Pursuit of Normalcy

Following an exceedingly challenging 2022, it is worth reviewing the events that transpired to help us understand where we are headed. It is fair to say that given all the ambiguity, the markets will be cautious given the lingering concerns of the global economic outlook and underlying indicators targeting inflation.

Stating with conviction, what awaits investors in 2023 would be purely speculative. We all experienced a high level of optimism that everything would return to normal when pandemic restrictions were eased, and that inflation would recede back to levels prior to the pandemic. That was not the case. To name a few obstacles in 2022, globally we have faced and continue to face the Russian invasion of Ukraine, supply chain issues, and sustained inflationary challenges. In addition, the news of the Queen's death and protests in Iran and China have added to this "eventful" paradigm.

Throughout the past year, the markets reacted in anticipation as investors of all status and influence applied their conjecture to the extent of the damages priced in. At the end of the day, investors had nowhere to hide. Apart from the energy sector, the equity side was left bruised in 2022. The table below highlights the economic strife faced in domestic and global equity markets. The same story goes for fixed income. Our neighbours south of the border had their worst combined equity and bond performance in over 100 years. The storyline was the same theme in Canada. Fixed income, known distinctly as a defensive asset class certainly did not deliver on its historical function to mitigate losses in the equity markets.

	Last	52 Week		Change (Local Currency)			
Index	**Price**	**High**	**Low**	**1 Day**	**QTD**	**YTD**	**1 Year**
North American							
S&P/TSX Composite	19,384.9	22,213.1	17,873.2	-0.52%	5.10%	-8.66%	-8.97%
S&P/TSX Small Cap	687.6	857.1	604.8	0.45%	7.76%	-11.18%	-10.82%
S&P 500	3,839.5	4,818.6	3,491.6	-0.25%	7.08%	-19.44%	-19.65%
DJIA	33,147.3	36,952.6	28,660.9	-0.22%	15.39%	-8.78%	-8.93%
NASDAQ	10,466.5	15,868.1	10,088.8	-0.11%	-1.03%	-33.10%	-33.51%
Russell 2000	1,761.2	2,288.3	1,641.5	-0.28%	5.80%	-21.56%	-21.68%
Global							
MSCI EAFE	1,955.5	2,367.1	1,617.7	0.63%	17.70%	-16.29%	-16.24%
MSCI Emerging Markets	957.5	1,270.3	836.9	-0.28%	9.32%	-22.29%	-21.70%
FTSE 100	7,451.7	7,687.3	6,707.6	-0.81%	8.09%	0.91%	0.66%
Nikkei 225	26,094.5	29,388.2	24,681.7	0.00%	0.61%	-9.37%	-9.37%
DAX	13,923.6	16,285.4	11,862.8	-1.05%	14.93%	-12.35%	-12.35%
CAC 40	6,473.8	7,384.9	5,628.4	-1.52%	12.35%	-9.50%	-9.75%
Hang Seng	19,781.4	25,050.6	14,597.3	0.20%	14.86%	-15.46%	-15.46%

After a three-year period of both abundance followed by calamity, there are some powerful lessons to be learned moving forward in one's investment journey:

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1. Avoiding the Noise

In the abrupt rebound from the 2020 COVID market crash, near zero percent interest rates, coupled with consumers flushed with cash, created irrational market behaviour. This period infused euphoria that higher-risk growth stocks (for example, Cathie Wood's ARK Innovation ETF) would continue to advance. The explosive bull market led to the ARK Innovation ETF posting returns over 150%, leading to immense inflows. At its peak in 2021, this ETF held slightly less than 28 billion in assets. 2021 and 2022 were disastrous (~23% and ~67% respectively) for the ETF which invested primarily in high multiple growth stocks. Although I am a huge believer in innovation and new progressive companies creating their own competitive advantage, I can say with complete certainty that triple digit growth year over year is simply not sustainable.

Remember the rise of the SPAC market? In 2020 and part of 2021, SPACs, otherwise known as Special Purpose Acquisition Companies, were a popular way for private companies to go public. They offered a "simpler" alternative to the IPO process by raising money through public investors to acquire companies. Funds are raised before a target company is pursued. The fundamental problem is that warrants issued by these shell companies should have been considered as liabilities, and not as equity. Most SPAC investors were incurring the costs of dilution that was effectively subsidizing the companies they brought public.

More recently, at the end of 2022, the immense impact of the crypto industry was felt at an unprecedented pace. FTX Exchange was a leading crypto currency exchange specializing in derivatives and leveraged products, filed for bankruptcy protection in November 2022. The sudden and immediate collapse was regarded as a failure of corporate controls that caused a contagion of redemptions across the entire crypto market. Bitcoin, the leading cryptocurrency, was trading at just under of 48k USD in March 2022, followed by a pronounced dip to below 17k to end the year. It now seems to be making a rally upward again to start off 2023. I will not claim to be an expert in the crypto space, but the continued fluctuation is a lot to bear.

Many investors will tend to move away from their investment philosophy to ride the wave or stand on the sidelines. The results can be disastrous when all eggs are put in one basket. This can be amplified if the chosen basket has not turned out to have a long shelf life in our changing capital markets.

2. Staying Disciplined

Often, especially during periods of heightened market volatility, I am inundated with new products or strategies that provide downside protection while participating in the market upside. There is always a caveat to the functionality of these investment products. Too many investors buy into the glamour of new products, new trends and overlook the virtue of simplicity. If you ignore the simplicity of a defined strategy, you generally expose yourself to elevated risk. The market rewards those that do their research. Over the past three years, those who remained calm and understood a defined asset allocation of high quality stocks, bonds and alternative assets that matched their risk tolerance were not shaken relative to their counterparts who steered in other directions. Disciplined, diversified and fundamentally sound positions will further establish one for their long (and short) term investment goals. Individual positions are not expected to yield 40% returns year over year. At some point, their valuations must retract. Understanding that investing is a journey not a race, will allow investors to stay within the bounds of their prescribed investment strategy.

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3. Professional Advice Matters

During the rally from the market lows in March 2020 did you notice the sheer volume of "do it yourself" investing? When markets were returning 20%+ investors questioned the validity and use of investment professionals and the related fees. Note that after 2022 those advertisements have less of a shelf life in mainstream media. Certain types of investors look to Private Wealth professionals with one objective of "alpha" generation, meaning outperformance of their relative benchmark. Over time, these investors realize that their financial professional has no control over the markets and the exogenous shocks that are constantly taking over global headlines. The true value comes from the relationship, which is to develop a strategy, provide consistent coaching, and understand client needs within the bounds of their entire wealth picture. A recent anecdote I learned in 2022 was that investors left to their own devices often attempted to time the markets based on speculation alone. For example, in the US Markets the Federal Reserve policy was driving the bus, and by October 13 2022, the S&P 500 index (a barometer of the US and global economy) fell to 3491 points. This was deemed its lowest level since November 2020. The illustration earlier in this passage states that the S&P 500 ended the year at 3839.5. Without the proper coaching many investors acted on their intuition and cashed out in an attempt to hedge their losses, missing out on some meaningful upside. Provided below is a dated example using our domestic markets. Relying on a distinguished investment professional during troubling times or periods of abundance will ensure that inappropriate decisions are not made that could gravely impact one's financial picture.

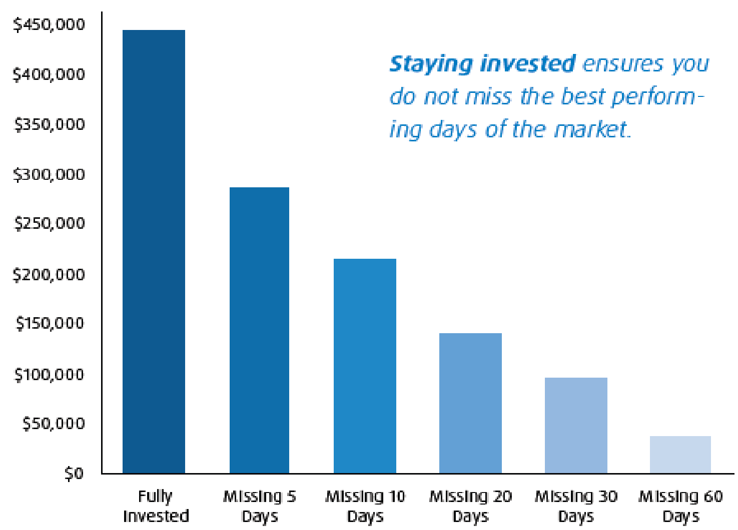
Remember it's all about ***time in*** the market, not ***timing*** the market.

When markets become volatile, most investors are prone to over-react and sell at the wrong time, accepting substantial losses. Over the long term, markets are resilient and investors who stay invested will recover their losses and grow their wealth.

Don't let short term noise disrupt your long term goals, stay invested and reap the rewards.

Value of $100,000 after 21 years invested from 2000-2021

Just missing a few days in the market can have a meaningful impact on your portfolio.



- **Staying invested,** your portfolio returned **344.3%,** and became **$444,255.**
- Missing the **5 best days,** your portfolio returned **186.5%** and became **$286,489.**
- Missing the **10 best days,** your portfolio returned **115.2%** and became **$215,244.**
- Missing the **20 best days,** your portfolio returned **40.6%** and became **$140,600.**
- Missing the **30 best days,** your portfolio lost **-4.1%** and became **$95,920.**
- Missing the **60 best days,** your portfolio lost **-62.5%** and became **$37,453.**

Source: Bloomberg, 2021.

Illustration is based on the S&P/TSX Composite TR Index from Jan 1, 2000 to December 31, 2021. Does not take into account income taxes payable by the investor that would have reduced returns. Examples provided here

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Where do we go from here?

Some leading economic indicators are suggesting inflation is on a meaningful decline from peak levels. We received an additional reading that US CPI dropped lower to 6.5%. Canada's CPI numbers followed suit this week lowering to 6.3%. Nevertheless, inflation numbers remain stubbornly high and need to fall much further before consumers and market participants begin to experience some semblance of normalcy. Our central banks should continue to maintain (or slightly tighten) their monetary policy which will result in more difficult financial conditions. This includes, but is not limited to, sustained high interest rates leading to stricter lending requirements, and declining stock valuations on the equity side.

Although experts in the economic field are oscillating between a short-lived recession versus something more structurally embedded over long-term, the average consumer is starting this journey on solid ground. There will be some economic resilience thanks to the average household's surplus savings from prior years coupled with the relative ease with which one can locate and negotiate a fair wage in this labour market. As the effects of these rate hikes continue to spread through businesses and the typical consumer, this storyline will likely pivot to a more pessimistic tone.

Earnings reports will set the table as the dominant proponent as to how tightening conditions are filtering through corporates. Most of the carnage, we believe has been factored into the asset prices. On the fixed income side, maturing positions are beginning to invest at rates much higher which is a positive from a coupon standpoint. Finally, we can put the "income" in fixed income after years of low rate environments. Our strategy team and local Counsel team remain cautiously optimistic about the year ahead. It is structurally encouraging to see some sense of order in our financial markets as central banks continue to orchestrate an environment that will brush off the aftermath of bubbles, fads and corporate failures.

"The individual investor should act consistently as an investor and not as a speculator." — Ben Graham

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