

Monthly Market Commentary

February 2026 & Geopolitical Update

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Broadening Leadership in a Shifting Landscape

February offered a tale of two markets. On the surface, the S&P 500 declined 0.8%, but beneath that headline number, a notably healthier picture emerged. The equal-weighted S&P 500 gained 3.5%, Large Cap Value rose 2.6%, and the Russell 2000 added 0.8%, a clear signal that market participation is widening.

The narrow dominance of mega-cap technology stocks that defined much of the prior bull market cycle appears to be giving way to a more broadly distributed rally. Diversified investors, often frustrated during the period of tech-led concentration, are beginning to see their patience rewarded.

The rotation away from growth was decisive. Large Cap Growth fell 3.4%, and the Nasdaq declined 2.3%, as investors grappled with mounting questions about artificial intelligence's disruptive potential. A wave of AI product launches sparked a reassessment, not just of who wins in an AI-driven world, but of which industries face existential pressure. Software, consulting, real estate services, financial services, and freight brokerage all came under scrutiny. Selling was sharpest in early February but stabilized as the narrative shifted toward AI as a productivity enhancer rather than a wholesale disruptor. That debate, however, is far from settled and will remain a recurring theme throughout the year.

At the sector level, the breadth of the rally was unmistakable. Utilities led all sectors with a 10.3% gain, followed by Energy at 9.4%, Materials at 8.4%, Consumer Staples at 7.9%, and Industrials at 7.1%. Seven of eleven sectors outperformed the index, a meaningful sign of rotation into more defensive and cyclical corners of the market, away from high-multiple technology names.

Bonds and Gold Rally as Investors Seek Safety

Fixed income delivered a strong month, with the U.S. Bond Aggregate returning 1.6%. The 10-year Treasury yield fell nearly 0.30%, closing below 4.00% for

the first time since October. Long-duration Treasuries gained 4.1%, and mortgage-backed securities returned 1.6%. Investment-grade corporate bonds outperformed high-yield, though widening credit spreads kept corporates from matching Treasury gains.

Importantly, the rally in bonds was not driven by expectations of imminent rate cuts. The Federal Reserve held rates steady at its January meeting following a December cut, and futures markets have pushed the next anticipated cut to no earlier than June.

Instead, the yield decline reflects a classic flight-to-quality dynamic: investors seeking lower-volatility assets amid tech sector turbulence, trade policy uncertainty, and rising geopolitical tensions. Gold reinforced this theme, gaining more than 10% in February, its strongest monthly performance in years.

Fed minutes from the January meeting continued to signal inflation vigilance. The economic data support that patience: January payrolls came in at 130,000, unemployment declined to 4.3%, manufacturing activity returned to expansion for the first time in nearly a year, and core CPI rose at a 2.5% annual rate, the slowest pace since early 2021. The Fed has room to wait, and the market increasingly expects it will.

Geopolitical Risk: The Middle East in Focus

Beyond the rotation story, rising tensions in the Middle East represent a meaningful variable for financial markets in the near term. Ongoing conflict in the region, particularly involving Iran, since the start of the US and Israel attacks, has elevated investor caution and contributed to an immediate increase in the demand for safe-haven assets like gold and Treasuries.

The primary transmission channel from the Middle Eastern conflict to global markets runs through energy. Approximately one-third of the world's seaborne oil supplies pass through the Strait of Hormuz, a narrow waterway separating Iran from the Gulf states. Any act of retaliation or escalation targeting this shipping route could have significant ramifications for both geopolitical tensions and energy markets. The

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Energy sector's 9.4% gain in February partly reflects this premium being priced into oil-linked equities.

The range of outcomes, however, is wide. Analysts have outlined scenarios ranging from a contained de-escalation with only a brief, small rise in oil prices to a significant escalation with substantial global economic repercussions.

In a contained scenario, financial markets may see brief turbulence, though global trade and economic growth would largely remain stable.

In a more severe scenario involving Strait of Hormuz disruption, research from the Dallas Federal Reserve suggests a temporary closure could drive WTI crude toward \$100 per barrel, resulting in a cumulative increase of 1.3 percentage points in the annualized headline inflation rate, though the inflationary effect would diminish once oil prices stopped rising.

History offers some perspective on how markets have weathered similar environments. Regional conflicts like this may lead to short-term volatility, but they are unlikely to disrupt economic activity sufficiently to drive a bear market.

When fighting occurs during a bull market, stocks typically resume rising well before the conflict ends. Historical market reactions to military conflict have often been short and quickly reversed, and the probability of a more severe and protracted scenario currently remains low.

The U.S. is also better insulated from oil shocks than in prior decades. As the largest single oil producer globally, representing around 20% of total output, the self-sufficiency of U.S. production limits the domestic impact of energy supply shocks from the Middle East.

However, these near-term risks deserve attention. The "perception" that conflicts could "worsen or spread" is the chief concern, with fear and uncertainty clouding the outlook, according to the World Economic Forum. While markets have historically shown resilience in the face of regional conflicts, much as they largely looked through the volatility following the onset of the Israel-Hamas conflict in October 2023, the situation warrants close monitoring.

For investors, the key watchpoints remain: the trajectory of oil prices, any signs of

Strait of Hormuz disruption, and whether the conflict draws in additional regional or global powers. In the absence of a significant and sustained oil supply shock, we believe the base case remains one of manageable short-term volatility against a backdrop of resilient economic fundamentals.

Please contact us if you'd like to discuss.

Dennis P. Barba, Jr.
CEO & Managing Partner

Michael P. Finkelstein, CFA
Partner

Robert Frenkel, CFP®
Chief Investment Officer

oxfordharriman.com

S&P 500 Index is a capitalization-weighted index calculated on a total return basis with dividends reinvested. The index includes 500 widely held U.S. market industrial, utility, transportation and financial companies.

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