FEDSPEAK MOTIVES VS REALITY

HEDGE FUNDS (Inception)	AUGUST 2022	YEAR-TO-DATE	ANNUALIZED
Venator Founders Fund (March 2006)**	**-0.6%**	**-32.7%**	**9.1%**
Venator Select Fund (September 2013)	**3.4%**	**-45.4%**	**8.3%**
S&P/TSX Total Return (March 2006)	-1.6%	-7.2%	6.2%
Russell 2000 (March 2006)	-2.0%	-17.2%	7.2%
S&P Toronto Small Cap (March 2006)	-2.6%	-9.9%	2.8%
S&P 500 (March 2006)	-4.1%	-16.1%	9.3%

ALTERNATIVE MUTUAL FUNDS (Inception)	AUG 2022	YTD	1-YR	3-YR	5-YR	10-YR
Venator Alternative Income Fund* (January 2020)**	**0.3%**	**-10.6%**	**-10.0%**	**1.9%**	**3.1%**	**5.6%**
B of A Merrill Lynch High Yield Index (August 2008)	-2.4%	-11.0%	-10.4%	0.8%	2.4%	4.4%

** As of August 31, 2022*

*** Venator Founders Alternative Fund, which holds the same securities as Venator Founders Fund, is available as a Liquid Alternative Mutual Fund; it is eligible to be held in both registered & non-registered accounts.*

**** Performance data prior to January 24, 2020, relates to Class F Units of Venator Income Fund, which was distributed to investors on a prospectus-exempt basis in accordance with National Instrument 45-106*

August was a wild month as corporate earnings were generally strong, with the markets 15% rally coinciding with the heart of the July 15-August 15 earnings season, before the Fed threw cold water on the earnings parade with a week to go in the month. Our own equity holdings had significantly better performance during a stellar earnings reporting season but were dragged down by the broader markets in the latter half of August. Our Income Fund was insulated from bond weakness due to its high coupon/low duration characteristics and we look forward to increased consistency as a result of our recent shift to higher coupon yields.

As noted above, earnings season was quite strong for our companies. We saw some truly eye-popping numbers this quarter. In terms of higher-profile positions, Uber put up a big beat for the second quarter in a row, although the stock still sits 30% below where it came into the year. The biggest "beat" came from previously written about pharma research outsourcer, Inotiv, which reported revenue of $172M vs $142M expected and EBITDA of $36M vs $23M expected; the stock is still down 50% this year even though revenue and earnings expectations are currently 20% and 50% higher vs January. By and large, our companies are still growing, they are growing faster than expected, they are outpacing their faltering competitors, and their balance sheets are getting stronger. That being said, with their competitors weakening, comparable valuations are weakening as well, which is weighing on our companies' valuations, which has been the "good houses in bad neighborhood" issue we have been facing this year.

As has been widely reported, financial markets *really* didn't like what Fed Chairman Powell had to say at his Jackson Hole confab last Friday. On the back of zero reported month-over-month inflation in July and an expected zero in August (along with an inflation *negative* leading indicator producer price index), Powell effectively said that one month doesn't make a trend and the fight against inflation continues. He also said to expect some "pain", which really upset the markets. But Chairman Powell said something else we found very interesting; he said not to expect any rate cuts anytime soon (echoing our thoughts from last month's letter, although we didn't expect him to actually address the notion of 2023 rate cuts directly).

Firstly, why was anyone expecting Powell to say anything other than this? Were people really hoping he would say, "it looks like input prices are down, inflation is licked, and we are going to stop raising rates and maybe even lower them next year – GAME ON!"? Even if that is actually the plan, *there was no way he was going to say this!!!* The Fed's motivation right now is to keep sentiment subdued until the economy gets back to a semblance of post-COVID productivity and supply chain normalcy. Let's not forget that we have seen three *major* shocks to the system in 20 years (two external) that resulted in a forced ratcheting down of interest rates to sub-1% – 9/11, the financial crisis, and COVID. A more “normal” historical rate is 3%-5%, depending on the state of the economy, with today’s conditions (inflation coming down rapidly but on the brink of recession) arguing more for “in the threes” than “in the fours”.

But we want to come back to the statement that we should not be expecting any rate cuts in the near future – presumably referring to next year. The market took “we are not done fighting inflation” plus “we aren’t going to reverse course for some time” as equaling “we think inflation is staying high *regardless* of the data, we are going to 6%, and we are staying up there even if we cause an outright depression”. Hence the sell-off. But, by committing to not reversing rates in the intermediate future, they also *implicitly* committed to not deliberately “overshooting” the mark. There is no plan to go to 7% and then ratchet back down to 5% if that proves too high. Whatever the high watermark is that they have in mind, they plan on sticking with it, which means we should get a pause in rate hikes, or at least a slowdown, sometime soon if the various inflation numbers continue to trend down and GDP remains subdued. Remember, contrary to popular fishing-for-clicks media would have you believe, prices don’t have to come *down* for inflation to get back below 2%, they just have to stop going up for 12 months. Next month will be month #2 of no sequential inflation. Maybe this was a COVID induced bout of high (10%+) but short-lived (January 2021 to June 2022) inflation after all...

We reserve the right to change our mind!

Brandon Osten, CFA
CEO, Venator Capital Management Ltd.