Birch Hill
INVESTMENT ADVISORS

April 2026

NAVIGATING ROUGH WATERS

US equities were little changed while international equities advanced during the first two months of 2026. In March, all equity markets turned lower. In 2026, rapid technological investment and rising geopolitical volatility have complicated traditional economic and market cycles. As we move into the spring, four primary forces—the Iran conflict, a "wait-and-see" Federal Reserve, the massive buildout of Artificial Intelligence (AI) infrastructure, and a shifting labor market—are presenting challenges and opportunities for investors.

THE GEOPOLITICAL TAX: IRAN AND THE ENERGY SHOCK

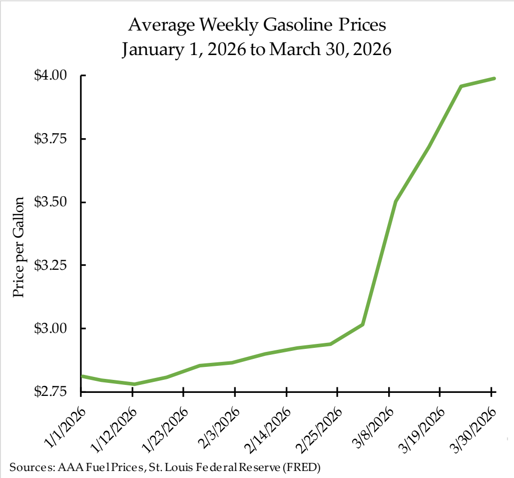
The escalation of the Iran conflict, which began on February 28th, specifically the disruption of traffic through the Strait of Hormuz, has reintroduced stagflationary risks that many hoped were in the rearview mirror. With the price of crude oil surging, we are seeing an immediate "inflationary tax" on global consumers.

For the US economy, the impact is felt through higher prices for gasoline, diesel fuel, jet fuel, home heating oil, and fertilizers. This energy shock acts as a drag on consumer discretionary spending, complicating the path for sectors like retail and travel that were already showing signs of fatigue. The duration of the Iran conflict, an unknown at this point, is key to inflation levels and economic growth in 2026.

MONETARY POLICY: HIGHER FOR LONGER

In response to this energy-driven inflation, the Federal Reserve held interest rates steady at the 3.50%-3.75% range during its March meeting. Prior to the energy price disruption, the Fed was widely expected to reduce short-term interest rates by 0.50% to 0.75% over the balance of 2026. Expectations have been revised to only a 0.25% cut. However, the timeline has become increasingly unclear.

Market Indicators		3/31/2026
	TOTAL RETURN	
US Stock Markets:	12 Mos	1st Qtr 2026
S&P 500 Index	17.8%	-4.4%
S&P 500 Equal Weight Index	12.8%	0.7%
DJ Industrial Avg.	12.2%	-3.2%
S&P 400 Mid Cap	17.3%	2.5%
Russell 2000 Small Cap	25.8%	0.9%
International Stock Markets:		
ETF Returns in US$		
EAFE Index (Europe, Australia, Asia, Far East)	23.1%	1.2%
Japan (MSCI Index)	28.9%	4.6%
China (FTSE 50)	2.7%	-6.2%
Emerging Markets Index	33.1%	3.8%
US Fixed Income Yields:	12/31/2025	3/31/2026
6-Month US T-Bill	3.59%	3.72%
2-Yr US T-Note	3.47%	3.79%
10-Yr US T-Note	4.18%	4.30%



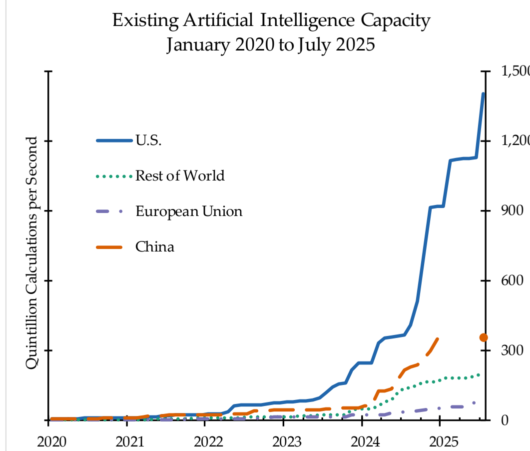
Birch Hill Investment Advisors LLC
One International Place, Suite 770
Boston, MA 02110
Phone: (617) 502-8300
BHBoston.com

The Fed is currently trapped in a dual-threat scenario. Cutting rates to support the labor market risks entrenching the new wave of energy-led inflation, while holding steady may exacerbate the "low-hire, low-fire" environment currently seen in the private sector. For fixed-income investors, this suggests that the era of volatility is far from over, as future rate expectations continue to drift based on the latest headlines from the Persian Gulf.

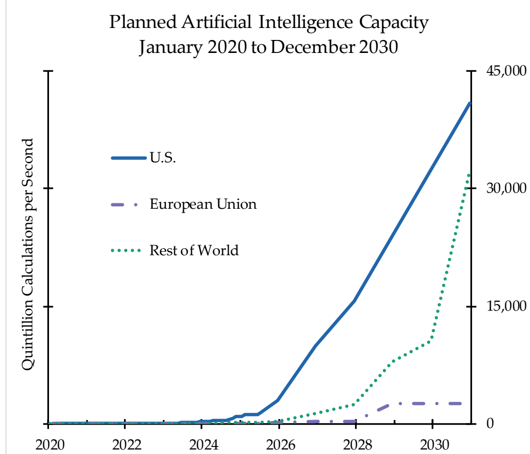
THE AI ENGINE: INFRASTRUCTURE AS GDP

Perhaps the most remarkable feature of 2026 is that, despite these headwinds, US Gross Domestic Product growth remains resilient. A meaningful portion of that resilience appears tied to the AI infrastructure buildout. By some estimates, AI-related capital expenditures—the "Hyper-Capex" from the likes of Microsoft, Amazon, and Alphabet—now accounts for nearly 40% of the growth in total US real GDP.

In a historic shift, business investment in data centers and specialized semiconductors has become a primary engine of marginal economic growth. We are no longer just in a tech boom; we are in a total industrial retooling. This buildout is providing a massive floor for the economy and corporate earnings. Companies selling products and services to data centers are particularly well positioned for the immediate future.



Source: Board of Governors of the Federal Reserve System



Source: Board of Governors of the Federal Reserve System

AI DISRUPTION AND THE LABOR MISMATCH

While the AI buildout is driving economic growth, AI disruption is beginning to manifest in corporate earnings and employment trends—both positively and negatively. We are seeing a widening "return dispersion" between companies that can effectively wrap AI around their business models and those whose traditional knowledge-based services are being threatened.

The February jobs report highlighted a growing mismatch between labor demand and supply. While sectors like information and healthcare saw pullbacks, there remains an insatiable, inflationary demand for power engineers, data center technicians, and AI researchers. We are witnessing a "silent" transformation of the workforce where total headcount remains stagnant, but the premium on specialized technical skills has never been higher.

WILL THE STRESSES OF 2026 RESULT IN FINANCIAL DISRUPTION?

When many changes occur at once, odds of financial disruption increase. We may be seeing this now in the form of falling values of private credit, an aggressive form of debt financing. The prevalence of other “creative” financial instruments suggests a level of caution in the current environment.

INVESTMENT OUTLOOK

While change is almost always present, investors now face multiple major shifts that could, in the shorter term, significantly impact valuations of specific companies and economic sectors as well as the overall economy. The US economy and US financial markets have proven to be amazingly resilient throughout history. We believe this long-term pattern is intact, but investors should be positioned to endure continued volatility for the foreseeable future.

Gary R. Mikula, CFA Robert A. O’Neil, Jr., CFA G. Bowen Cook, Jr., CFA Catherine M. Kennedy, CFP®
Timothy M. Malloy, CFP® Christopher P. Mikus, CFA, CFP® Brett A. Mirliani, CFA, CFP®, CPWA® Adam J. Desjardins, CFA