



I have news! And much to say! "I got a lot of problems with you people! And now you're gonna hear about it!"

Actually, I have no problem with you, personally, but I do have a serious problem with the market, because it's likely to have a serious impact on you, me, and - most importantly - our clients. As a prelude, **earnings drive performance, and current earnings are historically misleading**. It's obvious, because it's simple arithmetic. While I love literary fiction, I don't love financial fiction.

First, the news:

- Our ETF (which I'm not allowed to name in this type of communication) has grown 25% in AUM in just 2 months.
- The ETF Which Shall Not Be Named is expected to grow in AUM, based upon feedback, to a far greater degree in the months ahead.
- That ETF has grown roughly **20,000%** in a little over 3 years - from 2 to over 400mm.
- T.J. Gardner has joined Running Oak as our Chief Revenue Officer. He's more fun, provides a different perspective, and has over 15 years of experience serving RIAs in asset management, technology, and model portfolio construction. I highly recommend reaching out.

Why are we growing so quickly? The largest, most sophisticated RIAs that we have spoken to have pretty much all stated that Running Oak's Efficient Growth strategy is precisely what they are looking for right now.

“Okay, Lindsay, are you forgetting that I was a professional twice over — an analyst and a therapist?”

— TOBIAS, ARRESTED DEVELOPMENT

While Efficient Growth is intended to be a strategic, long-term investment, it has maybe never been more timely, tactically. At a time when many are concerned we're in a bubble (or simply an overly euphoric, unsustainable environment entirely divorced from reality) AND just about every equity investor owns a historically high percentage of the exact same tiny number of highly correlated stocks, the largest, most sophisticated of firms (that we have spoken to) have stated that Efficient Growth is the solution they're looking for to that which worries them most.

Everyone knows what happens if everyone is all-in on the exact same tiny number of stocks and cash or risk becomes a priority. And if everyone decides to sell a historic amount of the same tiny number of stocks at the same time, who's there to buy them? The two questions we have heard

most over the last few months are “How much is the appropriate allocation?” and “Where in our portfolio do we use it?”.

Performance Update

- Running Oak’s Efficient Growth portfolio was up 2.25%, net of fees, QTD (from July 1 through September 17th - when this was written) versus -0.25% and -2.26% for the S&P 500 Equal Weight and Russell Mid Cap Indexes.*

“It is a rock, though. Should beat everything.” — MICHAEL

*“There’s not a lot of logic to it. It’s kind of like on a boat with
‘Women and children first.’ I mean, why should they...”* — GOB

Fundamentally, why now? And by now, I mean literally right now, like this second.

The “AI When It Pays” Trade Roadmap

- The 10 best performing stocks in the Nasdaq over the 14 months prior to July 2026 were up over 2x (2x!) the 10 highest flyers in the Nasdaq at the very peak of the Tech Bubble.
- Those companies (predominantly chip stocks) were driven by the AI earnings/scarcity narrative. High Volatility, Unprofitability, Low Quality, and Meme stocks were the best performing categories over that 14-month period.
- Running Oak’s Efficient Growth invests in Profitability, High Quality, Growth and Low Volatility, and therefore lagged considerably.
- The AI earnings narrative is one giant illusion. (Analysis to follow.)
- Since June 2026, Efficient Growth and Sandisk, the poster child of the chip run, had a correlation of -43%. Over the prior 14 months, that correlation was low. Efficient Growth has been treated as though it’s anti AI.*

By the Transitive Property, if the AI Trade equals the Grand Illusion, and Efficient Growth is the opposite of the AI Trade, then Efficient Growth is the opposite of the Grand Illusion, and – therefore - Efficient Growth is based in reality, not illusion.

“I deceived you, mom. ‘Tricked’ makes it sound like we have a playful relationship.

— MICHAEL

The Grand Illusion

Earnings, expected earnings in particular, drive returns. Per Terri Campbell, CFA, “There is a very high long-run correlation between earnings and stock prices: the R^2 between S&P Composite earnings and price from 1871 through 2024 is 0.95, using Robert Shiller's 150-year dataset.”* Current earnings have arguably never been more misleading and unsustainable.

“It’s the only hair he’s got. He’s an alpaca.” — LUCILLE

“He has alopecia.” — MICHAEL

Definitions matter.

THE BASICS

$$\textit{Earnings} = \textit{Revenue} - \textit{Expenses}$$

“Relentless rules of humble arithmetic.”

— JOHN BOGLE

Revenue – Current revenue is WILDLY inflated.

1. **AI capex** represents roughly 5% of US GDP. That is a VERY large number for an economically unproven/unprofitable (albeit incredibly promising) technology.

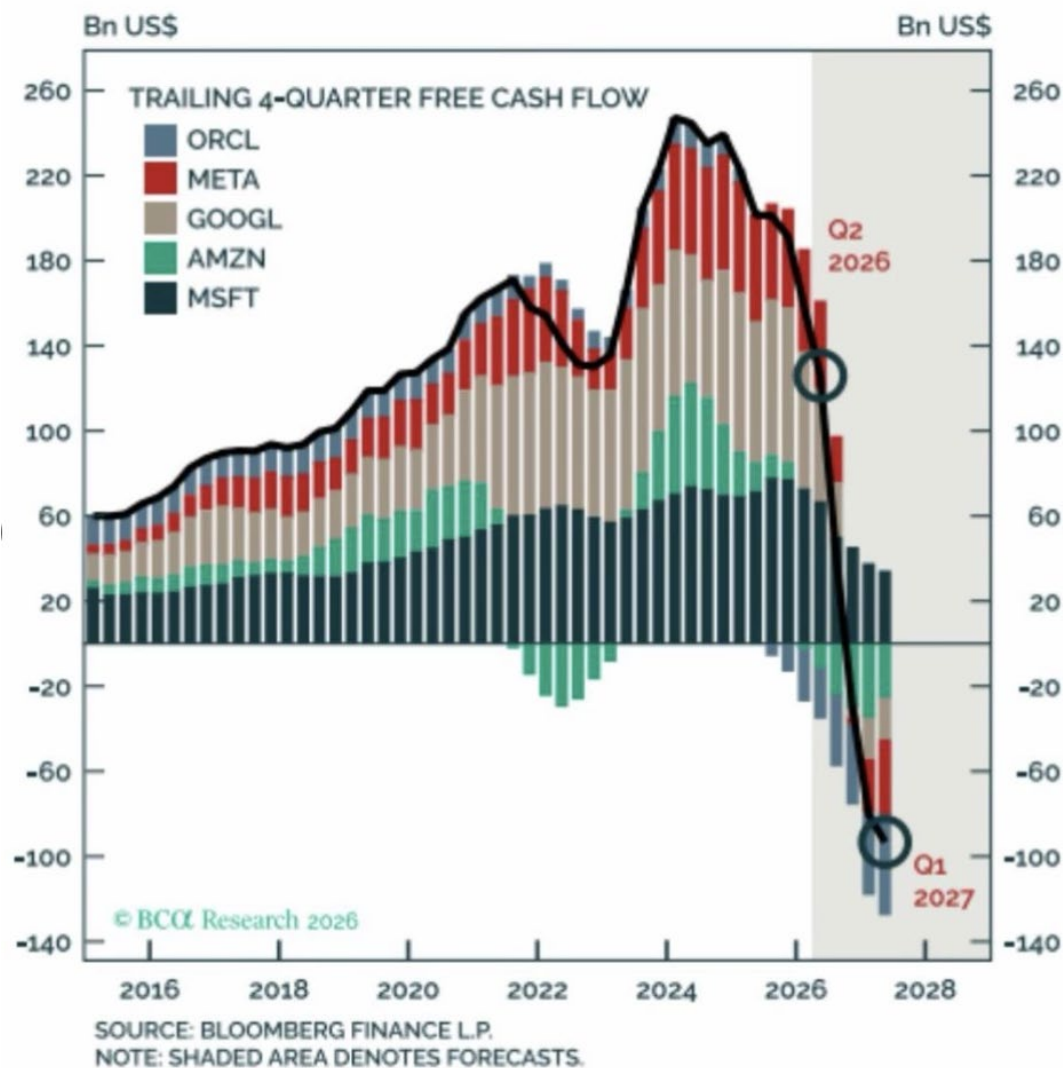
- That number is a result of hyperscalers spending piles of cash like nothing seen in history. Those piles are gone.
- That number is a result of hyperscalers spending cash flow from operations like nothing seen in history. That cash flow is being spent... entirely.

- That number is a result of hyperscalers flooding debt markets. Data center financing now represents 18% of the investment grade bond market, **more than all bank-related debt**. For bonds over 15 years in duration, data center related bonds now represent **42%** of the investment grade market. That is nuts.

“Unlimited juice? This party is going to be off the hook!”

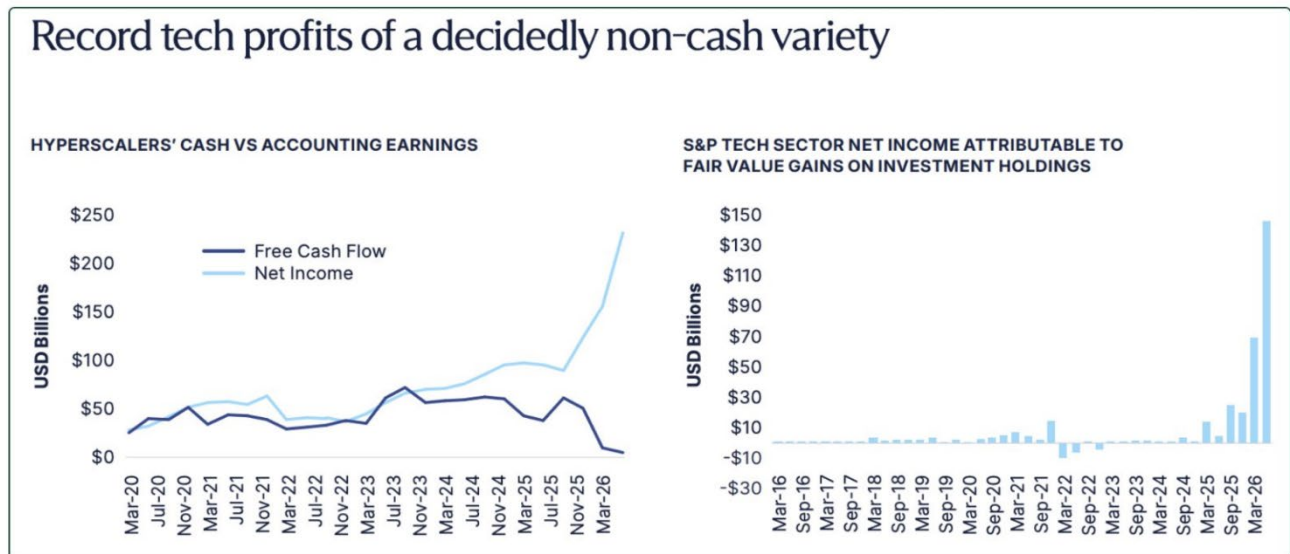
— BUSTER

None of the above can be repeated. The juice ain't unlimited. The cash is gone. The cash flow is spoken for; they can't go from 0 to 100% again. Markets can handle only so much debt before choking. (Notice rates rising.)



Per The Carlyle Group

Record tech profits of a decidedly non-cash variety



2. Circular Financing – "Ah, yes. The "Bob Loblaw Law Blog". You, sir, are a mouthful." - Tobias

Companies are handing other companies cash, so that the recipients of said cash will turn around and buy the products of those handing out the cash with the same cash they handed out. That's a mouthful, because it's convoluted and weird. That isn't how normal business works..., though such arrangements were common in 2000..., many of which were illegal...

Regardless of ethics and legality, this practice results in revenue.

3. Paper Profits – "Do you think I could have a hit of that juice box?" - Buster

Per GAAP accounting standards, changes in the value of investments must be reported. The value of a small number of historically massive, unprofitable, illiquid, private companies has risen dramatically - *presumably*. That rise in value is reported as gains, counting as profits. (For now, let's overlook the fact that the companies granting these giant private companies sweetheart deals, driving the values higher, are the ones realizing the paper gains.) Roughly **70%** of Alphabet's and Amazon's most recently reported earnings were simply paper profits, not actual business-related profits.



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An important observation from Goldman which points out that half The S&P's "record" earnings growth is just "Big Tech" marking up its own stock portfolio.

Here it is, verbatim, from the desk of Goldman's Ioannis Blekos: "S&P 500 EPS growth is tracking at 26% year/year excluding the 'other income' from mega-cap tech's appreciating equity investments. Including those gains, the headline growth rate is 45%."

i.e the "record" earnings season you have been told about - the one holding up the most expensive equity market in history - is running at 45% only if you count the gains that Nvidia, and its brethren, book when the stock portfolios they sit on go up.

Strip out the mark-to-market of Big Tech valuing its own venture bets, and the number nearly halves, to 26%.

Source: GS, zerohedge



Source: FactSet, Goldman Sachs Global Investment Research

4. **Tariff Refunds** - Whether counted as revenue or not, 10s of billions of dollars in tariff refunds are also driving earnings higher.

Conclusion: Numerous unsustainable and highly questionable dynamics are artificially making current revenue far higher than the actual sale of products and services.

Expenses – Current expenses are a fraction of the actual costs of generating related revenue.

5% of GDP is currently related to AI Capex. Capex is considered investment, meaning that cost can be depreciated.

“It’s vodka. It goes bad once it’s opened.”

– LUCILLE

The hyperscalers have extended depreciation cycles from 3 years to 5.

(First, consider whether that passes the sniff test. The world is changing faster than any time in history. Technology is evolving especially fast. Nvidia went from a chip cycle of 2 years to under a year. Yet... hyperscaler accounting assumes technology is changing more slowly, becoming obsolete more slowly. That’s odd. Could this be related to an ability to report far lower depreciation expense in an investment boom, significantly boosting reported earnings? Hmmmm... Incentives speak far more loudly than words.)

Given the same amount invested, the new 5-year depreciation cycle results in 20% depreciation expense. The long-time 3-year cycle results in depreciation expense of 33.3%, **almost 70% higher!** (Note: The depreciation cycles of the hyperscalers differ from company to company. 5 years is a rough average. Some are 4. Some are 6.)

“I hear the jury’s still out on science.”

– GOB

Wrapping it up: the current reported earnings growth that many on social media laud so loudly isn’t real. It’s an illusion. Wildly inflated revenue minus historically little depreciation expense naturally results in an earnings number that is preposterous. THAT is why valuations appear to be declining; some get it, and they aren’t shouting from the social media mountaintops. They are quietly positioning for the future, based on numbers and reality.

AI, while all but guaranteed to be transformational, simply doesn't currently make sense financially. Masayoshi Son, the CEO of SoftBank, gets it (though his intended message is somehow the opposite).

"We don't actually know how any of these companies will ever make money on AI, but that's not the point – it's AI. It's the future."

Per the Financial Times, SoftBank CEO Son "groused that any talk of an AI bubble is absurd, adding that he's willing to **waste** trillions of dollars a year for decades if that's what it takes to make AI a financial success." "Every year \$5 trillion, or 800 trillion yen, you might think that's a lie, but I am confident that's what it will cost."

"Don't actually know" and "waste trillions of dollars" are the exact words of a man who knows far more than most.

Why "waste" or invest in something we "don't actually know"? Efficient Growth is the "AI-When-It-Pays" trade. Invest in companies that make money today AND tomorrow.

I highly recommend listening to Meb Faber's recent interview of Paul Kedrosky. That is one of the very best AI-related interviews I have heard.

Tactically, why now?

"Mom always told us to curl up in a ball and remain motionless when confronted."

— BUSTER

Reallocating client assets based upon reality and simple arithmetic is a far better way to protect clients than curling up in a little ball and pretending.

1. AI earnings are an illusion. Depreciation expense, actual costs, are being kicked down the road, building an earnings wall, brick by brick. Owning a historically large amount of the exact same tiny number of companies worked out when those companies were generating historic cash flow and sitting on massive piles of cash. Now, they have no cash, negative cash flow, and are swimming in ever-rising debt. Status quo is a dangerous bet in a clearly changing world.

2. Which side of common sense do you want to be on?

"I'm trying to decide which gang to align myself with."

— GEORGE SR.

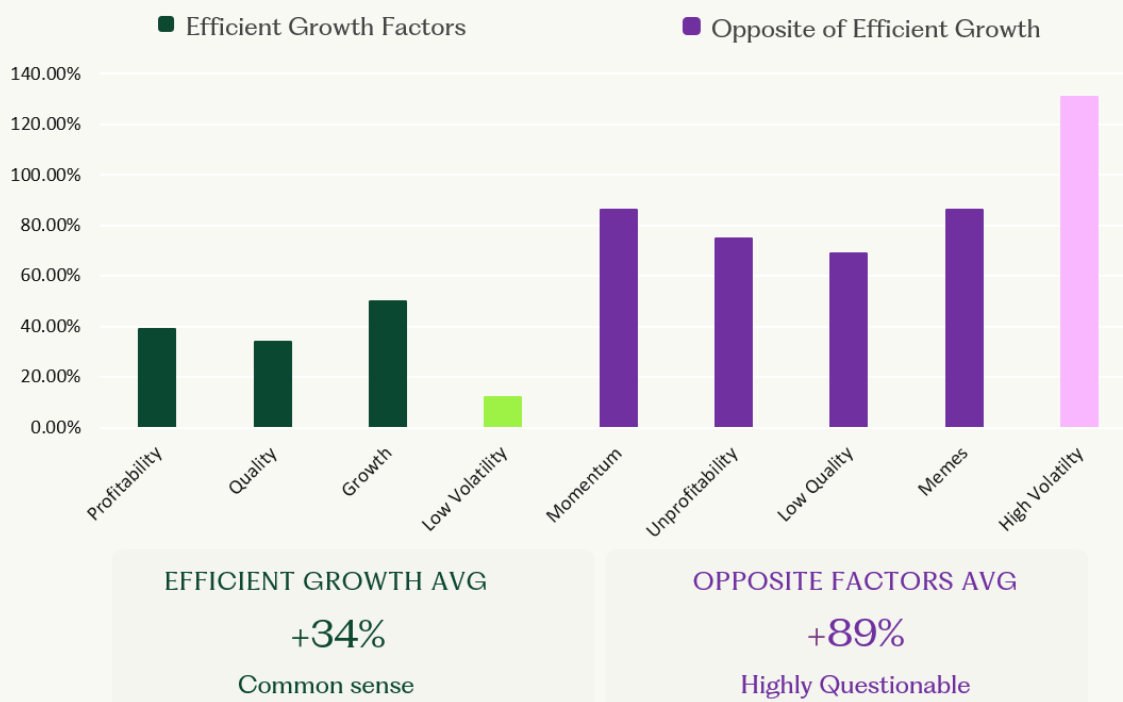
From May 2025 through June 2026, Profitability, High Quality, and Low Volatility lagged Unprofitability, Low Quality, High Volatility and Meme stocks to a historic degree. To put that more simply, companies that *lose* money absolutely crushed companies that *make* money to an extent only seen once in history - 1999. Efficient Growth, which invests in fast growing, profitable, high quality companies at attractive valuations (all of the qualities that make the most sense but performed the worst) lagged.

But...

if that performance dynamic was driven by the Grand Illusion,
and that which can't last forever doesn't last forever,
a reversion of that anomalous 14-month period is an excellent bet,
making Efficient Growth - in my opinion - an excellent bet.

When the Volatile Unprofitable Won

14-Month Returns — Common Sense Vs. The Highly Questionable



The Common Sense vs. Nonsensical bars represent the average of the four factors driving Efficient Growth versus the five factors that are the opposite (Momentum added to the Opposite Factors group). "When Nonsense Wins" chart: Source: Bloomberg. Nonsense refers to Running Oak's opinion of factors that do not represent desirable characteristics for long-term investors. Factor returns are as of June 30, 2026.

Mean reversion of the above – not even profitable companies outperforming unprofitable companies or High Quality companies outperforming meme stocks – would entail Common Sense

outperforming highly volatile, unprofitable, low quality, message board stocks by 60%. I am not saying that will happen, only that is what mean reversion would dictate.

While we're on this topic...

3. Mean reversion

"Reversion to the mean is the iron rule of the financial markets." - John Bogle

"The most important of these rules is the first one: the eternal law of reversion to the mean (RTM) in the financial markets." - John Bogle

"Remember reversion to the mean. What's hot today isn't likely to be hot tomorrow." - John Bogle

Historically, profit margins were the most mean reverting of financial metrics. Profit margins have defied mean reversion for decades for sound reasons.

1. Globalization led to higher profit margins as companies were able to utilize lower costs of labor.
2. Asset-light software companies were able to generate revenue with negligible variable costs.

Now? Globalization has been reversing for years, as growing nationalism outweighs capitalism. And AI is asset-really-freaking-heavy. Just look at the AI capex boom.

Meanwhile, despite the reversal of the two major factors that drove higher profit margins, profit margins are at highs. In fact, they're **40% higher** than the recent asset-light period from 2010 to 2024. Were profit margins to simply mean revert to the asset-light average, that would result in a 27% decline in profits, given the same level of revenue.

Profit Margin Contradiction

S&P 500 Profit Margin



Today

- Asset-heavy
- Deglobalization
- Profit Margin: 12.3%

2010 -2024 Asset-light

- Ave. Profit Margin: 9%

1990-2010 Globalization

- Ave. Profit Margin: 5.5%

**A potential 50% decline in profit margins assumes a return to a similar asset-heavy environment as was experienced in the 1990-2010 economy. There are a wide range of possible outcomes that could ultimately come to fruition depending on the level of onshoring activity (supply chains, physical capacity, etc.) that results from deglobalization. This reflects the opinion of Running Oak Capital and should not be relied upon as a statement of fact.*

"I care deeply for nature." — LINDSAY

"You're wearing ostrich-skin boots." — MICHAEL

"Well, I don't care about ostriches." — LINDSAY

Again, AI earnings, according to simple arithmetic, are an illusion. Revenue is both imaginary and unsustainable. Expenses are historically low and piling, building a wall that future earnings will inevitably hit. And just about every investor owns a historic amount of the exact same tiny number of companies that used to have historic piles of cash, used to have historic positive cash flow, now have neither, and are flooding debt markets.

It seems to be an ideal time to (at the very least) make a tweak and hedge bets. To quote Buster, clients **"do allow some nervous crying, but you can tell they don't like it."**



Aram Mughalyan  • 2nd

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Everyone is calling this an AI boom.

Yet 70% of Microsoft's entire AI revenue comes from one company.

Microsoft booked \$24.1B from OpenAI last fiscal year. Behind that sits \$261B of capex since 2022.

But here is the vulnerable part. Microsoft does not have a frontier model of its own.

Copilot still runs on GPT-5.4. Mustafa Suleyman, who runs Microsoft AI, says their own frontier model is 12 to 18 months away.

Even open source Chinese AI models are wayyy ahead of that.

Microsoft built the most expensive infrastructure on earth to rent out a model it does not own. Oops...

And it is not alone in the game.

Anthropic pays SpaceX \$1.25B a month for Musk's Colossus clusters in Memphis. That is \$15B a year, locked in through May 2029.

It signed another \$10B with Volta, a data center firm founded in January, for capacity on Bitdeer's Norway campus, backstopped by \$1.3B of JPMorgan letters of credit.

Everyone in that chain books revenue. Almost all of it starts at OpenAI and Anthropic.

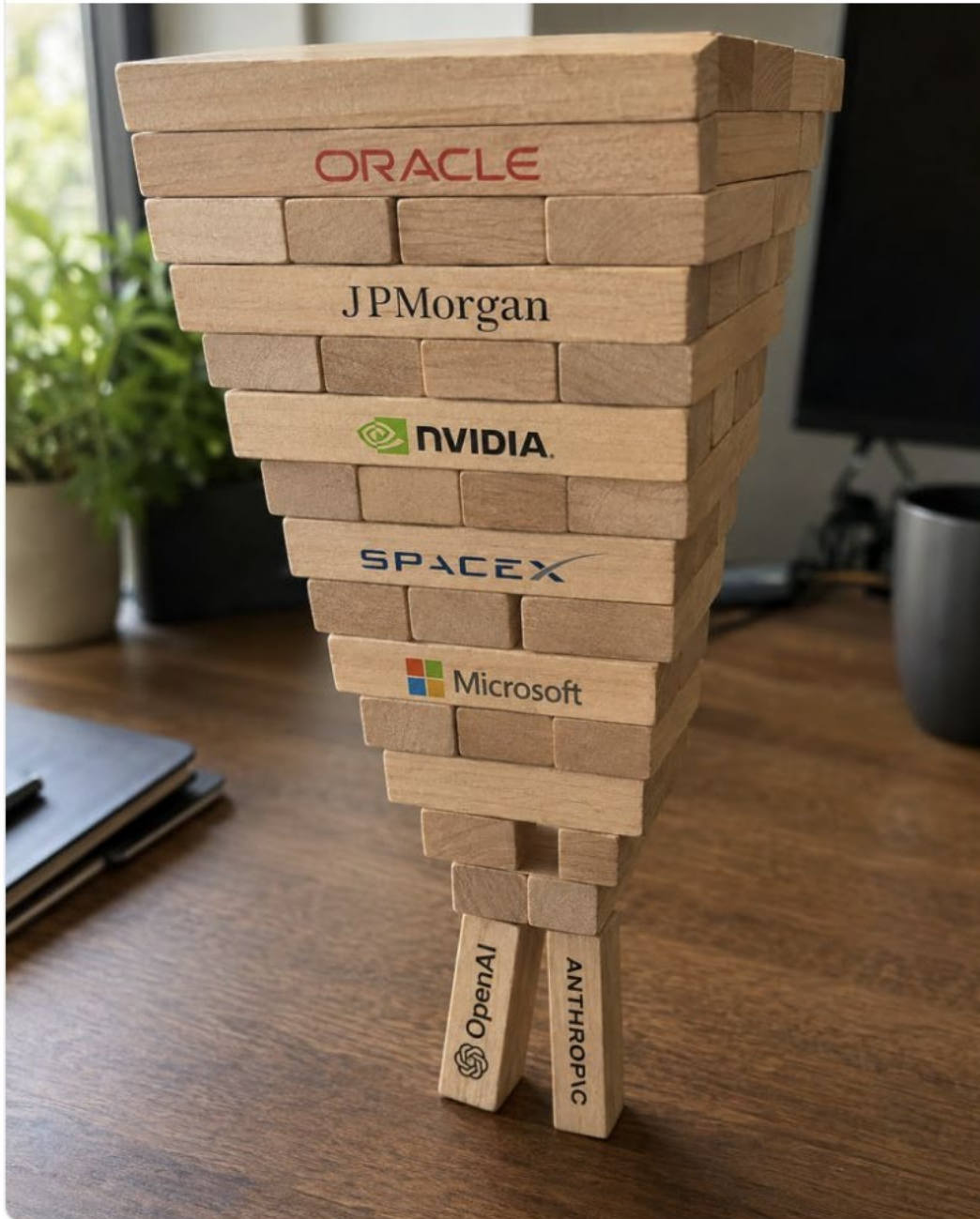
Many are calling this an AI bubble.

But a bubble is too many buyers paying too much. To me, this is too few buyers holding too much power.

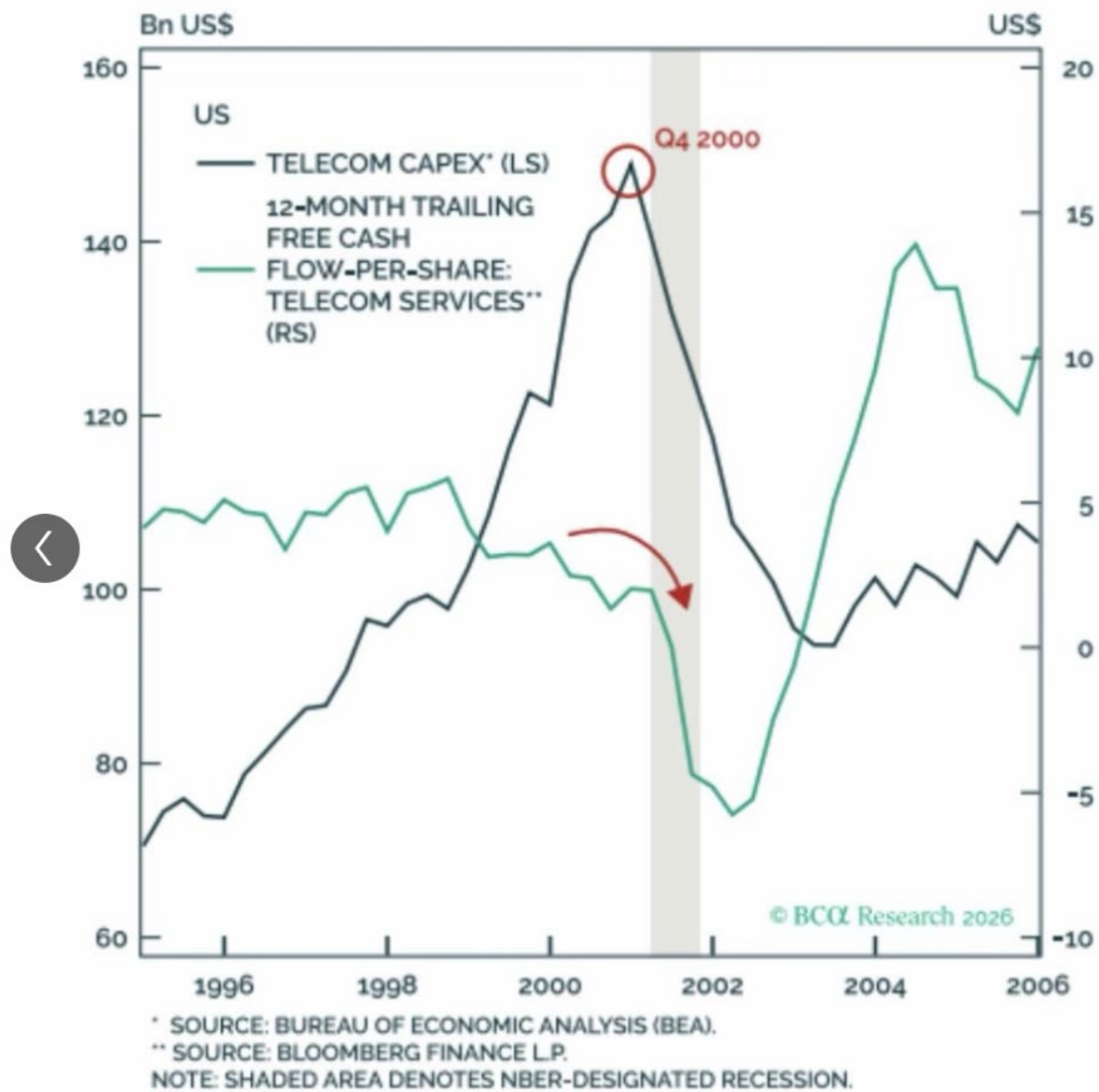
The risk is not that the demand is fake.

The risk is that it is unpredictable and it belongs to just 2 companies.

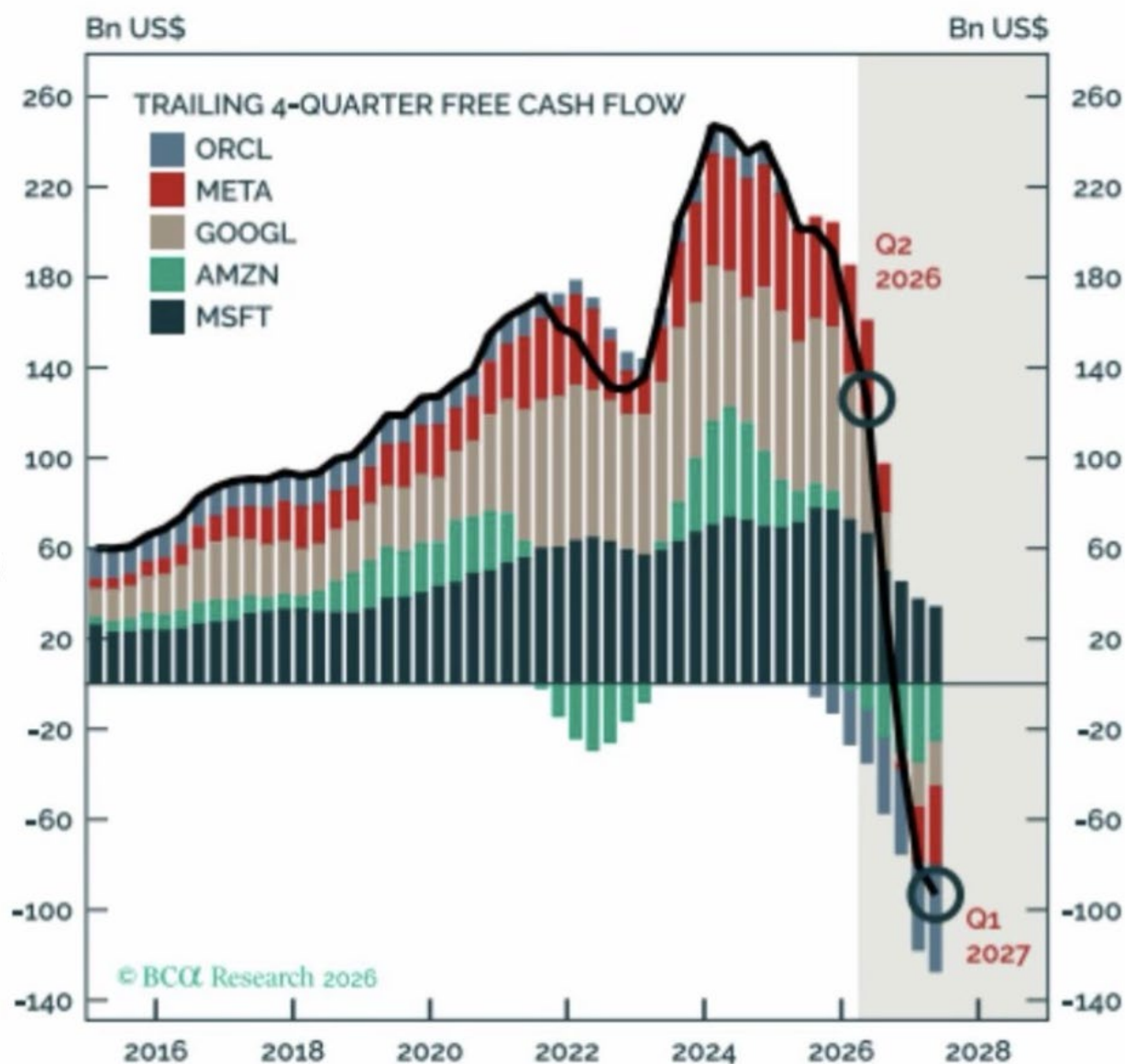
Now imagine what happens to that chain if growth at OpenAI and Anthropic simply flattens?



That was then.



This is now.



SOURCE: BLOOMBERG FINANCE L.P.
NOTE: SHADED AREA DENOTES FORECASTS.

Quick hitters:

Consistently Not Stupid - [Running Oak in 3 Words](#)

Invest Where Others Aren't (MARGE - Upper Mid/Lower Large Cap)

- Investing where everyone else is investing means higher prices, higher valuations, lower implied returns, higher implied downside.
- Investing where others aren't means lower prices, lower valuations, higher implied returns, lower implied downside and a margin of error.
- Investing where others aren't also provides valuable diversification.
- If the market goes up, others are likely to follow, propelling prices.
- If the market goes down, others can't sell what they don't own, meaning less selling and downside pressure.

It's win/win.

Running Oak's goal is to maximize the exponential growth of clients' portfolios, while subjecting them to far less risk of loss. In other words, we aim to help your clients realize their dreams and avoid their nightmares.

If you appreciate critical thinking, math, common sense, and occasional sarcasm, we would love to speak with you. Please feel free to set up a time here: [Schedule a call.](#)

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All indices are unmanaged and may not be invested into directly. The S&P 500 Total Return Index is a market capitalization-weighted index of 500 widely held stocks often used as a proxy for the stock market. The S&P 500 Equal Weight Index is the equal-weight version of the widely-used S&P 500. The index includes the same constituents as the capitalization weighted S&P 500, but each company in the S&P 500 Equal Weight Index is allocated a fixed weight, or 0.2%, of the index total at each quarterly rebalance. The Russell Midcap Index is a market capitalization-weighted index that measures the performance of the mid-cap segment of the U.S. equity market. It is a subset of the Russell 1000 Index, comprised of the 800 smallest companies in the Russell 1000, representing approximately 25-30% of the Russell 1000's total market capitalization.

Standardized performance for the Running Oak Efficient Growth Composite as of 8/31/2026 (gross/net): 1 year: 4.77% /4.42%; 5 years (annualized): 6.69% /6.16%; 10 years (annualized): 11.30% / 10.75%

Statements from advisors used as anecdotes within this letter were made by current clients of Running Oak Capital. No compensation was provided in exchange for these statements, and the clients identified have no known conflicts of interest with respect to their statements. Client experiences are not representative of the experience of all clients, and these statements are not indicative of future performance or services.

"When Nonsense Wins" chart: Source: Bloomberg. Nonsense refers to Running Oak's opinion of factors that do not represent desirable characteristics for long-term investors.

**Terri Campbell, CFA, "What Earnings Explain, and What They Don't: Insights from 150 Years of Market Data," CFA Institute Enterprising Investor blog, January 8, 2026.*

Historical Mid Cap stock prices relative to Large Caps - Source: Yardeni Research: [LargeCaps vs SMidCaps - Yardeni Research](#). Statement regarding Mid Cap stocks outperforming Large is reflective of historical performance of the Russel Midcap Index vs Russell 1000 Index.

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