CANVAS®
An investment service of O'Shaughnessy Asset Management, LLC

Q3 2022 Commentary

Index	Q3 2022	YTD 2022
MSCI All Country World	-6.71%	-25.12%
Russell 1000	-4.61%	-24.58%
MSCI World Ex-US	-9.81%	-25.58%
MSCI Emerging Markets	-11.57%	-28.11%
Russell 2500	-2.85%	-24.03%
Barclays Aggregate	-4.70%	-14.83%

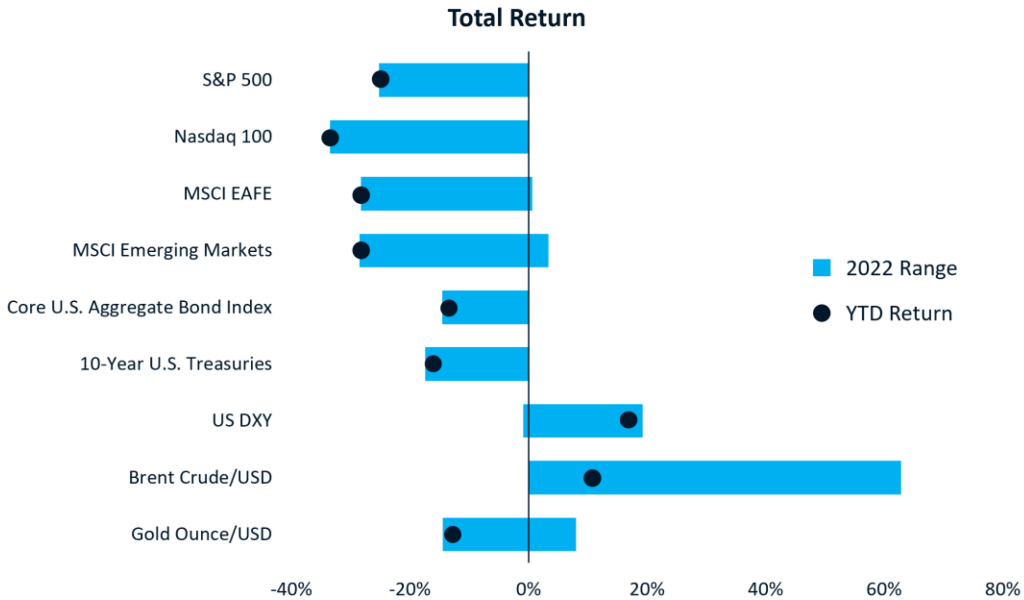
Key Points:

- Stocks and bonds retraced their full 2021 calendar year gains as the FOMC's continued hawkish stance, the Russia-Ukraine conflict, and global growth and inflation concerns all weighed on markets.
- Value and Shareholder Yield generally underperformed across universes while Momentum delivered outperformance. Low quality stocks notably outperformed.
- Stocks ranking highly on our Stability theme—stability in sales, earnings, share issuance, and price volatility—generally underperformed for the quarter but held on to relative outperformance year-to-date.
- In our Outlook section, we revisit the four themes that we believe will be prominent in coming quarters: inflation, fundamentals, shifts in stock-bond correlations, and international diversification. We expect monetary and macro developments will continue to generate higher than normal market volatility.

Q3 Developments

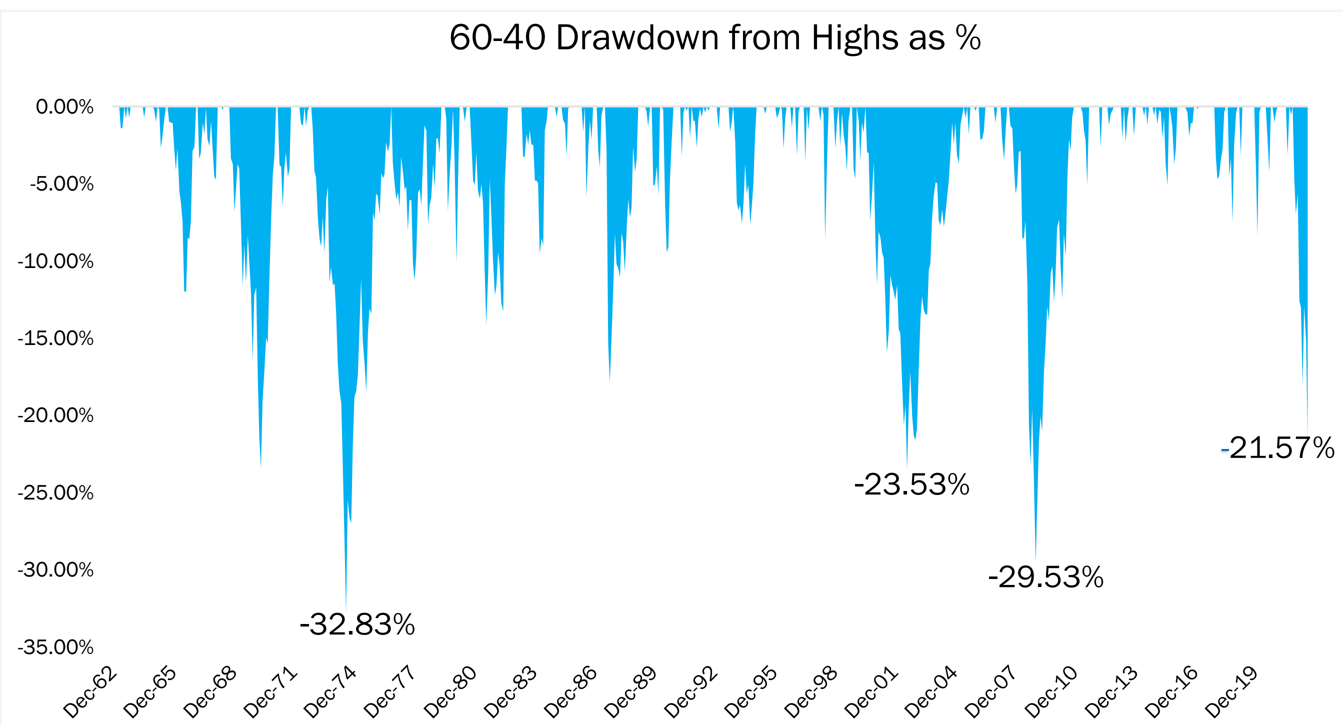
Global asset markets experienced another challenging quarter in Q3 as 2022 continues to be one of the worse on record for equity and bond markets. The U.S. Dollar provided a "safe-haven" for investors, even as inflation (trailing 12-month change in CPI) has been above 8% since March. The last time strong 5+% inflation persisted was the tail end of 1983, when it was retreating from the highs of the late 1970s.

The chart below highlights the performance of several important asset classes. Notably, the U.S. Dollar was the top performer, while commodities like oil and gold experienced weakness into the close of the quarter.



Source: OSAM Research, Koyfin

A good gauge for investor sentiment is the traditional 60-40 'balanced' portfolio (a 60% S&P 500 and 40% 10-Year U.S. Treasuries blend). Since 1963, the portfolio suffered its 6th and 4th worse months in April 2022 and September 2022. The -4.22% third quarter return brings the year-to-date decline to -21.57%. The portfolio has suffered this year as equities and bonds have exhibited strong positive correlation—something that has not been the case since the GFC.



Source: OSAM Research

Investors continue to wait with bated breath for each FOMC decision, and economic data release. The Bureau of Economic Analysis recently revised Q2 GDP to -0.6%, confirming the economy had contracted for the entire first half of 2022—a technical recession. The Atlanta Fed GDP Now estimate, which is a widely used estimate of annual real GDP growth, is forecasting annualized growth in the third quarter of 2.3%, or 0.57% for the quarter.

Factor Trends

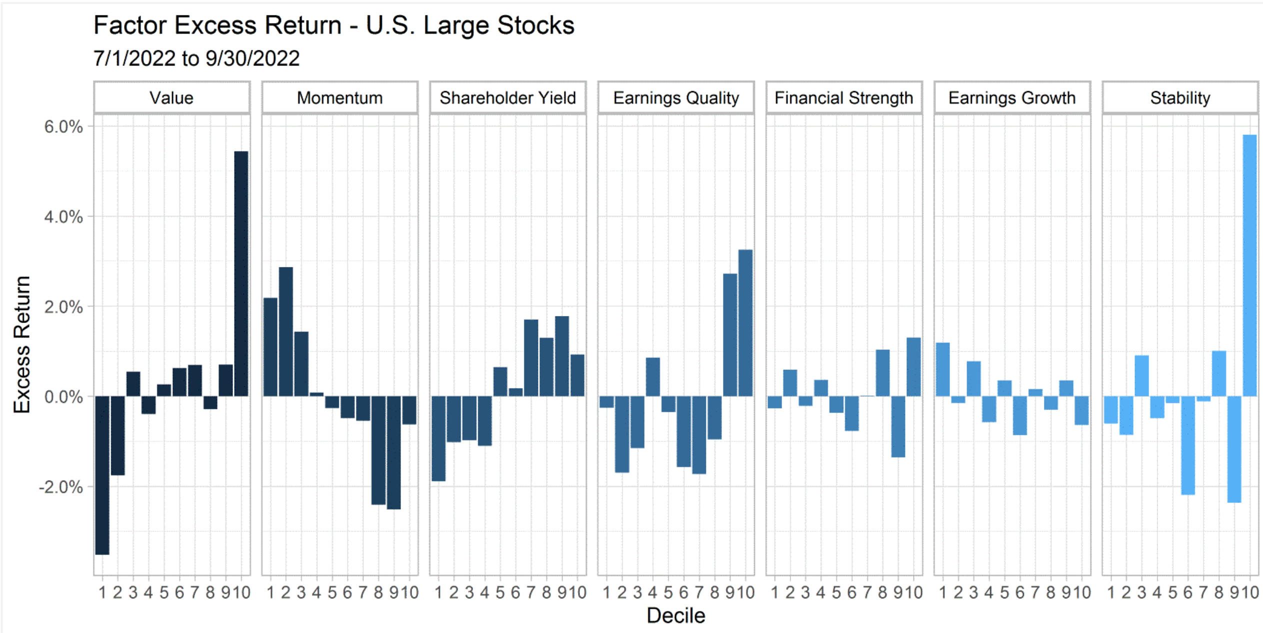
After an exceptionally challenging first half of the year, equity markets provided a brief respite from June 17th to August 17th, rallying nearly 20%, before reverting down -17% into the last day of the third quarter. The early summer move was a classic bear market rally, fueled by excessive bearishness at the lows and exhaustion (low volume) at the highs.

Source: OSAM Research

The history books are littered with these trend/counter-trend rallies in bear markets. One need only think to the half dozen such moves during the Tech Bubble bear market for a quick reference.

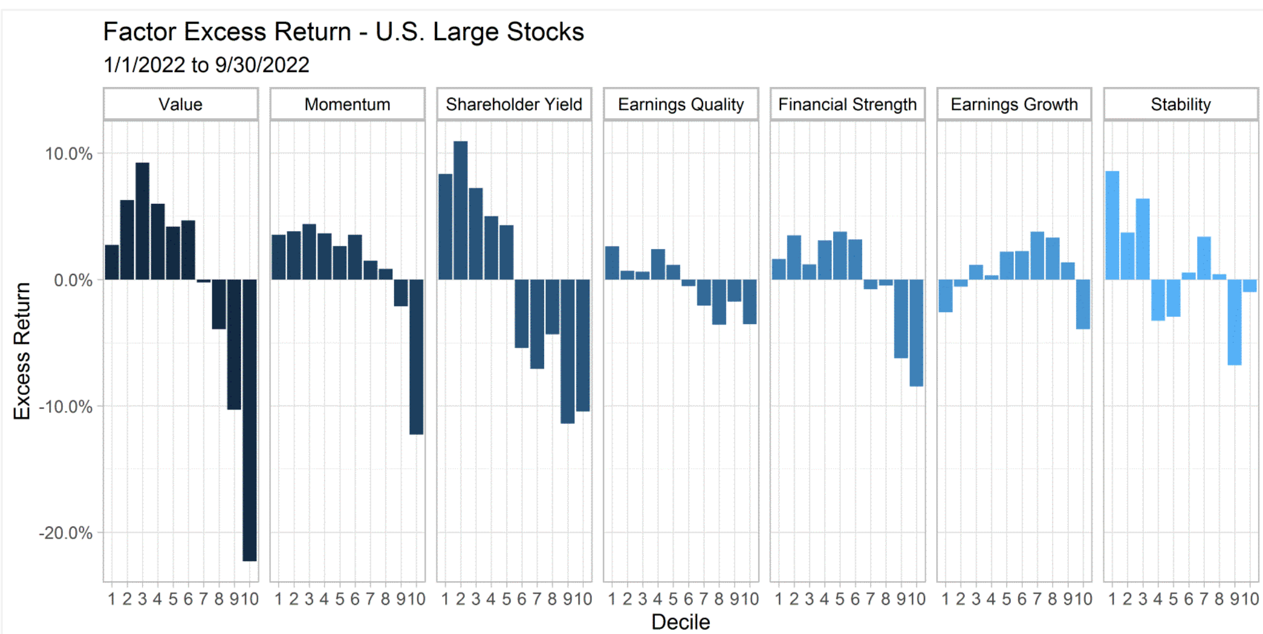
Aside from the volatility, what makes these moves so challenging is that the profile of outperforming stocks rotates swiftly. The stronger performers in the early summer bounce were expensive stocks with terrible momentum and quality—a junk rally. Smaller and unprofitable stocks disproportionately characterized the top performers. Conversely, outperformers in the late summer decline were mega caps with strong momentum, low volatility of underlying business fundamentals, and above-average shareholder yield and quality—a flight to safety.

For the quarter, the aggregate impact of the summer rally and decline resulted in value and shareholder yield underperforming across our investment universes and momentum generally outperforming. Low quality stocks outperformed early in the quarter and clung to those gains despite the market reverting down into the close of the quarter.



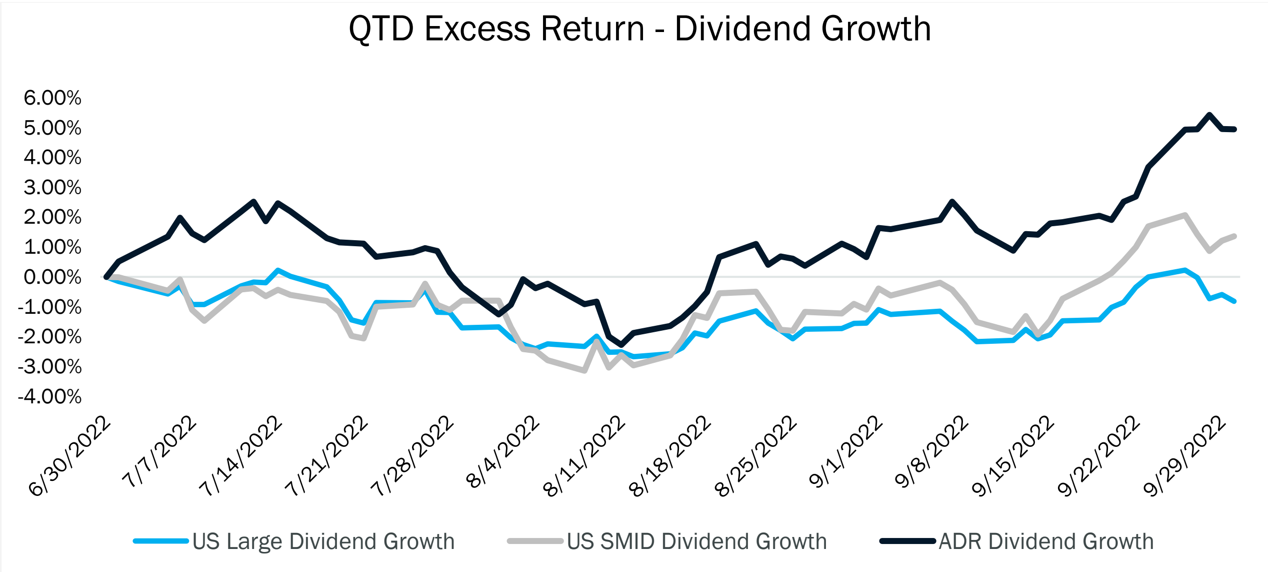
Source: Compustat, OSAM Research

Despite this flip-flopping, the longer-term factor profile of outperforming stocks during this bear market remained consistent with previous quarters.



Source: Compustat, OSAM Research

One theme that falls at the cross-section of current investor preferences for high quality, low volatility companies is Dividend Growth. Stable dividend growers historically offer downside protection in volatile and down markets given their more conservative posture, stable fundamentals, and income growth that generally exceeds the rate of inflation. That has certainly been the case on the full year, though the theme was roughly flat during the third quarter due to some headwinds from the early summer junk rally.



Source: Compustat, OSAM Research

Outlook

Our expectation the last few quarters was that equity market volatility would remain elevated. That has proven to be the case, with most markets down about 20% year-to-date and experiencing wide trading ranges. The summer range on the S&P 500 was a wide 18% from high to low! Elevated volatility can be particularly pernicious because it generates false positives in both directions. Bulls and Bears each get what they want, but both get trampled in the melee.

This volatility started in FX markets earlier in the year and has gradually spread to bonds, commodities, and equities. As that has occurred, equity investors have generally sought safety in high quality, low volatility stocks. This is all reflective of globally contracting liquidity, rising inflation, and pervasive central bank hawkishness.

Let alone the events of the first half of 2022, in the third quarter we experienced:

- European retail energy markets imploded, with the cost of electricity surging to multiples of the U.S. equivalent. Oil gave away all gains on the year in USD terms.
- Germany posted its first trade deficit in decades due to the high cost of electricity and the shutting down of production facilities, throwing Europe into a balance of payments crisis that is still unresolved.
- The Biden Administration released tens of millions of barrels of oil from the SPR and passed the Inflation Reduction Act of 2022.
- The Federal Open Market Committee (FOMC) raised the benchmark Fed Funds rate by 175 basis points, the largest increase in a three-month period since March 1982.
- The Bank of Japan unilaterally intervened in FX markets to defend the Yen for the first time since 1998. Though no announcement was made, it was rumored that the PBOC did as well.
- U.K. Gilt yields surged, and the Pound fell by near historic amounts at the announcement of Prime Minister Truss's aggressive fiscal plans, only to reverse the following day, followed by a reversal of said fiscal plans

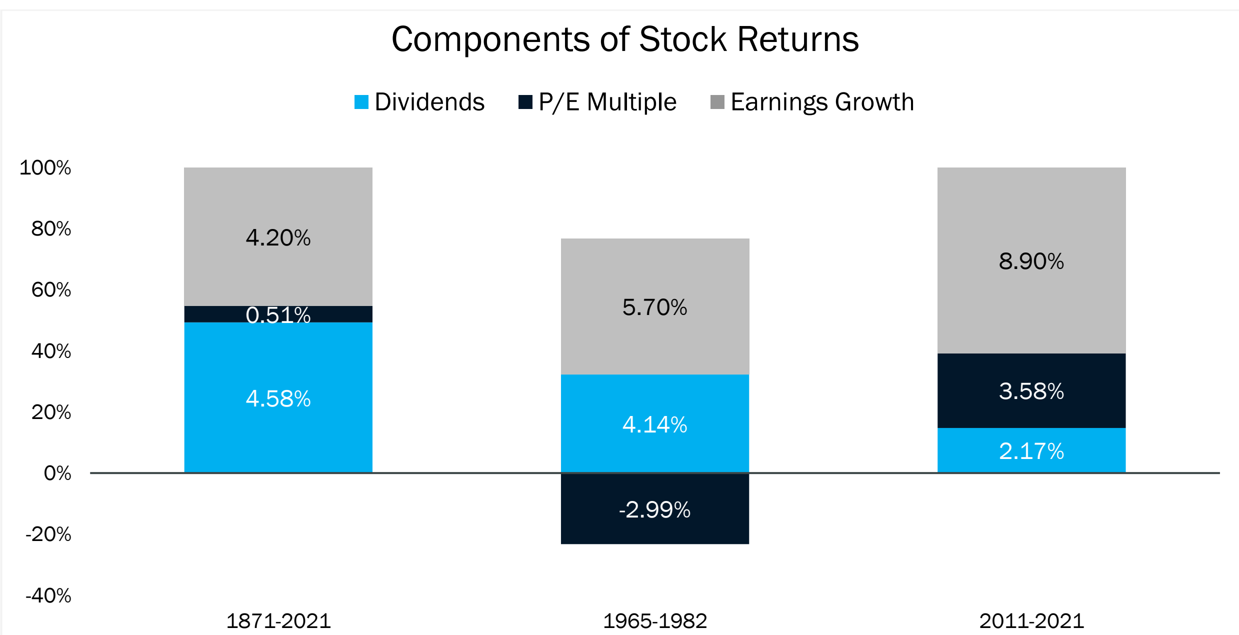
- U.S. CPI peaked at 9.0% for June versus the prior year. Not to be outdone, however, by the Producer Price Index which rose 22.4% year-over-year.
- U.S. real interest rates rose above the 1% level across the yield curve, the highest since November 2018.
- The trade weighted U.S. Dollar surged to the highest level since 2002.
- Quantitative Tightening went full throttle in September at $95 billion per month.

With this backdrop, it is no wonder volatility was a persistent theme as investors grappled with the new post-COVID elevated inflation regime. We expect volatility will most likely continue. In previous quarterly reviews, we have highlighted a few additional key themes that should be monitored going forward:

Inflation will likely run hot for a while. Unexpected inflationary pressures introduce tremendous uncertainty into corporate earnings and monetary and fiscal policy. With wholesale prices rising significantly higher than retail prices (PPI vs CPI), we suspect that the equity market may become bifurcated into those companies that can raise prices, and those that cannot. Those that can raise will help spur broad inflation across the economy, while those that cannot face compressed profit margins. In either case, there is a clear historical precedent for the market – valuation multiple compression that drags on total returns.

Fundamentals will matter again. Since the beginning of this bear market, low quality and negative earnings stocks have been substantially punished relative to inexpensive names with reliable earnings and dividend streams. With inflation running hot, liquidity contracting, and the cost of capital rising, a more conservative posture seems warranted. We have been waiting quite some time for fundamentals to matter again, so this is a source of excitement that we believe has legs.

The chart below breaks down the components of total return on the S&P 500 into its key drivers – earnings per share growth, return of capital, and multiple changes (the price-to-earnings ratio). Over long periods of time (left column), earnings growth and dividends (return of capital) are the key drivers. The right two columns zero in on two regimes, the Great Inflation from 1965-1982 and the post-Global Financial Crisis (GFC) recovery from 2011-2021.



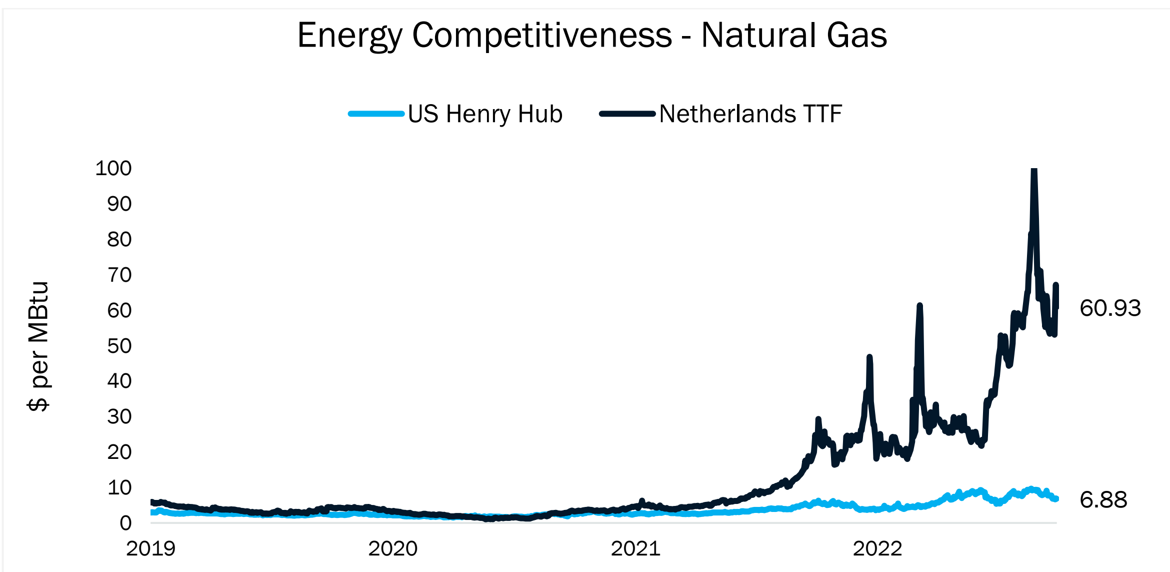
Source: Shiller, OSAM Research

During the Great Inflation, multiples contracted and were a significant drag of 2.99% annualized. Contrast that with the post-GFC regime where multiples contributed 3.58% to total returns. Given all the macro machinations previously mentioned, it seems unlikely that the next few years will resemble the post-GFC regime we just lived through.

With inflation likely running higher than we have been accustomed to and fundamentals mattering, it seems prudent for investors with factor allocations to lean into stocks with discounted valuation and higher quality characteristics; expensive stocks and those with poor quality seem poised to underperform.

International diversification may work again, but it's not clear when. Post-GFC policy interest rates converged at or below 0%. This was inherently unstable as it implies that growth and inflation are static across the global economy. Liftoff from the 0% bound provides flexibility for global policy rates to differ based on economic fundamentals. Rather than a one-way flow to safe-haven U.S. stocks, bonds, and currency, we might see investors evaluate non-U.S. equity opportunities on their merits, not just their sovereign's monetary policy in relation to FOMC actions.

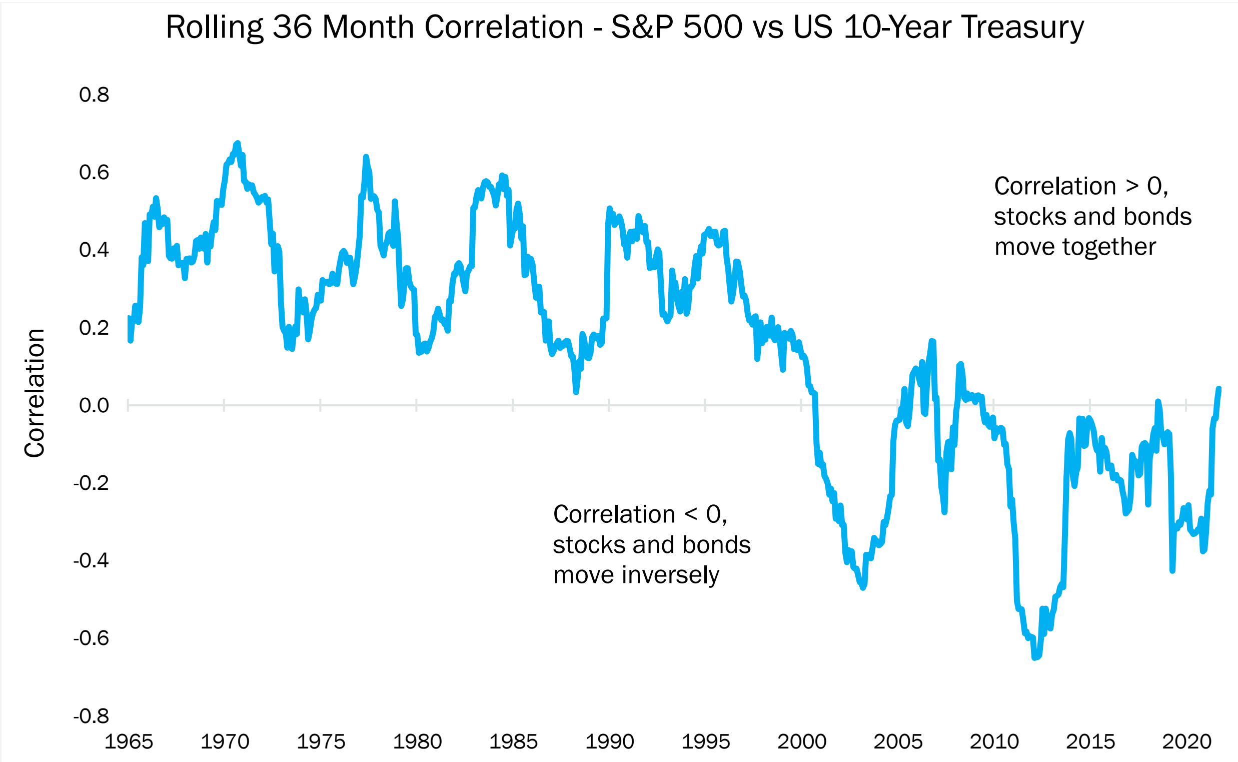
However, there are roadblocks for non-U.S. outperformance, notably Europe. Europe's energy infrastructure is not currently sound, due to the evolving Russia-Ukraine conflict and its associated sanctions. Europe's reliance on cheap Russian energy built over the last two decades will be an impediment to European competitiveness until an affordable workaround is devised. This was most evident in the price spikes for natural gas prices starting in late 2021, which went hyperbolic over the summer.



Source: Bloomberg, OSAM Research

Further, the continent is currently working through a balance of payments crisis that will require a coordinated solution among member states. Of course, European companies should not be evaluated solely on their sovereign's condition as European firms tend to source revenues from multiple geographies (including the U.S.) outside of their continental sphere. It will be interesting to see how European fundamentals evolve over the next few quarters.

Bonds will behave differently moving forward. As interest rates and inflation steadily declined over the last two decades, the risk premium for interest rate risk evaporated from normally safe U.S. Treasuries. The result was a beautiful diversification that resulted from an increasingly low correlation between stocks and bonds.



Source: FRED, Bloomberg, OSAM Research

Interest rates depend on expectations around inflation and real growth. With the path for both now uncertain, there has been a swift re-introduction of a risk premium for fixed income investments. This has implications for structuring portfolios that are drawdown sensitive (what portfolio isn't!?!). Allocators will need to be particularly attuned to return and volatility expectations for multi-asset portfolios.

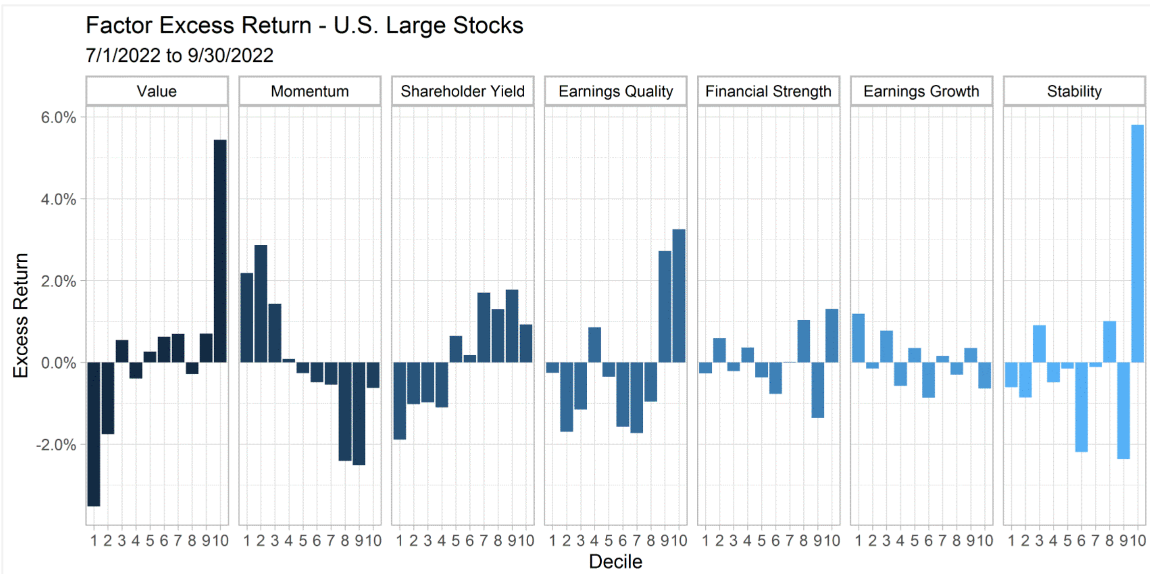
All told, it's as challenging an investment climate as ever. While we watch the large-scale macro machinations with keen interest, we take solace in the fact that all bear markets come to an end, even the long structural ones (Tech Bubble, GFC). It's only in retrospect that anyone can point to the true bottom. Until that point emerges, we will continue to focus on new research, disciplined execution of our strategies, managing for taxes, and reducing costs.

Factor Performance

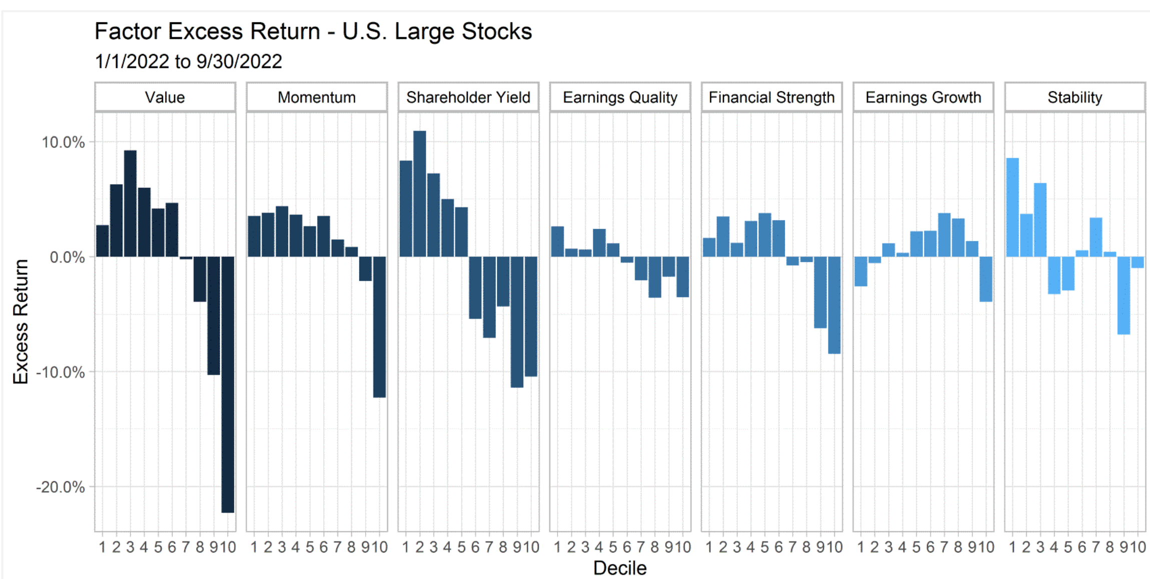
The charts below show the excess performance of the factor themes we monitor within each of our stock Universes. We think of Value, Momentum, and Shareholder Yield as selection factors—helping identify stocks we want to own and overweight for generating total return. Earnings Quality, Financial Strength, and Earnings Growth are quality factors that allow us to avoid stocks with non-cash driven earnings, weak balance sheets, and questionable underlying businesses. Stability is a selection factor for identifying stocks that tend to exhibit lower volatility and historically provide improved downside capture in drawdown. Column 1 for each of the panels represents the highest-ranking stocks on each factor while column 10 shows the lowest ranking. Historically, owning the highest ranked stocks and avoiding the lowest ranked stocks has resulted in successful investment outcomes.

We generally expect that factors will explain the majority of strategy performance and our quality exclusions and portfolio construction methodology will play supporting roles. Over certain, short, time periods, however, these aspects can have a greater influence on performance. So far this year, for example, our Large Cap active strategies did not outperform to the same extent as the factors would suggest, given headwinds from our portfolio construction process. This led us to overweight some poor performers (such as Ford, HP, and Dell in the U.S. and Volvo, Telenor, and Electrolux in international markets). As a result, large cap active allocations have generally outperformed, but to a lesser extent than the factors suggest.

U.S. Large Stocks

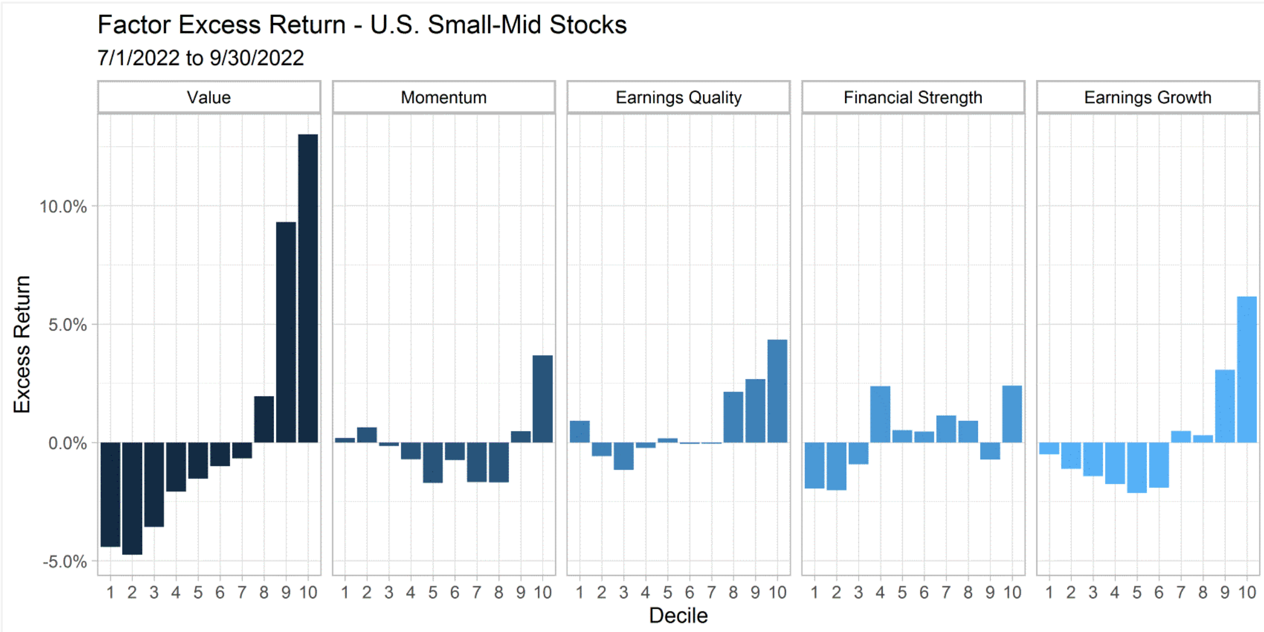


Source: Compustat, OSAM Research

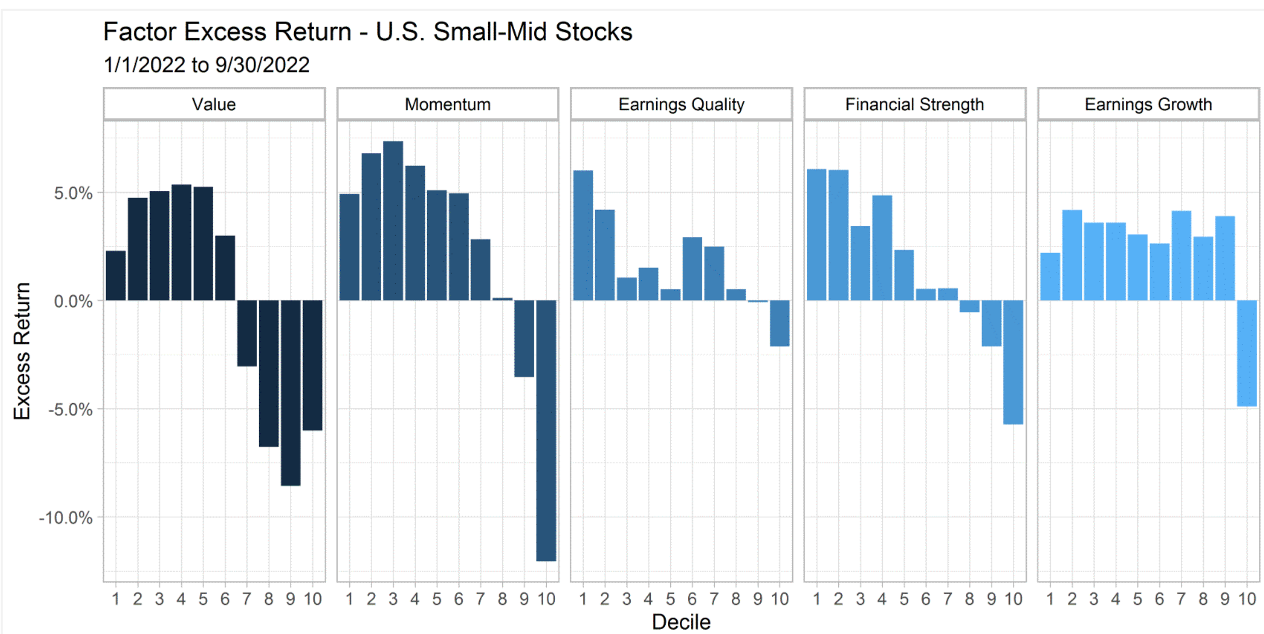


Source: Compustat, OSAM Research

U.S. Small-Mid Stocks

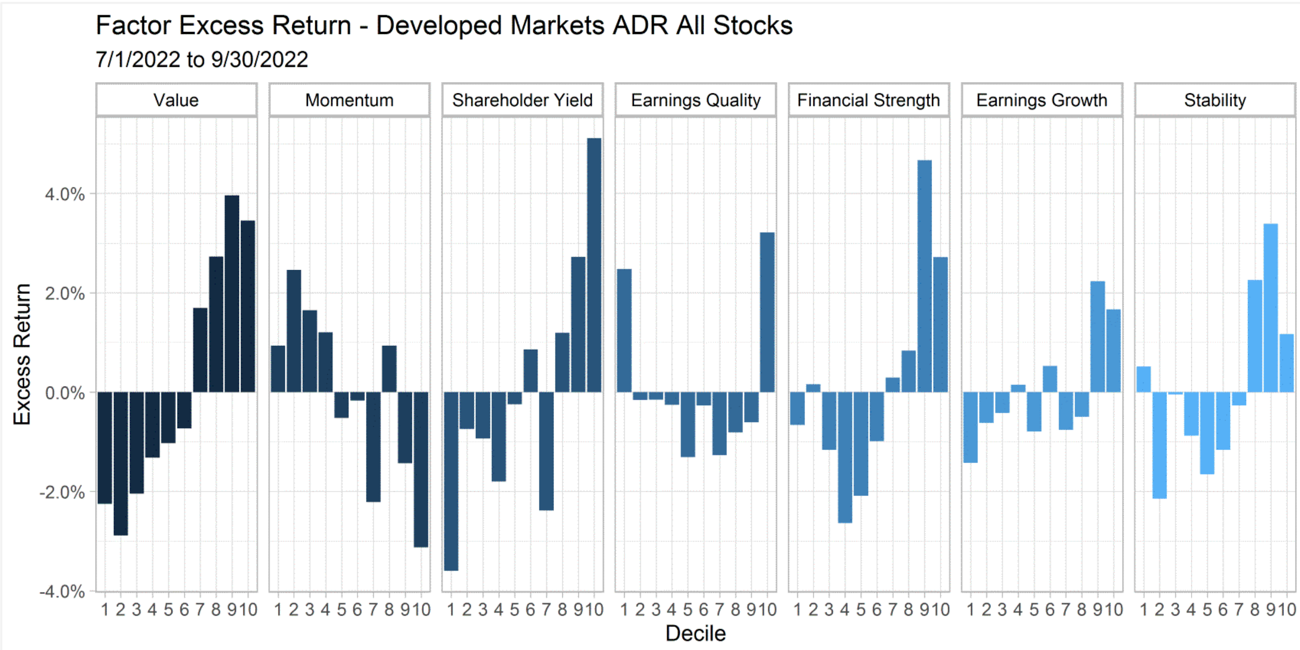


Source: Compustat, OSAM Research

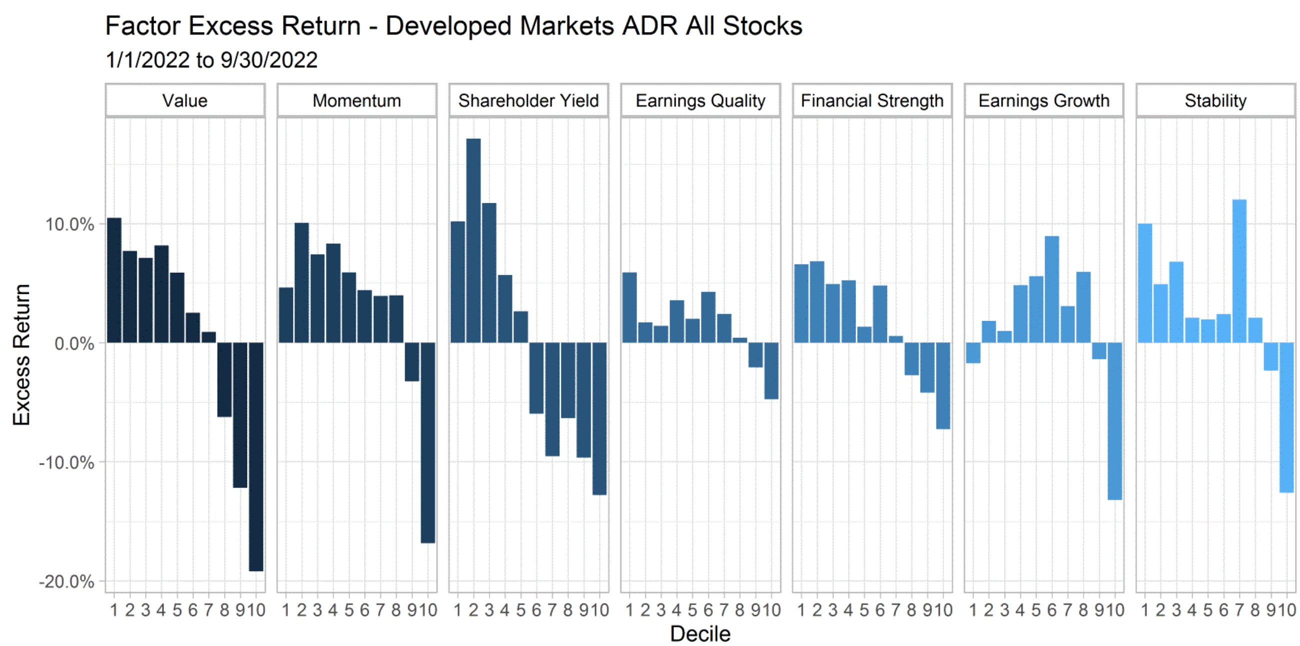


Source: Compustat, OSAM Research

Developed Markets ADR All Stocks

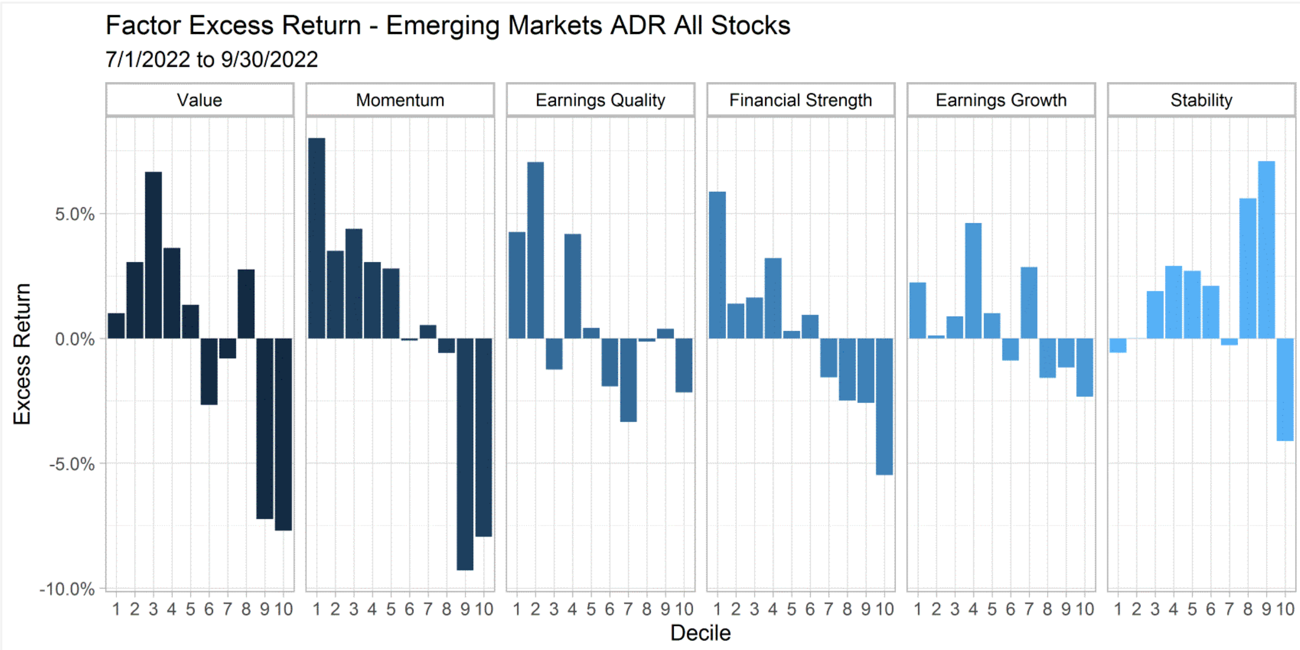


Source: Compustat, OSAM Research

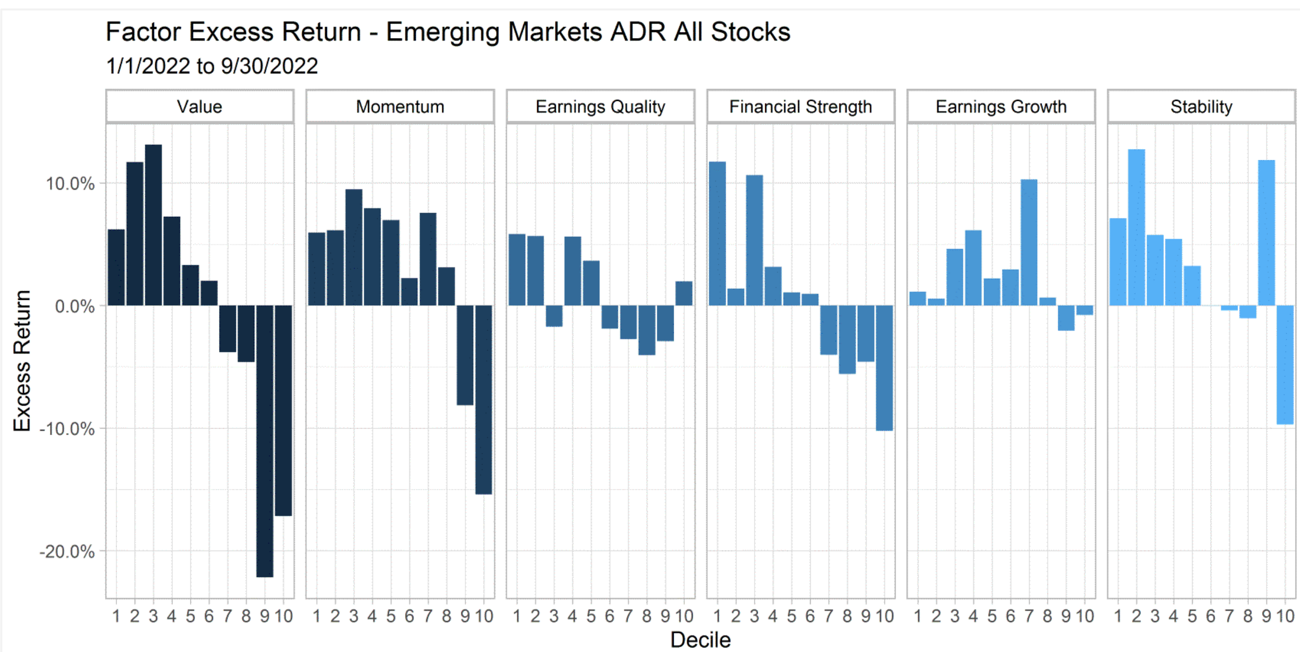


Source: Compustat, OSAM Research

Emerging Markets ADR All Stocks

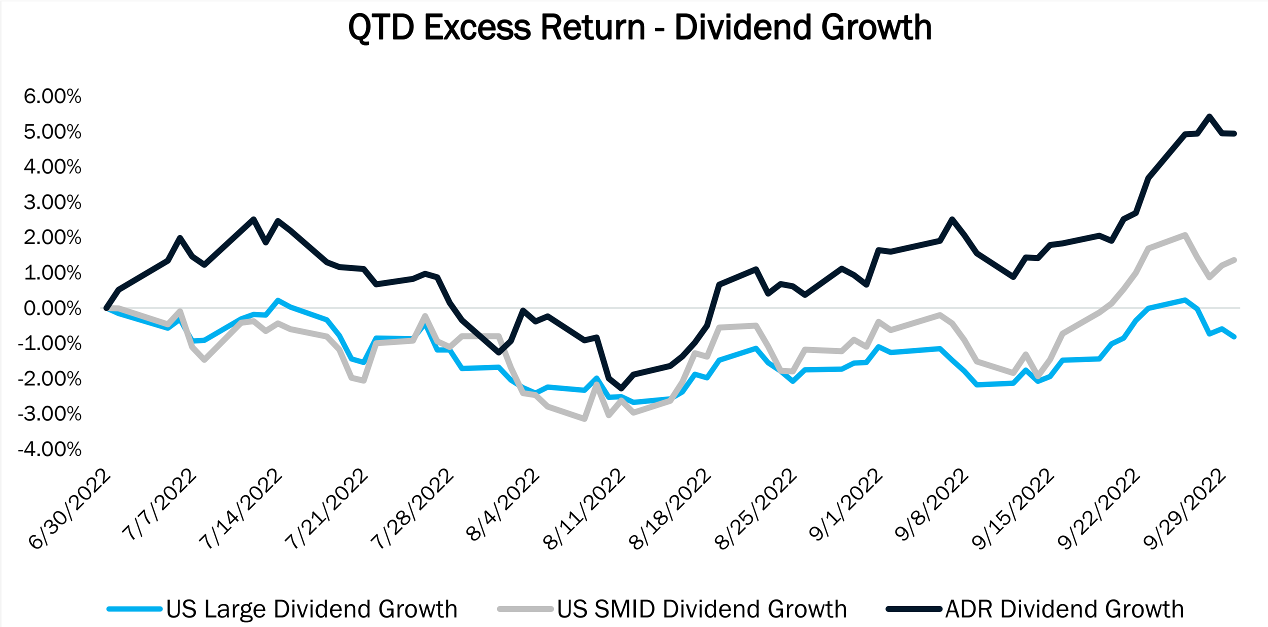


Source: Compustat, OSAM Research

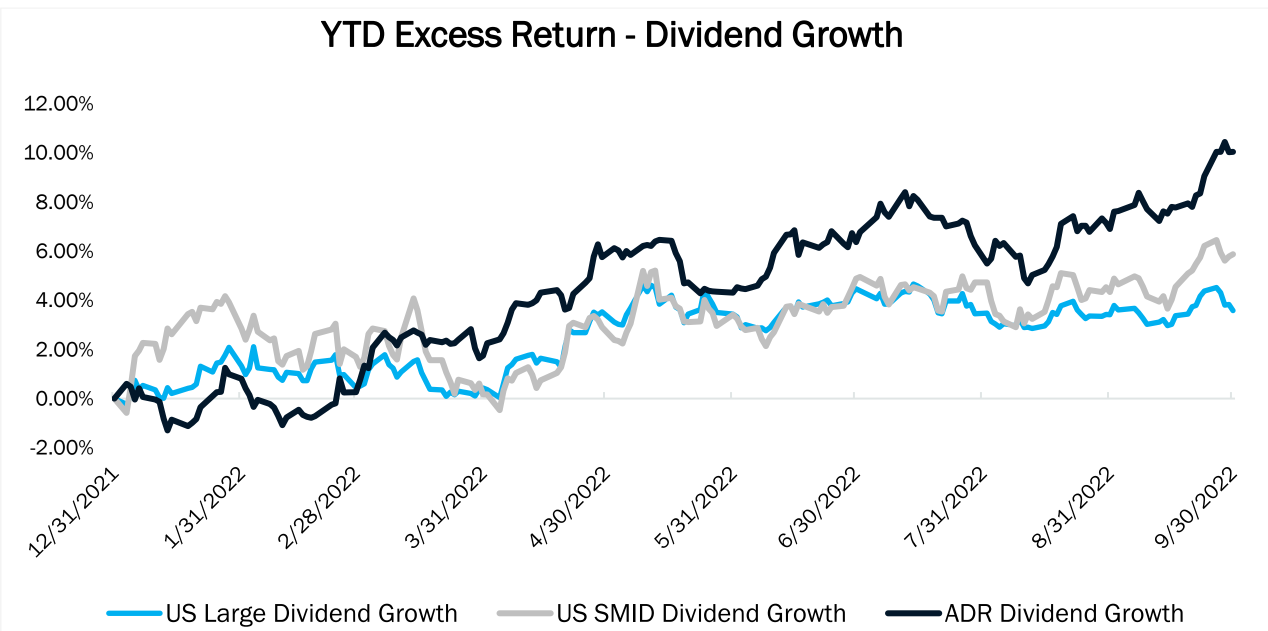


Source: Compustat, OSAM Research

Dividend Growth



Source: Compustat, OSAM Research



Source: Compustat, OSAM Research

CANVAS®
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Important Legal, Canvas®, Hypothetical and/or Back-tested Disclosure Information

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Reliance on Investment Professional: OSAM has relied, and shall continue to rely, on the investment professional's knowledge and experience to understand the inherent limitations of the performance presentation, including those pertaining to back-tested hypothetical performance. All performance presentations, including hypothetical performance, are the direct result of the investment professional's request, independent of OSAM. Depending upon the investment professional's direction and selection, hypothetical presentations can include both OSAM and non-OSAM Models and/or strategies. The below discussion as to the material limitations of back-tested hypotheticals apply to both OSAM and non-OSAM Models and/or strategies**.**

Intended Recipient: CANVAS content is intended for the investment professional only not to be shared with an underlying client unless in conjunction with a meeting between the investment professional and its client in a one-on-one setting. OSAM assumes that no hypothetical performance-related content will be provided directly to the professional's client without the accompanying consultation and explanation of the professional. The content is intended to assist the professional in evaluating the appropriate investment strategy for the professional's client.

OSAM Models. OSAM has devised various investment models (the "Models") for CANVAS, the objectives of each are described herein. The investment professional is not obligated to consider or utilize any of the Models. As indicated above, at all times, the investment professional, and not OSAM, is responsible for determining the initial and ongoing suitability of any Model for the investment professional's underlying client. Model performance reflects the reinvestment of dividends and other account earnings and are presented both net of the maximum OSAM's investment management fee for the selected strategy and gross of an OSAM investment management fee. **Please Note**: As indicated at Item 5 of its written disclosure Brochure, OSAM's CANVAS management fee ranges from 0.20% to 1.15%. The average percentage management fee for all CANVAS strategies is 0.36%. The percentage OSAM management fee shall depend upon the type of strategy and the corresponding amount of assets invested in the strategy; generally, the greater the amount of assets, the lower the percentage management fee**. Please Also Note:** The performance also do not reflect deduction of transaction and/or custodial fees (to the extent applicable), the incurrence of which would further decrease the performance. For example, if reviewing a strategy with a ten-year return of 10.0% each year, the effect of a 0.10% transaction/custodial fee would reduce the reflected cumulative returns from 10.0% to 9.9% on a 1-year basis, 33.1% to 32.7% on a 3-year basis, 61.1% to 60.3% on a 5-year basis and 159.4% to 156.8% on a 10-year basis respectively. **Please Further Note:** Transaction/custodial fees will differ depending upon the account broker-dealer/custodian utilized. While some broker-dealers/custodians do not charge transaction fees for individual equity (including ETF) transactions, others do. Some custodians charge fixed fees for custody and execution services. Choice of custodian is determined by the investment professional and his/her/its client. Higher fees will adversely impact account performance.

OSAM does not maintain actual historical performance results for the Models. In order to help assist the investment professional in determining whether a Model is appropriate for the professional's client, OSAM has provided **back-tested hypothetical (i.e., not actual)** performance for the Model. OSAM, with minor deviations that it does not consider to be material*, currently uses the Models **(i.e., live models vs. the reflected back-tested versions thereof)** to manage actual client portfolios (**see Model Deviations below**). The performance reflects the current Model holdings, which are subject to ongoing change.

Material Limitations: The Performance is subject to material limitations. **Please see Hypothetical/Material Limitations below.** During any specific point in time or time-period, the Models, as currently comprised, performed better or worse, with more or less volatility, than corresponding recognized comparative indices, benchmarks or blends thereof.

Past performance may not be indicative of future results. Therefore, it should not be assumed that future performance of any specific investment or investment strategy (including the Models), will be profitable, equal any historical index or blended index performance level(s), or prove successful. Historical index results do not reflect the deduction of transaction and custodial charges, or the deduction of an investment management fee, the incurrence of which would have the effect of decreasing indicated historical performance results. The Russell 3000 is a market capitalization-weighted index of 3000 widely held large, mid, and small cap stocks. Russell chooses the member companies for the Russell 3000 based on market size and liquidity. The MSCI All Country World Index is a market capitalization weighted index designed to provide a broad measure of equity-market performance throughout the world. The MSCI is maintained by Morgan Stanley Capital International and is comprised of stocks from 23 developed countries and 24 emerging markets. The Barclays Capital Aggregate Bond Index is a market capitalization-weighted index, meaning the securities in the index are weighted according to the market size of each bond type. Most U.S. traded investment grade bonds are represented. Municipal bonds and Treasury Inflation-Protected Securities are excluded, due to tax treatment issues. The index includes Treasury securities, Government agency bonds, Mortgage-backed bonds, corporate bonds, and a small amount of foreign bonds traded in U.S. The historical performance results for the Russell 3000, MSCI and Barclays are provided exclusively for comparison purposes only, to provide general comparative information to help assist in determining whether a Model or other type strategy (relative to the reflected indices) is appropriate for his/her investment objective and risk tolerance. **Please Also Note**: (1) Performance does not reflect the impact of client-incurred taxes; (2) Neither Model or the selected strategy holdings correspond directly to any such comparative index; and (3) comparative indices may be more or less volatile than the Model or selected strategy.

Hypothetical/Material Limitations-performance reflects hypothetical back-tested results that were achieved by means of the retroactive application of a back-tested portfolio and, as such, the corresponding results have inherent limitations, including: (a) the performance results do not reflect the results of actual trading using investor assets, but were achieved by means of the retroactive application of the Model or strategy (as currently comprised), aspects of which may have been designed with the benefit of hindsight; (b) back tested performance may not reflect the impact that any material market or economic factors might have had on OSAM's (or the investment professional's) investment decisions for the Model or the strategy; and, correspondingly; (c) had OSAM used the Model to manage actual client assets (or had the investment professional used the selected strategy to manage actual client assets) during the corresponding time periods, actual performance results could have been materially different for various reasons including variances in the investment management fee incurred, transaction dates, rebalancing dates (increases account turnover), market fluctuation, tax considerations (including tax-loss harvesting-increases account turnover), and the date on which a client engaged OSAM's investment management services.

MORE ABOUT CANVAS®

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- determining the initial and ongoing suitability of the Strategy for the client;
- devising or determining the specific initial and ongoing desired Strategy;
- monitoring performance of the Strategy; and,
- modifying and/or terminating the management of the client's account using the Strategy.

Hypothetical Limitations: To the extent that the investment professional seeks for CANVAS to provide hypothetical back-tested performance, material limitations apply-***See above***.

Model Deviations: As indicated above, OSAM, with minor deviations that it does not consider to be material*, currently use the Models to manage actual client portfolios (i.e., the live Models). The deviations include:

- the use of proxies if and when an ETF used in the back-test was not available*. While the back-tested and live strategies both utilize the same investment themes, back-tested proxies can deviate from live models based on limitations of historical information;
- back-tested data presented utilizes a month-end rebalance while actual live model performance reflects intra-month rebalances;
- OSAM, as a discretionary manager, can update its live models as determined necessary. These changes will then be applied retroactively to back-tested models, the resulting performance of which would be different than that of the actual historical models-***see*** **Hypothetical/Material Limitations** above; and,
- Financial statement information may be restated over time, which information was not reflected in the historical back-tested models. Companies will also have mergers and acquisitions or other corporate events that can retrospectively affect the names and corporate identities of organizations in the historical back-tests. Data providers providing pricing and return information may update historical data upon discovering deficiencies or omissions.

Strategy Sampling Impact: The implementation of OSAM strategies utilize a sampling of the underlying individual Strategy positions, and, as the result thereof, the underlying securities' weighting could unintentionally deviate +/- the Strategy allocation target OSAM calculates the CANVAS fees based on the mix of strategies that are utilized at the establishment of the account. Therefore, the sampling approach can cause deviations between the Canvas strategy allocation establishment (and its corresponding fee) and the implementation of that CANVAS strategy.

ESG Portfolios/Socially Responsible Investing Limitations. To the extent applicable to the strategy chosen by the investment professional, Socially Responsible Investing involves the incorporation of Environmental, Social and Governance considerations into the investment due diligence process ("ESG). There are potential limitations associated with allocating a portion of an investment portfolio in ESG securities (i.e., securities that have a mandate to avoid, when possible, investments in such products as alcohol, tobacco, firearms, oil drilling, gambling, etc.). The number of these securities may be limited when compared to those that do not maintain such a mandate. ESG securities could underperform broad market indices. Investors must accept these limitations, including potential for underperformance. Correspondingly, the number of ESG mutual funds and exchange-traded funds are few when compared to those that do not maintain such a mandate. As with any type of investment (including any investment and/or investment strategies recommended and/or undertaken by OSAM), there can be no assurance that investment in ESG securities or funds will be profitable or prove successful.

Tax Management Function: When requested by the investment professional, OSAM will use best efforts to work within Onboarding Budgets, Annual Tax Budgets, and Tracking Error Budgets. However, market and/or specific stock price fluctuations can occur quickly and can correspondingly adversely affect our ability to manage to specified budgets. Additionally, changes to tax budgets, cash flows in and out of an account, mandatory corporate actions, and funding with securities can also impact preciseness. The investment professional must accept this risk. In addition:

- OSAM has not, and will not, verify the accuracy of any tax-related information provided;
- In the event that any such information provided is inaccurate or incomplete, the corresponding results will be inaccurate or incomplete;
- Tracking Error Budgets are relative to the Model, not the benchmark;
- OSAM is not a CPA and this is not tax advice;
- Tax laws and rates change;
- While we seek to follow the investment professional prescribed target models, ranges, timeframes, tax budgets, and seek not to create wash sales or exceed expected tax budgets, there can be no assurance that the CANVAS tool will be able to accurately do so;; and,
- For specific personalized tax-related advice, consult with a CPA or other tax professional.

Fixed Income ETF Model-The models are constructed using passive fixed income ETFs. The models attempt to target varying levels of duration and credit exposure relative to the Barclays Aggregate Index. The expense ratios of the underlying ETF's are born by the investor and are separate and apart from CANVAS related fees.

Miscellaneous Limitations/Issues:

- Results in the Transition Portal reflect expense ratios corresponding to the specific funds indicated/provided by the investment professional. Expense ratios are provided by an unaffiliated database. Results also reflect projected future yields corresponding to such current indicated funds. Such data may not be precise;
- The risk-free rate used in the calculation of Sortino, Sharpe, and Treynor ratios is 5%, consistently applied across time;
- OSAM did not begin to offer CANVAS until April 2019. Prior to 2007, OSAM did not manage client assets; and,
- A copy of OSAM's written disclosure Brochure, Form CRS and Privacy Notice remains available on this CANVAS website or at www.osam.com.

Release and Hold Harmless

The professional, to the fullest extent permitted under applicable law, agrees to release, defend, indemnify and hold OSAM (including its officers, directors, members, owners, employees, agents, and affiliates) harmless from any and all adverse consequences, financial or otherwise, of any type or nature arising from or attributable to the professional's access to, and use of, CANVAS, including, but not limited to, any claims for alleged or actual client losses or damages of any kind or nature whatsoever (including without limitation, the reimbursement of reasonable attorney's fees, costs and expenses incurred by OSAM relating to investigating or defending any such claims and/or demands), except to the extent that actual losses are the direct result of an act or omission by OSAM that constitutes willful misfeasance, bad faith or gross negligence as adjudged by a court of final jurisdiction.

*****except in the unlikely event that the performance of the proxy used in lieu of the actual ETF was materially different (positive or negative)

Lastly, please be advised, without limitation, OSAM shall not be liable for Losses resulting from or in any way arising out of (i) any action of the investor or its previous advisers or other agents, (ii) force majeure or other events beyond the control of OSAM, including without limitation any failure, default or delay in performance resulting from computer or other electronic or mechanical equipment failure, unauthorized access, strikes, failure of common carrier or utility systems, severe weather or breakdown in communications not reasonably within the control of OSAM, inaccuracy or incompleteness of any third-party data, or other causes commonly known as "acts of God," or (iii) general market conditions. Under no circumstances shall OSAM be liable for consequential, special, incidental or indirect damages, punitive damages, or lost profits or reputational harm. Additionally, the responsibility solely rests on the "master user" of CANVAS at each independent firm, and NOT OSAM, to close out any associated users who may terminate at any time.

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