

Oppenheimer Investment Advisers

What Happened?

Eleven months after Liberation Day, geopolitical risk has again reasserted itself as the single variable that matters. Everything else: interest rates, spreads, equity valuations, is downstream of one question: how far does the Middle East conflict extend, and for how long?

As geopolitical headlines dominated the markets in March:

- Energy prices moved sharply higher following the escalation in the Middle East.
- Headline inflation expectations followed.
- The Federal Reserve's projected benchmark interest rate path forward shifted from two cuts this year to none.
- The bond market repriced significantly in a matter of weeks.

At its March 18th meeting, the Federal Reserve kept the Fed Funds Target Rate unchanged at 3.50%–3.75%. The decision itself was never in question given elevated uncertainty, little change to labor market conditions, firm inflation readings and upside risks to the inflation outlook. The statement, updated projections and press conference collectively emphasized uncertainty while providing limited policy guidance. Chair Powell expressed low conviction around the updated projections, noting publicly that "we just don't know" how geopolitical events will evolve. Powell also addressed his own tenure, indicating he would remain as Chair on a pro-tempore basis if a successor is not confirmed by the time his term expires on May 15th. He added that he would remain a Fed governor until the DOJ's investigation is "well and truly over with transparency and finality" and left open the possibility of serving on the Board through his governor term ending in 2028.

With crude oil moving from \$65 to above \$100 per barrel, the 5-year Treasury sold off 44 basis points. Because all bonds price off the Treasury curve, the repricing was broad-based. March produced an unusually sharp negative month for fixed income driven entirely by energy and geopolitics, not by any deterioration in credit fundamentals.

Reference Yields moved lower across the curve:

- 5-year Treasury: 3.50% → 3.94%
- 5-year AAA Muni: 2.11% → 2.68% (Taxable Equivalent Yield ~4.53%)
- 10-year Treasury: 3.94% → 4.32%
- 10-year AAA Muni: 2.52% → 3.16% (Taxable Equivalent Yield ~5.34%)

Taxable Equivalent Yield (TEY) represents the yield a taxable investment would need to provide to equal the yield of a tax-exempt municipal bond. TEY shown assumes the highest marginal federal income tax rate currently in effect and does not account for state or local taxes. Actual tax benefits will vary based on an investor's individual tax situation.

Reference Risk/Return Snapshot for the Month:

3/31/2026	MTD	YTD	2025	2024	TEY*	YTW**	DUR	#ofHldgs	RTG
ICE BofA Current 2-Year US Treasury Index	-0.49%	0.23%	4.85%	3.74%	3.80	3.80	1.91	1	AA1
ICE BofA Current 5-Year US Treasury Index	-1.53%	-0.01%	6.85%	1.23%	3.95	3.95	4.51	1	AA1
ICE BofA Current 10-Year US Treasury Index	-2.52%	-0.11%	7.82%	-1.69%	4.32	4.32	8.07	1	AA1
ICE BofA Current 30-Year US Treasury Index	-3.90%	0.30%	3.27%	-8.03%	4.91	4.91	15.77	1	AA1
BBG Municipal Bond	-2.32%	-0.18%	4.25%	1.05%	6.38	3.77	6.81	64,661	AA2/AA3
BBG Municipal Bond: 5 Year (4-6)	-1.77%	0.01%	5.03%	1.17%	5.10	3.02	3.67	6,798	AA2/AA3
BBG Municipal Bond: 10 Year (8-12)	-3.09%	-0.79%	5.92%	-0.33%	5.97	3.54	6.05	13,128	AA2/AA3
BBG Muni Managed Money	-2.76%	-0.48%	3.94%	-0.05%	6.09	3.61	7.86	26,504	AA1/AA2
BBG Muni High Yield (non-IG)	-1.90%	0.71%	2.46%	6.32%	n/a	5.66	7.63	5,938	BA2/BA3
BBG U.S. Corp Inv Grade	-1.98%	-0.54%	7.77%	2.13%	5.14	5.14	6.78	8,702	A3/BAA1
BBG Interim. U.S. Gov/Crdt	-1.22%	-0.02%	6.97%	3.00%	4.20	4.20	3.74	6,576	AA2/AA3
BBG U.S. MBS	-1.65%	0.40%	8.58%	1.20%	4.83	4.83	5.36	1,067	AA1/AA1
BBG U.S. Aggregate	-1.76%	-0.05%	7.30%	1.25%	4.57	4.57	5.88	14,086	AA2/AA3
BBG U.S. Corp High Yield	-1.18%	-0.50%	8.62%	8.19%	7.40	7.40	3.02	1,926	BA3/B1
BBG U.S. Treasury: TIPS	-1.34%	0.26%	7.01%	1.84%	4.26	4.26	4.16	48	AA1/AA1
BBG U.S. Treasury	-1.74%	-0.04%	6.32%	0.58%	4.14	4.14	5.82	296	AA1/AA1

* (Taxable Equivalent Yield = YTW adjusted for top Federal tax bracket + 3.8% surcharge for approp. Munis)

Source: Bloomberg, ICE and OIA

** (Index Performance shown for illustrative purposes only. Indexes are unmanaged and investors cannot directly invest in an index)

All yield figures represent gross market yields and do not reflect the impact of fees or expenses. Index performance is not indicative of the performance of any particular investment. Indexes are unmanaged and their returns do not take into account any of the costs associated with buying and selling individual securities. Individuals cannot invest directly in an index. Past performance is not indicative of future results.

What Are We Thinking?

The initial instinct in markets was to frame March's move as a replay of 2022. While that framing is understandable, we believe it is also analytically incomplete. In 2022, commodity prices surged broadly and simultaneously across categories as the pandemic economy reopened — the Federal Reserve was behind the curve, inflation became the dominant narrative, and bonds lost significant value as a result. What is unfolding today is structurally different: this is an energy-driven shock, not a broad commodity event. That distinction is consequential for understanding where rates go from here.

We believe a more instructive reference point may be 1990. During that year, Iraq's invasion of Kuwait pushed oil from \$20 to \$40. The S&P 500 declined 20 percent. The 10-year Treasury briefly exceeded 8 percent. Unemployment reached 6 percent. Inflation was elevated. The Federal Reserve did not raise rates. Benchmark interest rates were held as oil peaked and only cut when the Savings and Loan crisis tightened financial conditions to the point where growth became the dominant concern. Inflation gave way to recession risk and rate cuts followed.



Source: Bloomberg. Third Party Information is provided for informational use only and does not necessarily reflect the view of Oppenheimer Asset Management.

Additionally, two additional factors make today's version of that story more contained than it may appear. First, the U.S. economy is approximately half as energy-intensive as it was in 1990. Second, the Federal Reserve enters this episode with rates already 50 to 75 basis points above its own estimated neutral level (meaning the Fed has less work to do than the rate market is currently pricing).

The longer this conflict extends, the harder it becomes to treat the oil move as temporary. Refined products, jet fuel most visibly, are trading at elevated premiums. Beyond price, the more consequential risk is volume: whether supply constraints rather than cost alone begin to restrict real economic activity. Parts of the globe, with significant imported energy exposure, are already absorbing disproportionate pressure. References to rationing and shortage, words absent from market commentary for years, are reappearing. Even in a resolution scenario, the floor for energy prices is not where it was. Inventory drawdowns, infrastructure damage, and structural imbalances across key producing regions do not reverse quickly. The distribution of outcomes for oil, and by extension for inflation expectations and interest rate pricing, remains unusually wide.

In our base case scenario, we do not see a high probability path to Fed rate hikes from here. Wage growth is running below the pace required to sustain inflation above 2 percent. Even taking the last March payroll data into account, the labor market appears to indicate softening trends. Long-run inflation expectations still seem contained. A shock large enough to produce persistent inflation would almost certainly also produce enough demand destruction to bring growth concerns to the foreground, at which point the policy calculus shifts, as it did in 1990. Fed communications historically show little correlation between oil price spikes and incremental tightening decisions. The data continues to support patience.

Bottom Line: The magnitude and duration of the oil price shock will determine the severity of the macro disruption and the risk of forced demand destruction and recession. The resilience of the U.S. consumer still remains our base case. However, sustained energy prices at current levels would materially offset the consumer tailwind from OBBBA-related stimulus. Prolonged energy pressure would also raise the probability of a more defensive hiring stance across corporate America. Against that backdrop, the bar for Federal Reserve rate hikes is high. Inflation

expectations remain anchored. The United States is a net energy exporter. Those two structural conditions, together, create a favorable environment for short to intermediate maturity taxable and tax-exempt fixed income.



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* (Taxable Equivalent Yield = YTW adjusted for top Federal tax bracket + 3.8% surcharge for appropriate Munis, state and local taxes are not considered in this calculation). The views expressed herein are those of the authors as of the date indicated and may change without notice. They do not necessarily reflect the opinions of Oppenheimer & Co. Inc. or its affiliates and should not be construed as a firm recommendation or investment advice.

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