Market Update – December 2023

Where do we go from here?

"In the summer of 1950, the physicist Enrico Fermi and some colleagues at the Los Alamos Lab in New Mexico were walking to lunch, and casually discussing flying saucers - when Fermi blurted out "But where is everybody?" In a galaxy assumed to be filled with clever beings, why don't we see any? This dissonance is known as the Fermi Paradox.

We are seeing the same dissonance in US – "Where is the recession". Heuristically, we seem to be heading towards it (curve inversion etc.), but data inconsistencies are not helping this theme. As they say, absence of evidence is not evidence of absence, so I would like to stick to the recession around the corner theme.

I thought it appropriate to adumbrate some themes for 2024, more of a blue sky thinking. I will start with my favourite.

USDJPY: Japanese latest job's data suggests that hiring may be losing vigour. However, there exists a possibility of strong pay hikes in the upcoming spring wage talks (shunto). So, from my perspective, we could see a shift in yield-curve control and negative rates around mid Q2 2024, though you will see BoJ making enough noises and preparing the market before the actual move. If you link this with a possible climb down in US rates, then the stage is set for a reversion of the widening interest differentials. In short, 2024 could be the year of yen- probably heading towards 125.

DXY Index: Last year saw a lot of debate on de-dollarisation but that's probably a decade story though there are enough signs concerning the direction of travel. This does not change the facts about the decline for the year. We could expect USD index to likely head towards 90, driven primarily by a reversion in widening rate differentials and probable recession in the US. It is estimated that DXY moves 0.4% for every 10 bps move in the US two-year yields. We believe that the best way to play this trade is to be long Asian currencies against USD, with special emphasis on yen.

Rates: It would be hazardous to guess the timing of a rate cut but I am inclined to believe that we would see 75 bps cut in 2024. This would probably be followed up by another 75 bps cut in 2025. I am inclined to take a similar view on Eurozone, a 75 bps cut for 2024. At some point in time, the FED may have to dial down on balance sheet normalisation, else the volatility on SOFR may become unmanageable (RRP is also dropping significantly).

S&P: The darling of 2023 is probably going to see flat returns for 2024, if not negative. My view is that it has been priced to perfection at current levels. If we assume a growth 5%-7% over current earnings (considering US nominal growth) and index continues at current P/E, then from an index point of view, we probably have to adjust lower. If exit is not an option, then the obvious choice would be long the magnificent seven and pharmaceuticals.

Chinese Equity: I personally don't see any dramatic action from the Chinese on the economic front, which means Chinese equity would continue to remain cheaper with no meaningful upside, other than a few rallies driven by bargain hunting. The PBOC is clear about a cross-cyclical approach to the economy, taking action sooner in smaller steps over a longer time frame. This sounds good, but this would not work with an economy that is in a comatose state. In essence, 2024 could again be a muted year for equities. There are better markets to tread, so its fine to shun till we see fiscal measures to support growth. Personally, I have given up on their GDP targets, they don't mean anything, till the property sector is fixed.

Credit: I am of the considered opinion that the rally in fixed income assets is not over yet. It is better to seek safety in Investment Grade assets and duration would be a good ally to have. It is better to avoid credits in the single B rating space and give a wide berth to a lot of sovereigns in that space. There are, however, countries that could offer asymmetric upside rewards to risk taken. My list would include Venezuela, Argentina, and Sri Lanka.

Oil: Surprisingly, I have a very negative view on oil. Considering OPEC's ability to manage supply and the ongoing issue in the Red Sea, Oil ideally should be well bid, however price action indicates otherwise. With the prospect of a slowing global economy and increased production from the US, the downside seems more imminent. I am inclined to believe that we will head towards USD 55 per barrel from current prices. With China front-loading its oil import quotas for 2024, the expected price rise has been muted.

Some known unknowns

1. If there is a prolonged impact concerning Bab-El-Mandeb, then shipping is going to get expensive (re-routing around Cape of Good Hope and increased insurance costs) thus adding to inflationary pressures.
2. Taiwanese election outcome and China's response will have impact on regional tensions. This may have an impact on the semiconductor industry as well.
3. US Government shutdown looming in the month of January, and could this be a harbinger of the so-called recession?

Fund Positioning & Deployment Strategy

Data as of end December 2023

Aditum Global Sukuk Fund

The Fund continues to hold the existing duration positions with the cash component slightly increased. We may consider reducing the current duration just below 6 years, over the next few weeks. The WARF continues to straddle BBB-, with a possibility of a crossover strategy in the ratings space. We envisage maintaining a focussed approach in the Fund, keeping the number of holdings between 25-30.

	1M	3M	6M	1YR	S.I.*
Global Sukuk Fund	3.74	6.49	4.41	6.33	2.88
Sukuk Peer Group*	2.46	(0.15)	(0.33)	0.58	(5.62)

Past performance is not an indicator or guarantee of future performance. The value of shares in the fund and income received from it can go down as well as up, and investors may not get back the full amount invested. Performance may also be affected by currency fluctuations of the underlying holdings. *Peer group data source based on available data for liquid global sukuk funds managed out of the Middle East: FE Analytics, equally weighted against each constituent (USD share class).
*The performance data shown is for the duration of the Global Sukuk Fund I(acc) USD share class which commenced its investment program on 16 November 2020. Source: Bloomberg and Aditum Investment Management Limited, USD terms, bid to bid, income reinvested.

KEY METRICS	
Fund Size (US$m)*	83.34
Number of Holdings	30
Weighted Ave. Yield to Maturity*	5.88%
Weighted Ave. Modified Duration*	6.60
Weighted Ave. Credit Rating – Perps at Parent level*	BBB-
Weighted Ave. Credit Rating (best of 3)	BBB-
Weighted Ave. Credit Rating (worst of 3)	BBB-

*Metrics calculated excluding cash, Weighted Ave. Credit Ratings are based on the Best and Worst ratings from Fitch, Moody's and S&P

Aditum Global Alpha Fund

The Fund continues to stand pat on duration, however we may look to pare it down a couple of years over the next few weeks. We do not expect the credit composition to be altered and WARF will continue to hug the IG space. We continue to assume a focussed approach on the credit universe considered for the exposures.

	1M	3M	6M	1YR	S.I.
Global Alpha Fund	6.11	11.03	5.63	-	7.14

Past performance is not an indicator or guarantee of future performance. The value of shares in the fund and income received from it can go down as well as up, and investors may not get
*The performance data shown is for the duration of the Global Alpha Fund I(acc) USD share class which commenced its investment program on 8 March 2023. Source: Bloomberg and Aditum Investment Management Limited, USD terms, bid to bid, income reinvested.

KEY METRICS	
Fund Size (US$m)*	32.33
Number of Holdings	36
Weighted Ave. Yield to Maturity*	6.21%
Weighted Ave. Modified Duration*	10.4
Weighted Ave. Credit Rating (Worst of 3)	BBB
Weighted Ave. Credit Rating (Best of 3)	BBB+

*Metrics calculated excluding cash, Weighted Ave. Credit Ratings are based on the Best and Worst ratings from Fitch, Moody's and S&P

Aditum Target Maturity Fund 2025

Fund continues to hold a WARF of BB+ and we do not see a dramatic change in the rating stance. The leverage drawdown is close to the permissible limit and may continue to remain so.

	1M*	2M	3M	6M	1YR	S.I.	Dividends SI*
ATMF 25	4.00	7.65	4.07	2.50	3.55	(29.55)	20.00

*The performance is calculated from B(inc) USD share class since inception 14 June 2021.
Past performance is not an indicator or guarantee of futre performance. The value of shares in the fund and income received from it can go down as well as up, and investors may not get back the full amount invested. Performance may also be affected by currency fluctuations of the underlying holdings.

KEY METRICS	
Fund Size (US$m)*	71.91
Number of Holdings	46
Weighted Ave. Yield to Maturity**	7.45%
Weighted Ave. Modified Duration	1.8
Weighted Ave. Credit Rating (Worst of 3)*	BB+
Weighted Ave. Credit Rating (Best of 3)*	BB+

*Including leverage
**Unlevered

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