



1st Quarter 2026

Vanderbilt Avenue Asset Management (VAAM) forecasts a slowdown in economic growth as uncertainties grow. For some time, Vanderbilt has highlighted geopolitics amongst the uncertainties facing the investment markets. The Middle East war has brought this uncertainty front and center. There are at least two major issues: how long the war lasts and what Iran looks like after hostilities cease. Vanderbilt thinks the war's duration will be resolved sooner rather than later. It appears there are two extremes as to what the political situation in Iran will look like. One scenario has the current regime surviving in some form. This would result in continuing uncertainty and having the regime resuming rearming at some point. The other extreme would result in a more moderate leadership that would focus on peaceful coexistence and development of their economy. It is difficult at this point to accurately forecast which of these extremes (or somewhere in between) is the most likely. Another major issue is how the energy infrastructure in the region fares (e.g. Saudi oil production and refining, Qatar natural gas production and LNG exports, and the ability to transit ships through the Hormuz Strait). Qatar's gas infrastructure has already had damage that will take several years to rebuild. The various asset classes have initially responded to these events in different ways: stocks have been somewhat more resilient than expected, perhaps discounting the war as a short-term event, while the bond market has seen rates rise due to the potential inflationary impact from oil price increases. Commodities such as oil, have risen as expected while gold has declined in price (rather than rising due to safe haven buying) perhaps reflecting that hostilities will be a short-term event, and currencies have seen the US dollar strengthen due to safe haven buying. If the war is resolved sooner rather than later, oil prices should adjust by declining in price. Near term the oil exporters should benefit. This would include such exporters as Saudi Arabia, Canada, Norway and the U.S. Oil importers would be adversely affected and would include China, India, Japan and the European Union. The U.S. could potentially benefit in several ways. Shale producers in the U.S. can quickly raise production volume if oil holds at higher price levels. In addition, the U.S. has become an exporter of liquified natural gas that could see increased demand.

Reflecting a slowing economy, fourth quarter growth was at a 0.7% annual rate versus 4.4% in the third quarter. Consumer sector (approximately 70% of GDP) growth is slowing. It grew 2.0% in the quarter versus 3.5% in the previous quarter. Final sales to private domestic purchasers (a measure of underlying demand that eliminates the volatile trade and inventory levels in addition to the government sector) grew at 1.9%, down from 2.9% in the third quarter. In addition, economic growth is narrowly based. For example, software, 4% of GDP, accounted for 90% of overall GDP growth. Consumer debt delinquencies have increased. Lastly, 2025 job data was revised by -898,000. This reflects job losses from AI related firings as well as cautious hiring by companies. The job gains that have occurred have not been broad based but rather narrowly based around health care.

The federal budget deficit, already large, will continue to grow. The \$1.9 trillion deficit will grow due to larger defense funding (Trump has proposed an increase from \$900 billion to \$1.4 trillion by 2027 and this was before the Middle East war). In addition, entitlement expenditures (Social Security and Medicare) continue to grow. There have been suggestions to bring these expenditures under tighter control by eliminating the ceiling cap for social security contributions and/or raising the retirement age. The budget deficit used to be at 3% of GDP and has grown to 6% currently. Fifty percent of the deficit is represented by interest payments on the debt and fifty percent of the debt has short-term maturity with a risk of having to be refunded at higher interest rate levels. The growing deficits risks crowding out the private sector in

the debt markets. This could lead to more cautious capex and hiring by companies and a headwind to consumer spending.

The U.S. Supreme Court ruled that Trump's tariffs were unconstitutional and ordered refunds to companies that paid the tariffs. The amount to be rebated is approximately \$166 billion. The average tariff rate rose seven-fold from 2% to 14%. While we do not yet know where the tariff rate will settle post the ruling, it should be lower. It is estimated that consumers will ultimately pay 90% of the tariffs as companies raise their prices to cover the tariff cost. Tariffs represent a regressive tax. A lower tariff rate will represent a stimulus to growth and prove less inflationary. Rebating tariffs to companies that paid the tariff can be documented. For consumers that paid the tariff in the form of higher prices, it is less clear how they will be eligible for tariff rebates. So far tariffs have not produced the manufacturing rebirth that the Trump administration promised. Manufacturing payrolls dropped to the lowest level in four years.

Another sector of uncertainty that Vanderbilt cautioned about is private credit. Whereas surprises that arose were previously described as isolated incidents, there is now recognition that there are more systemic problems for this asset class. Problems that have risen include examples of poor due diligence, market valuations that are significantly overvalued, and lack of liquidity as withdrawal requests have now been limited by private credit funds. Some in the sector are now warning of a shakeout coming over the next 12-18 months.

Inflation remains above the Fed's 2.0% target. The most recent reading of Core PCE (the Fed's preferred measure of inflation) was 3.1% year-over-year versus 3.0% the previous month. This is before the recent oil price shock. Vanderbilt thinks a case can be made for a possible easing of inflationary pressures in the last half of 2026. Factors supporting this viewpoint include the following: the Middle East war is resolved sooner rather than later, and the price of oil will adjust downward, the easing of shelter inflation, wage growth slowing, recent productivity gains continue with a boost from AI and tariffs at lower levels. However, in the latter part of 2026, we have slowing growth with increasing inflation pressures, stagflation. This puts the Fed in a quandary-loosening monetary policy to support a weakening labor market or a tighter monetary policy to combat inflationary pressures. We think in the near term the Fed will hold monetary policy unchanged and continue to monitor incoming economic developments.

1st Quarter 2026 Fixed Income Summary

The fixed income markets experienced significant volatility as interest rates reacted strongly to domestic and global economic concerns. The first part of the quarter was dominated by unease surrounding a possible contagion generating from weak private credit loans to software companies that are at risk of becoming redundant in an AI led economy. Although the private credit market has not yet reached \$2 trillion in market value, parallels are being drawn to the global financial crisis that roiled global markets after a collapse in the \$7 trillion mortgage-backed security universe. Worries surrounding the private credit market and AI's negative impact on the labor market fueled concerns about an economic slowdown and resulted in decreasing interest rates through the end of February, with the 10-year treasury rate falling below 4.0% on the last day of February. However, the treasury rally was immediately halted when, on the very next day the U.S. declared war on Iran, and the 10-year treasury reversed, increasing by well over 30 basis points in mid-March to market concerns that now concentrated more on inflation than a slowing economy.

As rates fluctuated, the 2-year treasury yield which started the quarter at 3.47% closed at 3.79% at the end of March. The 30-year treasury yield, however, was nearly unchanged, starting the quarter at 4.84%, and closing out at 4.91%. The increase in rates at the short end of the yield curve stems from the diminished expectations for interest rate cuts by the Federal Reserve in their upcoming meetings. While two to three

cuts of 25 basis points each were anticipated by futures traders at the start of the year, those expectations have now been reduced to zero cuts. Even as the Federal Reserve stated after their March 18th meeting that the committee’s median expectation is for one 25 basis point cut in 2026, traders discounted it to zero because Chair Powell’s press conference suggested that the cut would hinge on the uncertain path of inflation, which is magnified in the current environment of tariffs and war ambiguity.

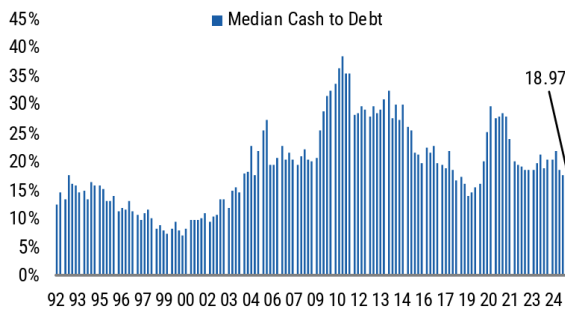
Treasury Inflation Protected Securities (TIPS)

Your portfolio holds an out-of-benchmark allocation to TIPS, which serve as a hedge against inflation in a fixed income portfolio, as they benefit from a rising inflation environment. TIPS valuation is based on actual inflation and inflationary expectations. In the first quarter, as inflation remained above 2% and inflation expectations measured by the TIPS breakeven rate increased dramatically (see chart below), as such, TIPS outperformed nominal fixed income treasuries.

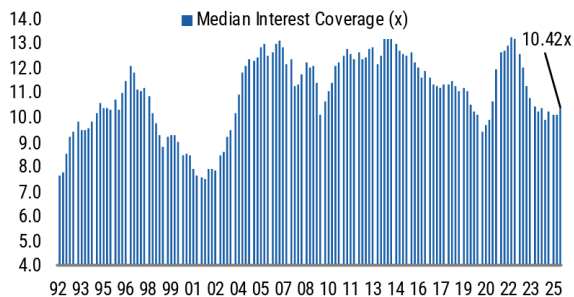


Corporate Bonds

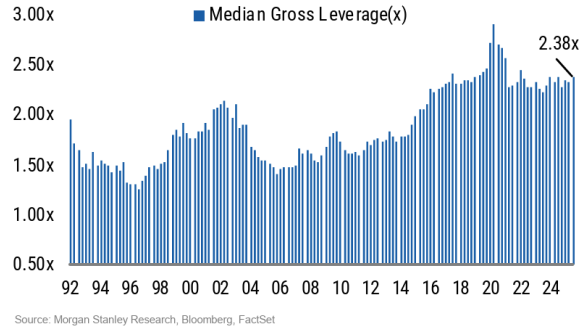
Despite weakness in private credit, investment grade corporate bonds’ fundamentals have remained solid. Cash to debt ratio, which measures the percentage of debt that can be paid off with operating cash flow increased to almost 19% and remains above pre-Covid pandemic levels. Likewise, interest coverage ratio which measures a company’s ability to pay interest on its outstanding debt using EBITDA (earnings before interest taxes depreciation and amortization) ticked up recently. However, leverage which measures debt over EBITDA also increased slightly, but still below pre-pandemic levels. See charts below. Spreads on corporate bonds, which were at historically tight levels at the start of the year, widened somewhat in concert with weakness in the private credit sector.



Source: Morgan Stanley Research, Bloomberg, FactSet



Source: Morgan Stanley Research, Bloomberg, FactSet



Housing

The housing market is slowly regaining activity as both sales and rental prices of homes are increasing at a slower rate. The most recent Consumer Price Index indicated that the shelter component of CPI is at 3%, a considerable decline from its 8.2% peak in 2023. Although housing inventory remains tight by historical standards due mortgage rate lock-ins, sellers are emerging as life changes propel sales and relocations. Additionally, mortgage rates have declined from a high above 8% in 2023 to slightly over 6% currently (see chart).



Chairman Powell highlighted during his FOMC press conference that the committee is pleased with progress on housing services inflation, and they hope that non-housing services inflation will also decelerate in the coming months. A slowdown in inflation would provide the Fed with a greater ability to lower rates to tackle the tepid labor market, which in turn would benefit home buyers, especially if mortgage rates continue to decline.