2022 Year-End Commentary

"It is better to be roughly right than precisely wrong."

- John Maynard Keynes

What Happened in 2022?

In the automotive world, the term "lemon" refers to vehicles that experience multiple issues and flaws. Similarly, 2022 was a "lemon year" for investors that was fraught with potholes including:

- surging and persistent inflation,
- the Russian invasion of Ukraine,
- aggressive Central Bank interest rate policy,
- plummeting stock markets,
- the worst bond market returns in decades, and
- a meltdown in risk assets like cryptocurrencies.

Last year was also a lesson in portfolio construction. Investors have traditionally diversified risk by complementing stock exposure with high quality bonds; what is known as a "balanced portfolio". The thinking being, when one asset *zigs*, the other *zags,* resulting in portfolios with lower risk for a similar expected rate of return.

Unfortunately, last year everything *zagged* at the same time. Both stocks and bonds fell as we witnessed the fastest monetary policy tightening by central banks in decades in an attempt to dampen inflation. The result was that traditional portfolio diversification failed for most investors.

At Westmount Wealth, we think about portfolio construction differently. We work to diversify beyond investing in stocks and bonds by offering clients exposure to quality alternative* (private) investments to decrease volatility, improve diversification and increase potential returns. In other words, another asset class to *zig* while stocks and bonds both *zag*.

*Alternative investments are also generally less liquid than more traditional asset classes and are not appropriate for all investors.

What Happened in the Bond Markets?

2022 was not a year for faint-hearted bond investors. After 41 years of interest rates generally trending downwards, a long-awaited reversal occurred in dramatic fashion as North American central banks worked to calm inflation.

The Bank of Canada increased rates seven times in 2022 taking the overnight lending rate from 0.25% to 4.25%. In the US, the Federal Reserve also increased rates seven times, taking the federal fund rate range from 0.25%-0.5% to the 4.25-4.50%.

Rising rates put pressure on bond prices. This resulted in the US Aggregate Bond Index ending down -13.01% for 2022. This was the worst calendar year return for the index over the last 46 years, eclipsing the previous low of -2.92%[4] in 1994.

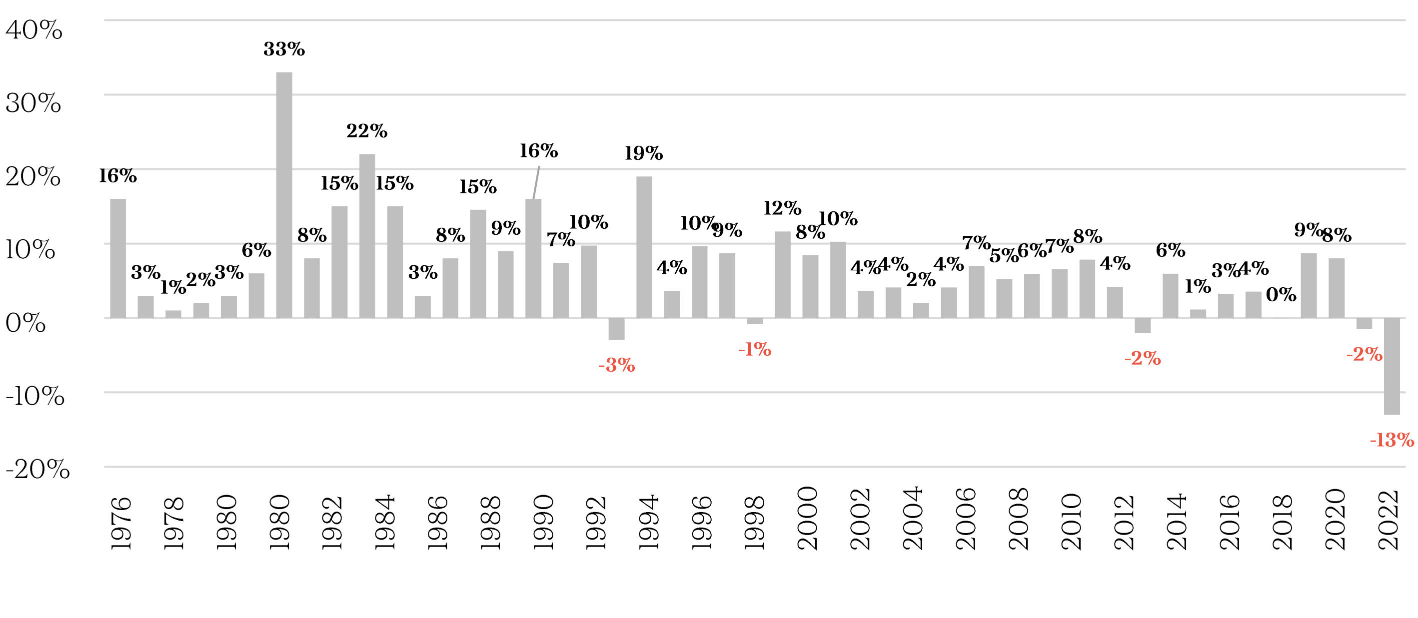
FTSE **Canada** Universe Bond Index — -11.69%[1] 2022

Bloomberg **US** Agg Bond Index (USD) — -13.01%[2] 2022

Bloomberg **Global** Agg Corp Bond Index (CAD) — -9.12%[3] 2022

Bloomberg US Aggregate Bond Index Calendar Year Returns

Only 4 years of negative returns in the last 46 years prior to 2022[5]



1, 2, 3. Source: Bloomberg L.P, Accessed 19 Jan. 2023., Total Returns for the period of Jan 1, 2022 to Dec 31, 2022

4. Source: "Aggregate Bond Index Vs. Stock Index 1980-2021." *The Balance*, 5 Mar. 2022, www.thebalancemoney.com/stocks-and-bonds-calendar-year-performance-417028. Accessed 3 Feb. 2023.

5. Source: Bloomberg. Factset, J.P. Morgan Asset Management. Returns are based on total returns. Intra-year drops refers to the largest drops from a peak to a trough during the year. For illustrative purposes only. Returns shown are calendar year returns from 1976 to 2022, over which time period the average annual return was 6.6%. Returns from 1976 to 1989 are calculated on a monthly basis; daily data used afterwards. Guides to the Markets – U.S. Data as of December 31, 2022.

What Happened in the Stock Markets?

To combat rising inflation, central banks around the world began aggressively raising interest rates. This caused stock markets to plunge, consumer confidence to drop, and fears of a North American recession.

Russia's invasion of Ukraine created further global supply chain disruptions and exacerbated the inflation problem, further increasing the probability of more rate hikes.

Stock market declines combined with once-in-a-generation losses in bonds left traditional balanced investors with one of the worst years since 1950.

An investor with 60% exposure to the S&P 500 and 40% to the US Aggregate Bond Index would have been down -16% in 2022. This was the third worst year for US Balanced investors in over 70 years!

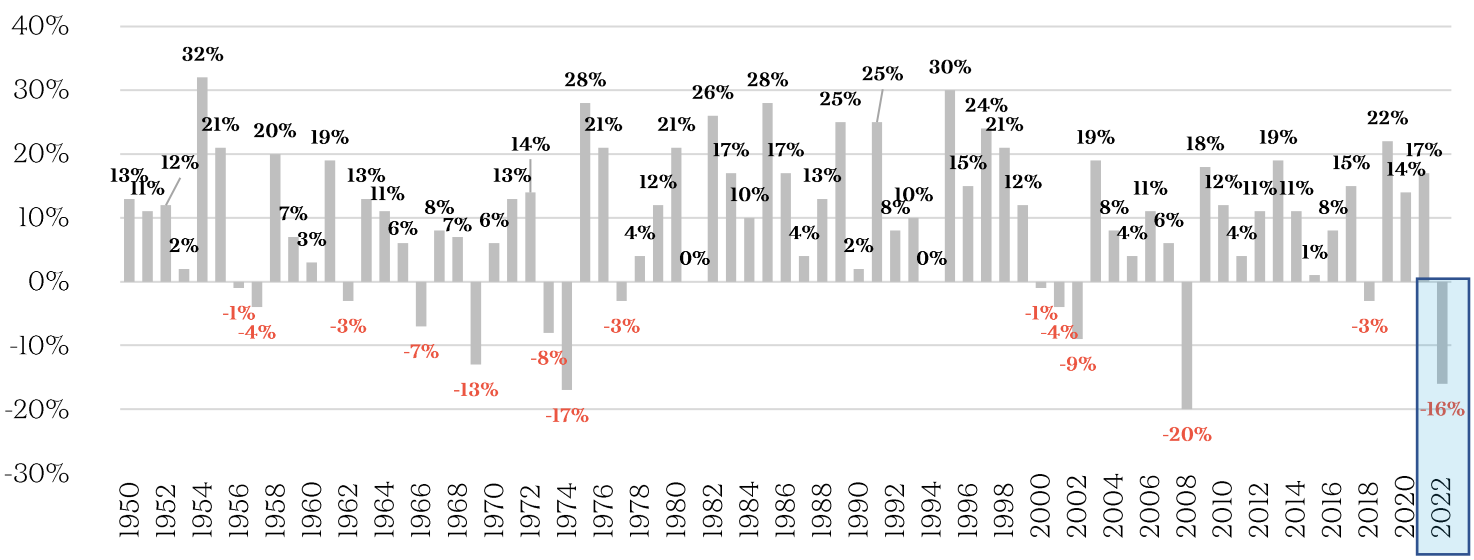
Canadian Stocks
S&P/TSX Comp. Index
-5.75%[1]
2022

US Stocks
S&P 500 (USD) Index
-18.13%[2]
2022

US Stocks
NASDAQ 100 (USD) Index
-32.51%[3]
2022

International Stocks
MSCI EAFE (CAD) Index
-7.92%[4]
2022

It Was a Tough Year for U.S. Balanced Investors[5]



1, 2, 3, 4. Source: Bloomberg L.P, Accessed 19 Jan. 2023., Total Returns for the period of Jan 1, 2022 to Dec 31, 2022

5. Source: Factset, Standard & Poor's, Robert Shiller, Yale University, Bloomberg, Ibbotson/Stategas, J.P. Morgan Asset Management. The 60/40 portfolio is 60% invested in S&P 500 Total Return Index and 40% invested in Bloomberg U.S. Aggregate Total Return Index S&P 500 returns from 1950 – 1970 are estimated using the Shiller S&P Composite. U.S. fixed income total returns from 1950-1975 are estimated using data from Strategas/Ibbotson. The portfolio is rebalanced annually. Guide to the Markets – U.S. Data as of December 31, 2022.

Why We Are Optimistic for 2023

1. Inflation is Coming Down

After seven consecutive interest rate hikes, U.S. inflation has been trending downwards for the last six months. This is a positive signal as it may mean central banks will hit pause on their interest rate policy.

2. China is Reopening

After three years, China recently abandoned it's strict zero-COVID policy. This will reinvigorate the world's second largest economy; an economy that suffered it's slowest growth last year in more than half a century[1]. This should ease global supply chains and reinvigorate manufacturing, commodities and travel.

3. Bonds Are Attractive Again

After a decade of low yields combined with the potential risk of rising interest rates devaluing bond prices (as we saw in 2022), bonds are finally attractive again. North American bonds are yielding 2-3 times what they were a year ago and now offer the possibility of capital gains should the US and Canadian central banks start cutting rates in late 2023/early 2024 (as is implied by the yield curve).

4. Stocks Tend to Rebound Following 12 Months of Negative Returns

Although recession fears persist, stock markets tend to be forward looking and we feel that the S&P 500 has already priced in a recession. Historically, the years following a large 12-month drop in the S&P 500 tend to offer favorable returns to investors as seen in the table below.

What Happens After Trailing 12 Month of Negative S&P 500 Returns of Greater than -20%[2]

Period End	Trailing 12 Month S&P 500 Returns	Compound Rate of Return Over Next 1 Year	3 Years	5 Years
9/30/1974	-42.56%	37.26%	18.27%	15.16%
3/31/2003	-30.64%	20.47%	8.56%	3.65%
12/31/1974	-30.04%	34.92%	15.27%	13.16%
3/31/2009	-23.93%	20.48%	14.14%	17.94%
9/28/2001	-23.03%	-20.21%	-3.50%	-0.20%
12/31/2002	-22.91%	5.85%	3.35%	2.84%
12/31/2008	22.62%	9.70%	7.45%	14.77%
9/30/2002	-20.21%	5.90%	5.21%	5.20%
	Average Returns	**14.30%**	**8.59%**	**9.07%**

1. Source: (2023, January 8). China reopens borders in final farewell to zero-COVID. www.Reuters.com/. Retrieved January 19, 2023, from https://www.reuters.com/world/china/china-reopens-borders-final-farewell-zero-covid-2023-01-08//
2. Source: Bloomberg. Index Used: SPX in CAD. Calculations created by The Vanguard Group analyst for Westmount Wealth on January 19th 2023. Data sourced from Bloomberg L.P. Accessed on January 19th 2023.

Why Hold Alternative Investments

To build a well-diversified portfolio and experience a smooth ride over time, it's important to invest in asset classes that perform differently under the same market conditions. At Westmount Wealth, we strive to help our clients improve their diversification into asset classes beyond traditional stocks, bonds and cash.

Appraisal-based investments in alternative asset classes like real estate, infrastructure, and private credit may help reduce swings in portfolio values as well as improve risk-adjusted returns. Please note, alternative investments are also generally less liquid than more traditional asset classes and are not appropriate for all investors.

We think of alternative investments as extra scaffolding for your portfolio.

Unfortunately, access to alternative investments can be challenging for a few reasons:

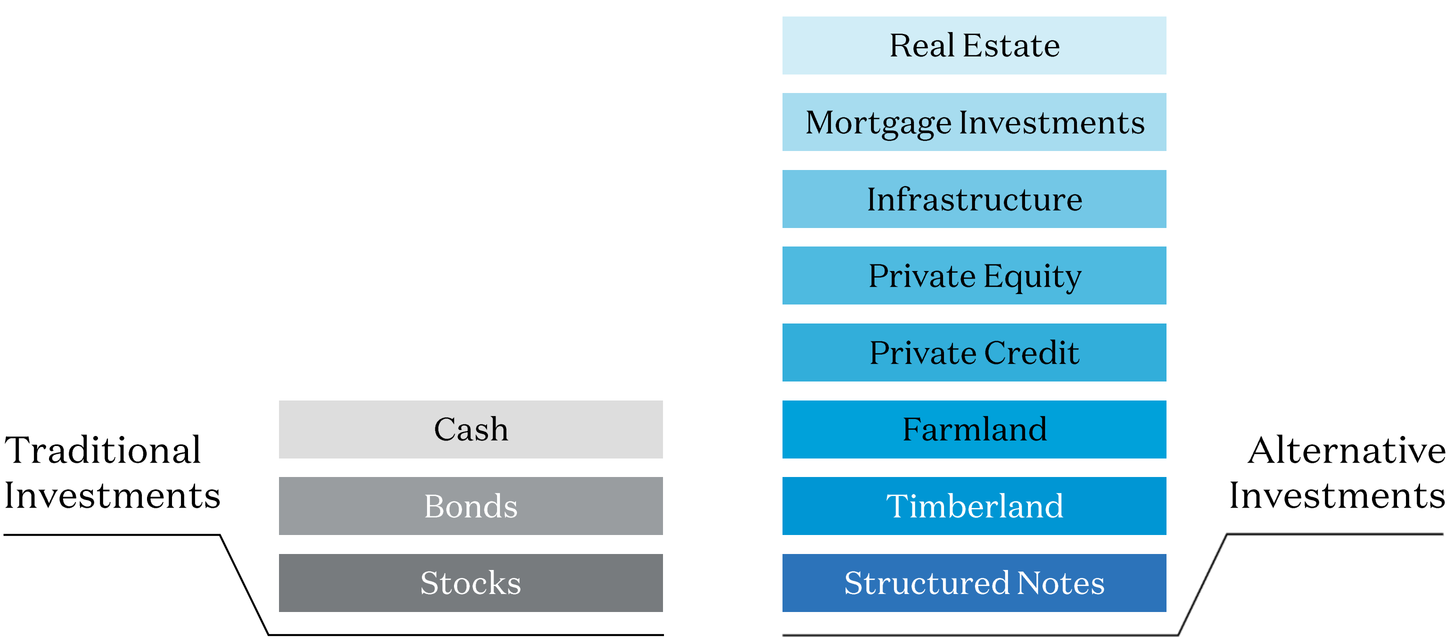
1. **Large Investments**
   Many alternative investments are designed for institutional investors and have high minimums.

2. **Illiquidity / Lock-ups**
   Alternative investments often require months or even years notice to be redeemed (sold).

3. **Redemptions Fees**
   It is common for private investments to have penalties if sold in the first few years.

4. **Harder to Properly Diversify with Limited Capital**
   Due to large investment minimums, individuals often hold only one or two private investments.

The **Westmount Alternative Income Fund** and the **Westmount Real Asset Fund** have been created exclusively for our Westmount Wealth clients to help overcome the challenges of access and liquidity often encountered when trying to invest in alternative assets.



Westmount Alternative Income Fund

The Westmount Alternative Income Fund provides diversified sources of income from various holdings including (but not limited to) structured notes, private credit and mortgage investments. Some of this debt is variable allowing income received from the investments to adjust in a rising rate environment.

These alternative income-producing investments should be viewed as a complement to your traditional bond exposure. In our model portfolios, we carved out a percentage that would normally have been allocated to bonds and diversified that portion into the Westmount Alternative Income Fund.

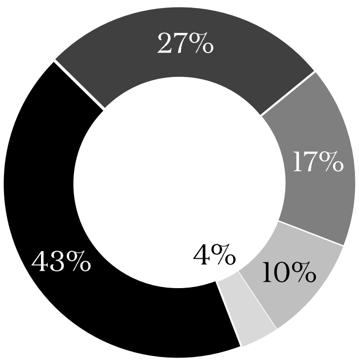
This decision had positive consequences for investors in our Westmount model portfolios as the **fund produced a positive calendar year return of +0.30%** during a year where the three previously mentioned traditional bond indexes lost -9.12% to -13.01% of their value.

Fund Total Return[1]

1 Year	0.30%
3 year	n/a
5 Year	n/a
10 Year	n/a
Since Inception	0.27%

Asset Class Breakdown[2]

- Mortgages (43%)
- Structured Notes (17%)
- Private Credit (27%)
- Long-Short Fixed Income (10%)
- Cash (4%)



1. Source: Returns on Westmount Alternative Income Fund provided by Investment Fund Manager, Majestic Asset Management as of 31 Dec 2022.
2. Breakdown of holdings by asset class in Westmount Alternative Income Fund as of 31 Dec 2022.

Westmount Real Asset Fund

The Westmount Real Asset Fund helps our clients diversify into private investments including (but not limited to) real estate (student housing, rental apartment buildings, industrial warehouses, etc.) and infrastructure assets (cell phone towers, fiber optic networks, solar farms, etc.).

Thanks to predictable cash flows, underlying tangible assets, and their critical role in our economy and society, private real estate and infrastructure tend to provide both stable returns as well as stable cash flows.

We have also committed to investing part of the fund in timberland and farmland and are waiting for our capital to be called by an institutional fund manager.

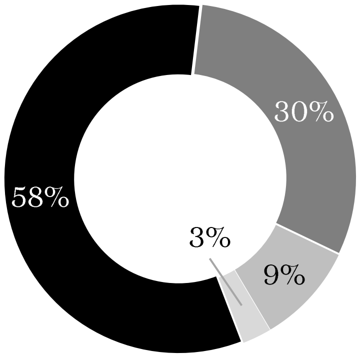
The **fund produced a positive calendar year return of +9.30%,** helping reduce portfolio volatility felt by falling stock and bond prices.

Fund Total Return[1]

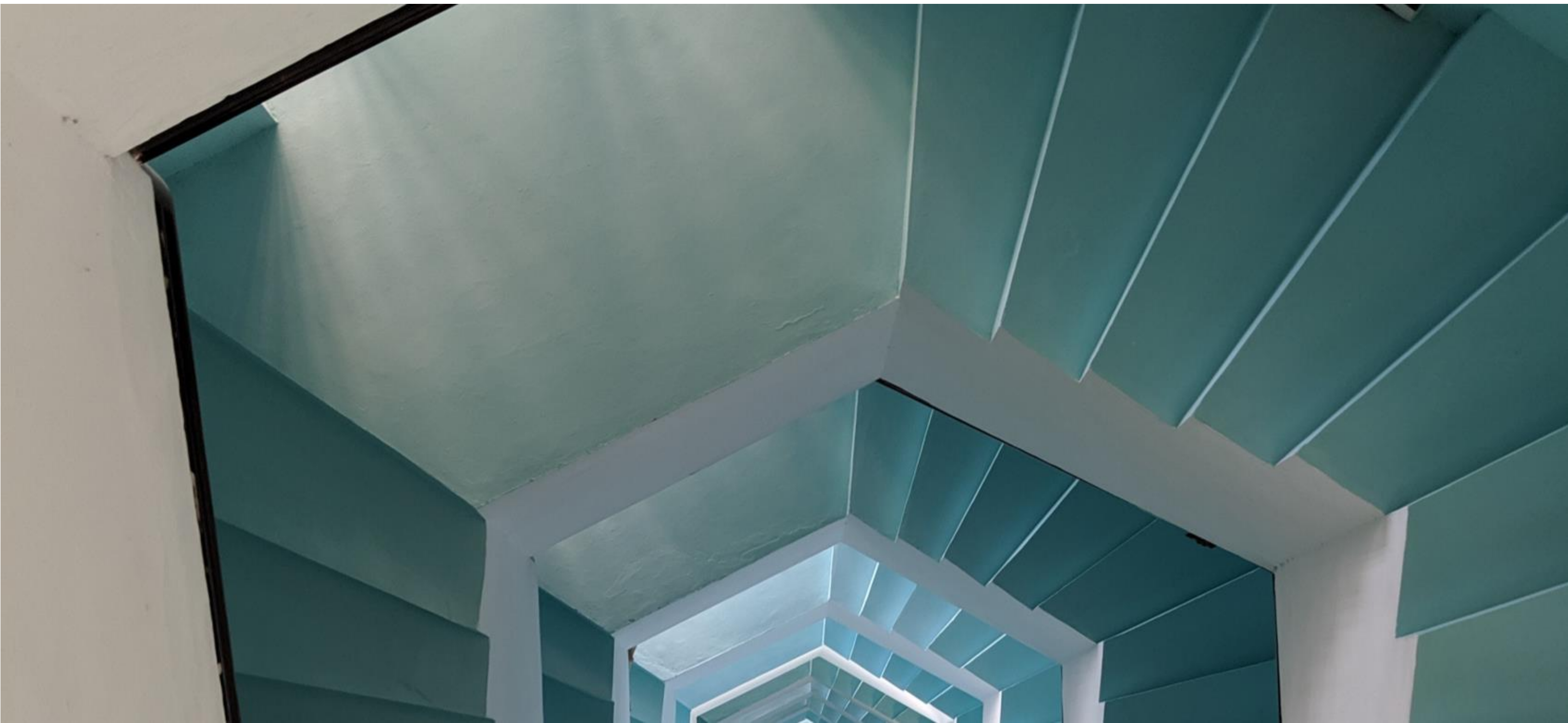
1 Year	9.30%
3 year	n/a
5 Year	n/a
10 Year	n/a
Since Inception	8.91%

Asset Class Breakdown[2]

- Real Estate (58%)
- Infrastructure (30%)
- Cash (9%)
- CAD-USD Currency Hedge (3%)



1. Source: Returns on Westmount Real Asset Fund provided by Investment Fund Manager, Majestic Asset Management as of 31 Dec 2022.
2. Breakdown of holdings by asset class in Westmount Real Asset Fund as of 31 Dec 2022.



The Bottom Line

2022 appears to have reset markets and we are optimistic about portfolio returns for 2023. Yes, a potential recession may add some short-term volatility, but we believe we are closer to the end (bottom) of this bear market than the start.

In this environment the best strategy is to remain highly diversified across asset classes (cash, bonds, stocks and alternatives) and to avoid large portfolio bets. As John Maynard Keynes said, *"It is better to be roughly right than precisely wrong."*

It is worth looking at portfolios and positioning: if your portfolio is still built for the last cycle (a steady decline in long term interest rates), there may be some preparation to consider. The inclusion of alternative investments helped mitigate some of the volatility in 2022 while further diversifying and we expect this approach to do the same moving forward.

If you, your friends, or family have assets elsewhere we welcome the opportunity to offer a second opinion on their portfolios.

Matthew Evans, CFP®, CIM®
Chief Investment Officer, Portfolio Manager
Westmount Wealth Management Inc.

Lorenzo Pederzani, CFA, CFP®, FCSI®
Chief Executive Officer, Portfolio Manager
Westmount Wealth Management Inc.