



Quarterly Commentary

September 2025
Third Quarter

“Predicting rain doesn’t count, building arks does.”

Warren Buffett

The Noah Principle

When constructing our portfolio, we try to assess risk factors, or storms which could potentially cause a permanent loss of capital. The power of compounding is astonishing, but permanent loss of capital is the hole in the boat that sinks the ship. There are company specific factors (idiosyncratic) that we can control – avoiding complex business models, investing in strong balance sheets, and aligning with competent management teams that obsess over capital allocation. There are also factors outside our control like fiscal and monetary policy, geopolitical events, or major dislocations between perception and reality that cause equities to swing to extremes on the valuation pendulum. Today, certain market participants seem convinced the sun will never stop shining, forgetting that rain will come again.

Parable of Most Valuable Object

In a grand room adorned with architectural detail sits a small, beautiful box. The crowd is speaking in awe about the box and one of the leaders points to the box and says, “This box is the most valuable box in the world.” This hushes the crowd as they wonder what might be in that box. One spectator asks, “What makes the box the most valuable?” The leader replies, “it is the most valuable because everyone desires it...its immeasurable value is proven by how much people want it.” The spectator then questions, “But what makes it so desirable?” to which the leader responds, “because it is the most valuable object!”

As we read this parable, we couldn’t help but compare this story to that of OpenAI. OpenAI’s chatbot ChatGPT is undoubtedly valuable: with 18 billion messages processed weekly and more than

one in ten people globally having used ChatGPT, the company’s reach is undeniable. OpenAI has raised approximately \$60 billion across 11 rounds, placing its latest valuation around \$500 billion. Revenues are projected at \$13 billion in 2025, alongside an expected \$8 billion cash burn. According to a reported leak, OpenAI anticipates over \$115 billion in cumulative cash burn by 2029 as it invests heavily in chips, data, and power infrastructure.

It has become the most desirable and—therefore—the most valuable private company in the world. Each partnership it forms adds billions of dollars of value to its partners’ market caps. In the last month alone, companies announcing OpenAI collaborations collectively added over \$400 billion in market capitalization in the two days post announcements.

AI: The Unknowable Revolution

We are not AI experts. Each investment and industry we analyze starts as a blank slate—an important advantage of being a generalist. We’ve previously uncovered investment opportunities in energy, housing, and office real estate long before consensus turned positive. Our approach is the same for AI: curiosity first, conviction later.

The capital allocation decisions and potential returns on the investments remain uncertain. Estimates for building a 1-gigawatt (GW) data center range from \$25 billion to \$50 billion and it takes an estimated two years to build 1GW. Bain & Company recently published a [report](#) noting that U.S. compute demand for AI could reach 100 GW by 2030 (more than the current electric generation capacity of the state of California). At the midpoint, this would require \$3.7 trillion in infrastructure spending, which is more than



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this year's \$2.1 trillion of cumulative sales of the Magnificent 7 companies.

This trajectory of AI spend is unsustainable, and the recent [MIT study](#) regarding AI productivity gains and “workslop” is concerning. Extraordinary optimism is fueling valuations that are moving beyond the scope of what is practical or rational and for the first time in seventy years, companies with increased capital spending are being rewarded with increasing stock prices. According to JPMorgan, AI-related companies have driven 75% of the S&P 500's total return and 90% of all capital spending growth since ChatGPT's launch in November 2022. However, according to Empirical Research, stocks in the highest quintile of year-over-year capex growth have traditionally underperformed the market as a group. As Carmen Reinhart famously said, “More money has been lost because of four words than at the point of a gun. Those words are ‘This time is different.’”

As it stands today, AI optionality is valued higher than profitability or fundamentals. Some companies without proven business models are valued in the tens of billions simply because they are synonymous with AI. We are tracking an equal-weighted basket of 20 AI-related companies (ex-Magnificent 7) and collectively, this “AI portfolio” commands a total market capitalization of \$725 billion, with estimated 2026 sales of \$18 billion and earnings of \$1.4 billion. This basket has returned over 200% year-to-date as of this writing and trades for 39x sales and 520x earnings.

By comparison, our own portfolio has less total capitalization yet generates over 15 times the estimated sales and 30 times the earnings of the AI portfolio. We have said repeatedly that “*significant opportunities arise when there is a momentous shift in market sentiment.*” This year, that shift has evolved into full-blown euphoria around AI while other proven businesses trade for attractive valuations.

We've seen this movie before. In 2021, we monitored a portfolio of newly minted software as a service (SAAS) IPOs that traded for 20x sales and generated no earnings. At the time, their surging stock prices raised questions among even the most disciplined investors about whether fundamentals still mattered. Within two years, that portfolio collapsed by 65%, and over a quarter of the companies were down 90% from peak.

Today's pattern rhymes. The AI package being sold to investors is one that promises a revolution but remains murky on economics. We highlight these observations not to proclaim an imminent risk, but to emphasize that it will rain again. We will continue to focus on building an ark strong enough to withstand the market's storms.

Conclusion

The market is at a fascinating juncture where sentiment, storytelling, and capital are converging at warp speed. The high-priced stocks of today may well be the cautionary tales of tomorrow. We can't predict the timing of these shifts but can prepare for them—building an ark sturdy enough to preserve but also compound your wealth.

As always, we remain grateful for your trust and partnership.

Sincerely,
Nixon Capital

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