



A Healthier Kind of Volatility

Shifting Sentiment Beneath the Surface

January has marked a subtle but important shift in markets, both in investment leadership and in the geopolitical backdrop. While geopolitical tensions have been present for some time, markets have largely taken them in stride. What has changed more quietly is investor sentiment.

Surveys show a gradual erosion in bullishness. Managers remain overweight equities, but with less conviction. Investors are still positioned for positive returns into 2026, yet increasingly cautious. The result is a market that remains invested but with less enthusiasm.

This backdrop helps explain the continued interest in alternatives such as commodities, precious metals, and hedge funds. These are increasingly being used to manage risk rather than as outright return drivers.

Markets Reacting More Appropriately to Risk

Recent equity market weakness, including the largest single-day decline since Liberation Day 2025, suggests markets may be starting to react more appropriately to geopolitical developments. While short-term volatility is uncomfortable, it reflects a more mature market response to macro risks.

Rather than ignoring uncertainty, investors are beginning to reprice it. This is an essential characteristic of a functioning market and helps reduce the risk of excessive complacency.

Geopolitics and Policy Uncertainty

Geopolitical risk remains elevated. President Trump's renewed focus on trade policy, including the threat of tariffs against NATO allies, has added to uncertainty and drawn criticism both internationally and within his own party. The use of tariffs as a political tool is emerging as a defining theme for 2026.

At the same time, continued pressure on the Federal Reserve to cut interest rates has raised questions around monetary policy independence. With no successor yet announced for the Federal Reserve Chair, markets are left to speculate on the direction of future policy.

A Rotation Away from Concentration Risk

These developments have contributed to a renewed rotation out of US equities and into international markets, a trend that first began to emerge in late 2025. Notably, this has not been accompanied by a strengthening US dollar, which would normally be expected in periods of heightened uncertainty.

Part of this shift reflects growing scepticism around the narrow nature of the AI-driven rally. A small number of mega-cap stocks have dominated US equity returns, leaving the broader market increasingly vulnerable to even modest underperformance from these names.

Value and Smaller Companies Regaining Attention

Beneath the surface, investor capital has been rotating into more traditional value sectors such as materials, energy, and consumer staples. With markets now pricing limited scope for US rate cuts in 2026, these areas are well suited to an environment of steady interest rates, persistent inflation above target, and ongoing economic growth.

This rotation is also evident in rising interest in US small and mid-cap stocks, which continue to trade at a significant discount to large caps. Improving earnings momentum is helping to close this valuation gap. Similarly, the S&P 500 equal weight index has begun to outperform, reflecting reduced concentration and greater exposure to value-oriented sectors.

What This Means for Portfolios

Taken together, these trends point to a healthier market structure. Capital is rotating away from richly

valued and highly concentrated areas towards segments that have lagged in recent years. Provided economic growth remains intact, this shift could support a more balanced and sustainable market environment into 2026.

Importantly, this is a hallmark of a properly functioning, cyclical market. Value discovery is returning, replacing the indiscriminate concentration seen in recent years.

TAM Positioning

Against this backdrop, TAM has focused on identifying high-quality managers in both US and global small-cap equities, alongside deep research into global value strategies. This positions us well to tilt further towards these areas should current trends persist.

For advisers and their clients, this environment remains constructive for globally diversified portfolios that are less reliant on a narrow group of AI-driven technology and consumer discretionary stocks.

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