Investment Playbook Weekly Update

18th – 22nd September 2023

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2022 ASIAN PRIVATE BANKER AWARDS FOR DISTINCTION
BEST INDEPENDENT WEALTH MANAGER ASIA PACIFIC

PRIVATE BANKING AWARDS 2023 ASIAMONEY
RISING STAR, SINGAPORE

2021 ASIAN PRIVATE BANKER AWARDS FOR DISTINCTION
BEST INDEPENDENT WEALTH MANAGER WEALTH PLANNING SERVICES

GLOBAL Private Banking INNOVATION AWARDS 2022

OUTSTANDING DIGITAL TRANSFORMATION IN COVID 19 BY A FAMILY OFFICE

BEST FAMILY OFFICE – MIDDLE EAST

BEST FAMILY OFFICE – UNITED ARAB EMIRATES

2021 ASIAN PRIVATE BANKER AWARDS FOR DISTINCTION
BEST INDEPENDENT WEALTH MANAGER INVESTMENT ADVISORY

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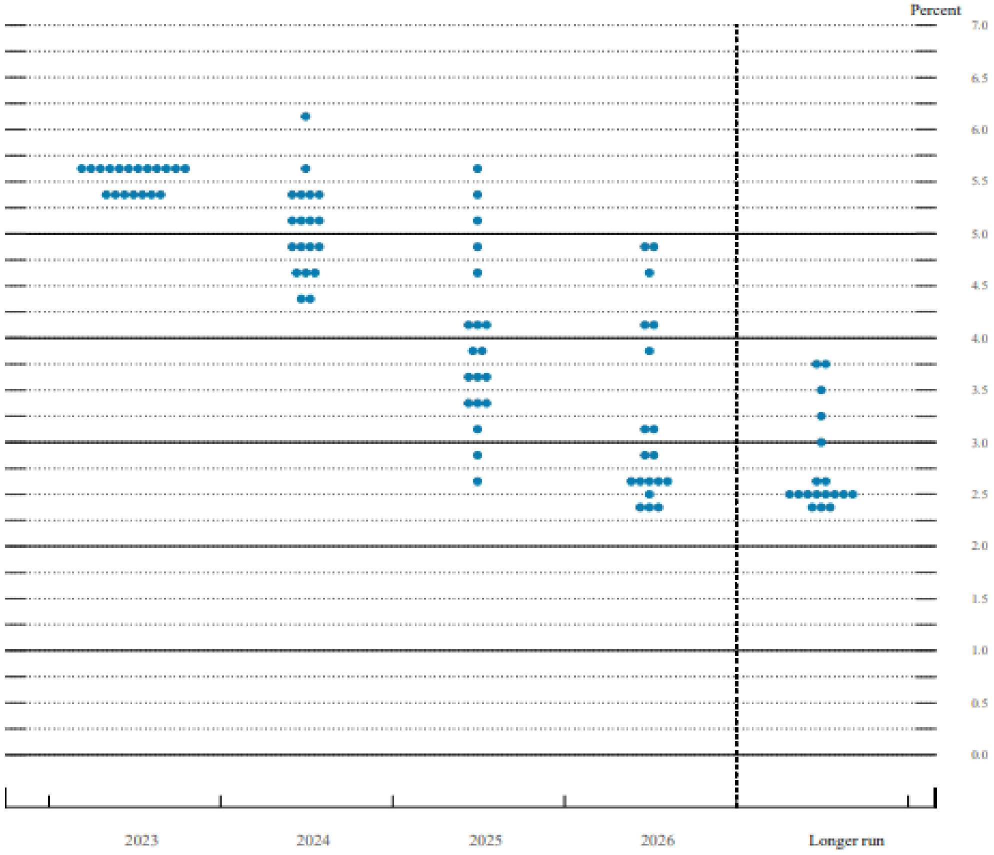
Charts of the week

1

The Fed Pauses

Shows A Hawkish Dot Plot

Fed Fund Rates Dot Plot



- The Fed held its target Fed Fund Rate range at 5.25% to 5.5%, while updated quarterly projections showed 12 of 19 officials favored another rate hike in 2023.
- Policymakers also see less easing next year, with the median forecast for the federal funds rate at 5.1% by year-end, up from 4.6% when projections were last updated in June.
- New projections for GDP growth increased to 2.1% for 2023 and 1.5% for 2024 (from 1.0% and 1.1%, respectively).

Source: Federal Reserve, September 2023

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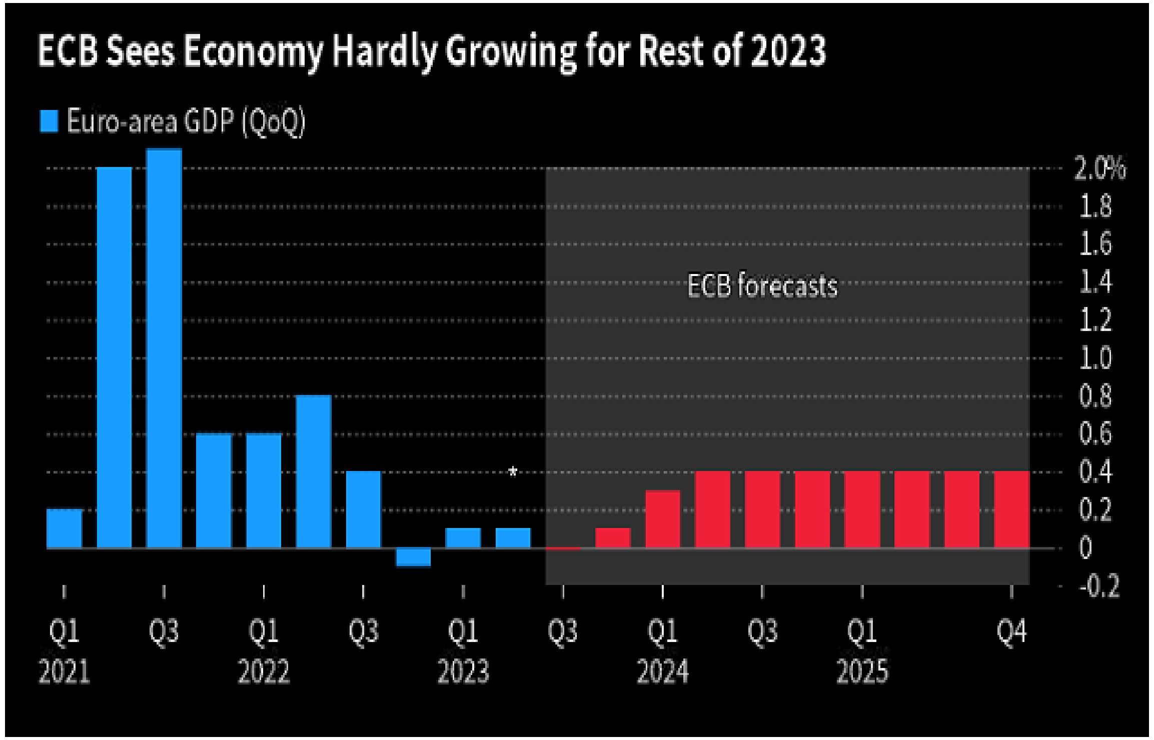
ECB Hiked Rate For A 10th Consecutive Time

Sacrificing Growth Over Price Stability



- The decision to hike the deposit rate by 25bps to 4% came amid a faltering economy.
- ECB Chief Lagarde admitted that growth will be "very, very sluggish" and forecasts acknowledged that the economy may even be on the verge of shrinking.
- The problem for policymakers is that inflation — in their own words — is still anticipated to stay "too high for too long." On both the headline gauge and an underlying measure that strips out energy and food, price growth is stuck above 5%.

 Source: Eurostat, Bloomberg, September 2023

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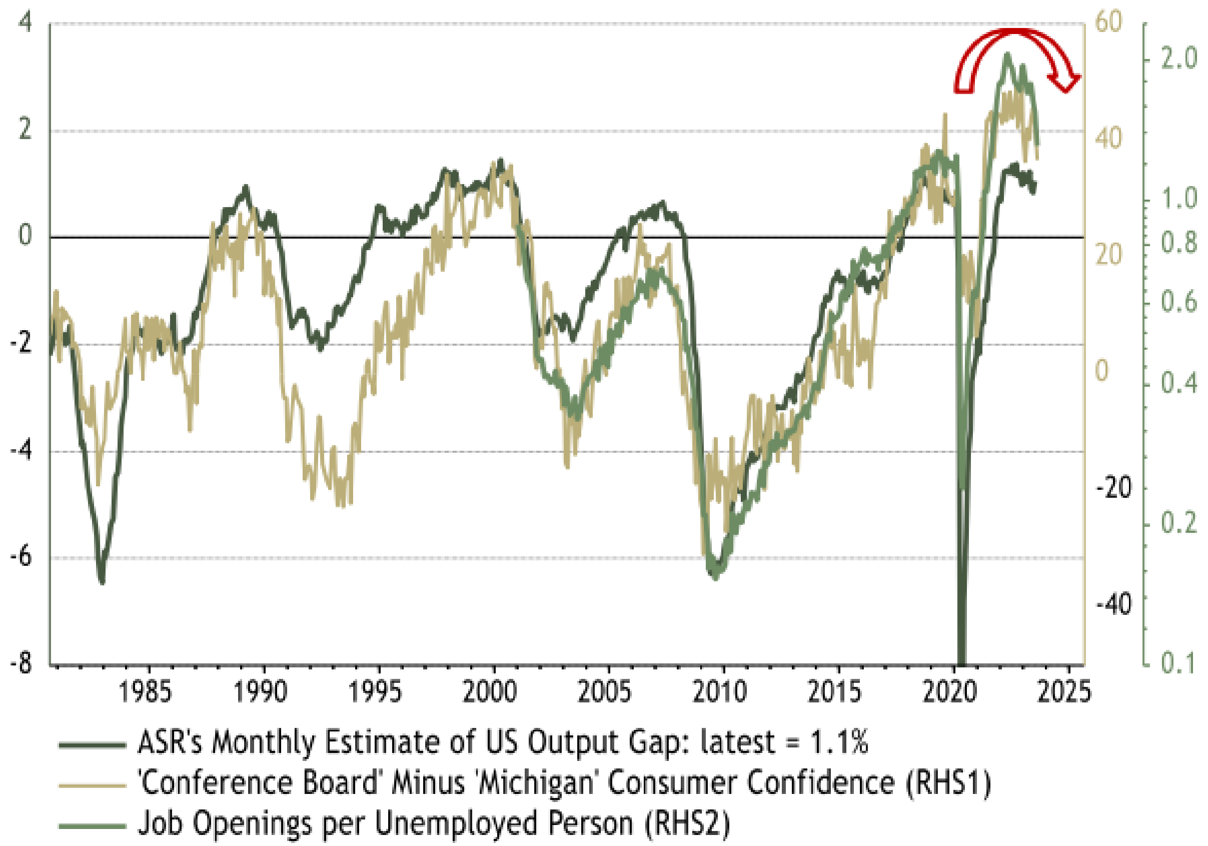
Not the Time to Settle for Soft Landing Narratives

Some Major Macro strategy Tectonic Plates are On the Move

Macro Indicators appear to be at a turning point



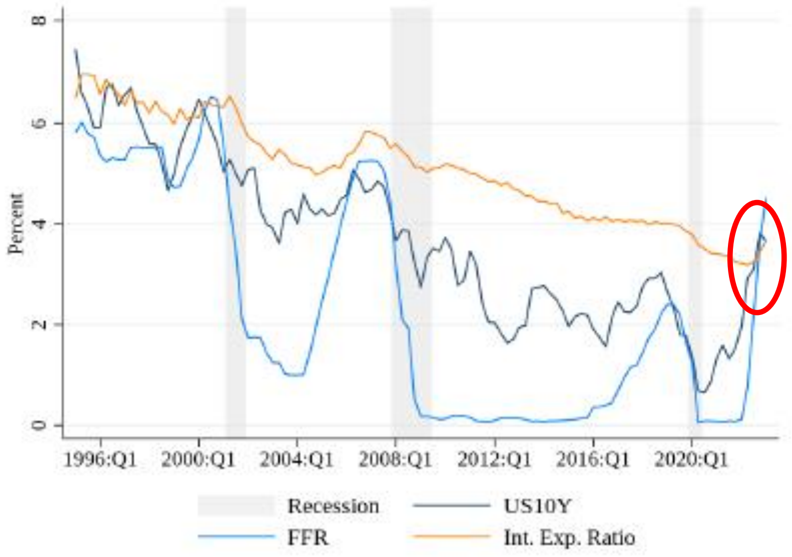
- US output gap (difference between US output and potential GDP) is turning less positive. Risk assets tend to outperform when output gaps are getting less negative/more positive – and vice versa.
- The gap between the Conference Board and University of Michigan measures of consumer confidence has begun to shrink. (*Both measures are important indicators of consumer sentiment and economic expectations in the US but have some difference in terms of methodology and frequency of release).
- And finally, ratio of job openings to unemployed is clearly decreasing.

 Source: ASR, September 2023

Why default rates in US is still low? (1/2)

Corporate Interest expense ratio lagged the Fed funds rate

Figure 1: Corporate Interest Expense Ratio and the Federal Funds Rate



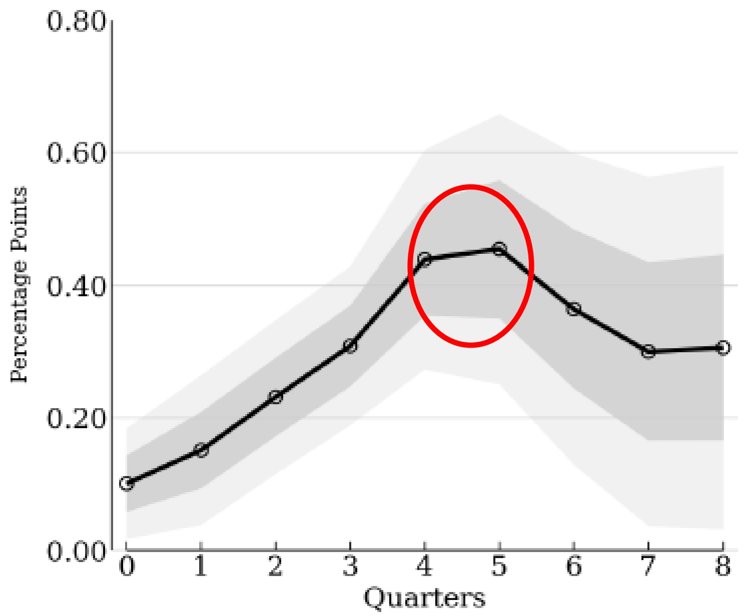
- The figure shows the time series of corporate interest expense ratio lagged the federal funds rate and the 10 Y Treasury yield.
- The actual impact of higher rates are starting to show now as can be evidenced by the upward skew in the interest expense ratio (refer the upward tick in the orange line).
- Delay in borrowing/ negative covenants in bond indentures are the key reason for the lag as per the Boston Federal Reserve, particularly post GFC.

Source: Federal Reserve of Boston, Aug 29th , 2023

Why default rates in US is still low? (2/2)

It takes 5 quarters to have the maximum effect of a rate hike.

Figure 2: Response to a 1 Percentage Point Increase in the Federal Funds Rate

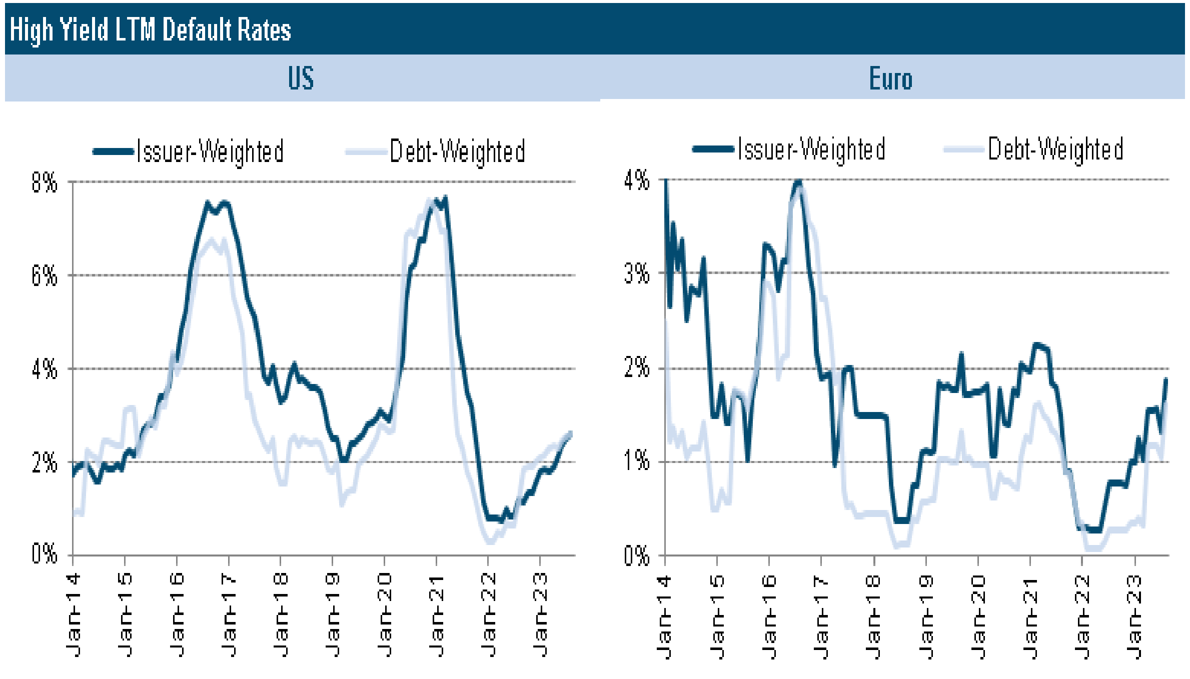


- The figure shows the change in the corporate interest expense ratio (in % points) following 1 percentage point increase in the Fed funds rate, relative to no change in the Fed funds rate.
- The light grey shaded area represents 95% confidence bands. It essentially states that the impact of 1 percentage point rate hikes translates to an approx. 0.65 (max) percentage point increase in corporate interest expense ratio.

Source: Federal Reserve of Boston, Aug 29th , 2023

Default Rates- US & EU

Increasing Defaults in US & EU high yield space



Source: CreditSights, ICE BofA HY Indices

- Default rates inched up both in US and EU high yield space. US HY default stood at 2.6% in Aug whereas in EU stood at 1.9%.
- Transportation and Retails sectors led the charts in US in the month of Aug with Western Global Alliance and Caravana.
- Distress Ratios in US fell to 9.5% (from 9.8% earlier) and so did in EU at 13.5% (from 14% earlier). While US distress ratio stood about 400 bps below GFC average, the EU distress ratio is 30bps above presently.

 Source: CreditSights, September 2023

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The Bursting Of The Global “Luxury” Bubble

Luxury stocks are correcting, offering a compelling opportunity for discerning investors.

Source: ASR Ltd. / LSEG Datastream, September 2023

- Based on findings from Absolute Strategy Research (ASR), the S&P's Global Luxury index has lagged behind by 10% in the last six months. This underperformance is attributed to both consumers depleting their COVID savings as well as the slowdown in China's economic recovery. Additionally, the reintroduction of US student loan repayments is on the horizon.
- In essence, there's a likelihood that revenue growth and profit margins may fall short of projections in the upcoming quarters. We recommend selling deep out-of-the-money puts on high quality stocks (weekly trade idea), providing an opportunity to acquire few quality names at approximately 20% less in a six-month span.

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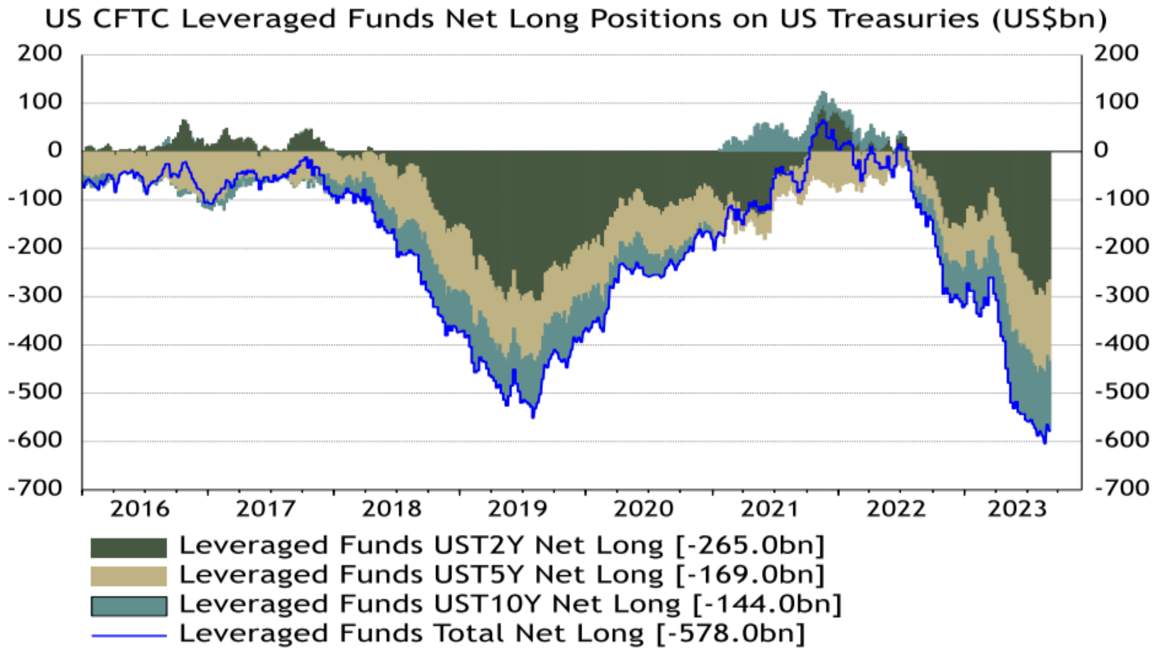
Hedge Funds Are Massively Shorting US Treasuries

The $600bn 'big-short' built up by Hedge Funds in US Treasury futures is raising concerns



Source: ASR Ltd. / CFTC, September 2023

- In March 2020, the US Treasuries market faced massive disturbances when COVID-19 led to huge losses for hedge funds, which had taken highly leveraged bets on Treasuries through derivatives and repurchase agreements. This resulted in forced sales that disrupted the Treasuries market until the Federal Reserve stepped in. By 2023, despite rising US rates since 2020 and the looming refinancing of a third of US government debt in 2024, the risky hedge fund "basis trade" seems to be returning. The US Federal Reserve's recent report indicates that hedge funds repo borrowing increased to $600bn from October 2022 to May 2023, surpassing its 2019 peak. The situation poses a financial risk due to its high leverage, leaving the market vulnerable to fluctuations in US rates.

Treasury Yields Hit A 16-Year High

The benchmark 10-year Treasury yield reached a session high of 4.45%, its highest level since 2007

- US yields hit a 16-year high ahead of the conclusion of the Federal Reserve's policy meeting on Wednesday, at which the central bank is expected to hold rates steady, but may indicate its willingness to keep monetary policy tighter for longer.
- Inflation has been elusive, placing central bankers in a complex predicament. If they overreact, they could jeopardize their economies. If they're too cautious, they might inadvertently allow prices to escalate.

Source: Bloomberg, September 2023

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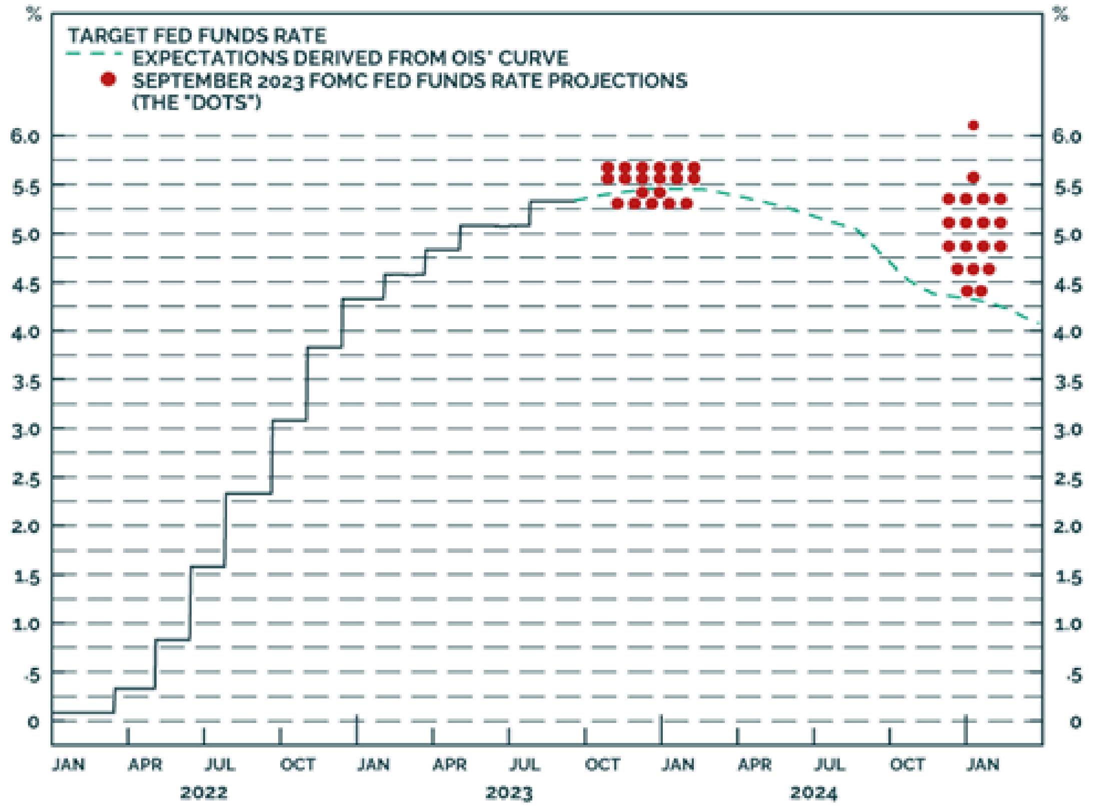
Higher For Longer

The benchmark 10-year Treasury yield reached a session high of 4.45%, its highest level since 2007



Source: BCA Research, September 2023

- The Fed held the funds rate steady on September 20th but did make significant changes to its economic and interest rate projections.
- First, the median forecast for real GDP growth was revised significantly higher for 2023 and 2024. The Fed also reduced its median unemployment rate forecast from 4.1% to 3.8% for this year and from 4.5% to 4.1% for next year.
- Finally, and most importantly, the Fed's median interest rate forecast was revised up significantly for 2024. FOMC participants continue to anticipate that one more 25 basis point rate hike will be necessary before the end of this year, and now anticipates far fewer 2024 rate cuts than was the case in June.

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Oil Back Above 90$

The surge in energy prices presents a significant challenge for central bankers

Source: Bloomberg, September 2023

- BCA Research remains bullish oil largely because they expect production discipline to be maintained by OPEC+, led by the Kingdom of Saudi Arabia (KSA) – this year and next.
- BCA does not expect KSA to extend its unilateral 1mm b/d production cut thru next year, as markets will be tight enough by then to support Brent prices above $100/bbl.
- BCA's 2024 Brent forecast is $118/bbl.

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LC Views - Summary

2

LC Views Summary (1/2)

<table>
<tr><th>Sub-Asset</th><th>Recommended Positioning</th></tr>
<tr><td>Rates</td><td>• The Fed left the Fed funds target range at 5.25-5.5% and continues to indicate the prospect of another 25bp hike this year. Longer term, the Fed is signaling less prospects of rate cuts with Fed officials now seeing interest rates coming down to 5.1% in 2024 (most likely two rate cuts of 25 bps each), higher than June's outlook for rates to finish next year at 4.6%. Chance of a recession has also diminished as it guides inflation back to 2%. Fourth quarter year-on-year growth has been revised up for this year to 2.1% from 1% while for next year it is up to 1.5% from 1.1%.</td></tr>
<tr><td>Credit</td><td>• We continue to favor investment grade bonds to build a strong foundation for the portfolio and seek to compliment the latter with selective high yield bonds for yield enhancement. While we recommend to allocate a larger portion of the portfolio in short duration bonds due to the elevated yields, we are actively extending duration (in IG credits) into the 5-10Y space with the spike in Treasury yields. We advise against increasing duration beyond 10 years as the risk-reward does not favor ultra-long ends. Due to the challenging economic outlook ahead, we see further opportunity in special situations bond funds, which could provide asymmetric returns in a prolonged distressed and disruptive credit market.</td></tr>
<tr><td>Equities</td><td>• There are two potential scenarios for the global economy. First, higher interest rates could further suppress global economic growth, leading to margin compression and possibly slower growth. Alternatively, if the economy demonstrates robustness (for instance, the Atlanta Fed GDP Now is a remarkable 5.8%!), Central Bankers would be compelled to continue raising rates to align inflation with the 2% target. In either scenario, equities are poised for challenges.

• The valuation of equities currently appears expensive:
- Historically speaking, with a forward P/E ratio at 19x, investors might find limited opportunities for substantial returns in the forthcoming 12 months.
- Even more pertinently, when compared to bonds and cash, equities seem less appealing. To illustrate, the disparity between the yield of 3-month US Treasuries and the S&P 500's dividend yield has expanded to a significant 400 basis points. Such pronounced differentials were last witnessed in 2000 and 2007, both instances that preceded major equity downturns.

• Considering the uncertain trajectory for equities over the next year, coupled with their elevated valuations and their comparative disadvantage against cash and bonds, our recommendation is to underweight equities in portfolios.</td></tr>
</table>

LC Views Summary (2/2)

Sub-Asset	Recommended Positioning
Currencies	• **Currencies** are expected to remain volatile throughout 2023. Given higher recessionary risks, the USD may strengthen over a short-term tactical horizon but for longer term investors, we continue to hold the view for a bearish USD. Exposure to JPY, EUR and GBP could be increased over time to benefit from the recent lows and a peak in dollar's strength driven by peak policy rates. We also recommend adding active managers (Macro funds) to monetize opportunities in currencies and rates.
Commodities	• Our long-term view for a bearish USD is likely to be supportive for Gold. We also like the yellow metal for structural reasons: diversification benefit, inflation hedge, geopolitical risk and de-dollarization trend. • Oil is likely to remain highly speculative this year as witnessed in March. On one hand, recessionary fears should temper demand. On the other hand, the production cut by OPEC+ members and already low oil inventories will support prices in the near term.
Real Estate	• 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. There will be opportunities to pick good REITs cheaper next year. • With the recent banking turmoil, Commercial Real Estate exposure is increasingly at risk given the large exposures the smaller banks have to the sub-sector. Clients holding on to any related exposures should consider removing them.

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