

Differentiated Alpha:

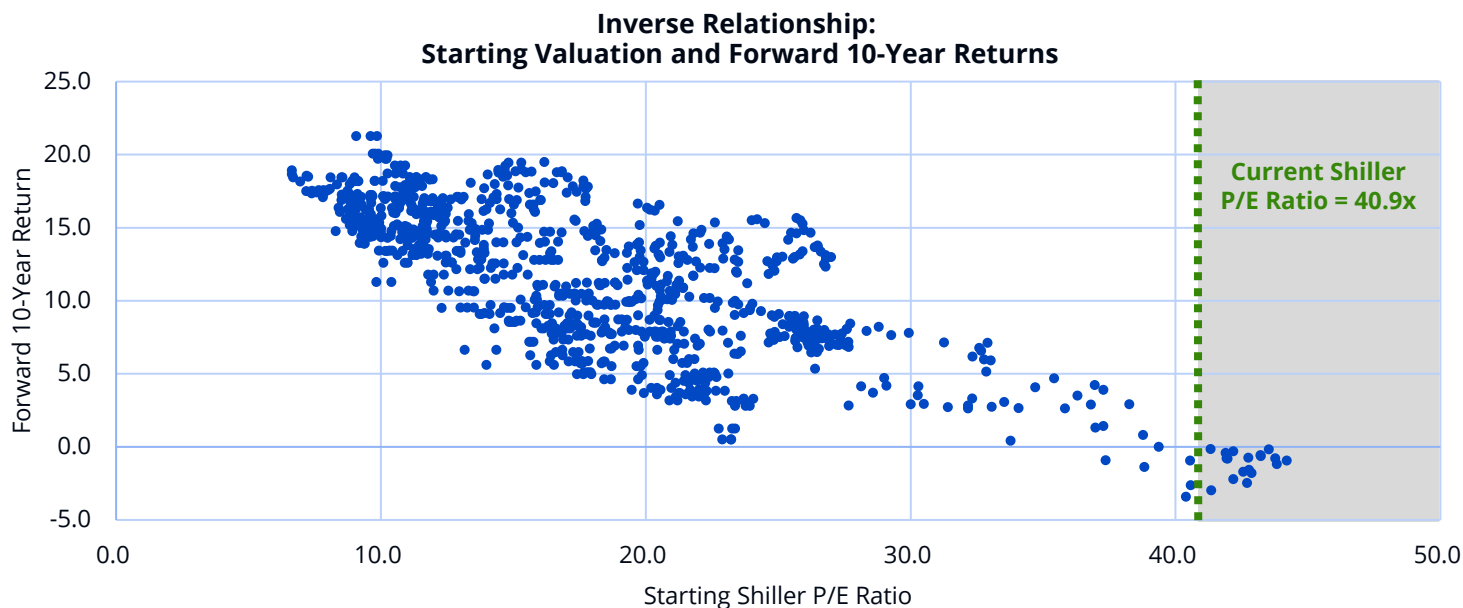
Positioning for a Lost Decade in U.S. Large-Cap Stocks

Second Quarter 2026

The Next Lost Decade?

High starting valuations point to weak long-term returns. Historically, measures like the Shiller P/E (price-to-earnings) ratio show strong, inverse relationships with long-term equity returns. When a market cycle initiates at an elevated P/E ratio, future gains are usually muted.

- Only 2% of historical valuations have been higher than today's level
- The average 10-year forward return has been -1.1%



Source: Morningstar and www.shillerdata.com. Market valuation is represented by the Shiller P/E ratio and is using monthly data from March 1936 to June 2016. Forward 10-year returns are represented by the S&P 500 Index and is using monthly data from March 1946 to June 2016.

Significance for Investors

Investors should consider reassessing exposure to cap-weighted, large-cap equities and explore complementary strategies to enhance portfolio resilience.

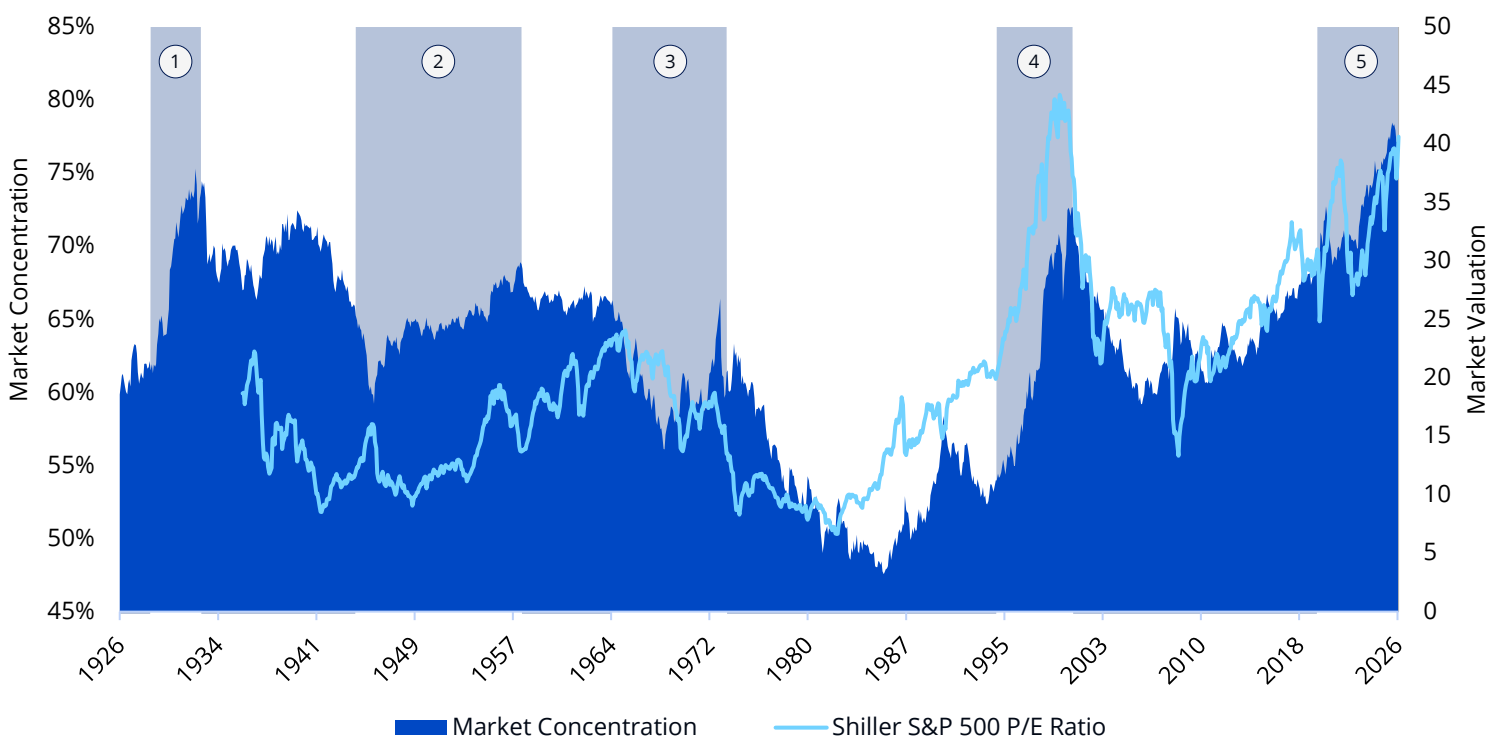
Concentration Risk at an All-Time High

Market concentration – the dominance of a small number of companies in driving overall market returns – is now at historic extremes.

Why This Matters

- 1. Stretched Valuations:** Leaves markets vulnerable to sharp pullbacks if growth expectations slip.
- 2. Hidden Concentration:** Reduces the diversification investors expect from broad index exposure.
- 3. Systemic Vulnerability:** Rises when overall market performance depends on just a few dominant firms.

**Top 10% of U.S. Companies by Size:
Market Concentration**



1 = Great Depression (1929-1932); 2 = Post-WWII Expansion (1945-1957); 3 = Nifty Fifty (1965-1973); 4 = Dot-Com Bubble (1995-2000); 5 = "Magnificent Seven" Era (2020-). Source: Kenneth French Data Library (portfolios formed on size) and www.shillerdata.com. Market concentration represents the value of the top decile of companies based on size divided by the entire value of the market and is as of May 31, 2026. Market valuation is represented by the Shiller S&P 500 P/E ratio.

The Pattern Is Clear

When too much capital chases too few stocks, momentum drives valuations higher, creating unsustainable imbalances. Eventually, either fundamentals fail to keep pace with expectations or investor psychology shifts, leading to sharp mean reversion.

Significance for Investors

To mitigate the risks, investors can diversify into attractively valued areas of the market, such as small-cap and international equities, which offer broader diversification and potential for higher long-term growth.

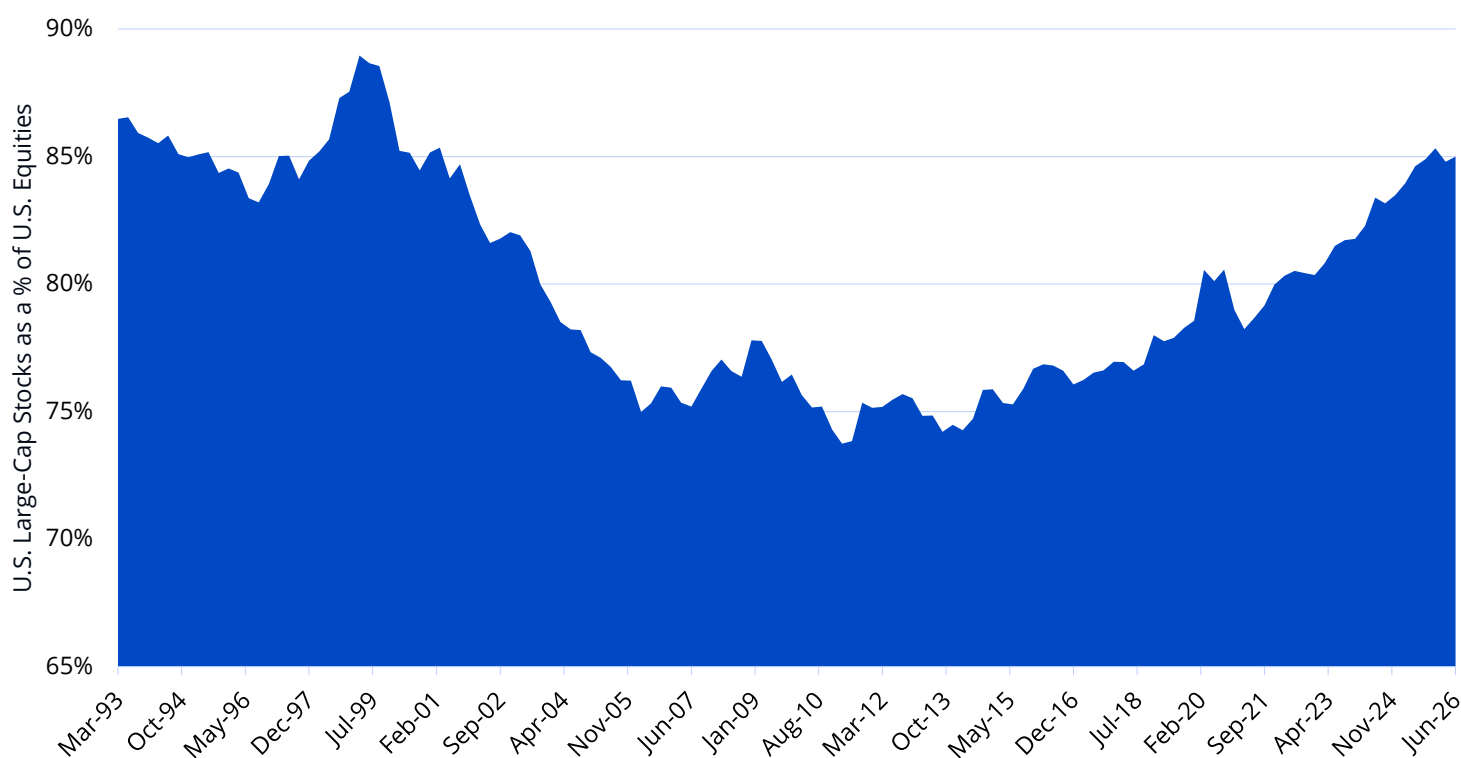
U.S. Large-Cap Equity Exposure Is Approaching Levels Not Seen in Decades

Investor outcomes are becoming increasingly influenced by large-cap market dynamics.

Market Conditions

1. **Investor Vulnerability:** U.S. large-cap stocks are dominating investor equity portfolios.
2. **Amplified Downside Risk:** Higher allocations fuel crowded trades and magnify selloffs.

U.S. Large Cap Stocks' Dominance Heightens Market Vulnerability



Source: Morningstar, from March 31, 1993, to June 30, 2026.

Time to Reassess?

When market leadership becomes narrow – often a sign of speculative excess or late-cycle dynamics – investors should reassess allocations, rebalance toward undervalued or overlooked areas, and reinforce risk controls.

Significance for Investors

Such extreme concentration in few asset classes raises the importance of seeking diversification to uncover differentiated sources of return.

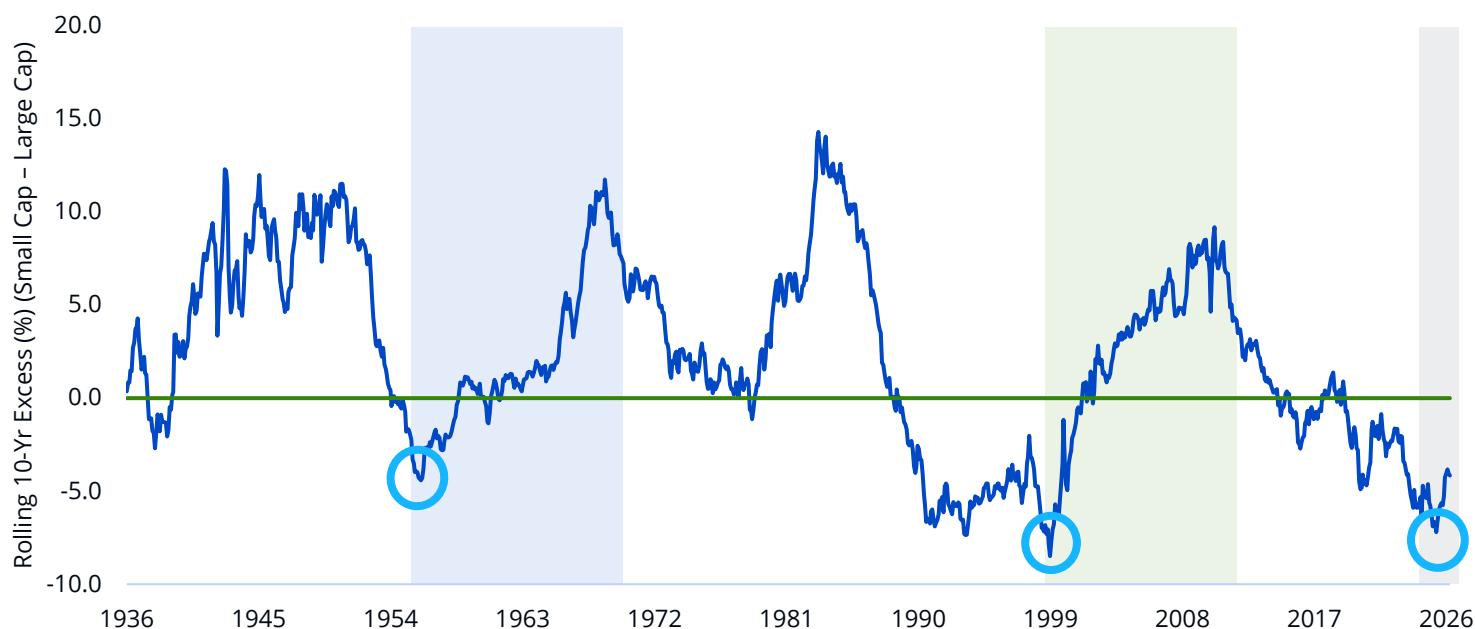
The Case for Small-Cap Stocks

Small-cap stocks' underperformance of today's magnitude has only happened twice before, with both instances followed by strong historical rebounds.

Potential Catalysts for Small-Cap Stocks

- 1. Valuations:** Small-cap stocks are trading at attractive entry points when compared to large-cap stocks.
- 2. Financing:** Lower borrowing costs, tighter spreads and falling interest rates favor small-cap stocks.
- 3. Mergers and Acquisitions Activity:** Historically, increased deal activity can lift small-cap performance.
- 4. Earnings Outlook:** Forward earnings expectations are improving; small-cap stocks are higher than large-cap stocks.
- 5. Currency Impact:** A weaker dollar benefits small-cap exporters.

A U.S. Lost Decade May Be a Tailwind for Small-Cap Stocks*



Sources: Kenneth French Data Library and Morningstar. Past performance does not guarantee future results. Data represents rolling 10-year excess returns from June of 1936 to May 2026.

	Small Cap Trailing 10-Year Underperformance*	Duration of Rebound	Annualized Return (Small vs. Large)	Growth of \$100 (Small vs. Large)	Starting Large-Cap P/E Ratio
1	-4.4%	12.5 years	20.3% vs. 10.0%	\$1,026 vs. \$343	18.2x (Near Post WWII Peak)
2	-8.5%	11.2 years	10.0% vs. 0.4%	\$284 vs. \$109	41.4x (Near Dot-Com Peak)
3	-7.2%	?	?	?	36.1x (Magnificent Seven)

Sources: Kenneth French Data Library, Morningstar and www.shillerdata.com. Past performance does not guarantee future results.

Note: Small-Cap Stocks represent the bottom 3 deciles of companies based on market cap and Large-Cap Stocks represent the top 3 deciles of companies based on market cap. *Small-Cap Stocks' 10-year annualized return minus large-cap stocks' 10-year annualized return.

The Case for International Stocks

International stocks offer exposure to a broader range of businesses, currencies and economies not fully represented in domestic portfolios. They currently trade at record discounts with higher yields, and recent reforms are designed to enhance global competitiveness.

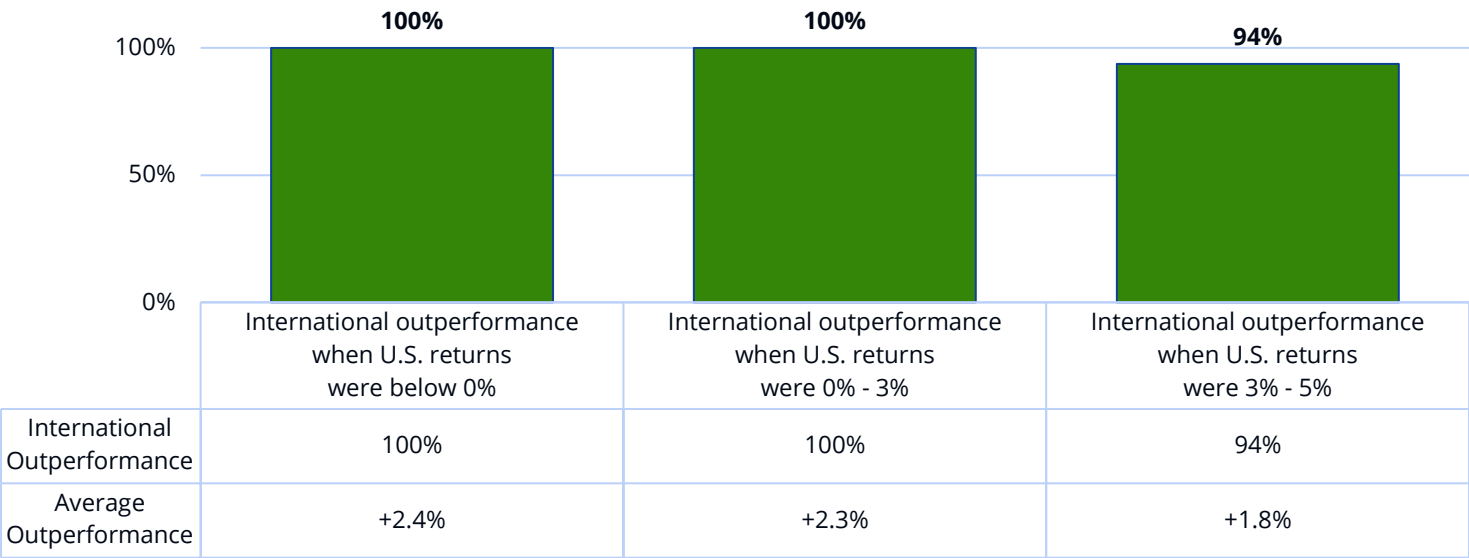
Potential Catalysts for International Stocks

- 1. **U.S. Dollar Weakness:** Provides a tailwind for international returns.
- 2. **Attractive Valuations:** Trading at record discounts versus U.S. equities.
- 3. **Earnings Growth:** Forward earnings-per-share forecasts have been revised upward.
- 4. **Market Cycle:** Extended cycle may be due for mean reversion.
- 5. **Recent Performance:** Could signal the start of a new leadership regime.

A U.S. Lost Decade May Be a Tailwind for International Stocks

During rolling 10-year periods dating back to 1978, international equities have outperformed U.S. equities 100% of the time when U.S. equity returns are modest or negative.

Rolling 10-Year Returns: U.S. vs. International Equities
(1978 - 2025)



Source: Morningstar. Past performance does not guarantee future results.

Making a Strategic Shift for Resilience and Returns

Investors should reassess their concentration in U.S. large-cap equities. Diversifying into international and small-cap stocks can enhance portfolio resilience, reduce concentration risk and broaden the sources of potential alpha generation.

Past performance does not guarantee future results.

Alpha: A measure of performance on a risk-adjusted basis. Alpha takes the volatility (price risk) of a fund and compares its risk-adjusted performance to a benchmark index. The excess return of the fund relative to the return of the benchmark is a fund's alpha.

Annualized Return: The annualized return is the geometric mean of the returns with respect to one year.

Duration: A measure of the sensitivity of the price (the value of principal) of a fixed-income investment to a change in interest rates. Duration is expressed as a number of years. Rising interest rates mean falling bond prices, while declining interest rates mean rising bond prices.

Price-to-Earnings Ratio ("P/E Ratio"): Current share price of a stock divided by its earnings per share.

Sharp Mean Reversion: Refers to situations where an asset's price experiences a quick and substantial deviation from its historical average, followed by a rapid return to that average.

Shiller P/E Ratio (CAPE ratio): A valuation measure that uses real earnings per share (EPS) over a 10-year period to smooth out fluctuations in corporate profits that occur over different periods of a business cycle.

Valuation: The process of determining the value of an asset or company. Stock analysts determine the value of a company based on current and future earnings, the market value of the company's assets and the balance sheet. A company with a high price-to-earnings ratio is said to have a high valuation or be highly valued. Bond analysts determine the value of a bond based on projections of future interest rates, and they use their valuation to determine whether a bond should be bought or sold at its current price.

Yield: The annual return on an investment, expressed as a percentage of the price. For stocks, yield is the annual dividend divided by the purchase price, also known as a dividend yield. For bonds, it is the coupon rate divided by the market price, called current yield.

All investing involves risk, including possible loss of principal. Any opinions herein, including forecasts, reflect the opinions of the author at the time of writing and are subject to change. This is not a complete analysis of market conditions and, therefore, should not be relied upon as investment advice.

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