RIVERPLACE · CAPITAL ·

23rd Anniversary

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WHY RIVERPLACE CAPITAL?

- Top Tier Financial Performance
- 100 Years Investment Experience
- Personalized Investing
- Individuality of Thought

NOTICE

Riverplace Capital welcomes referrals you make to us. It reflects the trust and confidence you have in our firm. We work very hard to give the best results possible given your needs, circumstances, and constraints. We will do so for anyone you may refer, and you can always be assured that we will respect your privacy.

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Written by Peter E. Bower, President.

the Lonely Bull

Separate from the herd of same-minded investment strategies

January 2022 A Quarterly Market Perspective by Riverplace Capital Number 94

Featured Sections

TALK WITH US

Everyone who has any study of economics understands that too much money chasing a given supply of goods causes prices to rise. Rising prices (inflation) cause interest rates to go higher, too. Afterall, why would investors lend money at rates less than the inflation rate? That would be tantamount to giving someone the use of your money and accepting less in buying power when it is returned.

Of course, our financial system is far more complex than this example, but these are the basic mechanisms. So why do we have low interest rates and rising inflation? Part of the answer may lie in the fact that the Federal Reserve has pumped so much money (liquidity) into our system that all of it is not looking for goods to purchase. Much of it may be saved. Banks have more money deposited than there is loan demand. They, along with many other entities and individuals, seek a return on these balances. So, they buy liquid Treasury bonds or others to put some of it to work. What does too much money chasing a limited supply of bonds do? Of course, it forces prices higher and yields lower.

The paradox is that with the injection of too much liquidity into our financial system, rates go down, even as inflation increases. Certainly, there may be other factors in setting interest rates, such as future economic growth expectations, fears of ongoing crises, and desire for some stability in outcomes. However, the current paradox seems to owe a lot to excess liquidity. The Federal Reserve is now in the process of reducing and eventually eliminating this excess. In time, interest rates should rise as supply and demand come into better balance. Then the economic relationships, as we have observed in the past, operate as expected.

We are happy to discuss this very interesting topic, ***Talk with Us.***

PERSPECTIVES

Last Year

Did this past year look easy? It wasn't. Even though investment returns are terrific, there was much to contend with in 2021. Firstly, there was a Greek alphabet of coronavirus variants raging around the world. Even though our federal government stepped up with tremendous fiscal support for the economy, recovery has been far from smooth. Then, there were the times when investors swooned because of fear of relapse. Another factor is the paradox of terrific liquidity and low interest rates, along with high inflation rates. (More about this in the *Talk with Us* section of this letter.) Additionally, bouts of volatility, seemingly coming out of nowhere, periodically unsettled investors – what fun!

After every pull-back, investors came back and continued to bid up stocks. Companies dealt with a myriad of challenges and kept producing excellent results. The consumer, with impressive resilience, kept buying. Government and industry produced miracles in the weapons against the pandemic. Investors took note and most stayed the course. The stock market set over 60 new highs.

After a whirlwind year, reflection provides much to be pleased about. Historically, last year's returns are outstanding. Thankfully, the market advance broadened out to include small, mid-size, and large companies, as well as growth and value ones. Of course, at the time nothing looked obvious. One concern after another kept popping up. At the end of the year, markets swooned again in response to the rapid spread of the Omicron variant of Covid-19.

Income and bonds continued to be a challenge for those needing a steady source of cash flow. That will continue to be the case for some time yet. Eventually, interest rates will rise, but will continue to take time. Thankfully, Riverplace Capital has put strategies in place to meet this need – so far so good.

After such a good year, and after several in a row, what can we expect now? Although no one can really know, our analysis indicates that we should remain optimistic. See the *Forecast* section for details.

> "If you aren't willing to own a stock for ten years, don't even think about owning it for ten minutes. Put together a portfolio of companies whose aggregate earnings march upward over the years, and so also will the portfolio's market value."
>
> *-Warren Buffet*

MAJOR INDICES

as of 12/31/2021

Large Cap Stocks (S&P 500)	**26.9**
Dow Jones Industrial Average	**18.7**
Mid Cap Stocks (S&P 400)	**23.2**
NASDAQ Composite	**21.4**
Small Cap Stocks (Russell 2000)	**13.7**
MSCI EAFE	**8.78**
Barclay Aggregated Credit Index	**-1.11**
Inflation	**6.8%**

Equity indices are 12-month returns excluding dividends.

FORECAST

Economy

GDP growth for 2021 is more than 5 percent. Depending upon final readings for the fourth quarter, it may be even higher. Nevertheless, this is a good rebound from the shut-down economy at the beginnings of the pandemic. Momentum going into 2022 is very strong. There is no reason to believe it will dissipate soon. American business has shown it can navigate the challenges of this environment quite well.

Supply chain challenges have been a persistent hindrance. These should gradually improve this year. In fact, they are already doing so. Cost pressures are also a concern. However, companies have been able to mitigate the impact of higher costs by raising their own prices and by finding more efficiencies within their operations. Automation is one immediate solution and can now be seen in a variety of services, not just in manufacturing. Have you ever sat down in a restaurant and placed your order through a kiosk at your table? How about parking in an automated garage? These are examples; expect more and more innovations in the future.

Equities

"Stocks are expensive." You hear this all the time. Historically, they are, but when taking into consideration the extremely low interest rates, then not so much. Many companies are also quickly growing into the expectations investors have placed on them. If one does not grow sufficiently, then investors punish the stock and quickly adjust the valuation downward. This is happening on a case-by-case basis.

Along with reassessments of individual prospects, investors are marking down the multiple they are willing to pay for future results. This is because they anticipate higher interest rates in the future. This is called P/E compression and is typical during rising rates. At the beginning of 2021, the P/E ratio of the S&P 500 ratio was 30. By the end of the year, it was under 24. Expect more of this.

Revenue growth for the S&P 500 is expected to be 7.3 percent and earning at 9 percent. All sectors are forecasted to grow. This is very encouraging and will further reduce the price/earnings ratio for the overall market. There is plenty of room for additional stock market gains. They are likely to be delivered with a hefty dose of volatility.

There continues to be a rotation of leadership in the stock market advance. Growth and value have swapped places several times this past year. This will probably continue in 2022.

Fixed Income

The Federal Reserve is now withdrawing its bond buying program. At the current pace, this program will end this coming spring. They have also signaled the market to expect 3 rate increases in 2022. This will be for Fed funds or the very short end of market maturities. All other rates should also begin rising. The extremely low rates prevalent today are not sustainable without massive Federal Reserve support.

We have predicted that interest rates should soon begin rising and will do so for years to come. The increases will not be smooth, but irregular and unpredictable, just like the stock market. Trends in interest rates last a very long time, even decades. The recent lows are historic. They should normalize over the next few years.

At the end of the year, interest rates declined again in fears that the Omicron coronavirus variant would slow the economy, another swoon. This is unlikely to last. We are all getting more adept at handling the waves of this pandemic. We also have many more tools to protect us from and fight this virus.

INVESTMENT STRATEGY

Equities

Riverplace Capital has been moving from an all-growth style to a more balanced approach for some time now. This has helped to smooth out the gyrations from one style to the other. Both have done well and should continue to. We may continue to add more value issues. We find more and more opportunity in this category.

No matter what style, patience will definitely be required. There are always scares that affect markets. It is reasonable to expect more in 2022. However, the underlying conditions still look positive for business.

Fixed Income

Short-term has been our mantra in managing fixed income assets for some time now. There will be no change in this stance, especially since we expect interest rates to irregularly climb for years to come.

Quality is paramount. There is too little improvement of yield in risky paper to warrant any investment. Also, we see fixed income assets as a means to reduce risk in a portfolio. Why introduce more? Risk and reward calculations are left to equity exposures.

Wealth Management

Riverplace Capital recently pulled back from emerging market exposures in asset allocation portfolios. China is an outsized part of these indices and portfolios. We now see Chinese assets as un-investable. No rule of law and a hostile government make for unacceptable risks.

Allocation to Europe and other developed markets, such as Japan and South Korea, have been increased. Valuations are much cheaper in these markets and recovery is taking place, just like in the U.S.; lots of opportunity. Other allocations remain the same.