TINA, Turbulence, & Magnificence

February 2026

"As long as the music is playing, you've got to get up and dance. We're still dancing." – Chuck Prince[i]

Boiling Frog Syndrome[ii]

At Moerus, we are focused on identifying investment opportunities and building portfolios from the bottom up, but that doesn't mean that we ignore the macroeconomic situation. Quite the contrary; while we don't make predictions of what macroeconomic variables will be in the future, we firmly believe it is of utmost importance to know what those macroeconomic variables are in relation to their broader history in order to "know the neighborhood we are in." This is more for our safety than as a speculation of what the future may hold – an attempt to avoid being swept up in manias and lofty expectations, which, in our experience, can create downside risk. As for the future, our crystal ball is just as cloudy as everyone else's (in fact, it's downright opaque), but what we do know is that it seems quite possible that investors are underestimating the downside risk of the current moment, given the exuberance around all things AI and the demanding (in our opinion) expectations that seem to have been priced in to many stocks.

In 2023, we wrote a short memo ("That ETF Might Be Riskier Thank You Think") outlining the potential risks we thought passive ETF investors could be facing, given the growing dominance of a few companies within global indices; the acronym at that time was FAAMG[iii]. This problem of the growing concentration of indices has only grown worse over the ensuing two and a half years, with the Top 10 holdings in the S&P 500 now accounting for an astounding 39% of the Index, while it was just under 30% back in 2023. In fact, the principal difference between 2023 and now seems to be the fact that Meta is now an AI company, having abandoned the Metaverse (which, at the time, was reputed to be the future of the company and the reason for its name change), and the fact that Nvidia has eclipsed all other companies in importance, resulting in the group name evolving to the "Magnificent 7" or "Mag 7" for brevity (in fairness, this is much catchier than "FAMTANG"). Looking backwards, this has been great as the Mag 7 stocks have been a key driver of index performance over the past several years. This is seen both in their record-setting allocations within many indices (the Mag 7 accounted for 34.4% of the S&P 500 as of early January 2026) and the divergence in performance between the Capitalization Weighted and Equal Weighted versions of the S&P 500. The Capitalization Weighted S&P 500 is up 86.0% over the three years ended December 2025, while the S&P 500 Equal Weighted was up just 43.3% over the same period[iv]. This extends beyond the Mag 7 to other technology firms, as Information Technology now accounts for 34% of the S&P 500 – a level not seen since the dot-com bubble and a statistic that doesn't even include some of the largest tech firms, such as Amazon (Consumer Discretionary) and Alphabet (Communication Services), that are categorized outside of Information Technology.

Still Dancing with TINA

One of the results of the exuberance around these companies and the trend towards passive investing has been a self-fulfilling virtuous cycle. As more investors give in to the belief that There Is No Alternative ("TINA") and increase their allocations to these areas, the dominance of these companies grows further. Even if investors are not actively allocating more to these companies, as assets flow into passive ETFs, they are also being allocated heavily to the Mag 7, given its significant weight in the indices that many ETFs track. However, to us, investors seem comfortable with this – why take a risk and allocate away from the stocks that seemingly everyone believes are the key to future performance? Professional investors, understandably, don't want to take the career risk of missing out on the AI boom. Even if investors do think there are signs of irrational exuberance, it seems like most investors have resigned themselves to the approach that they either have to "get on the train" or risk falling behind and losing their jobs. For most investors, the principal risk today seems to be FOMO ("Fear Of Missing Out") rather than poor performance, as their competitors are also heavily invested in the Mag 7. After nearly 17 years of success investing heavily in the US technology industry, it almost feels as if market participants can't imagine a scenario where it doesn't work out in the future. The problem with this, in our view, is that people buy passive ETFs because they want to get exposure to "the market" but, given the outsized influence of these companies, investors should understand that they are increasingly getting the Mag 7 as opposed to a broadly diversified index.

This Time is Different?

In investing, one of the adages to be most skeptical about is "this time is different." When comparing today's AI fervor to the excitement in the dot-com bubble, people often cite the lack of debt, the strong cash flow generating capabilities of today's tech companies, and the revolutionary nature of AI as reasons for this time to be different. While there is room for debate over the accuracy of this claim and the speed of change, especially given the eye-watering capital expenditures being announced, we believe this misses the point. We do not purport to be technologists, futurists, or experts in AI; what we *do* have a strong understanding of is the general dynamics of businesses, economics, and cycles across various business types and geographies around the world. This is a result of the accumulated experience resulting from our combined 80+ years of investment experience across the team, including some painfully earned first-hand experiences with some of the downside risks and external shocks that can manifest themselves. One of the key lessons we have learned over the years is that while it may feel different this time, it's most likely not – and that even when it is different, it still has a way of rhyming with history.

We believe that ruminating as to whether or not this is a "bubble" is a waste of time. Even if it is a bubble, there is no way to know what could cause it to deflate or when that may come about. The question to us is not "is this a bubble," but rather "how do I invest my capital in the context of the exuberance and potentially overly optimistic valuations (which could easily continue to increase apace) that exist today?" To be clear, we have no idea what the future holds and don't try to make predictions around how the future will work out. What we do attempt to do is have an understanding of what investors are pricing in to the markets in an attempt to better understand how all of these things filter into the bottom-up valuations that drive our investment process. Additionally, at Moerus, we seek to invest based on the here and now; not on our expectations of an unknowable future. In today's markets, there are a lot of things **we don't (and can't) know**: Who will win the AI race? Will the winner take all? How will the underlying technology change? Is the risk of foreign competition (e.g. China) underestimated? There are, however, things that **we do know** today: We believe that there are a lot of positive expectations priced into valuations today (perfection in execution, future dominance of markets by the incumbents/winners, and significant future cash flow generation, as a result of all of this). We also know that things don't always work out perfectly and that the future is, by definition, unpredictable and not as-yet written. Specifically, the question we seek to answer today is not "what will the upside be when these things work out as expected and how do we participate?" but rather "what is the downside if they don't and how do we avoid it?"

Look Out Below?

As with all things we do at Moerus, our primary focus is on mitigating the downside. Only then do we begin to think about upside potential. We have written extensively in the past about how we view risk (see our memo "Perspectives on Risk: How You Can Lose Money – Let's Count the Ways") and believe "risk" is incomplete without an adjective. As such, we think about three principal risks:

- **Market Risk**: Expected potential short-term variability (up and down) of stock price.
- **Price Risk**: Risk resulting from overly optimistic expectations for the future being priced in.
- **Business Risk**: Risk that the value of a business is permanently fundamentally impaired.

As we have noted in past letters, at Moerus, we seek to avoid the latter two forms of risk as much as possible, while we embrace the opportunities provided by Market Risk. To us, this simple approach feels almost completely opposite to the one the market is taking today regarding the Mag 7, where there seems to be an aversion to Market Risk – or at least an aversion to Market Risk that differs from the herd and the potential career risk that comes along with it – but there seems to us to be a comfortable embrace of Price Risk. While there may not be lot of perceived *Business Risk* in the Mag 7 and related securities, we believe that, given the lofty expectations, there is significant *Price Risk* that the market seems to be under-appreciating. To quote Fred Schwed Jr.'s classic investment book *Where are the Customers' Yachts?*, "Booms go boom."

The Seatbelt Sign is On

Hovering over these (in our opinion) sky-high expectations is the severe turbulence that global macroeconomics and geopolitics seem to be experiencing. Be it wars beginning or ending, the reintroduction of early 20th century trade practices, the seemingly never-ending policy U-turns of the current US administration and the unpredictable nature of what is in focus, technological disruption, or the imposition, reduction, and potential overruling of tariffs, there is so much complexity on both the macroeconomic and company-specific ends that it's almost easier to try to understand the inner workings of a Rube Goldberg machine. All these shifting currents have, in some ways, made investing feel more challenging than it has been in years. However, this is not a good reason to turn away from international markets and focus on what feels most comfortable to US investors: US companies. Quite the contrary, we believe that the current environment has created a significant opportunity for many companies across the world. As trade relationships are adjusted and as technology changes everything, many companies – both within and outside of the United States – have a significant opportunity to take market share, improve efficiency, and serve new customers.

At the same time, this geopolitical and macroeconomic turbulence, coupled with the market's obsession of focusing on fewer and fewer well-loved securities, seems to us to have created significant opportunities for investors in what we view as attractive valuations. Looking outside of the small subset of companies that the market currently finds attractive, international markets continue to be more attractive than they have been in recent years, from a relative valuation perspective, even after strong performance in 2025. Using two metrics as a simple point of comparison for valuations: at the end of 2025, the S&P 500 traded at a P/E of 28.6x and a P/B of 5.3x, while the MSCI ACWI (ex-US) traded at a P/E of 17.6x and a P/B of 2.6x[v]. This is not to say that investors should just indiscriminately allocate assets outside of the US – where they allocate to matters more today, in our opinion, than it has in many years. Additionally, many of these widely held companies seem to be priced for certainty, so a small misstep in the regulatory, political, or legal areas (all of which seem fraught with uncertainty today) could dramatically change the market's view on valuations of these companies.

A Bird in Hand…

So, what do investors do in today's market, one in which indexes have growing concentrations in the market's favored investments, there are (almost daily) seismic shifts in geopolitics and global systems of trade, and the market seems to be valuing securities as if a small handful of companies will be the only winners in the AI race? Simple – we believe that investors **should focus on the here and now**. Investors should seek to offset the outsized allocations in most portfolios to the various waves of the future and companies racing to be the winner-take-all victor of the AI race. We are finding what we believe to be fantastic long-term opportunities by focusing on companies outside of the market's very small area of focus – finding companies that will almost certainly benefit from the AI revolution in the form of new markets and reduced costs, but that are not "AI Investments."

We are **not** arguing that investors should abandon allocations to the US, AI, or technology investments, but rather that investors should be aware of potentially optimistic valuation multiples for some of these companies and the higher Price Risk that we believe may be associated with their higher multiples. Diversification is likely more important – and harder to simplistically achieve – for most investors in today's markets than it has been in a long time. But, by simple definition, the current market darlings **cannot all be the dominant market winners**, and some of their valuation multiples will be proven to be way too optimistic. It is this precise eventuality that we believe investors are not paying enough attention to. Gaining exposure to securities outside of this small locus of market focus is an easy way to offset some of this risk through diversification.

Diversity is the Spice of Life

The idea of diversification is in no way novel, but what is new is the fact that, after many years of the supremacy of growth investing, many Growth and Value Funds seem to be looking more the same, making diversification harder to achieve. We recall a prospective client who told us how they had selected a Growth Fund and a Value Fund as their International allocations in order to pursue a "barbell approach" to gain exposure to all different types of companies. Upon inspecting the holdings of the two "complementary" funds, it turns out that they had three of their top ten holdings in common. Looking today at the largest active International Value Fund and International Growth Fund by AUM, Taiwan Semiconductor Manufacturing Co Ltd. is the top holding in the Growth Fund and the fourth-largest in the Value Fund. As a matter of fact, looking at the ten largest International Funds (including growth, value, and core), TSMC was in the Top 10 Holdings of all but two portfolios. Additionally, among the same universe of large funds, there was not a single portfolio that did not share at least one of its Top 10 holdings with the top holdings of its peers. Diversification only works if the managers employing different investment styles actually invest in different securities. The ten largest actively managed International Funds only have an average Active Share of just 65%[vi].

While these are just anecdotal examples, they are reflective of the trend of larger, well-respected, and stronger performing investment management organizations having shifted over the years more towards what has been working to deliver performance, sometimes stretching (or even abandoning outright) their investment philosophy to conform to market trends in order to keep pace with others. This has resulted in many larger funds looking more like the index and more like each other, which has negative implications for diversification (a topic for a whole letter of its own). To counter this, we believe that it is imperative that selecting a manager to provide diversification is done in a way that investors actually get diversification. Strong historical performance and differing investment styles are not enough to diversify in today's environment; instead, we believe that investors should be seeking real diversification though managers with very high Active Share and exposure to out-of-index investments.

If Everybody Is Thinking Alike, Then Somebody Isn't Thinking
TINA and FOMO are real and understandable. Pragmatically, how can allocators protect themselves on the downside without taking the career risk that could come from stepping away from the herd and the investments that have worked for many years? Investors are compared to peers and relative performance is often the benchmark, but as another Wall St. cliché goes, "you can't eat relative performance." We believe that one way that allocators can solve this problem without avoiding these investments outright is by taking a closer look at the underlying holdings held by the managers or ETFs that they are investing in for diversification, with an eye towards reducing overlap and making sure that they are getting diversification.

In the scenario (unthinkable to some) that things do not work out perfectly for some of these highly valued companies – as is implied by their current valuations – allocations to out-of-index investments may provide some much-needed diversification. While the virtuous cycle of passive investors following capitalization-weighted indices – by design investing increasingly in the stocks that have recently gone up the most– may continue for some time, it can easily and quickly turn into a vicious cycle if sentiment shifts, given the current market dynamics. Said differently, while it may feel "safer" being part of the herd, it may actually turn out to be *less* safe, as the herd becomes more concentrated in their investments.

At Moerus, we have built a ten-year track record of investing differently (see our first Shareholder Memo, "Moerus Capital: An Introduction," for an overview of how we think). We do this not because it is fun, not because it is easy, and not because it is trendy; but rather because we believe that significantly mispriced opportunities can be found by looking where others are not, and that over the long term, this approach will deliver attractive returns to investors who are willing to think differently and stomach being apart from the herd. Our differentiated, asset-based investing approach (see our second Shareholder Memo, "Asset-Based Investing in an Earnings-Focused World") typically results in a portfolio of securities that, over the years, has looked quite different from both the index and our competitors, with high Active Share and exposures to securities not included in major indices. As a result, this track record has been achieved without the benefit of owning the technology companies the market seems to value so dearly. We note this not because we dislike technology companies, but simply to show that there may be another way, despite the market's view to the contrary. We believe that this approach has served our investors well and expect that it will continue to do so years into the future.

We believe that all investors should consider an allocation to strategies that offer diversification (i.e., different holdings and exposures to that of the index and other managers). This has been harder to find in both *passive* ETFs and mainstream *active* strategies, which, to us, are looking more and more the same.

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[i] This quote was famously made in July 2007 by Charles O. Prince III, CEO of Citigroup at the time.
[ii] Boiling Frog Syndrome is a metaphor that represents "creeping normalcy" or the inability to recognize gradual, dangerous changes until it's too late.
[iii] Meta (formerly Facebook), Amazon, Apple, Microsoft, and Alphabet (formerly Google).
[iv] Source: Index Factsheets and Bloomberg.
[v] Source: S&P 500 December 2025 Factsheet & MSCI ACWI (ex-US) Factsheet.
[vi] Active share is a measure of the difference between a portfolio's holdings and those of its benchmark. The industry uses it as a proxy for how "actively" an investment manager is managing a portfolio. Source of data is Bloomberg and Morningstar.com.

About Moerus Capital Management

Moerus Capital Management was founded in 2015 and is a 100% employee-owned organization. We run one global, deep value investment strategy that utilizes an opportunistic approach that results in a concentrated portfolio of securities in developed, emerging, or frontier markets where we are seeing the most attractive long-term opportunities. The investment team led by Amit Wadhwaney, Portfolio Manager and Co-Founder, has worked together for more than 15 years and has experience investing in most countries around the world.

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