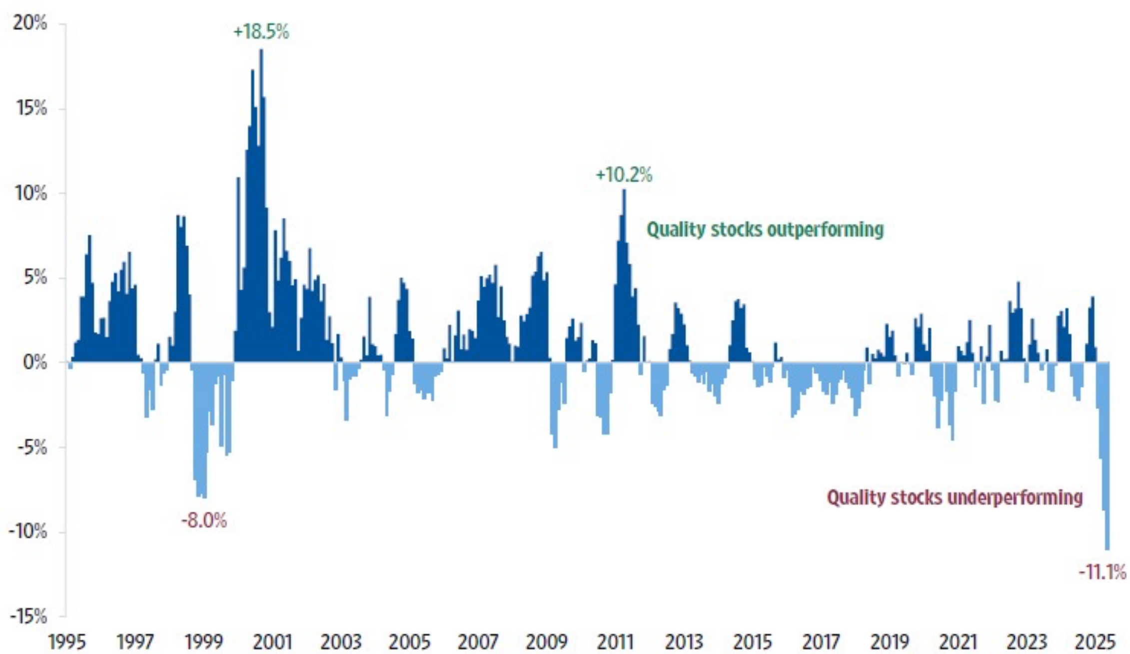
Wedgewood Partners Fourth Quarter 2025 Client Letter

<u>Annus Horribilis</u>

At Wedgewood, we've curbed our enthusiasm. We expect greater stock market volatility in 2025 than witnessed last year. Accordingly, we are patiently waiting for better prices for both new positions, as well as adding to existing positions.

Wedgewood Partners Client Letter, January 2025



As of October 31, 2025.
Source: Bloomberg.

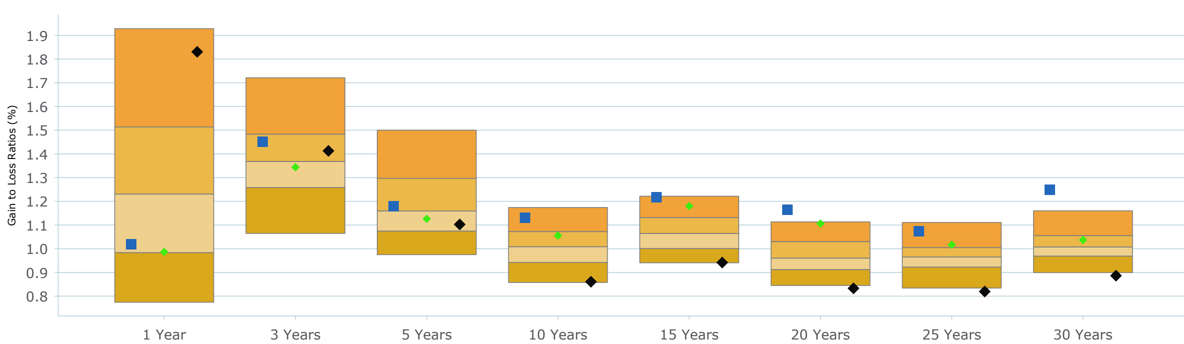
Review and Outlook

	4Q	YTD	1-Year	3-Year	5-Year
Wedgewood Composite Net	-1.8	4.3	4.3	20.3	11.4
Standard & Poor's 500 Index	2.7	17.9	17.9	23.0	14.4
Russell 1000 Growth Index	1.1	18.6	18.6	31.2	12.3
Russell 1000 Value Index	3.8	15.9	15.9	13.9	11.3
	10-Year	**15-Year**	**20-Year**	**25-Year**	**30-Year**
Wedgewood Composite Net	13.7	12.9	10.9	9.4	12.0
Standard & Poor's 500 Index	14.8	14.1	11.0	8.8	10.4
Russell 1000 Growth Index	18.1	16.6	13.2	9.7	11.0
Russell 1000 Value Index	10.5	10.8	8.3	7.7	9.2[1]

Manager vs Universe:Gain to Loss Ratio

As of September 2025

January 08, 2026 | 1/1



	1 YEAR	3 YEARS	5 YEARS	10 YEARS	15 YEARS	20 YEARS	25 YEARS	30 YEARS
Median	1.23	1.37	1.16	1.01	1.06	0.96	0.96	1.01
■ **Wedgewood Large Cap Focused Growth**	**1.02**	**1.45**	**1.18**	**1.13**	**1.22**	**1.16**	**1.07**	**1.25**
◆ Russell 1000 Growth	0.99	1.34	1.13	1.06	1.18	1.11	1.02	1.04
◆ S&P 500	1.83	1.41	1.10	0.86	0.94	0.83	0.82	0.89
Valid Count	781.00	760.00	731.00	631.00	518.00	402.00	270.00	146.00

Source: PSN Large Cap Manager Database. Data calculated as of the third quarter 2025 by PSN for managers on gross-of-fee return basis. Past performance is no guarantee of future results. PSN is a fee-based service. Future results may differ materially from past results. Please see additional disclosures on page 25.

[1] Portfolio returns and contribution figures are calculated net of fees. Contribution to return calculations are preliminary. The holdings identified do not represent all of the securities purchased, sold, or recommended. Returns are presented net of fees and include the reinvestment of all income. "Net (actual)" returns are calculated using actual management fees and are reduced by all fees and transaction costs incurred. Past performance does not guarantee future results. Additional calculation information is available upon request.

Q4 Top Contributors	Avg. Wgt.	Contribution to Return
Alphabet	9.28	2.38
Taiwan Semiconductor Manufacturing	9.43	0.87
Apple	7.38	0.50
Old Dominion Freight Line	2.40	0.38
Edwards Lifesciences	2.65	0.24

Q4 Bottom Contributors		
Meta Platforms	8.34	-0.85
Motorola Solutions	4.52	-0.69
United Rentals	4.09	-0.65
O'Reilly Automotive	3.40	-0.56
Tractor Supply Company	2.21	-0.55

2025 Top Contributors	Avg. Wgt.	Contribution to Return
Taiwan Semiconductor Manufacturing	8.78	4.45
Alphabet	8.13	4.16
Apple	7.01	0.42
Visa	6.12	0.78
Edwards Lifesciences	3.31	0.51

2025 Bottom Contributors		
UnitedHealth	1.97	-2.90
PayPal	5.98	-1.99
Copart	4.36	-1.80
CDW	3.47	-0.87
Motorola	6.62	-0.75

Top performance contributors for the fourth quarter include Alphabet, Taiwan Semiconductor Manufacturing, Apple, Old Dominion Freight Line, and Edwards Lifesciences.

Top performance detractors for the fourth quarter include Meta Platforms, Motorola Solutions, United Rentals, O'Reilly Automotive, and Tractor Supply Company.

During the quarter, we were quite busy. We bought Amazon and Chubb. Sold Pool Corp. Increased positions in CDW, Motorola Solutions, and Old Dominion Freight Line. We trimmed Alphabet twice, Apple, and PayPal.

Alphabet continued to make significant contributions to performance during the quarter. The Company's Google subsidiary reported that search revenues accelerated to +15% growth compared to a year ago. Google user query growth related to AI Overviews, along with automated ad creative services, helped drive this revenue growth. The Google Cloud segment revenue and backlog growth also accelerated, driven by AI workloads. Google Cloud processes 1.3 quadrillion - that is: 1,300 x 1 trillion - AI tokens per month, more than double from just a few quarters ago and many multiples more than some of its largest cloud competitors. Alphabet's long history of developing proprietary IT hardware and software will continue to help compound its profitability leadership during the AI era.

Taiwan Semiconductor Manufacturing also contributed to performance during the quarter. Broadcom's and Nvidia's CEOs have referred to the Company as a "precious source" and "the pride of the world" in silicon manufacturing, as the Company continues to execute flawlessly on its leading-edge node progression and capacity build-out, enabling the AI era by manufacturing nearly every compute accelerator (including GPUs) being marketed. The Company's advanced nodes allow accelerator designers greater flexibility to increase performance while limiting power requirements, a valuable proposition in an increasingly power-constrained compute infrastructure industry. Historically, mobile devices drove most of TSMC's revenue growth. More recently, high-performance computing (HPC) now driven most of the business. HPC revenues have doubled to more than $65 billion over the past six quarters, more than triple since late 2021. The Company continues to demonstrate pricing power, which should help drive excellent returns on capital as they likely accelerate their capacity buildout over the next several years.

Apple contributed to performance as adjusted earnings per share grew +13%, driven by +15% revenue growth in its services business, which accelerated compared to last quarter and generated over $100 billion in revenue over the past 12 months. Further, the Company guided to strong double-digit revenue growth in its holiday quarter, driven by double-digit growth in iPhone revenues, as it experienced strong demand after launching several new models in the previous quarter. Apple's multi-decade consistency in executing on hardware and software upgrades, along with increasingly proprietary silicon content, provides consumers with a dependable, high-quality user experience that should continue to drive adoption and trade-up.

Old Dominion Freight Line contributed to performance as investors rotated into more economically sensitive sectors late in the year. After favoring technology and particularly AI-focused investments for most of the year, investors became more optimistic about the possibility of a rebound in industrial activity, a core source of demand for Old Dominion's fleet. We added to positions before the rally as we expect the Company will continue to manage its capacity exceptionally well, keeping costs under control and taking price as it provides dependable service for its tariff-addled customers. We do not know how to time economic cycles, but we do know how to identify great businesses that should take profit share regardless of the macroeconomic backdrop. Over time, we expect the market to eventually reward those best-in-class businesses such as Old Dominion.

Edwards Lifesciences also contributed to performance during the quarter. The Company presented favorable seven-year data for its transcatheter aortic valves, whereas competitive valves have exited several key markets. Edwards can drive double-digit earnings growth over the next few years, as its long-term data serves to evolve the standards of care and will make it easier for patients, doctors, and health systems to opt for its minimally invasive alternatives versus open heart surgery.

Meta Platforms was a leading detractor from performance during the quarter despite reporting +26% revenue growth. Earnings per share grew less (+20%) after the Company ramped up spending related to its long-term AI ambitions. Meta's social media platforms are as popular as ever, with daily active users rising +8% during the September quarter compared to a year earlier, and users spending +5% more time on its applications. The Company's social media juggernaut – with just over *3.5 billion* people accessing one of Meta's platforms every single day - generates enormous volumes of highly valuable data for their global advertisers.

This might be surprising to many, but the Company has been using AI tools for more than a decade to manage and drive productivity across the different sides of this massive network. For example, their Andromeda machine learning system automatically retrieves and ranks tens of millions of potential ads based on each user's preferences and then selects and serves a fraction of those ads, replacing broader, more traditional audience segmentation with highly targeted selections, all in a matter of just seconds. Meta has a proven track record of making these highly productive AI investments that have yielded exceptional growth and returns on invested capital. We expect this to continue.

PayPal Holdings also detracted from performance during the most recent quarter. The Company reported healthy +8% volume growth across its branded checkout portfolio, driven by +10% growth in the U.S., leading to +12% growth in adjusted earnings per share. However, PayPal also reported a slowing in its volume late in the quarter, a trend they attributed to a weaker macro environment along with a slower than expected uptake in the rollout of their new checkout initiatives. In addition, the Company disappointingly announced it would make meaningful investments in the emerging agentic commerce industry, partnering with AI developers to bring PayPal to popular assistants such as ChatGPT and Perplexity, along with Alphabet's agentic solutions. We trimmed our PayPal positions during the quarter as we believe the combined slowing of transaction volumes and heightened expenses will result in slower profit growth than we previously expected.

Although Motorola grew its revenues +8% and grew earnings per share +9%, and expects to see similar growth in 2026, despite the headwinds of a government shutdown and dilution from their acquisition of aerial drone communications provider, Silvus Technologies, the stock was a poor performer in 2025. However, we expect to see accelerating growth into 2026 as organic orders have accelerated to double-digits in both products and services. As the stock sold off during the quarter, it traded to what were more attractive relative and historical forward price to earnings multiples; accordingly, we added to positions.

United Rentals detracted from performance during the quarter as the rental equipment industry cycled through a period of lower demand from U.S. non-residential construction activity. Revenues grew +6%, driven by strong demand for mega-projects and infrastructure, followed by data center power buildouts. The Company continues to invest in its fleet, especially new equipment, as leading indicators for broader construction activity are showing signs of recovery alongside a step-up in mega-projects over the next few years.

Tractor Supply Company also detracted from performance. The Company posted +7% growth in sales and +6% growth in operating income, as management concluded several long-term investments into its stores and distribution infrastructure. Tractor Supply has carved out a defensible niche in rural markets, particularly among higher-income earners, with approximately 80% of its sales derived from customers enrolled in its loyalty program. We expect to see accelerating earnings growth in 2026 as the Company laps its investments in final-mile delivery and direct sales, along with customer spending patterns that should normalize following a few years of abnormal weather.

Company Commentaries

Amazon

We have followed Amazon for many years – and owned its stock in the past. The stock has lagged the broader indices for the past five years, and valuation multiples have reverted lower despite cash flow returns on investment rebounding to near-record levels. Current management is more focused on managing capacity and costs after prior management spent several years aggressively building out both the e-commerce and AWS footprints. For example, the Company's EV/EBITDA multiple is trading around 13X for 2026, well below its pre-COVID-19 levels of 25X and the 10-year average of 17X. Meanwhile, cash flow returns have rebounded to more than 20%, driven by record margins. The current management team has done well to grow the businesses into their current overcapacity and better match that capacity to demand. We expect Amazon should be able to grow at double-digit rates, driven by increasing penetration of e-commerce and infrastructure as a service (IaaS), while expanding margins as they better manage capacity to demand.

For much of Amazon's history, the Company's retail unit invested far ahead of demand, with annual asset growth routinely outstripping revenue growth rates. The market often gave Amazon retail the benefit of the doubt that they'd either slow asset growth without slowing revenue growth or expand margins. Neither of these ever seemed to come to pass, or if they did, they were for brief periods. More recently, though, particularly since COVID-19, which also coincided with new management taking over from long-time CEO and founder, Jeff Bezos, Amazon has managed to drive NAM retail margins to new all-time highs. A large amount of this improvement has been helped by its advertising business, along with some improvement in spending discipline.

Amazon has added an incremental $50 billion in advertising revenue over the past five years. If we assume Google-like and Meta-like (Family of Apps) level operating margins, then we estimate Amazon Advertising could have added an incremental $20 to $25 billion in operating profit for the NAM and International segments. Indeed, those two segments have added about $28 billion in incremental profit. However, that means the rest of Amazon's retail business (i.e., 1st Party Fulfillment, 3rd Party Fulfillment, Subscription services, Brick and mortar, etc.) added an incremental $210 in billion in revenues and $2 billion to $8 billion in incremental profits. These are undoubtedly huge absolute amounts, but they are low single-digit incremental profit margins. We think those services can generate substantially more profitability if managed properly over the next several years.

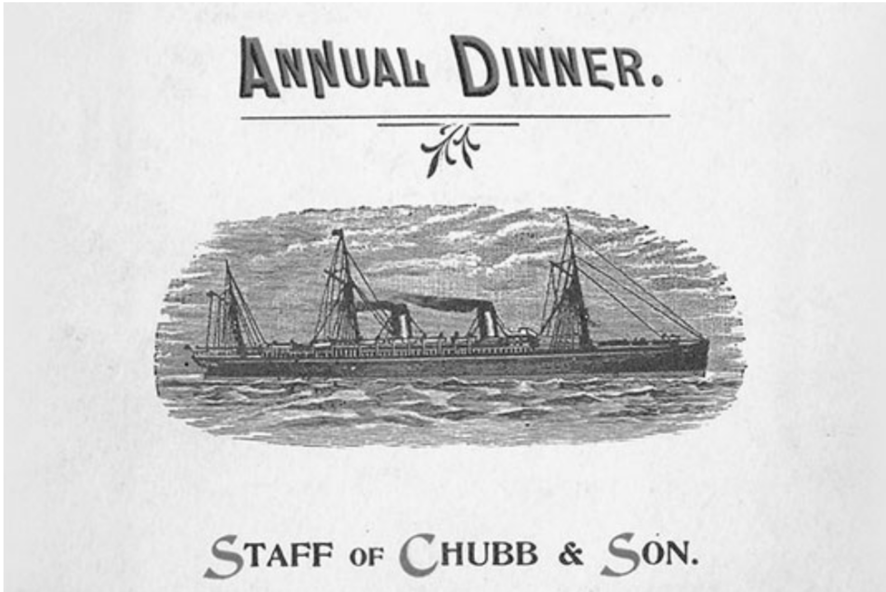
The majority of Amazon's profitability is generated by AWS, the pioneer and largest IaaS provider in the industry. AWS has fostered some of the largest businesses in the world, and even entire industries have been fostered by AWS over the past 20 years. While competition from Microsoft and Alphabet (Google) has been ever-present, investors have become overly pessimistic about the potential for competition from newer, so-called "neo-clouds" that are being built specifically to serve AI workloads. Amazon's incumbent leadership position and long history of developing proprietary hardware and software should continue to help drive exceptional revenue and profit growth. For example, as Amazon has deployed more capacity for AI-workloads - almost 4 gigawatts over the past 12 months (through September 2025) - revenue growth at AWS has accelerated to over 20%. Meanwhile, margins continue to push higher as the Company runs more workloads on proprietary hardware that is custom-designed for common, high-frequency jobs and avoids the markup of vendor hardware. Lower depreciation costs of proprietary hardware should help AWS keep well ahead of newer competition that depends on more expensive buildouts.

Amazon continues to plow back all of its cash flows into its business, which seems rational given the attractive returns on investment the Company is generating. The Company's returns have regained all-time highs, over 20%, as margins have expanded thanks to advertising, AWS growth, and a sharper focus on retail productivity. Despite these record returns and excellent growth, Amazon's valuation multiples, particularly EV/EBITDA, are trading at historically depressed levels. We started initial positions during the fourth quarter as we expect Amazon's growth, profitability, and valuation present an attractive long-term investment opportunity.

Chubb

We initiated a new position during the quarter in Chubb (CB), long a global leader in the property and casualty insurance industry. As you may know, Wedgewood has been somewhat unusual over time for a “growth” manager in holding positions across exceptional insurance-related industries, most notably as a 20-year shareholder in Berkshire Hathaway and, more recently, Progressive.

Chubb was founded in 1882 as a marine underwriting business in the New York City seaport district. While the Company is now domiciled in Switzerland, more than 60% of its revenues are generated in the U.S. The shares are listed on the New York Stock Exchange and are a component of the S&P 500 index.



Source: Company Reports

Much of the business may be characterized as "specialty" or "non-standard," which is the primary attraction for us. While Chubb offers more standard property and casualty insurance across both corporate and individual business segments, it leans heavily into areas such as risk engineering, director and officer insurance, or unique areas such as energy or aviation in its corporate segments. The Company also focuses more on mid-sized and small businesses than on large businesses, even within more standard P&C lines. Further, the Company maintains a small but meaningful U.S. agricultural insurance business, covering areas such as crops, cattle, and horse ranches. Many of the Company's corporate offerings are in areas not covered by mass-market insurance providers.

Chubb's personal insurance lines tend to focus on the lucrative high-net-worth clients (in the U.S., especially). These clients are generally concerned with adequately protecting significant and numerous valuable assets more than they are with price alone. Chubb also offers more standard lines like accident, health, and life insurance in faster-growing markets with less established mass-market competition, such as Asia.

Perhaps most importantly, the areas where the Company has more limited exposure may be most pertinent. Chubb tends to de-emphasize markets dominated by mass-market competition, markets that are more commodity-like and price-driven, and markets with heavily regulated pricing structures. For example, Chubb has limited exposure to the low- and mid-range U.S. auto insurance, where they would be competing primarily on price with the likes of State Farm, Progressive, Liberty, Allstate et al, all while trying to convince each state's insurance regulator that they should be able to take a price increase when necessary.

The Company's selection of attractive global insurance business lines, combined with impressive strength in underwriting and a reputation for excellent client service, supports an impressive business model characterized by steady premium growth and improving profitability, consistently generating double-digit percentage earnings growth over a long period of time. Additionally, like other insurance companies - with Berkshire Hathaway arguably being the most famous and successful example - Chubb has been generating additional income from its investment portfolio, consisting of both the Company's reserves set aside for insurance losses and regulatory capital requirements, plus retained earnings the Company has chosen to invest itself, rather than returning these profits to shareholders.

From an insurance underwriting perspective, the Company stands out as an outstanding insurance underwriter – truly, best-in-class. Chubb has a long history of not only accurately forecasting risk but also pricing its products, accordingly, enabling the company to earn an attractive and consistently improving return from assuming this liability for their clients. Their significant outperformance in relation to their peers also highlights their underwriting strength. The chart below shows both the company's improving underwriting margins over the past ten years, as well as its significant profitability advantage versus its peers.

P&C Combined Ratio vs. Peers

The company's underwriting results have outperformed the average of our peers over the last 10 years (2015-2024).

Averages				
	1 Year	3 Year	5 Year	10 Year
Peers*	93.8%	96.1%	96.5%	97.8%
Chubb	86.6%	86.9%	89.2%	89.8%

*Includes AIG, ALL, CNA, HIG, Liberty Mutual Group, and TRV.

Source: Company presentation

Combined Ratio: The key insurance industry metric measuring all insurance-related expenses in relation to revenues; this is the inverse of profit margin, that is, a lower ratio = higher profit margin. Less than 100 means that your underwriting is profitable. Add in investment portfolio interest income, plus steady underwriting profits, and the insurance business becomes quite a profitable endeavor.

Chubb's long operating history and its presence in every major insurance market in the world, with a variety of product lines, give it a vast set of proprietary information that it can layer on to the broad information sources available to everyone else in the industry - hence an element of the commodity nature of insurance. However, in some of their more esoteric specialty lines, these broad industry sources aren't as readily available. Furthermore, the Company invests in hundreds of risk consultants and engineers in both its corporate and personal insurance lines, helping customers to appreciate all their risks and enabling Chubb to serve them to their fullest extent.

As an example, we spoke with an equine ranch owner who had been insuring the ranch with a competing insurance company. This owner contacted Chubb for a quote. The Company dispatched a risk consultant out to the property to investigate this specific ranch in detail - something the incumbent insurance provider had never done. Chubb's consultant identified several important areas where the ranch was not currently protected. Ultimately, the owner was happy to insure the property with Chubb in a way that fully covered his specific property's risks.

Returning to the underwriting profitability comparison above, we would like to make another point. While Chubb's loss ratio obviously looks quite good in relation to its competition, clients may look at this chart and wonder if it provides evidence that we have been in a long, positive "insurance cycle." Chubb and its peers have all seen improving profitability over the past ten years. We asked this question ourselves, of course, as we would prefer to avoid a business in a cycle that may be turning negative in the near future. One of the attractions to Chubb's business model, as opposed to the model of, say, a large U.S. auto insurer, is that Chubb is not significantly exposed to any single "insurance cycle," as it has multiple cycles in multiple lines of insurance in multiple unique markets, including many small niche and specialty insurance lines. Each of these lines and geographic markets may be in different cycles at any given time; Chubb can shift its emphasis between these different cycles, as necessary. Furthermore, a very thorough underwriting process, and the ability to price as necessary - by staying away from excessive commodity businesses and price-regulated insurance markets - all help to insulate the Company against adverse insurance cycles in any of the various parts of its global business.

Although we understand that insurance of any kind feels very much like the antithesis of a feel-good customer service story, with the business model basically consisting of taking its customers' money and hoping never to give any of it back, Chubb is renowned for its claims service in relation to other insurance providers. As we have mentioned several times, Chubb avoids competing in commodity markets driven by competitive pricing; the Chubb model is to provide full coverage of a customer's risks at a fair price to customers who value the protection of their risks. Of course, it can be difficult to prove a reputation, but the Company has collected a variety of industry awards and recognitions for its claim service, and we suspect many of our readers are aware of the Company's reputation.

Like any insurance company, insurance revenues are driven by insurance premiums, impacted by growth in customers and policies, as well as pricing. Profits are then determined by insurance payouts and losses in relation to these premiums. Over the past five years, Chubb has reported 8% annual premium growth in the U.S. and 11% growth in international markets, with healthy growth across almost all areas of the business.

As previously discussed, the Company's strength in estimating and pricing risk consistently provides earnings leverage on this book of business, supporting double-digit earnings growth from the core insurance and underwriting business.

Additionally, over the past several years, Chubb's management team has focused on generating more income from its investment portfolio by retaining more of its underwriting profits for deployment in its portfolio. With the capital set aside for insurance reserves and statutory capital requirements invested in low-risk, liquid investments, they have chosen to invest additional capital in higher-return investments, particularly in private markets, generating higher returns from the portfolio. Because broad interest rate movements affect the value and yield of the most significant segment of the portfolio - the reserves/required capital in low-risk investments - income from the investment portfolio may fluctuate more variably than the company's underwriting income. We would like to focus on the fact that the portfolio has been rising steadily in size while also generating higher returns, meaning the investment portfolio has been contributing a greater absolute amount of income to the company, and this income has been growing at a double-digit percentage rate for the last several years.

Chubb Limited (CB)

Invested Asset Portfolio, 2015-2025

Total Assets (billions of $)		**Investment Income (adjusted, billions of $)**	
2015	66	2015	2.2
Q3 2025	166	2025 est	6.9
CAGR	**9.9%**	**CAGR**	**12.2%**

source: company reports

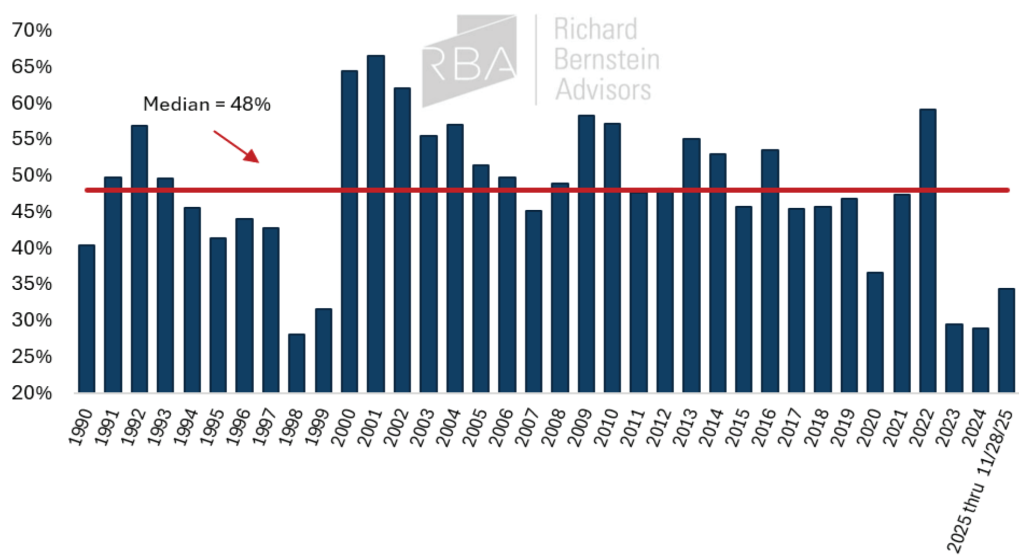
CAGR: compounded annual growth rate

Finally, we would remind our investors that a wide range of events has occurred in the global financial markets in the recent past, including the COVID-19 pandemic, stretches of tightening and loosening interest rates, and significant geopolitical upheaval. Therefore, we believe this performance from Chubb reflects quite consistent performance across a broad spectrum of market conditions. We believe the Company's multiple business lines and market exposures, and its resulting independence from any single insurance cycle, alongside its underwriting strength and rising investment portfolio returns, will continue to allow the Company to generate this consistent growth at attractive levels of profitability for the foreseeable future.

<u>Annus</u> <u>Horribilis</u>

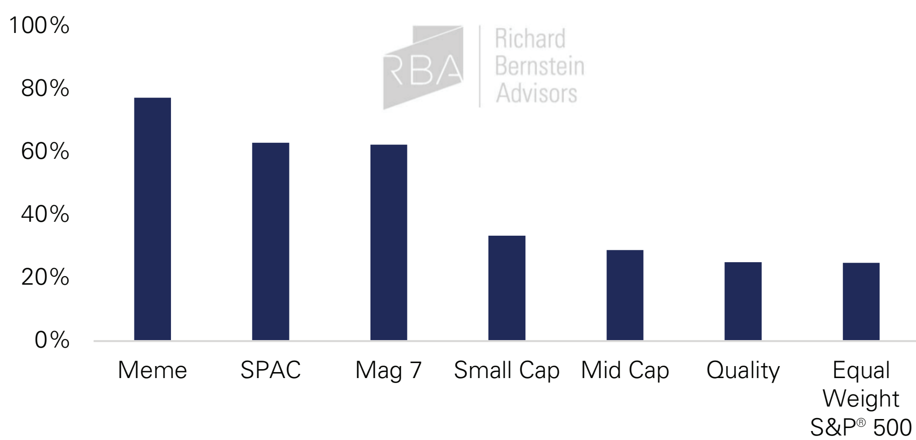
In January, we entitled our year-end Letter, ***Curb Your Enthusiasm***. The stock market ended 2024 with a second robust consecutive gain, resulting in a combined 2023-2024 increase of +58%. Our Composite compared favorably, gaining +68%. Scanning out a few more calendar years, our Composite has gained, mirabilis, approximately +30% over five of the past six years – with the bear of 2022 cracking our Composite down a sharp -28%. 2023 and 2024 were consecutive years in which speculative AI was ascendant, in which most stocks significantly failed to keep pace with the S&P 500 Index. 2025 was much of the same.

S&P 500®: Percentage of Stocks that Outperformed the Index
(Price Returns, 1990 – Nov. 28, 2025)

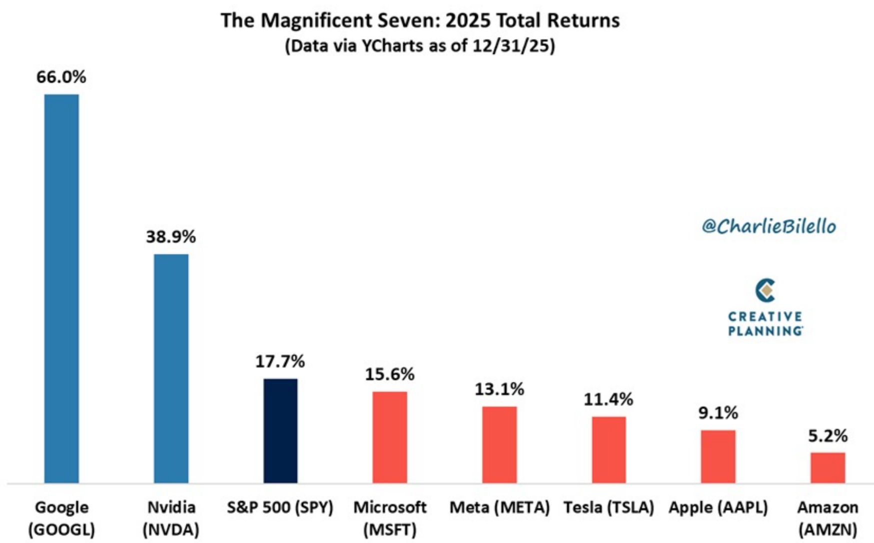


Source: Richard Bernstein Advisors LLC, BofAML US Strategy

Speculation Led Since Liberation Day
(Total Return, Apr. 8, 2025 – Nov. 25, 2025)



Our lack of enthusiasm for 2025 stemmed from our view of excessive market valuation in both the overall stock market and within the crowded Magnificent Seven trade, plus valuation concerns affecting much of our portfolio. Outside of our relatively large weightings in Taiwan Semiconductor Manufacturing and Alphabet, all of our other AI and technology-related portfolio holdings hurt our 2025 returns. None of this was a surprise, but it stung, nonetheless.



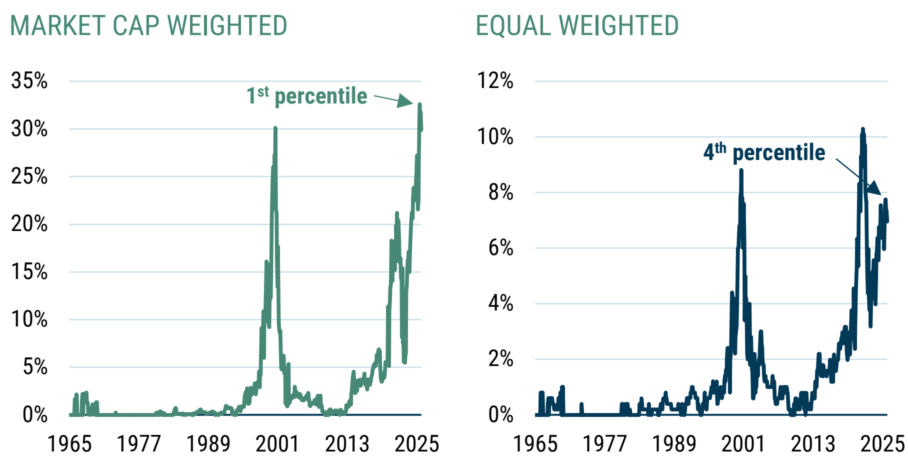
Unfortunately, we were more accurate on our portfolio than the S&P 500 Index. We have trafficked in "quality stocks" for more than 33 years, and this approach has served our clients well since 1992. It did not in 2025. The year would prove to be our worst relative calendar year since 1993. Horribilis, indeed.

What went wrong? Broadly, there were three buckets of underperformance to report. The first was poor stock selection. UnitedHealth was a kick in the teeth early in the year. Pool Corp struggled to reignite growth long after the ebullient COVID-19 growth spike. Both positions were sold. PayPal was the most frustrating of the year. In retrospect, we were too patient. Although 2024 was a stellar year with the stock up +39%, by late fall, earnings growth was once again interrupted. Looking ahead, 2026 looks like a year of more outsized investments (read: lower margins). The weighting in the stock was significantly reduced. Second, a number of our stronger performers during the two years of 2023 and 2024 were due for a valuation pause/retreat. Pause/retreat, they did. Long-held positions in this category include Motorola Solutions, S&P Global, Apple, Booking Holdings, Visa, and Meta Platforms. Third, by our portfolio risk management design, we have been structurally underweight AI-technology stocks for a few years now – even though our current five largest holdings are AI-tech. Trillion market capitalizations have seen to this dynamic headwind. Consider the collective weight of the top 10 holdings in the S&P 500 Index are *41%,* and the top eight AI-tech stocks in the Russell 1000 Growth Index amount to a whopping *57%!* Recall that we cap a maximum weighting for each common stock position at 10%. The Russell 1000 Growth Index has three stocks with a 10% weighting – NVIDIA, Apple, and Microsoft. This headwind, which we reasonably managed against over the past half-dozen years, poured it on us in 2025. Add it all up, and we only had just *two* of our portfolio holdings beat the major market indices in 2025 – Alphabet and Taiwan Semiconductor Manufacturing. Alas, a very poor year for stock picking, indeed.

As we enter 2026, the crowded AI trade and historically rich valuations haunt prudent investing. Even most non-Magnificent Seven stocks fail to scream "bargains." Further, speculative leverage remains historically high. Even the 2026 mid-term political season speaks to curbed enthusiasm.

S&P 500 ONCE AGAIN CONCENTRATED IN EXPENSIVE NAMES

% stocks with Price/Sales > 10x is at an extreme even after adjusting for select number of mega-caps

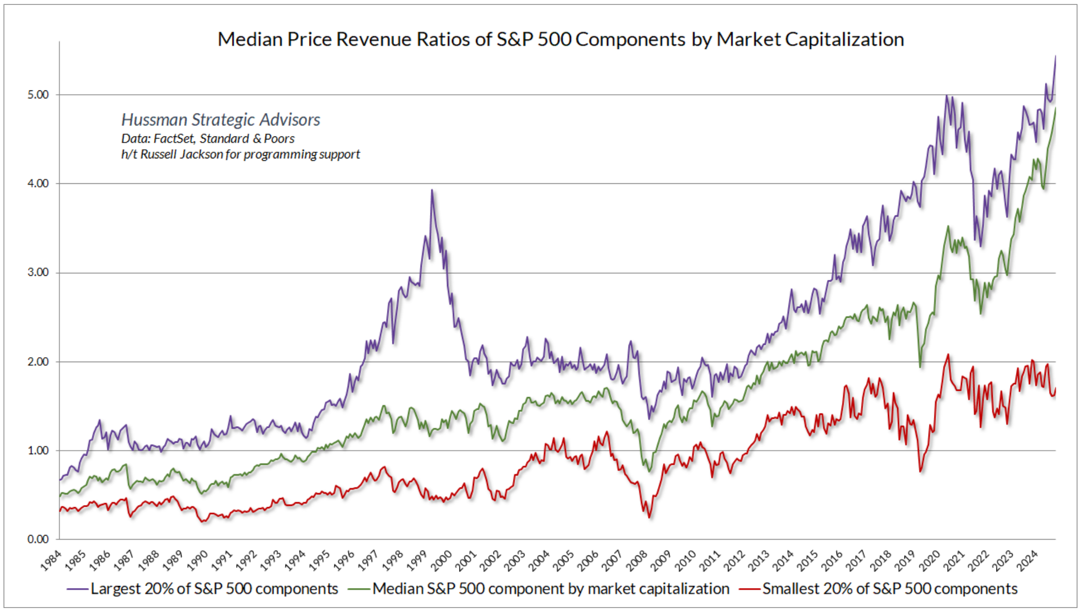


As of 10/31/2025 | Source: GMO

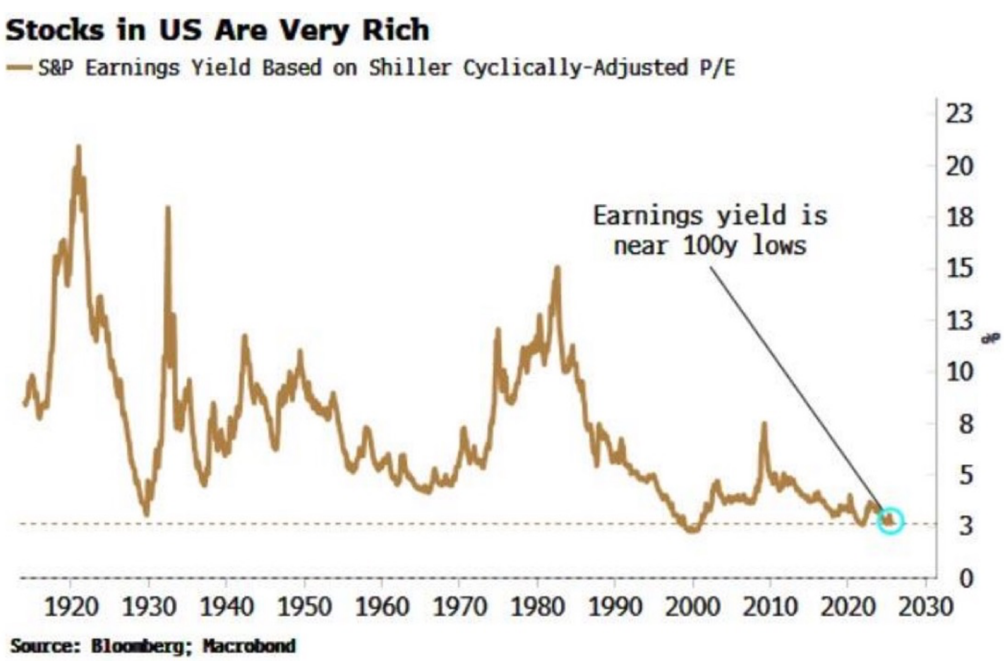
Weight of the top 10 companies in the S&P 500

% of market capitalization, % of last 12 months' earnings

Source: JPAM

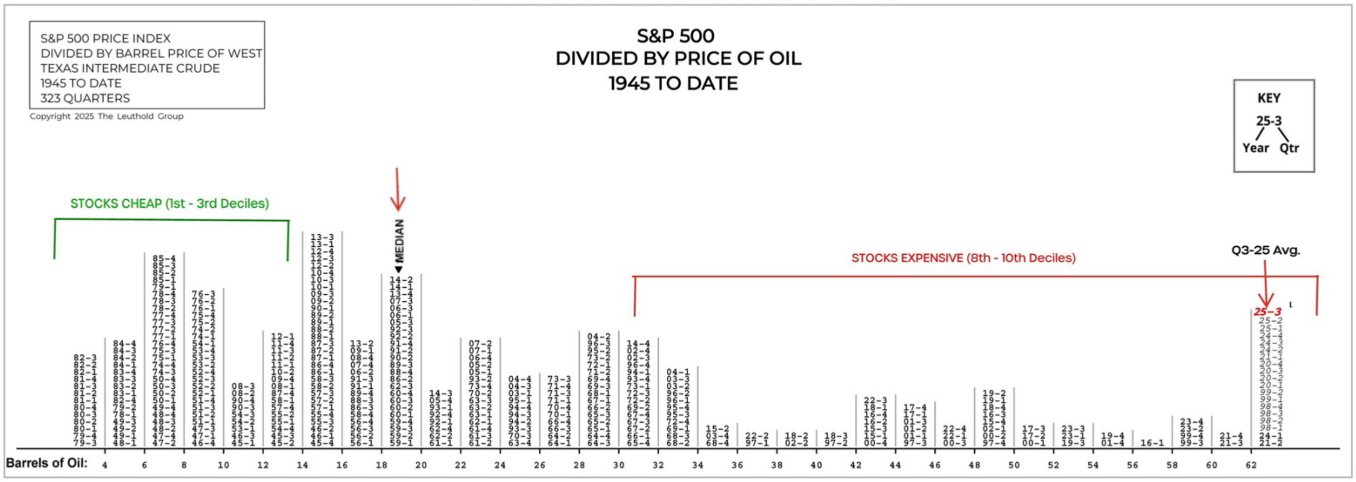


Median Price Revenue Ratios of S&P 500 Components by Market Capitalization
Hussman Strategic Advisors
Data: FactSet, Standard & Poors
h/t Russell Jackson for programming support
5.00
4.00
3.00
2.00
1.00
0.00
1984 1985 1986 1987 1988 1989 1990 1991 1992 1993 1994 1995 1996 1997 1998 1999 2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022 2023 2024
Largest 20% of S&P 500 components
Median S&P 500 component by market capitalization
Smallest 20% of S&P 500 components



Stocks in US Are Very Rich
S&P Earnings Yield Based on Shiller Cyclically-Adjusted P/E
Earnings yield is near 100y lows
23
20
18
15
13
10
8
5
3
0
1920 1930 1940 1950 1960 1970 1980 1990 2000 2010 2020 2030
Source: Bloomberg; Macrobond

Number Barrels of Oil to Purchase One Unit of the S&P 500

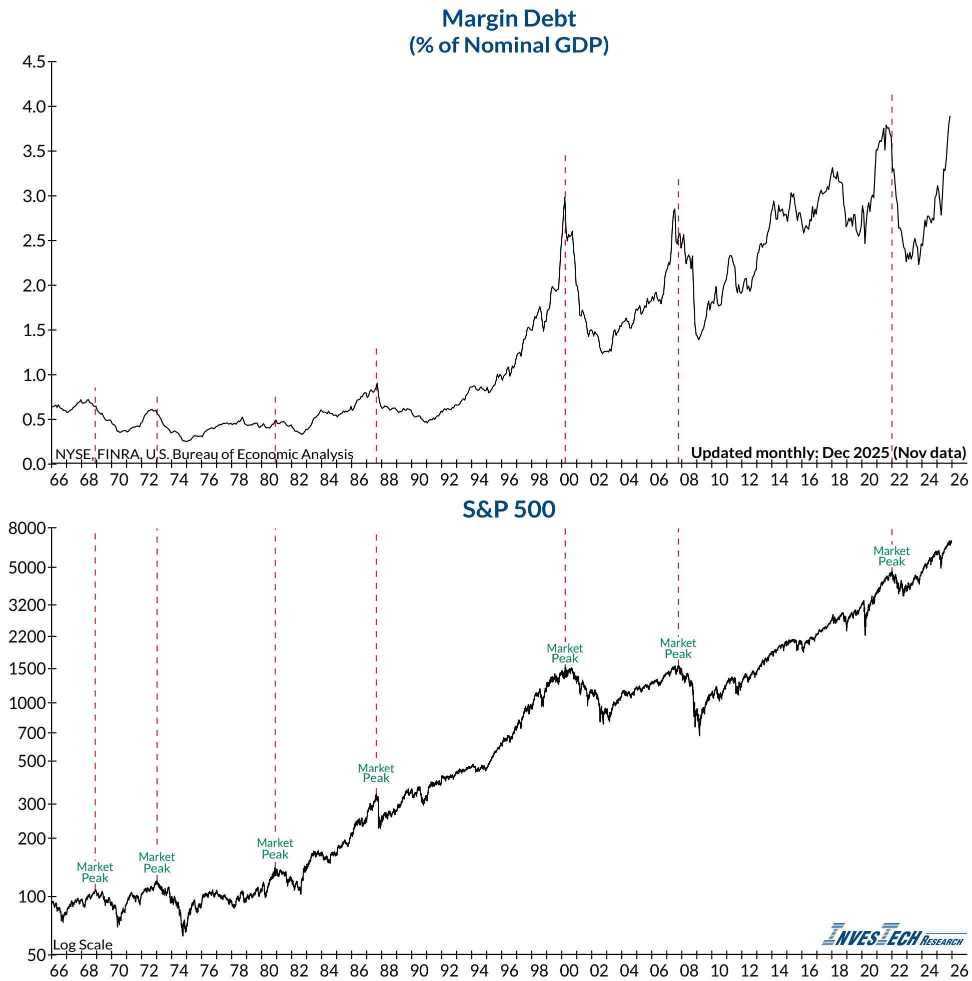


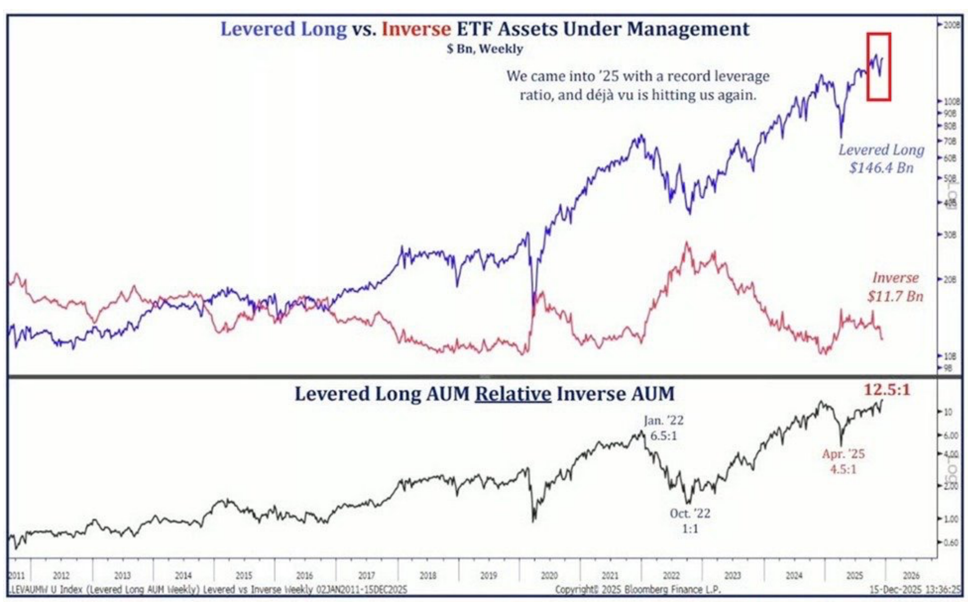
- **Q3 Average (Labeled 25-3): 98.5 Barrels; the 10th decile of valuations**
- **Conclusion: Stocks are currently overvalued based on data 1945-to-date**

Methodology:

- Measured by the number of barrels of oil it takes to purchase one unit of the S&P 500 index.
- Barrel Price is monthly data compiled by the Department of Energy, and is based on one barrel of West Texas Intermediate Crude.
- From 1945-to-present, the price of a barrel of oil has grown from $1.17 to $58.30 (Q3 avg.)
- Italics indicate outliers.

source: ZeroHedge

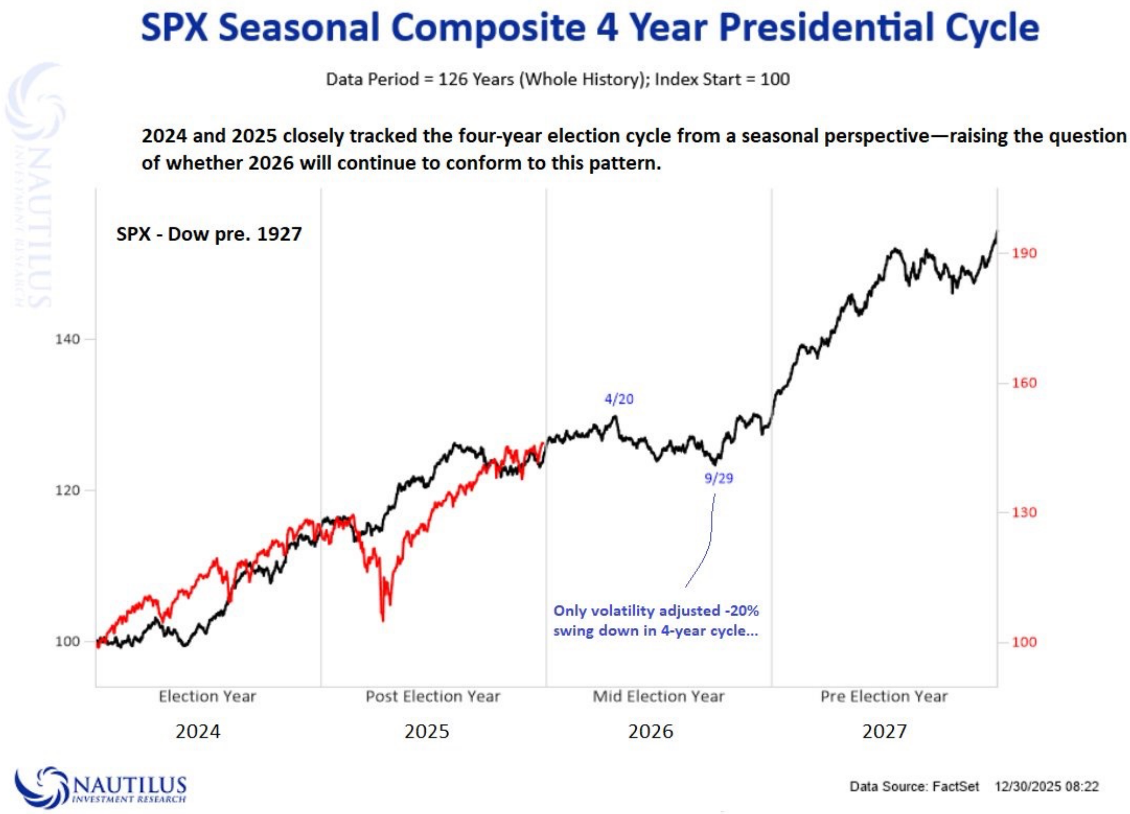




Source: Strategas, Bloomberg, 12/15/25

S&P 500 after Margin Debt increases by > 42% in the past 7 months
SubuTrade.com

	1 Month Later	3 Months Later	6 Months Later	9 Months Later	10 Months Later	11 Months Later	1 Year Later
1959 April	1.89%	5.07%	-0.12%	-3.44%	-2.55%	-3.91%	-5.59%
1972 June	0.23%	3.18%	10.18%	4.09%	-0.16%	-2.04%	-2.69%
1983 June	-3.03%	-0.94%	-1.62%	-5.05%	-4.53%	-10.19%	-8.63%
2000 February	9.67%	3.97%	11.07%	-3.77%	-3.38%	-0.03%	-9.26%
2007 May	-1.78%	-3.70%	-3.23%	-13.07%	-13.58%	-9.48%	-8.51%
2025 November							
Average:	**1.40%**	**1.52%**	**3.26%**	**-4.25%**	**-4.84%**	**-5.13%**	**-6.93%**
% Positive:	**60%**	**60%**	**40%**	**20%**	**0%**	**0%**	**0%**



Midterm Years Tend To Bottom Later In The Year And See Larger Corrections

S&P 500 Index Peak-To-Trough During A Midterm Year

		S&P 500 Index Return	
Year	Date of Low	Peak-To-Trough	Return One Year Later
1950	7/17/1950	(14.0%)	30.9%
1954	8/31/1954	(4.4%)	43.9%
1958	2/25/1958	(4.4%)	36.3%
1962	6/26/1962	(26.4%)	32.7%
1966	10/7/1966	(22.2%)	33.2%
1970	5/26/1970	(25.9%)	44.5%
1974	10/3/1974	(37.6%)	34.6%
1978	11/14/1978	(13.6%)	11.3%
1982	8/12/1982	(16.6%)	57.7%
1986	9/29/1986	(9.4%)	40.6%
1990	10/11/1990	(19.9%)	28.8%
1994	4/4/1994	(8.9%)	14.3%
1998	8/31/1998	(19.3%)	37.9%
2002	10/9/2002	(33.8%)	33.7%
2006	6/13/2006	(7.7%)	24.5%
2010	7/2/2010	(16.0%)	31.0%
2014	10/15/2014	(7.4%)	8.7%
2018	12/24/2018	(19.8%)	37.1%
2022	10/12/2022	(25.4%)	21.0%
Average	August 18	(17.5%)	31.7%
Median	September 29	(16.6%)	33.2%

Source: Carson Investment Research, Factset 11/16/2026
@ryandetrick

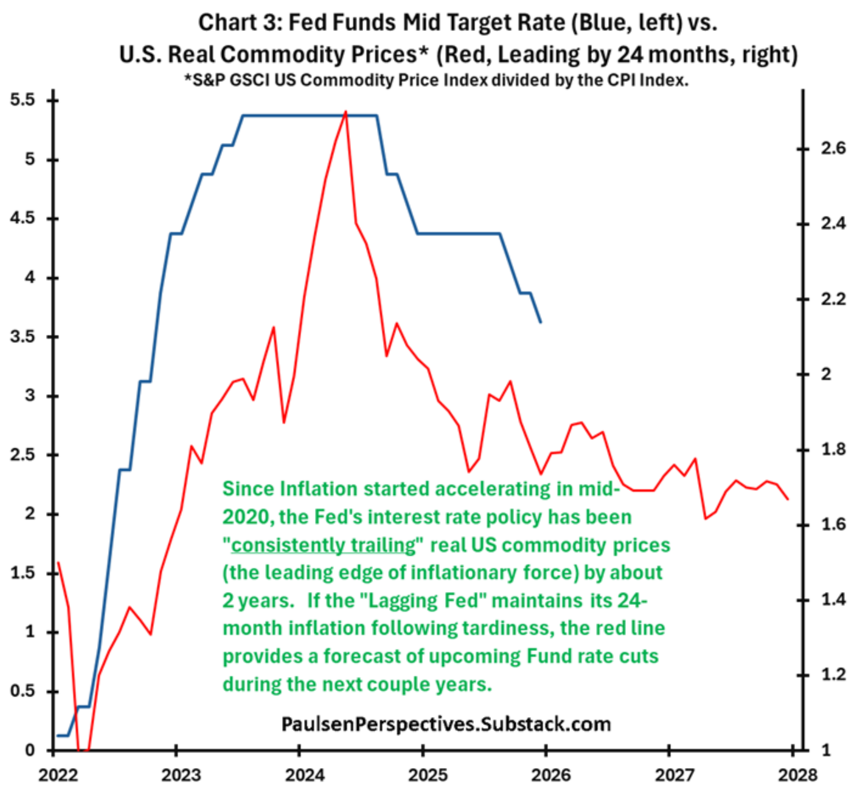
CARSON

What could be the "big" surprise for equity markets in 2026? Poorer expected corporate earnings growth? An AI demand bust? An AI supply disruption bust? Economic recession?

A spike in longer-term U.S. Treasury rates, due to an unexpected surge in inflation? The Federal Reserve reversing its current monetary policy of new, new QE? Inflation surprises to the downside, while the 10-year U.S. Treasury slowly descends lockstep into the lower 3% range. In this Letter, let us consider the latter surprise.

A favorite economic and market strategist of ours is Jim Paulsen (formerly of Wells Fargo Investment Advisors and The Leuthold Group). Paulsen posits:

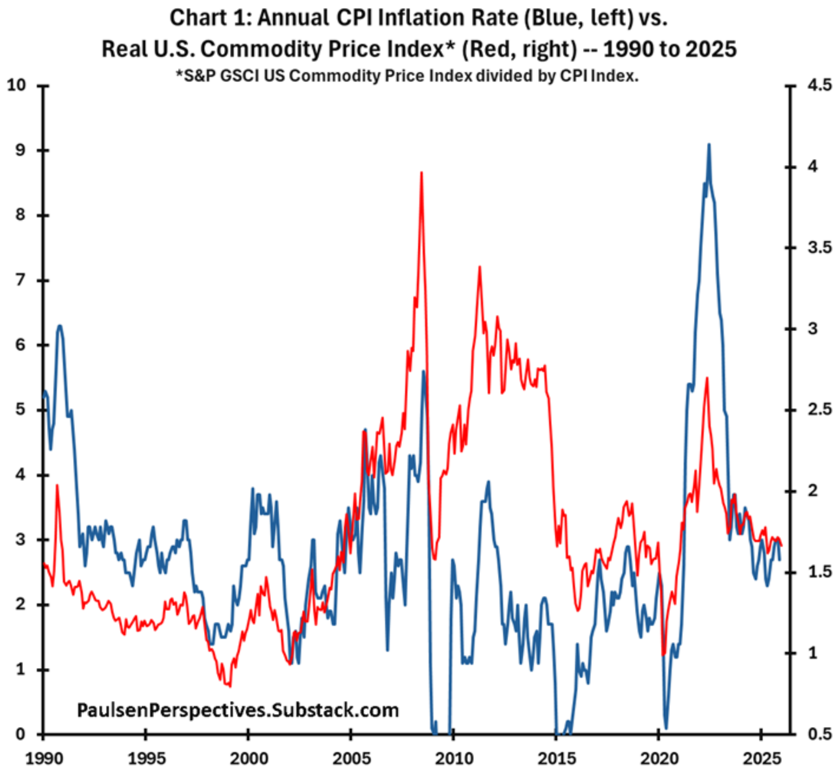
"Since the 2020 pandemic, the Federal Reserve's funds rate policy has been consistently trailing real commodity price movements by two years."



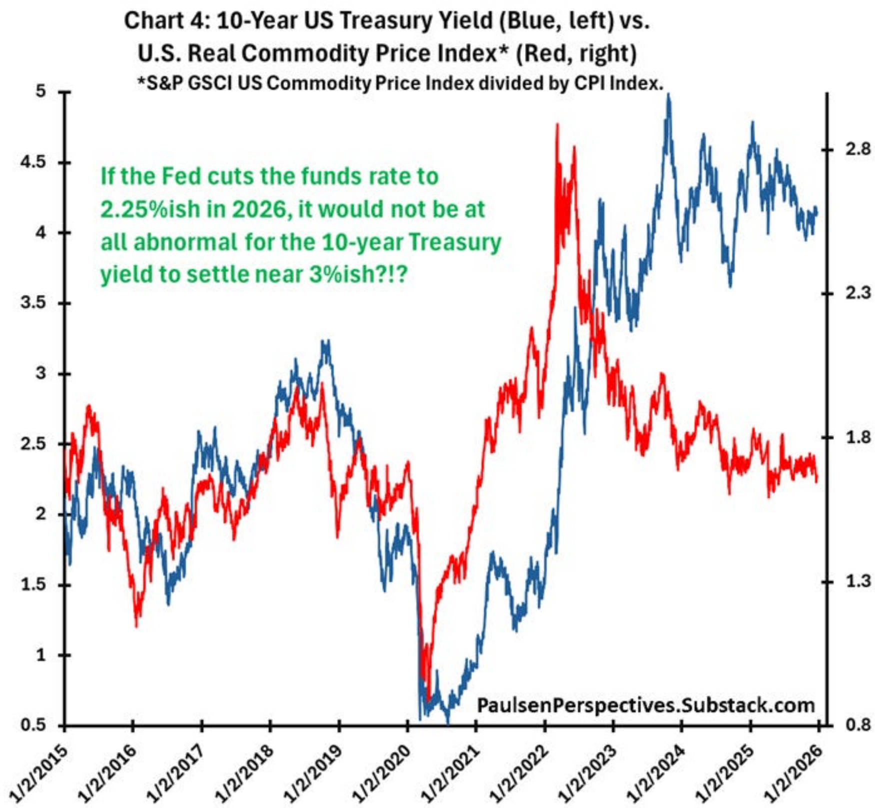
As background, Paulsen (in bold quotes) reminds us that the Federal Reserve's historical dual mandate has been both full employment and price stability. The shocks of the 2008-2009 Great Recession and the post-pandemic surge in inflation during 2020-2022 upended either a former focus on unemployment or the latter focus (obsession?) on inflation. Regarding "inflationary forces," Paulsen reminds us that one of the best indicators of leading inflation (and deflation) forces is the market price trends of commodities.

"One of the best indicators of "inflationary force" is real commodity prices. Commodity prices represent the leading edge of inflation frequently moving before underlying consumer price inflation changes…For policy officials, commodity prices also have the added advantage of adjusting daily in the financial

markets and therefore are much timelier than are monthly CPI reports released with a long lag…mostly, however, the Fed funds rate and real commodity prices tended to move up and down roughly coincidently during this time."



"Since the start of the pandemic in early-2020, however, the relationship between real commodity prices and the Fed funds rate has changed significantly. Real commodity prices began rising in April 2020 and would continue climbing by a substantial amount until June 2022. However, despite surging commodity prices, the Federal Reserve did not begin raising the Fed funds rate until almost two years later in March 2022. That is, after being nearly coincidental with most major commodity price movements during the previous 25 years, beginning in 2020, suddenly the Fed's policy relationship to the leading edge of inflationary force (i.e., real commodity prices) became "tardy"! And ever since, Fed funds policy has remained consistently laggard, trailing major moves in real commodity prices by about two years."



Consider too the secular slide in Owner's Equivalent Rent (OER). OER accounts for an outsized one-third of the Consumer Price Inflation (CPI). The sharp decline in OER over the past several months has set the stage for a lower CPI for most of 2026.

For the past few years, Powell & Co. has been obsessed with the so-called "star neutral 2%." This is basically a "neutral" economic policy, a sweet spot outcome whereby monetary policy is not too cold, nor too hot, aiming to achieve the Federal Reserve's ideal inflation target of 2%. We will leave the efficacy debate of "r-star" to the much-too-crowded space of political economists. Suffice it to say, the Trump administration's so-to-be announced Federal Reserve Chairman will be pro-growth, and surely dovish on monetary policy – may not give a wit about r-star.

If we had to consider two surprises for 2026, they would be a 10-year U.S. Treasury yield at say north of 4.5%, likely due to an inflation surge. Curbed enthusiasm for stocks would prevail hard. At the other extreme, south of say 3.5%, we would expect a much broader, ebullient stock market result. In this scenario of a lower, but steeper yield curve, stocks with more cyclical aspects to their business models could well catch up with their big AI-tech brethren.

Either way, in our estimates and opinion, the current risk-reward profile of our current portfolio possesses considerable redeeming attributes. On the growth front, our portfolio fundamentals, prospective earnings growth rates, profitability measures, and balance sheet strength are notably superior to the S&P 500 Index – and on par with the Russell 1000 Growth Index. However, on the valuation front, our portfolio is now in rarified territory. Our portfolio is at an unusual valuation par with the S&P 500 Index on a forward 12 months price-earnings basis – and at a 7-8 multiple turn discount versus the Russell 1000 Growth Index.

We like these odds for a performance reversal in 2026.

January 2026

David A. Rolfe, CFA	Michael X. Quigley, CFA	Christopher T. Jersan, CFA
Chief Investment Officer	Senior Portfolio Manager	Portfolio Manage

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