LC Investment Playbook Weekly Update

3 June, 2022

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

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

lighthouse-canton.com

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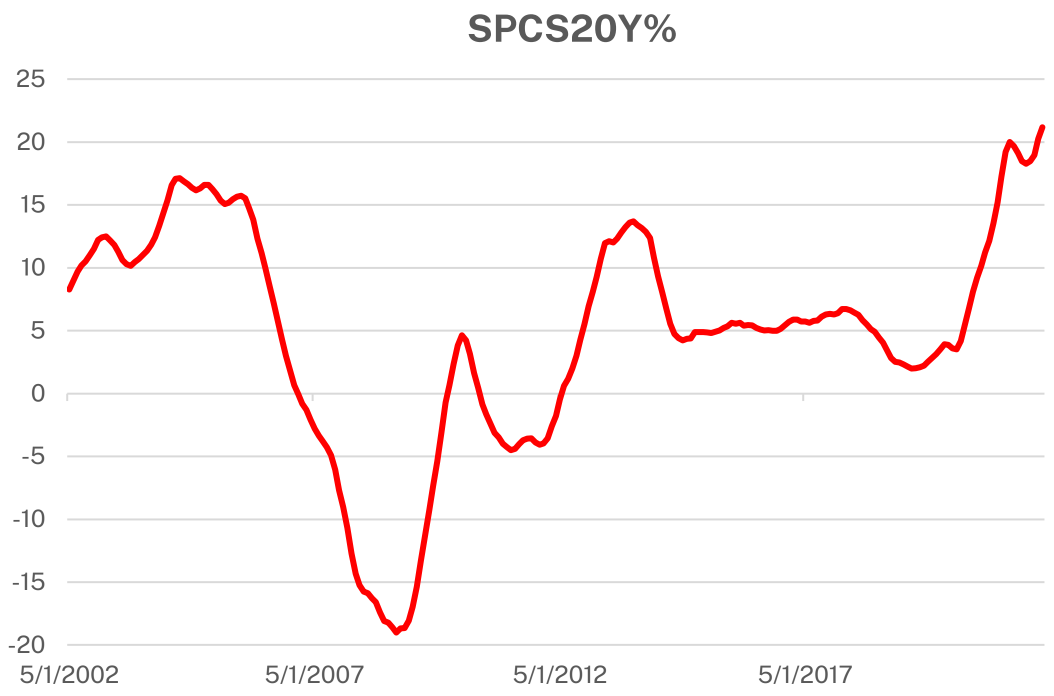
Macro Highlights

1

US Economy- Mixed Signals



S&P CoreLogic Case-Shiller 20-City Composite City Home Price NSA Index YOY%

Source: S&P/Case Shiller, Bloomberg and Lighthouse Canton 01st Jun 2022

- S&P CoreLogic Case-Shiller 20-City Index **Up 21.2% Y/Y; Est 20.0%.** 20-city SA index **rose 2.42% m/m in March after rising 2.39% the prior month**

- For both National and 20-City Composites, March's reading was the highest year-over-year price change in more than 35 years of data, with the 10-City growth rate at the 99th percentile of its own history

- Last week's poor home sales data stands in stark contrast to this week's home prices , perhaps suggesting that the economy still has some runway left for growth.

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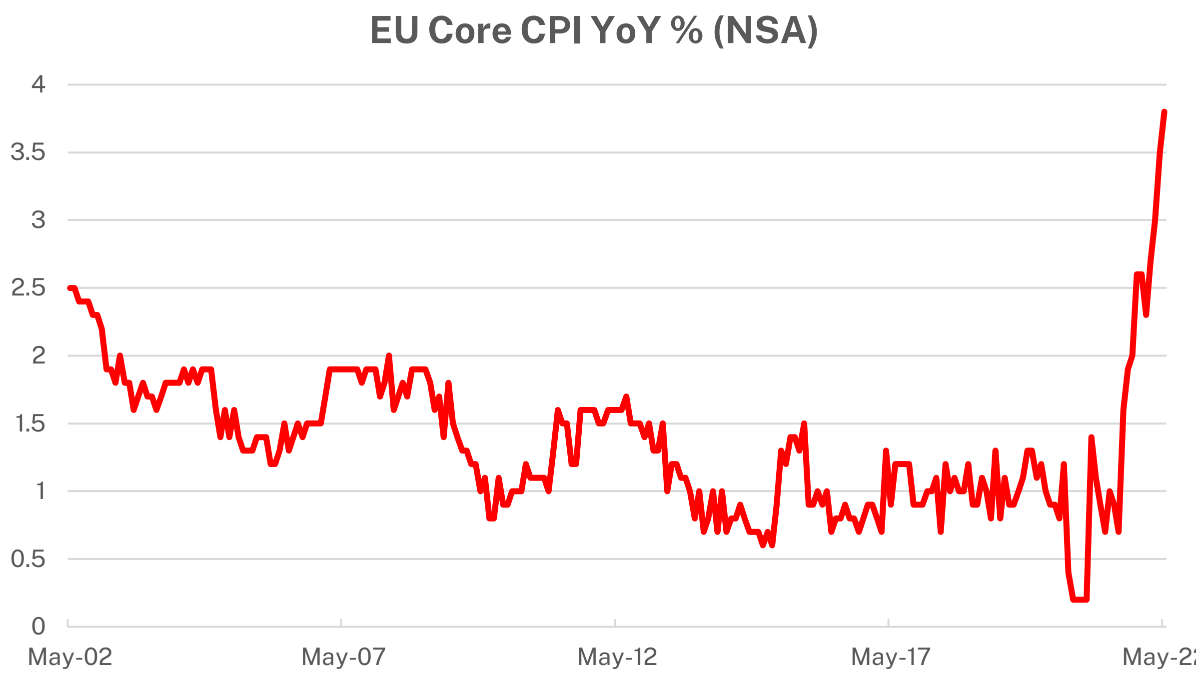
ECB getting ready?



- **Consumer prices jumped 8.1%** from a year earlier in May, exceeding the 7.8% median estimate in a Bloomberg survey.
- The acceleration was driven by food and energy after Russia's invasion of Ukraine sent commodity prices soaring. **A gauge that excludes volatile items like those rose 3.8%.**
- Some officials have floated the idea of hiking by a half-point in July for the first time in the ECB's history

Source: Eurostat, Bloomberg and Lighthouse Canton 01st Jun 2022

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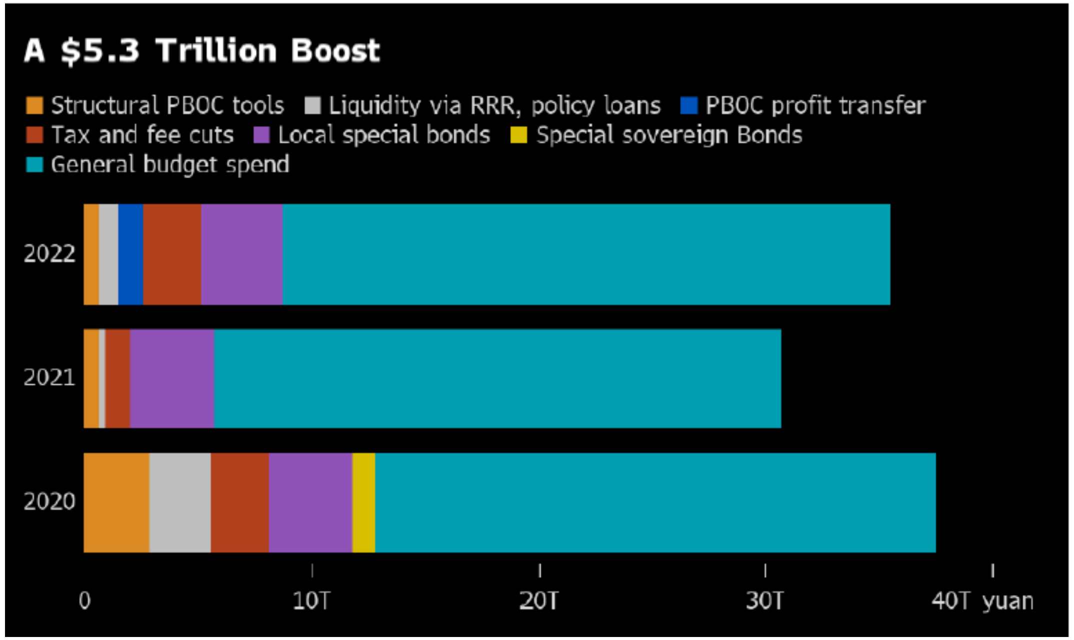
China's Easing and Fiscal Boost



Source: Bloomberg. 20th May 2022

- With the recent easing of lockdown measures in Shanghai and barring any policy reversals, sentiment is likely to improve and a gradual recovery is likely to ensue as production and mobility in the city picks up.

- China's State Council introduced a basket of 33 policies on 23 May, including fiscal credit and industry policies to support the corporate and household sectors and boost consumptions and investments with emphasis on stabilizing the labor market Based on Bloomberg's calculation, these stimulus equate to roughly a third of China's 17 trillion economy. This should serve to boost the economic recovery further as well.

Fixed Income Highlights

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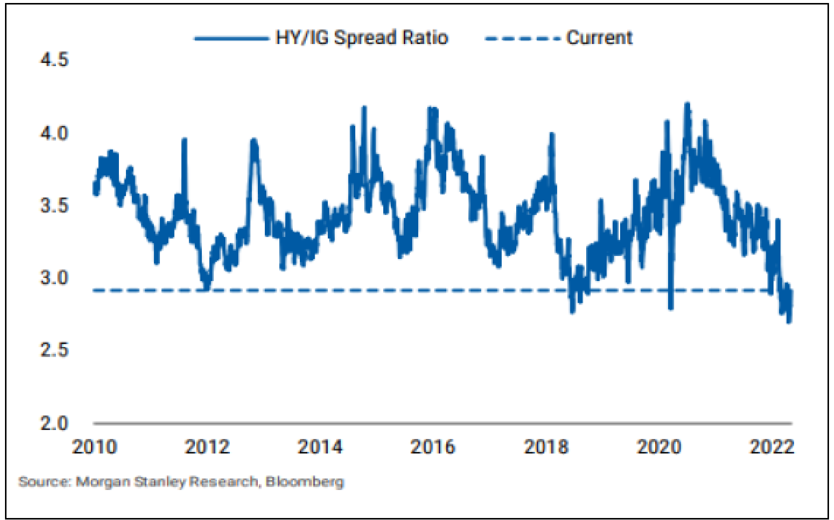
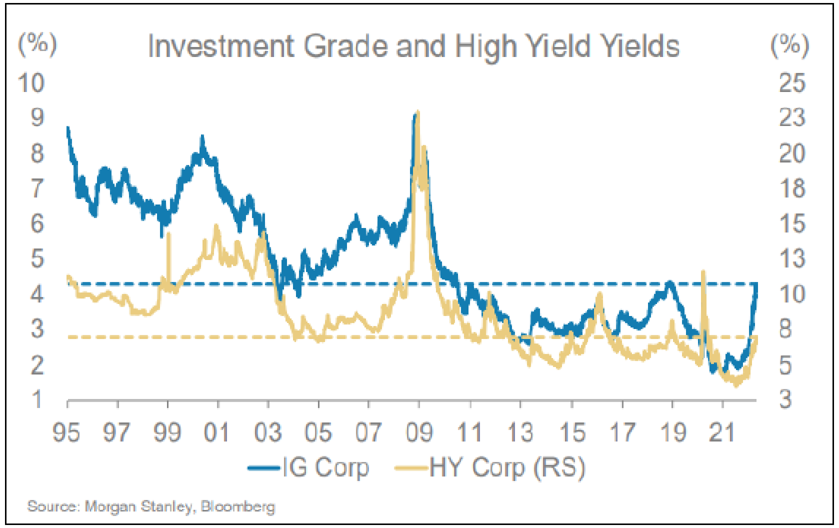
IG Yield at 10-Year High





In case you missed it

- As the market pricing in the interest rate hikes, there are increasing numbers of Investment Grade (IG) bonds trading at significant discounts to par.
- High yield bonds also had price corrections. But the HY/IG spread is still quite small. In terms of risk adjusted returns, IG bonds are now preferred to HY, considering where we are in the economic cycle.
- Short duration IG bonds, with bond yields over 4%, look attractive for buy-and-hold investors.

Source: Morgan Stanley, May 2022

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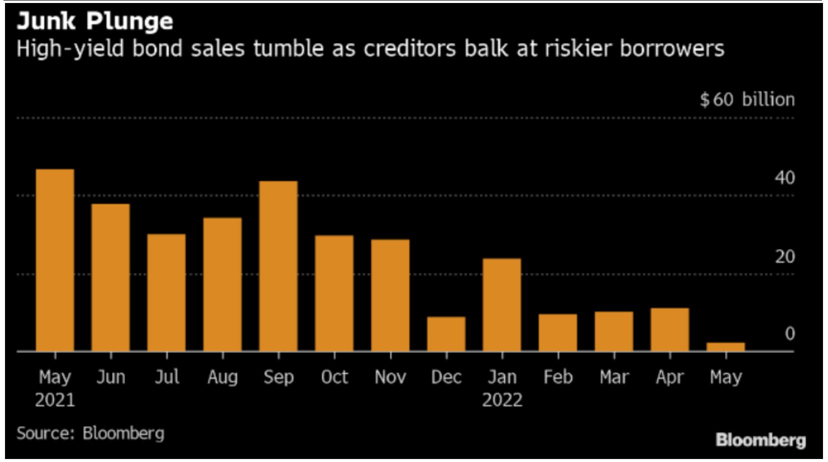
Zombie Firms To Face Hard Times



- Rising rates are reshaping the corporate borrowing landscape and according to Bloomberg Intelligence (Credit Research Team), "zombie" firms are likely to face a slow death in the US as easy-credit era ends.
- Firms that could once count on virtually unfettered access to the bond and loan markets to stay afloat are being turned away as investors girding for a recession close the spigot to all but the most creditworthy issuers. The fortunate few that can still find willing lenders face significantly higher borrowing costs as the Federal Reserve raises interest rates to tame inflation.

(Source: Bloomberg Intelligence)

Source: Bloomberg, June 1st 2022

Fixed Income – Executive Summary

- Clear disconnect between **data (20 city home price data on 01/06) and sentiment (consumer confidence data on 31/05)** in the **US** suggest that the chatter of Fed pause is likely to be premature . At least the household and corporate balance sheets point to that direction.

- Disconnect in data persists in the **UK** as well. House prices in the **UK** grew sharply on a MoM basis while mortgage applications fell pointing to the interest rate burden.

- Hawkish officials in the **ECB** are backing the idea of a 50bps hike. Inflation in parts of the 19-member bloc are much higher than the 8.1% printed with Germany reporting an 8.5% growth YoY in headline CPI.

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Equity Highlights

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Have S&P 500 stopped being expensive?

Source: Bloomberg, 27th May 2022

- After the large stock price correction and treasure yield uptick, the spread of S&P 500 earnings yield over nominal -10-year Treasury payout has dropped to around 2%. This may already seem inexpensive for some investors.

- However, do note that the combined $248 earning per share of S&P 500 next year is only estimated by analysts. On the other hand, in their annual reports, corporates expected a combined earning of only $227 a share. In addition, historically speaking, in a typical economic contraction, profits shrink by 13%. Taking both into consideration, the forward P/E would be 21x, which still suggests that the stock price may still have some downsides.

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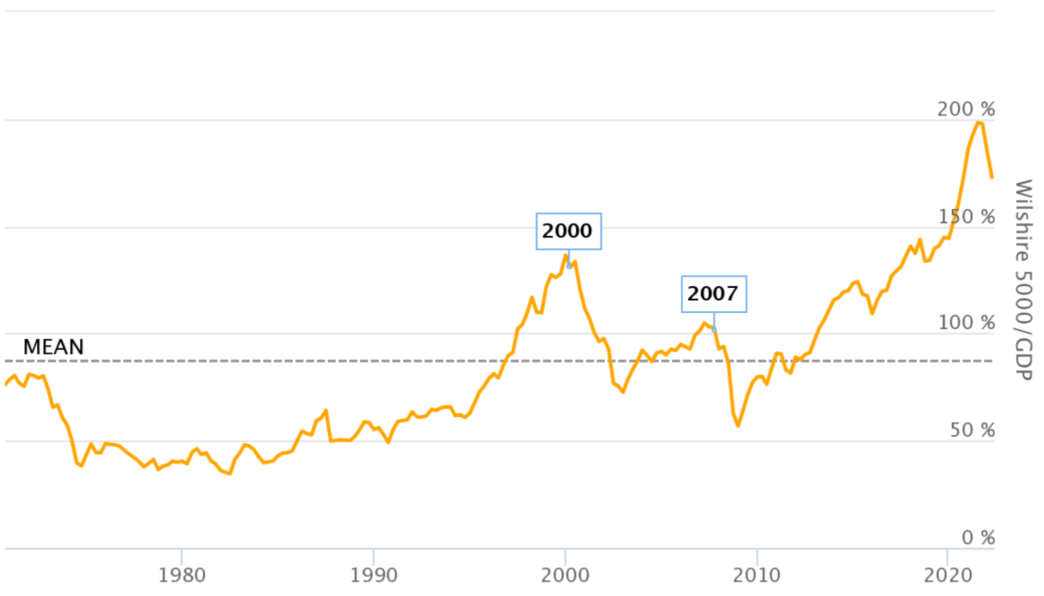
US market cap to GDP



Source: longtermtrends.net

- The market capitalization to GDP ratio or commonly known as the Warren Buffett indicator is a time series analysis of the relative costliness of the stock market.

- Historical deviations from the mean level of approximately 85% has tended to be followed by a mean reversion. The ratio was an effective indicator prior to the 2000's tech bubble burst and the 2008 global financial crisis.

- The ratio reached an all time high of approximately 201% in November of 2021 and has since then corrected to 164%. Going by the historical levels, the stock markets still seem to be expensive, even after the recent correction.

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Equities – Executive Summary

- **The US announced a quarter of negative GDP growth (-1.5% for Q1 2022),** making the chances of a recession in the US more likely. While inflation fears in the last few months had the market expecting a consistent stream of rate hikes at least into 2023, the slowing economic growth rates have made the situation less clear going forward as referenced in the recent **FOMC minutes where the Fed mentioned that any further policy action in 2023 will be data driven.** Additionally, the **Fed started shrinking its balance sheet from this Wednesday,** which is expected to further have an impact on asset prices in the coming quarters, as multiple members of the FOMC took note that this can have unexpected effects on the financial markets**.**

- On the other hand, **lockdowns were eased in China, which resulted in Chinese stocks rallying and provide some much needed stability to Chinese assets.** The likes of Alibaba and JD.com saw sharp spikes in the range of 6-8% before cooling off later, on Wednesday. **China also ordered a $120 billion credit line for infrastructure growth,** in a bid to support the contracting economic activity seen in April and similar assumptions for May as per various high frequency indicators.

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Currencies & Commodities

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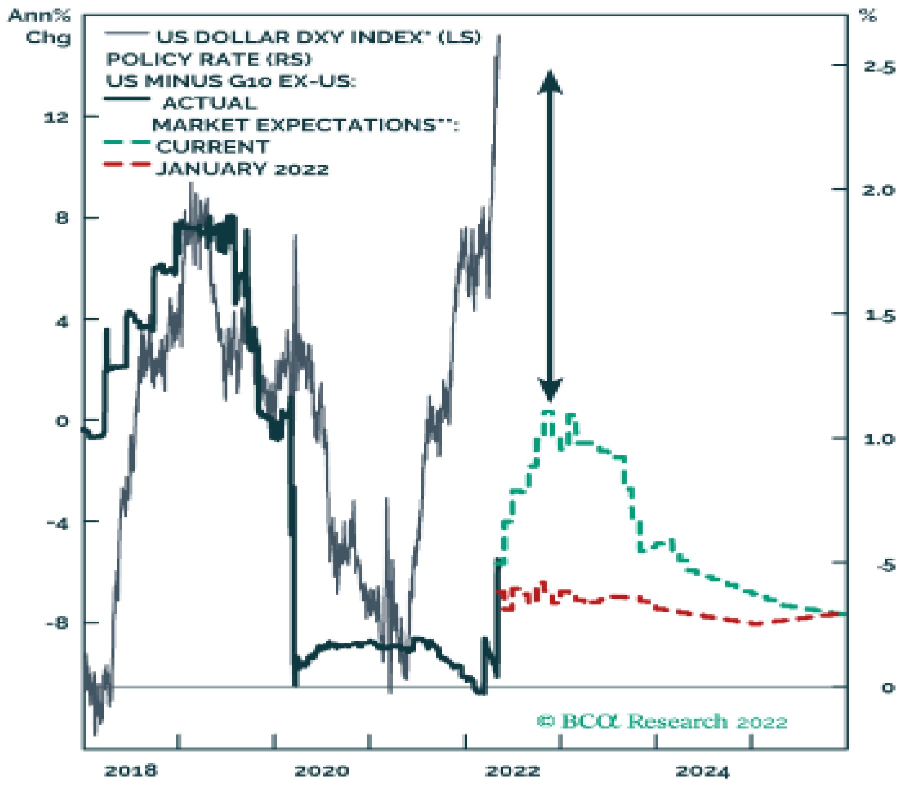
Exaggerated rates expectations in DXY

The Fed And The Dollar



* SOURCE: ICE FUTURES US.
** AS DISCOUNTED IN THE OVERNIGHT INDEX SWAPS CURVE.

Source: BCA. 20th May 2022

- DXY has been one of the best performing currency YTD on back of expectations for QT and rush to safe havens on back of recessionary fears.
- BCA opines that rate expectations are overly exaggerated in DXY pricing and that the USD is like near a capitulation point given deteriorating trade balances and likelihood of inflation pressures to recede this year.

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