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Endowment & Foundation Investment Outlook Webinar

James Stenstrom: Welcome. Welcome CAPTRUST clients. Super excited that all of you are able to join us this afternoon for our endowment and foundation investment outlook. Super excited to be joined by some of the senior investment professionals here at CAPTRUST to share some of the things we're thinking about and looking at as we move throughout 2026.

So just a couple of housekeeping notes as we get started. All of you are on listen-only mode. However, you do have the ability to type questions into the chat box, and I think all of us are looking forward to that part of the conversation because it'll keep people on their toes a little bit, and obviously we want this time to be meaningful to all of you and really touch on questions and concerns that you may have.

Also feel free to turn on closed captioning if that makes the conversation more accessible for you. So joining me today we have Mike Vogelsang, our chief investment officer; Kevin Van Buskirk, who leads our in- alternative investment due diligence, including private markets; Jim Underwood, senior director of portfolio management; and myself James Stenstrom, who leads the OCIO practice here at CAPTRUST, also moonlight as a panel host- Nice

if this goes poorly. Will be the first and only time I'm doing this. All of you are getting a chance to hear from us today, but included in the link when you get this in terms of the recording there'll be an opportunity for us to hear from you. So our annual endowment and foundation survey, the link will be going out.

It's live now. It's the one opportunity we have a year to really kinda systematically understand what's going on in the ma- the mind of endowment and foundation professionals and board members. So really excited to, to learn from all of you in terms of what you're doing, what you're thinking, and be able to share that back and provide some perspective on the back end in terms of what's going on with your peers and what they're particularly mindful of.

So with that, I'll turn it over to Mike to really highlight what thematically we're gonna be discussing today.

Mike Vogelzang: Yeah, thanks, James. Y- y- you could also look at us as four guys in blue sport coats, but, that I think that sh- that show's already taken. We've entitled our talk and discussion today A Wider Array of Outcomes.

We just feel like the market, given our alternative in, or, I'm sorry, artificial intelligence the market of that's being impacted by the political dynamic, the geopolitical dynamics of the Iran war the new chairman at the Federal Reserve, all of these things are swirling, making lots of noise.

And w- it feels to us like there's just simply a wider array of outcomes in the investment markets than may be normal. So with that, let's take a look at the first slide. And we're gonna be going through slides. We're gonna be chatting amongst ourselves as well we hope you s- you stick with us.

And again, jot those questions down as you as you receive them and remember them, and we'll be coming back to them at the end of the, end of our time together. So we really like this graphic. There's this idea in human psychology of what's called the end of history.

That is, where we are today is the last period of h- of history that the sorta path we've gotten here on the left side of this graphic the path we've gotten to here is actually been sorta preordained. And we all actually know intellectually there's lots of paths we could have used to get here.

And the green one on this particular idea is the one that we took. So now we're sitting at this middle point, and we have this enormous array of optionality in front of us. What might happen with AI? What might happen with elections? What might happen with the war in Iran? And every one of these paths are open for the market participants.

By the way, it's also an interesting way to think about your own personal life, right? As you're raising children, as you're thinking about mentoring other people, as you're thinking about your own career, where might you be going with all of these different choices in front of you? So it's an interesting way to think about how the future can unfold.

And we, today, we think, as we said, that the array of outcomes is substantially wider than normal. The next slide shows a- another way to think about that. In our business, in a very real sense, we are, all of us up here, risk managers. We

think about how to maximize our portfolio returns with a minimum of risk, so we think about risk and risk space all the time.

On the left side of this graph, you see this, a typical risk profile. We don't know the outcome, but we generally know what the distribution of those outcomes may be, right? We may end up somewhere in the left tail or the right tail. We may end up somewhere near the median. But generally, outcomes in the investment markets are often distributed fairly normally.

In a period of uncertainty, however- You can see that not only are the outcomes unknown, but the distribution of potential outcomes are also unknown. And it feels a little bit like that. It's quite unsettling actually to not know where we might end up as we move through time for the balance of 2026, and particularly with the impact of artificial intelligence, where we might end up in the next three, four, five years.

So with that we'll take a look at the next slide and give you a little inside view of what's going on in our investment committee. In the IC, we talk about lots of different topics. Usually, a couple of things bubble up to the surface, and we focus on those. Today, we feel like there's just a larger number than normal, and we're just gonna walk through these selectively with you.

So the first is really the geopolitical landscape. The second is the impact of artificial intelligence. What might AI actually do to, to the world, to corporate profits, to the market, to the economy, to labor, et cetera? And then the monetary and fiscal policy uncertainty that we're entering today.

The fourth one is interesting. It's this IPO tsunami. We have a... There's an event moving down the calendar towards us that frankly nobody's ever seen before, and we're gonna talk a little bit about that. And then also we're gonna take a look at private credit. Private credit has been a source of much consternation over the last few months, and Kevin is a super expert on what's going on there, and hopefully we'll dive into that a little bit and answer some questions we might have.

So with that, why don't we jump into the political landscape?

Jim Underwood: Thanks, Mike. I think just about any one of these subjects we could have an entire webinar over, so we're gonna have to move fairly quickly. But again we certainly encourage those questions to come to us. And we'll go as deep as we need to on just about any of these subjects.

We have no crystal ball on the outlook of the war in Iran. We don't know what's going to ultimately happen. I think most of our investment committee discussions really surround are what are gonna be the potential longer term implications of these, of this event? And generally, we think most of the longer term implications are gonna surround some type of energy policy.

I would argue over the last 30 years, most energy policies have fallen into one of three categories: energy sustainability, energy affordability, and energy security. And I think over the next 10 years, you're gonna see a much larger shift towards policies that really emphasize energy security, and that's gonna be a very meaningful impact to the overall global economy.

What this chart shows you effectively is, which areas of the world are going to be supported by changes in potential energy supply dis- chains. N- North America, for example, we're basically balanced. We consume about as much as we produce. Europe and Asia are really out of balance, meaning that they pr- consume a lot more than they produce.

And then obviously the Middle East and- is the area where it's supplying most of the energy capacity outside of that region, which is why it's been so disruptive from a sy- s- po- from a energy perspective and the risks that everybody's concerning.

Mike Vogelzang: Hey Jim, can I ask you a question?

Sure. So if the emphasis is shifting from affordability of energy, how cheap prices are at the pump, m- to more energy security for countries, does that imply a higher price for longer, I guess is the natural question?

Jim Underwood: Yeah. I, and I think that obviously the next slide will g- give us that, and that is a lot of our conversations at the investing committee says we argue that there's going to be a higher energy cost curve going forward.

What this chart shows you is what market expectations for oil prices were going to be at different points over the last this since... This is since April just before the war started. So effectively right before the war started, people are expecting December of thir- of 2026 oil prices would be somewhere in the neighborhood of \$65 a barrel at the end of the year.

It shifted up to \$70 a barrel. It shifted up again, \$80 a barrel. Now we're sitting at \$90 a barrel. And again, this is what we mean by a higher energy cost curve, and when you combine it with the previous slide, it really shows us what areas

of the market are vulnerable, meaning Europe and Japan and the f- the Asia markets, because they're importing a lot more energy resources from us from foreign sources, whereas other areas may be a little bit more insulated.

And I always, being the portfolio manager like to understand what are the portfolio management implications for these types of events? And the most obvious is, from a regional country allocation perspective, how are we thinking about portfolios? Clearly Europe, we think has challenges.

And to give you a little bit of a backstory Europe- the European financial markets are very cyclical in nature, meaning they rely on top-down growth from an overall economic perspective to generate profits. That's the reason why they're very cheap. We were somewhat optimistic middle of last year that generally over the last decade, they've survived by cheap energy from Russia, cheap goods and services from China, and cheap defense from the United States.

All three legs of those stool have been ripped out from under them. And as a result, we thought policymakers were going to have to be forced to to implement some pro-growth policies which would be very supportive of their economy. I would say our enthusiasm and confidence in that has diminished, one, because of the energy needs that they're going to have.

And then the other is because the central bank in Europe- Has one mandate, whereas the United States has a dual mandate of both inflation and, or s- price stability and unemployment. The European Central Bank only focuses on inflation. And so that single mandate, I think, is gonna become a challenge for the European economy.

So that's one thing that we're actively reviewing within portfolios, our exit- our exposure to Europe. I mentioned earlier the Asian part of the market is also gonna be severely affected. But we actually think there's some structural reasons why Japan actually has some continued support underneath it mainly because they did pass some pretty aggressive corporate reform structure.

And oh, by the way the government of Japan owns about half the public market. So again, reasons why we think there's areas outside the US, but clearly that's going to be the biggest investment implication in investments outside the US.

Mike Vogelzang: Just looking at this slide, Jim, I... the, my takeaway is that, back at the beginning of the year in January, the 20- the December 27, December 2027 price of oil was expected to be around 65 or \$70 a barrel.

Jim Underwood: 2026.

Mike Vogelzang: 20... No, but even '27. Oh yeah.

Jim Underwood: And-

Mike Vogelzang: And now that same price is expected to be somewhere around \$80 a barrel. And what impact does that have on inflation, on corporate profitability, on life in Europe, et cetera, et cetera? Europe is a great example, by the way, of that ration- or the hierarchy that you laid out.

Europe seems to have prioritized the sustainability of energy as opposed to the affordability of energy versus the security of energy. That's right. And it's just different sort of policy choices that they've

Jim Underwood: made. But clearly this is the most immediate certainly top of mind, and gonna have the biggest impact near term.

But going forward, I think the next subject that Mike's gonna cover is gonna be artificial intelligence which it clearly has the bigger upside long-term opportunity.

Mike Vogelzang: The joke, of course, is that, that o- Mike only has artificial intelligence, nothing native. So let's take a look at that.

There's all kinds of stories around AI and its impact on potential markets, impact on society at large, frankly, and unemployment and on, the job market for young people particularly is quite fraught today. Try to back up to, say, 40,000 feet and take a look at this chart.

We like this a lot. This is brought to us by the Federal Reserve Bank of Dallas. And it is probably the most impactful chart that you can think of over the last 150-plus years. So the light blue line here, the squiggly blue line that moves from bottom left to top right is real, that is after inflation, GDP per capita around the globe.

So it's every person on earth, how much gross domestic product, how much output is each person on the planet producing? And that number has grown, which is the orange line here, at 1.9% per year for 150 years. So it can, it, a wonderful-- We wouldn't have all of the things we have, the electricity to fire up these cameras or these lights, or our cars, or the medicine that we have, or any

of the conveniences of modern life if it wasn't for this 1.9% growth per year, right?

So an incredible statistic. We like charts that go from bottom left to top right. That's what we like in the investment markets, right? So the folks at the Dallas Fed have said, "Okay, what might, for the next decade, what might AI actually do to increase that real GDP per capita?"

And they came back with a rate of 2.1% for the next decade, right? Not a lot at least seemingly, going from 1.9 to 2.1, but think of that as a 10 or 11% increase in the rate of growth, and suddenly it starts to carry a parity, fairly large impact. So the first question is what has 1.9% brought us over the last 150 years?

It's brought us infant mortality down by about 90%. It's brought us almost universal education and universal literacy around the globe. It's extended life. It's brought us medicines that we never had before. It, it means most people around the country are getting four squares a day not, right? Food is not nearly the scarcity.

We don't have famines anymore almost anywhere in the globe. 1.9's brought us a lot, and so the question is what does 2.1 bring us? And is that even understated? Might we get even a bigger acceleration? AI has a, has an enormous power to impact our lives as we go forward. What the CADs at the Dallas Fed also decided to put on are a couple of these other lines.

The one that moves up and to the left is what they call the benign scenario. We call the age of abundance. So that is AI transforms our world. Our productivity, the GDP per capita, goes up tremendously. Goes up to 4 or 5% a year, 7% a year, and suddenly education is free, energy is free, right? Nobody has to work if they don't want to.

Food is free, effectively. Housing. The, you get this age of abundance where everybody's wealthy, right? That's an incredible opportunity and incredibly unlikely, frankly, at least for a while. Of course, the opposite end of that is what we've labeled the terminator scenario, which is the movie by Arnold Schwarzenegger, The Terminator, where humans end up extinct.

That's the best example of the widest array of outcomes we can possibly imagine. So that's, that, that's some of the things that we're wrestling with.

Jim Underwood: So- I would say that chart illustrates uncertainty better than just about any slide we can put together.

Mike Vogelzang: It's in some ways incredibly consistent.

Look at that orange line. Look at that light blue line for just a second. You see the 1929 market crash and the 30, 1930s global depression. World War II dragging that blue line above trend, and then back to trend. But other than that, the trend has been really stable- And yet now we have this incredibly wide array of outcomes.

So anyway, fascinating stuff, and it really impactful, I think, as we go forward. So let's take a look at the next slide. This is back to our favorite slide here, I think. Okay, here we go. Where we have this idea that- that's really colors our investment strategies at CAPTRUST, and that is this concentration or idea of preparing for markets as opposed to predicting outcomes.

AI's one of those. And just in February, we saw a wild array of articles and counter articles and rebuttals in the press. Perhaps you saw some of them. We can give them to you if you'd like. The first one was written by a guy named Matt Schumer. He wrote something, Something Big Is Happening, and his basic premise was that no matter how fast you think AI is coming, it's coming faster.

And then and right after that, a group ca- that heretofore really unknown, a group called Citrini Research wrote an article that just absolutely hit the public cons- cer- the public consciousness really with a hammer. And that was this idea of a deflationary scenario with AI, that AI could actually cause a jobless economy.

While the economy and the stock market continue to hit new highs, nobody's working, and so we have this deflationary cycle of this doom loop of AI. It was amazing to see the popular press hit with these couple of different outcomes.

Jim Underwood: I think the, what was most fascinating is the really optimistic view really didn't make a move in the markets.

The Citrini piece, even though nobody had really ever heard of the research firm, had a major impact- Yeah ... which from a portfolio management perspective made me pause and say, "Most portfolios are not prepared for a deflationary environment." And quite frankly, in that scenario, Main Street will further be pitted against Wall Street.

Yeah. And I think it becomes a very- Yeah ... significant policy risk. So it opened my eyes and made me forced to look at some strategies that we really haven't had to consider for the last 30 years quite frankly to make sure our

portfolios were at least, not that we think that option's gonna happen, but we wanna be prepared if it were.

Mike Vogelzang: Yeah, the lanterns and pitchforks are coming, right? We've already seen it with a couple of executives in AI. But yeah, the, again, this is this wide range of outcomes and it's really impossible to say. And so how do you as an investor as we think about how to build portfolios how do we build resilient portfolios that get through this kind of uncertainty and yet You know, allow our clients to prosper, pursue their mission, and fulfill the objectives that they have, and that's really what weighs on us.

Let's take a look at the next slide. So AI spending is accelerating, and by the way, Jim's point about the Citrini piece pushing the market down, I think it tells you what the market's priced for, right? The market's pricing in a much rosier scenario for AI than the doom loop scenario from Citrini.

And I think that's a risk in the market. If things continue to move nicely and continue up, I think we'll be okay. One of the causes for concern in the market is this slide, and this is... We've all heard that, that, the hyperscalers, and I think this is Microsoft, Meta, Alphabet, and Amazon, so think Google and Amazon Meta or Facebook, and Microsoft are spending.

They're considered the hyperscalers. That is, they're building the guts of AI, the large language models and so on. Their profitability is exploding. You can see that in a... With that, all that profitability, they're spending it all. That's the dark blue line here. Their CapEx, their capital expenditure growth, is soaring 70% this coming year, and their free cash flow, in other words, their earnings after all their CapEx, is actually beginning to shrink, and that's a s- that's something that Wall Street has really been paying attention to the first part of this year that was actually negative for those stocks, right?

We saw the Mag 7 or the biggest names in technology actually sell off while some other companies did pretty well. Let's take a look at the next slide.

Kevin Van Buskirk: Mike, r- real quick before we jump- Yeah ... to the next slide, I think something on this slide that, that strikes me a little bit on the private market side is how much the public markets are starting to bleed into the private side.

We see this very frequently with a lot of these public companies now are making equity commitments to private companies, and it's becoming a larger

portion of the growth in some of these public companies. So when you look at earnings, a li- a larger part of it are those companies.

If you look at Facebook and Alphabet, for example, they have investments in Anthropic. That was written up quite a bit over the last four quarters, and you're starting to see that impact the performance of these companies, which maybe, this slide isn't getting to yet on that kind of cash flow growth.

Mike Vogelzang: Yeah, that the sort of circular ownership is the idea of- ... "Hey, we'll buy Nvidia chips. If Nvidia invests in us, we'll use the Nvidia money to buy Nvidia's chips." Wait, is that real sales? It- That, that, that cyclical or circ- circularity of cash flow in these industries is really, is another reason for concern.

All right. We're gonna keep moving. We got a lot to cover. So the next slide is showing that a lot of folks have asked, "Is 2026 just another version of 1998 and 1999?" Where technology was booming, everybody was worried about, frankly, nobody was worried about a bubble. Today, everybody seems to be worried about a bubble.

On the left side of this page, I think it's really important to point out why this is different. Why today it's different. The dark blue area chart is the S&P 500 since two thousand and eleven. You can see it's up and to the right, one of those beautiful charts we like in our business. The gold line is a twelve-month operating margin.

That's on the right-hand scale here. So you can see back in two thousand and eleven, the operating margin for the S&P 500 was about fifteen percent. Today, it's over twenty and going higher. So the profitability underneath the S&P 500 is what's driving the price higher. So yeah, the market's a bit expensive, but it's not anywhere nearly as expensive as it was on profits and so on, as it was in nineteen ninety-nine, nineteen ninety-eight.

You can see the right-hand side capital spending growth. I won't spend a lot of time here, but needless to say the hyperscalers, again, Microsoft, Google, Meta, these were all incredible businesses because they were growing their earnings. They were at scales we've never seen before, and they didn't have any capital expenditures.

They were asset light. They didn't have to build a big factory like General Motors did or build huge warehouse-- build huge factories that built turbines like General Electric does. They just made software. So they had this wonderful

opportunity to make tons of money. That's changing today as they're investing more in capital expenditures.

So something we're watching very carefully and worried about a little bit. Next slide. We'll see some of the price action that's been going on underneath here. So stay on the left-hand side of the page with me on this one. This was the first quarter of this year. You can see that energy led the way in the performance derby up thirty-eight percent.

No big surprise given the Ukraine war and the Iran war, all the disruption in the Middle East, particularly the Strait of Hormuz. Oil prices went through the roof, and of course the stocks in those sectors did really well. We also saw materials and utilities do pretty well in the first quarter.

But look what didn't do well. Consumer discretionary, which by the way is Amazon. Technology, which we all know about, and consumer services, which are really Meta and Google all were down this quarter. So you had, you had-- If you were looking to buy these things, if you were looking to add your-- add to your exposure, you had an opportunity when the market was down four percent.

It was led by the biggest tech names. But if you waited more than a couple of days, it was too late. 'Cause look what's happened since April first. On the right-hand side of this page, technology is up thirty-two percent. I'll come back to the SOX index. The S&P is up thirteen, but almost everything else is up less than that, right?

Consumer services, utilities, energy is down nine percent. You could have won a bar bet with that one at the end of the-- beginning of the second quarter. Energy was up 38% in the first quarter, down 9% in the second. But look at the SOXX index. The SOXX index is really specifically from semiconductor companies.

So companies like Micron and AMD and Nvidia, people that make semiconductors. They were up 58% in about five weeks. It's a very tiny portion of the S&P 500. I think it's 7% without Nvidia, I think is the number. So 7% with Nvidia. And Nvidia, by the way, wasn't up that much. It was up double digits, but not a huge amount.

But things like Micron and AMD were up enormous amounts, and they- just that little thin sliver of the S&P 500 was up double and even triple digits in those first couple of- in the last five or six weeks, and as a result, dragged the

S&P 500 up 13%. So if you're in the game of trying to keep up with the S&P and you didn't own semiconductors, sorry, April was a tough month.

Jim Underwood: Yeah I read that only 22 stocks in the S&P 500 actually outperformed the S&P- ... over the last 30 days. One of the lowest levels we've ever seen.

Mike Vogelzang: Yeah, I think that's a 30-year record. Yeah, that, that's called not knowing the outcome with not knowing the distribution- ... when effectively 5% of the S&P 500 outperformed p- and 95% underperformed.

An enormously weird month of April. All right, let's take a look the next slide. This is just a re-repeat of what we already showed you, this idea of preparation versus prediction. This idea that AI could cause this massive productivity growth and sort of a, an age of abundance, or are we gonna head to the deflationary doom cycle?

The next slide is- shows you what it is we're watching. So we built a 36-month dashboard that sort of looks out 36 months. As an investment committee and said, "Okay, if we can plot the differences between, the age of abundance and hopefully not extinction but we can watch these things."

So some of the things we're watching that lag the market are what you see here, CPI, the GDP, unemployment rate. Those are all big numbers. They typically lag or are synchronous with the markets. But potential leading indicators on the right side are really important, and these are specifically focused on- How is AI driving shifts in the market?

So these are things like, are we seeing pricing pressure in contracts? Are contract durations happening? What about the cost curve per completed workflow? Are we seeing productivity growth? What about credit stress? Are we seeing credit stress popping up in particularly consumers? What about entry-level hiring?

It's always the canary in the coalmine if entry-level hiring is weakening. Fiscal policy tempo, wage compression, other things that are really real time telling us what's happening as as AI begins to unfold. So we're watching as best we can. Again it's hard to know what the distribution's gonna be.

But we think we think, we hope we have at least some insight into where we're headed.

James Stenstrom: Yeah, I think it's tough to have any insight into where you're headed if you don't know where you are. And so I think that's a really key component is identifying, hey, what are the forward-looking factors?

And trying to create, with such uncertainty across so many different things- Yeah ... try and create a framework to, to evaluate what we do know as opposed to just letting that, that wa- tsunami of uncertainty overwhelm the decision-making process. That's

Mike Vogelzang: exactly right.

Jim Underwood: All right. W- we're gonna speed up a little bit 'cause I know we, we-

we wanna make sure we have time for questions. We're gonna hit on monetary physical policy. Honestly, in any other year, this would likely be the top of the list because I think it's probably the most impactful longer term other than the AI story. But if you'll turn the slide effectively we, the big story is obviously the transition in the Fed chair position.

Clearly there's tremendous pressure on the new chairman to lower interest rates. There's a lot of questions about Fed independence. If you turn to the next slide we have low inf- low unemployment data. We've got high inflation data. I would argue both of these have uncertainty related to it.

We don't know how long inflation is gonna be influenced by high energy prices. We don't know how immigration has impacted the labor market data. We're gonna have to continue to evaluate those data outputs that come out every month under a under a lens that's continuing to change because of these uncertainties.

But when you put it all together, with new Fed chairman a real emphasis on having Fed independence by other parts of the Federal Reserve Board inflation running above target, u- unemployment somewhat questionable we would just argue that you put it all together and at least that's a formula for a potential policy error.

Again, to me, it's hard to predict what that policy error might be. And we're not saying they're going to make a policy error, it's just there's more moving parts that could likely lead to something going wrong from a policy perspective. And really from a portfolio perspective- The only thing that we really are focused on is we're not making a big duration bet here.

What we are looking at is exposure outside of 10 years. So any exposure we have to instruments that might be maturing 10 years from now, we wanna make sure we fully understand that, 'cause that's going to be the area of the yield curve that's gonna be most impacted by a policy error if we were to see one.

So-

Mike Vogelzang: Yeah, I think, Jim the expectations for rate cuts for this year were, I think, three or four rate cuts were expected by the end of the year- That's right ... earlier this first quarter. Today we're at basically flat. I don't think- Yep ... the market's- It's

Jim Underwood: a 65% chance of zero and a 30% chance of one rate hike.

Mike Vogelzang: One rate hike now. Wow. That's right. So yeah, we've seen the rate expectations for the federal funds rate anyway really turn around.

Jim Underwood: That's right.

Mike Vogelzang: Yeah. Let's go to the next topic. Th- this is, w- we're calling this the IPO tsunami. And let- let's go to the next slide. We'll try to move through this quickly.

But it's going to be catching a lot of attention this summer. You will be hearing about this if you're at the margin of markets, you're already starting to hear a little bit. But it's gonna be on the cover of every newspaper, every magazine, if those things even exist anymore. And that is this set of mega IPOs that are coming this fall.

SpaceX is gonna be the biggest one. We haven't seen anything really like it. OpenAI is right behind it. Anthropic is right behind that. We have a company called Databricks, which is almost as large as Anthropic, that's gonna be coming in. You already have a super concentrated market, and now we've got a bunch of really big dudes jumping into the small pond, right?

They're gonna jump in. A lot of water's gonna be displaced, and you're gonna see waves and ripples coming out of that for quite a while. So on the right-hand side of this page, I just wanna give you one sense of this. So let's say a company's worth \$1,000 and it comes public. Very often they, they list about, 200 about 100 to \$200 of their shares.

So 8- 80% of their shares stay private or stay in the hands of the owners. So 20% is what's called floating. SpaceX is the biggest company we've ever seen, second actually to Saudi Aramco but certainly the biggest tech company coming public. And only 3 to 5% of the entire company will be trading publicly.

What does that mean? It means everybody who wants some shares are gonna buy them regardless of the price. So it's setting the stage for a, even a bigger b-pop in this price of SpaceX. So these are really unprecedented ways to think about the IPO market. Take a look at the next slide.

This will give you some sense of it. We're trying to understand, as benchmark people, folks who worry and think about benchmarks all the time. We think about what this impact might have on benchmarks, and how the S&P, Standard & Poor's, might treat this differently in their benchmarks versus the Russell benchmarks, if you have those, and how these are gonna impact.

Each of them have different rules. They're all... Every company that's in this situation is lobbying these index companies, trying to get them to change the rules so they can be included more quickly. Some include it with float, some include it without. But you can see here, if SpaceX, Anthropic, and OpenAI each are between 1% and 3% of the S&P, those are the green bars on the left side.

By definition, the other large companies, Nvidia, Apple, Alphabet, Microsoft, Amazon, Broadcom, are all gonna shrink a little bit as a percentage, right? So think about the n- noise that's gonna be going on inside of those benchmarks. So something to be aware of this summer. We're working on it. We're gonna be doing more communication around it but it's gonna be having a significant impact.

So let's move on to private credit, 'cause that's always got a lot of questions in this world. We'll turn it over to Kevin.

Kevin Van Buskirk: Yeah. Thanks for that, Mike. I think, on the next couple slides, we're gonna look at kinda what's beneath some of the market headlines that we've seen as well as maybe where some risks are occurring.

So attempting to break apart a little bit of the signal from the noise, and I think this slide jumps right into the noise. I think, you see a couple of headlines here, but it felt every day I was waking up from an email from Mike or somebody with a new article from Bloomberg or the Journal raising concerns about kinda

one-off defaults some stress in the market, or some other issues that they're seeing.

And you also have some pundits to private credit, like Jamie Dimon, making cockroach analogies, which certainly made people's ears perk up. So for an industry that for the last decade has been a little bit of the media darling, has raised hundreds of billions of dollars has performed exceedingly well, this has been the first stress test that it's faced during that period of time.

So if you jump to the next slide It talks-- This slide gets to a little bit of where has that mess, where has these headlines resonated so far? I think the clear answer is on retail investor sentiment. If on the left side of the page, you'll see a lot of the more recent entrants to the private credit space from some of the largest money managers globally.

So you have the BlackStones of the world, BlueRock, or excuse me, BlueOwls of the world, Apollos of the world raising these funds which they call private BDCs or non-traded BDCs which are really targeted to the retail segment. There's also a good deal of in-institutional capital in there given kind of the liquidity framework of these funds.

But really the large majority of investors here are retail investors. And what they heard from a lot of these headlines, and they got a little bit concerned and one of the advantages of these funds, which is also a little bit of the downfall of this structure, is they do allow for more frequent redemptions and more liquidity.

So with the news stories that we saw in the first quarter, these retail investors made a race for the door. And what we saw in a lot of these funds is them reaching that five percent of NAV per quarter limit that these managers are held to from a redemption perspective, and that kind of exacerbated this media story with people not being able to get all their money out.

So while this is something we're definitely keeping an eye on, I think it's more of just a structural issue within these types of strategies versus a-an issue within private credit. And I think importantly, that slide on the right shows even though these private BDCs have raised an incredible amount of money over the last decade, they still represent a pretty small share of the broader private credit universe at around twenty percent.

So the core of the institutional private credit world is not seeing that, that rush for the exits that we are in the semi-liquid space.

James Stenstrom: Kevin, one, one thing that I think I want you to talk through a little bit is, I think the initial kind of emotional reaction is, "If I can't get all my money out," you went to the bank, right?

You can't get all... There's a problem. Whereas I think the structure in terms of being able to prevent significant outflows is really intended not to harm investors, but to protect long-term investors. So can you the head and the heart kind of contrast, what the reaction may be with what the intention behind the, that, that redemption policy may be?

Kevin Van Buskirk: Yeah. That is within the structure of these funds. Without that limit on the amount of redemptions payout, I don't think anyone would invest in, in these strategies. The underlying assets are illiquid for the most part. They're three-to-five year term investments, which doesn't line up with the liquidity of the semi-liquid structures.

So it's extremely important that lever is in place to protect investors who do want to stay in the fund, who don't wanna have to have the manager fire sale pools of loans at prices that don't e-equate to what the values actually are. So that's a hugely important aspect of these strategies, and, why we're not concerned on the surface that this is happening.

In its own right, that doesn't cause concern on our end as said. So if you jump to the next slide really quick. So w-we see where the media narrative has been resonating the c- the most. So on our end, we're looking at, we hear what the media's saying. Let's look at some of the fundament- fundamentals in this space.

Are there any flashing red indicators that, that we should be looking at that cause us some more concern? So here we looked at information from the CDLI, the Cliffwater Direct Lending Index which is a pool of thousands of underlying loans which, for the most part, is a proxy of the private credit universe.

And if you look at some of these figures leverage remains pretty conservative at about .9x. Non-accruals, which are essentially the part of a loan portfolio where borrowers are no longer paying their interest payments non-accruals remain below long-term average at 1.3%. That's typically around 2, 2.2 long-term average.

In addition, you're seeing realized losses and defaults below long-term averages. Those metrics don't scream weakness at this point. But that said, it's not all roses, and I know M-Mike turned to look at me there 'cause he really presses me

on this. But it's certainly not all roses in this space, and I think you, that a little bit on the chart on the right and a little on the box on the bottom on the left.

But there are some areas of stress that we're taking deeper look at. PIK income has increased as base rates have jumped. The number of loans on watchlist that managers has also increased as managers are becoming concerned that some of these companies will not be able to pay their interest payments in the future and might go on that non-accrual list.

And then we're also seeing plenty of evidence in some specific sectors which might be impacted by areas like AI for instance, the software sector which is on the next slide, kinda double-clicks on software. So within software, I think the biggest issue here, if it's an issue, but the biggest thing to think about is that left chart.

Software has become the largest part of the private credit universe due to many reasons that are shared on the center of this slide. For the last 10 years, software borrowers have had the strongest borrower profile. These companies have strong reoccurring cash flows. They have higher operating margins than their peers in other industries.

They're generally less capital intensive businesses. And for all those reasons, private equity has poured into it, and as a result, private credit has poured into it. So it's become this outsized position in the industry. Now, though, with the advent of AI and the concerns about where AI transition's gonna happen within different businesses software is certainly in the crosshairs and we believe that as well.

But what we do see is maybe an overgeneralization occurring in the industry and where everyone's throwing every software name in the same bucket and we don't believe that to be true. We do think there's a clear distinction between higher quality software names and lower quality software names.

So if you think on the high quality side, those are mission critical software applications within industries that are highly regulated, high barriers to entry. We think those types of businesses are still protected. On the other side, on the low quality side, we do believe that there is gonna be increased defaults in this space over the next five years, certainly more than we've seen over the prior five years.

Some companies here have pretty commoditized products, have products that could probably be easily automa- automate- automated, excuse me by AI. So

these companies are clearly in the crosshairs and ones that a lot of these managers are gonna have to take a look, a deep look at a- and give further comfort around some of the future borrowing in that space.

Mike Vogelzang: Yeah we were taking a look, to, to give a concrete example, we were taking a look in the public markets, not necessarily the privates, but the public markets if you think about a company like Adobe, their stock has gone from 40 times earnings to 10 because frankly, AI can eat most of their lunch, right?

AI, y- you can vibe code, you can do all kinds of really interesting things with AI that used to be, been done by Adobe. But a company like ADP, which makes all the paychecks up on this stage possible every two weeks, which we're happy for is a company that you can't do without. It's a very hard company to get out.

It's all it's almost an employment operating system between taxes, regulation, payment, payroll, 8- 401plans, et cetera, et cetera, et cetera. Very different profile- ... to your point about how software can be impacted by AI.

Kevin Van Buskirk: So I think wrapping up this section quickly, it's a big topic that I ran through pretty quickly there, but I think on our end, there's clearly some structural stress in the semi-liquid space that we're seeing.

The fundamentals, at least today, don't point to any kind of s- systemic weakness i- in- in the industry. But there are areas of concern that people need to double-click into. And those are mainly s- around software and the potential rise of PIK income, which I didn't get into deeply, but those are areas of concern that we just need to look at going forward.

But broadly, we don't see this as a market-wide issue at this point. These are just more idiosyncratic in nature.

James Stenstrom: Awesome. So I think we're gonna bring some questions up. You mentioned PIK income. So the first question, while we're loading the audience questions, what is PIK income? 'Cause it's one of my favorite euphemisms in the entire industry.

Kevin Van Buskirk: I- I don't know if we have time to go over PIK income here, but PIK income is- It stands for payment in kind ... payment in kind Is payment in kind. So essentially what it allows borrowers to do is borrowers who are potentially stressed or might not have the capital to, to pay interest payments it allows them to basically keep those interest payments reinvest into their

company, hopefully strengthen the company, and then in the future pay off the principal in addition to all the interest payments that they've missed.

So the in kind is basically anything

James Stenstrom: other than cash on your loan. Which would be a great way for all of us to pay off all of our debts.

Mike Vogelzang: Yeah. Sure. Yeah.

James Stenstrom: I think, one of the questions I th- I think is something that a lot of people have been, mentioned headlines, thinking about with AI, one, I think there's an assumption that corporate layoff announcements are above historical trends. One, is that accurate? And then two is it AI productivity gains that we're seeing or is it the best way to tell the Street that you have a great run business you're so innovative and you're laying off people 'cause of AI and, how much veracity do you think there is in a lot of those claims?

Mike Vogelzang: M- my take is that mostly it's a way to cover up over-hiring by some of the technology companies, and now they're trying to get back to the right level of hiring. If you think about what happened with Twitter when it was purchased by Elon Musk, what did he do? He laid off 60% of the staff. That was just because it had gotten bloated and overly, bureaucratic.

And so he said, "Hey, we can lay off 60% and still derive the same number of rev- same dollar in revenue," which he's done. We saw an e- example of that in Block. They laid off half of their companies and they said, "Oh, we're gonna go to AI." Maybe sure, at the margin they are. But I don't think we've seen any major push or honestly visibility that AI is somehow wiping out whole cadres of workers.

I just don't think we've seen it.

Jim Underwood: Yeah. We've seen it in the headlines, but we haven't seen it in the data.

Mike Vogelzang: Yeah. Honestly the job loss data, layoffs have been flat for a couple of years, right? We're in this, we're in this odd, very odd market where it's no hire, no fire kind of market.

We're not seeing the 30,000, 40,000 layoffs or 200,000 layoffs at General Motors or Ford or some of the big, huge industrial w- makers. It's just not

happening. The market's in good shape. We, we think employment's actually gonna be okay for a while.

James Stenstrom: Yeah, I think another question on the IPOs.

So I think when we were preparing, IPOs are professional stock sellers saying, "Now's a great time to sell this stock." Exactly

Mike Vogelzang: right.

James Stenstrom: And so I think as you mentioned with SpaceX, certainly some things that they're trying to do to support, the price of that stock increase demand. But- When we think about how investors, particularly investors on this call, are investing in stocks, generally it's through managers as opposed to them doing individual stock selection themselves.

Has that adjusted how we think about active versus passive management, particularly in that space?

Mike Vogelzang: I think the IPOs, as I said, are gonna have an impact, right? M- most of the folks on this call are very benchmark aware, as you said. They use active managers to take active risk relative to a benchmark.

The problem here is the IPOs are changing the benchmarks in a significant way, and as a result are causing active managers to try to figure out how they line up or game their portfolios to make sure they're capturing the returns. I think if SpaceX uses their market cap, they're fifth or sixth largest company in the S&P 500.

If they use their float, they're somewhere around AutoZone, the company AutoZone and its market capitalization, right? So just that little decision is gonna have a huge impact on how people have to build portfolios, create demand for the stock or not, right? It's gonna have a big impact, so we just don't know what those answers are at this stage.

Jim Underwood: But we are seeing, unlike 2023 when we saw the Mag Seven the pairwise correlation, and I know that's a complicated term, but basically it's how correlated are these stocks moving e- with each other. It reached about 75%, so- ... everything was going up or down at the same time. We've seen it drop down to below 25% here recently as we're starting to even see dispersion within these mega cap companies.

And I would argue going forward, all these massive free cash flow generators will be on one side, and then there'll be the free cash flow beneficiaries on the other side, and those capital investments or capital expenditures are going to be that. So for example, the Metas the Googles or the Alphabets, the Microsofts, they're the f- free cash flow generators.

And right now they're spending all their money paying it to NVIDIA for technology or for the chips. And again, if that dynamic changes, you're gonna see a massive dispersion. So even within these mega cap companies, we're seeing more and more dispersion.

Mike Vogelzang: It, but it even goes down to smaller companies.

They're not small anymore, but, w- we run a strategy we call the artificial intelligence equity strategy. We have 25 or so names run by our team here. And its objective is to find things that are the secondary impact of AI, right? So just not the big, huge NVIDIAs and so on.

We had a stock in that portfolio double last week in a day. They announced earnings, and- Why? Because the Powell Industries, they make they're suppliers and contractors to the data warehouse industry, right? And as a result, their earnings went up so much because of all this cash flow being spent by all the big companies that their stock doubled and actually got cheaper on a price to earnings basis.

So you're seeing those kind of weirdness, those kind of weird sort of inflections in this marketplace, and it's very hard to get your head around as you're watching the noise every day bounce around.

James Stenstrom: I think we have time for one more to address. We'll go back to you.

We'll go back to the beginning of the conversation with the Iran conflict. It feels like I, I see headlines on the Iran conflict every day. Hawkish, dovish. We go back and forth. At least for the past month the equity markets have gone one way regardless. So it feels like we're looking through the impact of this.

We took a look at the expected oil price at the end of the year, significantly below where we are today. I guess what causes that dynamic to change, in terms of- ... that being more of a headwind for investors?

Jim Underwood: I think right now there's a couple of factors that I would say.

One is from a fiscal policy standpoint, we have had a lot of tax refunds that are supporting the overall economy, so you're not seeing the impact in the economy. Two, while I showed you the chart that's had oil prices, at the end of 2026 from a Fed futures, cash futures standpoint, the prediction markets have, from a retail perspective, I'm not sure individuals have those same expectations.

So they may be a little bit more optimistic that oil prices are temporary and we're, that's just gonna pass through fairly quickly. And so I think those two together. And then I guess the third would be just the structure of the US economy right now. The vast majority of spending of US GDP comes from consumption.

And if you were to look at our consumption pattern the baby boomers right now are spending down their bala- their largest ever balance sheets, and they're just not impacted by it. So you're seeing the economy continue to do fine, people not as concerned about the long-term risk of energy prices.

And then you had some Fed stimulus there to kinda keep things supported.

Mike Vogelzang: The only other thing I'd add to Jim's comments are that I think the market is continuing to try to understand how profitable will the corporate structure be using AI, and I think it's coming up on the sort of the rosy side of that equation.

I think the market, where we've seen earnings growth explode this year. A lot of that is concentrated in the semiconductor chips, right? But you've still seen, we're expecting after- Two or three years of really strong grow- earnings growth in the S&P 500. We're seeing 22% growth rate now for 2026 estimated.

That's unheard of. And another 2027 where they're talking about 16, 17% earnings growth. It is crazy how strong corporate America is in the earnings growth we're seeing. So markets are just pricing that in and trying to figure out where this is gonna end. And right now, a small little blockage in a tiny little river called the Strait of Hormuz doesn't seem to be impacting it very much.

Awesome.

James Stenstrom: I think I threatened the people behind to, to read the disclosures. I think we'll spare everybody- ... those. But certainly appreciate all of you, all of our clients joining us today. It's certainly, all of our pleasure to have this conversation. We don't- 100% ... always get to talk with all of you as much as we'd like.

And certainly you'll be receiving a recording of this. A last plug for the endowment and foundation survey, as I mentioned. You heard from us, we'd love to hear from you. And certainly appreciate the time that all of you provided us today. Very grateful and humbled by that.

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