



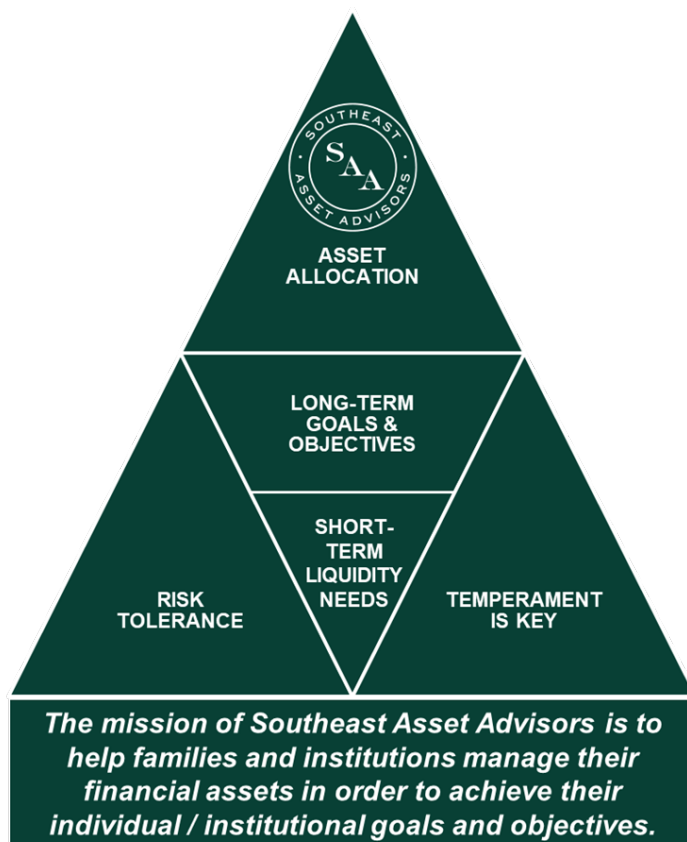
Member of
The Lanigan Group of Companies

Southeast Asset Advisors, LLC

Investment Management & Consulting
Thomasville – Atlanta – Tallahassee – Mobile – Charleston
www.assetadvisor.com

The Margin of Safety Quarterly ⁽¹⁾

October 2025



**SOUTHEAST
ASSET
ADVISORS**

WE STRIVE TO PROTECT AND GROW
OUR CLIENTS' CAPITAL OVER THE
LONG TERM BY:

- 1) Focusing on individual client goals and objectives.
- 2) Having the proper asset allocation to reflect each client's tolerance for volatility (i.e., temperament).
- 3) Stress testing short-term liquidity needs.
- 4) Investing with a value orientation and utilizing managers who understand the intrinsic value of a business and margin of safety along with passive strategies as appropriate.
- 5) Rebalancing portfolio holdings/managers when appropriate to take advantage of underpriced and to avoid overpriced assets based on the client's profile of asset allocation ranges.

⁽¹⁾ Margin of Safety (MOS): Many investing greats have said these are the most important three words in investing. We agree and call our quarterly letter accordingly. MOS is key in determining anything with variables occurring in the future, i.e., price to future value, all future outcomes, etc. Its magic is that the higher your MOS, the smaller your edge needs to be to have a favorable outcome.



TO: Clients and Friends
FROM: SAA Managing Directors
RE: 3rd Quarter 2025 Commentary
DATE: October 2025

The market melt up continues, led by the Mag 7 and fueled by AI and expectations of even lower interest rates.

What started as a volatile year in the first half of 2025 has become a steady march towards record highs in equities. On September 23, the S&P reached a new high, driven by gains in AI-related stocks as well as market expectations for future interest rate cuts. For the third quarter, the S&P 500 returned ~8% and ~14.8% YTD. International equities (as measured by the MSCI EAFE) returned ~4.8% in the third quarter and ~25.7% YTD. This international performance is helped by a ~10% decline in the value of the US dollar.

The Bloomberg Aggregate Bond index (duration ~5.9 years) returned ~2.0% for the quarter, and short-term bills (1-3 months) returned ~1%. We continue to keep fixed income in short to intermediate duration for the most part, as we worry about the deficit and inflation over the long term.

Valuation Musing

By almost any metric, valuation of the entire S&P 500 appears elevated as compared to history. Over 58% of the two-year 2023-2024 total return was due to the performance of just seven stocks (Mag 7). For the most part, these are fabulous companies that have grown to ~34% of the total value of the 500-stock index and are valued at ~33x P/E vs a high ~22x P/E on the other 493 non-Mag 7 companies. Beyond the elevated concentration and valuation quantitative metrics, investors' behavior gives the best understanding of irrationality sweeping through the markets. We are observing growing speculation and momentum driven investing outside our client base. Given this environment, we believe it is prudent to be more conservative and diversified, especially where you have no tax implications, and hold a greater allocation of short to intermediate T-Bills in less aggressive portfolios.





It is different this time.

These words are often repeated and are usually very expensive words when used!

Charlie Munger often said he was reluctant to give an opinion unless he knew the other side's argument better than they do.

So here goes..... the other side..... The Mag 7, unlike companies in the late 1990's, for the most part are producing huge cash flows and have great balance sheets. Many are AI-related. AI benefits to society are likely to be gigantic. Recently, an AI guru called this an "industrial bubble" as opposed to a financial bubble like in 2008. He further explained that society benefits from most of those past inventions as will be the case for AI. Another tech pioneer was quoted recently, "When people get excited as they are today about AI for example, every experiment gets funded, every company gets funded. Investors have a hard time in the middle of this excitement distinguishing between good ideas and bad ideas. That is probably what is happening today. That does not mean that anything that is happening is not real. AI is real, it is going to change every industry." We agree.

However, we are concerned about the huge leverage it will take if many of the data centers, etc. announced are built and funded. FOMO (fear of missing out) seems alive and well, not only with individuals but with companies that feel they must make AI investments (data centers, etc.) or fear they will miss out.

Questions? (See Appendix A)

We recently presented to an institutional client a list of questions that we think are important today. The first relates to AI, while the second concerns consumers. Both of these questions are important, but we think the answers are presently unknowable with any certainty. We will continue to look for clarity in answering these questions

As related to the AI question, we are in the "anxious" category. Semiconductors, chips and wafers (and rare minerals used to produce) are largely secular, as demand





is virtually assured for the distant future; nevertheless, the leaders in the semiconductor industry will eventually find a replacement or alternative, as that is capitalism at work. As one of our favorite managers says, “Semiconductors are both cyclical and secular.” We appear to be in a “melt up” phase in almost everything, as most AI-related industry leaders are producing earnings which are valued at an elevated multiple. We see some extreme valuations on companies with no profits. As example, startup Open AI has ~\$13 billion of revenue but no profits, at least for the near term, and appears irrationally priced. Another worrying sign is that we see some circular investments being made (invest in our company, then we will buy products from yours). This too, reminds us of the dotcom era.

The second question relates to the bifurcated consumer. The high-end consumer (~10% of the population) is health/wellness minded, and their increased spending is currently fueled by the wealth effect of stock market increases and increased values of their real estate. The top 10% of consumers account for ~50% of all consumer spending, while the lower-end consumers are bargain hunting (private label buydown, etc.) or just not spending. Many of the once stable but low-growth consumer products companies are trying to determine if this is a short-term issue or a long-term generational change in consumer behavior. We are watching this consumer behavior very closely to find an answer to these important consumer questions.

“Prediction is difficult especially about the future! Instead of trying to predict, we should prepare for increased volatility. Your temperament and being a long-term investor will always be key.”

- SAA Team

Predictions and Future

Valuations in the long term depend on a company’s long-term earnings or cash flow growth discounted at a reasonable interest rate. The future is always hard to predict, but we find predicting earnings and growth thereof is especially hard now, due to the many unknowns, not just in AI and the consumer area, but also in future tariffs (Supreme Court rulings), inflation, and deficits.





We Now Have a “Bubble of AI Fear”

Many predictors are giving their “crystal ball” predictions. As we go to press, *60 Minutes* featured Andrew Ross Sorkin’s (journalist) interview who said, “The economy is being propped up by the AI boom.” He stated that we do not know if this is a gold rush or a sugar rush, and we will not know which for a couple of years. He went on to discuss guardrails that are being changed to allow private equity/venture capital investments in IRAs and 401(k)s without the current required disclosure or other government safeguards in the past. We do think the risks for many of these investments are many times greater than in public companies. Many unaware retail investors may not fully appreciate the risks being taken and could be the losers making such investments via their IRAs.

Last week, Paul Tudor Jones said that we have the potential for further market melt-ups before a downturn in the markets. His prediction is closer to our view in the short term; however, the “when” is anyone’s guess.

Our game plan remains the same. Continue to determine the appropriate asset allocation for each client’s goals and risk tolerance.

We want short-term treasury bills to fund clients’ near-term needs. Next, we want to have enough fixed income to be a portfolio anchor in volatile times so one’s temperament can withstand any equity volatility. Lastly, we want equity holdings to be diversified and held in great businesses run by capable and honorable people. We want to buy companies at a reasonable price to value and hold for the long term with uninterrupted compounding, and we use managers that feel the same.





Thank you for your trust and confidence. We strive to make "deserved trust" the most valuable asset we can earn.

Please call us if your goals or objectives have changed.

We now have Fall weather to look forward to. Enjoy and celebrate living in the USA!

Your SAA Team

Attachment: Appendix A – Key Questions

“The only certainty is uncertainty.”

- SAA Team

“Margin of safety are the three most important words in investing. It is important in an estimate of private value and important in your asset allocation.”

- SAA Team

“In the short run, the market is a voting machine, but in the long run, it is a weighing machine (weighs free cash flow).”

- Ben Graham





If I had to give you a summary of value investing, this is what I would say. Six basic tenets. The first three are from Ben Graham. The fourth is from Buffett. The fifth is from Charlie Munger. The sixth tenet is from me.

Number one, a stock is a certificate of ownership. Number two, the market is here to serve you, not to instruct you. Number three, margin of safety provides both downside protection and better upside return. Number four, circle of competence allows you to accurately assess the odds and act accordingly. Number five, fish where the fish are and develop your competitive advantage. Number six, the modern world economy is cyclically secular, exhibiting long-term secular growth with short-term cyclicalities. So, for a global value investor wealth is the percentage ownership of global purchasing power. We build wealth by owning the most productive companies in the most productive economies and holding for the long term.

- Li Lu, Himalaya Capital



Key Questions and Answers Are Not Knowable For Sure

1. AI
 - a. Who will be AI winners?
 - i. First AI movers?
 - or**
 - ii. Everyone wins in productivity gains?
 - b. What is ROI on epic level AI/data center investment?
 - i. Will it ever pay off? If so, when can expect return? How far out and how much return?
 - c. Could new semiconductors be invented – less power usage?
 - d. Will U.S. be leader in AI race? Or China? Taiwan?
2. Consumer is very complicated/bifurcated!! Will that change?
 - a. Tale of 2 consumers – low end vs. high end
 - b. Top 10% of consumers makes up over 50% of spending – is this sustainable?
 1. What will make top consumers reduce spending – loss of wealth effect, i.e., decline in stock and/or RE prices?
3. Inflation and Interest Rates? Future rate? Different data – Fed, Treasury, and CBO? Whose is right?
4. Tariffs outcome / deficits etc?
5. Geopolitical / Mid-term elections outcome?

“In the short run, the market is a voting machine, but in the long run, it is a weighing machine”

“The only certainty is uncertainty”