



FEBRUARY 2026

## EXECUTIVE SUMMARY

The past year was dominated by extreme concentration, speculative momentum, and a singular obsession with artificial intelligence - while large swaths of the market were left behind. Our portfolio sits squarely in the latter camp, and the resulting divergence weighed heavily on performance. Our positioning reflected a deliberate decision to avoid areas where expectations had become unanchored from fundamentals and to instead concentrate capital in businesses trading at discounts to normalized earnings power, often in sectors and geographies that had fallen out of favor. That discipline came at a cost in a year when speculative behavior was rewarded, and patience was not.

Compounding these challenges, we made more unforced errors than usual. While reliving mistakes is rarely the most enjoyable exercise, it's one of the most invaluable components of a durable investment process. This letter reflects a candid assessment of those lessons and the changes we've made to reduce the likelihood of similar outcomes in the future. Importantly, we have not stood still.

Over the past year, we have materially reshaped the portfolio—exiting positions where our confidence eroded, reallocating capital toward higher-conviction opportunities, and sharpening our focus on businesses with simpler stories, stronger balance sheets, and clearer paths to value realization. What remains is a portfolio of businesses where revenue growth, margins, and free cash flow remain intact, even as valuations have compressed.

The result: the portfolio today trades at a substantial discount to the broader market on nearly every conventional metric. We believe this disconnect reflects pessimism and exhaustion rather than permanent impairment, and if we're right, our portfolio is positioned to benefit disproportionately as markets broaden and fundamentals reassert themselves.

## THE YEAR IN REVIEW

BlackRock CFO described 2025 as “one of those eye-watering white-knuckle roller coaster experiences.” That seems fitting. Last year kicked off with newfound confidence following Trump's inauguration and promises of a “golden age” for America. Optimism continued into February but was shattered with the announcement of Liberation Day tariffs. For a brief moment, the world teetered on the precipice of a major shift in the global economic order. But after a week of outright panic, the administration quickly reversed course, and risk appetite returned as quickly as it had evaporated—marking the S&P's fastest recovery in history.

For the full year, the portfolio declined by 1.4%, net of our highest class of management fees, trailing the MSCI ACWI's impressive 22.9% return.<sup>1</sup> We preserved capital during the year's early drawdown and outperformed by nearly 3% through the first quarter. But we failed to keep pace with the animal spirits that followed and gave back those gains as leadership took on an increasingly speculative tone after Liberation Day. The portfolio struggled into October, before turning a corner and closing out the year with two straight months of gains. While we are happy to have squeezed out a small gain on the year, we are disappointed with our relative performance. For the second consecutive year, we've generated lackluster returns, while broad indices have posted gains of more than 20%. There's no sugarcoating it. But context matters.

Momentum has been the single defining force across equity markets for the past several years, with performance increasingly driven by narratives rather than fundamentals. While a narrow group of fast-growing mega-caps dominated earlier in the cycle, leadership migrated further down the quality spectrum to close the year—with meme stocks, SPACs, heavily shorted names, and unprofitable companies among the strongest performers, as returns increasingly detached from reality.

Recent history notwithstanding, value and momentum can and have coexisted over time, and while both approaches have outperformed over the long term, cheap stocks have historically lagged during the most robust periods of momentum. The most challenging stretches for value tend to coincide with the later stages of a bull market when capital flows solely toward the most speculative opportunities. This pattern is consistent throughout history, but the current cycle has been one for the record books. For perspective, we note that the two years leading up to the market's 2000 peak were the strongest on record for momentum. These past two were a close second. And if we tack on 2023, it has been right on par with the dot-com era.

Strongest Momentum 2-Year Performance Periods Since 1998 (Non-Annualized)				
Rank	Time Period	Top Momentum Quintile	S&P 500 Index	Momentum Excess
1	1998-1999	130%	56%	75%
2	2024-2025	91%	47%	43%
3	2023-2024	92%	58%	35%

Source: Morningstar Direct

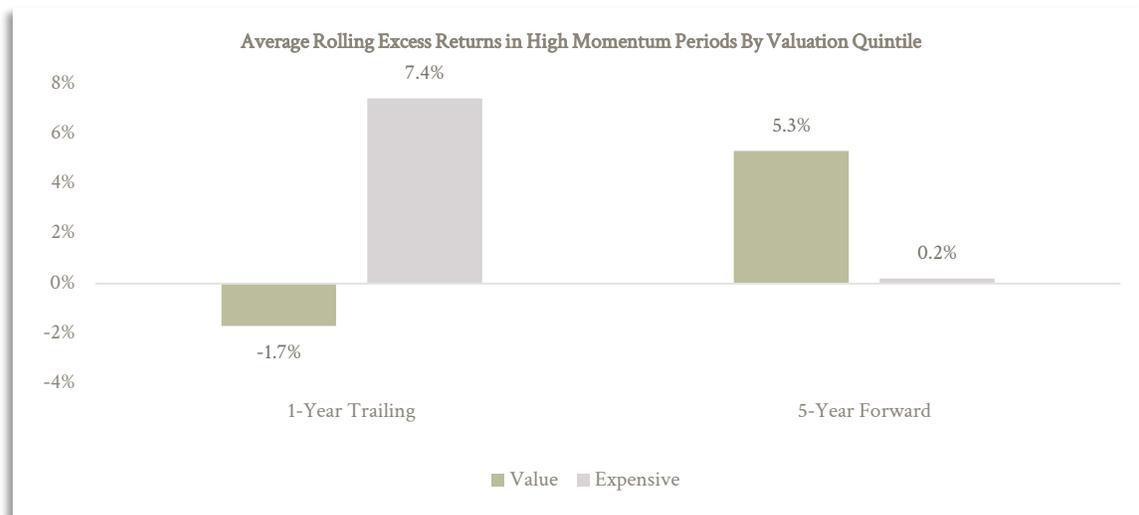
<sup>1</sup> For standardized performance data, including 1-year, 3-year, and since-inception net returns with benchmark comparisons, please refer to the Fact Sheet here. Past performance is not indicative of future results.

These late-cycle dynamics have clearly chipped away at our long-term alpha - after outperforming the MSCI ACWI by roughly 2% (net of fees) annually through 2023, we now find ourselves trailing the MSCI ACWI Index since inception. Again, context matters.

**As our long-time followers know, our best relative performance generally comes during challenging times, while our worst usually accompanies more frothy markets.** Consequently, taking a snapshot of a conservative, low-beta strategy at the peak of a momentum cycle is always going to be a difficult look. Just as taking a snapshot of an aggressive, high-beta strategy at the 2022 bottom looked terrible. Yet, that moment of maximum discomfort, when relative returns looked their worst, proved to be the best time to allocate to those strategies. If history is any guide, we suspect that moment is now for more conservative strategies.

**Mean reversion remains one of the most powerful forces in finance, even if it is routinely ignored.** That's why forward returns for value have historically looked best following extreme periods of speculative excess—cheap stocks have gone on to outperform meaningfully over the subsequent five-year periods, while expensive stocks struggle to meet elevated expectations (chart below). Yet most investors still prefer to chase what's working rather than allocate to what's been left behind.

If this momentum continues unabated, what's worked will likely keep working—and we will likely continue to lag. But after three consecutive years of 20%+ index returns, that seems like a long shot.

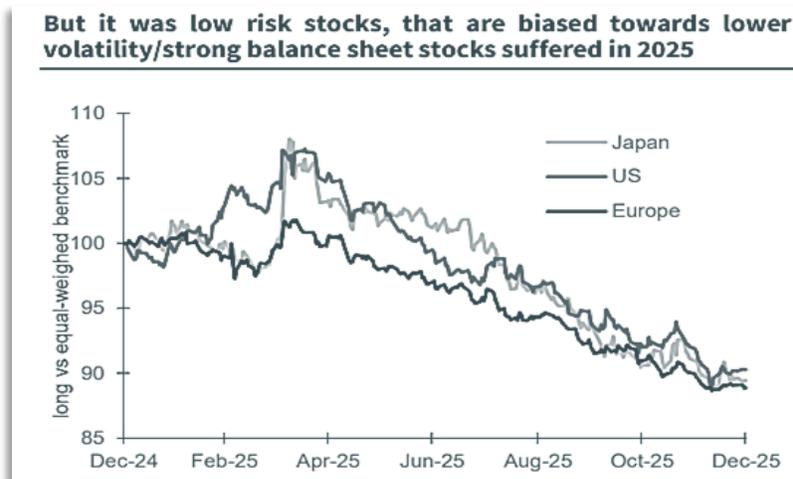


Source: Empirical Research Partners

## ADDRESSING RECENT UNDERPERFORMANCE

A friend recently compared investing with Broyhill to short selling. You're uncomfortably out of sync with rising markets that remind you daily that you're wrong. Most of the time, you're fighting the tape, resisting narratives, and watching others prosper while you wait. Most of the time, the market disagrees with you. Until it doesn't. That's just the nature of operating away from the consensus, and speculative rallies test that conviction more than skill. It's not easy to remain disciplined when the beaten path is paved with golden data centers by crypto millionaires. But we accept that discomfort in the short term to compound capital over the long term. We acknowledge that our recent performance is unlikely to convince anyone to give up on momentum investing in passive indices. But markets have a way of humbling certainty. When expectations reset, and sentiment bends back toward reality—as it always has—valuation and fundamentals should regain their footing. And patience should be rewarded.

**In investing, diversification is supposed to reduce both risk and volatility. Lately, however, it has simply reduced returns.** It's been difficult to outperform with fewer than a dozen stocks dominating the benchmarks. But it's not the first time. In 1999, amid soaring dot-com stocks, more S&P 500 companies fell than rose. Last year, anything AI-related—chip makers, power generators, producers of equipment used to build data centers—was up, while much of the rest of the market was down. In 1999, if you were an internet stock, you boomed. If you weren't, no one was interested. Much the same applies today to AI.



Source: SG Cross Asset Research/Equity Quant

AI-related stocks have accounted for 75% of S&P 500 returns, 80% of earnings growth, and 90% of capital spending growth since ChatGPT launched in November 2022.<sup>2</sup> If you haven't been riding the AI rocket ship, it's been almost impossible to keep up. High-beta, momentum-driven factors have dominated returns, funded by the steady unwind of positions in cheap, low-beta defensive stocks - areas we deliberately fish - which has significantly weighed on our performance.

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<sup>2</sup> JPM Eye on the Market, September 24, 2025

The cost of being totally out of sync with an AI-driven speculative market was compounded by a greater-than-normal share of unforced errors last year. We will make mistakes from time to time. But this has been a frustrating stretch. Bluntly, stock selection was poor, and errors were compounded by the uncomfortable side of concentration — the same structure that has historically produced our biggest long-term winners, worked against us last year.

**For the full year, a handful of large losses outweighed a solid group of winners.** The portfolio had six names (PM, DLTR, IQV, CRL, KOF, TMO) that contributed more than 100 bps to performance, and six names (AVTR, FI, FUN, BAX, NICE, VVV) that detracted by the same amount.

**Our largest contributors were Philip Morris, Dollar Tree, and IQVIA.** Winners shared a common thread: durable businesses with identifiable catalysts that the market had mispriced.

- **Phillip Morris was a top contributor for the second year in a row as the company continued to benefit from Zyn's explosive growth.** After years of skepticism, the trajectory of reduced-risk products became increasingly difficult to ignore. In our view, the stock's recent performance reflects a narrowing gap between perception and fundamentals, validating our thesis that the transition away from combustible cigarettes would drive a re-rating for the industry leader.
- **Dollar Tree rallied sharply after tariff-induced panic proved overblown and the cleaner post-Family Dollar business began to shine through.** While the turnaround has been uneven, the simplification of the business and improvements in execution at the core Dollar Tree banner reinforced our view that normalized earnings power is materially higher than the market had been discounting. We see the stock's recovery as a partial unwind of excessive pessimism rather than a full repricing of the opportunity ahead.
- **IQVIA contributed meaningfully as fears around biotech funding and clinical activity began to ease.** While sentiment toward the sector remains fragile, the company's role as a mission-critical infrastructure to drug development remains unchallenged. The first leg of the industry's recent rally was sparked by stabilization, rewarding patience through a prolonged industry downturn. We expect the next leg to gain steam as the recovery accelerates.

**Our mistakes were costly. Our largest detractors were Avantor, Fiserv, and Six Flags.** Losers also shared a common thread: financial leverage amplified by execution missteps.

- **Avantor was our biggest detractor from performance on the year.** When we initiated the position, we underwrote a classic recovery setup: orders bottom, gradually recover, and earnings inflect. While this cycle has played out longer than we initially expected, with uncertainty magnified by unpredictable government policy, the industry upturn has become increasingly difficult to ignore. The issue for Avantor has been that a cyclical downturn morphed into competitive and operational challenges, with company-specific execution masking the industry upturn. Consequently, we cut the position in half after the company announced management changes and second-quarter results that again fell short of our expectations, and reinvested the proceeds into Thermo Fisher, the primary beneficiary of Avantor's

challenges. We continue to maintain our reduced position in the company as we view AVTR as a rare strategic asset with multiple self-help levers, with the option of a strategic sale should those levers fail to impress recently engaged activists. In the meantime, the group remains under-owned with substantial capital on the sidelines still looking for an entry point, while revenues are reaccelerating, reshoring investments are set to provide incremental upside, and recent agreements between big pharma and the current administration have removed much of the downside risk associated with policy headwinds.

- **Fiserv was a close second.** This was a particularly painful loss because we thought we owned a dominant business with a flawless record of consistent execution, trading at a large discount to the market and to its own history. We increased our investment through the first half of the year because we believed the market was overly punitive in assessing short-term headwinds and slowing growth at Clover. As the stock's decline accelerated and the valuation collapsed, we actively questioned what we might be missing, seeking additional context, perspective, and data to stress our assumptions. In hindsight, we over-weighted the probability that the sell-off was driven by competitive dynamics and overlooked the probability of more structural issues beneath the surface. As it turned out, that "flawless execution" was a red flag. We immediately exited the position when we concluded the company was unanalyzable. We now believe the most similar analogue for Fiserv post the reign of former CEO Frank Bisignano, who resigned to join the current administration right before the stock's collapse, was the rubble left behind by Jack Welch at General Electric. For younger investors, not witness to Welch's glory days, Google's Gemini produced an impressive analogue available in this [report](#) and [dashboard](#).
- **Six Flags was our third-largest detractor from performance.** Our original underwriting leaned on our successful track record of investing in the industry, combined with operational upside and meaningful cost savings following the combination of Cedar Fair and Six Flags. We believed recession fears were misplaced, given historically resilient attendance at parks, and the merger created levers for improvement and balance-sheet optimization through asset sales, as the majority of the company's profits were generated by a handful of parks. We underweighted the risk that integration, weather, and a struggling low-income consumer would deliver significantly softer results in a tough discretionary backdrop, and that "fixable" would take longer than opportunity cost, or the company's overleveraged balance sheet, could justify. We sold half of our position after second quarter results fell short of our expectations and the CEO stepped down, and later fully exited the position.

**In summary, this year was a reminder that being different carries both opportunity and risk.** We were early in avoiding the most crowded areas of the market and late in benefiting from the rotation away from them. We also made mistakes—both in what we owned and in what we chose not to own. But when we saw evidence that a thesis had broken, we exited and reallocated capital to higher conviction opportunities. Conversely, where declines were driven by shrinking multiples rather than shrinking fundamentals, we increased our investments. While this discipline has served us well over the past two decades, "averaging down" clearly hasn't helped us lately.

## LESSONS LEARNED

**Over the years, falling knives have left the battle-scared hands of value investors with well-earned calluses.** Collectively, they are the price of admission for value's long-term outperformance. Broyhill is no exception to this rule. Provided our thesis remains intact, our approach has always led us to increase positions as prices decline. This is not reckless contrarianism; it's arithmetic; it's our edge. It's required to exploit what we see as the biggest pool of alpha left on the table today – time arbitrage driven by the duration gap between pods and passive. It's rewarded us handsomely over our history, which is why it remains central to how we invest.

**That said, this past year has forced us to confront the boundaries of that framework.** We don't believe the correct lesson is to stop averaging down. We think the right lesson is to be more disciplined about *when* and *how* we do it. It's always been difficult to distinguish between "the market disagrees with us" and "we are wrong." And there is a fine line between patience and inertia. That determination is only clear in hindsight. But what last year reinforced is the importance of recognizing a third category: situations where we can no longer responsibly underwrite the range of outcomes.

**To that end, we have refined how we translate conviction into capital allocation. Specifically, we have formalized several process improvements designed to introduce more discipline around adding to losing positions, and separate analytical conviction from behavioral persistence.** Practically, this means placing greater weight on a small set of non-negotiables before adding capital.

- First, we will cap the total capital invested at cost in any idea, regardless of how cheap it gets, as looking only at current portfolio weight after a stock has declined can be misleading. Capping cumulative cost basis prevents a 100bps drag from compounding into a 500bps drag.
- Second, when a position declines or underperforms substantially, we will now require an updated pre-mortem - a memo that argues the bear case as if the market is right and we are wrong - before any additional capital can be deployed. And we must identify new disconfirming evidence, not just repeat the original thesis at a lower price.
- Third, we must increase the probability weightings of our bear case to reflect what the market is telling us, because a big drop can suggest that a "tail risk" is no longer a tail, but the central tendency. Mathematically, increasing the downside probability decreases the expected return, removing or at least reducing the justification for buying more.

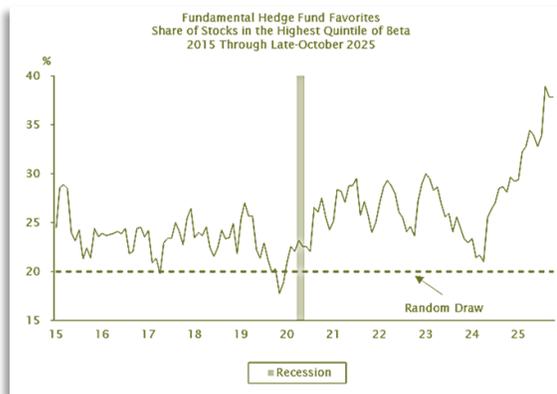
**Going forward, increasing a position will require more than a widening discount to our estimate of intrinsic value.** It will also require reaffirmed confidence in why the downside remains limited. When new information expands the distribution of possible outcomes—introducing paths that are harder to handicap or risks that are no longer transient—we will no longer treat lower prices as an open invitation to get bigger.

**These refinements do not represent a departure from our philosophy. They are an evolution of it.** We remain long-term, valuation-driven investors who believe the market routinely misprices uncertainty. But we are equally committed to recognizing when uncertainty crosses from uncomfortable to unquantifiable.

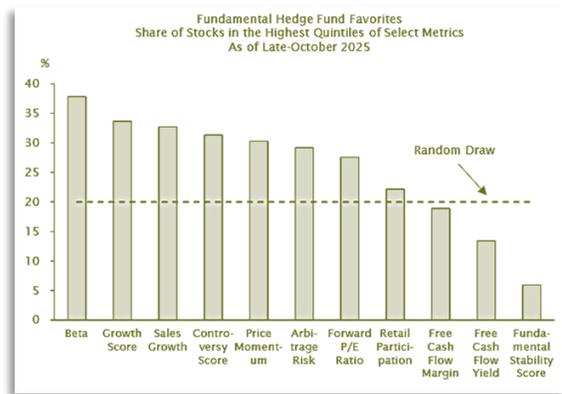
**There will always be periods when our execution and performance fall short, which is why we are always on the hunt for ways to improve our process without deviating from the tenets of our philosophy.** There's no manual for how to do this, so we approach it with a balance of humility and confidence, fix the obvious, stress-test the subtle, and dig into the corners we hadn't thought to look.

None of these changes who we are or what we do. We will remain concentrated. We will remain contrarian. We will continue to buy what others are selling when we believe the odds are in our favor. But we will be more systematic about how we do so, quicker to recognize when the facts have changed, and faster to act on that recognition.

Investors don't hire Broyhill to own the biggest companies in the market. They don't hire Broyhill to chase new technologies or to simply buy what's going up. There's no shortage of investors happy to do that - hedge fund portfolios are more correlated to retail favorites than at any point in recent memory, creating one enormous, crowded bet on a single narrative (chart below). Many of these investors are doing better for the time being. They are also taking greater risks than are generally understood, or that frankly, we are comfortable underwriting. We suspect those risks will soon be better understood and much more obvious. Until then, we are simply trying to generate reasonable returns for investors while not getting run over. We failed last year. And we've course corrected. But that, in a nutshell, is why we stayed on the sidelines rather than joined the folly.



Source: Empirical Research Partners



Source: Empirical Research Partners

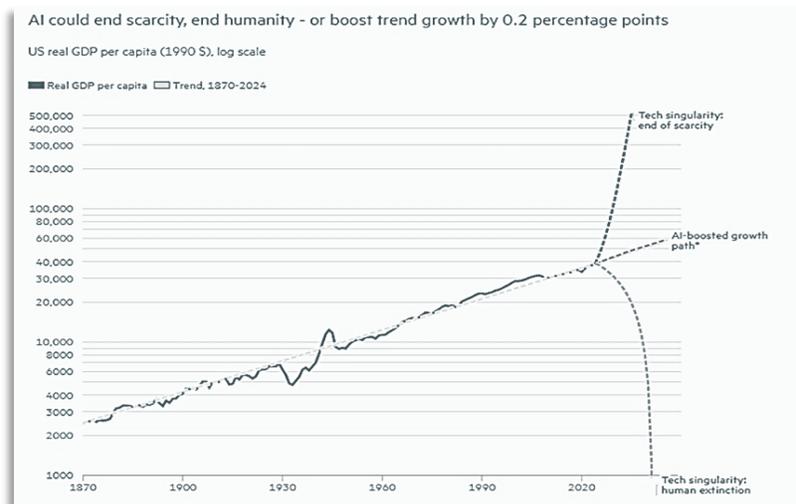
**The good news for forward-looking investors: the unusual momentum of the past few years has kept the spread between the “haves” and “have-nots” growing.** If history is any guide, that should reverse at precisely the moment patience feels most difficult. Or about now.

In the pages ahead, we'll detail how the AI capex cycle has magnified that gap—concentrating capital, attention, and optimism in a narrow set of winners while quietly starving the rest of the market and laying the groundwork for the most compelling opportunity set we've seen in years.

## THE (AI) CAPITAL CYCLE

*The railroads were a bubble and they transformed America. Electricity was a bubble, and it transformed America. The broadband build-out of the late-1990s was a bubble that transformed America. I am not rooting for a bubble . . . but given the amount of debt now flowing into AI data center construction, I think it's unlikely that we're going to get out of this technology that isn't overbuilt and doesn't incur us a brief painful correction.*

*- Derek Thompson, AI Could Be the Railroad of the 21st Century.*



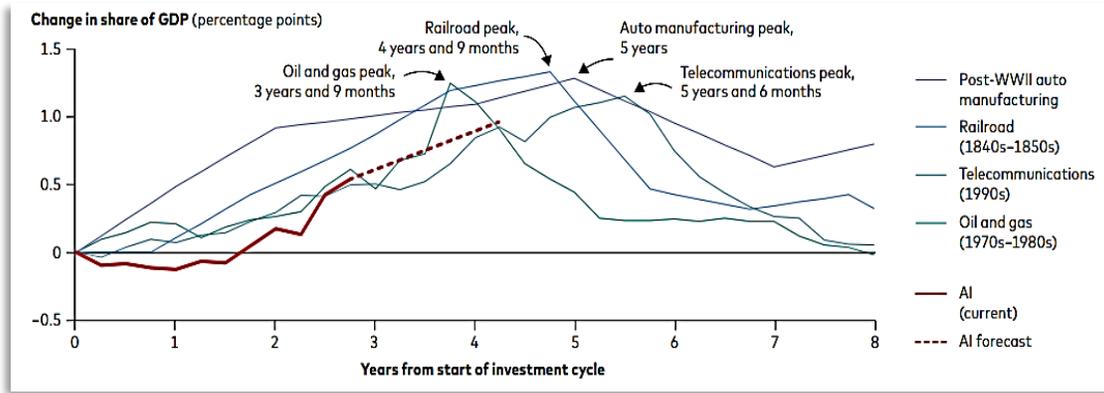
Source: Financial Times

The surge in AI-driven infrastructure is a powerful force on par with the greatest capital investment cycles in history. Previous cycles, such as the build-out of railroads in the 1800s, electricity in the 1920s, and the late 1990s surge in telecommunications infrastructure, required heavy investment to retool the economy for a new era. In every case, excessive enthusiasm led to excessive investment, resulting in far more infrastructure than was needed, asset prices far too high relative to fundamentals, and ultimately losses far greater than anyone imagined. These bubbles didn't deflate because the technology disappointed. They deflated because the economic benefits they produced were captured downstream by the consumers and companies that employed the technologies.

**While it's difficult to gauge where we stand in the current cycle, historical comparisons can provide some perspective – and a dose of humility.** Since the launch of ChatGPT in late 2022, AI investment has contributed roughly \$250 billion to US GDP, as capital expenditures by hyperscalers (major cloud providers operating massive-scale data centers) increased from \$160 billion (0.6% of GDP) to an estimated \$415 billion (1.4% of GDP) last year. Current estimates put the pace of spending on track to reach 2.1% of GDP this year - approaching levels that coincided with peak spending during the electrification of the US preceding the stock market peak in 1929, and the internet broadband buildout that accompanied the dot-com peak.

**It would seem the clock is ticking on this cycle.** The boom, now entering its fourth year, is already mature and in line with historical buildouts, which typically peaked over a 4-6-year period (chart below). Meanwhile, consensus is comforted that continued investments by hyperscalers will keep asset prices propped up, with consultants like McKinsey estimating global investment approaching \$7 trillion by 2030.

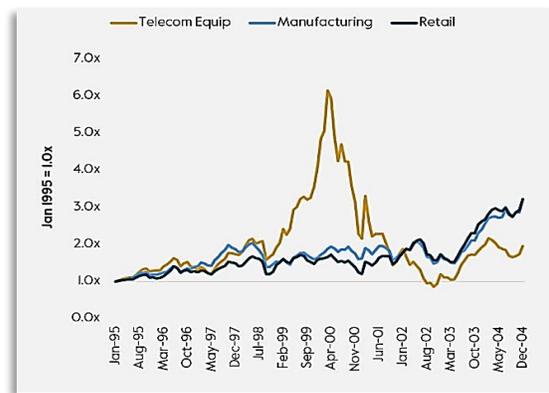
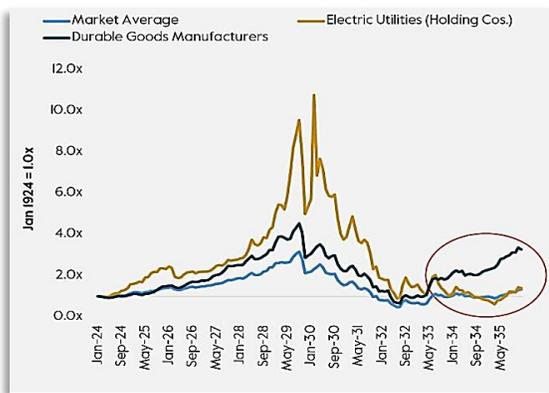
What the consensus appears to be overlooking, however, is that previous investment cycles have seen stocks peak 1-2 years *before* capital expenditures, and often while investments are still accelerating. The market doesn't wait for the last data center to be built. It doesn't care about the absolute level of investment. It sniffs out the change in growth. Notably, current estimates imply that growth rate is set to slow considerably this year.



Source: Vanguard

It is difficult to overstate AI's potential to transform the global economy. But the outlook for investors is more complicated. Sentiment is exuberant - AI has captured our collective imagination as venture capitalists write blank checks to AI startups with grand ideas and little revenue, market participants bid up valuations by hundreds of billions of dollars on the announcement of circular partnerships, and retail investors more attracted to gambling than a 40-hour work week, chase quantum computing stocks after 1000% gains over the past year. Meanwhile, risks are rising alongside elevated expectations, while history offers a sobering reminder: the early winners at the forefront of technological change rarely remain on top.

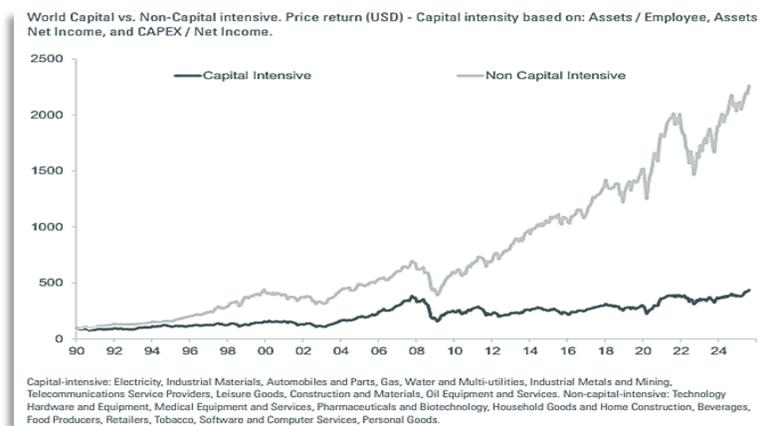
New technologies are transformative—but also notoriously and unforgivingly disruptive to incumbents, capital providers, and narratives alike. Early investors in newly created utility ventures and dot-com companies amassed large “paper” fortunes. Still, the vast majority were eventually wiped out as hundreds of local utilities consolidated to one or two regulated monopolies per region and thousands of VC-backed dotcoms went belly up. In both cases, it took decade(s) for the economy to absorb excess capacity and for stocks to recover to their prior peaks.



Source: The Carlyle Group

Simply stated, investors have gotten plenty of experience spotting technological revolutions throughout history; but they haven't gotten much better at identifying the winners from those shifts. Turns out, there's little correlation between blistering growth and actual profitability, and a world of difference between the manufacturers of new technologies and the ultimate beneficiaries. The pattern is not coincidental. Firms flush with cash and intoxicated by optimism consistently overinvest in projects that generate poor returns on capital. The market rewards the spending — until it doesn't. Consider that the original bull case for today's hyperscalers rested on their capital-light business models, but while the stocks scale new highs, that thesis has quietly inverted.

As the AI arms race has accelerated, capital expenditures at several hyperscalers have surged to levels that now resemble regulated utilities. The upside for utilities is that those investments are guaranteed a satisfactory rate of return. The downside of the AI arms race is that capital intensive companies tend to underperform over time.



Source: Goldman Sachs Global Investment Research

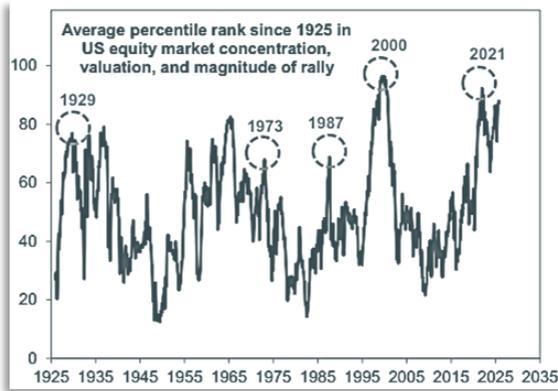
The silver lining? Initial investors and infrastructure builders suffered catastrophic losses. Still, those losses subsidized the creation of infrastructure for the users of that technology and the companies that built on top of it, who captured most of the economic value at a fraction of the cost.

This cycle appears to be playing out in a similar fashion, with businesses operating at the forefront of artificial intelligence changing hands at dizzying heights. But if AI proves to be as essential as electricity or the internet, the related economic gains will likely be just as diffuse, with benefits ultimately accruing to more traditional sectors of the economy that stand to gain meaningfully from productivity improvements, cost efficiency, and margin expansion. In a nutshell, value-oriented firms invest more cautiously and compound capital more efficiently. This would be consistent with history, as major economic transformations have often coincided with equity market transformations.

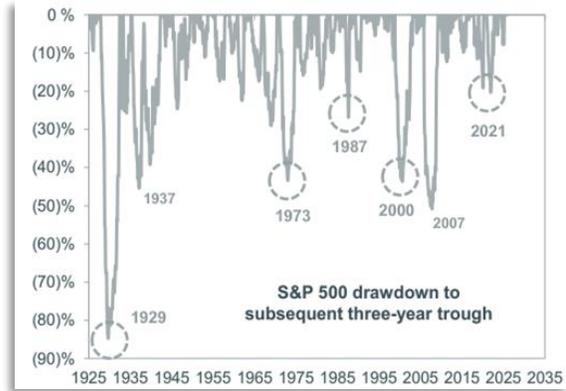
## WHERE WE SEE VALUE

The upside for investors is that there's no need to call the peak, duration, or ultimate winners of the AI cycle because there are plenty of other assets to choose from trading at compelling valuations. Said differently, tilting away from AI darlings does not require trimming equity exposure or accepting lower long-term expected returns, because investors are well compensated for taking on risk outside this narrow corner of the market today.

As a result, constructing a portfolio that doesn't rely on a continued AI-hype cycle without sacrificing upside is fairly easy. The hard part is having the courage and staying power to accept the enormous tracking error and the accompanying career risk that comes with deviating from concentrated, market-cap-weighted indices. Considering the magnitude of losses suffered by speculators throughout history's previous great technological shifts, increased tracking error seems like a small price to pay to avoid the potential for catastrophic financial losses.

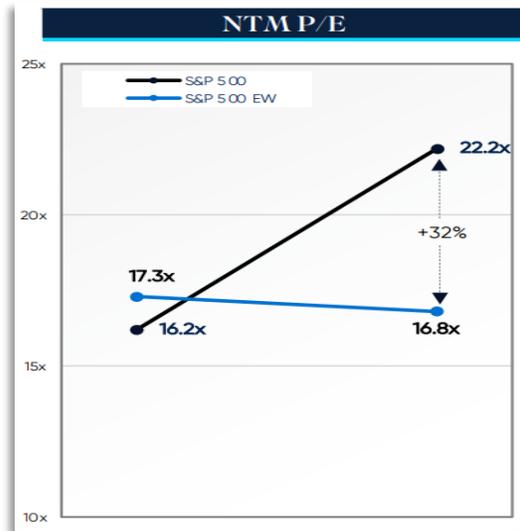
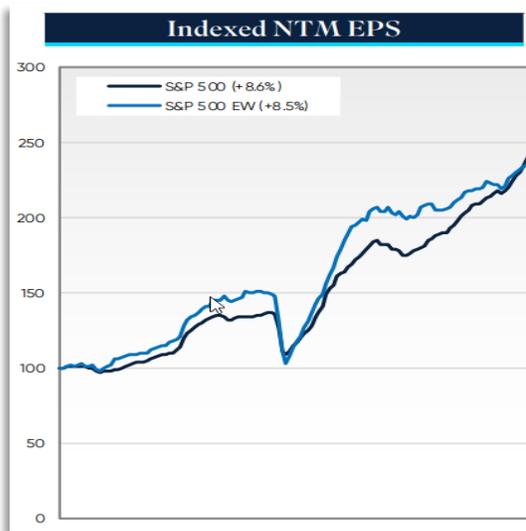


Source: Goldman Sachs Global Investment Research



Source: Goldman Sachs Global Investment Research

Encouragingly, market leadership has already begun to broaden, as the fourth quarter delivered a meaningful shift toward more diverse participation, and that shift has accelerated into the New Year. More encouragingly, we see ample runway for continued rotation, as dispersion remains elevated. In fact, in the three years since the launch of ChatGPT, cap-weighted indices have outperformed equal-weighted indices by more than 1,000 bps per year – a record more extreme than the tech bubble era and the most extreme on record. And contrary to popular opinion, earnings growth for both indices over the long term has been almost identical. Nearly all of the outperformance was driven by valuation.



Source: Lyrical Asset Management, Factset

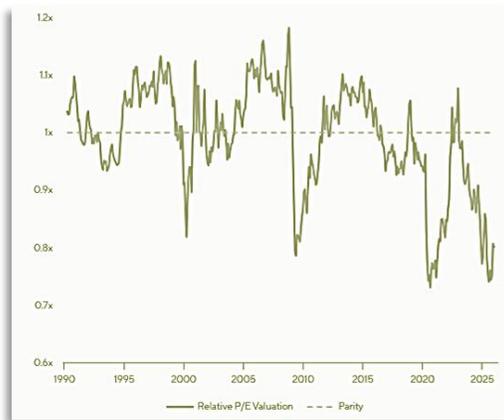
Now that investors are beginning to sniff out and appreciate the bargains on offer today, we think broad market leadership has a long way to go, as many assets outside US megacaps remain decidedly cheap. Against this backdrop, a number of opportunities stand out as particularly compelling. Value stocks everywhere are trading at some of the widest discounts on record. Nearly all sectors of the market outside of the world's largest companies have endured substantial multiple compression, with defensive equities at multi-decade lows, small- and mid-cap companies as cheap as they've been relative to large caps since the late 1990s, and opportunities abroad even more compelling. We believe this has created an extremely promising starting point for long-term outperformance.



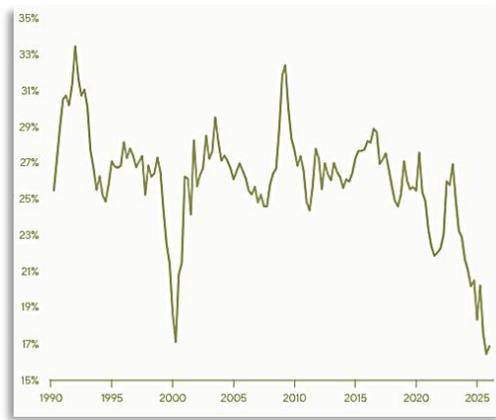
Source: Bank of America Global Investment Strategy

**We are finding exceptional value among global defensives.** These sectors have fallen to their lowest weighting since 2000, leaving them trading at a discount to both the market and their own histories, as sentiment has been deteriorating for years (chart below). Such dour sentiment is also evident in unusually high short interest, which creates the potential for meaningful buying pressure. From a portfolio construction standpoint, these sectors offer significant upside potential, and provide an element of defense, as big companies selling basic necessities tend to shine when the rest of the market is in trouble. Defensives have also historically been the best-performing sectors during rate-cutting cycles, with the added benefit of providing resilience if current AI enthusiasm proves misplaced or fades more quickly than expected.

DEFENSIVES RELATIVE FORWARD P/E RATIO



S&P 500 DEFENSIVE SECTOR WEIGHT

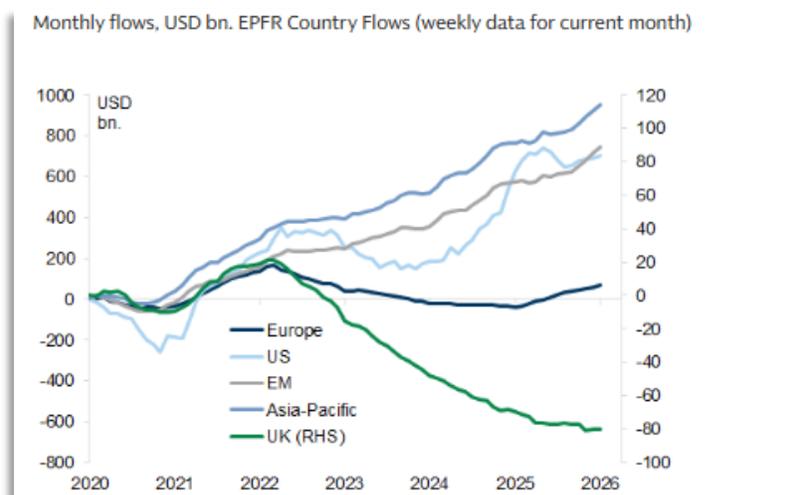


Source: GQG Partners, Empirical Research Partners

Consider Nestlé, the Swiss food and drink conglomerate. While historic inflation pressured margins over the last several years, the company is now successfully transitioning from defensive pricing to volume-driven growth. As prior cost increases fully catch up to consumer pricing—a lagging but reliable process—we expect a meaningful expansion in operating margins. The cost structure is further supported by stabilizing commodity cycles; while volatile inputs like coffee and cocoa have been recent headwinds, any normalization in these markets provides an immediate tailwind to the bottom line. Structurally, Nestlé is becoming leaner. Under new leadership, the company has streamlined its reporting zones and initiated aggressive workforce reductions and process automation. These efficiencies are not merely defensive; they are designed to redirect capital into high-impact marketing to accelerate organic growth. Despite these catalysts, the stock trades at a valuation multiple not seen in over a decade. Given the inherent stability of the consumer staples sector and Nestlé’s multiple internal levers for margin improvement, we believe the current valuation gap—both relative to the broader market and Nestlé’s own historical average—is fundamentally unsustainable.

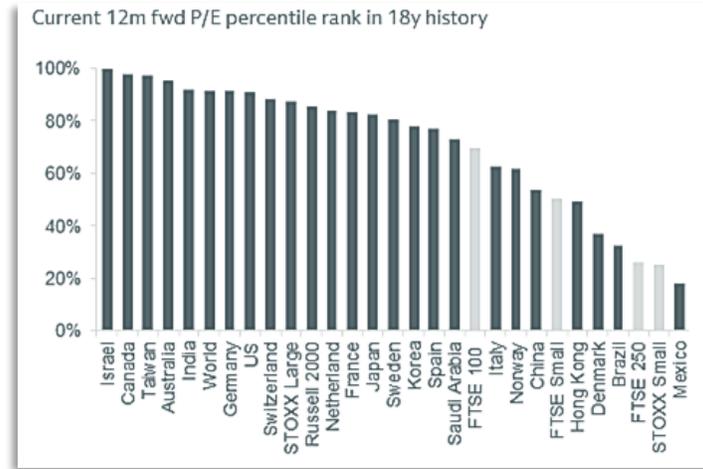
**Geographically, we continue to find some of the most attractive opportunities outside the U.S., as we see non-U.S. stocks offering better value, cheaper currencies, and,** in many cases, a more normal economic and political backdrop. And while American Exceptionalism continues to capture the collective imagination of investors, America’s market leadership took a back seat to the rest of the world last year – while the S&P itself rose by more than 17%, the World ex US posted its best year versus the S&P since 1993. In the short term, we think this may have escaped investors’ attention for the time being, given the strong absolute performance of US stocks. In the long term, we think investors will be well served to consider the implications of this shift, as American leadership has taken a sharp setback.

**Despite improving relative performance, investor skepticism remains entrenched.** Selling pressure across the UK remains relentless, while capital coming into broader Europe has barely turned positive after years of outflows.



Source: Goldman Sachs Global Investment Research

**Valuations outside of the US reflect this pessimism.** The discount applied to high-quality European businesses—many of them global leaders with diversified revenue streams—remains extreme by historical standards. Consistent with this view, the number of Western European holdings in our portfolio has continued to grow over the past year, a trend we expect to persist given the extreme undervaluation in the UK and the nearby continent.



Source: Datastream, Goldman Sachs Global Investment Research

Louis Vuitton Moët Hennessy is a good example of the opportunities we see in Europe. LVMH is a French multinational conglomerate specializing in luxury goods, including fashion, leather goods, perfumes, cosmetics, watches, jewelry, and wines and spirits. It owns over 70 prestigious brands, combining heritage craftsmanship with global retail and marketing expertise. The company’s earnings have been depressed due to a confluence of factors including luxury demand weakness across key markets, competitive shifts and market share dynamics, reduced profitability, and to some extent a lack of succession plan for Bernard Arnault. We think demand will return for luxury goods and with it will come improved profitability and a rerating in the stock.

## BOTTOM LINE

In a [rare interview](#), Dan Sundheim, Founder of D1 Capital, was asked which company he'd own if he couldn't touch it for 10 years. His response, we think, was informative - not only because of what he said, but because of who said it.

**There are very few tech companies I would say, I feel comfortable owning because tech just changes too quickly.** So, it wouldn't be a tech company. It would have to be a company with a moat that would be incredibly difficult to penetrate with a growth rate that was probably not super high, but well above GDP for a long period of time.

Sundheim is not a casual observer of technology cycles. He built his career investing in technology across public and private markets, internet platforms, and emerging technologies, which is precisely why his answer matters. It's not a dismissal of AI. It's a warning that reflects an understanding that technological leadership is often

fleeting, competitive advantages erode faster than expected, and long-term compounding depends less on narrative momentum than on durable economics.

That sentiment resonates deeply with our approach. Our priority has always been to compound capital prudently—not to chase every last dollar when risks are poorly understood, and returns depend on continued optimism rather than hard fundamentals. Our reluctance to participate in the AI frenzy has, without question, left money on the table. But like the circular financing of that party, we suspect that much of the capital being deployed with great enthusiasm today will ultimately find its way back to its rightful owners.

**In our view, the market has increasingly come to resemble a concentrated, momentum-driven growth fund. This is not an environment in which we feel compelled to abandon discipline.** If anything, it feels like a particularly poor moment to give up on cheap stocks with attractive assets, simply because they are unloved and being sold. So, we have no intention of replacing sound judgment with price momentum, chasing whatever philosophy happens to be working this quarter, or participating in the increasingly circular dynamics that characterize today's most crowded trades.

**We have deliberately chosen not to follow that path.** Very little of our portfolio is invested in stocks in broader market averages. Our portfolio looks nothing like the market. Relative to building data centers in space, it looks quite boring. And we find that comforting.

**We are positioned exactly where we want to be. And exactly where we believe we should be.** While we have rebalanced and refocused on higher conviction investments, with the majority of the portfolio invested in fresh names held for less than a year, our broader positioning remains consistent. We have maintained over 50% exposure to defensive sectors, over 50% allocated to small and mid-cap companies, and a significant allocation to businesses headquartered in Western Europe. We remain focused on identifying overlooked turnaround situations, significantly mispriced cyclicals, and businesses undergoing multi-year transformations—often where capital is scarce, sentiment is poor, and patience is required. We are concentrated in undervalued, established businesses where returns are driven by actual cash flows and durable moats—not by dreams of future products dependent upon the ultimate success of trillions in speculative capital investments. We own businesses with recurring demand, defensible economics, and multiple self-help drivers to create value.

**Notably, this positioning is not just Broyhill playing defense. It's the result of a decades-long process that leads us to opportunities where capital is scarce, where investors have abandoned opportunities, and where valuations and expected returns are as attractive as they've been in decades.** In an overvalued equity market dependent upon never-ending capital expenditure and a chorus of circular deals and partnerships, we sleep well knowing that we own many outstanding businesses at a substantial margin of safety.

We did not execute perfectly last year. We have been candid about that. We revisited our positioning many times throughout the year to ensure we weren't confusing confidence with rigidity, and we course-corrected when the evidence demanded it. But to be clear, our mistakes were not due to a rejection of technology.

We aren't avoiding AI. We understand it. We appreciate it. We have invested in it and will continue to do so – at the right price. And we use it extensively. Internally, we have embraced AI aggressively to enhance our research process, improve monitoring, and accelerate decision-making. But from an investment perspective, we remain

mindful that the greatest benefits of technological revolutions tend to accrue to users rather than producers—and that competitive forces eventually compress excess returns. So, rather than investing directly in technology, we have heavily invested in AI through companies we believe are set to gain the most from it.

**History suggests that extreme divergences in valuation, as we see today, have often been followed by multi-year periods of excess returns to value.** Over time, investing grounded in deep fundamental research has proven more profitable and more durable than chasing narratives or speculating on the promises of unproven technologies. We see no compelling reason to believe this cycle will be different. The weight of the evidence across economies and centuries remains clear: fundamentals and valuations matter.

We are keenly aware of the career risk that comes with sitting out the blow-off phase of a bull market. But we are equally aware of many more careers cut short by catastrophic losses. We've been doing this for over two decades and intend to keep doing it for at least two more. The trick to a lengthy career managing other people's money is threading the needle between analyzing fundamentals and accepting that markets routinely ignore them. Our willingness to accept discomfort while others follow the herd has historically been one of our greatest advantages—made possible by the long-term orientation of our partners.

For that trust, and that patience, we remain deeply grateful.

Sincerely,

A handwritten signature in black ink, appearing to read 'C. Pavese', with a long horizontal flourish extending to the right.

Christopher R. Pavese, CFA

# ABOUT BROYHILL

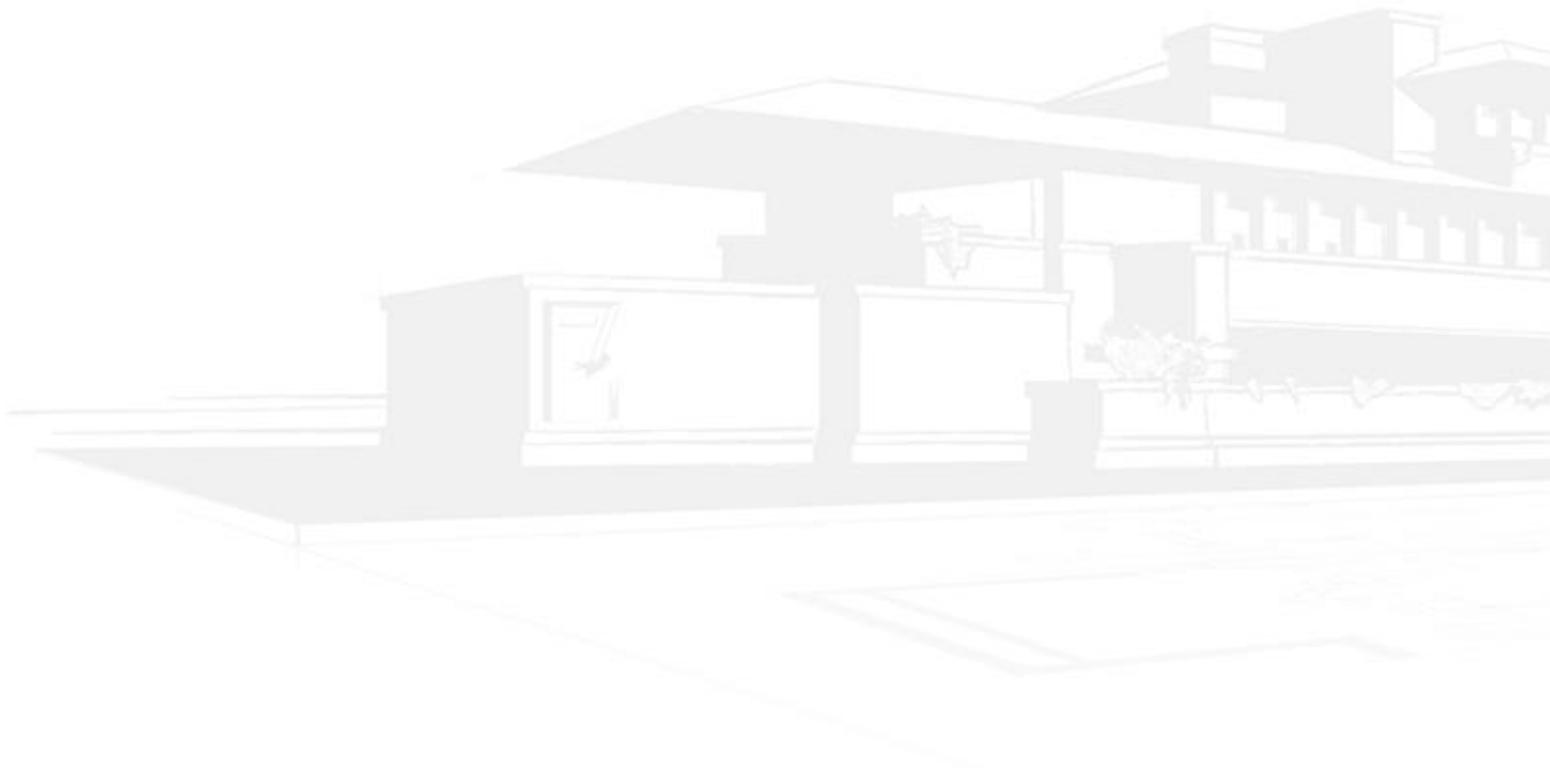
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