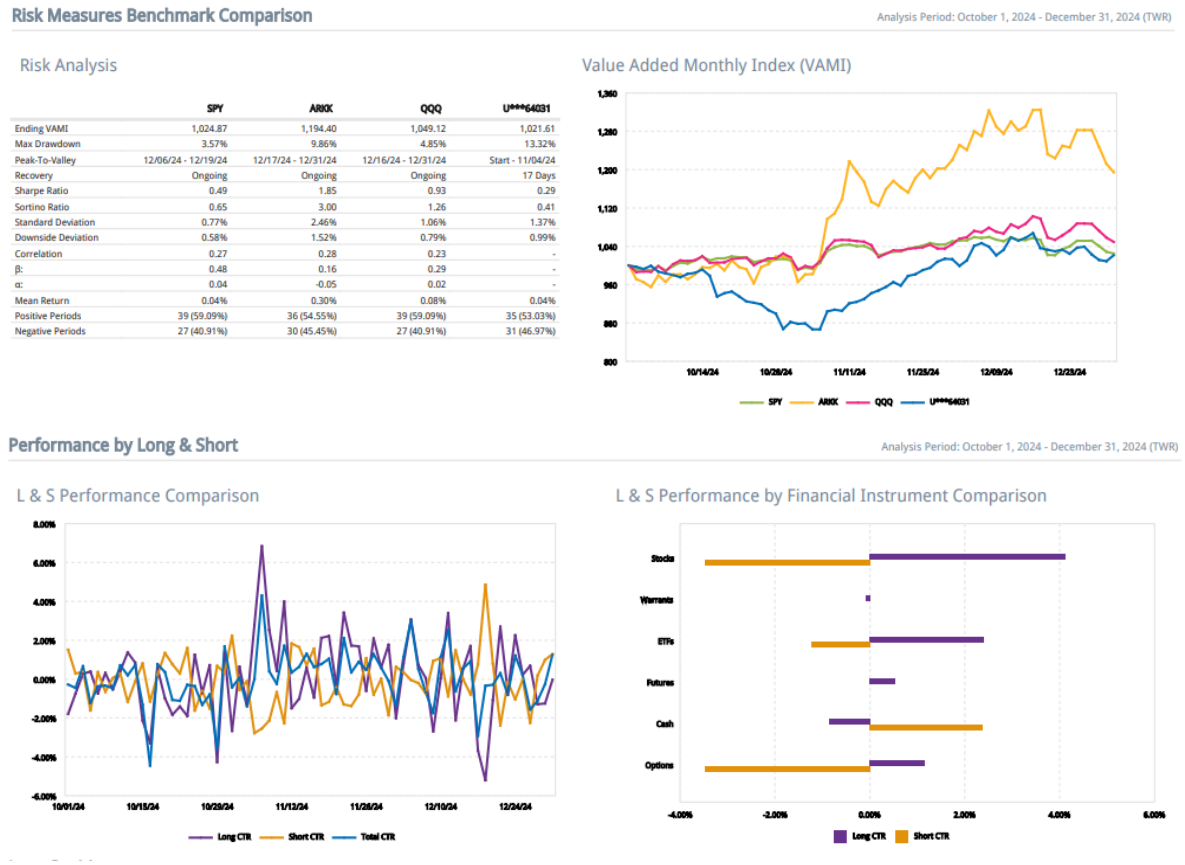
Reflections on the fourth quarter of 2024 and into 2025

Link for all Letters

Last quarter was marked by the election and the action around it. Broad indexes went up on the quarter, SPX up 2.5%, QQQ up almost 5%, IJH flat and ARKK up a whopping 19% (30% at some point) on top of 8% in Q3, however European indexes went down, and they went down A LOT measured in USD (FEZ down 10%). The word for this is dispersion, under the hood there was a massive speculative mania that pushed crazy/story/locura stocks up beyond what seemed imaginable. That made me suffer a little on the short side, since I avoid memes and crowded shorts until those have blown up a few people, it wasn't too bad.

The underperformance can be explained by my terrible month of October, which was due to two events that I will touch on later.



	SPY	ARKK	QQQ	U***64031
Ending VAMI	1,024.87	1,194.40	1,049.12	1,021.61
Max Drawdown	3.57%	9.86%	4.85%	13.32%
Peak-To-Valley	12/06/24 - 12/19/24	12/17/24 - 12/31/24	12/16/24 - 12/31/24	Start - 11/04/24
Recovery	Ongoing	Ongoing	Ongoing	17 Days
Sharpe Ratio	0.49	1.85	0.93	0.29
Sortino Ratio	0.65	3.00	1.26	0.41
Standard Deviation	0.77%	2.46%	1.06%	1.37%
Downside Deviation	0.58%	1.52%	0.79%	0.99%
Correlation	0.27	0.28	0.23	-
β:	0.48	0.16	0.29	-
α:	0.04	-0.05	0.02	-
Mean Return	0.04%	0.30%	0.08%	0.04%
Positive Periods	39 (59.09%)	36 (54.55%)	39 (59.09%)	35 (53.03%)
Negative Periods	27 (40.91%)	30 (45.45%)	27 (40.91%)	31 (46.97%)

I find **banks interesting again**, since KRE has given up most of the Trump victory gains, things like CUBI, PFBC and several OTC banks should provide a decent return in a few months (of course to really make money, we should focus on what the next quantum-like fever gonna be).

I made the mistake of **selling Applovin too soon**, I personally didn't expect it would become a PLTR like meme stock, but the lesson is always there, always wait until it is not just at a fair price, wait until it is egregiously expensive. I also made the mistake of being long tankers into Q4, a position I exited when the usual seasonality in rates didn't appear to be happening.

A position that did work was CIEN, finally the telco cycle bottom was apparent and the excitement about the datacenter has taken over.

The October meltdown:

I was long **Digital Value** in Italy, after the stock got unhalted I dumped my position and that was a 3.5% headwind on the quarter. TLDR was that the CEO (The CEO and founder nonetheless, instead of using a minion like proper criminals) was arrested giving an envelope with 30k in euros to an official in charge of the public contracts the company was opting to…

The CEO resigned and the CFO that had left the company a few months before, came back in.

The company opened down 80%, and although it was well below book value and half the business is with the private sector I did not want to own a stock that had a CEO bribing government officials. The worst case scenario was/is that the accounting could even be fraudulent, with public contracts inflated and that money funneled to the private side of the business (which is profitable as a segment, but what can you trust when punched in the face with such behaviour).

The stock has rallied quite a bit and some people are pointing to a legislative change regarding the legality of long term wiretaps. In any case, I am not going to find an edge in betting how bad the consequences are going to be, thus exiting the position and not looking back.

As for the lessons, in all honesty I cannot see anything that could prepare you or make you avoid such a situation. The company was well regarded, feedback was positive, some directives even graduated to Cellnex, the CEO was the main owner of the company, not a recent IPO.

I think this is one of those outlier events that hit you every number of years and the reason no position should be above 10% of the portfolio.

The second event in October was being long **TMDX into the third quarter results**. I knew they were probably not going to be stellar, as management had guided for a slow third quarter (however, previous soft guides had been met with massive beats, so not a history of management being conservative you could rely on) but also the third quarter is seasonal for

transplants and they are at a level in liver transplants as percentage of the total market of circa 30%, so general transplant volumes are more likely to affect the company.

The results were incredibly bad, a total growth stall with a guide for the fourth quarter (subsequently lowered - plus replacing the CFO) that didn't point to a quick recovery.

At this point one has to wonder if the DCD donor pool has reached a limit or maybe the OCS (Transmedics' machine) is no longer cost effective for the marginal transplants. I do believe they will own a part of the heart and liver markets because TMDX is enabling transplants there that would not take place otherwise, but we might have reached a ceiling in total transplant number.

I exited after the quarter. The stock has kept going down and it is one of the most shorted stocks. I might play it again if I feel the risk reward is favourable. This kind of flexibility should be expected for every position. Even if you look stupid for selling/buying, there is plenty of eyebrow raising stuff that one has to look through when investing. I am never going to forget the CEO of Applovin selling all his Class A shares at $10 per share in 2022.

The main mistake was bringing the weight to ~9% of the portfolio before the results, which was due to my bias of deeply knowing the company and the past success of the shares in the past. The lesson is not putting such big weights on companies that are not showing good momentum and avoiding the mentioned biases.

Despite beating the SPX in 2024 I am not quite happy with my 2024 performance (around 41%), I feel I made some easy to fix mistakes and I was run over by many ill timed/thought shorts during the year. I hope to improve in those aspects in 2025.

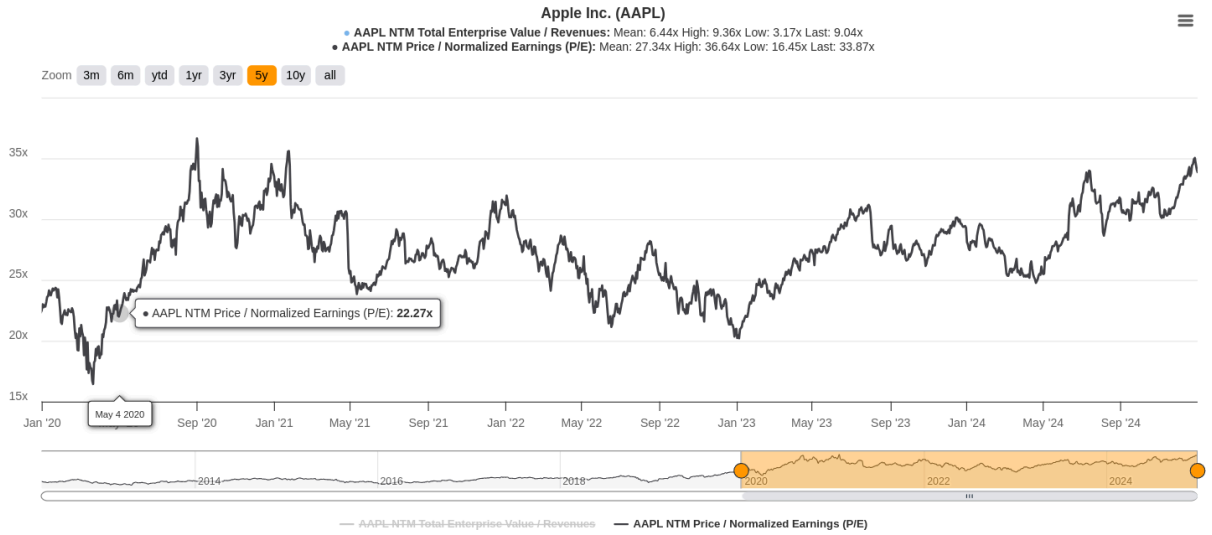
PS: Is the market expensive?

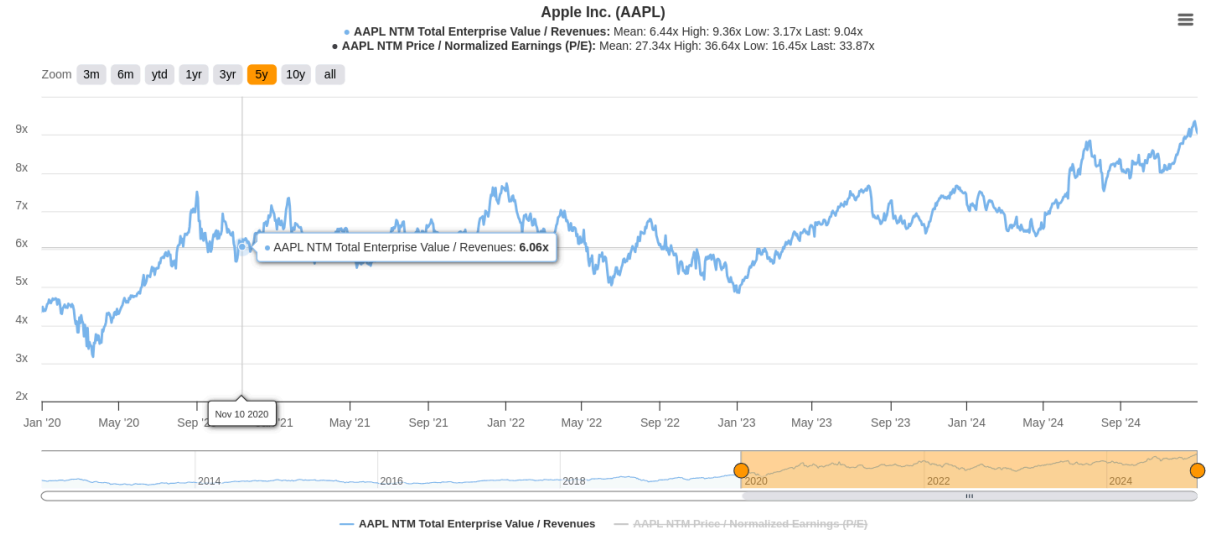
I see a lot of chatter around the market being at “super high PE”, “in a 90s environment” or “biggest % of world markets in history”. I understand ROIC and sector weightings have to be taken into account when making historical comparisons, so historical charts might not be entirely apples to apples.

I am a value investor, so I am going to perform a small exercise inspired on Prelude to Foundation when Hari Seldon realizes that he could try to develop psychohistory using Trantor itself, because using the whole galaxy was impossible due to the vast amount of inputs.

Let’s take the 7 biggest weightings in the SPX500 (which account for more than 31% of the index) and see if they are cheap or expensive, since taking a look at all 500 holdings is not feasible.

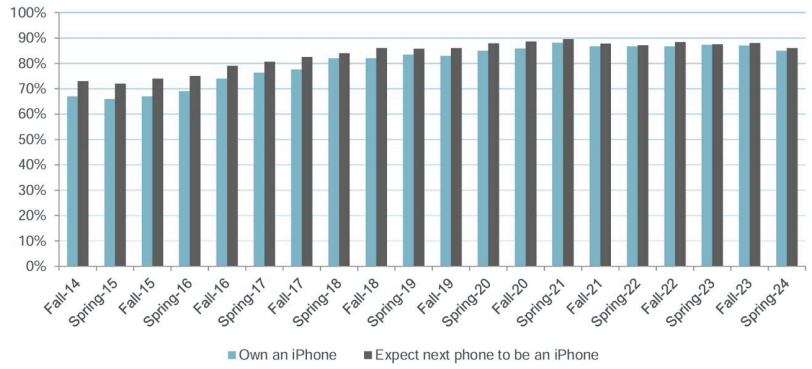
AAPL





Super solid company, clearly on the higher range of the last 5 years on P/E (2021 extreme, when long bonds gave 1%)

Super solid company that buys back 3% of shares every year. They do own the phone market and their grip on the younger generations make it that they will probably keep owning it for years to come.

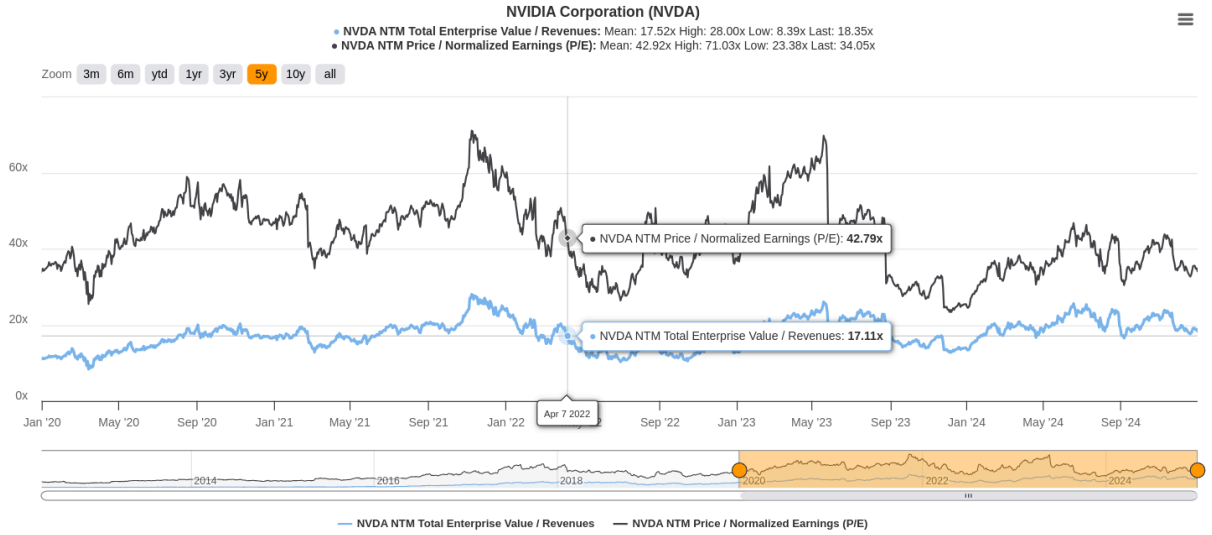


That's a brand moat as big as they make it but at 3% FCF yield and the risk that they lose the GOOG ~~ransom~~ payments for Safari's default search engine is probably a bit rich. If the market decides to rerate it to a P/E of 20 it would take 4 years of digestions if we assume profits grow at 7% and everything goes to buybacks.

NVDA

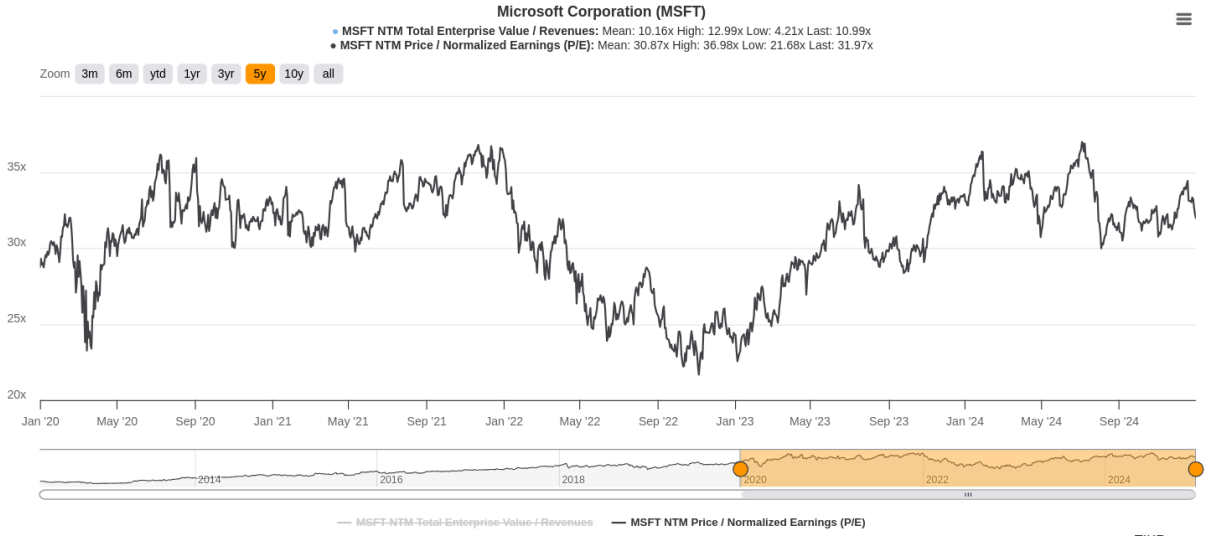
This is a growth story at a scale that we have never seen. The point is not on the multiple but on the sustainability of revenues and margins. Have we seen a cyclical buildup that will meet a slump at some point? Given the software advantage and how NVDA seems to making strides into automation and their own AI models I would probably buy that dip if it ever happens, but the question still lingers.

(112% revenue growth expected for NTM)

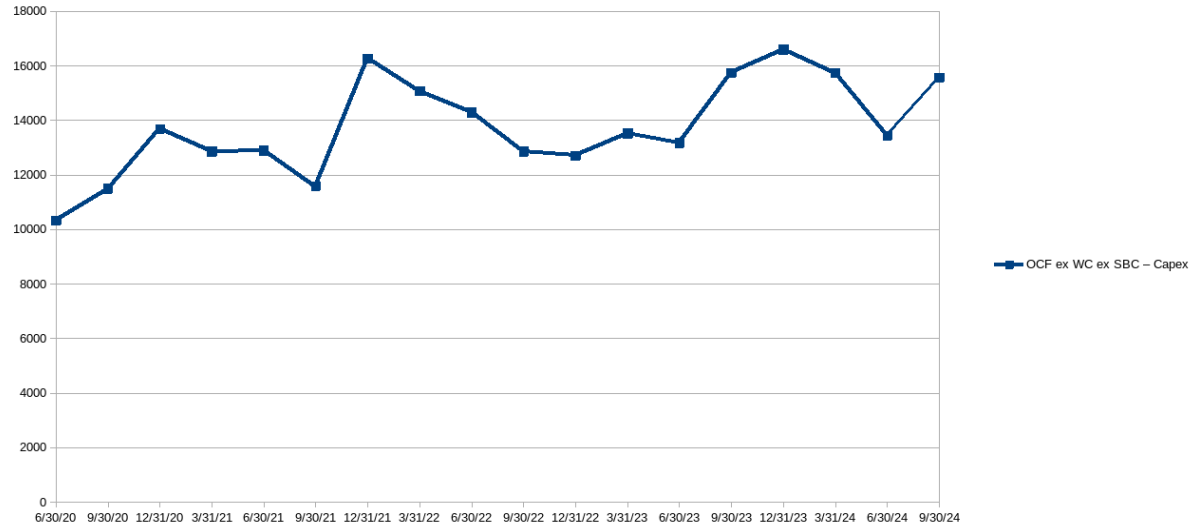


MSFT

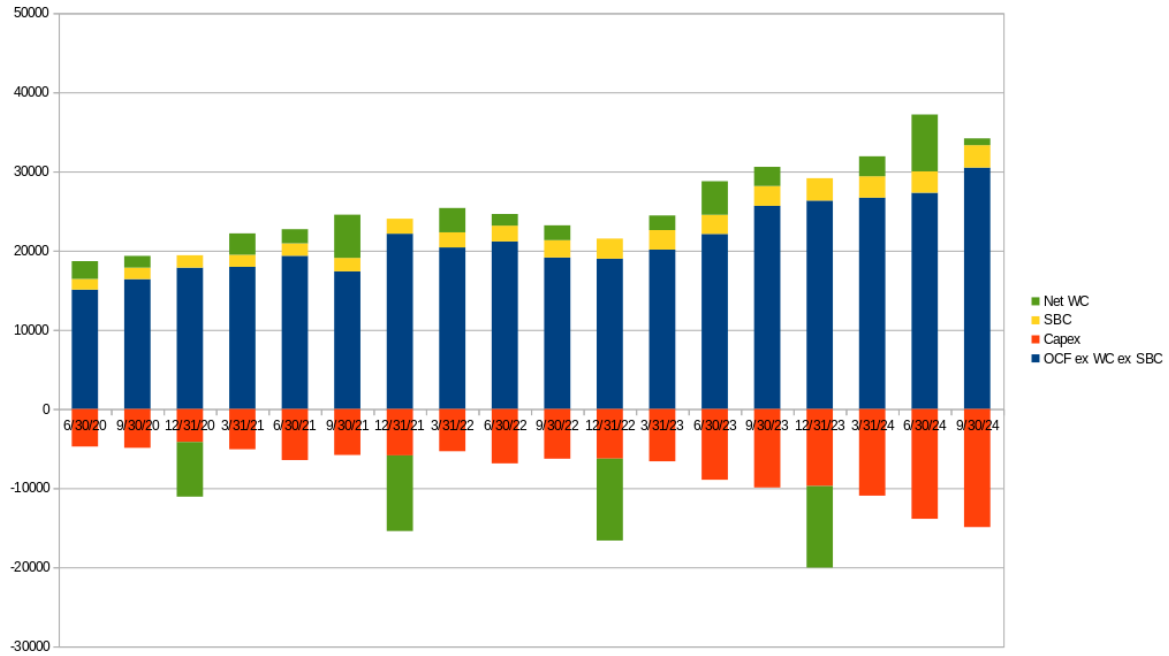
Back to the covid valuation range. Teens growth for income expected in perpetuity.



Not terrible for the SaaS king of the enterprise. It still surprises me when I see cashflow ex working capital ex SBC flattish for the last 3 years.

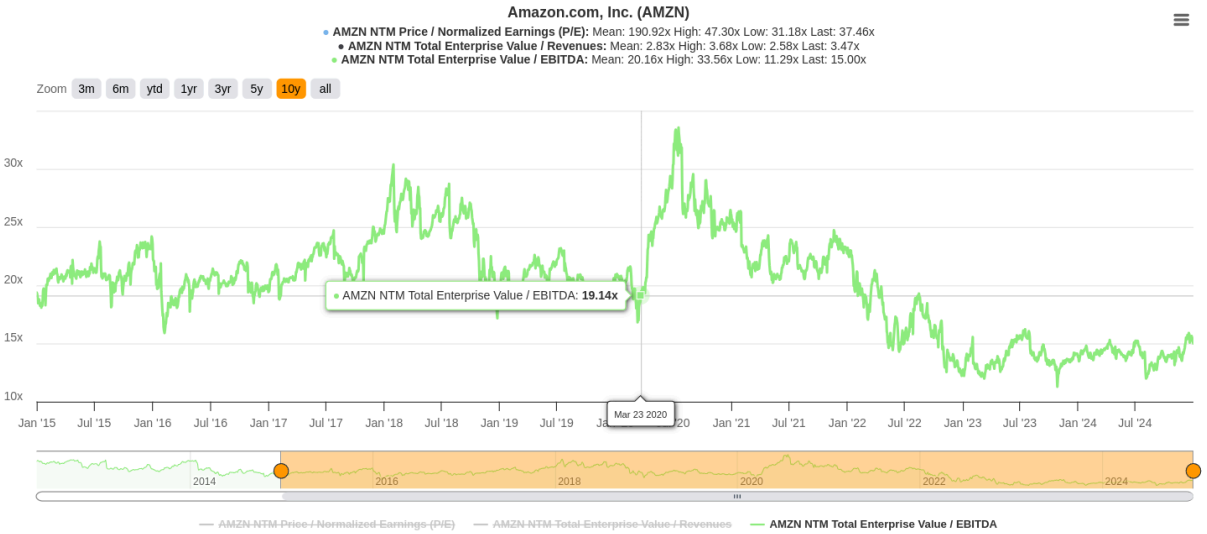


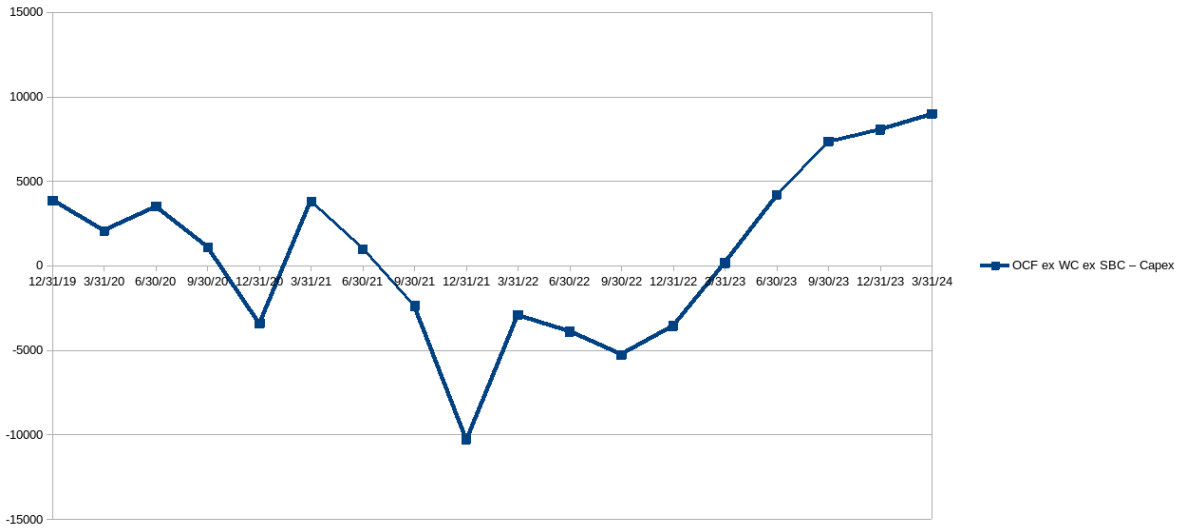
As you can see, it is mostly because of the capex push. As to wonder where all that money is going, check the NVDA growth rate. Some people are arguing that MSFT might go FCF 0 in their push for AI. I have no idea, but it is certain that we need those AI dollars to come back to the top line.



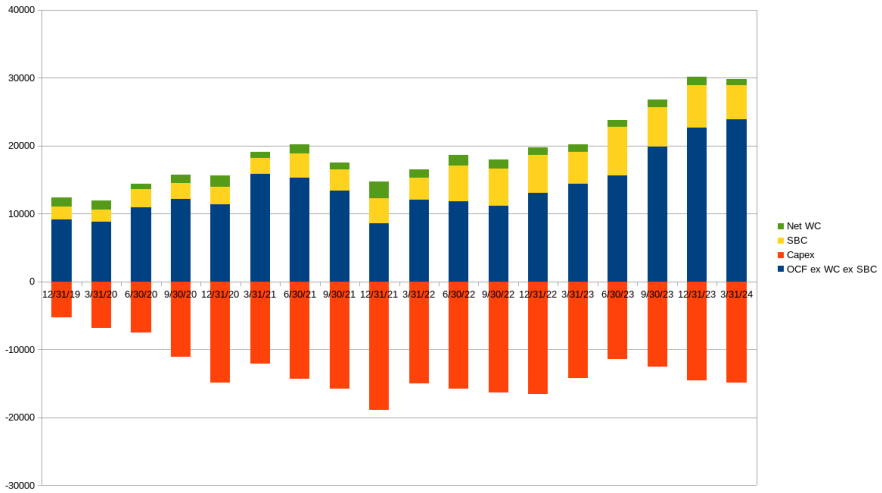
AMZN

I am going to be honest, I don't know how to value AMZN, certainly not on FCF metrics.





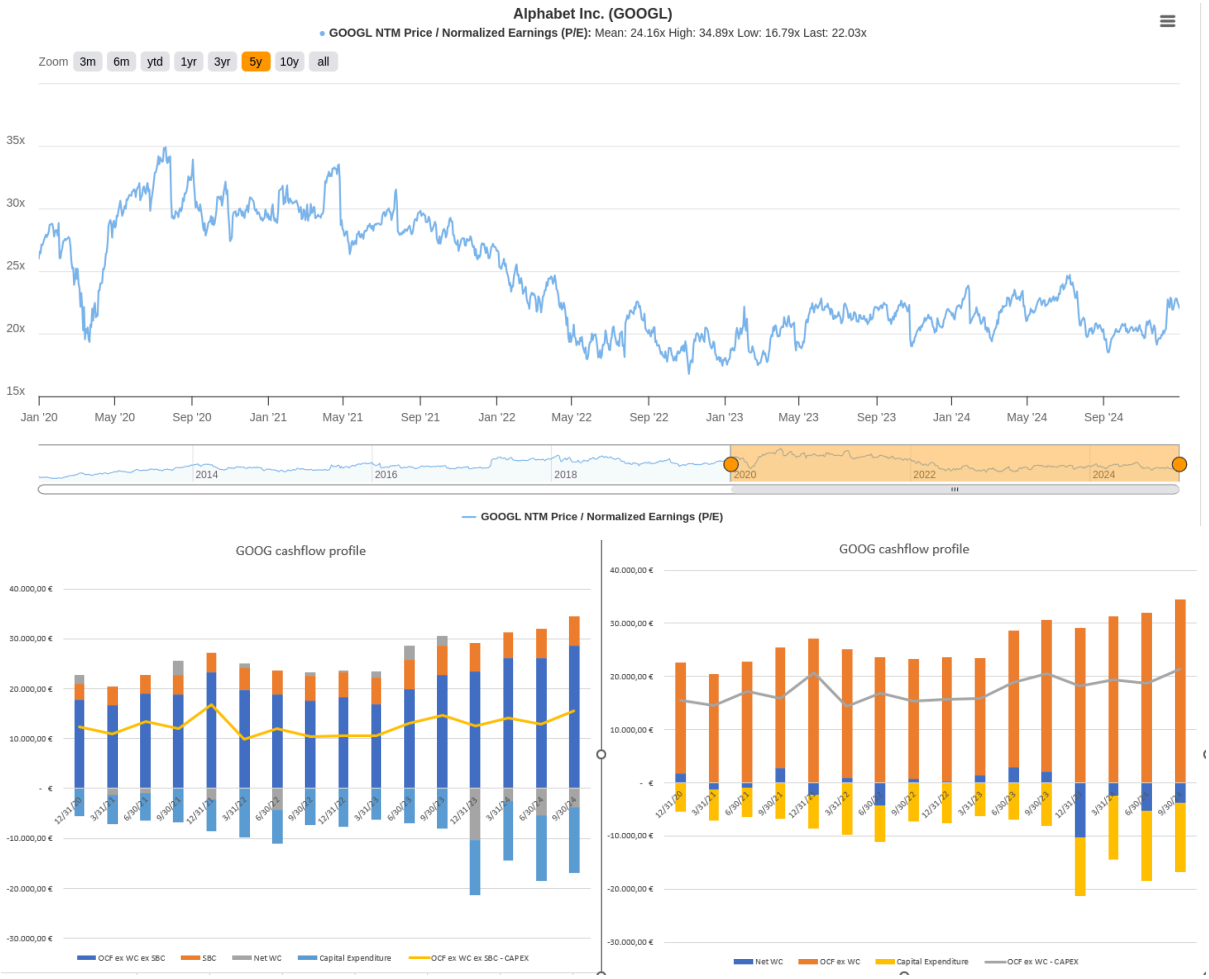
However OCF seems to be going up, and I guess that's enough for it to make it work.



Obviously it is all about AWS and the 3P marketplace not falling apart while they monetize it with ads. I am not sure how it is in the US, but in Spain Amazon just works right when it comes to ecommerce. AWS is profiling itself as a low cost provider of AI loads with a not perfect but cost effective Trainum chip. We see some capex increase but nothing major.

GOOG

Eerily similar to MSFT on cashflow but it's at 2022 multiples. Similar growth estimates.

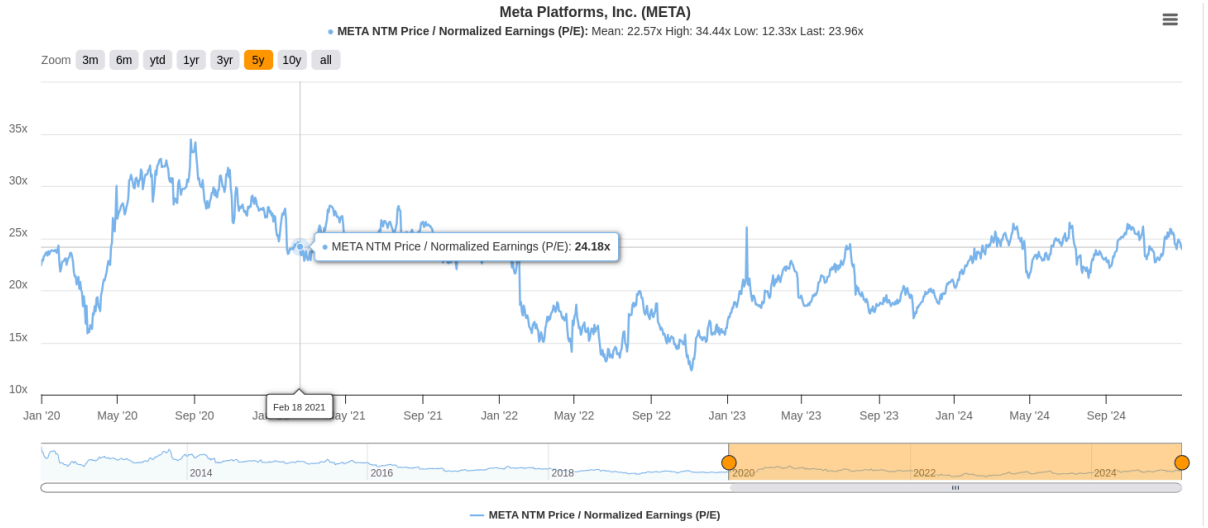


That capex better pay off, one could argue that GOOG has some advantage with their own silicon and the inhouse of their own OpenAI project, Waymo (It's actually happening) and quantum computers (I'll take anything at this point).

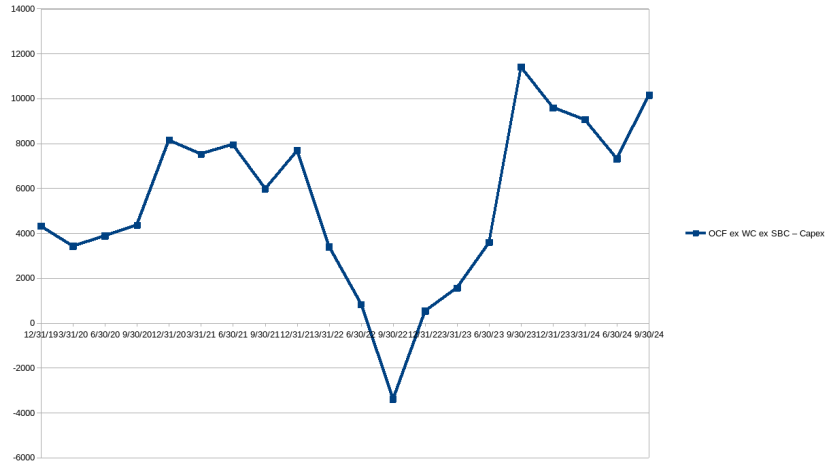
AI chatbots could be treat to search, or at least the massive gross margins of GOOG as the AI query is more expensive, even if it is Gemini answering what's the best restaurant in Manhattan, it'll be more expensive.

META

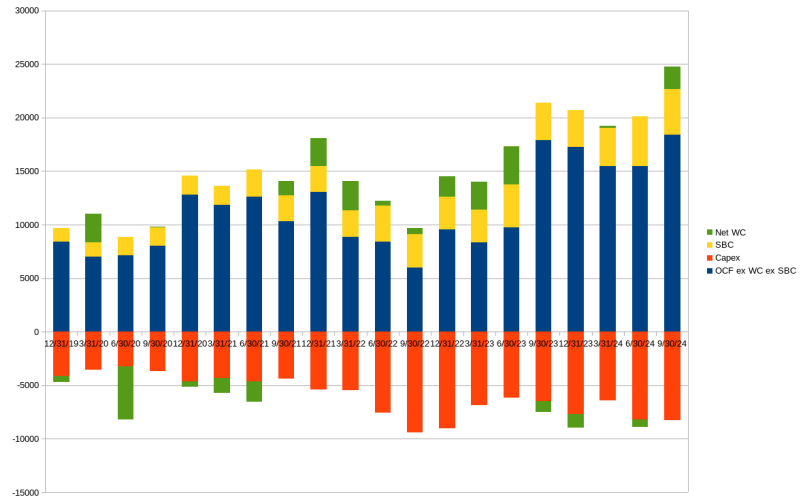
This one is more expensive than GOOG, but growth is expected to be a little bit higher.



Cashflow is a bit more muddy.



I guess the market likes this AI capex more than they liked the Metaverse bump in 2022.



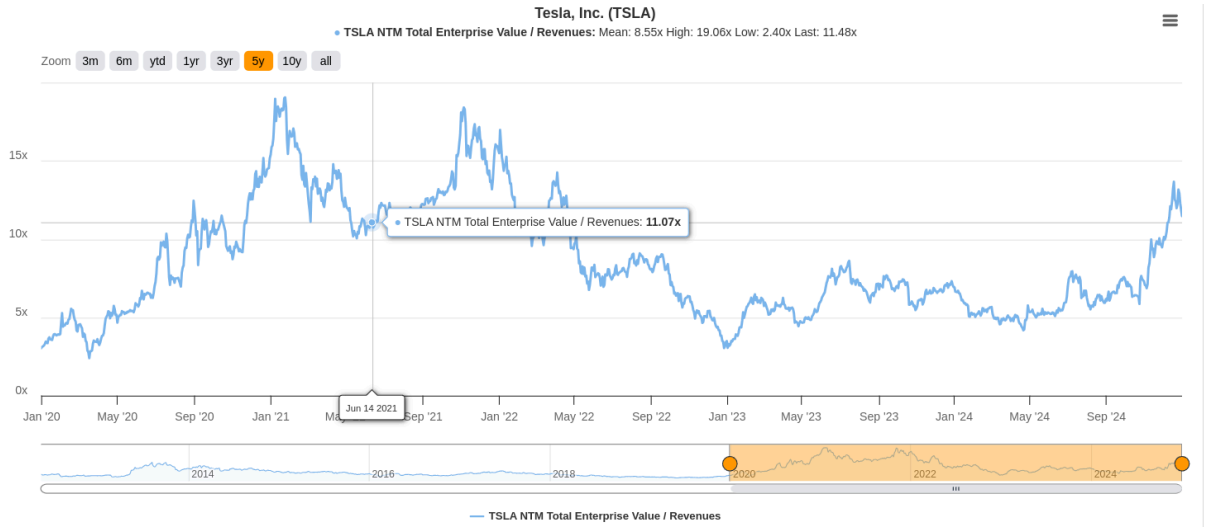
Not egregious, but as you can see more cyclical than the others. A lot of new capex eating all the increased OCF.

TSLA

If I have no idea about AMZN, don't ask about TSLA.

It is clearly (not?) only a carmarker. Full Self Driving, Optimus… I guess FSD is what got people excited here. Must is Trump's bestie now, but lifespan around Trump is short.

FSD is clearly not working now, but people are ready to believe it's close.



At the end of the day they make cars, sell some batteries, sell green credits and trades at x10 revenues.

CONCLUSION

As we've seen, some players that are reasonable on earnings need AI capex to pay off. I guess the worst case is that it doesn't work and they cut/rationalize a bit more, in that case NVDA would sell off.

We could see increased capex in search of a digital god, and NVDA will keep growing while distributable FCF goes down. Keep in mind that the actual depreciation cycle of those data centers might be shorter than the 4, 5 or 6 years big tech is using for amortization. Hard to say what would happen to the stocks, but I doubt the companies would go to 0 FCF without the support of the market.

AAPL is really expensive, but I thought the same 1 year ago. The others need the cycle (ads) and AI capex to work to be reasonably priced here. If anything fails we could see some stress.

I would say that some are really expensive AAPL/MSFT and some are uncertain NVDA/MSFT. AMZN will work as long as numbers go up, same with META. GOOG will go from excitement over Waymo/Quantum to fear what AI can do to search. All are more expensive today than one year ago. I wouldn't bet against them, but if something fails we could see them underperforming the market, and risks are mounting with that AI Capex.

Thanks for reading.
Rodrigo.

YTD figures

Risk Measures Benchmark Comparison

Analysis Period: January 1, 2024 - December 31, 2024 (TWR)

Risk Analysis

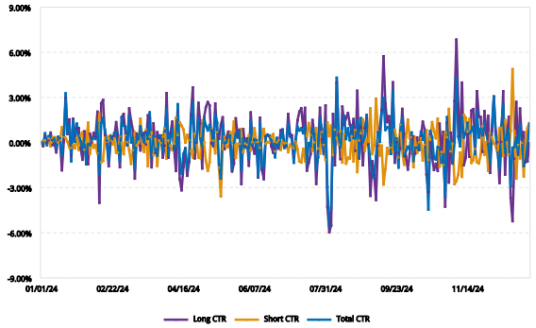
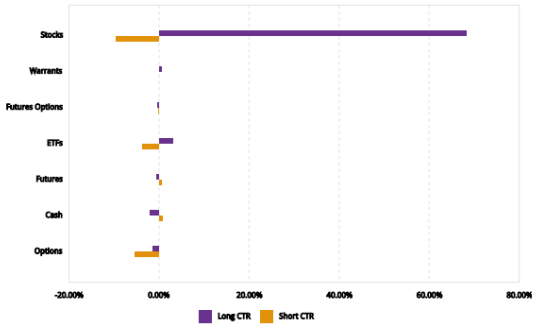
	SPY	ARKK	QQQ	U***64031
Ending VAMI	1,248.85	1,084.02	1,255.76	1,426.17
Max Drawdown	8.41%	24.63%	13.56%	14.58%
Peak-To-Valley	07/16/24 - 08/05/24	Start - 08/07/24	07/10/24 - 08/07/24	09/26/24 - 11/04/24
Recovery	33 Days	66 Days	65 Days	22 Days
Sharpe Ratio	1.43	0.26	1.08	1.58
Sortino Ratio	2.04	0.37	1.51	2.26
Standard Deviation	0.78%	2.21%	1.11%	1.27%
Downside Deviation	0.54%	1.56%	0.79%	0.89%
Correlation	0.50	0.39	0.45	-
β:	0.83	0.22	0.52	-
α:	0.18	0.30	0.22	-
Tracking Error	1.11%	2.08%	1.25%	-
Information Ratio	16.03	16.46	13.61	-
Turnover	-	-	-	1,315.61%
Mean Return	0.09%	0.06%	0.09%	0.14%
Positive Periods	159 (60.69%)	142 (54.20%)	158 (60.31%)	160 (61.07%)
Negative Periods	103 (39.31%)	120 (45.80%)	104 (39.69%)	102 (38.93%)

Value Added Monthly Index (VAMI)

Performance by Long & Short

Analysis Period: January 1, 2024 - December 31, 2024 (TWR)

L & S Performance Comparison



L & S Performance by Financial Instrument Comparison