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Neuberger Berman BKS Select All Cap Core Portfolio

PORTFOLIO MANAGERS: BKS Select Investment Group

Performance Highlights

The Neuberger Berman BKS Select All Cap Core Portfolio posted a positive return (net of fees) in the third quarter of 2025, but underperformed its benchmark, the S&P 500 Index (the S&P 500 or the Index) for the same period.

Market Context

Despite shifting trade policies and a weaker labor market, the S&P 500 rose steadily in the third quarter, finishing just below all-time highs. Better than expected corporate earnings, easier monetary policy, and lower bond yields propelled the market. The S&P 500 advanced 8.1% during the third quarter, lifting its year-to-date total return to 14.8%. Although large-cap technology stocks continue to account for much of the index return, lower interest rates also boosted other sectors of the stock market. The S&P 500 Equal Weight Index returned 4.8% and 9.9% in the third quarter and year-to-date periods, respectively.

We believe that corporate earnings for the balance of 2025 should remain strong and are projected to grow approximately 13% in 2026. Earnings growth has been led by mega-cap technology stocks in recent years, but the growth gap versus non-technology sectors could narrow in 2026 if the economy reaccelerates, potentially leading to a more balanced market. Elevated valuations persist, with the S&P 500 trading at about 22 times next year's earnings estimates. Valuations outside large cap technology stocks are more reasonable, with the S&P 500 Equal Weight Index trading at 17 times estimated 2026 earnings.

In September, the Federal Reserve (the "Fed") cut the Federal Funds target rate for the first time since December, lowering it by 0.25% to a range of 4.00% – 4.25%. This decision was prompted by softening employment data despite the fact that inflation remains above the Fed's target. Markets generally welcomed this move, believing that policymakers stood ready to tolerate somewhat elevated inflation to counteract slowing economic momentum. Lower borrowing costs for both consumers and businesses should boost economic growth. The committee signaled it may continue to decrease interest rates by an additional 1% over the next year, although future cuts will remain dependent on labor market developments and future inflation readings.

Trade negotiations remained a focal point during the quarter, with some clarity emerging following turbulence earlier in the year. The administration extended the 90-day pause on country-specific tariffs in early July and reached bilateral agreements with several countries, although negotiations with others, particularly China, remain active. Currently, aggregate tariffs on imported goods are nominally 17%, up from 2.5% at the beginning of the year, but realized tariff collections have been barely over half that amount because of supply chain adjustments and various loopholes. The legality of most of the tariffs remains under dispute, but alternative mechanisms to impose tariffs are largely available, so sustained elevated tariffs are likely. While businesses and consumers have thus far withstood these challenges remarkably well, their full impact has not yet been felt, and we believe that tariffs remain a risk to near-term growth expectations.

The fiscal stimulus provided by the "One Big Beautiful Bill Act" should bolster economic activity, particularly in 2026 and offset most of the incremental cost of tariffs. The legislation's corporate provisions, including immediate expensing of capital investments and research and development expenditures, should encourage businesses to accelerate spending and reinvest in productivity. Additionally, consumers are likely to benefit from higher limits on state and local tax deductions, elimination of tax on overtime and tips, the increased Child Tax Credit, and various other provisions. Lower interest rates, reduced taxes, potential productivity improvements driven by artificial intelligence, and deregulation should provide a tailwind for both business investment and broader economic growth during 2026.

The economy appears to have grown steadily in Q3, though with noteworthy areas of weakness. Job openings have decreased, particularly for recent graduates. Consumer spending has been resilient overall but uneven. Affluent consumers continue to spend, but lower income consumers have been much more cautious. Forward-looking manufacturing and services indicators appear mixed, while inflation is likely to rise as the full impact of tariffs takes effect.

Portfolio Review

The Neuberger Berman BKS Select All Cap Core Portfolio posted a positive return for the third quarter of 2025 but underperformed the return of the S&P 500 during the same period. Information Technology, Health Care, and Financials are the most heavily weighted sectors in our portfolio. During the quarter we increased our weighting in Financials, Healthcare and Communication Services and reduced our cash position.

Compared with the Index, the Portfolio's relative performance in the third quarter was negatively impacted by stock selection in Information Technology, Financials, Health Care, Consumer Discretionary, and Consumer Staples and positively affected by Communication Services and Utilities. Our sector weighting in Cash, Health Care and Communication Services detracted from performance while Consumer Staples, Information Technology and Real Estate were additive to our performance. Cash was approximately 5.9% at the end of the quarter.

Most client equity portfolios have enjoyed attractive absolute returns over the past couple of years. Performance relative to the S&P 500, however, has been challenging for most active managers, including ourselves. Since the new tariff policies were announced in April, the artificial intelligence ("AI") theme has dominated the capitalization-weighted returns for the S&P 500. We have maintained substantial AI exposure even as the valuations and index weightings have risen. As prudent risk managers, however, we have chosen to limit our concentration in these AI winners to protect against unanticipated downshifts in AI spending or development. Our caution in this regard has not yet paid off.

A more impactful factor to recent performance has been developments in several long-held, high-quality stocks that fall into the category we call "quality compounders." Quality compounders are corporations that deliver dependable earnings growth year after year. From time to time, however, even quality compounders encounter business challenges that temporarily throw them off track and result in stock price declines. When this happens, we step up our research intensity to re-examine our investment thesis and determine whether the long-term investment case is intact. This discipline traces back decades, and we have seen many impressive comebacks by companies that withstand our rigorous review.

Market Outlook

Against this backdrop, we see balanced risks. Positive factors include lower oil prices, fiscal stimulus from the tax bill, lower interest rates, investment in critical infrastructure (including data centers for artificial intelligence), and healthy household balance sheets in aggregate. Offsetting risks include trade policy uncertainty, labor market softness, the potential for higher inflation, and elevated market valuation levels.

All disciplined investors committed to an investment philosophy will find themselves out of sync with their benchmark at times. We have found that, despite periodic manias and crashes, ultimately valuation matters. We are mindful of the need to participate in promising trends, but we are not willing to take excessive risks with your capital.

We appreciate your trust and partnership. Please reach out with any questions or to discuss how recent developments may affect your long-term objectives. We welcome the opportunity to review your portfolio and its alignment with your goals and risk tolerance.

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The S&P 500 Index consists of 500 stocks chosen for market size, liquidity, and industry group representation. It is a market value weighted index (stock price times number of shares outstanding), with each stock's weight in the Index proportionate to its market value. The "500" is one of the most widely used benchmarks of U.S. equity performance. As of September 16, 2005, S&P switched to a float-adjusted format, which weighs only those shares that are available to investors, not all of a company's outstanding shares. The value of the index now reflects the value available in the public markets.

The S&P 500® Equal Weight Index (EWI) is the equal weighted version of the widely used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 EWI is allocated a fixed weight - or 0.2% of the index total at each quarterly rebalance.

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