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When writing the January quarterly letter, we didn't expect that the next letter would be about the effects of war on financial markets, yet that's where we are. The air attacks on Iran by a joint US-Israel force on February 28 took the world by surprise and have dominated financial markets since. Unfortunately, this is not the first time we've had to face this problem. Such military actions always distress financial markets, because they create uncertainty that strikes at the fundamental activity of businesses. As a result, markets are always on the alert for the danger of war. The stock market usually starts selling off at the first drumbeat, although it can be startled by a surprise strike (as with this one).

Virtually everyone has an opinion on whether such conflicts are wise foreign policy or whether they are morally justified, but as investors we must deal with *what is*, not *what should have happened*. In that regard, investors should focus on three questions. First, what is really happening? This is always difficult because the infamous "fog of war" is a real thing. Even combatants on the ground often don't really know what's going on. So, how is an investor halfway around the world supposed to know? We do our best to find out what's happening through a variety of sources, both public and private. Technology helps, too. For example, when the US or Iran declares that the Strait of Hormuz is open, anyone with an internet connection can monitor the ship traffic in the Persian Gulf and see if this is true. They may say it's open, but if no ships are traversing, then it really isn't.

The next question is, what is most likely to happen going forward? As investors, we are always dealing with the future (a tough subject!). The unpredictable nature of war makes this question even more difficult. As we often say, we are not really forecasters, we're odds-makers. We deal with probabilities by assigning a factor to each of the most likely outcomes, with the highest probability outcome becoming our "forecast." The problem wars present is that you really can't rule out many outcomes. Even the most probable outcome (in our minds) may well have less than a 50% probability. I could provide many examples from the history of warfare, but this short letter doesn't provide room. Suffice it to say that the best forecast is to remain prepared for any outcome.

The last question for investors is, what are the likely impacts of these scenarios on businesses and financial markets? This is an easier question for us if we have answers to the first two because we study daily the impacts of adverse events on businesses. In the case of the current conflict, all of the various scenarios really revolve around the same question: is the Strait of Hormuz open or closed? We take such waterways for granted, because in the modern world they are usually always open. But they're not called chokepoints for nothing. There are about two dozen relatively narrow passages in the world's seas where seaborne commerce regularly travels. Some are canals, but most are straits (narrow passages between two land masses). Of these, nine are deemed especially vital to world commerce, both for the volume of trade that traverses them and the lack of good alternative routes should they be closed. The Strait of Hormuz is easily among these most critical chokepoints.

Under normal conditions, about 120 commercial vessels per day transit this strait from one of the most resource-rich regions of the world to nations beyond. In addition to one-third of the world's crude oil, the following products transit the strait: about one-fifth of the world's liquefied natural gas (LNG), ammonia, and phosphate; about one-quarter of the world's refined petroleum products; about one-third of the world's fertilizer and helium; about 40% of the world's urea and methanol; and roughly half of the world's sulfur. These commodities are the building blocks of modern civilizations. Substantial reductions raise prices dramatically as processors and manufacturers scramble for supply, which results in higher prices for consumers. Outright shortages can also develop.

The stock market has been rather sanguine about all this. Of course, many companies can do well in this climate. Most commodity prices are up year-to-date, which means stocks of oil and gas and other commodity producers are higher. Many US oil refineries and chemical stocks have also seen gains because their North American inputs of oil and natural gas are much cheaper than world prices.

In the long term, well-run businesses are remarkably resilient to shocks of this kind. These businesses prepare for harmful uncertainties, scenario-test strategies to navigate adverse conditions, and implement those plans when they occur. If these conditions prove to be long-lasting, such businesses adjust their own strategies as needed. It is our observation that well-managed businesses emerge stronger from the stresses of these types of circumstances. This is why investment in quality common stocks, either directly or through exchange-traded funds, is the cornerstone of all our strategies.

As professional investors, we are professional worriers. We raise these issues not to alarm you, but to inform you that we are fully aware of the current risks, which are not new to us. Our macroeconomic team has been writing for well over a decade that the world is deglobalizing and doing so more rapidly than most people realize. The events in the Middle East have clearly accelerated this trend. It is our hope that hostilities end soon and that the Strait of Hormuz opens quickly and stays open, but we believe our investment strategies are well-prepared for any outcome.

We appreciate your confidence in us.

Gratefully,

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CEO and Chief Investment Officer

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