M|A|M
MONACO ASSET MANAGEMENT

Investment Outlook

Q3 2021

Executive Summary

- **Liquidity remains ample but tightening ahead.** The Fed is cornered. The September 2021 FOMC meeting will be crucial in terms of communication. Striking the right balance between supporting economic growth and announcing prospects of Quantitative Tightening. We believe the Fed will err on the side of caution in the medium-term. This should help push US 10-year bond yields towards our target of 2%.

- **Developed credit markets are at historically high valuations**. The benefit from a continued recovery in economic growth does not compensate for the headwind of rising long-term interest rates. Emerging market credit is the only area left providing real value.

- **The USD is in the midst of a tactical rebound.** Structurally, the USD bear market is still in play longer-term. We expect the EUR/USD to fall to 1.16-1.15 before resuming its uptrend. We increase our exposure to the USD to take advantage of this short-term rally.

- Equities, especially in the US, are at historically high valuations. Yet, **we expect equity markets to remain in an uptrend during the summer months** as economic re-openings compensate concerns about the Fed policy and the spread of the Covid Delta variant. We favour a barbel strategy of value and growth stocks. Should markets remain benign in the summer period, we may look to reduce portfolio risk ahead of the Fed September meeting.

- A short-term rally in the USD could exert **pressure on commodity prices in the short-term**. We look for a 5% correction on Broad Commodities Indices to add back exposure to this asset class. Our over-arching positive view on inflation makes us structurally positive on precious metals.

Investment Stance Overview

Covid vaccinations are plateauing in most developed economies. Pent-up savings are being spent. Economic re-opening are in full throttle. A lot of this classic "recovery" cycle is now behind us. This makes us question, what is next? The time for classic business cycles are long-gone. The global economy should return to its habit of short-term recovery and failures. The question is when is the next failure? This will depend entirely on the spread of the Covid Delta variant and the Fed's intention to reduce liquidity through quantitative tightening. With both equity and credit markets at historically high valuations, the risks are high. Q4 2021 promises to be "exciting" for the lack of a better word. We should exert a maximum level of caution. Until then, we believe risk markets will continue to grind higher this summer. Equity markets could continue to rally driven by large-cap technology stocks as investors turn to "safer" quality. Credit markets will patiently await guidance from the Fed. Yet, underneath the surface, the USD appreciation over the past few weeks cannot go un-noticed. Beside the effect from the hawkish Fed meeting in June, this could also mark a certain return to "safe havens". We look to also increase exposure to the USD in portfolios. As a result, we decided to tactically reduce our Commodities exposure and will carefully watch our investments in Emerging Markets. Overall, the summer months can induce additional complacency from investors. It may provide an opportunity to take a contrarian view and "hedge" portfolios as we approach Q4 2021. We will make sure to update you on any meaningful change in market views.

	Investment Stance						Quarterly Change*
	Very Bearish	Bearish	Neutral	Bullish	Very Bullish		
SOVEREIGN BONDS						**BEARISH DM**	-
US		■					-
Europe (Core)		■					-
Europe (Periphery)		■					-
Emerging Markets				■			-
CORPORATE BONDS						**BEARISH DM**	-
US High Yield		■					-
US Investment Grade		■					-
EUR High Yield		■					-
EUR Investment Grade		■					-
Emerging Markets				■			-
CURRENCY						**BULLISH USD**	-
USD				■			↗
EUR		■					↘
EM			■				↘
JPY		■					↘
GBP			■				-
EQUITIES						**BULLISH**	-
US				■			↗
Europe				■			-
UK				■			↗
Japan				■			-
Emerging Markets				■			-
COMMODITIES						**NEUTRAL**	-
Energy			■				↘
Precious Metals				■			-
Agriculture & Livestock			■				↘
ALTERNATIVES						**BULLISH**	-
Hedge Funds				■			-
Real Estate				■			-
Private Equity				■			-

** Change compared with previous quarter. One arrow means the stance has moved one place to the left or the right, two arrows means a move of two places, etc.*

Model Portfolios

The following model portfolios are based on current positioning at the start of Q3 2021. Considering the volatile nature of financials markets and our outlook, their compositions is likely to change throughout the quarter.

USD Based Portfolios

Asset Class	Last Price	Perf. 5D	Perf. MTD	Perf. YTD	MAM Outlook	Asset Allocation
Currencies						
Portfolio Bases						**100.0%**
EUR	1.19	-0.3%	-2.7%	-2.7%	Bearish	5.0%
USD	92.09	0.3%	2.3%	2.4%	Bullish	95.0%
Equities						**45.0%**
Developped Markets	**67.94**	**-0.1%**	**-1.6%**	**10.2%**	Bullish	**32.0%**
Europe	454.93	0.4%	1.8%	14.0%	Bullish	9.6%
North America	4,291.80	1.1%	2.1%	14.3%	Bullish	17.6%
Great Britain	7,064.94	-0.1%	0.6%	9.4%	Bullish	1.6%
Asia Pacific	28,791.53	-0.3%	-0.2%	4.9%	Bullish	3.2%
Emerging Markets	**1,377.15**	**1.2%**	**0.1%**	**6.7%**	Bullish	**9.0%**
Asia Pacific	764.28	1.0%	0.7%	7.2%	Bullish	5.9%
EMEA	275.72	-0.1%	-0.8%	14.3%	Bullish	2.2%
South America	2,656.48	1.3%	3.8%	8.3%	Bullish	0.9%
Thematic						**4.0%**
Asset Allocation	36.93	0.1%	-1.0%	8.1%	Bullish	4.0%
Fixed Income						**12.0%**
Europe						**0.0%**
Sovereign	221.50	0.0%	0.1%	-1.2%	Bearish	0.0%
Investment Grade	249.99	-0.1%	0.2%	-2.3%	Bearish	0.0%
High Yield	435.04	0.0%	0.6%	3.5%	Bearish	0.0%
North America						**0.0%**
Sovereign/<u>Tips</u>	2,736.36	0.2%	0.9%	-2.1%	Bearish	0.0%
Investment Grade	3,510.69	0.3%	1.5%	-1.4%	Bearish	0.0%
High Yield	2,420.11	0.3%	1.2%	3.5%	Bearish	0.0%
Emerging Markets						**5.6%**
Local Currency	417.23	0.0%	0.8%	-1.5%	Bullish	5.6%
Hard Currency	1,280.51	0.0%	0.7%	-0.6%	Neutral	0.0%
Others						**6.4%**
Convertible	996.26	0.1%	0.6%	3.6%	Bearish	0.0%
Trade Finance	110.29	0.0%	-0.1%	-0.2%	Bearish	0.0%
Broad Funds	541.12	0.0%	-0.8%	-3.2%	Bullish	6.4%
Commodities		**1.0%**	**0.4%**	**19.4%**		**6.0%**
Agriculture	85.38	0.9%	-4.3%	14.3%	Neutral	0.0%
Energy	29.33	1.8%	11.3%	44.4%	Neutral	0.0%
Industrials	156.42	1.7%	-2.9%	17.9%	Neutral	0.0%
Precious Metals	217.94	-1.4%	-7.8%	-6.6%	Bullish	6.0%
Alternatives						**20.0%**
Hedge Funds	1,433.05	0.3%	0.5%	3.8%	Bullish	15.0%
PE/Real Assets	2,034.89	-0.9%	0.1%	14.5%	Bullish	5.0%
Cash						**17.0%**

Source. MAM Research, Bloomberg

EUR Based Portfolios

Asset Class	Last Price	Perf. 5D	Perf. MTD	Perf. YTD	MAM Outlook	Asset Allocation
Currencies						
Portfolio Bases						**100.0%**
EUR	1.19	-0.3%	-2.7%	-2.7%	Bearish	75.0%
USD	92.09	0.3%	2.3%	2.4%	Bullish	25.0%
Equities						**45.0%**
Developped Markets	**67.94**	**-0.1%**	**-1.6%**	**10.2%**	Bullish	**32.0%**
Europe	454.93	0.4%	1.8%	14.0%	Bullish	12.8%
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Cash						**17.0%**

Source. MAM Research, Bloomberg

Asset Class Returns

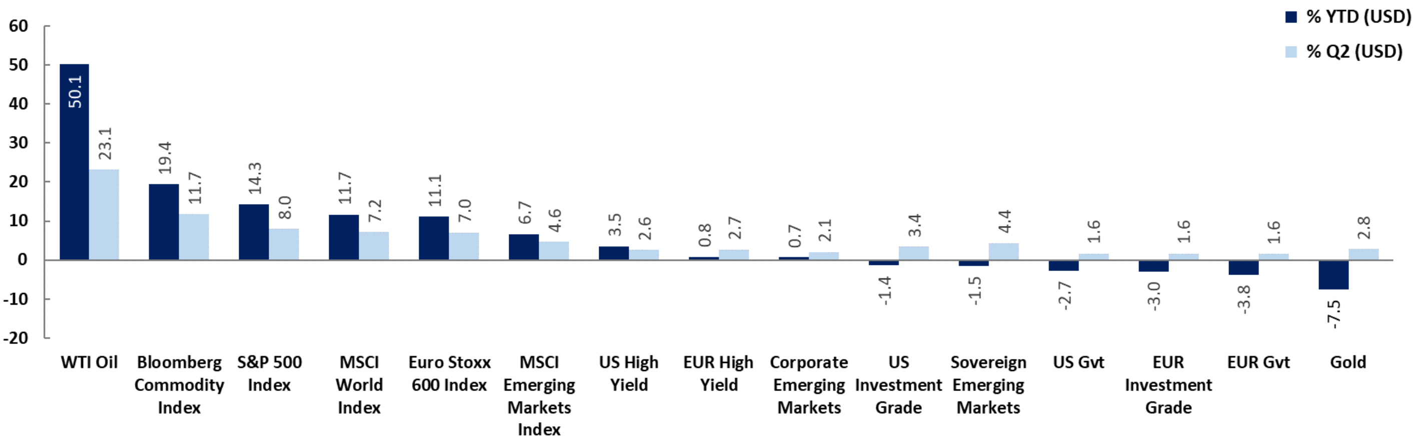
The market was somewhat taken by surprised at the June FOMC meeting when the Fed's dot plot indicated the potential for a first rate hike as early as late next year and the members of the committee agreed the time to start talking about potential tapering is fast approaching as inflation begins to overshoot the initial targets. Nonetheless, the central bank still re-iterated its view that inflation was mostly transitory rather than posing the risk of being more persistent. Ultimately, this send a small shock wave in the market and has been challenging the leadership established at the onset of the quarter over the past couple weeks.

Global equities were up 7.2% in Q2, up 11.7% YTD (in USD-terms). US equities were the best performing region with the S&P 500 index rising as much as 8.0%, up 14.3% YTD (in USD-terms). With cyclicals and value equities suffering from a pullback at the onset of the Fed meeting, European equities gave back some of their earlier gains to close up 5.7% in Q2, up 13.8% YTD (in EUR-terms). Emerging Market equities were a bit more muted up 4.6% in Q2, up 6.7% YTD (in USD-terms). The region's market is impacted by the emergence of new variants that threaten the growth outlook for local economies in light of lower vacations to-date.

Corporate bonds underperformed in the early stages of the quarter before catching a bid after the change in tone at the Fed, which is putting a cap on the potential for runway inflation through the dot plot. While we do not view the Dot Plot as a strong leading indicator for actual rate hikes, it has nonetheless received a lot of attention and contributed to the decline in rates and bond yields. The US Sovereign, US Corporate IG, and US HY indices were up 1.6%, 3.4%, and 2.7% (in USD-terms), respectively.

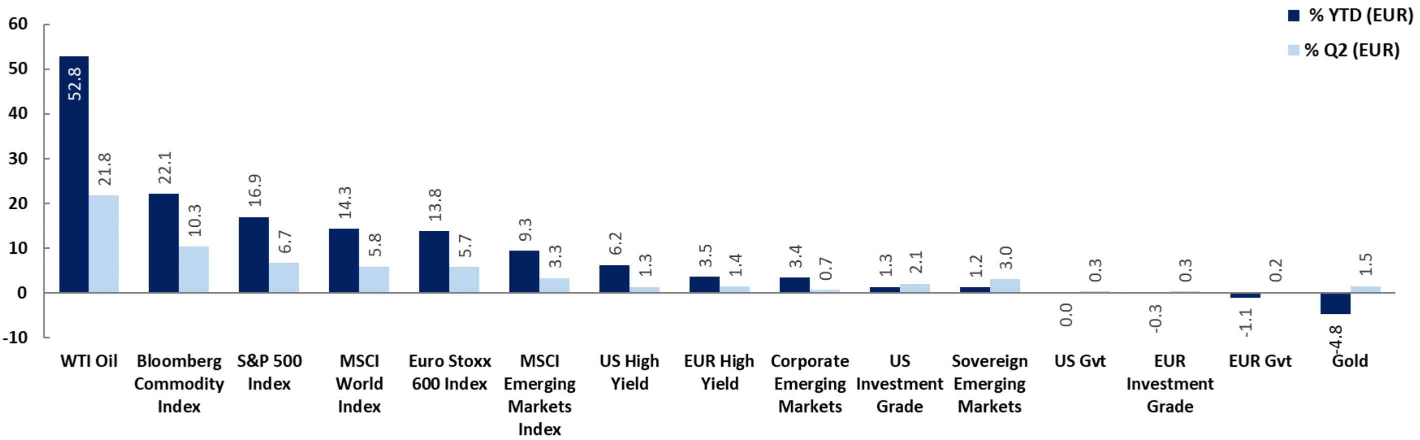
Although the dollar was slightly weaker over the quarter, it caught a bid over the past few weeks, post-FOMC meeting. In turn, this has been a source of headwinds for commodities. Nonetheless, WTI Crude Oil still managed to be up 23.1% in Q2, and up 50.1% YTD. Generally speaking, commodities performed quite well with the broad commodity index up 11.7%. Energy, agriculture, and metal prices performed quite well while precious such as gold, up 2.8%, only gained on the margin as the dollar weakened.

Chart 1. Asset Class Returns Q3 2021 vs. YTD 2021 (USD Base)



Source. MAM Research, Bloomberg.

Chart 2. Asset Class Returns Q3 2021 vs. YTD 2021 (EUR Base)



Source. MAM Research, Bloomberg.

MAM Actions

Equities

What have we done?

We took advantage of strong equity market since the start of the year and bought Put Spreads on US and European indices to protect the performance of portfolios ahead of the May-June period which is historically more volatile. We used the correction in May to close the Long Put leg of the trade and keep the Short Put leg open. We also added the MAM Positive Impact Fund in portfolios as a mean to play the rising capital flight towards ESG strategies. We switched investment vehicle in China to the Quaero China Fund which adds better value and diversification than the instruments previously held. Finally, following the Fed meeting in late June, we added a tactical Long in Nasdaq 100 ETF to increase exposure to the technology sector.

Our strategy going forward?

Equity market exposure is unlikely to change meaningfully in Q3 2021. It is worth mentioning that the September Fed meeting will take place at the end of Q3 2021. It is possible, should markets continue to rise this summer, that we decide to tactically lower exposure or hedge as we approach this event.

Fixed Income

What have we done?

We have kept our underweight credit constant throughout the quarter. We operated some switches by favouring exposure to the BlueBay EM Unconstrained Bond Fund. Within the EM credit universe, we like this fund for its ability to hedge duration and FX at pivotal moments.

Our strategy going forward?

Our underweight credit is unlikely to change at all in Q3 2021.

Commodities

What have we done?

We took advantage of the strong year-to-date performance to take some profit on our Long Commodities exposure. We sold holdings in the iPath Bloomberg Commodities ETF. We also sold 50% of the Silver positions and replaced it with a sale of Put options to profit from higher volatility on this metal.

Our strategy going forward?

We are likely to re-enter our Long positions in the iPath Bloomberg Commodities ETF at $25.3/share (-5%).

Currencies

What have we done?

We have kept FX exposure broadly constant throughout Q2 2021.

Our strategy going forward?

We are likely to increase exposure to the USD in EUR-accounts towards 25% (currently 10%) in order to offset the portfolios' sensitivity to the green-back. Conversely, we will decrease EUR exposure in USD-accounts.

Alternatives

What have we done?

We have increased exposure to pre-IPO opportunities (please see the last section of the Outlook for further details).

Our strategy going forward?

Our hedge funds' exposure is unlikely to change meaningfully over the course of Q3 2021.

Events

US Federal Reserve - What To Expect? September 2021, The Pivot Point

Following the conclusion of its scheduled June meeting, the Fed left policy unchanged - as expected. However, the committee grew more concerned about inflation and opened to a scenario of faster taper as actual inflation data comes in stronger.

In June, the Fed laid the ground work towards tapering its asset purchase program it launched at the start of the Covid-19 pandemic in order to stabilize the US economy. It also issued projections (i.e., Fed Dot Plot) suggesting increased chances for a rate hike as early as next year.

The Fed is currently on track to announce tapering at an upcoming meeting - we continue to think the September meeting is the most likely turning point with the actual tapering beginning early next year. We look for additional details to be released in the minutes of the June meeting. These will give investors a sense of how many members on the committee felt like it was time to have a robust discussion around the size of the balance sheet and the pace of asset purchases.

We expect the committee to have said robust discussion over the summer. More specifically, we see members addressing tapering at the July meeting so by the time the September meeting arrives, investors can be given a full guidance on the central bank's strategy such as when would it start tapering, what conditions must be met to kick it off, what is the magnitude of the tapering, and what period of time can we expect it to stretch over.

Given the uncertainty in the data and more specifically the imbalance between exceptional demand and constrained supply, Chair Powell was not yet ready to discuss the path for hikes. We expect rate hikes to remain a non-core topic in the Fed's communication this summer and solely expect it to progressively gain attention post-September meeting.

Ultimately, the Fed is walking a very tight rope here. Not only does it need to start scaling back stimulus for the next crisis, it needs to prevent an over-tightening that would slow down the economy ahead of a winter season potentially impacted by the pandemic once again. We expect some volatility ahead and post September meeting as a function of positioning adjustments.

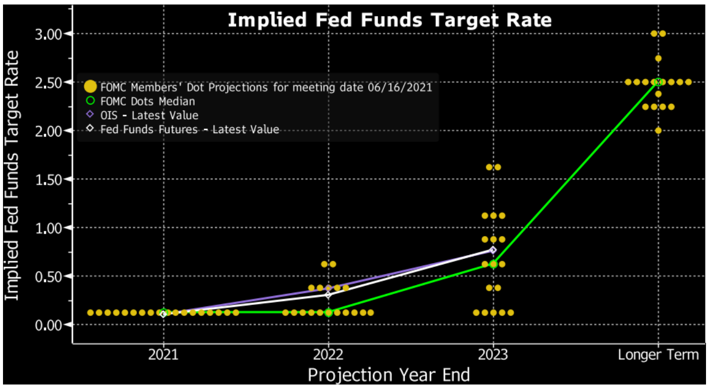
Earlier in the year, Powell suggested the Fed would follow the 2013-2014 tapering playbook. Back then, the central bank talked about tapering in May '13. Seven months later, it announced the begin of the beginning cycle, which kicked off the following month in January '14. The rise in rates did not occur for another two years after the actual tapering, in November '15. This time around, we expect a faster cycle with the Fed talking about tapering at its September '21 meeting, announcing the start of tapering at the December '21 or March '22 meeting, and kicking off the actual taper the following month. Under said scenario, we do not anticipate a rate hike for next year (too fast), but rather for the first half of 2023, or about 18 months after the beginning of the tapering cycle.

Figure 1. Fed Calendar

- July 1 (Est.) | June Meeting Minutes
- Jul. 27-28 | FOMC Meeting
- Aug. 8 (Est.) | July Meeting Minutes
- Aug. 26-28 | Jackson Hole Symposium
- Sept. 21-22 | FOMC Meeting

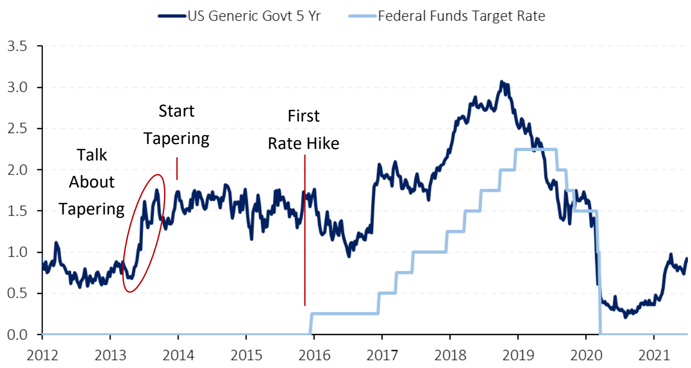
Source. MAM Research

Chart 3. Fed Dot Plot

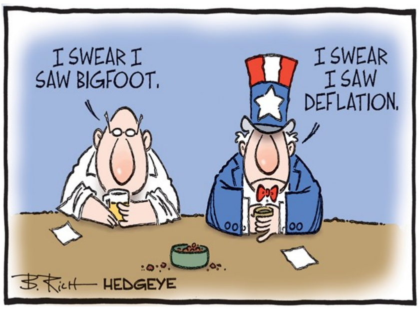


Source. MAM Research, Bloomberg

Chart 4. Last Fed Tapering Cycle (2013-14)



Source. MAM Research, Bloomberg



Economics & Rates

Conclusion. Three Words: Fed, Tapering, and Inflation. The reopening playbook is firmly at play. PMIs have peaked. Savings are being spent. The Fed is tilting more hawkish. Peak liquidity conditions are likely behind us **(Chart 5)**. The economic environment is turning mid-cycle. This is already visible in the bonds market with nominal yields stabilizing around 1.5%. The US Dollar is getting stronger on the back earlier rate hikes expectations. Lastly, certain high risk areas of the market are falling (i.e., lumber, bitcoin). Yet, financial conditions remain extremely loose **(Chart 6)** and accommodative, compensating for a rapidly falling Chinese credit impulse. As per the previous chapter, we currently expect the Fed to announce its tapering plan at the September meeting. The US 10-Year bond yields can break out from current levels and head higher towards 2.0% on a Biden infrastructure plan being voted and signs that inflation is in fine not transitory. Market positioning in US bond futures reverted back to neutral - ready for the next move lower. Arguably, near 2.0%, bond yields would offer an interesting risk-reward asymmetry to trigger a potential buy recommendation.

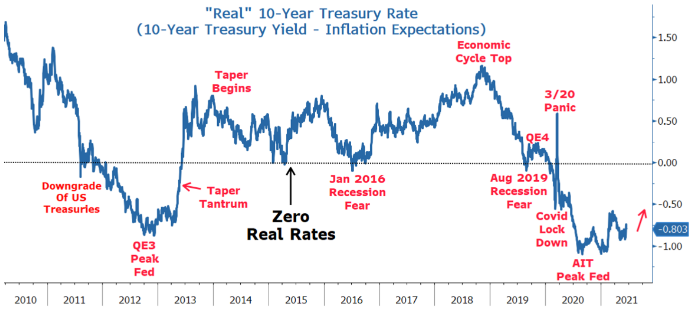
Although the Fed delivered a hawkish surprise at its June meeting - spooking markets along the way - monetary policy will remain fairly accommodative in the foreseeable future, at least relative to market expectations. The Fed dot plot, data driving recent market moves, has been a poor indicator of actual rate hikes - often overestimating how early the central bank actually ends up pulling the trigger rate hikes. We see the year-end 2022 hike as unlikely, implying the tapering cycle will take longer than the market is currently anticipating. In turn, this means the Fed will be letting the economy run hot for longer.

We continue to see inflation as a long-term risk rather than a short-term problem and remain confident it is likely to be more persistent rather than transitory. While we do not exclude some transient factors currently driving headline inflation numbers such as used car sales, we do see a plethora of reasons backing our view that inflation will eventually move persistently higher. Globalization is in retreat. The trade-to-manufacturing output ratio has been flat for over a decade **(Chart 7)**. Looking forward, the ratio could even decline as more companies shift production back home in order to gain greater control over their supply chains. Wage pressures have been fairly contained. However, the labour market tightness raises the prospect of broadening wage pressures. In turn, this draws the attention of companies with transcripts showing acceleration of wage related terms and surge in mentions of "labour shortage". Businesses have already expressed their intentions to raise prices to offset higher wages. Furthermore, investors should begin to scratch the base effect argument out of the transitory inflation thesis. Using Core PCE (Fed's favoured inflation measure), 2-Year annualized inflation is running above the average inflation target at 2.2% **(Chart 8)**.

Evidence we are pulling out of the low growth and low inflation environment lies in inflation and trends in capex growth. As we discussed, inflation should run persistently higher in the coming years. We expect investments to rise above long-term trends. The infrastructure bills set to pass in Washington will contribute to this capex cycle's hotness, taking investment-to-GDP ratios to multiple year highs. Driven by a sharp recovery in global capex, global GDP is set to rise above its pre-pandemic path over the next quarter at a time when excess savings in the US continues to run high which provide an important cushion to growth and inflation as inventories run at historically low levels.

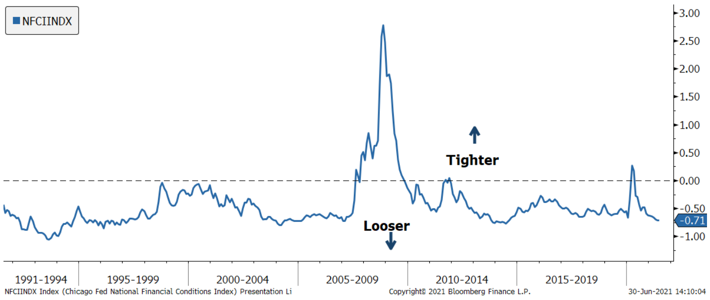
The asymmetry is quite clear here, room for even lower yields is extremely limited. Pushback on the dot plot's rate hike timeline could send nominal yields towards 2.0%, a level at where we could be inclined to buy on a more compelling risk-reward.

Chart 5. We Are Past "Peak Fed" For The Cycle



Source. Bloomberg

Chart 6. US Financial Conditions

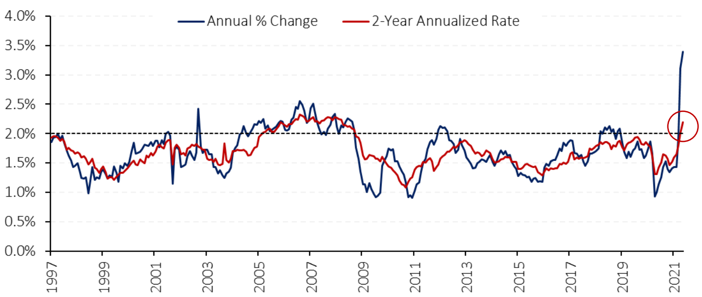


Source. Bureau of Labour Statistics, MAM Research (5-Year Annualized)

Chart 7. Globalization Plateaued A Decade Ago

Source. CPB Netherlands BEPA, World Bank, MAM Research

Chart 8. US Core PCE Inflation



Source. Bloomberg, MAM Research

Credit

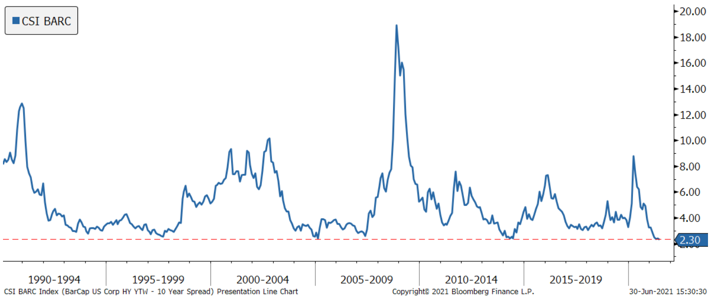
Conclusion. Bearish. Readers of this publication may start to feel that we have been "perma-bears" in credit. Indeed, we have been negative credit markets for some time now. However, this is the environment we have been dreading all along and our aim is to warn investors of the risks credit markets face going forward. The re-opening is now fully priced in by credit markets. The only area of value is Emerging Markets (EM). EM credit has lagged the rally a bit. There are some "challenged" areas such as Argentina and Turkey, but the rest of the universe still looks attractive.

US high yield spreads of 230bps are at 30-year historical lows **(Chart 9)**. Historically, when US high yield spreads are reaching current levels of 230bps, high yield no longer offer compelling returns. In fact, high yield offers negative returns over a 12-months view.

The conclusion on valuation is that the room for error has become razor-thin. The Fed's May financial stability report highlighted that valuations in many markets are now vulnerable to any deterioration in risk appetite. This is a reminder of the importance of expecting the unexpected: that's how markets work. This is also when the skeletons in the closet are exposed.

There is no place to hide in developed markets credit. Growth pickup for EM in the second half of the year, in our view, will be a supportive factor for both FX markets and high-yield credit in EM. EM credit spreads have tightened significantly but are still far off their 2017/2018 lows **(Chart 10)**. In order to play this thematic we invested in the BlueBay EM Unconstrained Bond Fund which so far has managed to weather the changing macro landscape in terms of interest rate and FX risk.

Chart 9. US High Yield Spreads (Monthly)



Source. Bloomberg, MAM Research

Chart 10. EM Corporate Credit Spreads (Weekly)

Source. Bloomberg, MAM Research

Currencies

Conclusion. Tactically Long USD, but remain structurally bearish. Until recently, the main driver of the Euro against the greenback has been the rather late European economic reopening. Fuelling the growth differential argument, but this is now mostly behind us. The focus is now switching back to (1) growth differential in favour of the US economy and (2) yield differential in favour of US rates. Both factors are turning dollar positive in the near term. While there are structural forces at play against the greenback (i.e., debt level, rising inflation), historically, the Fed tightening cycles have mostly been supportive of the dollar. In fact, the relationship is even truer against low yielding currencies such as the Euro. Positioning is still very bearish dollar **(Chart 11)** leaving limited room for further short-USD flow. For the coming months, we recommend increasing US dollar exposure of portfolios to "hedge" part of the allocation that is "playing" a weaker dollar outlook (e.g., precious metals, IO Macro Fund, IO Hypernova Fund, Emerging Markets) and tactically trade the dollar bounce. Technically, the EUR/USD could retest 1.16 (-2.5%) in coming weeks. We would then reassess.

The US dollar gained in the wake of the June Fed meeting while real yields rose. As data remain firm through the summer, Fed speakers and the June minutes confirm the FOMC's progressive trajectory towards tapering asset purchases, and stretched long TIPS positioning unwinds, we expect further US dollar gains.

We are watching a number of factors to evaluate these criteria. (1) Will real money investors - those who have been holding onto their dollar shorts - "throw in the towel"? We see high risk for this to occur with a pullback in short-USD positioning an important factor in amplifying the dollar strength **(Chart 12)**. (2) Fed speakers and US data remain key factors with the potential to amplify or blunt dollar strength. (3) Foreign central banks. If they grow concerned financial conditions are tightening, they may sound more dovish or ease further, amplifying dollar gains.

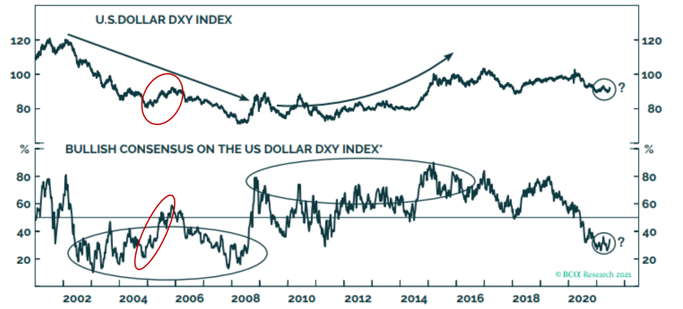
Dynamics for the dollar are very interesting today. The earlier than expected pivot to a relatively more hawkish tone at the Fed sent real yields higher and breakeven rates tighter - closer to zero **(Chart 13)**. If this environment persists for a few months, it implies market expectations for inflation will have moved lower fairly noticeably. A state of the world in which this view is maintained for more than two months is one where market expectations for the Fed are moving more and more hawkish. The longer the market stays in such mindset, the greater the risk it is over estimating just how hawkish the Fed actually is.

Perceived hawkishness would stand more in sharp contrast with the Fed's likely path of policy, particularly once data naturally starts decelerating. At that point, the market would then course correct away from overpricing hawkishness to very potentially overpricing dovishness. That dovish repricing would imply wider breakeven rates and, likely, lower real yields. If this dynamic plays out, we would be observing a regime shift in the autumn.

As such, we are in the midst of a tradable, but finite, USD rally, followed by a tradable correction in the US dollar lower again. Ultimately, this would imply a fairly broad-based dollar range for the next six months, consistent with our medium-term view on the greenback. We will be tactically increasing USD exposure in non-USD accounts to 25%, and reducing to a relatively more conservative 15% exposure after the bounce. Against the Euro, we look to sell USD near 1.15-1.16 (-3.3%/-2.5%) **(Chart 4)**.

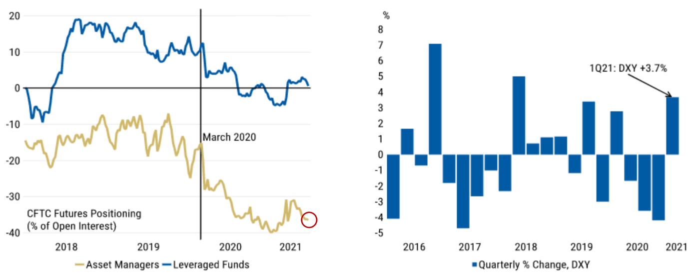
Elsewhere, we are turning more cautious and neutral on EMFX. Higher real rates in the US, a change in risk sentiment amid high short USD positioning, and risks growth differentials to widen between EM and DM as new variants exposure slow vaccination progress makes us more cautious on EM, notably currencies.

Chart 11. Sentiment Can Stay Bearish A While But Bounces Occur



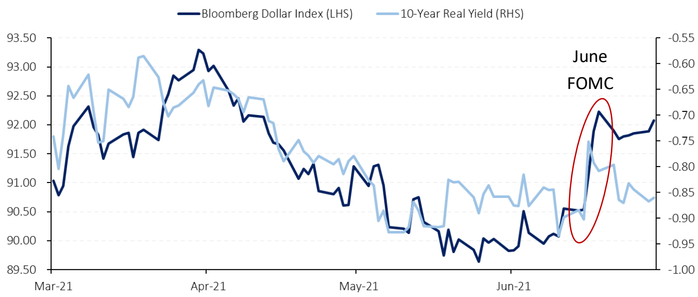
Source. Marketvane.net, BCA Research

Chart 12. Real Money Positioning Is Meaningfully Short Dollar



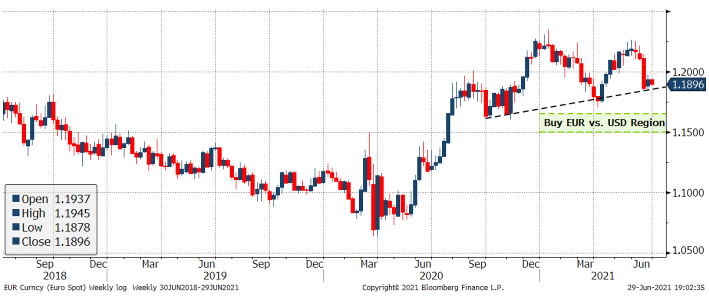
Source. Macrobonds, MS Research

Chart 13. US Dollar Gained As Real Yields Stopped Falling



Source. Bloomberg, MAM Research

Chart 14. EUR vs. USD Spot Exchange Rate (Weekly)



Source. Bloomberg, MAM Research

Equities

Conclusion. Bullish, but adopting a barbell strategy. We see equity markets edging higher over the summer driven by rising participation and lower liquidity. While H1 2021 was all about cyclicals relative to other factors, the outlook for H2 is murkier. We expect a continued cyclical recovery, albeit at a slower pace. Higher US rates into H2 should continue to favour cyclicals notably after the recent price underperformance. However, as markets begin to price a policy mistake by the Fed, that is too aggressive too fast, quality and growth stocks could prevail in coming quarter. As such, we continue to favour the barbell strategy approach of cyclicals and growth. Within growth we continue to like de-rated tech companies and most notably green-tech. Elsewhere, we focus on quality companies who are "growth compounders". Should our view for stronger markets over the summer materialize, we would take the opportunity to tactically reduce exposure or hedge the September Fed event. Over the coming months, we will look to reduce exposure to US small caps and EM - more sensitive to liquidity conditions - and buy quality stock ETF **(Chart 18)**.

The recent run of outperformance in cyclicals is among the best and fastest in history, and has now led their relative prices past pre-pandemic levels. On a market cap-weighted basis valuations rebounded to the 2017-18 level **(Chart 15)** - last period of robust growth. The bounce was about more than recapturing COVID losses. All in all, cyclicals look prime for consolidation. Relative performance has already stalled while the loss in momentum is quite visible. Peak rate of change in macro indicators has also been a key factor to their relative performance.

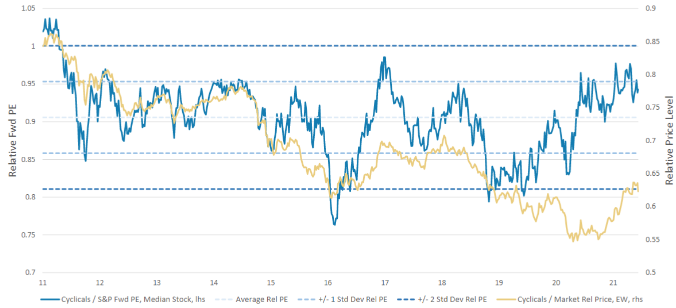
Beyond a deceleration in macro growth, valuations and earnings revisions now favour a more selective approach to cyclicals. The multiples of cyclicals tend to appreciate relative to the market in two ways: (1) excitement over better growth prospect or (2) high multiples being applied to trough earnings as the market extrapolates long-term recovery and normalization. In recent history, the former was true in the 2017-18 period while the latter was directly applicable in mid-2020. Albeit slightly off recent peaks, current above average multiples are clearly more a function of the "better growth" regime. While we are positive on growth, we are growing wary of expectations and watch for a potential payback of demand pulled forward.

We think the growth narrative is well understood by the market, hence the risks are more likely to the downside rather than the upside as the huge surge in retail spending in the past quarters potentially undermines the degree to which pent up demand is embedded in expectations. As mentioned above, we may be set for a payback which is truer in some sectors than others - Autos **(Chart 16)**, Sporting Goods, and Building Products. At the same time, it is interesting to read the number of corporate transcript mentions of a demand pull forward have picked up significantly in recent quarters and still remain quite elevated **(Chart 17)**.

As the room for cyclical outperformance is somewhat limited, we prefer to continue to adopt a barbell strategy of cyclical and growth with a selective overlay meaning we look for companies higher up the quality curve. With the risk premiums needing to discount higher real rates and slowing monetary policy support we prefer lower beta, higher liquidity, and quality firms that can deliver on expectations. Health Care is looking fairly attractive. We will look to tactically hedge or reduce exposure closer to the September Fed event when we think volatility could surge.

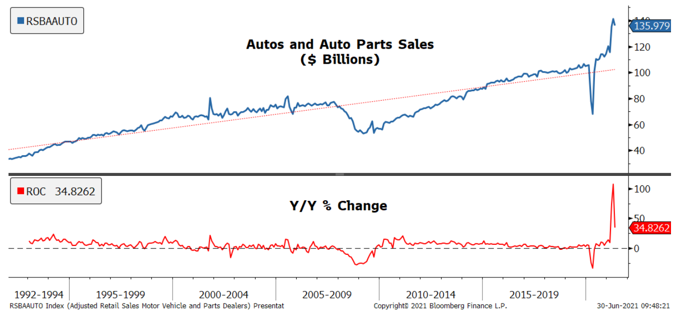
Risks for growth differentials to widen between EM and DM as new variants exposure slower vaccination paired with a stronger dollar and a dimmer short-term commodity - notably metals– outlook is likely to weigh on EM equities in the near-term.

Chart 15. Cyclicals Relative Valuation Likely Capped For Now



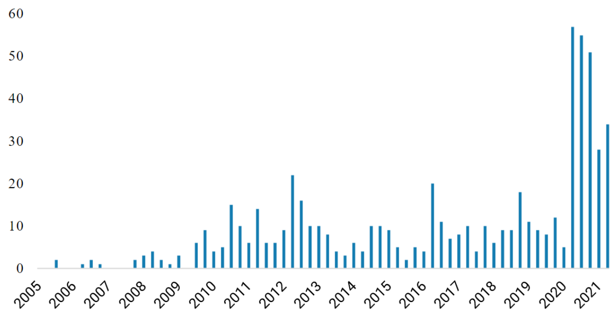
Source. Factset, MS Research

Chart 16. Autos Look Ripe For Payback



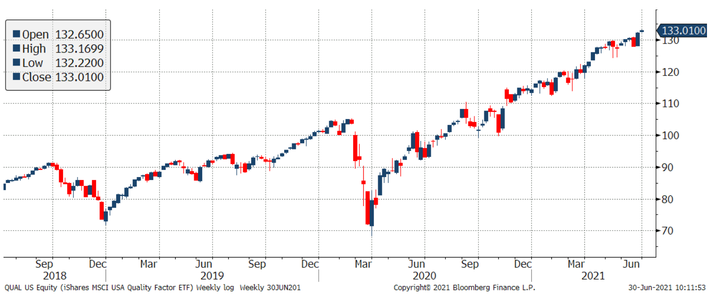
Source. Bloomberg, MAM Research

Chart 17. Transcripts Mentions of a Demand Pull Forward



Source. Alphasense, MS Research

Chart 18. iShares MSCI Quality Factor ETF (Weekly)



Source. MAM Research, Bloomberg

Commodities

Conclusion. Tactically Neutral. We keep a structurally bullish outlook on the asset class. However, in the short-term, the trajectory of a stronger US Dollar is likely to put a cap on performance in the coming weeks. Recently, we decided to reduce commodity exposure and tactically take profit. We maintained exposure to precious metals relatively constant considering the sector moved up less than the energy, metal, and agriculture commodities **(Chart 19)**. The exposure to precious metals also provides some degree of exposure to the asset class should either our profit taking view be wrong or the dollar does not benefit from a tactical rebound but instead weakens further. In the coming months, we will look to add back to commodities in a -5.0% correction **(Chart 20)** . Commodities are highly correlated with inflation. From an allocation perspective, the asset class provides one of the best hedges against near-term realized inflation and stagflation risks. Many commodities today such as energy, metals, and agriculture are trading in backwardation and valuations are reasonable. Positive roll-yield is an added tailwind that should continue to attract longer-term investor interest.

Uncertainty abounds on both supply and demand sides for oil, which should cause OPEC+ to approach supply hikes cautiously. Global oil demand is not out of the woods yet, and its continued recovery hinges on the pace of vaccination around the world as well as the ability to contain future outbreaks. OPEC+ is closely watching several metrics, including petroleum inventories which it aims to keep close to 2015-19 average level. In the meantime, there is insufficient capex spent on upstream. OPEC+ has been very effective in tightening global oil balances. The recent ramp up in refining activity in the US paired with depressed domestic production created a bid for oil. Paired with backwardation, this makes 2022 crude look cheap and we look to add on pullbacks.

Industrial metals important in future technologies are critical for the decarbonization of the global economy. Many mined metals are used in renewables or electric vehicles (EV). An EV has more than twice the amount of copper than an internal combustion engine (ICE), and it is heavily used in EV infrastructure. Copper prices could rise to 600c/lbs **(Chart 21)**. Against this backdrop, decarbonization effectively means a new ecosystem has to be built out, ranging from renewable power generation to energy storage and usage. Trading houses are increasingly focusing on metals. Copper, nickel, and cobalt stand out. We also highlight platinum-group metals (PGMs). PGMs were among the first to tackle emissions of ICEs. Miners expect PGMs to stay important since they play an essential role in the hydrogen economy.

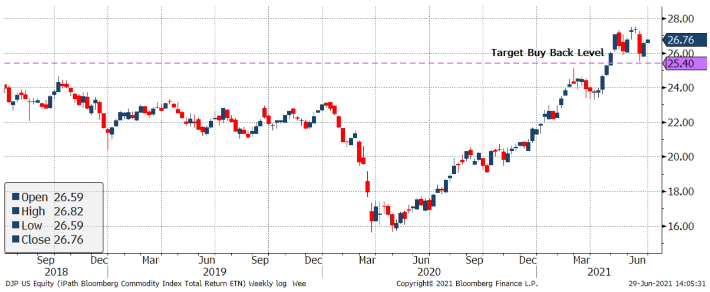
The rally in corn and soybean prices was led by supply and exports, and China's appetite for US corn should stay elevated. Chinese imports of corn have been enormous **(Chart 22)**, exceeding import volumes from any other year in recent history. While demand was coming from restocking efforts and a food security program, flows should stay strong going forward. China has been rebuilding its hog population following a devastating brush with the African Swine Flu (ASF). While it kept pork prices in China elevated for most of 2020 before collapsing in 2021 on concerns of a glut, China's hog population may be just 90% of its pre-ASF levels. As such, more rebuilding is possible. Paired with lower US production estimates and tighter global balances for corn with a poor South American crop, agriculture commodity prices should find support and remain elevated into 2021-22.

In coming years, markets will appreciate the supply constraints in place. Not only is there potential for prices to rise further on the back of strong fundamentals, but there are now early signs of cost inflation, not seen for more than a decade, which will allow for enduring price increases over the medium term.

Chart 19. Relative Perf. Of Precious to Non-Precious Commodities

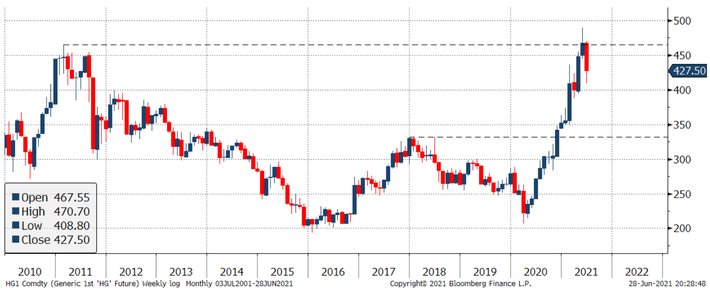
Source. Bloomberg, MAM Research

Chart 20. Broad Commodity ETF (Ticker: DJP US // Weekly)



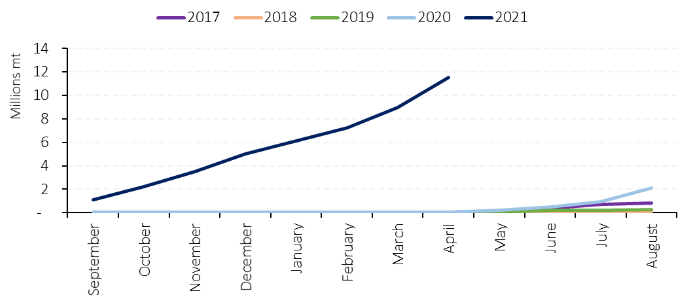
Source. BofA Research

Chart 21. Copper Continues Futures Prices (Monthly)



Source. Bloomberg, MAM Research

Chart 22. Cumulative US Corn Exports to China by Marketing Year



Source. USDA, MAM Research

Pre-IPO Investments

Conclusion. Bullish. We have been investing in pre-IPO opportunities since mid-2020 with a special focus on high growth disrupting companies. The rational is that listed technology companies are trading at record high valuations. Buying similar companies in the pre-IPO stage allows us to take advantage of a significant discount based on (1) illiquidity and (2) buying the stock 1-year before IPO, on average. Some of the earlier successes such as Palantir and QuantumScape have proven to be some quite profitable investments. We will continue to invest selectively in pre-IPO opportunities. In fact, we are in the process of planning a pre-IPO fund in Q4 2021 to reduce the administrative burden and cost from a client and asset manager perspective.

Please find below a brief update on some of the recent pre-IPO investments **(Table 1)**.

Table 1. MAM Pre-IPO/Early Stage Investments

Company Name	Industry	Transaction Type	Transaction Date	Transaction Price	Liquidty Event Type	Event Date	Current Price	Performance (ITD)	Gross MOIC
Palantir	Software	Pre-IPO	3-Mar-2020	4.65	IPO (Direct Listing)	24-Sep-2020	27.38	488.8%	5.9x
QuantumScape	Auto Parts	Pre-IPO	18-Aug-2020	6.57	SPAC Merger	30-Nov-2020	30.86	369.7%	4.7x
Company 1	Materials	Conv. Note	25-Sep-2020	3.82	-	-	-	-	-
Company 2	Digital Marketing	Pre-IPO	1-Nov-2020	3.91	-	-	-	-	-
UiPath	Software	Pre-IPO	18-Dec-2020	44.45	IPO (Direct Listing)	20-Apr-2021	71.28	60.4%	1.6x
Company 3	Software	Pre-IPO	10-Mar-2021	13.00	-	-	-	-	-
Company 4	Biotechnology	Early Stage	2-Apr-2021	10.00	-	-	-	-	-
Company 5	Software	Pre-IPO	7-May-2021	10.00	-	-	-	-	-
Company 6	Software	Early Stage	3-Jun-2021	10.00	-	-	-	-	-
Company 7	Food & Beverage	Early Stage	15-Jun-2021	10.00	-	-	-	-	-

Source. MAM Research

We consider the Palantir investment to be "realised" since IPO has happened and we have received the listed shares. This is partially the case also with QuantumScape as the listing has now occurred and we received 20% of the shares we subscribed for. We will be receiving the remaining 80% of the shares early Q1 2022. Palantir and QuantumScape are two companies that we fundamentally like. As such, our strategy is to hold the shares and use options (i.e., sale of Calls) to earn a premium and continuously improve the profit profile of the investment.

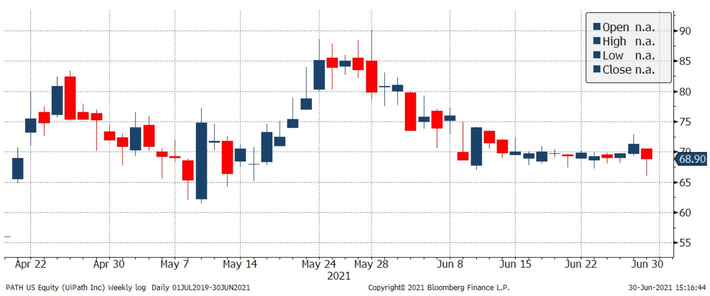
The latest portfolio company to list was UiPath. We invested in UiPath in December 2020. The company executed its IPO only four months later, in April 2021. While we invested at a high multiple, we knew the market would reward such a high growth software automation company with even higher multiples. We bought the shares at $44.45/share. The IPO priced at $56/share and the stock is currently trading at $68.9/share **(Chart 23)**. We will receive the listed shares 3 business days after publication of Q2 earnings, therefore on the 14th of October 2021. This means that this pre-IPO investment would have been "realized" in just under one year. While this is a template of our pre-IPO strategy, we are fully aware that market listing is management and market conditions dependent.

The portfolio company on which we recently had news is Company 2. Company 2 is a "brandtech" firm using technology to create marketing better, faster and cheaper for global clients.

The company is doing very well business wise as corporates realize the need to modernize their online footprint. Company 2 is contemplating an IPO in Q1 2022, meaning distribution of listed shares could occur sometime in Q3 2022. Should this happen, the investment would "realize" in just under two years which is what we anticipated. The IPO valuation discussed is compelling and would suggest very good returns for this investment also. However, market conditions need to remain healthy until then.

We hope to hear very soon from Company 3 and Company 5, two companies for which we expect an IPO late 2021 or early 2022. We will continue to keep you updated on developments in this area with hopefully some news on portfolio companies and new additions as well.

Chart 23. UiPath Spot Price (Daily)



Source. Bloomberg, MAM Research

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