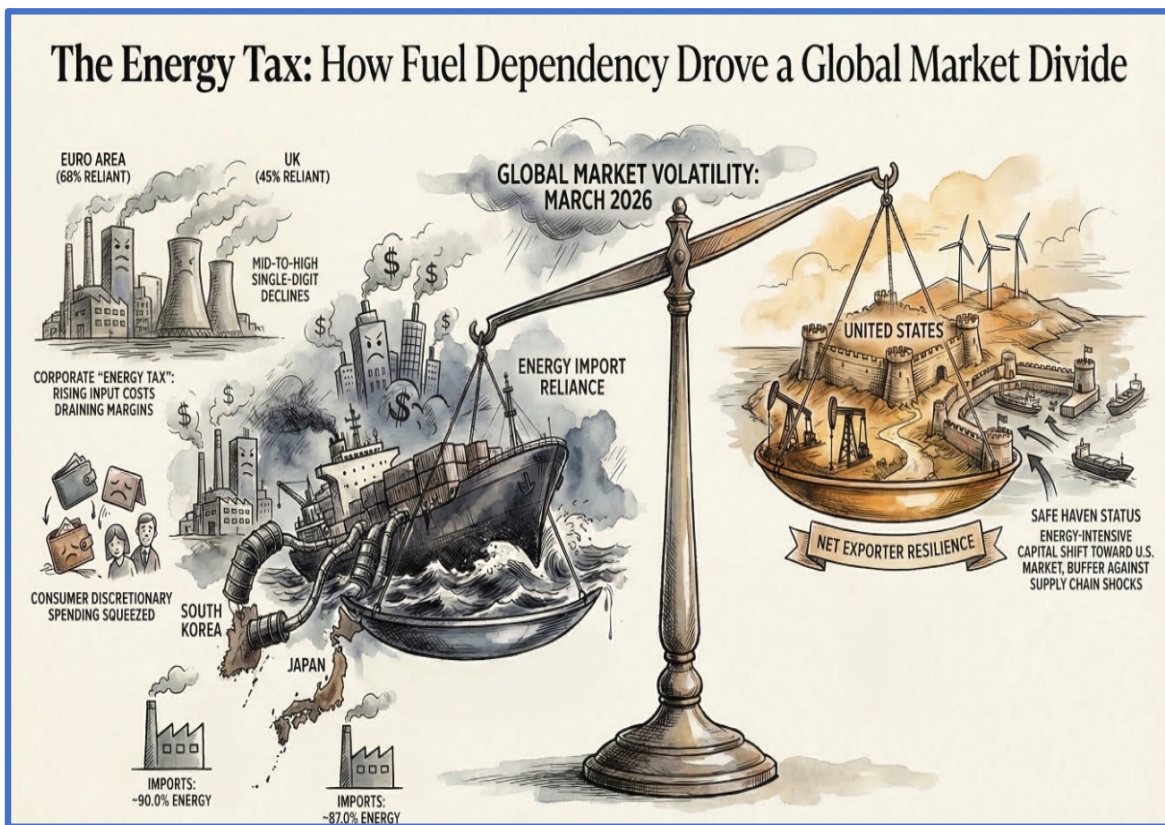




## The Energy Tax: How Fuel Dependency Drove a Global Market Divide

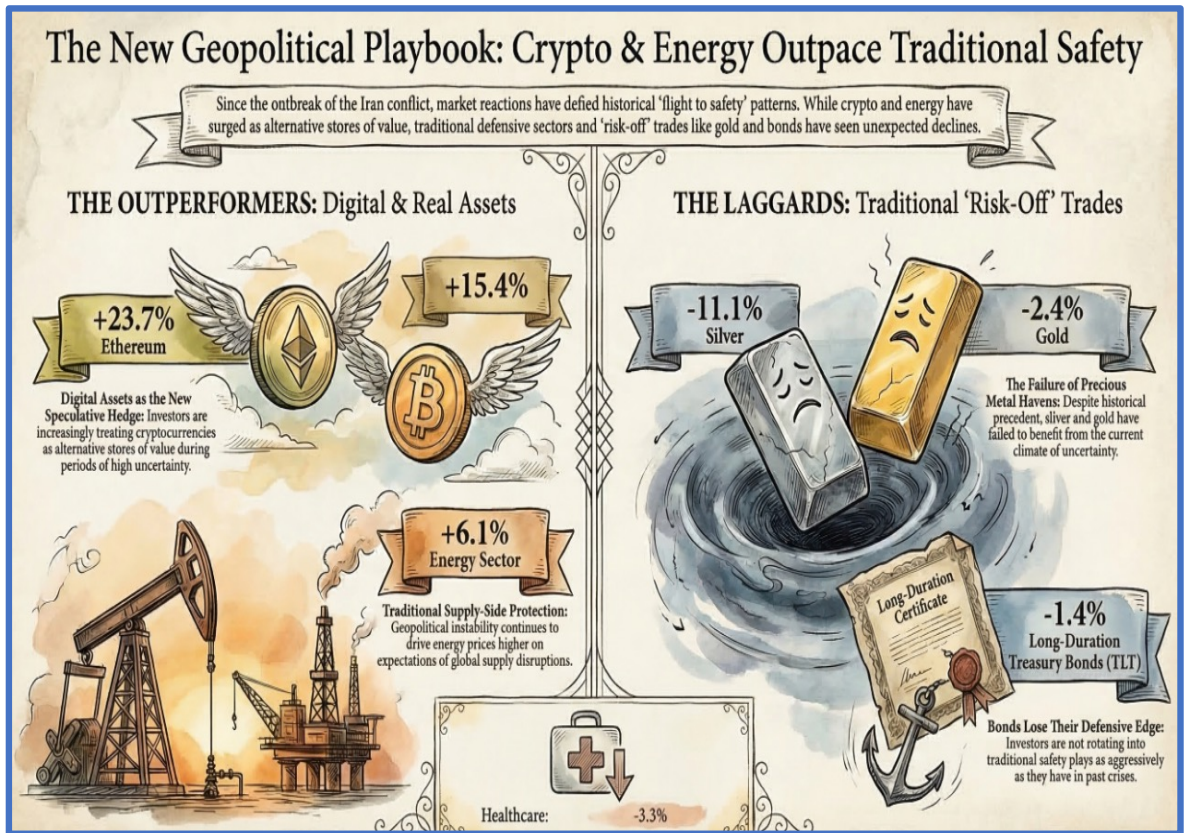


Source: Edward Jones

The recent volatility in equity markets offers a clear lesson in how energy security shapes financial resilience. Between March 1 and March 12, a surge in global energy prices exposed a stark divergence in market performance across major economies.

Countries heavily dependent on energy imports bore the brunt of the sell-off. South Korea and Japan—importing roughly 85% to 90% of their energy—saw equities plunge by 13.1% and 9.3%, respectively. For these industrial economies, rising energy costs function like an immediate tax, compressing corporate margins and eroding consumer spending power. The Euro Area (68% import dependence) and the UK (45%) faced similar pressure, posting mid- to high-single-digit declines.

In contrast, the United States stood apart. As a net exporter of energy, it largely avoided the severe drawdowns seen elsewhere. With a comparatively modest 3.0% decline over the same period, the S&P 500 continues to benefit from its position as a relative safe haven for energy-sensitive capital.



Performance 3/1/26 to 3/12/26

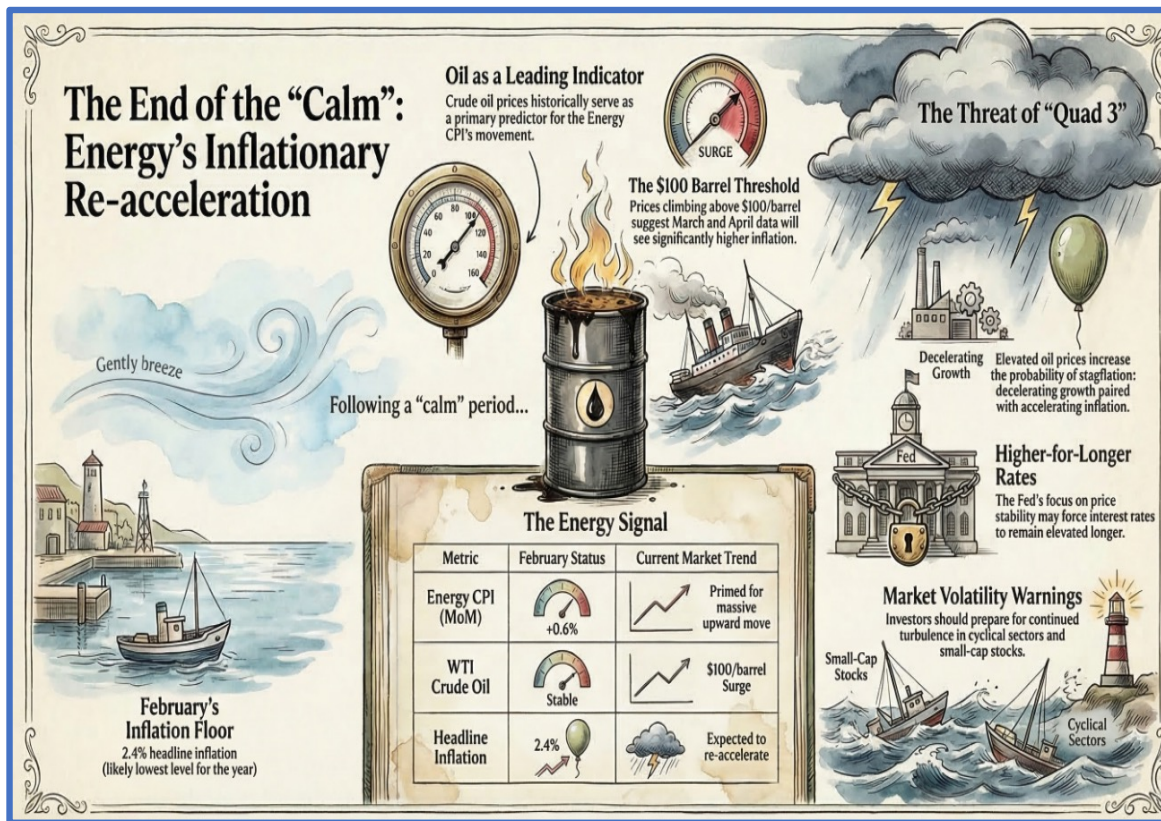
Source: Fundstrat

While the performance of global indices did not provide major surprises, that was not the case for other assets. Since the outbreak of the conflict, crypto and energy have clearly emerged as the top-performing segments relative to the S&P 500.

Leading the charge is Ethereum with an impressive +23.7%, followed by Bitcoin at +15.4%. This strength would suggest investors are once again viewing digital assets as an alternative stores of value or a hedge during uncertain times. Energy, up +6.1% is the expected response to a geopolitical instability around the disruption of oil supply.

However, some classic "risk-off" assets have been surprisingly weak. Long-duration bonds, represented by the 20+ Year Treasury ETF, are down -1.4%, while financials and gold have also declined. In the short-run, these investments seem to be reacting more to inflation concerns. However, they are likely to get a bid once decelerating economic growth becomes the primary concern of investors. Defensive sectors like healthcare (-3.3%) and staples (-2.5%) have also underperformed, signaling that investors are not rotating into traditional safety plays as aggressively as in past crises.

This divergence hints at a more complex market dynamic—one where liquidity, positioning, and evolving narratives around inflation and rates may be outweighing historical patterns. Overall, this data underscores a shifting landscape. Instead of a textbook flight to safety, markets are favoring selective growth and real-asset exposure. In today's environment, "risk-on" and "risk-off" may no longer be as clear-cut as they once were.

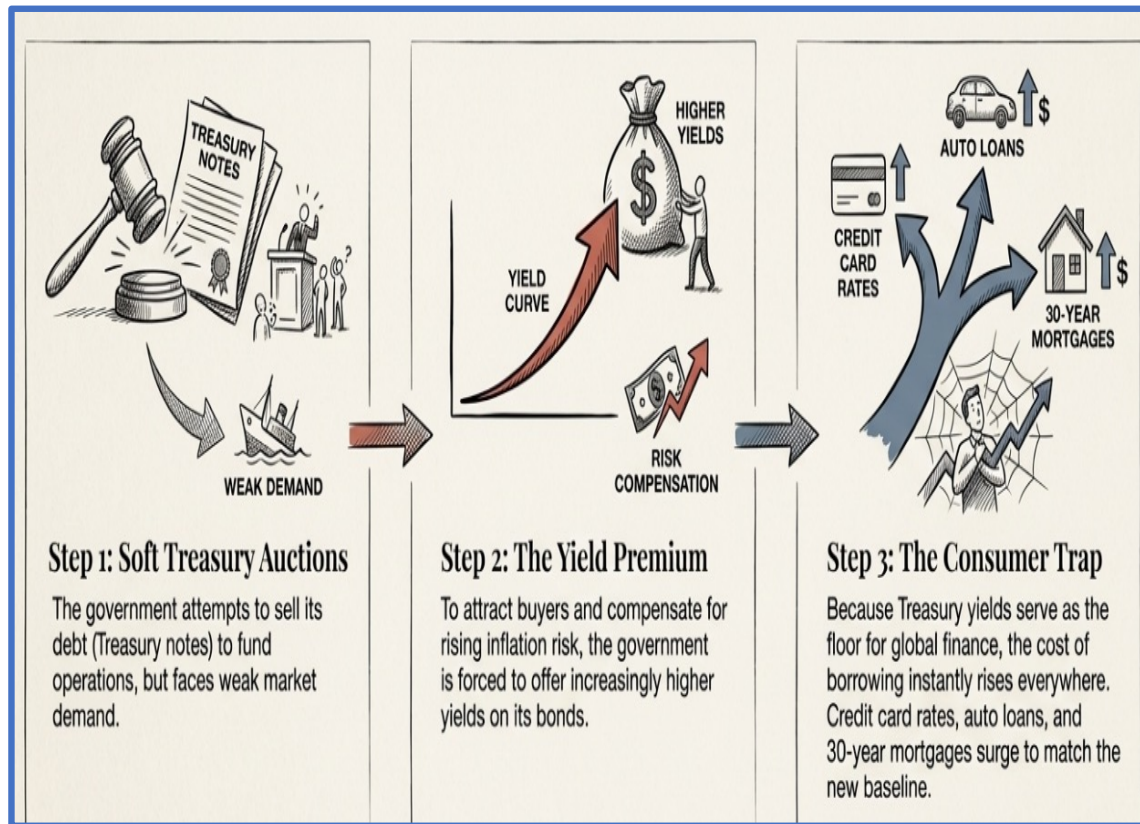


Source: Edward Jones

The price of oil and the energy component of the Consumer Price Index (CPI) are highly correlated. Historically, crude oil has served as a leading indicator for energy CPI. The recent sharp spike in oil prices—driven by geopolitical tensions and supply constraints—suggests the energy CPI is poised for a significant upward move. While February’s CPI report showed a modest 0.48% year-over-year increase in energy, the real-time surge in oil prices above \$100 per barrel suggests materially higher YOY readings for the March and April data.

An acceleration in year-over-year CPI has important implications for our economic framework. It signals a potential shift toward either Quad 2 (characterized by accelerating growth and inflation) or, more concerning, Quad 3—where growth decelerates while inflation accelerates, commonly referred to as stagflation. The longer oil prices remain elevated, the greater the probability the economy transitions into this stagflationary regime. This would be a meaningful departure from our outlook at the beginning of the year, when tax cuts and rate cuts were expected to provide a tailwind to economic growth.

The seemingly “calm” 2.4% headline inflation reading in February is likely to represent the floor for the year. With the Federal Reserve, under new leadership, focused on restoring price stability, this energy-driven reacceleration in inflation could necessitate a prolonged “higher-for-longer” interest rate stance. As a result, investors should be prepared for continued volatility, particularly in cyclical sectors and small-cap equities.



Source: Hedgeye Podcast

The current conflict is likely to widen the fiscal deficit, putting continued upward pressure on borrowing costs for both small businesses and consumers.

To finance expanding government operations and rising military expenditures, the U.S. Treasury must issue increasing amounts of debt. However, with the national debt approaching \$40 trillion, marginal demand from global buyers appears to be softening. When demand for Treasury securities weakens, the government faces tighter liquidity conditions.

To attract buyers, the Treasury is forced to offer higher yields—effectively increasing “risk compensation.” Investors require greater returns to offset the combined pressures of elevated inflation and an expanding supply of bonds. The result is upward pressure across the yield curve, raising the overall cost of capital.

This is where macro dynamics directly impact the real economy. Treasury yields serve as the benchmark for virtually all borrowing, so increases at the sovereign level quickly translate into higher financing costs across the system. Thirty-year mortgage rates have moved back above 6%, while auto loans and credit card rates remain near cycle highs.

The conflict in the Middle East acts as a powerful accelerant to this dynamic. Direct war-related spending—estimated at roughly \$95 billion over a short period—necessitates additional debt issuance, while oil prices near \$100 per barrel push inflation expectations higher. This dual pressure reinforces elevated yields, effectively locking consumers and businesses into a persistently high-interest rate environment.

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