



VERISMO FINANCIAL

Quarterly Recap – March 31st, 2026

The new year has introduced several new narratives to the markets, each bringing unique uncertainty. The impact of artificial intelligence looms; its capabilities are simultaneously exciting and threatening. Separately, private credit investors have been shaken by illiquidity and concerned about the quality of the investments. Finally, Trump’s attack on Iran and the resulting closure of the Strait of Hormuz for maritime traffic sent oil, gas, fertilizer, and even helium prices flying higher. The duration of the closure is not yet clear. The resulting impact on the worldwide economy is dependent on resolving the conflict quickly. Stocks were slightly lower during the quarter, though the relative complacency of the indices masks extreme underlying volatility for individual stocks. Similarly, bonds were roughly unchanged, but this performance hides underlying volatility in interest rates and credit spreads.

The economy remains relatively strong, but the Iran War has inserted itself as somewhat of a binary outcome. If normalcy is restored, the global economy might experience some indigestion but continue to grow. If the conflict persists, the price of oil and other products will almost certainly remain high. Except when coming off exceptionally low levels, when oil goes up 80% in a year it leads to a recession – that level is ~\$103.ⁱ The stakes are high! Separately, the labor market is exhibiting weakness, though perhaps this is the new status quo when immigration and the fertility rate are both low. Inflation will likely rise due to the spike in oil prices. This could push the Consumer Price Index above 4%. The market had expected the Fed to cut interest rates during 2026, but now it’s possible that they will instead need to raise rates later in the year to keep downward pressure on inflation.

Equity markets have reacted poorly to the strife in the Middle East, moving down roughly 10% from their all-time highs.ⁱⁱ Nevertheless, they are down only in the single digits for the quarter and are positioned to bounce higher as a result of any peace deal. Volatility is high as each new headline is parsed for its impact on the conflict. Interest rates are also volatile. Bonds initially were sold along with stocks as investors feared resurgent inflation. As the war drags on, inflation concerns will gradually give way to growth concerns. In a recession bonds will instead likely be viewed as a safe haven and instead trade in the opposite direction from stocks.

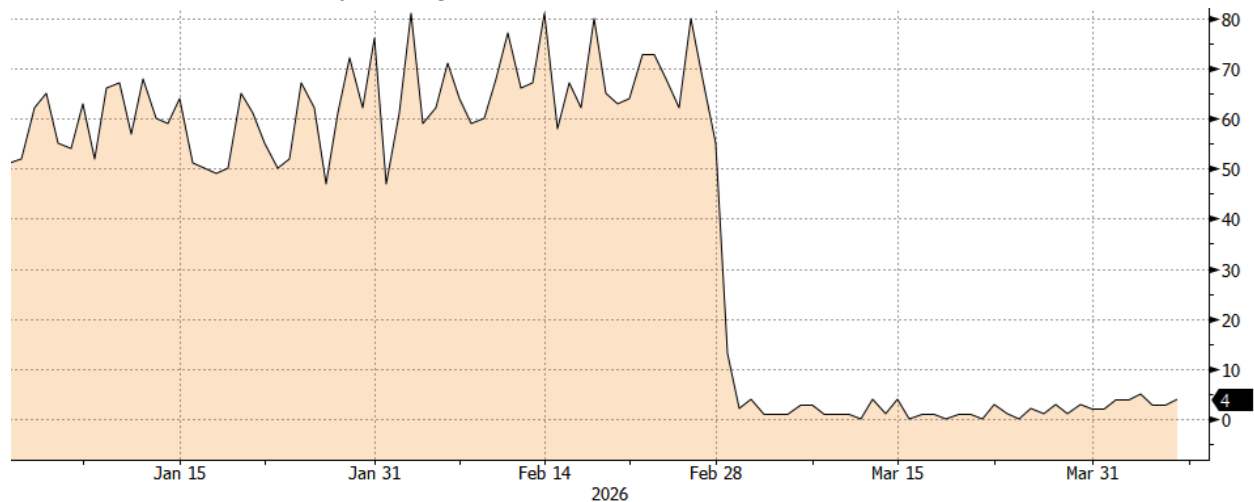
Each day of global disruption leads to worse outcomes for the economy, for markets, and from a humanitarian perspective. We are hopeful for a quick resolution but remain pragmatic about the timeline and resulting impact.

INDEX RETURNSⁱⁱⁱ	1st Qtr	2025	2024	TREASURY RATES^{iv}	3/31/26
MSCI All Country World	-3.1%	22.9%	18.0%	Fed Funds	3.63%
S&P 500	-4.4%	17.9%	25.0%	3 Month	3.59%
Dow Jones Industrial	-3.2%	14.9%	15.0%	2 Year	3.79%
Russell 2000	0.9%	12.8%	11.5%	5 Year	3.94%
EAFE	-1.1%	32.0%	4.5%	10 Year	4.32%
MSCI Emerging Markets	-1.9%	34.3%	8.0%	20 Year	4.91%
BC Aggregate Bond Index	0.2%	7.3%	1.3%	30 Year	4.91%

Economic Developments

The most important economic development during the quarter is the ongoing Iran War and the closure of the Strait of Hormuz. Roughly 20% of the world's oil travels through the Strait and is currently stuck.^v As we compose this newsletter on Wednesday April 8th a fragile ceasefire has just been announced for the next two weeks. The conflict is changing often, so we will refrain from detailed commentary about the current state of affairs.

The conflict's resolution will be important for the future trajectory of geopolitics. The United States was extremely capable at the start of the war, eliminating key political personnel, sinking the Iranian navy, and intercepting much of the retaliatory missiles. But since then, the administration appears largely impotent. They had to know in advance that the Strait of Hormuz would be leverage that Iran would use if it could. And yet weeks later Iran is still using the Strait to hold the world economy hostage.



The number of tankers crossing the Strait of Hormuz has fallen to basically zero. It's rumored that some tankers aren't being counted because they turn off their transponders. Others might be paying a \$2m toll.^{vi}

The Iranian resistance is now decentralized and inexpensive. The drones they use cost around \$25k, are built with easily sourced items, and can be launched from virtually anywhere. What they lack in sophistication, they can make up for with quantity. Launching hundreds at once can inflict millions or billions of dollars of damage if even 1 or 2% of them hit a target. It's currently also expensive to shoot them down; interceptor missiles cost millions of dollars. While they are effective at what they do, the relative price difference alone makes this an unsustainable long-term answer.

The military needs a fundamentally different approach to open the Strait, and then to keep it open. A major concern regarding this conflict is that it exposes the fragility of the current geopolitical peace. The Strait of Hormuz is hardly the only place where cheap drones can hit high value targets. We saw a similar strategy from the Houthis in the Red Sea for several years.

Jevon's Paradox has been mentioned often when discussing AI. It describes the paradox that when something becomes

When technological improvements that increase the efficiency of a resource's use lead to a rise, rather than a fall, in total consumption of that resource.

- Jevon's Paradox^{vii}

cheaper, we don't just do the same thing more efficiently. Rather, we do even more of it. Drone warfare in Ukraine and Iran is undoubtedly cheaper than it used to be. If so, does that mean we can expect more of it in the future?

We'll give a brief description of economic conditions as well, noting that uncertainty is very high. The trajectory of the economy is highly dependent on the resolution of the Iran War.

Inflation was already set to rise as several low data points would get removed and replaced with higher data points. A spike in the price of oil certainly doesn't help things. The impact of oil prices is yet to be felt by most of the economy, but made an immediate impact on gas prices. Gas has risen 40% since the start of the Iran War. Gas will likely add as much as .6% to the next CPI data point on its own. Inflation has been troublesome economically and politically and this will only make its impact more salient. While oil's price continues to rise, it's worth noting that the oil market is in "backwardation."^{ix} Futures contracts expire every month, and typically the price is basically the same from one month to the next. Backwardation is the situation where prices are high right now but declining in the future. The current backwardation demonstrates that investors expect the oil to start flowing again soon. Contango describes the alternative, more normal situation where prices are higher for contracts in later time periods.



Oil prices for immediate delivery (red) have risen much more than prices for later delivery (black), indicating optimism that the Iran War will not last.^x

The labor market is confusing. The unemployment rate remains low at just 4.4%. In contrast the monthly change in payrolls has clearly deteriorated.^{xi} Chairman Powell and other economists are coming to this realization. With tightly controlled immigration and a low fertility rate there is not a huge need for new job creation.

Sort of lost in the busy news cycle was the Supreme Court's tariff ruling. This was highly anticipated by Trump's critics and investors. The Court ultimately ruled against the Trump tariffs that were up for debate.

Though hundreds of billions of past and future tariffs are affected, the decision ultimately hardly impacted markets when it was announced.^{xii}

"For the last three months [payroll growth]'s average right around zero, so I'm kind of in this kind of odd spot where my brain understands the math, but I can't get through my gut that this is okay. I've been doing this for 45 years as an economist, and if you told me zero was normal, I'd say you got to be out of your [mind].. the idea we'd get a [negative] 92,000 and the Fed would go 'eh, whatever,'... your head would explode."

- Federal Reserve Governor Chris Waller, March 20th, 2026, describing the change in what's "normal" for the labor market^{viii}

Preserve – Interest Rate Commentary

The Federal Reserve did not adjust interest rates during the first quarter, which is what was expected at the beginning of the year.^{xiii} The Fed did release a new Summary of Economic Projections (SEP), including an interest rate Dot Plot, but was appropriately dismissive of its use for predicting policy at the moment. The Fed's Dot Plot has rarely been accurate when

projecting out more than a few months; its predictive power during a fresh Middle Eastern conflict is probably close to zero.

Market expectations have shifted greatly as a result of the Iran War. Where two or more cuts were expected to start the year, we now expect none. The market even has a small possibility of a rate hike mid-year.^{xiv} Raising interest rates in this environment might seem confusing. But this is a similar setup as in 2022, with war causing a spike in oil prices and a slumping economy. If inflation is resurgent, the Fed should not stimulate the economy to compensate. If they do, it will just put more pressure on oil prices to rise further. During an oil shortage we need to reduce demand, not subsidize it. It's most likely that the Fed just holds interest rates where they are as they wait for more data, refraining from giving the markets a confident message one way or the other.



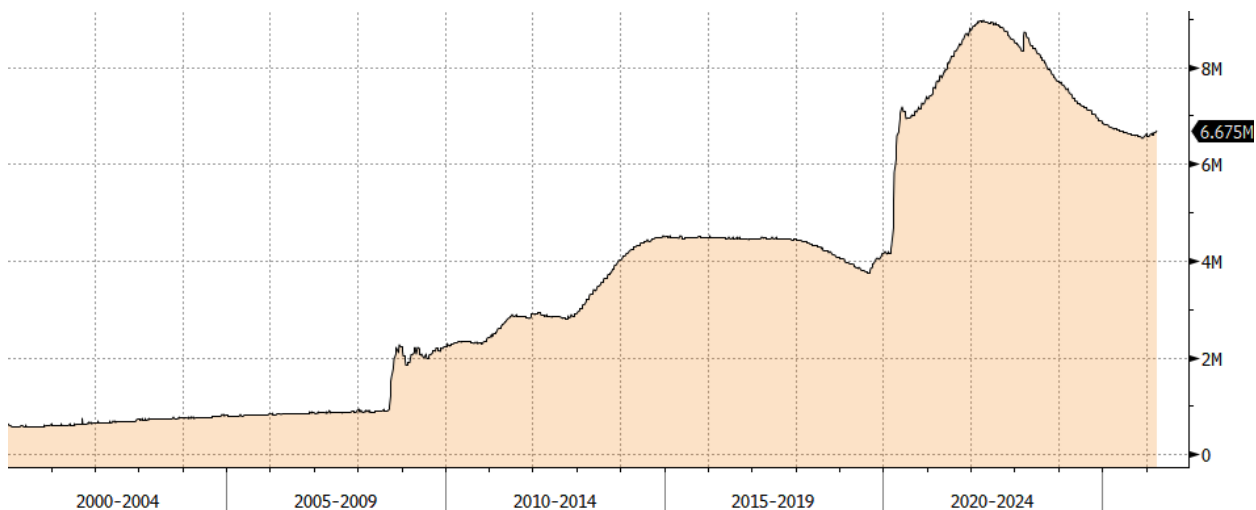
Payroll growth has gradually fallen over the last three years. The last six months average out to roughly zero. Yet from September 2025 to today the unemployment rate has actually fallen!^{xv}

Long-term interest rates have moved dramatically higher as the conflict has continued. The two-year yield has flirted with the psychologically-important level of 4%, the 10-year yield with 4.5%, and the 30-year yield with 5%. All three of these levels were last touched together during the tariff angst last year and were probably instrumental behind-the-scenes for the President to change his approach.^{xvi} As we've gotten to these levels in recent days, the President has offered conciliatory messages, likely in an attempt to placate markets. However, jawboning the markets with tweets has its limits. It worked well during the tariff chaos. But in that instance the President was fully in charge of policy. Investors coined the term TACO – Trump Always Chickens Out – noting that when the stock market falls, Trump changes his policy. But the current conflict has multiple players. Each time he tweets it becomes less effective as a strategy as investors fail to see meaningful actual deescalation of the conflict. The Iranian president has even called out the behavior, saying that Trump is manipulating markets.

Interest rates are likely to remain volatile but rangebound. They've currently moved higher as we expect higher inflation. If oil prices rise even further we will likely instead start to see interest rates fall. At some persistent price level, likely around \$125, the economy will probably experience a recession as a result. If oil were to hit \$150 or \$200 it's a virtual certainty.

In January Trump announced his pick for the next Federal Reserve Chairman as Kevin Warsh. This was viewed approvingly by markets. Warsh has experience with Federal Reserve policy from working with Chairman Ben Bernanke in 2008. At the time he was wary of Quantitative Easing ("QE" – Fed purchasing bonds in the open market to stimulate/manipulate

interest rates), a concern which proved prescient. It turns out that expanding the balance sheet is very easy and encourages speculation and bubbles. Reducing the size of the balance sheet, on the other hand, is difficult. Who wants to buy an asset when they know that there's hundreds of billions of dollars more of it coming soon? He was also concerned about inflation as a result of QE, a concern which turned out to be misplaced. His heterodox opinions in 2008 prove his willingness to be contrarian and consider alternative viewpoints. His focus on the size of the Fed's balance sheet will be interesting to watch. It's possible that a major theme of his tenure will be reducing the Fed's impact on markets. Theoretically the Fed should have little impact on markets. They can only change the interest rate that banks charge each other for overnight loans. That doesn't seem like it should impact stock prices! But through QE the Fed is able to manipulate every part of the interest rate curve and also becomes one of the world's largest asset managers. That has an extraordinarily larger impact on asset prices.



The Federal Reserve took (at the time) extreme action in 2008 by doubling the size of its balance sheet. Through the 2010's it expanded further with multiple rounds of Quantitative Easing. Their Covid response doubled it again.^{xvii}

With the conflict in Iran, changes in the labor market, and resurgent inflation, Warsh will have a difficult directive from day one. Further complicating matters is the Department of Justice's investigation into current Chairman Powell, which could delay the transition. We also await the Supreme Court's decision about whether President Trump can "fire" Fed Governor Lisa Cook. So on top of the economic concerns, there are a variety of politically self-inflicted issues challenging Fed policy and credibility. Warsh will doubtless have a more favorable relationship with Trump, having just been anointed by him, but some of the rancor from previous years will likely remain. We have already seen more "dissents" in votes about Fed policy decisions as of late. That is likely to continue – probably a good thing overall, discouraging groupthink and giving more insight into each Fed official's mindset. But it will also make messaging from Warsh less clear and reduce his ability to steer official policy on his own. The market has a habit of "testing" new Fed Chairmen with crises. It's clear that Warsh will have a complex landscape to navigate.

Earn – Bond Market Commentary

The bond market was very quiet for much of the first quarter. In fact, bond market volatility was at its lowest since 2021. This tranquility was more normal before 2020 but we haven't experienced it since the Fed started raising interest rates in 2022. The relative calm was

broken when the Iran War began. Interest rates rose dramatically and intraday moves were sometimes extreme as traders reacted to headlines.^{xviii}

Credit spreads were at the lowest levels ever, reflecting confidence in the economy. That is, investors were being compensated very little for taking credit risk in corporations. These spreads have increased as the conflict continues, though they are still narrower than at any time from 2020-2023.^{xix} We noted these tight spreads in our newsletter at year end; tight spreads aren't necessarily bad, but they do limit the upside and create additional downside risk.

Private credit has been in focus for more than six months. This asset class had been a darling for retail investors. They were often able to get 1% in income per month with virtually no volatility, as the portfolio's investments were only assessed monthly or quarterly. Because the bespoke loans don't trade in the open market, there is not an obvious way to fairly value them. Different managers might have similar loans but price them differently. Because of the illiquid nature of the portfolio, asset managers often have lock-ups on the investments, and reserve the right to limit redemptions, typically to 5% of the portfolio per quarter. These investments in semi-liquid vehicles have been something we have historically avoided recommending to clients. The ability to redeem provides liquidity, but it can be an illusion. Often when investors want their money back, it's in times of panic and they'd be better served by waiting. Unless an illiquid offering is truly unique, attractive, and unavailable in a liquid form, we prefer investments with daily liquidity such as stocks, mutual funds, and closed-end funds. Note that closed-end funds can also be impacted by panicky market conditions, and taking advantage of that dynamic is an important part of our team's income strategy. However, a critical difference is that when those funds trade poorly, the fund manager is at least not forced to liquidate a portion of the portfolio to meet investor redemptions.

The initial fear surrounding private credit was related to their lending standards. Two auto loan companies defaulted on their loans in 2025. This prompted fear that perhaps the underwriting standards for these managers were too lax. Maybe there was too much money going into private credit, so managers had difficulty finding enough businesses requiring loans? As more time elapsed, investors regained confidence that these two defaults were idiosyncratic and not related to any systemic underwriting issues.

More recently the investments have come under renewed scrutiny. Artificial Intelligence threatens to upend many business models, challenging their ability to repay their loans. As these concerns have grown, the private credit industry finds itself in somewhat of a spiral. Investors are concerned about the value of the underlying loans. They're also worried about the redemption limits – if they can only get 5% out per quarter, they could be waiting for five years to get it all out! The somewhat rational response is to get your money out now, before it gets worse.

As the stories about private credit redemptions circulate, more investors are taking this same approach. We've seen redemption requests climb from high levels – but still less than 5% - to extreme levels above 15% for some funds.



Private BDCs are valued where the manager says they are, and investors can vote by depositing or withdrawing funds. Meanwhile the MVIS Public Business Development Company Index shows that investors have deteriorating faith in the strength of the portfolios.^{xx}

It's not clear how this story will evolve. A large private REIT fund had a similar issue in 2022 which it was able to ultimately resolve in an investor-friendly way. The current issue is shared by many different funds with many different managers, further compounding the problem. If the managers want to exhibit conviction in the strength of their portfolios, they could consider buying the public BDCs at a discount. If they believe in the value of the portfolio, this is a trade with potentially significant upside which also benefits other investors by narrowing the discount.

While it is a troubling story for some investors, the private credit market is probably not large enough to cause systemic issues for the economy. What's really remarkable is how it's played out without many actual defaults in the underlying portfolios. It's possible that many of these managers will continue to restrict redemptions and allow the portfolio to continue to chug along. After a few quarters or years investors might regain confidence and this could be much ado about nothing.

Grow – Stock Market Commentary

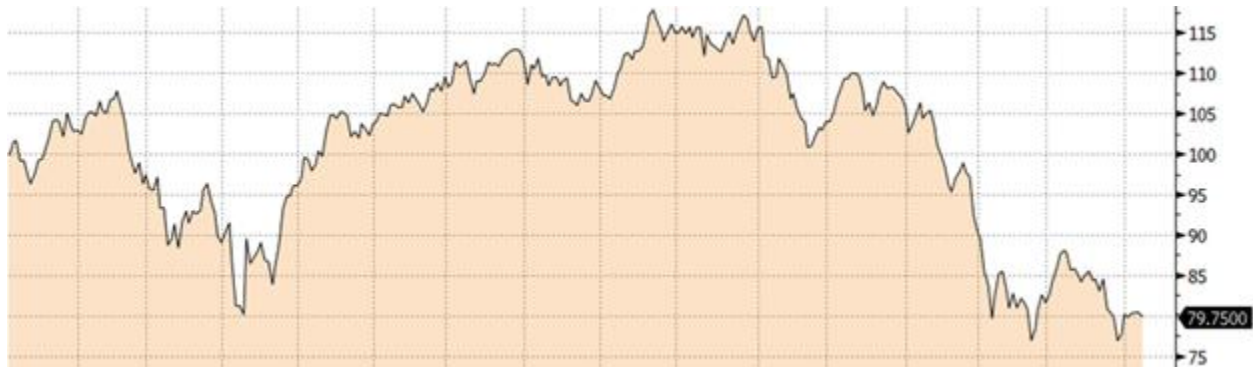
Many indexes behaved well to start the year. Small stocks and international stocks specifically outperformed. As the Magnificent 7 stocks have stagnated, investors looked elsewhere for the next idea.^{xxi}

Stocks then moved lower since the Iran War started. The only major sector that's positive for the year is Energy. While stocks are well below their recent highs, the move during the quarter was relatively small. Clearly investors are hoping that the Iran War doesn't metastasize into a larger economic event. As each week goes by without a resolution, stocks have continued to slide lower.^{xxii}

The relatively stable performance of the indexes has masked some extreme moves under the surface. During the quarter there was a large run-up in precious metals, a collapse in software stocks, and extreme moves in the stocks most affected by the Iran War.^{xxiii}

AI's relationship with the market has changed. While AI is still in the early innings of implementation, investors are taking note of its increasing capabilities and rapid trajectory. Many multi-billion-dollar companies could be superfluous once AI is fully integrated into the economy. Software is the primary sector that's most at-risk, and that sector has fallen 25% during the quarter.^{xxiv} But there are other sectors that are exposed as well. These companies might be fundamentally sound right now, kicking off profits with nice margins. But investors are looking into the future and asking if the business model will make sense in 3, 5, or 10 years. Fundamental analysis of a company might use a price-to-earnings multiple or some other multiple to determine the value of a stock. Earnings that are predictable and stable and growing might earn a high multiple, while earnings that are uncertain and declining might earn a lower multiple. Now investors must also determine a term we'd call "AI Existential Risk." That is, what is the probability that this company will be fundamentally challenged by AI?

Technology stocks have been some of the best performers for years because of the promise of AI. Now the capabilities of AI are betraying those same companies, threatening to render them redundant in the near future.



The North American Expanded Technology Software Index shows the damage that's been done to software stocks. These stocks have been a battleground between investors who believe that AI will replace the capabilities of many companies, and those who believe its future capabilities are overstated.^{xxv}

Investors seeking to avoid this dynamic have invested in HALO companies – heavy assets, low obsolescence. These companies operate in the “real world” with machinery or factories and are deemed to be at low risk for disruption from AI.

We are cautious in the current environment, noting the binary nature of the Iran War and the opacity of the negotiations for those on the outside. If a resolution is reached soon, the market can resume its march higher without much concern. But if the conflict drags, or if the Strait of Hormuz is abandoned to the Iranians, that introduces major long-term friction to the global economy. Other market narratives are currently not material to the direction of stocks.

Best regards,



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The S&P 500 Index consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market value weighted index with each stock's weight in the Index proportionate to its market value.

The MSCI All Country World Index (ACWI) captures large and mid cap representation across 23 Developed Markets (DM) and 24 Emerging Markets (EM) countries.

The Dow Jones Industrial Average is a price-weighted index of 30 "blue-chip" industrial U.S. stocks.

The Russell 2000® Index measures the performance of the 2,000 smallest companies in the Russell 3000® Index, which represents approximately 8% of the total market capitalization of the Russell 3000 Index.

The MSCI EAFE Index is a free float-adjusted market capitalization index that is designed to measure the equity market performance of 21 developed markets, excluding the U.S. and Canada.

MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance of 23 emerging markets.

Bloomberg U.S. Aggregate Bond Index is a broad-based measure of the investment grade, US dollar-denominated, fixed-rate taxable bond market.

ⁱ Bloomberg

ⁱⁱ Bloomberg

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^{iv} Bloomberg

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^{vi} Bloomberg

^{vii} Wikipedia.com

^{viii} CNBC

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