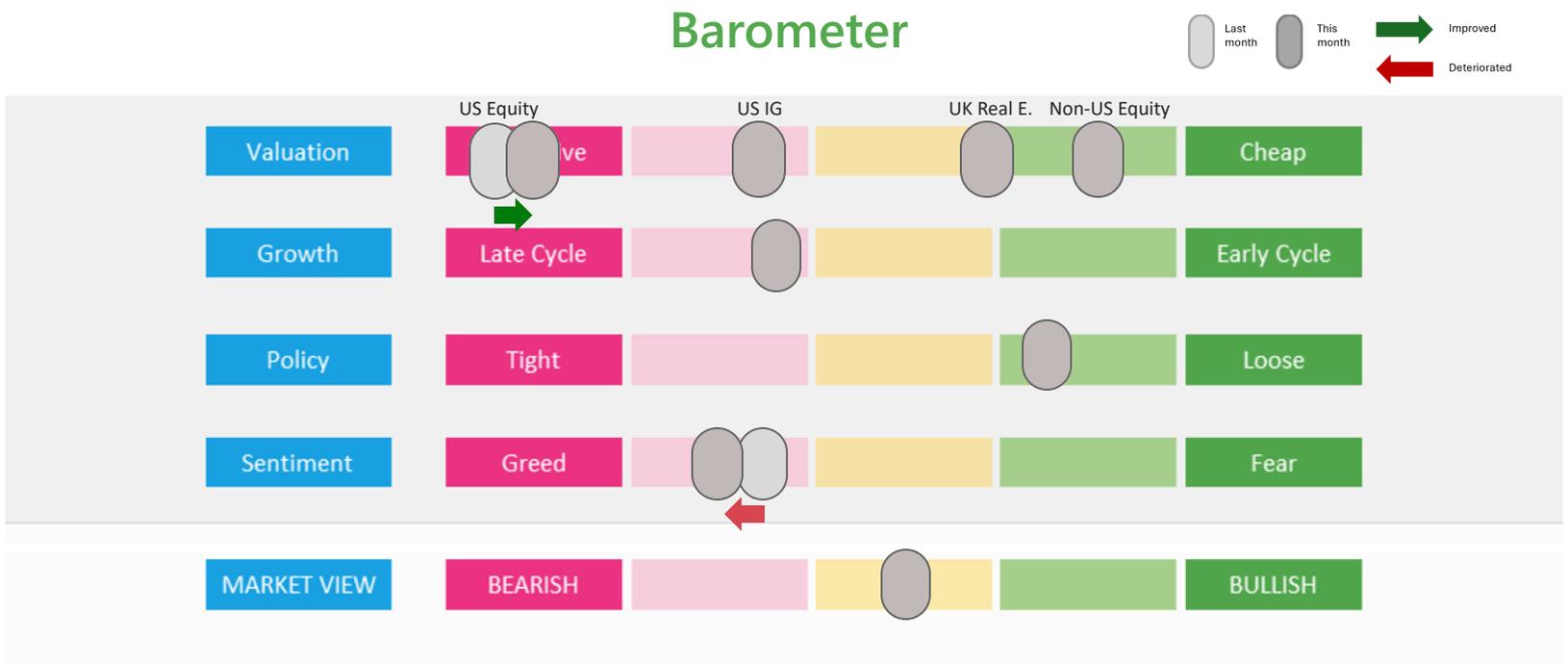


Market Barometer



New Stagflation Risk but Fundamentals Excellent

The US/Israel attack on Iran injects uncertainty into what are otherwise excellent macro fundamentals supporting risk assets.

The **underlying positives** are:

- Earnings are growing and earnings growth is accelerating, and not just in the US but around the world.
- Earnings breadth remains positive, with (unusually) more upgrades than downgrades
- The risk-free rate has been remarkably controlled, with the 10 year US treasury yield in a tight range (4.0-4.5%)
- Credit spreads remain extremely well-behaved despite all the news around "cockroaches" in the private credit market

However, the situation in the Middle East has the potential to derail these positives, risking a stag-flationary impulse to the world economy.

In our **Charts of the Month** we look at:

- Oil's impact on inflation
- Europe and the UK's greater susceptibility to an oil shock than the US
- The benefits of a normal yield curve and non-ZIRP
- The ability of revisions strategies to hedge equity risk

For now we choose to focus on what we know (excellent fundamentals) and look through risk that could pass quickly (the Iran situation). However, the longer it drags on the more it risks stagflation.

Contents

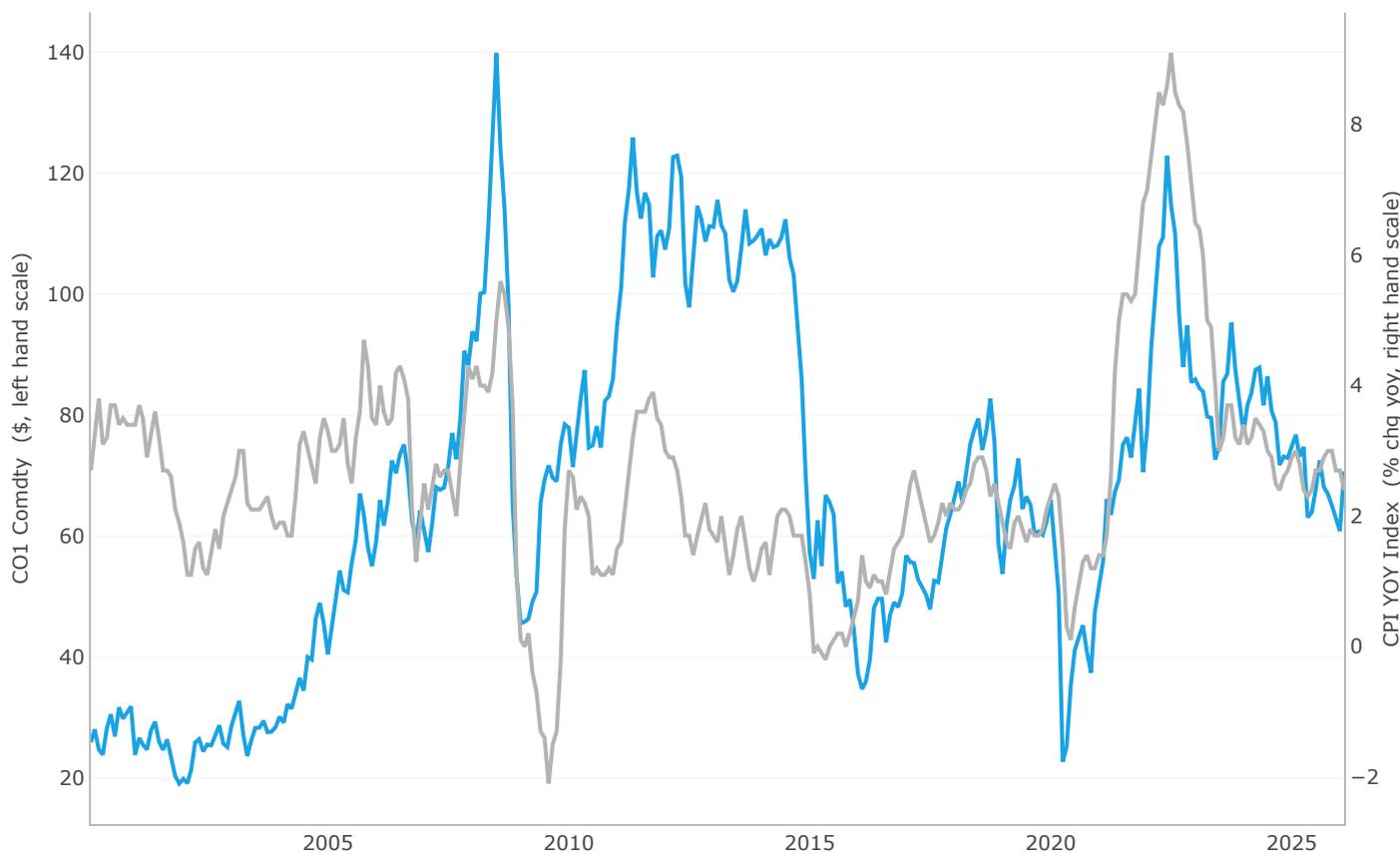
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Charts of the Month (1 of 4)

The oil price is very influential on inflation and growth, maybe surprisingly so given how much less oil intensive the developed market economies have become over the last few decades. This raises the questions, as we go to print with bombs falling in the Middle East and the Strait of Hormuz closed to shipping, of **how much inflation might now spike and whether that might be enough to cause a recession**.

Our view (on day four of Operation Epic Fury) **is that it is unlikely to overwhelm good economic fundamentals**. To list the positives: the US economy still has meaningful stimulus of the OBBB and even the IRA as a tailwind; interest rates are 3.75% now, not the 0.25% they were in the Ukraine commodity shock, so policy wouldn't need to move as far in reaction; the mini-cycle is anyway moving higher as PMIs are supportive; and the US is a big net exporter of oil and gas. **So as the engine of world growth, the US is unlikely to stumble assuming the Iran campaign does indeed last weeks not months or years**.

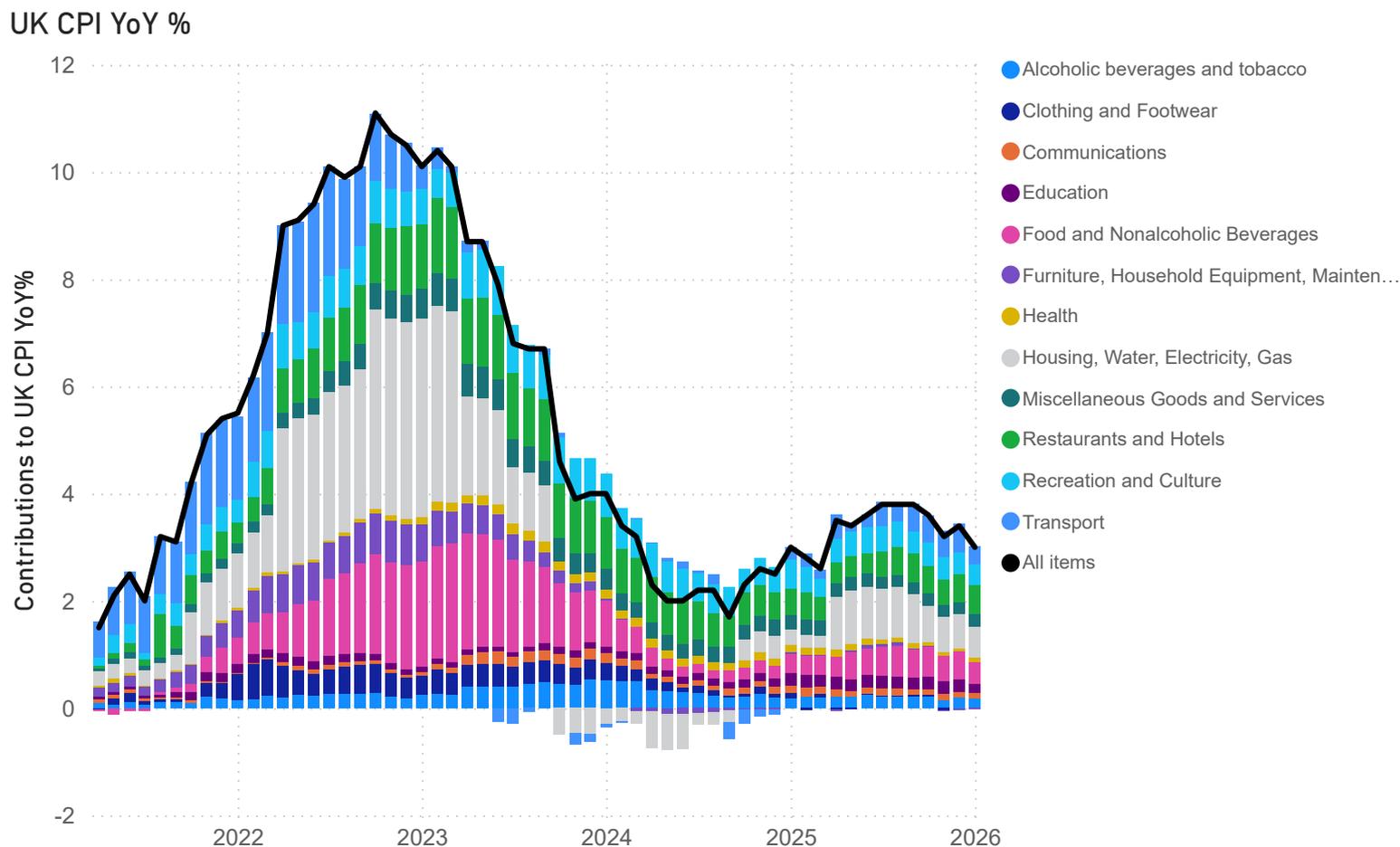
Oil Price (left) vs US CPI YoY (right)



Charts of the Month (2 of 4)

The Iran war impact on Europe and the UK is however substantially worse than it is for the US. Both are net importers of oil and of natural gas. Around 3/4rs of UK gas imports are from Norway but Qatar is a major supplier of LNG. Berenberg estimates that if the Brent crude oil price stayed at its new higher level of \$80 for the rest of this year, CPI inflation would be 0.7% points higher than currently forecast. This would mean that the trend lower in inflation, from currently 3% towards the consensus 2.4% for 2026 could reverse course and see inflation actually accelerate. That would make further rate cuts extremely unlikely, and would therefore have spillover consequences dampening growth.

The UK and European outlook is therefore critically dependent on the duration of the conflict.

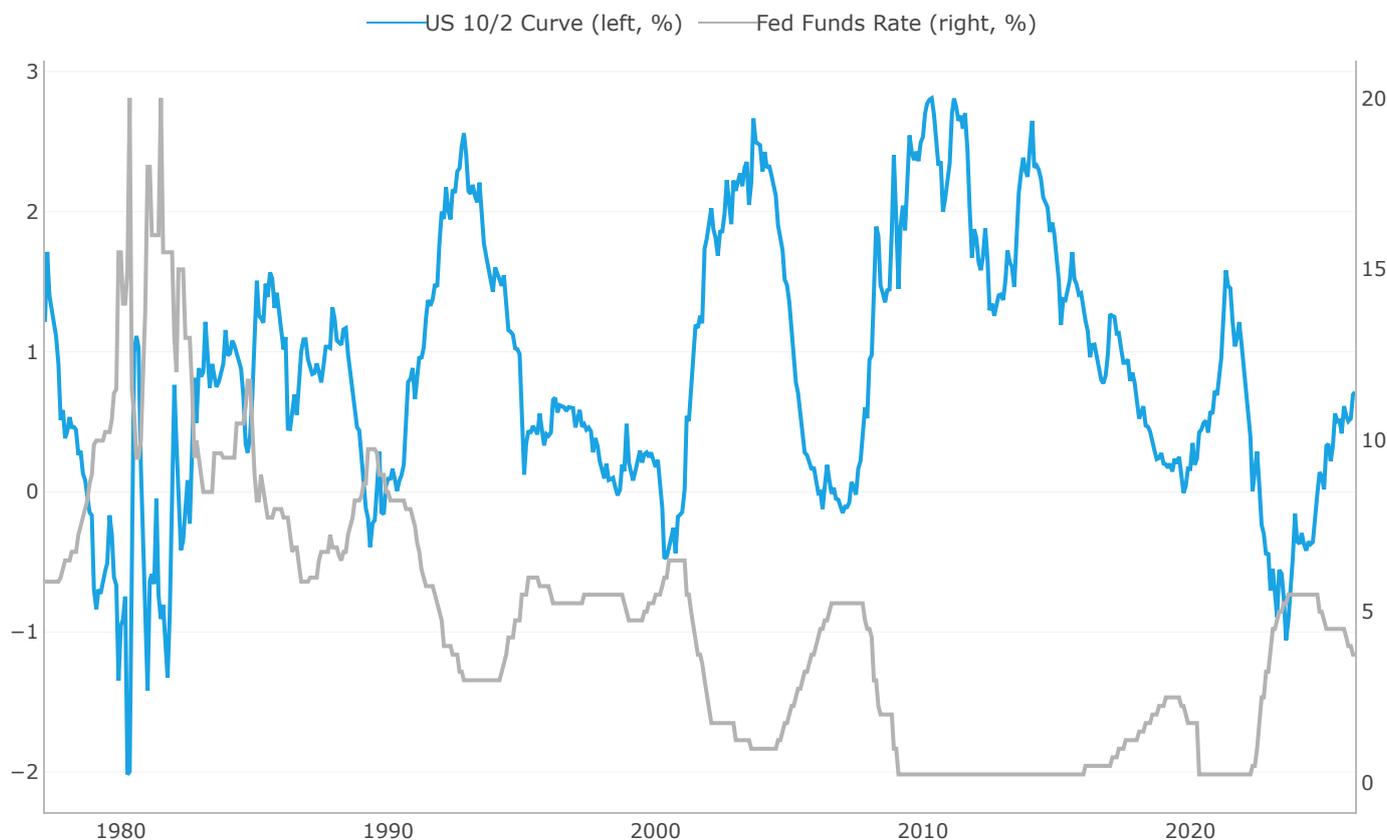


Charts of the Month (3 of 4)

A steeper curve is here to stay, in our view. The chart shows the symbiotic relationship between the direction of the Fed funds rate and the change in slope of the 10-2yr US yield curve. As short rates rise, the curve flattens. As short rates fall, the curve steepens.

On the assumption that rates don't have to be raised in response to an Iran-war induced inflation shock we expect that the curve will remain reasonably steep (currently +69bps spread between the 10 year yield and the 2 year yield). On the further assumption that the days of "secular stagnation" are behind us we expect that rates will not head back to zero. Between these two assumptions, a "normal" yield curve, reasonably steep and with rates not at zero, is a **healthy environment for banks and for the extension of bank credit.**

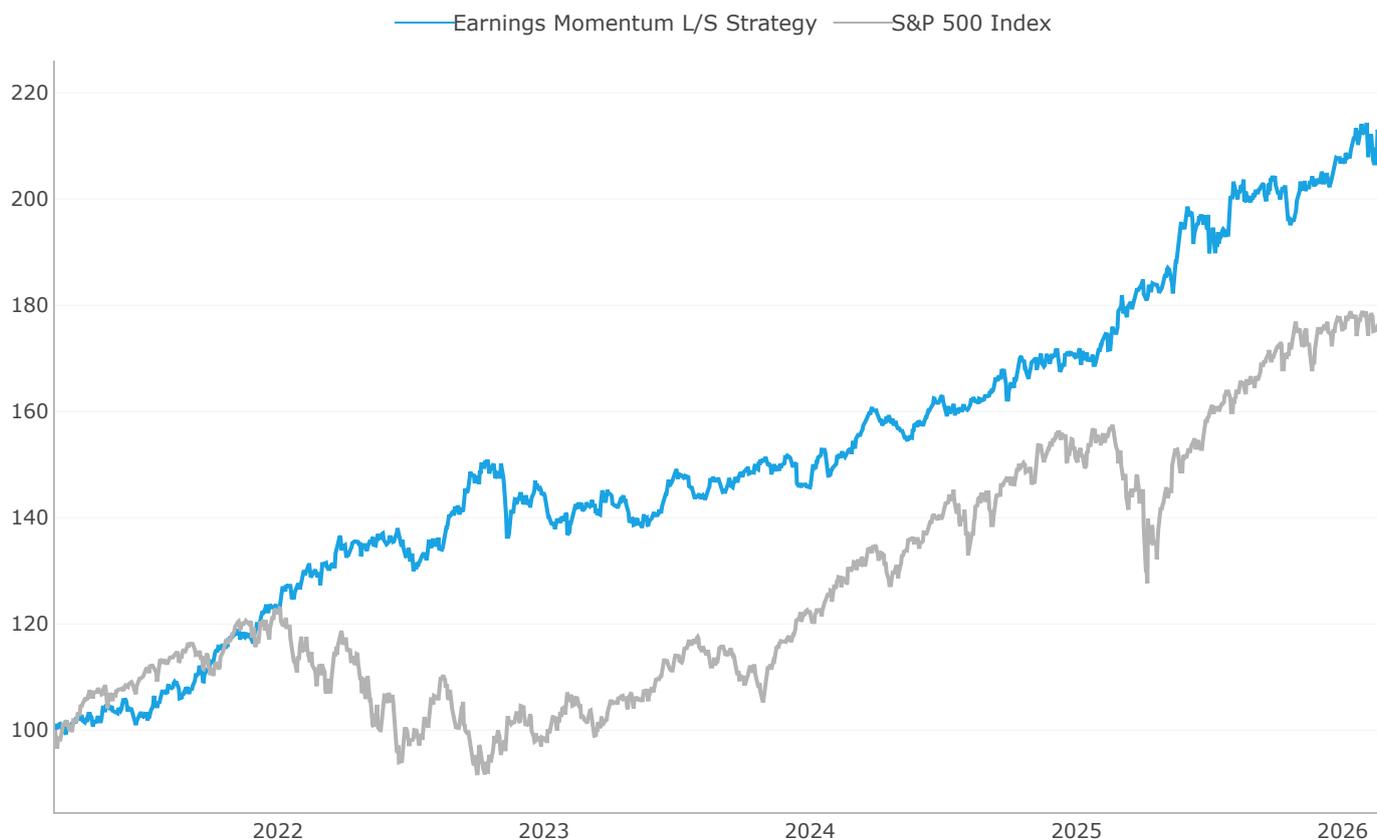
US Yield Curve (10yr-2yr treasury yield spread, %) vs Fed Funds Rate



Charts of the Month (4 of 4)

Earnings revisions strategies can help hedge equity risk. The chart shows the returns to a long short equity strategy that buys stocks with good earnings revisions and sells those with bad earnings revisions (in blue) and shows the S&P 500 (in grey). Note that the long short strategy worked well in the 2022 inflation-driven correction and in the 2025 tariff-driven correction. And so far it is working well in the 2026 Iran War-driven wobble.

Earnings Momentum vs S&P 500



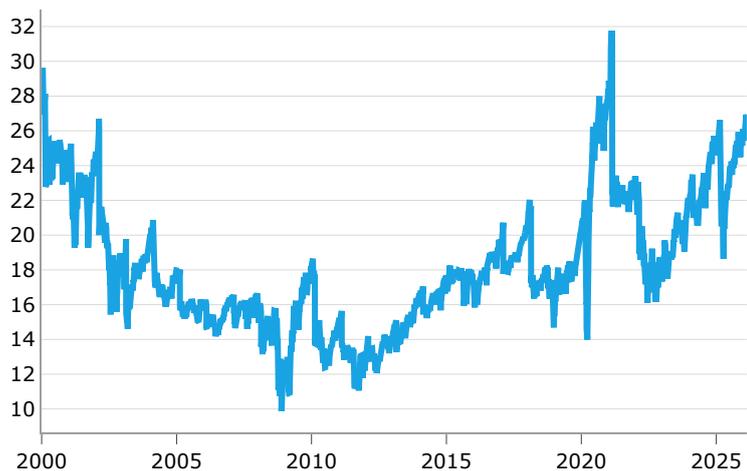
Equity | USA

Markets are beginning to reassess the Hyperscalers as their investment cycle accelerates. Google, Meta and Amazon have all guided capex 35% above market expectations, pushing the "Big 3+"¹ toward spending almost 90% of operating cashflow². We've previously highlighted the hurdle this creates for maintain returns. This pressure has now only increased. Recent announcements highlight the funding shift, from internal cash to corporate debt, with a chunky issuance of ~\$140bn a year expected for the next three years³.

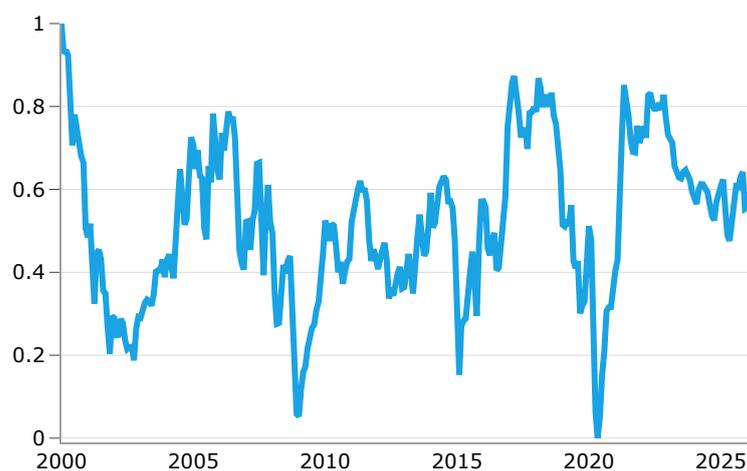
The move from capital light to capital heavy is being priced in: the "Big3+"¹ are down between 3%–20% YTD², and the broader "Mag 7" is down over 6%. Meanwhile, the beneficiaries of this capex wave - materials and industrials - are up double digits over the same period.

S&P 500 Valuations

S&P 500 Forward PE



Composite Value Indicator Model



CAPE / Shiller P/E



S&P 500 Equity Risk Premium



Note | Composite Value Indicator was built at Morgan Stanley in 1997 and is published with permission. It is an aggregate of seven equity yields adjusted for bond yield, T bills yield and inflation, and is expressed here in its percentile range. The CAPE / Shiller PE is today's price divided by the average earnings of the last 10 years. The Equity Risk Premium is calculated as the Shiller earnings yield minus the real bond yield.

Sources | S&P 500 PE: Bloomberg as at Feb 2026. Shiller PE/CAPE: Morgan Stanley, CVI Model: CCLA as of Feb 2026, Equity Risk Premium: CCLA as of Jan 2026. 1: Big 3+: Amazon, Microsoft, Google, Meta, Oracle. 2: Bank of America: 'Equity Strategy: Earnings Tracker Week 5...': 16 Feb 2026.

Equity | Regional

Japan is drawing renewed attention after Prime Minister Takaichi's decisive election win. **Global investors are increasingly rotating out of crowded US tech and into cheaper markets that still offer exposure to the AI theme - and Japan fits that shift well.** The country is emerging as an AI hardware powerhouse, supported by semiconductor strength and data-centre demand.

Positioning has risen sharply this year from around the 50th in Dec 2025 to above the 75th percentile by Feb 2026. Japan is already up more than 11% YTD, and unsurprisingly with most of that driven by re-rating. Earnings momentum remains positive across key sectors, with FY2025 profits expected to grow around 4%.

Europe

UK | Shiller P/E



Europe (Ex-UK) | Shiller P/E



Asia & Emerging Markets

Japan | Shiller P/E



EM | Shiller P/E



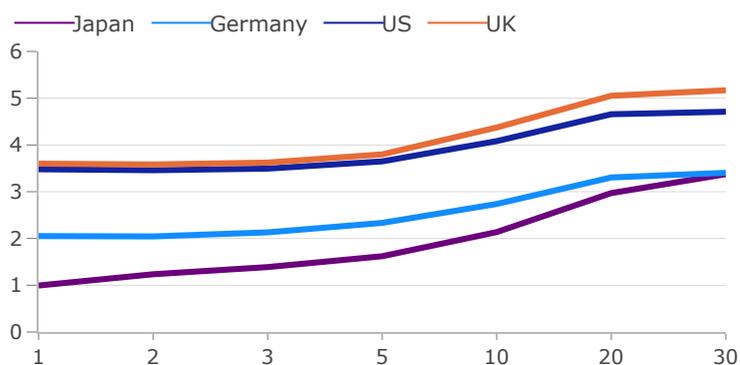
Bonds - Sovereigns

On 20 Feb the US Supreme Court ruled using IEEPA¹ for broad tariffs was unlawful, though it left open whether the \$130bn already collected must be refunded. As flagged in our January issue, both the decision and the administration's response were expected. Tariff use will shift to other Sections³, keeping 2026 revenues "virtually unchanged" (Scott Bessent). With deficits steady and T-bills the likely refund instrument, long-end yields held firm.

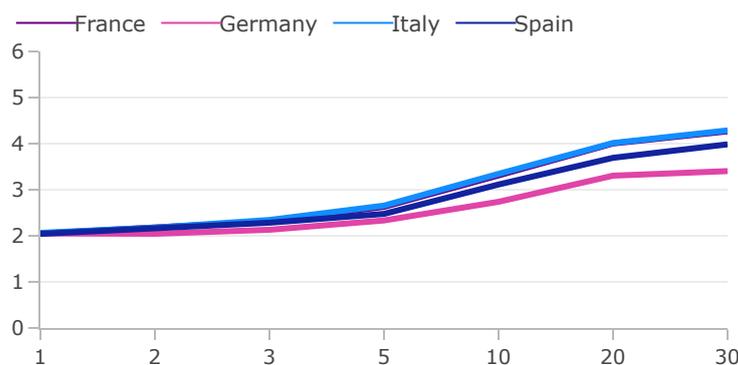
Separately, the SNP² plan to issue the first Scottish bond - "Kilts". Only £1.5bn in size, analysts see pricing ~0.3ppts over Gilts. Nonetheless, its AA-rating relies on continued access to UK Treasury funding; without it, spreads and ratings will likely worsen - making it a relatively poor financing tool - but a useful live meter of political risk.

Global Government Yields

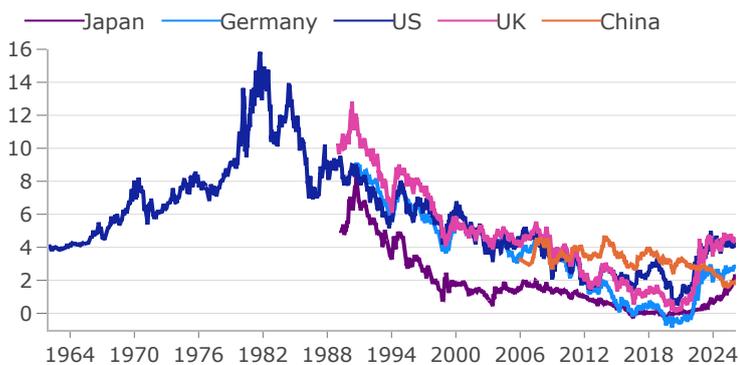
Global Treasury Yield Curves (Term vs %)



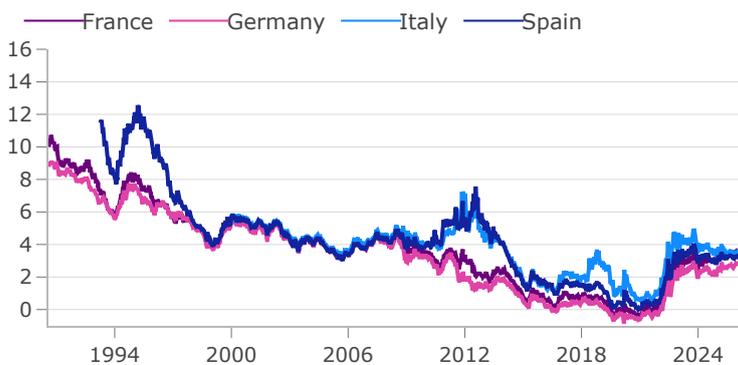
European Treasury Yield Curves (Term vs %)



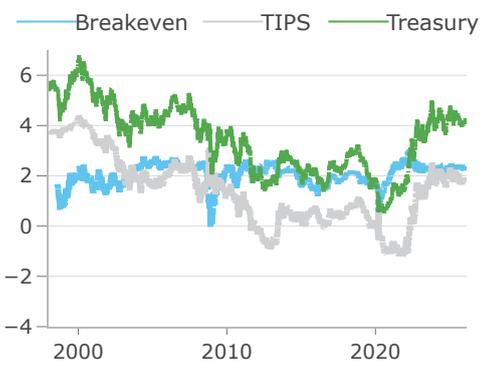
Global 10Y Yields %



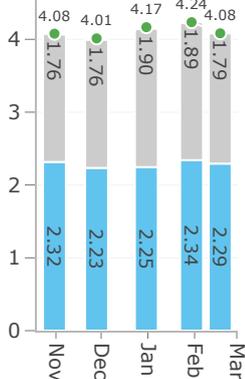
European 10Y Yields %



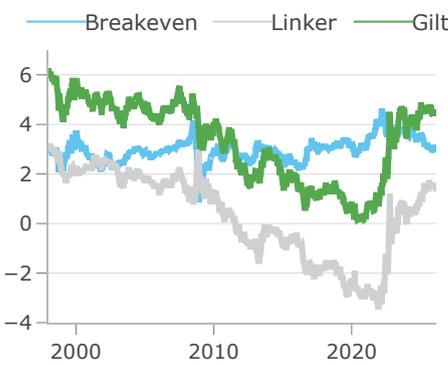
US 10Y Yields Breakdown %



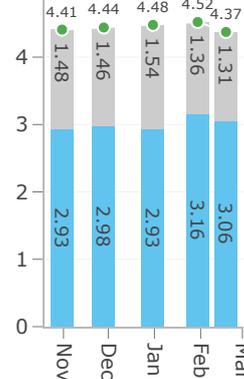
Last 6 Months



UK 10Y Yields Breakdown %



Last 6 Months



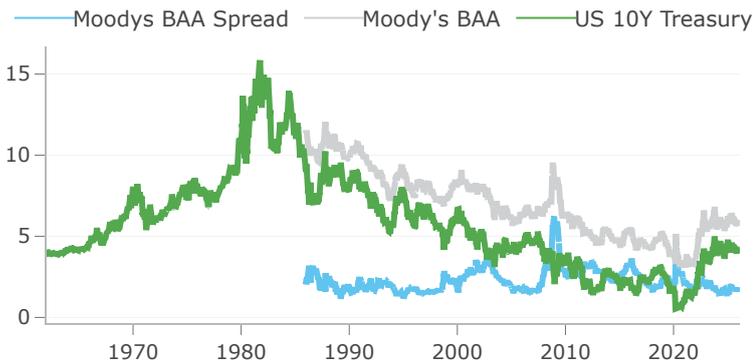
Bonds - Credit

A sharp sell off in US software shares spilled into IG¹ bonds, with sectors such as software, data providers, BDCs¹ and three others² widening about 17bps on average since 22 Jan.³, while their equity counterparts fell 14%. But these sectors make up <3% of the IG market, so the overall impact was limited. Only 5% of the index moved between 5–9bps wider; in comparison to 41% of the index during the Nov. 2025 spike⁴.

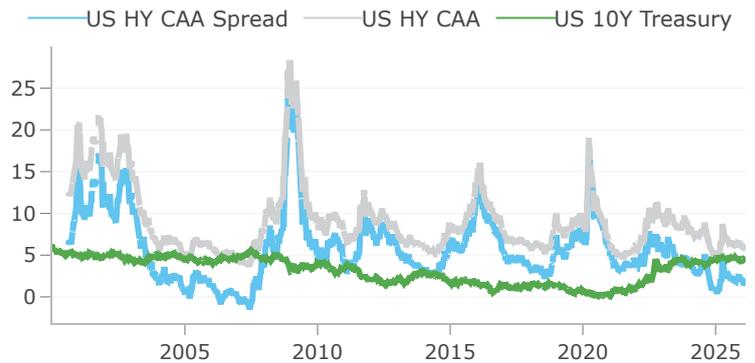
The 2026 backdrop still looks supportive: steady growth, low recession risk and solid company finances. Earnings show resilient revenues and firm margins. The main vulnerability is valuation, especially as net issuance may rise 30% this year on the back of pent-up M&A activity and Hyperscaler's issuance. The latter is already increasing spreads in the CDS market.

Global Credit Yields

US Corporate Investment Grade Yield %



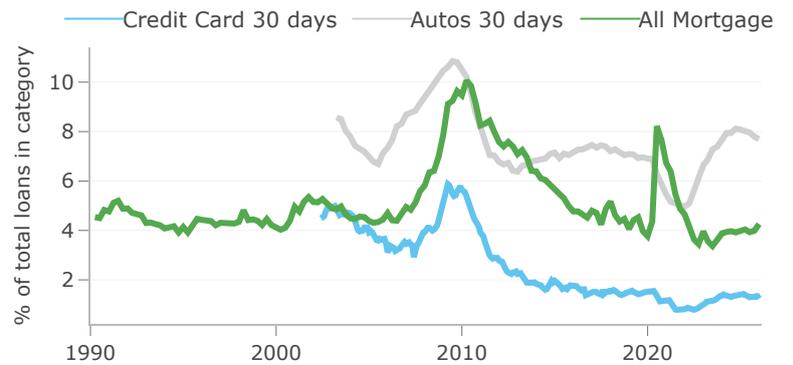
US Corporate Sub-Investment Grade Yield %



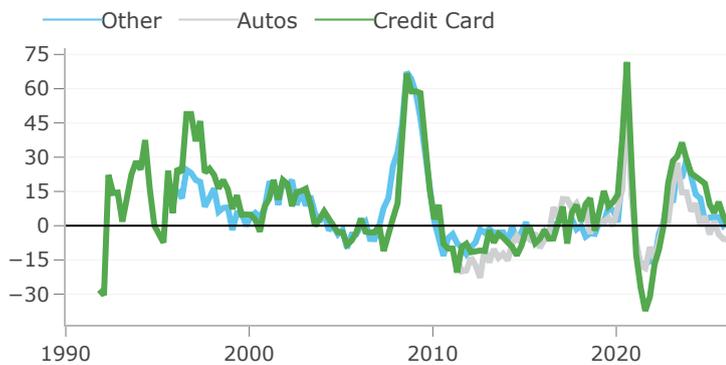
US Tr. vs IBoxx IG and HY Total Return \$ (100= 31 Dec '98)



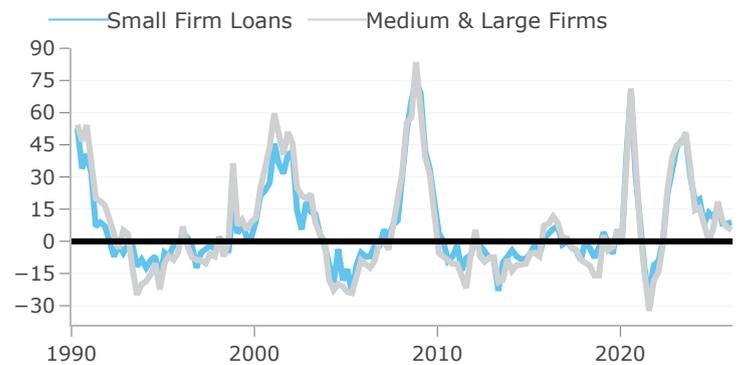
US Delinquencies %



Net % of Banks Tightening Consumers Credit Conditions



Net % of Banks Tightening C&I Credit Conditions



Sources | Federal Reserve, Senior Loans Officers Survey, CCLA, Bloomberg as at Feb 2026. 1: IG: Investment grade, BDC: Business development companies. 2: Insurance brokers, wealth managers, real estate sectors. 3: 22 Jan 2026 to 13 Feb 2026. 4: Bank of America: "IG Credit Strategy": 13 Feb 2026.

Alternatives

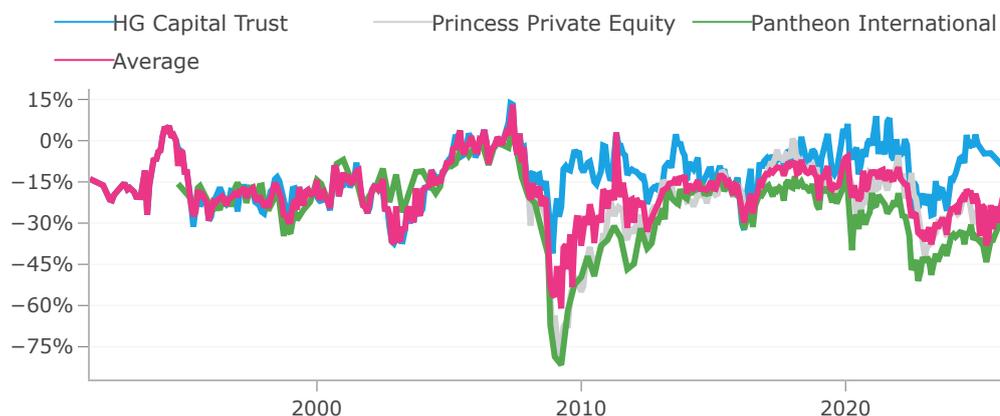
A new class of materials called perovskites is gaining traction in neuromorphic (brain-inspired) chip design. They can “store” information directly on the chip, enabling high-speed, ultra-low-power processing that early tests suggest can outperform conventional GPUs¹. **One study recorded 99.2% accuracy while using just 1.7% of a GPU’s energy!**² **Advancements are being made on the software side too, DeepSeek’s ‘Sparse Attention’ method changes how large models search for answers, cutting compute time by “more than half”³.**

While still early, such an advancement could be a threat to the commodity and energy complex that has been riding the AI infrastructure wave. Think, power companies, uranium, copper, private off-grid energy construction.

Global Valuations

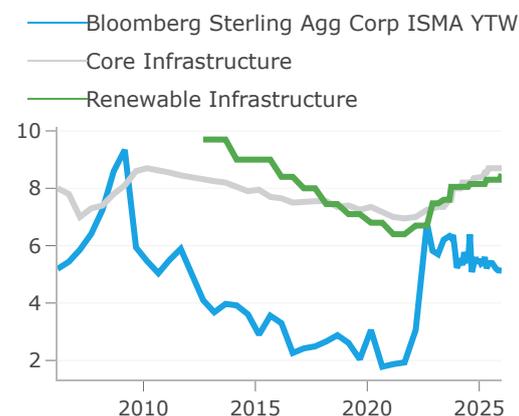
Listed Private Equity

Discount To NAVs



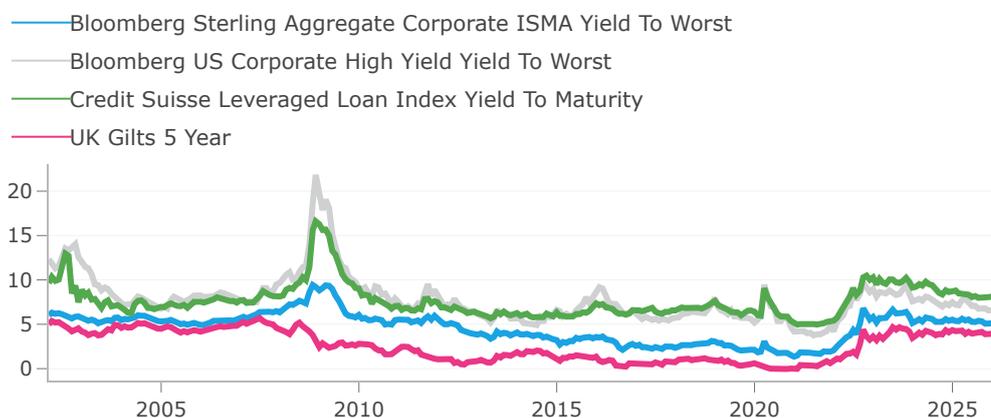
Infrastructure

Infra. Discount Rates vs Bond Yields



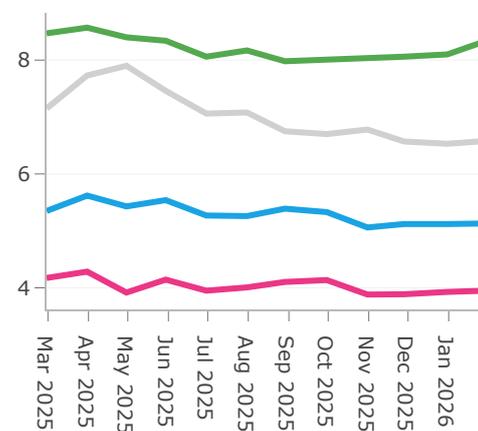
Contractual Income

Income Yields



Last 12 Months

Income Yields



Sources | Infrastructure: CCLA, Bloomberg; Contractual Income: Bloomberg, Pitchbook. Data as of Jan 2026. Listed Private Equity Discount to NAV graph: We have used these three securities to give a broad market representation, data as of Dec 2025 (latest data). 1: Graphical Processing Unit. 2: Wiley Advanced: 'Perovskite Neuromorphic Engine...' 13 July 2025. 3: www.cyberessentials.org 'DepSeek introduces revolutionary v3.2...' 30 Sept 2025.

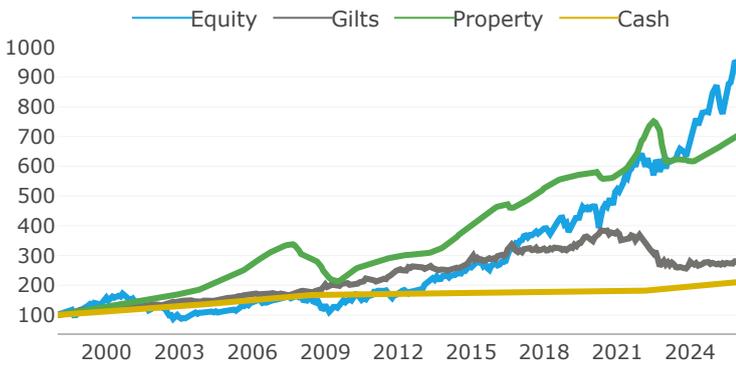
Property

London's prime office market is showing attractive supply-demand dynamics. Vacancies in the City are expected to fall to zero by 2028¹, while demand for top tier space is already ~25% above its nine year average². Yet supply is extremely limited: only 4.75 million sq. ft of new offices are due over the next five years, against 11.2 million sq. ft of leases expiring¹. Assuming normal 20% renewal rates¹, this leaves a large supply gap.

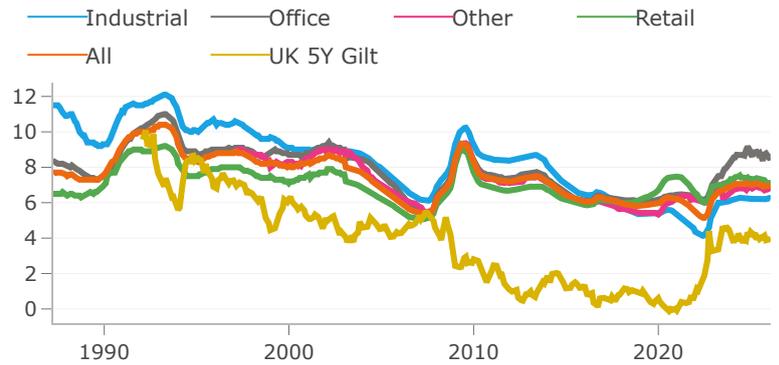
Rents are responding, with some investors achieving 10–15% increases on pre lets². Construction delays since Brexit and Covid have squeezed the pipeline - limiting ESG compliant stock. Plus costly moving and fit-out rates are forcing tenants to stay put and upgrade, further exacerbating the shortages and propping up rents. Similar themes are playing out in prime Paris, Frankfurt and New York markets too.

UK Commercial Property Market

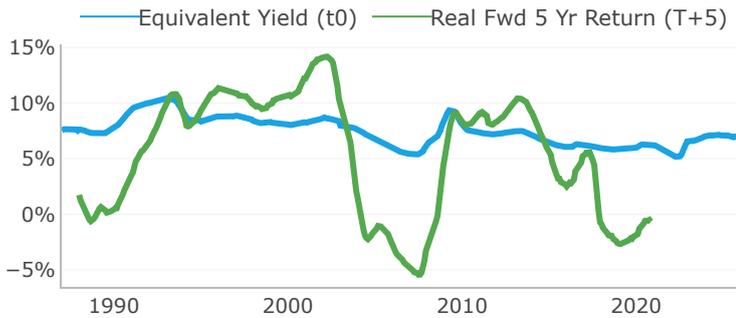
25 Years Of Return 1998=100



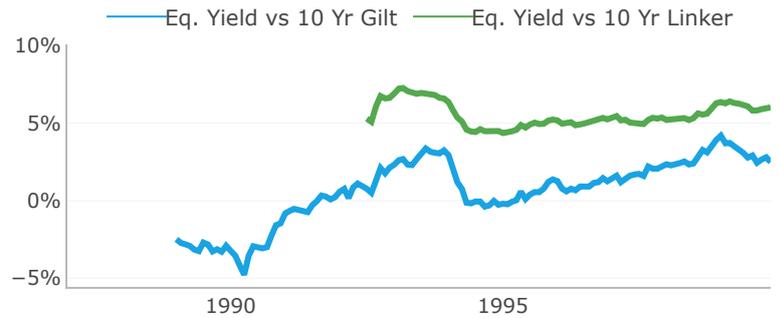
Equivalent Yields vs Gilt Yields %



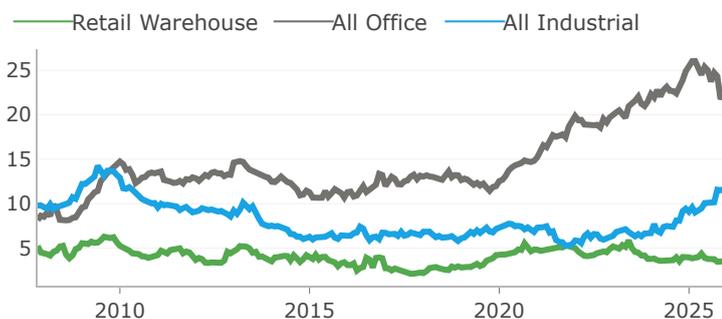
MSCI UK All Property Monthly TR Index %



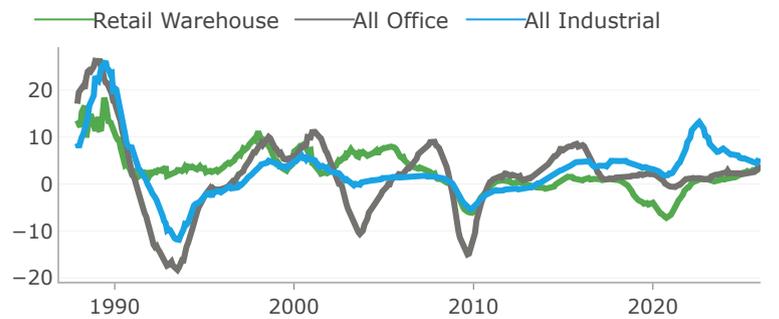
MSCI UK All Property Index - Equivalent Yield Spreads



Vacancy Rate %



Nominal Rental Value YoY Growth %



Sources | Equivalent Yields, Vacancy Rate, and Nominal Rental Value charts: MSCI UK Monthly Property Index as at Jan 2026. 25 Years of Return, All Property Monthly TR Index as at Jan 2026. 1: FT: 'London office shortage...' 6 Jan 26. 2: FT: 'City of London risks running out...' 3 Dec '25.

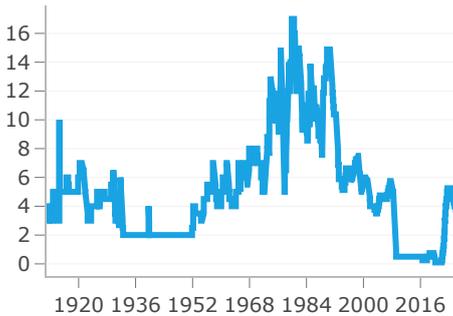
Cash

Chancellor Rachel Reeves is set to benefit from falling debt-interest costs for the first time since taking office in July 2024. Bloomberg Economics expects about £1.5bn in extra fiscal headroom for the March Spring Statement. This follows a 25bp fall in 10-year gilt yields since the November budget.

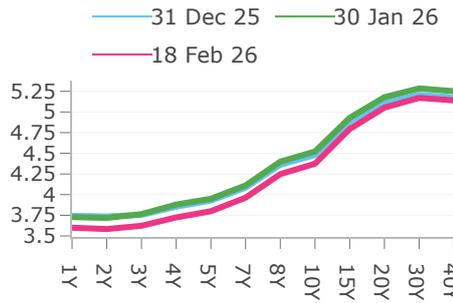
Keeping to her "one budget per year" approach, a key shift this year is that the OBR will no longer assess progress against fiscal rules at Spring Statements. Previously this check allowed up to a 0.5% of GDP deviation without explanation; without it, that flexibility disappears. There is also timing risk: if the OBR uses an earlier forecast window, the fiscal gain could shrink to around £500m.

UK Sterling Market

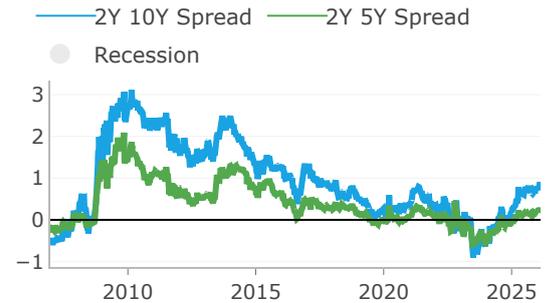
Official Bank Rate



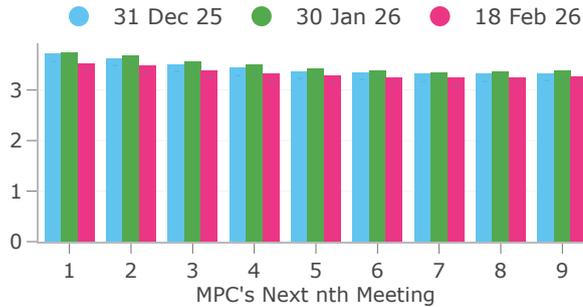
UK Gilt Curve



Gilt Spreads



Rate Expectations For Future MPC Meetings



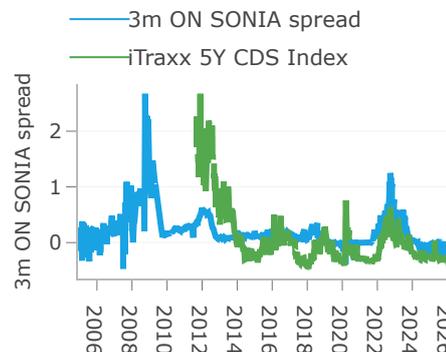
1Y Forward Market Rate Expectations



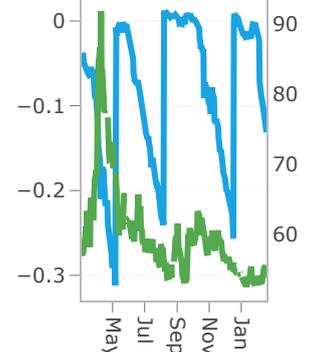
Inflation Readings YoY% | Colour by 10Y Z-Score*

Year	2025			2026
	Oct...	Nov...	Dec...	Jan...
RPI	4.30	3.80	4.20	3.80
CPI	3.60	3.20	3.40	3.00
CPI Core	3.40	3.20	3.20	3.10
CPI Services	4.50	4.40	4.50	4.40
CPI Goods	2.60	2.10	2.20	1.60
Priv. Wages	3.50	3.30	3.50	

Market Stress



Last 12 Months



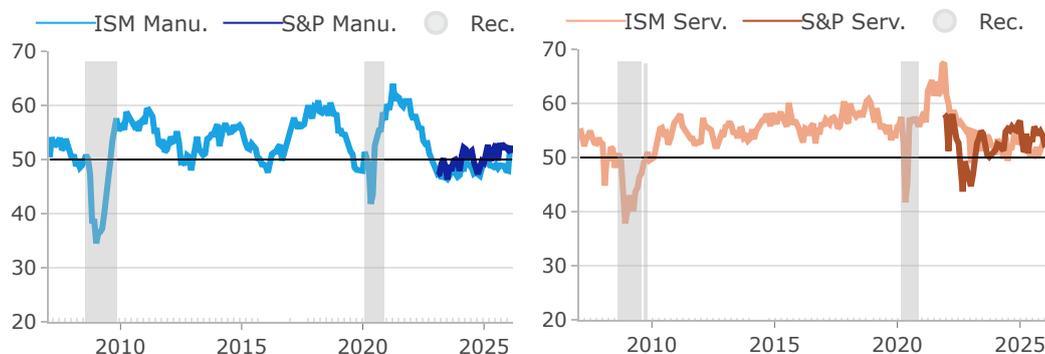
Sources | ITraxx CDS is the Markit iTraxx Europe Senior Financial Index, comprising 30 equally weighted credit default swaps on IG European entities. *10 year z-score applied on each series, coloured using gradient with score of 0 as green, at least +/- 2 standard deviations away scores as red. Bloomberg for all charts, as of Feb 2026.

Global PMIs

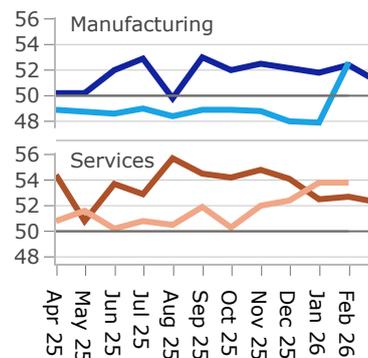
Revisions to US job data show hiring slowed sharply in 2025: only around 180k new jobs were created, averaging 15k a month - well below 2024 (168k a month), 2023 (216k), and 2022 (380k). This aligns with weaker business hiring surveys. The January boost of 130k is also likely to be revised down in time.

But softer demand for new roles isn't the same as job losses. Unemployment fell from 4.4% to 4.3% in January, even as more people looked for work, and layoff rates remain steady at 1.1–1.2%, close to historical norms. **Overall, the labour market still looks resilient. No pressure on the Fed from here (at least for now).**

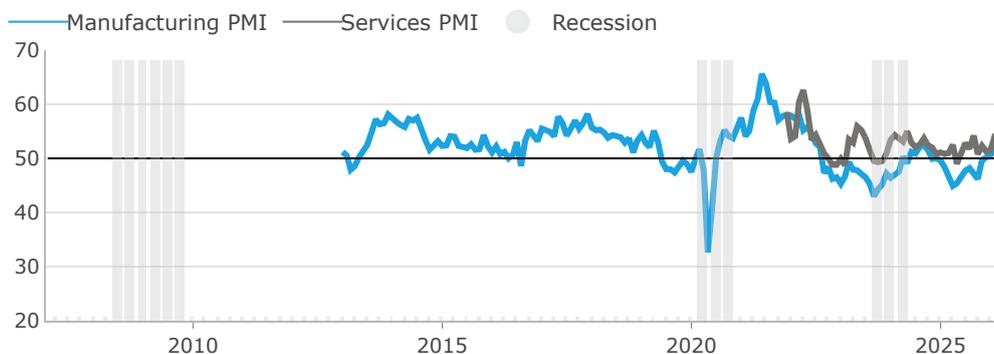
United States



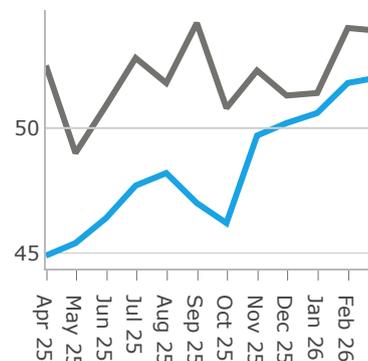
Last 12 Months



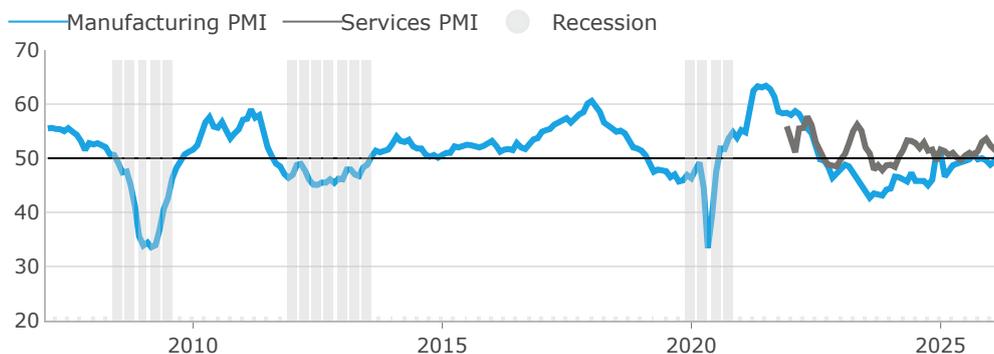
United Kingdom



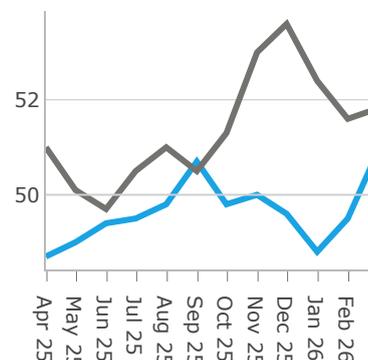
Last 12 Months



Eurozone



Last 12 Months

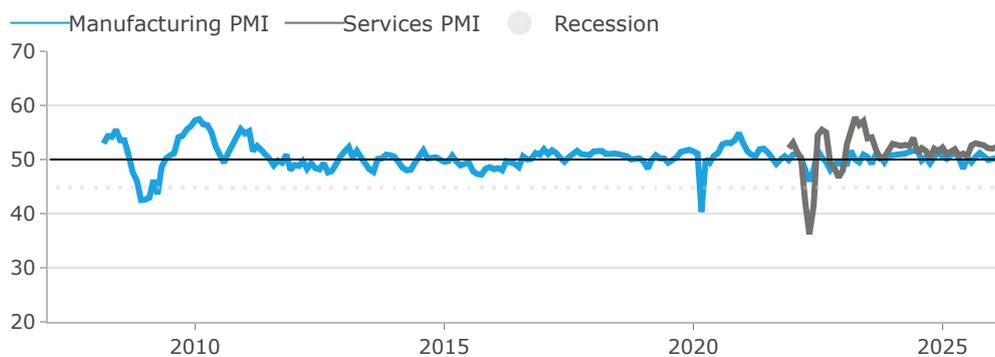


Global PMIs

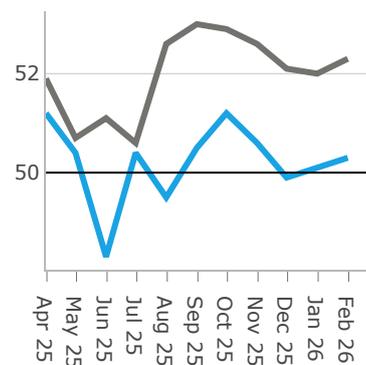
Global activity strengthened in January, with the J.P. Morgan Global Composite PMI rising to 52.5, marking three years of uninterrupted expansion. Services remained the main driver, especially financial services, while manufacturing continued its gradual recovery. Growth leadership shifted toward Australia, the UK and Japan, with India still the strongest emerging market.

New orders improved across most sectors suggesting resilient demand, but not enough to pick up business sentiment. Optimism dipped to a 3 month low on global trade concerns. Unsurprisingly labour demand stayed flat making it 18 months around the 50 mark. Input and output prices still remain above averages.

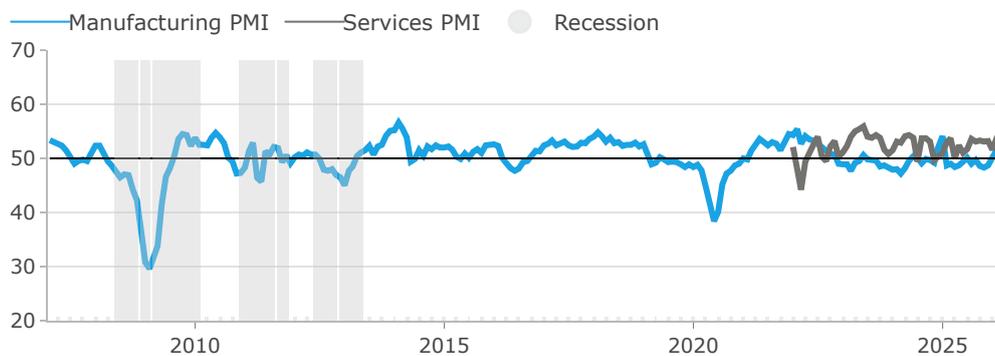
China



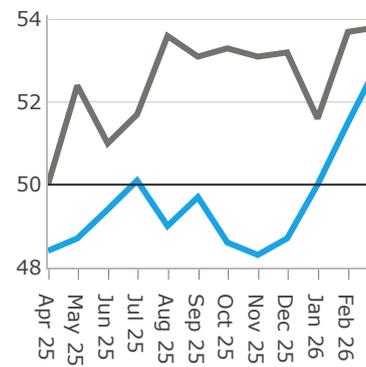
Last 12 Months



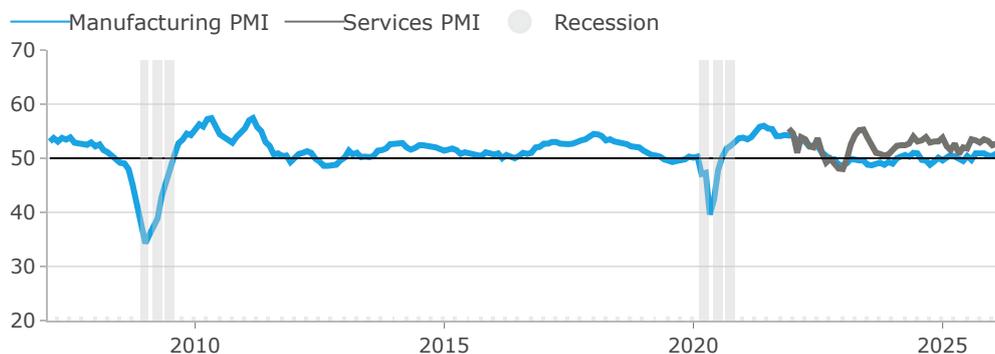
Japan



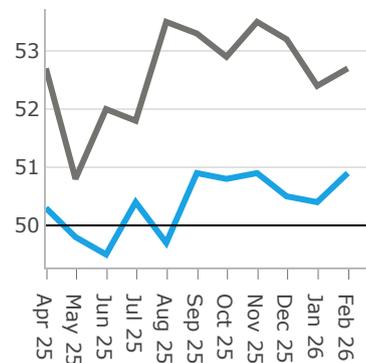
Last 12 Months



Global



Last 12 Months



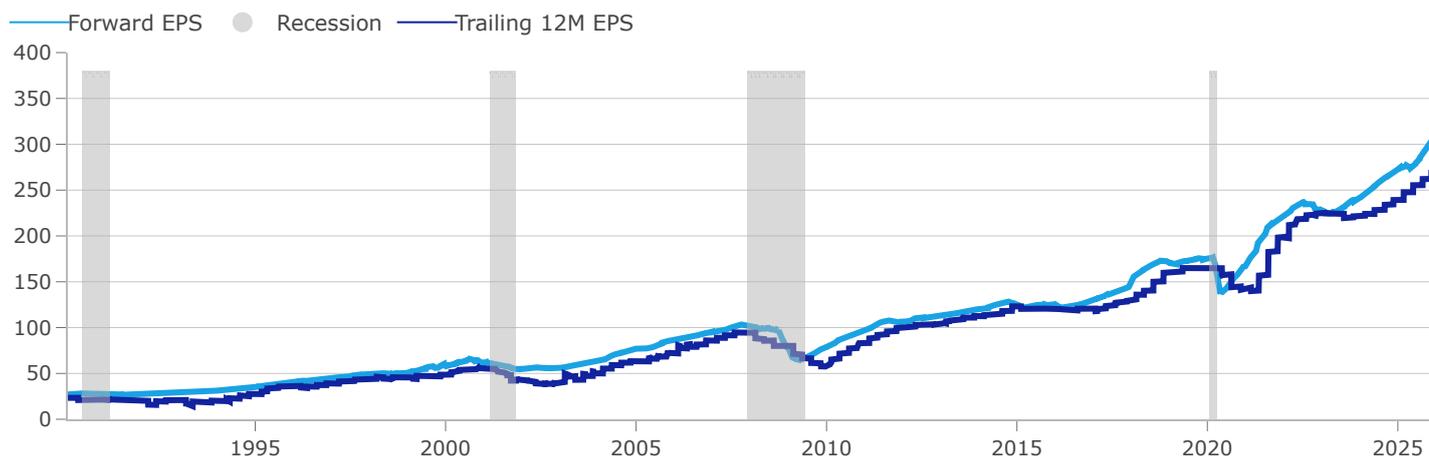
Earnings | USA

While there is plenty of debate about how AI might reshape the future, the recent past continues to show firm momentum. In week 5 of the Q4 2025 earnings season, 67% of companies beat expectations, up from 60% the week before. Analysts now expect 12% year on year earnings growth versus the original 7%. Revisions remain positive and company commentary has been broadly stable, suggesting earnings strength is widening.

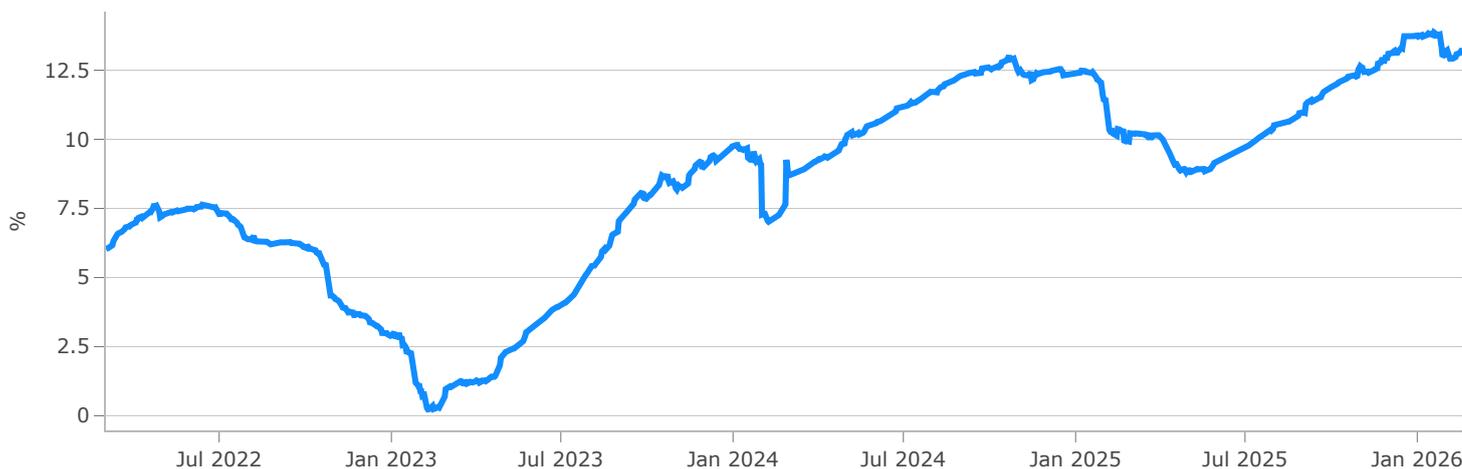
But fragility sits in the background. Capital spending is set to rise 25% year on year, with around 80% of that coming from Hyperscalers and other major tech players. Historically, top-decile capex spenders underperform the market in future years on average. Tariff effects may also weigh, with pre-tariff inventories likely exhausted, some estimates pointing to a potential 6% hit to EBIT if tariffs are fully applied.¹

S&P 500

Bloomberg Est. EPS & 12M Trailing EPS



Rolling Forward EPS Growth Forecasts



Sources | S&P500 12M Forward EPS using Bloomberg BF transformation, 12M Trailing EPS from Bloomberg as at Feb 2026. 1: Data for commentary taken from Bank of America: 'US Equity Strategy: Earnings Tracker Week 5...' 17 Feb 2026.

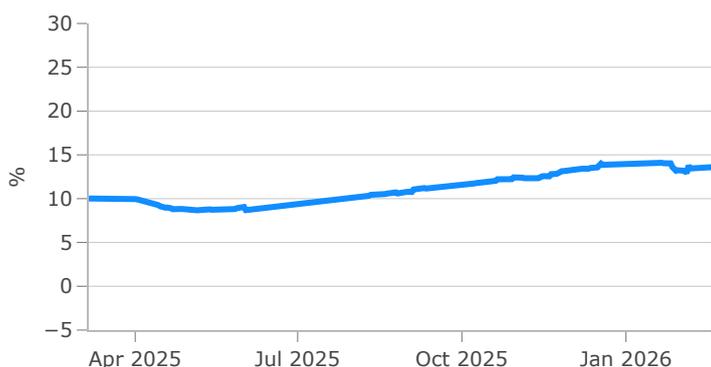
Earnings | Regional

Developed markets have picked up their blended forecasted 12M forward Earning Per Share (EPS) growth rates. USA is now ~15%, above last January's peak. Europe (ex UK) and UK are following a similar pattern around ~10% respectively.

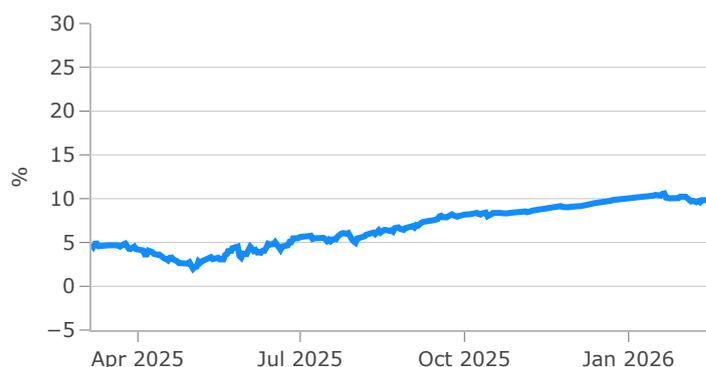
Emerging Markets continue to outpace other regions with an EPS growth rate above 25% - beating last year's peak.

Regional Rolling 12M Blended Forward Earnings Growth

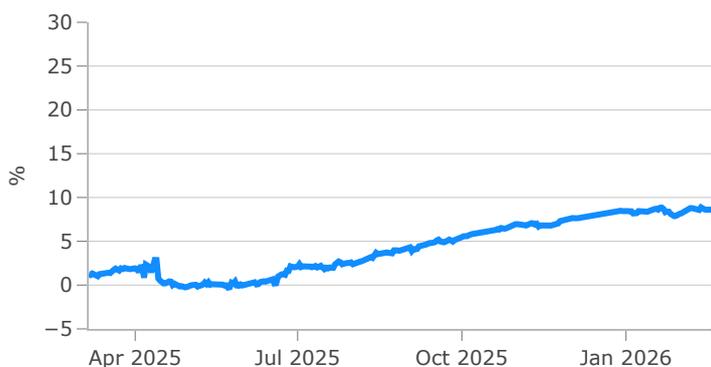
MSCI USA



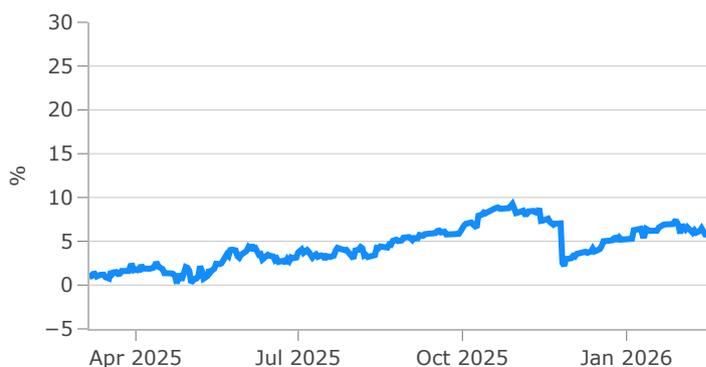
MSCI EU ex UK



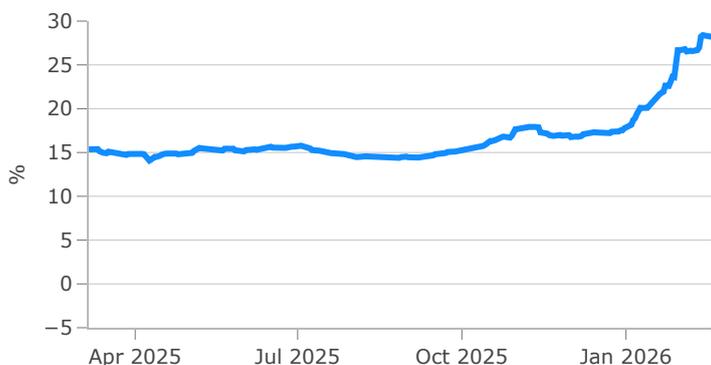
MSCI United Kingdom



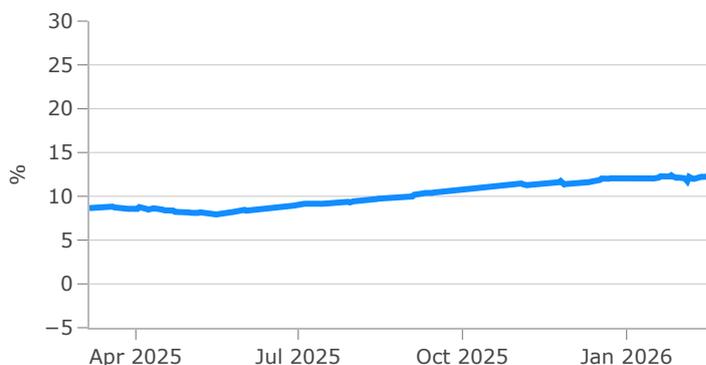
MSCI Japan



MSCI Emerging Markets



MSCI World

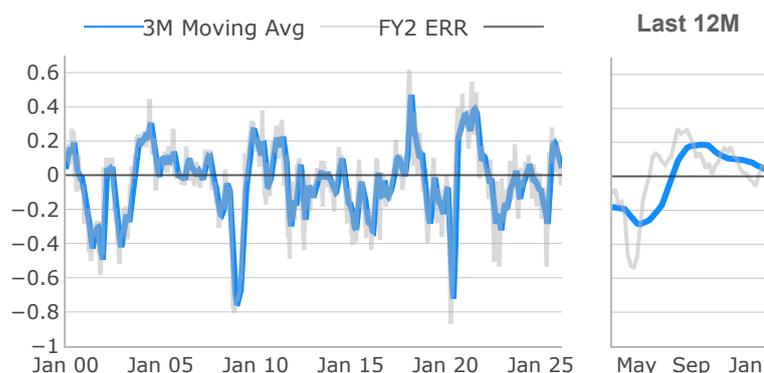


Earnings Revisions

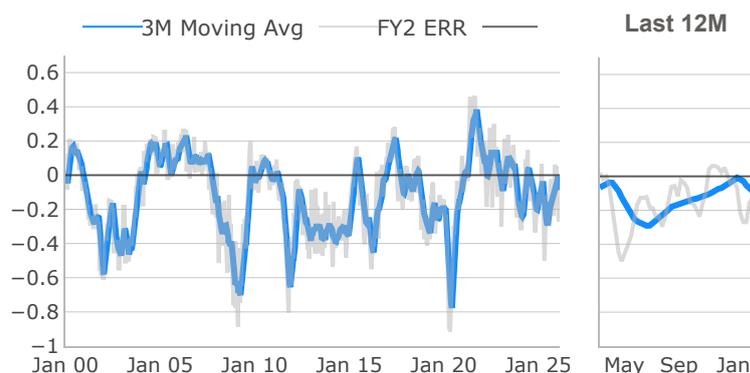
These charts show the breadth of earnings revisions, i.e. # upgrades minus # downgrades / total estimates, so it is a directional measure showing how widespread upgrades or downgrades are. Historically, troughs in revisions breadth have been favourable times to add risk.

Global Earnings Revisions Ratios

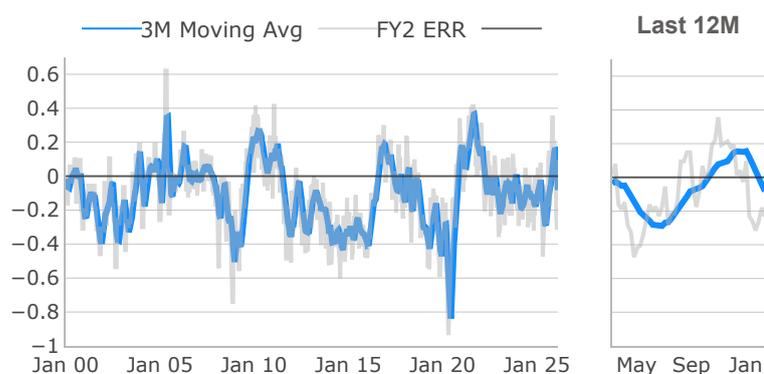
USA



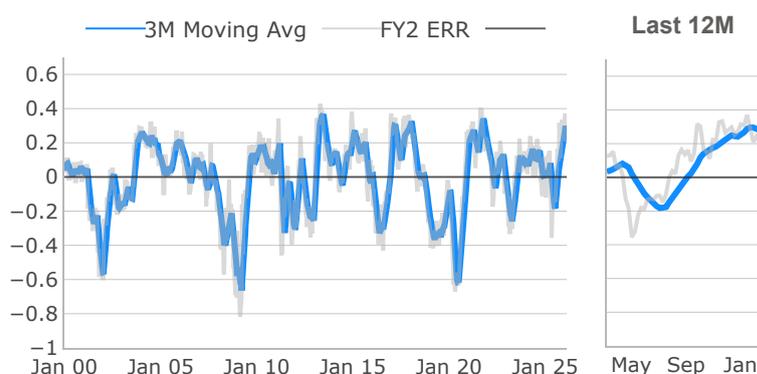
Eurozone



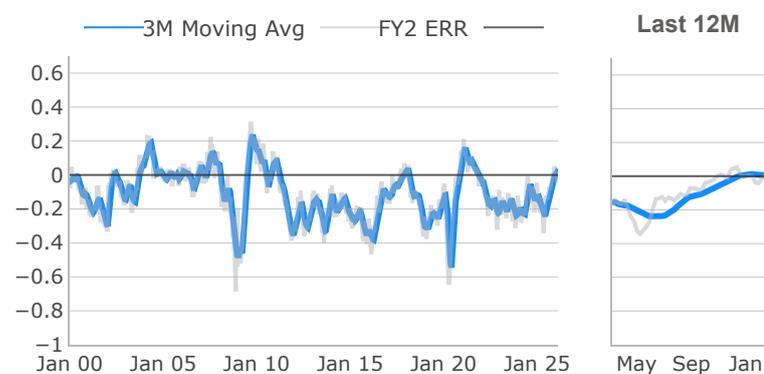
UK



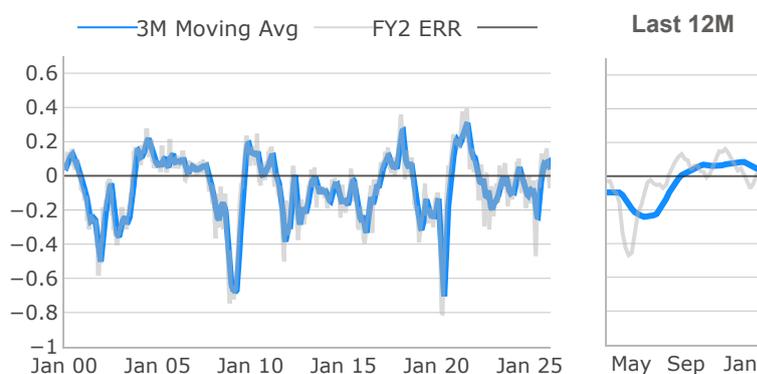
Japan



Emerging Markets



World

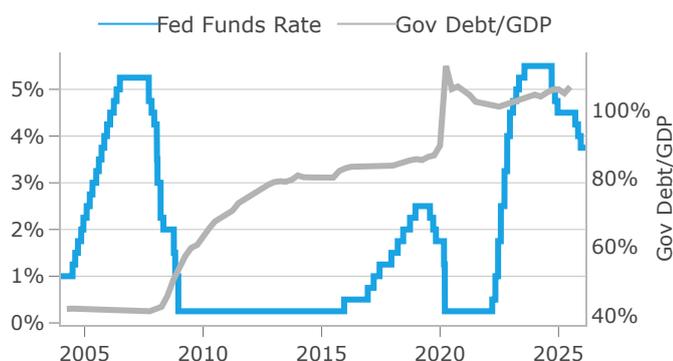


Policy

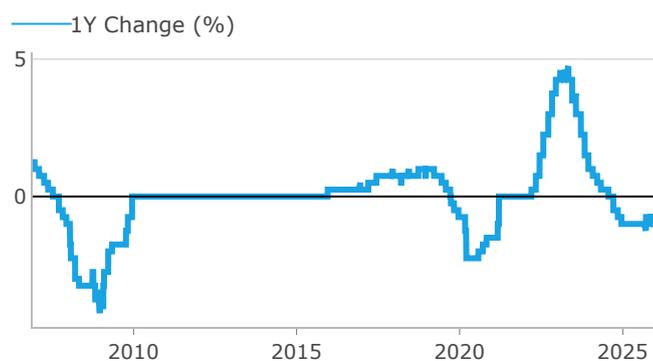
Kevin Warsh was nominated by President Trump on 30 January to become the next Chair of the US Federal Reserve. His confirmation is still pending, but his policy signals already matter. Warsh has argued that AI-driven productivity could help lower inflation. This alongside a smaller Fed balance sheet and lighter bank regulation, he sees as creating room for interest-rate cuts.

At the same time, he has called for fewer market backstops and less public guidance - an approach that could mean tighter liquidity and a reduced safety net for markets. He also favours closer alignment with the US Treasury. **The immediate market reaction was notable: the dollar² rose (0.9%, highest since May '25), the US bond curve bear steepened¹ as investors priced in cuts, and gold and silver fell sharply (~6% and 25% respectively).**

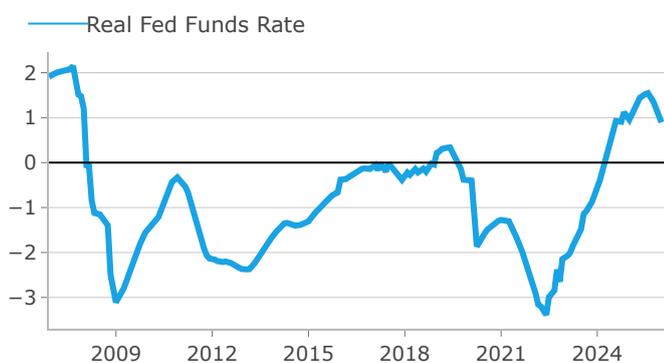
Fed Funds Rate



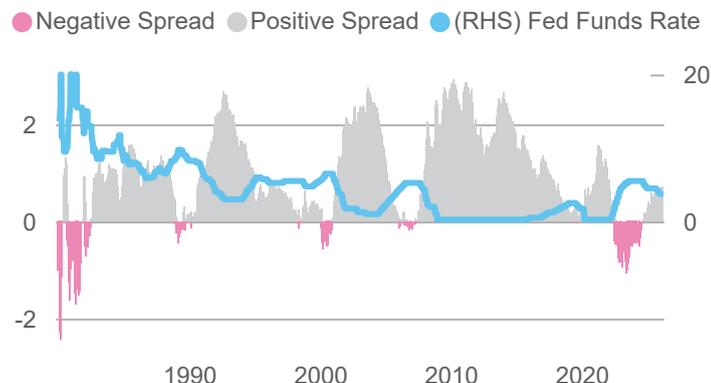
Change in Fed Funds Rate



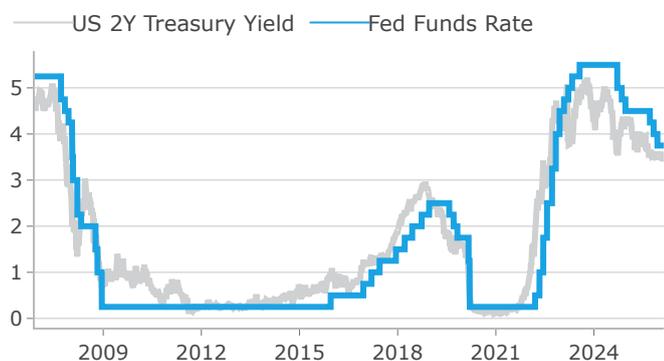
Real Fed Funds Rate (Using 2Y MA CPI)



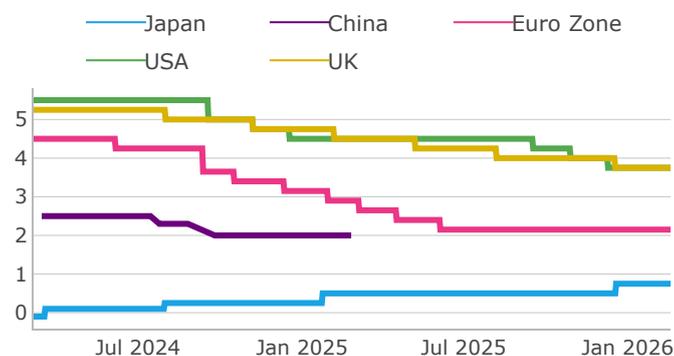
Fed Funds Rate vs 2s10s Curve



Fed Funds Rate vs 2Y Treasury



Global Comparison



Sources | Bloomberg for all charts, as of Jan 2026. 1: Greenland-Iceland-UK Gap: a geographical chokehold separating the Atlantic from Europe. 1: Bear steepened: when the the long-end yields move more than the short-end yield, thus widening their gap. 2: Dollar Index (DXY)

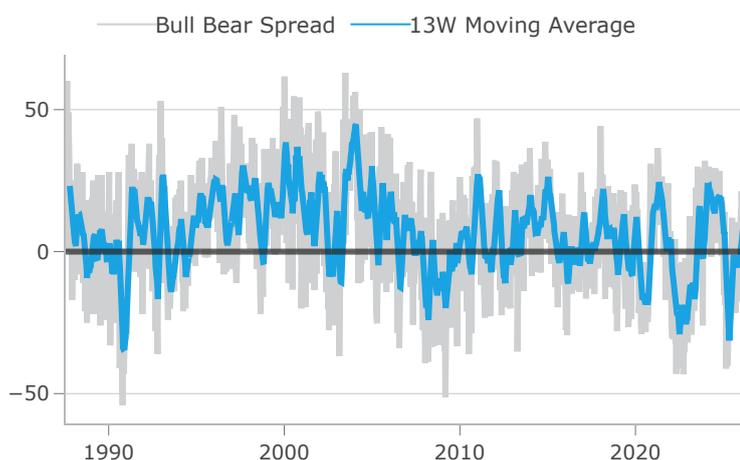
Sentiment

The Bank of America “Bull & Bear” Indicator has risen to 9.4, which is very close to its maximum reading. This suggests investors are extremely optimistic. Historically, when the indicator reaches these levels, markets have sometimes struggled afterwards.

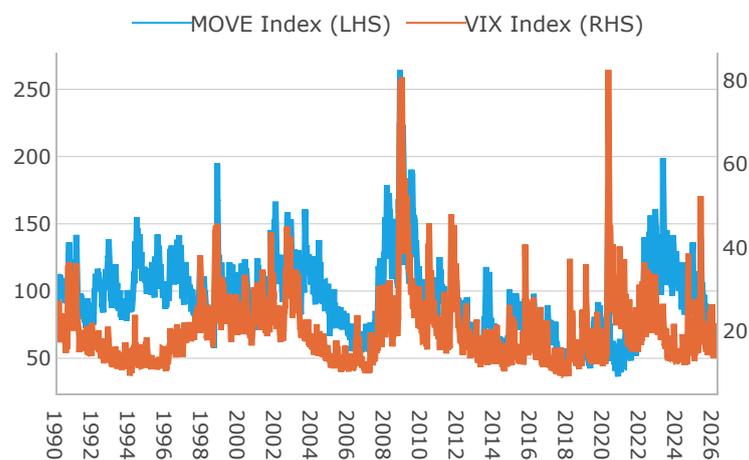
The latest move reflects strong positive sentiment across areas such as hedge fund positioning, money flowing into shares and bonds, and overall credit market conditions.

US Equity Indicators

AAll Bull Bear Spread



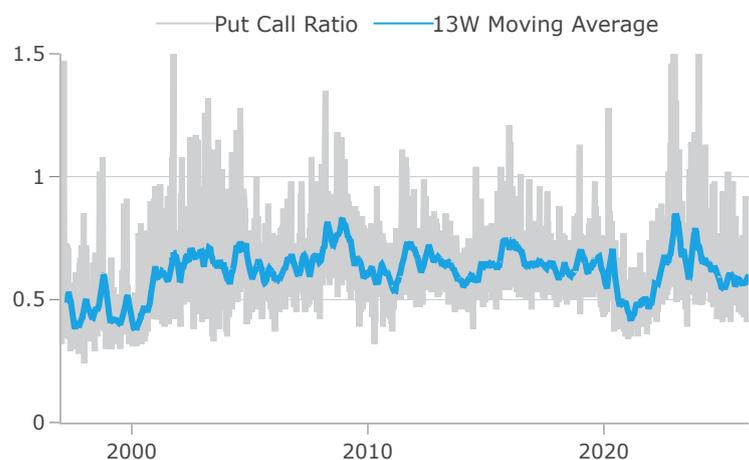
Equity vs. Bond Sentiment



Michael Hartnett's Bull & Bear Indicator (BAML)



Equity Put Call Ratio

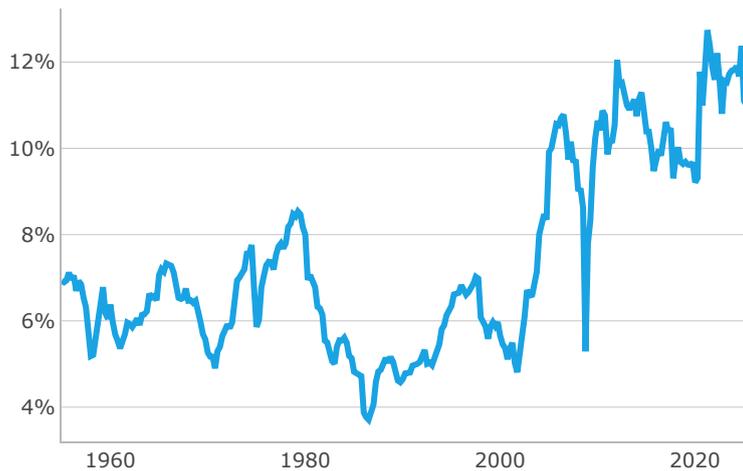


The Big Picture

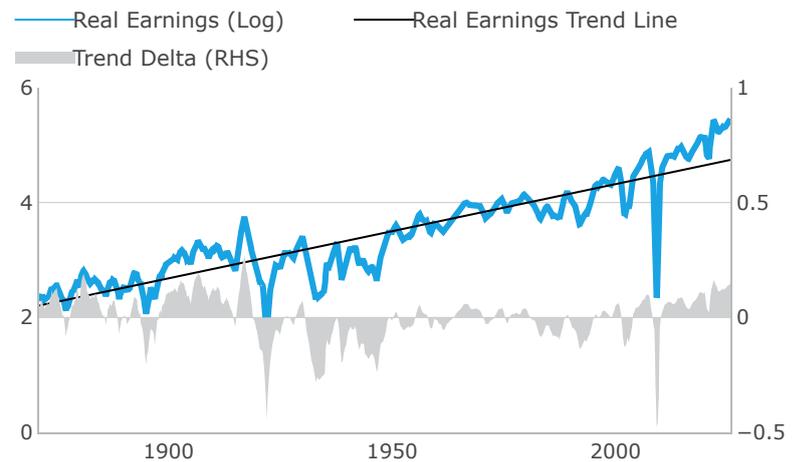
Here we highlight some longer-term imbalances that, **should** they correct, would have an outsized impact on risk asset returns. We don't make predictions but we do watch these. US corporate profit is just off the highest share of GDP that it has ever been since 1929. Its corollary (not shown) is that the wage share is at the lowest level it has been in almost as long. Allied to this, the top right chart shows that earnings are as far above their long run trend in absolute terms as they have also been since 1929. Domestic non-financial debt is also extremely elevated. All of this suggests that if old relationships hold and we get mean reversion, US forward 10 year returns could be much lower than suggested by the ERPs.

Long Term Imbalances

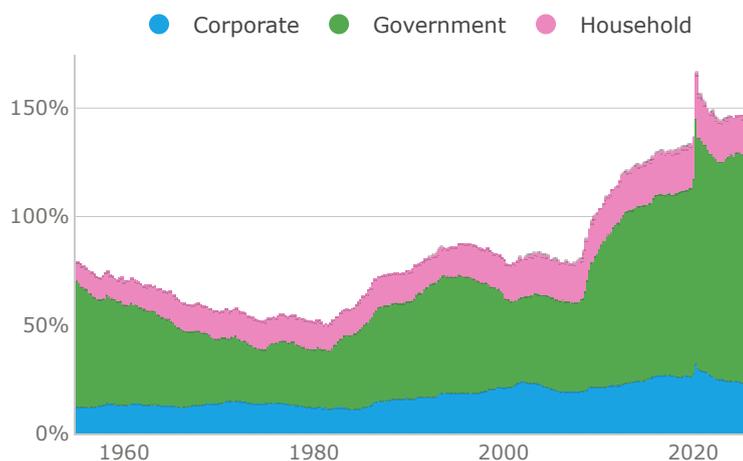
Profit Share of GDP



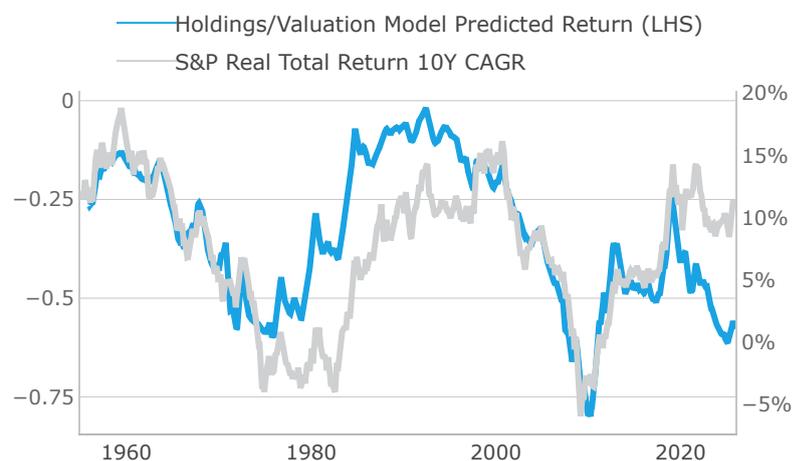
Earnings Deviation From Trend



Non Financial Debt as Share of GDP



S&P 500 10Y Forward Returns



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