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Active Risk Allocation

August 2022

Status

Eye of the storm - asset divergence, bonds vs stocks

peak inflation growth

- Inflation remain sticky
- activity moderation manageable
- margin pressure

Risk overview;

Short-term **Negative**

Medium-term **Neutral**

☐ Stocks – underweight (improved)

- Low vol factor overweight, and defensive sectors

☐ Bonds – underweight (improved)

- Underweight Europe. Overweight US credit

☐ Alternatives – overweight

- Non-interest rate sensitive, non-directional, uncorrelated assets and strategies

☐ Macroeconomics

- Central bank rate hikes & Quantitative Tightening(QT)
- China CoVID-19 “grand re-open” vs Omicron
- Global supply disruptions (post-covid demand, war, trade war)

☐ Indicators

- OPRA: **Negative** / Improving (risk gauge for balance risk/risk free)
- OMRI: **High** / **Neutral** (model volatility gauge)



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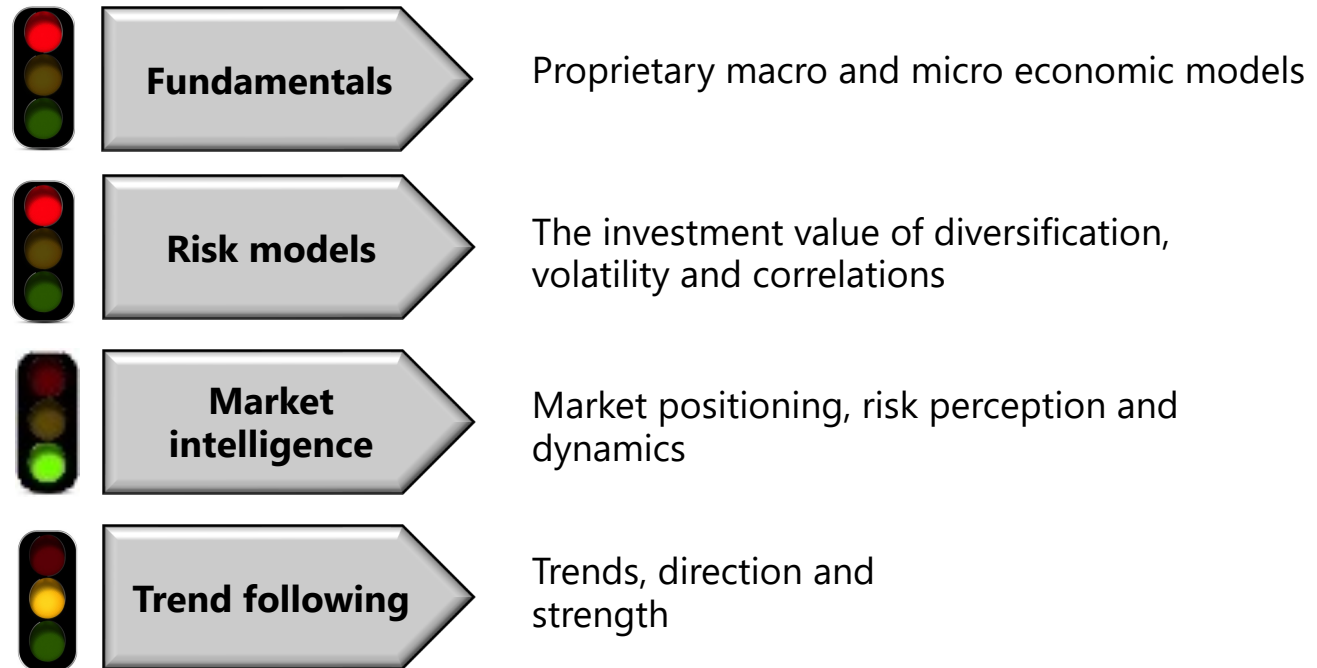
Active Risk Allocation

The state of indicators

Investment
process

Indicators

Highly sophisticated models
analysing about 150 indicators



OMRI[®] Origo Market Risk Indicator

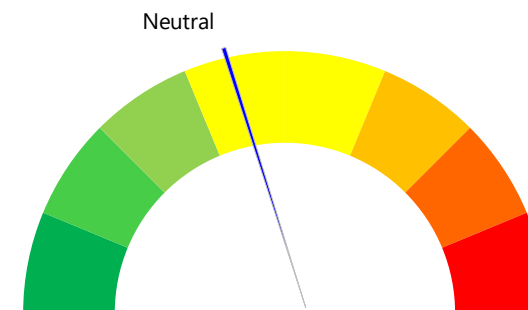
Short-term risk gauge

Improvement in the
Market intelligence
factors

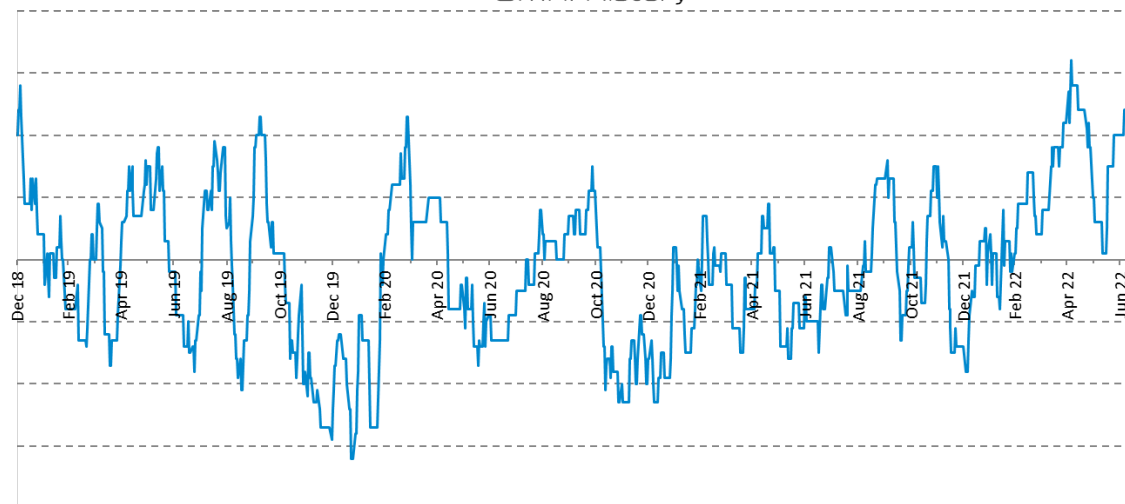
Geographically, US lead
while Europe financial
conditions continue to
deteriorate

09 August 2022

Indicator	Sentiment	Last update
X-Asset correlation	Feels good	09 Aug 2022
Economic Surprises	Neutral	09 Aug 2022
Financial Conditions	Neutral	09 Aug 2022
Global Financial Stress	Neutral	28 Jul 2022
Gepolitical Risk	Feels good	31 Jul 2022

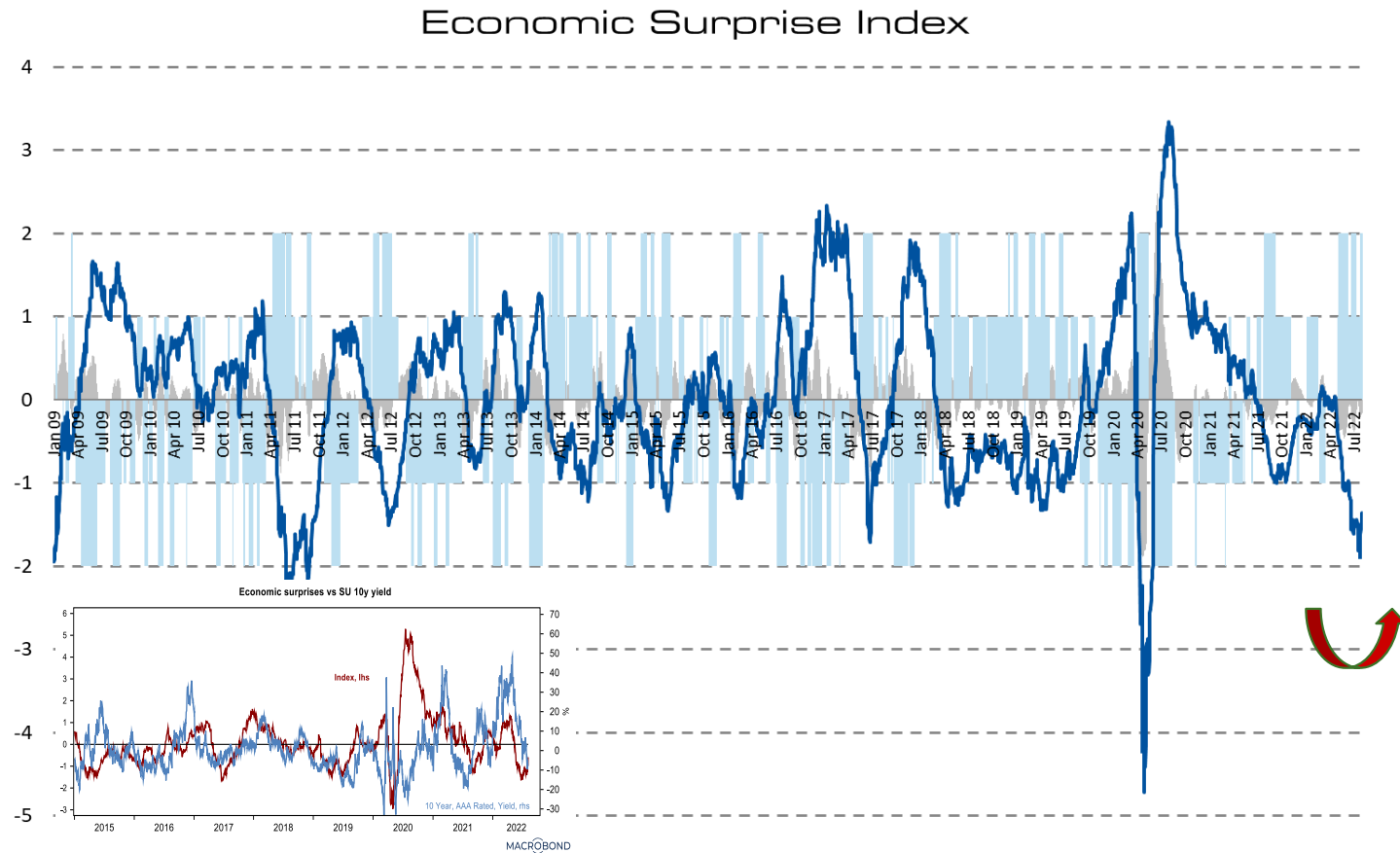


OMRI History



Fundamentals

- **Macroeconomic models**
- Volatility and risk budgeting
- Market intelligence
- Technicals and trend following



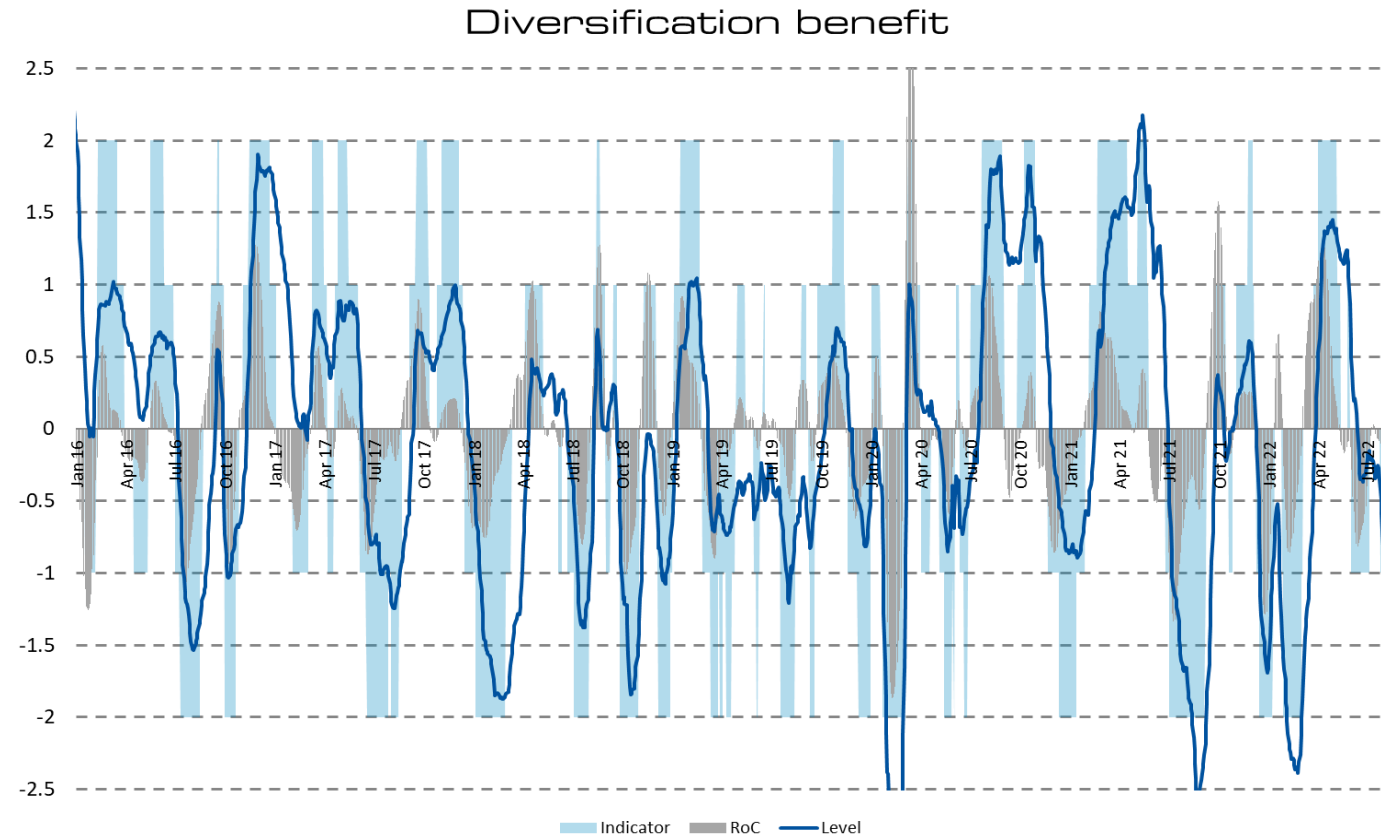
Improving from a low level, suggesting analyst' have lowered expectations towards the reality of activity moderation.

Temporary support for bonds is about to reverse.

The ESI (above centre) is a powerful indicator of coming stress.

Volatility and Risk budgeting

- ☐ Macroeconomic models
- ☒ **Volatility and risk budgeting**
- ☐ Market intelligence
- ☐ Technicals and trend following



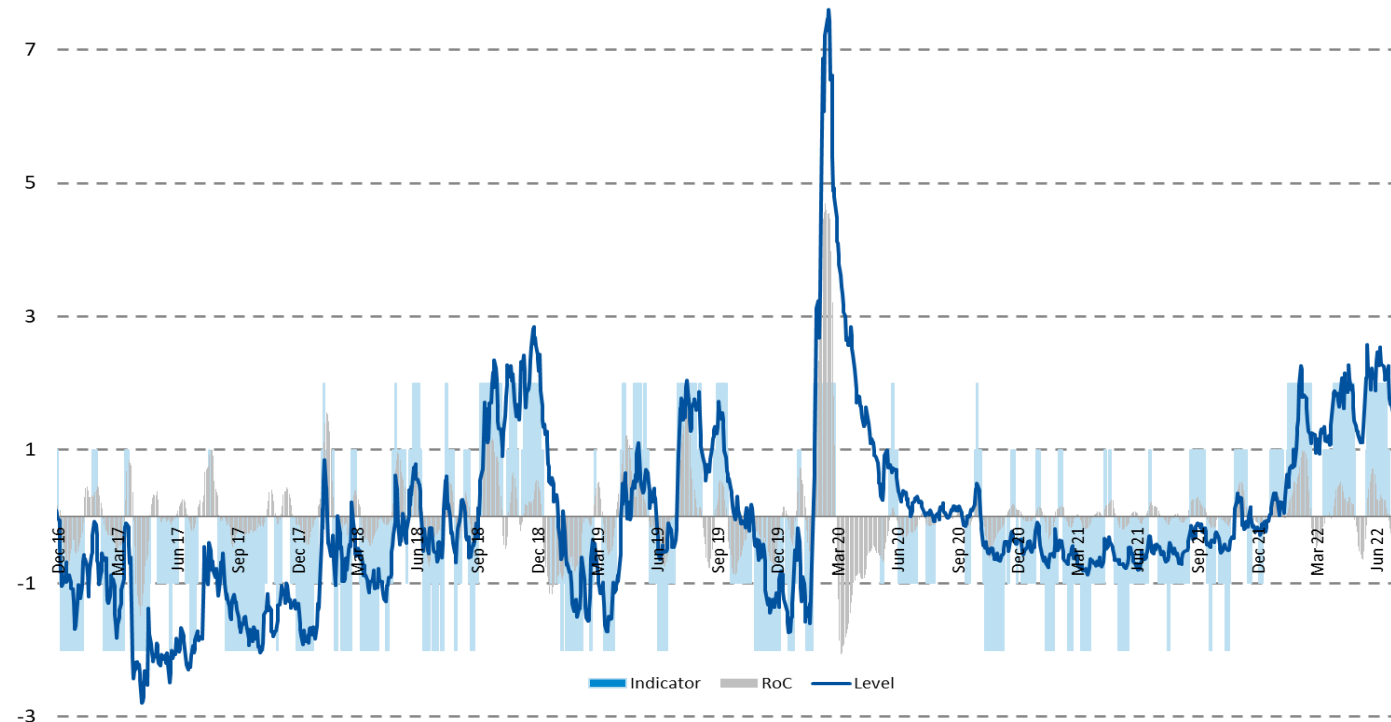
No longer any "Markowitz benefit" in a broad based portfolio composition.

The 60/40 passive fixed combination is based on the assumption of constant negative correlations, despite this being more an exception than a rule over the past 10 years. When the diversification benefit is low, there is not much to be gained from diversifying. Cash and alternatives should then be meaningfully increased.

Market intelligence

- ☐ Macroeconomic models
- ☐ Volatility and risk budgeting
- ☒ **Market intelligence**
- ☐ Technicals and trend following

Global Financial Stress Indicator



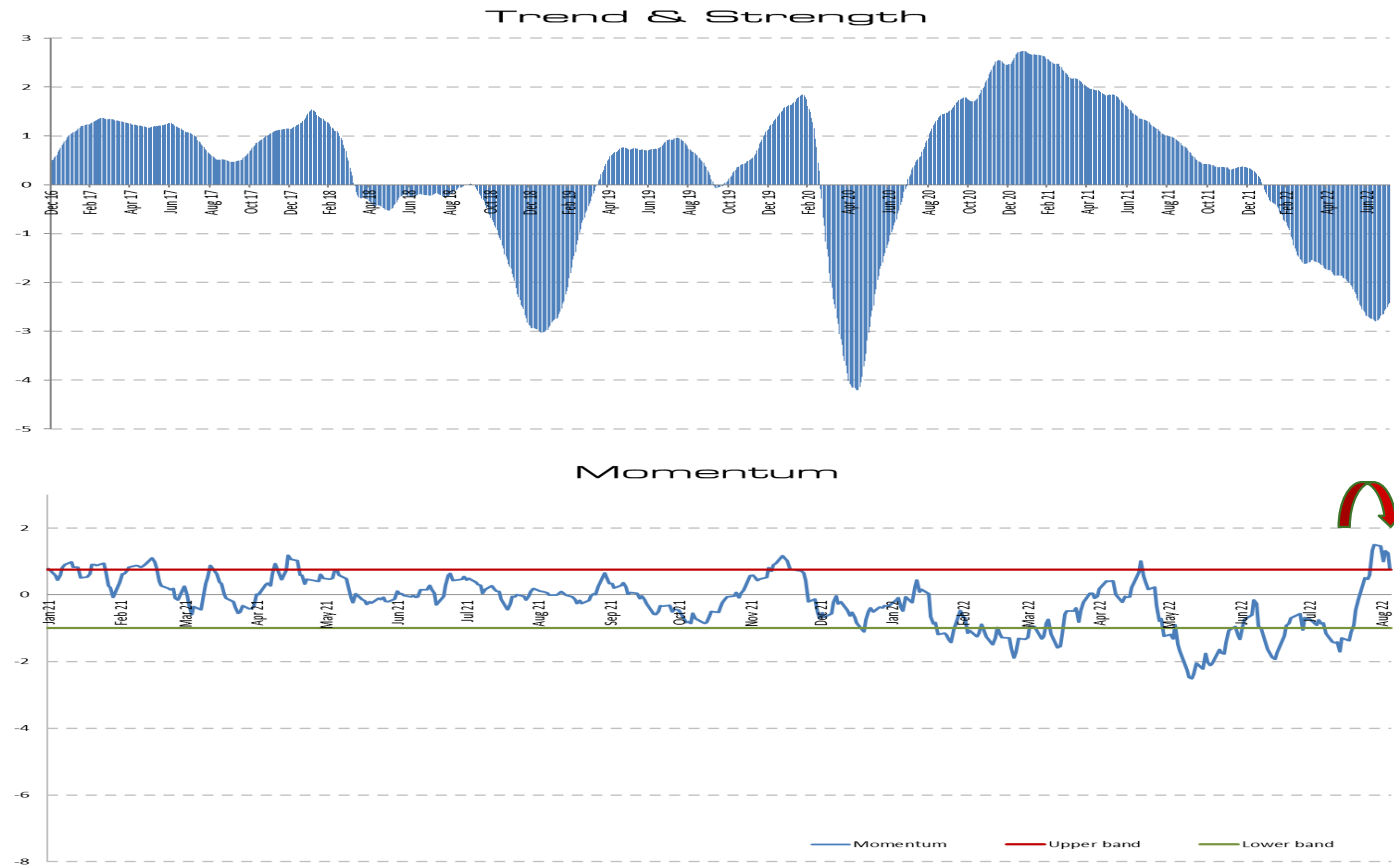
Persistently high since turn of year 2022, but currently improving from a high level of financial market stress.

This factor flagged the largest change to market risk perception over July.

A measure of global cross market measure of risk, hedging demand(volume, skew) and investor flows in the financial system.

Technical

- ☐ Macroeconomic models
- ☐ Volatility and risk budgeting
- ☐ Market intelligence
- ☐ **Technical and trend following**



The pattern through 2022 remain consistent with volatility around a falling trend. Short-term, long stocks positioning vulnerable to negative surprises. Medium-term in all interest rate sensitive assets has turned neutral.

Trend strength in the various market is an expression of the persistence of the currently existing trend.

Current status



Macroeconomics

Beyond peak deflation, continued growth moderation and sticky high inflation.

Basis for US to continue rate hikes and QT. China re-open for a bumpy ride.

Europe slowdown entered recession territory.



Market Risk and market intelligence

Less bad than feared economic and micro earnings data temporary lifts market animal spirit.

stagflation/recession scenario

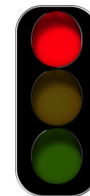
complicated by trade- and energy-disruption.



Technicals

Medium-term negative trend in risk assets improves, turning neutral.

Short-term technicals keep switching between buy/sell, indicating a trading channel around a falling trend.



Volatility and risk budgeting

Portfolio risk increase as despite assets rise they now move in synch.

Continued high level of asset volatility supports our theory for having entered a new regime around Sep 2021.

On the radar



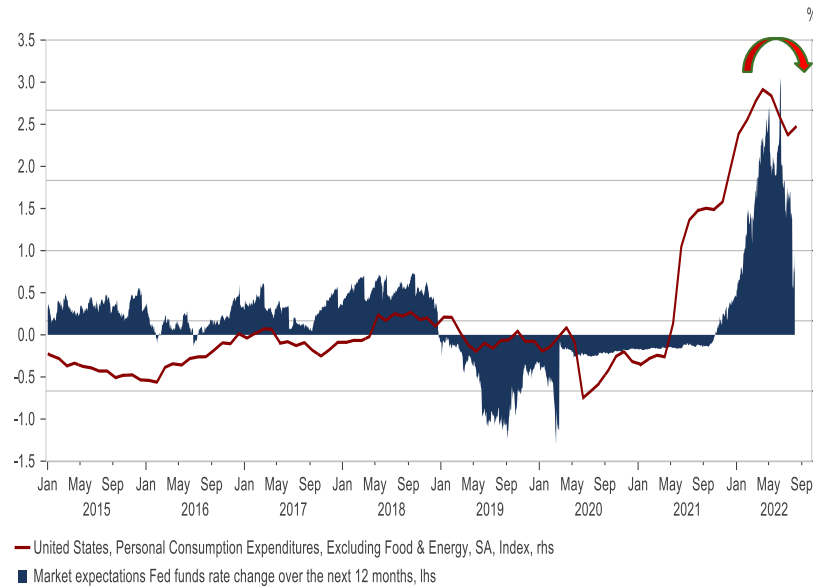
Macro risk — Inflation

Stagflation risk abiding CBs are still behind the curve

Inflation soaring heading into 2022 ..

- + Russia-Ukraine war
- + China “zero-CoVID”, grand re-open vs Omicron
- + DeGlobalisation

Peak inflation growth (US)



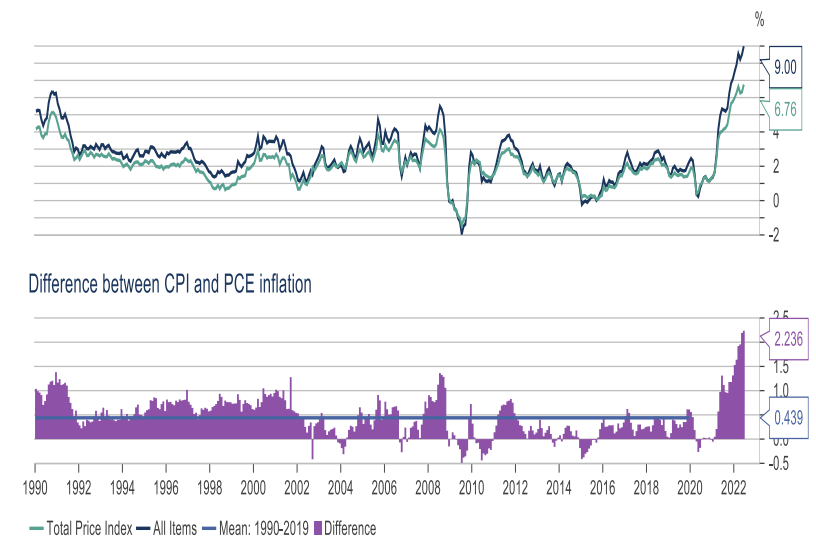
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Consumer price inflation expectations (based on breakeven rate)



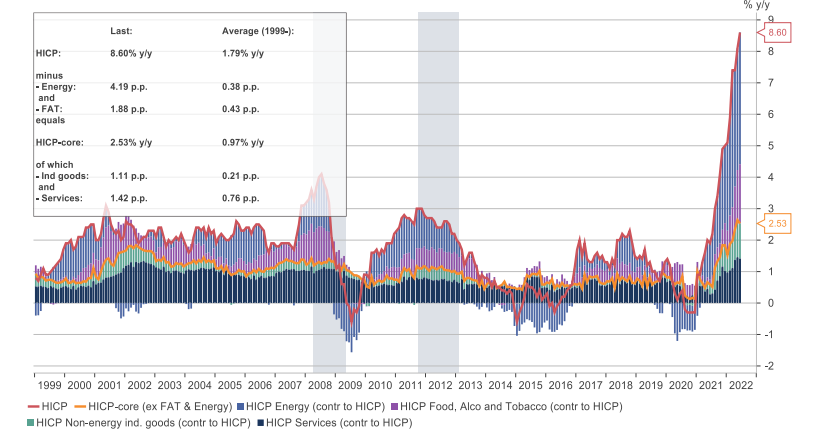
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US CPI vs PCE



MACROBOND

Contributions to eurozone inflation



MACROBOND

Macro risk — activity

Recession risk rising, but still manageable

US and Global activity has ample latitude => Fed tightening will continue

US economic activity set to slow as central bank tighten MP

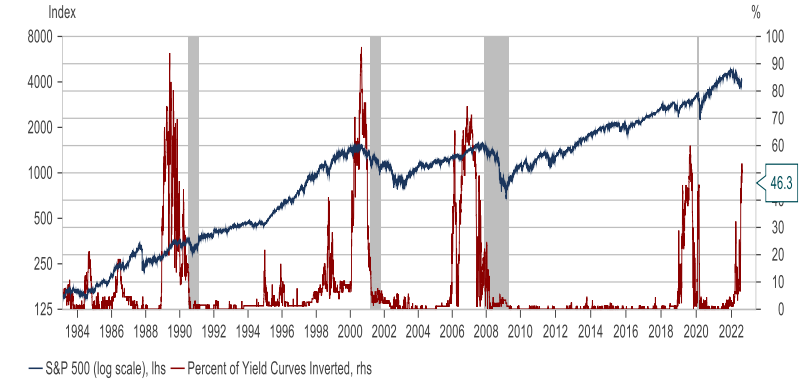
Last decision from central banks: Hike (+1), Cut (-1)



MACROBOND

Rising number of inverted yield curves signal recession

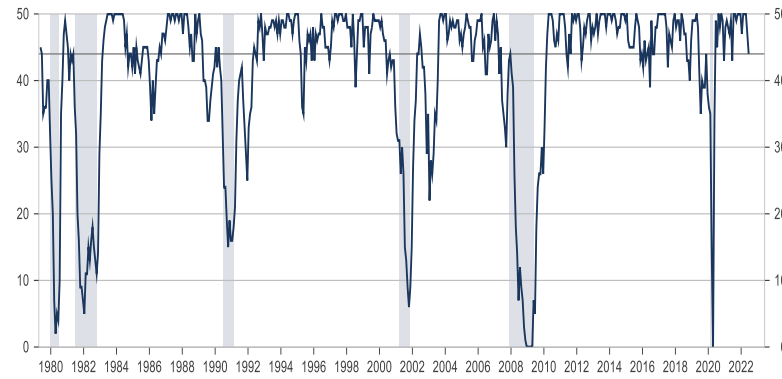
United States



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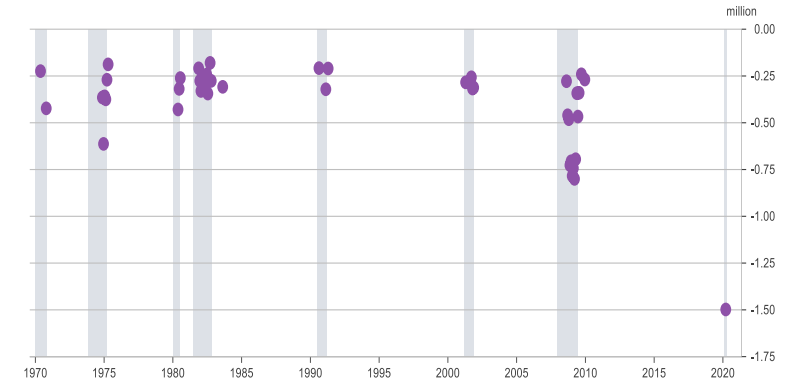
Number of US states with increased economic activity

Source: Federal Reserve Bank of Philadelphia coincident index (-6 threshold)



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Recession indicator - Non-farm payroll declines

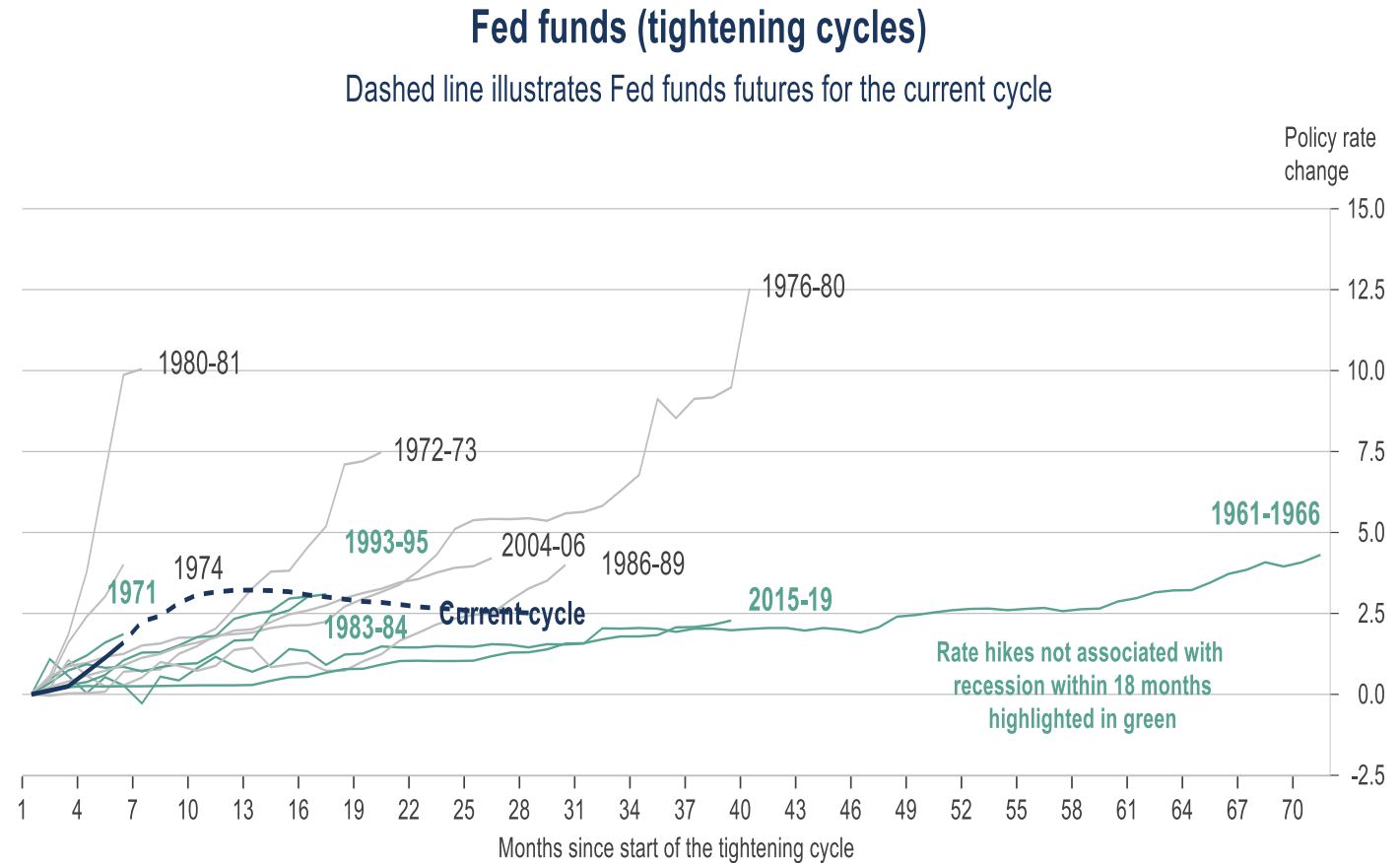


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Macro risk — Fed Funds

FF hikes vs Recession

A short tightening cycle?
Really?



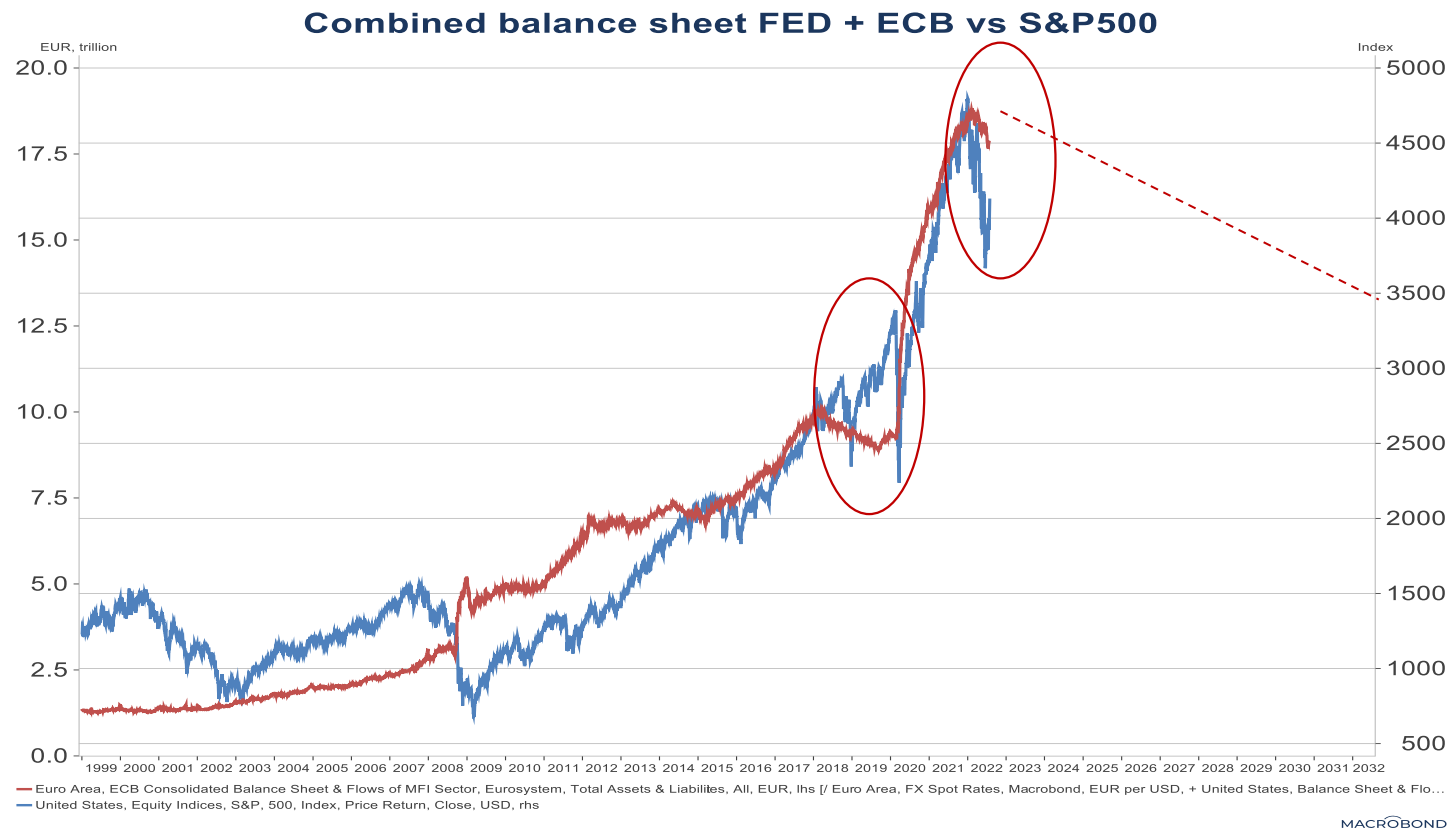
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Capital markets - stocks

July celebrated the not so bleak past.

The future is just getting started

Fed Minutes April; Combined rate hikes + QE reduction of 60-100bn/m – excess of 1 tn USD per year – every year, the next 10 years

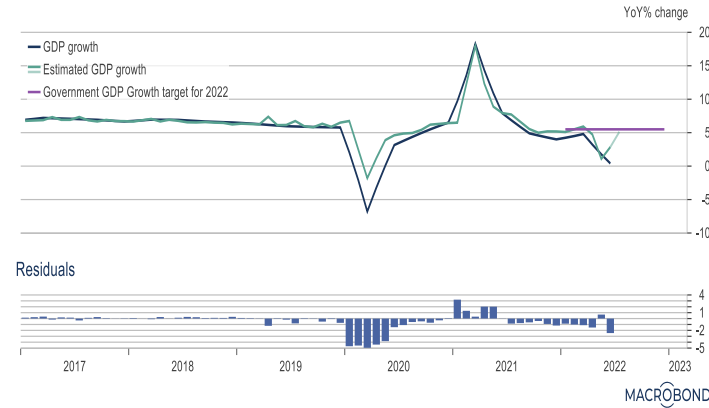


Macro risk - China

China, a Evergrande 2.0 ?

- PBoC May 2022 stimulus
- June "grand re-opening"
- Zero-CoVID policy
- Tech crackdown
- Changing demographics
- Real estate deceleration

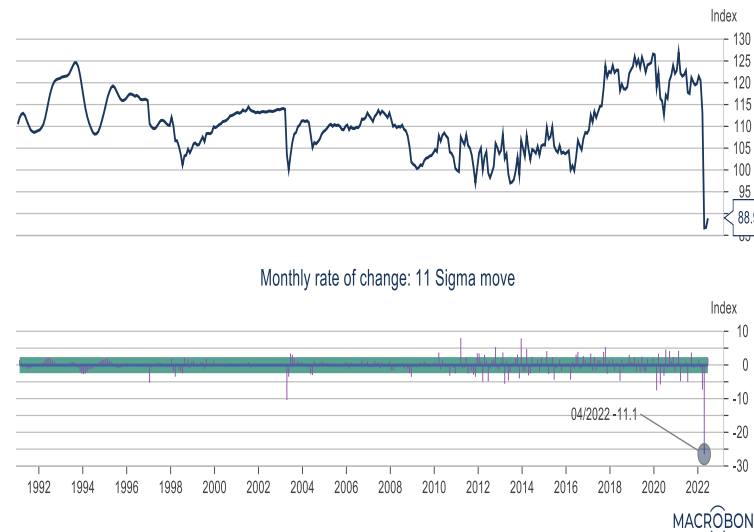
China GDP forecast model



Real estate market (China)



China consumer confidence



GEM / MSCI ratio

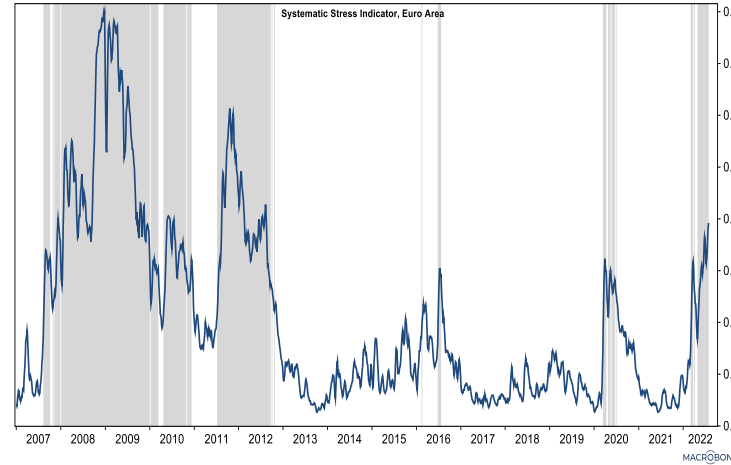


Macro risk- Europe

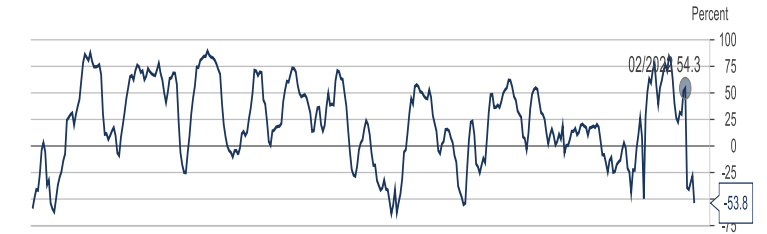
Euro debt crisis 2.0 ?

- ECB emergency anti-fragmentation, "Transmission Protection Tool" (TPI) tool - donors vs PIGS
- The Putin-put
- The age put

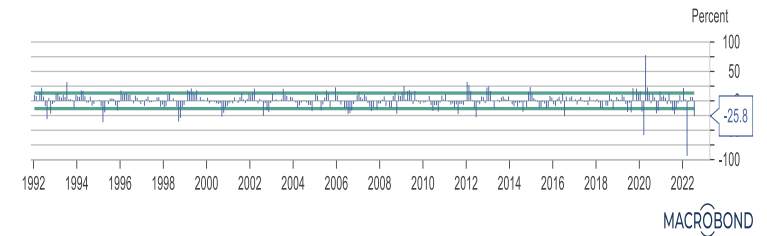
European Financial Stress



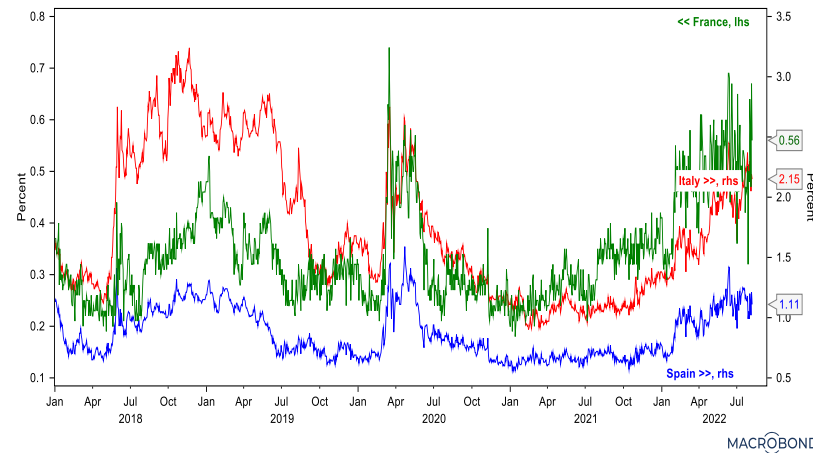
Germany's economic expectations experience record decline



Monthly value change with standard deviation bands

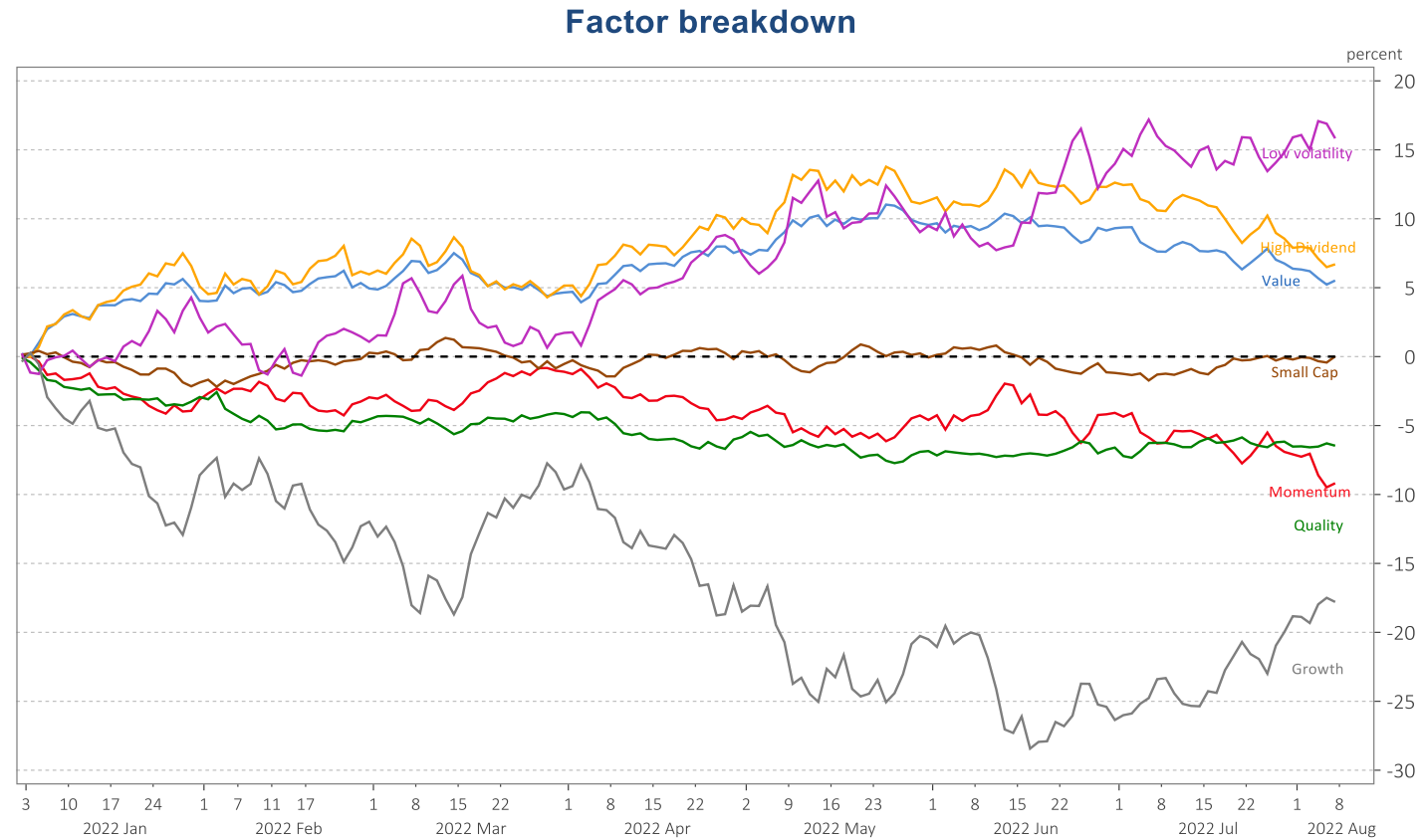


Government 10 Year spreads over Germany, Yield



Capital markets - factor styles

Low vol factor
outperformance.
Growth factor bottom-
fishing dynamics



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