Unified

Q4 2022 Review

NATIONAL BANK FINANCIAL
WEALTH MANAGEMENT

my WEALTH UNIFIED

Looking back on the 4th quarter of 2022

Once again, the financial markets had an eventful quarter, with investor sentiment swinging back and forth between pessimism and optimism. Indeed, after a difficult start to the fourth quarter, an encouraging inflation report and an accommodating speech by the chair of the Federal Reserve led to a dramatic market rebound in November. However, this upward movement ran out of steam at the end of the year, as the markets grew concerned about aggressive rate hike projections from central banks in the face of inflation. Ultimately, quarterly performance was generally positive for both stocks and bonds, but overall, 2022 remains a challenging year for a majority of investors.

On the positive side, the slowdown in inflation was an important source of market optimism during the quarter. Not only did gasoline prices continue to fall, but more importantly, the normalization of supply chains and the decline in several commodity prices allowed durable goods inflation to decelerate significantly. In addition, the labour market remained strong and consumer spending held up; as such, economic activity in North America remained relatively healthy in recent months.

However, what is unique about the current environment is that economic "good news" are not always good news for the financial markets, as the resilience of the labour market complicates the Federal Reserve's fight against inflationary pressures. Specifically, services inflation – which is closely tied to wage growth and thus to the strength in employment – still shows few signs of slowing. Thus, the Fed brought its monetary policy into restrictive territory in November, a generally challenging environment for equities that also comes with elevated recession risks.

Going forward, a faster than expected slowdown in inflation would represent the most optimistic scenario, provided it prompts central banks to stop – or even reverse – their cycle of rate hikes sooner than anticipated and thus avoid a recession. That said, a significant risk factor remains excessive monetary tightening by a Federal Reserve that cannot afford to underestimate the persistence of inflationary pressures yet again.

Quarterly Highlights

Market Total Returns

Asset Classes	Dec	Q4	2022
Cash (S&P Canada T-bill)	**0.3%**	**0.8%**	**1.4%**
Bonds (Canada Broad Universe)	**-1.2%**	**0.0%**	**-11.5%**
Federal Government	-1.2%	-0.1%	-9.2%
Corporate	-0.5%	0.5%	-10.1%
Corporate BBB	-0.6%	0.6%	-10.5%
S&P/TSX Preferred shares	-1.7%	-3.2%	-18.1%
U.S. Corporate (US$)	-0.2%	3.5%	-15.4%
U.S. High Yield (US$)	-0.8%	4.0%	-11.2%
World Equities (MSCI ACWI US$)	**-3.9%**	**9.9%**	**-18.0%**
S&P/TSX	-4.9%	6.0%	-5.8%
S&P/TSX Small Caps	-1.8%	8.4%	-9.3%
S&P 500 (US$)	-5.8%	7.6%	-18.1%
Russell 2000 (US$)	-6.5%	6.2%	-20.4%
MSCI EAFE (US$)	0.1%	17.4%	-14.0%
MSCI Emerging Markets (US$)	-1.4%	9.8%	-19.7%
Commodities (GSCI US$)	**-1.4%**	**3.4%**	**26.0%**
WTI Oil (US$/barrel)	-0.3%	0.4%	6.7%
Gold (US$/oz)	3.4%	8.3%	-0.6%
Copper (US$/tonne)	1.7%	8.9%	-14.1%
Forex (US$ Index DXY)	**-2.3%**	**-7.7%**	**7.9%**
USD per EUR	3.7%	8.9%	-6.2%
JPY per USD	-5.0%	-9.4%	13.9%
CAD per USD	1.1%	-2.0%	7.2%

CIO Office (data via Refinitiv, as of 2022-12-30)

CIO Office (data via Refinitiv)

Fixed Income

- Canadian bonds posted losses in December as medium and long-term yields rose in the face of hawkish Central Bank discourse.
- As a whole, 2022 is actually the worst year in history for Canadian bonds (-11.5%). This loss is in addition to the decline seen in 2021 (-2.7%), marking the first time the Canadian bond universe has experienced two consecutive annual declines.

Equities

- The dramatic stock market rebound of the fourth quarter ran out of steam in December, particularly in North America. The S&P/TSX (-4.9%) and S&P 500 (-5.8%) underperformed the EAFE region (+0.1%) and emerging markets (-1.4%).
- However, for the full year, the S&P/TSX (-5.8%) was an impressive outperformer, benefitting from strong exposure to commodities. It was a much more challenging period for the MSCI EAFE (-14.0%), the S&P 500 (-18.1%) and MSCI Emerging Markets (-19.7%), all of which posted their worst annual performances since 2008.

FX & Commodities

- In December, the price of oil declined for the sixth time in seven months. Thus, despite the Russian invasion of Ukraine and the dramatic rebound that followed, oil prices end the year with a relatively modest gain of 6.7%.
- On the currency front, the U.S. dollar declined in December, particularly against the euro. It was a different story for the year as a whole, as the Greenback appreciated significantly amid aggressive monetary tightening by the Federal Reserve.

Fixed Income | Index Plus

Your Fixed Income investments are divided to diversify, produce steady income, and protect your money. Cost is managed to ensure you retain as much of your income as possible.

Target Asset Allocation

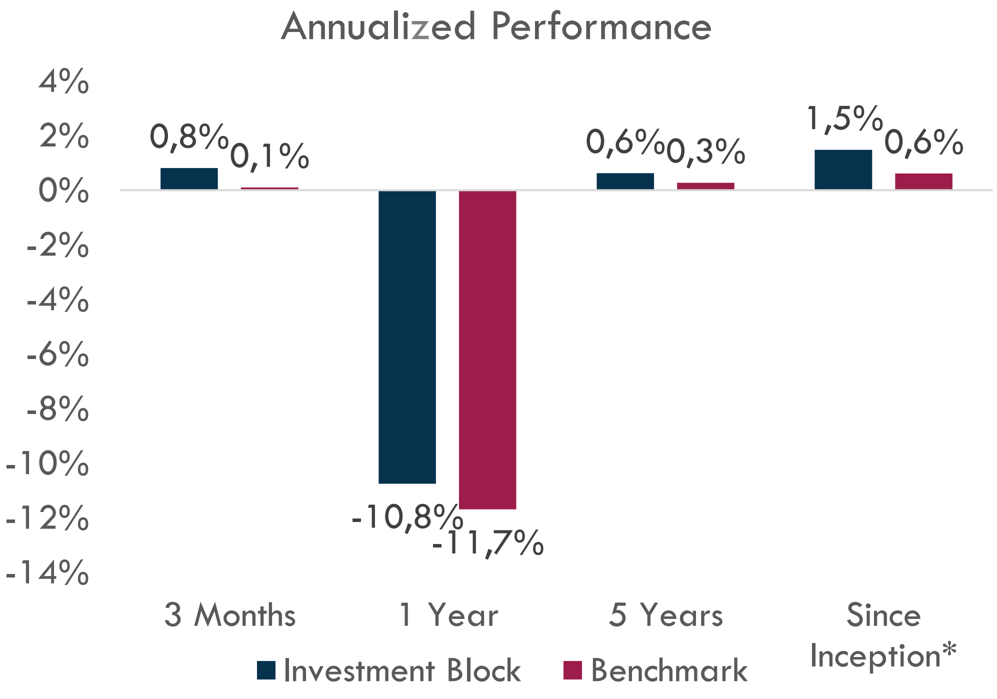
iShares High Quality Canadian Bond	25.5%
Vanguard Canadian Aggregate Bond	23.3%
Horizons Active Corporate Bond	20.5%
PIMCO Monthly Income ETF	15.1%
BMO Mid Provincial Bond	10.1%
Horizons Active Preferred Share ETF	5.5%

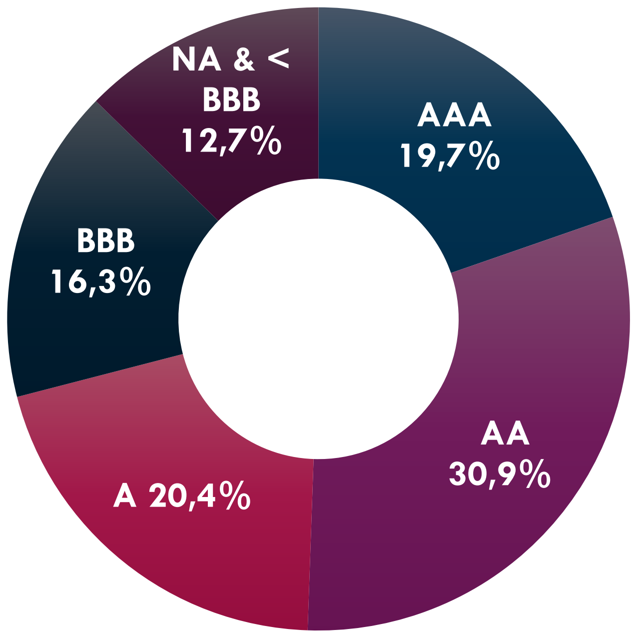
Statistics

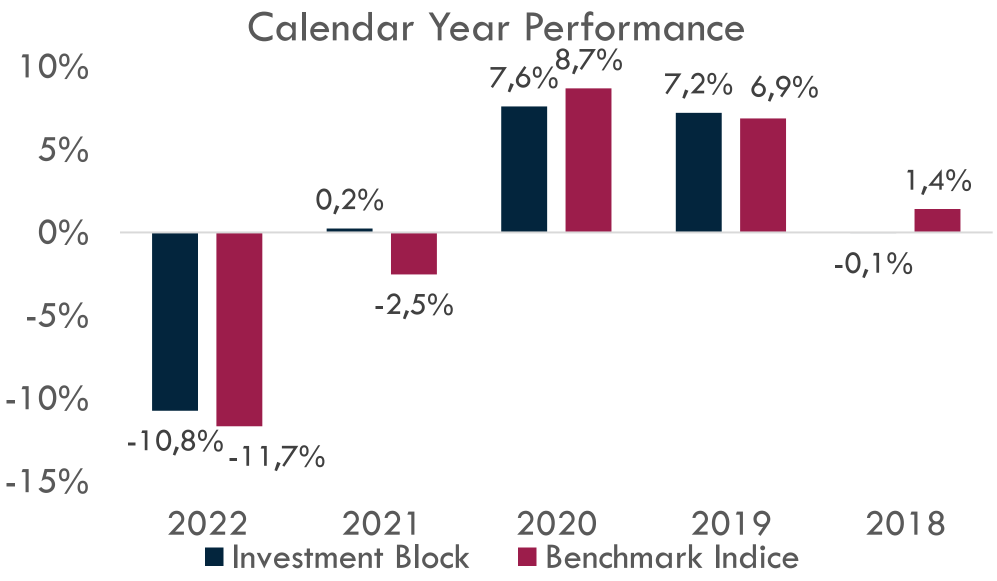
Yield to Maturity	4.13%
Duration	5.93

Benchmark

FTSE Canada Universe Bond







Comments

Shorter duration than the benchmark.

Overweight in quality corporate bonds.

Global diversification is used to diversify and mitigate risk.

Canadian Equity | Income Blend

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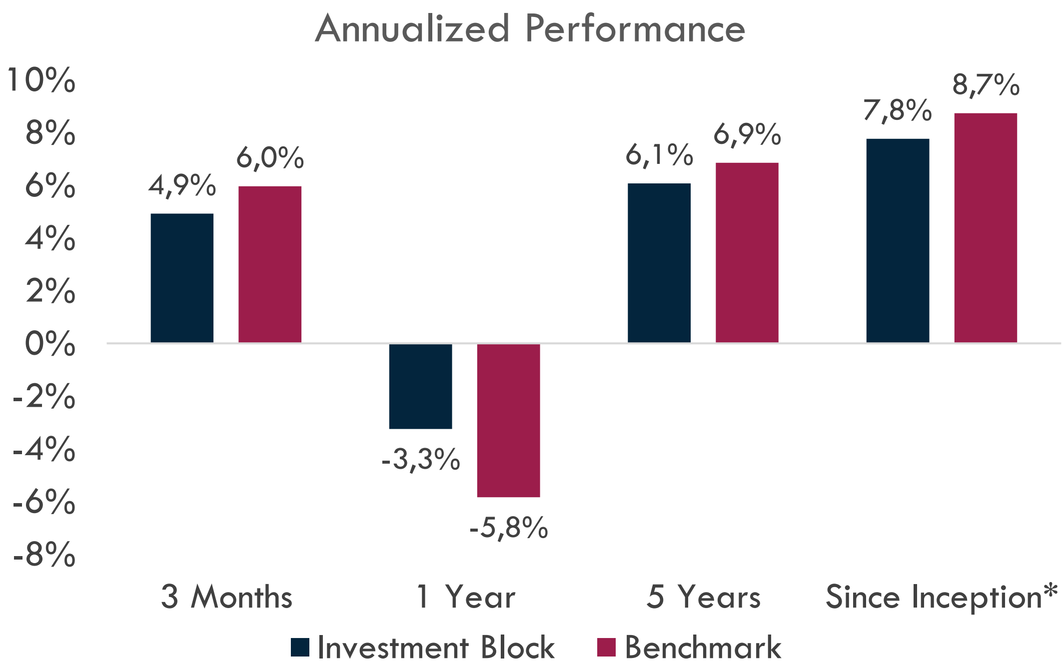
Your Canadian equity holdings are comprised of a blend of hand selected and broad-based investments, designed to achieve the ideal combination of wealth preservation, long term investment results, and cost control.

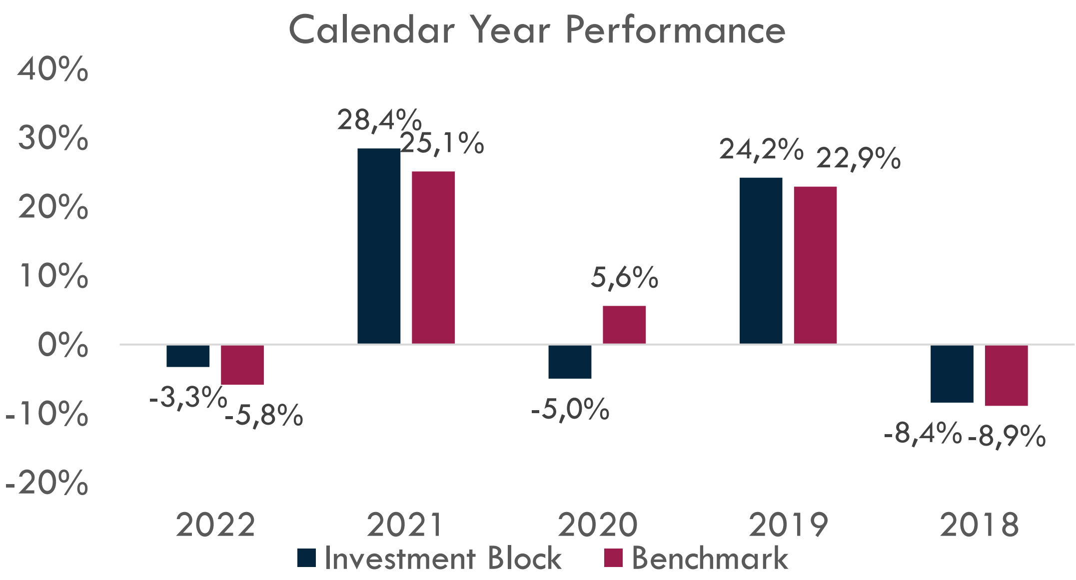
Target Asset Allocation

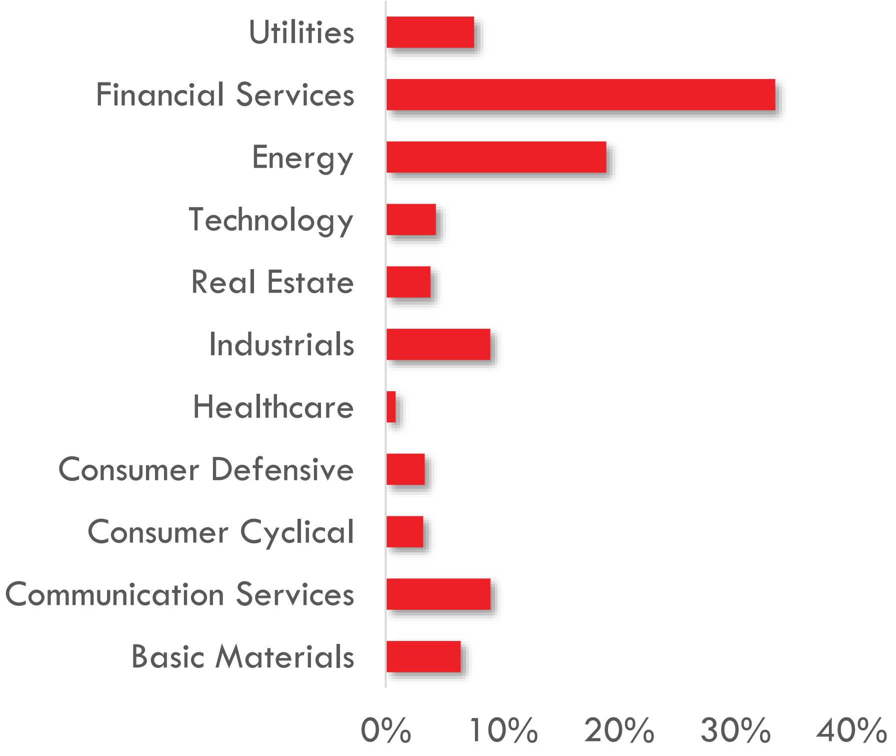
NBI Equity Income (Montrusco Bolton)	25.3%
iShares S&P/TSX High Dividend Composite Index	24.1%
Mackenzie Canadian Dividend	20.1%
Fidelity Canadian Core Equity	15.3%
BMO S&P/TSX Composite Index	15.2%

Benchmark

S&P/TSX Composite TR







Comments

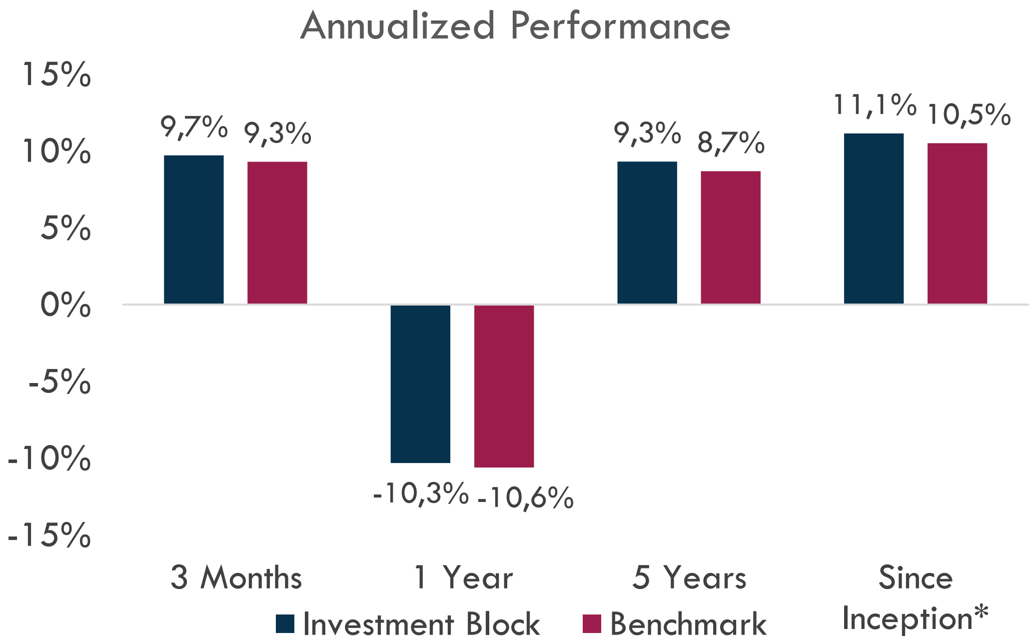
Overweight in large cap stocks compared to the index.

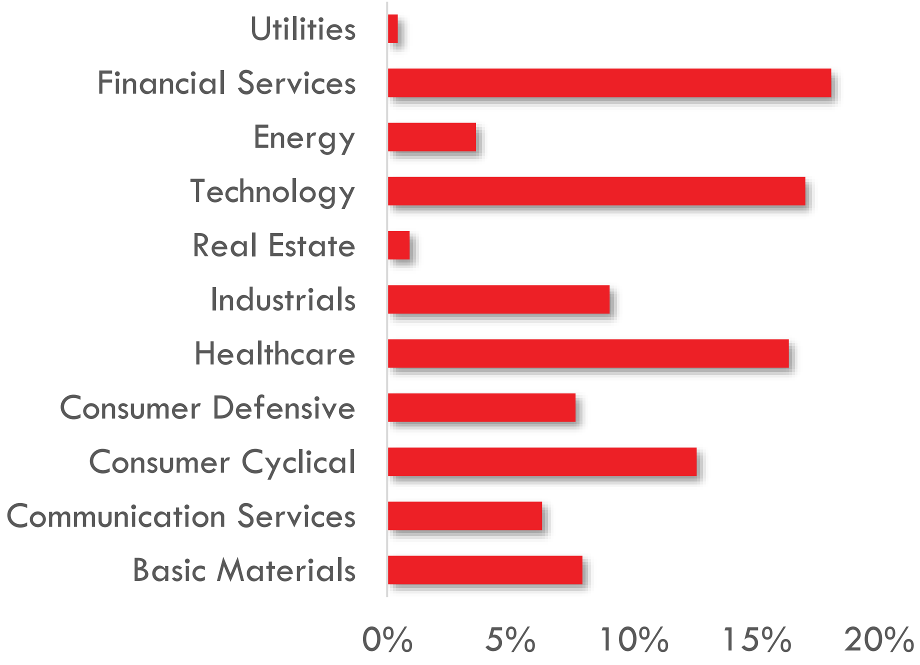
Bias for value and dividend-paying stocks.

Overweight equities from defensive sectors.

Global Equity | Pure Active

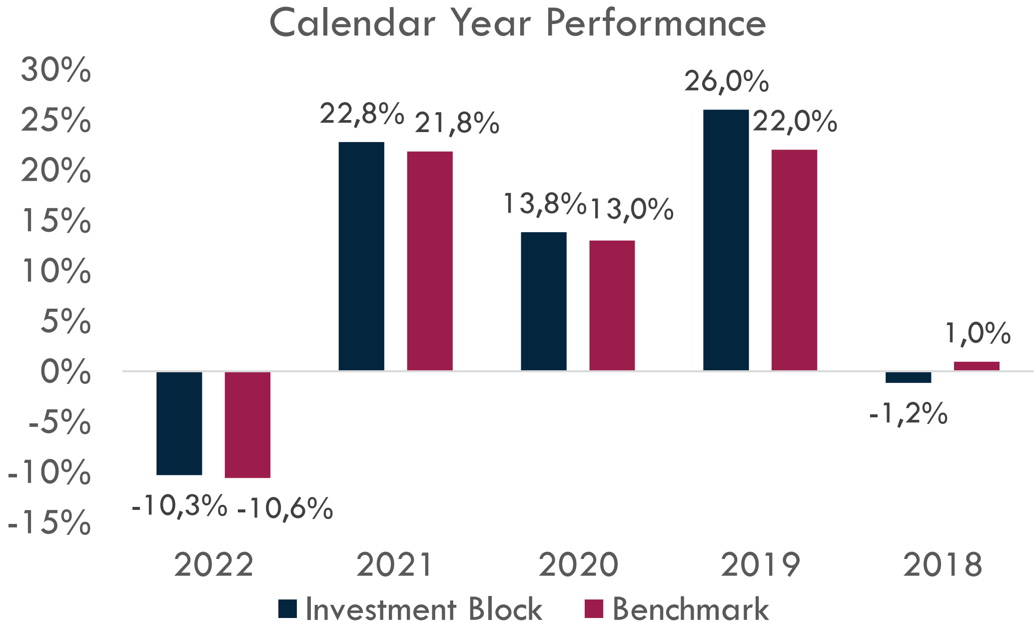
Your Global equity holdings are invested by managers with proven track record of identifying high-quality investments from around the world. You will benefit from global growth through hand selected investments.





Target Asset Allocation

NBI US High Conviction Equity Hedged (Fiera)	34.3%
Mackenzie Global Dividend	29.5%
Fidelity International High Quality Index ETF	15.0%
Fidelity American Core Equity	14.4%



Benchmark

NBF Global Equity Benchmark

Comments

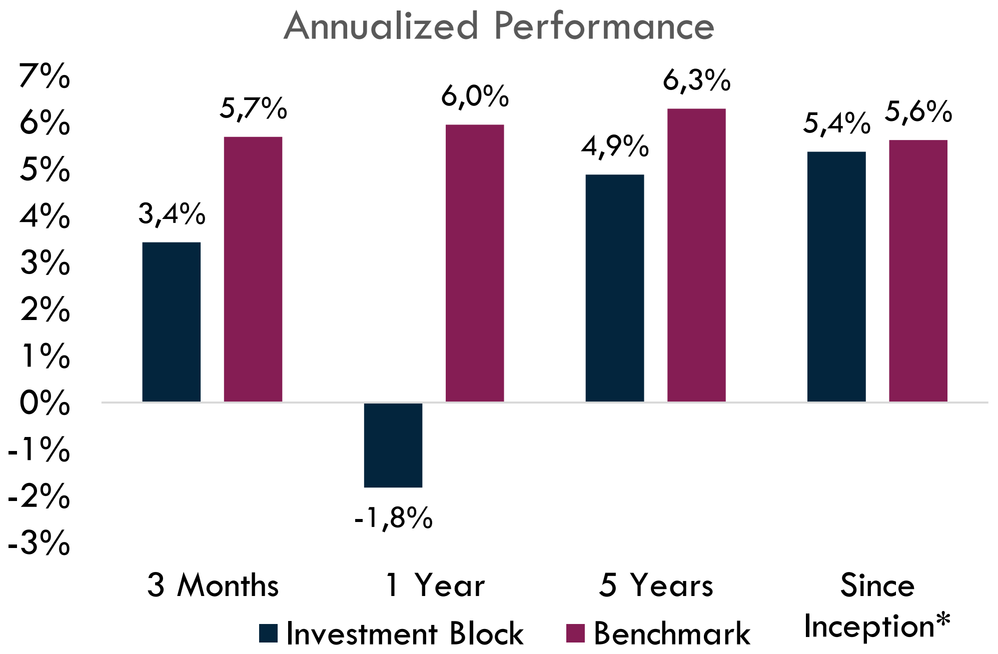
The market cap is similar to the benchmark.

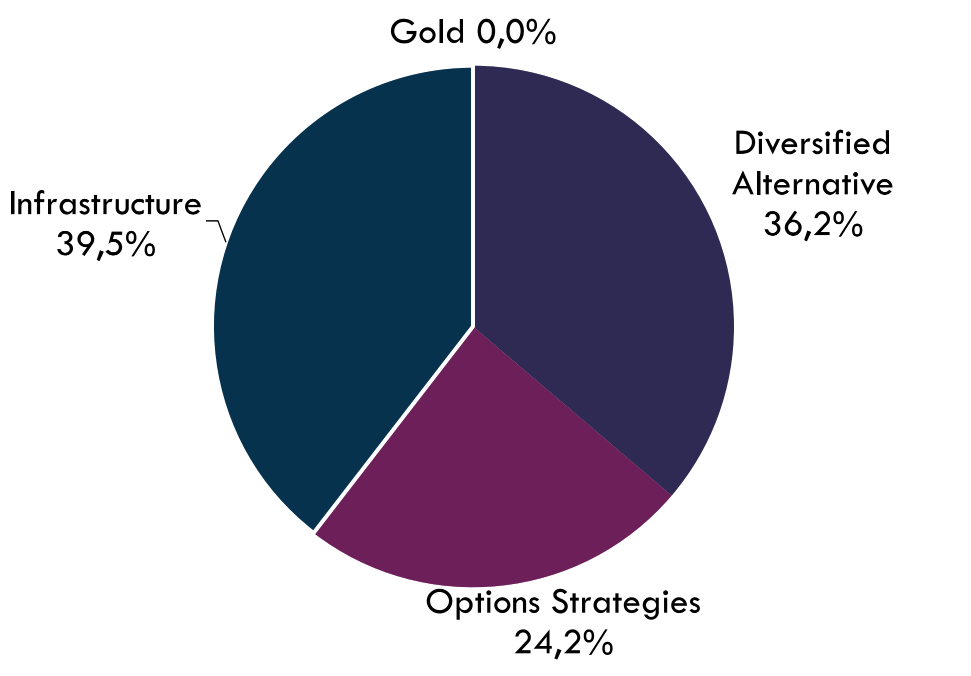
Overweight position in quality and growth at reasonable price (GARP) stocks.

50% of the U.S. Equity exposure is hedged against the $CAD.

Alternatives | Blend

Your holdings in Alternatives will be invested in a combination of publicly traded infrastructure as well as non-traditional strategies, designed to reduce fluctuation within your portfolio and to generate income.



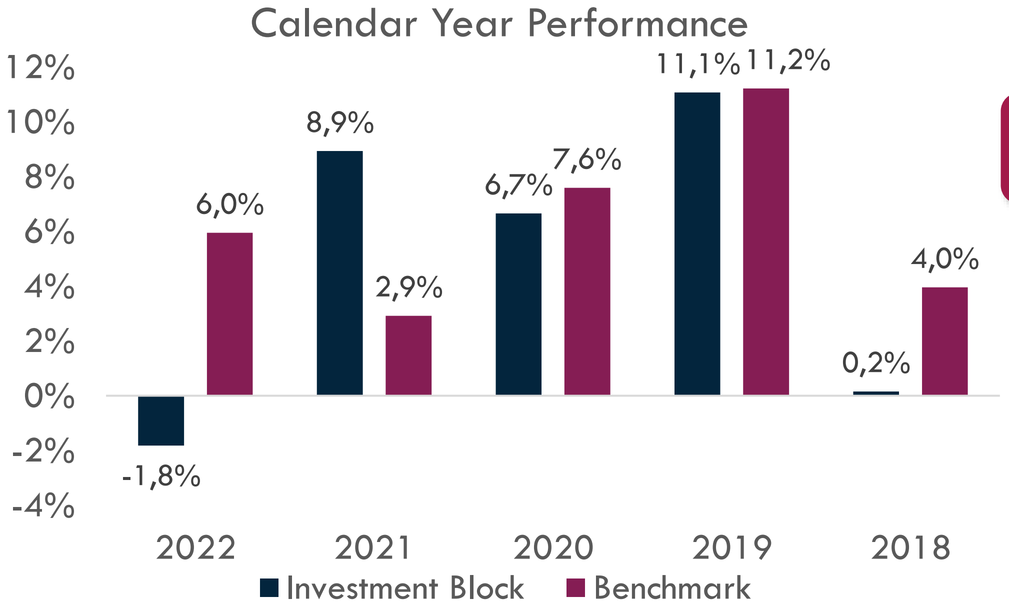


Target Asset Allocation

NBI Real Assets Pooled Fund	26.5%
Mackenzie Diversified Alternatives	24.8%
iShares Global Infrastructure Index ETF	13.1%
Dynamic Premium Yield	12.8%
NBI Liquid Alternatives	11.4%
Structured Payoff Strategies Pooled Fund	11.4%

Benchmark

NBF Alternative Benchmark



Comments

Diversified mix of alternative strategies to smooth out returns and reduce portfolio volatility.

Infrastructure and real assets hold a mix of private and listed investments such as real estate, farmlands, timberlands and infrastructure assets that provide regular cash flows, protect against inflation and reduce your portfolio overall risk.

Myths vs Reality and Historical Perspective

Being well informed and remaining objective is essential to maximize your investment success.

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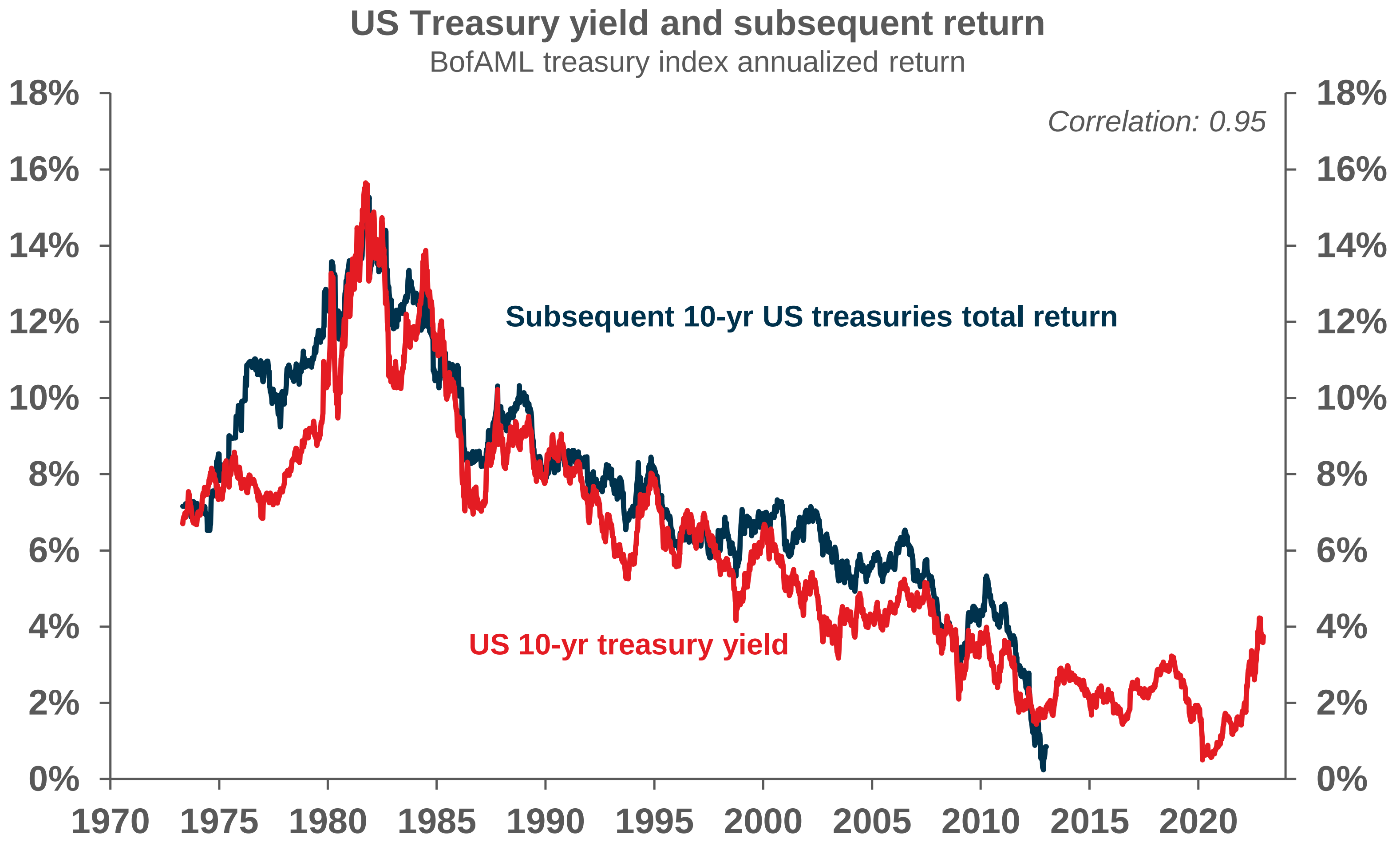
Fixed Income Return Expectations



Over an investment period matching a bond's maturity, subsequent annualized returns will match closely the starting yield to maturity.

In the case of government and investment grade bond indexes, differences between the two measures can occur due to reinvestment risk, the changes in index composition over time, as well as downgrades and defaults for non government bonds.

The Canadian bond universe posted its worst performance ever in 2022 with a 11.5% decline. However, investors can expect much more attractive return on a forward basis as the current yield to maturity of the index is now around 4% which will help make up for the heavy losses incurred earlier this year.

CIO Office (data via Refinitiv)

Are Rate Hikes Bad for Stocks?

MYTH

Stocks generally perform poorly when central banks hike their policy rate.

REALITY

Each rate hike cycle has its own set of circumstances that often bring additional volatility to markets. However, what normally prompts central banks to raise their policy rate is usually an economy that is showing strength and is expected to continue to do so; a typically favorable environment for stocks.

Case in point: since 1996, the yearly total return of the S&P/TSX averages 6.2% when the Bank of Canada hikes the overnight rate at least once, lower than the 9.3% average of all years over that same time period but still well into positive territory. Similar findings in the United States, where the average yearly total return of the S&P 500 is 8.1% when the Federal Reserve hikes its policy rate at least once.
To be clear, these historical trends are no guarantee for any specific year, as evidenced by the year 2022, whose unique circumstances led to substantial setbacks for stocks. Nevertheless, **over the long run, odds remain in favor of patient investors, regardless of the ups and downs of policy rates.**

Markets and rate hikes (data since 1996)

Canada

Year	# of rate hikes*	Total return (S&P/TSX)
1997	5	15.0%
1998	3	-1.6%
2000	4	7.4%
2002	2	-12.4%
2005	3	24.1%
2006	4	17.3%
2010	3	17.6%
2017	2	9.1%
2018	3	-8.9%
2022	16	-5.8%
Average (rate hikes)		**6.2%**
Average (all years)		**9.3%**

United States

Year	# of rate hikes*	Total return (S&P 500)
1997	1	33.4%
1999	3	21.0%
2000	4	-9.1%
2004	5	10.9%
2005	8	4.9%
2006	4	15.8%
2015	1	1.4%
2016	1	12.0%
2017	3	21.8%
2018	4	-4.4%
2022	17	-18.1%
Average (rate hikes)		**8.1%**
Average (all years)		**10.7%**

CIO Office (data via Refinitiv)

Market Timing in the Long Run

MYTH

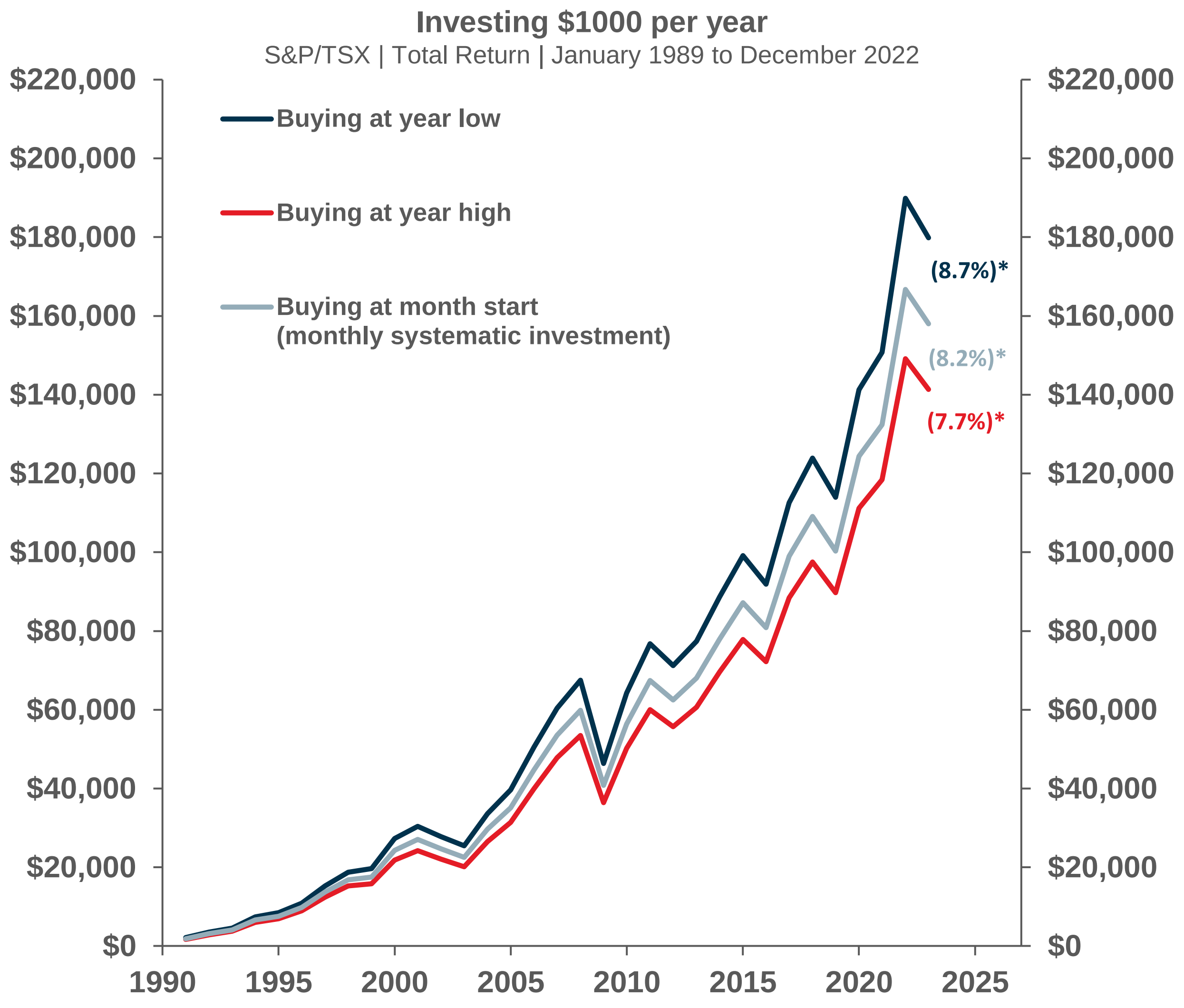
The timing of your annual savings investment is of utmost importance for the well-being of your portfolio in the long run.

REALITY

The timing of your annual savings investment will make a difference in the long run, but it is far from being the critical factor many seem to believe.

Case in point: consider an investor blessed with the power of perfect market timing (blue line) compared to another investor cursed with systematically picking the worst possible day to invest each year, over 30 years (red line). In the end, the market timing champion would have outperformed the most unfortunate of all investors by a mild 1% / year. If we take the more realistic example of an investor saving systematically at the beginning of each month, this annual outperformance shrinks below 1%.

How is such a small gap possible? Simply because in the long run, the first year's return is superfluous. **What truly matters is the frequency of savings and passage of time, not market timing.**



CIO Office (data via Refinitiv)

Reasons to Sell?

MYTH

Selling in times of heightened uncertainty can protect investments from heavy losses.

REALITY

Selling in times of heightened uncertainty is generally the best way to ensure heavy losses, as it often rhymes with selling low and missing the rebound.

More importantly, one should keep in mind that **the only certainty is that there will always be uncertainty, as it is the price to pay for capital appreciation in the long run.**

And – need we add – it isn't in the media's best interest to report the latest news with nuance and historical perspective; better to let fear and pessimism easily set in. However, **the chart on the right should act as a reminder that letting emotions take over is a good recipe for short-term gain, but long-term pain.**

CIO Office (data via Refinitiv)

Average Return?

MYTH

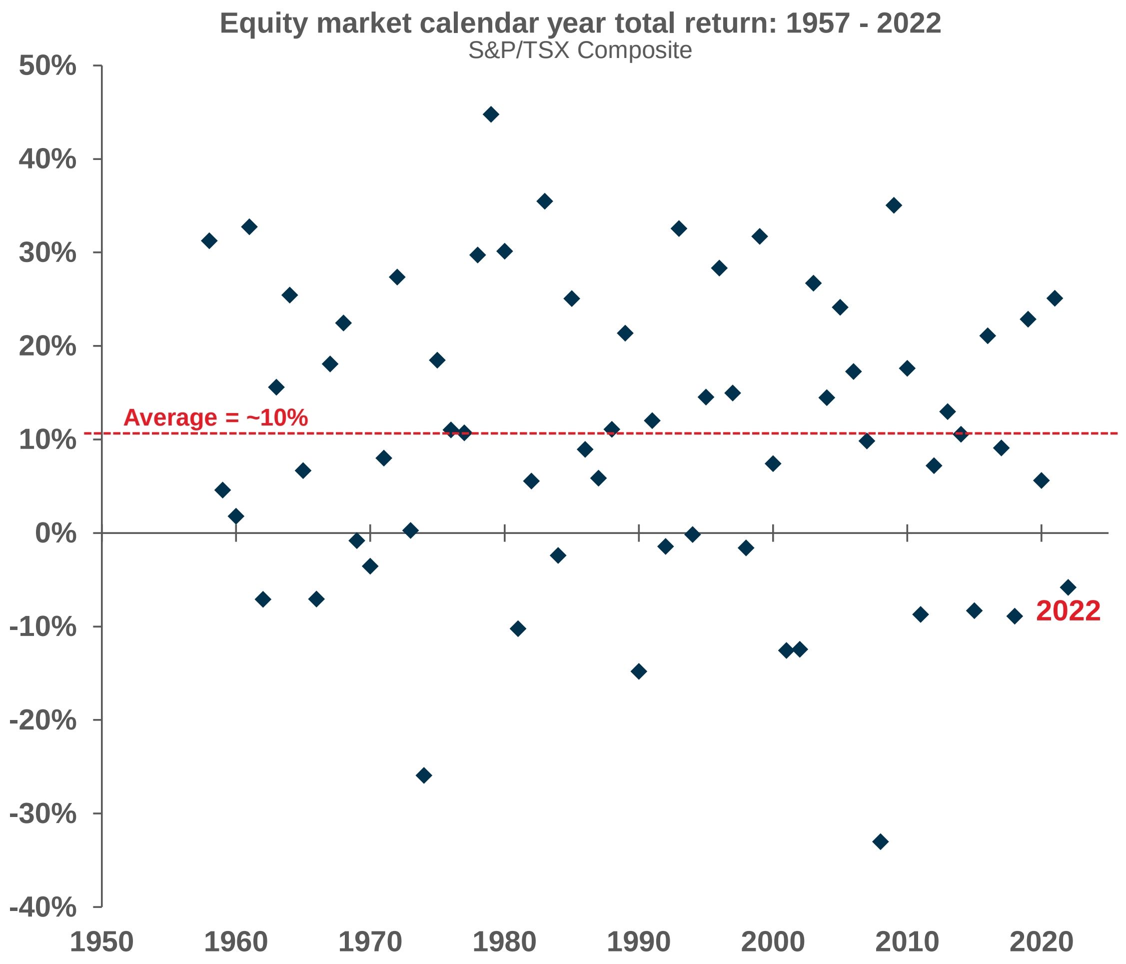
Since the long-term historical average annual return on the stock market is ~10%, investors should expect to see calendar-year returns near 10%.

REALITY

Quite the contrary, it is likely that investors will only rarely see a calendar year where equity returns are close to their long-term historical averages. Case in point: since 1957, only 8 years out of 63 have seen the Canadian stock market generate performance near average (+/- 2%).

One likely reason for this myth is the common misconception that "average" is synonymous with "typical." However, there is no such thing as a "typical" year in the stock market.

As a result, **investors should expect a wide range of possible outcomes in any given year, whereas only the passage of time can lead to an annualized return near the market's long-term average.**



CIO Office (data via Refinitiv)

Equity Performance in the Long Run

MYTH

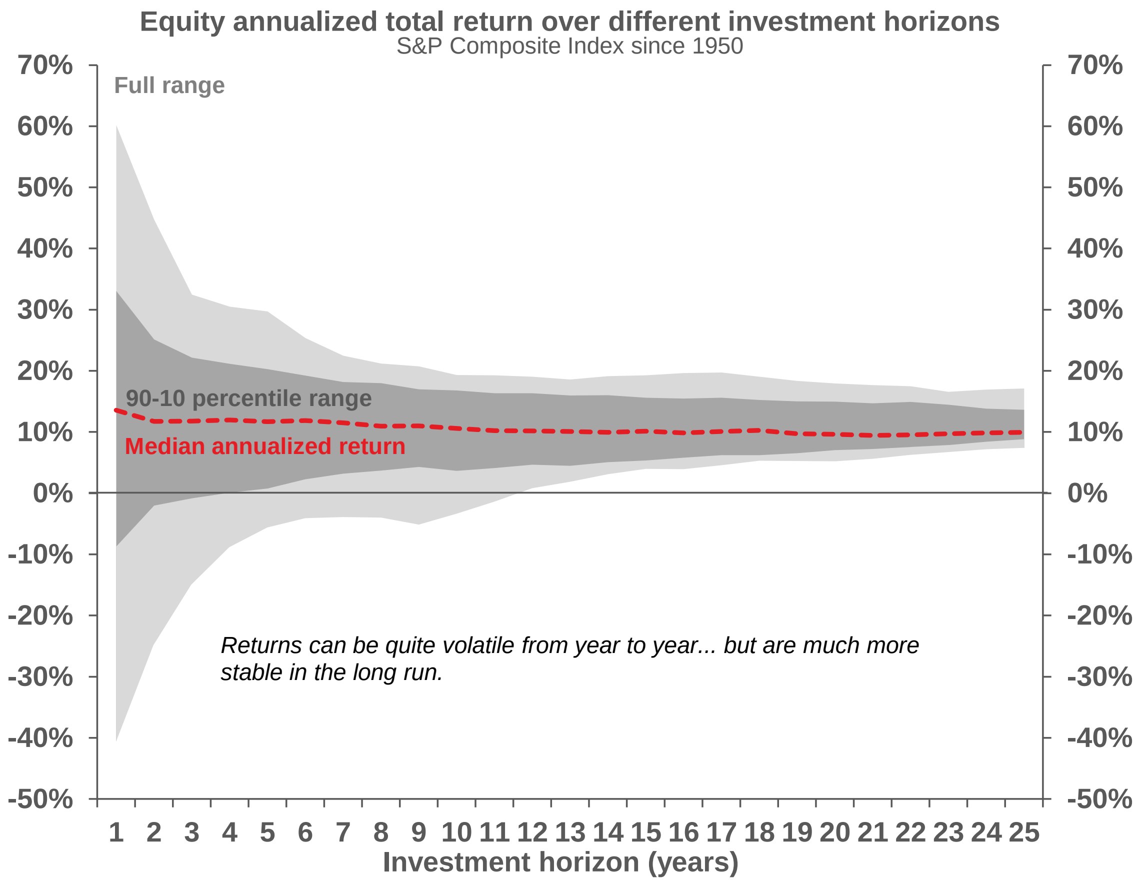
Investing in the stock market is akin to gambling at a casino.

REALITY

It is true that daily market fluctuations resemble a coin toss. Nevertheless, two fundamental reasons make investing completely different from gambling.

First, unlike the world of gambling, investing in the stock market is not a zero-sum game, as evidenced by the positive median annualized return (red dotted line). In the long run, equity returns come from companies' ability to grow their earnings, not from other investors' misfortune.

Second, while gambling remains just as uncertain no matter how long you "play", the opposite occurs within equity markets, as evidenced by the narrowing range of outcomes over time (grey area). The longer one "plays" (i.e. remains invested), the greater the chances are of converging towards the premium investors earn for bearing equity risk.



CIO Office (data via Robert J. Shiller at http://www.econ.yale.edu/~shiller/data.htm)

Home Country Bias

MYTH

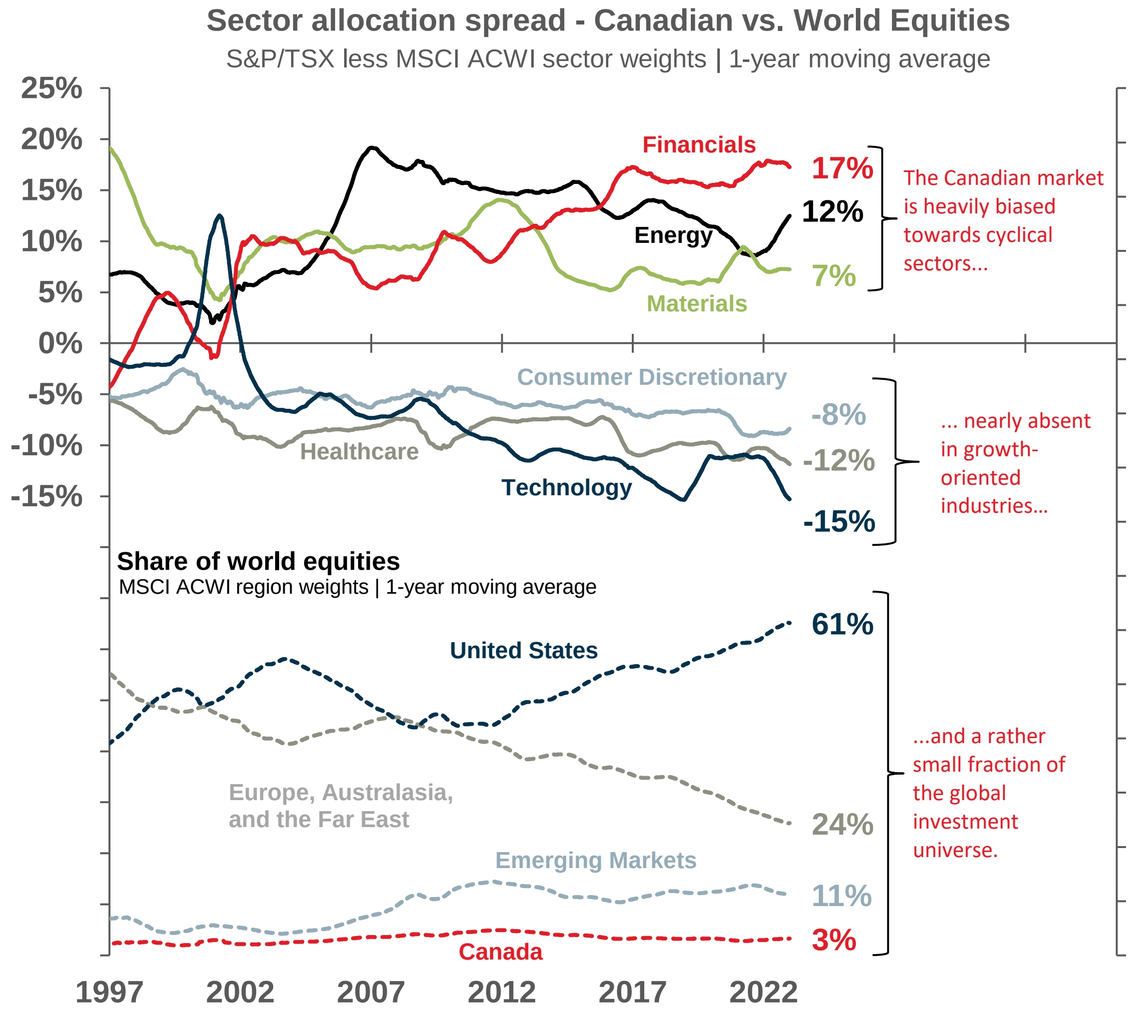
It is more prudent to invest most of your portfolio in companies domiciled at home and thus of greater familiarity than to “risk it” with foreign corporations.

REALITY

While predominantly investing in domestic equities might seem sufficient and feel comforting, such a portfolio could, in fact, be just the opposite. **Do not confuse familiarity with safety.**

For instance, Canada’s stock market’s high concentration in some of the most cyclical sectors and its relative lack of growth-oriented companies poses a risk that can result in unpleasant surprises if left undiversified.

The good news is that there are plenty of opportunities abroad to complement for such risks. After all, Canadian stocks only represent 3% of the global equity investment universe… a far cry from the ~45% they account for in Canadians’ portfolios*. Home bias indeed!



* "Coordinated Portfolio Investment Survey" for 2014-2018.

CIO Office (data via Refinitiv) *Estimate base on an average from FMI’s

Should Investors Fear Recessions?

MYTH

Investors should be fearful of recessions as they entail heavy financial losses.

REALITY

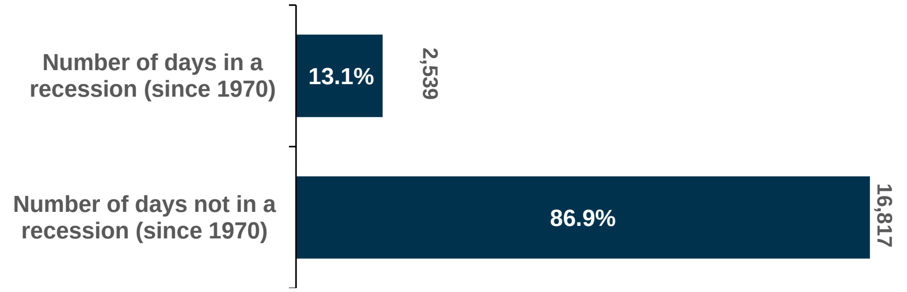
It is true that the most turbulent periods for markets are generally concomitant with recessions. As such, those with eyes riveted on daily stock exchange prices are very likely to experience fear in times of economic downturn.

However, if we step back from market fluctuations and look, rather, at the historical performance of a basic balanced portfolio (60% stocks, 40% bonds) during the last six recessions, we see that the average return was actually zero. Not something to celebrate, but far from the financial catastrophe many seem to believe – especially when we consider returns in the previous and following years. What's more, let's not forget that recessions are relatively rare events, covering only 17% of the last 50 years.

Therefore, **it is not the recession that investors should fear, but fear itself… or rather the risk of materializing heavy losses, when in the grip of emotion, at an untimely moment.**

Balanced portfolio (60/40)* total return

Recessions (NBER)	12-months Before	During Recession	12-months After	Full period**
Nov 1973 - Feb 1975	7%	-7%	12%	11%
Jan 1980 - Jun 1980	11%	9%	7%	31%
Jul 1981 - Oct 1982	9%	15%	26%	57%
Jul 1990 - Feb 1991	4%	6%	9%	21%
Mar 2001 - Oct 2001	-1%	-5%	-8%	-14%
Dec 2007 - May 2009	1%	-16%	9%	-8%
Feb 2020 - March 2020	16%	-9%	22%	28%
Average	**7%**	**-1%**	**11%**	**18%**



Data via Refinitiv. *60% MSCI World (in CAD) 40% ICE Bofa Broad Canada Universe (FTSE 91-day index for the 1973-1975 recession).
**Total return from 12-months before a recession until 12-months after a recession. Recession dates are from the NBER.

Are GICs a Risk-Free Alternative?

MYTH

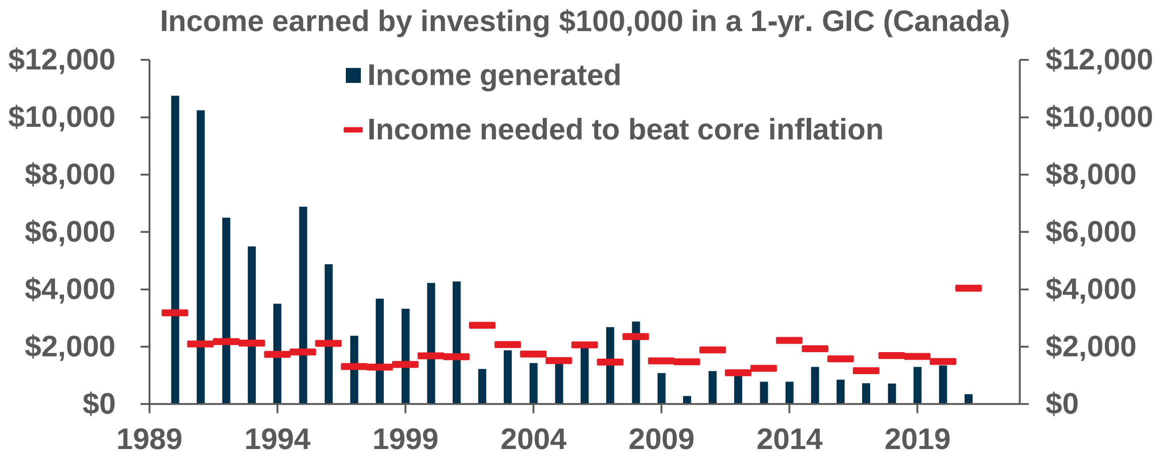
Guaranteed Investment Certificates (GICs) offer a risk-free alternative for investors seeking to at least preserve the purchasing power of their assets.

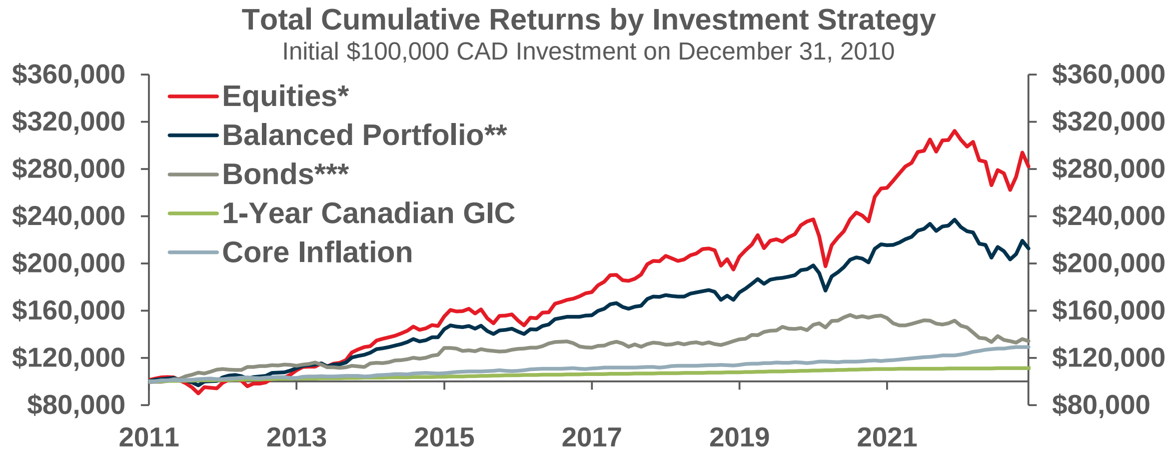
REALITY

GICs are indeed among the safest investment vehicles available. However, their returns, while guaranteed, generally fail to cover inflation, leaving their holders at risk of seeing their purchasing power decline over time.

It should be specified that this observation is a reflection of the low interest rate environment prevailing over the past several years. For instance, although a 1-year GICs provided income above inflation in the 1990s, this has not been the case since 2009.

Ultimately, the selection of an investment vehicle depends on risk tolerance - GICs may therefore be the right choice for some. However, **a key risk for investors whose investment horizon is measured in years may not be the short-term volatility of other assets, but rather the potential erosion of their purchasing power over the long run.**





Data via Refinitiv. *35% S&P 500, 35% S&P/TSX, 20% MSCI EAFE, 10% MSCI EM; all in CAD. **60% Equities, 40% Fixed Income ***100% ICE Bofa Broad Canada Universe

CIO Office

Back to basics: Diversification

Over short periods of time, asset classes will take turns out-performing and under-performing. A diversified portfolio helps protect your investments against market fluctuations.

2014	2015	2016	2017	2018	2019	2020	2021	2022
S&P 500 13.7%	**Balanced* 6.7%**	S&P/TSX 21.1%	MSCI Emerging 37.8%	Cash 1.5%	S&P 500 31.5%	Gold 20.9%	Commodities 40.4%	Commodities 26.0%
Balanced* 11.8%	Canadian Bonds 3.6%	US High Yield 17.5%	MSCI EAFE 25.6%	Canadian Bonds 1.3%	S&P/TSX 22.9%	MSCI Emerging 18.7%	S&P 500 28.7%	Cash 1.4%
S&P/TSX 10.6%	S&P 500 1.4%	S&P 500 12.0%	S&P 500 21.8%	**Balanced* -1.5%**	MSCI EAFE 22.7%	S&P 500 18.4%	S&P/TSX 25.1%	Gold -0.7%
Canadian Bonds 9.1%	Cash 0.7%	MSCI Emerging 11.6%	Can. Pref. Shares 13.6%	US High Yield -2.3%	MSCI Emerging 18.9%	**Balanced* 9.8%**	Can. Pref. Shares 19.3%	S&P/TSX -5.8%
Can. Pref. Shares 6.8%	MSCI EAFE -0.4%	Commodities 11.4%	Gold 12.8%	Gold -2.8%	Gold 18.0%	Canadian Bonds 8.6%	MSCI EAFE 11.8%	CADUSD -6.8%
US High Yield 2.5%	US High Yield -4.6%	Gold 7.7%	**Balanced* 9.7%**	S&P 500 -4.4%	Commodities 17.6%	MSCI EAFE 8.3%	**Balanced* 11.1%**	**Balanced* -10.1%**
Cash 1.0%	S&P/TSX -8.3%	Can. Pref. Shares 7.0%	S&P/TSX 9.1%	CADUSD -7.8%	**Balanced* 15.6%**	US High Yield 6.2%	US High Yield 5.4%	US High Yield -11.2%
Gold -1.7%	Gold -10.9%	**Balanced* 7.0%**	US High Yield 7.5%	Can. Pref. Shares -7.9%	US High Yield 14.4%	Can. Pref. Shares 6.2%	CADUSD 0.8%	Canadian Bonds -11.5%
MSCI Emerging -1.8%	MSCI Emerging -14.6%	CADUSD 3.0%	CADUSD 6.8%	S&P/TSX -8.9%	Canadian Bonds 7.0%	S&P/TSX 5.6%	Cash 0.2%	MSCI EAFE -14.0%
MSCI EAFE -4.5%	Can. Pref. Shares -14.9%	Canadian Bonds 1.5%	Commodities 5.8%	MSCI EAFE -13.4%	CADUSD 5.0%	CADUSD 2.0%	MSCI Emerging -2.2%	Can. Pref. Shares -18.1%
CADUSD -8.6%	CADUSD -16.0%	MSCI EAFE 1.5%	Canadian Bonds 2.7%	Commodities -13.8%	Can. Pref. Shares 3.5%	Cash 1.1%	Canadian Bonds -2.7%	S&P 500 -18.1%
Commodities -33.1%	Commodities -32.9%	Cash 0.5%	Cash 0.6%	MSCI Emerging -14.2%	Cash 1.7%	Commodities -23.7%	Gold -4.3%	MSCI Emerging -19.7%

CIO Office (data via Refinitiv, as of 2022-12-30)

*A 60% stocks / 40% bonds portfolio made of: 21% S&P/TSX, 21% S&P 500, 12% MSCI EAFE, 6% MSCI Emerging Markets and 40% ICE BofA Canada Broad Market, all in C$.

Historical Perspective on Bear Markets

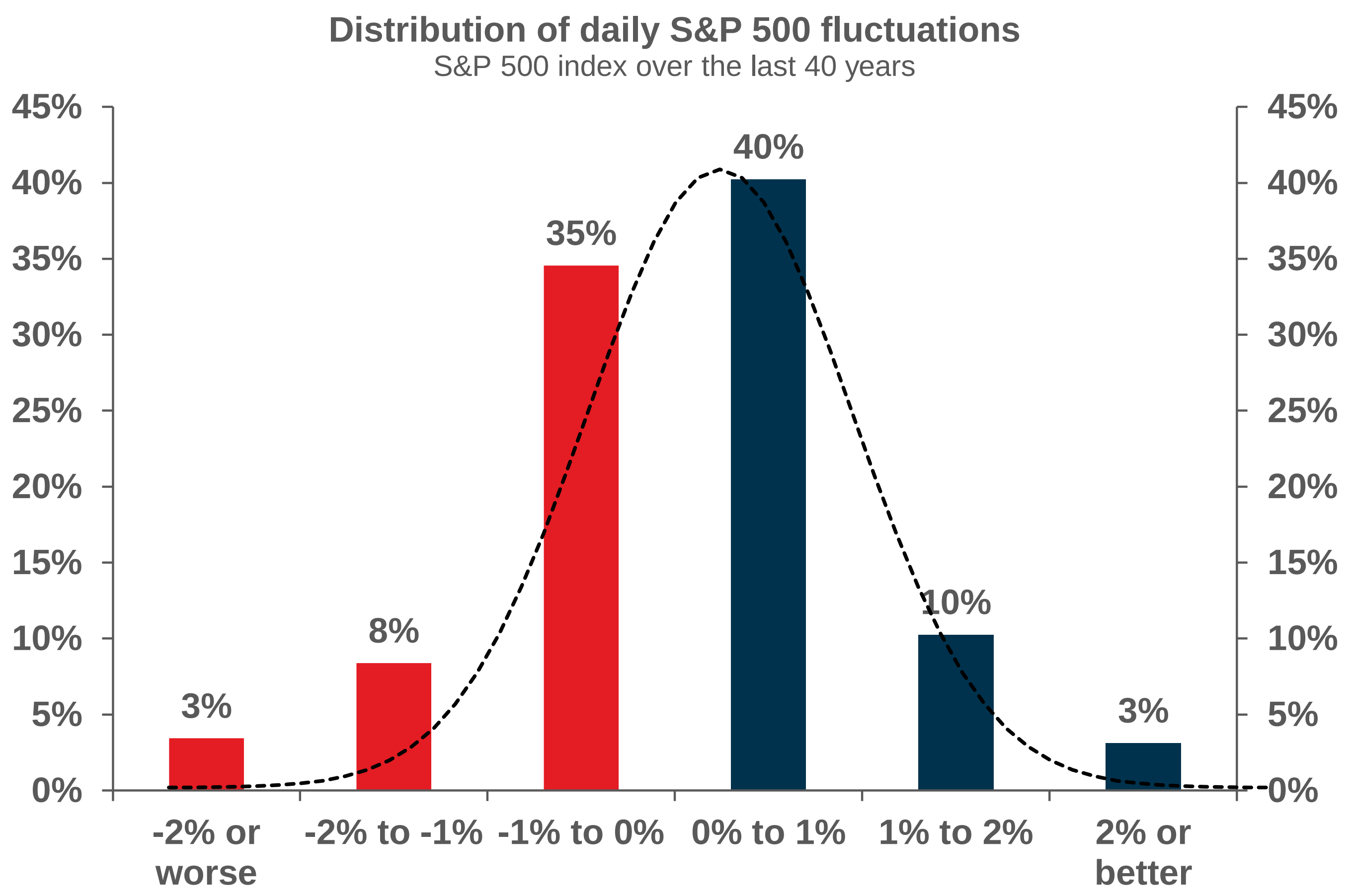
S&P 500 Bear Markets (1950-2022)

Peak	Trough	# days	Period Drawdown	# days to recover	Cumulative price return over the following: 6 months	12 months	24 months	36 months
1956-08-02	1957-10-22	446	-22%	337	8%	31%	47%	42%
1961-12-12	1962-06-26	196	-28%	434	20%	34%	53%	71%
1966-02-09	1966-10-07	240	-22%	209	22%	32%	37%	30%
1968-11-29	1970-05-26	543	-36%	650	19%	48%	54%	61%
1973-01-11	1974-10-03	630	-48%	2,114	35%	37%	68%	54%
1980-11-28	1982-08-12	622	-27%	83	43%	58%	48%	88%
1987-08-25	1987-12-04	101	-34%	600	13%	19%	50%	35%
2000-03-24	2002-10-09	929	-49%	1,694	13%	28%	45%	57%
2007-10-09	2009-03-09	517	-57%	1,480	48%	63%	96%	94%
2020-02-19	2020-03-23	33	-34%	148	52%	74%	99%	--
2022-01-03	2022-10-12	282	-25%	--	--	--	--	--
	Average:	**413**	**-35%**	**775**	**27%**	**43%**	**55%**	**59%**

Ibbotson. S&P 500 bear markets are defined as periods when the index fell at least 20% from its all time high.

CIO Office (data via Refinitiv)

Daily Stock Market Fluctuations



Market fluctuations are normal, both mathematically* and literally. While only the few "extremes" end up in the evening news and morning shows, the truth is they don't matter all that much.

What really matters is the accumulation of "0% to 1%" days that rarely make the headlines, but explain much of the 12.3% S&P 500 annualized total return over the last 40 years…

…despite the fact that the index closes in the red almost every other day.

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