TERRA NOVA
ASSET MANAGEMENT

February 2026
Market Highlights

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In Brief

January was marked by geopolitical shocks and policy uncertainty, yet U.S. equities finished modestly higher (1.4%) as investors continued to buy dips amid resilient economic data and shifting expectations for central-bank policy. Tensions involving Venezuela, Greenland, and Iran, alongside a spike in long-dated Japanese yields briefly triggered the sharpest selloff since October before stocks rebounded and the S&P-500 briefly moved above the 7,000 level for the first time. Energy and defense stocks led gains as oil prices surged, while technology lagged following sharp post-earnings drop in Microsoft. Attention later turned to monetary policy after the Fed heldates steady and to leadership changes when President Donald Trump nominated Kevin Warsh as the next chair, prompting markets to reprice the outlook for 2026 rate cuts and helping stabilize sentiment into month-end.

The bond market was volatile but finished largely stable, with U.S. Treasury yields briefly rising on geopolitical stress and global rate moves before easing back as expectations around Federal Reserve policy were repriced. Treasury auctions were well absorbed, pointing to steady demand, while corporate bonds remained orderly, with issuance continuing and credit spreads little changed despite equity swings. Overall, interest-rate levels fluctuated during the month but ended close to where they began, leaving fixed-income markets resilient rather than under pressure, with income levels still attractive and volatility driven more by headline risk than by any fundamental deterioration in credit conditions or funding markets.

Economy

January economic data pointed to continued U.S. expansion despite market volatility, with activity and inflation figures largely reinforcing a soft-landing narrative. Service-sector momentum remained firm, as the ISM Services index rose to 54.4, its highest level in more than a year, while fourth-quarter GDP was revised higher to 4.4%, underscoring late-2024 economic strength. Labor-market data were mixed, but constructive. Non-farm payrolls increased by 50,000, below expectations, yet the unemployment rate edged down to 4.4%, suggesting conditions remained stable rather than deteriorating. Inflation pressures continued to ease, with December core CPI running at 2.6% year over year, below forecasts.

Labor Market

January's labor data pointed to continued normalization rather than deterioration, with payroll growth slowing to about 50,000, while the unemployment rate edged down to 4.4%. Wage pressures continued to cool and job openings showed further signs of rebalancing after the exceptionally tight conditions of prior years, reinforcing the view that labor markets are settling into a more sustainable pace and supporting the broader soft-landing narrative heading into early 2026

Corporate Earnings

January's earnings season was broadly stronger than anticipated, with most large U.S. companies reporting results above consensus forecasts and reinforcing confidence in underlying profit trends. Technology results were a focal point, as Microsoft weighed on sentiment after disappointing cloud guidance, while Meta

Platforms delivered a more upbeat outlook tied to continued AI investment. Outside those exceptions, margins held up well and forward guidance remained constructive, pointing to solid demand and disciplined cost control. Overall, earnings results supported the view that corporate profitability remains resilient, even as investors grow more selective around growth assumptions and capital-spending plans.

Thoughts

The U.S. dollar weakened roughly 10–12% against the euro over the past year, but this move remains within historical trading ranges and does not yet signal a structural regime shift. Despite narratives questioning U.S. economic leadership, cross-border data show continued foreign demand for U.S. assets: private investors added about $1.5 trillion to U.S. equities and bonds through late 2025, foreign direct investment totaled roughly $324 billion, foreign holdings of U.S. Treasuries reached a record $9.4 trillion, and central-bank dollar reserves have remained near $7 trillion. Unlike the early-2000s, dollar down-cycle, today's backdrop features stronger relative U.S. productivity, deep capital markets, narrower external deficits, and persistent safe-haven flows during periods of stress, supporting a base case in which EUR/USD trades in a broad range rather than entering a prolonged secular decline. Interest-rate differentials and sustained capital inflows reinforce this view, while the costs embedded in currency-hedged strategies argue for selectivity rather than permanent, full coverage. Overall, the evidence suggests the dollar's recent weakness reflects cyclical forces rather than structural erosion at this stage.

Stock Market Outlook

The stock market outlook remains constructive, but more selective after several years of strong gains, with returns increasingly driven by earnings delivery and sector fundamentals rather than broad multiple expansion. Continued economic growth, easing inflationary pressures, and a more accommodative monetary backdrop support corporate profitability, while investment in AI and productivity-enhancing technologies remain a key structural tailwind. At the same time, elevated valuations in parts of the market, geopolitical uncertainty, and shifting policy expectations argue for periodic volatility and uneven leadership across sectors. Overall, the environment favors disciplined participation in equities, with performance likely shaped by company-specific execution and earnings durability rather than a uniformly rising market.