

## Portfolio Manager Commentary

### Fourth Quarter 2023

Portfolio / Index	Q4-23 Return	1-Year Return	3-Year CAGR	5-Year CAGR	Since Inception CAGR
Focused Growth Composite	+12.8%	+53.2%	+0.6%	+15.1%	+11.2%
S&P 500 Total Return Index	+11.7%	+26.3%	+10.0%	+15.7%	+11.8%

*Returns are net of fees as of 12/31/23 and annualized if period is greater than 1 year*

Dear Client,

Happy New Year! 2023 represented a year of tremendous healing for our Focused Growth portfolio returns following a terrible year for growth equities in 2022. Our Focused Growth portfolio returned 53.3% in 2023 well out-pacing the 26.3% returns of the S&P 500. Looking back over the last five years, this portfolio has delivered compound annual returns of 15%. If you had told me on January 1<sup>st</sup> 2019 that our Focused Growth portfolio would compound at 15% over the next five years, I would have happily accepted that deal and assumed we were in for a prolonged period of economic and geopolitical stability conducive to steady, compounding earnings growth. While the 15% return CAGR did in fact occur, nothing else about the past five years has been remotely normal. 2019 and 2020 were excellent years for our Focused Growth portfolio despite seemingly having no other similarities. 2019 was a year that delivered excellent returns across almost all asset classes following the growth scare of late 2018, and 2020 brought a global pandemic that left many dead and effectively shut-down the global economy. 2021 was less generous to our style of investing as the global reopening led to a rally in lower quality cyclical stocks while also triggering inflation levels not seen since the early 1980s. 2022 featured a coordinated and aggressive tightening cycle by central banks around the world in an effort to get the runaway inflation of 2021 under control. The result was a rout in growth equities not seen since the turn of the century that saw even the stocks of many of the world's best companies seemingly left for dead. 2023 was a different story. The doom and gloom consensus on the broader economy failed to materialize, many of the top technology companies aggressively adjusted their cost structures to more appropriate levels, and after over a decade of heavy investment it became apparent that the dawn of the AI revolution was finally upon us. As we look forward to 2024, we are optimistic. In this letter we will discuss the implications of a shift in macro focus from Fed Policy to the Presidential election, explain why the notion of a bubble in the "Magnificent Seven" stocks is not accurate, and illustrate through an interesting chart why we believe that the healing process in the relative performance of our Focused Growth portfolio that took place in 2023 has room to continue. Finally, we will take a look at four critical questions/controversies that we believe will be key drivers of 2024 returns for our portfolio.

**2024 Election:** In 2022 and for much of 2023, Jay Powell and the Federal Reserve dominated the broader macro discussion. The way things are looking now, the 2024 macro conversation is going to be dominated by Donald Trump and Joe Biden. One of the quirks of the asset management industry is that we are probably one of the only industry groups that welcomes this change. During election years featuring an incumbent President, the average S&P return is a very solid 12.8%. I think that there are several reasons for this, all of which are fairly intuitive. First, every fiscal policy put into place over the last several years by the incumbent administration was designed to have maximum impact for the re-election campaign. Further, despite what promises to be 11 months of pondering the end of democracy or life as we know it if the wrong person wins the election, expect very little to actually get done in Washington D.C. in 2024. Instead, every issue that has been ignored for years will suddenly become of such paramount importance that it can only be decided by an election. This means gridlock, gridlock equals stability and stability is the friend of business. Finally, the Federal Reserve tries to stay as far out of the way as possible during Presidential election years. Practically speaking for 2024, this means a bias towards implanting a few rate cuts during the Spring and Summer as a form of recession insurance and wrapping up any monetary policy actions by Labor Day. While some of you may view a Trump/Biden rematch as something more akin to “A Nightmare on Elm Street” sequel rather than cinematic masterpieces such as Godfather II or Rocky II, from a financial standpoint we are better off hanging on the words of Presidential candidates than Federal Reserve Governors.

**The Magnificent Seven:** The Magnificent Seven was a highly acclaimed Western released in 1960. The movie was so popular that it spawned three sequels, a television series and a 2016 remake. Sadly, in 2023 it became an overused phrase in the financial world to describe seven companies that have little in common besides their enormous size. Despite the massive differences in the underlying drivers for the individual companies comprising the “Magnificent Seven” they were spoken about as a single monolithic entity and came to represent a market whose positive performance in 2023 was driven almost entirely by a horde like crowding into a few select securities. As usual, the truth is a little more complicated than a thought that can be expressed in a 10 second soundbite.

Let’s take a closer look at the “Magnificent Seven. The “Magnificent Seven” consists of Apple (a consumer electronics company), Microsoft (a software company and cloud service provider), Tesla (an electric car company), Amazon (an e-commerce behemoth and cloud service provider), Alphabet (a leader in global search and owner of YouTube), Meta Platforms (a social network) and Nvidia (a GPU chip designer). These companies have two things in common: One, they are very large, high-quality, global leaders in their space. Two, their

stocks delivered incredible returns in 2023. Beyond that, their growth rates, fundamental drivers and valuations are very different. Through a series of charts, I am going to break down the returns generated by each of these stocks in 2023, the one and two year forward P/E multiples afforded each of these stocks heading into 2023, the change in the earnings outlook for each company that occurred during 2023, and the forward P/E multiple afforded each stock exiting 2023. With each chart, I'll offer a bit of context and through this process you will see why we own the four members of this group that we currently hold (Alphabet, Amazon, Meta and Nvidia) and why we reject the notion of a bubble and feel confident about the outlook for these stocks in 2024.

#### Chart 1- 2023 Returns:

	2023 Return
Amazon	81%
Alphabet	59%
Meta	194%
Nvidia	239%
Apple	49%
Microsoft	58%
Tesla	102%

This chart requires little explanation other than to set the table for the rest of this exercise and acknowledge that each of these stocks delivered incredible returns in 2023.

#### Chart 2- The 2023 Set-up

	Closing Price 12-31-22	2021 EPS	2022 EPS	2023 Consensus EPS Estimate on 12-31-22	2024 Consensus EPS Estimate on 12-31-22	2023 P/E on 12-31-22	2024 P/E on 12-31-22
Amazon	\$84.00	\$2.10	\$1.18	\$1.78	\$3.01	47.2	27.9
Alphabet	\$88.73	\$5.57	\$4.55	\$5.25	\$6.16	16.9	14.4
Meta	\$120.34	\$13.80	\$9.83	\$8.14	\$10.34	14.8	11.6
Nvidia	\$146.14	\$4.44	\$3.33	\$4.35	\$6.00	33.6	24.4
Apple	\$129.93	\$5.60	\$6.10	\$6.60	\$7.38	19.7	17.6
Microsoft	\$239.82	\$8.87	\$9.45	\$10.37	\$12.29	23.1	19.5
Tesla	\$123.18	\$2.15	\$3.96	\$4.00	\$5.60	30.8	22.0

This chart contains a lot of information, but it is important to provide the set-up for each of these stocks heading into 2023. The chart has the closing price of each stock as of 12-31-2022, actual results for 2021 and 2022 as well as the consensus earnings per share estimates as of end of year 2022 for 2023 and 2024. Starting with the

four stocks that we own (Amazon, Alphabet, Meta, and Nvidia) they all had disappointing fundamental results in 2022, and with the exception of Meta, were expected to bounce back in 2023. Amazon and Nvidia were both expected to continue their strong cyclical recoveries into 2024 whereas Alphabet was expected to fill the earnings gap in 2023 that occurred in 2022 before resuming more normalized growth in 2024. Not surprisingly, the earnings multiples afforded each of these stocks at the start of the year was consistent with that narrative. Meta was a bit of a special case in that it exited 2023 battling the concern that management was determined to forge forward with profligate spending while the core business fundamentals showed weakness. What a difference a year makes, but Meta being afforded a trough multiple on what we now know to be trough earnings makes better sense in hindsight. As for Apple, Microsoft and Tesla, the viewpoint heading into the year was that Apple and Microsoft would continue steady as she goes whereas Tesla would have a year of digestion in 2023 following a doubling of earnings in 2022. Again, the multiples afforded these stocks at the start of the year seem reasonable in hindsight. Of course, we now know that what actually occurred in 2023 versus what was expected to occur is a very different story.

### Chart 3- 2023 What Really Happened

	2023 Consensus EPS Estimate on 12-31-22	2024 Consensus EPS Estimate on 12-31-22	2023 Consensus on 12-31-23	2024 Consensus on 12-31-23	2023 Estimate Change	2024 Estimate Change
Amazon*	\$1.78	\$3.01	\$2.71	\$4.14	52%	38%
Alphabet*	\$5.25	\$6.16	\$5.74	\$6.72	9%	9%
Meta*	\$8.14	\$10.34	\$14.64	\$19.57	80%	89%
Nvidia*	\$4.35	\$6.00	\$12.49	\$21.77	187%	263%
Apple	\$6.60	\$7.38	\$6.20	\$6.71	-6%	-9%
Microsoft	\$10.37	\$12.29	\$10.41	\$12.26	0%	0%
Tesla	\$4.00	\$5.60	\$3.07	\$3.87	-23%	-31%
<i>* 2023 and 2024 Estimates are Internal Burke Wealth Management Estimates.</i>						

This chart shows the difference between what the consensus view of the earnings outlook was at the beginning of 2023 versus what it is now. For three of the four “Magnificent Seven” constituents in our portfolio, the difference between expectations heading into the year and reality was massive. First and foremost, Jensen Huang take a bow. The difference in Nvidia shows two things: First, the degree to which the timing and magnitude of the AI revolution as it relates to spending on high speed GPUs in the data center was underestimated by all (including yours truly). Second, anyone who uses the word hype during a TV interview to describe Nvidia’s share price performance in 2023 spent more time in the make-up chair than looking into what

actually happened with this business in 2023. We can and will debate the future as it pertains to Nvidia, but let's at least acknowledge what has already occurred. Meta was another company where the expectations were disconnected from reality. To be fair, heading into 2023 there were already signs that Meta's management had gotten religion with regards to the cost structure and some of this was reflected in the stock's run from \$90 to \$120 during the last six weeks of 2022. However, the degree to which management could cut costs without harming the business as well as the benefits from a stronger than feared macro-environment were underappreciated. The full earnings pivot from 2022 was filled in and then some in 2023 and the current outlook for 2024 is for continued fundamental strength. Amazon is a little different because, to be fair, relatively small changes in the profitability of the retail business result in outsized impacts on earnings. That said, the unfolding margin story in Amazon's US retail business is central to our investment thesis and we think, has much more room to go. Finally, the modest improvement in Alphabet's outlook that occurred in 2023 was consistent with a better than feared macroeconomic environment. As for Apple, Microsoft and Tesla, the outlook for Microsoft was continued excellence, Apple fell a little short of the expectations, while Tesla's outlook saw a materially lower reset over the course of 2023.

**Chart 4- Yes, Nvidia Really did get Cheaper in 2023:**

	<b>Closing Price 12-31-23</b>	<b>2023 P/E on 12-31-22</b>	<b>2024 P/E on 12-31-23</b>	<b>Change in Forward P/E</b>
Amazon	\$151.94	47.2	36.7	-22%
Alphabet	\$140.93	16.9	21.0	24%
Meta	\$353.96	14.8	18.1	22%
Nvidia	\$495.22	33.6	22.7	-32%
Apple	\$192.53	19.7	28.7	46%
Microsoft	\$376.04	23.1	30.7	33%
Tesla	\$248.48	30.8	64.2	108%
<b>S&amp;P 500</b>	<b>\$4,770</b>	<b>16.6</b>	<b>19.4</b>	<b>17%</b>

From an investment standpoint, this is really the key chart and shows why, despite the stellar returns from our 4 "Magnificent Seven" holdings in 2023, we remain optimistic about their prospects for 2024. We will discuss the key investment controversies surrounding Nvidia and Amazon later in this letter, but one fact that is indisputable is that the gains that these stocks saw in 2023 were earnings driven and not the result of a valuation driven hype cycle. Where they go from here will depend on execution and how the competitive dynamics of

their respective markets evolve. That is ground we are happy to battle on. Meta is a little different in that while its valuation expanded during 2023, the current level seems more realistic given its strong franchises and commitment to continued cost discipline. The outlier in our view would be where things stood a year ago when legitimate questions were being raised about competitive positioning relative to Tik-Tok and a management team that appeared out of touch and out of control on costs. Alphabet's earnings outlook is modestly better than it was a year ago and the valuation has expanded off of trough levels. We think this is conducive to returns in-line with earnings growth from here. Of the three "Magnificent Seven" companies that we don't own, it really is mostly a case of simply liking other stocks better.

### Returns Follow Earnings Growth:

We have frequently said that over time, equity returns will track earnings growth. This remains true. However, this does not mean that the relationship is going to track perfectly and linearly. Graphically speaking, think of the earnings of a portfolio as a line whose slope is the earnings growth and market returns as a sine wave over that line that reflects market rotations that can see a portfolio's returns overshoot or undershoot its fundamentals at any given period. At the risk of going one step too far with the charts and graphs in this letter, we are going to take a look at a graph that tracks the earnings growth of our Focused Growth portfolio versus the cumulative returns since inception in Q4-18.

**Figure 2**

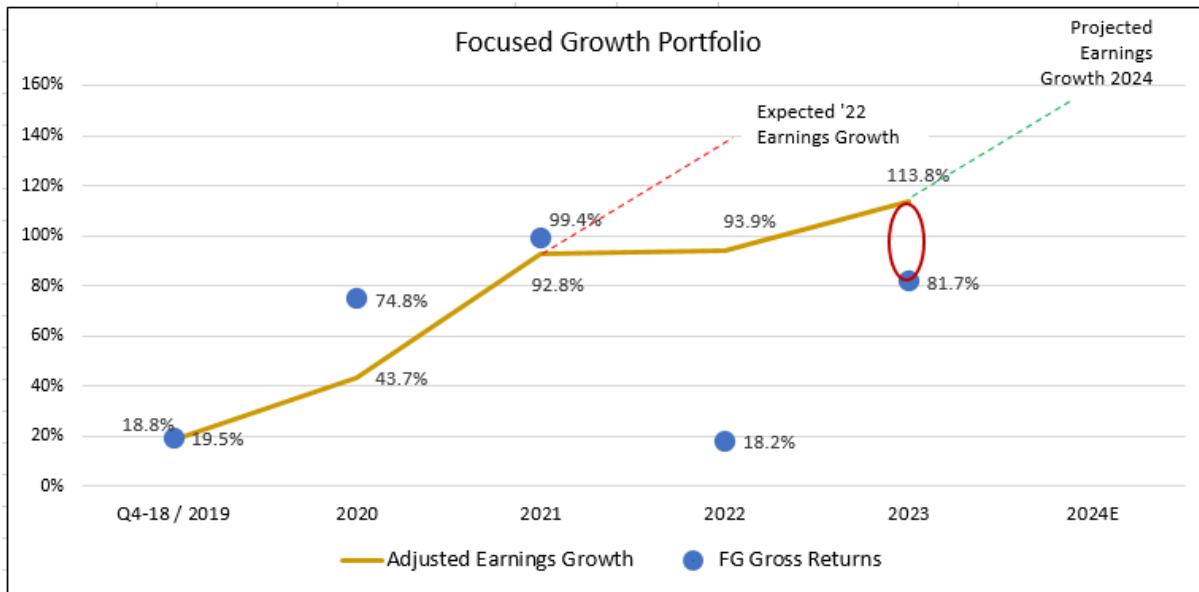


Figure 2 above shows the weighted average adjusted earnings growth of our portfolio versus portfolio returns since we launched the strategy in Q4-18. Note that we have made adjustments that remove outliers (Nvidia and Amazon growth rates were removed for 2023 so as not to skew results) so this graph is directionally accurate

but precisely wrong. That said, it does a pretty good job of explaining why we had the sharp declines of 2022 followed by the sharp recovery of 2023. It also shows that our “catch-up” period may have more room to go. As you can see, during the period from inception through 2021, portfolio returns tracked earnings growth pretty closely. This is even more the case if you look at the 2020 pandemic and 2021 reopening as a single period. 2022 was a different story. Heading into 2022, we were of the belief that portfolio earnings would resume mid-to-high teens growth from the 2021 base. This is shown in the red-dashed line on the graph. This was in-line with the “new normal” school of thinking. Habits had changed during the pandemic and earnings had a step function higher change in the 2020/2021 period and would resume growth from that higher base. This did not prove to be the case and instead of high-teens earnings growth in 2022, portfolio earnings were basically flat. With this type of shortfall, a down year would be expected. Instead, what we got was a 40% collapse that implied minimal growth for our portfolio companies going forward and reset valuations accordingly. We never believed that was the case and 2023 bore out our faith in the structural growth of our portfolio companies. However, our portfolio is still tracking below where the earnings growth would imply it should be. This could imply that multiples were a little frothy when we started, we still have some room for returns to catch-up to fundamentals, or a little of both. Further, if you look forward to 2024 and beyond, we project weighted average earnings per share growth of the portfolio to be roughly 20% per year. Finally, it is worth noting that the forward P/E of our portfolio currently stands at roughly 24x- near the lower end of the long-term range. It is for these reasons that despite the 53.3% returns delivered in 2023, we are confident in the future returns of our Focused Growth Portfolio.

#### **The Battleground Issues for 2024:**

In the spirit of the Presidential election year in which we will all be inundated with reports of polls from the “battleground” states, we thought we’d close this letter with a look at the battleground issues for 2024 that we believe will be critical to the returns of our portfolio.

**Will the 2023 AI Infrastructure Buildout Be Followed by an AI Application Explosion in 2024?** We have not been shy about our belief that the Artificial Intelligence Revolution will be transformational for business. Even so, the path to realizing the productivity benefits of AI will not be linear. 2023 was a year of massive investment in the data centers that will supply the compute power necessary for generative AI. We believe that this investment will continue. However, 2024 needs to be a year in which the applications that will provide the practical benefits of AI to enterprises needs to come into clearer focus. For our portfolio, this means that Snowflake will be a key partner that helps large enterprises get their data organized and structured such that

companies like Salesforce and ServiceNow can deliver the custom applications that will unlock massive AI based productivity. As we've noted previously, software applications tend to follow hardware investments by 3-6 months. We have gotten a glimpse of some of the early AI applications from Salesforce and ServiceNow and are encouraged. We need to see business investment match management rhetoric in the months to come. This will mean a step up in demand for cloud based software providers and that should equate to another year of strong returns for the stocks of these companies.

**As Nvidia Exits 2024, Will 2025 Look to Be a Year of Continued Growth or an Earnings Reset?** Nvidia is up roughly 10x since our initial investment in 2019. Included in this period was a fall of 65% from a peak in November of 2021 to the trough in October of 2022. This is a great company and has been a great stock but make no mistake, there is no free lunch here. Nvidia is now a trillion dollar market cap and in order for the good times to continue, we will need confirmation that the 2023/2024 spike in data center spending is not a one-time event but rather the beginning of a reset of data center computing towards GPU powered parallel processing. The first test of this thesis will be in 2025. I realize that new competitors are launching GPUs designed to compete with Nvidia's next generation H200 chip set and think it is cute that AMD is expecting its recent launch to generate 2024 sales in excess of \$1B. However, as much as its customers seek to encourage new supply partners or develop their own chips, 2024 is going to be another banner year for Nvidia. Unfortunately, that is widely known and largely reflected in the current share price. The controversy is around whether 2025 sees a reset in earnings towards the \$16 per share level or continued growth off of the higher base towards something like \$26 per share. For this to happen, we are going to need to reach a virtuous cycle whereby data center infrastructure begets software innovation which begets further data center infrastructure investment. This investment will also need to broaden from the Cloud Service Providers who are desperately trying to escape Nvidia's near monopolistic stranglehold on the GPUs necessary for generative AI and grow to include large enterprises making their own investments in AI. Longer term, we are confident that Nvidia's leadership in accelerated computing will maintain its standing as one of the most consequential companies in the world. As it relates to 2024, the unfolding outlook for 2025 is going to be the biggest near-term driver of this stock.

**Will Amazon's Retail Margins Continue to Exceed Expectations or Will Another Investment Ramp Dampen Gains?** Throughout its history, few companies have received the benefit of the doubt more so than Amazon. No matter the size, scale or duration of an investment, the market always seemed willing to underwrite Jeff Bezos' vision. Andy Jassy has to be wondering what in the world happened. Right or wrong, fair or not, since Jassy took the helm at Amazon investors seem to have decided that they would like to see current period profits

to go along with the vision of global domination. To his credit, Jassy seems to understand this new reality and has openly acknowledged the potential for Amazon to meet and exceed all-time high retail margins following a period of massive investment from 2020-2022 which saw the company spend \$165 billion in CAPEX and effectively double the size of its employee and warehouse footprint among other things. This investment period happened at roughly the same time that the check came due on the perpetual benefit of the doubt afforded the stock and led to the share price being cut in half from August of 2020 through December of 2022.

The conventional wisdom on Amazon is that so goes AWS, so goes Amazon stock. I don't think it is that simple. I take the long-term success of AWS as a given, and outside of the one day volatility around earnings releases regarding whether growth is accelerating or decelerating, I don't view AWS as much of a concern. The sleeper issue at Amazon is retail margins, more specifically North American retail margins. In 2022, North American retail margins were -0.9%. For the first 3 quarters of 2023, that improved to 3.4%. The all-time peak four quarter performance is 5.7% (late 2018/early 2019). We think they can go a lot higher and will get there sooner rather than later. These differences may not seem like a massive change, but things add up when you talking about a \$350 billion revenue business. The same goes for the glorious day when International Retail profits flip from losses to gains. Simply stated, the massive investment in employees, trucks, planes and warehouse space that Amazon made from 2020-2022 made it the proverbial puppy with big paws. As it grows into this new footprint, we think investors are going to finally get a glimpse into the long-term profitability of this behemoth.

**Will our Golden Age of Cable Thesis Finally Start to Come into Clearer Focus or will Competitive Pressures Lead to Another Year of Tepid Profit Growth?** If you've read prior editions of these letters, you know that we think that the cable companies are the low cost provider of telecommunication services (broadband and wireless) and that the market share and margin opportunity in wireless is a multiple of the current consensus thinking. The Golden Age of Cable thesis is that these competitive strengths will begin to be revealed during a period in which the threat from fixed wireless broadband abates and capital intensity returns to previous, lower levels. What I have done in two short sentences is articulate an investment case for Comcast and Charter that might actually move the investment discussion beyond the quarterly trends in net broadband additions. Sadly, to date, neither company has accepted my offer to take over all of their corporate communications.

Let's unpack the Golden Age of Cable thesis a bit. To start, this is a three year process in which cable financials and competitive positioning will improve materially from current levels. In 2024, we believe that it will become clear that the wireless customer additions that began in earnest in Q4-22 will transition from customers added

on promotion to full paying customers. Charter is the company to watch here as they were the more aggressive of the two companies in going after wireless additions. Comcast has joined the fight and after seeing the early success of Charter's initiatives, has ramped up wireless promotions in its own footprint. As a reminder, both Charter and Comcast have a perpetual wholesale agreement with Verizon whereby they can offload any wireless traffic that they sell and can't serve onto Verizon's network at wholesale rates. They also have the ability to expand their existing wireless network wherever they choose and given that roughly 60% of traffic occurs in 3% of their footprint, the opportunity is ripe to cherry pick the most heavily trafficked areas. We think wireless gross margins will prove to be north of 60% whereas current consensus thinking has them closer to 20%. Both Charter and Comcast serve ~30M broadband households so the ability to profitably and quickly grow wireless within their existing customer base is enormous. We think that comes into clearer focus in 2024 with the catalyst being Charter converting the promoted wireless customers of 2023 into the full pay customers of 2024.

2025 is year two of our Golden Age thesis and this centers around the competitive threat from fixed wireless broadband abating. Fixed wireless broadband is a broadband product that is sold, most notably by T-Mobile, by using excess wireless spectrum. It is an inferior product compared to cable broadband or Telco Fiber but it has gained traction among low-end broadband users. Importantly, T-Mobile estimates that its existing spectrum footprint can support 7M-8M customers. They had 4.2M at the end of Q3 and are adding about 560K new customers per quarter. Although the cable companies contend, and we believe, that this is an inferior product that will not keep up with the ever growing demand for bandwidth (think Thursday Night Football streaming), fixed wireless broadband has adversely impacted net cable broadband adds and been a thorn in the side of Comcast and Charter for the last couple of years. By the second quarter of 2025, assuming the current run rate of net additions, T-Mobile's foray into high speed internet will have reached its capacity. This will have a positive impact on cable broadband additions and attention can turn from how many customers can fixed wireless take to how many they can keep.

The final chapter of the Golden Age of Cable thesis occurs in 2026 when the current ramp up in CAPEX spending required to upgrade cable plant broadband speeds to 1 Gig symmetrical and beyond will be completed. Upon completion of the current upgrade cycle, capital intensity will fall, margins will rise and free cash flow will spike. This will occur against a backdrop of continued wireless gains and abating fixed wireless pressure. There you have it. The multi-year Golden Age of Cable thesis in its entirety. Now, we just need to sit back and hope it happens as described.

As we turn the page on 2023 and look ahead to 2024, we have a tremendous sense of gratitude and excitement. We are grateful to you, our clients, who stuck with us through the dark days of 2022 to enjoy along-side us the rebound of 2023. We are grateful that the snapback in the share prices of our portfolio of high quality growth companies happened while we were still able to maintain some semblance of our sanity. We are excited about the prospects for the years ahead and believe that our portfolio is well positioned to benefit from the upcoming AI revolution. We thank you for the confidence and trust you place in us. As always, don't hesitate to reach out if you have any questions or topics you would like to discuss in greater detail.

Happy New Year!



Ken Burke  
Chief Investment Officer

## Disclosure

*The Burke Wealth Management Focused Growth Composite, created on October 1, 2018, contains fully discretionary large cap equity accounts that is measured against the S&P 500 Total Return Index and the Russell 1000 Growth Index. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. The Burke Wealth Management Focused Growth Strategy invests exclusively in a portfolio of high-quality companies.*

*The S&P 500® Total Return Index is a widely recognized, unmanaged index of 500 common stocks which are generally representative of the U.S. stock market as a whole. Ordinary dividends are reinvested across the index and accounted for in the Total Return index calculations. The Russell 1000® Growth Index is an unmanaged index that measures the performance of the large-cap growth segment of the U.S. equity universe. It includes those Russell 1000® Index companies with higher price-to-book ratios and higher forecasted growth values.*

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