Madison INVESTMENTS

U.S. EQUITY INVESTOR LETTER

December 31, 2025

To our investors and partners,

Once again, the stock market had an excellent year overall. And once again, returns were stronger the larger the company. After two years of calling attention to this trend, we had hoped that we wouldn't have to do it again, but here it is.

	2023	2024	2025
Russell Top 50 Mega Cap	37.8%	34.2%	19.9%
Russell Top 200	29.9%	27.4%	19.2%
Russell Midcap	17.2%	15.3%	10.6%
Russell 2000	16.9%	11.5%	12.8%

The outperformance of the largest stocks in 2025 was not as acute as in the previous two years, but was significant nevertheless. Markets tend to exhibit regression to the mean, but the timing is impossible to predict, and there is no doubt that there are fundamental, economic reasons why the stocks of some of the largest companies have performed well, meaning that the pull of gravity may exert itself much later than in past cycles.

While the largest companies get most of the press, the actuality is that market drivers for the past year or two have been more about the increasingly speculative and risk-seeking behavior of investors, rather than pure company size. The speculative mentality just happens to be more visible when it occurs among the largest stocks. We expect this speculative fervor too, will succumb to the pull of gravity over time.

Just because we can't predict the timing of any return to sanity, however, doesn't mean we should throw up our hands and invest in stocks where the long-term risk-rewards don't make sense. The music may still be playing, but that doesn't mean we have to keep dancing.

RISK, TIME, AND MANAGEMENT

In the German movie *Run, Lola, Run*, from three decades ago, the title character gets entangled in her boyfriend's criminal venture, and must come up with 100,000 Deutsche marks[1] within twenty minutes to save his life. After several failed attempts to procure the money, she ends up at the local casino. With the 100 marks that she mustered up to that point, she proceeds to the roulette wheel. She places the entire amount on one number, which has the highest winning payoff available, but with the lowest probability at 35 to 1. Miraculously, she wins (this is a movie). Still far short of the required amount, she puts her entire winnings right back on the same number for another bet, and once again, the wheel

[1]The Deutsche Mark was the currency of Germany before they adopted the euro.

accommodates and stops on her number. With more than the necessary amount in hand, she sprints out of the casino to save her boyfriend.

Now, of course, this is a movie. But the screenwriter was onto something. Which is that Lola did exactly what the rules of probability would suggest she do in that time-constrained situation. If you are playing a negative outcome game such as roulette, the most appropriate strategy is one that requires you to make the fewest number of bets to reach your targeted winnings. It's the converse of the rule that when you play against the house, the longer you play, the more likely, and the more, you will lose. Note that Lola's strategy is not actually a winning strategy, since there is no such thing when playing a negative outcome game. It's merely the best of the bad strategies, the one that maximizes the odds of getting to the desired amount in the short amount of time allotted.

Lola's betting tactic is a splendid demonstration of the relationship between risk and time. It seems to reflect the framework of too many investors today, for whom the stock market is a type of casino. Given the short time horizon and the lack of deep understanding of the how stocks should be valued, they reach the all-but-logical choice, whether consciously or not, to strive for the quickest path to riches. We're not claiming that everyone's time horizon is twenty minutes. But even twenty weeks or even twenty months, is short, in our opinion. In investing, the shorter you go, the more likely you are playing a negative outcome game.

Intelligent investing is the antithesis of a casino game. We consider it an undertaking, which with proper effort and method, can provide participants an edge over the house, given a sufficiently long time frame. This last point is crucial, as one needs the law of large numbers to have effect, to even out the inherent unpredictability in the economy, human behavior, and our infinitely complex environment. If we purchase the right securities at the right prices following a proper method, the inevitable failures will be more than offset by the successes.

For Lola, time was her enemy. At Madison Investments, time is our friend. We invest in companies that are well-managed and well-financed, and are expected to grow profits over many years, not simply the next few. These companies get better and better every year. To describe such investments, we reach back another thirty years before *Run, Lola, Run*, to the 1960s song More Today Than Yesterday. Its chorus sings, "I love you more today than yesterday / But not as much as tomorrow / I love you more today than yesterday / But darling, not as much as tomorrow."

When we look back at our investments that we like more today than yesterday, a common reason seems to be exceptional management. We've talked often about how good management is one of the pillars of our investment philosophy. But it seems that even after many decades of practice, we still underestimate its impact. This past year, some of our best-performing investments were long-time holdings where accumulated management actions continued to bear fruit. Some of our worst were those where a series of management missteps have accrued. We will keep learning, and re-learning.

One of the main difficulties is that the influence of real differences in management quality compounds over time, so can take years to truly see. Yet, the average tenure of a CEO of a large public company is about seven years. The median is five. Thus, often by the time there's enough of a record to judge a CEO by, there's not much time left for an investor to benefit. We deal with this in one of three ways. One, we try to find companies that don't just have an excellent CEO, but have an entire managerial or corporate culture that is excellent. Two, we try to find CEOs that seem to have a long runway ahead

of them – either because of their age or because of a governance structure that supports and rewards long-term behavior. And three, we try to evaluate CEOs through other means than simply their track record as CEO. What is their track record at other positions? How do they articulate their strategy? How do they seem to make decisions? How is their incentive compensation structured?

Warren Buffett famously wrote that "when a management with a reputation for brilliance tackles a business with a reputation for bad economics, it's the reputation of the business that remains intact." While we agree, our experience has been that some of our best investments have been in industries with average to moderately above-average economics, but with "A+" management. And we have had some poor experiences with industries or companies with excellent economics, but "B" or "C" management. Of course, what we're really looking for are "A" management running "A" businesses. We believe we have plenty of those in our portfolios. We like our companies today. But hopefully, not as much as we will tomorrow.

Respectfully,

Haruki Toyama

DISCLOSURES & DEFINITIONS

This letter was written by Haruki Toyama, Head of Mid and Large Cap Equities and Portfolio Manager on the respective strategies.

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