

KENSINGTON MONTHLY COMMENTARY

February 2026

(As of 2/28/2026)



Editor's note: Subsequent to month-end, geopolitical tensions in the Middle East escalated materially and have become an important driver of market sentiment. We will address those developments more fully in the March commentary.

Equity Markets

February was a month of narrow index performance but much broader underlying movement. The cap-weighted S&P 500 slipped modestly, while the S&P 500 Equal-Weighted Index, small-caps stocks, and international equities posted stronger gains. In other words, headline index returns understated the amount of rotation taking place beneath the surface. The S&P 500 fell 0.87% in February, while the S&P 500 Equal Weight Index rose 3.4%. The Russell 2000 gained 0.71%, and developed and emerging-markets international equities also advanced solidly.

A clear theme this month was improving market breadth. Recent years have been dominated by a relatively small group of mega-cap stocks, but February looked different. Market leadership broadened, sector rotation intensified, and stock-specific outcomes mattered more than the index itself. Environments with greater dispersion between stronger and weaker performers often result in more varied market outcomes, which can affect the opportunity set for active strategies.

A second theme was continued pressure on parts of the software universe as investors reassessed how artificial intelligence may affect long-term business models. The market appears to be asking a reasonable question: if AI lowers the cost of building software and reduces switching friction over time, should some of the sector's historical valuation premiums come down? That does not mean established platforms are doomed. Many may still benefit from scale, embedded workflows, and proprietary customer data. It suggests that investors are becoming more selective and less willing to assign peak multiples based only on growth expectations.

We also continue to watch the private credit space closely. Private credit has attracted enormous capital in recent years, helped by higher yields, low reported volatility, and the perception of diversification benefits. But a portion of that return profile has been supported by leverage, illiquidity, and valuation smoothing. As underlying credit stress rises, those structural features matter more. As of March 6, 2026, Fitch reported that the default rate in its US private market-rated portfolio rose to 9.2% in 2025, up from 8.1% in 2024. That does not necessarily signal systemic stress, but it does underscore that limited price discovery should not be mistaken for limited risk.

Fixed Income

Bonds turned in a strong performance in February with longer-term Treasury and high-grade corporate yields falling significantly. The 30-year Treasury gained 4.55%, the 10-year Treasury advanced 2.77% and the Bloomberg US Investment Grade Index was up 1.29%. Mortgage-backs gained 1.67% while the more credit-sensitive High Yield Index lagged, up 0.19%.

Economic data added to that tone. The second estimate of fourth quarter 2025 GDP was revised lower, though one of the cleaner underlying demand measures, real final sales to private domestic purchasers, still increased at a 1.9% annualized rate. That combination supports a view we have held for some time: the economy is slowing from above-trend levels, but private sector demand has not collapsed.

The labor market is also looking softer at the margin, particularly on the hiring side. Job Openings and Labor Turnover Survey showed January job openings at 6.9 million (3/13/2026), while ADP reported only 22,000 private payroll additions in January, with professional and business services down 57,000 (2/4/2026). We would characterize this as a lower-hiring, lower-firing environment. Businesses do not appear to be cutting aggressively, but they are clearly more cautious about adding staff.

Federal Reserve and Policy

The Federal Reserve did little in February to change the market's baseline view. At its January meeting, the FOMC said economic activity had been expanding at a solid pace, job gains had remained low, and inflation was still somewhat elevated. Chair Powell also said policy was "well positioned" after the prior rate cuts, reinforcing the idea that the Fed is in little hurry to move again until the data becomes more decisive.

Attention also shifted toward the future leadership of the Fed after the White House formally sent Kevin Warsh's nomination to the Senate on March 4. Markets are still working through what a Warsh-led Fed might mean in practice, but the broad takeaway is straightforward: the debate is no longer only about how much to cut rates, but also about how monetary policy, balance sheet policy, and productivity trends may interact over the next cycle.

Closing Thought

February was a useful reminder that flat headline returns can mask meaningful change underneath the surface. Equity market leadership broadened, labor demand continued to cool, and investors became more discerning about both technology valuations and private market risk. For investors, the bigger story was the shift happening beneath the calm surface of the index.

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