INVESTMENT OBJECTIVE

To achieve long-term capital appreciation with a focus on diversification and downside protection by investing across asset classes in Canadian and Global companies with market cap exceeding $500 million.

INVESTMENT PHILOSOPHY

The team employs a disciplined approach by combining a systematic and fundamental selection process that favours quality companies with growing earnings.

When building a balanced portfolio, the Fund will invest in a mix of fixed-income securities and equities across a diverse range of regions and sectors.

The team has flexibility with the asset mix, strategically taking advantage of market opportunities.

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INTRODUCTION

It was a difficult quarter for global financial markets. Q3's brief and aggressive bear market rally ended with widespread declines. The market has been contending with what may be the most challenging macroeconomic environment in the last 30 years. Many central banks continued to aggressively raise interest rates to curb persistently high inflation. The negative impact of the Russia-Ukraine conflict continued, while Europe coped with an energy crisis elevating recession pressures. Supply chain issues and labour shortages remained, while interest rate differentials have triggered large currency moves. In the short term, it is difficult to find much good news. However, staying focused on capital preservation while patiently seeking opportunities as they arise will benefit investors in the long term.

In this edition, we'll share our perspective on current market themes and trends plus the latest economic developments. We'll dive deeper into the levers we use to protect capital and how we take advantage of long-term investment opportunities when they arise.

Equities

After a strong rally in July, stocks fell sharply in August and September as central banks made clear that interest rate increases and monetary tightening would continue amid higher inflation. North American equity returns were broadly lower for the quarter. The S&P/TSX Composite Index fell 2.2%, while the S&P 500 and NASDAQ returned -5.3%; -4.1%, respectively. Year-to-date, the S&P 500 is down 24.8%, its fourth worst performance since 1926.

International markets also finished weaker. Europe's ongoing energy crisis, the Russia-Ukraine conflict and double-digit inflation led to a significant repricing of recession risk. Germany's DAX, France's CAC 40 and the UK's FTSE 100 fell -5.2%, -2.7%, and -3.8%, respectively in Q3. Asia followed global equity markets lower. Japanese equities fell, while China's CSI 300 was the weakest market in the quarter, down 15.2%.

Emerging markets suffered losses against a backdrop of slowing global growth, higher food and energy prices, and a strong U.S. dollar. Despite these strong headwinds, there were some positive performers including India, Indonesia, and Brazil. Higher commodity prices and narrowing opinion polls for Brazil's upcoming Presidential election supported Brazil.

Overall, the All Country World Index ETF posted a negative return of -7.2% in U.S. dollars or -0.3% in Canadian Dollars.

Fixed Income

The uncertainty over inflation, the economy, and the pace of interest rate changes weighed on global bonds. In Canada, government bonds , (FTSE Canada All Government Bond Index) delivered positive returns in the quarter up 0.6%, barely making a dent in the poor returns witnessed year-to-date.

** All returns in local currency unless otherwise stated.*
Source: FactSet, Morningstar,Raymond James Ltd. Performance as at September 30, 2022

Currency Volatility

Interest rates have been moving aggressively higher as central banks globally continued to tighten monetary policy to curb persistently high inflation. Generally, higher interest rates increase the value of a country's currency as higher rates attract overseas investors' money. However, the volatility in interest rate differentials of countries has been wreaking havoc on foreign exchange rates.

Recent rate rises have led to a sharp strengthening of the U.S. dollar relative to the euro, the Japanese yen, the British pound sterling and the Canadian dollar. The UK has drawn a lot of attention for its poorly received fiscal package and high inflation brought on by rising energy prices which has sent the Sterling and long-term bond prices to multi-decade lows versus the U.S. dollar. The Canadian dollar has not fared much better. Versus the US dollar, the Canadian dollar fell 6.9%, while the Sterling fell 8.3% and the yen fell 6.6%.

Canadian dollar weakness was however a positive for Canadian investors. For example, the S&P 500's -5.3% return in U.S. dollar terms equated to a +1.8% return in Canadian dollars.

*All returns in local currency unless otherwise stated.

WHAT'S AHEAD FOR MARKETS?

Our outlook has not changed materially since Q2. Enduring structural themes continue to guide our long-term view on what will shape the markets.

Corporate earnings expectations

At the end of Q2, our view was that there was potential for S&P 500 companies' earnings to fall below $200 in 2023. We are starting to see that the deceleration of growth is starting to impact earnings; however, aggregate earnings levels are still above the $200 level for the S&P 500. According to research provider, FactSet, earnings estimates for 2022 and 2023 are $220 and $238, respectively. This puts the U.S. equity market on a PE of 15x for 2023 (at time of writing). Although we think earnings need to fall further, we have been pleasantly surprised by the consumers' resilience and corporations' ability to pass on price to offset rising costs. While the consumer still continues to surprise on the upside, excess savings built up during the pandemic will likely continue to diminish over the next 6 to 8 months. Higher energy, food and borrowing costs will also pressure earnings in the coming months. As the rest of the economy adjusts to higher rates, will this surplus in savings create a bridge for a potential soft landing? It is possible, but not our base case. Lower oil prices and improved supply chains may help the Fed deliver a soft landing, but it is difficult to predict what type of recession the world could see.

Interest rates

Another uncomfortably high inflation reading for September kept the Federal Reserve on track for a 0.75 point rate increase, bringing the benchmark federal-funds rate to a range between 3 and 3.25%. Notably, Chair Powell was candid about the risks at the latest meeting, conveying the negative impacts to the economy.

Policy makers signaled plans to continue lifting rates, projecting short-term rates will peak at 4.6% by the end of 2023. This is often referred to as the terminal rate. This level implies over 125 basis points of further hikes – 75bps in November followed and a further two at 25bps. We are already witnessing the impact of rising rates. The U.S. housing market is slowing with mortgage rates north of 7%.

Rates and bonds

Higher interest rates also sent yields soaring, driving much of the sell-off in global bonds. Year-to-date the Bloomberg Global Aggregate Bond Index is down 21%, while the Bloomberg U.S. Aggregate Bond Index fell nearly 16% (U.S. dollar terms). These are some of the worst returns for either index since 1976 (U.S.) and 1990 (global) which has wiped out trillions of dollars from pension funds, sovereign wealth funds and investment funds. While these declines may impact the investment landscape in the short-term, in the long-term we believe the need for income generating assets will remain. When the equity market recovers, great companies with strong cash-flow generation and solid growth prospects will command a significant premium again.

The implications for Emerging markets are beginning to be felt. Global borrowing costs are rising but we have yet to see corporate bond markets react to a significant slowdown in economic activity. As this is precisely what the Fed is trying to accomplish, it appears that the corporate bond market is in a wait and see mode. Investment Grade and High yield markets have repriced, but spreads are not as wide as they would be if we are looking at a severe recession in 2023.

At the beginning of January this year, the portfolio held less than 2% in bonds, avoiding much of the downside witnessed by traditional 60/40 portfolios. We have begun to add credit positions, but only very short, dated issues.

Unknown Unknowns

"As we know, there are known knowns; there are things we know we know. We also know there are known unknowns; that is to say we know there are some things we do not know. But there are also unknown unknowns — the ones we don't know we don't know." - Donald Rumsfeld, February 12th, 2002, then Secretary of Defense of the United States.

One such "unknown unknown" this quarter was the U.K. bond crisis which showed how rapid jumps in interest rates could quickly create cracks in the financial system. Many pension funds employ a liability-driven investment strategy that aims to reduce volatility without lowering returns by using derivatives. As interest rates rose in the UK and bond prices fell, pension funds were forced to sell to generate cash collateral, which in turn drove bond prices still lower. The UK central bank stepped in to restore order, but this example illustrates how unknown unknowns can appear as we traverse a regime change and interest rate normalization. To handle changing market dynamics whether known or unknown, we design resilient portfolios with exposure to several asset classes, regions and uncorrelated assets.

With such significant upheavals taking place across the fixed income and currency landscape, from country to country, it is important to have a well-balanced approach when investing long term portfolios. The challenges witnessed in the United Kingdom highlight that bond market instability is not confined to emerging markets. It happened in a country with a significantly lower debt to GDP ratio than Canada currently has. A warning to other countries, that fiscal largesse seen over the last few years may not be tolerated by the global bond market. We have stressed in the past that Canada has a unique position being so closely tied to the world's dominant economy and currency. We hope our policymakers use this advantage but are aware and fearful that complacency and hubris may create conditions for an avoidable policy error in this uncertain period in the global economy. We stress again that portfolio balance is imperative for capital preservation.

Rate implications in Canada

2022 and 2023 will be a shock for Canadian borrowers. Rates in Canada will have to keep pace with the U.S. If the Bank of Canada fails to deliver, the prospects for the Canadian dollar are bleak. Already down versus the U.S. dollar for the year, the Canadian dollar fell 6.9% in the quarter. As we import a great deal from the U.S., the inflation rate is becoming harder to tame.

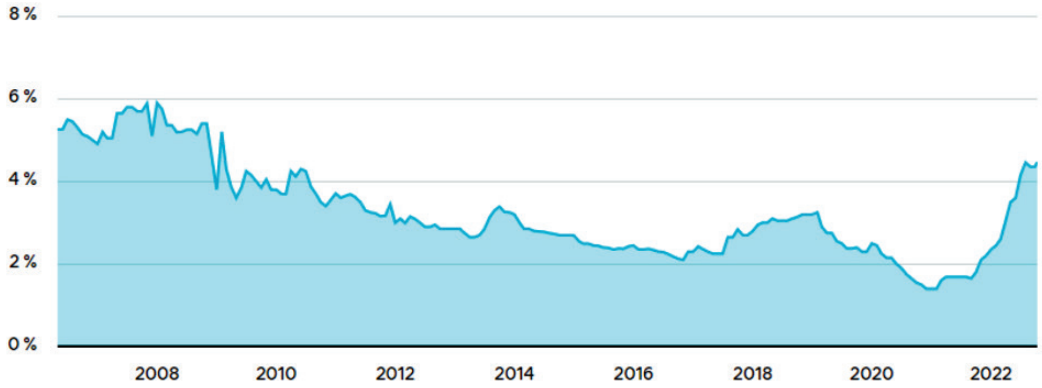
Canadian consumers with more debt, higher taxes and relatively short-dated mortgages are more interest rate sensitive than their U.S. counterparts. The average mortgage in Canada is $374,000 according to the CMHC (August 2022), which is 57% higher than it was in 2015. Mortgage rates in the last 1 to 2 years were attainable around 2.5%. Unfortunately, incomes have not risen in the same way, and mortgages rolling over in the next 12 to 18 months may well double the previous mortgage cost.

A growing number of economists are forecasting Canada will enter a recession if the Bank of Canada continues to aggressively raise interest rates to fight inflation. While the path to normalization will be painful, the problem was created by central banks with loose monetary policy and free money for far too long. It was not sustainable. Now the current economic situation requires fiscal restraint. If the Bank of Canada does not raise rates in line with the U.S., expect a weaker Canadian dollar. This situation has the potential to create a feedback loop where a lower dollar will lead to higher import costs leading to higher inflation (and the need for higher rates) for longer.

Higher mortgage rates will also impact those with fixed mortgages. According to the Canadian Association of Accredited Mortgage Professionals, highlighted in the chart on the left, mortgage rates fell below 4% in 2010 and have remained there until recently. Most five-year fixed mortgages today are posted at rates well above 5%. We will see this slow-moving change work its way through consumer spending in 2023 and 2024.

HISTORICAL DISCOUNTED 5-YEAR MORTGAGE RATES

From 2006 – Today

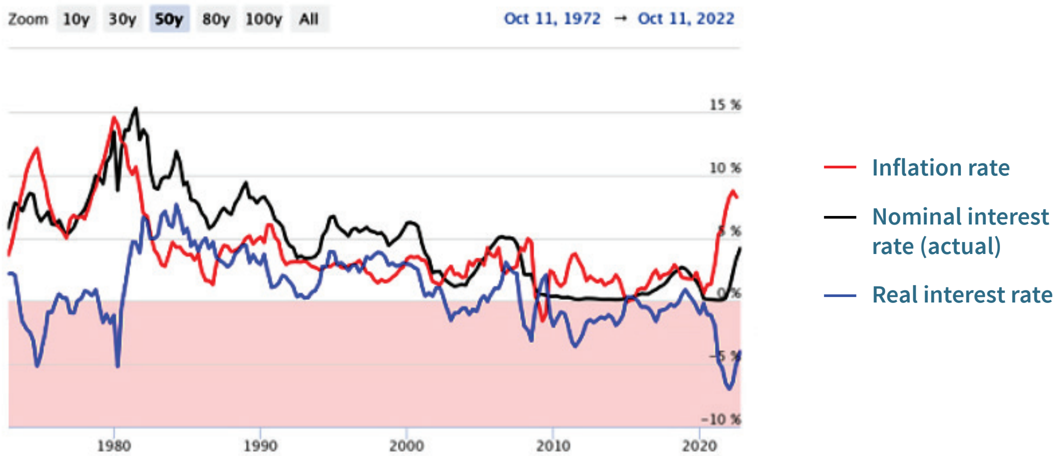


Source: Canadian Association of Accredited Mortgage Professionals

Higher for longer

Looking back for most of 1980's,1990's and 2000's, the nominal interest rate exceeded the inflation rate. Rates were far too low after the global financial crisis, and the zero-rate many investors experienced is being used as the baseline for how markets and investors should perceive the current market malaise. On the contrary - for a healthy and functioning market and global economy, interest rates need to rise, normalize, and stay higher for longer. This is the future we need to be preparing for and living with.

NOMINAL VS. REAL INTEREST RATE VS. INFLATION

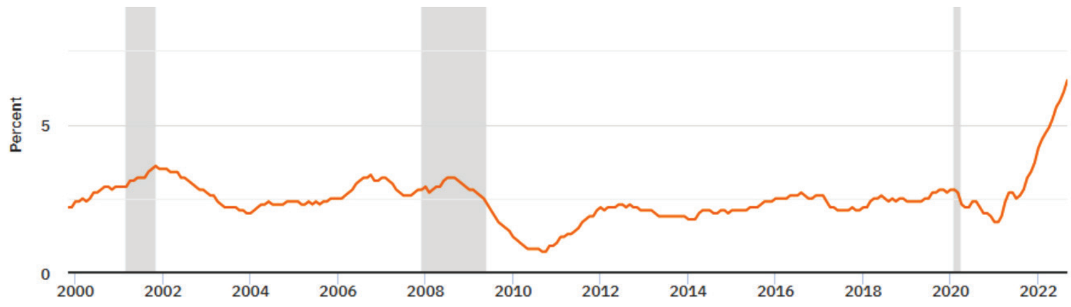


Source: longtermtrends.net/real-interest-rate

It has long been the case that the normalisation process would be painful, but it is our view that as we get through this process, immense opportunities will be presenting themselves and indeed many already are. Are investors ready for a return of normal monetary conditions? By observing the recent market gyrations, it would appear not, yet.

We think it is unlikely that inflation will come down soon and we see inflation potentially at 3.5 to 4.5% in late 2023. Atlanta's Fed Sticky Price Inflation data, a gauge that measures a basket of items that tend to be more cost resistant to change (removing fast-moving prices like food and energy), has made new highs this year (see chart below). This is telling, as this gauge has been a good forecast for inflation on a 12-month forward basis. Rate normalization, which we have been anticipating for over two years, will continue and we believe that normal rates will be in the 5.5 to 6.5% range.

STICKY-PRICE CPI



Grey bars indicate periods of recession

Source: Federal Reserve Bank of Atlanta

U.S. dollar strength

In 1971, at a multi-lateral government meeting in Rome, then U.S. Treasury Sec. John Connelly told heads of state that the dollar is ***"our currency, but it's your problem."*** A harsh statement from President Nixon's post-Bretton Woods policy architect but one that would be repeated often in the coming decades. The problem is as real today as it was then, but there is little discussion of how the broad dollar strength disrupts global markets.

We are seeing irregularities in the macroeconomic environment today that differ from those in historically similar circumstances. In a strong U.S. dollar world, emerging market currencies and bonds typically suffer. They have not suffered uniformly, as in past crises. Japan, Europe, the U.K. and other western nations are facing declining purchasing power not seen since the 1970's. Why? We believe this is mostly due to the new regime we are entering, which we have discussed previously. Countries in the West that were once perceived as rich, are struggling with balance of payments when energy costs escalate wildly. Countries with commodities are faring better, whereas those without energy infrastructure and long-term plans are suffering, highlighting the new hard asset regime.

Many economies are not able to withstand the higher rates seen in the U.S. and their currencies reflect this. Recall economic theory – currencies are generally valued off of interest rate differentials between countries. The country with higher interest rates will encourage foreign investment, therefore raising the value of their currency relative to another. It is becoming increasingly important to pay attention to global foreign exchange and its potential impacts to the portfolio. To navigate these risks, diversification across global assets is key. We maintain a well-balanced approach to managing global interest rates and currency risks to prevent loss in the portfolio.

Energy

Perhaps a statement from OPEC+ along the lines of John Connelly above would be ***"oil is our commodity, but it's your problem"***. Clearly, the Russian President is proving this point to western Europe. The latest OPEC+ production cuts at the $85 range suggest that this is a war being fought on many fronts - physically in Ukraine, and financially in central banks, sanction programs, and global commodity markets. OPEC+ production cuts have reinforced our view that the world is shifting in unexpected ways. The U.S. Administration's request to postpone oil supply cuts to help alleviate high gasoline prices is something that has not been seen in a long time - adding to an already complex multipolar world.

The energy sector remains the best-performing sector year-to-date, by a wide margin. We believe oil prices are likely going to remain well above $80 for some time. We continue to maintain our energy exposure as we believe capital expenditure will improve. Our energy company exposure is exceptionally well valued on a multi-year view as we are focused on investing in large-cap integrated businesses with strong balance sheets and production growth.

Cautious optimism

It is easy to grow pessimistic in tough markets especially given today's interest rate headwinds and a difficult economic environment. However, at some point the market will eventually bottom, and when it does, the returns are typically excellent as illustrated in the below chart.

S&P 500 INDEX CORRECTIONS & BEAR MARKETS (2000 – CURRENT)

High Date	S&P 500 High Price	Low Date	S&P 500 Low Price	10%+ Market Corrections	1-Year Return After Lows	2-Year Return After Lows
3/24/2000	1527.5	4/14/2000	1356.6	-11.2%	-12.8%	-18.1%
9/1/2000	1520.8	4/4/2001	1103.3	-27.5%	2.1%	-20.3%
5/21/2001	1312.8	9/21/2001	965.8	-26.4%	-12.5%	7.3%
1/4/2002	1172.5	7/23/2002	797.7	-32.0%	23.9%	36.2%
8/22/2002	962.7	10/9/2002	776.8	-19.3%	33.7%	44.5%
11/27/2002	938.9	3/11/2003	800.7	-14.7%	38.2%	49.9%
10/9/2007	1565.2	3/10/2008	1273.4	-18.6%	-43.5%	-10.0%
5/19/2008	1426.6	10/10/2008	899.2	-37.0%	19.2%	29.6%
10/13/2008	1003.4	10/27/2008	848.9	-15.4%	25.3%	39.3%
11/4/2008	1005.8	11/20/2008	752.4	-25.2%	45.0%	59.4%
1/6/2009	934.7	3/9/2009	676.5	-27.6%	68.6%	95.1%
4/23/2010	1217.3	7/2/2010	1022.6	-16.0%	31.0%	33.5%
4/29/2011	1363.6	10/3/2011	1099.2	-19.4%	32.0%	52.7%
5/21/2015	2130.8	8/25/2015	1867.6	-12.4%	16.3%	30.8%
11/3/2015	2109.8	2/11/2016	1829.1	-13.3%	26.6%	43.2%
1/26/2018	2872.9	2/8/2018	2581.0	-10.2%	4.9%	28.9%
9/20/2018	2930.8	12/24/2018	2351.1	-19.8%	37.1%	57.5%
2/19/2020	3386.2	3/23/2020	2237.4	-33.9%	74.8%	99.2%
1/3/2022	4796.6	9/27/2022	3647.3	-24.0%	?	?
			Average (2000-2021):	-21.2%	22.8%	36.6%
			Median (2000-2021):	-19.4%	25.9%	37.7%
			Average (1980-2021):	-18.9%	24.9%	39.2%
			Median (1980-2021):	-17.1%	25.9%	44.5%

Source: FactSet; Data as of September 27, 2022

We remain cautious given the prevailing conditions and risks but are continually seeking out long-term buying opportunities. Although valuations are not excessively high, not all risks have passed we believe there is still room for downside, particularly in the mega caps.

The growth stock rout has mostly played out with many solid businesses down over 70%. Since discussing growth stock overvaluations in Q4 2020, investor sentiment for the longer-term prospects for corporate earnings for growth stocks has shifted and stocks have re-rated.

Capital preservation is paramount to Tall Oak Private Wealth's investment approach.

What is capital preservation? It is the difference between approaching investing with the question: How much can I lose? versus How much can I make on that? The priority is to avoid high-risk situations. Capital preservation requires greater caution whether that means investing for a shorter time or adding other safeguards.

– Financial Tactics and Terms for the Sophisticated International Investor, Harry D. Schultz

In particular, high-value growth stocks with no earnings re-rated extensively, yet a large cohort of growth stocks carrying huge market caps remains. When they unwind, it will impact the overall market which will be especially problematic for passive investors. With values improving, we are starting to see more investing opportunities. We believe our current stock positions are trading at good valuation levels and are poised to participate in the upside when markets rebound.

We've positioned the portfolio defensively and continue to focus on capital preservation. We believe this is the best course of action in the current challenging environment. While this may at times limit near-term upside, as was the case in the quarter's bear market rally, we believe that defensive, high-quality positions while selectively seeking out exceptional opportunities, will better position the portfolio for the long-term.

PORTFOLIO POSITIONING

Fixed Income

- Bonds markets are still set for their worst year in decades. Long-duration assets have shown significant volatility this year and we anticipate this will continue. We are gradually and selectively adding to our investment grade bond position, as opportunities arise. The portfolio has had limited additional exposure since Q2.
- We added more short-dated bonds with strong yields in sectors we think will weather a significant economic slowdown. Our bond, cash, and alternatives positions closed the quarter at 33.3% with Investment Grade bonds representing 16.7%; the highest level we have held. Our average weighted duration in Investment Grade credit is 1.8 years, with a 5.8% annual yield. We believe high-quality investment-grade bonds with only slight duration risk offer compelling risk-return attributes should we enter a recession in 2023.

Equities

We added to two key themes in the quarter:

3. **Low volatility, less economically sensitive**

   This quarter, we added to positions that we believe to be well-placed to weather ongoing inflation challenges. Seed and pesticide manufacturer, **Corteva**, was added, increasing the portfolio's agriculture exposure. The agricultural giant has numerous brands including Pioneer seeds which offers Canadian farmers crop protection products that help lower costs and increase yields. We saw inter-quarter share price weakness as an opportunity to add Corteva. Agriculture's long-term growth prospects remain positive given continued global crop supply issues. Along the same theme, we modestly increased our position in the Norwegian seafood producer, **MOWI.**

   Shifting to Healthcare, we increased our position in Danish Pharmaceutical company, **Novo Nordisk**. Their focus on fighting diabetes and obesity, two long-term health conditions, means there are well-positioned to grow regardless of the economic environment. We believe health care, particularly in emerging Asia will also drive long-term growth prospects for the company.

4. **Increased our energy exposure**

   We continue to find opportunities in the energy sector, particularly those in production and infrastructure companies where we see excellent growth opportunities after years of underinvestment. We built upon our position in U.S. base oil services company, **Schlumberger** and added a new position in Italian steel tube manufacturer, **Tenaris**. Tenaris' business combines the production and sale of seamless and welded steel tubular products for the oil and gas industry. Energy infrastructure is a key theme for the portfolio, and we added the position with a forward-year PE ratio of 7.5x. **Williams Co**, a U.S. gas production and distribution business was another addition. Gas transmission and services make up the majority of the company's revenue and Williams Co has shown that it is a very stable business with long-term growth prospects which is not reflected in the stock's PE multiple. It also has a supportive 5.8% dividend yield. We also own the debt of this company within our credit portfolio. Finally, we increased our position in **EOG Resources** during the late September sell-off in energy names. EOG has exposure to both oil and natural gas. The stock has a healthy Free Cash Flow Yield of 7% and a sub 9x PE ratio.

PORTFOLIO MANAGEMENT TEAM

SHAWN JAKUPI CFA®, CFP®
Portfolio Manager

Shawn is a Founding Partner of Tall Oak Private Wealth. He holds the title of Portfolio Manager and co-manages the Tall Oak Capital Appreciation Fund. Shawn has the Chartered Financial Analyst (CFA) and Certified Financial Planner (CFP) designations. Shawn has grown a deep knowledge of global financial markets through a commitment to education and has developed a strategic investment mindset over his 20+ years of experience. Both are key to building discretionary portfolios that help clients meet their financial goals.

MEHENDI KAMANI CFP®, CLU, CIM®
Portfolio Manager

Mehendi is a Founding Partner of Tall Oak Private Wealth. He holds the title of Portfolio Manager and is also a Chartered Investment Manager, a Certified Financial Planner, and a Chartered Life Underwriter. He has 25 years of financial services industry background including senior management positions with banks, insurance firms, and mutual fund companies. His diversity of experience has provided him with unique insights into financial planning and wealth management.

BEN LEGGE
Portfolio Manager

Ben joined Tall Oak Private Wealth as a Partner in 2020, holds the title of Portfolio Manager, and co-manages the Tall Oak Capital Appreciation Fund. Ben is driven by a passion for exploration and understanding of global financial markets and has helped clients and institutions pursue their investing goals over the last 27 years. His diverse capabilities span equities, fixed income, hedging strategies, and multi-asset portfolio construction. Throughout his distinguished international career, Ben's held senior-level executive positions at some of the world's largest asset management companies overseeing multi-billion dollar portfolios.

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It is important to remember that although markets may get more difficult in the months ahead, we continue to be laser-focused on creating portfolios with strong risk parameters to weather the storm. The better we weather this storm by preserving your capital, the greater the investment opportunity we will have in the quarters ahead.

We intend to be opportunistic when making new investments on our client's behalf, and we believe markets will offer some excellent long term opportunities in the quarters ahead.

Sincerely,
Your Tall Oak Private Wealth Team

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