



Edgemoor's Quarterly Report

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Uncertainty Breeds Volatility

The third quarter ended September 30th, 2026, saw increased volatility across both equity and bond markets due to continued uncertainties around the Iran War, skyrocketing oil prices, persistent inflation, and the upcoming U.S. midterm elections.

In a reversal of the strength of equity markets in the second quarter, markets see-sawed throughout the third quarter as investors reacted to movements in interest rates, inflation, oil prices, and the national debt. By the end of quarter, returns for stocks turned flat-to-slightly negative for the month of September, though they remained positive for the year.

Q3 Performance Review

The S&P 500 Index, the broadest measure of the U.S. equity market, posted a total return of 2.3% in the third quarter of 2026, a notable slowdown from the 15.2% total return in the second quarter. But for the nine months ended September 30th, the S&P 500 Index still notched a double-digit return of 12.7%.

The tech-heavy NASDAQ similarly delivered a total return of 2.5% in Q3 and 16.1% year-to-date, though it too saw heightened volatility.

Of the eleven sectors within the S&P 500 Index, eight have posted positive returns for the year so

far and three have been negative. Of the positive performers, two sectors - energy and information technology - beat out the index's 12.7% year-to-date return, while three others - healthcare, industrials, and materials - came in just slightly behind it, indicating a broadening of market returns. The three sectors with negative performance year-to-date were communication services, consumer discretionary, and utilities.

The Bond Market Makes Headlines

Much of the notable activity during the third quarter happened in the usually sleepy bond market, where a steep rise in yields in September sent bond prices falling. As a result, the Bloomberg Aggregate Bond Index declined -3.5% in Q3 and -2.9% for the year-to-date period.

The rise in U.S. interest rates has occurred across the yield curve, meaning short, intermediate, and long-term bonds have all seen an increase in their respective yields. However, the gap between short-term and long-term rates has narrowed significantly.

For example, the benchmark 10-year Treasury yield topped 5.3% in late September, a rate not seen since 2002, while the 30-year Treasury yield rose above 5.5%, a level last seen in 2004.

The takeaway for many investors has been that it may not be worth taking the duration risk of

longer-term bonds for only a marginally higher yield.

What's Driving Rates Higher?

The rapid rise in rates has not been limited to the U.S., with global bond yields reaching their highest levels since the mid-2000s, reflecting the mounting uncertainties around the Iran and Middle East conflicts, global trade disruptions, and persistent inflation.

Let's review some of the factors that have contributed specifically to the higher U.S. rate environment:

Geopolitics/Surging Energy Prices: Renewed tensions in the Middle East and the continuing blockade of oil shipments through the Strait of Hormuz have sent energy prices soaring. The price of U.S. Brent crude has hovered between \$90 - \$100 per barrel for most of September, sparking higher inflation expectations. Higher inflation expectations generally translate into higher long-term interest rates.

Mounting U.S. Debt: U.S. National debt hit \$40 trillion dollars in August 2026, more than double the amount just ten years ago and now 125% of U.S. GDP. This has increased the rates that investors now demand to hold U.S. Treasury obligations and driven up long-term interest rates. In addition, the surge in A.I.-related bond issuance by many of the tech giants has also driven bond yields higher.

Lack of Guidance from the Fed: The Fed has turned more opaque about forward guidance under new Chair Kevin Warsh. This has led to investors becoming less certain about the path of interest

rates, causing every data point and market headline to lead to bigger swings in sentiment and, in turn, higher overall yield expectations.

The Federal Reserve Changes Course

The Federal Open Market Committee (FOMC) raised its benchmark, short-term, Fed funds rate at its September meeting by 25 basis points (1/4 of 1%) to a target range of 3.75% to 4.0%. It was the first rate increase since 2023 and was driven mainly by stubbornly high inflation that has stayed well above the Fed's target annual rate of 2%. Despite outside pressures, the FOMC stuck to its policy priorities and voted unanimously (12-0) for the rate hike.

The impacts of higher rates are felt by all borrowers - from consumers with credit card debt or auto loans, to businesses trying to raise money to expand and grow, to the federal government, which now must pay higher interest rates on its Treasury borrowings.

Conversely, savers are now earning higher rates on their cash instruments like CDs, money market funds, and short-term Treasury bills.

Looking ahead, markets are now pricing in at least one additional rate hike this year, likely at the Fed's December meeting.

The U.S. Economy Still Showing Resilience

Despite all the economic challenges posed by higher inflation and interest rates, the U.S. economy continues to show remarkable resilience in several areas.



The first is corporate earnings growth. We have noted before that earnings are one of the primary drivers of equity market returns over the long term, because higher earnings generally translate into higher valuations for stocks. And we are currently in an earnings upcycle that appears poised to continue for some time to come.

For Q3 2026, the earnings of all the companies in the S&P 500 Index are projected to grow an average of 30%, which would be the third straight quarter of earnings growth above 25%. For 2027, the estimates are currently for 14%-15% earnings growth.

The exponential growth in earnings is largely, though not entirely, tied to the massive amounts of spending related to the artificial intelligence (A.I.) infrastructure boom. A multi-year capex cycle is underway across data centers, power generation, and chip manufacturing, with more than \$5 trillion projected to be spent through 2030.

U.S. GDP growth is another area of economic resilience. Second quarter GDP growth was revised upward to 2.2%, in line with Q1 growth of 2.1%. For the third quarter, estimates range from 2.5% to 5% growth. So, overall, the U.S. economy is still expanding at a healthy pace.

Both consumer spending and business investment continue to fuel U.S. GDP growth. Despite higher costs for everything from groceries to gasoline, U.S. consumers continue to spend at a healthy clip, with August spending surging 0.9% month-over-month (3.4% annualized), the fastest pace in over a year. While September spending dipped to 0.3% (2.8% annualized), the U.S. consumer still seems willing and able to spend.

Similarly, business investment has grown significantly, rising 8.5% in the second quarter, marking the fastest pace in over 5 years. The growth was driven heavily by A.I. spending and multi-year highs in private equity and venture capital investments.

What We are Watching Next

We are watching the labor market closely because, while remarkably steady over the last few years, it did post disappointing job growth data in September, which could impact everything from GDP growth to future Fed actions around interest rates.

The September jobs report cited just 29,000 non-farm jobs created last month, down sharply from the 95,000 expected and the 133,000 jobs created in August. The U.S. unemployment rate rose to 4.2%, though this remains an historically low rate of unemployment. The slower rate of job growth could lower the odds of a rate hike by the Fed at its October meeting, so we will be watching this closely.

Finally, we will be watching the outcome of the November mid-term elections, which could see a change in the balance of power in Congress. And while the control of Congress and the White House usually doesn't impact markets over the long term, this midterm election potentially carries more weight in the near term, particularly if it results in changes to policies related to tariffs, the war in Iran, and regulations around artificial intelligence, just to name a few.



Our Outlook

Our near-term outlook is that volatility may continue in equity and bond markets until there is more clarity around the conflicts in the Middle East, as well as the direction of oil prices, inflation, and interest rates.

Despite these uncertainties, we do expect the U.S. economy to remain on a positive growth trajectory and for corporate earnings to continue to grow for the remainder of this year and into next year.

We also expect the A.I. infrastructure boom to continue to drive growth in a variety of sectors, including information technology, healthcare, financial services, communication services, and utilities.

Portfolio Implications and Actions

We remain cautious on equity markets in the near term, given the prospects for continued volatility.

But, the overall valuation of the S&P 500 Index is approximately 20 times forward earnings, which is in line with historical averages. Looking within the index, we find that not all sectors or companies are fully valued, so we remain actively focused on finding pockets of opportunity to buy great companies at prices below our estimate of their intrinsic value.

In addition to individual equities, we continue to favor high-quality bonds and dividend-paying securities that generate current income for clients with balanced portfolios. With current yields of 5% – 6%, these securities offer an income cushion that offsets the potential volatility of equity holdings. We also find 6-to-24 month Treasury

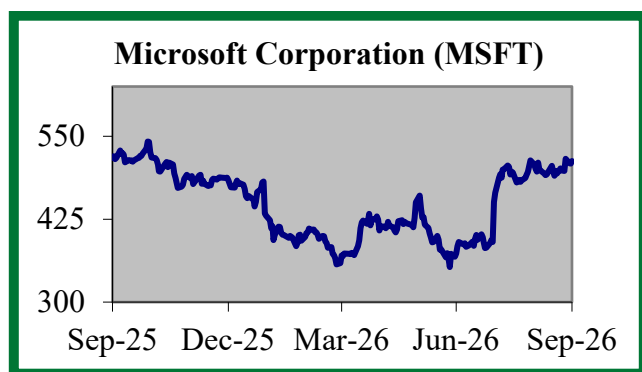
bills with annualized yields of 4.3% to 4.9% attractive for clients with excess cash. (See below for a more in-depth discussion of our Treasury bill investment strategy).

Overall, our long-term, time-tested investment philosophy remains unchanged and continues to favor high-quality companies with strong revenue and cash flow characteristics, leading market shares, wide economic moats, and solid growth prospects. We believe our active approach to individual security selection allows us to construct broadly diversified client portfolios designed to weather market turmoil and be well-positioned for long-term growth and appreciation.

Analysis of Selected Securities

The following are reviews of three selected securities we are currently buying for client accounts.

Microsoft Corporation (MSFT)



Source for price chart and financials: FactSet. Past performance is not indicative of future results. Please see disclosures on page 9.

Price (09/30/2026)	\$512.90	Forward P/E	24.8
Market Cap (\$T)	\$ 3.8	Price/Book	8.6
Dividend Yield	0.8%	Price/Sales	11.5
Return on Equity	34.0%		
5-yr. EPS growth	17.4%		

Microsoft is the world's largest independent software developer and the fourth largest company by market capitalization at \$3.8 trillion. Since CEO Satya Nadella took the helm of Microsoft in 2014, he has transformed the company from a PC-based software business into a high-value commercial and cloud application business with an integrated product offering that enables enterprise efficiency, cloud transformation, and business intelligence. Nadella's "cloud-first, mobile-first" strategy has accelerated the company's growth, profitability, and market share and led Microsoft to become a

leader in high-growth areas like cloud services, internet applications, and artificial intelligence.

As the second largest cloud services provider globally, Microsoft's Azure has benefited from A.I.-fueled demand for computing power, which has accelerated its growth and narrowed Amazon Web Services' market leadership. The Azure cloud platform has captured 20% of the estimated \$600 billion public cloud infrastructure market, generating annual run-rate revenues of over \$100 billion. The public cloud infrastructure market is projected to exceed \$1 trillion in just a couple of years, suggesting that Microsoft's cloud business will continue to have attractive growth prospects.

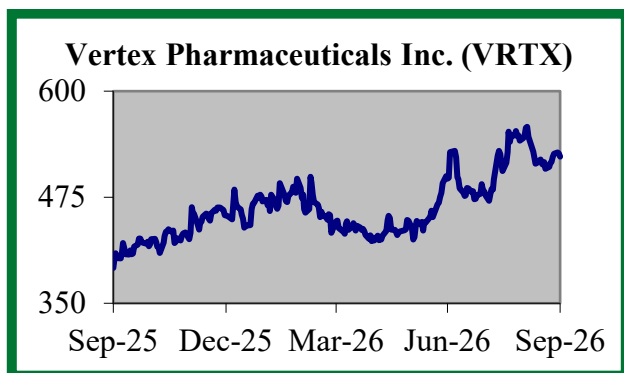
Microsoft has also adapted its A.I. strategy as the technological ecosystem and competitive landscape continues to evolve. Its redesigned Copilot platform is now being described by CEO Satya Nadella as a new "OS for work" being run, in part, on in-house developed models designed to compete with Anthropic and OpenAI, which were once strategic partners. Microsoft's deep entrenchment throughout global enterprise productivity software is an inherent advantage as the company deploys and integrates A.I. workloads across its entire productivity suite.

Microsoft's enterprise market leadership creates a network effect around its applications and operating systems and results in high switching costs for its customers, which support the firm's wide economic moat. Its huge commercial user base, strong customer relationships, and massive amounts of customer data position the company well for strong secular growth across all its business segments.

Microsoft's financial position is very strong, and management has reasserted its commitment to remaining free cash flow positive after capital expenditures, unlike many of its cloud peers. As of fiscal year-end 2026, the company generated \$67 billion of free cash flow and had \$91 billion of cash and marketable securities on its balance sheet, providing ample support for the company's A.I.-related investments.

Microsoft shares trade at a premium to the overall market at 25 times forward earnings, but we believe this premium is warranted by the company's strong earnings, cash flow-generating power, robust growth prospects, and dominant and defensible market position.

Vertex Pharmaceuticals, Inc. (VRTX)



Source for price chart and financials: FactSet. Past performance is not indicative of future results. Please see disclosures on page 9.

Price (09/30/2026)	\$ 522.81	Forward P/E	25.5
Market Cap (\$B)	\$ 132.5	Price/Book	6.5
Dividend Yield	0.0%	Price/Sales	10.5
Return on Equity	23.5%		

Vertex Pharmaceuticals is a biotechnology company focused on developing and commercializing therapies for rare diseases. Currently, the company generates the majority of

its revenues from a portfolio of cystic-fibrosis drugs that effectively treat the rare, chronic lung condition. The patents for these disease-modifying treatments run through 2039 and face limited competition due to the complexity of developing a new, more effective therapy.

Sales of Vertex's dominant cystic-fibrosis franchise generate substantial cash flows that are reinvested into the research and development of the company's expanding drug pipeline, which includes several promising new medicines that represent multi-billion dollar revenue opportunities. A prime example is Casgevy, an FDA-approved gene-editing treatment which Vertex created in conjunction with CRISPR Therapeutics that delivers a one-time cure for two blood diseases, sickle cell disease and beta thalassemia. Another promising drug is Journavx, which was approved by the FDA in January 2025 to treat moderate to severe acute pain. Vertex is currently making progress in expanding the distribution of Journavx, which is the first non-opioid pain medication approved in over twenty years.

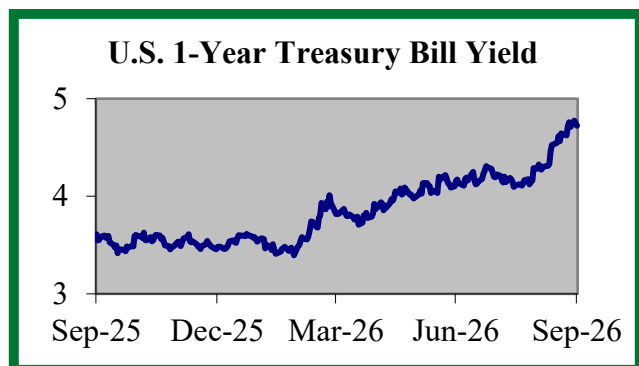
The company is also expanding its pipeline into treatments for certain types of kidney diseases, type-1 diabetes, diabetic neuropathy, and muscular dystrophy. In July 2026, Vertex announced the acquisition of Crinetics Pharmaceuticals for \$8.8 billion, which further diversifies its drug portfolio by providing promising, late-stage treatments for rare endocrine diseases.

Meanwhile, Vertex remains financially strong. The company had no long-term debt and \$13.6 billion of cash on its balance sheet as of June 30, 2026. Revenues have grown at a 14% compound

annual rate over the past five years and returns on equity are consistently above 20%.

Due to decades of research on cystic fibrosis, Vertex has built up a unique skillset around small-molecule drug design. This makes it one of the few companies capable of capitalizing on a strong pipeline of drugs in multiple therapeutic areas, a quality we think offers Vertex multiple avenues for continued success.

U.S. Treasury Bills



Source for price chart and financials: FactSet. Past performance is not indicative of future results. Please see disclosures on page 9.

1-Year T-Bill Yield
(as of 09/30/2026) 4.72%

The short-term U.S. Treasury market has been an increasingly attractive place to invest cash as interest rates have risen across the yield curve.

As a reminder, as interest rates rise, bond prices fall. Longer-duration bonds are more vulnerable to interest rate risk than shorter-term bonds, meaning their prices can fall further with every percentage increase in their corresponding yields.

Edgemoor has been buying short-term Treasury bonds as part of clients' income portfolios for several years. We currently find the 6-month to 2-year maturities the most attractive, as these bonds yield between 4.3% and 4.9%, carry minimal duration risk, and are backed by the full faith and credit of the U.S. government.

When held to maturity, these shorter-duration bonds are repaid at their full face value, so there is virtually no price risk. And if they are rolled into a new short-term Treasury upon maturity, that may be done at an even higher yield if interest rates continue to rise.

Because annual headline inflation remains sticky at 3.4%, well above the Federal Reserve's target of 2.0%, it is likely that the Fed will keep short-term rates elevated for the foreseeable future. Most recently, the Fed raised its short-term Fed Funds rate by 25 basis points (1/4 of 1%) to a target rate of 3.75% - 4.00% in September 2026. The market currently expects the Fed to make no change at its October meeting, but to raise rates by another 25-basis points at its final meeting on December 9, 2026.

We will continue to watch the yield curve and purchase bonds that we think offer the best return potential with minimal duration risk.

Sources: FactSet, Morningstar, S&P/CFRA, Schwab, ValueLine, Black Diamond Performance Reporting, Yahoo Finance, Bank of America, JP Morgan Markets, MarketWatch, WSJ and Argus reports.



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The S&P 500 index is an unmanaged market-capitalization-weighted index of 500 common stocks chosen for market size, liquidity, and industry group representation to represent U.S. equity performance. The S&P 500 index is discussed for comparative purposes only. The comparisons have limitations because the indexes have volatility, investment, and other characteristics that differ from the investment strategies of Edgemoor. Further, it is not possible to invest directly in the indexes.

The NASDAQ measures all NASDAQ domestic and international based common type stocks listed on The NASDAQ Stock Market. The NASDAQ Composite includes over 3,000 companies.

The Barclays U.S. Aggregate Bond Index is a broad base, market capitalization-weighted bond market index representing intermediate term investment grade bonds traded in the United States. The Index is frequently used as a stand-in for measuring the performance of the U.S. bond market. In addition to investment grade corporate debt, the Index tracks government debt, mortgage-backed securities (MBS) and asset-backed securities (ABS) to simulate the universe of investable bonds that meet certain criteria. In order to be included in the Index, bonds must be of investment grade or higher, have an outstanding par value of at least \$100 million and have at least one year until maturity.

The MSCI ACWI ex USA Index captures large and mid-cap representation across 22 of 23 Developed Markets (DM) countries (excluding the US) and 24 Emerging Markets (EM) countries*. With 2,308 constituents, the index covers approximately 85% of the global equity opportunity set outside the US.

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