Kwartaalupdate KEYPRIVATE

third quarter 2022

In the third quarter of 2022, inflation continued to be the main talking point among investors, economists, portfolio managers and central bankers. In many Western countries, we saw inflation figures of 10% and more. Figures we have not seen for the past 20 years or longer. Needless to say, the central banks stepped h ard on the monetary brake: short-term interest rates were raised sharply in the US and the euro zone. As a result of this aggressive monetary policy, long-term interest rates rose and the stock markets fell. On the economic front, this rang the alarm bells about a recession. This report provides an overview of the most important economic and financial trends. As well as a commentary on our net returns and a look into the future.

Geert Van Herck
Chief Strategist KEYPRIVATE

Economic environment

Counting down to the global recession: this is how we can best describe investor behaviour in the third quarter of 2022. Almost all the economic growth indicators published in the major economic regions pointed to a sharp slowdown in economic activity and it is just a question of waiting for the first negative growth figures to be published. Figure 1 shows the evolution of one of the most closely monitored economic indicators: global manufacturing confidence (the JPMorgan Global Manufacturing PMI index). Figure 1 shows that this indicator has been on a downward trend for a number of quarters. This points towards a steady decline in global industrial production. The index was at 50.3 points in September 2022: this is still just above the critical 50-point threshold. Above 50 points, we are looking at expansion of economic activity, but it is clear that the chance of a figure below 50 points is especially high. This would clearly indicate a recession or a very sharp slowdown in growth!

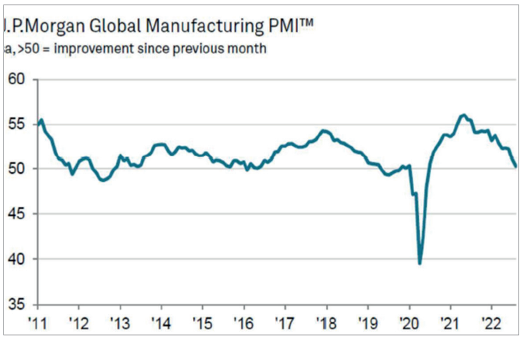

Figure 1: Trend in global manufacturing confidence in industry (JPMorgan Global Manufacturing PMI index)
Source : JPMorgan, S&P Global

Figure 2: Trend in companies' order books
Source : JPMorgan, S&P Global

What still causes the members of the Keyprivate investment committee the greatest concern is the trend in companies' order books. After all, new orders represent future production for companies. Figure 2 shows the trend in companies' order books. Here, too, even a quick glance at this figure shows a clear downward trend over a number of quarters. In other words, month after month we are seeing a decline in new orders at the companies working in the industrial and services sector. The global nature of the economic slowdown is underlined by the same decline in export orders from companies working in the industrial and service sectors. We can therefore treat the figure below as being a leading indicator of trends in global manufacturing confidence. Fewer orders will lead to a fall in economic activity, which could lead to a drop in business confidence!

The decline in global economic activity is far from encouraging news for investors. However, if we want to highlight one positive development (and one that might instil some courage in investors), it is the expected fall in inflation figures. Worldwide, we have seen a strong surge in inflation figures in recent months. This was caused by the sharp rise in commodity prices. Companies that received higher commodity bills passed on (part of) these higher costs to their customers and distributors. This led to a rising price trend (= inflation). However, figure 3 clearly shows that in the last few months, there has been a downward trend in the prices that companies in the industrial and services sector have had to pay (= input costs) and the prices they charge their customers (= prices charged). This trend reversal has everything to do with the correction affecting the commodities market. On the basis of these indicators, we are expecting lower inflation figures in the months ahead! This should allow the financial markets to take a deep breath and start a recovery.

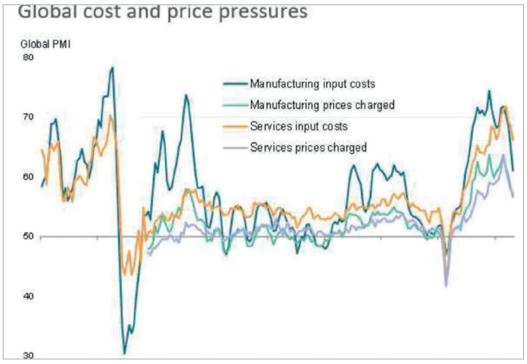

Figure 3: Trend in prices in the industrial and service sectors- Source : JPMorgan, S&P Global

Conclusion: from the analysis of global manufacturing confidence carried out above, we see two important trends. On the one hand, it is clear that we are on the brink of an international recession, and on the other hand, fears of this recession are causing a correction in commodity prices. On this basis, most economists are expecting lower inflation figures in the months ahead. For the Keyprivate investment committee, it is particularly important that lower inflation figures can give the markets some breathing space: a recovery in the equity and bond markets could be fuelled by expectations of lower global inflation, which would result in less nervousness among investors.

Financial markets third quarter 2022

Equity markets

For equity investors, the third quarter was one to forget as fast as possible. As more and more investors realised that we were heading towards a global recession, a selling spree got underway during the summer. A recession is obviously not good news for corporate earnings trends. In addition, the rise in long-term interest rates was a negative factor for the equity markets. Table 1 shows that the average stock exchange lost around 5%. The MSCI World (with a large exposure to US equities) was able to post a positive return in the past quarter due to the rise in the dollar (it was a negative return in dollars). If we look at stock markets' performance since the start of the year, we can see that the average stock market has lost around 15% - 20%. One of the hardest hit asset classes is European small cap stocks. It is a share class that has primarily cyclical stocks and those have been hit the hardest by fears of a recession.

Return on share trackers Q3 2022 (in EUR)	
MSCI World	-2,07 %
MSCI Emerging Markets	-4,77 %
MSCI Europe	-4,33 %
MSCI Europe small caps	-8,88%

Table 1: Return on Keyprivate share trackers Q3 2022
Source: Bloomberg

Return on share trackers 9M 2022 (in EUR)	
MSCI World	-11,90 %
MSCI Emerging Markets	-15,71 %
MSCI Europe	-17,42 %
MSCI Europe small caps	-29,44 %

Table 2: Return on Keyprivate share trackers 9M 2022
Source: Bloomberg

Bond markets

The most important fact of 2022 so far is undoubtedly the very sharp correction in the bond market. This correction is unprecedented: to see bond losses of more than 10%, we have to go back a long way in history. We do not need to look far for the main culprit for these price drops: the high inflation figures in the Western world mean that central bankers have thrown the zero interest-rate policy in the bin. Both short-term and long-term interest rates are adapting to this new reality. The lower interest rates that started in the early 80s have now clearly come to an end!

Table 3 shows what prices did in the third quarter. Thanks to the rise in the dollar, emerging market bonds (which we have had in our portfolio for a long time) have posted a positive return. The underlying index of this tracker is quoted in dollars and the final conversion into euro created a positive result. It will no doubt surprise many investors, but Turkish, Mexican and Brazilian bonds were among the best bond investments this year. These three countries make up about 20% of the tracker.

Since the start of the year the tracker that follows emerging market bonds has also lost the least. Looking at the different types of eurobonds, we see losses of -10.80% for inflation-linked bonds, -14.50% for high-quality corporate bonds, -15% for high-yield bonds and more than 16% loss for euro zone government bonds. In short, there was no escape, and we limited the losses as much as possible for investors in our defensive and neutral portfolios (which are nevertheless invested around 40% - 60% in bonds).

Returns on bond trackers Q3 2022 (in EUR)	
Government bonds of the Euro zone	-5,11 %
Bonds on emerging countries	2,64%

Table 3: Returns on Keyprivate bond trackers Q3 2022
Source: Bloomberg

Returns on bond trackers 9M 2022 (in EUR)	
Government bonds of the Euro zone	-16,77%
Bonds on emerging countries	-9,65 %

Table 4: Returns on Keyprivate bond trackers 9M 2022
Source: Bloomberg

Commodity markets

It will come as little surprise to investors that industrial metals were the weakest link in the global commodity markets in 2022. Copper, zinc and other cyclical commodities are for once not in demand right now, as the global economy heads for a recession. In the first few months of 2022, large quantities of industrial metals were still being purchased because of the war in Ukraine and the fact that sanctions for Russian commodity exports (Russia is, for example, a major nickel producer) were likely to make supply tighter. But since June/July this year, the geopolitical factor has moved into the background and the commodities market is mainly driven by the recession factor. We would like to remind readers that the Keyprivate investment committee sold its industrial metals tracker at the end of May to invest part of the return in gold. Since the end of May, the commodities market has also experienced a correction, but gold has lost much less than industrial metals. The strategy to follow in the commodities component of our portfolios is also damage limitation.

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Performances trackers on commodities Q3 (in EUR)	
Industrial metals	-7,55 %
Gold	-1,28 %

Table 5: Returns on Keyprivate commodity trackers Q3 2022
Source: Bloomberg

Performances trackers on commodities 9M (in EUR)	
Industrial metals	-17,02 %
Gold	6,54 %

Table 6: Returns on Keyprivate commodity trackers 9M 2022
Source: Bloomberg

Net returns on Keyprivate portfolios 9M 20222022

Table 7 shows the net returns achieved by our 10 Keyprivate profiles. Overall, we are satisfied with these results. We would like to remind readers that the first 9 months of 2022 were negative for virtually all asset classes. Nevertheless, we would like to draw attention to the more dynamic profiles (7–10), that fell less than the average world stock market.
Some observations on the net returns in the first 9 months of 2022:

• The average loss for our Keyprivate portfolios over the first nine months of 2022 is between 10.50% and 12%. Given a correction phase in almost all asset classes, we remain relatively "satisfied" with these losses. Once again, we are achieving our goal of limiting losses during the more difficult times on the stock markets. This is a basic objective for the members of the Keyprivate investment committee. When analysing net returns, always bear in mind that virtually everything has fallen in value this year. In tables 1 to 6 the reader can see the figures: the average bond market lost more than 10% and the average stock market lost over 15%!

• One rotation took place in the third quarter of 2022: at the end of August, we sold a part of the MSCI Europe tracker (-5%) to increase the MSCI World tracker holding (+5%) with the proceeds. The members of the Keyprivate investment committee chose this transaction because the US economy is far less hard hit in terms of energy than the European economy. The chances that the recession will hit harder in Europe than in the US played a part in this decision. We remind the reader that US equities account for more than 60% of the MSCI World tracker.

• In order to limit the losses in our portfolios as far as possible, the members of the Keyprivate Investment Committee chose to overweight trackers with underlying indices in dollars in the portfolios. This means that the fall in these indices in dollars is cushioned by their conversion into euro. At the end of the third quarter, profile 3 had a dollar exposure of 70%, profile 5 was 65% and profile 7 was 50%. We obtain these percentages by adding together the weightings of the emerging market bond tracker and the MSCI World tracker.

2022	
Profile	Net
1	-8,64 %
2	-9,36 %
3	-9,85 %
4	-10,36 %
5	-10,47 %
6	-10,12 %
7	-10,70 %
8	-11,26 %
9	-11,45 %
10	-12,21 %

Table 7: Net returns 9M 2022 (30/09/2022

Net returns 01/01/2016 – 30/09/2022									
profile		2016	2017	2018	2019	2020	2021	2022	Cumulative net returns since 2016
3 - Very defensive	100	2,37 %	2,24 %	- 6, 65 %	4,90 %	-1,90 %	10,29 %	-9,85 %	**0,03 %**
5 - Balanced	100	4,63 %	4,64 %	- 4,84 %	5,02 %	-1,92 %	12,37 %	-10,47 %	**7,96 %**
7 - Dynamic	100	7,52 %	7,13 %	- 7,78 %	7,11 %	-1,44 %	15,12 %	-10,70 %	**15,28 %**
10 - Very agressive	100	5,47 %	8,99 %	- 8,84 %	6,17 %	1,16 %	16,62 %	-12,21 %	**15,23 %**

These net returns were based on real portfolios started up on 4 January 2016 (the first trading day of 2016). These portfolios have therefore been through every re-balancing process. The net returns calculation includes annual management fees and all taxes.

Looking to the future

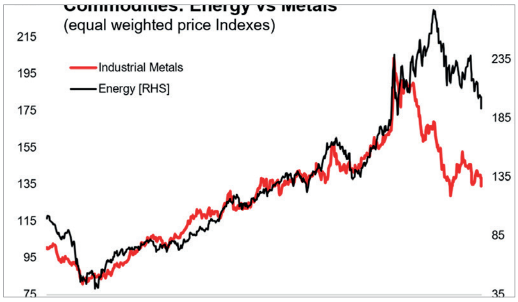

Figure 4: Trends in commodity marketsSource :Topdown Charts

We have already stated this several times in this quarterly report, but it is still a unique case that all major asset classes experienced a major correction in 2022. Since the start of 2022, equities and bonds have been under pressure, but commodities have continued to rise due to the geopolitical situation. But this rise in the commodities market also came to an end. Figure 4 shows the price trend for industrial metals such as copper and zinc, and energy (oil and gas): a clear downward trend has now started from the peak in the second quarter of 2022. Commodity investors are now primarily concerned about the fear of recession and less with the war in Ukraine. The Keyprivate investment committee sees this correction as the harbinger of lower inflation figures. And these lower inflation expectations could lead to a relaxation in the bond market, which could in turn support the equity market. Finally, the prospect of lower inflation figures could also convince central bankers to raise short-term interest rates less quickly. All of this should lead to a more positive sentiment on the financial markets and a year-end rally.

In previous periods of extreme nervousness and volatility in the financial markets, there has often been a flight to safe havens such as gold, US Treasuries or the Japanese yen. The remarkable fact of 2022 is that these safe havens have not worked this time. Figure 5 shows the trends of these three major safe havens (GLD = gold, TLT = US Treasuries and FXY = Japanese yen). In the 2008 crisis and during the coronavirus crisis, these safe havens really lived up to their name. But in 2022, they clearly were hardly involved. The main point of this figure is to illustrate that diversification into more defensive asset classes did not work in 2022. One way to absorb the risks of a diversified portfolio was to increase the cash position. In our Keyprivate portfolios, we have had 15% cash at all times since the start of the year (10% more than the minimum 5% required). This is also one of the reasons why we were able to limit the losses in the Keyprivate portfolios.

Figure 5: trends of some traditional safe havens
Source : All Star Charts

Conclusion: in the third quarter of 2022, fears of recession and inflation dominated. As a result, the correction in the international equity and bond markets continued. The commodity markets have also joined the rout in the past quarter. In an environment where all asset classes are under pressure, the Keyprivate investment committee has pursued an investment strategy that tries to keep losses as low as possible. A strategy that has been successful to date, because if you look at the net returns for 2022 you can see that the Keyprivate portfolios are losing less than the average equity and bond markets. At the end of the third quarter of 2022, our strategy is to overweight dollar-related investments in the portfolios and maintain the cash holdings at 15%. All this in order to limit the damage in the fourth quarter should the corrections continue into the last quarter of this year. One potentially positive scenario for the financial markets is that the correction in the commodity markets will mean lower inflation figures. This may give investors the courage they need to press the buy button rather than the sell button.

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