Callan Institute

First Quarter 2026

# Capital Markets Review

## What Else Can We Throw At Economy?

ECONOMY

2 PAGE

Despite a war, tariffs, deportations, and more, the U.S. economy continues to show strength and markets continue to rally. Can it last? While making predictions about the economic future is always tricky, investors seem to be driven by a fear of missing out.

## Returns Against a Benchmark Improve

INSTITUTIONAL INVESTORS

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The tough 1Q26 for stocks helped public DB plans and nonprofits roughly match a 60% equities/40% bonds benchmark in the one year ending 3/31/26. Bond-heavy corporate DB plans lagged. For institutional investors, the Iran conflict's impact on oil prices dominated conversations.

## Global ex-U.S. Stocks Lead in Down Quarter

EQUITY

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The S&P 500 Index fell 4.3% in 1Q26; only 6 of the 11 S&P sectors posted gains. Global ex-U.S. equities led U.S. stocks during the quarter. Value outperformed growth across EAFE and emerging markets in 1Q26, supported by strength in Energy following the Iran conflict.

## Mixed Performance as Volatility Returns

FIXED INCOME

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The Aggregate modestly declined by 5 bps, driven by the rise in rates. Credit spreads were resilient early in the quarter but widened into quarter-end amid software and AI-related concerns. Global fixed income returns were negative for 1Q, with developed markets underperforming.

## Real Assets Navigate a Mixed Environment

REAL ESTATE/REAL ASSETS

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For private real estate, income boosted performance while appreciation only delivered modest returns. Commodities delivered strong gains, led overwhelmingly by energy. REIT performance was positive overall but varied significantly by sector and region.

## Fundraising Takes a Big Hit in 3Q25

PRIVATE EQUITY

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Private equity data for the full year 2025 is not yet available. For 3Q25, fundraising dropped but deal activity rebounded. Buyouts also roared back, and the AI boom continued to drive venture capital activity. Returns for 3Q lagged public markets, driven by conservative valuation policies.

## Defaults Stay Low Despite Headlines

PRIVATE CREDIT

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Private credit defaults (2%) have historically been significantly less than high yield default rates. This has continued to be the case during the current environment. The top four funds raised in 4Q25 were concentrated outside of U.S. direct lending.

## Mixed Results as Markets Shift Rapidly

HEDGE FUNDS/MACs

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Managers saw mixed results in 1Q26 as markets rapidly shifted after the start of the U.S.-Iran conflict. Broader hedge fund indices delivered gains but most other strategies saw losses. We expect the outlook for strategies to improve amid macro instability.

## Another Gain for the DC Index in 4Q25

DEFINED CONTRIBUTION

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The Callan DC Index™ rose 2.4% in 4Q25, while the Age 45 Target Date Fund was up 2.8%. Balances within the Index rose by 1.0%, driven by investment gains. Turnover hit its lowest level ever. In a rarity, TDFs saw net outflows.

## Broad Market Quarterly Returns

**U.S. Equity**
Russell 3000

**-4.0%**

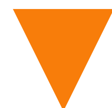
**Global ex-U.S. Equity**
MSCI ACWI ex USA

**-0.7%**

**U.S. Fixed Income**
Bloomberg Agg

**0.0%**

**Global ex-U.S. Fixed Income**
Bloomberg Global Agg ex US



**-1.9%**

Sources: Bloomberg, FTSE Russell, MSCI

# So What Else Can We Throw At This Economy to Slow It?

**ECONOMY** | Jay Kloepfer

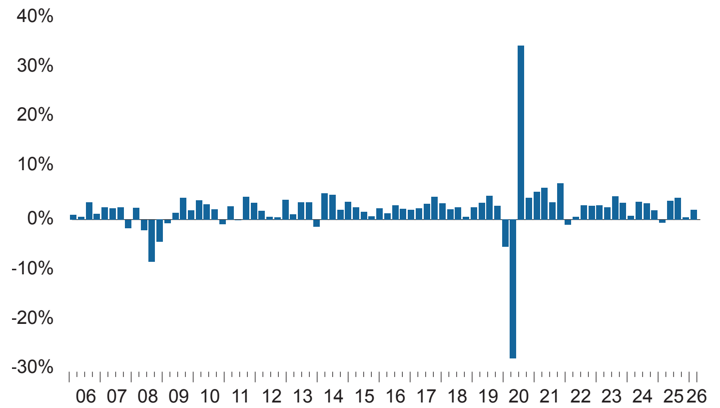
Real GDP rose 2% in 1Q26, the first broad economic measure that included the impact of the Iran war and the spike in oil prices on the U.S. economy. A gain of 2% suggests a resilience to the economy that has persisted after a seemingly endless string of triggers to capital markets and economic uncertainty. 2025 saw the inauguration of President Trump; the chaotic introduction of a very wide and constantly changing schedule of tariffs in 1Q25; the deployment of Immigration and Customs Enforcement (ICE) forces into American cities, interrupting the daily economic activity of the surrounding city (or area); a surge in deportations of undocumented immigrants, many of whom made up a sizable portion of the labor force in agriculture, services, and construction; a sudden halt to legal immigration; and the cessation of job creation in the U.S. labor market. Let's not forget a government shutdown that began in October 2025 and lingers to this day, with some government employees' pay still being withheld into 2Q26. The U.S. began 2025 with a small decline in GDP (-0.6%) in 1Q, but then growth surged through the second and third quarters and finished the year with a solid gain of 2.0% for the entire year.

Then the U.S. and Israel began a war with the bombing of Iran on Feb. 28, 2026. Aside from the death and destruction in the Middle East, the immediate global impact of the action was on the price of oil, which shot from $60 per barrel at the start of the year to over $100, and the closing of the Strait of Hormuz, through which 20% of the world's supply of crude passes. Customers in Asia have been particularly affected by the restriction in oil supply. While the supply impact may be regional, the price of oil is set globally. The U.S. may tout energy self-sufficiency, but the price of West Texas Intermediate (WTI) crude is not set by U.S. supply/demand conditions, but in the global energy market. In addition to energy markets, the focus of many analysts has been on business and consumer confidence, which has plummeted since the start of March, a typical response to the outbreak of war. However, the U.S. economy continued its streak of resilience into 1Q26 with this latest GDP report.

Looking forward, a macro rule of thumb is that for each $10 rise in the price of a barrel of oil, U.S. GDP growth is reduced by 20 basis points. The $40 rise through the end of March suggests an 80 bps hit (almost 1 percentage point) to GDP growth. If prices go higher, or remain elevated into 2027, the impact will build, and the risk of an energy-triggered recession rises.

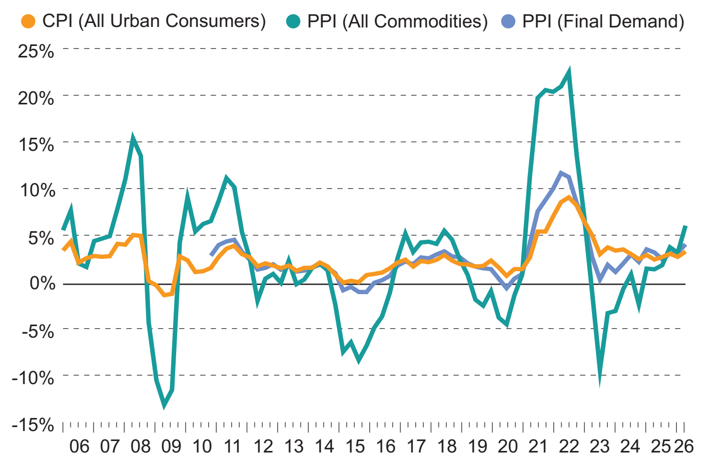
A disconnect that Callan pointed out in 2025 continued into 2026, namely, that economic indicators which once provided solid direction on the course for the U.S. and global economies and the capital markets appear to have lost either their relevance or their predictive power. The data appears to be sound, but their signals are no

**Quarterly Real GDP Growth** (20 Years)




Source: Bureau of Economic Analysis.

**Inflation Year-Over-Year**




Source: Bureau of Labor Statistics.

longer clear, or it is increasingly difficult to separate signal from noise. Inverted yield curves used to presage recessions, but we have been in some form of inversion since 2023 without a recession. Consumer confidence and job creation have plummeted, yet spending remains robust and as a result consumption and GDP show resilience.

Callan has developed a new chart we will begin to distribute monthly that we call "EconIndicators," starting in 2Q26. A review of the chart that includes data through 1Q26 highlights the anomaly between traditional measures of economic health, sentiment, and market prices and the seemingly robust economic activity reported through broad measures like GDP, consumption, housing, imports, and exports. For example, consumer sentiment is at an all-time low, yet consumer spending continues apace. The spread between yields on risky bonds like investment grade credit and high yield are extremely tight. That suggests spreads have nowhere to go but wider, usually a sign of a weakening economy—yet these spreads continue to grind tighter. The forward price/earnings ratio for the S&P 500, which is an indicator of how cheap or expensive the stock market is relative to its own history, has retreated from a near-record high set just before the Iran conflict, but the ratio is still well above its long-term average. Investors appear loathe to miss out on a continued market run. Stocks globally have rallied to regain their losses incurred when the Iran war began, and non-U.S. stocks have rallied the most. Fear of missing out is a powerful factor.

### The Long-Term View

| Index | 1Q26 | Periods Ended 3/31/26 | | | |
|---|---|---|---|---|---|
| | | 1 Yr | 5 Yrs | 10 Yrs | 25 Yrs |
| **U.S. Equity** | | | | | |
| Russell 3000 | -4.0 | 18.1 | 10.9 | 13.7 | 9.3 |
| S&P 500 | -4.3 | 17.8 | 12.1 | 14.2 | 9.2 |
| Russell 2000 | 0.9 | 25.7 | 3.8 | 9.9 | 8.5 |
| **Global ex-U.S. Equity** | | | | | |
| MSCI EAFE | -1.2 | 21.3 | 7.9 | 8.4 | 5.9 |
| MSCI ACWI ex USA | -0.7 | 24.9 | 7.0 | 8.4 | 6.3 |
| MSCI Emerging Markets | -0.2 | 29.6 | 3.7 | 7.8 | 8.7 |
| MSCI ACWI ex USA Small Cap | -0.5 | 27.8 | 5.7 | 8.0 | 8.5 |
| **Fixed Income** | | | | | |
| Bloomberg Agg | 0.0 | 4.3 | 0.3 | 1.7 | 3.6 |
| 90-Day T-Bill | 0.8 | 4.0 | 3.3 | 2.3 | 1.8 |
| Bloomberg Long G/C | -0.8 | 2.2 | -2.9 | 1.2 | 4.9 |
| Bloomberg Gl Agg ex US | -1.9 | 4.2 | -2.9 | -0.4 | 3.1 |
| **Real Estate** | | | | | |
| NCREIF Property | 1.2 | 4.8 | 3.7 | 4.7 | 7.2 |
| FTSE Nareit Equity | 4.8 | 6.8 | 5.8 | 5.6 | 9.1 |
| **Alternatives** | | | | | |
| Cambridge PE* | 2.6 | 9.5 | 12.6 | 13.4 | 10.5 |
| Cambridge Senior Debt* | 1.1 | 7.8 | 8.3 | 8.0 | 5.0 |
| HFRI Fund Weighted | 1.0 | 14.0 | 6.1 | 6.8 | 5.9 |
| Bloomberg Commodity | 24.4 | 32.3 | 14.0 | 8.0 | 2.8 |
| **Inflation** – CPI-U | 1.9 | 3.3 | 4.5 | 3.3 | 2.5 |

*Data for most recent period lags. Data as of 3Q25.
Sources: Bloomberg, Bureau of Economic Analysis, FTSE Russell, Hedge Fund Research, MSCI, NCREIF, Refinitiv/Cambridge, S&P Dow Jones Indices

### Recent Quarterly Economic Indicators

| | 1Q26 | 4Q25 | 3Q25 | 2Q25 | 1Q25 | 4Q24 |
|---|---|---|---|---|---|---|
| Employment Cost: Total Compensation Growth | 3.4% | 3.4% | 3.5% | 3.6% | 3.6% | 3.8% |
| Nonfarm Business: Productivity Growth | 0.8% | 1.6% | 5.2% | 4.2% | -0.9% | 1.4% |
| GDP Growth | 2.0% | 0.5% | 4.4% | 3.8% | -0.6% | 2.4% |
| Manufacturing Capacity Utilization | 75.4% | 75.5% | 75.9% | 75.6% | 75.3% | 76.2% |
| Consumer Sentiment Index (1966=100) | 55.4 | 52.5 | 58.3 | 55.0 | 64.5 | 72.1 |

Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve, IHS Economics, Reuters/University of Michigan

# Returns Against a Benchmark Improve

## INSTITUTIONAL INVESTORS

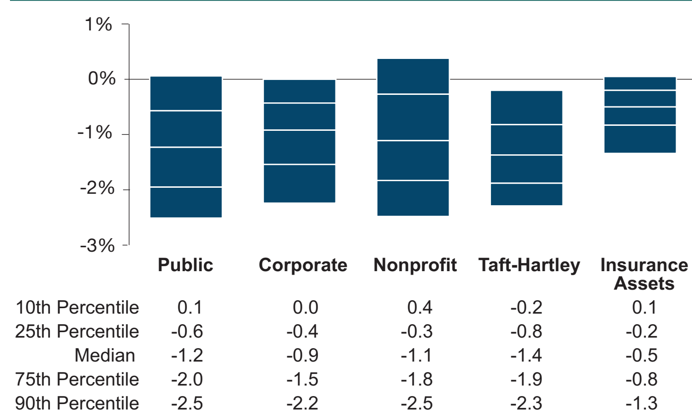
### Investor Performance

- A tough 1Q26 for stocks helped public defined benefit (DB) plans and nonprofits match a 60% equities/40% fixed income benchmark over the one year ending 3/31/26.
- Bond-heavy corporate DB plans trailed the benchmark by roughly 4 percentage points.
- Over longer time frames institutional investors have struggled to match the benchmark, as strong U.S. equity gains have made it challenging to keep up.
- DC-focused indices, with higher equity allocations, did better both over the short and longer term.
- Public DB plans and nonprofits did well versus the benchmark in 2025, while corporate DB plans lagged.
- From 2021-24, the 60/40 benchmark topped institutional investor returns in years of gains, while it lagged in the one down year (2022).

### Macroeconomic Issues

- The Iran conflict and the impact on oil prices and the energy markets dominated discussions during the quarter.
- While the Federal Open Market Committee held steady on rates in 1Q26, with the Fed Funds rate remaining at 3.50% – 3.75%, the transition to a new chair will be a subject of ongoing monitoring by institutional investors.

**Quarterly Returns, Callan Database Groups** (3/31/26)




| | Public | Corporate | Nonprofit | Taft-Hartley | Insurance Assets |
|---|---|---|---|---|---|
| 10th Percentile | 0.1 | 0.0 | 0.4 | -0.2 | 0.1 |
| 25th Percentile | -0.6 | -0.4 | -0.3 | -0.8 | -0.2 |
| Median | -1.2 | -0.9 | -1.1 | -1.4 | -0.5 |
| 75th Percentile | -2.0 | -1.5 | -1.8 | -1.9 | -0.8 |
| 90th Percentile | -2.5 | -2.2 | -2.5 | -2.3 | -1.3 |

Source: Callan

- GDP came in at 2.0% for 1Q, released after the quarter end, despite headwinds hitting the U.S. economy.
- Inflation continued to stay above the Fed's 2.0% target.

### Public DB Plans

- Interest in private credit has been significant for public DB plans for a prolonged period, with just a dip in 3Q25, according to the results of our proprietary Consultant Survey.

**Callan Database Median and Index Returns* for Periods Ended 3/31/26**

| Database Group | Quarter | 1 Year | 3 Years | 5 Years | 10 Years | 20 Years |
|---|---|---|---|---|---|---|
| **Public Database** | **-1.2** | **12.2** | **10.1** | **6.3** | **8.4** | **6.9** |
| **Corporate Database** | **-0.9** | **8.3** | **7.0** | **3.0** | **6.1** | **6.0** |
| **Nonprofit Database** | **-1.1** | **12.8** | **10.7** | **6.4** | **8.3** | **6.8** |
| **Taft-Hartley Database** | **-1.4** | **11.7** | **9.8** | **5.9** | **7.9** | **6.6** |
| **Insurance Assets Database** | **-0.5** | **7.5** | **7.1** | **3.6** | **4.6** | **4.6** |
| **All Institutional Investors** | **-1.1** | **11.6** | **9.8** | **5.8** | **7.9** | **6.7** |
| **Large (>$1 billion)** | **-0.8** | **11.5** | **9.3** | **6.3** | **8.3** | **6.9** |
| **Medium ($100mm - $1bn)** | **-1.3** | **11.5** | **9.9** | **5.8** | **8.0** | **6.7** |
| **Small (<$100 million)** | **-1.2** | **12.1** | **10.3** | **5.7** | **7.8** | **6.5** |
| 60% S&P 500/40% Bloomberg Agg | -2.6 | 12.4 | 12.4 | 7.4 | 9.3 | 7.9 |

*Returns less than one year are not annualized.

Source: Callan. Callan's database includes the following groups: public defined benefit (DB) plans, corporate DB plans, nonprofits, insurance assets, and Taft-Hartley plans. Approximately 10% to 15% of the database constituents are Callan's clients. All database group returns presented gross of fees. Past performance is no guarantee of future results. Reference to or inclusion in this report of any product, service, or entity should not be construed as a recommendation, approval, affiliation, or endorsement of such product, service, or entity by Callan.

- A much larger share of clients planned to cut U.S. equity allocations rather than increase them.
- More clients planned to increase or decrease global ex-U.S. equity allocations compared to 3Q25.
- Fixed income interest was small, and lower than in 3Q25 for either increases or decreases.

### Corporate DB Plans

- In 3Q21, we started asking consultants about corporate DB plans with a focus on three key areas: funded status, funded basis, and plan goals.
- Clients were roughly evenly split on the goals for their plans, with pension risk transfer, closing the funding gap, and "other" the top choices.
- This is a subtle shift from previous quarters, when typically a single goal topped the list.
- The share of plans with a funded status above 100% hit the highest level since we started asking these questions, as it did in 3Q25.

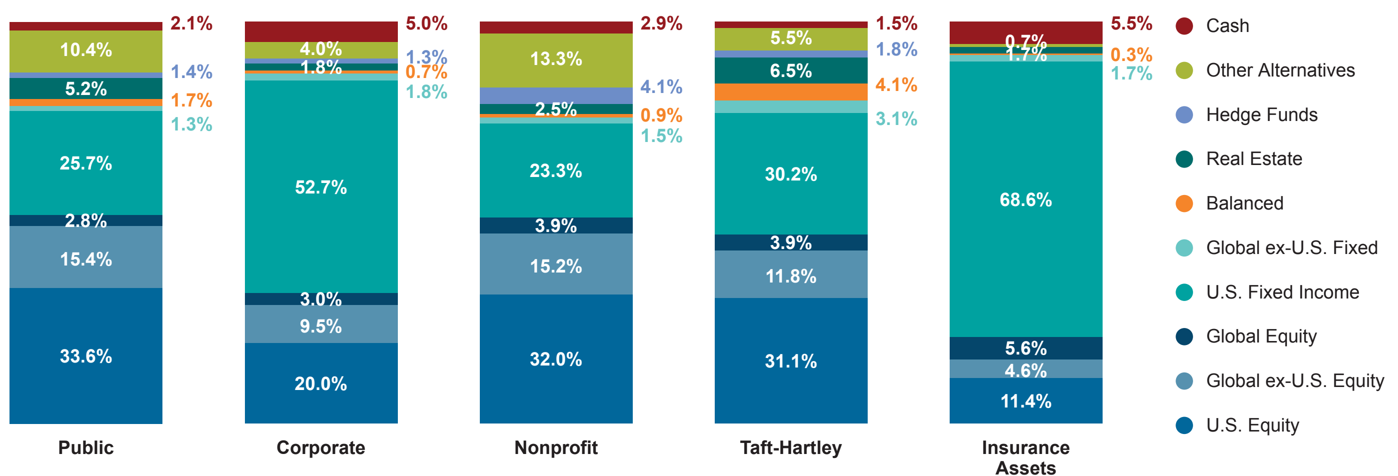
### Nonprofits

- Interest in increasing allocations to private real estate fell to 0%. Roughly 10% of nonprofit clients over time have historically planned to add to the asset class, but other quarters have seen the same 0% level of interest.
- Hedge funds interest also hit 0%, a shift from prior surveys.
- Clients' interest in increasing private credit allocations continues.
- Plans to change private equity allocations were relatively muted, and little changed from prior quarters.

### DC Plans

- Fees remained the top issue for DC plans, as they have been for years.
- Compliance and investment structure have shifted over time as Nos. 2 and 3.
- The share of clients with entirely passive TDFs has remained at a high level, hitting 45% in 3Q22 and still elevated in 1Q26.

**Average Asset Allocation, Callan Database Groups**




Note: Charts may not sum to 100% due to rounding. Other alternatives include but is not limited to: diversified multi-asset, private credit, private equity, and real assets.
Source: Callan

# Equity

## U.S. Equities

### S&P 500 Fell Against a Volatile Market Backdrop

– The S&P 500 Index fell 4.3% in 1Q26. Challenged results were driven by multiple factors: geopolitical conflict exacerbating inflation fears; investor rotation out of stocks that have reached lofty valuations; and a shift within the Magnificent 7 as its components saw starkly different returns based on concerns around software and uncertainty around the benefits of AI capex to future revenue growth.
– Only 6 of the 11 S&P sectors posted gains. Energy (+38.2%!) was the best-performing sector followed by Materials (+9.7%) and Utilities (+8.3%). The worst-performing sectors were Information Technology, Financials, and Consumer Discretionary, all down over 9%.
– Small cap indices outperformed large cap indices and value outperformed growth across the market cap spectrum.

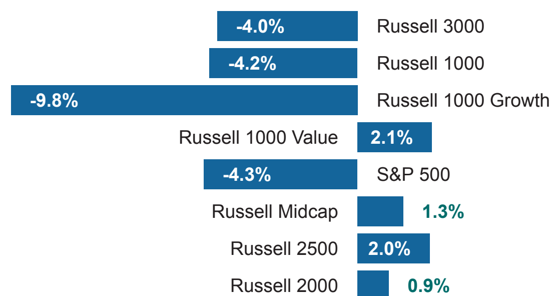
### Key Characteristics of First Half of Quarter

– Fundamentals started to matter! A strong earnings season supported a broadening of market returns, and most notably, an extension of the outperformance in small caps that began in the latter half of 2025.
– Large cap performance meaningfully disaggregated, particularly within the Magnificent 7. Drivers of underperformance include investors' concerns about: 1) Peak valuations on the heels of high AI capex; 2) Displacement of software and other applications by AI.

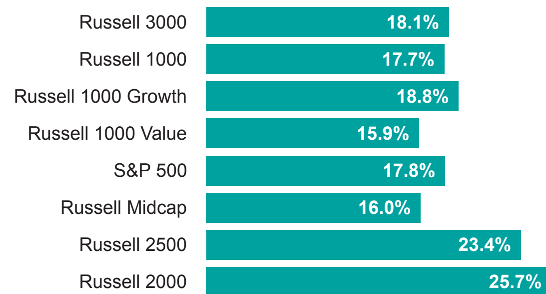
### Key Characteristics of Second Half of Quarter

– The U.S./Iran War began on Feb. 28, kicking off sharp equity declines through March 23.
– The Energy sector was up nearly 40% as fears of supply shortages pushed up crude oil prices. The sector also benefited from the "HALO" (hard assets, low obsolescence) trade as investors rotated from valuation-rich areas and those potentially displaced by AI.

**U.S. Equity: Quarterly Returns** (3/31/26)

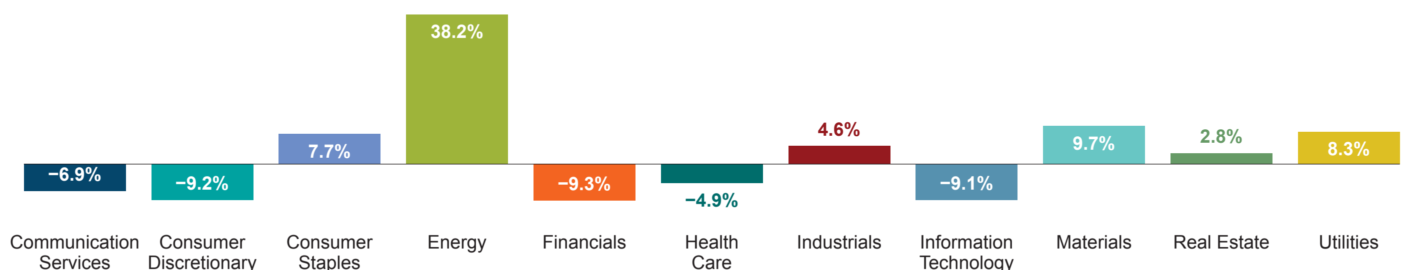



**U.S. Equity: One-Year Returns** (3/31/26)




Sources: FTSE Russell and S&P Dow Jones Indices

**Quarterly Performance of Industry Sectors** (3/31/26)




Source: S&P Dow Jones Indices

## Global Equities

### Global ex-U.S. Stocks Lead in a Down Quarter

- Global ex-U.S. equities outpaced the U.S. in 1Q26.
- The MSCI EAFE Index declined slightly in 1Q26 following a period of strong performance in 2025, as modest gains in the U.K. and developed Pacific were offset by weakness across the euro zone.
- Within emerging markets, China lagged, reflecting weak consumer confidence and ongoing local government debt pressures. India also underperformed, facing valuation compression and energy-related headwinds as a net commodity importer amid geopolitical tensions involving Iran.
- Semiconductor-oriented markets such as Taiwan and South Korea supported results amid strong AI-driven demand. Latin America also outperformed, led by Brazil, benefiting from commodity strength and currency tailwinds.

### Growth vs. Value

- Value outperformed growth across EAFE and emerging markets in 1Q26, supported by strength in Energy and other commodity-sensitive sectors following the Iran conflict.

### U.S. Dollar

- The U.S. dollar strengthened modestly during 1Q26 (+1.7%), acting as a slight headwind to global ex-U.S. equity returns.

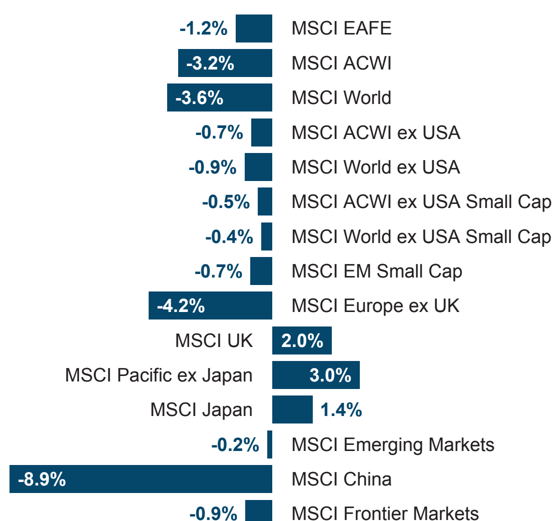
### Strength Has Been Thematic, Not Broad

- Performance in 1Q26 continued many of the same themes from calendar year 2025.
- Significant dispersion within Technology stocks continued as AI beneficiaries such as semiconductors, memory, etc., have seen remarkable strength, while potential AI losers like software continued their downtrends.
- Hard asset sectors that are deemed immune to AI concerns and/or AI beneficiaries such as Materials, Utilities, and Energy continued to perform well.
- Both Consumer Staples and Consumer Discretionary stocks remain under pressure as a variety of concerns around economic sensitivity, margin risk, valuations, etc., persist.
- Active manager relative performance has been very closely tied to the amount of exposure portfolios have to specific industries and themes.

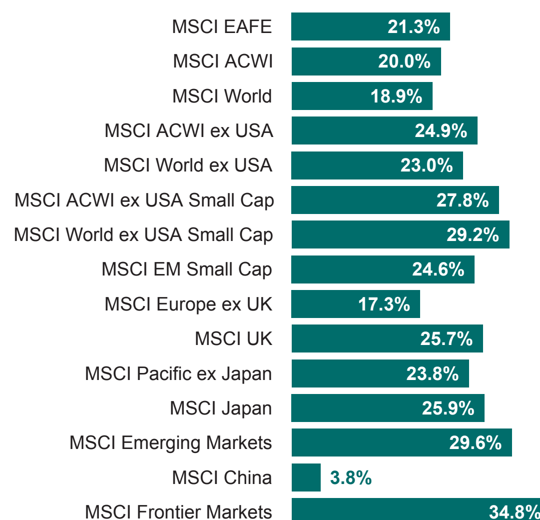
### Momentum and Value Are Winners

- Factor tailwinds and headwinds largely continued in 1Q26 from 2025 with momentum and value leading markets.
- Over recent timeframes, active non-U.S. value managers have delivered meaningful absolute and relative returns versus both core benchmarks and growth peers. However, value benchmarks have been a more difficult bar to surpass.

**Global ex-U.S. Equity: Quarterly Returns** (U.S. Dollar, 3/31/26)




**Global ex-U.S. Equity: One-Year Returns** (U.S. Dollar, 3/31/26)




Source: MSCI

# Fixed Income

## U.S. Fixed Income

### Mixed Performance as Volatility Returns

- Volatility picked up during 1Q26, driven by the U.S./Israel strikes on Iran and renewed inflation concerns as oil prices moved higher.
- Treasury yields rose across most of the curve, with the largest increases in intermediate maturities, resulting in slight curve flattening with the 2s/10s spreads narrowing 20 bps.
- The Fed held policy steady, while the latest dot plot reflected reduced expectations for easing and greater consensus among policymakers, with the majority signaling one cut or fewer.

### Performance and Drivers

- The Bloomberg US Aggregate Index modestly declined 0.05%, driven by the rise in rates.
- Corporate credit underperformed Treasuries due to spread widening, with lower-quality segments lagging higher-quality.

### Valuations

- Credit spreads were resilient early in the quarter but widened into quarter-end amid software- and AI-related concerns.

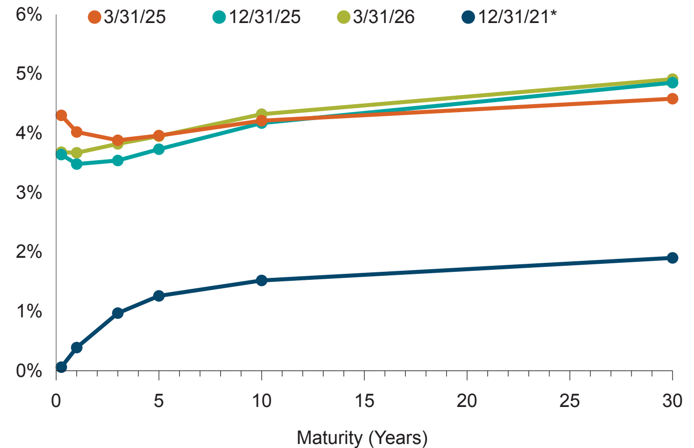
### Relative Value Favors Securitized Over Corporate Credit

- Rich valuations have reduced the attractiveness of credit, contributing to a steady decline in corporate allocations since late 2020 as managers have moved closer to neutral relative to the Bloomberg Agg.
- In contrast, securitized allocations increased meaningfully beginning in 2022 as improved risk/return characteristics and more attractive relative value supported a shift in positioning; allocations have largely plateaued more recently but remain elevated versus history.
- Relative to the Agg, the median manager's corporate overweight has narrowed materially, while securitized has shifted from a modest underweight to a meaningful overweight, underscoring an ongoing preference for securitized over corporate risk.

### AI-driven Financing Needs Boost New Issuance

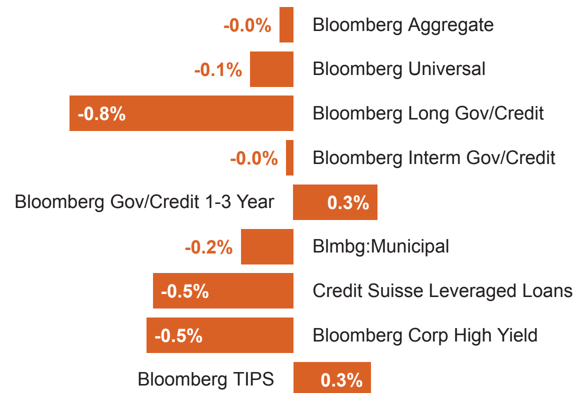
- Corporate bond issuance surged in 1Q26, marking the strongest quarter since 2Q20. Investment grade issuance was

**U.S. Treasury Yield Curves**

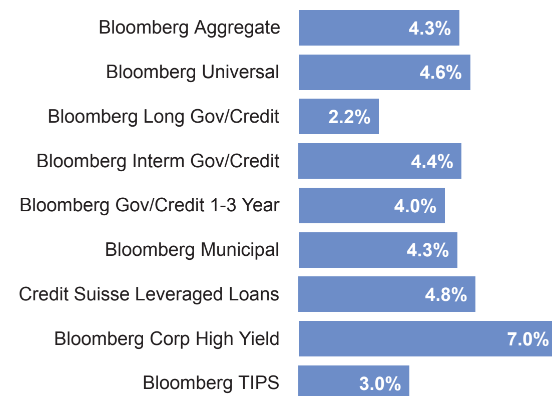



Source: Bloomberg
* Last non-inverted yield curve.

**U.S. Fixed Income: Quarterly Returns** (3/31/26)




**U.S. Fixed Income: One-Year Returns** (3/31/26)




Sources: Bloomberg and Credit Suisse

particularly robust, already reaching roughly 35% of 2020's record annual total and running 14% ahead of last year's pace, despite 2025 posting the second-largest annual issuance on record.

### Municipal Bond Yields Rise

- Municipal bonds generated flat-to-negative performance in 1Q as municipal yields rose and the market entered its typical seasonal supply dynamic—munis have historically experienced an uptick in net new issuance March-April.
- The AAA-rated municipal bond yield curve continued to steepen in 1Q with the front-end slightly declining and longer maturities rising 20 – 35 bps.

### New Issuance Remains Historically High

- Tax-exempt issuance was elevated relative to history with 1Q seeing a total of $122 billion new issuance, a 12% YOY increase, as state and local governments spend on infrastructure, and inflation has increased costs.
- Municipal bond fund flows were on pace to be the third-largest yearly inflows on record.

### Muni Valuations Improve

- Muni/Treasury ratios increased to levels above their five-year averages.

## Global Fixed Income

### Weakness Amid Geopolitical Uncertainty

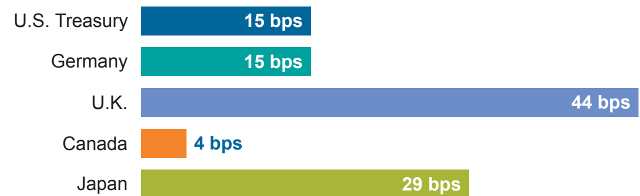
- Global central banks struck a more cautious tone late in the quarter amid inflation concerns and rising geopolitical tensions; but largely held rates unchanged.
- Growth expectations began the quarter broadly stable, with early indicators pointing to continued expansion, but moderated into quarter-end as uncertainty increased. The ECB revised its near-term outlook down, citing weaker consumption and investment.
- Global fixed income returns were negative for the quarter, with developed markets, particularly in Europe, underperforming.

### U.S. Dollar Strengthens

- After initial weakening, the U.S. dollar rallied over the quarter as demand for safe-haven assets increased, benefiting hedged global returns relative to unhedged exposures.

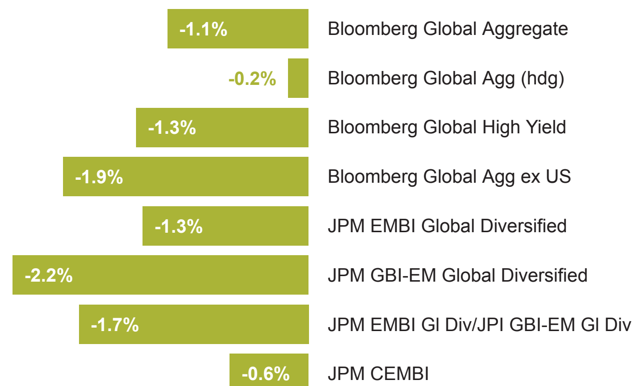
### Change in 10-Year Global Government Bond Yields

4Q25 to 1Q26



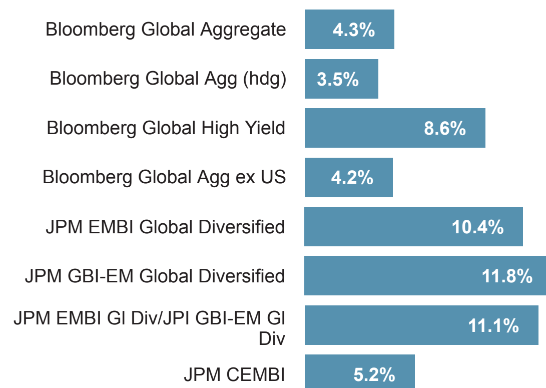

Source: Bloomberg

### Global Fixed Income: Quarterly Returns (3/31/26)




Sources: Bloomberg and JPMorgan Chase

### Global Fixed Income: One-Year Returns (3/31/26)




Sources: Bloomberg and JPMorgan Chase

### Emerging Market Debt Drops

- Emerging market debt declined across both hard and local currency segments as rising global yields weighed on performance. Despite the near-term weakness, EMD performance remains positive over the past year.

# Real Assets Navigate a Mixed Environment

**REAL ESTATE/REAL ASSETS** | Munir Iman

Real assets delivered a nuanced set of results in 1Q26, with signs of stabilization emerging in private real estate even as public markets reflected a more uneven recovery. Income remained the primary driver of returns across private markets, while listed real assets benefited from a sharp rally in energy-related sectors.

### Private Real Estate: Income Leads, Appreciation Lags

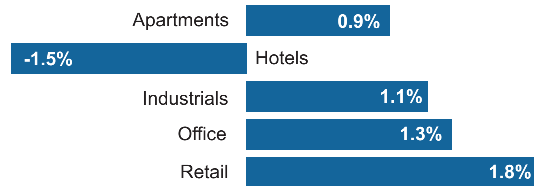
Private real estate performance showed modest improvement during the quarter. The NCREIF Open-End Diversified Core Equity (ODCE) Index gained 1.0%, driven largely by income returns of 0.8%, while appreciation contributed just 0.2%.

Sector-level results highlight the uneven nature of the recovery. Industrial properties were the lone sector to post positive appreciation, while the Residential, Hotel, Office, and Retail sectors experienced declines. Hotel properties, in particular, stood out for negative appreciation, underscoring ongoing volatility in more economically sensitive segments. Regional performance also diverged, with the West lagging due to softening industrial fundamentals in Southern California.

### Transactions and Capital Markets: Activity Rebounds

Transaction activity continues to recover from its recent trough. On a rolling four-quarter basis, both transaction volume and value have increased and now exceed five-year averages.

**Sector Quarterly Returns by Property Type** (3/31/26)




Source: NCREIF

### Liquid Real Assets: Energy Drives Performance

In liquid markets, commodities delivered strong gains, led overwhelmingly by energy. The S&P GSCI Energy Total Return Sub-Index surged amid geopolitical tensions and supply concerns, while other commodity sectors—including metals and agriculture—also posted solid gains.

Listed real assets reflected a similar pattern. Natural resources equities benefited from higher energy prices, and listed infrastructure generated positive returns as investors rotated toward more defensive sectors.

REIT performance was positive overall but varied significantly by sector. U.S. REITs rose 4.9% for the quarter, outperforming the broader equity market, while global REITs gained 1.0%. However, performance dispersion remained pronounced, with self-storage advancing sharply while the Office and Residential sectors declined.

**Callan Database Median and Index Returns* for Periods Ended 3/31/26**

| Private Real Assets | Quarter | Year to Date | 1 Year | 3 Years | 5 Years | 10 Years | 20 Years |
|---|---|---|---|---|---|---|---|
| **Real Estate ODCE Style** | **1.0** | **1.0** | **3.7** | **-2.1** | **3.1** | **4.4** | **4.6** |
| NFI-ODCE (value-weighted, net) | 1.0 | 1.0 | 3.1 | -2.8 | 2.3 | 3.8 | 4.6 |
| NCREIF Property | 1.2 | 1.2 | 4.8 | 0.0 | 3.7 | 4.7 | 6.2 |
| NCREIF Farmland | -0.2 | -0.2 | -0.1 | 0.6 | 4.0 | 4.7 | 9.3 |
| NCREIF Timberland | 1.1 | 1.1 | 4.9 | 6.8 | 8.7 | 5.5 | 6.1 |
| **Public Real Estate** | | | | | | | |
| **Global Real Estate Style** | **1.3** | **1.3** | **9.9** | **7.9** | **3.1** | **4.7** | **5.2** |
| FTSE EPRA Nareit Developed | 8.8 | 8.8 | 17.7 | 11.2 | 7.8 | 7.6 | 7.7 |
| **Global ex-U.S. Real Estate Style** | **-3.7** | **-3.7** | **12.4** | **6.2** | **-0.4** | **3.8** | **3.5** |
| FTSE EPRA Nareit Dev ex US | -4.5 | -4.5 | 15.7 | 5.7 | -1.4 | 1.5 | -- |
| **U.S. REIT Style** | **4.0** | **4.0** | **5.7** | **8.6** | **5.5** | **6.3** | **6.6** |
| FTSE EPRA Nareit Equity REITs | 4.8 | 4.8 | 6.8 | 9.1 | 5.8 | 5.6 | 6.1 |

*Returns less than one year are not annualized. Sources: Callan, FTSE Russell, NCREIF

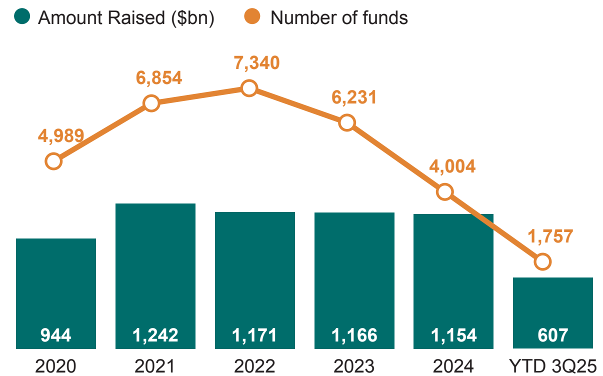
# Fundraising Takes a Big Hit in 3Q25

**PRIVATE EQUITY** | Ashley Kahn

**Fundraising ▶** By both volume and deal count, fundraising for YTD 3Q25, the latest data available, declined by ~30% versus YTD 3Q24. Persistent exit backlogs and limited distributions have constrained LP capacity for new commitments.

**Deal Activity ▶** Deal volume rebounded sharply during 3Q, rising 80% versus 2Q25 and returning to levels last seen in 2021. Deal count continues to drop, however, falling an additional 6% this quarter. The divergence between rising deal volume and declining deal count has persisted throughout the year, reflecting the continued concentration of capital in larger transactions.

**Annual Fundraising** (9/30/25)




Source: Pitchbook

**Buyouts ▶** Buyouts roared back in 3Q25 after a brief lull in 2Q. Greater macroeconomic certainty, strong public markets performance, and Fed rate cuts fueled a rapid rebound in activity, confirming that the 2Q25 slowdown (following April's Liberation Day) was only temporary.

**Venture Capital and Growth Equity ▶** The AI boom continues to drive venture capital activity, with deal volume and valuations pointing to a bull phase in venture's typically cyclical market. Capital is concentrated in the largest transactions; YTD 3Q25 deal volume is up 33% from the same time last year, while deal count is down 21%. AI "mega deals" (>$1b) represented 70% of 2025 deal value.

**Exits ▶** Exit volume picked up meaningfully, with 3Q activity nearly doubling 2Q levels. M&A has driven the majority of the recovery in exits, posting the strongest rebound with YTD 3Q25 volume up by 57% from the same point last year. IPOs have also regained momentum in 2025, led by several high-profile listings like Figma and Navan. YTD 3Q25 activity is up 20% from the same point last year.

**Returns ▶** Private equity posted steady gains of 2.6% in 3Q25, although trailing public equity's strong performance. Over the short term, private equity's more conservative valuation practices mean the asset class lags when public equity posts such outsized returns.

**Private Equity Performance (%) (Pooled Horizon IRRs through 9/30/25*)**

| Strategy | Quarter | 1 Year | 3 Years | 5 Years | 10 Years | 20 Years |
|---|---|---|---|---|---|---|
| Venture Capital | 5.4% | 14.4% | 2.6% | 12.2% | 13.6% | 12.4% |
| Growth Equity | 3.0% | 10.9% | 6.3% | 11.1% | 13.6% | 12.9% |
| Buyouts | 1.7% | 8.3% | 9.5% | 13.6% | 14.2% | 12.8% |
| **Private Equity** | **2.6%** | **9.5%** | **7.2%** | **12.6%** | **13.4%** | **12.3%** |

Note: Private equity returns are net of fees. Sources: LSEG/Cambridge and S&P Dow Jones Indices
*Most recent data available at time of publication

Note: Transaction count and dollar volume figures across all private equity measures are preliminary figures and are subject to update in subsequent versions of the *Capital Markets Review* and other Callan publications.

# Defaults Stay Low Despite Headlines

**PRIVATE CREDIT** | Constantine Braswell

**Credit Market Environment** ▶ The broad high yield credit default surge anticipated by the post-2022 tightening cycle did not fully materialize (increase from 2% to 3.5%). In other recent cycles high yield default rates have increased from 5% to 11% (2000-01); 2% to 15% (2007-09); and 3% to 8% (2020-21). The long-term average U.S. high yield bond default rate is about 4%.

Private credit defaults (2%) have historically been significantly less than high yield default rates. This has continued to be the case during the current market environment:

- Amend-and-extend activity and sponsor equity support delayed or mitigated distress.
- Private credit's control orientation has enabled earlier intervention versus syndicated markets. Documentation protections such as debt covenants have played a critical role in lender positioning and recovery outcomes.

However, credit risk may be getting deferred rather than eliminated as maturities extend forward.

Widely covered credit events in late 2025 and early 2026 drew increased attention to underwriting standards and recovery expectations. These cases, which primarily impacted the broadly syndicated loan market, were idiosyncratic rather than systemic, concentrated in cyclical and rate-sensitive sectors, and/or related to fraud. They reinforce dispersion in manager performance driven by underwriting and monitoring rigor and workout capability.

**Fundraising** ▶ The top four funds raised in 4Q25 were concentrated outside of U.S. direct lending. In 4Q25, asset-backed finance/specialty finance strategies led capital formation, followed by direct lending, then special situations. We continue to notice increased interest in strategies that complement core direct lending.

**Spreads** ▶ Average M&A loan spreads compressed from 388 bps and YTMs of 9.0% in December 2024 to 325 bps and 7.5% by December 2025, reflecting sustained credit spread tightening and materially lower all-in borrowing costs.

By year end, renewed compression pushed yields toward cycle lows, supported by lower base rates, persistent investor demand for leveraged credit, and continued improvement in issuer fundamentals, allowing M&A loan pricing to end the quarter at the tightest spreads and lowest yields of the past year.

**Loan Volume** ▶ M&A-related institutional loan issuance reached $142.4 billion in 2025. This includes $59.4 billion for LBOs, $40.5 billion for sponsored add-ons, and $42.5 billion for corporate M&A. Despite this uptick, volumes remain well below 2021 peaks, constrained by valuation mismatches, slower deal execution, and lingering macro uncertainty that continue to temper large-scale transaction flow.

**Returns** ▶ Over the past 10 years the asset class has generated a net IRR of 8.9%, outperforming leveraged loans as of 3Q25, the latest data available. Higher-risk strategies have performed better than lower-risk strategies.

**Private Credit Performance (%) (Pooled Horizon IRRs by Strategy through 9/30/25*)**

| Strategy | Quarter | 1 Year | 5 Years | 10 Years | 20 Years |
|---|---|---|---|---|---|
| Senior Debt | 1.1 | 7.7 | 8.3 | 7.9 | 7.8 |
| Subordinated | 2.0 | 9.9 | 12.1 | 11.0 | 10.9 |
| Credit Opportunities | 1.8 | 7.0 | 10.6 | 8.5 | 9.0 |
| **Total Private Credit** | **1.6** | **7.7** | **10.3** | **8.9** | **9.2** |

Source: LSEG/Cambridge
*Most recent data available at time of publication

# Mixed Results for Managers as Markets Shift Rapidly

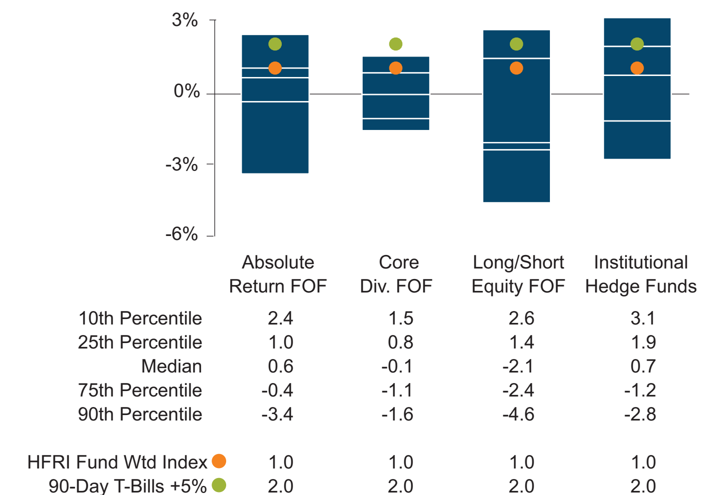
**HEDGE FUNDS/MACs** | Joe McGuane

U.S. equity markets ended 1Q26 sharply lower, reversing a positive start to the year as March brought broad de-risking tied to the U.S.-Iran conflict, higher oil prices, rising inflation expectations, and a repricing of rate-cut expectations. Market weakness was concentrated in March, with correlations moving higher and few areas of the market providing protection outside of energy and defensives. The 10-year Treasury yield rose from 4.17% to 4.32% during the quarter, with the move concentrated in March as oil jumped above $100 and the market repriced inflation risk rather than stronger growth.

The quarter also reflected a notable leadership shift. The S&P 500 declined, but equal-weighted equities and small caps held up better, suggesting more pressure on the very large cap and most-crowded areas of the market. Energy was the standout sector, while Financials, Technology, Industrials, and Consumer Discretionary were meaningful detractors.

Serving as a proxy for large, broadly diversified hedge funds with low beta exposure to the equity market, the median manager in the Callan Institutional Hedge Fund Peer Group rose 0.7%. Within this style group of 50 peers, the average Callan hedged credit manager gained 1.9%, as they were helped by hedges and idiosyncratic catalysts. The average Callan hedged equity manager lost 1.5%, as managers with net-long exposure and positions in software, financials, and AI-sensitive business models generally struggled during the quarter.

**Hedge Fund Style Group Returns** (3/31/26)




| | Absolute Return FOF | Core Div. FOF | Long/Short Equity FOF | Institutional Hedge Funds |
|---|---|---|---|---|
| 10th Percentile | 2.4 | 1.5 | 2.6 | 3.1 |
| 25th Percentile | 1.0 | 0.8 | 1.4 | 1.9 |
| Median | 0.6 | -0.1 | -2.1 | 0.7 |
| 75th Percentile | -0.4 | -1.1 | -2.4 | -1.2 |
| 90th Percentile | -3.4 | -1.6 | -4.6 | -2.8 |
| HFRI Fund Wtd Index | 1.0 | 1.0 | 1.0 | 1.0 |
| 90-Day T-Bills +5% | 2.0 | 2.0 | 2.0 | 2.0 |

Sources: Callan, Credit Suisse, Federal Reserve

**Callan Peer Group Median and Index Returns* for Periods Ended 3/31/26**

| Hedge Fund Universe | Quarter | 1 Year | 3 Years | 5 Years | 10 Years | 15 Years |
|---|---|---|---|---|---|---|
| **Callan Institutional Hedge Fund Peer Group** | **0.7** | **8.8** | **8.9** | **7.5** | **7.7** | **6.9** |
| **Callan Fund-of-Funds Peer Group** | **0.1** | **12.2** | **9.8** | **5.6** | **6.1** | **5.0** |
| **Callan Absolute Return FOF Style** | **0.6** | **8.3** | **7.3** | **6.0** | **4.9** | **4.1** |
| **Callan Core Diversified FOF Style** | **-0.1** | **12.2** | **9.7** | **5.6** | **6.2** | **5.2** |
| **Callan Long/Short Equity FOF Style** | **-2.1** | **14.7** | **12.0** | **5.1** | **6.7** | **5.8** |
| HFRI Fund Weighted Index | 1.0 | 14.0 | 10.0 | 6.1 | 6.8 | 5.1 |
| HFRI Fixed Convertible Arbitrage | 1.8 | 9.2 | 8.9 | 6.1 | 6.8 | 5.3 |
| HFRI Distressed/Restructuring | 2.6 | 12.2 | 10.5 | 6.7 | 7.8 | 5.6 |
| HFRI Emerging Markets | -0.4 | 15.0 | 11.1 | 4.7 | 6.5 | 3.8 |
| HFRI Equity Market Neutral | 1.2 | 10.2 | 9.3 | 6.9 | 4.4 | 3.8 |
| HFRI Event-Driven | -0.5 | 11.2 | 9.7 | 5.9 | 7.0 | 5.4 |
| HFRI Relative Value | 1.7 | 7.5 | 7.8 | 5.5 | 5.5 | 4.9 |
| HFRI Macro | 4.8 | 12.1 | 6.5 | 5.9 | 4.2 | 2.9 |
| HFRI Equity Hedge | -0.5 | 18.2 | 12.2 | 6.4 | 8.2 | 6.0 |
| HFRI Multi-Strategy | -0.1 | 14.2 | 12.3 | 5.3 | 5.8 | 4.3 |
| HFRI Merger Arbitrage | 1.2 | 10.7 | 7.9 | 6.1 | 5.7 | 4.7 |
| 90-Day T-Bill + 5% | 2.1 | 9.0 | 9.7 | 8.3 | 7.3 | 6.5 |

*Net of fees. Sources: Callan, Credit Suisse, Hedge Fund Research

Within the HFRI Indices, the best-performing strategy was macro, which had a strong quarter and gained 4.8%, as managers profited from commodity, currency, and volatility-related positioning. Relative value strategies ended up 1.7%, as convertible bond, credit arbitrage, and interest rate trading pushed performance higher. Event-driven strategies fell 0.5%. Equity hedge strategies ended 0.5% lower, as software and financials detracted from performance, while energy, industrials and biotech positioning were able to offset some of that negative performance.

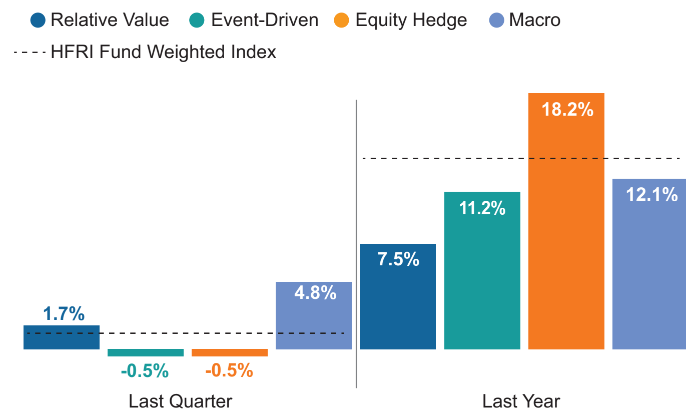
Across the Callan Hedge FOF database, the median Callan Absolute Return FOF gained 0.6%, as their exposure to macro and relative value strategies helped offset negative performance from equity hedge. The Callan Long-Short Index fell 2.1%, as its exposure to technology and AI-disrupted businesses detracted from performance. The Callan Core FOF index ended down 0.1%: macro and relative value manager performance was able to offset most of the negative equity hedge performance.

Since the Global Financial Crisis, liquid alternatives to hedge funds have become popular among investors for their attractive risk-adjusted returns that are similarly uncorrelated with traditional stock and bond investments but offered at a lower cost. Much of that interest is focused on rules-based, long-short strategies that isolate known risk premia such as value, momentum, and carry found across the various capital markets. These alternative risk premia are often embedded, to varying degrees, in hedge funds as well as other actively managed investment products.

Within Callan's database of liquid alternative solutions, the Callan MAC Risk Parity median return was 3.4%, as managers were able to profit off currency and commodity exposure. The Callan MAC Long Biased median return was 0.3%, as energy equity exposure was able to offset negative performance from growth equities during the quarter.

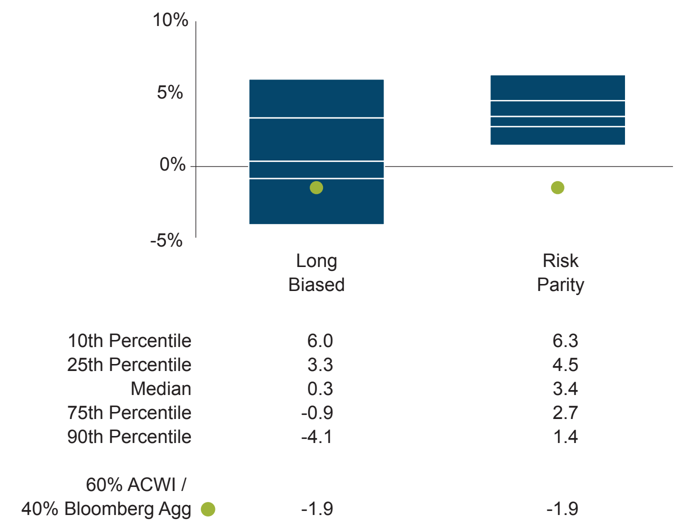
As 1Q wrapped up, the backdrop is increasingly favorable for hedge funds. Geopolitical risks will continue and inflation concerns have returned as oil prices have spiked, and macro volatility, higher interest rates, and cross-asset dispersion will create more alpha opportunities. Elevated equity valuations and crowding around growth sectors provide ample opportunity to generate alpha both on the long and short side of the portfolio.

**HFRI Hedge Fund-Weighted Strategy Returns** (3/31/26)




Source: HFRI

**MAC Style Group Returns** (3/31/26)




| | Long Biased | Risk Parity |
|---|---|---|
| 10th Percentile | 6.0 | 6.3 |
| 25th Percentile | 3.3 | 4.5 |
| Median | 0.3 | 3.4 |
| 75th Percentile | -0.9 | 2.7 |
| 90th Percentile | -4.1 | 1.4 |
| 60% ACWI / 40% Bloomberg Agg | -1.9 | -1.9 |

Sources: Bloomberg, Callan, Eurekahedge, S&P Dow Jones Indices

# Another Gain for the DC Index

**DEFINED CONTRIBUTION** | Scotty Lee

### Performance: Index Gains for Third Straight Quarter

– The Callan DC Index™ gained 2.4% in 4Q25. The Age 45 Target Date Fund (analogous to the 2045 vintage) had a higher quarterly return (2.8%).

### Growth Sources: Balances Rise Due to Investment Gains

– Balances within the DC Index rose by 1.0% after a 3.5% increase in the previous quarter. Investment gains (2.4%) were the primary cause.

### Turnover: Net Transfer Activity Remains Negligible

– Turnover (i.e., net transfer activity within DC plans) was just 0.01% in 4Q25, its lowest level since Index inception. This indicates minimal participant-driven reallocation across asset classes during the quarter, reinforcing that changes were largely driven by market performance rather than investor behavior.

### Net Cash Flow Analysis: TDFs See Net Outflows

– Automatic features have historically led target date funds (TDFs) to receive the largest net inflows in the DC Index. However, in 4Q25, TDFs experienced net outflows of 2.5%.

### Equity Allocation: Exposure Sits Above Long-Term Average

– The Index's overall allocation to equity (75.3%) rose slightly from the previous quarter's level (75.1%). The current equity allocation continues to sit above the Index's historical average (69.1%).

### Asset Allocation: U.S. Large Cap Equities See Gains

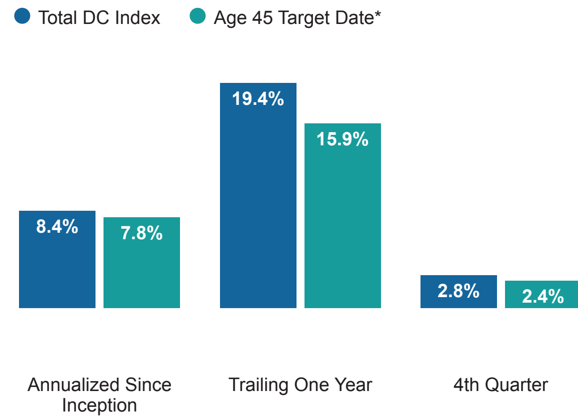
– U.S. large cap equity (29.4%) was the asset class with the largest percentage increase in allocation despite outflows, signaling the asset class was an outperformer. Conversely, stable value (4.9%) and target date funds (36.3%) experienced the largest declines in allocation.

### Prevalence of Asset Class: Money Market Funds Rise

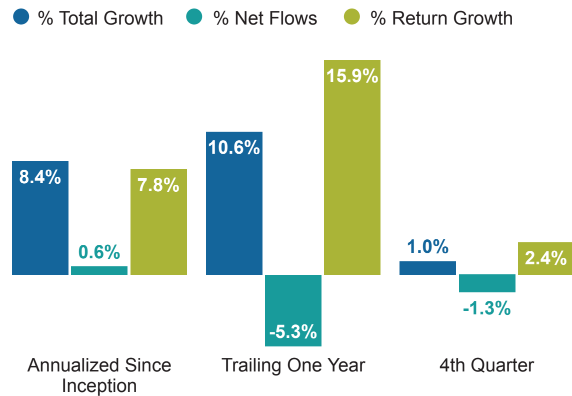
– The prevalence of money market funds (56.1%) rose by 0.8 percentage points. Other notable movements included a 0.8 percentage point decrease in the prevalence of global equity offerings (18.9%).

*Underlying fund performance, asset allocation, and cash flows of more than 100 large defined contribution plans representing approximately $400 billion in assets are tracked in the Callan DC Index.*

**Investment Performance** (12/31/25+)




**Growth Sources** (12/31/25+)




**Net Cash Flow Analysis 4Q25)**
(Top Two and Bottom Two Asset Gatherers)

| Asset Class | Flows as % of Total Net Flows |
|---|---|
| Real Estate | 31.2% |
| Emerging Markets Equity | 29.7% |
| U.S. Small/Mid Cap | -17.7% |
| U.S. Large Cap | -48.3% |
| **Total Turnover**** | **0.0%** |

+ Data provided here is the most recent available at time of publication.

Source: Callan DC Index

Note: DC Index inception date is January 2006.

* The Age 45 Fund transitioned from the average 2040 TDF to the 2045 TDF in June 2023.

** Total Index "turnover" measures the percentage of total invested assets (transfers only, excluding contributions and withdrawals) that moved between asset classes.

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The *Capital Markets Review* is a quarterly macroeconomic indicator newsletter that provides thoughtful insights on the economy and recent performance in the equity, fixed income, alternatives, real estate, and other capital markets.

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