Capital

2024 Annual Letter

CapitalAlphabet, LLC

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Alphabet

Risk means more things can happen than will happen.
*   - Elroy Dimson*

The S&P 500 Index(SPY), undoubtedly the most widely used index of stock market was up around 25% in 2024, once again dominated by the 'Magnificent Seven' – Alphabet, Amazon, Apple, Meta, Microsoft, Nvidia, and Tesla. SPY index delivered one of its strongest two-year periods since 1997-98. My unease surrounding the lofty valuations of the MAG7 companies persisted throughout the previous year, prompting me to reduce our stake in Meta. To date, this caution has been unnecessary. By previous standards, the present level of MAG7 security prices contains a substantial speculative component with a corresponding risk of loss. Perhaps other standards of valuations are evolving which will permanently replace the old standard. I don't think so. I may very well be wrong. However, I would rather sustain the penalties resulting from over-conservatism than face the consequences of error, perhaps with permanent capital loss, driven by "New Era" mindset where trees really do grow to sky, has led to surge in optimism, potentially overshadowing the inherent challenges and limitations that inevitable accompany rapid technological advancement.

While I neither predict market trends nor attempt to time the market, I'm optimistic about the current environment. Expected returns over the next decade are projected to be within the 3-6% range, creating a favorable landscape for identifying significantly undervalued securities, it's crucial to remember that these returns won't be evenly distributed. As you all know, equity markets are inherently volatile, and I anticipate a decade marked by significant ups and downs, a true test of skill for stock pickers who can thrive in the midst of uncertainty.

My primary goal as portfolio manager is to achieve a long-term performance record that consistently exceeds comparable indexes. Without superior performance, there's no reason for these funds(SMA's) to exist. However, this outperformance shouldn't be expected to be constant. If we achieve an excellent track record, it likely means we significantly outperform during stable or declining markets and perform at or slightly below average when markets surge.

I would consider a year in which we decline by 15%, while the average declines by 30%, a far superior result compared to a year when both the average and our portfolio rise by 20%. Over a period of time there are going to be good and bad years; there is nothing to be gained by getting enthused or depressed about the sequence in which they occur.

The above dose of philosophy is being dispensed and will be repeated every year as I want to make sure our new partners understand my objectives, my measure of attainment of these objectives, and some of my known limitations.

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2024 Performance

There has been emphasis in our letters on a suggested standard of performance involving relatively good results in periods of declining or level prices but relatively unimpressive results in rapidly rising markets. We were fortunate to achieve reasonably good results in 2024 without relying on the high-flying performance of MAG7 stocks, We achieved a net gain of 26.57%. It's important to understand that outperforming the market or even generating positive returns cannot be expected every year or reporting period.

We take concentrated positions, typically holding only 5 to 10 stocks within our portfolio. Partners should understand that even with our highest-conviction investments, this concentrated approach means there will be periods of volatility. Additionally, many of our investments are unconventional, and we cannot predict when mr. market sentiment will align with our valuations.

CapitalAlphabet Performance vs. the S&P 500

Year	Portfolio Gain	S&P 500 Gain
2022*	29.91%	-6.69%
2023	28.88%	26.19%
2024	26.57%	24.89%
Cumulative Return	111.92%	47.04%
100k invested at start will be	$211,920	$147,040

*CapitalAlphabet started in June 2022
Note: These represent CapitalAlphabet's time-weighted net results (after expenses, but before management fees). Client net results depend on their specific fee agreements.

Our Method of Operation

Our avenues of investment break down into two categories. These categories have different behavior characteristics, and the way our money is divided among them will have an important effect on our results, relative to the SPY in any given year. The actual percentage division among categories is to some degree planned, but to a great extent, accidental, based upon available factors.

The first category consists of generally undervalues securities. This has been our largest category of investment, We usually have fairly large positions (5% - 20% of total assets) in each of five or six securities, with smaller positions in another ten or fifteen. Some of these work out very fast like Meta and others many times take years. It is difficult at the time of purchase to know any specific reason why they should appreciate in price. Before making any of these securities into large positions we looks for these qualities, Good and understandable business, Hight return on capital employed , run by trusted management with good margin of safety.

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For other small positions, we are looking to obtain a lot of value for the price paid, from companies generating high free cash flows, which are then used for dividends or share repurchases. We will reduce these securities going forward as our timing of purchases has been considerably better than our timing of sales. Analyzing our past two and a half years of results has highlighted my limitations quite clearly. Here are our bottom performers over the years.

Company Name	Attribution
Gear Energy	-1.78%
SIRI	-1.51%

On the topic of bottom performers, here is what I wrote in the last year letter..
I get very excited when I find companies trading at 3-4 times current free cash flow per share and keep forgetting that these commodity companies fate relies on external factors like commodity prices and global trends. I always treat them as work-outs but if they are not working out as expected then I need to abandon the strategy of 20% work-outs and just invest in good businesses.
Gear was a roughly 2% position in our fund when I last discussed it. While management finally secured a buyer for their oil assets, the sale price fell short of initial expectations. However, I believe there's still value to be extracted from this corporate event. By acquiring Gear at a discount to the cash proceeds we will receive, and by holding onto shares of the newly formed company (NewCo), I anticipate generating some return. However, this outcome falls short of our initial aspirations and, when considering risk-adjusted returns, I would categorize it as unfavorable.

SIRI is a new purchase this year. We acquired it as we reduced exposure to other high-flying stocks, which negatively impacted our 2024 performance by at least 3%. However, I believe SIRI has the potential to deliver strong performance over the coming years, Hope we didn't cut flowers and waster the weeds.

If the aforementioned under performers failed to provide sufficient evidence, the following top performers over our fund life, unequivocally demonstrated my strengths. The logical course of action is to repeat whatever works for us.

Company Name	Attribution
Naspers	39.90%
Bank of America	38.70%
META	16.93%

Our second category consists of "work-outs". These are securities whose financial results depend on corporate action rather than supply and demand factors created by buyers and sellers of securities. For instance, as previously discussed, GEAR, following the announcement of a corporate event with a predictable timeline, allowed us to estimate, with reasonable accuracy, the

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timing and amount of expected cash proceeds. Corporate events such as mergers, liquidations, reorganizations, spin-offs etc. An important source in recent years has been in ignored oil sector, mergers and sell-outs between various oil producers.

This category will produce reasonably stable earnings from year to year, we will look extremely good if it turns out to be a declining year for the general market or quite bad if it is a strongly advancing like past two years. While it would be very nice to be 100% in generals in advancing markets and 100% in work-outs in declining markets, I make no attempt to guess the course of the stock market in such a manner. We consider both these categories to be good businesses on a long-term basis, although their short-term price behavior characteristics differ substantially in various markets.

We'll track our annual performance against the S&P 500 as a benchmark, but our true focus is maximizing long-term portfolio value. This approach encourages prudence – avoiding market fads or simply indexing to collect fees like many funds do. My commitment to long-term thinking will be our north star. Our net assets at the beginning of 2025 amounted to $1,600,000. All my retirement savings are invested in this fund and I intend to maintain these positions for the next 25 years, until IRA distributions begin. This directly aligns my incentives with those of our investors – we're truly 'eating our own cooking'. The minimum investment for new investors last year was $25,000. I am considering increasing this threshold this year. As we attract more investors from outside Texas, we may need to register in those states, which would significantly increase our administrative burden.

I believe transparency is key in money management. Investors and managers should have a shared understanding of goals, performance metrics, timelines, and the processes involved. My goal is to ensure my clients feel confident in my decision-making and understand our mutual objectives. We only invite investors aligned with our goals, strategy, risk tolerance and who feel we are making rational decisions. This ensures mutual understanding and a strong foundation for a successful partnership.

Cordially,

Venu G. Vallabhaneni