SUMMITRY

Summitry Select Portfolio Update – Q4 2024

	Q4'24	1 YR	3 YR*	5 YR*	INCEPTION*
Summitry Select, gross	8.2%	31.8%	---	---	13.2%
Summitry Select, net[2]	8.0%	30.8%	---	---	12.6%
S&P 500 TR	2.4%	25.0%	---	---	11.2%

*Annualized. Strategy inception, 1/31/2022.

Note: An investor's actual performance may differ from the performance information presented due to, among other factors, alternative fee schedules, capital contributions and withdrawals.

1/13/25

The fourth quarter of 2024 capped off a second consecutive year of exceptionally strong returns for our portfolio. The Summitry Select Composite appreciated +8.2% (+8.0%, net) during Q4 and ended the year up +31.8% (+30.8%, net). The Composite has returned +38.1% (+37.3%, net) annualized over the past 2 years and +13.2% (+12.6%, net) annualized since inception, nearly 3 years ago.

Last year was also a good one for the broader market, with the S&P 500 total return index ending the year up +25.0%. Returns for the index were driven by the "Magnificent 7" stocks (AAPL, AMZN, GOOGL, META, MSFT, NVDA, and TSLA), which accounted for 55% of the S&P 500 price return during 2024.[1] We own 4 of them (GOOG, META, AMZN, and MSFT), but we have also found opportunities in other areas of the market. Our best performers during 2024 were TSM and NFLX. Neither were members of the Magnificent 7, and TSM is not even a member of the S&P 500.

While we believe the aggregate value of the businesses in our portfolio increased during 2024, we also believe their share prices increased faster. As a result, we expect the prospective rate of return for our portfolio will be lower than we experienced over the past couple of years. However, the companies in our portfolio, and their return profiles, could look very different in the future. We purchase securities intending to hold them for many years, but we are also unafraid to make changes when warranted.

At the portfolio level, we continue to hold a sizeable cash balance that earns an acceptable rate of return while we search deliberately for new opportunities that meet our standards for quality and price.

Q4 Portfolio Activity

During the fourth quarter, we sold out of Netflix (NFLX) and Carmax (KMX).

[1] *J.P. Morgan Asset Management Guide to the Markets 1Q 2025*

- Netflix is an example of a company where we believe the stock price appreciated significantly more than our estimate of business value. We have no specific concerns about near-term business results, the company's competitive moat, or its management and strategic direction. The reason we decided to exit our position was solely because we were no longer confident the prospective rate of return on NFLX stock was sufficient to justify inclusion in a concentrated portfolio like Summitry Select.
- Carmax is a situation where business performance did not meet our expectations. Competition from new entrants like Carvana (CVNA) has disrupted the market for used cars in the United States and Carmax' business has not been as resilient as we expected. While KMX has many advantages based on their scale and wide geographic footprint, it appears these advantages may be less powerful as more vehicles are purchased online. We acknowledge that Carmax management may still be able to leverage the company's advantages to greater success in e-commerce vehicle sales, but we lost confidence that this is the most likely outcome.

We also purchased a new position in Starbucks (SBUX).

- Starbucks is facing near-term challenges due to competition and economic weakness in China and prior management missteps in North America. We believe the Starbucks brand and the habitual nature of coffee consumption provide a stable foundation for new management to turn around the company's results. The COVID-19 pandemic disrupted consumer behavior, altering daily routines and driving rapid growth in e-commerce and mobile ordering. Starbucks responded with a slew of operational changes that were necessary at the time, but many are no longer needed. In our opinion, previous management was too slow to adapt to the post-pandemic reality, and the result has been sub-par experiences for both customers and employees of the iconic coffee chain. We believe the Board's decision last fall to hire Brian Niccol as CEO will serve as the catalyst that returns Starbucks to consistent profitable growth. Niccol is no stranger to restaurant turnarounds, coming to Starbucks after a very successful stint running Chipotle Mexican Grill (CMG). We followed Niccol's playbook at Chipotle and are confident that his plan to simplify the Starbucks menu, improve operations, and restore the "third place" feel of the company's cafes will improve both growth and profitability. We do not expect the pace of improvement to be even, and it is likely we will experience setbacks along the way, but we are confident that Niccol is leading Starbucks in the right direction.

Investment Performance

During 2024, our best performers were TSMC (+92%), Netflix (+67% at exit), and Meta (+66%).

- TSMC (TSM) customers like Nvidia, Google, Amazon, and AMD continue to see robust demand for chips powering AI applications. We expect this dynamic to continue through 2025. While AI has captured much investor attention, TSMC is also poised to benefit from an upturn in demand for chips that power mobile phones and PCs, as replacement demand for those devices is set to improve, following several years of OEMs digesting demand pulled forward by the COVID-19 pandemic.

Meeting all this demand will require significant additional capital investment, but we expect TSMC's dominant position will continue to provide pricing power to protect the company's attractive margins and returns on invested capital. We could see geopolitics reemerge as a concern for TSMC in 2025, as the incoming Trump administration considers modifications to export controls, tariffs, and relations with China. For now, we continue to believe the rewards outweigh the risks, but this is a dynamic we monitor closely.

- During 2024, Netflix management's decision to crack down on password sharing continued to drive paid subscriber gains and higher profitability. The shares responded accordingly. Moreover, the company's forays into live sports and entertainment began showing signs of success, with positive implications for the company's nascent advertising offering. We have little doubt that Netflix is a great business with an outstanding management team, but as highlighted above, we are no longer confident the prospective rate of return on NFLX stock is sufficient to justify inclusion in a concentrated portfolio like Summitry Select.
- Sentiment around Meta (META) has come a long way since a terrible calendar 2022, when the shares lost nearly two thirds of their value. At the time, investors were concerned that competition from TikTok would impair Meta's social networks and CEO Mark Zuckerberg's plans to accelerate investment in unproven categories like the Metaverse would lead to lower earnings. However, Zuckerberg has since walked back his aggressive Metaverse plans. Additionally, Meta's AI investments have driven increased engagement on Facebook and Instagram, higher return on spend for advertising customers, and higher revenue despite continued competition from TikTok.

Our worst performers during 2024 were Ulta Beauty (-11%), Universal Music (-9%), and Agilent (-3%).

- Concerns about the health of Ulta Beauty's (ULTA) customer base and the impact of increasing competition on margins persisted through the end of 2024. However, there are reasons to be optimistic about the years ahead. We believe the beauty category is remarkably resilient and Ulta's unique business model continues to earn attractive margins, despite increased competition. There are already signs of improvement, as the company pre-announced that fourth quarter results are tracking ahead of expectations for both revenue growth and profitability thanks to a strong holiday shopping season. We expect 2025 will see less competitive intensity, as Sephora completes their roll out to Kohl's locations, and we are also encouraged by the appointment of Kecia Steelman as CEO last week. Steelman is an Ulta veteran with a successful track record improving store operations. We think Steelman will bring added urgency to improve store assortment, as one of her first tasks as CEO will be to hire a new Chief Merchandising Officer.
- Universal Music Group (UNVGY) sales growth during the first three quarters of 2024 was somewhat disappointing, as streaming revenue growth decelerated despite price increases by distributors like Spotify (SPOT). However, UMG's revenue from Spotify grew at a healthy double-digit rate, as price increases had little impact on churn. This bodes well for future revenue growth at UMG, since other streaming services are also likely to raise prices over time. We continue to believe that UMG retains

an exceptionally strong competitive position due to their leading market share, which allows the company to dictate favorable terms with music distributors for the benefit of the company and the artists it represents. Absent a change in this competitive dynamic, we are inclined to ride out occasional periods of underperformance such as we experienced this year.

- As we have discussed in previous letters, Agilent's (A) business has been negatively impacted by high interest rates, since customers typically finance expensive capital equipment purchases. While financing conditions improved modestly during 2024, the weakening economy in China, which accounts for roughly 20% of Agilent's annual revenue, has curbed investor enthusiasm. We continue to await an inflection in the company's larger North American capital equipment business that has been pressured not only by high interest rates, but also a tough funding environment for smaller biotech customers.

Concluding Thoughts

Last quarter, we noted that our crystal ball was particularly foggy, and this remains the case. We have an incoming Trump administration proposing broad tariffs and reevaluating a slew of government programs and regulations, while armed conflicts continue to roil the Middle East and Europe. Although we never claim to know for certain what we can expect in the future, we are confident that market volatility will create opportunities and patient investors that own good businesses at attractive prices will be rewarded. As always, thank you for placing your trust in us to search for those opportunities on your behalf. Please do not hesitate to reach out with any questions.

Sincerely,

The Summitry Select Team

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