Summit Trail Advisors

Monthly Download

February 2026

Summary

◆ **Markets were mixed** in February as leadership continued from areas outside of US Technology companies. Future AI capabilities rattled numerous industries including software, wealth management, and logistic companies. International equity markets continued their reversal of US performance dominance, supported by cyclical sector strength and a softer US dollar. Fixed income markets benefited from a meaningful decline in Treasury yields, reinforcing expectations that the Federal Reserve remains patient as inflation moderates and growth stabilizes.

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Market Overview

◆ **Equity markets** delivered uneven performance in February, with meaningful dispersion across regions and industries. US Large Caps lagged as continued weakness in software weighed on index returns, while hardware-related technology and telecom equipment remained more resilient. International markets outperformed the US, supported by broader sector composition and investor preference for non-software segments of the AI ecosystem. Small caps modestly outperformed large caps, aided by stronger contributions from Materials and Industrial-linked areas as potential beneficiaries from the ongoing data center build-out in the US.

- US Large Cap stocks (S&P 500) fell 0.8% as weakness in software and Communication Services offset gains in Utilities, Energy, and Materials. The S&P 500 Equal Weight Index was up 3.6%, posting another strong month of outperformance versus the market cap-weighted index, while the Magnificent Seven Index declined 7.3%. Year to date, the S&P 500 is up 0.7%, despite continued pressure on mega-cap growth stocks.
- US Small Cap stocks (Russell 2000) rose 0.8%, benefiting from a smaller drag from software and stronger performance in Materials, Communications, and Energy. The relative outperformance versus large caps also reflects sector weight differences, as small caps carry materially higher exposure to interest-rate sensitive areas like Financials, Real Estate, Housing and Industrials. Year to date gains now stand at 6.2%.
- Non-US stocks (MSCI EAFE Net) gained 4.6% as developed international markets benefited from currency tailwinds and a sector composition less concentrated in Technology. Japan surged over 8% for February. Year to date gains are10.1%.
- Emerging Markets (MSCI Emerging Markets Net) were up 5.5%, driven by a weaker US dollar and ongoing memory chip shortages that are driving Samsung, SK Hynix, and Taiwan Semiconductor. Korea was up 22% in February and Taiwan returned almost 13%. Year to date returns are up 14.8%.

◆ **Interest rates** were firmer with the curve flattening in February as long-term yields declined more than short-term yields. The 10-year Treasury yield fell 28 bps to 3.96% from 4.24% at the beginning of the month, reflecting moderating inflation readings and steady central bank policy. The Federal Reserve, Bank of England, and European Central Bank all held rates steady during the month while signaling continued data dependence.

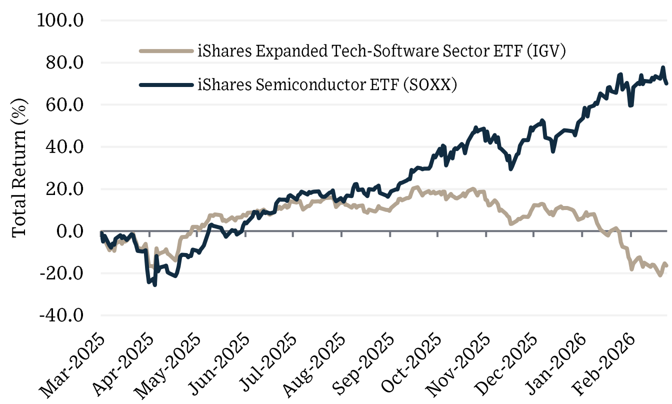
- High Grade Taxable bonds (Bloomberg US Aggregate) returned 1.6% in February as declining Treasury yields supported performance in higher quality fixed income sectors. Year to date gains are1.8%.

- Municipal bonds (Bloomberg 1-10 Year Muni Bond) added 0.9%, driven by lower yields and improved demand conditions. Municipal bonds are now up 1.9% in 2026.
- Investment Grade bonds (Bloomberg US Corporate Investment Grade) were up 1.3% for the month, outperforming High Yield as duration benefited from falling yields. High Yield bonds (Bloomberg US Corporate High Yield) rose 0.2% as subdued credit spreads provided income support but lagged higher quality credit. Year to date performance for Investment Grade and High Yield bonds are up 1.5% and 0.7%, respectively.

◆ **Commodities** (Bloomberg Commodity Index) advanced 1.1% in February. Gold and Silver continued their multi-month rallies, up 10.6% and 18.8% respectively. Bitcoin futures continued their recent weakness and fell 21.6%. WTI Crude Oil was volatile on shifting US-Iran headlines but ended the month up 2.8%. Commodities are now up 11.6% in 2026.

Economic Commentary

Software Stocks were already under pressure entering February, and volatility intensified as advances in artificial intelligence's ability to code sparked concern that businesses may be able to easily replace enterprise software systems in the future. The iShares Expanded Tech-Software Sector ETF (IGV), a widely followed proxy for the software industry, fell 9.7% for the month and has declined 22.8% year to date. The central issue is not current earnings, which have generally continued to grow albeit with weaker expectations. Given price declines and stable earnings, many large software companies are trading at multiples below sectors like Consumer Staples[1]. Software companies were significant beneficiaries of the pre-AI technology cycle including the post-Covid markets in 2020, returning more than double the S&P 500 index from 2017 through 2020 at 34.6% annually. Public (and private investors) were attracted to their recurring revenue, business-to-business model and high operating margins. Markets are now anticipating that rapid advances in generative AI could reduce the need for standalone applications or compress pricing in categories where software features become easier to replicate. Releases from Anthropic's Claude model look increasingly capable of coding and programming that were long thought unreachable except for the largest IT departments. Enterprise software companies have tried to message their own AI strategy with many software companies embedding AI solutions directly into their products to automate workflows, improve analytics, and strengthen customer retention. From a cost standpoint, software companies' largest expense to date are employees responsible for coding and programming. If systems like Claude can enhance productivity or replace some portion of coders entirely, software company margins may benefit more than the market is anticipating. At present, there is limited evidence of broad software contract cancellations, structural revenue declines, or widespread labor displacement tied directly to AI adoption. Enterprise software systems remain deeply embedded within corporate infrastructure and replacement cycles tend to be gradual rather than abrupt. Investors are now reassessing how much they are willing to pay for software businesses and market re-ratings of earnings multiple are

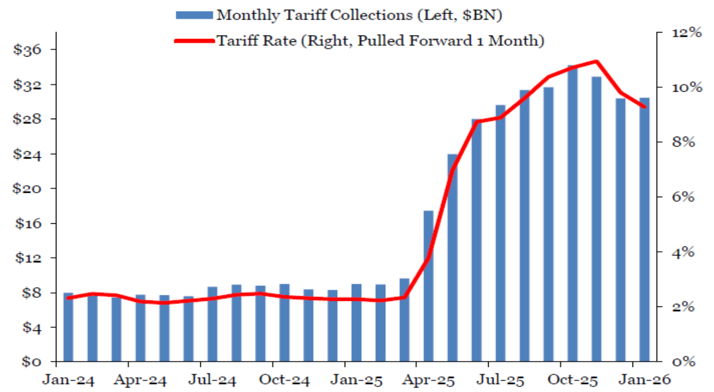


Divergence Within Technology: Software vs. Hardware ETF performance
Source: Factset as of 2/28/26

[1] *Salesforce and Adobe, large positions in the IGV ETF, currently trade at 15x and 11x forward earnings, while Proctor & Gamble and Colgate Palmolive, large Consumer companies trade at 22x and 25x forward earnings, respectively.*

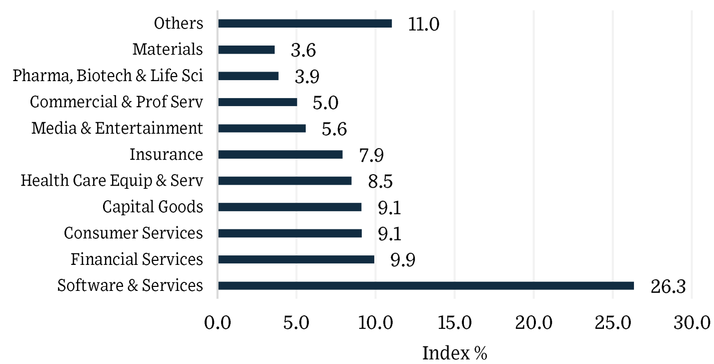
unlikely to reverse in the near-term while too many variables remain unknown. AI will reshape parts of the technology ecosystem over time, but current market action reflects uncertainty about timing and magnitude rather than evidence of immediate disruption.

The Supreme Court issued a 6-3 opinion ruling against President Trump's use of emergency authority under the International Emergency Economic Powers Act (IEEPA) to impose broad tariffs. The decision halted collections under that framework and required the Trump administration to pivot to alternative legal tools to implement tariff policy. The White House responded by implementing a 10% across-the-board tariff under Section 122 of the Trade Act of 1974, a temporary authority that allows tariffs for up to 150 days without Congressional approval. While the new rate is lower than some previously enacted levels, it does not represent a return to the low-tariff environment of the prior decade as effective tariff rates remain elevated by historical standards and additional authorities such as Sections 301 and 232 remain available for more targeted tariff measures. The Court did not directly address whether companies would receive refunds for tariffs previously collected under IEEPA and several firms have already begun filing claims. If refunds are ultimately granted, the process is likely to be prolonged and could introduce incremental fiscal and earnings uncertainty along the way. For businesses, however, the greater challenge is not the precise tariff percentage but the evolving legal framework itself as supply chains operate on multi-year planning cycles and shifting authority complicates capital allocation decisions. Even with a lower headline rate, companies must account for the possibility of further adjustments depending on geopolitical and trade developments. The broader takeaway is that tariffs are increasingly becoming a structural feature of the US economic landscape rather than a temporary negotiating tactic. Markets appear to be adjusting to that reality with measured volatility as long as tariff rates stay in an acceptable range.



Gross Monthly Customs Duties Collections & Effective Tariff Rate
Source: Strategas

Private Credit moved into focus in February on the same software-related concerns from AI detailed above and following stress at Blue Owl Capital, where elevated redemption requests in one of its non-traded vehicles required asset sales and adjustments to liquidity terms. The episode was widely covered in the financial press and quickly broadened into a narrative that private credit as a whole could face pressure, particularly given certain funds' exposure to software and other growth-oriented sectors being impacted by AI. Blue Owl has meaningful exposure to technology and software-related lending, including concentration within its technology-focused BDCs. Blue Owl announced it would unwind Blue Owl Capital Corp II and transition assets into affiliated vehicles in an effort to address liquidity demands and stabilize the structure, emphasizing that the issue at hand centers more on redemption mechanics than immediate widespread credit impairment. We believe it is important to clarify certain aspects of private lending that are often not reported properly in the public media. In our opinion, the growth of private credit vehicles and assets has not increased systemic risk. Private credit today largely fills a role once occupied by banks prior to the Financial Crisis, providing direct lending to middle-market companies that may not access traditional capital markets. Unlike banks, most private credit funds are backed by high net worth and institutional capital rather than deposit liabilities, which limits transmission risk to the broader financial system. And while many private credit funds use leverage at the fund level, it is far less leverage than bank balance sheets, even with improved capital requirements in a post-Financial Crisis world. The second issue is that much of the growth in Private Credit has been in open-end funds like interval funds or tender-offer fund and private BDCs that have been marketed to high net worth and retail investors. All open-end funds that own private assets have liquidity mismatches when investor redemption terms are more flexible than liquidity on the underlying assets. These interval, tender offer, and private BDC products often create the illusion of liquidity when investors want it and despite voluminous disclosures are likely "oversold" to investors. Private BDCs for example are often presented as likely to go public over time without representing the discount public BDCs often trade at to their net asset value. Despite the liquidity profile, GPs can often manage the mismatch as long as the underlying assets are not impaired. We saw this during 2022-2023 with Blackstone's Real Estate Investment Trust (BREIT) which was gated for multiple quarters but ultimately cleared out its redemption queue as underlying performance stabilized. Where the private credit space goes from here will likely depend most on the how the underlying loans ultimately perform. While software exposure is elevated in certain segments of the non-traded BDC universe, there is little evidence at this stage of a broad deterioration in credit fundamentals tied directly to AI disruption. A meaningful economic downturn would increase default risk, but the more immediate issue for some sponsors may be refinancing and maturity timelines rather than insolvency. These recent developments underscore the importance of adequate sector and credit diversification, thoughtful fund structure, and disciplined underwriting rather than signaling broad systemic instability across private credit.



Morningstar LSTA US Leveraged Loan 100 Index Sector Exposure
Source: Morningstar as of 1/31/26

On February 28th, the United States launched Operation Epic Fury after negotiations with Iran failed to deliver an agreement regarding Iran's nuclear program. February 28th marked the second time in 2026 US citizens woke up to news of a military operation in a foreign country. The US has laid out objectives for the military action that are plausible with air power dominance including dismantling Iran's nuclear program, missile industry, and Navy. There are signs of progress towards each of these objectives at time of this publication. What is far more difficult to accomplish with solely air power, and where the US track record is mixed at best, is the concept of regime change and whatever follows Operation Epic Fury. Markets have sold off modestly since the military action began but have generally been orderly. Historically, geopolitical events have limited market impact when they take place in areas that make up very small portions of overall global economic output (Iran is the 44th largest economy as of 2025 and <0.5% of global GDP according to the International Monetary Fund). The bigger issue facing markets are rising oil prices (now up 40% since the start of the year) and diminishing expectations of the Fed's ability to cut rates if higher energy prices contribute to inflation. The other flashpoint is the Strait of Hormuz and how long global shipping routes will be impacted by the conflict. Military operations are by definition unpredictable, but we do not believe the Iran conflict should have lasting impact on markets assuming the duration fits into the administration's expectations. Public approval for military conflict like the Iran operation has been waning for years, but support looks higher for a shorter-term conflict that is measured in weeks. Given 2026 is a mid-term election year, the Trump administration will want to focus on making their economic case to voters and will be sensitive to inflation or other ways that case could be weakened by an extended military conflict. Markets will likely remain volatile over the coming weeks, but economic data remains relatively strong, jobless claims remain low despite AI headlines, and earnings growth for the most recent quarter surpassed 14%. Investors often need to be wary of mid-term election years like 2026, but the Iranian conflict should join the historical precedent of why geopolitical events have short-term impact on markets.

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