Investment Playbook Weekly Update

20th January, 2023

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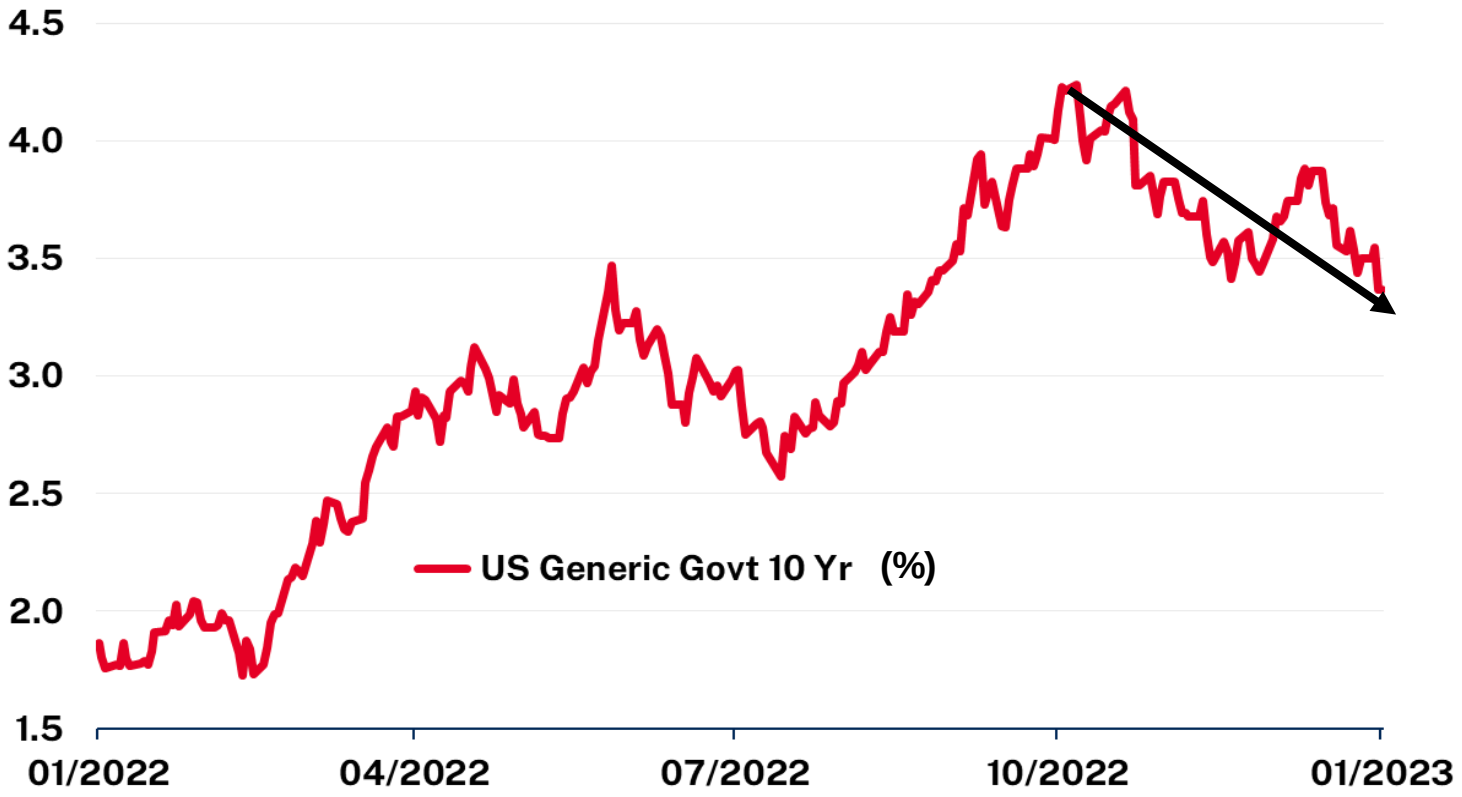
Charts of the week

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US 10Y Yield Has Receded To 3.36%

Recession fears act as a glass ceiling on long dated bonds



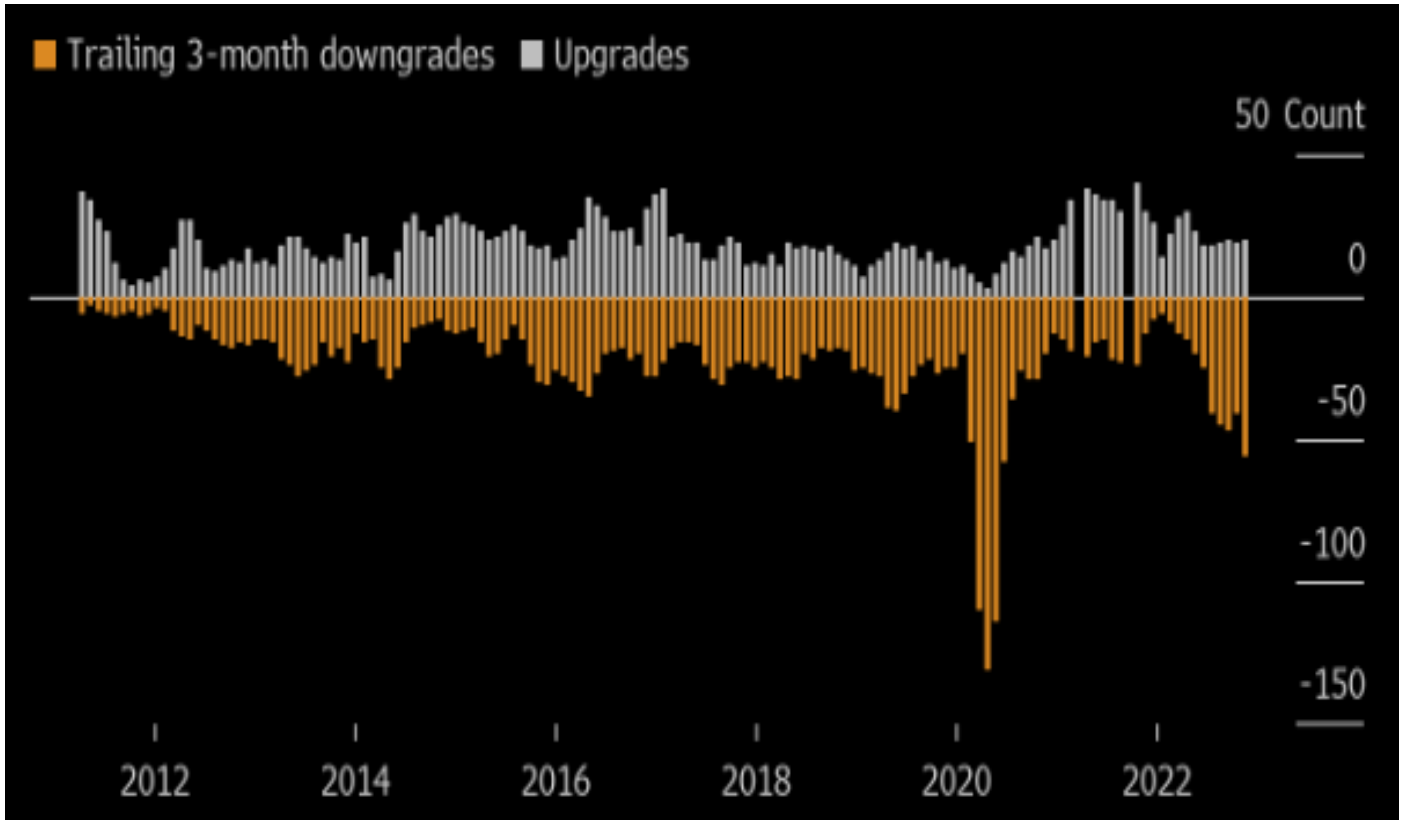
- The 10Y US treasury yield has dropped almost 100 bps since October 2022.
- The spread between UST 3M & UST 10Y is now at -134bps, at its most inverted since 1980.
- Such a drop is due to receding inflation as well as a potential economic slowdown (recession fears).
- Any chance to see the 10Y US Treasury yield moving back above 4%, should be taken as an opportunity to add duration to the portfolio.

Source: Bloomberg, January 2023

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US Loan Downgrade Pace Accelerates

Trailing three-month downgrade pace jumped to highest since 2020



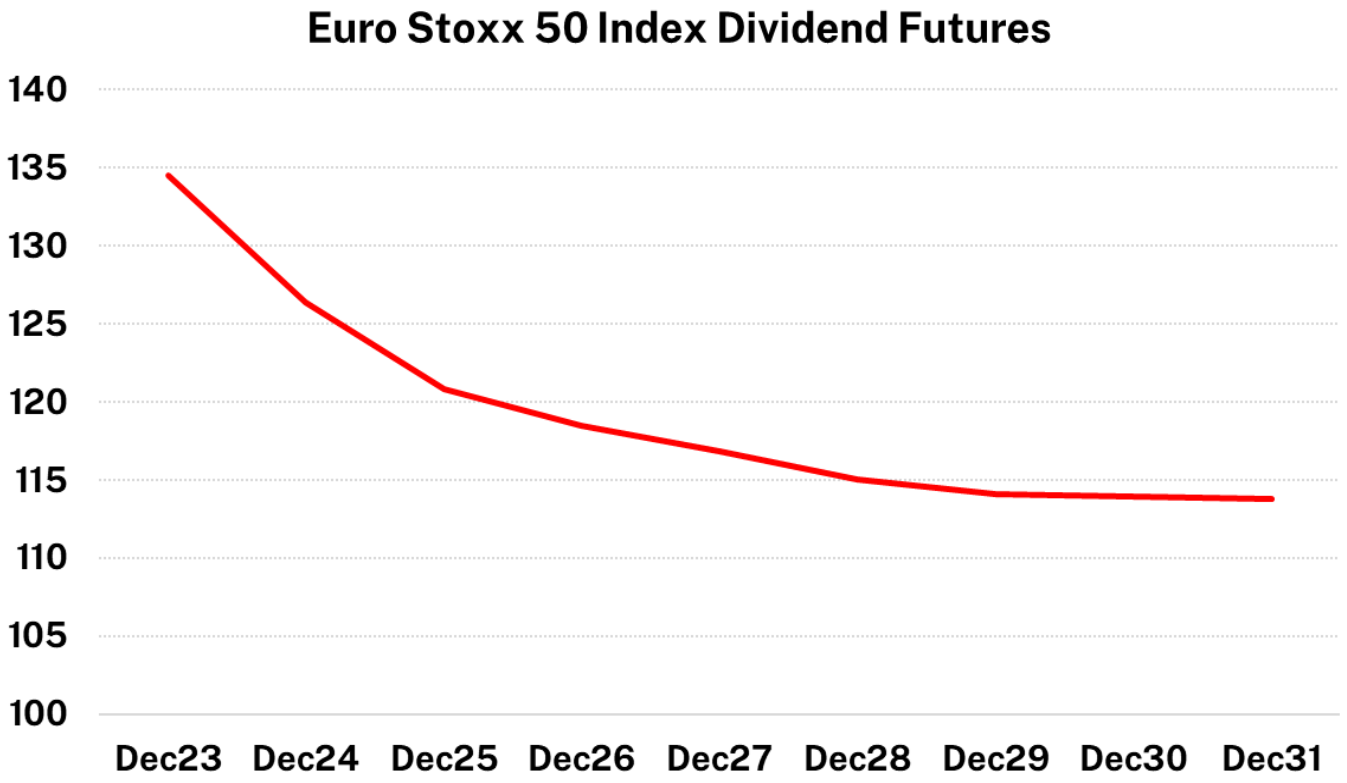
Source: Citigroup, Bloomberg, January 2023

- The number of bonds being downgraded is increasing significantly quicker than those being upgraded by rating agencies.
- This illustrates the difficulty for the weakest issuers to refinance their debt.
- The trend is unlikely to reverse soon because Central Bankers have made it clear that rates would be higher for longer. A recession in the coming quarters is likely to exacerbate the problem.
- Distressed managers (our top conviction currently) are likely to do well since the number of opportunities looks quite supportive.

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European Dividends: Bearish View

The Euro Stoxx 50 dividend curve is downward sloping until 2031.



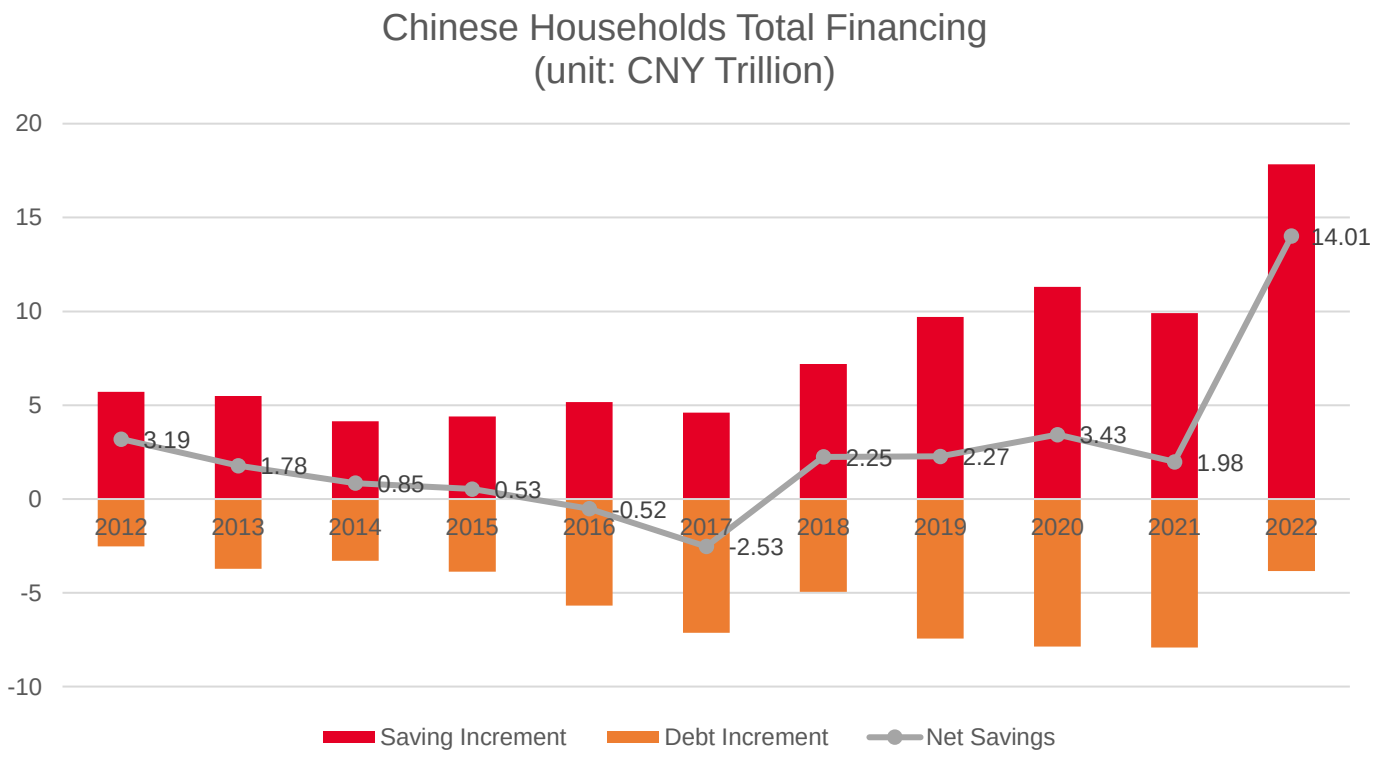
- The Dividend Futures curve illustrates investors' anticipation regarding the level of dividends that will be paid in the coming years.
- The curve is downward slopping for European stocks indicating either a depressed economic environment or the anticipation that companies will reduce the amount of dividends paid going forward.
- Since the latter explanation sounds dubious, it's more likely investors are implying more pain in the coming years for European stocks.

Source: Bloomberg, January 2023

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Chinese Households - Excess Savings

PBoC report showed that the excess savings in 2022 is larger than the previous ten years combined.



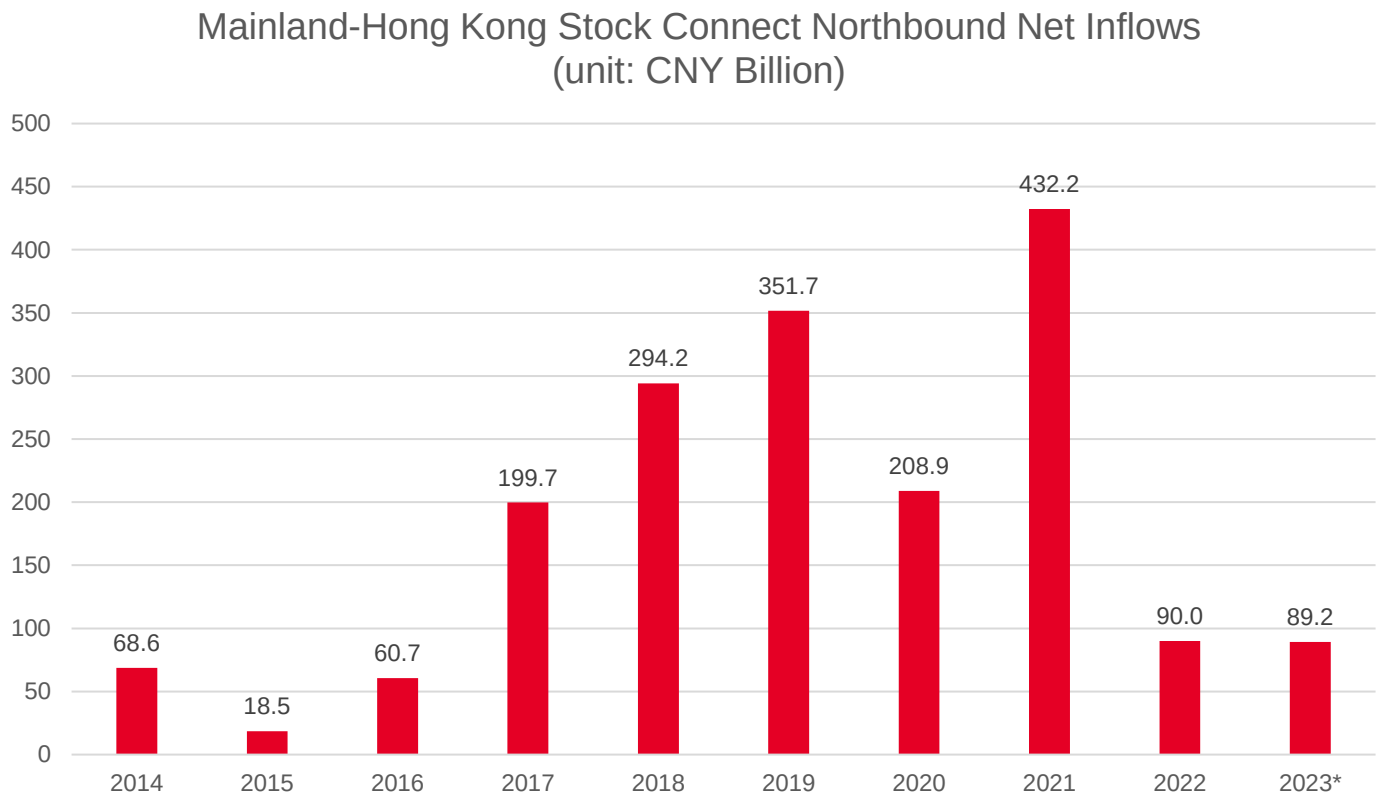
Source: PBoC, Lighthouse Canton, January 2023

- In 2022, Chinese household's excess savings reached a historical high, CNY 14 trillion (~$2.1 trillion), due to reduced consumption as a result of zero-covid controls, as well as low willingness to invest in either financial markets or real estates.
- After reopening, consumer spending has been recovering strongly. The December retail growth beat consensus, despite the large infection waves in all major cities.
- However, domestic investment is not recovering as fast, especially in the property market. The situation needs to be monitored.

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Buying the Dip on Chinese Onshore Assets

Net inflows in the first 11 trading days in 2023 is close to the total amount of 2022.



- International investor sentiment has been significantly boosted by China ending the zero-covid controls, providing support to the property sector and easing crackdown on large internet platform companies.
- Chinese assets, including A shares, H shares and ADRs, are still relatively cheap, after the recent rally.

Source: HKEX, Lighthouse Canton, January 2023

**Till 17th Jan 2023*

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LC Views - Summary

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LC Views Summary (1/2)

Sub-Asset	Recommended Positioning
Rates	• **Rates will be higher for longer globally**. Central Banks have no choice but to keep on tightening financial conditions to drive inflation, supposedly back to 2%, over time. Risky assets are likely to remain under stress and we anticipate volatility to remain reasonably high across risky asset classes in 2023. For this reason, we reiterate our views to keep a significant allocation to liquid alternative strategies and bonds which present low correlation to equities and / or thrive during periods of stress.
Fixed Income	• **Bonds now command attractive yields,** and the portfolio should have a larger allocation to the asset class. Short Duration (<3) Investment Grade bonds are attractive and should be part of any portfolio. We recommend being extremely selective with High Yield bonds and recommend adding duration if/when 10Y US Treasury yield (currently at 3.4%) get closer to 4%. We also recommend adding distressed managers who benefits from markets dislocations and mispricing. We expect Fed rates in the U.S. to peak in Q2 next year at 5.0%-5.25% but, contrary to what is implied by fixed income investors, we do not believe that the Fed will have to cut rates later this year. Should that be the case (steep recession), equities are likely to be trading much lower by year-end.
Equities	• We hold a slightly bearish view on equities over the next 6-12 months given that interest rates are expected to continue rising and economic growth, while not collapsing, is softening. Equities have discounted higher interest rates, but not the decline in profits that those rates will, in time, bring about. Like in most bear markets, investors should not be surprised by short term rallies (10-15%), as is the case, so far in 2023. While valuations have reverted towards their long-term average (Fwd. P/E 17x for S&P 500), earnings are bound to be revised lower in the coming quarters. In such a context, we recommend (by order of preference) Long/Short managers, Fixed Coupon Notes (FCNs) with low strikes (75%) and quality stocks. We acknowledge that many stocks have now reached attractive levels and will look to opportunistically add exposure to them over time.

LC Views Summary (2/2)

Sub-Asset	Recommended Positioning
Currencies	• **Currencies** are expected to remain volatile throughout 2023. We recommend adding active managers (Macro funds) to monetize opportunities in currencies and rates. Exposure to EUR and GBP could be increased over time to benefit from the recent lows.
Commodities	• We like Gold for several reasons: diversification benefit, inflation hedge, geopolitical risk and weakening USD. • Oil is likely to remain highly speculative. On the one hand, the slowdown of the economic activity globally, (recessionary fears) should reduce demand progressively in 2023. On the other hand, the lack of capex spending during covid as well as the possibility for OPEC to reduce production will inevitably support prices in the long run. China's re-opening is another positive influence on the price of oil.
Real Estate	• **Real Estate** represents a good hedge against inflation, with its steady income, often linked to inflation. Tightening financial conditions have started to cause sharp repricing in property prices globally and threaten rental growth rates. The risk of further correction in real estate prices should not be underestimated.

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