CAIM CROWN AGENTS INVESTMENT MANAGEMENT

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Geopolitics dominates as Middle East conflict escalates

In February 2026 US Treasuries posted strong total returns as falling inflation and sharply rising geopolitical risks drove yields lower across the curve. Headline CPI slowed to 2.4% year-on-year from 2.7%, reinforcing confidence that disinflation remains intact and supporting expectations that the Federal Reserve can ease later in the year. Yields declined meaningfully, with the 10-year moving back below the 4% level having traded as high as 4.30% earlier in February. Late-month developments in the Middle East, including the attack involving Iran, triggered a clear risk-off move, widening credit spreads and prompting a flight to quality that further supported US Treasury demand. Macroeconomic data were mixed but generally consistent with moderating price pressures and slowing, though still positive, growth, leaving the Treasury market well bid into month-end. Elevated geopolitical tensions following the US / Iran conflict and disruptions around the Strait of Hormuz should sustain a baseline bid for low-risk assets like US Treasuries as investors seek safe-haven assets amid heightened risk premia. However, the outlook is tempered by inflation risks from higher energy prices: oil benchmarks have surged sharply on supply-route disruptions and conflict escalation, with prices rising significantly higher if the crisis persists, which would put renewed upward pressure on consumer prices and complicate the timing and magnitude of monetary policy easing by the Federal Reserve.

The UK Gilt market broadly followed the move in US Treasuries, with yields drifting lower and prices supported by softer inflation data and growing expectations of monetary easing. Headline UK CPI eased to 3.0% in January from 3.4% in December, the lowest reading in nearly a year, helping to reinforce the narrative that price pressures are continuing to abate and underpinning demand for gilts. This disinflation backdrop pushed 10-year gilt yields down modestly through the month as markets priced in a higher probability of Bank of England cuts in the coming meetings. At the same time, gilts remained positively correlated with USTs, as global safe-haven flows amid geopolitical risks cushioned yields and limited volatility. Looking ahead, the outlook for gilts remains constructive as moderating inflation and BoE rate cut expectations should generally support valuations, though sterling and gilt yields could face renewed pressure if external inflation drivers—such as higher global energy prices tied to elevated Middle East tensions—filter through to UK price statistics.

European government bonds tracked the global rally, with Bund yields declining modestly in sympathy with Treasuries and Gilts amid softer global inflation prints and risk-off flows. However, domestic dynamics were more complex. Media reports suggesting that Christine Lagarde could step down early—potentially allowing French President Emmanuel Macron and German Chancellor Merz to influence the nomination of her successor ahead of the French presidential elections—introduced an element of political uncertainty into ECB leadership expectations. Despite this, the ECB has not signalled imminent rate cuts, and easing prospects remain much more limited than in the US or United Kingdom. With core European government bond yields still comparatively low, valuations appear relatively rich on a cross-market basis, leaving limited room for further compression absent a material shift in growth or policy guidance.

Japanese government bond markets continued to diverge from the US and Europe. The market remained driven by domestic factors, notably political uncertainty and the Bank of Japan's tightening cycle. With policy rates already raised and further increases likely, the front end stayed under pressure. However, the significant backup in yields since late 2025 has improved valuations, and higher carry is beginning to attract domestic real money demand. Elevated issuance and fiscal expansion keep term premia firm, but at current yield levels JGBs offer better value than earlier in the cycle. The outlook remains shaped primarily by further BoJ rate hikes and domestic political developments rather than global risk sentiment.

Chinese government bonds remained relatively stable, with low yield volatility and limited correlation to moves in USTs, Gilts or EGBs. Domestic liquidity conditions stayed accommodative and the PBOC maintained a measured policy stance, anchoring the front end and keeping the curve well contained. The renminbi strengthened during the month, supported by capital inflows and a softer US dollar, reinforcing demand for onshore duration. However, recent adjustments by the PBOC to FX forward reserve requirements are likely intended to moderate further CNY appreciation and smooth currency volatility. Overall, CGBs continue to offer diversification benefits given their low cross-market beta and comparatively stable yield profile.

Emerging market sovereign debt faced a more challenging backdrop. The JP Morgan EMBI Global spread widened from 223bp to 236bp, marking a meaningful reversal of the persistent tightening trend that had been in place since April 2025. The move reflected a combination of risk-off flows linked to geopolitical tensions and some profit-taking after an extended period of strong performance. Higher US Treasury volatility and renewed sensitivity to energy prices also weighed on sentiment, particularly for lower-rated sovereigns. While fundamentals across much of the asset class remain broadly stable, the widening highlights that valuations had become tight and that EM spreads are vulnerable to shifts in global risk appetite and US rate expectations.

The following chart shows the yield on 10-year US Treasury Notes over the past year

US Treasury 10-Year Yield

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

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FOREIGN EXCHANGE

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The die is cast…

At the time of writing this commentary, the geopolitical events that unfolded over the final weekend of the month already make February's financial market developments feel like distant history. However, viewed from the perspective of the past few days in March, the performance of several asset classes now appears entirely logical.

Markets closed February on a cautious note, with gold emerging as the preferred destination for financial flows. After advancing nearly 14% in January and moving into overbought territory (with the Relative Strength Index rising well above 80.00), many market participants expected gold to retrace and enter a consolidation phase. The first trading day of February appeared to confirm this expectation, as prices moved sharply lower.

In the final days of January, gold reached a new all-time high of 5,595 (on 29 January), only to fall by more than USD 1,000 within two days, briefly approaching the 2026 low recorded during the first trading sessions of the year. Gold traded as low as USD 4,402 on 2 February. This ultimately proved to be the low for the month, as a sharp recovery followed, with prices rebounding toward USD 5,000. Gold subsequently stabilised at that level, building a base for much of the remainder of the month. During the final week of February, prices moved higher again, closing the month at USD 5,280.

As for the G10 currencies, performance was mixed, with volatility contained and trading ranges largely confined within +/- 1%. Two currencies stood out. The Australian dollar advanced by 2.20%, supported by a favourable interest rate differential and diversification flows. At the other end of the spectrum was the British pound, the weakest G10 performer, shedding 1.49% against the US dollar. This weakness reflected an unfavourable domestic political outcome and market expectations that the Bank of England will continue its monetary policy easing cycle.

The Chinese renminbi also deserves mention, delivering a solid performance at the start of the Lunar New Year — the Year of the Fire Horse — with a gain of 1.38%. The renminbi strengthened to its highest level since 2023. This performance can be attributed to international diversification flows seeking increased exposure to Chinese equities.

Outlook for the coming weeks

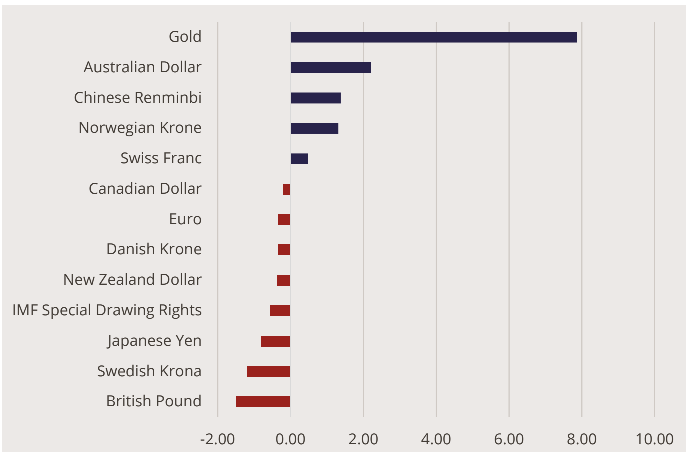
Strong US dollar–negative diversification flows from US-based investors, observed over the past few months, are likely to reverse sharply back toward US assets. In the initial phase of a risk-off environment, history suggests that US dollar strength should once again become one of the defining features of this rapidly evolving landscape.

Over a longer horizon, however, global capital originating outside the United States — wary of potential unpredictability in the investment environment — will likely continue to seek diversification opportunities. Once the initial panic subsides, the depth, liquidity, and scale of Eurozone markets suggest they could become a primary destination for such flows. Within Europe, the Scandinavian bloc offers compelling alternatives, particularly the Norwegian krone.

Outside Europe, both the Australian and Canadian dollars appear attractive. A similar constructive view applies to China. By contrast, emerging markets — previously a key destination for diversification flows — may need to wait. Investment strategies are likely to adjust their models in response to elevated energy prices, their impact on macroeconomic fundamentals, and the potential policy adjustments that many emerging market central banks may be forced to implement.

One conclusion appears clear: the current events in the Middle East could have a lasting and potentially profound impact on economies, financial markets, and asset valuations worldwide. The world we knew in February has changed — the Rubicon has been crossed.

February performance vs. USD (%)



Source: CAIM, 27 February 2026.

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Capital Markets Monthly
EQUITIES

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United States

Markets see rotation as AI exuberance wanes somewhat

US equities fell over the month despite resilient macro data. Markets continued shifting from broad AI optimism to more company-specific differentiation, with rising concern about AI's disruption, especially for software firms. Markets also had to contend with news that the US Supreme Court ruling (6–3) that the administration's use of IEEPA for broad tariffs was unconstitutional. The administration responded by signalling plans for a 10% global tariff under Section 122, potentially rising to 15%. Geopolitical risks increased as US/Israel–Iran tensions pushed oil to a seven-month high, culminating in US and Israeli strikes on Iran at month-end.

The "goldilocks" outlook of lower rates and solid growth faced resistance after hawkish FOMC minutes. Officials noted signs of a stabilising labour market, and several supported more two-sided language on future moves, leaving open the possibility of hikes if inflation stays above target. While far from signalling imminent tightening, it reinforces that most of the Committee is in no hurry to cut further.

Macro data remained supportive. The latest Employment Report was much stronger than expected, with the biggest monthly payroll gain since December 2024, and unemployment unexpectedly falling to 4.3%. January CPI also came in below expectations, a sufficiently dovish outcome for traders to increase the number of rate cuts priced in by December 2026.

With Q4 earnings season nearly complete, results have exceeded expectations, supported by strong revenue growth and firm margins. Analysts have also raised 2026 earnings estimates over the past two months. Among the Mag 7, Nvidia fell sharply post-earnings despite beating all major metrics and issuing a strong outlook. Alphabet posted a solid revenue beat, with Google Cloud up 48% to $17.7bn, while Amazon's net sales guidance was broadly in line. However, investor focus shifted to rapidly rising capex plans and its funding implications with Alphabet, Amazon, Meta and Microsoft together now projected roughly $650bn of capex in 2026. Outside of Mag 7, Walmart shares fell after a weaker-than-expected outlook, highlighting some conservatism by the new management team. The broader consumer sector and market took this as potential evidence of softness in the US economy.

US equities swung throughout the month, with the major cap-weighted index finishing lower while equal-weighted indices rose, highlighting the breadth of the rotation trade. Fears over AI's disruptive impact triggered sharp selloffs across sectors, initially hitting software, then spreading to asset management and commercial real estate. These groups, along with the Magnificent Seven, were the clear underperformers as investors questioned the durability of their growth leadership.

Financials were further pressured, with wealth managers reacting to new AI-driven tax-planning tools, and sentiment weakened further after Blue Owl Capital restricted withdrawals from a private credit fund, raising concerns about broader redemption risks. On the positive side, consumer staples held up better amid a shift toward defensive names. Utilities and materials outperformed, while elevated oil prices, supported by ongoing geopolitical tensions and protracted talks with Iran boosted the energy sector.

Europe

Market gains still more valuation rerating than earnings driver

European equities rose in February, supported by stronger-than-expected macro data and sentiment gains after the US Supreme Court struck down President Trump's global import tariffs. At its latest meeting, the ECB left the deposit rate unchanged at 2%, as expected. President Lagarde said inflation was now in a "good place" and signalled no imminent policy shift in either direction.

Q4 results show Europe's earnings recovery remains on track, supported by more upbeat corporate commentary on the economic outlook, constructive guidance, and strong capital return plans. FY26 earnings revisions have been broadly stable through the season, with estimates little changed since last summer. Basic Resources, Tech, and Banks stand out with the most positive revisions.

All sectors gained in February except Financials and Technology, where sentiment remained cautious due to high valuations and ongoing uncertainty around consumer strength, AI spending, and potential disruption. Siemens dropped sharply amid rising concerns that industrial software could also be vulnerable to AI-driven displacement.

Developed Asia

Japanese markets rise on Takaichi stimulus hopes

Asian equities delivered mixed performance in February. Hong Kong lagged due to IT sector concerns, though signs of a property-market recovery continued to support sentiment.

Japan posted strong gains after PM Takaichi secured a historic post-war majority, raising expectations for more aggressive fiscal policy and stronger growth. Yen weakness was reinforced by reports that Takaichi expressed caution about further rate hikes in discussions with BoJ Governor Ueda, alongside news that two reflationist nominees were selected for the BoJ board, developments seen as supportive of additional stimulus.

Emerging Markets

Emerging-market equities extended their outperformance versus developed market indices, led by strength in IT.

Regionally, EM Asia outperformed, with Korea and Taiwan boosted by tech-hardware stocks and, in Korea's case, governance reforms. LatAm benefited from commodity exposure and firmer currencies, while EMEA delivered more muted returns due to weakness in financials.

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