

# Investment Playbook Monthly Update

September 2022

**LIGHTHOUSE  
CANTON**

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  
WEALTH PLANNING SERVICES



**2021**  
ASIAN PRIVATE BANKER  
AWARDS FOR DISTINCTION

BEST INDEPENDENT WEALTH MANAGER  
INVESTMENT ADVISORY

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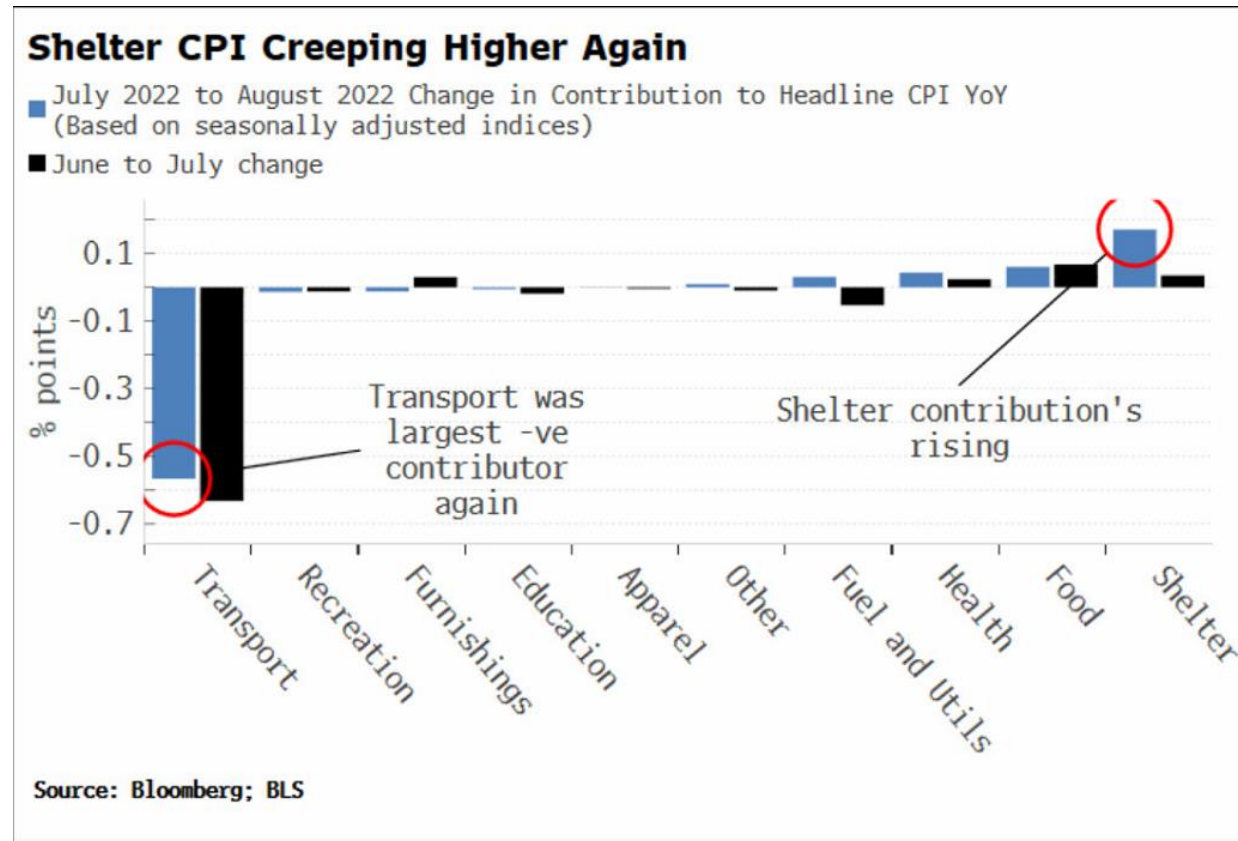
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# Macro & Fixed Income

1

# US CPI- Shelter is the pain point

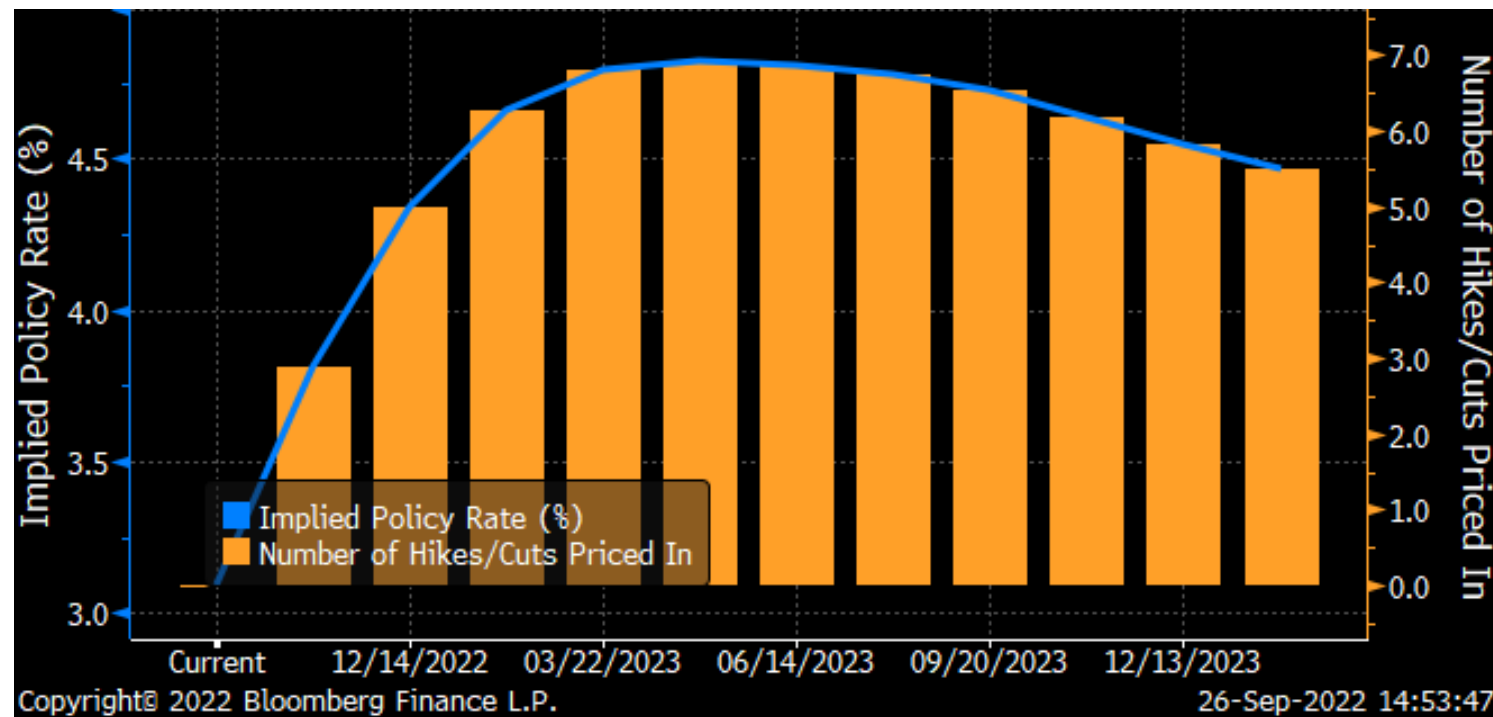
Increased contribution is likely to keep CPI prints higher for long (sticky component)



Source: Bloomberg, September 2022

# Fed Funds Rates Expected At 4.8% By Q1 2023

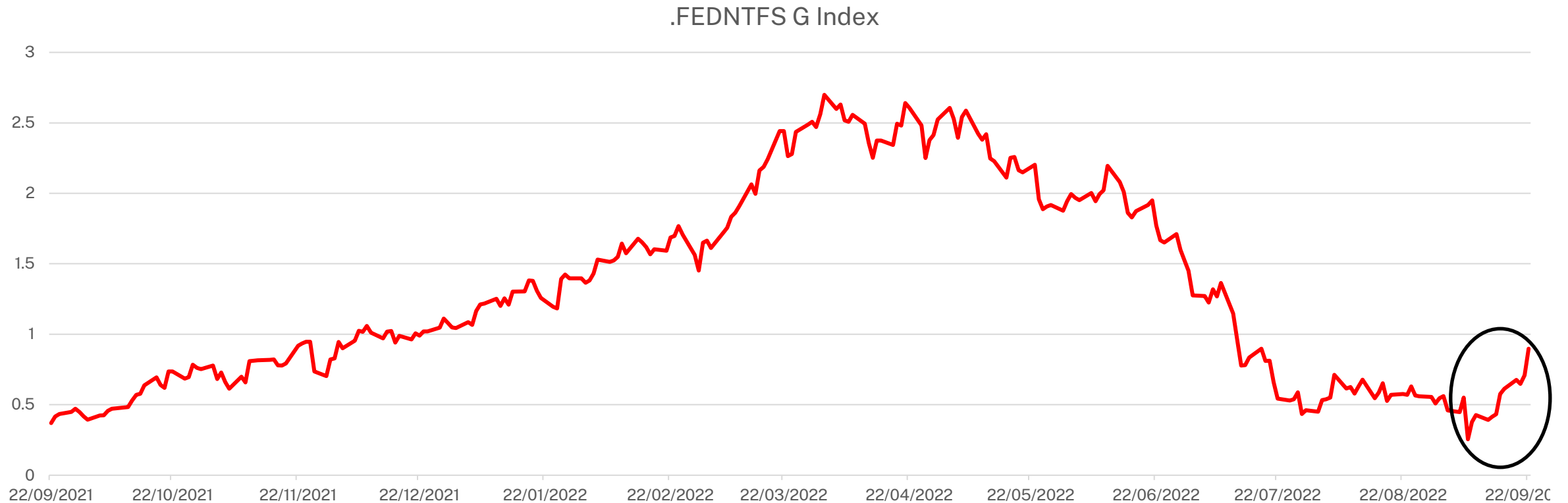
Higher (for longer) rates will act as a strong headwind for risky assets



Source: Bloomberg, September 2022

# Fed near term forward spread

**Relative steepening of the Fed's preferred gauge of curve spreads helps it to be more hawkish**

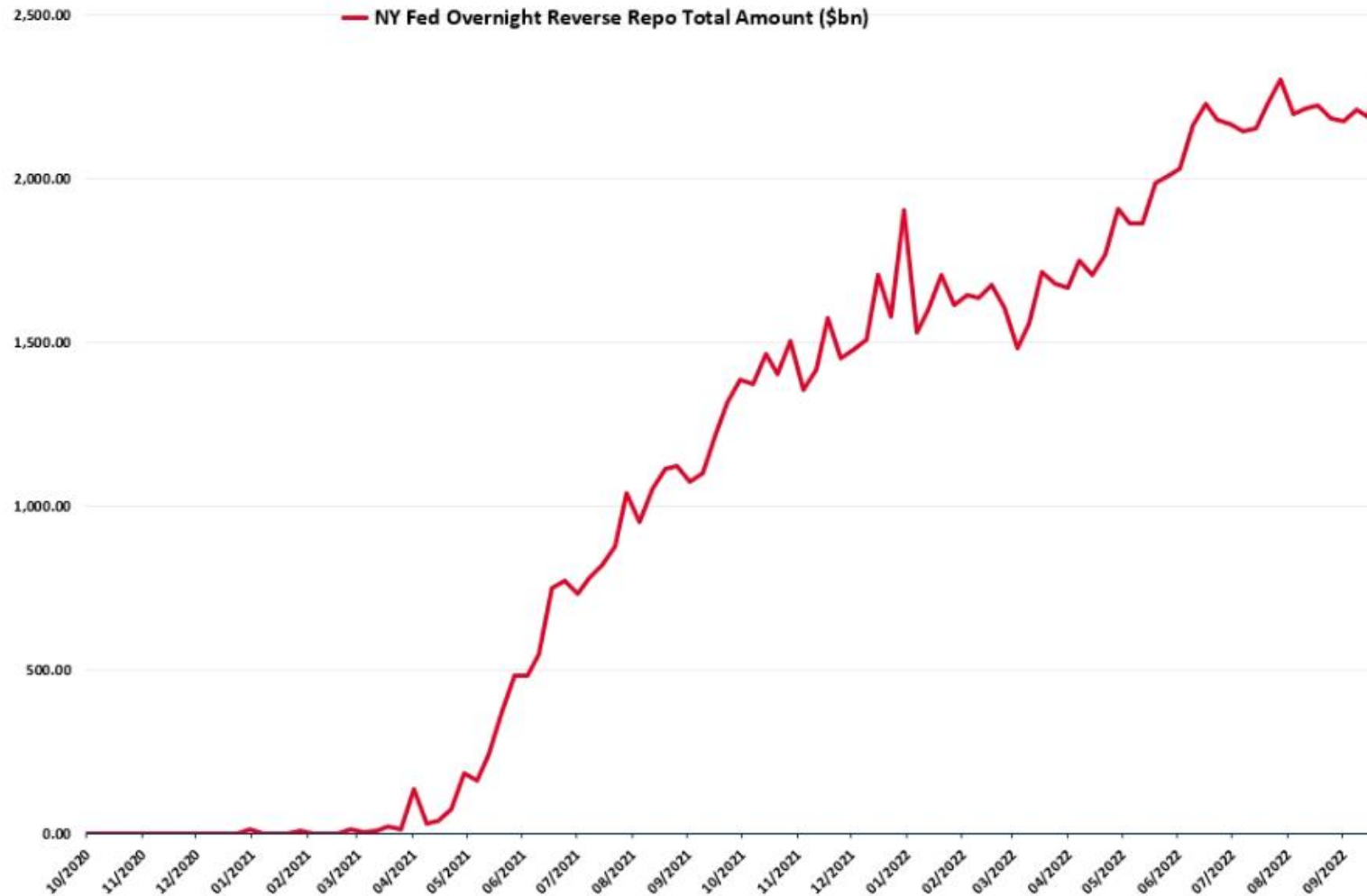


Source: Bloomberg, September 2022

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# Looking for Safety

Investors stash a record \$2.3tn in the Fed's overnight reverse repurchase facility.



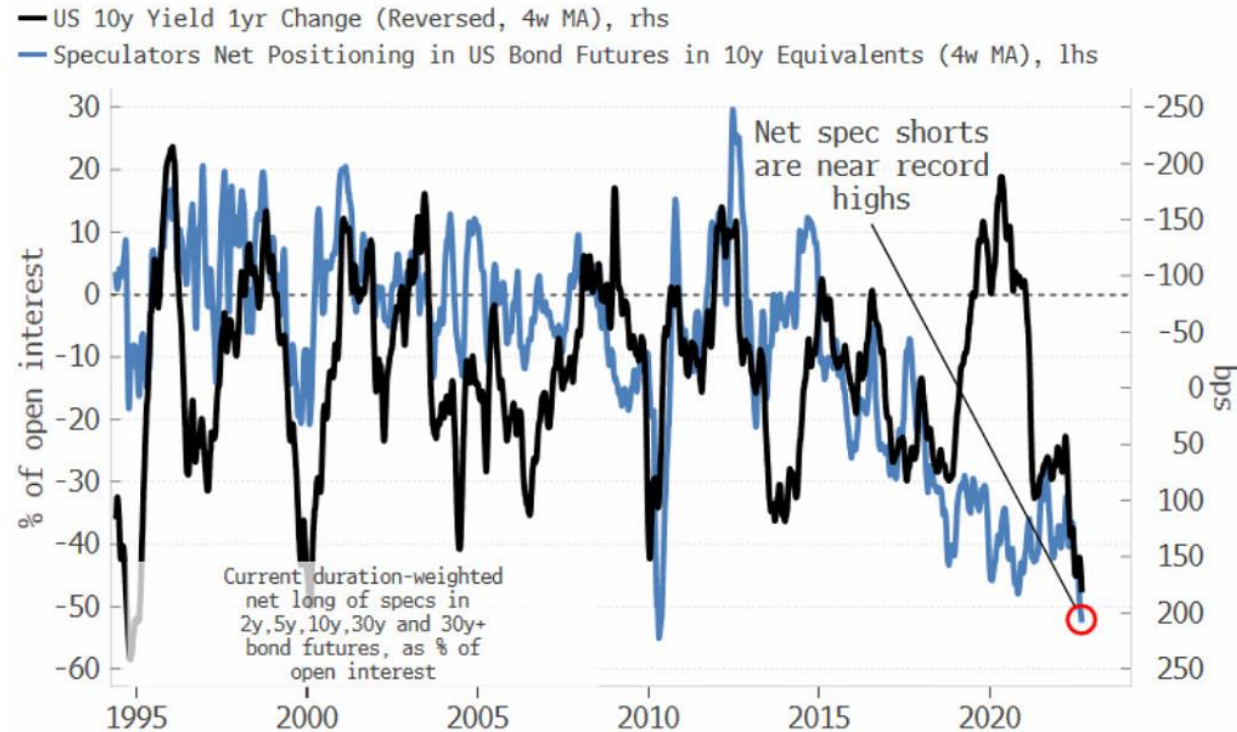
Source: Bloomberg, Lighthouse Canton, September 2022



# US Bond Futures- Market Positioning

Net shorts are near record high and likely to continue if CPI numbers continue to surprise.

## Net Short Positioning in Bond Futures at Extremes



Source: Bloomberg

Source: Bloomberg, September 2022



# Housing Market Sending Recessionary Signals

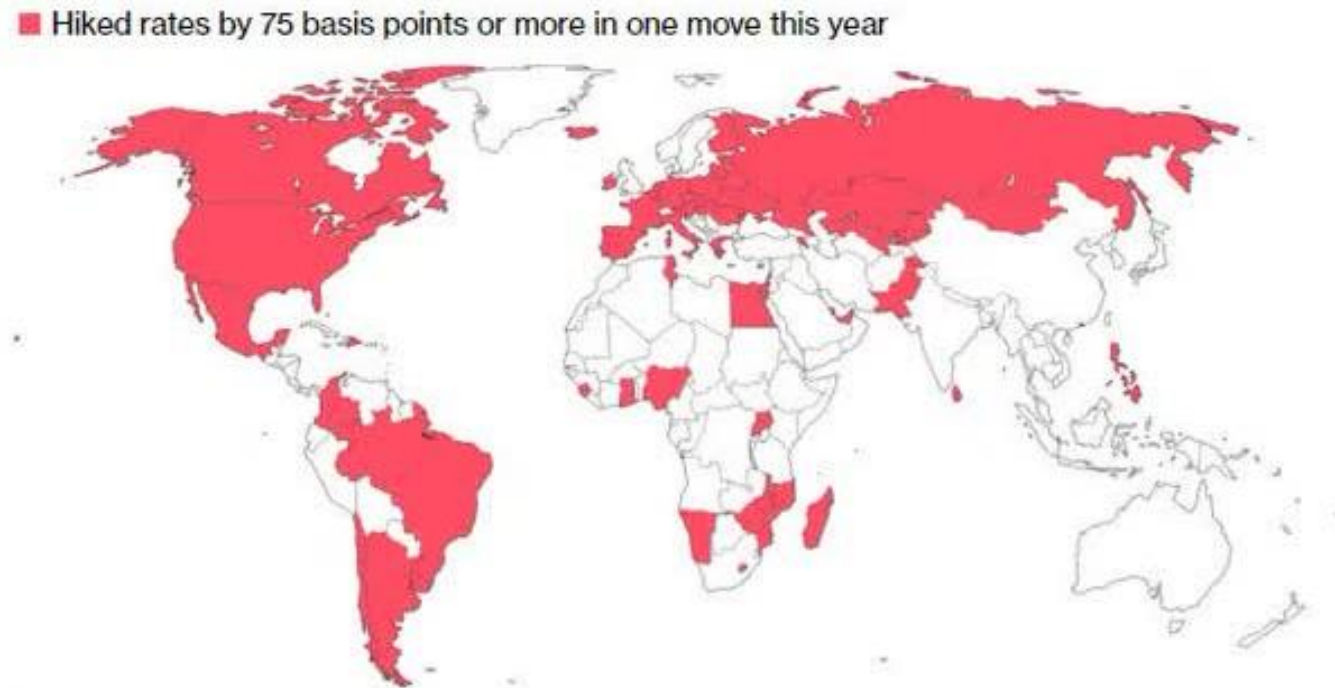
Unemployment is likely to surge in the near term which historically an arbiter of recession



Source: ASR, September 2022

# Jumbo Hike Club

**ECB joins more than 40 central banks that have increased rates by at least 75 bps in one go**

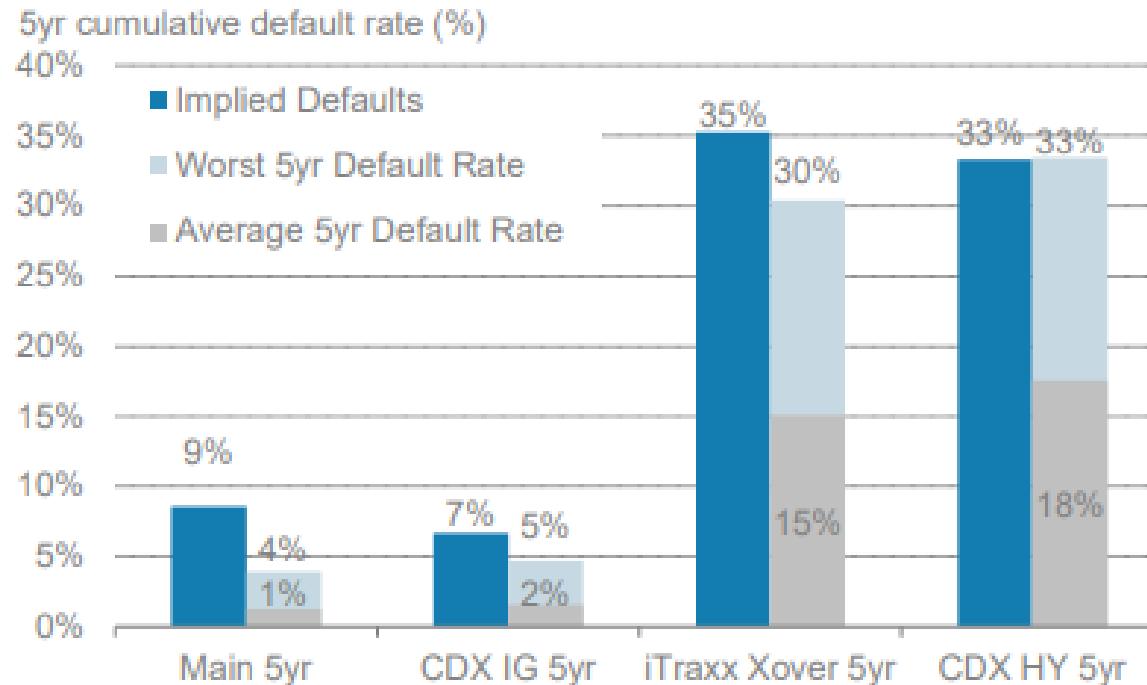


**Source: Bloomberg, Sep 2022**

# European Credit – GFC type scenario priced in

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

## Credit vs. Historical Default Rates



Note: Implied defaults calculated using 35% recovery rate. Historic defaults calculated using Moody's default data since 1970 and current index ratings composition. Source: Morgan Stanley Research, Bloomberg, Moody's

Source: Germany, Federal Network Agencies, September 2022

# Fixed Income – Overview

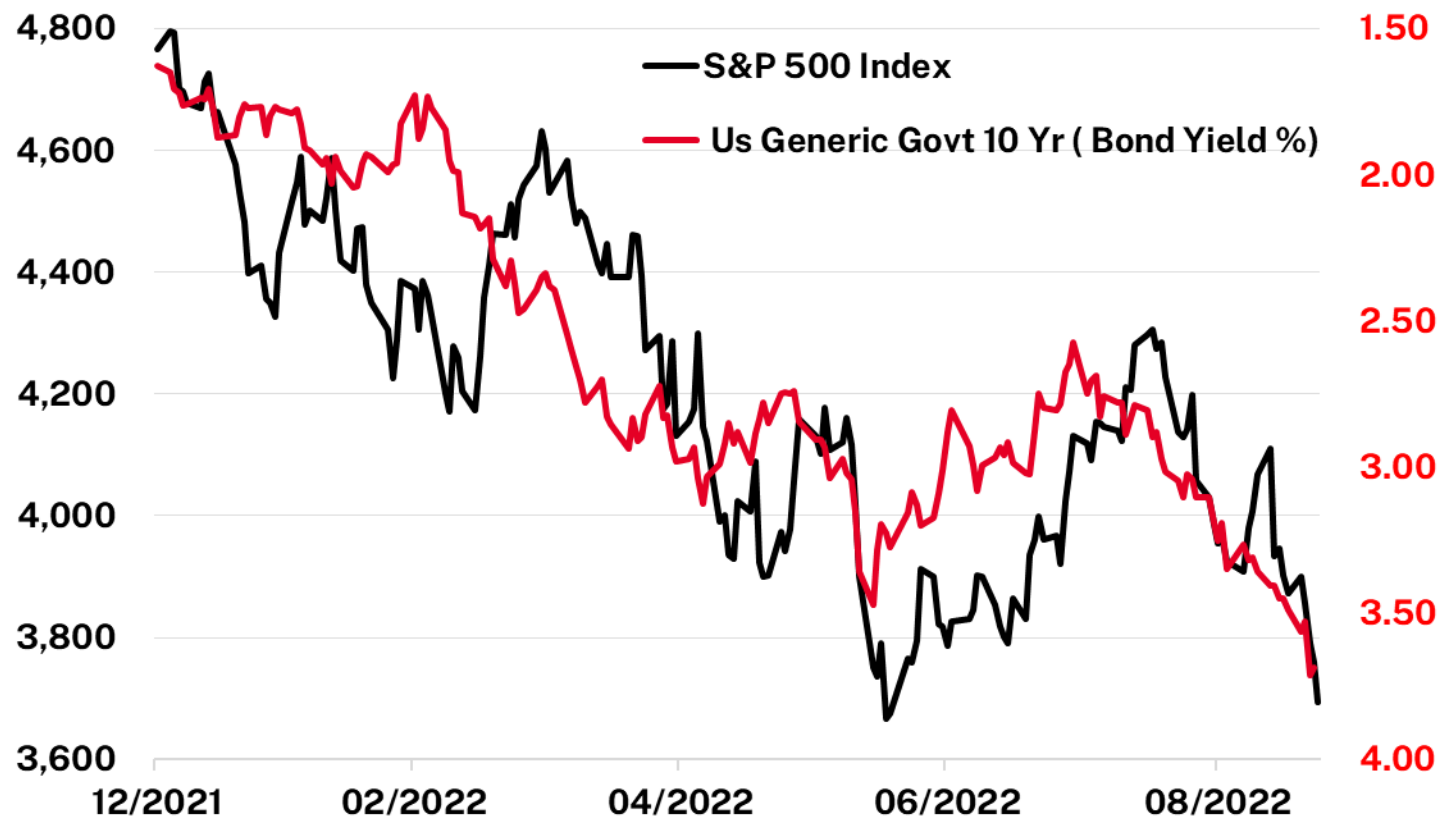
	Sub-Asset	Region	IC Outlook (2Q23)	IC Comments	Recommended Positioning
Long Term Rates	10Y Rate	US	↑	<ul style="list-style-type: none"><li>Despite potential downward pressure on long term rates as a result of recessionary fears, we broadly agree that there is further room for longer term rates to move higher as long as the Fed maintains its resolve in combating inflation.</li><li>Fed balance sheet roll off likely to add further upward pressure on long end of yield curve.</li></ul>	<ul style="list-style-type: none"><li>We think now is a good time to start adding fixed income exposures as yields are admittedly starting to look attractive. That said, this should be done progressively as rates are expected to trend higher in the near term.</li><li>We are <b>selectively bullish on bonds in US IG credit</b> with duration &lt; 3 over a 12 months horizon.</li><li><b>Avoid EU names, PERPs, Cocos, High Yield and long Duration (&gt;3) bonds</b> for the moment.</li><li><b>Add Distressed managers</b> to benefit from dislocations and mispricing.</li></ul>
		EU	↑	<ul style="list-style-type: none"><li>Like the US, Europe’s long term rates are likely to trend higher given the ECB’s acceleration in the pace of hikes and firm resolve to tame inflation.</li></ul>	
Credit	IG Spread (bps)	US	↔	<ul style="list-style-type: none"><li>Global Corporate bonds are likely to face headwinds up until 1H23.</li><li>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.</li></ul>	
		EU	↑		
	HY Spread (bps)	US	↑		
		EU	↑		

# Equities

# 2

# Equities Moves Explained By Rates In 2022

**S&P 500 YTD performance has been primarily driven by US rates, not fundamentals.**

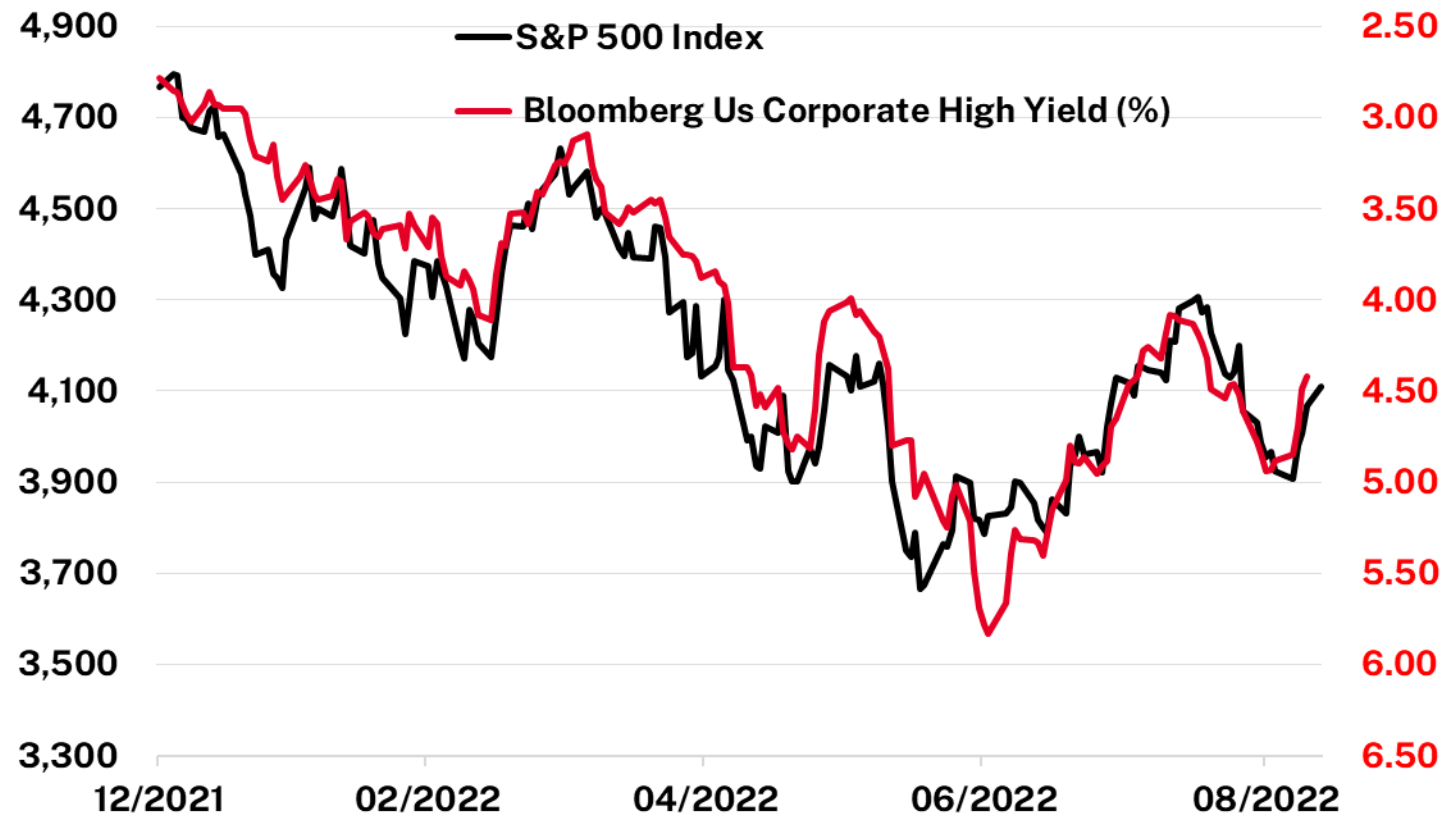


Source: Bloomberg, September 2022

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# Equities And High Yield At Record Correlation

**3M Correlation between S&P 500 and US High yields is -0.75 so far in 2022 (Weekly obs)**



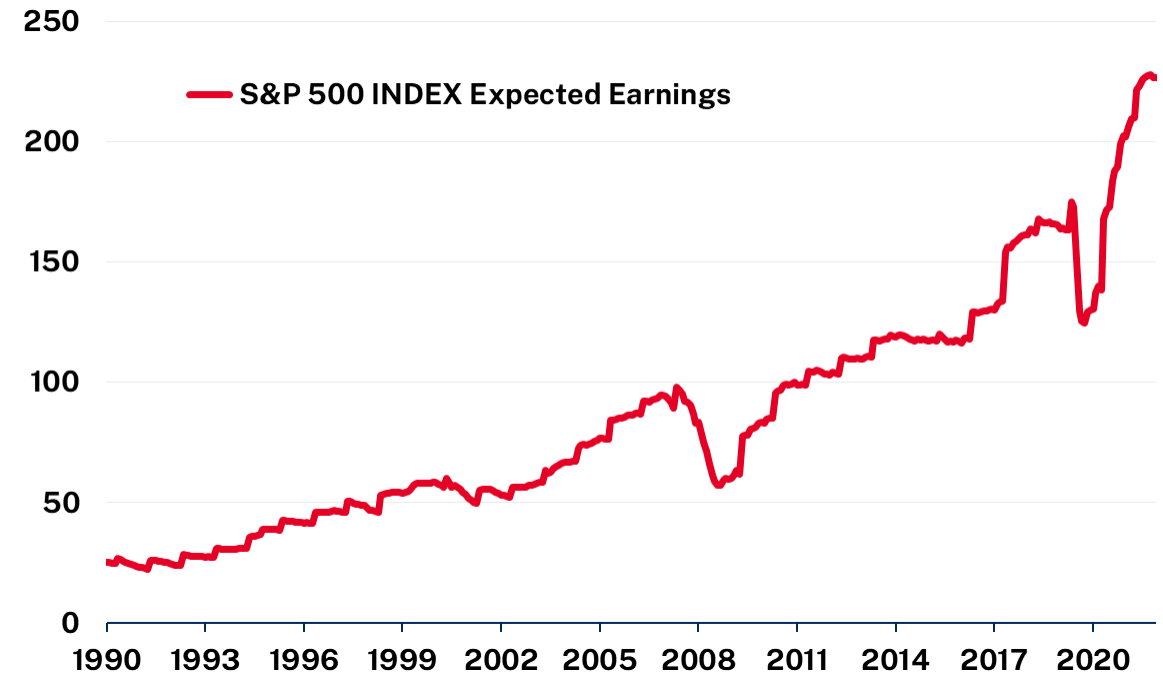
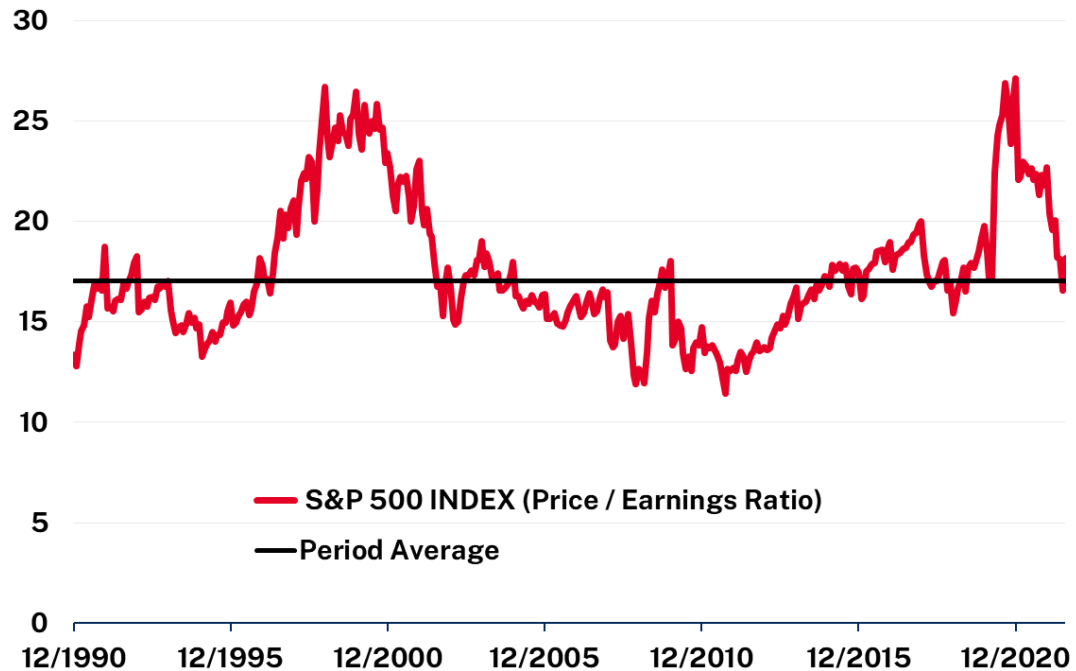
Source: Bloomberg, September 2022

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# US Equities: Earnings Will Be Decisive

**S&P 500's P/E ratio is back to its long-term average (17.5x) but earnings may disappoint**

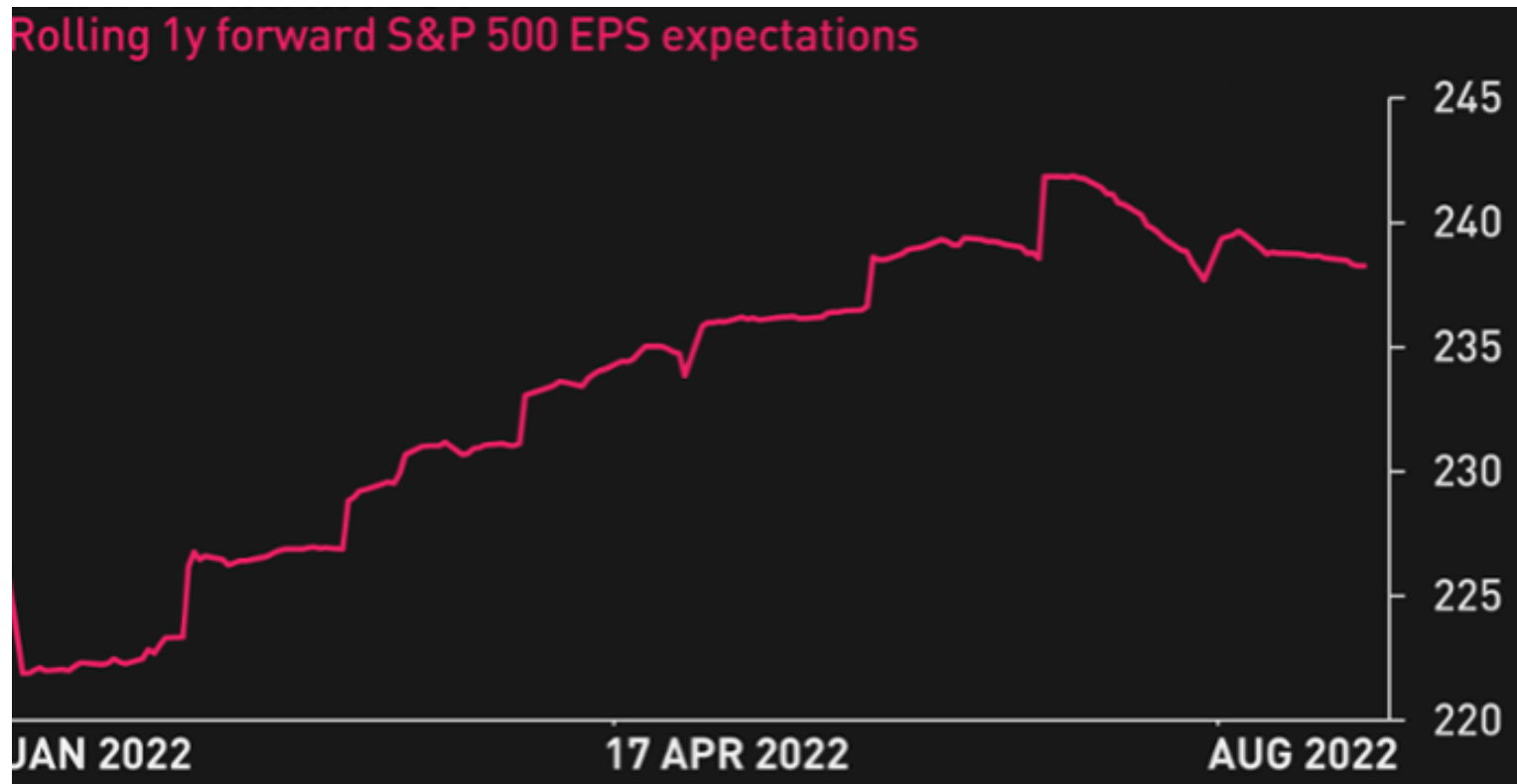


Source: Lighthouse Canton, Sep 2022

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# Peak Earnings?

Rolling 1y forward EPS expectations have started to drop for US Equities (S&P 500 index)



Source: Bloomberg, September 2022

# S&P 500: Strong Support Being Tested

**3640 pts was already tested in June. Breaking down that level may lead to further correction**

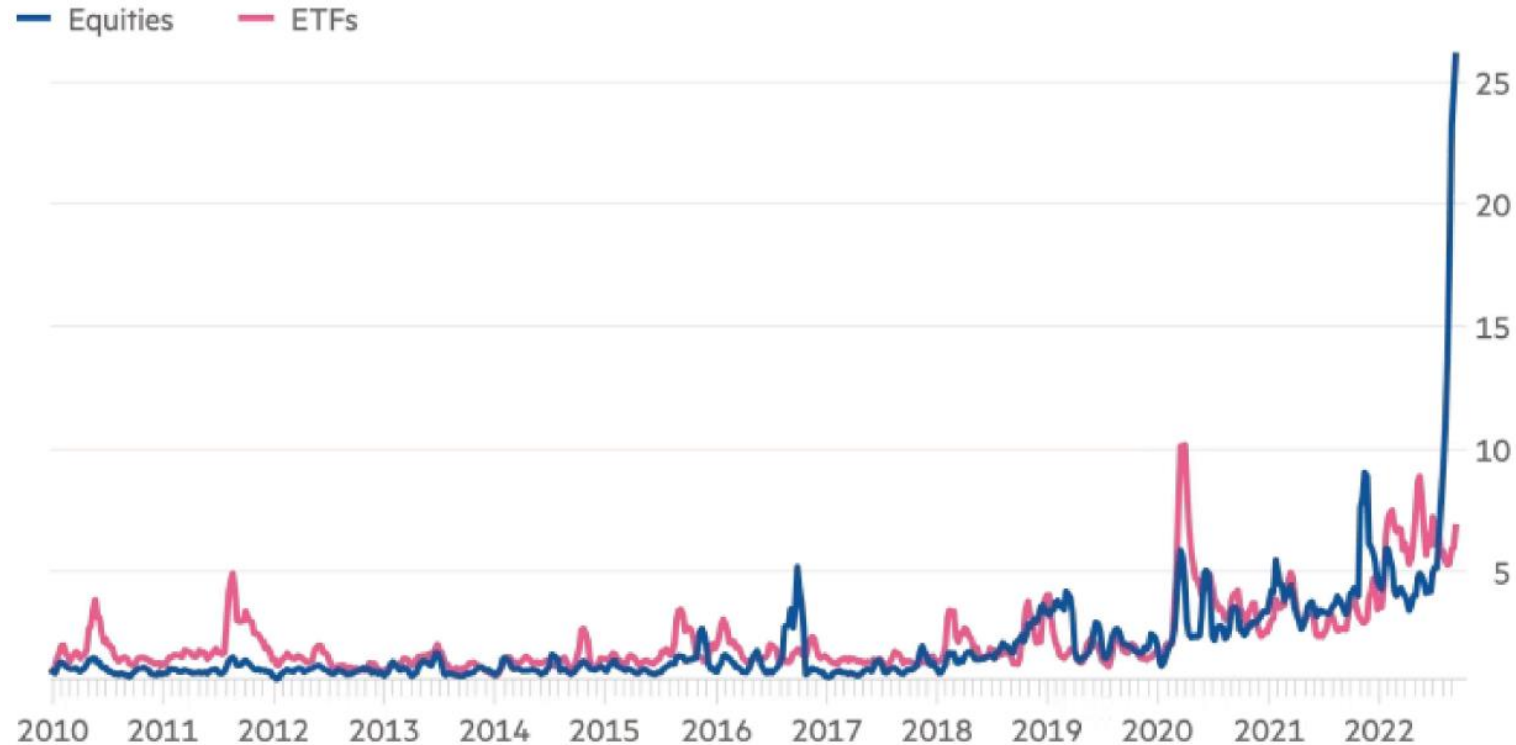


Source: Bloomberg, September 2022

# Looking for Safety

**The amount of put options purchased to protect the downside has reached a 12-year high.**

Premiums spent to initiate new put option contracts, trailing 4-weeks (\$bn)



Data only includes large open-to-buy put option transactions  
Sources: Options Clearing Corp, Sundial Capital Research

Source: FT, September 2022

# Equities – Overview (1/2)

Region	IC Outlook (2Q23)	IC Comments	Recommended Positioning
US (S&P 500)	↓	<ul style="list-style-type: none"> <li>Analysts have been downgrading their S&amp;P 500 earnings expectations for the past three months.</li> <li>We hold a bearish view on US equities over the next 6-12 months given that interest rates are expected to continue rising and economic growth, while not collapsing, is softening.</li> <li>Moreover, US Equities are likely to continue to be negatively correlated with long-term rates and are exposed to any hawkish comments from the FED.</li> </ul>	<ul style="list-style-type: none"> <li>Earnings expectations continue to look too optimistic across <b>US and EU and have room to correct further</b> over the next 12 months. This month, FedEx suspended its guidance for the year while missing estimates for the quarter. The stock tanked over 20% as the market took this news into its grasp.</li> <li>We <b>do not think it is time to increase beta on portfolios</b> yet and recommend a cautious stance in terms of positioning.</li> </ul>
EU (STOXX 600)	↓	<ul style="list-style-type: none"> <li>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.</li> <li>Despite the bleak economic situation, the consensus STOXX 600 earnings growth expectations is at &gt;10%, a fairly optimistic scenario in our opinion. We expect more earnings misses to materialize over the next 12 months.</li> <li>According to Deutsche Bank, investors have redeemed \$83 billion from European equities in the past 6 months.</li> </ul>	<ul style="list-style-type: none"> <li>Consider adding <b>Long/Short managers</b> who can take bi-directional bets and who should benefit from current dispersion.</li> <li>There are some good quality companies which we have on our list that appear oversold with high implied volatility – making them good candidates for <b>FCNs/ELNs structure</b>. This is a good way to maintain a defensive stance while benefiting from high carry from coupons. <b>Do not</b> go beyond 6M in maturity.</li> </ul>

# Equities – Overview (2/2)

Region	IC Outlook (2Q23)	IC Comments	Recommended Positioning
China (CSI 300)	↔	<ul style="list-style-type: none"> <li>▪ 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.</li> <li>▪ 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.</li> <li>▪ 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.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Investors should <b>continue to remain invested in low beta long short managers</b> (FengHe, Luxence) for now. Indeed, <b>we do not recommend taking on full beta risk just yet.</b></li> <li>▪ For direct stocks, we <b>prefer bottom-up picks with strong earnings</b> this year and clear growth trends ahead.</li> </ul>
India (NIFTY 50)	↔	<ul style="list-style-type: none"> <li>▪ Indian equities continue to outperform global equity markets on the back of strong economic growth expectations and inflation prints not getting out of hand</li> <li>▪ Valuations are however expensive, with the Nifty trading at close to 21 times earnings, which is more than its historical average of 18.6 times earnings.</li> <li>▪ Despite the sanguine view on the region, we think a strong dollar serves as the biggest headwind to any meaningful upside to Indian equities.</li> </ul>	<ul style="list-style-type: none"> <li>▪ We recommend a <b>cautious and staggered approach</b> 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.</li> </ul>

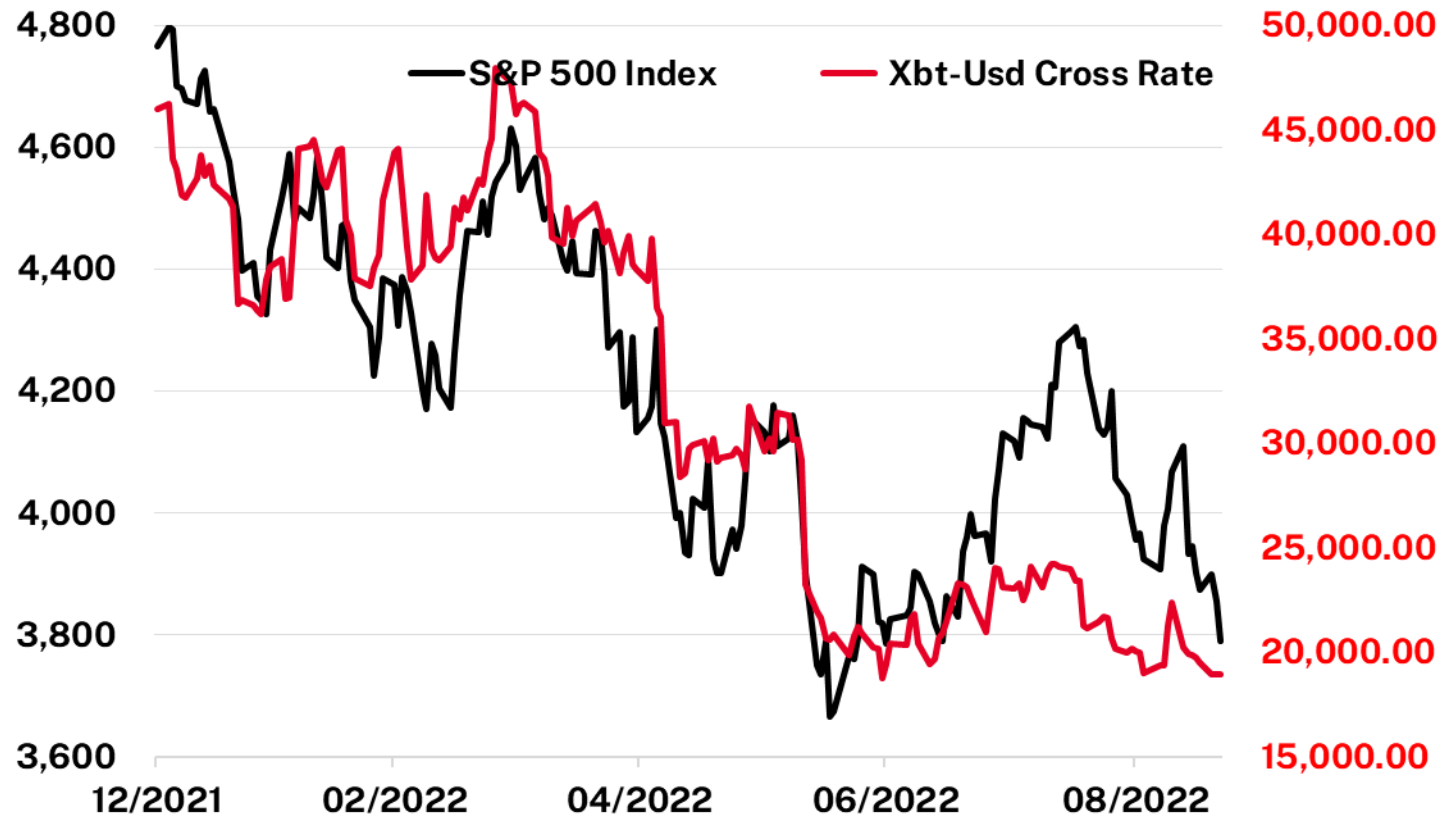
# Alternatives

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# Cryptos Are A Leveraged Play On Equities

So long for DEFI. Cryptos and Equities are actually the same trade.



Source: Bloomberg, September 2022

# GBP Crashes To All-Time Low

The pound plunged 5% to an all-time low after more tax cuts



Source: Bloomberg, September 2022

# EUR In Free Fall

Italy far-right's landslide victory is sending EUR to a 20y low



Source: Bloomberg, September 2022

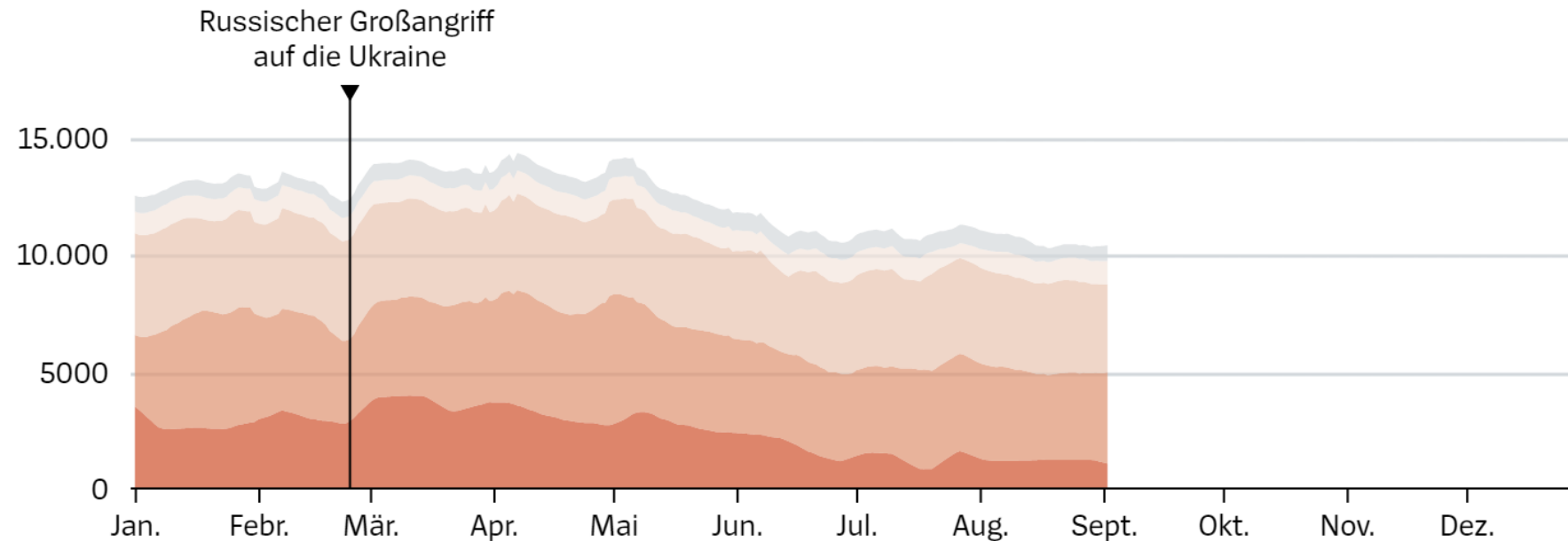
# Europe Energy – Russian Gas Contribution

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

## Europas Erdgasimporte nach Herkunft

Tageswerte in GWh

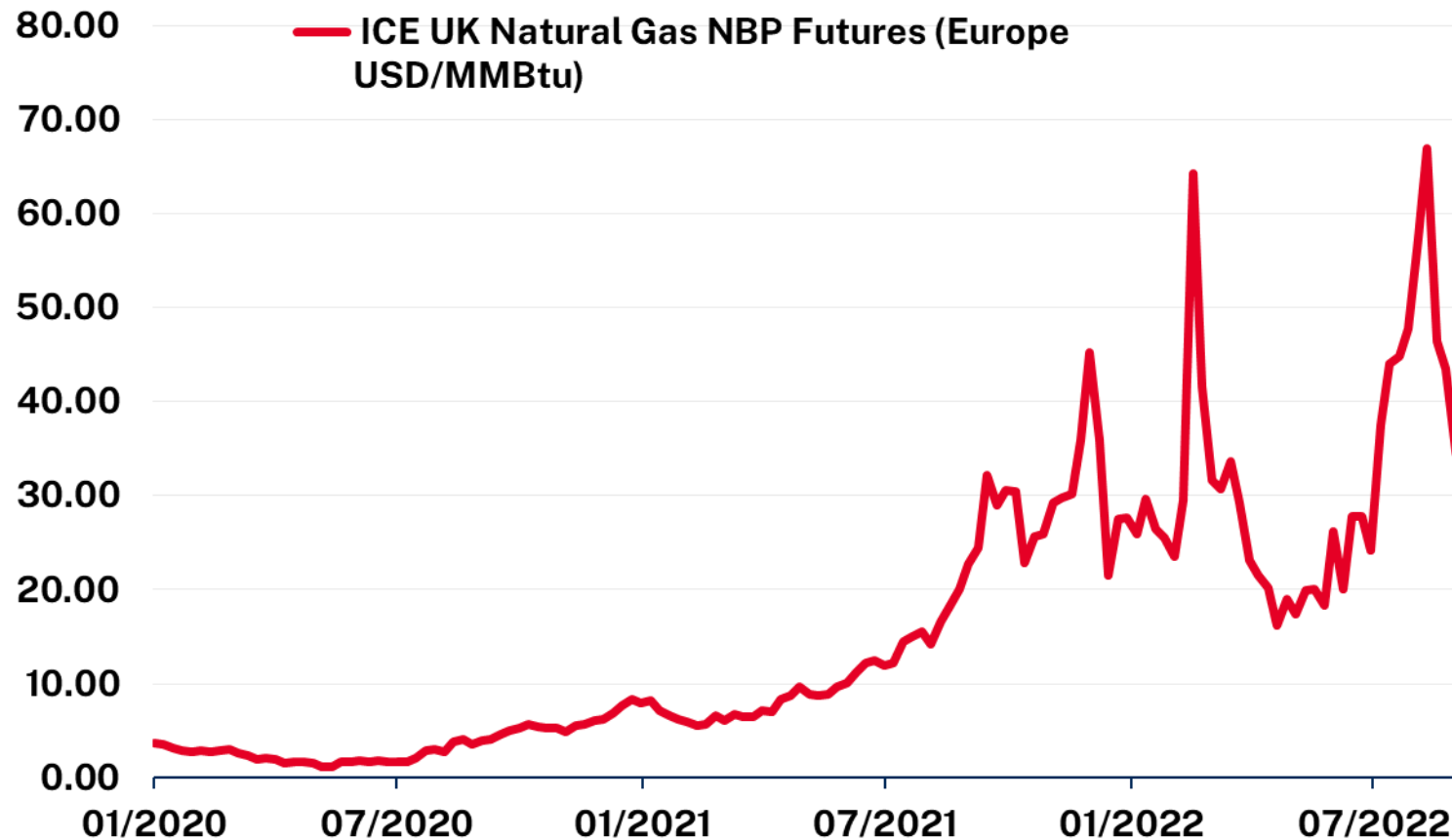
Russland LNG Norwegen Algerien Sonstige



Source: Der Spiegel, September 2022

# European Natural Gas At Record High

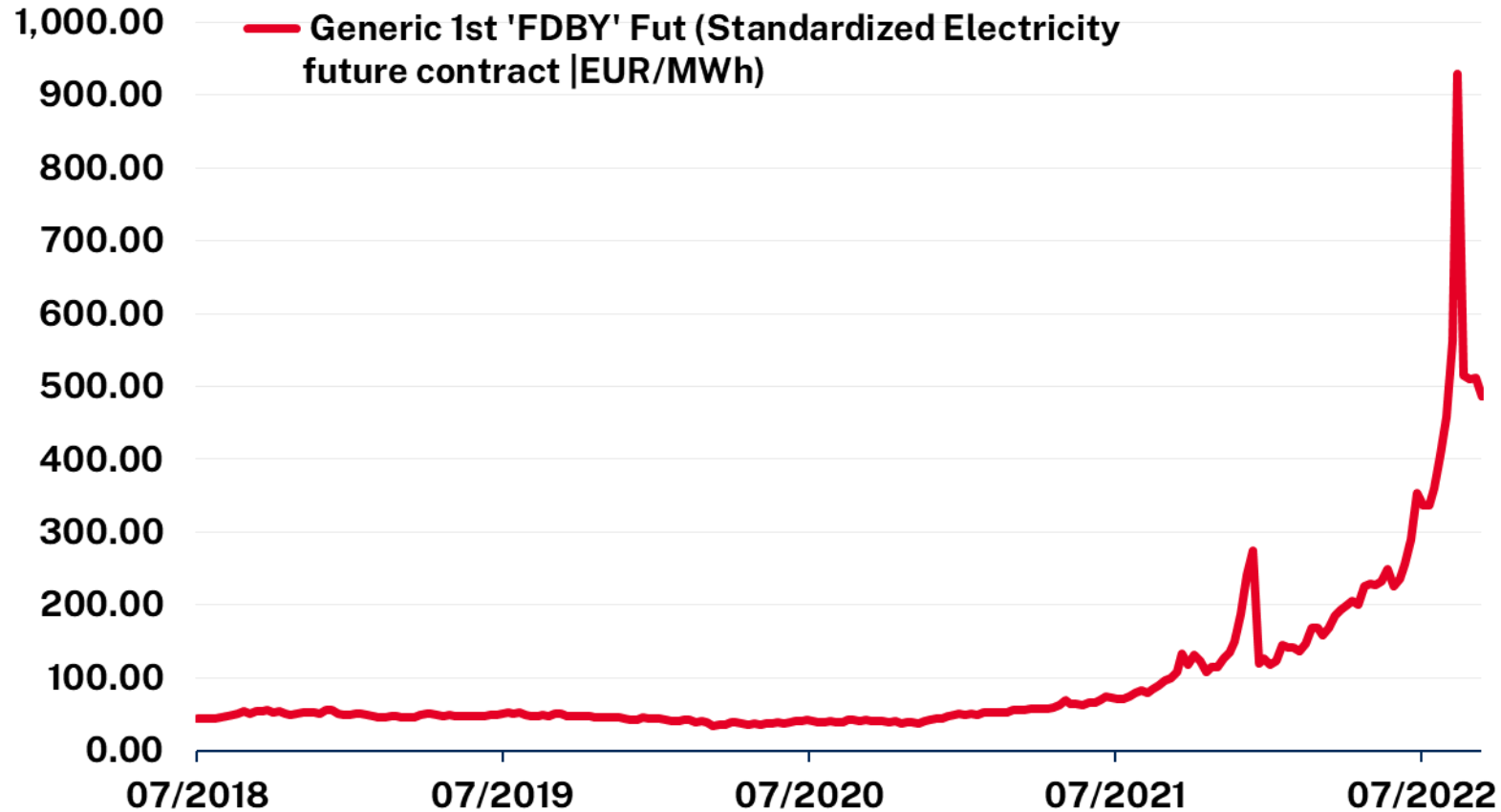
European natural gas prices should remain elevated and volatile as winter-shortage risks persist



Source: Bloomberg, September 2022

# European Electricity At Record High

Utility bills will be significantly higher for European households in the coming quarters



Source: Bloomberg, August 2022

# Alternatives Summary

- Allocate to **Real Estate** to hedge against inflation (BREIT, etc.)
- Start Allocating to **EUR & GBP** shares classes for Alternatives (Serone, Katch, etc.).
- Avoid **EM currencies** (INR, CNY, etc.).
- Allocate to **external managers** for commodities (Delbrook, Aventail, Orion, etc.)

Source: Bloomberg, August 2022



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