Market Update: February 2026

The AI Divide: Winners, Losers, and the Global Rotation

February has been a month of stark contrast. While the major indices remain resilient, the "surface-level" stability masks a significant shift in investor behavior. We are no longer in a market where a rising tide lifts all boats; instead, we have entered a phase of aggressive discernment, where the gap between AI leaders and those vulnerable to disruption is widening at a record pace.

Key Market Drivers

- **The "Disruption Penalty":** This month, the market has begun to aggressively punish companies perceived as being on the wrong side of the AI curve. We are seeing a "de-rating" of traditional service providers and legacy software firms that have failed to integrate generative AI effectively. For these companies, the penalty for being "disrupted" is swift, with valuations compressed as investors flee toward firms with a clearer defensive moat.

- **The AI Infrastructure "Moat":** Conversely, the "Enablers"—those providing the chips, cooling systems, and power grid infrastructure—continue to see massive inflows. The narrative has shifted from if AI will change the economy to who owns the essential toll booths of that change.

- **A Patient Fed with New Leadership:** With no formal meeting this month, the focus turned to the nomination of Kevin Warsh as the next Fed Chair. The current committee remains patient, holding rates at 3.50%–3.75%. With U.S. GDP to only slow a bit this year and unemployment ticking back down, the Fed is waiting for definitive evidence of cooling inflation before moving toward an easing cycle.

One of the most notable themes of February has been the continued resurgence of international equity markets. As U.S. mega-cap tech valuations face increased scrutiny, global markets are offering a compelling "catch-up" trade.

- **Japan's Structural Rally:** Japan remains a standout. A combination of corporate governance reforms and a clear political mandate has pushed the Nikkei to fresh heights. Investors are increasingly viewing Japan as a high-quality alternative to expensive U.S. growth stocks.
- **European Cyclicals:** Europe has shown surprising strength, particularly in Germany and Italy. Stronger-than-expected performance in the banking and luxury sectors has provided a counterbalance to the volatility in the tech space.
- **Emerging Market Opportunities:** We are observing a strategic rotation into Emerging Markets (EM). With the U.S. dollar stabilizing, EM equities—which trade at a significant valuation discount—are becoming an essential tool for diversification and yield.

The Bottom Line

February has reinforced a constructive but more balanced investment environment. Inflation is easing, policy is gradually becoming more supportive, and the economy continues to expand — albeit at a slower pace. At the same time, valuations are fuller and expectations are higher, which argues for discipline.

The Bottom Line *Continued*

Our view remains that this environment favors diversification and quality over chasing momentum. If the Fed continues executing a careful easing cycle and growth remains stable, equities can continue to grind higher over time. But patience and thoughtful positioning remain essential. While we believe that small cap stocks, international and non-tech related equities will continue to perform well, we do believe there will be an opportunity for some of the mega-cap tech stocks to once again reassert their leadership at some point this year.