



Market Commentary

Weekly perspective on current market sentiment

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Last week's S&P 500 Index: -2.1%

Frictions

Key takeaways

- As we have been reminded of several times over the course of the last month, an unexpected event can happen without warning and at just about any time.
- It's actually times like the present that remind us why portfolio diversification is such an important tool for a long-term investor.

Analysts can do enormous amounts of statistical analysis and modeling to help them come up with conclusions and projections of what might happen down the road in the economy or with an individual stock or equity index. But when an event like the military action in Iran suddenly comes into play, much of this analysis can almost be thrown out the window. As we have been reminded of several times over the course of the last month, an unexpected event can happen without warning and at just about any time. When you wake up in the morning and look at the overnight headlines, you might be surprised at what has occurred since you fell asleep. That is the environment we live in at the current moment.

We all know the recent financial media headlines have largely been directed toward the Iran conflict. But in recent weeks and months, there has also been quite a bit of conversation surrounding Private Credit. Anxiety around this asset class has increased with concerns about transparency. Higher interest rates have also played a role, as some companies owned by private credit firms might have a tougher time refinancing existing debt. Higher interest rates can also reduce returns and might weaken the economics behind some of these deals. Private credit returns largely rely on selling companies to realize gains through initial public offerings (IPOs) or strategic sales.

The potential economic effects of these two market concerns revolve around energy price-driven inflation from gasoline to food and, in the case of private credit, stress in the debt markets that may slow lending and growth. Our 2026 base case remains for above-average economic growth in the U.S. and record earnings for the S&P 500. With that outlook in mind, we believe the basic structure of a diversified portfolio is where we prefer to be positioned.

It's actually times like the present that remind us why portfolio diversification is such an important tool for a long-term investor. As a gardener might do, a long-term investor diversifies a portfolio to survive unexpected storms and other growing conditions. And just as the gardener prunes, so too does the investor rebalance during periods of divergent returns. Knowing and "pruning" your allocations relative to your risk tolerance and well-thought-out investment plan can help you stay on the right track toward reaching your long-term financial goals.

Let's look at an example of the rebalancing process. If an investor's portfolio held a neutral weighting in the Energy sector coming into the year or prior to the Iran conflict, the equity portion of that portfolio would now likely be noticeably overweight relative to that sector's weighting in the S&P 500 (4.2% at the time of this writing). We would suggest that investors consider bringing their Energy sector exposure back down to a neutral weighting and reallocating those funds to our most favored Financials sector and/or the favored Industrials and Utilities sectors. Also, when looking at overall commodity exposure, we suggest the consideration of rotating funds from energy-related commodity sectors toward the industrial metals and precious metals sectors.

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