

2026 Challenges: of Oil and Semiconductors

Roughly ten weeks into 2026, the U.S. equity markets are essentially where they started. The S&P 500 index is down 1.2% as of Wednesday, March 11th. The seeming quiet in the stock market is certainly not due to a lack of noteworthy events so far this year.

On January 3rd, the U.S. military seized Nicolás Maduro, President of Venezuela and his wife from Caracas and transported them to New York to stand trial on narco-terrorism, drug and weapons charges. While Venezuela has significant oil reserves, the removal of Maduro has had no material impact on the price of oil. It will be years before the necessary infrastructure can be built to increase oil production.

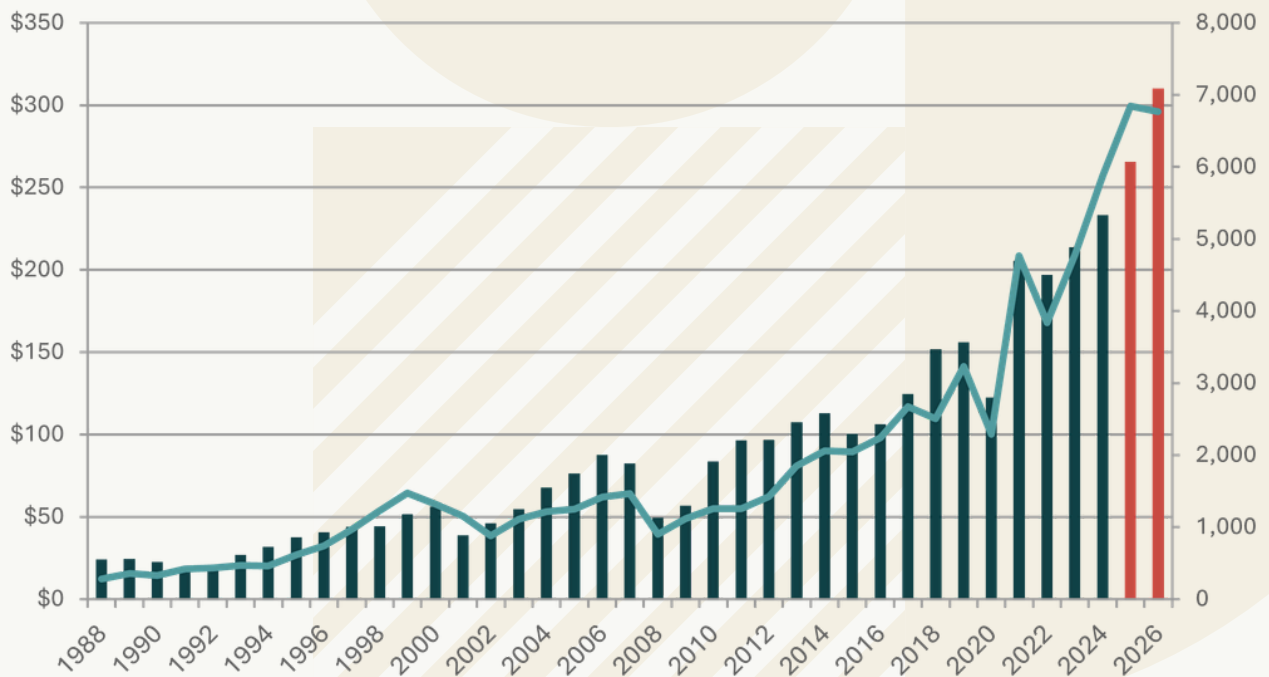
On February 20th the Supreme Court ruled that the Trump administration does not have authority under the International Emergency Economic Powers Act to enact tariffs. The administration terminated the so-called reciprocal tariffs on February 24th and issued a new 10% global tariff under section 122 of the Trade Act of 1974 which allows temporary measures for balance-of-payment concerns. As a result, the estimated cost of tariffs for the average household was cut in half, resulting in a \$700 additional annual expense. The ruling has potential to have a positive impact on inflation as the year progresses.

On February 27th U.S. and Israeli forces launched a pre-emptive attack on Iran targeting leadership

and military infrastructure. The strikes killed Ayatollah Ali Khamenei along with high-ranking officials. Importantly for the global economy, approximately a quarter of the world's daily oil consumption is transported through the Strait of Hormuz which passes along the Iranian coast and is only 21 miles wide at its narrowest point. Shipping traffic through the Strait has halted since the conflict began. Consequently, the price of oil has jumped more than 50%. The Middle East has become a major shipping and transportation hub, not just of oil. A lengthy shutdown of transport will have an impact on inflation and supply chains.

Meanwhile, investors continue to struggle this year with concerns

S&P 500 PRICE PERFORMANCE VS CORPORATE EARNINGS



around the health of the private credit industry and the competing disruptive risks and financial rewards of emerging AI technologies. Leading private asset management companies such as Apollo Global, KKR, and Blue Owl Capital are down 25%, 29% and 35% respectively. The iShares Software ETF (IGV) is down 19% this year.

It should not be a surprise that the best performing sectors are defensive in nature. Of course, energy is the best performing, up 26% due to the conflict in the Middle East. Consumer staples, which include food and beverage companies, are up 10%, while industrials are up 9% as are materials and utilities.

Despite the geopolitical and economic uncertainty, the U.S. equity markets have been resilient. We are encouraged that despite the many challenges at the start of 2026, most of our positions are positive so far.

For our market outlook, we are paying more attention to economic fundamentals than geopolitical concerns. The US economy has cooled. Although the rate of inflation remains elevated at 2.4%, it has been stable. The job

market has weakened but not enough to be alarming. The likelihood of a recession in 2026 is low, in our opinion. We do not anticipate a significant change in interest rates this year unless unemployment accelerates and inflation comes in lower than expected. If the war in Iran lasts more than several weeks and tariffs remain, inflation is a concern.

Our North Star is corporate earnings. Wall Street analysts continue to forecast accelerating earnings growth in 2026 over last year. The combined earnings for all the companies in the S&P 500 is expected to reach \$310.24, representing spectacular 17% growth from \$265.41 in 2025. If earnings can meet these expectations, we expect to see positive returns for U.S. equities this year.

Generally, we discount both geopolitical and political events on the performance of the equity and fixed income markets. Events have a significant impact on our perception of the state of the world; the economic consequences are considerably less. We counsel clients to view investment decisions through the lens of earnings and growth.

Any conflict involving Taiwan and China would be a different story, however. While the market has taken Russia's invasion of Ukraine or Trump's tariff policy or our actions in Venezuela and Iran in stride, any disruption in Taiwan would have a profound deleterious impact on the global economy.

Recently, there seems to be a greater appetite for unilateral expansionist adventures from world powers. It is certain that Chairman Xi has observed the global responses to Putin's incursion into Ukraine and our actions in both Venezuela and Iran.

The importance of Taiwan to the global economy is hard to understate. Oil is the economic fuel of the past. The importance of oil in the global economy has already been replaced by advanced semiconductors. Taiwan produces more than 60% of the semiconductors consumed worldwide and more than 90% of the advanced chips. Of the advanced semiconductors, with etching of less than 10 nanometers, the U.S. manufactures exactly 0%. The hope is that we can produce 14% of the advanced chips by 2032.