The first quarter of 2026 kicked off a volatile start to the year for markets. A war in Iran, combined with AI fears and jitters in private credit, spooked investors and contributed to a slide in risk assets. The quarter ended with the Aggregate Bond Index virtually unchanged and the S&P 500 Index down 4.6%. The total decline in stocks was relatively modest despite the myriads of negative headlines.

At the start of the year, markets were expecting one to two 0.25% rate cuts by the Federal Reserve in the second half of the year. Those expectations have since shifted as inflation risks have re-emerged due to the Iran war. The sharp climb in oil prices, combined with geopolitical turmoil, has led to modestly higher interest rates as well as a slight jump in inflation expectations. The effects of a prolonged conflict would potentially be detrimental to the global economy. That said, the likelihood of a prolonged conflict appears slim, as market volatility and political pressure weigh on the maximum timeline of U.S. involvement in this war.

Despite current headwinds, the U.S. economy has remained resilient. The low-hire, low-fire trend continues, with the unemployment rate sitting at a historically low 4.3% as of March. Consumer spending remains solid, with a 0.5% increase in personal consumption expenditures (PCE) for February. By tracking economic data from 2Q 2020 to 2Q 2025, the Dallas Fed estimates that the top 20% of earners are responsible for 57% of consumer spending in the U.S. Under the surface, however, lower-income earners are struggling, as seen in weaker real wage growth and rising debt delinquency levels among subprime borrowers.

Energy was the best performing sector in the stock market, as crude oil prices recorded their largest monthly increase on record in March. In contrast, technology stocks underperformed, with the Magnificent Seven down more than 12% for the quarter. This marks a sharp reversal from the past three-plus years, during which mega-cap tech contributed disproportionately to the market's gains. We still view valuations as elevated, with a forward P/E of approximately 21x on the S&P 500. That said, fundamentals continue to support this rich multiple, with all-time-high profit margins and consistent upward revisions to forward EPS estimates.

Software companies were hit particularly hard in Q1, with the IGV (iShares Software ETF) down more than 24%, as investors rushed to dump shares of legacy software names due to obsolescence risks from powerful new AI models, such as Claude's Opus 4.7. Markets are increasingly concerned that companies like Adobe and Salesforce may face diminished roles in a world where "vibe coding" via AI models is widely available and inexpensive for enterprises. Flagship portfolios have no direct exposure to pure-play software stocks. We will continue to

Prepared by Flagship Capital Management, Inc.
400 W State Street | Suite 3 | Media, PA 19063
T 610.565.9580 | flagshipcap.com

A copy of Form ADV, our registration statement with the Securities and Exchange Commission, is available at the FINRA website.

monitor this development, as we expect the rapid advancement of AI to eventually impact most parts of the market—and society more broadly.

In the fixed-income space, sharp moves in yields related to the Iran conflict dampened total returns for bonds. The 10-year Treasury continues to trade within its 3.8%–5% range, briefly touching around 4.5% in Q1 during peak uncertainty. We expect limited downside for longer-term bond yields, as markets price in the potential impact of sustained inflation and dovish monetary policy.

The deterioration in private credit is a concerning development. This breakdown highlights the risks associated with a rapidly growing investment space characterized by opaque disclosure requirements and limited regulatory oversight. However, with credit spreads on public corporate bonds remaining at historically tight levels, broader credit markets appear to be signaling that this is an isolated issue within private equity and private credit. Our flagship portfolios maintain limited exposure to private credit, primarily through Janus Henderson CLO ETFs. We remain constructive on these holdings due to their protected (higher tranche) payout structure and relatively lower volatility.

This has been a challenging quarter for investors, but periods of volatility can create opportunities. Our focus remains on staying diversified, maintaining quality exposure across sectors, and positioning portfolios to weather inflationary pressures while participating in long-term growth trends. Thank you for your continued trust in our services. As always, please do not hesitate to contact us with any questions or concerns, or to schedule a portfolio review.

Prepared by Flagship Capital Management, Inc.
400 W State Street | Suite 3 | Media, PA 19063
T 610.565.9580 | flagshipcap.com

A copy of Form ADV, our registration statement with the Securities and Exchange Commission, is available at the FINRA website.