It´s All About Asset Allocation

July 2023, Newsletter#85

I am glad to announce that in the last Lipper Ratings update, our **fLAB fUNDS in USD and SGD have been awarded with the highest ranking (5) for Total Return**, reflecting our great historic total return performance relative to peers in our SGD and USD share classes. I remind you fLAB Core and Satellite are in the MAS List of Restricted Schemes for Accredited Investors.

LIPPER LEADERS

About Lipper >>

Fund Lookup Results

Highest 5 4 3 2 1 Lowest

Back to Fund Lookup

Fund Name	Fund Company	Asset Type	Classification	Total Return	Consistent Return	Preservation	Expense
fLAB fUNDS Sicav - fLAB Core H SGD	Link Fund Solutions Luxembourg SA	Mixed Assets	Mixed Asset EUR Flex - Global	5	5	2	3
fLAB fUNDS Sicav - fLAB Core H USD	Link Fund Solutions Luxembourg SA	Mixed Assets	Mixed Asset EUR Flex - Global	5	4	3	3
fLAB fUNDS Sicav - fLAB Satellite H USD	Link Fund Solutions Luxembourg SA	Mixed Assets	Absolute Return EUR Low	5	4	4	3

What an incredible first half! The global equity markets against most odds, **climbed a wall of worry defying all the fears that have plagued investors during this time**, especially among those most reluctant. It has to be recognized there were plenty of them: In January, they said the economy was about to fall into recession. In February, inflation was not going to decline fast enough. In March, the banking system was going to collapse. In April, the Fed was going to tighten too much. In May, the rally was too narrow and in June, hawks in circles again (maybe they never left…). As long as bears remained plentiful, the market was able to continue to rise. In spite of, or perhaps because of the pessimism, the market staged one of its best first halves on record. The S&P 500 jumped 15.9%, the best since 2019 and second best this century. The quick recovery from the regional banking crisis brought skeptics off the sidelines. The artificial intelligence fever emulating Buzz Lightyear "To Infinity and Beyond" and FOMO (Fear Of Missing Out) did the rest.

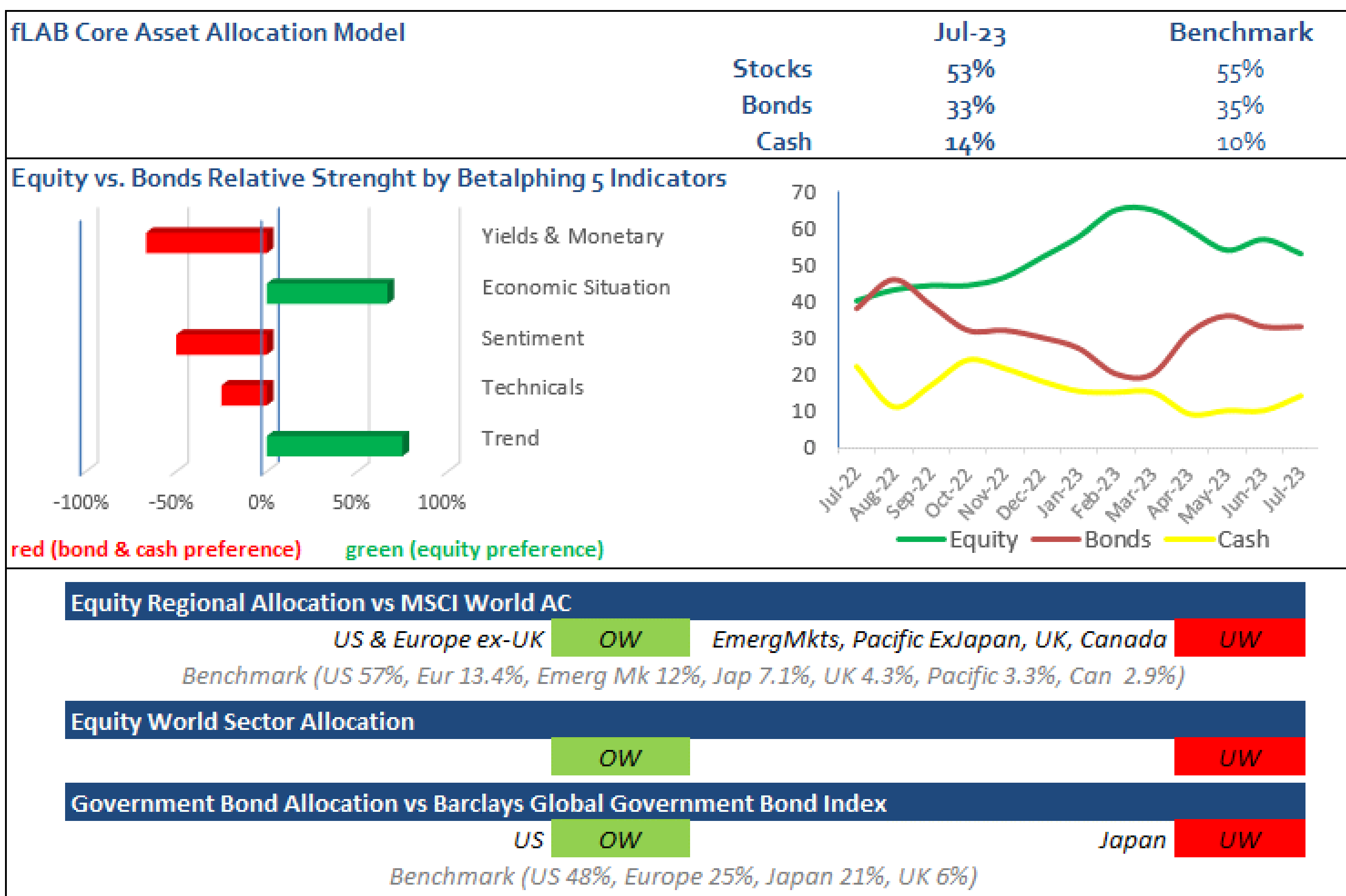
What does a strong first half mean for the second half? **More often than not, positive momentum continues**. Historical data show that when the S&P 500 rose at least 10% over the first six months, over the following six months, the index has risen 75% of the time by a median of 9.7%. One can also fear, can there be too much of a good thing? History suggests yes, but 2023 has not fit the bill. In the four cases the S&P 500 rose more than 20% in the first half, the index fell every time in the second half by median of 6.5%.

Equity markets will have to deal with several challenges ahead. The world economy not only has

shown notable resilience but has even seen its economic momentum accelerating in 1H. **However, the ability to keep this pace will be more arduous in the second half**. Businesses and households will continue to face tighter credit conditions in the U.S. and Europe as the impact of the past year's tight monetary policy continues to slowly work its way into the global economy. Not to mention, that for the first time since before the financial crisis, cash is a reasonable alternative to equities. The S&P 500 GAAP earnings yield is below the T-bill yield for the first time since 2001. Earnings growth may need to accelerate more than analysts are suggesting for investors to justify reallocating into equities. A few days to kick off the second quarter earnings season, it should be noted that earnings expectations for Q2-Q4 are higher than for Q1. So even if earnings growth continue to recover, the market may not be as pleasantly surprised. **Finally, we have to talk about sentiment.** Excessive optimism has been achieved in both, short and intermediate-term indicators (the latter for the first time since January 2022). When this happens at the same time, it leaves the market vulnerable to a pullback. An eventual cyclical top might be premature to us: it rarely comes when sentiment barely reaches the optimism zone. Instead, sentiment composites should remain in excessive optimism in the face of bad news as a sign that the market has reached the top of the wall of worry.

Our Global Flexible Fund, fLAB Core H-USD, has appreciated 1.49% in June, posting an outstanding return of 6.68% YTD.

In July, our Asset Allocation model reduces equities slightly (-4%) in favor of cash (+4%). Excessive optimism and attractive yields, both in absolute (global yield curve) and relative terms (corporate yield vs earnings yield) restrain a major allocation into stocks at this time.



fLAB Core Asset Allocation Model	Jul-23	Benchmark
Stocks	53%	55%
Bonds	33%	35%
Cash	14%	10%

Equity Regional Allocation vs MSCI World AC

US & Europe ex-UK	*OW*	*EmergMkts, Pacific ExJapan, UK, Canada*	*UW*

Benchmark (US 57%, Eur 13.4%, Emerg Mk 12%, Jap 7.1%, UK 4.3%, Pacific 3.3%, Can 2.9%)

Equity World Sector Allocation

	OW		*UW*

Government Bond Allocation vs Barclays Global Government Bond Index

US	*OW*	*Japan*	*UW*

Benchmark (US 48%, Europe 25%, Japan 21%, UK 6%)

The MSCI ACWI jumped 12.89% (in local currency terms) in the first half. Japan and the U.S. led the global market advance, Europe gave back some of its relative strength from Q1 and China & Hong Kong dragged down Pacific and Emerging Markets benchmarks. Mega-cap tech stocks lifted the U.S. over international, Growth over Value, and large over small. Most of the S&P 500's gains in the first half have been driven by just a handful of the index's largest constituents. From a

sector perspective, **this has been the most lopsided start to a bull market on record as participation in the rally had mostly been limited to Growth sectors**. Breadth has started to broaden in June, which is very positive for the continuation of the rally in the coming months, but its improvement has not been accompanied by a decisive rotation in leadership, at least not yet. Defensive sectors have had a historically bad start and are extremely oversold. Mean reversion, a moderation in S&P 500 momentum, the Fed tightening cycle, and a deteriorating economic outlook could contribute to a defensive sector resurgence in the 2H but so far, this is not the case. That, combined with exigent valuations by the companies that have led the rebound has carried us to adopt a neutral sector positioning for the summer, still keeping our geographical bets.

In Government bonds, we sustain a constructive view for the second half although we believe the main markets will likely to be choppy. Short-term yields are being pushed up by continued tightening by central banks in the developed markets. Longer-term yields are being pulled down by slower growth and cooling inflation expected later this year. **As a result, yield curves remain deeply inverted.** Technically, the March peaks are significant in this battle. We would be surprised to see the US 10-year Treasury hold above the recently smashed 4.00% for very long, confirmed by German 10-year yields above 2.75. These levels should provide an upward cap to global yields. Otherwise, we would tactically adjust the duration. But lingering inflation and hawkish central banks mean bonds can remain under pressure. **Rising fears of a recession later this year may see equity investors eager to book profits and use bonds to preserve gains leading to Treasuries** breaking out of their range. Until then, a hawkish Fed will likely continue to suppress sentiment. We enter summer keeping our fixed income exposure at 33% and its duration at 10.23 (3.45 for the overall fund), especially after the last bounce of yields and the extreme optimism in equities.

Our Relative Return Fund, fLAB Satellite H-USD, which has been flat over the past month, is accumulating 1.99% YTD.

The compartment is investing 51% in a low risk, low duration diversified fixed income portfolio plus 22% in some uncorrelated and tactical positions, being the rest in cash. In June, the fund has benefited from the good path of our equity multistrategy allocation (14%), aligned with the good results of the global equity benchmark. In a risk-on framework, gold (4% exposure) has continued its correction while global commodities have finally rebounded (+2,59% Longer Dated All Commodities ETF).
The Fund, which has a duration of 2.17 years, has not been immune to the widespread rebound in bond yields and weak bond performance (public and corporate) over the past two months. Credit hold up relatively better this year than safety debt as it has taken longer for economies to respond to central bank tightening cycles. But recession risk can’t be rule out. For the time being, we keep bond portfolio duration at 4.25 and continue to lean defensive within credit. We will remain flexible in terms of risk exposure and duration, trying to take advantage of the opportunities arising from an uncertain framework, given investor’s changing interest rate expectations.