WHO BENEFITS FROM "HIGHER FOR LONGER"?

HEDGE FUNDS (Inception)	AUGUST 2023	YEAR-TO-DATE	ANNUALIZED
Venator Founders Fund (March 2006)**	**-9.0%**	**17.4%**	**8.4%**
Venator Select Fund (September 2013)	**-14.5%**	**23.3%**	**6.4%**
S&P/TSX Total Return (March 2006)	-1.4%	6.9%	6.3%
Russell 2000 (March 2006)	-5.0%	9.0%	7.1%
S&P Toronto Small Cap (March 2006)	-1.3%	4.4%	2.9%
S&P 500 (March 2006)	-1.6%	18.7%	9.6%

ALTERNATIVE MUTUAL FUNDS (Inception)	AUG 2023	YTD	1-YR	3-YR	5-YR	10-YR
Venator Alternative Income Fund* (January 2020)**	**0.4%**	**6.8%**	**1.2%**	**2.3%**	**2.2%**	**4.3%**
Venator Founders Alternative Fund (July 2021)**	**-9.1%**	**16.2%**	**-5.2%**	**-**	**-**	**-**
B of A Merrill Lynch High Yield Index (August 2008)	0.5%	7.2%	7.0%	1.9%	3.2%	4.4%

** As of August 31, 2023*
*** 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*
***** Venator Offshore Fund is available as the US dollar version of Founders Fund strategy*

Markets struggled a bit in August. While consensus is largely set on the interest rate hike cycle being done, or close to done, the wall of worry is focused on "higher for longer". Short-term market moves are hyper focused on macro narratives. The latest little economic data point swings broader indices daily and correlations are currently so high that a mere 0.5% move sends 80% of all stocks in the same direction. Rare is the day when we see a 60/40 split of stocks moving in opposite directions. Whatever company specific news was reported yesterday is irrelevant in the face of a 3,000-person shortfall in employment data or a 0.05% tick in the 10-year treasury bond. Macro narratives are so much easier than company analysis. Certain creative macro analysis "statistics" can be cherry picked to say almost anything. We are always amused when we hear some harbinger of doom confidently announce that in the last 100 years there have been five instances of X following Y with the Fed doing Z and in four of those times the markets dropped 15% in the next nine months. It sounds good and is incredibly specific and fills airtime, but with a sample size of five, no serious statistician would put much weight on this stuff.

Some of our biggest to-date gainers gave back some of those gains as small caps suffered last month. Our homebuilders and building product companies saw a checkback later in the month on some Fed rate commentary (we could still raise rates) even though "higher for longer" is basically a Goldilocks scenario for the sector (retail was also weak, but we have limited exposure to that sector). Any talk of high rates has historically been bad news for the sector, and we saw drops in our names whenever Powell and Co pontificated on the longevity of 5%+ rates. This is material for us as homebuilders, land developers and building products are currently the largest component of our portfolio.

We wouldn't go so far as to say "This time it's different" but, rate increases shouldn't be looked at in a vacuum. The current shortage of housing in the US is a function of a decade of underbuilding in the wake of the 2008-2009 housing crisis. It is also a function of a long period of low rates that have locked in existing mortgages below 4%, while a new mortgage will cost you 7%. This has resulted in a lack of existing home inventory pushing new homes to a historically high one-third of all homes sold. But there has been an additional tailwind for large public homebuilders. Higher rates and tighter lending standards have made financing much more onerous for smaller builders, leaving large builders with a greater share of a growing pie.

That the sector cut back production in the back half of last year (because they didn't see this dynamic coming either) meant a slow first half of this year in terms of volumes, but surprising profits due to the durability of margins. But for the next several quarters, they will be looking at easy year-over-year comparisons that should make growth look strong. While this growth could be fleeting as demand levels off next year, the additions to book value will be sticky with no land impairments on the horizon. With last month's weakness, our homebuilders again trade below our forward book value estimates (and some are below current book value).

We also believe there are several good opportunities in distributors that supply the homebuilders. They will be subject to the same easy year-over-year comparable results that will benefit the builders. In the case of distributors, business is often split roughly 50/50 between building and repair/renovation. We would expect the latter business to improve as well, although not to the same extent as new construction. Large project business has grounded to a halt, but, with the average home being 40+ years old, there is plenty of ongoing maintenance to be done.

We agree with the "higher for longer" view and can envision a sub-3% inflation rate with interest rates holding at 5%+. The economy is coming off a very strange and unprecedented three-year stretch, but we don't think that 5% is an abnormally high rate (this was the rate in the booming 1990s), so we don't see any urgent reason for it to be lowered barring a "hard" landing for the economy (another favorite macro debate). There will always be emerging growth opportunities to invest in on a special situations' basis. But in terms of a sector of the economy that directly benefits from "higher for longer" from a business perspective, we can think of no better business than the building of new homes for the next five years. That we are buying at discounts to book value only makes the risk/reward that much more attractive.

We reserve the right to change our mind!

Brandon Osten, CFA
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