



Market Update

While the stock market remains near all-time highs, 2026 began with significant volatility and several new and unexpected narratives. Stocks look to continue the three-year rally, though perhaps with different parts of the market leading the way. Bonds have barely budged, a stark contrast to the volatility elsewhere. That's even more surprising considering that Trump revealed the name of the next Federal Reserve Chairman! Finally, commodities and crypto have seen outsized moves. Gold and silver exploded higher, then fell dramatically. Meanwhile bitcoin is trading at half the price of just four months ago.

The most heavily anticipated financial news to start the year were the Supreme Court's ruling on tariffs and President Trump's final choice for Federal Reserve Chairman to replace Jay Powell. The Supreme Court has not yet made a ruling, with the next possible date coming later this month. Investors wait with bated breath, but there remains no update here. Prediction markets still put a 35% probability of the Court ruling in favor of Trump. But the devil will be in the details – specifically whether the government issues refunds, and how Trump reinstates the tariffs.

The financial markets adaptation of "The Apprentice" finally came to an end as Trump announced that Kevin Warsh would be his nominee to lead the Federal Reserve starting in May. Warsh has experience serving on the Fed, including during the Great Financial Crisis when he was instrumental in helping Bernanke work with the major banks. Investors are satisfied with the choice. Trump has been seeking a nominee who will advocate for lower rates, potentially risking a rise in inflation. Undoubtedly Warsh currently has that outlook. But it's worthwhile to note that in 2008 Warsh was particularly concerned with the risk of inflation – an opinion that that turned out to be wrong, and which was nearly twenty years ago, but which nevertheless demonstrates ideological flexibility and heterodox thinking. Warsh was also critical of quantitative easing (QE) at the time. These were asset purchases by the Fed to stimulate the economy, but which led to the massive expansion of the Fed's balance sheet in a manner that's proven difficult to unwind. It's likely that the Federal Reserve's interest rate decisions will feature more dissenting votes going forward. So even if Warsh wants to cut interest rates no matter what, he'll still need to convince six other voters to go along with that decision.

The US Dollar weakened substantially in the second half of January. There was no obvious driver of the weakness, but rather several headwinds that accumulated in a fall of roughly 4%. It was driven partially by Federal Reserve interest rate cut expectations. Investors continue to monitor the deficit and government spending. Finally, geopolitical tensions have been elevated with threats of tariffs and annexation of Greenland. Commodities – gold and silver most notably – were extremely volatile near the end of January, partially driven by USD weakness and partially by a frenzy of momentum buying. It continues to be the most volatile commodities market action in modern history. The bubbly upward momentum in commodity prices ended on the day Kevin Warsh was nominated. It's possible that markets were anticipating the nomination of someone else – perhaps

someone with less credibility in the eyes of the market. Prices are still very elevated and volatile but appear to have made a “top” for now. That’s reassuring, as continued rising prices would be an ominous warning about inflation. Interestingly, the price of bitcoin has gone in the opposite direction this year and has been cut in half since its peak in October.

Artificial Intelligence headlines continue to drive major moves in the market. They continue to be a huge piece of major indexes. We recently described how the “Magnificent 7” have stopped trading in a majorly correlated manner with each other. This makes sense – the major AI providers compete directly with each other. And the major semiconductor company is able to charge sky-high prices to the other companies. At some point the gains from one company come at the expense of the others. This change happened around September, when Gemini overtook ChatGPT as the de facto premier AI model.

In early February a private AI company named Anthropic sent parts of the market reeling when they released an impressive legal tool. The tool itself wasn’t the issue, but rather the ease with which it was created. Software-as-a-service (SaaS) has been a profitable business model for years with very consistent cash flows. To get these cash flows, the companies sell or license a product, then charge monthly or annual fees to use it. Anthropic showed the ease with which their AI could duplicate this sort of workflow. We are probably at least a few years away from AI-enabled workflows becoming commonplace, but the market feverishly took note of this development. Software stocks were most impacted, with many falling 20% or more. More worryingly (or encouragingly, depending on your outlook) this headline continues the drumbeat of AI becoming ever-more-capable of duplicating a large amount of white collar work at a fraction of the cost. The productivity gains have the potential to be enormous, as will the change to the employment landscape. The major AI trade narrative now is determining which companies will benefit from the technology, and which ones it poses an existential risk to.

Private credit and private equity were also impacted by the AI development. Private credit has a large exposure to technology companies of different types. Undoubtedly some of these companies will be negatively affected by the new capabilities of AI. Some of them will also be positively affected, but the unfortunate aspect about lending money is that your upside is capped at “getting your money back” while the downside is “not getting any money back at all.” Private equity is known to have large exposure to SaaS companies. Established businesses with entrenched customers and consistent cash flows are very attractive for private equity. It’s easy to be confident when borrowing money to buy them. But with the recent developments in AI, we can’t assume that the consistent cash flows at high margins will be there forever. The businesses won’t go away overnight. But there’s now a menacing threat on the horizon, though whether it’s three, five, or ten years away is uncertain. Business development companies (BDCs) – a good proxy for private credit generally – and managers of private equity funds have traded broadly lower as a result.

Equity markets have been generally strong to start the year, with the S&P 500 near all-time highs and overall volatility muted. But if you look under the surface, there is tremendous volatility in individual stocks and sectors. There seems to be a major rotation happening, out of the Magnificent 7 and into small companies, value companies, and companies that are part of the “physical economy” such as industrials, energy, financials, and utilities. International stocks with their low valuations have also benefited, as well as from the falling value of the dollar.

As snow finally melts from the Chicago streets, we hope you’re enjoying the last weeks of winter. We’ll be in touch with our regular quarterly newsletter in April.

Best regards,



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