Wealth Management

Quarterly report

Q1 2026 market review

Forward-looking
for generations

Cover image
Bauer brothers, Hortus Botanicus, detail from "Lilium," 1776/1804

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> "While the action in Venezuela was contained, the escalation in the Middle East has had far broader consequences.
>
> Sanjay Rijhsinghani, Chief Investment Officer

Summary: Q1 2026

Two powerful themes have driven markets in 2026. The first is the geopolitical uncertainty triggered by President Donald Trump's sharp shift in US foreign policy. The second is the AI-driven sell-off, with markets shifting from favouring AI leaders to focusing on companies whose business models are most threatened by the rapidly developing technology. These trends reversed the market's strong start to the year, as investor attention turns to supply chain vulnerabilities and the potential growing risk of stagflation, when high inflation leads to weaker growth.

At a glance

- Iran war reshapes global outlook
- Rising energy prices create more inflation pressure
- Markets recalibrate to changing outlook
- Rate expectations shift from cuts to hikes
- Software companies come under increasing scrutiny

Macro summary

Few anticipated gunboat diplomacy – the pursuit of foreign policy objectives using military force – would become a defining feature in 2026. Trump had built his campaign on opposing foreign military action, insisting he would use his deal-making skills to end multiple conflicts, notably Russia's invasion of Ukraine.[1]

The opening quarter has instead been marked by direct US military action. The US launched an operation in Venezuela to remove President Nicolás Maduro, threatened to take over Greenland, and conducted joint strikes with Israel targeting Iranian military and nuclear facilities intended to destabilise its regime. While the action in Venezuela was contained, the escalation in the Middle East has had far broader consequences.

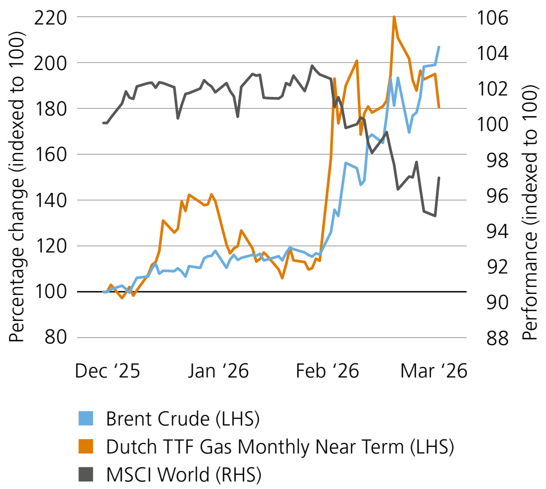
Iran war broadens out across the Gulf

Iran responded to the strikes by targeting energy infrastructure across the Gulf and restricting passage through the Strait of Hormuz, the 21-mile passageway where about 20% of the world's oil supply passes daily.[2] The result has been a significant repricing in energy markets, sending oil and natural gas prices higher and materially affecting global inflation expectations.

Equities initially held up against earlier geopolitical developments, but most gains were erased in March as the Iran conflict and its economic impact weighed on markets. European and Japanese equities were up 7% and 16% to the end of February, before ending the quarter down 0.8% and up 4%, respectively.

The US was more mixed – the headline-level S&P 500 was little changed to the end of February, while the equal-weighted S&P 500 index – which gives each constituent the same weighting regardless of market capitalisation – was up 7%. However, as the quarter progressed, the S&P 500 ended down 4.4% while the equal weighted S&P 500 finished just slightly positive. Asian equities were hit hard by the conflict in the Middle East as the continent receives a significant amount of oil from the Strait of Hormuz. Over the quarter, Hong Kong's Hang Seng Index lost 3% while China's Shanghai Composite fell 1.8%. Bond yields moved higher as investors shifted from pricing rate cuts to hikes amid heightened inflation uncertainty.

MSCI World vs crude oil and natural gas prices



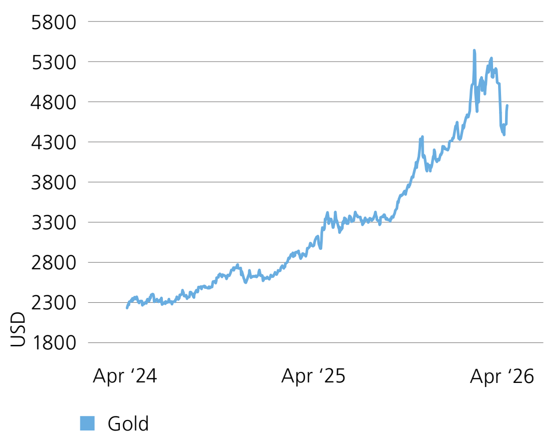
Source: Bloomberg

The conflict in Iran sent oil prices surging in the quarter. Brent crude rose 94%, its biggest quarterly jump since the start of the Gulf War in 1990, to close the quarter at USD 118 per barrel.[3] Natural gas rose 71% in Q1 as liquefied natural gas (LNG) disruptions emerged, and secondary effects on commodities such as sulphuric acid and fertiliser flows have added complexity beyond the energy sector.

[1] How to Avoid a Forever War in Iran | WPR
[2] Iran war: What is the Strait of Hormuz and why does it matter? - BBC News
[3] Deutsche Bank, Bloomberg

Even traditional safe-haven assets such as gold have not been immune. After a strong 2025 and a record start to the year, gold fell 11.6% in March following the escalation of the conflict. While gold typically performs well during periods of uncertainty as investors seek assets that preserve value, in extreme risk-off environments investors often sell their best-performing and most liquid holdings to raise cash. Its effectiveness as a safe haven is also highly dependent on the broader macro backdrop, particularly inflation, interest rates and currency movements.

Gold price per ounce (USD) over two years



Source: Bloomberg

The conflict is expected to feed directly into inflation – higher crude prices will raise transportation costs, airline fares and freight rates, while also affecting consumer sentiment. In addition, restricted shipping lanes are raising availability concerns for essential commodities. However, if a resolution is reached in the Middle East, the inflationary impulse would likely prove temporary, giving central banks scope to look through the near-term pressure rather than respond with further rate hikes.

AI developments shift focus to competitive threats

It was a solid earnings season, although shares of software companies suffered significant falls after the release of industry-specific plug-ins for Anthropic's new Claude Cowork tool. This tool – which uses language instructions to complete complex, multi-step work including file organisation and document creation – appears to compete with traditional software-as-a-service (SaaS) models. This has led investors to reassess SaaS company valuations. As a result, the S&P 500 Software Industry Index fell 24% in the first quarter, with most declines occurring before the war.

Central banks weigh energy shocks and growth impact

At the start of 2026, most expected central banks to continue cutting interest rates. This outlook has been upended by the ongoing Middle East conflict.

The Federal Reserve (Fed), Bank of England (BoE) and European Central Bank (ECB) all met mid-March and as expected, each left policy rates unchanged, citing the uncertain outlook shaped by rising oil and natural gas prices, which will likely fuel inflation and weigh on growth. Businesses and consumers will need to adapt to higher costs and supply chain disruption, which could intensify if the conflict continues. Policymakers must now decide whether to pause the cycle or even raise rates as inflation pressures mount.

On 30 January, Trump nominated Kevin Warsh to replace Fed Chairman Jerome Powell, subject to confirmation and pending the ongoing investigation into Powell. The Fed is no longer expected to cut rates but will likely hold.

Expectations for the BoE have shifted from two cuts this year to pricing in possible rate hikes to control inflation. The BoE's latest forecast shows inflation hitting 3.5% in July.[4] Similarly, markets expect the ECB to raise rates a few times this year, although before tightening policy, global central banks will need to weigh the trade-off between containing inflation and supporting growth.

Takaichi victory opens door for fiscal expansion

On 8 February, Japanese voters handed Prime Minister Sanae Takaichi and the long-ruling Liberal Democratic Party a supermajority in the lower house of Parliament – the first party in the post-war era to achieve such dominance. This gives Takaichi greater political room to pursue her agenda, which includes a tougher stance on immigration, a review of rules around foreign ownership of Japanese land, and policies to increase spending while cutting taxes to stimulate the economy.

Japanese equities posted strong gains post-election, although some of these gains had tapered off by quarter-end. Japan's Topix (Tokyo Stock Price Index) rose 16% through February but ended the quarter up only 4%. Before the election, Japanese government bonds sold off amid election pledges for more consumption tax cuts, with 30-year yields rising to 3.86%, the highest since their introduction. Yields fell back from these highs, only to rise again with the Iran conflict.[5]

Supreme Court ruling clouds US trade policy

On 20 February, the US Supreme Court ruled that sweeping tariffs imposed by Trump on key trading partners violated federal law, dealing a major blow to the administration's trade strategy and creating uncertainty over existing agreements. In response, the administration introduced a replacement tariff framework, starting at 10% and potentially rising to 15%, using a little-tested provision that allows the president to impose broad tariffs for up to 150 days without congressional approval.

Markets brace for geopolitical and AI shifts

Looking ahead to the remainder of 2026, markets are likely to remain highly sensitive to both geopolitical developments and the pace of technological disruptors. The ongoing conflict in the Middle East will continue to influence energy markets, global supply chains and inflation expectations.

In our experience, while these periods are unsettling and unpredictable, history reminds us that knee-jerk reactions tend to cost investors over the long run. We continue to actively monitor developments in markets and stand ready to reposition portfolios should opportunities arise. Volatility often creates attractive entry points and maintaining a disciplined, long-term approach can allow investors to capture gains as markets recover.

[4] Interest rates held at 3.75% as Bank of England warns Iran war 'shock' will push up inflation - BBC News
[5] Deutsche Bank, Bloomberg

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Sanjay Rijhsinghani, Chief Investment Officer

Fixed income

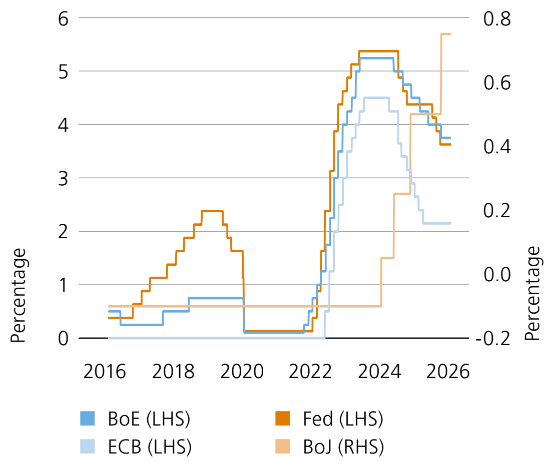
The first quarter illustrated how the supply shocks of recent years have drastically shifted perceptions of central bank reactions. Following Russia's invasion of Ukraine in 2022, markets took time to adjust to the reality of the rate-hiking cycle central banks were about to embark on.

From the onset of the war in Iran in February, however, we saw the anticipated rate cuts quickly fade, with markets moving to price in hikes for both the ECB and BoE by the end of the quarter. This resulted in large swings in yields across global government bonds, which had previously been declining throughout the year to the end of February. While earlier supply shocks had shown a fading impact on inflation over previous quarters, the closure of the Strait of Hormuz and the significant increases in energy costs mean central banks will need to closely monitor if this latest shock is a one-off or will result in stickier inflation.

Why this supply shock is different from 2022

There are several clear differences between this developing global supply chain shock and previous ones, including the starting position of global economies and interest rates. Back in 2022, interest rates were close to zero with the ECB still operating a negative interest rate policy. Today, outside of Japan, central banks are no longer maintaining an accommodative stance. This means that if further action were deemed necessary, there would likely be less need for aggressive policy tightening than in the past.

Central bank policy rates over 10 years (%)



Source: Bloomberg

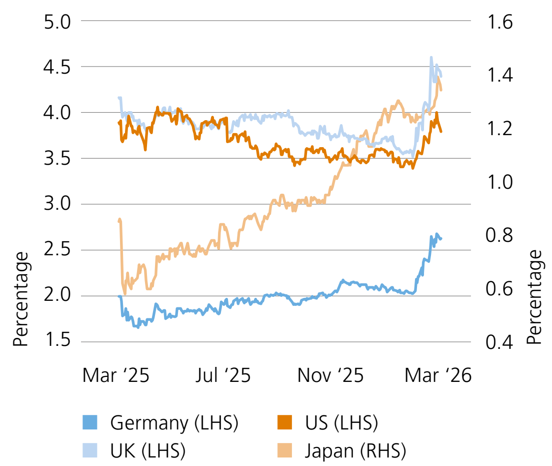
The other key difference is the state of the labour market. In 2022, the world was starting to emerge from the pandemic with a large degree of pent-up demand and savings. This resulted in a very tight labour market and put employees in a powerful position to negotiate higher wages. This led to a wage-price spiral, which kept inflation elevated for some time.

Labour market dynamics shift

Today, the picture is different. Prior to the latest conflict, the Fed eased policy in Q4 2025 as it highlighted concerns about the softening labour market. The narrative was also focused on how rapid developments in AI could potentially lead to a sharp increase in unemployment, underscoring that employees could no longer demand higher wages.

By the end of Q1, markets expected the ECB to hike as much as three times this year, which would take policy from 2% to 2.75%. Meanwhile, the BoE was seen to hike rates twice from 3.75% to 4.25%. However, given that unemployment has increased above 5% over the past year, and the hit to growth from the conflict for the UK is significant, this has raised doubts these hikes would be necessary. The last time around, the fiscal support played a big part to offset the pressure on households, but the fiscal constraints make such policy unlikely this time around. Nevertheless, two- and 10-year gilt yields rose by 0.67% (to 4.41%) and 0.44% (to 4.92%) respectively in Q1. For German bunds, they rose by 0.5% (to 2.63%) and 0.15% (to 3%) respectively over the same period.

Two-year government bond yields (%)



Source: Bloomberg

Meanwhile, given the US is a formidable energy producer, the hit to its growth is smaller and to some degree offset by fiscal support emanating from the so-called "big, beautiful bill". While its bond yields have also moved higher, some still expect the US to continue its rate cutting cycle towards the end of the year as underlying inflation appears contained and was moving lower prior to the war in Iran.

AI-fuelled issuance boosts public credit

Publicly-traded credit remained well supported throughout the quarter, with spreads widening moderately but seeing little actual stress. The start of the year was marked by a large increase in issuance from technology companies to fund their AI spending, with Amazon and Alphabet raising a staggering USD 37 billion and USD 32 billion from bond markets this year. These are both among the largest deals ever, particularly when excluding M&A funding.

While public credit was resilient, concerns over private credit captured headlines. News that funds from Blue Owl were halting redemptions after hitting well over 5% of quarterly redemption limits resulted in a cascade of investors looking to redeem private credit positions. Blackstone, Apollo, Ares and Blackstone followed suit in restricting redemptions, putting the bonds and share prices of these businesses under pressure. The renewed scrutiny of these opaque investments mean pressure will likely persist, while spillover effects will be examined carefully.

> "From the onset of the war in Iran, we saw the anticipated rate cuts quickly fade, with markets moving to price in hikes for both the ECB and BoE by quarter-end.
>
> Jeremy Sterngold, Deputy CIO and Head of Fixed Income

Equities

The first quarter was very much a case of before and after. Before the US-Israeli joint strikes on Iran on 28 February, the MSCI World, MSCI Europe, and the Shenzhen Composite were all up between 2% and 5%, while Japan's Topix Index rose over 13%. The US stock market juggernaut had paused, with the S&P 500 broadly flat. After the strikes, however, all these indices declined (MSCI World -7%, MSCI Europe -8%, Shenzhen -7%, Topix -11%, and the S&P -4%). Pretty much every equity market around the globe ended up falling over the quarter, with just a few exceptions.

Korea defies the downturn on AI chip strength

Firstly, Korea's Kospi Index continued its phenomenal run, with its fourth double-digital quarter in a row, three of which were over 20%, including Q1 2026. Its 48% gains before the Middle East conflict more than offset the 19% pullback after. Korea's strength was all about technology, specifically memory chips, which are the latest part of the industry to see huge demand from AI result in significant pricing power. Samsung Electronics rose 38% and SK Hynix 24% during the quarter. By the end of Q1, those two stocks accounted for 40% of the Kospi.

Energy exposure lifts UK

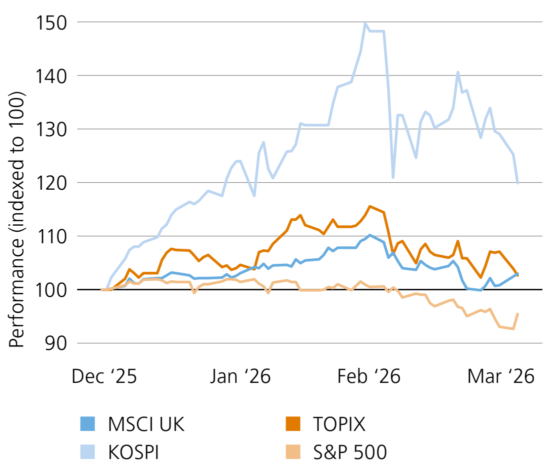
Secondly, the MSCI UK Index followed up its excellent 26% total return in 2025 – better than the S&P 500 and Nasdaq – with another 4% return in Q1 2026. This is largely due to Shell rising 32% and BP 42% as the oil price almost doubled on the de facto closure of the Strait of Hormuz. The continued strength in global pharmaceutical stocks also helped lift UK stocks, where AI appears to be a tailwind rather than a headwind. In an uncertain world, the defensive characteristics of these companies stand out. While Anglo-Chinese bank HSBC rose 7%, this was the exception. Lloyds fell 6%, Barclays dropped 17% and NatWest declined 11%, as the UK's status as a significant oil importer raised fears of an inflation spike and growth slump.

Japan's trading houses steal the spotlight

Thirdly, the Topix index – which also beat both the S&P 500 and Nasdaq in 2025 with a 25% total return – rose 3.6% over the quarter. Semiconductor equipment maker Tokyo Electron gained 8%, but the real winners were the trading houses, which benefited from commodities exposure – Mitsubishi Corporation rose 48% and Mitsui & Co. returned 30%. Warren Buffett's prescience was shown once again given his 10% stake in each company. On the flipside, amongst car makers, Toyota fell 6% while Honda dropped 18% over worries higher gas prices will weigh on both driving and demand for new cars.

The S&P 500 fell 4% in Q1. However, the S&P 500 Equal Weighted Index rose 1%, showing that the largest stocks were the ones driving the index down.

MSCI UK vs S&P 500 vs KOSPI vs TOPIX over Q1



Source: Bloomberg

Indeed, the largest companies – Microsoft (-23%), Meta (-13%), Amazon (-10%), Broadcom (-10%), Alphabet (-8%), Apple (-7%), Nvidia (-6%) and Tesla (-17%) have lost a combined USD 3 trillion in market value since the turn of the year, roughly a quarter off the total value of listed stocks in the UK. The fact that the largest stocks fell so much meant that more than half the sectors in the S&P 500 actually posted a positive return, with the energy sector, up 38%, leading the pack.

Defensives reassert themselves

Utilities, having become an AI-adjacent sector – all those AI data centres need a lot of energy – returned to their defensive ways, rising 8%. The defensive consumer staples sector rose by the same amount. Even though some oil price-driven inflation seems inevitable, which means US interest rates may well remain higher for longer (good news for banks' profits), concerns over the impact of the Iran war on economic growth coupled with private credit exposure meant the US financials sector fell 9%.

Sector divergence across Europe

Within the 1% fall in the MSCI Europe, the IT sector rose 2%, with semiconductor manufacturing equipment maker ASML gaining 21% after its Q4 2025 earnings showed a robust order book with orders exceeding revenues for only the second quarter over the last couple of years. The energy sector gained 42% given the move in oil prices. The consumer discretionary sector succumbed to the same economic growth concerns as UK banks, falling 18%.

Ultimately, whether the Iran-US ceasefire holds will set the tone for equity markets over the coming weeks and months.

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> Russell Harrop, Head of Equities

Key market data

Key market data (as at 31 March 2026)

Asset class	Level	1m %	3m %	6m %	1y %	3y %	5y %	YTD %
Equity indices (total return) *								
MSCI United Kingdom (GBP)	2916	-5.92	4.05	11.42	22.98	49.48	87.99	4.05
S&P 500 (USD)	6528	-4.98	-4.33	-1.79	17.80	65.63	76.74	-4.33
Euro Stoxx 50 (EUR)	2768	-9.14	-3.49	1.48	9.46	42.06	65.84	-3.49
Nikkei 225 (JPY)	51064	-13.23	1.44	13.65	43.37	82.10	75.00	1.44
MSCI World (USD)	3315	-5.63	-3.05	0.30	18.34	61.24	71.77	-3.05
MSCI AC Asia Pacific ex Japan (USD)	879	-10.70	1.39	5.97	28.45	55.82	36.42	1.39
MSCI Emerging Markets (USD)	88858	-10.51	2.19	7.99	31.36	62.96	38.19	2.19
10 year bond yields **								
UK	4.84	0.59	0.37	0.15	0.17	1.32	4.02	0.37
US	4.32	0.36	0.15	0.17	0.11	0.83	2.58	0.15
Germany	3.02	0.35	0.17	0.32	0.33	0.70	3.32	0.17
Japan	2.33	0.22	0.27	0.70	0.82	2.01	2.25	0.27
Commodities (USD)								
Gold	4647.60	-11.14	7.44	21.01	48.83	136.04	169.19	7.44
Oil	118.35	63.29	94.49	76.59	58.35	48.36	82.47	94.49
Currency								
GBP-USD	1.32	-1.92	-1.96	-2.05	2.17	6.65	-4.42	-1.96
GBP-EUR	1.14	0.51	-0.07	-0.11	-4.22	0.57	-2.51	-0.07
EUR-USD	1.15	-2.41	-1.89	-1.94	6.67	6.05	-1.97	-1.89
USD-JPY	159.09	1.90	1.50	7.72	6.39	19.54	43.97	1.50

Source: Bloomberg, ICE, London Stock Exchange, MSCI, Standard & Poor's, Stoxx Tokyo Stock Exchange

* Performance is given on total return indices, but the levels are for the main indices.
** Displayed as absolute changes in yields, rather than percentages.

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