Markets
& Convictions

December 2022

RJ Management

Macro

- Since the beginning of October, markets have experienced a significant AND generalized rebound
- Equities as of the 13th of December (+10.53% S&P500 / +10.62% Nasdaq / +14.3% Stoxx 600 / +17% MSCI Emerging)
- As well as risky bonds such as High Yield (+5.3%) or emerging zone (+13%)
- Not forgetting sovereign bonds (+4% for the USD Treasury 10 years / +7% for the German BUND 10y)
- Markets fell with a very strong correlation during the first half of 2022 and we are witnessing today this rebound under the same correlation conditions
- Nevertheless, markets are still negative since the beginning of the year (-16.7% S&P500 / -29.1% Nasdaq / -10.6% Stoxx Europe 600 / -14.6% SMI)
- This rebound is largely due to the first visible signs of a turnaround in inflationary pressures
- Decline in the latest US figure (CPI @ 7.7% vs. 9.1% in June) but also in Europe (HICP @ 10% vs. 10.6% in October)
- And there is a clear improvement in various strategic nodes that have impacted our economies following the exit of the COVID (lower prices on: used cars / transportation / energy and agricultural products)
- The monetary tightening of the FED (in the lead) which increased its key rate from 0.25% last March to 4.5% today, is having an effect
- Slowing down our economies by increasing the cost of credit
- The market is therefore anticipating the long-awaited "PIVOT": the FED will slow down its rate hike, or even stop it
- The futures on rates indicate that the market is now expecting a maximum point on the FED rate at 5% for June 2023 and then a drop to 3% at 18 months...
- The situation in Ukraine does not seem to worry the markets anymore when we know that the price of oil is trading at USD 76 (lower than the level of February 24, 2022 = invasion of Ukraine by Russia where Brent was trading around USD 90)

Convictions

- Yes, inflation will fall, but it should not reach the famous 2% target
- Some elements are much more structural than used cars in the current inflationary configuration
- The labour market and wage inflation should continue to feed a higher inflation regime than during the last 20 years (probably an average around 5% over a relatively long period)
- As well as the geopolitical situation which suddenly throws us in front of the past strategic mistakes of our western world
- The permanent "green washing" has made us forget that an energy transition could not be orchestrated solely by ESG-labelled funds
- But by a common vision between citizens / political powers / institutional investors AND scientific realities
- To believe today that by taxing the famous "super profits" we will find answers is simply demagogy
- We need massive investments in energy and research to allow us to organize a transition
- We need massive investments in the reindustrialization of our old Europe to guarantee the production of our goods, medicines, etc...

- And "at the same time" the cost of credit is increasing!
- We are convinced that for the last 18 months we have been witnessing an important sectoral rotation which is generating profound movements
- Back to 2020 - Example: Google issues debt (bonds) for USD 10 BLN offering an average coupon of 1.2% and an average maturity of 2040!
- So much for "free" money (this is 2020!). With this capital Google buys back its own shares on the stock market (the famous buyback), a more interesting strategy than dividends because it makes the stock go up and is not taxed for many investors (capital gains vs. income)
- With the same stock rising sharply, Google hires the best engineers on the planet, promising them generous salaries (over USD 300k per year for first-time hires)...but a large part is paid in shares.... Everybody is happy, these shares are only going up!
- Suddenly the crisis of 2022 arrives with an inflationary regime
- The Google bond offering a coupon of 2.5% maturity 2060 issued at 100% in 2020, is now worth 65% !!!
- The share price has lost 37%, meaning that the share buyback program has gone up in smoke and many shareholders would have preferred to receive a dividend
- Are the employees still as happy with their stock option plans?
- As you can see, this world is changing
- As well as many assets using the cheap leverage of the last few years (Real Estate / Private Equity... beware of the crisis coming)
- In this context of such rapid rate hikes, it is almost impossible to avoid the credit crisis and the strong economic slowdown (see recession)
- And the FED will not cut its key rate so quickly: if it did so, it would "break" in a few moments all its efforts and credibility of the last months to fight inflation AND the price of energy would explode upwards
- We are convinced that we are also witnessing a real change in the balance of world economical trades
- The last visit of the Chinese president to Saudi Arabia is a strong and perhaps historic sign => exchange of oil for YUAN (and no longer USD / China & Saoudi Arabia... to read)
- In this context of economic slowdown and higher inflation, we will have to navigate with a more modest sail
- We still favour the energy theme (Westbeck Energy Opportunity / our direct holdings such as TotalEnergies - BP - Shell - Eni) / European financials (Axiom European Banks)
- Short-duration bonds in both the West and in emerging countries
- We have recently issued a synthetic bond allowing to guarantee a large part of the capital (97%) at 18 months while taking advantage of the positive performance of Chinese equities (after the election issues, the exit of the 0 COVID policy seems inevitable).

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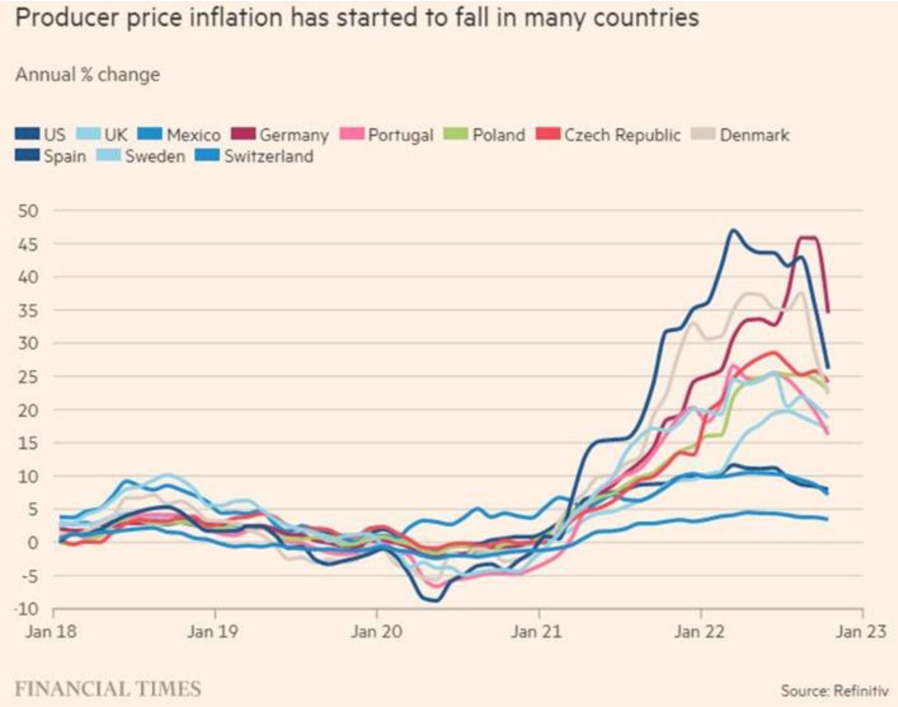
Charts of the Month : Inflation on production side in different countries + S&P500 unable to break its downward trend



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