VALUE CONTRARIAN
ASSET MANAGEMENT

2022
Full Disclosure

Over the coming years we want to advise investors that the Value Contrarian Fund **may** be **more volatile** than has been the case in the past. Here is our reasoning:

1) When your Fund is fully invested, we are subject to the full volatility of the financial markets. As we don't short stocks, **cash** is often the simplest, risk-free instrument to bluntstock market volatility.

2) Berkshire Hathaway, Warren Buffett's investment vehicle, represents approximately 20% of your fund's assets. We view this as a strong investment in all market conditions. Nonetheless, there will be years (like 2019 & 2020) where Berkshire underperforms the market and will impede your Fund's returns.

3) In general, a rising Canadian dollar and a weakening US dollar will also affect your Funds results, due to our significant U.S. holdings. Presently, the Canadian dollar is approximately 74.5¢. However, if over the coming years it rose to 85¢ or 89¢, this would add a stiff headwind to your fund's net results.

Predicting currency moves is about as easy as predicting the weather this time next year. Good Luck!

Benjamin Horwood

Bank of Commerce Centre
1155 boul. René Lévesque W., Suite 2500
Montréal, Québec
H3B 2K4, Canada

Tél. : +1.514.398.0808
Fax : +1.514.398.9602
info@valuecontrarian.com
www.valuecontrarian.com

2022 Third Quarter
Value Contrarian Equity Fund

Dear Partners,

> **We're now going through a period which is <u>payback time</u> [for the excesses during the 2009-2021 period of super cheap money/interest rates].**
>
> **Nick Moakes**
> **Chief Investment Officer**
> **Wellcome Trust**
> **December 1, 2022**

> **I'm surprised how little the market realises how far the Fed might go [and] how little investors care about <u>monetary credibility.</u>**
> **[Meaning Chairman Powell wants to go down in the history "credibility" books as an <u>inflation slayer</u> Aka: <u>Paul Volker</u>, and <u>not</u> seen as an <u>inflation spreader</u>, Aka: Fed Chairman <u>Arthur Burns</u>]**
>
> **Tatjana Puhan**
> **Deputy Chief Investment Officer**
> **Tobam Asset Managers**
> **December 1, 2022**

> **The idea is that we can engineer a painless reversal in inflation without sustaining damage to the real economy... That idea is <u>not based on prior historical experience</u>, and I don't think it's in the cards.**
>
> **Carmen Reinhart**
> **Chief Economist – World Bank**
> **May 13, 2022**

The Fed raised interest rates this year at the most rapid pace since the late 1970's/early 1980's to battle inflation that is running near 40-year highs. Long dormant inflation had been picking up as the pandemic lockdowns were easing. Over the past two years, with all the over-the-top covid stimulus programs and supply chain bottlenecks, the economy and job markets have been on steroids! The Russian invasion of Ukraine was another strong catalyst stoking the inflation fires.

The Fed's inflation fighting game plan, at its core, is simple. Reduce inflation by slowing the economy through higher interest rates, lower stock prices and a stronger dollar. Combined, this typically <u>curbs demand</u>. In particular, Chairman Powell seems convinced that the <u>job market needs to weaken</u> to get wages and in turn inflation under control.

Historically, the recent <u>inverted yield curves</u> (whereby short term rates are higher than long term rates) is indicative of a red flashing warning: <u>Recession Dead Ahead</u>! At the end of the day, rate increases <u>take time to work their way through the economy</u>. Thus, central banks, might not know for years if they have tightened <u>too much</u>, or <u>not enough</u>. This is where <u>today's investor "exuberance" may be jumping the gun</u>!

In our opinion, it will take time to work through the excesses created by years of ultra low to zero interest rates and the flood of easy Covid money. It may take more pain than expected to put this "<u>inflation genie</u>" back in its bottle. Stopping a fully loaded freight train is no easy task!

Only time, and hindsight, will tell if we are entering a 5-7 year period of what I call a "Phoney Bull Market"** (see below). Of course, any future oil crisis or geopolitical showdowns, will only create further conditions for market weakness!

A very important question for investors to ponder: will 2022/2023 represent the ultimate bear market lows of this cycle? Or will the ultimate lows only be reached during a future bear market – <u>date unknown</u>. If the latter scenario is the case, then the intervening years are what your manager calls a "<u>Phoney Bull Market</u>".

****A Phoney Bull Market is a period in which: 1) Record stock market index highs are made, but not permanently, <u>only temporarily</u>. 2) When the most recent bear market lows are surpassed on the downside in <u>future bear markets</u>. Example: the bear market lows of 2002 were surpassed by new lower lows in March 2009. The bear lows of 1966 & 1970 were ultimately surpassed by new lower lows in November 1974. <u>In simple terms, in a Phoney Bull Market, the first bear bottom does not represent the ultimate future bear market lows</u>! Sometimes, it takes <u>a few bear markets</u> to reach the cycle bottom! <u>Ouch!</u>**

Third Quarter Performance

> **One of the things I've learned over my nearly 40 years of doing this is markets are pretty smart, <u>but</u> that doesn't always mean that at any moment they're 100% right.**
>
> **David Solomon**
CEO Goldman Sachs
December 12, 2022 – Wall St Journal

> **The conditions for a fundamental <u>bear market low</u> never occur when the Fed is still <u>raising rates</u> (in the here and now) and into an <u>inverted yield curve</u>.**
>
> **David Rosenberg**
Rosenberg Research
November 11, 2022

> **Now money has a cost. You can't just throw money at unprofitable businesses, very risky businesses. We need to have a much more sensible allocation of capital.**
>
> **Alexandra Moris**
Chief Investment Officer
Skagen Funds Norway
December 1, 2022

Your Fund ended the third quarter with a net asset value of <u>$3,850.86</u> per unit, a decrease of <u>($352.85)</u> from the December 31, 2021 net asset value of <u>$4,203.71</u> per unit (after distribution). Your Fund returns: -(8.39%) Year to Date at September 30th.

The stock market is a great way to get rich slowly, albeit with bumps along the way. One year you're a "hero", the next you're a zero! Boasting too much, in my opinion, is simply <u>bad karma</u> in the money management business. Bringing investors some credible positive news in a down year like 2022, is certainly desirable to lift investor spirits.

The Canadian stock market (in relative terms) is having a "great" year. That's to say, not losing nearly as much as all the other major indexes. Here are the Year to Date (at November 30th) stats. Dow: -(2.89%) , S&P 500: -(13.10%) , Nasdaq-QQQ: -(25.9%) TSX Comp: -(1.00%) , VC Fund: -(0.77%).

Yes, equity markets have rallied furiously since the September 30 month end. Irrational exuberance? Delusional exuberance? When the tide goes out again, 2023 will reveal who has been swimming naked! Bring your sleep masks, as it may not be a pretty scene to watch.

2022 reminds us of the 2000-2002 tech/telecom/internet bear market sell-off. Specifically, the similarities lie in the devastation caused to the Tech sector during both eras, while the old industrial/boring companies remained relatively unscathed.

Thus today, "old economy" CP Rail, CN Rail, Thompson Corp. are all reaching 52-week highs. While Berkshire Hathaway is in positive territory year to date. Meanwhile, the sexy FAANG tech stocks are mostly in the cellar, sporting double digit stock market losses.

The VC Fund's credible performance in 2022 (so far) can be attributed to 4 basic elements:

1) Our "anchor"- An outsized position in Warren Buffett's Berkshire Hathaway stock. A hodge podge of basic industrial companies, cash and the cherry on the top - a huge dollop of Apple shares.

2) A large cash position – Approximately 28% of assets. Resulting from a combination of pruning the portfolio over the previous 12 months, and an influx of new money in 2022.

3) The Canadian dollar has fallen from 0.79 at year-end 2021 to 0.72 on September 30th. With approximately 52% of our assets linked to the US$, we have benefited from the falling Canadian dollar. A cautionary note, be prepared to see the Fund's positive FX situation reverse when the bull market resumes.

4) No major blowups. Simply stated, by not losing much, you automatically win.

In conclusion, John Kenneth Galbraith once famously said: "There are two kinds of forecasters: those who don't know, and those who don't know they don't know".

Your fund manager will tell you straight out – "I know I don't know" the short to medium term direction of the stock markets – however, it's always fun to put on my 33 year old fund manager thinking cap and take a "guess" on the future:

1) The 2023 bear lows, may subsequently usher in a few years of a "Phoney Bull Market, including new record market highs. But, it's our hunch that the ultimate market lows will only be reached in some future bear market further down the road.

2) Fed Chairman Powell does not want to go down in the history books with an egg on his face for not being aggressive enough in the fight to tame the inflation tiger. New market lows are always a distinct possibility in 2023.

3) In a real recession, both old economy and new economy sectors are devastated. That has not occurred so far in 2022. Until that happens, a true business/stock market cycle bottom has not been reached.

4) Over the long-term (15+ years), the markets will rise with the economy.

5) Long term – as Buffett says, "Never bet against America".

OUTLOOK

History teaches us that soft landings [in the economy] represent the triumph of hope over experience.

Larry Summers
Harvard Economics Professor
Fortune Interview Oct/Nov 2022

[Chairman Powell] has told associates that he hasn't changed his view that the bigger mistake the Fed could make would be to fail to get inflation under control.

Nick Timiraos
Wall St Journal
December 5, 2022

The only function of economic forecasting is to make Astrology look respectable.

John Kenneth Galbraith
Economist

Rising interest rates, rising interest rates, rising interest rates. The immediate effect of Fed chair Powell's tighter monetary policy is that interest rates and bond yields have "screamed higher" in 2022. That means risk assets such as stocks and real estate now have competition for your investment dollars. GIC's, and other fixed income investments, paying 4%-5%, are now a credible (short-term) investment alternative.

Simply stated, in 2022 "the case for investing in risky assets has been seriously dented". More specifically, the case for investing in unprofitable, hot fintechs or SPACs is no longer a layup.

However, pick the right "washed-out" sector in this bear market (ie; Chinese blue chip internet stocks in November) and 50% gains are possible off the bottom.
It's all about picking the undervalued sector, sector, sector.

Yes, there is long-term money to be made by investing in equities during a bear market, or a Phoney Bull Market. Patience is an important key to success, while waiting for that great "pitch". And remember, there's no obligation to swing at every pitch.

Respectfully yours,

Benjamin D. Horwood
Portfolio Manager
December 9th, 2022

Value Contrarian Equity Fund
Next Fund purchase
Date: December 23, 2022
Call today: 514 – 398-0808

P.S. Do visit us at our web site: **www.valuecontrarian.com**

**We're often asked: "When is the best time to invest in the Value Contrarian Fund?" Although there is no best time, since it is impossible to time the market, a preferable entry point is when the Fund has produced a month of negative returns or a year of underperformance. Unfortunately, human nature prefers the exact opposite.

Overall, long-term shareholders in the V/C Fund benefit from a sinking stock market, the same as a regular grocery shopper benefits from declining food prices. So when stock markets plummet – as they will from time to time – "neither panic nor mourn". It's good buying news for your Fund.