

Market Commentary

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Military Action in the Middle East Drives Market Declines

Markets finished lower as an early-week rally faded into a late-week selloff. Stocks initially rallied as President Trump said the “war is very complete, pretty much,” and oil prices plunged, but the strength reversed as geopolitical tensions escalated and oil rebounded.

The S&P 500 fell 2%, with Energy the only sector in positive territory. The Nasdaq had a smaller decline of 1.5% as investors rotated toward tech stocks and mega caps amid the volatility, while the Russell 2000 declined by 3%.

Bonds also traded lower as rising oil prices and inflation concerns pushed Treasury yields higher. Commodities were mixed: oil rebounded toward \$100 per barrel as the Strait of Hormuz remained closed, while gold posted a modest loss despite the market volatility. The week ended with tensions unresolved.

Key Takeaways

1. Tensions Remain Elevated in the Middle East & Continue to Impact Markets

The Strait of Hormuz remains effectively closed, and the energy shock remains the dominant market story. Oil has increased by approximately 40% since the beginning of the war.

The VIX spiked to an 11-month high before partially recovering, and Fed rate-cut expectations for 2026 have dropped from three to one. Equity markets have held up better than might be expected, with the S&P 500 down less than 3% since the end of February.

The key question is how quickly oil flows normalize, which will determine whether the supply disruption is contained or becomes a drag on economic growth. Markets are likely to remain volatile until geopolitical tensions ease.

2. Labor Market Conditions Continue to Soften

The U.S. economy lost approximately 92,000 jobs in February, below expectations for an increase of 50,000–60,000 jobs. Prior months were also revised lower, with December flipping from a reported gain of 48,000 to a loss of 17,000, meaning the labor market has shed jobs in three of the past five months. Unemployment edged up to 4.4% from 4.3%.

Part of the weakness was due to a Kaiser Permanente strike that kept close to 31,000 healthcare workers off payroll during the survey period, though it has since been resolved. Labor market conditions put pressure on the Fed to resume cutting rates, though the timing remains uncertain heading into the March meeting this week.

While some of the weaknesses reflect temporary distortions, the broader trend points to a softening labor market.

3. Consumer Spending Remains Solid Despite Headline Decline

The January retail sales report showed a modest decline of 0.2% month over month, below expectations for a flat reading. Weakness in motor vehicles and gasoline stations pulled the headline lower, though reduced gas spending mostly reflected lower January fuel prices rather than weaker demand.

Stripping out those categories, sales rose 0.3%, and the control group, which feeds directly into GDP calculations, also gained 0.3%, suggesting underlying consumer spending was more resilient than the headline implied. However, the recent oil shock introduces a new variable that could weigh on consumer spending in the months ahead.

4. Inflation Was Easing, But the Oil Price Shock Could Create New Pressures

Headline CPI rose 0.3% month over month and 2.4% year over year, in line with January. Core inflation, which excludes the volatile food and energy categories, rose 0.2% month over month and 2.5% year over year. Shelter costs, which have been the most stubborn component of inflation, continued to ease, with rent posting its smallest monthly gain since January 2021.

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The data suggests inflation continued to ease early in 2026. February's data is encouraging, but it was collected before the oil shock. Looking ahead, a key matter is whether the rise in oil prices will impact inflation and complicate Fed policy.

5. The Fed's Meeting is the Big Event This Week

Investors expect the Fed to hold rates steady at 3.50–3.75%. We believe the focus will shift to the updated dot plot, which will signal how many cuts policymakers expect in 2026 and whether higher oil prices are influencing their inflation outlook.

The Fed faces a difficult balancing act: inflation has been stabilizing, and the labor market is softening, but rising oil prices introduce a new inflation risk. The market expects one 0.25% rate cut this year, though two cuts are possible if energy prices stabilize. Until the oil shock's impact on inflation becomes clearer, the Fed is unlikely to provide the policy clarity markets want.

Should Your Investment Strategy Change?

A recognizable trend emerges whenever major headlines intensify. International conflicts and increased market volatility typically result in investors asking the same questions. What does this mean for me? Is this the event that finally derails everything? Is what I've built at risk?

These reactions are completely natural. When uncertainty enters the world and/or markets, our instincts go straight to risk. But the right next step isn't panic, it's pause. Take a step back, look at the facts, and evaluate the situation with a clear head instead of reacting emotionally.

If history has taught us anything, it's that we've faced serious challenges before. Markets have navigated wars, recessions, political tension, and global disruptions.

The investment strategies we build aren't designed only for calm markets. They are balanced. They are designed to help weather periods when volatility spikes. While we certainly don't ignore the headlines and near-term market risks, we also stay focused on long-term goals.

Please contact us at any time if you'd like to discuss your individual portfolios.

Have a good week,

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