

Executive Summary: After three consecutive years of double-digit returns, the S&P 500 begins 2026 from historically elevated levels. While fundamental support exists for continued gains, extreme sentiment readings, stretched valuations, and midterm year seasonality suggest a choppier path ahead. This environment favors strategies that balance equity participation with downside protection.

Rare Air

The S&P 500 rose 1.4% in January 2026. A positive January is historically a good sign - when January is positive, the S&P 500 has historically averaged full-year returns around 12-15%.

However, the magnitude of recent gains presents a meaningful challenge going forward. 2025 was the third straight double-digit year for stocks, and there have only been two examples in 100 years where we get a fourth year:

- 1957 (post-war boom & record expansion, streak continued for 6yrs)
- 1999 (tech bubble, followed by 3yrs of losses)

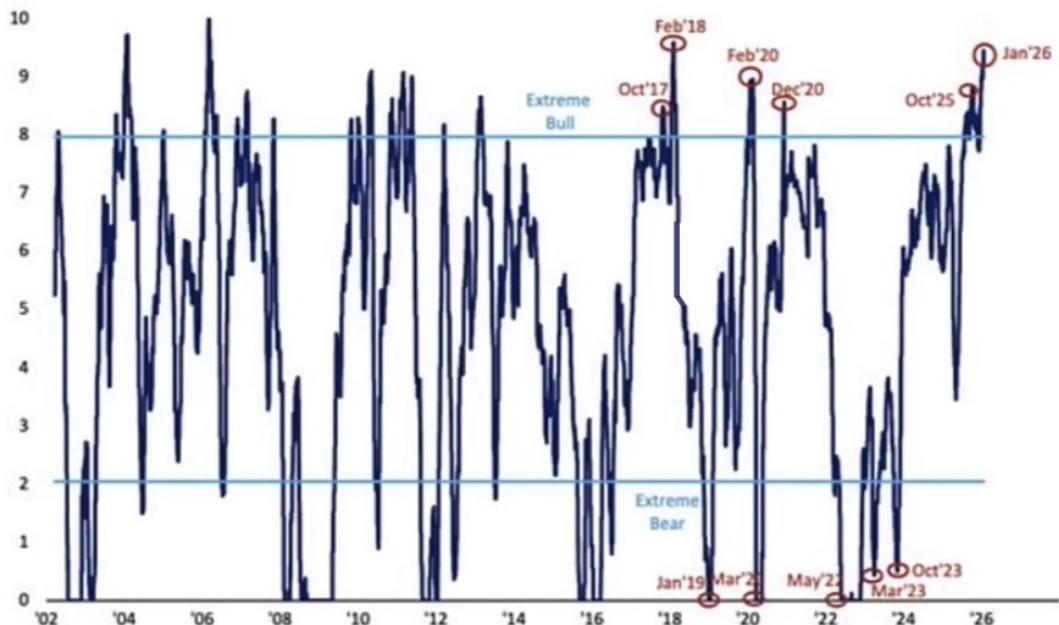
While 1957's expansion continued, it occurred with debt/GDP at 60% vs today's 125% and started from much more modest valuations. The 1999 parallel, which shared today's extreme valuations, ended in a 50% decline.

This is clearly Rare Air. The key question facing investors: Are we in the early stages of an AI-driven expansion that, combined with pro-growth fiscal policy, can sustain elevated valuations? There is some fundamental support for this. Corporate profit margins are near record highs and changes at the Fed could lead to even more market accommodation. Additionally, demographic trends have turned favorable for the first time in decades, The Millennial generation is now bigger than the Boomer generation that drove the economic expansion of the 1980s & 1990s.

However, several factors warrant caution. Market valuations are at all-time highs (market cap/GDP is at 2.3x), and Debt/GDP is at 125% (compared to 50-60% for both periods above). Elevated debt service constrains fiscal flexibility and may limit the economy's growth potential.

Market Sentiment at Extremes

According to Bank of America's Bull/Bear indicator, which dates back to 2002, we are in "Extreme Bull" territory. In fact, it is the second highest reading since before the 2008 market crash.



Source: BofA Global Investment Strategy, EPFR Global, FMS, CFTC, MSCI

It bears noting that this analysis tracks the percentage of newsletter writers who have a bullish long-term view. This differs from shorter-term indicators like the Fear & Greed Index, which, after a choppy start to February, currently shows a Neutral reading of 50.

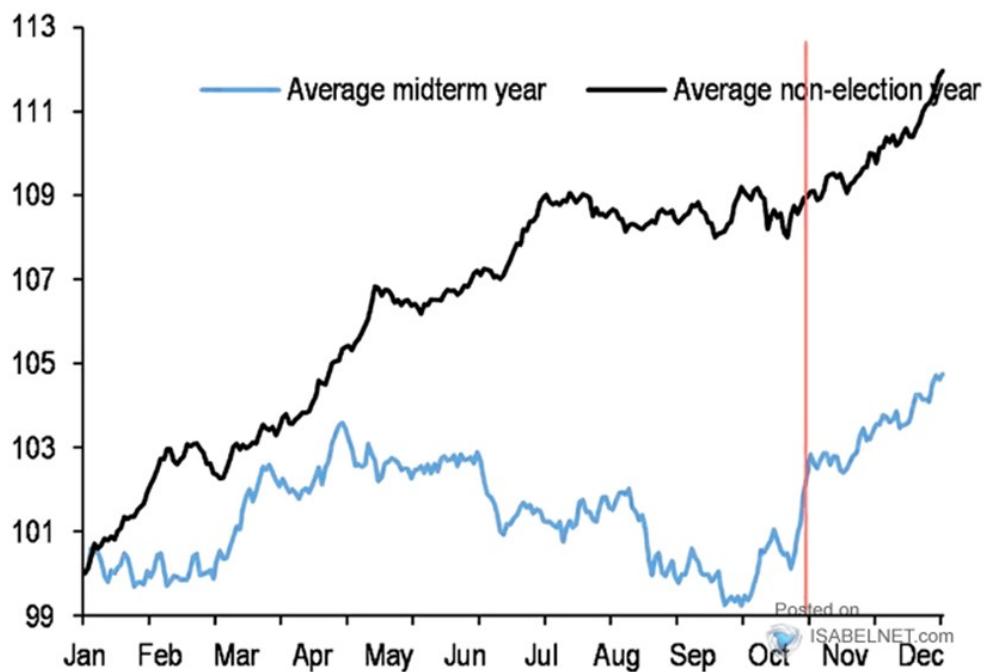
This environment warrants careful consideration of market cycle dynamics and the emotions that typically accompany them. We are clearly somewhere in the green section. But have we seen Euphoria yet? Perhaps in some of the AI stocks we have. But many companies are still trading at average multiples. Regardless of the precise stage, the preponderance of evidence suggests late-cycle conditions warrant a more defensive posture. This environment favors capital preservation over aggressive risk-taking.



Midterm Year

Additionally, 2026 is a midterm election year—historically the most challenging year in the presidential cycle. It's important to know that midterm years are typically choppy and sideways moving. See the blue line below, which show the average pattern of the stock market during midterm years since 1946. It's traditionally been the most challenging year of the four year cycle. Notably, midterm years since 2002 have averaged returns of just 4.2%, compared to 11.5% for the full 4-year cycle. Given we're already starting from elevated levels, 2026 may test investors' patience.

Average S&P500 level (indexed at 100 in Jan) for midterm and non-election years. Sample starts in 1946



Source: J.P. Morgan

The Case For Hedged Equity

While equities remain the cornerstone of long-term wealth creation, risk management becomes paramount during extended periods of strong performance. There are times it makes sense to hedge that equity exposure. Our covered call strategy has a 24+ year track record of delivering 82% of the S&P's annual return at 40% **less** risk. There have been seven significant market selloffs over this timeframe (presented individually below). For every \$100 lost in the S&P during these drawdowns, our clients typically lost only \$58 (42% protection). And they stayed invested through the recovery rather than capitulating at the bottom.

Over our 24+ year track record, there have been 7 market sell-offs greater than 10%

- Average S&P 500 sell-off - 22.0%
- Van Hulzen - 12.7% >>> 42%+ protection vs S&P
- Covered Call Index (BXM) - 16.7%

Time Period	ABSOLUTE RETURN				DOWNSIDE CAPTURE		
	S&P 500	BXM	HYG	VAM	BXM	HYG	VAM
A) October 2007 - February 2009	-50.9%	-35.8%	-23.7%	-33.7%	70%	47%	66%
B) April 2010 - August 2010	-10.9%	-4.3%	-2.2%	-1.8%	39%	21%	16%
C) April 2011 - September 2011	-16.3%	-12.2%	-7.2%	-8.7%	75%	44%	54%
D) September 2018 - December 2018	-13.5%	-10.8%	-4.2%	-5.1%	80%	31%	38%
E) February 2020 - March 2020	-19.6%	-21.3%	-12.0%	-14.6%	109%	61%	74%
F) January 2022 - September 2022	-23.9%	-17.0%	-14.4%	-13.7%	71%	60%	57%
G) February 2025 - April 2025 (daily)	-18.7%	-15.5%	-3.2%	-11.4%	83%	17%	61%
AVERAGE	-22.0%	-16.7%	-9.6%	-12.7%	75.4%	40.2%	52.4%

Key Point: Our strategy has provided better protection than its equity and covered call benchmarks during every major pullback of the last 20 years (average downside cushion of 40%+).

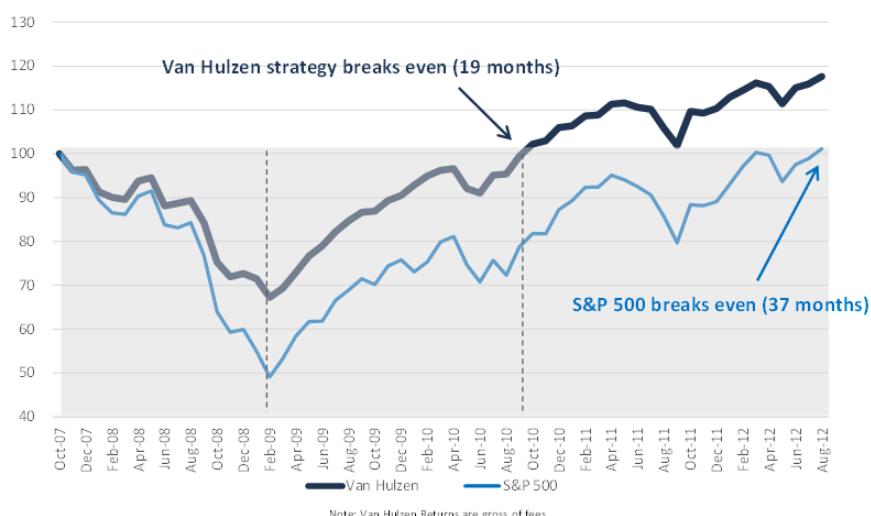
Note: There is no assurance that the Strategy will achieve its investment objectives. The use of covered call strategies does not ensure profits or guarantee against losses. VAM returns are presented gross of fees.

Upside participation

Downside protection is only valuable if accompanied by meaningful participation in subsequent recoveries. By preserving capital during drawdowns, the strategy reached new highs in 6 of 7 recovery periods—typically in roughly half the time required by the S&P 500. The 2008-09 crash and recovery is a great example.

How Did the Strategy Perform in 2008-2009?

It took 37 months for the S&P 500 index to make up its losses from the 2008-09 stock market crash. The Van Hulzen covered call strategy reached break even after 19 months.



Our strategy has achieved new highs faster than the S&P 500 in 6 of the 7 sell-offs from the previous page, typically in about half the time. Losing less during sell-offs makes it significantly easier to recover your losses.

Of course, in strong bull markets like 2023-2025, our strategy captured less upside due to the call premiums we collect. However, this is precisely the trade-off that provides the downside protection shown above.

2026 Outlook: Choppy Road Ahead, Stay Invested but Hedge Your Bets

Our 2026 outlook reflects cautious optimism tempered by late-cycle realities. The backdrop remains constructive: inflation has moderated meaningfully from its peak, central banks are closer to the end of their tightening cycles, and earnings growth expectations remain positive. Following three consecutive years of double-digit returns, risk-reward dynamics have become less favorable. Valuations are stretched in segments of the market and policy uncertainty persists.

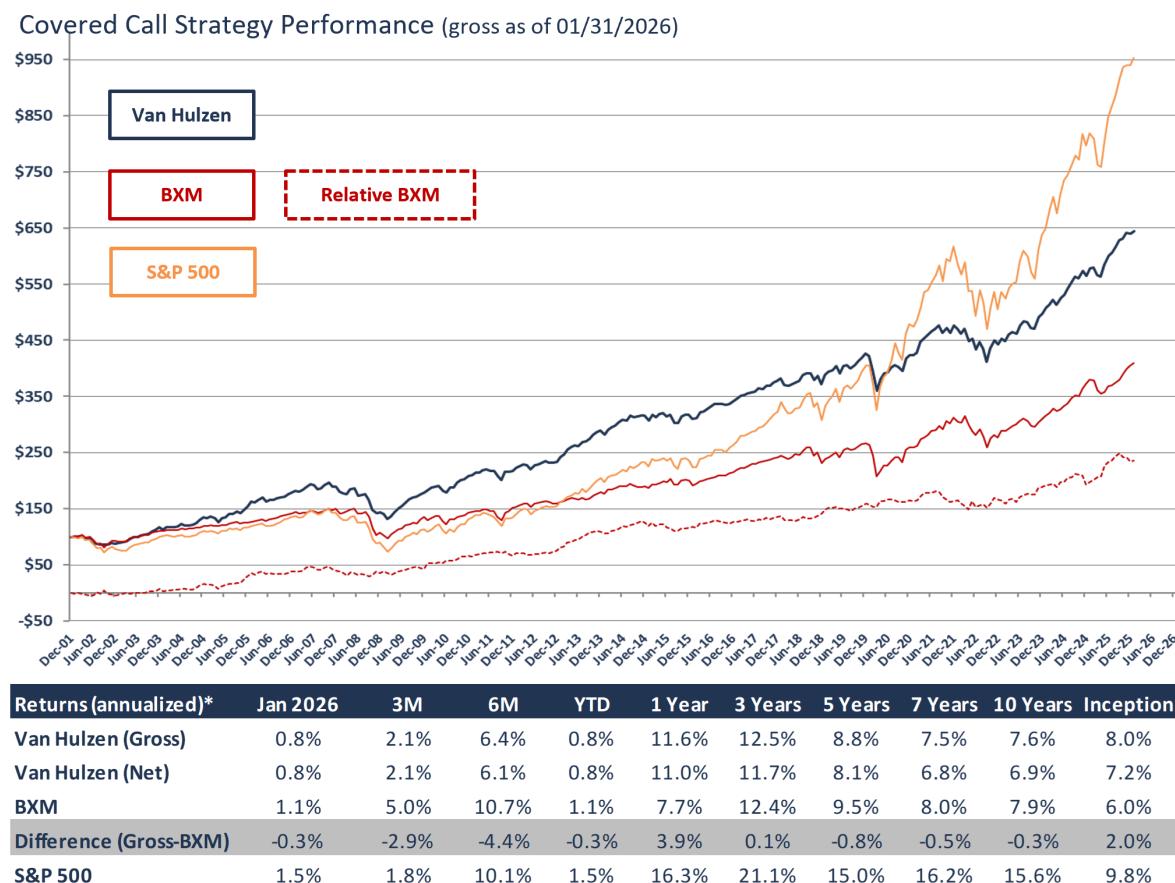
In this environment, risk management becomes increasingly important. Quality, diversification, income, and downside resilience are as important as ever as markets transition from recovery-driven gains to more normalized returns. Going forward, equity returns will depend more on earnings growth and capital discipline than on valuation expansion.

Against that backdrop, hedged equity strategies appear particularly well-positioned for the next several years. Three consecutive years of double-digit returns have meaningfully shifted the risk-reward calculus. Hedged equity offers a way to remain invested in stocks while dampening volatility, managing drawdowns, and potentially smoothing returns through different market regimes. These strategies have historically performed best during periods of elevated volatility, sideways markets, or modest positive returns—conditions we believe are increasingly likely.

In summary, In summary: equity markets can continue to advance, but the path forward will likely prove choppier and more selective than recent years. A disciplined approach balancing participation with protection—particularly through allocations to hedged equity—appears well-suited to navigate the next phase of this market cycle.

Van Hulzen Covered Call Strategy

The Van Hulzen Covered Call strategy invests in US companies that we consider to have high shareholder yield (dividends and share repurchases) and uses call options with the goal of reducing portfolio volatility and creating incremental income. The goal is a portfolio that has equity exposure while seeking higher than average annual income (target of 6-8% annual), although there is no guarantee that the strategy will achieve its objective, generate profits or avoid losses. Below you will find the graph of the Van Hulzen Covered Call Strategy and the Covered Call Index BXM.



*Inception date : 12/31/2001. Figures greater than one year are annualized. Van Hulzen returns represent actual returns from composite of accounts. Source: Bloomberg, Tamarac

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