MARKET LETTER

January 2022

As we look back on the year 2021, we are astounded at the consistent, steady climb to new all-time highs for the equity markets. In spite of the ongoing disruption of the global Covid-19 pandemic, equity investment returns were remarkably strong, especially when one considers the concentrated nature of the narrow market leadership since the beginning of this pandemic. In the last two years, the top 10 performers have driven over half of the cumulative return of the S&P500. This past year can best be summarized as one of significant speculation as investors largely brushed off concerns about the pandemic, increasingly high inflation, and massive supply chain disruptions to help drive the equity markets to new all-time highs. The stock market also experienced new, speculative drivers in 2021 as small retail investors (Redditors/Wall Street Bets) banded together to drive a buying frenzy in smaller stocks such as GameStop and AMC. In addition, SPAC's, "blank check" shell corporations designed to take companies public without going through the traditional IPO process, raised a whopping $162B in 2021 and options market activity hit the highest level since 1973. New investment vehicles/investors are typically healthy for markets and hopefully are not just byproducts of a frothy, long-in-the-tooth bull market. As we closed out this crazy 2021 year, the S&P500 had gained 26.9%, the Dow Jones Industrial Average gained 18.7% and the NASDAQ gained 21.4%. Many anxious investors remain fearful that we may have borrowed investor returns from the future with this robust equity performance in the midst of the ongoing pandemic. Alta Capital however remains encouraged by the strong economic environment that appears conducive to sustained growth in the post Covid-19 global economy.

In last year's letter, we stated that we "expect inflation to be of increasing importance to investors in 2021 and we anticipate interest rates to remain at or near their current historic low levels. Longer term however, we believe interest rates will likely begin to creep higher." This outlook continues to remain our view in 2022 as we anticipate continued inflation, largely driven by increasing wages and ongoing supply disruptions. The Consumer Price Index ended 2021 with inflation rising at the fastest pace since 1981. We anticipate the Federal Reserve will attempt to get inflation under control in 2022. Fed policy makers have indicated plans to increase the fed funds rate at least three times in 2022 to counter inflation. While higher interest rates can typically pressure equity valuations, we believe investors should not be too concerned just yet. In spite of these potential rate increases, interest rates in general remain historically low. Interest rates in 1981 were well over 10%, significantly distant from where they are currently.

We believe that the economic environment in 2022 will remain constructive for equities and once again offer investors the best investment option for the coming year. The U.S economy should continue to slowly recover from the pandemic and corporate earnings should continue to rebound, although year-over-year growth comparisons will become more challenging. Last year, we mentioned that the lion's share of the market's price appreciation during this pandemic can be attributed to Price/Earnings multiple expansion. This expansion of PE multiples may be sustainable in the short term, but is very unlikely to continue in the longer term. We anticipate that the majority of equity price movements in 2022 will once again be driven by traditional earnings growth and less so by additional multiple expansion. This earnings growth should help drive positive returns within the Alta Quality portfolios.

ALTA CAPITAL MANAGEMENT

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