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CAPITAL

Flower City Capital

Quarterly Investor Report

Summer 2026

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Investment Update

Summer 2026

Dear Members of Flower City Capital,

Global stocks delivered their strongest quarterly return since 2020, gaining 11.9% through June 30.[1] While index-level performance was strong, significant volatility persisted beneath the surface.

It's difficult to discuss the impact of AI on markets without sounding overly dramatic. Simply put, AI has fueled one of the largest investment booms in history. *Chart 1* shows technology's share of U.S. investment reaching a new high, surpassing the peak seen during the dot-com era. *Chart 2* highlights AI investment's growing contribution to U.S. GDP growth. AI-related companies are driving earnings growth and account for much of the stock market appreciation this year (*Chart 3*).

Nowhere is this trend more evident than semiconductors. Data centers require vast quantities of advanced chips, giving manufacturers substantial pricing power and driving profit growth. Hyperscalers (the large tech companies building AI infrastructure) are investing heavily in anticipation of attractive long-term returns and increased cash flow in the years ahead (*Chart 4*). The result was an 88.0% gain in chip stocks[2] in the second quarter (*Chart 5*).

Chart 1

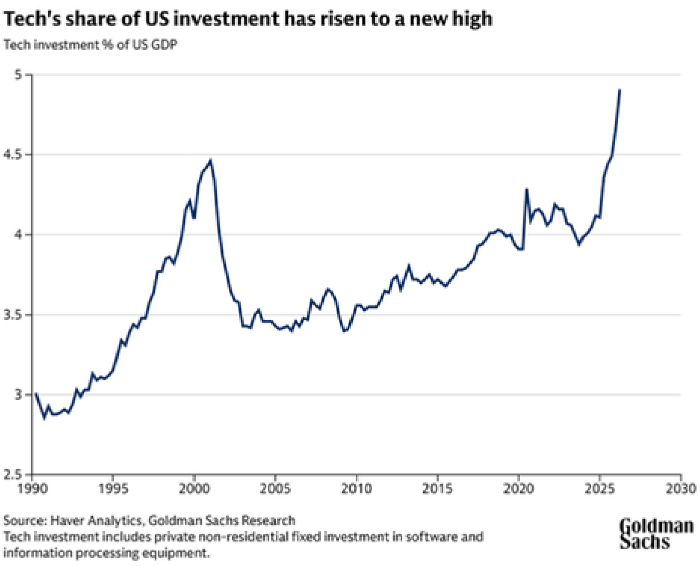
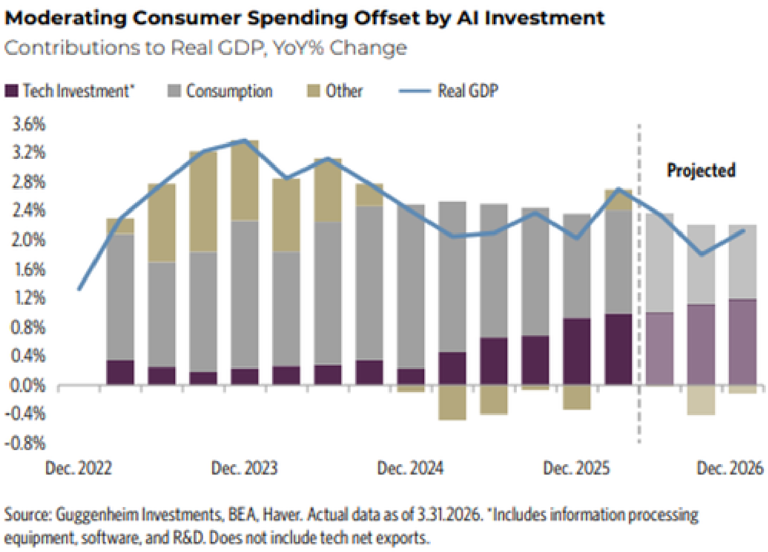


Chart 2



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[1] *Vanguard Total World Stock Index Fund ETF (VT)*
[2] *Philadelphia Semiconductor Sector Index (SOX)*

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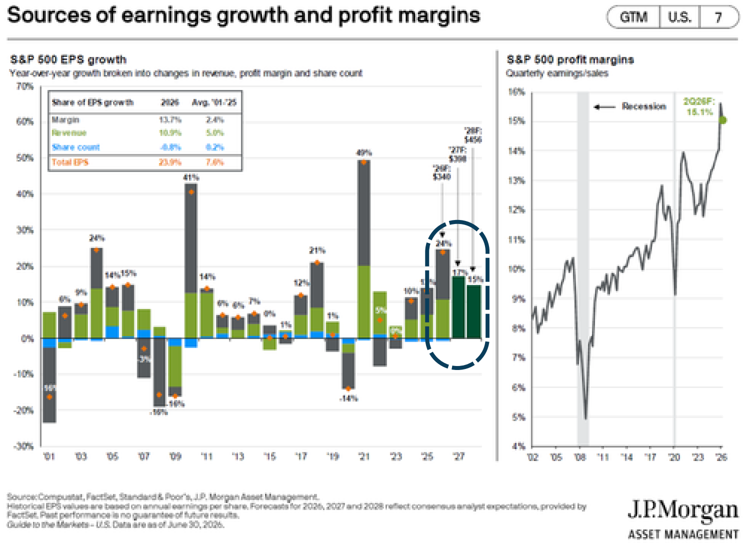
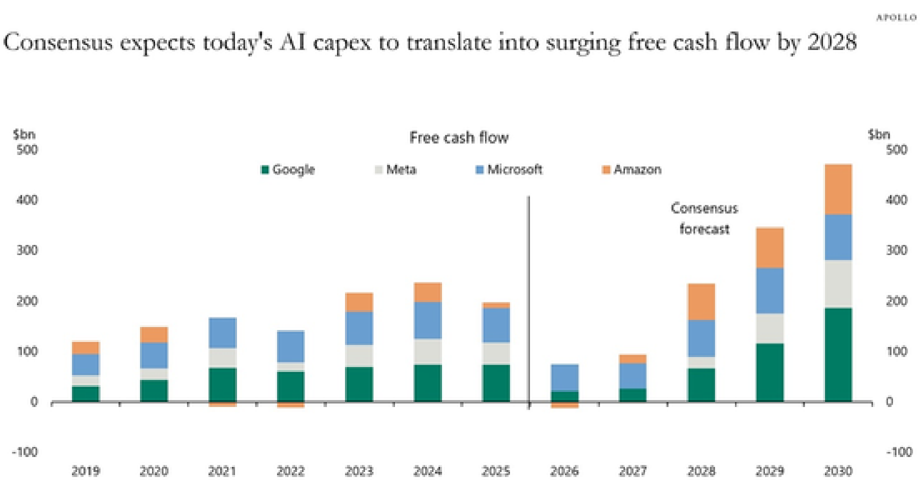
Chart 3



AI spending is driving earnings growth and profit margins in turn

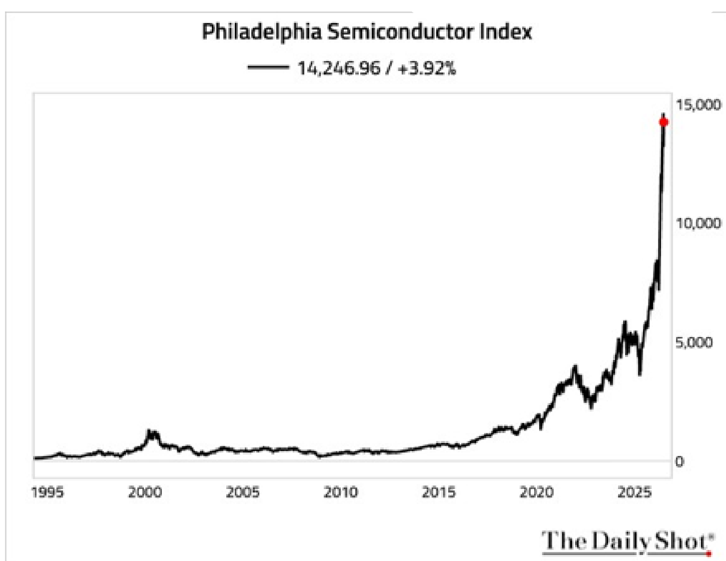
Chart 4



Hyperscalers are forecasting a deferred return on their investment

Chart 5

Chip makers surged in Q2 as a result of AI spending



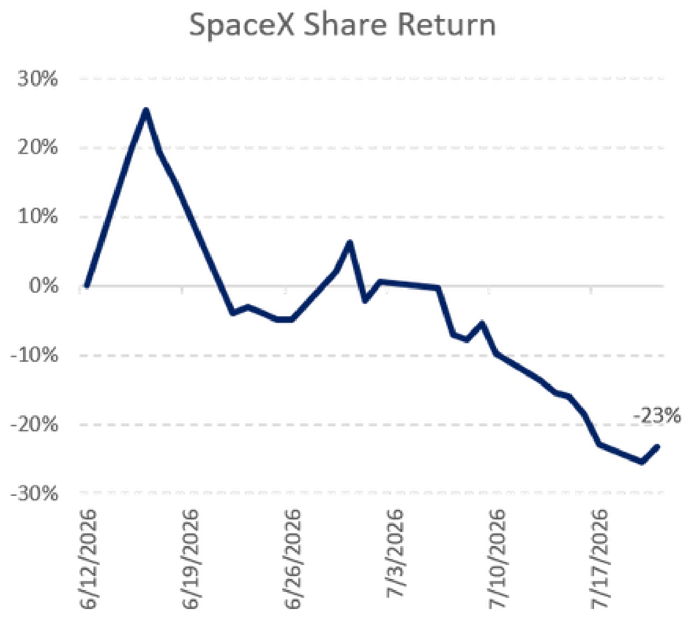
The Market is on Bubble Watch

If the significant investments being made into data centers and semiconductors fail to generate their forecasted returns, it would be reasonable to expect both economic growth and equity markets to cool. The challenge lies in assessing the durability of the AI investment cycle. Most leading AI labs are privately held, and public companies generally do not separately disclose AI-related revenues and profits from other parts of their business. This leaves investors to piece together an incomplete picture from limited data and anecdotal evidence. While comparisons to the late 1990s have become increasingly common, attempting to call a market top or position portfolios around a correction is often a fool's errand.

Beyond the extraordinary gains in semiconductor stocks, speculative activity has increased across several areas of the market. Margin balances continue to rise (borrowing money to invest in more stocks) and the issuance of leveraged ETFs has accelerated to record levels. Another notable sign of investor enthusiasm was the occurrence of the two largest IPOs in history during the quarter (SpaceX and SK Hynix). Market booms often attract sellers eager to capitalize on favorable conditions. Notably, both companies were trading below their IPO prices at the time of writing this letter *(Chart 6)*.

Spacex shares are down 23% since IPO, another sign of investor enthusiasm

Chart 6



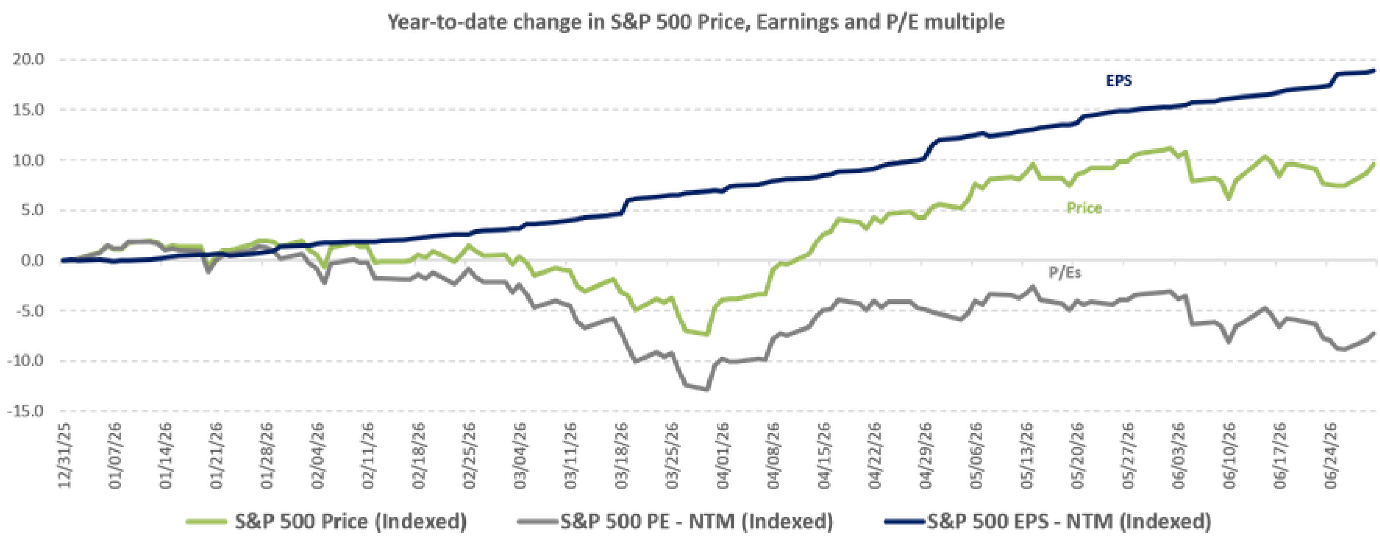
On the Other Hand...

There are compelling arguments against the existence of a bubble. This year's market gains have been driven largely by earnings growth rather than expanding valuation multiples. In that respect, the market has actually become less expensive. The same is true for many of the hyperscalers, whose share prices have been relatively flat while their bonds have weakened. *Chart 7* reflects this dynamic, showing the growth in Earnings Per Share (EPS) alongside decline in Price-to-Earnings ratios (P/E).

We're already seeing evidence that investors do not expect today's exceptional growth to persist indefinitely. Semiconductor stocks, for example, have pulled back since quarter-end. While demand for AI infrastructure remains strong, many parts of the ecosystem resemble the characteristics of a commodity business, with ever more supply coming online. Models often rely on similar underlying data, computing power, and architectures, rendering competitive advantages difficult to sustain as innovations are quickly replicated by competitors. The market appears to be recognizing the realities of a more normalized future and discounting prices accordingly.

S&P 500 earnings has grown YTD while price multiples have declined

Chart 7



FactSet, June 30, 2026

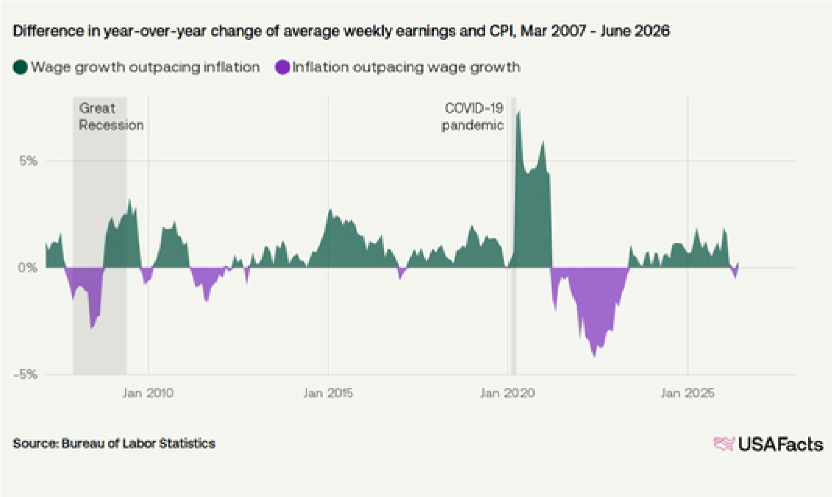
What are the Results?

Unprecedented investment in AI infrastructure, elevated government spending, and resilient consumer demand have helped sustain economic growth but have also contributed to inflationary pressures.

Since 2020, both wage growth and inflation have averaged approximately 4% annually. As shown in *Chart 8*, inflation significantly outpaced wage growth for much of the 2021-2023 period putting pressure on household budgets. When prices rise faster than incomes, even a strong labor market can leave families feeling stretched.

Headline inflation measures provide a broad view of price increases, but many essential household expenses have risen even faster, such as housing and health insurance. As a result, real living standards have improved little despite years of nominal wage growth. This disconnect helps explain why consumer sentiment has remained subdued even as equity markets trade near record highs.

Chart 8



Inflation and wages have been in a give and take pattern post pandemic

In conclusion, our strategy is unchanged in this environment: own the broad market and avoid unforced errors. We will continue to be patient as we selectively add diversifiers and less correlated assets to portfolios over time. As always, we are available any time to review your portfolio and ensure it remains aligned with your long-term goals.