

Capital Markets Monthly **FIXED INCOME**

February 2026



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The New Chairman of the Federal Reserve will have much to consider

In January 2025, the US Treasury market delivered a below coupon return as income was diminished by small price declines as yields drifted higher. This reflected resilient economic data and some inflation concerns rather than any immediate policy shift. Markets had fully priced in no action from the Federal Reserve at its 28 January meeting, so the decision to hold rates steady passed without disruption, but longer-dated Treasuries remained under pressure. Political noise intensified last month, with Donald Trump stepping up public pressure on Jay Powell to cut rates, while the nomination of Kevin Warsh as the next Fed chair added uncertainty about the future direction of monetary policy. Kevin Warsh is poised to take over as chair of the Federal Reserve with impressive relevant experience, but he may be tested almost immediately by inflation and volatile financial markets. Once known as an inflation hawk, Warsh now appears aligned with Donald Trump's push for aggressive rate cuts, betting that an AI-driven productivity boom, tax cuts, and deregulation will deliver strong growth without reigniting inflation. He likely intends to shrink the Fed's balance sheet, sideline forward guidance and the dot plot, and rely mainly on the policy rate. However, a recent rise in producer prices and tariff pressures may complicate the outlook for inflation over the near term. Cutting rates further in a strong economy may create unwanted results such as an unsustainable equity rally, a weaker dollar, a steeper yield curve, and even renewed inflation. Warsh could quickly find himself at odds with colleagues unwilling to ease while inflation stays above target. That said, should weakness in labour markets persist while inflation stays in check, there will be scope for rate cuts throughout the first half of 2026.

UK gilt markets softened in January 2026, with yields ending the month modestly higher despite an initial rally in the first half of January. Inflation data showed a slightly stronger-than-expected headline CPI print at 3.4% y/y, although core CPI remained stable at 3.2%, offering some reassurance that underlying price pressures were not accelerating. Economic momentum appeared firmer than anticipated, with PMIs and GDP data pointing to stronger growth, even as labour market indicators continued to show signs of weakness. Against this backdrop of mixed signals for monetary policy, the ICE BofA UK Gilts All Stocks Index returned -0.10% over the month, reflecting the net upward move in yields as optimism on growth outweighed lingering concerns around inflation and

employment. No change is expected to the Bank Rate at the Bank of England's Monetary Policy Committee meeting on 5th February, although the prospects of rate reductions in the first half of 2026 remain strong.

European government bond markets rebounded in January 2026, supported by a modest decline in core yields and stabilising policy expectations. The ICE Bank of America German Government Index returned a healthy +0.42% over the month, reversing part of December's weakness and providing a constructive start to the year. Markets continued to price a prolonged period of policy stability from the European Central Bank, with no near-term rate moves anticipated, helping to anchor front-end yields and reduce volatility. Peripheral spreads versus Germany remained well supported and broadly stable, with France continuing to grind tighter and no renewed stress evident across Southern European issuers. While longer-dated bonds remained sensitive to supply dynamics and structural selling pressure—particularly from Dutch pension funds continuing their gradual reallocation away from long-duration assets—the pace of curve steepening moderated during the month. Overall, January's performance reflected improved investor confidence, better carry dynamics, and selective demand for high-quality duration following the late-2025 sell-off.

Japanese government bond markets remained under intense pressure in January 2026, with the sell-off extending decisively to the long end of the curve. Thirty-year JGB yields surged to nearly 4%, underscoring the scale of the ongoing repricing as investors adjusted to a structurally higher rate environment. Ten-year yields remained elevated above 2%, reinforcing the view that Japan has firmly exited its ultra-accommodative monetary regime. Following the December rate increase, markets increasingly expect additional policy tightening of around 50–75bp over the course of 2026, reflecting sustained inflation momentum and improving domestic growth conditions. The sharp rise in long-dated JGB yields also generated contagion effects across other G7 government bond markets, with global long-end yields pressured higher as Japanese investors reassessed overseas allocations and hedging costs. Recent commentary from Bank of Japan officials has continued to emphasise the need for a gradual but persistent withdrawal of monetary accommodation, while remarks by Governor Kazuo

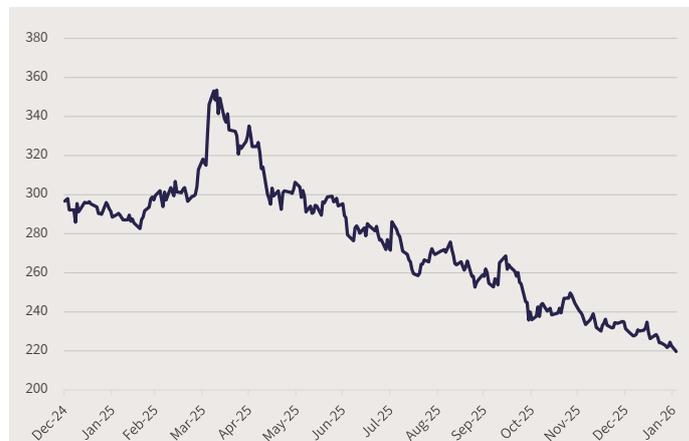
Ueda reiterated that further rate increases will remain conditional on inflation and economic data. Overall, upward pressure on JGB yields is expected to persist, particularly at the long end, implying continued headwinds for JGB performance and ongoing spillovers into global duration markets.

Chinese government bonds staged a solid recovery in January 2026, with the ICE Bank of America China Government Index returning a +0.4% over the month. This rebound followed a soft end to 2025, during which the market delivered a modest 0.1% calendar-year return—its weakest annual outcome since 2017. Despite this, recent performance should be viewed in the context of the asset class’s historically low volatility and consistently defensive characteristics, particularly at a time when many global government bond markets have experienced pronounced drawdowns and heightened duration risk. Chinese government bonds therefore continued to provide meaningful diversification benefits within global fixed-income portfolios. The broader backdrop also remained supportive, with relative monetary policy stability and a resilient domestic investor base helping to anchor yields. In addition, currency dynamics continued to underpin returns, with the renminbi remaining firm against the US dollar, reinforcing foreign-investor outcomes and overall market resilience.

Emerging market debt extended its strong start to 2026, with the J.P. Morgan EMBI Global spread tightening further through January to around +219 bp, underscoring continued investor demand and supportive market technicals. The compression over recent months reflects generally improved risk sentiment, resilient sovereign fundamentals across many issuers, and a continued search for carry in a low-yield environment. While spreads had been above 350 bp as recently as April 2025, the tightening trend has been broad-based and persistent, contributing to solid total returns in hard-currency EM sovereign debt. One of the more striking developments during this period was the sharp rally in Republic of Ecuador bonds, where successful issuance and improving market access boosted both sentiment and flows for other high-yield EM credits. This rally highlighted how positive credit narratives can drive performance even in higher-beta segments of the index and further supported overall spread compression. Against this backdrop, emerging market debt continued to offer diversification benefits for global fixed-income portfolios, helped by the asset class’s attractive carry and the broader macro environment supportive of EM external debt performance.

The following chart shows the yield spread versus US Treasuries of the JP Morgan EMBI Global Index

JPM EMBI Global Spread



Source: Bloomberg Finance L.P., 2 February 2026.

Capital Markets Monthly FOREIGN EXCHANGE

February 2026

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The New Fed Chair and the US Dollar's Recent Fortunes

It was an explosive start to the year for financial markets, with geopolitics taking centre stage. Events in Venezuela, followed by the most serious crisis within the NATO alliance since its founding, dominated headlines and prompted an extraordinary series of high profile statements from Western political leaders at the World Economic Forum in Davos.

Despite these unusual developments, most asset classes initially remained calm. However, some of the comments from Davos — including suggestions to diversify away from U.S. assets — tested investor patience, and as is often the case, the foreign exchange market sounded the first alarm bells.

The U.S. Dollar Index (DXY) began the year at around 98.30, a technically neutral level, and then gradually climbed, breaking above its 50, 100 and 200day moving averages. Normally, such price action would suggest growing momentum, but this time the advance lacked strong follow through. DXY peaked near 99.50 on the day the Davos symposium opened — it's high for January — before retreating back toward 98.30 as investors awaited clarity from policymakers.

Some market participants interpreted parts of the Davos dialogue as a signal to reduce exposure to the U.S. dollar, and in the days that followed, the DXY slid sharply, losing roughly three figures as negative sentiment built. This downward pressure was amplified by speculation that Japanese authorities might intervene in the FX market to support the yen, with some rumours even suggesting possible coordination with U.S. policymakers — though these were later denied by U.S. officials.

The effect showed most clearly in major exchange rates: USD/JPY weakened significantly, sliding toward levels near 153 amid intervention talk, while EUR/USD rallied above the key 1.2000 level, briefly touching 1.2080 as euro strength gathered momentum.

As market concerns spread, U.S. Treasury Secretary Scott Bessent publicly denied that the United States was planning or considering joint action with Japan to support the yen — reaffirming the U.S. “strong dollar” policy on January 28. This announcement provided a short-lived relief for the dollar.

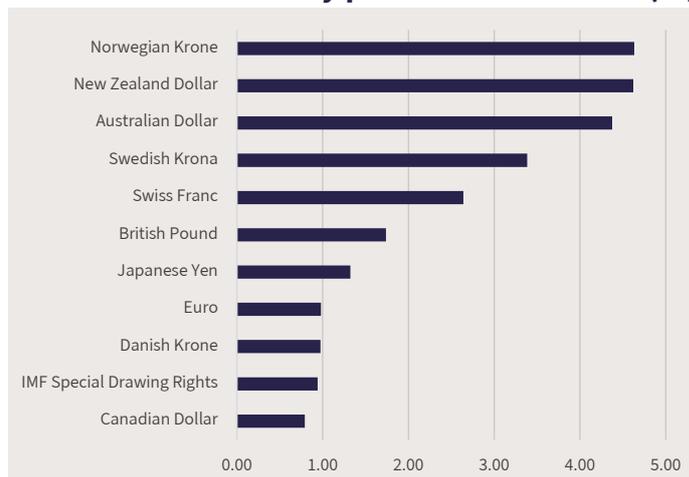
The more sustained support for the U.S. dollar came from a surprise political development: the nomination of Kevin Warsh as the next Chair of the Federal Reserve by President Donald Trump. Warsh, a former Fed governor during the global financial crisis, is widely perceived by markets as a figure who could bring credibility and stability to the central bank's leadership — countering earlier fears that a more politically influenced candidate might fuel dollar outflows.

News of Warsh's nomination helped the dollar recover some ground. USD/JPY rebounded to finish the month near 154.80, representing a modest strengthening from recent lows, while EUR/USD retraced part of its gains, closing January around 1.1840.

Among other major currencies, January was particularly favourable for so called “high beta” G10 currencies. The Norwegian krone (NOK) led gains with a strong performance, followed closely by the New Zealand dollar and Australian dollar, while the Canadian dollar posted more modest appreciation (detailed figures shown in the table below).

Elsewhere, the Chinese renminbi (CNY) strengthened modestly, ending the month comfortably below the psychologically significant 7.00 level, positioning itself well ahead of the Lunar New Year celebrations, the Year of the Fire Horse.

January performance vs. USD (%)



Source: CAIM, 30 January 2026.

Capital Markets Monthly EQUITIES

February 2026



United States

Market gains but headline risks remain

U.S. equities advanced in January, with the S&P 500 briefly moving above the 7,000 level as economic data continued to outperform expectations. Despite the strong headline move, underlying volatility remained elevated, driven in part by rising geopolitical tensions across Venezuela, Iran, and Greenland. The Federal Reserve was a central focus for markets. A Department of Justice criminal investigation reignited discussions around central bank independence, adding to policy uncertainty. The FOMC delivered its third consecutive rate cut, while on January 30 President Trump nominated Kevin Warsh as the next Fed Chair—another development investors are watching closely.

The latest FOMC meeting delivered few surprises. As expected, the Committee held rates steady at 3.50–3.75%, though Governors Miran and Waller dissented in favour of a 25bps cut. The statement leaned modestly hawkish, upgrading economic growth to “expanding at a solid pace” from the previous “moderate” description and noting the labour market is “showing signs of stabilisation.” Chair Powell’s press conference struck a balanced tone. As anticipated, many questions centred on Fed independence, the ongoing DOJ investigation, and the recent Supreme Court hearing involving Governor Lisa Cook. Powell largely declined to engage on these issues, keeping the focus on the economic outlook and the data-dependent path ahead.

Macro data in January was broadly supportive. The December employment report showed the unemployment rate unexpectedly falling to 4.375%, with November revised lower. Other labour indicators, including a firmer quits rate, steady jobless claims, and low Challenger layoffs, also suggested resilience. While this reduces fears of a sharp labour-market downturn, payroll growth remains narrow and subdued. December CPI was softer than expected, with core CPI easing on the back of falling goods prices. Used cars, trucks and IT commodities, including computers, smartphones, etc. all declined. However, some viewed the report less positively, noting that the weakness was led by a handful of outlier categories. The Cleveland Fed’s trimmed mean, which removes such outliers, still rose +0.31% on the month.

As Q4 earnings season progresses, U.S. large-cap results have been broadly reasonable. While the share of S&P 500 companies beating earnings expectations is running below recent averages, the size



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of the upside surprises is larger than usual, lifting index-level earnings relative to where expectations stood at quarter-end. In financials, revenues less than the prior quarter but remaining above the three-year average. Banks continue to report lower-than-expected credit-loss provisions, supported by stable asset quality and slightly improved macro forecasts. JPMorgan will assume the Apple credit-card program from Goldman Sachs, representing a net loss for JPM and a gain for GS. Looking into 2026, banks generally anticipate mid-single-digit revenue growth, underpinned by steady gains in both net interest income and fee income. Expense growth is expected to run near 3%, asset quality should remain broadly stable, and management teams continue to signal active share-repurchase plans.

Among the Mega-Cap 7, performance has been mixed. Meta rallied after guiding to stronger ad-driven sales and signalling higher 2026 capex. Microsoft slipped despite modest earnings beat, as cloud revenues only met already-elevated expectations and capex came in higher than anticipated. Tesla rose on a clean beat and plans to deploy \$20bn in 2026 to streamline its EV lineup and accelerate robotics and AI initiatives. Apple delivered a solid Q4 sales beat and issued upbeat Q1 revenue guidance, helped by strong iPhone 17 demand and a rebound in China. However, rising costs tempered the positive headline numbers.

U.S. equities gyrated over the month but produced gains with a rotation into cyclical stocks with energy, materials and industrials outperforming. Energy stocks gained on stronger oil prices due to the increased geo-political risk premia especially from US/Iran issues. This also helped defence stocks as well as comments from President Trump regarding increasing the military budget to \$1.5tn in 2027. The materials sectors saw strength via precious metals, due to investors becoming more concerned about potential currency debasement and future inflation, these were supported by the ongoing geopolitical uncertainty. Financials were an underperformer, as earnings guidance for some of the money centres did not reach lofty expectations together with President Trump’s post that he was calling for a one-year cap on credit card interest rates of 10%. How realistic that is to implement is a moot point and it may reduce credit to the poorer population.



Europe

Encouraging start but need the earnings to come through

European equities began 2026 with strong momentum, extending the rally that closed out 2025. Markets were supported by easing financial conditions, improving macro data, and a better-than-expected Eurozone Q4 GDP print of 0.3%, which boosted confidence and aided cyclical sectors sensitive to growth expectations.

Inflation data also helped sentiment. Euro Area inflation for December came in below expectations, easing residual concerns about a potential hawkish tilt from the ECB and reinforcing the view that the next move is more likely to be a rate cut rather than a hike.

Fourth-quarter earnings have been broadly in line with expectations, but share-price reactions have skewed negative. Mixed 2026 guidance has not kept pace with elevated expectations, signalling a shift toward a more selective and valuation-sensitive market. Visibility on earnings remains crucial given headwinds from a stronger euro and rising long-term bond yields.

Sector performance was varied. Materials and energy outperformed on the back of firmer commodity prices. The Information Technology sector was more mixed, with semiconductor names such as ASM International advancing, while software names, including SAP underwhelming. Luxury goods were notable laggards, with the sector weighed down by a sharp drop in LVMH following disappointing earnings.



Developed Asia

Diversification theme and earnings results provide support

Asian equities began 2026 on a strong footing, supported by broad-based gains and improving investor inflows. Hong Kong outperformed as Q4 GDP beat expectations, with growth shifting from external to domestic demand.

Japan saw sharp market moves after the announcement of a February 8 snap election, which initially boosted equities on expectations of fiscal stimulus and early-month yen weakness. Later in the month, however, fiscal concerns drove long-end JGB yields higher as election pledges for consumption-tax cuts triggered a sell-off. The Bank of Japan added a hawkish tone, keeping rates on hold but raising its inflation outlook and signalling further tightening. This strengthened the yen and prompted profit-taking after early gains.



Emerging Markets

Emerging market equities outperformed developed markets, led by Information Technology, where memory-chip makers rallied on stronger AI-driven demand and record-strong 4Q results including from Samsung and SK Hynix. Materials also outperformed, supported by firm precious and base-metal prices despite a late-month pullback. A weaker U.S. dollar provided a major macro tailwind.

Regionally, Latin America led thanks to its materials exposure and high beta to dollar weakness, while CEEMEA and EM Asia delivered in-line performance.

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