GLENMEDE
PRIVATE WEALTH

The Case for Small Caps and Private Equity in 2026

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As we transition to a new year, we expect to see continued global growth even as we recognize that this growth may be uneven from one region to another. We also anticipate continued volatility, though it is always difficult to predict the catalysts. As long-term investors, we are less concerned with shorter-term bouts of volatility and instead focus on identifying opportunities to compound capital at competitive risk-adjusted returns.

The Foundations of a Strong Portfolio

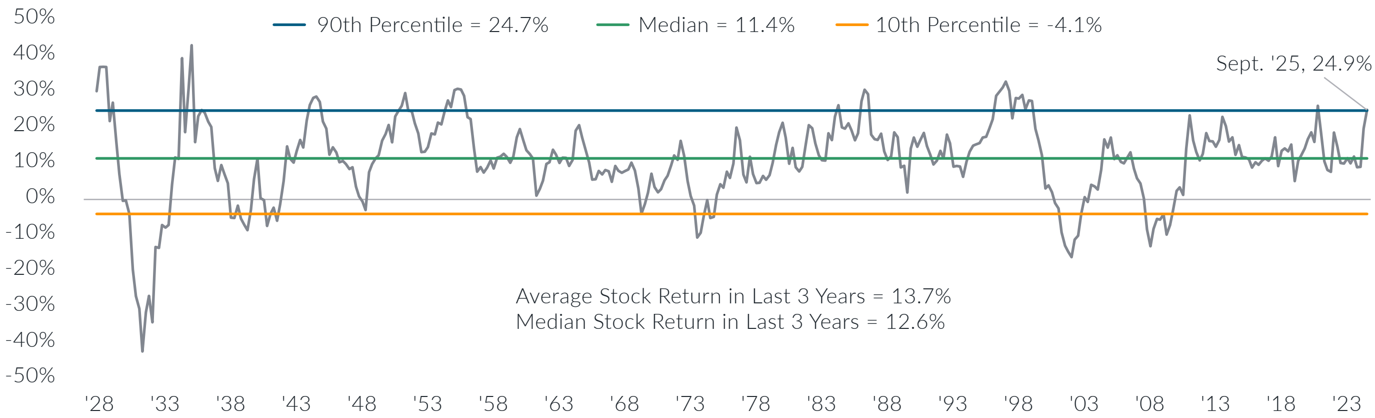
It is always a good idea to align investments with one's ability and willingness to take risk. Incongruency can create discomfort or worse, including the permanent impairment of capital. When volatility manifests itself, it is typically most acute over shorter periods (12 to 18 months). If you can weather volatility without reacting or, even better, take advantage of it, you can build a great foundation for compounding capital over the longer term. We spend a lot of our time trying to understand the return and volatility profile of our clients, which is foundational to building a portfolio appropriate for them.

Some areas of the market (e.g., components of the technology and communication services sectors and their associated concentration) have been trading near all-time highs and at elevated valuations, while other areas of global capital markets have appeared relatively more attractive and reasonably priced. Regarding the former, we remain concerned with portions of the market that are priced for long-enduring excellence. Two areas where we continue to find opportunities are U.S. small cap equities and private equity. Our view is that small cap and private equity have been de-emphasized by many investors as they gravitate toward more popular and thematic areas of the market. After a period of relative underperformance, we are constructive on the forward-looking prospects for these two asset classes.

U.S. Large Cap Equity

Large cap indices, such as the S&P 500 and Russell 1000, have experienced abnormally large appreciation in recent years (Exhibit 1). The magnitude of these returns is an uncommon phenomenon, with the 3-year return at the 91st percentile and the 5- and 10-year returns at the 78th percentile.

Exhibit 1: S&P 500 3-Year Rolling Annualized Return



Source: Ibbotson (1926–1987), S&P, FactSet (1988–present)

Data as of 9/30/2025

Based on these numbers, it is tempting to think that the market has been great for most stocks. However, given the narrowness of the market, we would not be quite as enthusiastic. As shown in Exhibit 1, the average and median stock return has been substantially less than the market average, with the Magnificent 7[1] and other thematic stocks disproportionately driving market returns. We are skeptical about whether these patterns are repeatable, not because the "big growers" are bad companies, but because they are priced as if they can sustain such growth well into the future. Of all market sectors, creative destruction is very pronounced with technology because innovation is in constant motion. Although these popular thematic companies may pose a headwind to future returns for the S&P 500, we continue to see reasonable valuations across other sectors.

U.S. Small Cap Equities

Rarely have small caps traded at a larger discount to large caps than they do currently. In our view, small cap equities represent one of the more compelling investment opportunities available across capital markets, with some caveats. Over several years, the quality of the Russell 2000 has deteriorated, as defined by the proportion of nonearning companies comprising the index (Exhibit 2). This nonearning cohort typically does not outperform over the long term (Exhibit 3), though they do exhibit sharp counter-trend rallies over the short term. In other words, nonearners typically exhibit long periods of underperformance punctuated by brief moments of glory, something we just experienced from the second to third quarters of 2025 (Exhibit 4).

Exhibit 2

Market Cap Weight of Nonearners in Russell 2000 | *Number of Nonearners as % of Russell 2000 Constituents*

Source: Glenmede, FactSet

Data as of 9/30/2025

Exhibit 3: Returns and Profitability—Trailing 10-Years

Russell 2000 Quintiles	Average Weight	Annualized Return (%)	Return on Invested Capital, LTM
Quintile 1 (Highest Profitability)	21.3%	18.0	18.4
Quintile 2	19.8%	11.9	6.7
Quintile 3	19.0%	8.3	2.6
Quintile 4	15.0%	2.9	-5.7
Quintile 5 (Lowest Profitability)	10.1%	-2.7	-69.5
N/A	14.7%	14.1	--

N/A: companies with missing return on invested capital (ROIC) data, or companies without full membership in the index during the time period. The quintiles based on ROIC are rebalanced on an annual basis.

Source: Glenmede, FactSet | Data from 11/30/2015 to 11/30/2025

Exhibit 4: Returns and Profitability—Q2-Q3 2025

Russell 2000 Quintiles	Average Weight	Total Return (%)	Return on Invested Capital, LTM
Quintile 1 (Highest Profitability)	30.0%	23.5	18.4
Quintile 2	25.3%	14.4	6.3
Quintile 3	19.7%	14.4	1.8
Quintile 4	14.5%	24.4	-8.2
Quintile 5 (Lowest Profitability)	10.1%	47.5	-67.4
N/A	0.4%	36.1	--

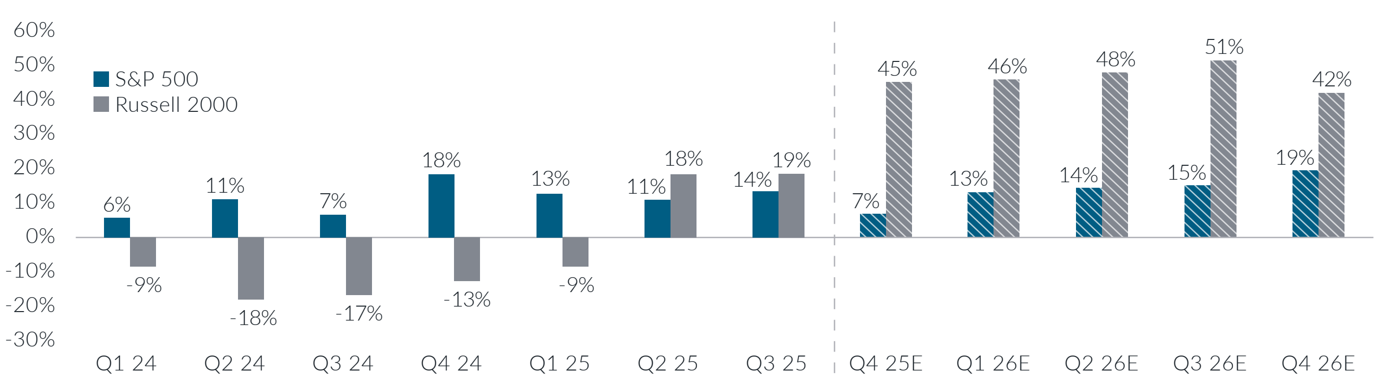
N/A: companies with missing ROIC data, or companies without full membership in the index during the time period.

Source: Glenmede, FactSet | Data from 3/31/2025 to 9/30/2025

Given these factors, we are most interested in high-quality small companies, which we define as those companies generating good free cash flow margins, attractive returns on capital, and disciplined capital allocation. While the trend of passive investing in domestic large caps has been increasing in recent years, we believe small caps are an area where it pays to be more active given lower quality and greater market inefficiencies.

In our opinion, the backdrop for small caps is quite constructive. Solid economic growth and fiscal policy tailwinds should help support top-line growth. Declining interest rates should act as a tailwind as smaller companies typically employ more leverage and floating rate debt. In fact, we are seeing an improving absolute and relative earnings picture for small caps (Exhibit 5). Lastly, with small cap companies at record low weights as a proportion of the total U.S. equity market and a lack of investor appetite after a long period of underperformance, we believe the odds are in our favor for this contrarian view.

Exhibit 5: Earnings Growth, Quarterly Year Over Year



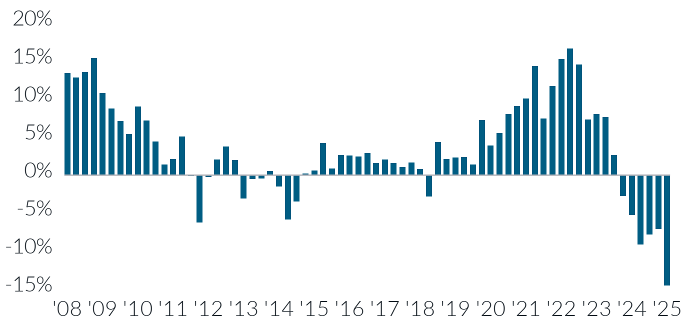
Source: Glenmede, FactSet | Data as of 12/18/2025

Private Equity

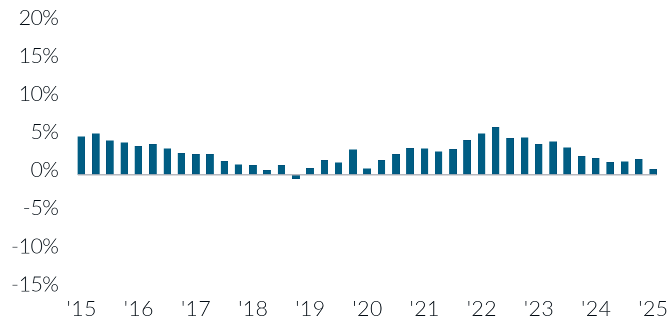
For clients with long (10 to 15 or more years) investment time horizons and an appetite for complexity, we believe private equity offers a compelling opportunity to compound portfolio growth. Over intermediate and long-term periods, private equity has often outperformed public equities, as defined by the S&P 500 (Exhibit 6). With that said, over recent 3-year rolling periods, private equity has experienced one of its largest levels of relative underperformance compared with public equities. We expect mean reversion to swing in favor of private equity over future rolling periods.

Exhibit 6:

3-Year Rolling Excess Return of Private Equity Versus S&P 500



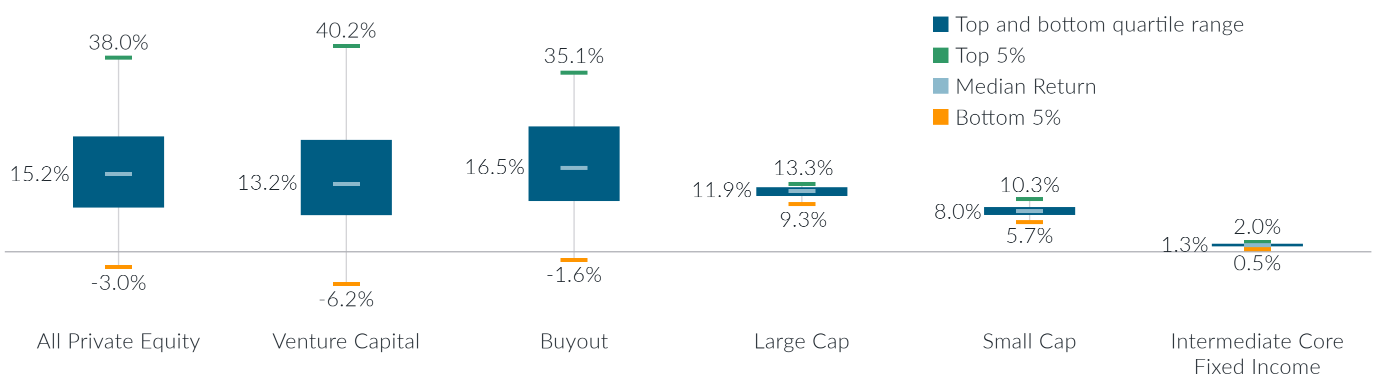
10-Year Rolling Excess Return of Private Equity Versus S&P 500



Source: MSCI North America Private Equity Index | Data as of 6/30/2025

A key consideration when investing in private equity is the large dispersion of returns between first quartile partnerships and the median (Exhibit 7), which looks very different than the dispersion in public market asset classes. This data demonstrate how important it is to have access to top-tier partnerships across multiple vintages. Moreover, there is a strong serial correlation in the performance of top-tier partnerships—those with top-tier performance often maintain superior outcomes for their funds across various vintages.

Exhibit 7: Private and Public Performance Ranges by Strategy



Source: Glenmede, MSCI Burgiss, Morningstar | Data as of 12/31/2024

Over the course of 2026, we intend to develop a pipeline of select direct and commingled private equity investment opportunities for eligible investors. Spanning buyout, growth, and venture, we expect these opportunities will be focused on several economic sectors, including healthcare, technology, industrial, and business services, to name a few.

Prepared for Opportunity in 2026

As we progress through 2026, you can expect to hear more about our thoughts on various opportunities and how we are positioning portfolios. We are prepared to take advantage of opportunities when they constitute a “fat pitch” but remain most focused on the long-term compounding of capital while generating competitive risk-adjusted returns.

For now, I wish all of you a happy new year and remain your partner in purpose.

[1] The Magnificent 7 (or Mag 7) is a group of major tech companies with stock growth that, on average, far outpaced the high-performing S&P 500 over the past decade, but particularly in 2023 and 2024. Coined in 2023, the group consists of Alphabet (Google), Amazon, Apple, Meta Platforms, Microsoft, Nvidia, and Tesla.