

Second Quarter 2026 (July 1, 2026)

The second quarter rally has been driven primarily by hopes for a lasting resolution to the Middle East conflict and a surge in confidence in AI-led earnings growth, particularly across some of the most cyclical areas of the economy. Secondary and tertiary sectors like semiconductors, power, and industrial infrastructure companies are benefiting as investors continue to be enthusiastic about a multi-year AI capex cycle. That said, the advance has become more contested late in the quarter due to higher Treasury yields, affordability concerns for the consumer in the general economy, and worries about the scale of AI infrastructure spending. In short, the second quarter has been a momentum stock quarter led by AI infrastructure stocks, but with growing debate over whether valuations and capital intensity are beginning to outrun near-term fundamentals.

AI Rising Tide Lifts a Lot of AI Boats...Especially the Dinghies

As mentioned above, cyclical AI-related stocks dominated returns in the second quarter. These companies are called cyclical because their profits can move sharply from year to year depending on the economy, capital spending cycles, interest rates, and investor appetite for risk. In many cases, they do not have the same long-term competitive advantages we seek in our core holdings, such as durable pricing power, recurring revenue, high switching costs, or consistently high returns on capital.

Cyclical stocks can perform very well when demand is at its strongest at the beginning of a cycle and investors are especially enthusiastic about a favorable future. They can carry added risk because current earnings may be temporarily elevated. A stock can look inexpensive on today's earnings, but if those earnings are near a cyclical peak, the valuation may be misleading. When the cycle turns, earnings estimates can fall and valuation multiples can compress at the same time, creating meaningful downside.

This distinction is especially important in AI infrastructure. We believe AI is a powerful long-term investment theme, but not every AI beneficiary will capture durable economics. Some companies will own critical technology, platforms, or recurring revenue streams. Others may benefit from a temporary surge in orders tied to data center construction, power demand, cooling, semiconductors, or industrial infrastructure. In momentum-driven markets, investors often treat these companies similarly, even though their long-term

economics may be very different. We believe our AI investments are characterized by companies with unique competitive positions and therefore are more likely to offer durable earnings growth over a complete cycle.

Consider Intel (INTC), which we do not own, the stock is up an amazing 216% for the second quarter. Before this year, the last period in which INTC grew its earnings was from 2016 to 2021 when net income advanced to over \$22 billion from \$13.1 billion and earnings per share (eps) grew to \$5.47 from \$2.33 per share. Since 2021, Intel's net income had collapsed to a net loss in 2024 of \$787 million, or -\$0.13 per share as the company lost the dominant chip position once associated with the "Intel Inside" era. Today, however, investors are increasingly optimistic about a potential turnaround driven by AI-related CPU demand and the possibility - though still lacking meaningful supporting data - that Intel can deliver advanced chip manufacturing services at scale, including packaging and, potentially, an external foundry business. While the intermediate-term AI landscape is difficult to forecast, analysts estimate Intel's net income could get back to \$5.5 billion or \$1.08 per share this year and possibly \$16.5 billion or \$3.75 per share by 2030. To put that in perspective, Intel currently trades at \$130 per share, or 120x expected 2026 earnings, 84x expected 2027 earnings based on Eikon estimates, and even 35x the ambitious profit expectations four years from now. In other words, investors are willing to pay \$130 per share today for 2030 earnings that would still be roughly one-third below 2021 levels. By comparison, shareholders paid an average of \$58 per share in 2021, less than half today's price when it earned net income of \$22.5 billion versus \$5.5 billion expected this year. In short, Intel is priced not just for perfection, but for a new paradigm—one that may or may not occur. And unlike in the past, the company no longer holds a dominant competitive position in the marketplace.

Why We Prefer Wide Economic Moats

An economic moat is a company's durable competitive advantage — something that protects its profits from competitors over many years. A moat lets a company earn high returns on capital for longer than normal because competitors cannot easily copy, undercut, or displace it. We prefer companies with economic moats because we believe they deliver superior, long-term, risk-adjusted returns. The list below is a sampling of our holdings across our portfolios that we believe have wide economic moats, as well as the moat type:

<u>Moat type</u>	<u>Portfolio Example</u>
Network effects	Visa, Mastercard, Meta
Switching costs	Microsoft
Cost advantage	TJ Maxx
Brand / intangible assets	Apple
Patents / regulatory barriers	Eli Lilly, S&P Global
Scale / ecosystem	Nvidia, McKesson

Economic “Moats” Funding Cyclical AI

A corollary to the cyclical stock leadership of the past 15 months, which accelerated in the second quarter, is that many companies with “economic moats” have seen their stock prices down meaningfully or only up slightly despite significant earnings growth. In many cases, we believe these stocks have served as market participants’ funding sources for the cyclical AI infrastructure leaders. Please see below examples of companies with wide moats from each of our portfolios, their stock price change in the first half of 2026 and their durable earnings growth outlook:

	Stock Price Change YTD	2026 Earnings Growth Outlook**
SEM Select Growth		
Mastercard	-10.0%	16.0%
Nvidia	7.3%	87.0%
Stryker*	-10.4%	11.6%
SEM Dividend Growth		
Cencora	-16.2%	11.1%
Microsoft*	-22.9%	15.7%
Rollins	-30.5%	12.0%
SEM Small to Mid-Cap		
Fair Isaac	-29.3%	44.4%
IDEXX Labs	-22.2%	11.9%
Veeva Systems	-20.5%	11.9%

* MSFT and SYK are in Select and Dividend Growth

** Source Eikon as of 6/30/26

High Beta or Low Volatility; Tortoise or the Hare

As further evidence of the AI trade soaking up investor funds from high-quality businesses, a recent *Wall Street Journal* article noted the S&P 500 High Beta Index—a rough proxy for cyclical stocks because it includes the 100 stocks in the index with the highest share price volatility—has returned 104% since proposed high tariff rates were rolled back on April 9 of last year. By contrast, the S&P 500 Low Volatility Index, which includes the 100 least volatile stocks in the index, is up just 8%.

	4/9/2025 – 6/30/2026
S&P 500 High Beta Index	104%
S&P 500 Low Volatility Index	8%

Data Source: FactSet

It would be easy to conclude that low-volatility stocks underperform over time. They seem to be overly defensive. However, as the article also noted, the Low Volatility Index handily outperformed the High Beta Index since inception over the nearly 35 years leading up to April 9th, 2025, since earnings are generally more durable than their volatile peers. Market dynamics over the past 15 months have been truly unusual as volatile stocks, with volatile earnings, rarely outperform for very long.

	11/30/1990 –4/9/2025
S&P 500 High Beta Index	2,538%
S&P 500 Low Volatility Index	3,036%

Data Source: FactSet

Summertime

The market’s enthusiasm for lower-quality cyclical AI beneficiaries may continue. Momentum cycles often last longer than expected, especially around transformative technologies. But over time, we believe the distinction between true compounders and temporary beneficiaries becomes clear. Our objective is not to own every company touched by AI, but to own those most likely to convert AI-related demand into durable earnings growth, high returns on capital, and long-term shareholder value.

Periods like this can be uncomfortable because stock prices do not always reflect business progress in the short term, as all three growth portfolios - SEM Select Growth, SEM Dividend Growth and SEM Small to Mid-Cap, currently lag despite being composed of strong, quality businesses. In some cases, companies with the strongest competitive positions have become funding sources for more speculative AI infrastructure trades. We have seen similar environments before. The elongated disconnect between portfolio profits and portfolio returns has been challenging, but the opportunity between the portfolio's intrinsic value and share price is only growing.

We believe our portfolios are positioned for that normalization, with exposure to businesses that combine secular growth opportunities with durable competitive advantages. Eventually, earnings durability, free cash flow, and returns on capital matter again.

Market participants often do not like to buy stocks when they are on sale, preferring popular affirmation today over returns tomorrow. We believe that all three of our portfolios are undervalued and it is worth the consideration to add to your investments or reallocate from current investments that may have recently benefited from the enthusiasm for certain AI stocks.

We appreciate your continued trust and patience. Our capital remains invested alongside yours, and we remain focused on owning high-quality businesses capable of compounding value through changing market environments. Best wishes for an enjoyable summer!

Sincerely,

<i>Don</i>	<i>Dan</i>	<i>Amy</i>	<i>Eric</i>
Donald R. Jowdy	Daniel T. McNichol	Amy A. Lord, CFA	Eric K. Lynch
CIO	President	SVP / Co-PM	Managing Director/ Co-PM

Investment advisory services are offered through Suncoast Equity Management, LLC, a Securities and Exchange Commission Registered Investment Advisor.

Performance Disclosure

Suncoast Equity Management, LLC (SEM) is an independent investment management firm established in 1997. Suncoast Equity Management is primarily an equity investment manager that invests in U.S.-based securities. The Select Growth composite includes all discretionary, fee-paying portfolios managed within this strategy. The creation and inception date of the Select Growth composite is 12/31/1997. As of 1/1/2022, the Suncoast Equity Management composite was renamed the Select Growth composite.

The Select Growth composite is an equity only composite employing the principles of Benjamin Graham & Warren Buffett. The discipline is a bottom-up fundamental approach and blends value and growth parameters. The portfolio consists of between 18-22 stocks.

Bundled fees include management consultant fees, custodial, trading, and advisor fees. Performance is calculated gross of all foreign withholding taxes. Additional information regarding policies for valuing investments, calculating performance, and preparing GIPS Reports, as well as a complete list and description of composites, is available upon request.

For the non-bundle fee accounts, the performance results presented are net of actual investment advisory fee and net of all transaction costs. For the bundle fee accounts, the performance results presented are net of actual investment advisory fee and net of all transaction costs and expenses. Investment advisory fees are described in Part II of Suncoast Equity Management, LLC's Form ADV. The management fee schedule is as follows: 1.00% fee on assets managed. The Firm does not assess performance-based fees.

It is impossible to invest directly in an index. The performance of an index does not reflect any transaction costs, management fees, or taxes. The indices used for comparison are as follows: The Standard and Poor's 500 Total Return Index is an unmanaged index with no expenses, which covers 500 industrial, utility, transportation, and financial companies in the U.S. markets. It is a capitalization-weighted index calculated on a total return basis with dividends reinvested.

The composite dispersion represents a measurement of the consistency of the composite's performance results with respect to the returns of the individual accounts within the composite over an annual period. The annual dispersion is measured by the asset-weighted standard deviation of the composite and is calculated using net of fees returns. Only portfolios that have been managed for the full period are included in the composite dispersion calculation. In accordance with the GIPS standards, dispersion data is not provided for years in which the composite is comprised of five or fewer accounts and of periods of less than one year.

Valuations and returns are computed and stated in U.S. Dollars. The Firm does not use leverage or derivatives to implement the intended strategies.

Beginning in June 2002, accounts that experience cash flows in excess of 10% of the account's market value are temporarily removed from the composite. These accounts are added back to the composite when they are considered fully invested. The minimum account value for inclusion in the composite is \$100,000. Additional information regarding the treatment of significant cash flows is available upon request.

The 3-year annualized Ex-Post Standard Deviation is calculated using 36 consecutive monthly net of fees returns to the end calculation period. Suncoast Equity Management adheres to the GIPS valuation hierarchy principles.

Past performance does not guarantee future results. Investment returns and principal value will fluctuate. Investments may be worth more or less than their original cost when sold. It should not be assumed that investment decisions we make in the future will be profitable. Current performance may be lower or higher than the performance data shown. Returns include the reinvestment of all income.

Suncoast Equity Management claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. GIPS® is a registered trademark of CFA Institute. CFA Institute does not endorse or promote this organization, nor does it warrant the accuracy or quality of the content contained herein. Suncoast Equity Management has been independently verified for the periods 12/31/97 – 12/31/24. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards. Verification provides assurance on whether the firm's policies and procedures related to composite and pooled fund maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis.

The Select Growth composite has had a performance examination for the periods 12/31/97 – 12/31/24. The verification and performance examination reports are available upon request.

For any additional information, please contact the Chief Compliance Officer at (813) 963-0502.