Letter to Investors

July 13, 2026

The Artificial Intelligence ("AI") investment cycle continued to drive equity market performance during the first half of the year, with leadership shifting from the companies funding the AI infrastructure buildout (including the "Magnificent Seven") toward the companies providing the critical components and technologies required to support its expansion.

Several Carderock Capital selections benefited from this shift. During the first half of the year, four AI-related investments appreciated more than 50%, with our strongest performer gaining more than 150%. Companies such as Quanta Services, Monolithic Power Systems, Amphenol, and Lam Research contributed meaningfully to your portfolio returns. While we are pleased with these results, we recognize that periods of significant market enthusiasm can create temporary supply-and-demand imbalances, similar to other investment cycles throughout history. We believe these opportunities can be rewarding, but they are unlikely to persist indefinitely.

Importantly, the current market environment has also created attractive opportunities outside of today's AI leaders. Many high-quality companies within our Quality Growth universe have underperformed the broader market despite strong fundamentals and durable business models. In our view, some of these companies are currently trading at valuations that reflect short-term investor sentiment rather than their long-term earnings potential. This disconnect creates opportunities for investors with a long-term perspective.

Earlier in the AI cycle, investors rewarded companies such as Microsoft, Google, Amazon, and Oracle for their leadership in developing the computing infrastructure needed to advance artificial intelligence. However, as the capital required to build data centers and expand AI capabilities has increased significantly, investors have begun evaluating whether the long-term economic returns will justify these investments.

Key questions facing the market include:

- The sustainability of current levels of AI investment and capital spending
- The impact of higher interest rates and financing costs
- The ability of companies to generate attractive returns on infrastructure investments
- The opportunity cost of prioritizing AI spending over dividends or share repurchases
- The pace of AI adoption and the development of practical applications
- The long-term economic benefits for both developers and users of AI technology

As Quality Growth investors, we remain focused on companies with durable competitive advantages, strong balance sheets, proven business models, and the ability to generate consistent cash flows over time. We view AI as a transformative technology that has the potential to improve productivity, increase efficiency, and enhance the capabilities of businesses across many industries. While the ultimate impact of AI remains difficult to predict, we believe the strongest companies will be those that successfully integrate this technology into their operations while maintaining their underlying competitive advantages.

Looking ahead, our investment decisions continue to be guided by several key themes:

- Stable employment conditions and resilient consumer spending continue to reduce the likelihood of a significant economic downturn.
- Current challenges within private credit and private equity markets appear manageable and are unlikely to create broad economic contagion.
- Strong hospital and senior living occupancy rates continue to support demand for healthcare services, supplies, and surgical equipment.
- Improving pharmaceutical approval trends provides a favorable environment for biotechnology and life science companies.
- Limited housing inventory, improving homebuilder margins, and recent housing policy developments suggest the potential for improvement in the housing market.
- The highest percentage of stocks since the technology bubble of the early 2000s are currently moving independently of the broader market, creating attractive opportunities for diversification.
- Expanding earnings expectations across multiple sectors continue to support the benefits of a diversified portfolio rather than concentrated market exposure.

Portfolio Positioning

Our portfolio activity during the first half of the year reflects our continued focus on identifying attractive long-term opportunities:

- Purchases exceeded sales as we continued reallocating capital from securities with elevated valuations into companies where we believe the long-term opportunity is more attractive.
- Cash allocations remain near historically low levels and below our normal targets, reflecting our constructive outlook for equities and the broader economy.
- With investment-grade corporate bonds spreads near historically tight levels and significant corporate debt issuance expected, we have maintained a balanced allocation between government and corporate bonds.

Our investment philosophy remains unchanged. We continue to believe that successful long-term investing requires discipline, diversification, and a focus on valuation, risk management, and business fundamentals. While recent market performance has been driven by a concentrated group of companies and themes, history has shown that market leadership evolves over time. We believe a broadly diversified, balanced, and growth-oriented portfolio is well positioned to benefit from continued technological advancement and the broader economic opportunities created by innovation.

As always, if you have any questions or if your personal circumstances have changed, please do not hesitate to contact us.

Warmest Regards,



Daniel A. Kane, CFA
President



Stephen F. Knapp, CFA
Director of Research



Jeanne C. Goedecke, CFA
Portfolio Manager

We invite you to review our regulatory disclosure brochure (Form ADV Part 2) and Client Relationship Summary (Form CRS) as filed with the U.S. Securities and Exchange Commission (SEC) pursuant to the Investment Advisers Act of 1940. You can access these materials through our website (www.carderockcapital.com) or through the SEC's Investment Adviser Public Disclosure database, available on their website at https://adviserinfo.sec.gov/firm/summary/104570. With reference to Rule 206(4)-2, Carderock Capital urges you to compare the information on your statement with the statements received from your custodian. Please call if you have any questions.

"Today's AI-driven bull market bears more than a little resemblance to the dot-com boom that ended 26 years ago, but there are differences. It's created two pockets of opportunity: so-called AI losers, like Salesforce and Accenture, and then sectors that are out of favor, like healthcare. Some of the healthcare names have run hard recently, but there are still companies that are seeing pressure. Everywhere that there is a little bit of a stink or concern, you're seeing names fall behind. Everyone is chasing this one group of names that's doing well currently and showing strong earnings revisions, leaving a lot of other stocks behind." Evan Lorenz, "*Discard of the Bubble,*" **Grant's Interest Rate Observer**, June 19, 2026.

"SpaceX poses a critical problem for investors, and passive funds in particular. Mostly, it reveals the conceptual problem with passive indexing- that it erodes the concept of ownership. Thirty years ago, a fund manager would say they 'owned' a stock. Now they say they're 'overweight.' Once, if you didn't like a stock you simply wouldn't buy it. With the rise of indexing and benchmarking, that no longer follows. Put 5% of your fund into Nvidia and you'd be desperate for the company to succeed. But with Nvidia now 7.9% of the S&P 500, a 5% holding becomes a big 'underweight,' and the manager bizarrely would prefer a company they own to do badly." John Authers, "*The Bad Gnus on SpaceX,*" **Bloomberg**, June 16, 2026.

"The legendary investment sage Benjamin Graham famously wrote that 'in the short run, the market is a voting machine, but in the long run, it is a weighing machine.' When it comes to the current AI boom, the short run may be drawing to a close and the long run is approaching fast. Private market investors have been maniacally voting for OpenAI and Anthropic, bidding up the target valuations for their planned flotations to about $1 trillion apiece. Investors will eventually discount the hype and weigh these companies' long-term abilities to generate hard cash. On that score, there are huge doubts about both companies. Most importantly, it is not clear that either of them has a sustainable business model. The costs of remaining at the frontier of AI are punishing, but the penalties for falling behind may be even worse." John Thornhill, "*Why OpenAI and Anthropic May Struggle to Float,*" **Financial Times**, July 5, 2026.

"New Federal Reserve Chair Kevin Warsh's biggest problem, beyond a doubt, is the president who chose him. Donald Trump wants much lower interest rates regardless of economic conditions, and he isn't shy about saying so. Warsh's stated views will constantly be judged not by whether they make sense on the merits but whether they comply with what he might or might not have told the president to get the position. The more you pay attention to what Warsh has said on monetary policy before he was in the running for the top job, the odder Trump's nomination of him seems. As an amply credentialled and experienced central banker, he's long advocated a tight focus on controlling inflation as opposed to muddling that goal up with others. His underlying ideas remain much more hawkish than Trumpish." Clive Crook, "*Let's Count the Ways Kevin Warsh Will Disappoint Trump,*" **Bloomberg**, June 9, 2026.

"Some investors are growing concerned about the speed at which analysts' estimates are rising. Some fear rising costs for AI companies, a drop in demand for the technology or a difficulty turning spending into profits could see earnings fall short. Supernormal profits are unsustainable, but trying to time the turn is a mug's game. Capex trends that have caused investors to crowd into tech hardware and energy stocks aren't necessarily structural if there's no clear path to return on investment. But what of it? Music's playing, keep dancing. Who wants to be the idiot to go all-cash the day before Zuck announces artificial superintelligence? Prices will either go up or down. There's no predicting which." Bryce Elder, "*This is Nuts Upon Nuts. When's the Crash?,*" **Financial Times**, July 3, 2026.

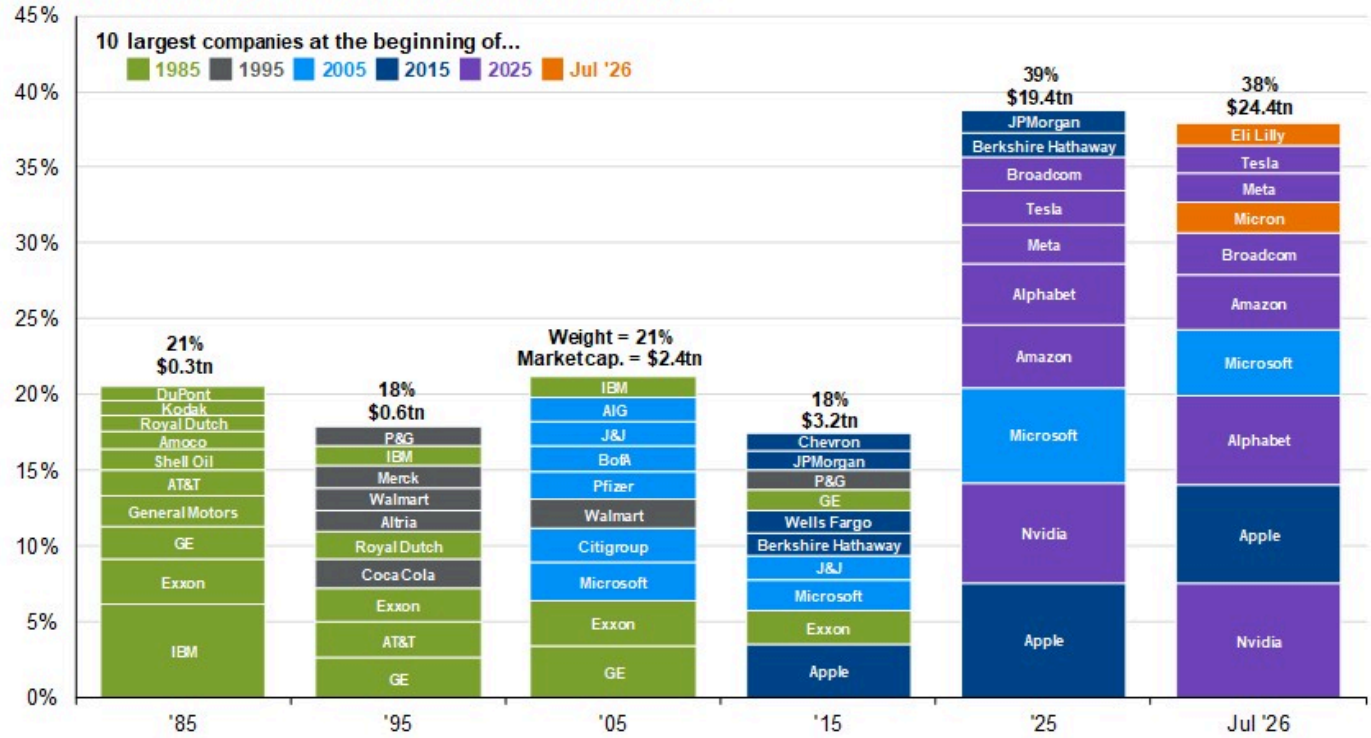
P/E of top 10 and remaining companies in S&P 500
Next 12 months



Weight of the top 10 companies in the S&P 500
% of market capitalization, % of last 12 months earnings



Top 10 companies in the S&P 500
Index weight on the first day of the indicated year and month for current year

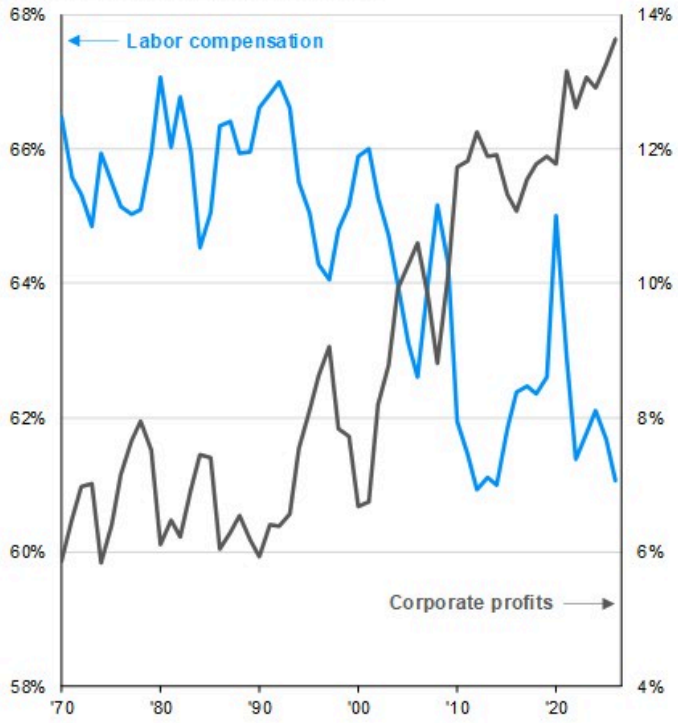


Forward P/E ratio is the most recent S&P 500 index price divided by consensus analyst estimates for earnings in the next 12 months, provided by IBES since January 1996 and FactSet since January 2022. The remaining stocks represent the rest of the 490 companies in the S&P 500, and their P/E ratio is calculated by backing out the nominal earnings and market cap of the top 10 from that of the S&P 500. Companies are organized from highest weight at the bottom to lowest weight at the tip. Market wights are provided by Bloomberg through 2025 and FactSet thereafter. Data are as of June 30, 2026.

Sources: FactSet, Standard & Poor's, J.P. Morgan Asset Management, and Bloomberg

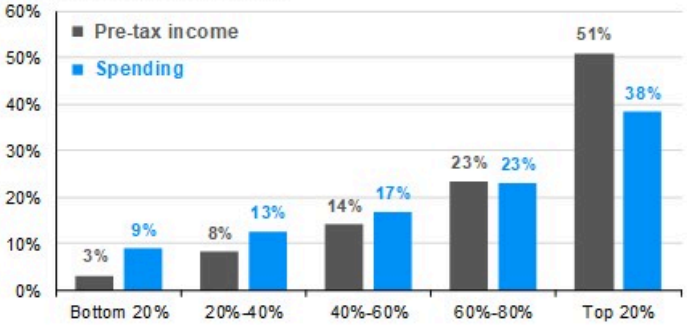
Labor compensation vs. corporate profits

Share of national income, annual and 1Q26



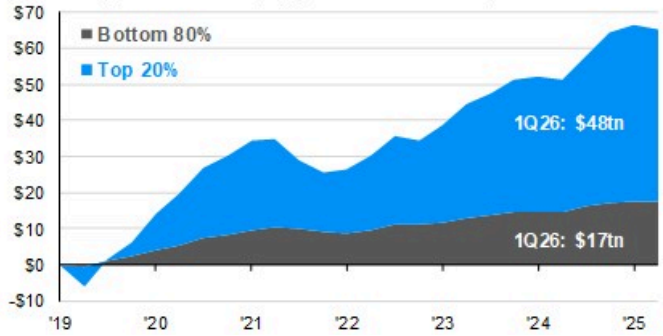
Consumer share of total pre-tax income and spending

By pre-tax income cohort, 2024



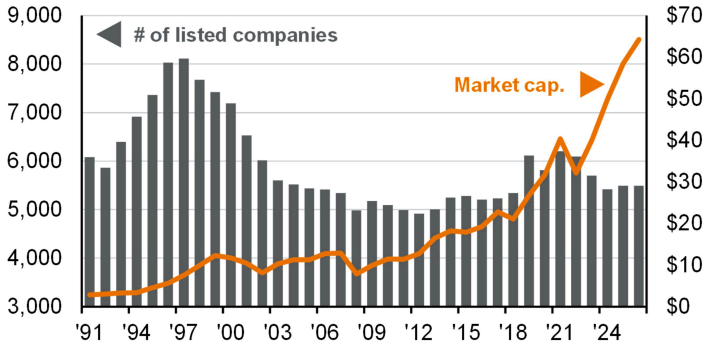
Net worth growth by income cohort

Cumulative growth from 4Q19, by pre-tax income cohort, USD trillions



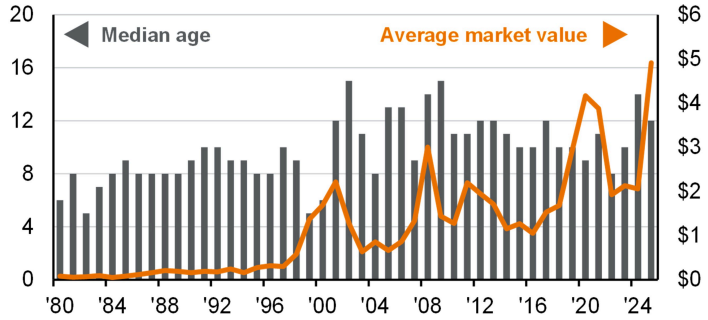
Number of listed U.S. companies* and market cap.

Count, S&P 500 market capitalization in USD trillions



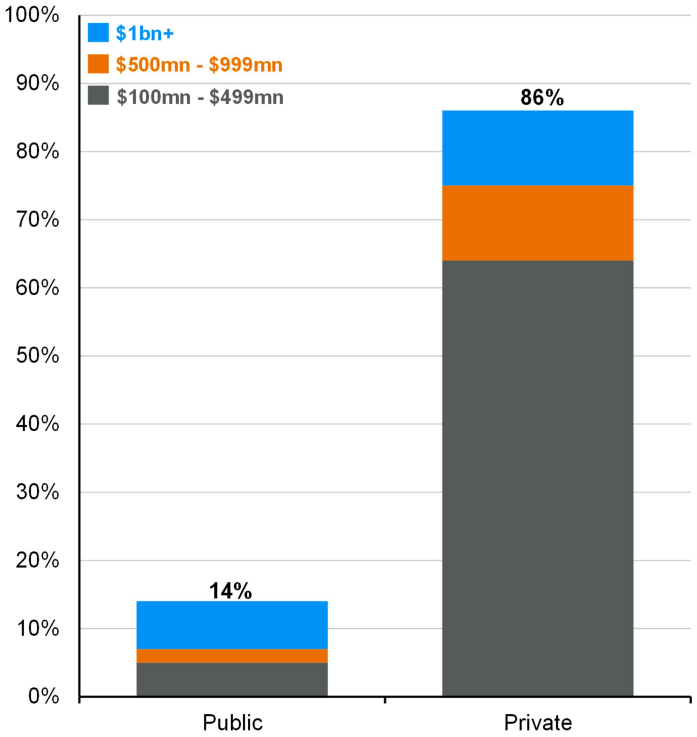
Median age and average market value at IPO

Years, USD billions



U.S. companies split public vs. private

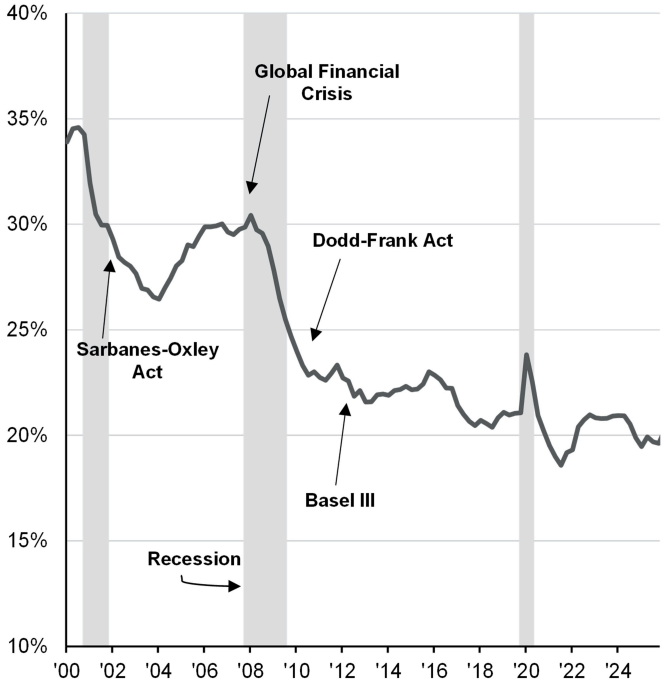
Companies with revenue greater than $100mn, share public vs. private



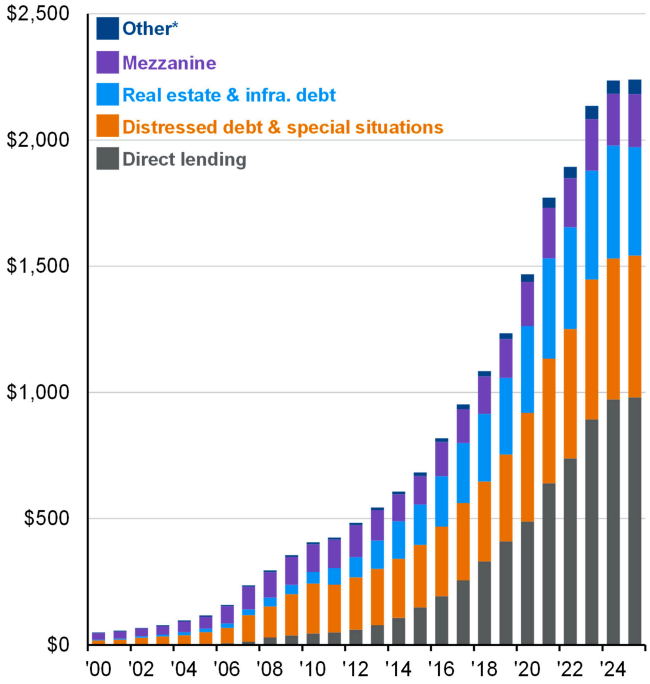
(Top Left) Labor adjustments include wages and benefits. Corporate profits are calculated after tax and with capital consumption and inventory valuation adjustments. (Top Right) Data sourced from the 2024 Consumer Expenditure Survey. (Bottom Left) Number of listed US companies is represented by the sum of the number of companies listed on the NYSE and the NASDAQ. Average market value is calculated by dividing the total market value at first closing price by the total number of IPOs for each period. The sample is IPOs with an offer price of at least $5, excluding ADRs, unit offers, close-ended funds, REITs, natural resource limited partnerships, small best efforts offers, banks and S&Ls, and stocks not listed on CRSP (CRSP includes Amex, NYSE, and NASDAQ stocks).Data are as of June 30, 2026.

Sources: FactSet, Standard & Poor's, J.P. Morgan Asset Management, and Bloomberg

U.S. bank lending
% of total nonfinancial corporate debt, quarterly



Global private credit AUM by type
USD billions, end of period



(Right) 2025 data are as of 3Q25. *Other includes venture debt and fund of funds. Data are as of June 30, 2026.

Sources: FactSet, Standard & Poor's, J.P. Morgan Asset Management, and Bloomberg