

15 minutes

# Oil Shock Meets AI Boom

Monthly Perspectives  
May 2026

# Oil Shock Meets AI Boom

Higher oil prices are squeezing households and reshaping industries, yet investors continue betting that the AI boom can offset the damage.

By Kevin Yulianto, Portfolio Manager | TD Wealth

Analysts, in the wake of the Iranian Revolution of 1979, have often wondered what would happen if conflict flared up in the Middle East and disrupted the flow of oil from the Gulf. Of course, since then we have had the Gulf War in 1990, the Iraq invasion in 2003 and more recently the Israel-Gaza conflict in 2023 to 2024. But none of them involved the closure of the Strait of Hormuz for an extended period, which is the case today.

This, for many strategists, is the nightmare scenario — a Middle East conflict unleashing ripples that hit every corner of daily life. Oil isn't just about fuelling cars and planes; it's woven into almost everything we touch and use, from food containers and electronics to auto parts, athletic wear and essential medical supplies. All of these rely on crude oil derivatives. In the U.S., a staggering 26% of crude oil powers industrial production for consumer goods, second only to the 68% that keeps transportation moving. The impact is everywhere — and it's impossible to ignore.

Currently, an estimated 14.4 million barrels per day is being disrupted, equivalent to around 13% of global supply (Figure 1). This is highly disruptive for the global economy and markets. Europe has lost about 20% of its normal supply of jet fuel and is facing a shortage by the summer.

## Executive Summary

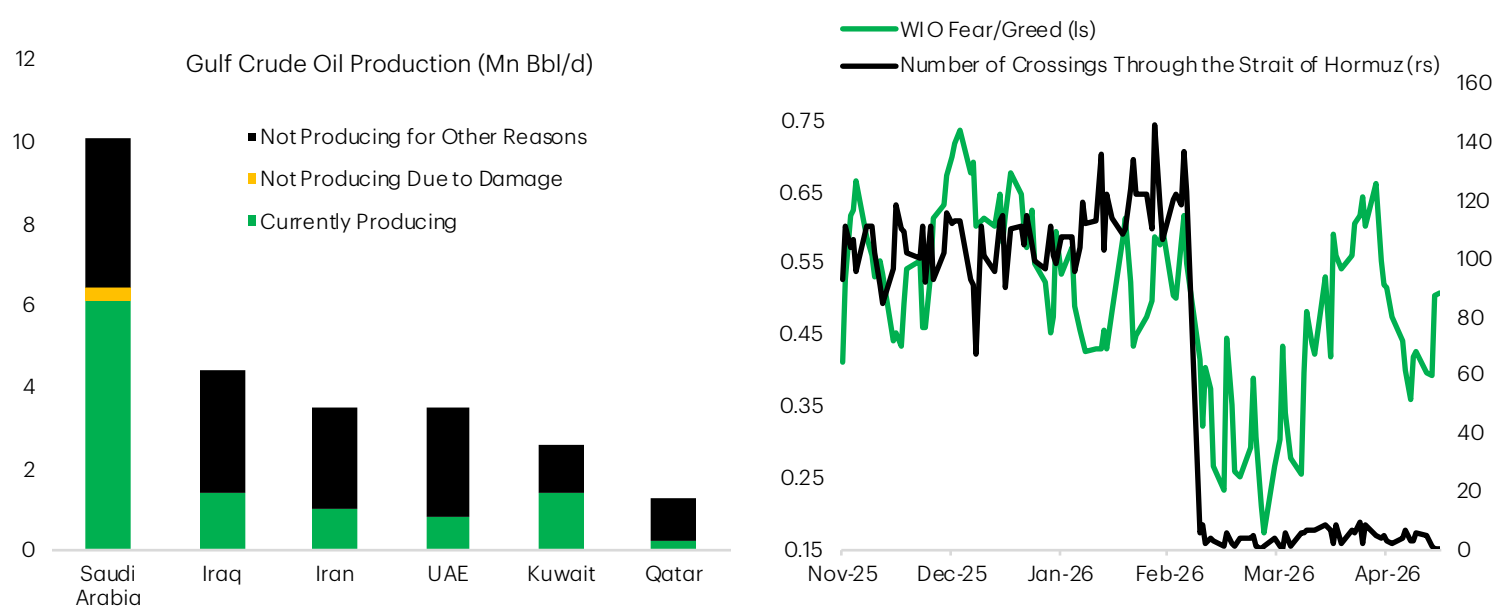
The blockade of the Strait of Hormuz has disrupted approximately 13% of the global oil supply, causing a jump in the price of fuels and other oil derivative products, which will impact consumer spending and economic growth worldwide.

Equity markets have remained resilient, supported by other economic drivers, such as AI investment and accelerating manufacturing activity.

Conventional energy producers outside the Gulf benefit from higher prices, although the crisis also accelerates the shift toward renewable energy and electric vehicles in energy-importing countries.

The conflict is creating winners and losers across sectors, highlighting the importance of a diversified portfolio and active management to capitalize on sectoral shifts and market volatility.

**Figure 1: The strait remains closed, but markets have turned optimistic**



Source: Macrobond, Wealth Investment Office as of May 7, 2026

And yet, almost two months since the shooting began, equity markets have reached new highs, and credit spreads are even tighter than before the war, recovering sharply following the mini-correction in February and March. In a lot of ways, it feels like a repeat of the market volatility seen in April last year during the tariff war between the U.S. and China. Are equity and bond markets complacent? Or are there other drivers that offset this headwind to the global economy?

Well, if ever there could be a counterweight to the nightmare scenario playing out in the Strait, the rise of artificial intelligence is it. Investors continue pouring capital into AI infrastructure — as well as manufacturing and electrification themes poised to benefit from the AI revolution — helping global equity markets shrug off worsening geopolitical headlines. The result is an increasingly uneven economy: consumers and energy importers are facing growing strain, while parts of the industrial, commodity and technology sectors continue benefiting from structural investment tailwinds.

An end to the war, of course, would represent the ultimate tailwind. While the timeline remains uncertain, the prevailing incentives strongly encourage both the U.S. and Iran to resolve the conflict swiftly. For the United States, a prolonged engagement in the Middle East is undesirable, particularly since elevated energy prices continue to exacerbate the cost-of-living crisis. This concern becomes even more pressing in an election year, when economic pressures rise to the forefront of voters' minds.

Recent weeks have seen indications that President Trump is employing “brinkmanship” — escalation with the intent to ultimately de-escalate — a tactic reminiscent of his approach during the escalation of tariffs against China the previous year. This method is designed to bring both parties to the negotiating table and avoid a lengthy conflict that could further destabilize domestic economic conditions.

Meanwhile, the Iranian economy is likely in a multi-year recession and is under heavy pressure amid U.S. sanctions. Domestic inflation has risen to above 50% year-over-year, and the Iranian rial has lost over 96% (not a typo) of its value against the greenback. With revenue from crude oil drying up, the Iranian government — already unpopular among most of the Iranian population — will soon be incapable of delivering basic services and buying support from its shrinking base of supporters. For its survival, the regime needs to shore up its economy quickly and earn foreign currencies.

If the Strait remains closed beyond the next couple of weeks, oil prices could go parabolic, given that the volume of crude oil on the sea — a buffer for energy importers — has fallen significantly as it has been gradually delivered to refiners in Asia over the past two months. Shortages of oil derivative products will likely also start to affect the real economy and eat into company margins across industries. Risk assets will

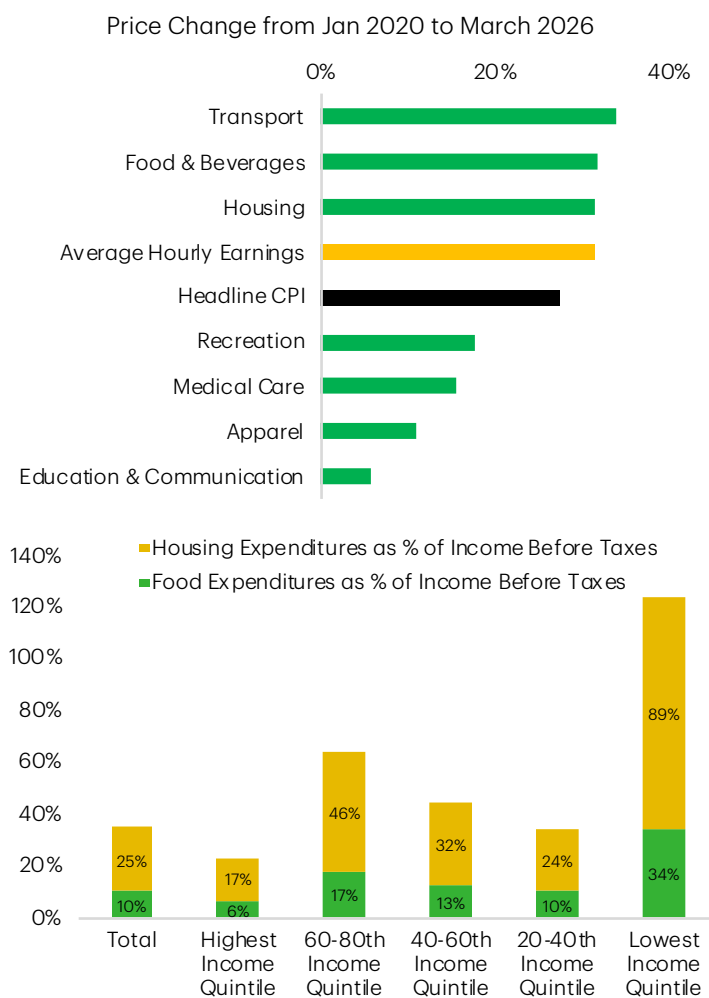
likely sell off again under this scenario, which would increase the incentive for a peace deal to pass through — but not before more permanent damage to the global economy is done.

### The War's Impact at Home

In the U.S., the price of gasoline has risen more than 50% — from \$2.80 per barrel at the beginning of 2026 to \$4.50 today — affecting the price of goods and services and also raising food prices. Since the pandemic began, transportation and food costs have risen 34% and 32%, respectively, faster than the average wage growth of 31% (Figure 2a).

Perhaps no surprise, then, that the Michigan Consumer Sentiment Index has dropped to lows not seen since Russia's invasion of Ukraine in 2022. In the U.S., given that lower-income households spend more proportionally on housing, food and transportation, this income group has seen higher inflation than the general population since the pandemic began (Figure 2b). This will be key as we get closer to the midterm elections in November, where the Democrats are currently expected to win the House majority and potentially the Senate too.

**Figure 2. Pain not being distributed equally**

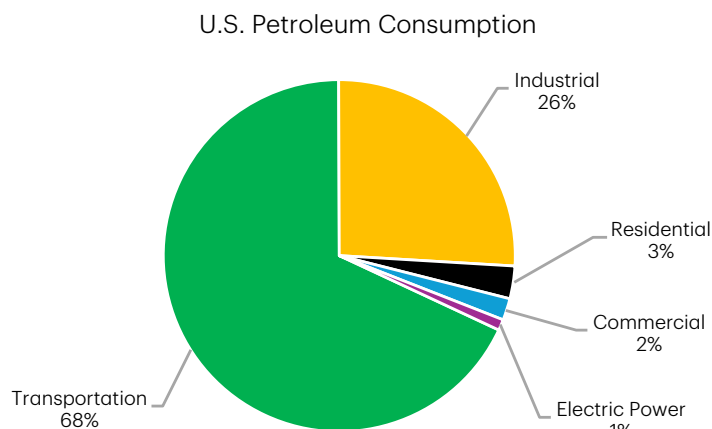


Source: Macrobond, Wealth Investment Office as of April 30, 2026

Outside the energy and food categories, we will likely also see higher prices for anything derived from plastics. Polypropylene is perhaps the most important polymer due to its high chemical resistance, fatigue resistance and high melting point — making it the perfect precursor for many plastics produced globally. Together alongside polyethylene terephthalate, these two polymers constitute the base for most goods sold in dollar stores today. This means that the approximately 20% jump in polypropylene prices following the war will likely reverberate through the supply chain and eventually lead to higher consumer prices across different categories in the coming months — further pressuring household spending (Figure 3).

Already, in its first-quarter financial report, Procter & Gamble forecast an earnings hit greater than \$1 billion from surging oil prices, which raise the costs of shipping, packaging and materials for products such as Tide detergent, Pantene shampoo and Pampers diapers. The company also warned that it may raise prices for consumers to offset the higher input costs.

**Figure 3: Prices across the oil derivatives market have leapt**



Source: Macrobond, Wealth Investment Office as of April 30, 2026

Another obvious victim of higher oil prices is the airline industry, which has been cancelling flight plans and increasing seat prices and fuel surcharges for remaining flights. Air Transat and United Airlines, among others, have announced plans to cut 3% to 6% of their flights in the coming two quarters. If the Strait of Hormuz remains closed in the coming weeks, it's possible that the prices of crude oil and its derivatives will rise above the recent highs as we get closer to the summer holiday season (Figure 4).

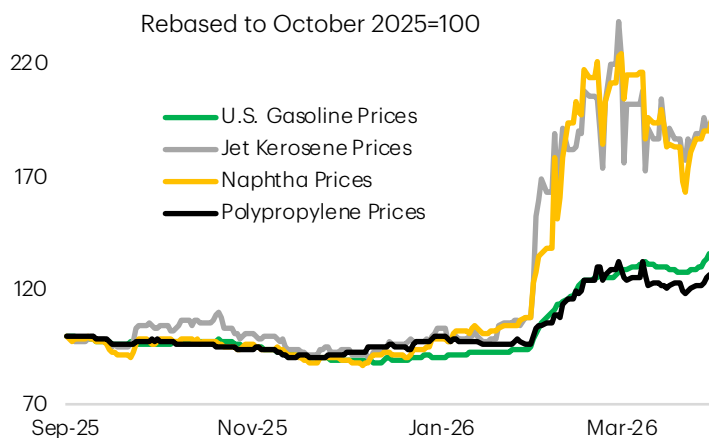
### Oil Derivatives 101

**Gasoline & Diesel:** Main fuels for transportation.

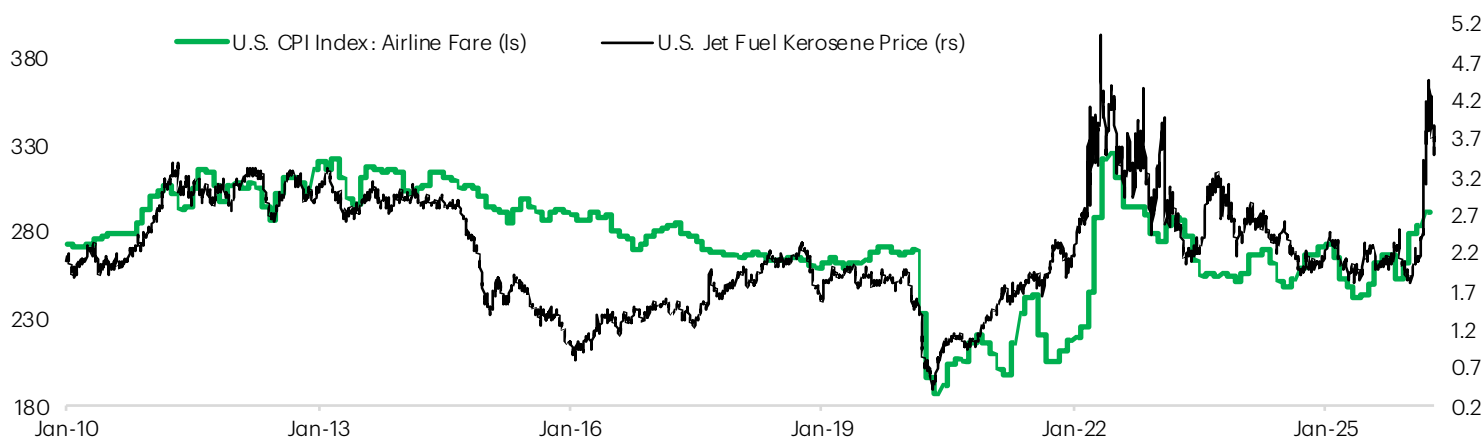
**Kerosene:** Used in aviation fuel.

**Naphtha, Fuel Oils:** Petrochemical manufacturing, heating.

**Lubricants & Asphalt:** Machinery and construction



**Figure 4: Airline tickets set to rise for summer**



Source: Macrobond, Wealth Investment Office as of April 30, 2026

### Tailwinds for the U.S.

**Acceleration in manufacturing activity.** Investment spending on AI remains strong, which will have trickle-down effects across the industrial, energy and utilities sectors.

**Higher tax refunds are a tailwind in H1/26.** Liquidity and financial conditions remain easy, while the U.S. administration will be incentivized to boost the economy as we approach mid-term elections in November.

**Productivity from AI implementation across industries.** The fear that AI will replace human labour is gradually emerging, especially in the tech and industrial sectors. This is positive for corporate earnings in the long run, given that return on capital tends to increase in tandem with productivity growth. Labour, however, is likely to see its share of income continue to decline.

### Headwinds for the U.S.

**Slowdown in consumer spending growth.** This was happening even prior to the war. Residential investment also continues to be a drag on growth, given housing affordability issues.

**Corporate profit margins will face increasing scrutiny.** Input costs are rising and top-line growth is slowing in many industries. In response, several companies (Nike, Disney, Oracle, GM, Meta, Microsoft) have announced layoffs this year,

**Fiscal and monetary conditions may become less supportive in H2.** Companies are now asking for \$160 billion in tariff refunds, which could add 0.4% of GDP to the U.S. fiscal deficit. The deficit could move back to above 6% of GDP later this year. Meanwhile, the jump in food and energy prices will likely delay the timing of a Fed rate cut.

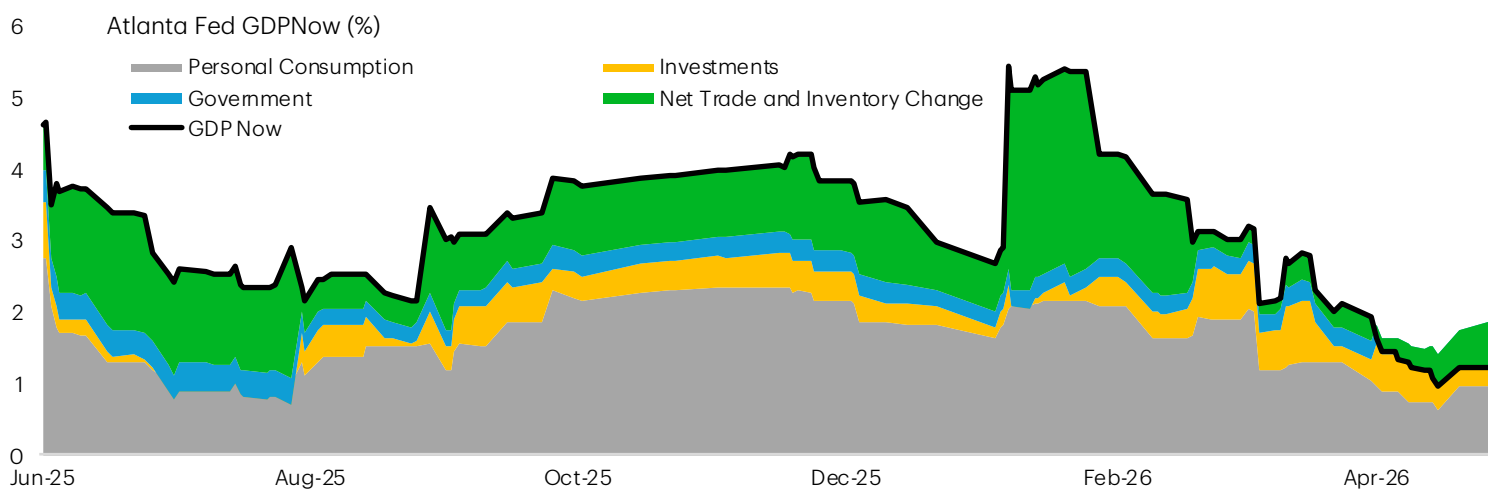
Consumer spending, already weakening in the past few quarters, will face even stronger headwinds in the coming quarters. Figure 5 shows that estimates of U.S. GDP growth have fallen to only 1.2% currently from the trend around 2% in the second half of 2025, primarily due to the sharp slowdown in consumer spending.

The blockade is also affecting the production of natural gas and its adjunct products, whose prices are already rising, including fertilizers and other chemicals used in manufacturing advanced technological goods. Given the importance of fertilizer in agriculture, this will put upward pressure on food prices around the world.

The bottom line is that price pressure arising from the war in Iran will continue to surface in the coming months and become a headwind for household spending in the U.S. and elsewhere. In this environment, the bar for the Federal Reserve and other major central banks to cut policy rates is higher than at the beginning of the year. Meanwhile, voters will want support from their respective governments, either through direct stimulus, suspension of fuel excise taxes, price controls or other measures to help ease the burden on median voters.

Despite the daily negative headlines, however, there are reasons to be optimistic. The softer U.S. labour-market trend seen over the past 18 months seems to have stabilized, while AI capex spending does not seem to be ending anytime soon, based on the guidance and order books of companies across the tech hardware supply chain.

Figure 5: U.S. GDP estimate has fallen sharply

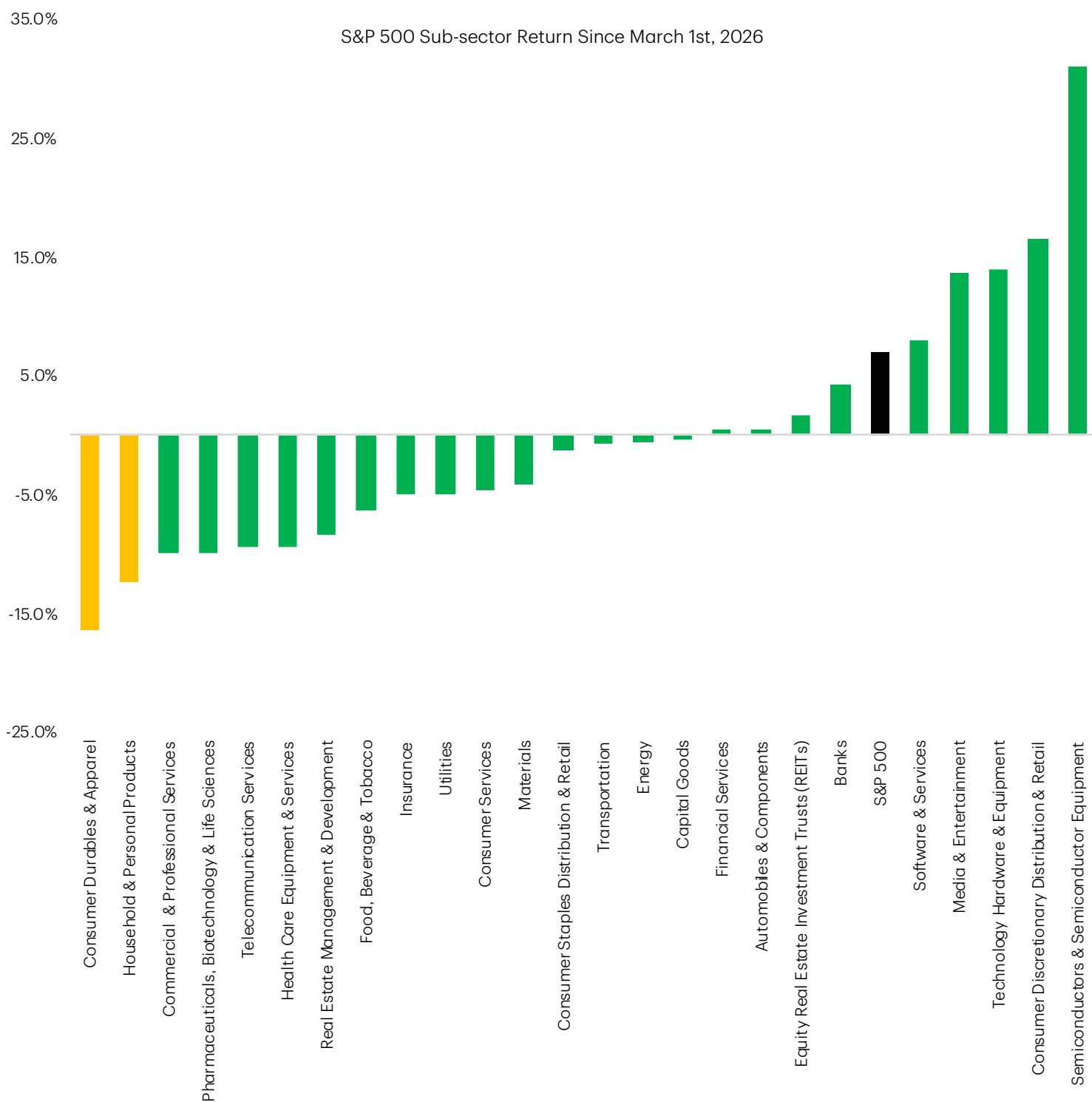


## Winners, Losers and the AI Revolution

The equity-market reaction to the war in Iran could perhaps be summarized as “consumers doomed as AI boomed” (Figure 6). Yes, things are bad, especially for lower-income households. But other good things are happening too that are supporting equity markets.

As usual, spikes in energy prices tend to force consumers to reduce spending on both staples and discretionary goods. Poor stock-price performance of companies in household and personal products (Procter & Gamble, Colgate-Palmolive and Kimberly-Clark) and consumer durables and apparel (Nike, Tapestry, Kate Spade, Lululemon Athletica and Ralph Lauren) should not come as a surprise.

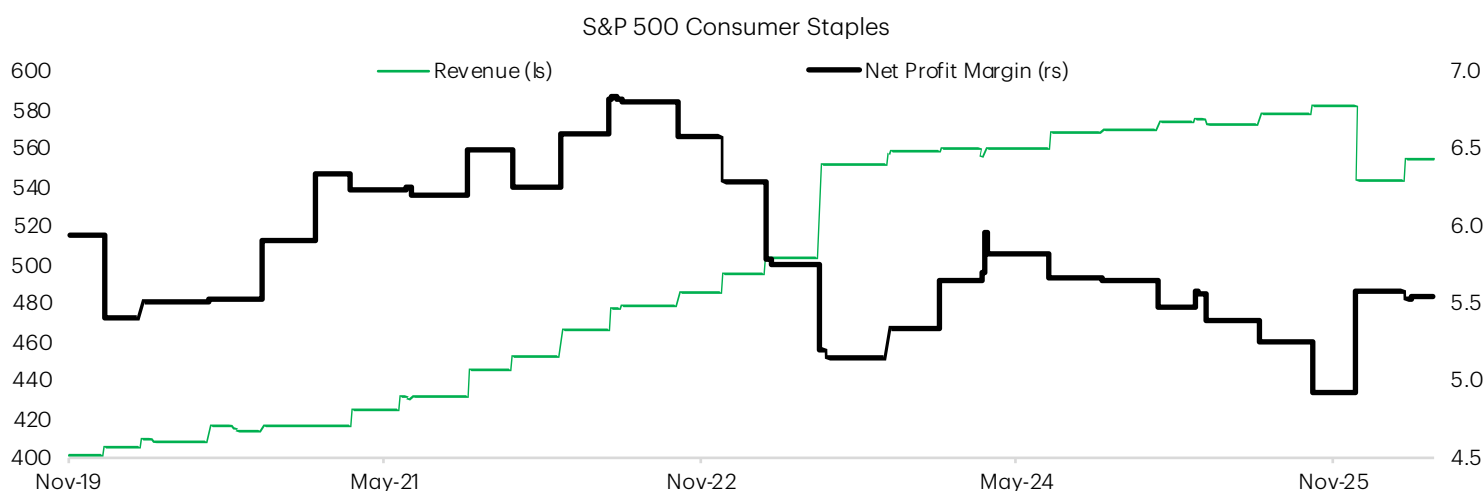
**Figure 6: Wide dispersion among S&P sub-sectors since the war began**



The slowdown in consumer spending over the past two years means that many consumer-goods producers were on the defensive even before the conflict, with many seeing contractions in sales volume (Figure 7). Several consumer staples names, including PepsiCo (classified under food, beverage and tobacco), have cut the price of their products in the past year. The expectation is that lower prices will help drive stronger volume growth and translate into higher revenue.

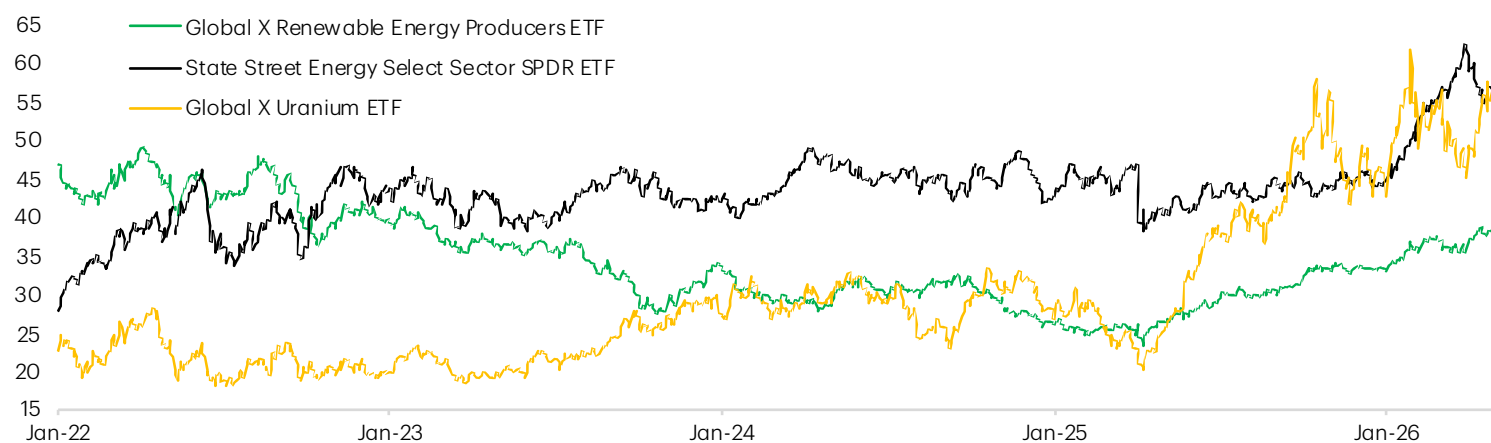
Demand for luxury goods has also taken a hit, especially from the Gulf area. In its first-quarter financials, Louis Vuitton Moët Hennessy reported a double-digit decline in sales from the Middle East region, with demand for watches, jewellery and cosmetics seeing a larger decline relative to leather goods, wine and spirits. Aside from the hesitancy by local residents to go shopping amid the missile attacks, weaker demand is likely also explained by less travel to the Gulf region amid mass flight cancellations in March and April.

**Figure 7: Staples pinched by belt-tightening**



Source: Macrobond, Wealth Investment Office as of April 30, 2026

**Figure 8: Renewables rise on diversification push**



Source: Macrobond, Wealth Investment Office as of May 7, 2026

Conventional energy producers outside the Gulf are expected to be the major beneficiaries from the conflict in the Middle East, but the spike in oil prices is also a blessing for the renewable energy sector, which includes solar, wind and nuclear power. In fact, the current energy crisis is accelerating efforts to diversify away from carbon-based sources, especially for countries that are highly reliant on crude oil imports such as China, South Korea and Japan.

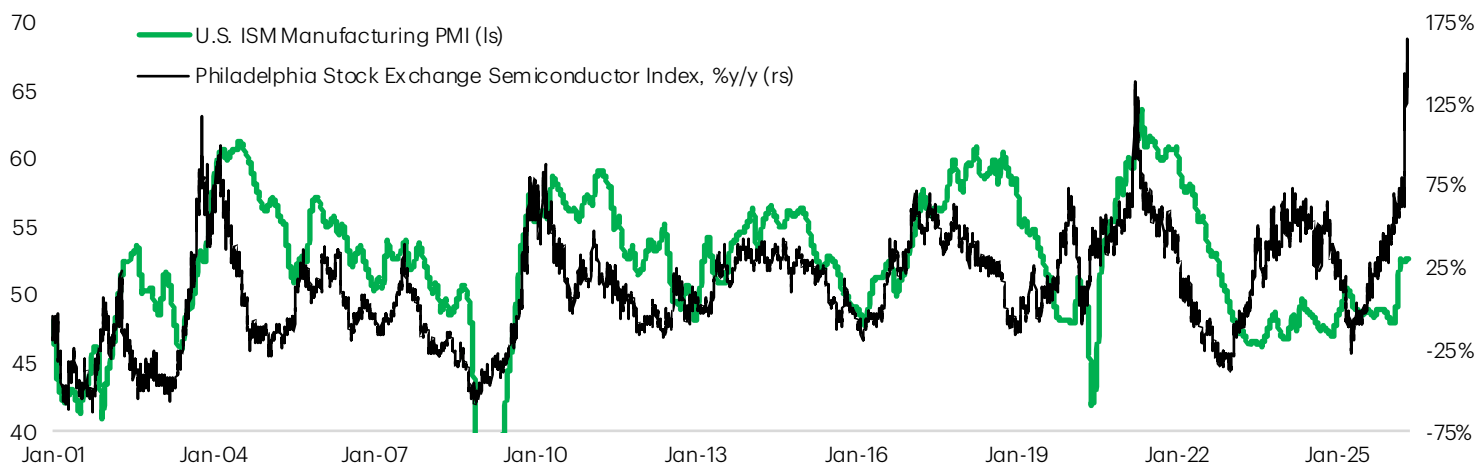
At the end of March, South Korean President Lee Jae-myung said that the country “must shift to renewable energy very quickly” to diversify its energy sources. Figure 8 shows that stock prices of companies involved in the supply chain of renewable energy have risen sharply since the U.S. attack on Iranian nuclear facilities in June 2025. Similarly, consumer demand for electric vehicles should also pick up in the near term, as we saw following the oil-price spike during the Russian invasion of Ukraine in 2022.

Higher energy prices also have indirect implications for investment in AI infrastructure. As AI adoption broadens across industries and regions, access to cheap and reliable energy sources will become increasingly important. Figure 9 shows that the stock price of chipmakers and semiconductor equipment manufacturers have surged 31% since the beginning of the Middle East conflict — significantly outperforming the broader benchmark — mainly due to continued upward revisions to AI capex spending and also increased conviction on the monetization of such large spending.

The buildout of AI data centres has helped bolster demand for industrial goods, but there are also signs that demand from non-AI companies has started to pick up too. The U.S. ISM Manufacturing PMI has shifted into expansion since January this year, following three years of contraction (Figure 9). We are still early in the acceleration of manufacturing activity, which normally extends around 24 to 36 months. Encouragingly, though, multiple companies in the industrial sector have also highlighted strength in their project pipelines and backlogs of AI and non-AI goods orders in the recent earnings season.

The silver lining is that geopolitical shocks create winners and losers across the economy and equity markets. A well-diversified portfolio should help investors navigate periods of crisis, while active management could provide value by rotating from sectors that are overvalued or overbought to those trading at a discount with improving fundamentals. As the crisis subsides, trimming defensive positions to add to risk could also translate to additional alpha in the long run. In the end, successful investors tend to be those who are most adaptable to change.

**Figure 9: Rapid and unmitigated spending on AI capex could lift American industry**



Source: Macrobond, Wealth Investment Office as of May 7, 2026

## Meantime, Risk Assets Keep Climbing

Global risk assets continue to climb the wall of worries. Since the pandemic in 2020, we have seen multiple crises — global rate hikes in 2022, the U.S. regional banking crisis in 2023, U.S. tariff chaos in 2025 and this year's Middle East conflict — that prompted corrections in the equity markets, and yet global markets have continued their upward trajectory over the longer run.

In the short run, the equity market is affected by changes in investor sentiment, positioning of high-frequency traders, fund flows and myriad other factors. In the long run, however, the trajectory of equities is a function of changes in earnings, growth rates and discount rates. The good news is that earnings growth for global equity markets remains strong, with a consensus estimate of 13.8% in the coming year, with dispersion across sectors. Meanwhile, the Fed is now expected to hold rates steady at least until mid-2027. Although this is more hawkish compared to expectations of two rate cuts in 2026 at the beginning of the year, the bar for a policy rate hike is also high, given the negative impact of higher oil prices on economic growth.

From an asset-allocation perspective, we continue to advocate for greater diversification into commodities as well as exposure to alternatives due to the reduced effectiveness of fixed income securities as a portfolio hedge. While the price of oil should decline, given that the peak of the conflict is in the rear-view mirror, the price of other commodities such as copper could benefit from an improving global growth outlook.

The backdrop of a widening gap between winners and losers, combined with a higher-rate backdrop, is creating a more fertile environment for active equity and multi-strategy mandates. Strategies that are uncorrelated to the broader market and have the ability to go both long and short are particularly well positioned — benefiting not only from increased dispersion but also from the return on carry in a higher-rate environment.

# Market Performance

		(%)	(%)	(%)	(%)	(%)	(%)	(%)	(%)	
<b>Canadian Indices (\$CA) Return</b>		<b>Index</b>	<b>1 Month</b>	<b>3 Months</b>	<b>YTD</b>	<b>1 Year</b>	<b>3 Years</b>	<b>5 Years</b>	<b>10 Years</b>	<b>20 Years</b>
S&P/TSX Composite (TR)	145245	3.81	7.00	7.90	40.10	21.54	15.51	12.61	8.39	
S&P/TSX Composite (PR)	33964	3.65	6.39	7.10	36.72	18.07	12.19	9.31	5.25	
S&P/TSX 60 (TR)	6947	4.25	7.67	7.46	36.18	20.39	15.23	12.75	8.60	
S&P/TSX SmallCap (TR)	2686	6.71	9.34	18.86	80.22	29.11	16.23	11.72	6.21	
S&P/TSX Preferred Share(TR)	2516	2.51	2.47	2.87	20.10	15.41	6.77	6.90	3.79	
<b>U.S. Indices (\$US) Return</b>										
S&P 500 (TR)	16089	10.49	4.19	5.70	31.05	21.69	13.14	15.26	11.00	
S&P 500 (PR)	7209	10.42	3.89	5.31	29.45	20.02	11.51	13.32	8.90	
Dow Jones Industrial (PR)	49652	7.14	1.55	3.31	22.09	13.34	7.95	10.82	7.65	
NASDAQ Composite (PR)	24892	15.29	6.10	7.10	42.68	26.74	12.26	17.95	12.59	
Russell 2000 (TR)	15401	12.21	7.46	13.21	44.41	18.19	5.75	10.98	8.17	
<b>U.S. Indices (\$CA) Return</b>										
S&P 500 (TR)	21900	7.93	4.42	4.86	29.17	21.87	15.48	16.19	12.10	
S&P 500 (PR)	9813	7.86	4.11	4.47	27.59	20.20	13.82	14.23	9.97	
Dow Jones Industrial (PR)	67586	4.66	1.77	2.49	20.34	13.51	10.18	11.72	8.71	
NASDAQ Composite (PR)	33883	12.62	6.32	6.25	40.63	26.93	14.58	18.91	13.70	
Russell 2000 (TR)	20964	9.61	7.68	12.31	42.34	18.36	7.93	11.88	9.23	
<b>MSCI Indices (\$US) Total Return</b>										
World	22329	9.64	3.49	5.83	29.68	20.22	11.80	13.22	8.88	
EAFE (Europe, Australasia, Far East)	15651	7.56	1.08	6.36	25.22	15.88	9.38	9.39	5.67	
EM (Emerging Markets)	4394	14.73	5.28	14.61	47.51	21.28	6.54	9.68	6.13	
<b>MSCI Indices (\$CA) Total Return</b>										
World	30395	7.09	3.71	4.99	27.82	20.40	14.11	14.13	9.96	
EAFE (Europe, Australasia, Far East)	21305	5.07	1.29	5.51	23.42	16.05	11.64	10.27	6.72	
EM (Emerging Markets)	5981	12.07	5.51	13.70	45.40	21.45	8.74	10.57	7.17	
<b>Currency</b>										
Canadian Dollar (\$US/\$CA)	1.36	-2.40	-0.23	-1.03	-1.57	0.07	2.02	0.79	0.98	
<b>Regional Indices (Native Currency, PR)</b>										
London FTSE 100 (UK)	10379	1.99	1.52	4.51	22.18	9.66	8.29	5.22	2.76	
Hang Seng (Hong Kong)	25777	3.99	-5.88	0.57	16.53	9.02	-2.14	2.04	2.21	
Nikkei 225 (Japan)	59285	16.10	11.18	17.77	64.47	27.13	15.52	13.53	6.47	
<b>Benchmark Bond Yields</b>			<b>3 Months</b>	<b>5 Yrs</b>	<b>10 Yrs</b>	<b>30 Yrs</b>				
Government of Canada Yields			2.30	3.19	3.54	3.92				
US Treasury Yields			3.67	4.01	4.37	4.97				
<b>Bond Indices (\$CA Hedged) Total Return</b>		<b>Index</b>	<b>1 Mo (%)</b>	<b>3 Mo (%)</b>	<b>YTD (%)</b>	<b>1 Yr (%)</b>	<b>3 Yrs (%)</b>	<b>5 Yrs (%)</b>	<b>10 Yrs (%)</b>	
FTSE TMX Canada 91-day Treasury Bill Index	489	0.20	0.54	0.72	2.51	3.90	3.02	1.99		
FTSE TMX Canada Universe Bond Index	1204	0.12	-0.23	0.35	1.63	3.20	0.74	1.78		
FTSE TMX Canada All Government Bond Index	1119	0.03	-0.22	0.29	0.99	2.48	0.20	1.34		
FTSE TMX Canada All Corporate Bond Index	1512	0.40	-0.25	0.55	3.61	5.34	2.33	3.06		
U.S. Corporate High Yield Bond Index	325	1.53	0.23	0.59	6.87	7.45	3.37	4.98		
Global Aggregate Bond Index	266	0.17	-0.51	-0.41	0.98	2.68	-0.05	1.39		
JPM EMBI Global Core Bond Index	593	2.55	-0.03	0.11	10.44	8.15	1.10	2.65		
S&P/TSX Preferred Total Return Index	2516	2.51	2.47	2.87	20.10	15.41	6.77	6.91		

Source: TD Securities Inc., Morningstar®, TR: total return, PR: price return, as of April 30, 2026.

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