Hutchinson
CAPITAL MANAGEMENT

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"It ain't what you don't know that gets you into trouble. It's what you know for sure that just ain't so."
– Mark Twain

INVESTMENT PERSPECTIVES

Energy, AI Expectations, and the Discipline to Hold

As we enter 2026, markets find themselves in a peculiar position: major indices hover near all-time highs, yet the investing landscape feels anything but comfortable. Labor market data has softened, geopolitical tensions flare unpredictably, and the artificial intelligence boom continues to reshape capital flows across sectors, most notably in energy, where data center demand is rewriting long-held assumptions about electricity consumption and generation mix. Meanwhile, the gap between AI-related projections and historical precedent has widened to levels that warrant serious examination.

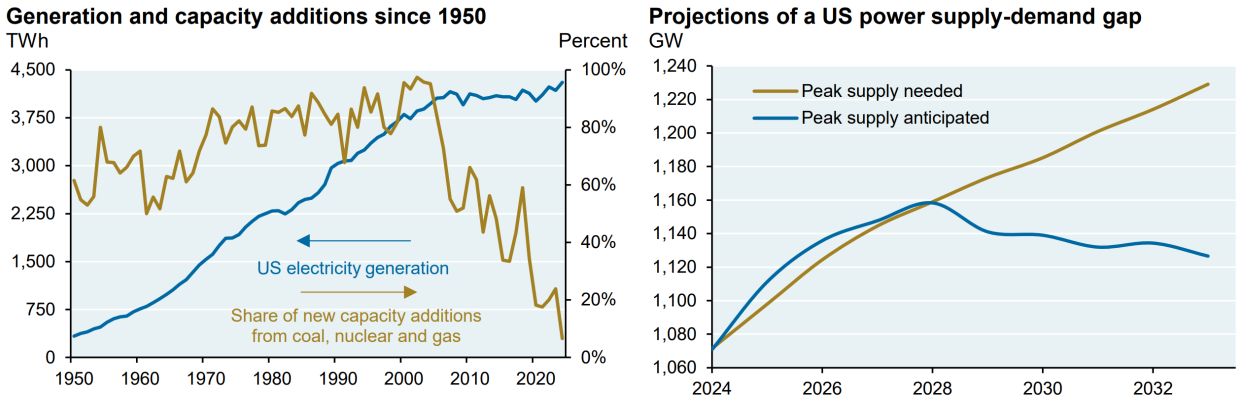
Against this backdrop, this quarter's *Investment Perspectives* explores three themes: how AI-driven electricity demand is creating a supply gap that will take years to close, and why the energy transition, while real, won't happen overnight; what base rate analysis reveals about the extraordinary growth projections embedded in AI valuations; and why the psychology of holding through uncertainty remains the most underrated skill in long-term wealth creation. Though varied in subject, these themes converge on a single insight: each rewards investors who can distinguish between compelling narratives and fundamental value, and who possess the temperament to act on that distinction.

Energy Markets: AI Demand, Geopolitics, and Long-Term Fundamentals

The intersection of artificial intelligence and energy markets has emerged as one of the most consequential investment themes of this decade, with data center electricity consumption fundamentally reshaping demand projections across the power sector. According to the International Energy Agency, global data center electricity consumption reached approximately 415 terawatt-hours in 2024, roughly 1.5% of worldwide electricity demand, and is projected to more than double to 945 TWh by 2030. In the United States, the picture is even more dramatic: data centers consumed over 4% of total electricity in 2024 and are forecast to reach nearly 8% by 2030. The geographic concentration of this demand creates both challenges and opportunities, with Virginia alone seeing data centers consume 26% of the state's total electricity supply in 2023, while Texas, Oregon, and Arizona emerge as the next frontier for massive AI infrastructure buildouts.

The central challenge is straightforward: demand is growing faster than supply, and the gap will persist for years. Despite the technology sector's stated commitment to renewable energy and carbon neutrality, the immediate, dispatchable power requirements of AI workloads are overwhelming the capacity of intermittent renewable sources. The IEA projects that fossil fuels will meet over 40% of additional data center electricity demand through 2030. Major utilities serving Virginia, Georgia, and the Carolinas have announced plans to add 20 gigawatts of new generation capacity by 2040, with two-thirds of projected load growth tied directly to data centers. Projects like Meta's $30 billion Louisiana data center campus, which will feature on-site gas generation, illustrate a pragmatic reality: the energy transition is happening,

but it won't happen overnight, and the world will need reliable baseload power from multiple sources for the foreseeable future.



Source: J.P. Morgan

Beyond AI-driven demand, traditional geopolitical factors continue to influence energy markets, though their impact has been more muted than many anticipated. The June 2025 U.S. strike on Iranian nuclear facilities briefly elevated concerns about Strait of Hormuz disruptions, through which 20-25% of global seaborne oil trade passes, yet WTI crude remained range-bound between $55 and $80 per barrel throughout the year. U.S. military action in Venezuela similarly failed to produce sustained price volatility, reflecting Venezuela's diminished production footprint of roughly 1% of global output despite holding the world's largest proven reserves. The structural importance of oil to the U.S. economy remains underappreciated by many investors: oil accounts for approximately 90% of transportation energy consumption and roughly 33% of industrial production. While the oil intensity of GDP has declined across developed economies, the September 2025 expiration of federal EV subsidies and Ford's decision to discontinue the F-150 Lightning, the first all-electric version of the best selling truck, suggest that oil 's relevance will persist longer than many analysts projected just two years ago.

What does this mean for portfolios? The AI-driven transformation of electricity demand, combined with persistent geopolitical uncertainty in traditional oil markets, argues for emphasizing companies with sustainable competitive advantages, strong balance sheets, and management teams with proven capital allocation discipline. We're not interested in chasing short-term price movements in response to geopolitical headlines or speculating on which technologies will ultimately power the next generation of data centers. Energy market volatility driven by political events or technological hype typically creates noise rather than signal for those of us focused on fundamental value. The businesses best positioned to navigate this environment are those generating strong free cash flows, maintaining financial flexibility to capitalize on opportunities, and trading at reasonable valuations relative to their intrinsic worth.

Base Rates and AI: Historical Context for Extraordinary Claims

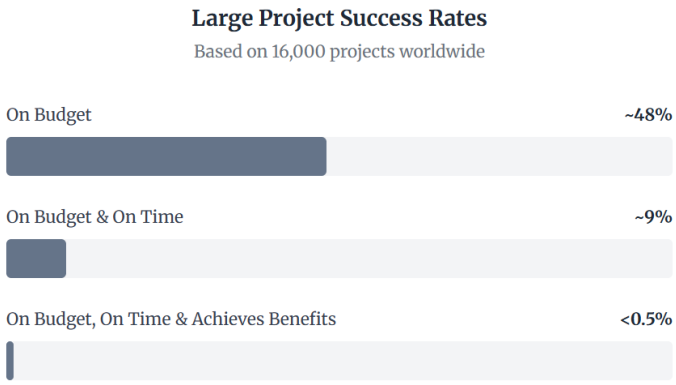
One of the most valuable disciplines in investing is the practice of consulting base rates before making forecasts about individual companies or technologies. Base rates represent the historical frequency of outcomes across a relevant reference class, providing an empirical anchor against which to evaluate specific predictions. An example of this would be throwing two dice and counting the number of times they came up with certain totals. This approach, championed by researchers like Michael Mauboussin, Head of Consilient Research for Counterpoint Global at Morgan Stanley, proves especially valuable during periods of technological enthusiasm when narratives can overwhelm sober analysis.

Consider OpenAI's (ChatGPT creator) published revenue projections: the company reported revenues of $3.7 billion in 2024 and shared forecasts with investors projecting $145 billion by 2029, implying a compound annual growth rate of ~108% over five years. To evaluate whether such growth is plausible, we must ask a simple question: how often has any company achieved this in the history of corporate

America? The answer, drawn from a database of nearly 19,000 public companies dating to 1950, is instructive: never. No company starting at comparable revenue levels has ever sustained growth at this rate over a five-year period.

The statistical context makes the challenge even clearer. Among companies with revenues between $2.5 billion and $5 billion, the mean growth rate over subsequent five-year periods has been approximately 7%, with a standard deviation of roughly 10.6%. A 108% compound growth rate represents a 9.5 standard deviation event: a statistical outcome so rare as to be effectively unprecedented in the historical record. This does not mean such growth is impossible; OpenAI may indeed become the singular outlier that rewrites the record books. But we must recognize that assigning high probability to such an outcome requires extraordinary confidence in factors that differentiate this situation from thousands of prior cases. The base rate analysis doesn't tell us what will happen; it tells us what has happened across comparable situations, providing essential context for calibrating our expectations and sizing our positions appropriately.

Beyond revenue growth projections, base rates offer sobering perspective on the massive infrastructure buildout accompanying the AI wave. Research compiled by Bent Flyvbjerg, an Oxford professor and the world's leading scholar on megaproject management, drawing on a database of 16,000 major projects worldwide, reveals that fewer than 50% of large projects come in on budget, fewer than 9% finish on budget and on time, and fewer than one-half of one percent deliver on budget, on time, and achieve their intended benefits. The AI infrastructure buildout, encompassing data centers, power generation, and transmission capacity measured in tens of billions of dollars, represents precisely the type of ambitious, complex project where historical experience suggests caution. This doesn't mean the infrastructure won't ultimately get built or prove valuable; the fiber optic networks constructed during the dot-com boom eventually became essential infrastructure for the mobile internet era. But the path from announcement to operational deployment rarely follows the optimistic timelines embedded in current valuations.



Source: Flyvbjerg, B. "How Big Things Get Done"

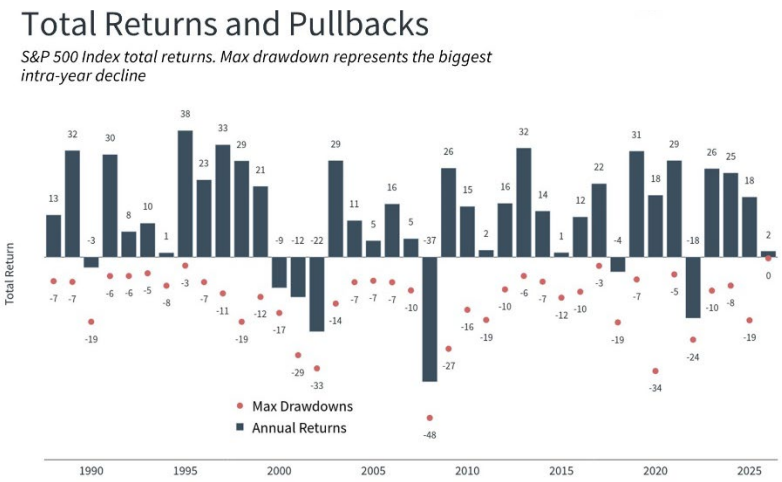
We embrace base rate thinking as a cornerstone of how we allocate capital. When evaluating any investment thesis, particularly those involving transformational technologies, we begin by asking what historical experience tells us about similar situations. This approach doesn't preclude investing in companies with ambitious growth plans; rather, it helps us calibrate appropriate position sizes, required margins of safety, and realistic expectations for how long thesis validation may take. We recognize that every successful growth company was once an outlier that defied base rates, but we also recognize that for every company that achieved escape velocity, dozens of others with similar narratives failed to reach their projected trajectories. By grounding our analysis in historical experience while remaining open to exceptional outcomes, we aim to construct portfolios that can participate in genuine technological transformation while protecting capital against the inevitable disappointments that accompany periods of elevated expectations.

The Psychology of Holding Through Uncertainty

The current market environment presents a particularly challenging psychological landscape: equity indices near all-time highs coexisting with genuine uncertainty about labor market deterioration, geopolitical flashpoints, persistent inflation concerns, and unprecedented policy experimentation. This combination of strong recent returns and legitimate forward-looking risks creates fertile ground for behavioral errors in both directions. Some investors, anchored to recent gains and fearing they will miss further upside, abandon the discipline that served them well through prior cycles. Others, fixating on the litany of risks, retreat to cash at precisely the moment when staying invested matters most for long-term wealth creation. Neither response serves the goal of compounding capital over time, yet both feel entirely rational in the moment to those making them.

The core problem is that we don't experience gains and losses objectively. Daniel Kahneman and Amos Tversky, the psychologists whose research forms the foundation of behavioral economics, famously observed that "losses loom larger than gains." This describes loss aversion: the tendency to feel the pain of losses roughly twice as intensely as the pleasure of equivalent gains. That asymmetry shapes decisions in ways we rarely recognize, and it creates an emotional response that can overwhelm rational analysis precisely when discipline matters most.

When we view the S&P 500 over decades, stock market downturns appear as temporary interruptions in a long upward trajectory. Yet in the moment, these same declines trigger powerful responses that drive investors to act against their own interests. The historical record shows that markets have risen in roughly two-thirds of calendar years, yet significant pullbacks occur within most of those years. Last April's tariff-driven selloff offers a vivid illustration: those who exited near the bottom, responding to fear rather than fundamentals, missed the 34% rally that followed. The availability heuristic compounds this problem, causing recent dramatic events to loom larger in our mental calculus than base rates and historical context would warrant. We overweight vivid, recent information and underweight the statistical reality that markets have navigated through countless crises, conflicts, and policy mistakes while still delivering positive long-term returns.



Source: Clearnomics

The antidote to these behavioral pitfalls lies not in suppressing emotion but in building systems and frameworks that encourage decision-making toward long-term objectives. This begins with acknowledging that uncertainty is not a temporary condition to be waited out but rather the permanent backdrop against which all investment decisions occur. There has never been a moment in market history when the future felt certain; there have only been moments when investors collectively chose to ignore the uncertainties that were always present. The investors who compound wealth over decades are not those who correctly predict macroeconomic outcomes or time market cycles, but rather those who maintain exposure to quality businesses through the inevitable periods when holding feels most

uncomfortable. Our average holding period of over five years, compared to the market average of less than ten months, reflects our deliberate commitment to allowing business fundamentals rather than market sentiment to drive returns.

We recognize that intellectual understanding of behavioral biases does not immunize anyone, including us, from experiencing them. The discomfort of holding through uncertainty is real, and dismissing it as irrational does nothing to address the lived experience of watching portfolios fluctuate while headlines suggest action is required. What we can offer is perspective grounded in decades of market history and a process designed to separate signal from noise. The businesses we own possess the strong balance sheets, sustainable competitive advantages, and proven management teams that have historically navigated through periods of economic and geopolitical stress. By focusing on what we can evaluate with reasonable confidence, the quality and valuation of individual businesses, rather than what we cannot predict, the timing and magnitude of macroeconomic shifts, we position portfolios to benefit from the long-term growth in corporate earnings that has rewarded those who stayed invested across every prior period of uncertainty.

In Conclusion

Energy shortfalls, base rate analysis, and the psychology of holding through volatility share a common thread: successful investing requires both analytical rigor and emotional steadiness, and the two reinforce each other. Understanding why extraordinary projections rarely materialize makes it easier to resist chasing them; recognizing the permanence of uncertainty makes it easier to stay invested despite it.

We remain optimistic about the long-term prospects for patient, disciplined investors. The AI transformation is real, even if the path from here to there will prove bumpier and more circuitous than current valuations imply. The energy transition is also real, but it will unfold over years, not quarters, creating opportunities for companies that can supply reliable power while the infrastructure catches up. And markets will, as they always have, reward those who can distinguish between price and value, and who possess the temperament to act on that distinction when it matters most.

Our commitment to you remains unchanged: we will continue to focus on businesses that can compound value across a range of economic scenarios, maintain the discipline to buy quality at reasonable prices rather than chase momentum, and hold through the inevitable periods of volatility that test every investor's resolve. These principles have served us well through past cycles, and we believe they will continue to do so.

Thank you for your continued trust and partnership. As always, we welcome your questions about current market dynamics, portfolio positioning, or your specific financial objectives.

DISCLOSURES:

As of December 31, 2025, the following were the ten largest holdings of HCM:

Name of Issuer	% of Equity Portfolio	12/31/2025 Closing Price
Alphabet Inc Class A	7.96%	$313.00
Berkshire Hathaway Inc Class B	6.61%	$502.65
Apple Inc	6.21%	$271.86
Microsoft Corp	5.89%	$483.62
Bank of America Corp	5.50%	$55.00
Progressive Corp	4.24%	$227.72
Jacobs Solutions Inc	3.88%	$132.56
Waters Corp	3.29%	$379.83
Markel Corp	3.21%	$2,149.65
Capital One Financial Corp	3.17%	$242.36

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