FEG



PORTFOLIO INSIGHTS

Much Ado About Nothing, For Now

Third Quarter 2026

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In Brief

The third quarter was awash in uncertainty around rising rates, upcoming midterm elections, geopolitics, and the artificial intelligence (AI) revolution to name a few of the more notable items. But despite all the nervous news flow and pivotal changes, returns for the major asset classes were largely flat once the dust settled. Heightened focus is now on interest rates, not only for the potential impact on the bond market, but also for the likely ripple effects on other asset classes—and even on the fiscal stability of the United States as the national debt has now topped $40 trillion. The 10-year Treasury yield increased more than 0.5% in the quarter, and as of this writing stands north of 5%, the highest level in nearly two decades.

The conflict in the Middle East continues to drag on, wreaking havoc in energy markets. Politicians on both sides of the aisle are beginning to attack data center construction as an easy soundbite to try and win votes. Both could become market and economic headwinds as power and data center capacity are essential ingredients for sustaining the AI-fueled economic boom.

In the third quarter the four major asset classes—equity, fixed income, real assets, and diversifying strategies (hedge funds)—were all roughly within +/-3% of flat results. Global equity markets were on the right side of zero, posting slightly positive results. Fixed income and real assets, on the other hand, were down roughly 3% in the quarter given rising rates and the corresponding decline in bond prices and impact on duration sensitive assets like real estate and infrastructure. Finally, diversifying strategies came in somewhere in between fixed income and risk assets (i.e., equity and real assets).

KEY AREAS OF FOCUS FOR REMAINDER 2026 INCLUDE:

- **Rates:** As Warren Buffett famously said, "interest rates are to asset prices, what gravity is to the apple." The direction of rates from here will have a meaningful impact on asset class performance. That includes short-term rates as set by the Federal Reserve, as well as longer-term rates as set by the market.

- **Frontier AI labs revenue:** Much attention has been given to the magnitude and momentum of hyperscaler capex spending. For that to continue, the major frontier AI labs, Anthropic and OpenAI chief among them, must continue their meteoric revenue growth rates to drive the demand for compute power, data centers, chips, etc. This is the epicenter of the strong equity market earnings we have experienced year to date, and key to the future earnings trajectory. One company's capex is another company's revenue.

- **Policy:** How the conflict in the Middle East plays out and the ongoing impact on energy prices and supply chains is another key item to watch closely. Additionally, which political party is in control of the House and Senate after the midterm elections will carry consequences for what can or cannot get done in Washington D.C. and what market-shaping economic policies may be in play or on the horizon.

While the third quarter was relatively flat for investment returns, the year-to-date results for 2026 have been robust. Equity markets have delivered mid-teen returns over the first nine months of the year, while real assets and hedge funds are in the mid-to-high single digit return range. The market movements, technological change and policy dynamics are incredibly fascinating to study and research. For long-term investors, we also must not overreact to any of them and keep our sights on the strategy and objectives we have in place and codified in investment policy statements.

PUBLIC MARKETS OVERVIEW

Strong Earnings Meet a Higher Cost of Capital

Public markets delivered a deceptively calm third quarter. Broad U.S. and developed international equities finished modestly higher, emerging markets were roughly flat, and bonds declined as yields rose. Beneath those headline results, however, the environment changed meaningfully. The Federal Reserve (the Fed) resumed tightening, the 10-year Treasury yield moved above 5%, energy prices climbed, and market leadership narrowed late in the quarter. Strong earnings and investment in AI helped large-cap equities absorb higher capital costs. Index-level returns understated the repricing beneath the surface.

Interest rates were the clearest transmission mechanism across markets. The Fed raised its policy rate in September as higher energy prices complicated the inflation outlook, reversing the earlier easing narrative. The 10-year Treasury yield ended September at 5.27%, up 83 basis points during the quarter, while breakeven inflation also moved higher. The Fed controls the overnight lending rate, but growth, inflation expectations, and Treasury supply influence longer-term borrowing costs. The implications extend well beyond fixed income, as the risk-free rate influences both asset valuations and the cost of financing across the economy.

DEBT, INFLATION, AND GROWTH SHAPE LONG-TERM YIELDS

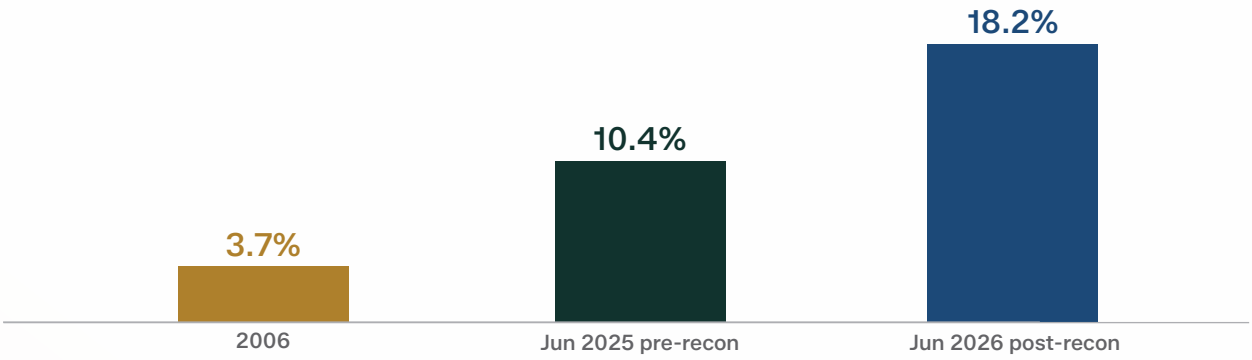
Daily 10-year U.S. Treasury yield, October 2024 through September 2026



Sources: FactSet. Data as of 9/30/26.

TECHNOLOGY NOW REPRESENTS NEARLY ONE-FIFTH OF VALUE

Information technology weight in the Russell 1000 Value Index in 2006, and after June 2026 reconstitution.



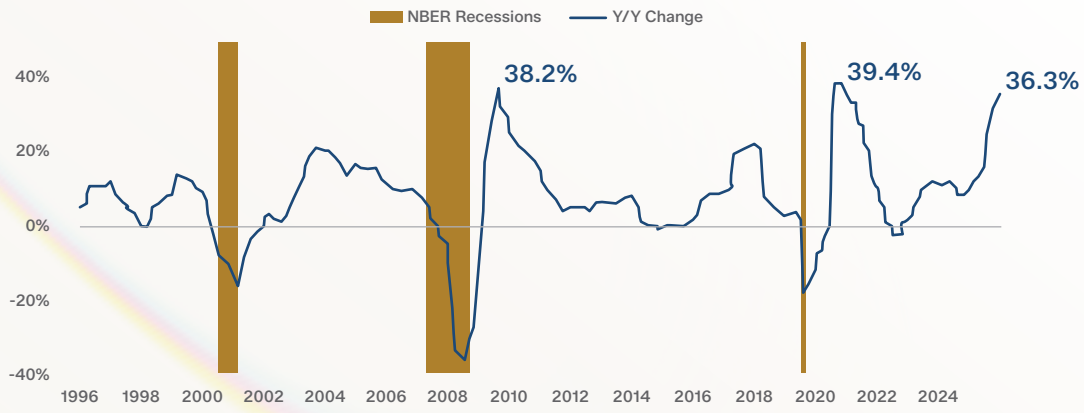
Sources: FactSet and State Street Investment Management.

Equities proved relatively resilient, but performance was far from uniform. The broad market Russell 3000 Index gained 1.4% during the quarter, while the Russell 2000 Index fell more than 7% as higher financing costs weighed on smaller companies. Large-cap value outpaced growth, yet technology remained a strong sector, highlighting how traditional style labels increasingly overlap with the AI theme. Developed international equities posted modest gains, while emerging markets were essentially flat. By September, gains had become increasingly concentrated in large technology companies even as most sectors and smaller-cap stocks weakened.

Earnings remained the principal support for equity markets. Forward earnings expectations have risen at a pace comparable to prior post-recession recoveries, aided by demand for semiconductors, data centers, electrical equipment, and other components of the AI buildout. Exceptional growth becomes harder to sustain as comparisons become more demanding. At the same time, AI investment is becoming more capital-intensive. The largest technology platforms still generate substantial cash flow, but spending is increasingly shifting from internally funded capital expenditures to bond markets and special-purpose financing. This extends the AI story into fixed income and raises the importance of financing costs and the returns earned on new investments.

S&P 500 EARNINGS GROWTH RIVALS POST-RECESSION RECOVERIES

Year-over-year growth in S&P 500 next-twelve-month earnings estimate.



Sources: FactSet and NBER. Data through August 31, 2026.

Fixed income absorbed the clearest impact of higher rates. The Bloomberg U.S. Aggregate Bond Index declined 3.5% during the quarter as rising yields pressured bond prices, with long-duration securities experiencing the largest losses. Credit spreads also widened, more so in high yield than in investment grade, while floating-rate bank loans were a notable exception. Higher starting yields improve income, but the third quarter demonstrated that the speed and magnitude of rate changes still matter. Bonds may provide attractive income, yet their diversification benefit can be challenged when inflation concerns push yields higher as risk assets are repriced.

Real assets displayed a similarly sharp internal divergence. U.S. and global REITs fell roughly 6% during the quarter, and global infrastructure declined more than 7%, reflecting pressure on capital-intensive and rate-sensitive assets. Energy moved in the opposite direction: the S&P 500 Energy sector gained about 17%, while WTI crude rose roughly 30% as Middle East disruptions renewed concern around global supply. The move also complicated the inflation backdrop and the Fed's policy calculus. Real assets again demonstrated why the category should not be viewed as a single trade, as commodities, real estate, and infrastructure can respond very differently to the same macroeconomic environment.

The approaching midterm elections added another source of policy uncertainty, particularly around taxes and spending. History, however, provides little reason to treat election outcomes as a broad market-timing signal. Earnings, inflation, and interest rates have a more direct connection to asset prices, even as congressional control can shape sector outcomes. The more consequential question for investors is whether corporate cash flows can justify current valuations while absorbing a higher cost of capital.

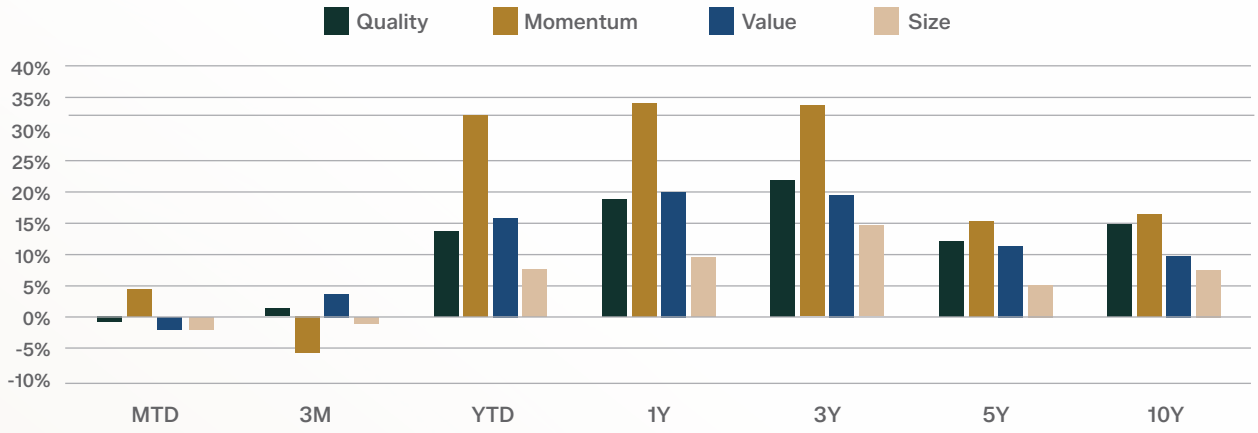
The third quarter did not overturn the constructive fundamental backdrop, but it did complicate potential future gains. While earnings remain strong, and AI-related investment continues to create opportunities, higher rates are placing greater pressure on financing-dependent companies and assets, while the AI buildout itself is becoming increasingly reliant on capital markets. For diversified portfolios, the environment reinforces the value of thoughtful asset allocation, disciplined manager selection, and multiple sources of return. The headlines may have produced more noise than return, but the underlying message was meaningful: capital is no longer as cheap, raising the hurdle for investments to generate attractive returns.

GLOBAL EQUITY

Resilient Markets, Widening Dispersion

Global equities remained resilient despite a challenging macroeconomic backdrop. The MSCI World Index gained just under 2.0% during the quarter, supported by resilient economic growth and strong corporate earnings. However, renewed Middle East tensions pushed oil above $100 per barrel, reigniting inflation concerns and prompting central banks to raise rates. Bond markets experienced significant volatility, with the 10-year Treasury yield surpassing 5%. Importantly, earnings growth rather than multiple expansion has increasingly supported equity returns, raising the importance of sustained profitability heading into the end of the year.

MSCI ACWI FACTOR PERFORMANCE



Source: MSCI. As of 9/30/26.

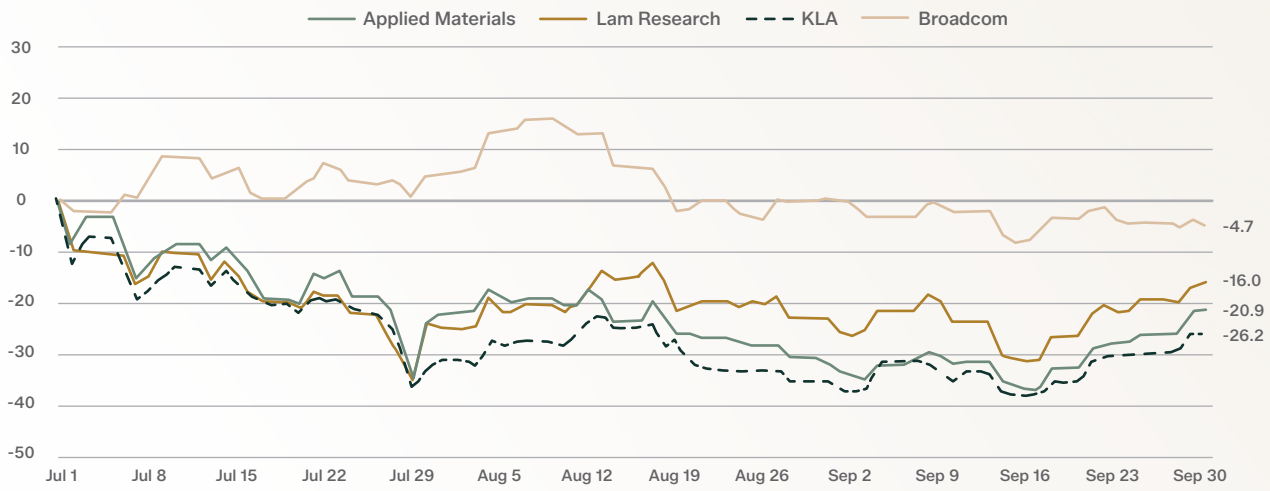
U.S. equities advanced, although performance dispersion and narrow market leadership challenged active managers. The S&P 500 Index gained just over 2.0%, while the average U.S. equity fund declined around 2.4%. Energy benefited from higher commodity prices, technology remained supported by earnings growth, and healthcare rallied following greater clarity on pharmaceutical pricing. Conversely, small caps and utilities struggled amid rising yields. U.S. growth outperformed value, contrasting with global markets where value led, highlighting differences in regional market leadership and the continued challenges of navigating concentrated benchmarks.

International developed markets lagged, with significant differences across European markets. Eurozone equities declined, pressured by higher energy costs, European Central Bank (ECB) tightening, and relatively weaker earnings momentum. Europe's limited exposure to AI-related investment also weighed on relative performance. Conversely, UK equities gained approximately 2.5%, benefiting from their greater exposure to energy, financials, and materials. Looking forward, increased European fiscal spending on defense and infrastructure could create attractive opportunities, although selectivity remains important given uneven earnings growth and higher financing costs.

Japan continued to outperform, supported by structural reforms and improving corporate fundamentals. The TOPIX appreciated in local currency, supported by strong earnings, accelerating share repurchases, and continued corporate governance improvements. Leadership broadened beyond technology, with financials benefiting from rising domestic interest rates and cyclical businesses attracting investor interest. Despite currency volatility and monetary tightening, Japan's improving shareholder returns and corporate profitability remain supportive of opportunities for active managers.

Emerging markets struggled as the first-half AI rally lost momentum, although country-level dispersion remained significant. The MSCI Emerging Markets Index declined approximately 0.4%, with South Korea and Taiwan pressured by a sharp correction in semiconductor and memory-related companies. India also underperformed amid elevated valuations and higher energy costs. Conversely, Brazil and South Africa benefited from commodity strength and improving inflation trends, while China delivered modest gains. These divergences reinforce the importance of country and sector selection rather than relying on broad emerging market exposure.

SEMICONDUCTORS STUMBLE



Source: Morningstar, FEG. As of 9/30/26.

The AI trade experienced a meaningful rotation rather than a broad reversal. Semiconductor equipment and memory companies experienced significant drawdowns as investors questioned the sustainability of AI infrastructure spending. Meanwhile, hyperscalers and software businesses rebounded, with Microsoft gaining more than 33% during the quarter. Hedge funds increasingly rotated away from momentum and memory exposure toward quality, hyperscalers, and agentic AI. With substantial debt issuance financing the AI buildout, investors may increasingly differentiate between companies funding infrastructure and those successfully monetizing AI investments, creating opportunities for fundamental stock selection.

FIXED INCOME

Rising Yields and Renewed Volatility

U.S. Treasury yields rose sharply in the third quarter. The 10-year rose 83 basis points (bps) to 5.27%, near its highest level since 2007, while the 2-year rose 72 bps to 4.87%. With 10-year breakeven inflation up only 12 bps, most of the increase came through real yields, reflecting a repricing of the policy path and stronger growth rather than a notable shift in long-run inflation expectations. Oil rebounded above $100 per barrel; core PCE (Personal Consumption Expenditure Index), the Fed's preferred measure of inflation, held at 3.0% year over year in August; and weak auctions and heavy corporate supply added further pressure. The Bloomberg U.S. Aggregate Bond Index (the Agg) returned -3.5% for the quarter, while long-duration Treasuries fell nearly 9%.

The Fed raised its benchmark rate by 25 bps to 3.75%–4.00% at its September meeting, its first hike since 2023, after three members favored a hike at the July meeting. The September vote was unanimous, and the committee raised its median 2026 rate projection to 4.1%, implying one additional hike this year. Uncertainty around the policy path pushed rate volatility sharply higher, with the MOVE Index rising from the high 60s in July and August to above 100 by late September, its highest level since March.

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Central banks outside the U.S. continued to lean hawkish, and European rate volatility rose alongside the U.S. The ECB raised its key rates by another 25 bps in September, lifting the deposit rate to 2.50%, with markets pricing additional hikes ahead. The Bank of England held its policy rate at 3.75%, though three members again voted for a hike. European sovereign yields climbed to multi-year highs, with the 10-year German Bund yield reaching roughly 3.5% and 30-year UK Gilt yields approaching 6%. Fiscal and political risk premia also resurfaced, as French yields rose to their highest level since 2008 and Italian spreads over Bunds widened meaningfully late in the quarter.

High-yield bonds declined in the third quarter, with the asset class down 1.8% as rising Treasury yields outweighed carry, though shorter-duration bonds cushioned losses relative to investment-grade corporates, which fell 3.9%. High-yield option-adjusted spreads (OAS) ended September at 3.12%, up 37 bps quarter to date, with most of the widening occurring in the final week of September and concentrated in CCC-rated credits. All-in yields above 8% offer a more attractive starting point for forward returns, but spreads remain tight by longer-term standards and leave limited cushion for a deterioration in fundamentals.

Bank loans were the standout in public credit, returning 1.9% as floating-rate coupons reset higher. A rebound in collateralized loan obligation (CLO) issuance lifted demand while net new supply remained limited, and the index spread-to-maturity tightened 10 bps to 427 bps. Software loans led the rebound, returning 4.9% for the quarter, though the sector remains negative year to date with an average bid near 88, versus roughly 97 for the rest of the market. Beneath the surface, dispersion widened: CCC loans lost 2.6% while single-Bs gained 2.5%, and the share of loans priced below 80 edged up to 7.0%.

REAL ASSETS

Real Estate Recovery Stalls Amid Higher Interest Rates, While Geopolitics Drives Volatility in Energy Markets.

U.S. Real Estate Investment Trusts (REITs) declined in the third quarter of 2026, reversing strong performance earlier in the year. Investors shifted their focus to the impact of higher interest rates on property values after the Fed's September rate hike and suggestion it may raise rates again in the fourth quarter to combat higher inflation. All REIT property sectors posted negative returns during the quarter, with timber REITs showing the sharpest declines due to their ties to the housing sector, which was expected to be negatively impacted by higher mortgage rates. Gaming stocks also underperformed, in part due to competition from growth in digital gaming, which reduced traffic at physical casinos. Conversely, healthcare REITs outperformed on a relative basis, as their businesses are viewed as more resilient to higher interest rates. REIT take-private transactions slowed in the third quarter compared to earlier in the year, as REIT discounts to private market valuations narrowed. While real estate fundamentals have stabilized after the downturn that began four years ago, sentiment turned cautious in the third quarter, in the wake of higher interest rates. For the quarter, Global REITs posted returns in line with U.S. REITs.

All REIT property sectors posted negative returns during the quarter, with timber REITs showing the sharpest declines due to their ties to the housing sector.

Within publicly listed real estate, dispersion among property types continues to characterize the market year to date, with some sectors proving more resilient amid emerging headwinds. Diminishing public-private valuation spreads will likely lead to fewer privatizations through the fourth quarter.

Oil prices rose sharply during the third quarter as a tentative agreement in June to resolve the war with Iran deteriorated with ongoing attacks on ships in the Strait of Hormuz and pipeline infrastructure in the Middle East. As a result, oil prices rose to approximately $100/barrel before pulling back in late September on renewed speculation of a resolution to the conflict. Flare-ups continued into the fourth quarter, however, pushing oil prices higher. While shipping traffic stabilized in September, a full normalization of the energy supply chain is expected to extend well into 2027. U.S. oil production remained at record highs of just under 14 million barrels per day, and the U.S. rig count rose during the quarter, according to Baker Hughes. Natural gas prices declined for the quarter and year to date due to strong supply growth. While the Middle East conflict led to global natural gas supply disruptions, the U.S. was largely unaffected due to its abundant domestic supplies.

Geopolitical events, particularly the Middle East conflict and the Russia/Ukraine war, continue to drive volatility in energy markets, with no signs of abating and are likely to persist through year-end. The result will likely be higher inflation and rising interest rates, which could create headwinds in the global economy.

DIVERSIFYING STRATEGIES

A Mixed Quarter for Hedge Funds

Hedge funds, as measured by the HFRI Fund Weighted Composite Index, were broadly flat during the quarter. Year-to-date returns, however, remained strong.

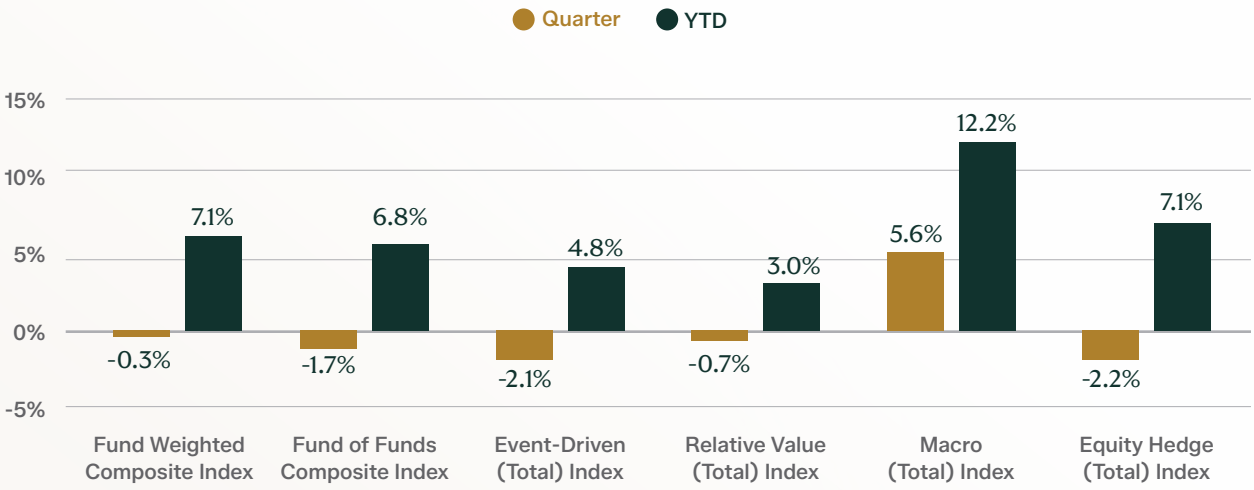
Macro posted strong gains, benefiting from both commodity and currency trading amid central bank activity. Systematic strategies outperformed their discretionary counterparts.

Relative value was slightly down, as losses in sovereign bonds, corporate credit, and convertible arbitrage outweighed gains from asset-backed and volatility managers.

Equity hedge returns were negative with losses in healthcare and biotech, technology, and energy specialists. Fundamental strategies fell, while quantitative strategies were modestly down, and equity market neutral posted gains.

Event-driven strategies posted losses, driven by declines in special situations and stressed strategies. Activist and credit arbitrage strategies were also slightly down, while merger arbitrage was positive.

HFRI INDICES PERFORMANCE RETURNS IN U.S. DOLLARS



Source: Hedge Fund Research. Data as of 9/30/26.

PRIVATE MARKETS

Some Signs of Life, but No Definitive Turn

The private capital markets tend to move slowly, then suddenly and are situationally dependent. The third quarter experienced a modest rebound in exit activity though realizations were concentrated with the largest companies. Higher interest rates continue to be a headwind as they increase the financing costs of acquisitions. The strong public equity market has given some strategic acquirers the confidence to seek assets that could drive value.

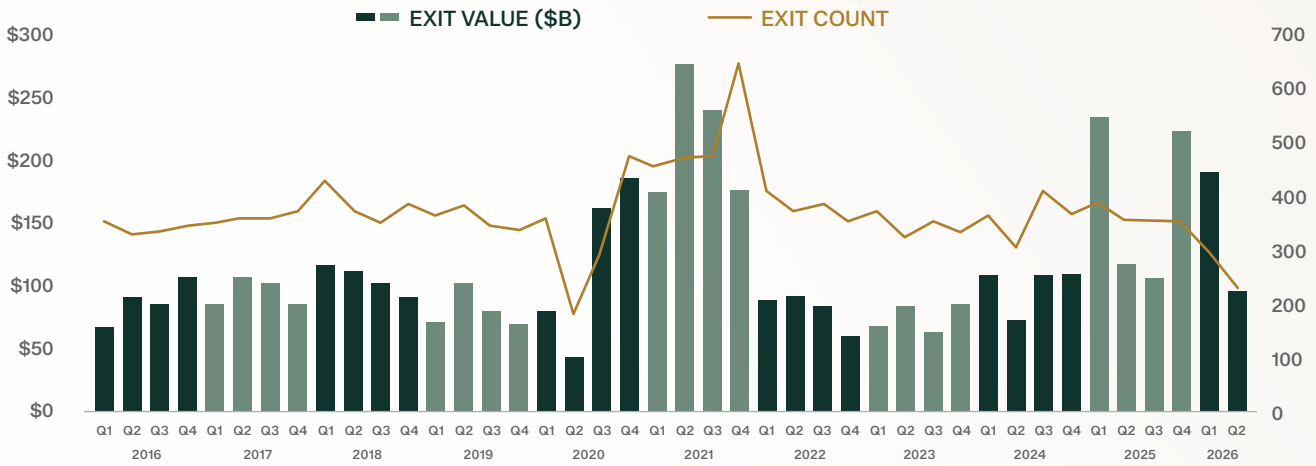
According to PitchBook, private equity investment activity rose in the third quarter after deal value reached its lowest point since 2023 during the second quarter. Deal value rose 21% while the number of deals rose 6%, reflecting a rise in the average deal value. It is worth remembering that the abnormally low second quarter was affected by the so-called "SaaS-pocalypse" that occurred earlier this year and the associated concerns about valuations and technology obsolescence in the face of AI-driven themes.

Private equity exit value rose 50% during the third quarter compared to the second quarter. Exit activity was still driven by a smaller number of large transactions. Transactions can be uneven over the short term, so one quarter does not make a trend. Looking ahead, higher financing costs will likely put pressure on realization activity. Sponsors still struggle with bid-ask spreads for assets in the current environment. Exit activity was driven by publicly traded strategics, which saw a 136% quarter-over-quarter increase.

AI continues to disrupt the technology sector in numerous ways. Legacy venture- and growth equity-backed technology companies are rapidly adopting and implementing AI solutions into their product suite. New native-AI companies are growing significantly and garnering high valuations. Technology innovation will create opportunities for the survivors to generate strong returns while leaving those companies that fail to adapt struggling to survive. In aggregate, valuations rose for venture-backed companies. Credit funds continue to pull back from the sector over concerns about growing losses. Direct lending deal count was up modestly in the third quarter but was well off the levels experienced in 2024 and 2025.

Exits from private energy companies and power generation assets rose for the second consecutive quarter. PE firms sought to trade assets benefiting from higher energy prices and rising demand for power driven by data centers.

U.S. PRIVATE EQUITY EXIT ACTIVITY



Source: PitchBook, as of 6/30/26.

PRIVATE EQUITY

Capital Concentrates as Liquidity Remains Constrained

Buyout

Buyout fundraising remains challenging as limited liquidity continues to constrain limited partner (LP) budgets. U.S. private equity managers raised roughly $160 billion across 223 funds during the first half of 2026. This is roughly in line with the pace of fundraising in 2025, when managers raised $308 billion for the full year. Capital remains concentrated among larger, established managers. Funds below $1 billion accounted for only 16.7% of commitments. First-time and emerging managers continue to face a difficult fundraising environment.

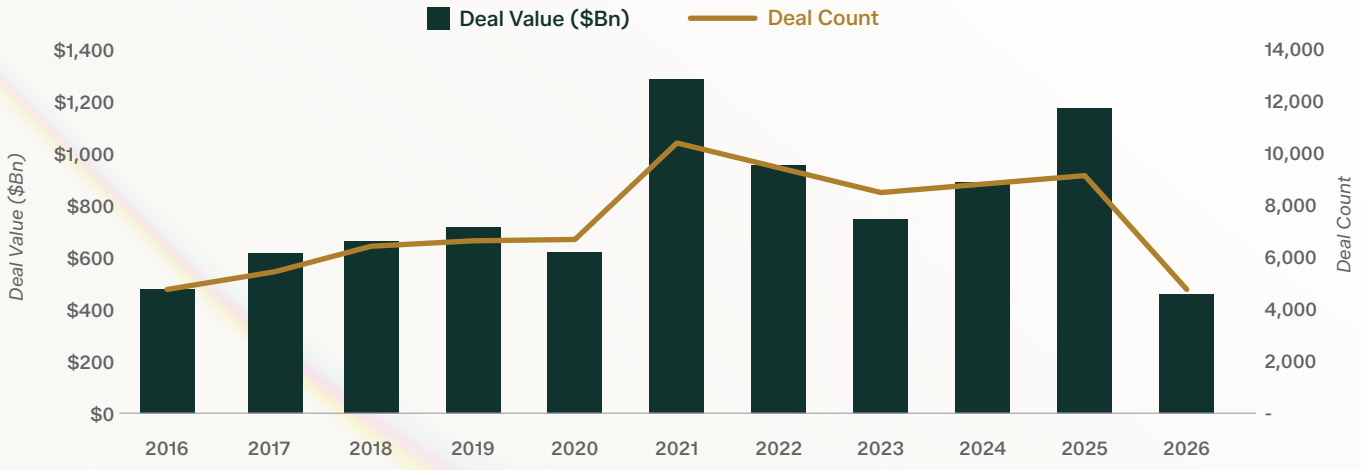
Deal activity slowed in Q2 after a stronger start to the year. Sponsors completed roughly 2,384 transactions totaling $177 billion during the quarter. First-half deal value reached $461 billion. Deal count remained relatively stable, but activity shifted toward smaller transactions as large-cap and take-private activity declined. Higher interest rates, wider credit spreads, inflation, and geopolitical uncertainty weighed on activity. AI disruption also created greater uncertainty around software investments. Add-ons represented roughly three-quarters of buyout transactions, while new platform activity declined.

Liquidity remained a key challenge. Q2 exit value fell to approximately $103 billion across 353 exits, down 46% from Q1. First-half exit value totaled approximately $294 billion. Exit activity remained concentrated in larger transactions. The initial public offering (IPO) market showed some improvement, but the reopening remains narrow.

We continue to favor buyout managers with strong operational capabilities and disciplined entry valuations. Higher financing costs and less potential for multiple expansion increase the importance of revenue growth and margin improvement. Managers who can create value through operating improvements should be better positioned in the current environment.

U.S. BUYOUT FUNDRAISING ACTIVITY ($Bn) BY YEAR

Data as of June 30, 2026



Data source: FEG; PitchBook "Q2 2026 US Private Equity Breakdown"; Most recent data available.

Venture Capital

Venture capital (VC) fundraising has improved, but capital remains concentrated among large, established managers. U.S. VC funds raised $72.4 billion across 405 funds during H1 2026, nearly matching the $74.9 billion raised during all of 2025. Funds of $1 billion or more accounted for $49.5 billion of the H1 total. Three managers—Andreessen Horowitz (a16z), Founders Fund, and Thrive Capital—accounted for 48.1% of all capital raised.

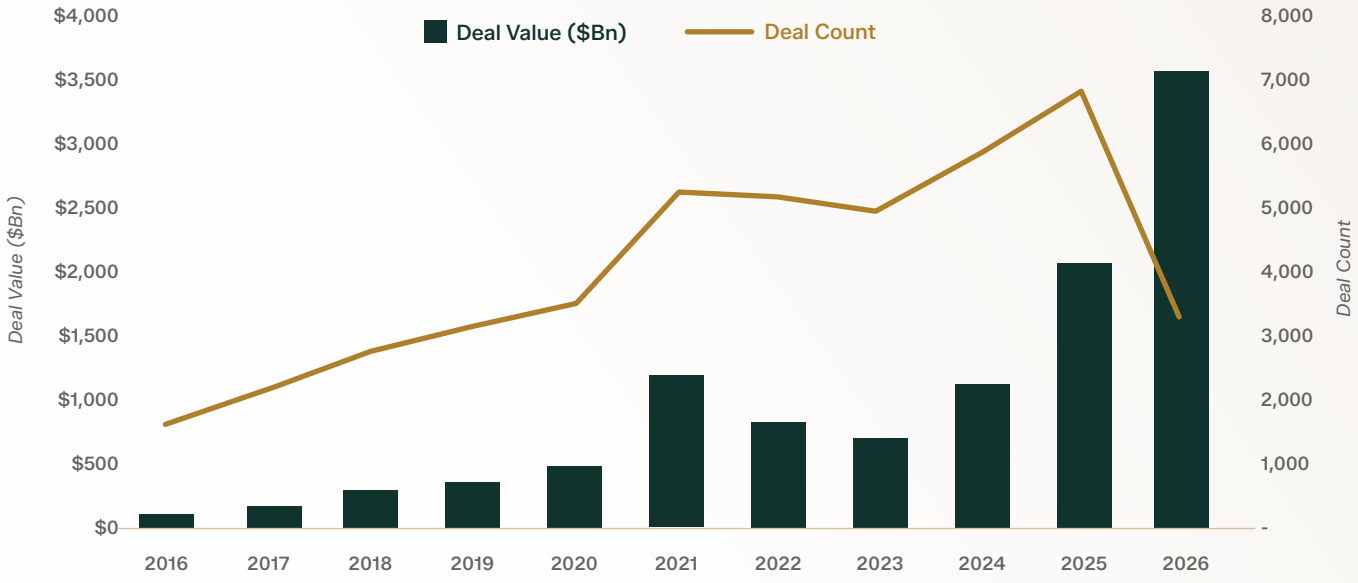
Deal activity also increased but remained heavily concentrated in AI themes. U.S. venture investment reached $412.7 billion across an estimated 9,646 deals during H1 2026. This was nearly 30% above the total deal value for all of 2025. AI accounted for 86% of deal value and 43% of deal count. Megadeals of $100 million or more represented 87.5% of total capital invested. Outside of large AI financings, investment activity remains more selective.

Exit activity improved, but broader liquidity remained constrained. Large public listings, including SpaceX, and acquisitions, including xAI, have driven significant headline exit value. However, exit activity remains concentrated in a small number of companies and has not yet translated into broad distributions to LPs. Exit options remain limited for many venture-backed companies.

We remain selective in venture capital. We favor high-conviction managers with differentiated sourcing, disciplined underwriting, and strong execution. AI continues to drive a significant share of investment activity and valuations. This increases the importance of manager selection and entry discipline. We favor managers who can identify durable businesses and create long-term value across market and innovation cycles.

U.S. VC AI DEAL ACTIVITY ($Bn) BY YEAR

Data as of June 30, 2026



Data source: FEG; Pitchbook "Q2 2026 Pitchbook NVCA Venture Monitor Summary"; Most recent data available.

PRIVATE DEBT

Stabilization Amid Selective Stress

Private credit markets showed signs of stabilization in the third quarter of 2026. Redemption requests at non-traded Business Development Companies (BDCs) eased at several of the largest platforms, suggesting the retail-driven outflow cycle that began earlier in the year is moderating. Institutional appetite remained strong, with U.S. private debt fundraising running ahead of last year's pace. New deployment was subdued, as direct lending volume backing leveraged buyouts totaled $10.7 billion. Competition from the broadly syndicated loan market increased, with a record $16 billion of direct lending loans refinanced into the syndicated market. Competition for higher-quality, non-software borrowers has also pushed spreads modestly tighter.[1]

Fundamentals remained broadly stable through the second quarter, with stress concentrated in identifiable pockets rather than spreading across portfolios. Among the largest BDCs, roughly 86% of debt remained marked at or above 95% of cost. Weakness clustered in second-lien software loans, where nearly two-thirds of exposure is marked below 80 and three borrowers account for most of the distress.[2] Pressure has also been more pronounced among the smallest borrowers and among buyouts made in 2021 and 2022 at peak valuations.

FEG favors strategically allocating to institutional private lending strategies to exploit the persistent illiquidity premium. If conditions weaken further, a broader distressed opportunity set could emerge, supporting both private lenders and distressed managers.

[1] ***Source: PitchBook.*** *Data as of 9/30/2026.*
[2] ***Source: PitchBook.*** *Data as of 6/30/2026.*

PRIVATE REAL ASSETS

Private Real Estate Values Stabilize While Distress Persists Among Multiple Regions and Property Types

Private market real estate values showed a slight increase in the second quarter of 2026 (the latest available data). According to the NCREIF Property Index, real estate values rose 1.3%, once again led by retail and senior housing properties, continuing the trend of prior quarters. Retail continues to benefit from strong consumer spending and limited new supply relative to other property types, while senior housing continues to attract capital due to strong demographic trends.

By contrast, the office sector lagged due to weaker fundamentals, with occupancy in many markets failing to reach pre-pandemic levels. Nevertheless, some tech-driven office markets, like San Francisco, have seen significant improvement. Fundraising remains challenging, with timelines often extending over 18 months.

Distressed opportunities in private real estate largely stem from banks and property owners finally relinquishing properties to buyers with fresh capital after years of extensions. The key challenge for private real estate is its performance relative to other asset classes over the past four years, which has led investors to reduce their allocations. Renewed concerns about higher interest rates have also led to lower allocations.

Tentative Agreement to End Middle East Conflict Calms Energy Markets

Geopolitical factors dominated energy markets during the third quarter, as the war in Iran led to persistent supply disruption. A cease-fire between the U.S. and Iran in June calling for an end to the conflict and a reopening of the Strait of Hormuz quickly deteriorated. Oil prices topped $100/barrel, and skyrocketing global diesel prices, a key input into transportation and shipping, led to concerns about rising inflation and the prospect of more interest rate increases.

Upstream energy saw multiple exits by private energy funds during the quarter, notably the announcement that EnCap would sell assets to Matador Resources. Three of the largest private equity energy firms (Quantum, EnCap, and Natural Gas Partners) are in the market seeking to raise multi-billion dollar funds on the back of strong returns over the past five years.

Expectations for a real estate recovery were tempered in the third quarter, with positive sentiment fading in listed real estate securities, a trend that could ultimately spill over into private real estate valuations. Market and property type selection will be key factors driving performance for real estate investors, along with the ability to increase net operating income amid a rising interest rate environment. Fundraising for private real estate, however, remains challenging, with many funds taking 18–24 months to raise capital, given the overhang of lackluster performance for fund vintages deployed at the top of the market.

Access to power has emerged as a key factor in the large technology companies' buildout of AI infrastructure, all of which have announced aggressive capital expenditure plans for 2026. Increased power demand, along with growth in LNG exports, however, has failed to drive higher natural gas prices. Other basic inputs into data center construction (copper, aluminum, steel) are also poised to benefit from the ongoing AI infrastructure buildout. A renewed focus on energy security in the wake of geopolitical conflicts is beginning to drive greater investor interest in private energy strategies in the second half of the year.

LOOKING AHEAD

Breadth of Active Risk

Our view coming into the year was "party in moderation." By this we meant that leaning slightly overweight equities at the expense of fixed income was the right posture for 2026. By mid-year we went further underweight fixed income, tactically in favor of either diversifying strategies or real assets depending on the strategic asset allocation outlined in client policy statements. To date, these moves have largely been beneficial, but we continually monitor market conditions and will make changes to positions if we believe it prudent to do so.

Equities and real assets provide exposure to the positive fundamentals and earnings backdrop, as well as exposure to AI-driven growth. That has generally been a good thing, and we are keeping a close watch on frontier AI lab revenue and the return on invested capital of the hyperscalers' capex for signs of where the economy and earnings are headed. Diversifying strategies provide a reasonable return stream, in our view, that is not too highly correlated to traditional asset classes, interest rates, or the AI theme, and sources of uncorrelated return have greater appeal in the current market environment where AI is creeping into most asset classes.

It bears repeating that we continue to take most of our active risk from manager selection, which complements our tactical views to drive results. One of the tenets of our investment philosophy is breadth of active risk. We want to have lots of shots on goal, such that any one investment decision cannot make or break our results. This means we are not only looking for best-in-class managers but also spend a great deal of time considering things such as position sizing and the complementarity of managers we select. We also consider total portfolio exposures to traditional factors like growth and value, as well as new factors driving markets like AI winners and losers. While we are long-term investors, we engage with markets and the portfolio every day so we can navigate short-term volatility and stay on target for meeting long-term objectives.



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The S&P 500 Index is a capitalization-weighted index of 500 stocks. The S&P 500 Index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.

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All data is as of September 30, 2026 unless otherwise noted.

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