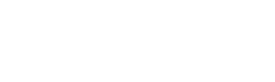


THIRD QUARTER OF 2025

October 22, 2025

Ed Zhang





Before commenting on the market, please note that we will be hosting our annual dinner for our clients and friends at the Briar Club in Houston on Thursday, January 29th. We will have time for the

Change

2.0%

1.5%

1.0%

0.5%

Consider the chip layer:

capital to purchase Nvidia's chips.

roughly 10% of the company.

debt-fueled player breaks the stable oligopoly.

benefit the economy for decades to come.

worst was past us.

non-residential demand has been solid.

expected to grow ~170%+ this year to \$24B.

Sincerely,

Ed Zhang

any trading strategy.

Dear Clients and Friends,

speech with Dan Clifton of Strategas Research Partners returning as our speaker. Dan is an expert on politics and its impact on the financial markets and spoke at our dinner back in 2023. You should receive a formal invitation in mid-December. We hope you can make the event, and we will be live streaming it for those who cannot attend. **Market Update** Despite the highest tariffs to US consumers since 1933 and a 22% correction in the S&P 500 earlier

usual fellowship and our outlook for the markets. We will also return to our format of a keynote

this year, we enter Q4 with equities near all-time highs and monetary policy easing. On Sept 17, the

Fed cut short-term interest rates to 4.00%-4.25%, citing progress on inflation and softer labor. This

supports growth without declaring victory. Headline consumer price index (CPI) is up 2.9% yearover-year; helpful but not a green light. Markets are pricing two more 25 basis point cuts by year-end to 3.50%-3.75%, which is contingent on cooling of core service and wage inflation. If inflation stalls, the Fed can pause which sets up a measured, not rapid cutting cycle. FRED Personal Consumption Expenditures Excluding Food and Energy (Chain-Type Price Index) 2.5 2.0



slight drop in housing rental prices also helped. Core PCE sits in the high-2s, with stickiness in services, not tariff-exposed goods. Relief in energy commodity prices also helped, even as electricity and natural gas prices rose. On a net basis: the major swing factors preventing regular Americans from feeling noticeable tariff pain were deflation across goods and import/shipping.

That said, low-income consumers are strained, while high-income consumers remain resilient. As

short-term interest rates drift down and real incomes stabilize, 2026 could see a modest recovery in

overall consumer spending. We prefer owning businesses with a higher-income customer base,

cheaper traded input helped, with import prices flat-to-down through mid-2025. Post-COVID,

goods prices normalized as prices of used cars and durables rolled over and shipping got cheaper. A

durable pricing power, and clear value propositions over broad rate-sensitive cyclicals. Regarding confidence across the economy, we are watching for whether inflation re-accelerates (energy, tariffs) and the pace and for loosening of mortgage/credit. On the corporate side, boardrooms are leaning into mergers & acquisitions. Valuations have reaccelerated even with mixed deal volumes as we see larger and strategic deals. This is due to funding costs easing and companies pursuing scale. Regulatory timing can stretch closings, but momentum is positive where synergies are real. We expect continued M&A across Al-adjacent tech, infrastructure, and select industrials with the middle-market improving as rate volatility fades.

revenue, disciplined capital allocation, and improving efficiency. Are we in a bubble? Contribution to real GDP growth US real GDP growth contribution from tech capex Percent, 2Q rolling average Percent 2.5% 3.5% Contribution from tech capex

> consumption expenditures

Information processing

equipment & software

value chain, from the chipmakers up to the cloud providers.

3.0%

2.5%

1.5%

1.0%

0.5%

Contribution from rest of economy

durability. We continue to favor businesses with pricing power, high gross margins, recurring

0.0% 1Q23 2Q23 3Q23 4Q23 1Q24 2Q24 3Q24 4Q24 1Q25 2Q25 2022 2023 2024 2025 Source: Bridgewater, August 2025 Source: REA Bloombern JPMAM Q2 2025 Capex defined as Capital Expenditure Corporate investment in Artificial Intelligence has been the primary driver of the market, with capital

What's notable is that these aren't straightforward transactions. They represent a form of vendor and circular financing, where capital and equity are exchanged in a closed loop. Skeptics point to this as being eerily reminiscent of Cisco's vendor financing during the dot-com bubble, where Cisco would fund its own customers' purchases. This is the first clear sign that the market is entering a new, more speculative phase.

Until recently, the Al infrastructure boom could be characterized as a disciplined, although

expensive, race funded almost entirely by the massive free cash flows of a few hyperscalers:

capacity, linked to the ambitious "Stargate" data center project. To fulfill a contract of this magnitude -requiring an estimated 4.5 GW of power, Oracle has no choice but to tap the debt markets.

This is the inflection point. As Doug O'Laughlin from Fabricated Knowledge notes, the entrance of a

"What we have lacked in this cycle so far is almost no debt-led funding. The Oracle RPO shows what's possible if you're willing to flex your balance sheet, and this will kick off an uneasy race... What had been a disciplined, cash-flow-funded race may now turn into a debt-fueled arms race." This shift into leverage and circular financing models feels like a classic late-cycle marker. It echoes

Given these classic bubble markers—parabolic capex, a shift to debt and circular financing, and narrative-driven valuations—our approach remains cautious and selective. • Our Preference: We favor platforms with fortress balance sheets and repeatable free cash flow (namely hyperscalers like MSFT, AMZN, GOOGL, META) that can fund their AI ambitions internally and pace spending as monetization clarifies. Their diversified profit pools (cloud, ads,

In short, while we see signs of a capital expenditure bubble, we believe this momentum-backed phase can persist. We will continue to participate selectively, focusing on companies where the moats and cash flows are real, while actively avoiding potential balance-sheet accidents. Ferguson Plc (NYSE: FERG)

cap semiconductor conglomerate, Broadcom sells primarily design and critical components for leading-edge chips as well as data-center infrastructure software. We believe the real fight in AI is between Nvidia and Broadcom. With a fresh inflection underway, Broadcom is positioned to be the #2—if not #1—winner over the next decade. Led by arguably one of the greatest CEOs of all-time in Hock Tan, Broadcom excels at gamechanging M&A and has consistently executed for shareholders producing one of the most successful stocks in the past 2 decades. It competes with NVIDIA in AI and networking chips, while its sticky,

non-cyclical software (92% gross margin) buffers cyclicality in semiconductors. Whereas NVIDIA

delivers general-purpose "glove-fits-all" compute stacks, Broadcom dominates custom Al chips

(ASICs) with Google as its anchor customer, designing application-specific computing chips for

Google's many applications (Search, YouTube, Cloud). Meta and OpenAl have also signed multi-

billion-dollar deals to make their own chips. Custom-Al revenue rose 225% in 2024 to \$8.6B and is

Broadcom (NASDAQ: AVGO)

We added Broadcom to Equity Income in April; it has been our best year-to-date performer. A mega-

across Broadcom's non-Al businesses. Broadcom sits in a duopoly behind NVIDIA across the AI stack—owning the Ethernet scale-out, custom AI chips for the biggest buyers, a high-margin software cash engine, and iPhone connectivity. 2026 should be another step-up year in Al and networking, with subscriptions fueling steady free cash flow. As always, we are grateful for your continued trust and partnership, and we are always happy to answer any questions you may have so please feel free to email, call, or come into the office to see us.

and unaudited. These returns reflect the reinvestment of any dividends and interest and include returns on any uninvested cash. In addition to management fees, the managed accounts will also bear its share of expenses and fees charged by underlying investments. The fees deducted herein represent the highest fee incurred by any managed account during the relevant period. Past performance is no guarantee of future results. Certain market and economic events having a positive impact on performance may not repeat themselves. The actual performance results experienced by an investor may vary significantly from the results shown or contemplated for a number of reasons,

References to indices or benchmarks are for informational and general comparative purposes only.

There are significant differences between such indices and the investment program of the managed

accounts. The managed accounts do not necessarily invest in all or any significant portion of the

securities, industries or strategies represented by such indices and performance calculation may not

be entirely comparable. Indices are unmanaged and have no fees or expenses. An investment cannot

be made directly in an index and such index may reinvest dividends and income. References to

indices do not suggest that the managed accounts will, or is likely to achieve returns, volatility or

other results similar to such indices. Accordingly, comparing results shown to those of an index or

including, without limitation, changes in economic and market conditions.

performance of any entity or transaction may differ materially from those reflected or contemplated in such forward-looking statements. The information contained herein is believed to be reliable but no representation, warranty or undertaking, expressed or implied, is given to the accuracy or completeness of such information by Brasada. Second Quarter

> April 7, 2025 by Jonathan Reichek, CFA February Read More Read

of 2025

Timir

Regarding earnings and valuation, profits must carry returns. With the S&P 500 near all-time highs and forward 12-mo price-to-earnings 22-22.5x (above 5- and 10-yr averages), expansion of stock valuation multiples is limited. The next leg up depends on continued profit growth and free cash flow

expenditure extending beyond GPUs to the entire infrastructure stack: power, networking, real estate, and software. However, the nature of this investment is undergoing a profound shift, and to understand it, we must look at the company at the center of it all: OpenAl. To understand OpenAl's current position, the best historical analogy is not a recent mobile platform like iOS, but rather Microsoft Windows in the PC era. Just as Microsoft leveraged DOS, and the

applications built for it to become the default operating system for the enterprise and then

consumers, OpenAI has leveraged ChatGPT to aggregate hundreds of millions of users. This massive

user base is the ultimate source of power, allowing OpenAI to exert gravitational pull on the entire AI

This leverage is now being used to orchestrate the buildout of the AI ecosystem on OpenAI's terms.

Nvidia: After receiving a \$100 billion investment from Nvidia, OpenAI is deploying much of that

- AMD: To create a second source and reduce reliance on a single supplier, a playbook move

straight from IBM's handling of Intel in the 1980s, OpenAI struck a deal to purchase 6 gigawatts

worth of AMD's chips. In return, AMD granted OpenAI warrants for up to 160 million shares, or

Microsoft, Google, Amazon, and Meta. That has fundamentally changed, and OpenAl is again the catalyst. To secure the staggering amount of computing power it needs, OpenAI has entered into massive, long-term contracts that its partners cannot fully fund from their own cash flow. The most prominent example is the reported ~\$300 billion deal over five years with Oracle for compute

the telecom bubble, where strategic equity spending gave way to massive debt issuance to fund fiber buildouts, leading to overcapacity and spectacular bankruptcies. Today, the profits in the Al industry are flowing primarily to the suppliers, Nvidia, data centers, and power companies, while the "true AI companies" face uncertain revenues and intense competition, another concerning sign. This dynamic fits perfectly within the framework described by Byrne Hobart in his book Boom, which

argues that capitalism occasionally disregards normal return-on-capital constraints to single-

mindedly fund a new technology. Debt, as O'Laughlin states, is the "real accelerant". This FOMO-

driven parallel investment can be incredibly productive, solving many interlocking problems at once.

The critical question for investors, however, is what durable infrastructure will remain if/when the

bubble eventually bursts? The telecom boom left behind swathes of dark fiber that power our

internet today. An Al bubble spent on GPUs with a three-year useful life offers a far less durable

foundation. A bubble that spurred a massive buildout in power generation, on the other hand, would

software) and control over distribution provide a cushion. We also favor the essential "picks and shovels" suppliers who own critical bottlenecks in the tech stack and get paid on the buildout, thus avoiding the downstream utilization risk. • Our Concern: The real risk lies with new entrants and those in the middle of the stack who lack diversified businesses, rely on speculative financing, and are entirely dependent on the hope that Al adoption and monetization will arrive before the funding dries up.

Ferguson is the largest scaled specialty distributor for North American plumbing/HVAC/waterworks. Its revenue is split ~51% residential, 49% non-residential; ~60% repair & replace (R&R) and 40% new housing builds. About 85% of revenue is finished goods; plumbing is ~50% of mix. ~95% of revenue is U.S., the rest Canada. Their customer base comprises of 22% waterworks, 17% residential trade plumbing, 14% residential build/remodel, 14% commercial/mechanical, 14% fire/fabrication/facility/industrial, 12% HVAC, 7% residential digital.

When we began due diligence for Equity Income early in the year, sentiment was washed out: FERG

shares traded down 16% post-earnings on fears of commodity deflation and weak outlook. Yet

revenue held despite housing weakness. The market priced in zero new-home construction growth

plus low-single-digit commodity price deflation. In our opinion, the stock selloff was overdone: (1)

housing demand had been weak for over 2 years, (2) commodity products are only 25% of FERG's

mix, (3) specialty distributors had consistently shown pricing resilience. With residential (40% of

revenue) in the 5th-6th inning of weakness and non-residential (waterworks/civil/infra) strong, the

The overhang was uncertainty on timing: new-home recovery might lag while non-residential could

slow first. FERG's share price implied only low-single-digit earnings growth over the next two years,

but our math suggested an easy path to beating expectations. So far, pricing power has held, and

Consistent with our playbook, we expect continued compounding organically and via accretive M&A.

Management has consistently added 2 pts of growth from small bolt-on acquisitions at attractive

valuations, with immediate profit uplift when plugged into Ferguson's procurement, tech, and

logistics rails. Scale drives a structural edge-better sourcing, working-capital efficiency, tech-and pricing has proven sticky through deflation scares. Diversification has helped Ferguson outperform smaller, concentrated peers while housing construction remains stalled. Multi-year tailwinds persist in waterworks, commercial, civil infrastructure, and industrial; data-center buildouts also help pull through demand for commercial plumbing/HVAC/pipes/valves/fittings.

In networking, what allows these chips to talk to one another and work in conjunction and an adjacent and hypergrowth category in AI compute, Broadcom leads with Ethernet-the standard technology across non-Al clouds/enterprise data centers—pressuring proprietary approaches; NVIDIA in response even announced its own Ethernet solution. Its data-center software (VMware) is the 800-lb gorilla in server virtualization, helping manage

computing costs (including AI). This high-margin segment should grow teens this year as customers

shift from licenses to subscriptions, then at least mid-single digits. Broadcom also holds a near-

We bought our position after a >30% pullback in share prices on tariff fears that implied a 30% EPS

cut over 2–3 years. We saw as severely oversold given (1) Broadcom's lower China-tariff exposure, (2)

Google's rapid Al-chip progress driving demand for more chips from Broadcom and interest from

other hyperscalers, (3) continued share gains/innovation in networking, and (4) upcoming recovery

monopoly in iPhone connectivity (chips for cellular/Bluetooth/Wi-Fi/GPS).

Share in X Request An Intro This quarterly update is being furnished by Brasada Capital Management, LP ("Brasada") on a confidential basis and is intended solely for the use of the person to whom it is provided. It may not

be modified, reproduced or redistributed in whole or in part without the prior written consent of

Brasada. This document does not constitute an offer, solicitation or recommendation to sell or an

offer to buy any securities, investment products or investment advisory services or to participate in

The net performance results are stated net of all management fees and expenses and are estimated

benchmark are subject to inherent limitations and may be of limited use. Certain information contained herein constitutes forward looking statements and projections that are based on the current beliefs and assumptions of Brasada and on information currently available that Brasada believes to be reasonable. However, such statements necessarily involve risks, uncertainties and assumptions, and prospective investors may not put undue reliance on any of these statements. Due to various risks and uncertainties, actual events or results or the actual

Latest Insights UPDATE BRASADA **Understanding Tariffs** Second Quarter of 2025 First Quarter of 2025 July 1, 2025 by David Sharestani, CFA

OR CALL US TO SCHEDULE: (713) 630 8390

Our Services Insights

Your Trusted Private Investment Partner

Regulatory Disclosure | Privacy Policy

in **D**

Copyright @ 2025

Read More On Our Latest Update

Financial Planning **Retirement Planning**

Investment Research Economy, Policy & Macro **Investor Presentations** Contact (713) 630 8390 | 1

nfo@brasadacapital.com 3200 Southwest Fwy, Suite 2160 Houston, TX 77027

QUARTERLY

Request An Intro



Quarterly Commentary Investment Advisory Portfolio Management News

Meet Our Team Who We Serve The Brasada Difference

April 9, 2025 by Guy Davis, CFA

Read More

UPDATE

Read More

About Us

A Lifelong Partnership Begins Today Schedule your complimentary strategy session with our experienced financial advisors to explore tailored wealth and investment strategies that align with your financial goals. Our team is ready to assist you in making informed decisions to optimize your future today.