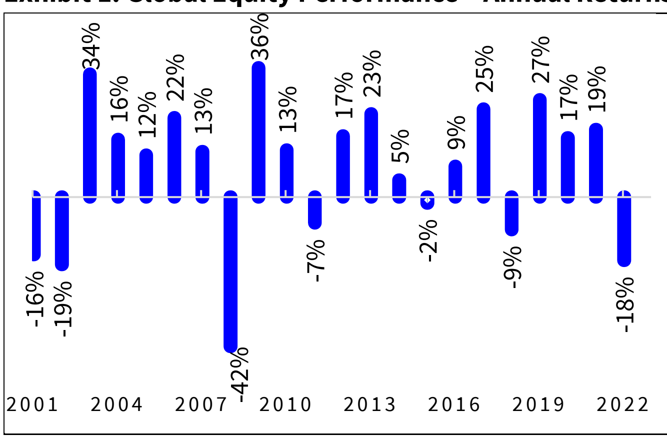
January 17, 2023

We hope this letter finds you well and that you enjoyed a happy and healthy holiday season. As we turn the page on a new year, we are reminded that each year brings with it new opportunities. We will continue to focus on capitalizing on attractive investment opportunities in the year ahead.

In this quarterly letter, we recap recent financial market performance and briefly discuss the economic and market outlook. We touch on several investment themes, and remind investors of the importance of staying invested during market downturns and following a disciplined investment strategy to maximize long-term investment returns.

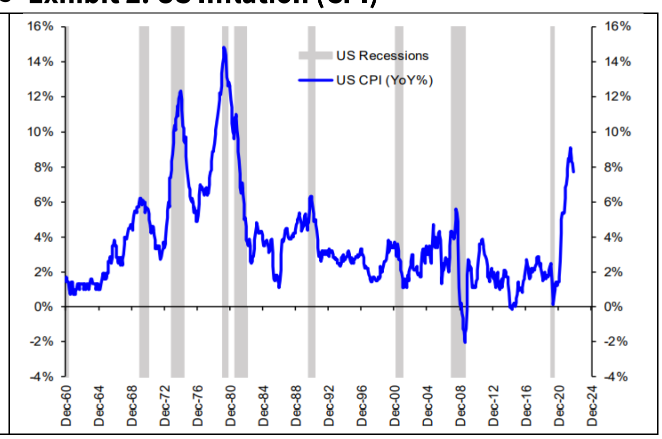
The year 2022 was a challenging year in financial markets and marked the worst year for global equities since 2008 (Exhibit 1). Labour shortages, pandemic-induced supply-demand imbalances, and disruptions related to the war in Ukraine, contributed to a surge in inflation to levels not seen in 40 years (Exhibit 2).

Exhibit 1: Global Equity Performance – Annual Returns



Source: FTSE All-Country Total Return, Factset

Exhibit 2: US Inflation (CPI)

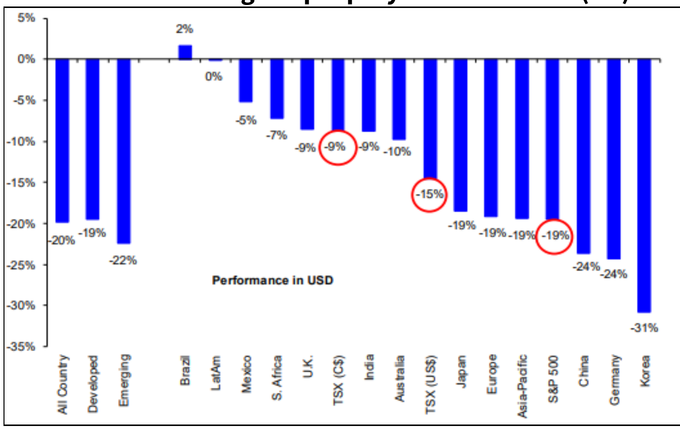


Source: Scotiabank GBM Portfolio Strategy, Bloomberg

Central banks responded by aggressively increasing interest rates in an attempt to slow the economy and restore price stability. It was one of the most aggressive tightening cycles in over 50 years. Sharply higher interest rates put downward pressure on the valuations of financial assets with equities and bonds suffering a steep valuation compression.

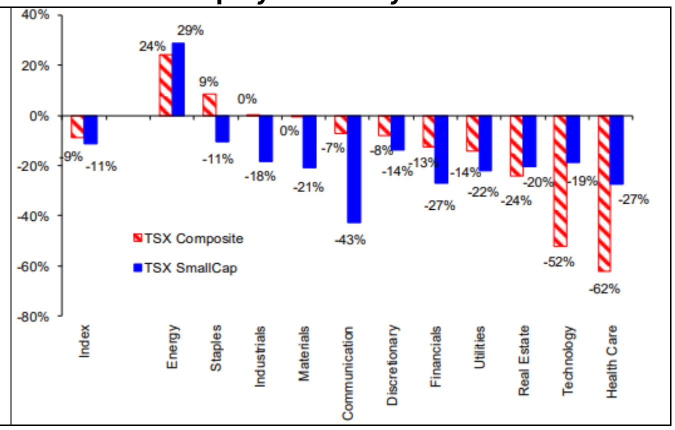
Equities in most regions experienced double-digit declines in 2022 and the MSCI World Index (Price Return) was down 19.5%. The U.S. benchmark S&P 500 Index (Total Return) fell 18.5% while the tech-heavy NASDAQ Composite Index (PR) fell 33.1%.

Exhibit 3: Global Large Cap Equity Returns - 2022 (PR)



Source: Scotiabank GBM Portfolio Strategy, Bloomberg

Exhibit 4: Cdn Equity Returns by Sector - 2022

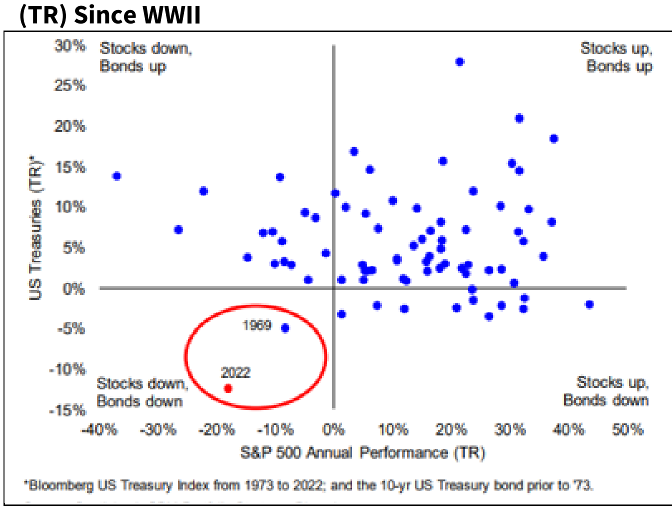


Source: Scotiabank GBM Portfolio Strategy, Bloomberg

Canadian equities were broadly lower in 2022, although the impact on the resource-heavy S&P/TSX Composite Index ('TSX') was muted by the strong performance of resource equities as Energy and Materials now comprise 30% of the TSX. Oil and other commodity prices spiked following the Russian invasion of Ukraine and energy prices remained inflated throughout the year. The S&P/TSX Energy Index (PR) was the best-performing industry sector in 2022, climbing 30.3% and contributing to the TSX's negative 5.8% total return.

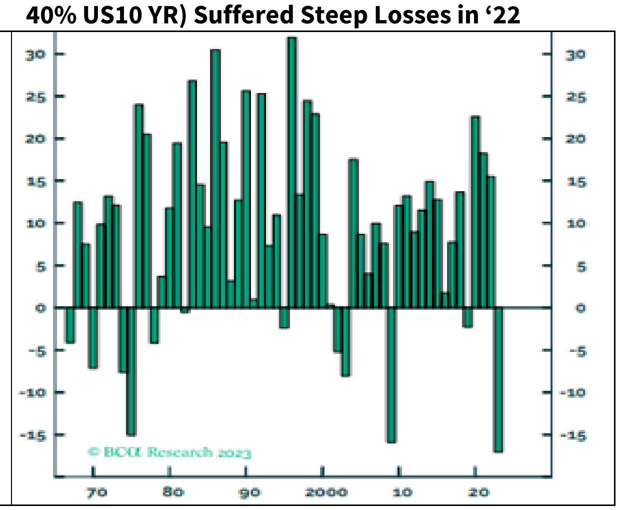
Bonds suffered the worst sell-off in decades as interest rates spiked. The Bloomberg U.S. Aggregate Bond TR Index fell 13.0%, its worst selloff since the beginning of the series in 1976, while the FTSE Canada Universe Bond Index fell 11.7%. The year 2022 marked the first time in 40 years that equity and bond markets both experienced double-digit declines (Exhibit 5), and the traditional 60/40 stock/bond balanced portfolio suffered sharp losses (Exhibit 6).

Exhibit 5: U.S. Equities and Bonds Annual Performance (TR) Since WWII



Source: Scotiabank GBM Portfolio Strategy, Bloomberg

Exhibit 6: Balanced Portfolios (60% S&P 500 & 40% US10 YR) Suffered Steep Losses in '22

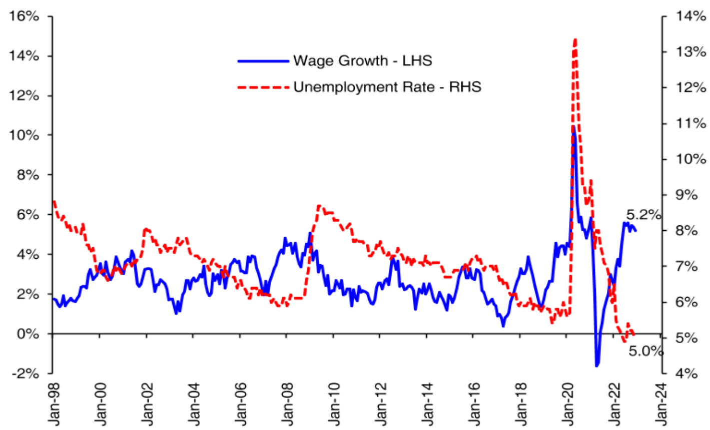


Source: BCA Research Inc.

Inflation remains elevated, labour markets are tight (Exhibit 7), and central banks have indicated that further interest rate increases are necessary to restore price stability. That said, the tightening cycle is very likely in its final innings and additional rate hikes are expected to be fewer and more modest.

There are already some early indications that inflation is beginning to recede as energy prices soften and supply disruptions ease. Supply and cost pressures should continue to ease in the year ahead as the impact of higher rates is felt throughout the economy with an estimated time lag of 6 – 18 months.

Exhibit 7: Canada Unemployment Rate & Wage Growth



Source: Scotiabank GBM Portfolio Strategy, Bloomberg

We expect investor focus will increasingly shift to deteriorating economic data as growth continues to slow. Recessionary concerns are beginning to weigh on earnings expectations and we expect further revisions to earnings estimates in the months ahead. Negative earnings revisions create a potential headwind for equity performance in the short term.

Embracing Volatility to Maximize Long-Term Returns

Investor sentiment has been weak, which is unsurprising given recent financial market returns and the challenging macro backdrop. It is important, however, to not lose sight of longer-term investment objectives in times of market volatility. Economic and market cycles are a normal part of long-term investing and volatility can create opportunities. As we know from many years of history, stocks offer attractive long-term growth potential, albeit with greater fluctuations than other asset classes.

As we noted in our Q3 letter, it is often during times of extreme uncertainty and pessimism that equity markets can exhibit days with sharply positive performance. History demonstrates that on average, the best performing days occur within just two weeks of the worst performing days. Investors who miss these positive days (sometimes inflection points) can experience markedly lower equity returns over the long term. Importantly, investors that try to time the market risk the permanent loss of capital. Large market drawdowns are often followed by periods of excess returns (Exhibit 8), and patient, long-term investors can reap the rewards by staying invested through full market cycles.

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Exhibit 8: Following Large Market Drawdowns, Longer-Term Investors Are Generally Rewarded Over the Next 3-5 Years for Leaning into Dislocations

S&P 500 Worst Returns Since 1928

Year	Return	+1 Year	+3 Years	+5 Years	+7 Years
1931	-43.8%	-8.6%	35.4%	162.1%	119.1%
2008	-36.6%	25.9%	47.6%	126.1%	160.2%
1937	-35.3%	29.3%	14.2%	18.7%	76.7%
1974	-25.9%	37.0%	57.8%	99.2%	150.1%
1930	-25.1%	-43.8%	-23.0%	11.6%	-4.8%
2002	-22.0%	28.4%	49.0%	81.7%	45.2%
1973	-14.3%	-25.9%	25.7%	24.5%	94.5%
1941	-12.8%	19.2%	77.4%	120.6%	145.3%
2001	-11.9%	-22.0%	10.9%	34.4%	-10.0%
1940	-10.7%	-12.8%	30.0%	110.2%	102.5%
Averages		**2.7%**	**32.5%**	**78.9%**	**87.9%**

Source: NYU

Disconnect Between Public and Private Valuations: Redefining ‘Risk’ and ‘Volatility’

In recent years, there has been an influx of fund flows into private investment funds that have constraints on capital redemptions. In contrast to public equities that offer transparency and are valued on a real-time basis on major stock exchanges, private funds offer less transparency and are valued less frequently. This results in a smoothing of returns. Headline volatility is reduced with private funds, and investors are comforted by the perception that the funds are less ‘volatile’ or ‘risky’ than public securities.

At Seymour, we do not characterize ‘risk’ as volatility for long-term investors, but rather we define risk as the permanent loss of capital that can occur either 1) when a company’s profitability is permanently impaired or 2) when valuations are impaired and do not recover during an investor’s investment time horizon. We view ‘volatility’ as opportunity for long-term investors, and note that market sell-offs create opportunities to buy high-quality companies at discounted valuations and capture excess returns.

We view ‘volatility’ as opportunity for long-term investors

Investors typically demand a premium to compensate for the illiquidity associated with private investments relative to liquid public investments. However, currently, there is a material disconnect between valuations of public equities, which in many cases are trading at material discounts to intrinsic value, and those of private assets. This disconnect is unlikely to persist in the long term as sophisticated investors take advantage of the arbitrage opportunity. We have already seen a number of privatizations of publicly-traded companies at healthy premiums to current trading values, and we expect this trend will continue as long as equity markets remain depressed. We believe public equities offer more attractive opportunities today for long-term investors that are willing to embrace volatility.

Investors that Follow a Patient, Disciplined Investment Strategy Will Ultimately be Rewarded

At Seymour, we follow a relatively simple, straight forward investment strategy of buying shares of high-quality, well-managed publicly-traded companies with attractive business models and long track records of prudent capital allocation and solid earnings growth. We focus predominantly on non-resource companies with predictable earnings streams that trade at reasonable valuations, and we try to avoid taking on valuation risk. Our investment style can be characterized as [Quality] Growth at a Reasonable Price.

Following the recent market selloff, we are finding very attractive, and in some cases compelling, longer-term opportunities

As Scotia strategist Hugo Ste-Marie indicated in a recent strategy piece, “Quality has not offered the level of outperformance that would be more typical of the style”. Although this style has been out of favour more recently, we remain confident in its ability to produce attractive risk-adjusted investment returns over the long term. Following the recent market selloff, we are finding very attractive, and in some cases compelling, longer-term opportunities within our investment portfolios, offering excellent opportunities for long-term investors.

To recap, it has been a challenging period in financial markets and we expect market volatility will continue until the macro outlook improves. In periods of market volatility, it is important to stay focused on longer-term investment objectives, remain disciplined and stick to a well-defined investment strategy. We remind investors that markets are forward-looking, and equities will lead the economic recovery. It is typically in the final months of recession when sentiment is weak that equity markets will begin to rebound, and the combination of an earnings recovery and a valuation re-rate can produce very attractive equity returns. Patient, long-term investors will ultimately be rewarded for their discipline.

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We wish all of our readers a happy, healthy and prosperous year ahead. As always, please do not hesitate to reach out with any questions or concerns.

Warm regards,
The Seymour Team