ODLUM BROWN
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THE
KWAMMENTARY
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Everything, Everywhere, All at Once (ish)

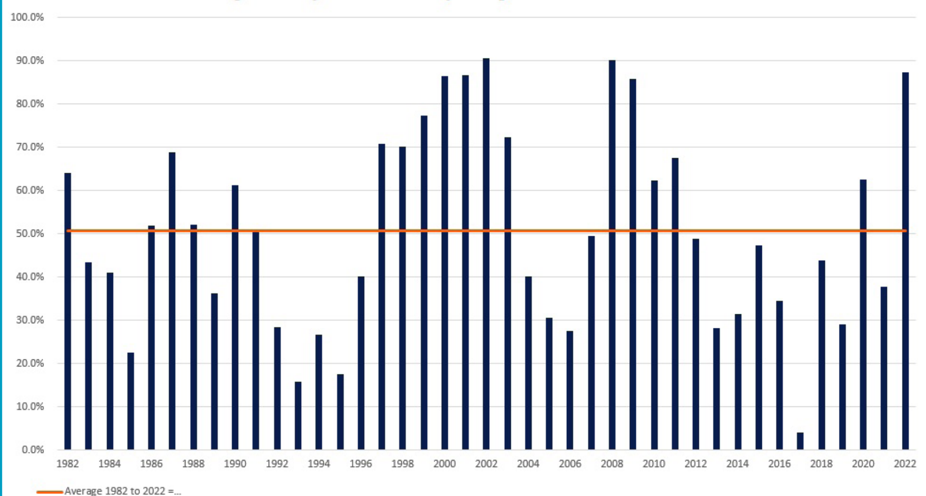
This past Oscars season saw the film *Everything Everywhere All at Once* take home multiple awards, including Best Picture, Best Actress and Best Supporting Actor/Actress, making it the most awarded film of all time. The story centres on an immigrant family and explores themes related to the immigrant experience, intergenerational familial relationships, and (surprisingly) multiverse theory. As I am both an immigrant and a self-professed nerd, this movie was right up my alley, and I thoroughly enjoyed it. With all that said, it was a lot to digest, and I distinctly remember being mentally exhausted when it was over (aptly named, in my opinion). Some of the plot points moved the story forward, while others seemed to have been added for the sake of extra minutes. In many ways, much of 2022 and the first quarter of 2023 have left many (myself included) feeling the exact same way.

Everything

Coming off a severe downturn in markets last year, sentiment at the beginning of the year seemed to be disconnected from the reality that most businesses had experienced. As of Q4 2022, the S&P 500 Index reported earnings decline of 4.9% (with over 69% of companies reporting by December 31). Contrast that to the approximate 20% decline for the S&P 500 for 2022, and we can arrive at a couple of conclusions:

1. Markets must have been elevated at the beginning of 2022, to the point of being disconnected from reality in certain sectors.
2. Geopolitical uncertainty (Russia/Ukraine, zero-COVID China) and economic uncertainty (inflation, interest rate hikes, zero-COVID China) shook investors enough to cause them to exit the market more than reality would dictate, given where earnings had ended up.

There was pronounced volatility in "long-duration" sectors like Information Technology, largely as a consequence of interest rates moving up as quickly as they did (↑ interest rates = ↓ long-duration assets). Fixed income was not spared either, however, which caught investors off guard. Using the iShares Core Canadian Corporate Bond Index ETF as a proxy for Canadian fixed income, the asset class registered a 10% decline in 2022. On the U.S. side, it was a similar story, with the iShares U.S. Investment Grade Corporate Bond Index recording a 12% decline in 2022 (in CAD). Not only did the directionality of markets seem out of character, but the path they took to get there seemed to defy reason. According to research from LPL Research, 2022 (to



Source: LPL Research, S&P Dow Jones Indices, Bloomberg, 08/30/22
All indexes are unmanaged and cannot be invested into directly.
Past performance is not guarantee of future results.
The modern design of the S&P 500 Index was first launched in 1957. Performance before then incorporates the performance of its predecessor index, the S&P 90.

September) recorded some of the most choppy intraday volatility since the Global Financial Crisis (GFC) of 2007-08, with almost 90% of trading days showing greater than 1% swings in a trading session. Anecdotally, I recall multiple instances last year where I would leave the office for a meeting or go for lunch with markets up half a percent only to come back an hour later to find them down half a percent or more. When these levels were seen last, it made more sense given their backdrop (GFC in 2007-08, dot-com bubble and burst from 1999/02). This theme has extended through 2023, as the market grapples with interpreting/reinterpreting/misinterpreting economic data and comments from central banks.

Everywhere

Although 2022 saw persistently strong economic data, rate hikes throughout the year affected certain sectors more quickly than others. If we look at layoffs, for example, we can observe that a healthy portion of those impacted were in the tech space. This makes sense given the preceding two years of rapid workforce expansion in the sector when rates were low and cash was plentiful. This year, these decisions are being made everywhere as businesses across sectors look for ways to reduce the impact of a slowing economy on their earnings. I expect to see this trend intensify as we begin to feel the full cumulative effect of rate hikes, pointing towards a lower demand/lower inflationary environment in the future. This is just one of many trends playing out across the spectrum of businesses and industries as the previous year's rate hikes start to take hold, but the direction of this trend cannot be mistaken. We're not in Kansas anymore.

The real test will be whether the effect of these deflationary decisions will warrant a change in monetary policy.

All at Once (ish)

The real crux of all the uncertainty, in my opinion, is threefold:

1. How pronounced will the impending slowdown be?
2. Will it be enough to allow for lower rates?
3. Will lower rates happen soon?

At the beginning of the year, the prevailing belief was that we could experience a moderate slowdown coupled with a significant reduction in inflation (allowing for lower rates). In order to have a moderate slowdown, however, inflation had to come down quickly ***and*** rates would have to follow suit. Everything had to happen all at once (ish), and as the year progressed it was becoming more apparent that these conditions may not be met. This highlights the most important dynamic of the immediate environment: a hyperfixation on the minutiae and the prevalence of short-term investment perspectives as a result. There is an almost infinite number of "plot" points to the story of how things will ultimately end up. Keeping up with them can be a massive task, and trying to draw long-term inferences from them compounds that difficulty – assuming you've picked the right points in the first place. Not only is this a tiring exercise (and less enjoyable than watching the aforementioned film), it is largely unnecessary given our views on how to grow your wealth consistently and responsibly.

Here's what we do know about the response to these questions, so far:

1. It is tough to see how much of a slowdown will materialize from this environment, but there will be bumps along the way (i.e., Silicon Valley Bank, crypto blow-ups, stress in lending markets)
2. Eventually there will be an economic environment that warrants lower rates, but it is anyone's guess as to when. The spectrum of opinions ranges from "rates have been too high since the end of last year" to "rates need to stay in this higher range for a while still," and this is coming from policymakers responsible for making these rate decisions. So, I can confidently say that I am just as unsure as they are.
3. Tough to say. "Soon" is relatively subjective in this environment, and due to that subjectivity, we will see volatility in response to those with closer timing expectations seeing the prerequisite conditions unmet.

In spite of all of this (and perhaps because of this), the opportunities for patient investors continue to grow. Sectors that were out of favour under the previous investment environment are now looking increasingly attractive (e.g., Energy, Materials and Infrastructure). Similarly, asset classes that were previously considered stale are now earning their keep in portfolios (e.g., fixed income). These developments allow for more dynamic portfolios, but more importantly they allow for a focus on a longer-term perspective. It is still important to be aware of some

of the shorter-term "plot" points as they provide some useful insights. However, if we imagine watching a movie the same way, *Everything Everywhere All at Once* turns into a film about filing taxes appropriately as opposed to a story about family. It is not a great way to enjoy a movie, and it is an even less enjoyable way to invest.

Don't Miss the Plot

As mentioned before, the investment environment has shifted quite dramatically. In the context of the story of "investing," this shift has all the elements of a comeback narrative built on resilience and dedication to the process (think 80s action movie). Our focus continues to be on the factors that matter to businesses: having a competitive edge and durable operations, an ability to generate cashflow in tough environments, and a responsible balance sheet and access to liquidity. Our focus is also on putting other asset classes to work. I believe positioning with the longer-term view in mind will set one up with the best seats in the house to watch this story unfold. All you need now is some popcorn.

I would welcome the opportunity to share more about how Odlum Brown can help you achieve your financial goals.

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