We made three portfolio changes. First, we exited PepsiCo. The position no longer fits our Increasing Health Focus and Demographics and Longevity themes, and the dividend now absorbs a substantial portion of free cash flow, leaving limited capacity to fund repositioning and dividend growth simultaneously. Second, we initiated a 1.25% position in Kroger as a first tranche investment, reflecting its stronger dividend coverage and improving higher-margin businesses while acknowledging execution risks ahead of the October 20 investor update. Third, we rebalanced Shell and Chevron to model weight and halved the ConocoPhillips model weight after price appreciation created a larger-than-desired sector overweight, while maintaining exposure to the portfolio's long-term Future of Energy theme.

Exit PepsiCo (PEP)

We exited our position in PepsiCo. The decision reflects a weakening fit with our Increasing Health Focus theme as consumers place greater emphasis on nutrition, weight management and healthier everyday choices. PepsiCo's portfolio remains heavily exposed to high-calorie snacks and beverages, categories that may face sustained pressure as preferences evolve and GLP-1 medication adoption broadens.

This shift creates a more challenging long-term demand backdrop for several of PepsiCo's core categories and may require greater spending on product reformulation, portfolio repositioning and marketing to sustain growth. Although the company has meaningful brands, scale and distribution advantages, we see less thematic alignment and a less compelling path to durable growth than in consumer businesses positioned more directly around value, fresh food and health-conscious consumption.

PepsiCo's international footprint continues to align with our Global Middle Class theme, and its ~4.5% yield was amongst the highest in the Dividend Growth strategy. However, those positives were not sufficient to offset the increasing health-related headwinds. The company's elevated payout ratio and low free cash flow dividend coverage of close to 1x reinforced the decision, leaving limited capacity to invest in portfolio adaptation while sustaining dividend growth. In our view, declining thematic fit and constrained financial flexibility no longer justified the position.

Initiate Kroger (KR) at 1.25% Model Weight

We initiated a position in Kroger at a 1.25% model weight. The position replaces a portion of PepsiCo's consumer staples exposure and moves both strategies closer to benchmark staples weights—both relative to the equal-weight S&P 500 and, more meaningfully, to the ProShares S&P 500 Dividend Aristocrats ETF, where staples carry a larger allocation. The initial size reflects our view that Kroger is an attractive quality opportunity, balanced against the need for further evidence that management can stabilize market share and improve operating performance.

Kroger fits our Dividend Growth framework at the intersection of consumer resilience, value-oriented consumption and operational improvement. Food is non-discretionary, and a slower or more uncertain economic environment may reinforce demand for Kroger's combination of affordability, convenience and loyalty-driven engagement. Its scale, purchasing power, private-label franchise, digital fulfillment network, vertical integration and customer-data ecosystem are difficult for smaller competitors to replicate. Although Walmart, Amazon, Costco and regional operators remain formidable competitors, Kroger's valuation already discounts share pressure, creating a relatively low hurdle for improvement when execution stabilizes.

The dividend profile is central to the thesis. Kroger raised its quarterly dividend 11.4% to $0.39 per share effective September 1, marking its 20th consecutive annual increase. The company's recurring cash generation, investment-grade balance-sheet flexibility, and excess free cash flow provide multiple avenues for shareholder returns. Continued repurchases can further enhance per-share earnings and allow dividend growth to outpace growth in aggregate cash dividends, although the durability of that contribution depends on future authorization and execution.

New chief executive Greg Foran provides a potential catalyst as Kroger moves beyond the failed Albertsons transaction and refocuses on operational execution rather than financial engineering. His early plan emphasizes market-share stabilization, digital growth, supply-chain optimization, customer retention and profitability improvement. Three higher-margin businesses are increasingly important to that effort. In the quarter reported September 11, Kroger Precision Marketing grew profit 24%, its best result since 2021, supported by first-party data across 63 million households and a loyalty program associated with more than 95% of transactions. eCommerce delivered its second consecutive profitable quarter, with adjusted sales up 20%. Kroger private label brands generated more than $39 billion in fiscal 2025 sales and represented roughly 29% of sales excluding fuel, while Private Selection grew 14% in the quarter. Cost savings are running ahead of plan, and the Kroger Global Capability Center is expected to contribute more meaningfully in 2027 and 2028.

Balance-sheet leverage of 1.91 times adjusted earnings remains below management's 2.30–2.50-times target range and provides strategic flexibility. That capacity supports the pending $1.65 billion acquisition of Giant Eagle, expected to add roughly 200 stores and $9 billion in sales when it closes in 2027. At the same time, the transaction adds integration and capital-allocation risk. Approximately $800 million of repurchase authorization remains, with no successor program announced, even though buybacks have meaningfully contributed to current per-share earnings growth.

The October 20 investor update is the next important test because management has deferred key elements of its strategic framework, including the specifics of its price-investment plan and cost-savings targets. We will be watching for evidence of market-share stabilization, improved fresh-category shrink, inventory growth that is better aligned with sales, credible second-half free cash flow delivery, and a disciplined response to price competition. Kroger is a durable, cash-generative quality-value story with an attractive combination of current income, dividend growth potential, buybacks and valuation upside. We therefore view the 1.25% allocation as a first-tranche position, with additional investment contingent on confirmation that the new leadership team can convert Kroger's competitive assets into sustained operational improvement.

Energy Sector Trim

We trimmed energy exposure in line with our sell discipline and portfolio guardrails after price appreciation made the sector overweight too large relative to the benchmarks. In the strategy, energy had risen from a 7.50% model allocation to 9.00%, creating the strategy's largest active sector position at approximately 490 basis points above the equal-weight S&P 500 and 752 basis points above the Dividend Aristocrats ETF. Because that excess exposure resulted from market drift rather than a new Investment Committee decision, we acted to restore intentional position sizing. We reduced the ConocoPhillips model weight from 2.50% to 1.25% and rebalanced Shell and Chevron to their previously approved model weights of 3.75% and 1.25%, respectively.

The trim is first and foremost a risk-control decision, not an attempt to time crude oil. As of the date of our investment decision, ConocoPhillips was up 46.8% year to date, Chevron 38.2% and Shell 30.2%, leaving sector exposure increasingly dependent on a geopolitical premium that we did not underwrite. Brent's move from above $110 per barrel in March to roughly $79 in early August and back toward $92 in late August shows how quickly that premium can change, while most forecasters still expect a global oil supply surplus in 2027. Energy is also the portfolio's weakest dividend-growth cohort, with three-year weighted dividend growth of 1.31% versus approximately 7% for the Dividend Growth strategy overall. The income cost of correcting the overweight is modest: after redeployment at the non-energy portfolio's average yield, the estimated net yield impact is roughly two basis points.

Importantly, the objective is to reduce commodity-price exposure, not eliminate energy exposure. After the trim, the strategy retains a deliberate 6.25% energy allocation—approximately 215 basis points above the equal-weight S&P 500 and approximately 477 basis points above the Dividend Aristocrats ETF. We believe this remains an appropriately sized expression of our Future of Energy theme. Liquefied natural gas as a bridge fuel, rising power demand from data centers, electrification and industrial reshoring, and nuclear power's transition from constrained to strategically necessary are multi-year structural drivers that do not depend on where Brent trades next quarter. The remaining overweight also preserves energy's inflation- and geopolitical-hedging characteristics.

We favor retaining the integrated operators at their model weights because they provide the defensive characteristics we want from the sector. Shell and Chevron yield 3.17% and 3.40%, respectively, and their downstream, refining, LNG, and trading businesses can partially offset upstream weakness. Shell has repurchased at least $3 billion of stock in each of the past 19 consecutive quarters, distributed 44% of cash flow from operations over the trailing 12 months, and reduced gearing to 19%. Chevron's Hess integration is also running ahead of plan, with $1.5 billion of run-rate synergies captured six months earlier than expected and 50% above the original target. Reducing the sector by concentrating more of the cut in ConocoPhillips therefore improves the quality and resilience of the remaining energy allocation rather than simply making it smaller.

ConocoPhillips bears the larger reduction because it has no downstream, refining, or trading business to cushion declines in crude prices, making its earnings and free cash flow more directly sensitive to the commodity. We continue to hold a 1.25% position because the company remains a high-quality operator and new chief executive Andy O'Brien brings a finance and strategy background that may support continued execution and capital discipline. The resulting sector position is still a meaningful active overweight, but one set deliberately by conviction and portfolio guardrails rather than by the oil tape.

Disclosures

This letter may contain "forward-looking statements" which are based on Brookmont's beliefs, as well as on a number of assumptions concerning future events, based on information currently available to Brookmont. Current and prospective clients are cautioned not to put undue reliance on such forward-looking statements, which are not a guarantee of future performance, and are subject to a number of uncertainties and other factors, many of which are outside Brookmont's control, and which could cause actual results to differ materially from such statements. All expressions of opinions are subject to change without notice.

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The Brookmont Dividend Growth Strategy Composite contains fully discretionary accounts with similar value equity investment strategies and objectives. For comparison purposes, the Dividend Growth Strategy Composite is measured against a combination of two indices. The S&P Dividend Aristocrats Index was used prior to November 2013; ProShares S&P 500 Dividend Aristocrats ETF is used subsequently. The ProShares S&P 500 Dividend Aristocrats ETF is an exchange-traded fund designed to track the S&P 500 Dividend Aristocrats Index. The fund focuses on U.S. large-cap companies in the S&P 500 that have increased their dividends for at least 25 consecutive years, giving investors exposure to businesses with long records of dividend growth, financial durability, and shareholder returns.

NOBL is equal-weighted, which helps reduce reliance on a small number of very large companies and can provide broader exposure across dividend-growing stocks. It is typically considered by investors seeking a blend of income, quality, and lower-volatility equity exposure, though it may lag broader growth-oriented indexes when non-dividend-paying or faster-growing companies lead the market. There is no representation that this index is an appropriate benchmark for such a comparison. The volatility of this ETF may be materially different from the performance of the strategy.

Gross returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. Net-of-fees performance was calculated using actual management fees. Additional information regarding the policies for calculating and reporting returns is available upon request.

Your account returns might vary from the composites returns if you own securities that are not included in the Strategy or if your portfolio dollar-cost averaged into the Strategy during the reporting period.

The firm maintains a complete list and description of composites, which is available upon request. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. The composite policy requires the temporary removal of any portfolio incurring a client-initiated significant cash inflow or outflow of at least 15% of portfolio assets. The temporary removal of such an account occurs at the beginning of the month in which the significant cash flow occurs and the account re-enters the composite at the beginning of the month which follows the cash flow by at least 30 days. Additional information regarding the treatment of significant cash flows is available upon request.

Brookmont Capital Management claims compliance with the Global Investment Performance Standards (GIPS®). To receive a complete list and description of Brookmont's composites and a presentation that adheres to GIPS standards, please contact Suzie Begando at 214-953-0190 or write Brookmont Capital Management, 5950 Berkshire Lane, Suite 1420, Dallas, TX 75225.

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