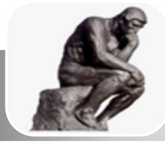
NEW DIMENSIONS CAPITAL

MONTHLY BULLETIN April 2023

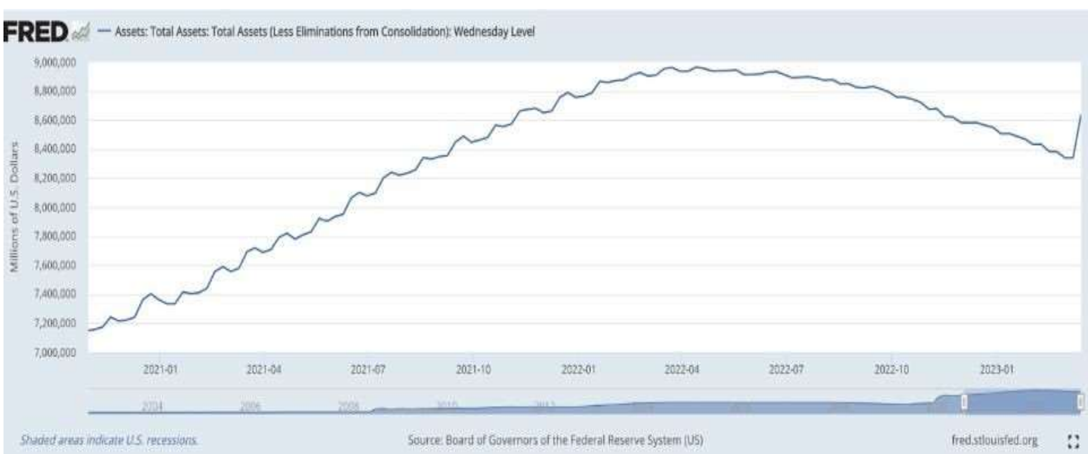


Thought of the Month

The third month of 2023 was not less exciting than February, with the following three themes driving markets and, consequently, our investment strategy and portfolios' performance.

1 – An unravelling collision between banking sector and inflation.

Inflation has become a ubiquitous buzzword, with the U.S. consumer price index at 6% YoY in February. The rapid increase in interest rates has led to the failure of three U.S. banks - Silicon Valley Bank, Silvergate, and Signature Bank and of course the end of an era for 166-year-old Swiss bank Credit Suisse, which was purchased by UBS for $3.2b. After a year of downsizing its assets, the Fed expanded its balance sheet by nearly $300 billion last week (refer to chart below).



If banking stresses persist or accelerate, that would have a deflationary effect on the economy, making rate hikes less urgent. If banking issues fade, however, the Fed would be under more pressure to increase rates to combat inflation. With this backdrop in mind, the Fed increased rates by 25 basis points last Wednesday and indicated that, while the Fed aspires for another hike in their dot plot forecast this year, disinflationary events will require continual monitoring ad expectations are building towards a persistent high-level of inflation.

Wharton Professor Jeremy Siegel said that "Fed sees the impact of SVB's failure to be equivalent to a rate hike of 25 basis points, though it's likely double or triple that amount". The probability to stabilize the banking system and tame inflation at the same time is very low.

Markets are pricing in a 62% chance the Fed will decide to keep interest rates at the same level at their next policy meeting, with a 51% chance of 25-basis-point rate cut in July, according to the CME FedWatch tool.

2 – Property markets are showing signs of distress, especially Commercial Real Estate (CRE)

Renewed stress in the banking sector has focused attention on the balance sheets of regional banks, or more specifically, their exposure to commercial real estate (CRE). Small banks hold 28.7% of assets in CRE loans, compared to 6.5% of assets in CRE held at large banks.

The rise in remote work (the outright level of remote work is still running at roughly 7x above the pre-pandemic level), the rapid pace of rate hikes and the recent layoffs are trends driving vacancies at levels close to all time highs. In US, the vacancy rate in the office sector, at 12.5%, is comparable to where it was in 2010 after the Global Financial Crisis.

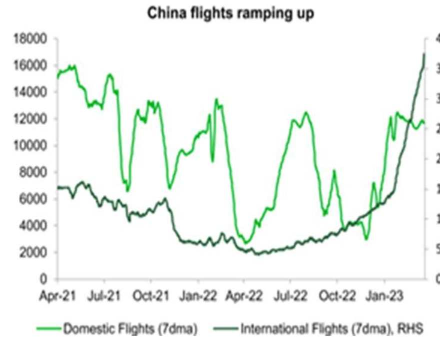
CRE prices across all sectors are currently down just 3.5% from the peak in 2021 (according to data from NCREIF). Given higher interest rates, we will likely see more price deflation on a go-forward basis. However, history suggests that CRE down cycles are less detrimental to GDP than residential real estate down cycles, given there is less spill over from CRE to the consumer.

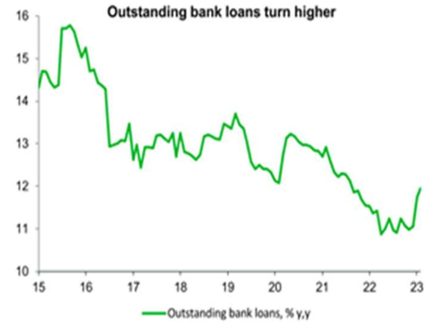
Since everyone is cautious on US regional banking sector, worries persist about the commercial real estate sector, especially the office real estate. With positive views on Logistics, Industrial, Retail real estate, we think that once Fed will confirm rake cuts at the end of 2023 or 2024, the whole sector will perceive a revival in valuations (not immediate and significant, but a definite reversal in price trends).

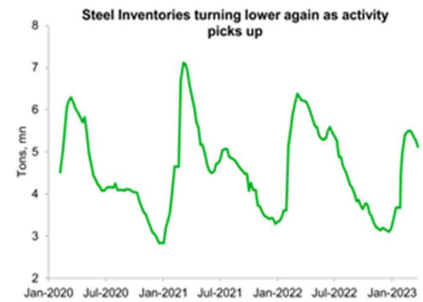
3 - China reopening and recovery expectations – part II

Many indicators measuring Chinese activity have normalised or at least shown marked improvement, with activity in Q1 coming in stronger than anticipated. Measures such as road traffic congestion, metro passengers, mail deliveries, & box office revenues have all strengthened. Passenger flights have ramped up including international. Manufacturing indicators have improved as reflected in recent PMIs while freight and cargo traffic domestically have rebounded.

There have been various signs of improvement in the property sector, albeit from very weak levels. Real estate investment, land purchases and building starts have strengthened, developer funding has become less negative, while construction and sales are turning around. Significantly, transactions are rising once again and not only in tier 1 cities, with price increases also spreading to tier 2&3 cities, reflecting a broader bottoming. There has been a pickup in bank loans, which highlights that demand for credit is finally picking up as confidence returns.







Source: TD Securities, Macrobond.

All seem to follow the path set by Chinese Premier Li Qiang that vowed that China would open wider to foreign companies "regardless of changes to the global environment" at the 3-day China Development Forum, which hosted 70 foreign executives, including Apple's Tim Cook, Bridgewater 's Ray Dalio and Deloitte 's Sharon Thome.

From the News Desk to the Investment Team

- Mar 9th: China's Communist Party takes aim at hedonistic bankers, The Economist.
- Mar 15th: The U.S. economy added 236,000 non-farm jobs in March, unemployment rate lower at 3.5%.
- Mar 16th: ECB raised its key interest rate by 50 basis points, to a 15-year high of 3.0%.
- Mar 17th: PBoC injects liquidity in the banking system, cutting specific reserve requirement ratios.
- Mar 19th: The Federal Reserve must choose between inflation and market chaos.
- Mar 23rd: BOE raised the interest rate it pays on commercial bank deposits by 25 basis points to 4.25%.
- Mar 24th: After Credit Suisse's demise, attention turns to Deutsche Bank.
- Mar 27th: China's manufacturing sector strengthened in February 2023.
- Mar 29th: Commercial-property losses will add to banks' woes, The Economist.

In March we witnessed large movements in short-term bond yields as Fed Chair Powell testified to the U.S. senate banking committee that economic data in the U.S. was stronger than anticipated and that therefore the Fed would likely need to raise interest rates faster and further. However, two days later reality hit with the collapse of Silicon Valley and Signature Bank which completely changed the expectations for further rate hikes.

China continues to benefit from reopening, with the reopening boom experience leaving a lot to desire. We expect that the government will continue taking steps to limit downside risks to the economy by stimulating domestic spending and the housing sector.

Fixed income markets rallied on expectations that the Fed is nearing the end of its most rapid rate hiking cycle in decades. The Bloomberg U.S. Aggregate Index and U.S. High Yield Index returned 2.5% and 1.1%, respectively. The yield on the 10-year U.S. Treasury Note declined 0.42% in March to finish the month at 3.49%.

Citigroup, Tyson, Foods, Meta, Amazon, and Disney announced significant layoffs in March. Despite such announcements throughout the first three months of 2023, the unemployment rate remained at a low 3.5%.

However, the Labour Department reported that job openings decreased in February to the lowest level since May 2021.

Looking forward:

- We expect that headline inflation data to stay soft over the coming months, mainly due to the lower Shelter component of inflation. The risk may come from potential reacceleration of inflation the second part of the year.
- Tight commodity supply conditions may limit the extent of price declines during what many analysts see as a recessionary period. Capital spending on oil production is at a 3rd of the peak level, with many companies prioritizing shareholder benefit ahead of additional investments.
- US$ remains expensive, trading 19% above its Purchasing Power Parity (PPP) fair value but we need to stay aware of the short-term cyclicality of the US$ and its characteristic countercyclical feature – should recession become reality (shallow or not) the US$ is expected to strengthen.

Investment Views

In our March 2023, we have made several changes to our investment portfolio. At the cost of a lower weight in the Singapore Real Estate allocation, we have invested in the (up- and mid-stream) Energy sector in US and initiated new positions in North American Real Estate firms that pay monthly dividends. We lowered the overweight in Singapore Real Estate sector and balanced it with allocations in Singapore banks, monthly dividend distributing and consumer staples companies.

Although central banks will maintain their focus on inflation, we expect policy rates to have reached their peak in key regions. The policy outlook has already been repriced in financial markets, with yields and rates lower.

Mar-23	GLOBAL GROWTH	APAC GROWTH	GLOBAL QUALITY	APAC QUALITY	GLOBAL MINVOL	APAC MINVOL	GLOBAL DYIELD	Global IG 1-3Y	Global IG 3-5Y	GLOBAL HY
	EQUITIES							BONDS		
1 MONTH	6.93%	3.36%	6.84%	4.10%	3.96%	2.71%	2.30%	1.10%	1.47%	0.92%
1 QUARTER	15.10%	4.31%	10.54%	6.42%	2.10%	2.53%	1.66%	1.47%	1.39%	3.15%
1 YEAR	-9.82%	-10.18%	-6.01%	-10.65%	-5.10%	-7.59%	-3.38%	0.86%	-3.16%	-4.53%
3 YEARS	55.82%	20.79%	55.91%	24.32%	27.88%	11.60%	43.44%	0.43%	-6.49%	14.52%
5 YEARS	63.76%	6.93%	69.70%	17.72%	31.94%	-5.43%	31.82%	7.18%	-3.44%	5.48%
10 YEARS	1.7909498	61.98%	196.43%	-	102.49%	32.90%	83.79%	13.63%	1.46%	36.60%

This month report on main factors performance (see the above chart) includes Global Yield, as it finally shows signs of life. If had a subdued performance for last two quarters, especially in Jan and Feb 2023 when it strongly underperformed Growth and Tech globally (same stands for the APAC indices/ factors).

With rates closer to their peak levels, sectors and regions that were depressed by the perspective of further rate hikes caused by sticky inflation may reverse in performance and recover some of the earlier losses. Signs came already from a slower APAC versus Global in monthly and quarterly performance and a relative recovery in bonds market.

For additional information, please contact **New Dimensions Capital**:
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In short-term, our Investment Committee analysing the following:

- Regional/Country diversification:
  - Japanese equities for its low valuations and decent earnings growth in addition to the Yen perceived as strengthening this year. Asset repatriation will support the currency and inherently, the Japanese companies.
  - China Equities, at a lower allocation, targeting the higher dividend paying SOEs involved in the revival of the construction activity (government stimulus, housing sector growth, infrastructure).
- Real-estate sector 'rejuvenation' – we work on reallocating from commercial into logistics or retail, and from US to Canada. CRE lending in Canada is dominated by large banks, pension funds, life cos (and some others) which are well-capitalized, though some undoubtedly may tighten their underwriting standards in the current environment.

At the end of March 2023, Vanguard produced the 10-year annualised nominal return and volatility forecasts based on data as of 31st December, 2022. For equities, we are looking at lower projections on US Growth and higher in US Real Estate and Global ex-US unhedged equities (mind this is long-term projection, and a reaction to the recent performance of the respective sectors):

Equities	Return projection	Median volatility
U.S. equities	4.4%–6.4%	17.2%
U.S. value	4.5%–6.5%	19.8%
U.S. growth	2.4%–4.4%	18.3%
U.S. large-cap	4.3%–6.3%	16.9%
U.S. small-cap	4.7%–6.7%	22.6%
U.S. real estate investment trusts	4.6%–6.6%	20.3%
Global equities ex-U.S. (unhedged)	6.7%–8.7%	18.5%
Global ex-U.S. developed markets equities (unhedged)	6.5%–8.5%	16.7%
Emerging markets equities (unhedged)	6.3%–8.3%	26.3%

In the short to medium term, some of our investment views are clustering around:

- We expect **both inflation indices to soften**, together with the unemployment figures and the economic growth readings. The lower inflation is dearly needed by the US banking system as this will allow the Fed to stop hiking rates and start hinting of rate cuts. As of now (mid-April 2023), we see a 71% Bloomberg consensus that the Fed will cut rates over the next 6 months.
- **The equity rally** may fade as the dichotomy between the real economy and markets is increasing even as the earnings outlook is getting weak. Our view is to favour value in US and Japan and keep positive on high-dividend stocks especially the ones with monthly distribution (except Japan).

- In EM equities, we see **China improving** on the back of a better growth outlook, cheap relative valuations and relevant stimulus by the government.

We will not add risk but replace risky allocations to ones that show longer duration and better cross-sectional valuations.

New Dimensions Capital – About Us

A statement we heard a lot over the month:

"**Housing markets globally could be the big hurdle to central banks raising rates enough to tackle sticky inflation**".

This comes in line with our view that there is a divergence between the headline numbers and the way market understands and absorbs it.

During various client meetings in March, we realised that although income is a continuous need for our individual and corporate clients, actual performance should also be part of a consistent stream of income. With bond and fund investments that did not fare well the first two months of the year, we have received interest in investment products that provide stable returns proving resilience against exceptionally volatile bonds and the persistent currency risks.

Investors that have already gained exposure in real estate market in Singapore or in Asia, in general, are aware of currency risks ahead of the reversal in US$ trend once the Fed confirms rate cuts. This may trim profits coming from lower interest rates effect on real-estate holdings or high dividend distributing companies and is a strong request from several prospective clients of New Dimensions Capital.

March was a very active month at New Dimensions Capital, with all team members engaged to take advantage of a strong but very dynamic market. Some unknowns persist, but so are our market hedges.