Investment Playbook Weekly Update

9 September 2022

LIGHTHOUSE CANTON



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Macro & Fixed Income

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Macro – Executive Summary

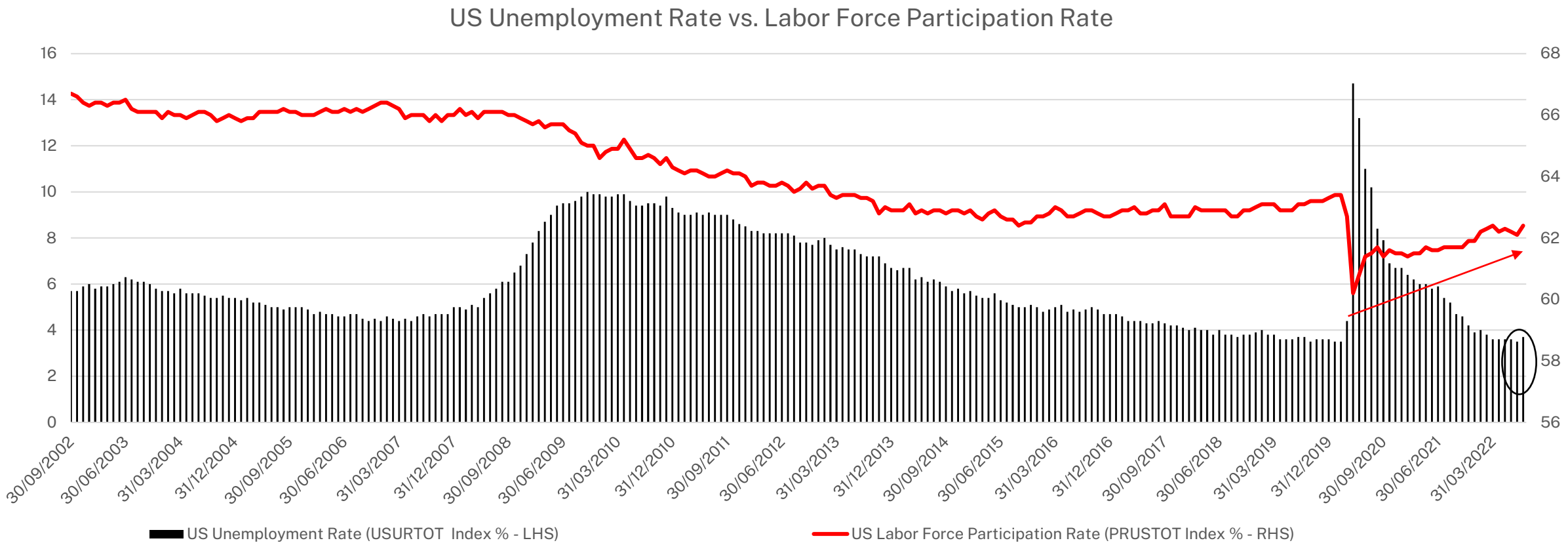
		Current Quarter	Market Expectations (3Q22 to 4Q22)	Δ *	Market Expectations (1Q23 to 2Q23)	Δ*	LC Views
US	Real GDP Growth (QoQ)1	-0.6%	2.8%	+	2.3%	-	▪ Core inflation remains elevated and sticky, and benchmark real rates are still negative. Pressures from shelter costs are building. ▪ Guidance from Jackson Hole is loud and clear: the central bank is committed to ensuring that inflation returns to target. Consequently, we do not believe that the Fed will reverse its policy and start decreasing rates next year, as implied by the Futures market. ▪ Upbeat economic data that came in this week (labor market and manufacturing and services activity) surprised to the upside and reinforces this view although the labor market might be showing first signs of easing.
	Inflation (QoQ)[2]	8.5%	1.0%	-	2.9%	+	
	Unemployment (QoQ)[3]	3.7%	3.7%	-	4.0%	+	
	Probability of Recession[4]				50.0%		
	Policy Rate[5]	2.5%	3.7%	+	3.8%	+	
EU	Real GDP Growth (QoQ)[6]	0.6%	9.9%	+	-1.8%	-	▪ Inflationary risks continue to be on the upside but with the weak economic outlook, the ECB should keep its cautiously hawkish stance. Money markets fully priced in a percentage-point of tightening by the ECB's October meeting. ▪ Core inflation continues to climb higher which is putting the ECB increasingly behind the curve. ▪ We think risk of policy error is high and the possibility for upside rate surprises should not be underestimated.
	Inflation (QoQ)[7]	9.1%	1.9%	-	3.1%	+	
	Unemployment (QoQ)[8]	6.0%	6.9%	+	7.1%	+	
	Probability of Recession[9]				55.0%		
	Policy Rate[10]	-0.1%	1.6%	+	2.2%	+	
UK	Real GDP Growth (QoQ)[11]	2.9%	4.1%	+	-1.5%	-	▪ Investors expect Bank of England to continue to raise interest rates aggressively with at least 6 more rates hike of 25 bps each over the next 12 months.
	Inflation (QoQ)[12]	10.1%	5.8%	-	1.9%	-	
	Unemployment (QoQ)[13]	3.8%	4.0%	+	4.5%	+	
	Probability of Recession[14]				60.0%		
	Policy Rate[15]	1.8%	3.5%	+	4.4%	+	

Macro – Executive Summary

		Current Quarter	Market Expectations (3Q22 to 4Q22)	Δ *	Market Expectations (1Q23 to 2Q23)	Δ *	LC Views
China	Real GDP Growth (QoQ)[16]	-2.6%	15.9%	+	-11.8%	-	▪ Although policymakers have ramped up stimulus measures, poor housing market dynamics, weak domestic demand, an impending contraction in exports due to a strong dollar and the zero-covid policy will limit the effectiveness of these efforts. ▪ The main economic risk for China is deflation and the continuation of underwhelming economic growth. Core and service consumer price inflation are both below 1% and property prices are deflating. Falling prices amid high debt levels is a recipe for debt deflation. - BCA (15 Aug) ▪ The recent bailout funds that have been announced only account for 1.5-2% of last year's total financing for developers. The fragmented nature of China's property market also makes bailouts difficult to organize and implement. ▪ Recent attempts by the government to revive the housing market are likely to prove unsuccessful given poor household income growth. BCA highlights that there has been no recovery in the Chinese economy in past cycles, without a revival of the housing market.
	Inflation (QoQ)[17]	2.7%	1.6%	-	0.6%	-	
	Unemployment (QoQ)[18]	4.0%	4.0%	+	4.0%	-	
	Probability of Recession[19]				20.0%		
	Policy Rate[20]	4.4%	N.A.	+	3.7%	-	
India	Real GDP Growth (QoQ)[21]	13.5%	9.1%	-	-1.6%	-	▪ Q1FY23 real GDP growth of 13.5% surprised on the downside. Compared to pre pandemic levels, growth was quite tepid, specially in the services sector. ▪ RBI is expected to hike rates in the next two policy meets by 35 bps to 60 bps and then pause to assess the impact on growth and inflation. The future policy direction will depend on the RBI's timeline to bring inflation down to its 4% target and prevailing growth conditions.
	Inflation (QoQ)[22]	6.7%	2.3%	-	2.5%	+	
	Unemployment						
	Probability of Recession[23]				0.0%		
	Policy Rate[24]	5.4%	N.A.		N.A.		

Data points to easing US Labour market

Both rising unemployment rate (3.7%) and participation rate (62.4%) signals easing labour markets

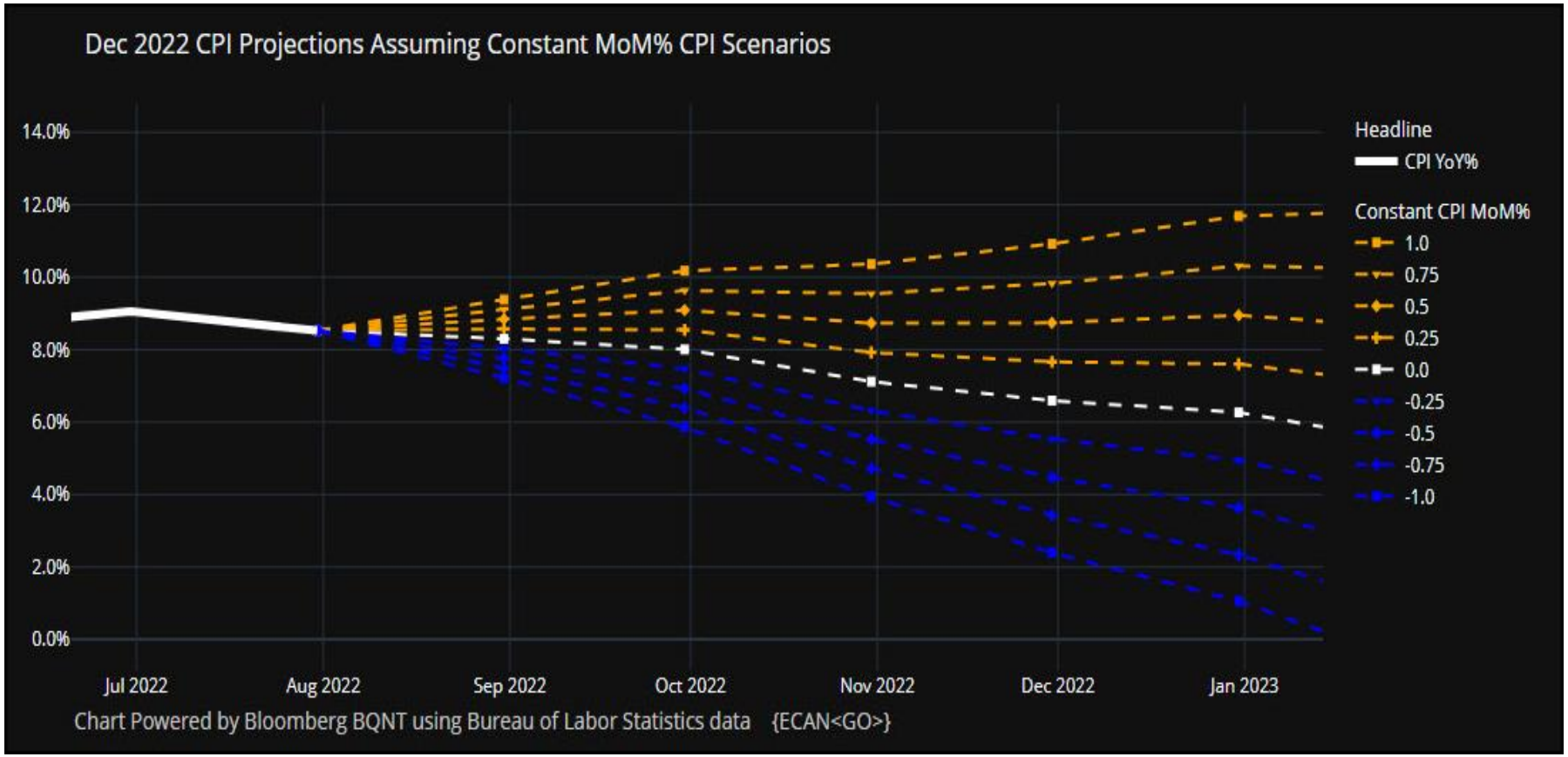


Source: Bureau of Labor Statistics, Bloomberg, September 2022

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US CPI – Decisive factor

After mixed labour market data Sept CPI is crucial to September FOMC rate decision



Source: Bloomberg, September 2022

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Macro – Executive Summary (Sources)

1) "GDP US Chained 2012 Dollars QoQ SAAR ", GDP CQOQ Index, Source: Bureau of Economic Analysis. Forecast data derived from "GDP US Chained 2012 Dollars NSA", GDNSCHWN Index, Source: Bureau of Economic Analysis.
2) "US CPI Urban Consumers YoY NSA", CPI YOY Index, Source: Bureau of Labour Statistics. Forecast data derived from "US CPI Urban Consumers NSA", CPURNSA Index, Source: Bureau of Labour Statistics.
3) "U-3 US Unemployment Rate Total in Labor Force Seasonally Adjusted", USURTOT Index, Source: Bureau of Labour Statistics.
4) "United States Recession Probability Forecast", ECRPUS 1Y Index, Source: Bloomberg.
5) "Federal Funds Target Rate - Upper Bound", FDTR Index, Source: Federal Reserve.
6) "Euro Area Gross Domestic Product Chained 2010 Prices QoQ", Source: Eurostat. Forecast data derived from "European Union Gross Domestic Product Chained 2010 Prices ", ENGKEU27 Index, Source: Eurostat.
7) "Euro Area MUICP All Items YoY NSA »", ECCPEMUY Index, Source: Eurostat. Forecast data derived from "Eurostat European Union HICP All Items NSA", CPALEU Index, Source: Eurostat.
8) "Eurostat Unemployment EU SA", UMRT27 Index, Source: Eurostat.
9) "Eurozone Recession Probability Forecast ", ECRPEU 1Y Index, Source: Bloomberg.
10) "ESTR Volume Weighted Trimmed Mean Rate", ESTRON Index, Source: European Central Bank.
11) "UK GDP Chained GDP at Market Prices YoY ", UKGRABIY Index, Source: UK Office for National Statistics. Forecast data derived from "UK GDP Chained GDP at Market Prices", UKGRABMI Index, Source: UK Office for National Statistics.
12) "UK CPI EU Harmonized YoY NSA", UKRPCJYR Index, Source: UK Office for National Statistics. Forecast data derived from "UK CPI EU Harmonized NSA", UKRPCHVJ Index, Source: UK Office for National Statistics.
13) "UK Unemployment ILO Unemployment Rate SA", UKUEILOR Index, Source: UK Office for National Statistics.
14) "United Kingdom Recession Probability Forecast", ECRPGB 1Y Index, Source: Bloomberg.
15) "UK Bank of England Official Bank Rate", UKBRBASE Index, Source: Bank of England.
16) "China GDP Constant Price QoQ SA", CNGDPQOQ Index ,Source: National Bureau of Statistics of China. Forecast data derived from "China GDP Constant Price", CNGDGDP Index , Source: National Bureau of Statistics of China.
17) "China CPI YoY", CNCPIYOY Index,Source: National Bureau of Statistics of China. Forecast data derived from "China CPI MoM", CNCPIMOM Index, Source: National Bureau of Statistics of China.
18) "China Qtrly Registered Unemployment Rate in Urban", CNUERATE Index, Source: National Bureau of Statistics of China.
19) "China Recession Probability Forecast", ECRPCN 1Y Index, Source: Bloomberg.
20) "China 1 Year Benchmark Lending Rates" , CHLR12M Index, Source: The People's Bank of China.
21) "GDP Growth Annual % India", GDPGAIND Index, World Bank Group. Forecast data derived from "India Qtr Real GDP By Expenditure Cons 2011-12 Prices ", IGQREGDP Index, Source: Central Statistics Office India.
22) "India CPI Combined YoY", INFUTOTY Index, Source: Central Statistics Office India. Forecast data derived from "India CPI Combined", INFUTOT Index, Source: Central Statistics Office India.
23) "India Recession Probability Forecast", ECRPIN 1Y Index, Source: Bloomberg.
24) "Reserve Bank of India Repurchase Rate Policy Announcement", INRPYLDP Index, Source: Reserve Bank of India.

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Fixed Income

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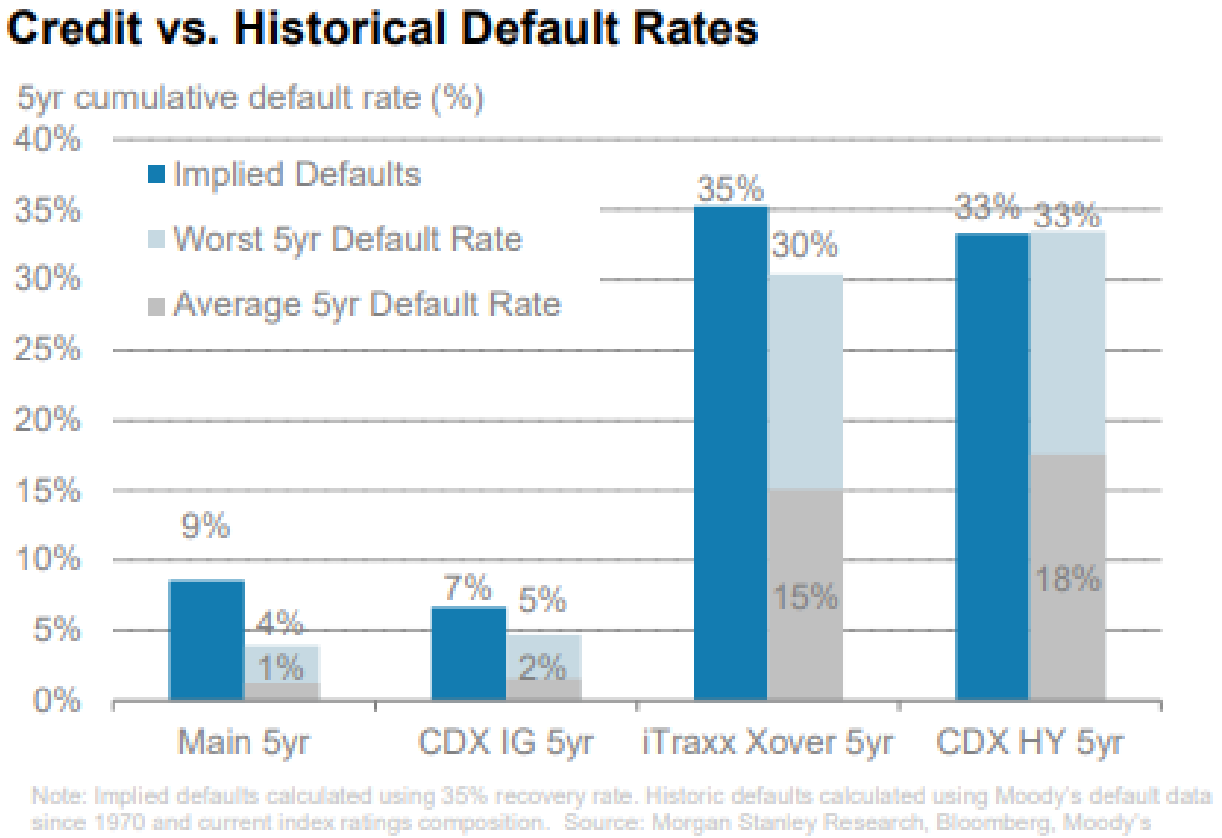
Fixed Income – Overview

	Sub-Asset	Region	IC Outlook (1Q23-2Q23)	IC Comments	Recommended Positioning
Long Term Rates	10Y Rate	US	↑	▪ Long term rates are likely to trend sideways as stagflationary forces could intensify by 1H23. ▪ Fed balance sheet roll off likely to create upward pressure on long end of yield curve. ▪ Despite potential downward pressure on long term rates as a result of recessionary fears, we broadly agree with BCA's view that there is further room for longer term rates to move higher as long as the Fed maintains its resolve in combating inflation.	
		EU	↑	• Long term rates are likely to trend sideways as stagflationary forces could intensify by 1H23	
Credit	IG Spread (bps)	US	↔	• Global Corporate bonds are likely to face headwinds up until 1H23. • Policy rates in 1H23 are expected to rise across DM, while corporate spreads should widen on back of a global economic slowdown and higher refinancing rates, with HY to be the most heavily impacted.	▪ We are selectively bullish on bonds as there are pockets of opportunities, we see in US IG credit. We suggest reallocating progressively to Investment Grade Bonds (Duration < 4) after September FOMC to lock in attractive risk adjusted carry. ▪ Avoid PERPs, Cocos, High Yield and long Duration (>5) bonds for the moment. ▪ Add Distressed managers to benefit from dislocations and mispricing.
		EU	↑		
	HY Spread (bps)	US	↑		
		EU	↑		

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European Credit – GFC type scenario priced in

European Crossovers are pricing in a cumulative 5Y default rate of 35%



Source: Germany, Federal Network Agencies, September 2022

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Equities Highlights

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Equities – Overview

Region	IC Outlook (1Q23-2Q23)	IC Comments	Recommended Positioning
US (S&P 500)	↓	▪ We hold a bearish view on US equities over the next 6-12 months and think the June/July rally is unsustainable given that interest rates are expected to continue rising, valuations are above their long-term average and economic growth, while not collapsing, is softening. ▪ US Equities are likely to continue to be negatively correlated with longer term rates for the rest of the year and are exposed to any hawkish comments from the FED. ▪ Elevated volatility likely to create dispersion which is a very ripe environment for Long/Short Strategies	▪ Take advantage of recent market rebound to reduce equity positions and take a more defensive stance in anticipation of another potential leg down. ▪ Consider adding lower beta equity managers who can take bidirectional bets.
EU (STOXX 600)	↓	▪ We think EU is in a precarious situation as it is likely to already be in recession. Elevated gas prices and energy rationing efforts would keep a lid on any growth prospects, and we anticipate corporate earnings pressure to intensify into 1H23. ▪ Despite the bleak economic situation, the consensus STOXX 600 earnings growth expectations is at >10%, a fairly optimistic scenario in our opinion. We expect more earnings misses to materialize over the next 12 months.	▪ Given more downside expected, we think it is still not a good time to be increasing exposure to European equities yet.

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Equities – Overview

Region	IC Outlook (1Q23-2Q23)	IC Comments	Recommended Positioning
China (CSI 300)	↔	▪ We reckon that Chinese valuations are attractive, but equities are likely to stay undervalued as growth is expected to slow down with Zero Covid Policy placing a lid on economic activity and profit outlook. ▪ A preliminary deal between the US SEC and China PCAOB has been reached allowing American accounting regulators to inspect the audit records of Chinese companies listed in New York. However, because of the structural nature of the US-China geopolitical rivalry, the road to success will be long and full of obstacles. ▪ We think markets are likely to trend sideways. Supportive policies and relaxations to ZCP would be key recipes to an eventual tailwind for market sentiments. Visibility remains very low on this front.	▪ We do not recommend taking on full beta risk just yet. Investors should continue to remain invested in low beta long short managers (FengHe, Luxence) for now. ▪ For direct stocks, we prefer bottom-up picks with strong earnings this year and clear growth trends ahead.
India (NIFTY 50)	↔	▪ India's economy seems to be holding up well despite higher oil prices. ▪ Recent correction in commodity markets (especially energy) and renewed FII buying has led to a strong rally in Indian equities (Nifty 50) In July and Aug 2022. ▪ Valuations on equities are slightly higher than their 20Y average but not at unrealistic levels. ▪ Despite the sanguine view on the region, we think a strong dollar serves as the biggest headwind to any meaningful upside to Indian equities.	▪ We recommend a cautious and staggered approach when it comes to allocating to Indian equities, as we await further clarity with respect to how the global macro situation unfolds and whether Indian corporate earnings can hold up in an increasingly tougher macro environment and a more restrictive monetary stance being taken by the central bank.

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Weak Chinese Equity Earnings Overall

~1% YoY earnings growth reported in 1H22, equating to 43% of full year 2022 consensus estimates

Sectors	All China					A shares				HK-listed				US-listed			
	# of cos reported	% mkt cap reported	1H22 earnings growth yoy	1H22 earnings % of 22E est.	2Q22 growth yoy	% mkt cap reported	1H22 earnings growth yoy	1H22 earnings % of 22E est.	2Q22 growth yoy	% mkt cap reported	1H22 earnings growth yoy	1H22 earnings % of 22E est.	2Q22 growth yoy	% mkt cap reported	1H22 earnings growth yoy	1H22 earnings % of 22E est.	1Q22 growth yoy
Cons. Disc.	715	97%	-14%	33%	-13%	100%	-16%	32%	-21%	96%	-4%	27%	41%	91%	-15%	36%	-14%
Cons. Stap.	282	99%	-9%	37%	22%	100%	-4%	37%	32%	92%	-26%	39%	-11%	24%	NM	46%	NM
Comm Svcs	207	99%	-1%	46%	5%	100%	-15%	43%	-21%	100%	5%	48%	11%	94%	-5%	40%	49%
Energy	110	100%	72%	73%	79%	100%	65%	72%	76%	100%	87%	77%	88%	-	-	-	-
Financials	191	100%	-1%	49%	3%	100%	1%	49%	5%	100%	-5%	49%	-2%	90%	-11%	52%	-5%
Banks	66	100%	7%	52%	6%	100%	8%	52%	7%	100%	6%	51%	4%	100%	-59%	67%	-72%
Brokers	107	100%	-40%	34%	-26%	100%	-27%	34%	-12%	100%	NM	25%	-95%	91%	-9%	53%	-4%
Insurance	18	100%	-14%	47%	13%	100%	-16%	47%	11%	100%	-12%	48%	15%	38%	NM	-2%	-52%
Health Care	527	98%	16%	43%	-8%	100%	11%	43%	-6%	95%	120%	34%	-4%	73%	NM	20%	NM
Industrials	1305	99%	5%	38%	-12%	100%	-5%	36%	-11%	97%	30%	44%	-27%	67%	NM	68%	NM
Info. Tech.	888	100%	16%	35%	26%	100%	7%	32%	13%	99%	58%	47%	71%	91%	NM	4%	91%
Materials	807	100%	5%	41%	-6%	100%	8%	42%	-3%	95%	-10%	37%	-30%	2%	NM	-	NM
Real Estate	231	99%	-58%	19%	-56%	100%	-59%	17%	-71%	98%	-57%	20%	-38%	99%	NM	-34%	NM
Utilities	144	98%	-25%	44%	-21%	100%	-13%	41%	-4%	90%	-40%	48%	-64%	-	-	-	-
Market	5407	99%	1%	43%	1%	100%	2%	43%	1%	97%	-1%	44%	2%	90%	-14%	39%	-4%
Market ex fin.	5216	99%	2%	40%	0%	100%	3%	40%	-1%	97%	1%	41%	4%	90%	-15%	37%	-4%
Market ex fin. & energy	5106	99%	-6%	37%	-8%	100%	-4%	36%	-9%	97%	-9%	38%	-7%	90%	-15%	37%	-4%
New China	2466	99%	4%	39%	5%	100%	7%	39%	7%	97%	13%	39%	11%	97%	-15%	39%	-6%
Old China	2941	99%	0%	45%	0%	100%	1%	44%	-1%	98%	-3%	45%	0%	54%	NM	10%	NM

Source: LGT, Sep 2022

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Forex, Commodities & Alternatives

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Commodities – Overview

	Sub-Asset	IC Outlook (1Q23-2Q23)	IC Comments	Recommended Positioning
Commodities	Gold	↔	▪ There are two opposite forces for Gold. ▪ On the one hand, gold is likely to face near term headwinds on back of higher rates (which is an opportunity cost for gold holders) and a strong dollar. ▪ On the other hand, increasing holdings of gold in global central bank reserves points to a de-dollarization trend which could act as tailwinds for the yellow metal.	▪ We believe that some allocation to gold makes sense as a means to hedge longer term inflation and geopolitical shocks. ▪ As it is difficult and extremely tricky to time and trade the yellow metal, our recommended way to gain exposure is via external managers (Delbrook - gold equities, Drakewood - gold futures/options)
	Oil	↔ / ↑	▪ Oil should continue to remain volatile on back of higher recession risks globally. ▪ However, geopolitics remain a wild card which makes the near-term outlook uncertain. ▪ Supply side conditions remain fairly tight and inelastic, especially with OPEC exercising some restraint on production despite high oil prices.	- N.A.

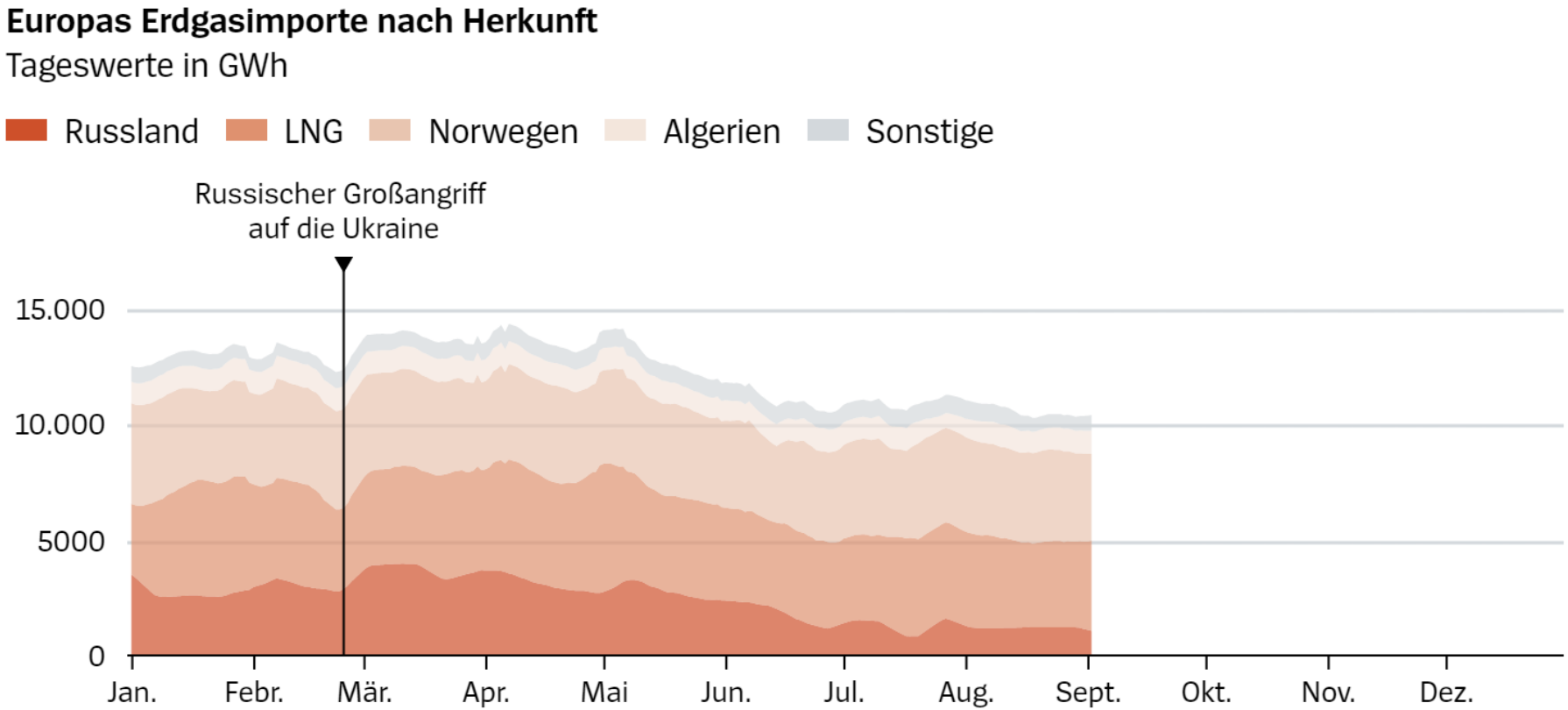
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Forex – Overview

	Sub-Asset	IC Outlook (1Q23-2Q23)	IC Comments	Recommended Positioning
FX	USD	↑	▪ We anticipate the dollar to maintain its strength throughout 22 as recessionary fears accelerate. ▪ This trend could reverse should the FED start reversing its monetary policy, which is very unlikely in the coming quarters.	• Big picture, we do believe the dollar's strength is overstretched. • However, recessionary fears as well as a hawkish fed will continue to underpin its strength. • Despite its strength, longer term investors may consider gradually adding DM currency exposures (EUR or GBP) as they are 1) trading at historically cheap valuations (EUR & GBP) versus the dollar, and 2) Sharper rate hikes in these economies are expected to narrow the interest rate differentials between the US.
	EUR	↔	▪ At parity (Vs USD), the currency looks cheap by historical standards and could benefit from ECB starting increasing rates faster than anticipated and/or a termination of the Ukrainian war.	
	GBP	↑	▪ Inflation seems out of control in the UK. The BoE will have to act swiftly and aggressively increase rates to keep inflation below 10% which should narrow the interest rate differentials between the US and reverse some of its YTD losses.	
	CNY	↓	▪ The PBOC is very supportive and has started decreasing interest rates. The CNY is likely to be soft if the rates differential widens with other central banks ▪ Chinese export volume started to decline in August due to weaker external demands, which does not bode well for the CNY - BCA (Sept. 8). To support the currency, the PBOC cut forex reserve requirement ratio for 200 bps (from 8% to 6%) on Monday (Sept. 5). This is unlikely to stop the depreciation. More actions could be expected from China.	
	JPY	↓	▪ The JPY is unlikely to rebound as the rates differential increases with other central banks.	

Europe Energy – Russian Gas Contribution

At ~11%, Russia overall has a lower contribution to European important than the headlines may suggest

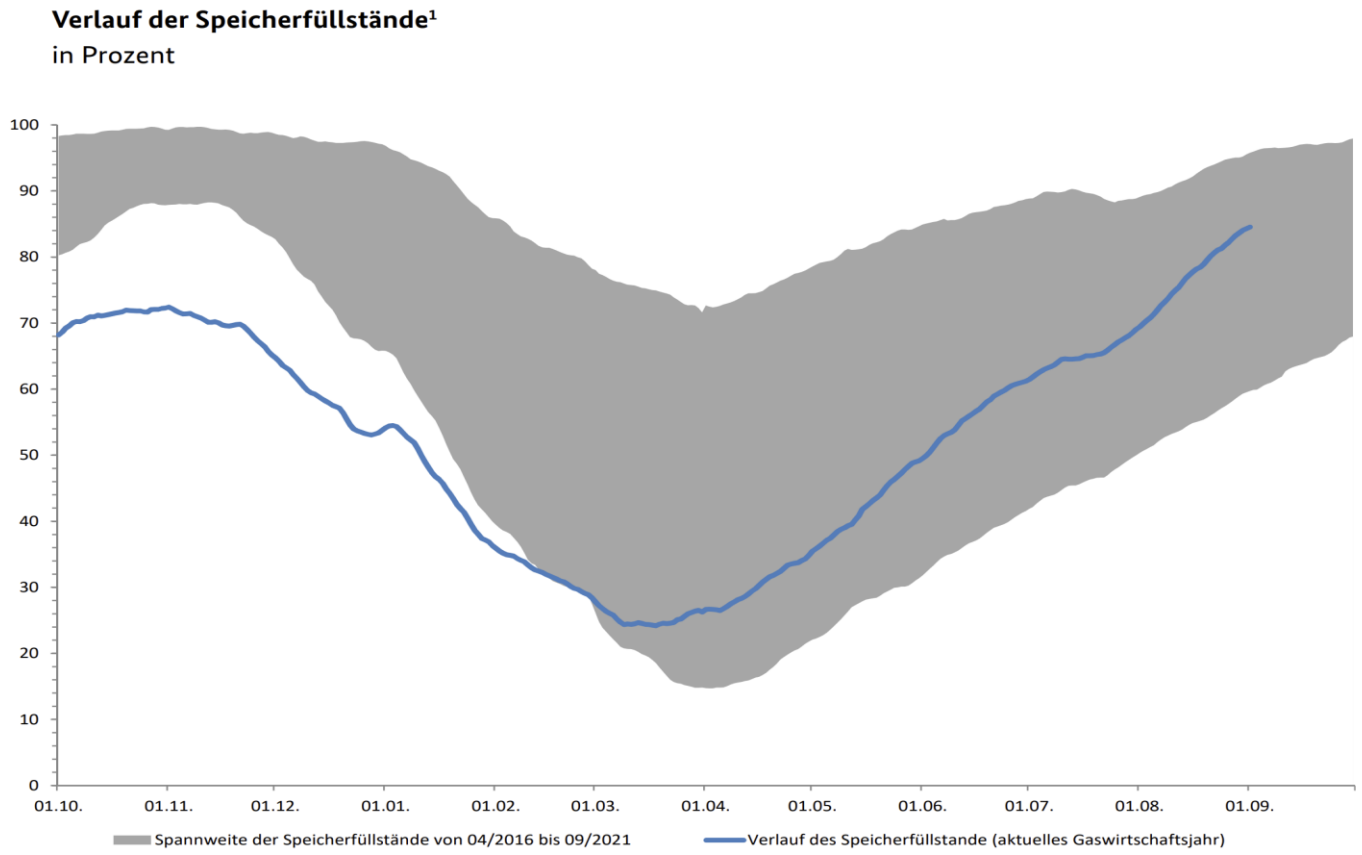


Source: Der Spiegel, September 2022

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Europe Energy – Gas Rationing is Key

% of filled gas storage in Germany has risen considerably and is now higher than in previous years

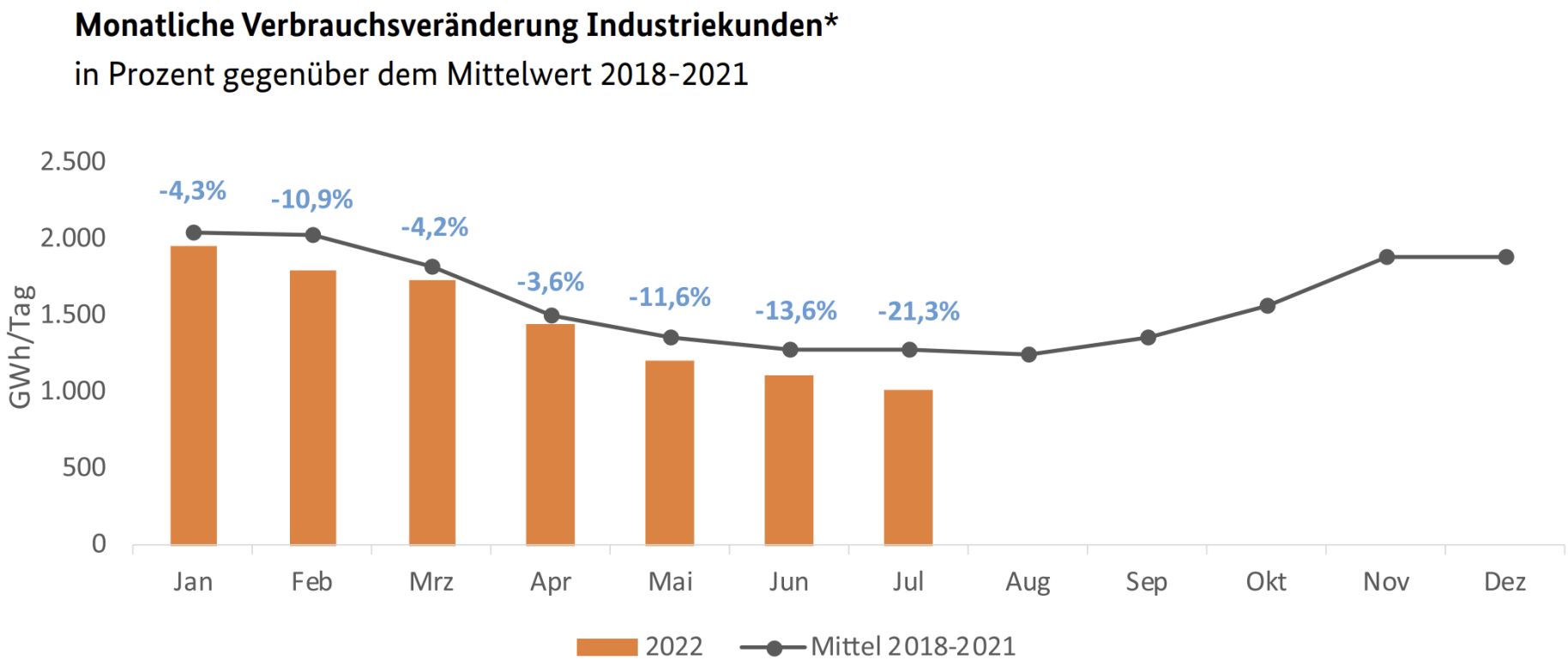


Source: Germany, Federal Network Agencies, September 2022

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Europe Energy – Gas Rationing is Key

Gas consumption is lower than 2018-2021 averages and savings seem to have accelerated



Source: Germany, Federal Network Agencies, September 2022

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EU Likely Able Cope without Nord Stream 1

20% gas demand reduction required (with a cold winter) to get to 90% storage level next winter again.

Theoretical annualised demand destruction/reduction (vs. baseline of 380bcm) to reach 90% storage again by 1 November 2023

Bcm	Scenario 1	Scenario 2 bis (most likely)	Scenario 2	Scenario 3
Loss of Russian supply	-140	-125	-110	-99
Additional LNG	60	60	60	60
Additional gas pipelines	10	10	10	10
Net supply reduction	-70	-55	-40	-29
EU 27 Natural gas demand destruction/reduction needed	**-70**	**-55**	**-40**	**-29**
%	**-18%**	**-14%**	**-11%**	**-8%**
EU 27 Natural gas demand destruction/reduction needed (with a cold winter)	**-90**	**-75**	**-60**	**-49**
%	**-24%**	**-20%**	**-16%**	**-13%**

Source: Kepler Cheuvreux estimates, Scenario 1 zero Russian natural gas pipeline supplies from 1 November 2022, Scenario 2 bis: zero gas supply from Nord Stream 1 and latest Ukraine gas transit (equivalent to 15bcm on an annualised basis), Scenario 2: zero gas supply from Nord Stream 1 and Ukraine gas transit (equivalent to 30bcm on an annualised basis), Scenario 3: current Nord Stream 1 gas flows of 11bcm (annualised) corresponding to 20% capacity and Ukraine gas transit (equivalent to 30bcm on an annualised basis), or +41bcm of supply vs. Scenario 1

Source: Kepler Equity Research, September 2022

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