GATE ADVISORY

GLOBAL ALLOCATION TACTICAL EXPERTIZE

2022 Outlook

12.23.2021

2022 Outlook. *Not to be forwarded. For professionals only. For personal use only!*

Outlook 2022: A New Era getting Real!

At the end of 2020, your scribe had started the previous Outlook 2021 with the following questions and comments from the initial document were added:

.

1. Global economic growth: Rapid catch up (effective vaccines?) or "Groundhog Day" infection? "The all-in strategy can work with humans, but a virus has no mood. It just follows its evolutionary path without worrying about the rest. " "The infection in the global economy would not appear to be waning as quickly as strategists anticipate. ".

2. Biden: Post-Trump Era complete shift or simple transition? Is the USA back in the game? (Dollar? US equities? Govies? Overweight?).
"To schematize where the United States is, and part of the world, we have to draw a parallel with the 1970s. Moreover, on a generational level, we are also going to experience a demographic earthquake with Millennials replacing Baby Boomers … "
"In addition, the Fed cannot control the dollar as well as its bond and equity markets. Suppose it wants to continue its accommodative policy. In that case, it cannot afford an inflationary shock caused by a fall in the dollar, for example, especially if it is the Yuan that benefits.
This vision of a momentary halt in the dollar's decline will raise the question of the allocation to emerging countries. "

3. China: The new leader or the eternal second? Taiwan? Xi Jinping target (double the GDP, decarbonization)?
"For the moment, Hong Kong concentrates all the risks on the real estate plan, and the authorities do not stop regulating the sector in order to force the developers to be more rigorous as regards the financing of the projects. In fact, 2020 marks the first drop in prices for 12 years ... "
"Your scribe points out that the Chinese authorities will not have the same regard for digital giants as Westerners. Just look at what they've done to the Alibaba Group and its subsidiary Ant Financial ... "

4. Liquidity Binge: MMT or Reset? Suitable for all assets, including Private Equity?
"As a result of monetary policies pushing trillions of dollars in bonds into negative interest rates, investors will increase the share of the alternative. Equity risk should be considered globally, so if equities are preferred, Private Equity must also be. "
"Due to the duration effect, multiplied tenfold by zero or even negative rates, the inflation/currency pair is explosive, raising fears that a small upward variation in rates could have serious consequences. "

5. Inflation: the awakening of the tiger?
   "This question was already in our 2020 strategy. Indeed, the pandemic linked to Covid-19 has only revealed the existing problems, both in our societies and in our economies. The disconnection from the financial markets is solely due to the actions of central banks and the increase in retail trading. "
   "Inflation is the only data difficult for central banks to manage (The BOJ has spent its last 20 years trying to create inflationary conditions without succeeding.), Yet debt and leverage have become so extreme that currencies could also serve as the last adjustment variable. The latter is also difficult to control by central banks, as the currency markets are deep. "
   "History suggests that the risk of inflation is most significant when the conviction of low inflation is strongest, and the view is entrenched in intellectual and political frameworks. "
   "In addition to supply chain disruptions, reindustrialization policies, and rising commodities, monetary policies will have their share of responsibility (in the rise in inflation) ..."

6. Bonds/Equities: Crossroad or Collision course? Still need to be Barbell?

"As economically, will we have a restart or a reset on asset allocation? The subject was discussed in the first point. But it looks like the 60/40 allocation may not work in such volatile markets. "

"On stocks, your scribe places visibility first. China, without question, offers the best visibility being a state-run economy. It is necessary to integrate:

- *The appreciation of the Yuan,*
- *The possible normalization of the monetary policy of the PBOC (which worried the OECD and the World Bank).*
- *Xi Jinping's desire to double the country's GDP over the coming decades*
- *To have decarbonized the Middle Empire by 2060."*

"The United States is in second place. We developed the subject in a previous chapter.»

The year 2022 will be like driving on ice. It will be necessary to favor handling over speed.

Our approach will be based on a 3x3x3, three-dimensional, matrix.

T.I.N.A : There Is no Alternative to equities
S.I.G : Short is Good in bonds

This matrix makes it possible to understand and apprehend the major challenges of 2022. Since 2016, the T.I.N.A. has generated a historical flow of frustrations with all types of active managers.

Your scribe will try to be less literary than other years. You already read a lot of strategies for the next year and the goal is to be effective.

Why a new era? Gramsci's quote has never been so cruel in truth: "The old world is dying, the new is slow to appear, and it is in this chiaroscuro that monsters arise. "

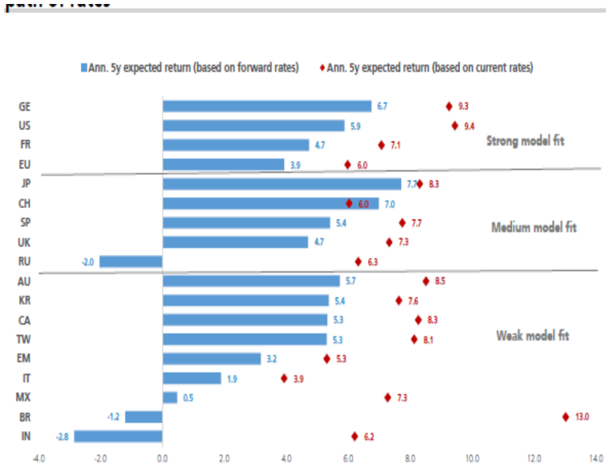
For the first time since the 1980s, the bond bull market is coming to an end and inflation could become structural.

For the first time in a decade, it appears that the NIRPS and ZIRP cycle is coming to an end.

For the first time in decades, China is on the way to overtaking the US on a significant number of economic metrics.

The change of age brings two important currents in asset allocations that had already been expressed by the title of our Outlook 2021: Collision Course.

On the one hand, equity valuations and Expected Returns are no longer supported by economic growth, swelling central bank balance sheets, and low or even negative rates.



	Alpha impact (drift of the model)	Beta impact (direct impact of current ERP on future excess returns)	Cash (added back to back out total return from excess returns)
GE	-8.2	17.6	-0.1
US	0.8	7.6	1.1
FR	-1.7	8.9	-0.1
EU	-2.1	8.2	-0.1
JP	0.2	8.1	0.0
CH	-3.8	7.3	2.6
SP	-6.3	14.2	-0.1
UK	-4.6	11.2	0.7
RU	-11.8	9.7	8.4
AU	2.2	5.1	1.2
KR	0.2	5.8	1.7
CA	0.5	6.5	1.4
TW	-2.3	10.0	0.4
EM	-3.4	7.6	1.1
IT	-0.1	4.2	-0.1
MX	-4.2	4.6	6.5
BR	-1.8	4.0	10.7
IN	-0.8	1.5	5.6

Source : Bloomberg, UBS

On the other hand, bonds will suffer from the normalization of central bank monetary policies. The effect of Duration will be felt or be "discovered" depending on the professionalism of the investors.

The duration effect is more violent when the rates are low, and the maturities are long. Example: the Austrian 100Y! A 150-bps movement in rates causes a 135% variation in prices ...

Investors have lengthened the durations or downgraded the ratings of the bonds purchased to chase a few basis points of additional yields.

To be precise and to answer the questions of our 3x3x3 matrix concisely, that is to say, 27 queries, we have posed four areas of investment that your scribe considers crucial in 2022.

1 – The Dollar King and his Prince, the Yuan

This positioning is essential, as it conditions investments in general and concerns emerging countries, in particular.

Some emerging countries will still benefit from the appreciation in commodity prices or the forced digitalization of our economies. Some will have current accounts allowing their currency to be maintained.

But in a rising rate cycle and a strong dollar (this has been our positioning since 2020 regarding the American currency), you will understand that emerging market assets could suffer.

Added to this is the possibility of taking a country's central bank by those in power. The example of Turkey is quite telling. The country's central bank cut rates as inflation rises above 20%, under the will of Erdogan, forcing the government in December 2021 to raise the minimum wage by 50% (in local currency) ...

This pauses question regarding the Yuan. For us, China is no longer an emerging country. However, being viewed as such by 95% of index builders, we're going to pretend this is the reality.

While the PBOC has held a less accommodating focus in recent years, in relative and absolute terms, versus other central banks, it can afford to be more accommodating in 2022.

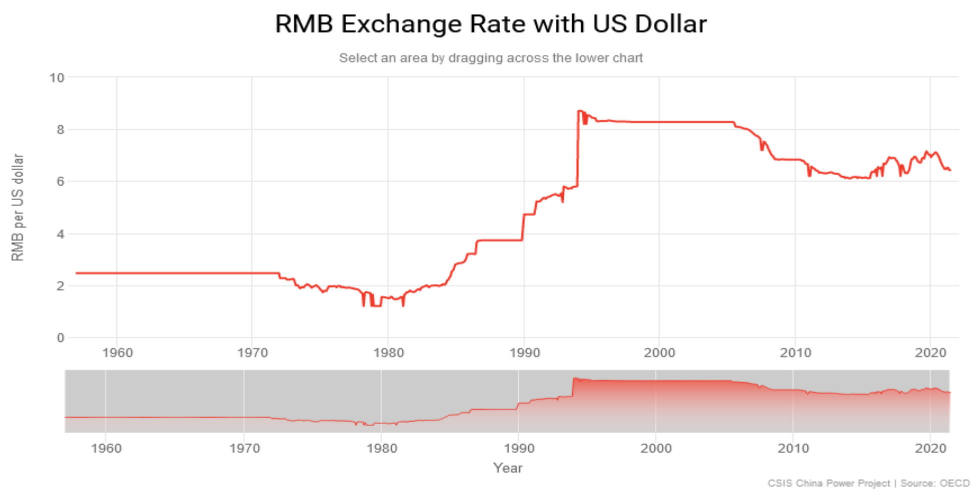
But there again, we have the telescoping between two currents. The FED will raise rates (at least three times in 2022), while the PBOC, with long Govies yields of more than 3%, could very well lower its own. But you quickly forget the PPI and the effect on the currency.

The producer price index rose 12.9% in November, "slower" than the 26-year October high of 13.5% but faster than the 12.4% expected in a Reuters poll with analysts. It is obvious that we do not see the PBOC taking the path of the Turkish central bank ...

Inflation drives rates up significantly if the CPI and wages soar, which logically happens when the PPI enters a specific regime.

The Yuan had one of the best performances of the world currencies against the King Dollar. The Chinese currency is already undervalued by 20 to 30% depending on the metrics considered.

China has a massive positive current account, foreign exchange reserves exceeding $ 3tn, and faster economic growth than developed countries.



If the Yuan can be affected by the divergence in monetary policies between the FED and the PBOC, it is clear that China wants a strong Yuan, and this for three reasons:

- This accelerates the currency's adoption by central banks, which include it more and more in their basket of reserves. If it has become the third currency, it only counts 2% of the total. However, the CNY accounts for 5 to 10% of international trade.
- A strong Yuan limits the impact of rising commodity prices generally denominated in USD.
- This allows China to lend to emerging countries along the Belt & Road easily.

However, a strengthening of the Yuan is further inflationary pressure at a worldwide level. For example, most T-shirts sold in the USA are "made in China," not to mention auto parts and electronic components. Brands "made in the USA" are, in fact, "made in China": Ray-Ban, Hush Puppies, Arrow Shirts, Gillette, Barbie, Woolrich, Huffy, Levi’s, Converse, Nike, and Black & Decker.

Ultimately, we remain favorable to the Dollar and the Yuan versus other currencies.

2 – Inflation and the Pandemic

We will not revisit the comments from our previous Outlook, but it is fair to say that central banks made a misdiagnosis. Inflation is not transient, as is the pandemic at this point.

a- Impact on monetary policies and economies

In fact, from the onset of the pandemic, both monetary and political decisions did not address the correct variable in the equation.

Everything revolves around the simple fact: Transmission = Mutation. The two decisions that will only increase the risks of a correction in financial assets are:

- Vaccination of the elderly instead of the young; and the abandonment of emerging countries in the distribution of vaccine doses.

- The disproportionate increase in liquidity without knowing what the Covid was at the start of the pandemic.

These two decisions triggered successive waves of variants, impacting the Supply Chain, and the historic rebound in financial assets. Thus, the inflationary effect has only been increased tenfold.

Against this backdrop, central banks have no choice but to stop asset purchases and raise rates. The inflation regime is the most critical data and will allow us to gauge the pace of monetary policy normalization.

Indeed, the more it settles at a high rate, the more quickly monetary policies will tighten. While a cycle of rate hikes can quickly calm any consumer overheating, this is not necessarily true when it comes to bottlenecks in the supply chain.

Suppose you add in wage increases, the only economic metric that did not benefit from rising financial markets and falling rates. In that case, you get an explosive environment for long-duration assets.

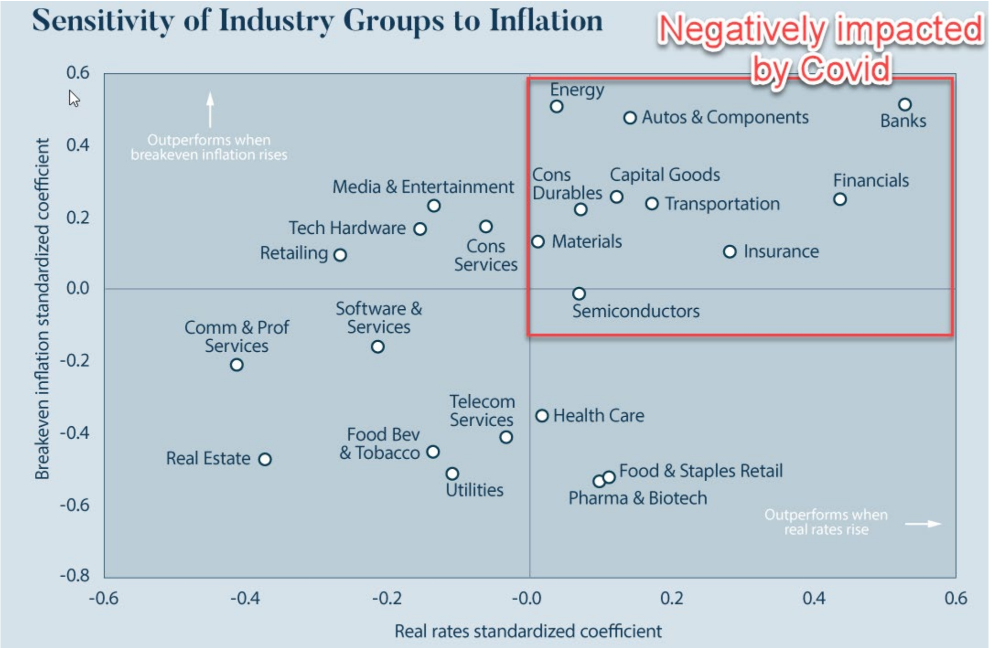
According to the American press, the National Employment Law Project (NELP), 21 states and 35 cities and counties are expected to increase their minimum wages on New Year's Day.

With some governors taking action later in the year, a total of 25 states and 55 localities - a record 80 jurisdictions - will raise their compensation floors sometime in 2022, according to the NELP.

A base salary of $ 15 an hour is becoming commonplace. The California minimum will hit $ 15 for the first time on Jan. 1 for large employers. New York State, already $ 15 in New York City and fast-food workers statewide, will extend that benchmark to Long Island and Westchester County on New Year’s Eve 2021/2022.

b- Impact in equities

This gives the table below. While historically, sectors could benefit from inflation and rising rates, the latter are negatively impacted by the pandemic.

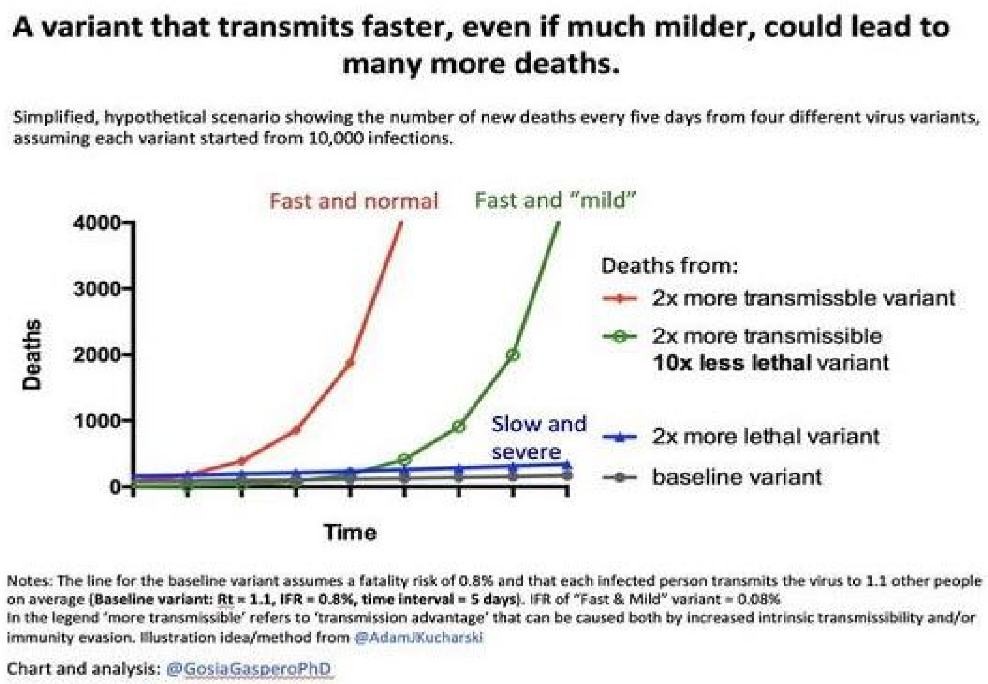


With the rise in rates, the thorny question of Duration arises, the problem of which we mentioned in the preamble.

However, sectors in the red box (above) could benefit from less catastrophic consequences than anticipated from Omnicron. The fact that Western populations are predominantly vaccinated, and that the effect of the latter variant seems less dangerous, may suggest this possibility.

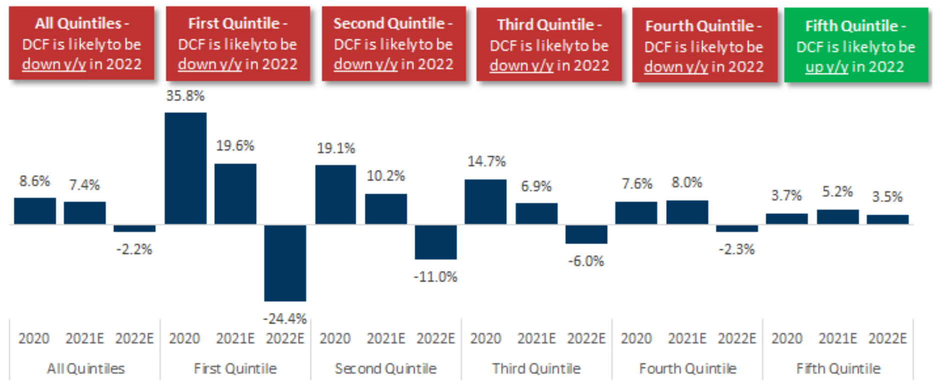
Suppose your scribe subscribes to this optimism after Q1 2022. In that case, it seems mathematical that more people being infected with Omnicron could result in as many deaths in absolute terms as due to the Delta variant.

In addition, British studies highlight that the youngest age group, and therefore the least vaccinated, is the most affected ...



This brings us to the dichotomy between growth expectations in corporate earnings and downward revisions to GDP growth.

Exhibit 2: We anticipate double-digit declines in discretionary cash in-flows for the bottom two US income quintiles next year

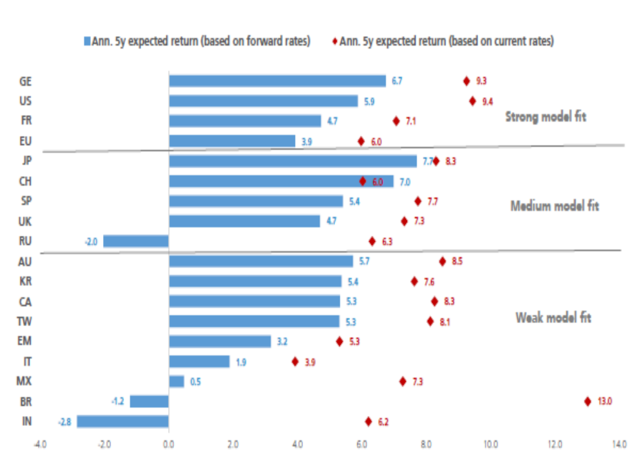


Source: Bureau of Economic Analysis, Goldman Sachs Global Investment Research

The generation of cash flows will be affected by the increase in raw materials, wages, and certain benchmark currencies.

Therefore, the bond markets will fight against the duration effect and the equity markets against the optimistic expectations of future valuations.

All Expected Returns on equities are revised downwards if Forward rates are considered.

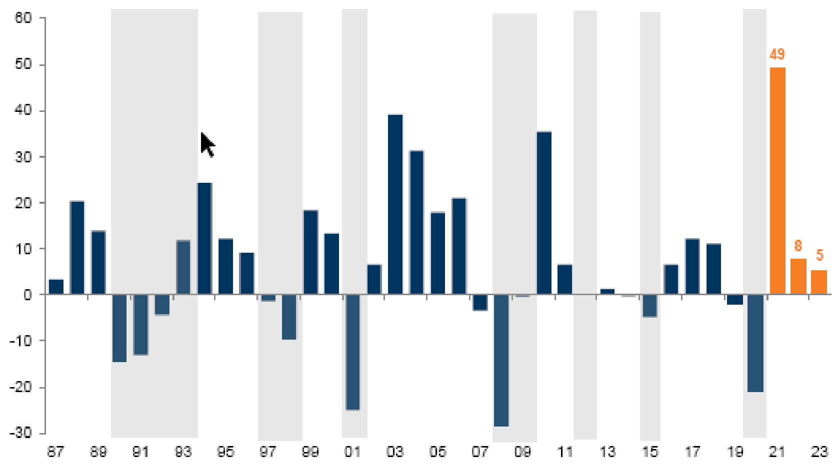


	Alpha impact (drift of the model)	Beta impact (direct impact of current ERP on future excess returns)	Cash (added back to back out total return from excess returns)
GE	-8.2	17.6	-0.1
US	0.8	7.6	1.1
FR	-1.7	8.9	-0.1
EU	-2.1	8.2	-0.1
JP	0.2	8.1	0.0
CH	-3.8	7.3	2.6
SP	-6.3	14.2	-0.1
UK	-4.6	11.2	0.7
RU	-11.8	9.7	8.4
AU	2.2	5.1	1.2
KR	0.2	5.8	1.7
CA	0.5	6.5	1.4
TW	-2.3	10.0	0.4
EM	-3.4	7.6	1.1
IT	-0.1	4.2	-0.1
MX	-4.2	4.6	6.5
BR	-1.8	4.0	10.7
IN	-0.8	1.5	5.6

Source : Bloomberg, UBS

We will switch to single-digit equity earnings growth in 2022, in sharp contrast to 2021.

Exhibit 4: After the strong rebound of 2021, we expect global earnings to grow 8% in 2022
MSCI AC World annual realised earnings growth, grey shading indicates recessions (US, Europe, Japan, or EM)



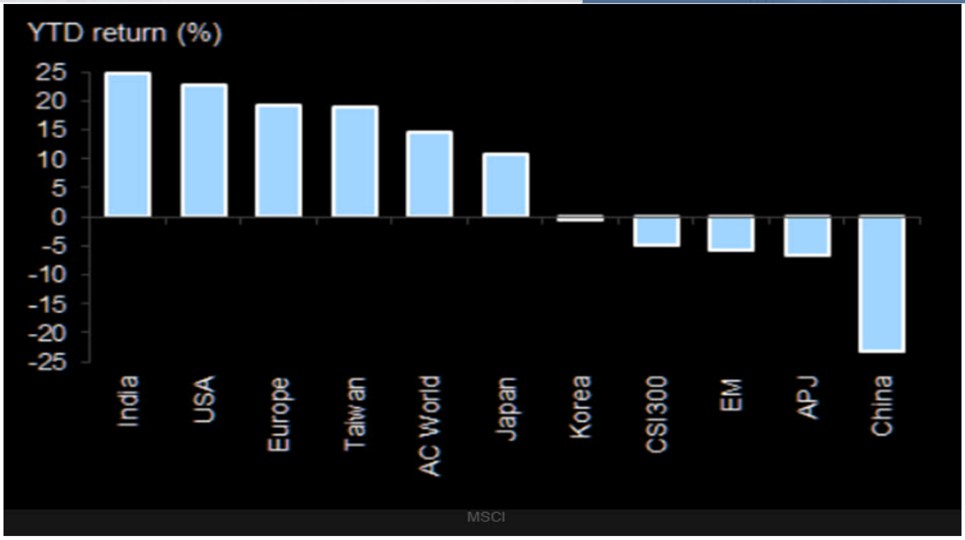
Source: I/B/E/S, Datastream, Goldman Sachs Global Investment Research

Over 2022, the growth expectations of the US equity indices do not include a high inflation regime (therefore a rapid cycle of rate hikes), nor a wave of Profit Warning in Q4 2021 and Q1 2022.

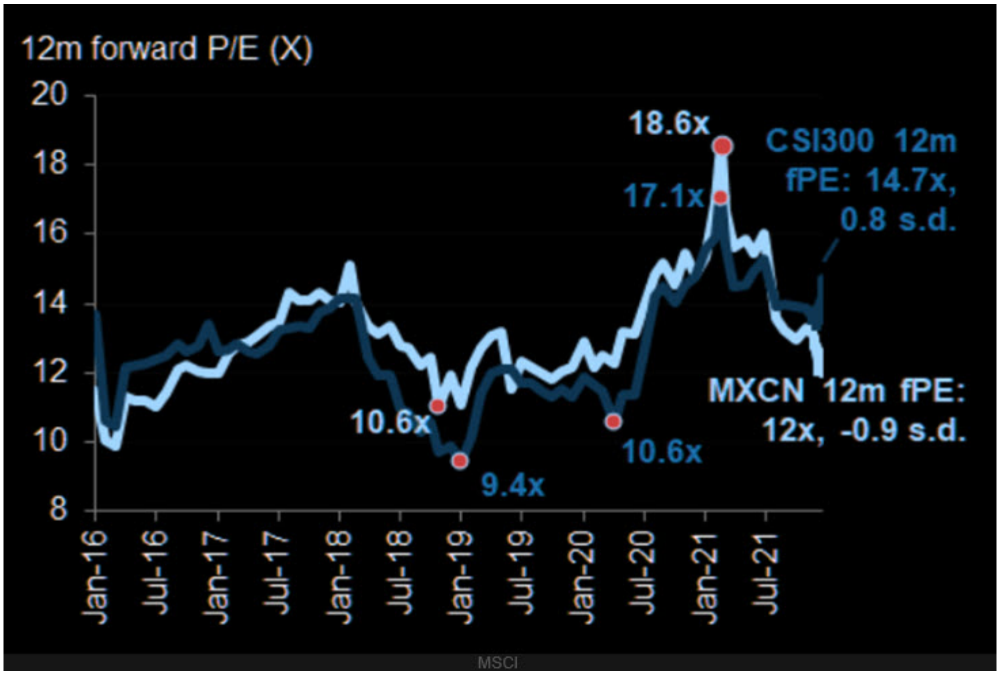
Economic growth is not yet in question, although the risks of stagflation are genuine.

Therefore, we must consider the assets that could benefit from an accommodating monetary cycle and an attractive valuation.

The only country that can benefit from such conditions is China. The Middle Empire is by far the worst performer of 2021.



In terms of valuation, Chinese equities offer a significant discount.



And when it comes to improving credit conditions, the following charts speak for themselves, pointing out that conditions in the US are ultra-accommodating.

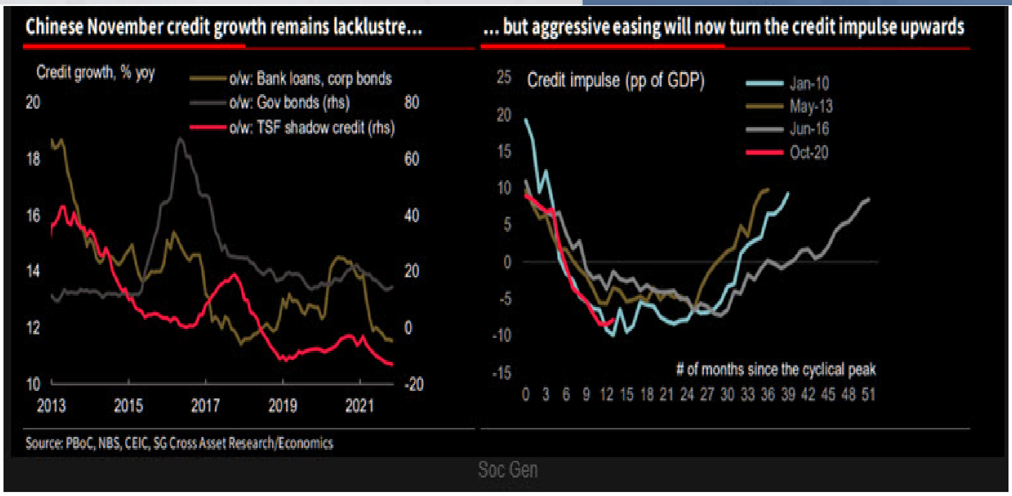
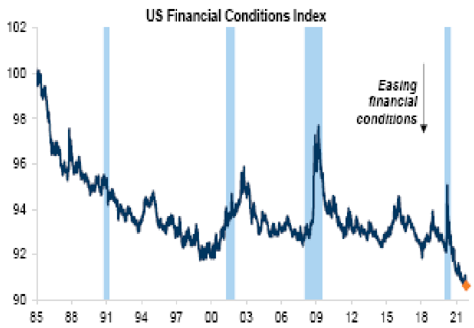
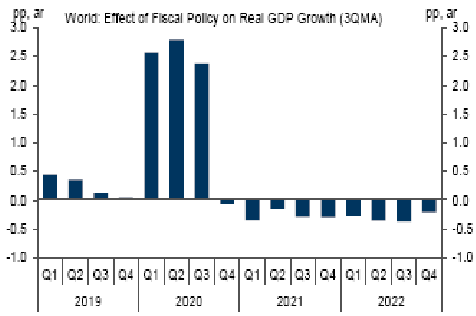


Exhibit 2: US financial conditions are remarkably easy...
Shaded areas: US NBER recessions



Source: Goldman Sachs Global Investment Research

Exhibit 3: ...but the fiscal boost is starting to fade
Contributions to global real GDP growth



Source: CBO, Bureau of Economic Analysis, Haver Analytics, Goldman Sachs Global Investment Research

The political strength of the powers will be one of the keys to 2022. Indeed, only China has a stable political structure. In the US, the midterm elections could give Republicans back both houses of Congress.

But Biden doesn't even need that to be in trouble. Only one Democratic senator, Joe Manchin, can block the launch of the BBB.

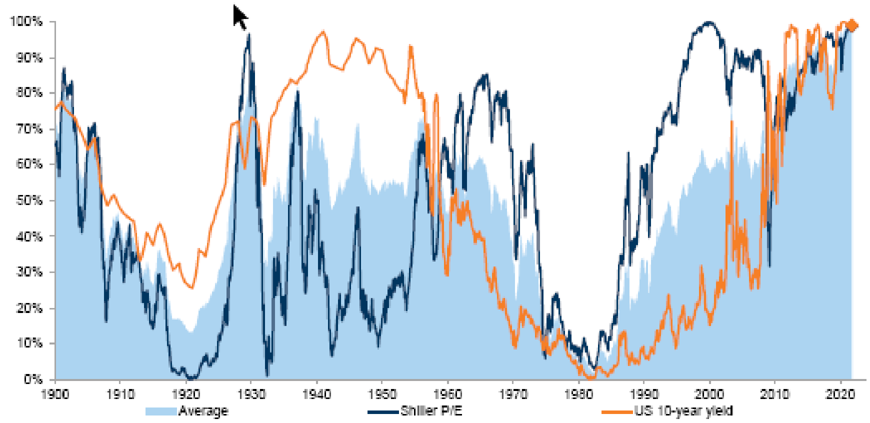
In Europe, the new German government is the alliance of three political parties that do not have the same values. Above all, the Foreign Office is in the hands of a very vindictive environmentalist towards Russia (the country's leading energy partner) and China (the country's top trade partner).

A new government will be elected in France in Q2 2022, leaving doubt about the Franco-German positioning. Amid this political spectrum, the ECB will have a lot to do with a Bundesbank that does not want to hear about inflation.

The advantage, or the problem (depending on the point of view), is the TINA effect can be fueled by the overall high cost of financial assets, making that of equities more "bearable."

While TINA has primarily benefited TECHs, this segment is the most sensitive to rising inflation. Conversely, the longer the pandemic lasts, the more the digitization of our world will become accentuated with the Metaverse as an absolute expression.

Exhibit 8: Expensive valuations after the bull market in every major asset class, similar to the Golden 1920s and 1950s
Valuation percentile (since 1871)



Source: Robert Shiller, Datastream, Goldman Sachs Global Investment Research

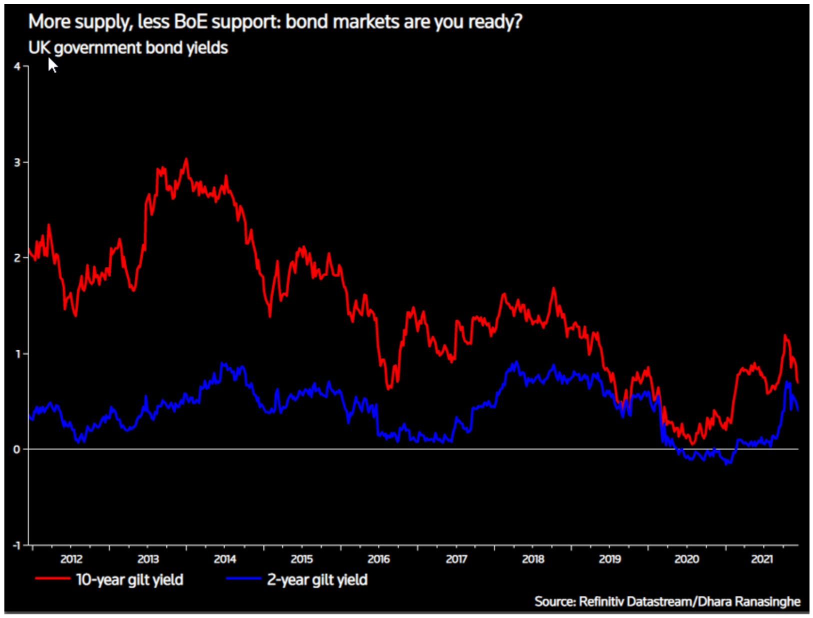
c- Impact in bonds

A fall in bonds due to rising rates and the withdrawal of central bank asset purchase programs may be favorable for stocks in 2022.

Central banks, the most trusted group of bond buyers in the developed world, could cut debt purchases next year by up to $ 2 trillion in the big four advanced economies, implying an increase of potentially significant borrowing costs for many governments.

But if central banks set a timeline for exiting stimulus measures from the pandemic era, a shortage of well-rated bonds, especially in Europe, could become excess.

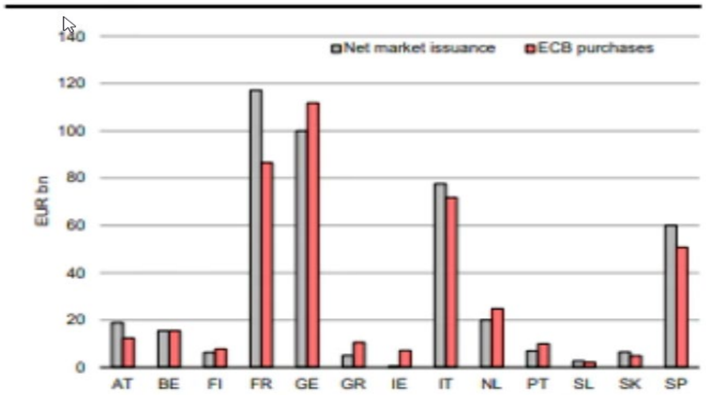
JP Morgan estimates that central bank bond demand in the US, Britain, Japan, and the Eurozone will fall by $ 2tr in 2022 after reducing $ 1.7tn this year.



The question is whether investors will be ready to replace central banks when the rates of return of the Govies are, for developed countries, largely lower than those of the dividend yield of the major indices.

This means that the crushing of spreads between issuers of government bonds could end and, finally, widen, reflecting an unavoidable reality. It is not normal for France to issue debt at only 35bps more than Germany, or a quarter of Italy's spread ...

CHART 14: ESTIMATED ECB PURCHASES VS. NET MARKET ISSUANCE



"Net market issuance" includes all market instruments, including those not eligible for purchase by the ECB (e.g. BTP Futura and international bonds). "German net issuance" includes net issuance by German agencies and states that is eligible for purchase.

Source: ECB, eurozone debt agencies, UniCredit Research

According to the previous chart, the fact that the ECB can step back from the dance floor means that the coupon on Bund issues is expected to rise, pushing higher Govies yields in France, Italy, and Spain. To this must be added the widening of spreads ...

This shock could come at the worst time for states, at a time when fiscal stimulus packages will be essential in trying to absorb the shocks of successive waves of variants.

Goldman believes the bond markets have failed to accommodate a faster reduction in the Fed's balance sheet. If the US Treasury uses Bills to fund itself from the public, bond volatility will be an essential asset to manage.

In particular, the Fed acts as a source of inelastic price demand, providing an outlet for risk, which gives liquidity providers some confidence.

The depth of the rate market has already deteriorated since Q3 2021, and the Fed's withdrawal from its role as a “safe” buyer may lead to additional vulnerability.

While MOVE has already incorporated more volatility, it is not guaranteed that all investors are adequately prepared or positioned.

At the same time, monetary funds will have to be watched closely. The SEC has passed 5 new rules:

1) Increase the share of total assets that must be held in cash or other highly liquid assets to 25% for overnight liquidity and 50% for weekly liquidity (compared to 10% and 30% previously),
2) Remove the ability of funds to charge fees for redemptions or impose "gates" if liquid assets fall below certain thresholds,
3) Require blue-chip, tax-exempt institutional funds to use a swing pricing mechanism that adjusts the net asset value when the fund has net redemptions,
4) Further changes in reporting requirements and
5) Requiring to convert stable NAV to a floating share price when fund returns are negative.

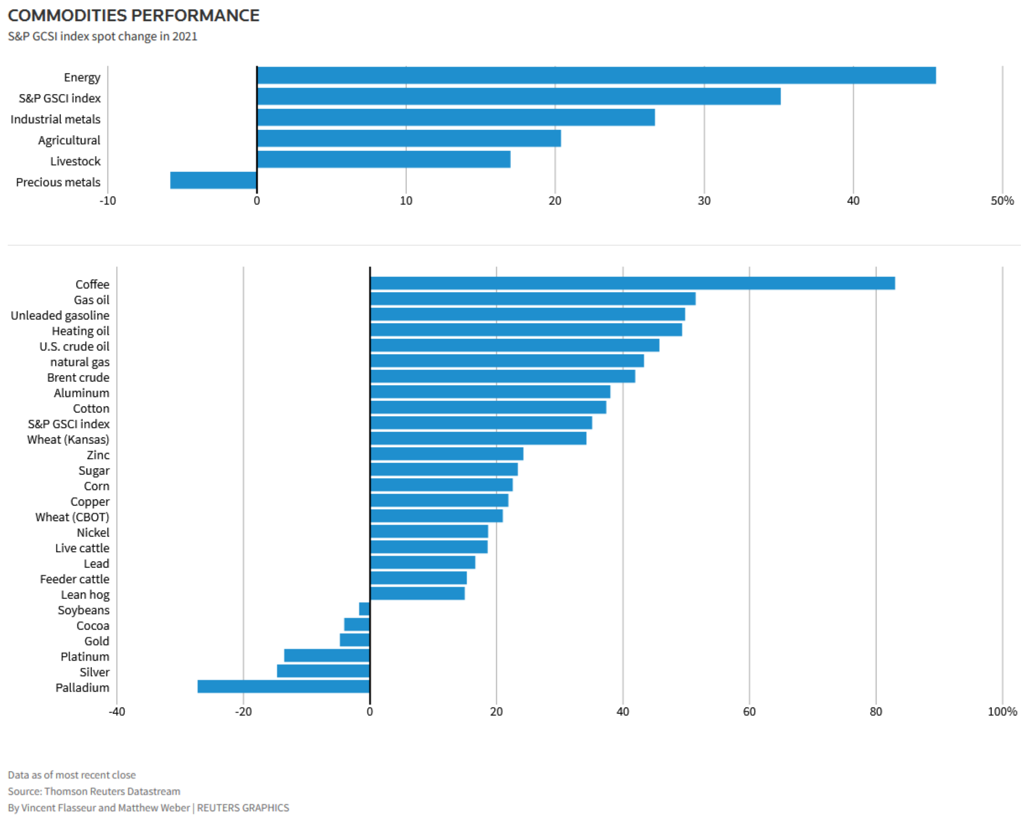
Currently, according to Crane Data, blue-chip funds totaling around $330bn in assets under management have weekly liquidity below the proposed 50% threshold.

Over time, implementing specific provisions could lead to outflows of less liquid assets such as CP (Commercial Paper) as funds seek to comply with the higher liquidity buffers.

And this brings us to the Stablecoins, which have become the first buyers of CPs (see our comments on upcoming regulation).

d- Impact in commodities

In general, commodities offer stunning performance in an inflationary environment. For the moment, hydrocarbons and agricultural raw materials have verified this adage. Precious metals did not. While the automotive crisis, linked to the lack of semiconductors, has impacted Palladium and Platinum, gold and silver have not yet fulfilled their role of shields against inflation.



The dollar's strength can be evoked when one observes the weak performance of precious metals. It seems that the assets depicted in the next paragraph played the role of a safe haven.

e- Impact in cryptocurrencies

A sign of the times, it seems that cryptocurrencies have taken on the role of safe haven.

We won't be rewriting what was mentioned in the 2021 Global Macro Insight, but in essence:

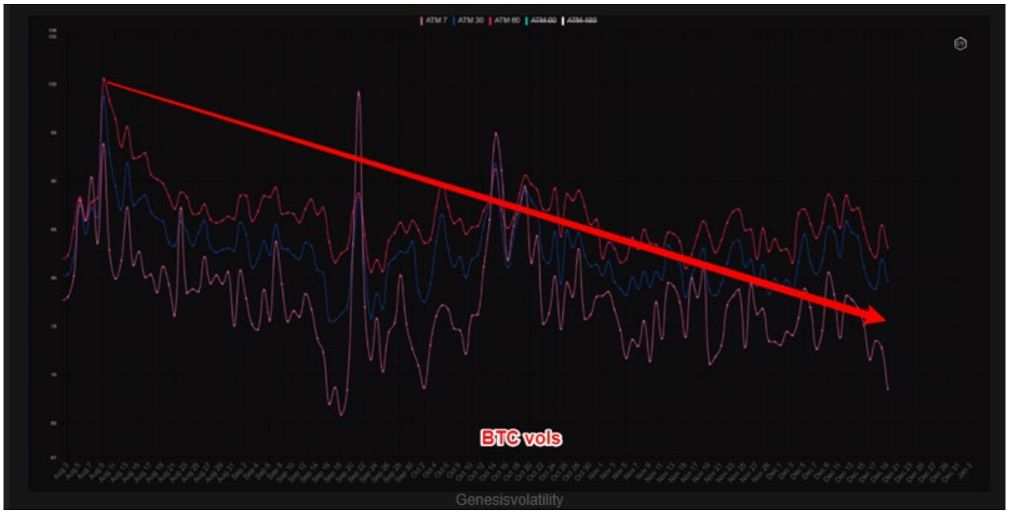
- The BlockChain will be as revolutionary as the Internet in the 80s / 90s.

- States (China first) will assimilate this technology to create CBDC (Central Bank Digital Currency). This means a complicated future for Cryptos serving only as payment.

- Faced with the risks of destabilization of the American monetary system represented by Stablecoins and the resurgence of decentralized finance (a term often used by central bankers to talk about cryptos), regulation will be omnipresent in 2022.

While we favored Bitcoin early last year, volatility and the advent of CBDCs caused us to change our minds during the year. Cryptos called "utilities" are worthy of interest in the long term.

The drop in volatility could attract some end investors. But here again, the regulation could thwart specific plans.



f- ESG as a source of inflation

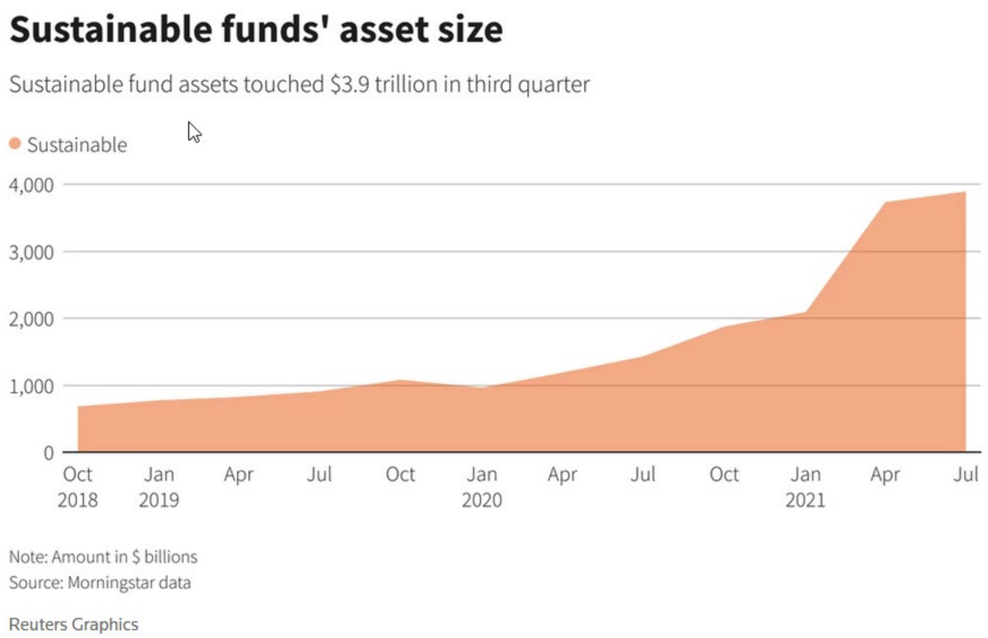
It comes full circle. We have talked about the impact of inflation and the pandemic on the economy and asset classes, but a flow of investment itself generates inflation.

Environmental activism is pushing big investors to stop funding specific industries. The direct consequence is the reduction of R&D and exploration budgets. At the same time, the finance cost is higher when it is available.

This militates for inflationary pressure on the sources of energy of the hydrocarbon type and their by-products. As the energy transition period begins, the entire economy will pay the price.

The number of sustainable funds captured in Morningstar's global sustainable universe increased by more than 51% in the third quarter, reaching 7,486 funds at the end of September.

Funds focused on environmental, social, and governance (ESG) issues saw their combined assets climb to $ 3.9 trillion at the end of September.



The SFDR (Sustainable Finance Disclosure Regulation) aims to help invest $ 1.15tn in green investments over the next decade, eliminate the uneven climate-related information currently provided by financial market players and give an advantage to companies offering truly sustainable products.

In conclusion of this part.

If the 10YUS rate drops below 1.40%, this will be a signal that institutional investors are positioning themselves in "risk-off" mode. Short-duration bonds will be hit by rate hike expectations at the start of the year, followed by long-duration bonds if inflation gets too high.

Credit should be avoided, and as much investing in equities, the returns do not compensate for the risk. While earnings alerts are plentiful at the start of the year, investing in High Yield won't be good.

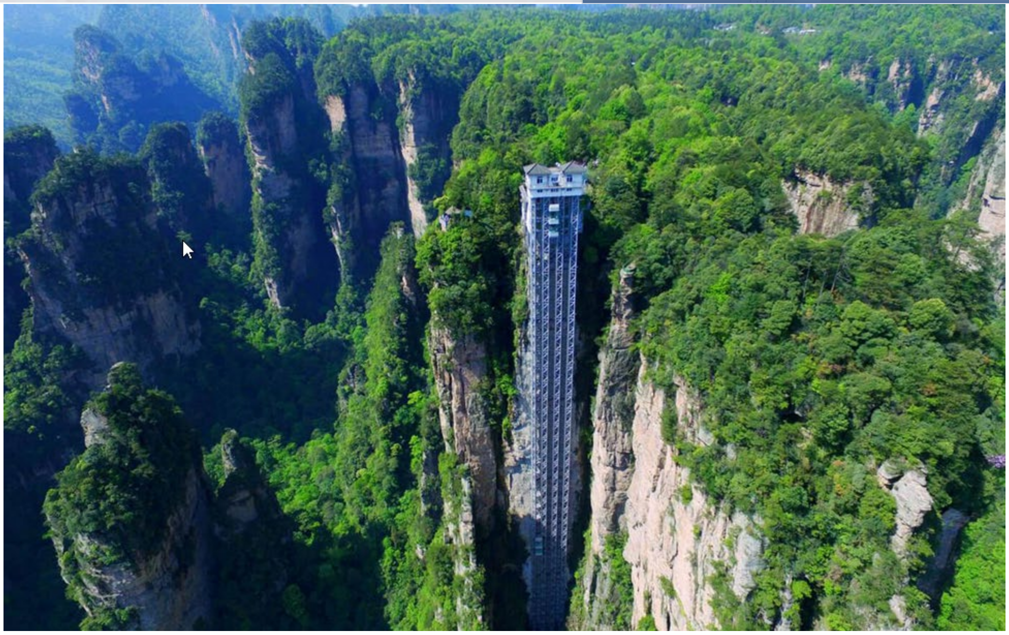
If a Supply shock on the Govies is possible, the end of central bank asset purchase programs will lead to the revival of variations in the spreads between countries' borrowing rates.

THEREFORE, this TINA effect has triggered over the last 12 months, inflows on equities equivalent to those of the past 19 years ...

We would still be very positive on US equities if the performance of 2021 had not been generated by 5 or 10 stocks of the S&P500 or the NASDAQ ...

Only 35% of NASDAQ stocks are above their 200-day moving average. Regarding the S&P500, it seems that the index is in apnea if we believe the abysmal score of the "Advance / Decline" index. ".


Breadth Divergence at 2000 Tech Bubble Top
Advance Decline Accumulation (LHS)
S&P 500 Index (RHS)
20,000
15,000
10,000
5,000
0
-5,000
1,600
1,400
1,200
1,000
800
600
5//1997
7//1997
9//1997
11//1997
1//1998
3//1998
5//1998
7//1998
9//1998
11//1998
1//1999
3//1999
5//1999
7//1999
9//1999
11//1999
1//2000
3//2000
Source: Bloomberg
© 2021 Crescat Capital LLC



3 – Can China generate “balanced” and redistributive growth?

The answer is yes. The drops in RRR and LPR in December 2021 demonstrated the PBOC’s ability to act.

We believe that regulation has not finished its work in the internet sector or real estate developers.

If this wave of regulation has caused layoffs, China will bet on the decarbonization of its economy to create new champions and many jobs.

The “Two Sessions” in March will be essential and will prepare the 20th Committee of the Chinese Communist Party. This apex meeting will be the occasion to promulgate laws and state interventions along certain lines.

Monetary and political support plans will be announced, and here are the eight takeaways from CEWC for December 2021:

- Adhere to the cycle adjustment and keep the growth within a "reasonable range."

- Monetary policy: maintain ample liquidity, reduce the reserve ratio shortly and promote monetary growth by broadening the impact of the central bank (reduction of carbon emissions, small and micro-enterprises, etc.).

- Fiscal policy: maintain flexibility and improve the efficiency of government funds. The "tax relief and reduction" policy for small and medium-sized enterprises and low-income people is expected to increase, and the use of equity funds can be accelerated.

- Policies related to real estate: the end of financing should be more flexible; the policy of local demand can be "temporary," "indirect," and a relaxation of local margins. Strengthen the construction of affordable housing.

- Investment in infrastructure: improve efficiency in the use of capital. The pipeline of local infrastructure projects remains the primary bottleneck. The standard of local bond issues can be released, and new infrastructure can still become a new growth point.

- Relevant policies for the prevention and control of epidemics: The possibility of policy relaxation in the foreseeable future is extremely low.

- The importance of stimulating consumer policy may increase: in addition to policies aimed at reducing direct taxes and subsidies for low-income people and small and micro-enterprises, it is not excluded that policies aimed at encouraging the consumption of "big" durable goods to be more implemented,

- Policies related to reducing electricity consumption, environmental protection, and raw material costs.

Therefore, the month of March will see the advent of a new policy in China, favorable to our themes. Regarding real estate, this same period will be the rendezvous with the debt wall of Evergrande.

Your scribe believes that the consensus makes two misinterpretations:

- Real estate will be put in working order according to Party doctrine. This means that the restructurings will not be painless for insurers and holders of USD developer debt.

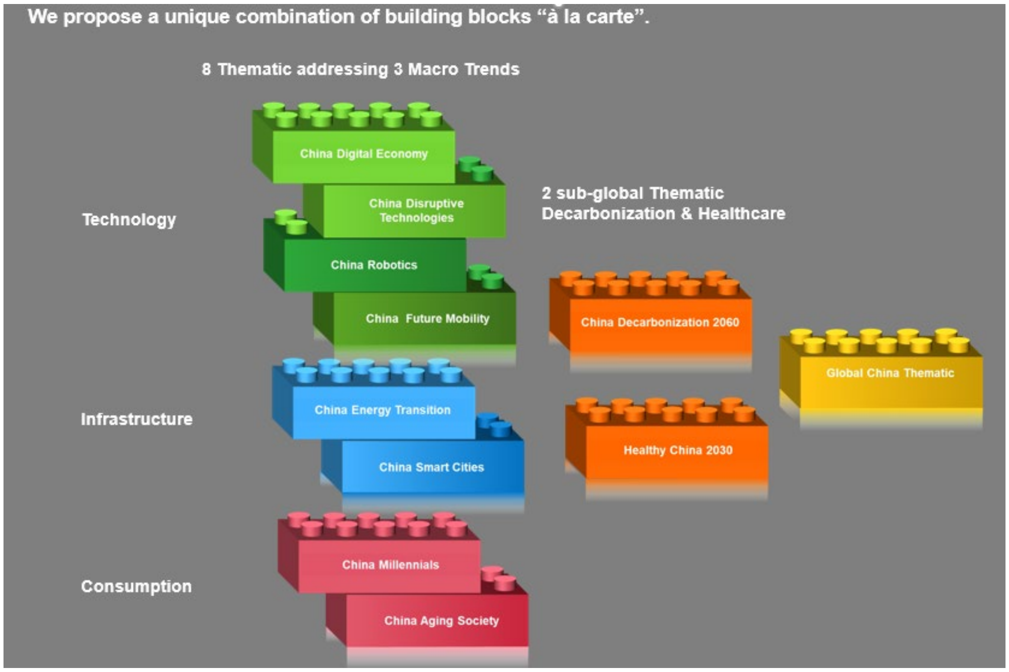
- Consumption in China will indeed change. Chinese consumers prefer brands like Shanghai Tang over Ralf Lauren and Anta over Nike. However, the gamble on a Western-style economy remains risky due to the Chinese people's circumspection to specific changes.

The one-child policy is struggling to be erased due to the lack of infrastructure and tax support to allow it. If pension funds grow, many households prefer to save just under half of their monthly salary.

The Chinese authorities have talked about balance, so nothing to do with American politics. Moreover, the Chinese consumer (overwhelmingly) is not the Western consumer.

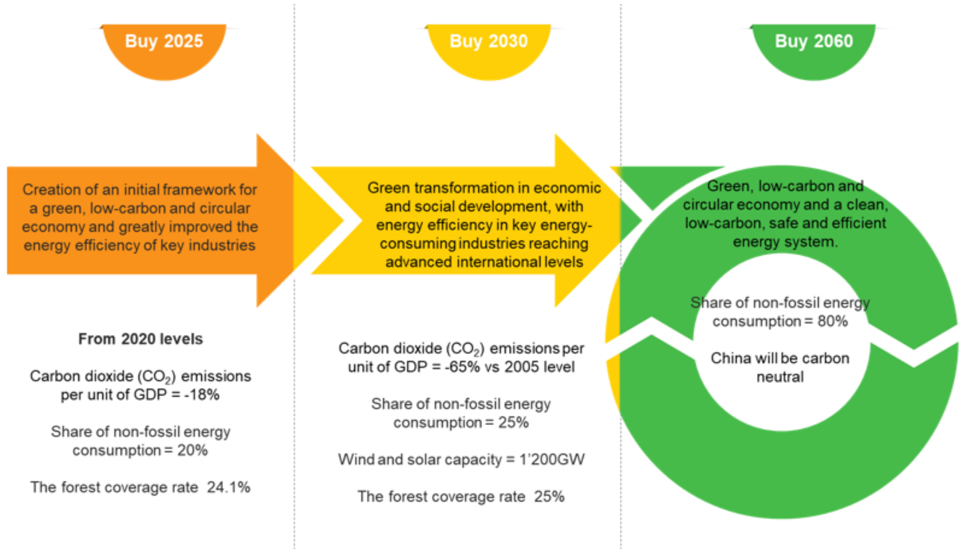
We do not prefer to interpret CEWC messages. These have been somewhat vague, and the interpretation of strategists looking for a new "call" has generated this interest in consumption in China.

The themes that we propose are fed by the five-year plans and the quantified objectives of Politburo. These are facts and not interpretations. The two pillars of these plans are decarbonization and health.



Much of China's economic and geopolitical strategy will revolve around decarbonization.

Here are some graphics from our China Decarbonization 2060 presentation.



11 major guidelines, based on 37 articles, make it possible to understand this theme in the decades to come. The first two articles are summarized in the graph above.

Promoting comprehensive green transformation in economic and social development	In-depth industrial restructuring	Accelerating the development of a clean, low-carbon, safe and efficient energy system
3. Strengthening guidance in planning of green and low-carbon development. 4. Optimizing plans for regional green and low-carbon development. 5. Accelerating the formation of green production modes and living patterns.	6. Optimizing and upgrading industrial structures. 7. Firmly curbing irrational expansion of energy-intensive and high-emission projects. 8. Vigorously developing green and low-carbon industries	9. Strengthening dual-controls over energy intensity and gross energy consumption. 10. Significantly improving energy efficiency. 11. Strictly controlling fossil fuel consumption. 12. Actively developing non-fossil energy. 13. Deepening reforms of energy systems and mechanisms.

Accelerating the construction of a low-carbon transportation system

14. Improving the transportation structure.

15. Encouraging the use of energy-conserving and low-carbon transportation vehicles.

16. Encouraging low-carbon means of transportation.

Improving the quality of green and low-carbon development of urban and rural areas

17. Promoting low-carbon transformation in urban and rural development and management mode.

18. Vigorously promoting energy-conserving and low-carbon buildings

19. Moving faster to improve the energy consumption structure of buildings.

Strengthening research on green and low-carbon technologies and promoting their application

20. Strengthening basic research and research on cutting-edge technologies.

21. Speeding up the research, development, and dissemination of advanced and applicable technologies.

Continuing to consolidate and improving carbon sink capacity

22. Consolidating the carbon sink capacity of ecosystems.

23. Increasing the carbon sink capacity of ecosystems.

Promoting a green and low-carbon mode of opening up

24. Accelerating the development of a green trade system

25. Promoting the development of green Belt and Road.

26. Strengthening international exchanges and cooperation.

Improving laws, regulations, standards, and statistical and monitoring systems

27. Improving laws and regulations.

28. Refining standard and measurement systems.

29. Enhancing statistical and monitoring capacity.

Improving policy mechanisms

30. Improving investment policies

31. Actively developing green finance.

32. Improving fiscal, tax and pricing policies.

33. Developing market-based mechanisms

Strengthening organization and implementation

34. Strengthening organization and leadership.

35. Strengthening overall coordination.

36. Reinforcing local responsibility.

37. Tightening oversight and assessment.

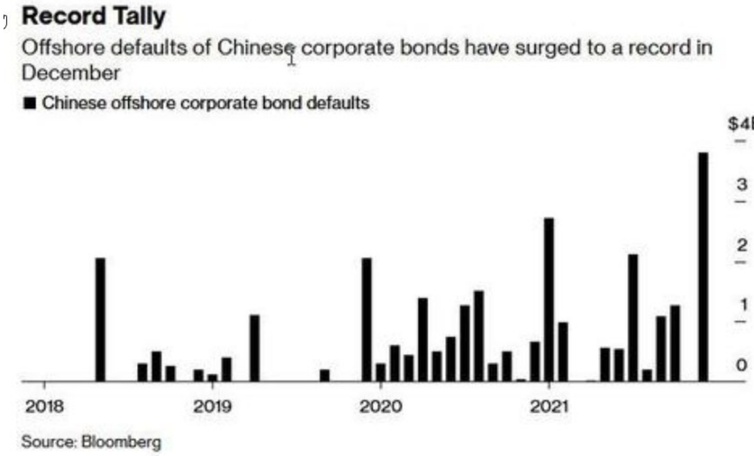
By 2022, China’s capacity to install renewable energy sources will be equivalent to all countries in the world.

At the same time, the issue around real estate in China will be a significant headwind for the year 2022.

Its weight in the economy and the heritage of the Chinese is well established. However, we do not believe that this risk is systemic.

A considerable cleaning will be done in the real estate development sector, but Xi Jinping has the means to contain any contagion. This does not mean that the insurance industry will be spared.

The default rate exploded at the end of 2021, but March and April 2022 crystallized our fears.



Before the industry is (more or less) saved by the state, it must demonstrate that it can help itself through losses absorbed by the owners of these companies.

Counting Losses

Evergrande's Hui leads wealth losses among Chinese property tycoons

Name	Company	Current Net Worth	YTD Losses
Hui Ka Yan	Evergrande	$6.1B	$17.2B
Wang Jianlin	Wanda	8.2	6.9
Yang Huiyan	Country Garden	23.7	6.3
Hui Wing Mau	Shimao	4.4	5.2
Sun Hongbin	Sunac	3.3	4.5
Kei Hoi Pang	Logan	5.2	3.2
Wu Yajun	Longfor	13.9	2.2
Cai Kui	Longfor	8.3	0.9
TOTAL	-	73.1	46.4

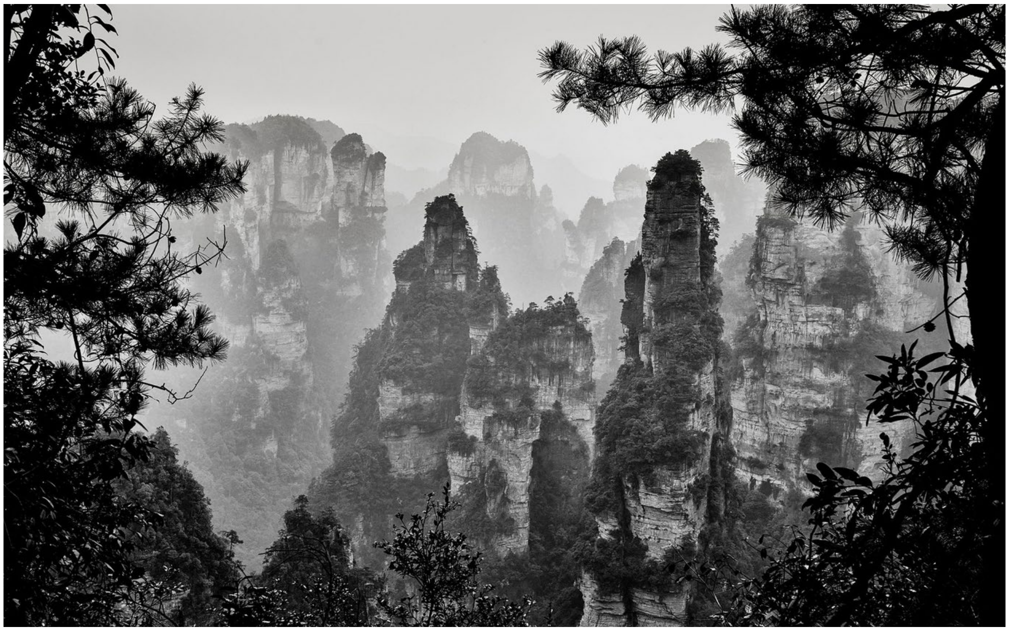
Source: Bloomberg Billionaires Index as of Dec. 15

Considering the case of Ping An, the insurer's total exposure to real estate is CNY185.5bn, spread roughly evenly across equities, debt, and investment property and representing around 4.8% 4.9% of its total investment portfolio of CNY 3,800 billion, according to a note from Citi.

China is the only country with complete independence on its currency and can implement an accommodative monetary policy.

Decarbonizing the economy will cost China $ 5tn over the next few decades. So these are $ 5tn of investment opportunities.

A five-year plan of $ 600 billion will generate as many opportunities as possible on health.



4 – Real estate and Private Equity in this context?

In this last part, we will mainly discuss Private Equity. Real estate is an undeniable source of diversification. However, it is not necessarily the sector to favor in the context of rising rates.

There are only two main risks to be included in this asset class:

- Financial real estate (purchase for-profit and not live there) is predominant. It is based on the fragile equilibrium of underlying prices on record levels and financing rates, conversely, remarkably low.

- The pandemic has put teleworking in the spotlight, emptying city centers and offices. The vacancy rate is only too rarely included in the calculations of the profitability of real estate.

These two points call for a bit of caution. As your scribe began his career in finance in 1995, he knows that this asset class can show double-digit losses in an extraordinary context.

Regarding Private Equity, after a brief interruption due to the virus, the transaction fever returned in the second half of 2020, according to data from Mergermarket and Dechert. This momentum does not appear to be waning as we approach 2022.

The figures speak for themselves: in Q1 2021, 4,605 buybacks were carried out worldwide, breaking the previous annual record. Globally, the industry is on track to break records in terms of value. The $ 1.170 billion in transactions from January to September 2021 exceeded all previous annual figures since 2015.

According to Mergermarket and Dechert, private equity firms have raised $ 630 billion in the first nine months of 2021. Based on current trends, fundraising could exceed $ 1.2 trillion this year and next.

Few General Partners (GP) will complain about having too much money at their disposal. However, if you extrapolate this to the entire private equity industry, the vast reserves of dry powder become a problem.

This always leads to increased competition and higher entry fees, making it more challenging to achieve the promised returns if multiples do not increase during the holding period.

Within private equity, GPs will hesitate to invest in assets with fixed characteristics (see the comments above on real estate), similar to those of bonds, such as real estate leases, which are particularly exposed to the effects of inflation. As prices and costs rise, significant secular trends, such as technology and healthcare, will be in high demand.

The term Continuation Fund could become fashionable. Most private equity analysts predict that one of the effects of the crisis will be the sale of successful holding companies to continuation funds, which usually happens through a secondary transaction led by the GP.

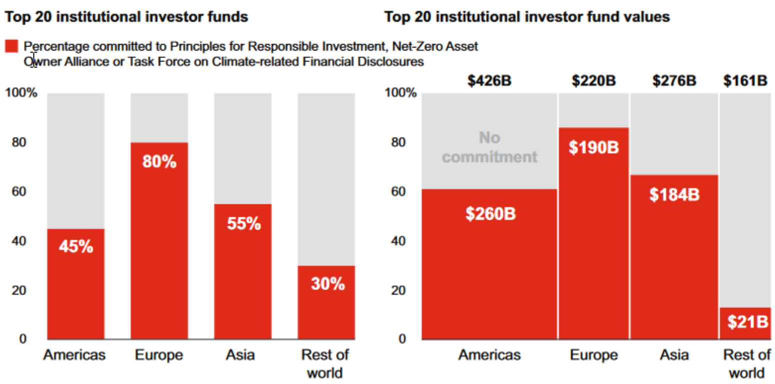
Investors can earn higher returns in these transactions than assets sold to third parties, and PMs can earn more carried interest.

We believe that Buyout strategies will still be favored. This strategy had demonstrated its relevance in an asset allocation in 2020.

Figure 1: Despite massive disruption from Covid-19 and other crises, the buyout market held its own in 2020

Notes: Investments—includes add-ons; excludes loan-to-own transactions and acquisitions of bankrupt assets; based on announcement date; includes announced deals that are completed or pending, with data subject to change; Exits—bankruptcies excluded; IPO value represents offer amount and not market value of company; Fund-raising—includes closed funds only and represents the year in which funds held their final close; buyout includes buyout, balanced, coinvestment and coinvestment multimanager funds
Sources: Dealogic; Preqin; Bain analysis

What about ESG? For once, Europe is in a leadership position on "commitment" in ESG investments.

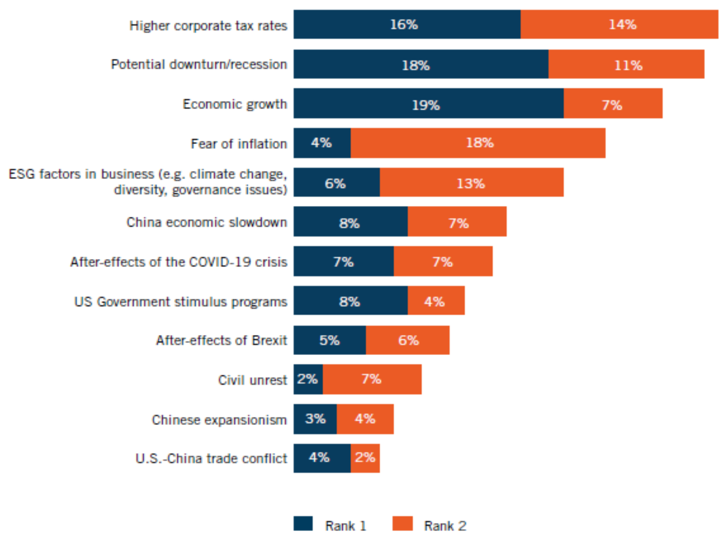


Notes: Excludes funds of funds; includes all other investors with a known allocation to private equity; Asia excludes Australasia; PE allocation amount for some investors not available
Source: Preqin, accessed June 2020

If the SPACs have been in fashion since 2020, it seems that the regulation can calm the enthusiasm in the use of this vehicle, which is not innovative. Both the accounting rules for the options attached to the SPACs, the IPO procedure, and the colossal fees charged by the banks, all these points will be addressed by the regulation with an impact on investors using this type of vehicle.

Here are the main risks subject to Private Equity for 2022, according to a survey by Deshert.

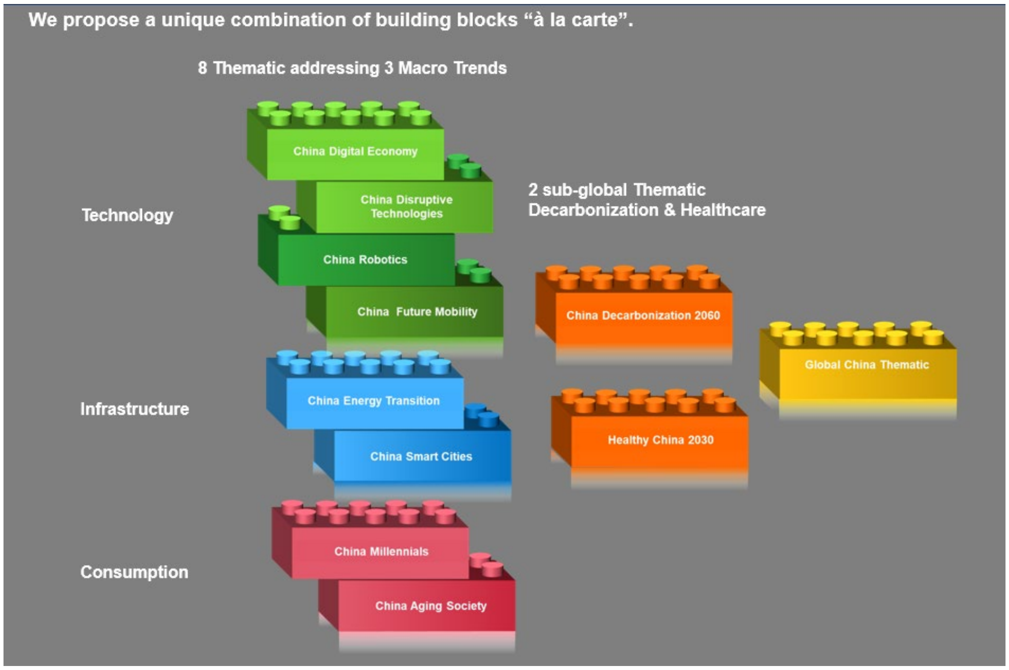
IN YOUR ESTIMATION, WHICH CURRENT OR UPCOMING DEVELOPMENTS WILL HAVE THE BIGGEST EFFECT ON THE DEAL ENVIRONMENT OVER THE COMING 12-18 MONTHS? (RANK THE TOP TWO 1-2, WHERE 1 IS MOST IMPORTANT)



In summary

The year will be complicated. States will increase fiscal and regulatory pressure due to variant waves and inflation.

Overweight in equities and commodities.
For equities.
Overweight in China, mainly via thematic in line with the precepts of the Politburo.



Slight overweighting in the United States. We prefer the theme of infrastructure, centered on the Bide plan.

Beware of the High Dividend Yield theme, which could suffer from a violent acceleration in inflation. Priority should be given to companies that can "guarantee" sufficient positive cash flows, despite increases in procurement and salary costs.

Underweighting in emerging countries unless they benefit from surplus current accounts and the proportion of debt dependent on the dollar remains contained.

Underweighting in Europe, whose 2021 outperformance is quite an anachronism.

On a global level, the themes on 5G (which will benefit from the development of Metaverse) and space will be favored.

Overweight in Private Equity: Focus on Buyout and thematic.

For commodities.
Overweight in agricultural commodities, gold, silver, and uranium.
Underweight in oil

For bonds: Underweight

Underweight in the US Short-duration Govies, and Long-duration in Europe (Govies).

Favor steepeners on the US curve for the second half of the year and strategies to widen the spread between the bond rates of various states now.

Underweight emerging bonds excepted Overweight Chinese bonds (excluding real estate developers, although, after March 2022, this sector will be one to watch).

Don't invest in TIPS, but in Breakeven

Alternative investments:

VIX (tactical only)

Jacques Lemoisson

GATE ADVISORY
GLOBAL ALLOCATION TACTICAL EXPERTIZE

2022 Outlook

12.23.2021

2022 Outlook. *Not to be forwarded. For professionals only. For personal use only!*

Outlook 2021 Disclaimer

None of GATE Publishing LLC (“GATE Publishing”), GATE-IM LLC (“GATE IM”) or GATE Advisory is registered as an investment adviser under the Investment Advisers Act of 1940, as amended (the “Advisers Act”), or the securities laws of any state or other jurisdiction, or in any other regulatory capacity. GATE Publishing is responsible for the opinions and content in Outlook 2021. All opinions expressed by Mr. Lemoisson in or through the document are solely those of Mr. Lemoisson.

The investments and strategies discussed in the Outlook 2021 are impersonalized and do not take into account any reader’s particular investment objectives, financial situation, or needs and are in no way tailored to the specific investment portfolio of any single reader.

The information in the GMI is based on data currently available to Mr. Lemoisson, as well as various expectations, estimates, projections, opinions, and beliefs with respect to future developments, and is subject to change. Neither Mr. Lemoisson, GATE Advisory, nor any other person or entity undertakes or otherwise assumes any obligation to update this information.

The distribution and/or publication of the Outlook 2021 should not be construed by any reader as GATE Advisory’s (i) solicitation to effect or attempt to effect transactions in securities, or (ii) provision of any investment-related advice or services tailored to any individual’s financial situation or investment objective(s). All content is provided for informational purposes only and should not be construed as investment, tax, accounting, or legal advice, as an offer or solicitation of an offer to sell or buy any security, or as an endorsement, recommendation, or sponsorship of any company, security, or fund... In making any investment decision, each subscriber must rely on its own examination of each investment, including the merits and risks involved, and should consult with its investment, legal, tax, accounting, and other advisors and consultants prior to making any investment. Past performance is not a guarantee of future results.

Capital at risk. This content has been prepared for professional investors only. All financial investments involve taking risk which means investors may not get back the amount initially invested.