

Newsletter: April 2026

After reaching 7,000 for the first time ever in January, the S&P 500 traded below 6,400 towards the end of March, its lowest level since August of last year. In this letter we intend to discuss three themes as they unfolded during the first quarter that have contributed to the equity market's recent selloff from its all-time highs, including how these themes are affecting some of our individual investments. We conclude with a brief discussion of our outlook.

Theme #1: The potential disruption of software and other businesses from artificial intelligence

Since ChatGPT was launched by OpenAI in late 2022, people have experimented with the chatbot in myriad ways, businesses have utilized artificial intelligence (AI) in an effort to increase productivity and efficiency, and large technology companies have invested a tremendous amount of capital in data centers and related technical infrastructure that provide the computational power behind AI. Among the ongoing debates sparked by the rise of AI are whether AI-generated output tends towards the high-quality or mere "slop," the extent to which the adoption of AI will lead to significant job losses, and the risk that enormous capital investment by large technology companies constitutes a financial bubble.¹

Despite all the attention that AI has garnered in the last few years, it was not until just a few months ago that capital markets started more meaningfully to price in the fear that certain software companies and other businesses could be substantially disrupted by their customers' adoption of AI. A proximate catalyst for this fear was the release in early February by Anthropic, which competes with OpenAI, of a series of easy-to-use AI tools that could, with seemingly impressive proficiency, write and summarize documents, analyze and organize data, write software code, and complete various other tasks within a computer interface. Would the availability of such tools reduce the demand from corporate customers not only for traditional enterprise software but also for professional and information services of all kinds? Across the market, hundreds of billions of dollars of market cap were quickly lost in response. In our portfolio, a number of stocks were affected, including **Roper Technologies (ROP)**, **CoStar Group (CSGP)**, and **Microsoft (MSFT)**.

ROP owns a collection of businesses that primarily provide "vertical" software—that is, software designed for a single industry sector or niche, such as compliance software for insurance companies. Vertical software tends to be narrow but deep, highly customized, closely integrated with the customers' systems and processes, based on proprietary customer data, system-of-record (e.g., electronic medical records), and mission-critical. We believe that vertical software with these characteristics is the least likely to be disrupted by third-party AI tools, which lack customization and deep integration. Many of ROP's vertical software businesses are in regulated industries, which further solidifies ROP's relationships with its customers, for which switching software vendors is costly and risky to begin with. Perhaps most importantly, ROP's businesses are actively deploying AI features and functions into their own software offerings, which underscores that AI represents an opportunity for incumbents that integrate the new technology into their suite of services.

CSGP provides real estate data, analytics, and marketplaces, and has an enormous proprietary database based on decades of customer relationships. In our view, CSGP's proprietary database constitutes a unique strategic asset that is well insulated from third-party AI tools, which are trained on publicly available data. And like ROP, CSGP is incorporating AI capabilities into its products and services. Separate from the AI debate, CSGP's share price has been buffeted in recent months by the company's continuing investment in its residential real estate effort, which

¹ We have discussed AI in multiple recent newsletters. For prior newsletters, please see our website: <https://beckmack.com/>.

is not yet profitable (in contrast to its highly profitable and much larger commercial real estate business) and which has drawn the attention of activist investors; this is a topic we may revisit in future letters.

Unlike ROP and CSGP, **MSFT** is major provider of “horizontal” software—e.g., Excel, Word, and PowerPoint are used by more than a billion people in both their individual lives and in virtually every kind of business. There are, however, several important respects in which MSFT’s overall business is not merely protected against but also positioned to benefit from AI adoption. For instance, MSFT has released Copilot and Copilot Cowork, which function as an AI-based digital assistant and digital agent, respectively. These and other tools facilitate deeper and more productive engagement with the underlying horizontal software, which are already a core part of their users’ daily workflows. MSFT’s Azure is the second largest public cloud business, which is experiencing unprecedented demand growth related to the AI buildout, which requires data centers with enormous computational capacity. MSFT also owns part of both OpenAI and Anthropic, has exclusive access to OpenAI’s intellectual property through 2030, and has its own proprietary AI models.

For ROP, CSGP and MSFT, the short-term share price action has been dominated by the emergent AI competitive threat, while the long-term impact on business values will reflect the companies’ own competitive responses, including their incorporation of AI into their products and services and their continuous adaptation to the evolving requirements of their customers. Amid the emergence of a disruptive technology, businesses that stand still will indeed be disadvantaged, but for those that innovate what begins as disruption can become a source of competitive strength. AI will change the contours of certain industries and how they function—e.g., the principal way that software is priced may shift from a per-seat model to a consumption-based model—and successful operators will be those that navigate these changes with aplomb.

To a lesser extent, other stocks, such as **Arthur J. Gallagher (AJG)** and **Charles Schwab (SCHW)**, have also been caught up in the so-called “AI scare trade,” and the basis for apprehension in these cases has been thinner than in those described above. But regardless of how reasonable or unreasonable AI-related apprehension may be in any particular instance, the rapid repricing in the market reflects a broader phenomenon: future earnings growth across a range of industry sectors, especially software, is now being valued more cheaply in response to greater perceived uncertainty regarding business durability. A corollary is that **the prospective risk/reward in businesses whose long durability we can still underwrite with conviction has become more attractive in this environment.** For each of the portfolio companies discussed above, we now own the stock at a cheaper multiple of this year’s earnings (as compared to the beginning of the year), while we believe that the future earnings growth trajectory remains largely intact.

Theme #2: Is there a crisis brewing in private credit?

In recent months there has been a barrage of negative press about private credit, which has adversely affected the share prices of **Apollo Global Management (APO)**, **Blackstone (BX)**, and other alternative asset managers. In preview, our perspective is that **while the business prospects of APO and BX have rarely been brighter than they are today, the stocks are valued more cheaply as a multiple of current and future earnings than they have been in years.**²

Though private credit has been much in the press, the term is often used loosely and not precisely defined. There are two essential criteria: (i) lending by financial institutions other than banks; and (ii) loans that are not publicly traded or otherwise highly liquid. The first criterion emphasizes the identity of the lender, and the second emphasizes a characteristic of the loan. In the looser usage of the term, sometimes only one criterion applies, and sometimes the intended reference is to a smaller subset within private credit. A common example of the latter is leveraged lending by business development companies (BDCs). “Leveraged” lending refers to lending to

² We discussed BX and APO at length in our October 2023 newsletter.

borrowers that already have a lot of debt on their balance sheets, and BDCs are a kind of closed-end investment company that makes loans and whose own stockholders tend to be retail investors.

For background, here is a sequence of relevant recent events:

- The Federal Reserve reduced short-term interest rates in late 2024 and then again in late 2025. Much of private credit, and especially leveraged lending, tends to be in the form of floating-rate loans, which are priced as a fixed spread over short-term interest rates. Thus, as short-term interest rates move lower, floating-rate loans generate less interest income. For BDCs, floating-rate loans are their primary asset, hence lower interest rates mean lower earnings, and as a result several BDCs have reduced their dividends.
- In September of last year, both subprime auto lender Tricolor and auto parts seller First Brands, which are independent of each other, filed for bankruptcy amid accusations of fraud. Most of the companies' debt had been originated by banks.
- During the fourth quarter of last year, the share prices of publicly traded BDCs declined and traded at significant discounts to net asset value (NAV), which is based on a loan-by-loan fair value analysis conducted by BDCs every quarter. The discounts to NAV reflected (i) concerns that fair value was overstated and/or would decline due to credit losses and (ii) announced or anticipated dividend reductions.
- At the same time, nontraded BDCs experienced an increase in redemption requests. Because they do not trade on public stock exchanges, nontraded BDCs offer liquidity to their shareholders on a quarterly basis, and typically up to 5% of NAV can be redeemed per quarter. If redemption requests exceed that limit, then a BDC either prorates redemptions (e.g., if redemption requests are 10% of NAV, then redemptions will be 50% of the requested amounts) or elects not to enforce the limit. Because the underlying loans held by BDCs are not highly liquid, the redemption limit is intended to prevent a forced or hasty sale of assets at discounted valuations, which would harm non-redeeming shareholders. On the other hand, if assets can be sold at fair value, then redeeming in excess of the limit avoids negative headlines about the BDC "gating" investors.
- The sharp AI-induced market correction noted above also ensnared BDCs, alternative asset managers, insurance companies, banks, and other financial institutions that had made loans to or otherwise invested in businesses that are perceived to be at risk of being disrupted by AI adoption.
- In late February, UK property lender Market Financial Solutions (MFS) filed for the UK equivalent of bankruptcy, and, like Tricolor and First Brands, it too was accused of fraud. Unlike those other two companies, however, MFS borrowed significantly from non-banks, including from a company partly owned by APO.³
- In the first quarter, some BDCs reported credit deterioration in their loan portfolios, and nontraded BDCs yet again experienced elevated redemption requests, with some opting to prorate redemptions and others redeeming in excess of the limits.

This fact pattern, filtered through a voluminous amount of negative press that is not always careful or complete, is the backdrop for the large recent declines in the share prices of APO and BX. Despite these challenges, why are we so excited about the business prospects for these two companies?

At 3% and 8%, respectively, **BDCs represent a small portion of APO's and BX's assets under management (AUM)**. For businesses whose total AUM routinely grows in the double-digit percentages, these amounts are simply not that significant. There is also no evidence of "contagion" whereby volatility in BDCs migrates to other channels, and indeed there are indications that some investors redeeming from BDCs are reallocating that capital to other alternative asset products.

The BDC market is undergoing a momentarily uncomfortable but ultimately healthy recalibration, whereby retail investors and the financial advisors who invest on their behalf gain a fuller appreciation of the investors'

³ The exposure of ATLAS SP Partners, in which APO owns a stake, to MFS represented less than 1% of ATLAS's balance sheet.

liquidity needs, their investment parameters, and BDCs as an investment vehicle. The 5% quarterly redemption limits have always been front and center in nontraded BDC disclosures; this is by no means a case of having to “read the fine print.” Every financial asset under the sun can be profiled in terms of its risk, return, and liquidity, and any capital invested in nontraded BDCs ought to be regarded as largely illiquid and the prospective investment returns as sensitive to interest rates.

A few years ago, BX’s nontraded real estate investment trust (REIT), BREIT, experienced a similar temporary period of elevated redemption requests and elected to prorate redemptions. And just like the current moment with BDCs, the financial press relentlessly covered BREIT at the time, which in turn temporarily weighed on BX’s share price. **BREIT, which began in 2017, today has \$55 billion of AUM** and has generated more than a 9% net return since inception, which is far in excess of the returns of publicly traded REITs during that period.

The alternative asset management industry has **multiple powerful secular tailwinds**:

- As societies become ever richer, their aggregate **investable wealth tends to grow more quickly than their underlying economies**. For both institutional and individual investors, the ability to invest this wealth across different asset classes and geographies and to allocate capital optimally within a framework of return, risk, and liquidity (see above) thus becomes increasingly important. Alternative asset managers provide the depth of expertise and the breadth of distribution and product capabilities to meet this growing demand.
- With respect to individual investors, there is a **retirement crisis underway in the US** and across the globe, whereby much of the working-age population is not on track to generate sufficient lifetime savings. Consider the traditional 60/40 portfolio, where 60% is invested in an S&P 500 index fund and 40% is invested in Treasury securities. First, this portfolio is extremely liquid, even though the investor is saving for retirement and will not draw on this capital for many years or even decades. Second, the power of compounding is such that over 30 years the difference between compounding at 7% and compounding at 8% is that at the end the latter will be worth 32% more than the former. Hence, the potential for somewhat less liquid investments to generate superior returns could prove to be a critical component of a solution to this crisis. APO is already the leading provider of fixed annuities, and we expect that the offerings of alternative asset managers will become accessible in the 401(k) channel.⁴
- **Individual firms and economic sectors have enormous capital needs** both today and in the coming decades. The transition to clean energy, the need to upgrade and expand utility infrastructure and the electric grid, the aforementioned investment in data centers, and the onshoring of industrial manufacturing capacity require tremendous amounts of capital over the next several years.
- **The banking system accounts for a progressively smaller portion** of the total amount of credit extended throughout the economy, and its reliance on customer deposits as a funding source handicaps its ability to make large capital commitments to the kind of long-duration projects mentioned above.
- As with many other sectors, the alternative asset management industry is characterized by a **strengthening competitive position among the largest and best operators**, as institutional and individual investors consolidate their activity among the platforms with the longest and most successful track records and the broadest product offerings. These top competitors, which include APO and BX, are also those investing the most in technology, which further differentiates them from smaller peers.
- Despite the impressive historical growth of the industry, we expect both institutional and individual investors to **increase their allocations to alternative assets** for many years to come, not merely in dollar terms but also as percentages of their investable wealth or capital, which itself will continue to grow.

⁴ The S&P 500 has also become increasingly concentrated among a small number of the very largest stocks, and it was in this context that APO CEO Marc Rowan remarked, “We basically have levered the retirement system of the country to NVIDIA,” whose weighting in the S&P is close to 8%. The companies in the S&P 500 collectively account for less than 20% of total employment in the US.

APO and BX share **many other attributes that we associate with great businesses**, including: (i) recurring revenues in the form of management fees, which are increasingly generated by permanent capital;⁵ (ii) strong and rising profit margins; (iii) the ability to grow fee-related earnings without having to reinvest large amounts of capital, which facilitates robust and growing dividends; (iv) clients that tend to be repeat customers; (v) the retention of significant amounts of “dry powder”—i.e., excess liquidity or committed but uninvested client capital—which allows the companies to take advantage of market dislocations and thereby to grow during downturns; (vi) great cultures that attract the best talent; (vii) high insider ownership and the continued involvement of the founders through successful management successions.

Finally, we believe that **the stocks today are substantially undervalued** relative to their business quality and future growth and that the prevailing undervaluation reflects consternation about private credit that will eventually subside. Over time the share prices tend to follow AUM growth, which drives earnings growth, but every so often the trajectories of the share prices and of AUM growth diverge, which creates a compelling opportunity to own truly great businesses at discounted valuations. Now is one of those times.

Theme #3: The unknown duration and consequences of Operation Epic Fury

Our discussion of the war in Iran and the Middle East will be brief and will focus only on factors that are relevant to investing. The sheer duration of the war and of the exceptional conditions associated with it—e.g., the closure of the Strait of Hormuz—is among the most important factors. Simply, the longer it lasts, the more damage will be done to the economy, commodity and financial markets, household budgets, and corporate health.

The rapid rise in the price of oil, though mitigated by the US’s status as a net energy exporter, has caused a comparable increase in the price of gas at the pump, which is a major item in many household budgets. As we have discussed in recent letters, economic growth in the US had already become more compositionally lopsided, with higher-income households accounting for an increasingly disproportionate share of consumer spending—by some measures, the top 10% now account for roughly half of all spending. Lower-income households, which were already grappling with debt burdens and inflation, are now forced to accommodate higher gas prices. We expect their spending in other areas to be curtailed and for credit trends in these cohorts to worsen.

Oil and its derivatives are important inputs for a range of businesses and economic sectors, which now face higher input costs and which thus may increase the prices of their own products and services. Prior to the breakout of war, industrial stocks had been one of the best-performing sectors in the market this year, as investors searched for companies that were insulated from the AI disruption risks discussed above.⁶ The commencement of armed conflict catalyzed an abrupt change in these sectoral shifts, as many industrial businesses are now disadvantaged by higher energy costs.

Our portfolio experienced this energy-driven sectoral reversal to some extent, with **Somnigroup International (SGI)** experiencing potential cost inflation related to petroleum-based bedding foam, long-haul truckers whose vehicles are serviced by **Rush Enterprises (RUSHA)** paying higher diesel prices, and other businesses, such as **Zurn Elkay Water Solutions (ZWS)**, **Sunbelt Rentals (SUNB)**,⁷ and **Ferguson Enterprises (FERG)**, facing higher freight and transportation costs. If the underlying energy commodity markets normalize, then these cost pressures will

⁵ Permanent capital, also referred to as “evergreen,” does not have to be returned to investors by some future date. This is in contrast to the traditional drawdown structure, which is typical of private equity funds and which eventually must exit its investments and return all of the capital to investors.

⁶ A new acronym, “HALO,” was even coined for this phenomenon: heavy assets, low obsolescence.

⁷ Formerly known as Ashtead Group. In early March, the company formally changed its primary stock exchange from the London Stock Exchange to the New York Stock Exchange, in conjunction with which the company also changed its corporate name to Sunbelt Rentals, under which brand name the company has been doing business since inception.

be temporary. Despite these recent headwinds, RUSHA, FERG, and ZWS outperformed the S&P 500 during the first quarter. Pipeline operator **Enterprise Products Partners (EPD)** has also been a strong outperformer.

As increases in the prices of oil and other commodities lead to increases in various input costs, which in turn lead to increases in the prices of finished products and services, there is a broadly inflationary effect throughout the economy, which is aggravated by the fiscal pressure from increased military spending. In response to faster inflation, the Federal Reserve's standard playbook is to increase short-term interest rates or to keep them higher than it otherwise would. Yet interest rates are a particularly blunt and indirect tool when the principal source of inflation is a supply shock. And higher interest rates are likely to most affect the very households on whose budgets elevated gas prices are already having a disproportionate impact. In any case, since the beginning of the year the fed funds futures market has shifted from pricing in more than two quarter-point interest rate reductions by year-end to pricing in none.

Outlook

The outbreak of this war is a powerful manifestation of the inexorable role played by exogenous shocks in financial markets. Investing is always and everywhere characterized by risk, uncertainty, and imperfect information, and thus epistemic humility is of paramount importance even in the best of times. The shock of war is a Tysonian punch in the mouth that underscores the necessity of knowing, and respecting, what one does not know.⁸

As of this writing, we certainly do not know when or how the war ends. Throughout our portfolio and based on what has thus far transpired, we do not believe that short-term financial performance will be significantly impaired or that long-term business value will be lower than what we have underwritten. The longer the duration of the war and of the energy shock in particular, the greater the risks of stagflation—i.e., slow economic growth or outright recession coupled with faster inflation. Macroeconomic data for now remain consistent with an economy that continues to expand, and the financial performance of our portfolio companies and feedback from their management teams suggest a still favorable operating environment on balance.

Independent of the war, we expect some degree of further credit deterioration throughout the economy, primarily from the continued strain on lower-income households as well as from the excessive debt that certain companies assumed in the very low-interest rate environment coming out of the pandemic. Many businesses that took on too much debt circa 2021 and that have since fallen short of their financial targets are now struggling, in the face of higher interest rates, to service that debt and may need to restructure their balance sheets. Some of these businesses are grappling with the additional headwind of AI-related disruption, but in our view the main theme of corporate credit stress is overleverage rather than AI.

If the economy were to enter a recession, we would expect that to affect the short-term financial performance but not the long-term business value of our portfolio companies. Great businesses tend to strengthen their competitive positions during recessions, as they are better able than their peers to take advantage of dislocations through some combination of healthier balance sheets, smarter capital allocation, and superior management and operations. We believe that our portfolio companies would emerge competitively stronger within their respective industries on the other side of any future economic downturn.

We sometimes think about our portfolio as if it were a portfolio of dollar bills that will each grow into two-dollar bills over the next five to seven years, where that growth represents the projected increase in intrinsic business values based on the expanding earnings power of the individual companies. At any point in time, a company's share price may be above or below its corresponding intrinsic value, and today we think that we own many dollar bills selling for, say, 70-80 cents. As long as we do not sell dollar bills for less than 100 cents, we avoid crystallizing

⁸ The boxer Mike Tyson once said, "Everyone has a plan until they [sic] get punched in the mouth."

what would otherwise be merely a temporary share price drawdown into a permanent loss of client capital. And in the meantime, our research is dedicated to the underwriting of a path by which that dollar of intrinsic value, for each of our portfolio companies, grows into two dollars over the next five to seven years.

In the discussion above about APO and BX, we referred to the power of compounding, and this power of course derives from the nature of exponential growth: if capital compounds at 12% for 30 years, for instance, it will be worth nearly 30 times its original amount by the end. But a crucial component of the power of compounding is the necessity of staying invested. Over the last 30 years, if one was invested in an S&P 500 index fund but somehow missed out on just the 10 best-performing days for the index, one's returns would have been less than half of what they would have been if one had been continuously invested. Drawdowns in the share prices of individual companies and in the overall market periodically occur, but **only if one sells at these discounted prices do drawdowns affect one's long-term investment returns, which are otherwise ultimately determined by the long-term growth in the intrinsic value of the underlying businesses.**

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