Valara Capital Management, LLC

April 12, 2022

Dear Friend of Valara Capital Management,

For the first quarter, ended March 31, 2022, Valara Partners, LP. produced total returns, net of fees, of 10.82%, versus -4.60% for the S&P 500 index. Value, as a style, dominated growth and the S&P 500 and Valara led them all.

QUARTERLY REVIEW

Economic uncertainty rose dramatically in the first quarter. The positive of declining cases and deaths associated with Covid (Omicron), in the West, was swamped by a laundry list of negatives. At the start of the quarter, inflation, particularly in key commodities like oil, was the most prominent concern. This was significantly intensified with Russia's invasion of Ukraine in early March. Russia is an important supplier of a great number of essential commodities, particularly to Europe, and the West's severe sanctions/bans on Russia's exports pushed prices into overdrive. Oil, which started the year in the mid-$70's, rose to roughly $90, pre-invasion, and then promptly spiked to $140 a barrel, before easing back. Similar impacts were seen in various fertilizers, metals and food items. In addition to the significant price increases of key economic inputs, the enormous step up in geopolitical risk creates an important challenge to business decision makers and greatly exacerbates the already crippling impacts that Covid placed on supply chains. The economic press is now warning about supply shortages of daily use items and governors of several states have attempted to mute the impact of high energy prices by suspending taxes on gasoline. In the midst of all of this, economic projections have declined but the consensus is still expecting growth of roughly 3% for 2022. None of this (except possibly inflation) will help the "elephant in the room" problem of elevated debt levels, fiscal deficits and the potential erosion of the US dollar's global position.

The above uncertainty impacted markets, manifesting as lower stock and bond prices and greatly increased market volatility. The US 10-year Treasury yield has risen from approximately 1.50% at the end of last year to over 2.70 as I write this. The Federal Reserve has steadily raised expectations of future tightening as inflation has run out ahead of them. Currently, the market is pricing in over 200 basis points of additional rate increases this year. While US stock market volatility increased, with day-to-day swings of 1-3% becoming more common in the period, overall, stocks took the quarter's events remarkably in stride. China, Russia and those countries closest to the war in Ukraine generally suffered the most. China had the misfortune, after having had a relatively good experience with the early pandemic, of getting severely hit in Q1. Lockdowns were reinstituted with pronounced effects on their economy and markets. Russian investors were faced with a collapse and then remarkable rebound in the Ruble. The German stock market declined 13% as the third worst major market behind Russia and China.

PERFORMANCE COMMENTARY

Value put in a strong relative performance, but still declined 1.16% in the period. Growth was down 9.15% and the S&P, which is a blend of styles, fell in between at -4.91% (price only). Small cap stocks lagged large caps and bond credit spreads widened, which is typical in an environment of increasing perceived risk. The three worst sectors were all prominent growth components: Communication Services -11.5%, Consumer Discretionary -9.5% and Technology -8.6%. The leaders were Energy +37.7%, Gold Miners (not technically a sector) +19.7% and Utilities +4.0%.

Both sector weighting and individual stock selection were significant positives for Valara in the quarter. As you know, our large sector overweights have been in materials (largely gold miners) and energy, with modest overweights in industrials and financials. While all four sectors outperformed, both energy and gold miners were

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in the top three, as noted above. In terms of individual positions, Mosaic Co., up 69%, was our big winner in the quarter and we started with a position size of just under 7%. We had seven other positions that were up over 20%: Murphy Oil +55%, Baker Hughes +51%, NOV +45%, Archer Daniels +34%, Barrick Gold +29%, Newmont +28% and ConocoPhillips +27% (to our sale price). Of course, we also had laggards, which included Footlocker -34%, Mohawk -32% and GAP -20%. All of our noteworthy under performers, with the exception of Gilead and Viatris, were smaller positions.

With the numerous big moves in our portfolio, it will not be surprising that we did a fair amount of trading. As noted above, we sold out of our position in ConocoPhillips. We also sold out of Quest Diagnostics and Pfizer. We sold 85% of our position in Mosaic and reduced Murphy Oil, Archer-Daniels and Textron. In turn, we put the proceeds into new positions in Footlocker and TechnipFMC while adding to BorgWarner, GAP, Discovery, Viatris and Gilead, among others. With these repositioning actions we not only locked in performance from our big wins but were able to redeploy capital into names that significantly improve our expected future returns.

OUTLOOK

Despite the continued optimism of the consensus economist, the possibility of falling into recession increased in the quarter. In our last letter, I highlighted my belief that one was overdue and needed. It's ironic, in our nominally capitalistic society, that most people don't grasp that recessions are the forest fires of the economy – needed to clear out all the dead/dying wood and debris and promote growth of the strong and healthy. We are in an environment of unusually heightened ambiguity. There are myriad threats and challenges but also the expectation that the governmental and financial authorities will come to the rescue of markets and the economy, if required. While it is particularly difficult to predict the near term, I think that the current economic outlook is too positive. With inflation almost 8%, war in Europe, Covid in China, the Federal Reserve playing catch up and the yield curve bouncing around the flatline (inversion being a harbinger of recession), I lean in the direction of a weaker than expected outcome. I do believe that, if recession occurs, it will be different than recent experiences, in that it will be accompanied by some degree of inflation. In short, our basic opinion has not changed - we are late in an economic cycle which has been unusually micro-managed by the Federal Reserve and fiscal authorities.

The markets are replete with signals that suggest participants generally agree with this view - and have for some time. Many cyclical stocks plunged to new relative low prices during the Covid market collapse in the Spring of 2020 and have never really recovered. We have added several of these to our portfolio: Discovery, BorgWarner, Foot Locker, are examples. While we are not macro investors, and instead make our investment decisions based primarily on valuation, our portfolio has more cyclical exposure than one might expect given our more cautious economic outlook. When valuation is extreme trying to time the cycle becomes especially risky and difficult. Following the 2000 Technology stock bubble that ended in the 2001 recession, most cyclical stocks (value stocks) defied the economic trend and significantly outperformed. This may, or may not, happen if we enter recession in the near future. None the less, I wish our partners to understand that our cyclical exposure has been taken fully aware of what may come and with a strong opinion that the valuation opportunity is extreme.

Our basic strategy remains to evaluate each investment on its own intrinsic value and to stay disciplined on the price we pay and/or receive on sale - letting the market overreact and vacillate around us. We will stay true to our investment process. Thank you for you continued support and feel free to call or email with any questions or concerns.

Sincerely,

Robert W. Simmons, CFA
Principal