



Weekly Update

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- The narratives are changing every day
- IS AI going to kill software or kill all white-collar jobs (some and no)
- OpenAI is cutting its capex but boosting its revenues (forecast)
- Nvidia earnings are great and nobody cares
- Is good economic news now bad?
- Karaoke killing the freight logistics industry?
- Headline Vol is still subdued compared to the moves under the surface
- Companies have started adopting AI, but the growth from here is expected to slow (?)
- The Fed is becoming a little more torn (but it does not matter until June anyway)
- Revenues are beating expectations and accelerating
- Inflation metrics are contrasting, but the market is getting behind the disinflation trend
- 4Q GDP disappoints (blame the govt shutdown)
- Business surveys are ok but slipping
- But Business Spending is still growing
- Quick Hits
- Where did all the crypto money go?
- Chart Crime of the week
- Positioning

	Last	5d %	YTD %	1yr %
S&P 500	6,909	0.7%	0.9%	16.0%
QQQ	\$609.24	1.0%	-0.8%	18.4%
US 10 YR	4.01%	4.08%	4.17%	4.27%
USD/DXY	97.8	97.9	98.3	107.2
VIX	18.7%	20.2%	15.0%	21.1%
Oil	\$65.42	-1.5%	13.6%	-5.0%

*10yr, DXY, and VIX are levels not changes

** Oil is front month futures, beware

The only thing certain in this market is that the narrative will change every single day. This financial bipolarity largely stems from the swings in Artificial Intelligence. One day, Anthropic's coding capability is going to render every software company useless (and profitless). The catch phrases are "questioning the durability of the model" and "what is the terminal value?" Some days this is considered a boon for the AI infrastructure stocks

(semiconductors, memory chips, data center buildout including energy, utilities, and industrials). Other days, this revolution in coding and business efficiency is somehow going to eliminate “every white-collar job in 12-18 months” (paraphrasing the head of Microsoft’s head of AI...yes, he is biased). A random research boutique that lives in the Twitterverse even scared the market when it published its worst-case scenario for the future (massive unemployment and a collapse in consumer spending with blah blah blah). While there is plenty of noise around the future viability of OpenAI (including from us), the private company continues to have deep pocketed investors line up to invest in it. And some of the circular deals have been scrapped for straight-up equity deals (although there is still plenty of circularity). Then again, OpenAI cut its own capex forecast through 2030 from \$1.4t to *only* \$600b. But they also said revenues would hit \$280b by this time! Nvidia delivered amazing earnings...but it caught the market on a bad day and was somehow punished...along with every other AI infrastructure play. Dell is popping this morning from its AI business. Coreweave is plunging from its.

Even the strong economic data has turned into “good news is bad news.” The strong(ish) employment report from two weeks ago, declining Jobless claims, solid business spending, and tame inflation (although the stronger than expected PCE is having some question the disinflationary trend...not us) have put a lid on rate cut hopes for now. Tensions with Iran are flickering back and forth. Some parts of the US government are still not funded fully. Homeland Security remains the political hot potato. And we have not even mentioned the tariff situation! The Supreme Court struck down the IEEPA tariffs. But Trump has already rolled out replacement ones. While some countries are looking to renegotiate deals, other countries are signing new ones. And some companies are forging ahead with lawsuits to recover already paid tariffs (the plaintiff list is over 1400 long including Costco and FedEx). But the Supreme court left this door open, so who knows how that will proceed (or linger).

Looking ahead, we still want to be long the market and diversify across sectors (meaning have more exposure than just Big Tech and related sectors). Broad economic strength, accelerating Earnings, and an accommodative Fed (post-Powell) should provide the backdrop for positive returns. AI will continue to flip-flop the daily narratives. We will try to tune out the noise and stick with the data.

➤ Karaoke killing the freight logistics industry?

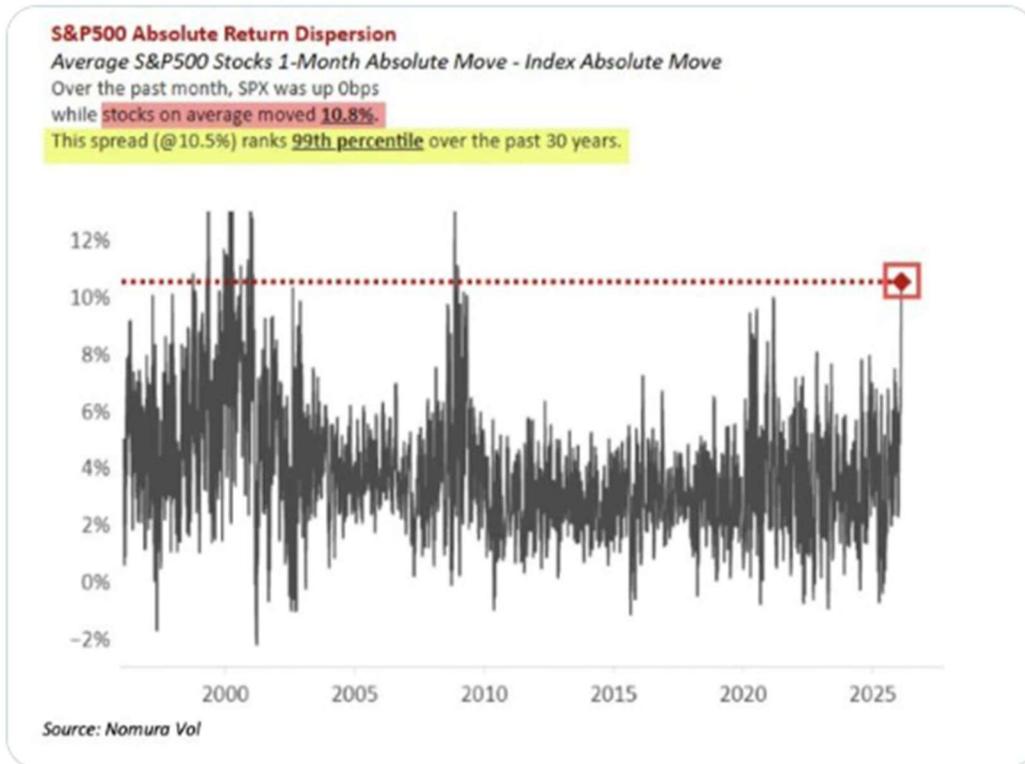
We have been talking about the spillover effects of AI. Some of the second derivative trades make sense. Legal services and financial data providers have come under fire for being ripe for disruption. Why pay an army of paralegals (not to mention lawyers) when AI can do the same work at a fraction of the time and at a fraction of the cost. Trimming some fat from banks and brokerages and other legacy industries makes sense, too. But perhaps some of the AI extrapolation has gone too far. Recently, freight logistics companies were under attack. A company called Algorhythm announced that it can scale freight volumes by 3-4x using its AI platform. CH Robinson and other established freight companies lost billions of dollars in market cap. But this upstart competitor has a market value of \$5mm with less than \$5mm in revenues. The best part is this company is not really an upstart but rather a retreat. Alert: Business change and Name change! Algorhythm was previously called The Singing Machine Company. Its core business was to import karaoke machines.

➤ Headline Vol is still subdued compared to the moves under the surface

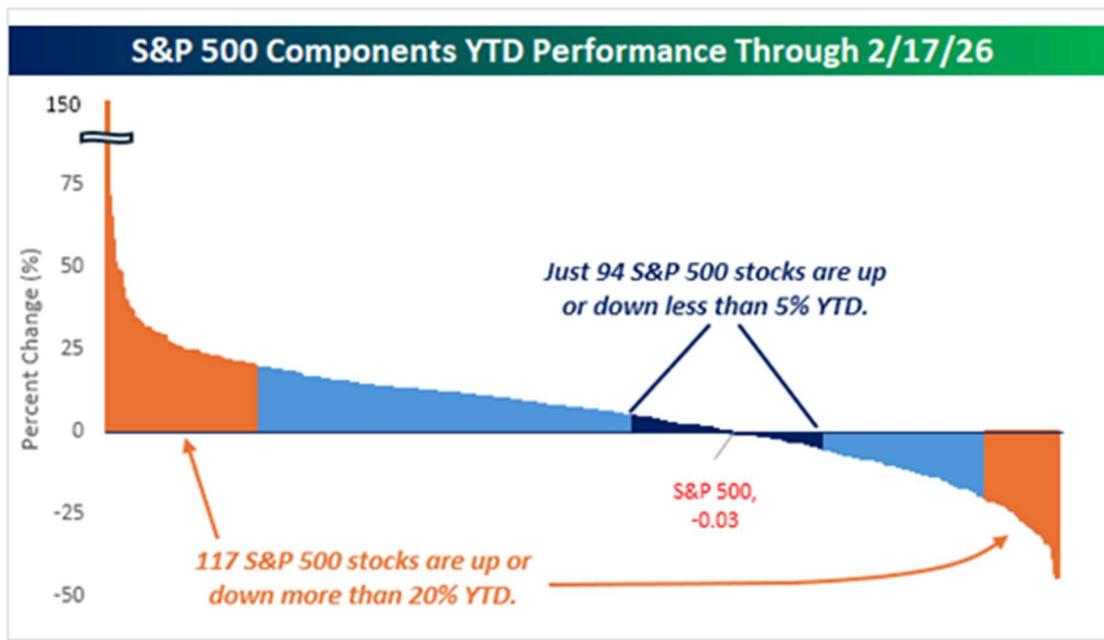
We have been focusing a lot on the anomalous relationship between headline Volatility and the array of large moves in individual names. Nomura points out that the index was exactly flat over the last month (mid Jan to mid Feb). But the average move of each stock in the S&P 500 was +/- 10.8%. Moves like this wreak havoc on long/short strategies or highly leveraged hedge funds in general. We have been reluctant to use one of our favorite terms “death rotations.” But this kind of underlying Vol with very little index Vol is just that. In the past, these episodic shocks have led to broad pain, albeit short-term in nature. But we are now inclined to think that these tensions might be more prolonged. In other words, we will have to wait to find out the winners and

losers in the AI trade going forward. The new technologies (plural) will surely boost economic growth. Thus, the top-level index will be ok, but the AI disruption will likely chop back and forth until revenues are cemented or until capex is cut. (We call this a Metaverse moment akin to when Zuckerberg turned on a dime and stopped spending billions of dollars on pretend characters and virtual neighborhoods.)

Here is the % Return Dispersion:



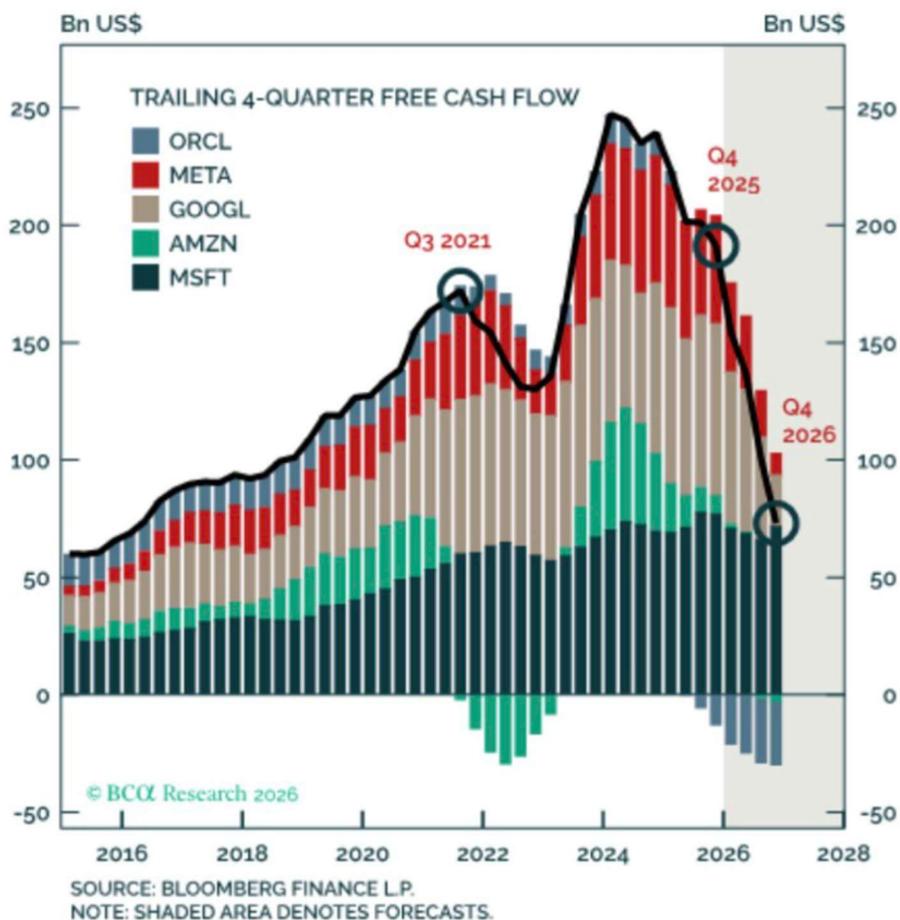
Bespoke has written about the same dynamic. This chart shows the wild swings in individual stocks (as of last week):



Source: Bespoke Investment Group • S&P 500 component YTD return distribution

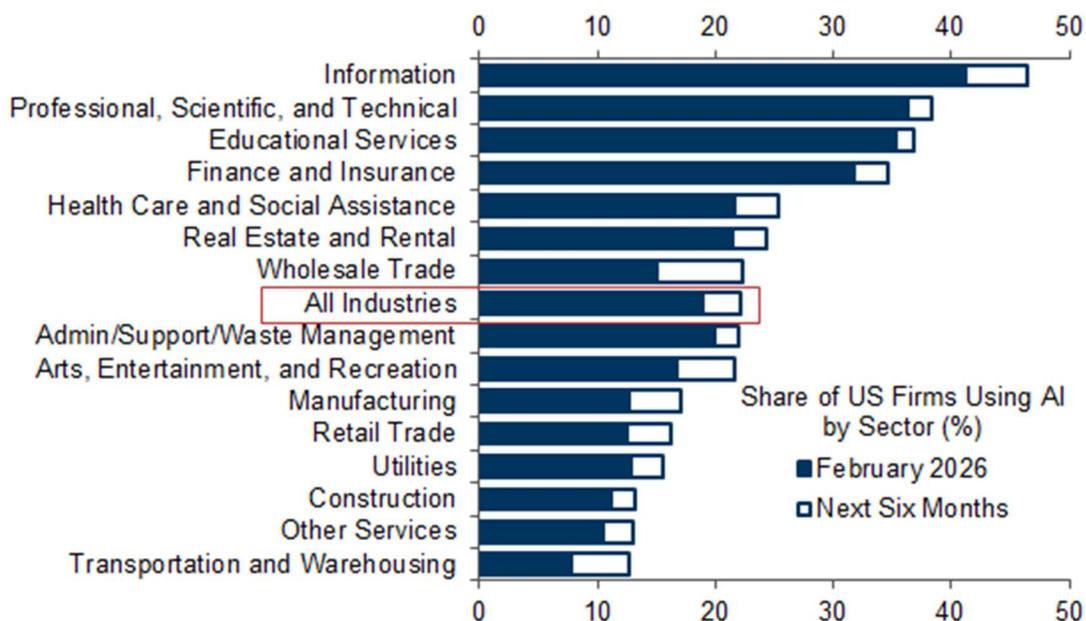
We would add that while headline Vol is still very low compared to the individual names, the number of instances during which the market moves beyond its trailing 2-standard deviation has reached one of its highest levels since we have been tracking this with our proprietary model (Dec 2022). Specifically, the 2-standard deviation of returns on the S&P 500 over the last year is 2.46% (as of last week). For the trailing 30-day period, it is 1.54%. Over the last year, there have been eight instances of the market return exceeding this 2-standard deviation move. Over the last 30 days, there have been four. Yes, these numbers are small and can be volatile, so we do not give them too much credence in isolation. But when combined with the other numbers (high dispersion, low headline Vol, average stock move, etc), we think it means we will continue to see outsized moves.

This chart from BCA shows what might cause another Metaverse moment...the massive erosion of Free Cash Flow (this chart extrapolates into the future...but this is based on what the companies have said they are going to spend on capex).



- Companies have started adopting AI, but the growth from here is expected to slow (?)

This survey data seems crazy to us. The current usage might be right, but we think the uptake going forward is going to scale rapidly. Labor productivity gains from AI are pegged between 24% (academics) and 32% (companies themselves). If this efficiency is anywhere close to being accurate, more AI uptake is on the way (and hence why the Free Cash Flow is plummeting...planning for it to rebound).



Source: Census Bureau, Goldman Sachs Global Investment Research

- The Fed is becoming a little more torn (but it does not matter until June anyway)

Fed: It appears the rift among the various Fed members is growing. In the minutes from the last FOMC meeting (policy implementation meeting), it was noted that several members wanted to continue cutting rates, some want to hold steady for some time, and some said further cuts were not appropriate. Furthermore, “several participants indicated that they would have supported a two-sided description of the Committee’s future interest rate decisions, reflecting the possibility that upward adjustments to the target range for the federal funds rate could be appropriate if inflation remains at above-target levels.” We think this is mostly a moot point. We think there is near 0% chance that Powell advocatess for any rate cuts during his last few months on the job (he might still be on the board, but he will no longer be Chairman). The chances of a cut in June sit around 47%. It was around 61% a month ago. This move is largely a function of the decent data (the uptick in PCE inflation notwithstanding).

- Revenues are beating expectations and accelerating

We have been noting the accelerating pace of Earnings growth this reporting season. With about 75% of the S&P 500 done, Revenues are also surprising and growing more than expected. One knock from the pundits is that all the Revenue strength has been in Technology. While this sector’s growth has certainly been strong, Materials and Utilities are the only two that have not improved since the early predictions back in July. (This data does not include Nvidia or the other big names this week.)

Exhibit 7. 2025Q4 Blended (Reported & Estimated) Revenue Growth

Sector	Today	1 Jan	1 Oct	1 Jul
Consumer Discretionary	5.4%	4.4%	3.0%	2.4%
Consumer Staples	4.1%	4.1%	3.3%	2.7%
Energy	-0.3%	-2.4%	-3.0%	-4.4%
Financials	6.5%	6.4%	4.0%	3.5%
Health Care	10.8%	8.9%	8.1%	7.3%
Industrials	8.2%	6.2%	6.2%	5.5%
Materials	3.6%	3.6%	6.1%	6.0%
Real Estate	8.1%	6.8%	6.2%	5.7%
Technology	20.6%	18.1%	13.7%	10.8%
Communication Services	10.4%	8.6%	7.7%	5.8%
Utilities	6.3%	6.1%	6.4%	7.3%
S&P 500	8.6%	7.3%	6.0%	4.9%

Source: LSEG I/B/E/S

- Inflation metrics are contrasting, but the market is getting behind the disinflation trend

Inflation cooled again as we expected. The Consumer Price Index (CPI) in January increased +0.2% vs the +0.3% increase in Dec. The change over the last year dropped to +2.4%. This is down from +2.7% in Dec. The “Core” inflation increased a little more at +0.3%, but this was the same as Dec. The annual “Core” fell to +2.5% down from +2.6%. Energy was the biggest mover on the downside with a -1.5% monthly drop. Food price changes reversed back to only +0.2%. Both Food at Home and Away from Home slowed (+0.2% and +0.1%). Even Electricity prices fell albeit only -0.1%. These jumped +0.7% in Dec. Shelter prices increased by +0.2% which is down from +0.4% in Dec. Rent and OER (Owners’s Equivalent Rent...that quirky measure whereby you guess the rental value of your home) both increased +0.2%.

The PCE inflation (change in the Personal Consumption Expenditure index), however, unexpectedly increased. Prices increased by +0.4%. This is an acceleration from +0.2% in November. This brings the annual rate to +2.9% (an increase from 2.8%). The “Core” also increased +0.4% vs +0.2% last, month. This brings the annual rate to 3% from 2.8%. Even though the Fed says they watch the PCE, the market tends to watch the CPI.

- 4Q GDP disappoints (blame the govt shutdown)

The advanced (first) reading for 4Q GDP disappointed by a wide margin. GDP only grew +1.4% (in real terms, taking inflation into account). This is down from the +4.4% in Q3. The market was expecting +3%. The Atlanta Fed’s GDPNow had tracked lower throughout the data releases (from the early +5.4% to +3% last week). The professional guessers (Wall Street economists) were expecting +1.9%. The big miss was born out of the government shutdown. Government spending dropped -5.1% which was a -09% drag on GDP. An increase in Fixed Investment and decent Consumer Spending were the bright spots. We think the market largely shrugged off this bad miss because the Retail Sales figure from December already flagged the weakness (despite the anomalous Consumer Spending). GDP growth for 2026 remains on track for above trend levels. The first read from the Atlanta Fed for Q1 GDP stands at +3.1%.

Personal Spending in December increased by +0.4%. This is the same as in November. Personal Income decelerated to +0.3% vs +0.4%.

- Business surveys are ok but slipping

The early reads (Flash) for the S&P PMIs were weak. The Composite slipped from 53 in January to 52.3 in Feb. Manufacturing fell from 52.4 to 51.2. Services slipped from 52.7 to 52.3.

The Philly Fed's Manufacturing index strengthened to +16.3 from 12.6. Employment Sagged but Business Conditions surged. New Orders dropped a bit. Prices cooled. The NY Fed's Empire State Manufacturing index was flat around 7. The Dallas Fed Manufacturing index climbed out of negative territory but just barely (-1.2 to +0.2). Services reversed into negative territory (+2.7 to -3.2). The Richmond Fed's Manufacturing index slipped deeper into negative territory (-6 to -10). Services also slipped. The Kansas City Fed Manufacturing index increased from -2 to +10.

➤ But Business Spending is still growing

The headline Durable Goods Orders for December dropped -1.4% vs November. But when you strip out lumpy Transportation Orders, they grew +0.9%. If you strip out Defense Orders (which results in the Core Capital Goods Orders, aka business spending), they grew by +0.6%. This is a deceleration from +0.8% in November, but it is still positive growth six months in a row.

Industrial Production is also growing. It increased +0.7% in January. It has been positive for 13 months in a row. It was negative for all of 2023 and 2024.

Factory Orders appear negative on the surface (-0.7% Dec vs Nov). But the same Transportation dynamic is at play here. Stripping this out, Orders increased +0.4% (vs the +0.1% last month).

➤ Housing data is mixed

Existing Home sales fell -8.4% in January. The annualized run-rate dropped to 3.91mm. This is one of the lowest levels in three years. And the three-year trend is still light-years below the pre-Virus level (never mind the Virus period surge). Pending Home Sales in January dropped slightly -0.8% vs Dec. Building Permits improved in December by +4.8%. 1.46mm annualized run-rate is the highest in nine months. New Home Sales in December slipped after a big surge in November (this is government data affected by the shutdown, so it is all over the place right now). Generally, we would say this data (New Homes) is slowly accelerating to above the pre-Virus Fear trend. The Housing Market Index (aka homebuilder survey) slipped a touch to remain in miserable territory. This contrasts with the improvement in New Home Sales...this is likely a sign that smaller builders are suffering at the hands of the larger builders.

The average 30-year mortgage rate decreased from 6.21% to 6.17%.

Weekly Mortgage Applications increased slightly. New mortgages are slumping a bit (still trending well over the last year, but a recent slowdown) while refinancings are accelerating.

➤ Other economic data is better

Jobless Claims dropped back to 208k after two weeks around 230k. This week was 212k. Continuing Claims ticked up to 1.864mm from 1.852mm. But then they continued their downward trend to 1.833k.

The Weekly ADP Employment change increased 11.5k and 12.75k over the last two weeks (+7.75k before)

Michigan Consumer Sentiment remained steady. 1-year Inflation Expectations fell from 4.0% to 3.4% (and this is the biased survey, so that is saying something).

The Trade Deficit widened to \$70.3mm. It is back to the range before Liberation Day.

Redbook Retail Sales increased +7.2% and 6.7% over the last two weeks (vs 6.5% before).

Consumer Confidence in February ticked up slightly (and January was revised higher).

- Where did all the crypto money go?

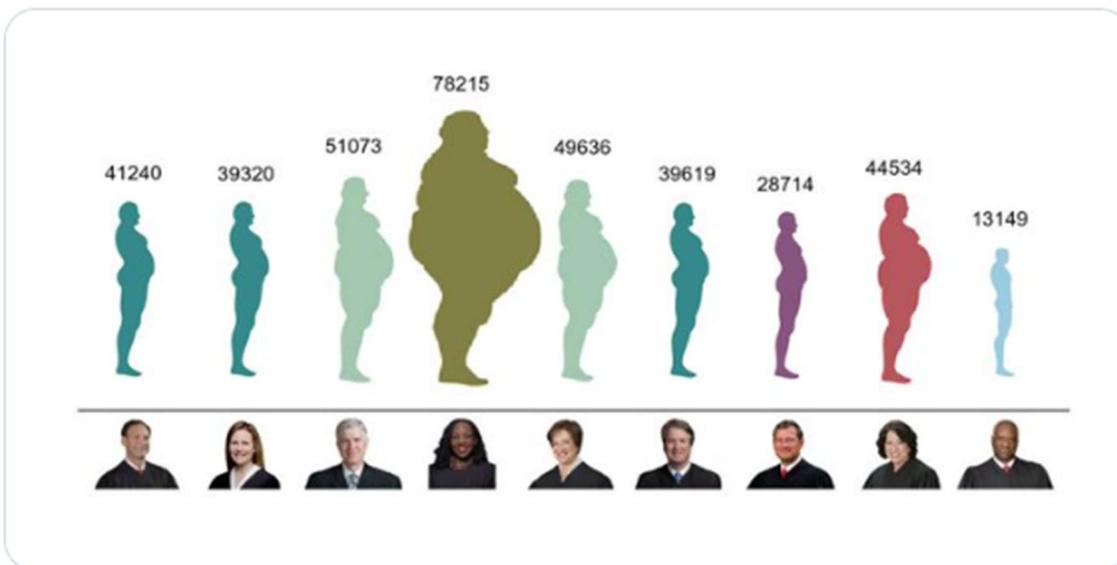
Two weeks we wrote about the misinformed insider information surrounding whether Cardi B would “perform” during the Super Bowl. We noted that Polymarket declared “dancing” as “performing,” so the rapper Preme (?) lost his sure-thing of a bet (to the tune of \$177k). But Kalshi, technically legal and regulated in the US as opposed to the offshore Polymarket, declared the bet too complicated because Cardi B might have been lip syncing the words during a song. So, the bet was resolved at the last traded price before the show.

Since the beginning of 2025, 31% of all physical crypto crimes (people being kidnapped, tortured, etc) have occurred in France. Where is Jerry Lewis when you need him.

- Chart Crimes of the week

Yes!

So I plotted the number of words spoken by each Supreme Court Justice in 2023 in the form of fat guys:



The President of France posted the original version of this. Of course, it is absurd because most countries are building their own data centers and are not relying on foreign investment. But we mostly like it for Inspector Clouseau guy trying to figure out the silly labeling (Macron did not have this on the original chart).



➤ Quick Hits

- There is an airline in India called Cheap-O Air.
- California is clarifying its no-blackjack gambling law (other than on tribal lands). Players can no longer bust by going over 21. Instead, the winner will be determined by a point system (getting closest to a moving point target).
- The same law says getting dealt blackjack will no longer be an automatic winner.
- Robert Duvall's first movie role was Boo Radley in To Kill a Mockingbird.
- A judge has ruled that chicken wings do not need to be made from the wings of a chicken.
- The same judge clarified that chicken wings or even boneless wings are a cooking style.
- At the beginning of the social media trial (Meta/Facebook and Alphabet/Google are the defendants, the accusations are that social media sites are addicting and harming children), the judge warned the gallery to not be recording any of the proceedings including with video-enabled glasses. A handful of observers immediately took off their Meta glasses.
- The goalie for the US Women's hockey team is the first Pittsburgh native to win a gold medal in the Winter games since 1924.
- Jerry West, the late, great player and GM of the Lakers, once hit a hole-in-one at the Riviera golf tournaments' pro-am day. As a prize, he was awarded four Lakers tickets (and a parking pass).
- Tug-o-war was an Olympic sport from 1900 to 1920.
- The British won the gold in 1908 by cheating with metal spikes.
- Porcupine quills were once used as toothpicks.
- Men suffer from long-term hiccups more often than women.

TSLAQ: Not much to report in Muskland. He is focusing on politics and digging tunnels in Nashville (in addition to Nevada and Texas). He claims he can dig for 99% less than the typical tunneling cost. That is incredible. It is likely a function of government and not some new technology. Either way, we like it.

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