this position with technological impacts eliminating some higher-paying, white-collar jobs. We suspect the economy will adapt to create new high paying jobs of a different kind, but some pain may have to be endured as the economy and job market adjusts. Fortunately, jobs data still shows a fairly healthy balance and no significant deterioration of the overall labor market.
- We monitor both public and private markets closely for the signals they can give on the economy as a whole. Liquidity and efficiency in private markets is still not at the level that we would like to see. Price discovery continues to be challenging in some cases, and bid-ask spreads remain wide and volatile. The new signal that has come this past quarter has

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been from the private credit market. Extremely high valuation multiples during the pandemic-driven zero interest rate environment seen four to five years ago are now becoming problematic as private credit lenders issued what they felt at the time were low loan-to-value loans that have now turned into un-refinanceable, low debt service coverage loans driven by a collapse in valuation multiples and higher interest rates. Defaults have begun to tick up, but concerns over defaults accelerating have caused capital to leave that space in a rapid fashion. Funds cannot meet redemption requests and investors are becoming increasingly concerned. The question of the day is whether or not this could turn into a "contagion" situation as we saw in the Great Financial Crisis. Fortunately, the size of the private credit market is much smaller than the mortgage market that triggered the GFC, potentially mitigating this contagion risk. Further, on the surface it appears the securitization and prolific use of derivatives for speculation is far lower than it was in that mortgage market. That being said, we are aware of some use of derivatives and unique structures in this space that could create surprises. The bigger risk is that defaults on these loans create a larger freeze in the extension of credit throughout the economy, triggering a down leg in the business cycle and an economic contraction.

Stocks: The major indices continued to chop sideways most of Q1, as they had in Q4 of 2025, before the attacks on Iran triggered a surge in oil prices that caused the indices to resolve lower and end the quarter in a corrective mode.

- The S&P 500 ended the quarter at 6,529, down about 4.6% year-to-date. The downward volatility was broad as what had been healthy rotation during the sideways chop turned into a downtrend that spared few sectors. Energy was a bright spot driven by higher crude prices, but most other sectors fell into quarter end. This was a discouraging development that brought with it deterioration in Hollencrest's stock market indicators, signaling warnings to raise cash, which we did. We remain hedged with the majority of our remaining target equity exposure and are looking for more oversold conditions or a confirmed rally to shift positioning more aggressively.
- On the bright side, valuation has improved substantially. The S&P 500 approached a 23x P/E multiple at its highest point. Through this sideways, and now down, correction, earnings expectations have continued to grow. That continued growth combined with two quarters of no meaningful price gains lead to that multiple declining to a level closer to 19x at its recent low. This is a setup that could allow a new uptrend to start without concerns of immediate overvaluation and the related caution required. With geopolitical issues resolved, we could end up right back on track to hit our earlier end-of-year S&P target of 7,500-7,750.

Bonds and Rates: Rates had been rangebound for a number of months prior to the surge in oil prices igniting inflation fears that drove rates higher at the end of the quarter.

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- The 10-year Treasury's yield ended the quarter at 4.32%, up about 37 bps from one month prior. Looking back to the start of the year, its yield is up only about 16 bps, however recent action showed a change in trend that could result in higher rates going forward. We still believe the 10-year's yield should stay in a trading range of 4% to 4.5% unless inflation truly takes hold and sends the yield toward 5%. This would be a bad outcome and could drive a decline in economic growth, however, it could also result in yields finally becoming attractive enough to reallocate towards fixed income.
- The short end of the curve, particularly the 2-year Treasury, showed significantly more relative volatility. At the start of the year, debates were more focused on how much more the Fed could cut and how much lower short-term yields could fall. Instead, shorter-term inflation expectations have caused the 2-year's yield to spike from 3.38% to nearly 4% in less than a month's time. Now debates are more focused on if the Fed will have to hike later this year to contain inflation. We expect no action from the Fed as our base case.
- Credit spreads have been remarkably stable considering what is going on in the world and in the private credit markets. While there has been some spread widening, the move does not reflect any sort of distress and is still far from actionable in our view. As private credit issues proliferate and more defaults in that market are reported, we would expect further widening. The level of this widening will indicate whether or not contagion from private credit could take hold.

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