Active Risk Allocation

The state of indicators

May 2023

ORIGO CONSULTING

Independent | Transparent | Disciplined

Status

Gap in Fundamentals vs Markets

- activity slowdown accelerate, labour market resilient, consumers holding up
- policy rates will continue to rise, not drop
- "China grand re-open" – losing steam
- "bank crisis" addressed surgical along with other "zero-rate victims"
- margin pressure accelerate, as do SMB bankruptcies.
- USD under pressure

Risk overview;

Short-term **Negative**

Medium-term **Neutral**

Stocks – underweight

- Low vol, dividend and large cap factor … traditional defensive allocation

Bonds – underweight

- Overweight IG credit

Alternatives – overweight

- Non-directional, uncorrelated assets and strategies

Macroeconomics

- Economic activity moderating. Economic surprises turning negative
- Price headline to half a year after Russian war – core to stick around for 2025
- Maximum centralbank tightening impact to arrive 2H 2023
- Fed liquidity 12 Mar 2023 "bank crisis" is reversing for QT
- Bank crisis deposit outflow will continue, but the scale is manageable

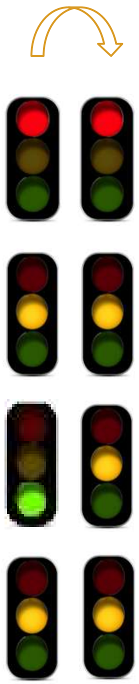
Indicators

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

Investment process

Indicators

Highly sophisticated models
analysing about 150 indicators

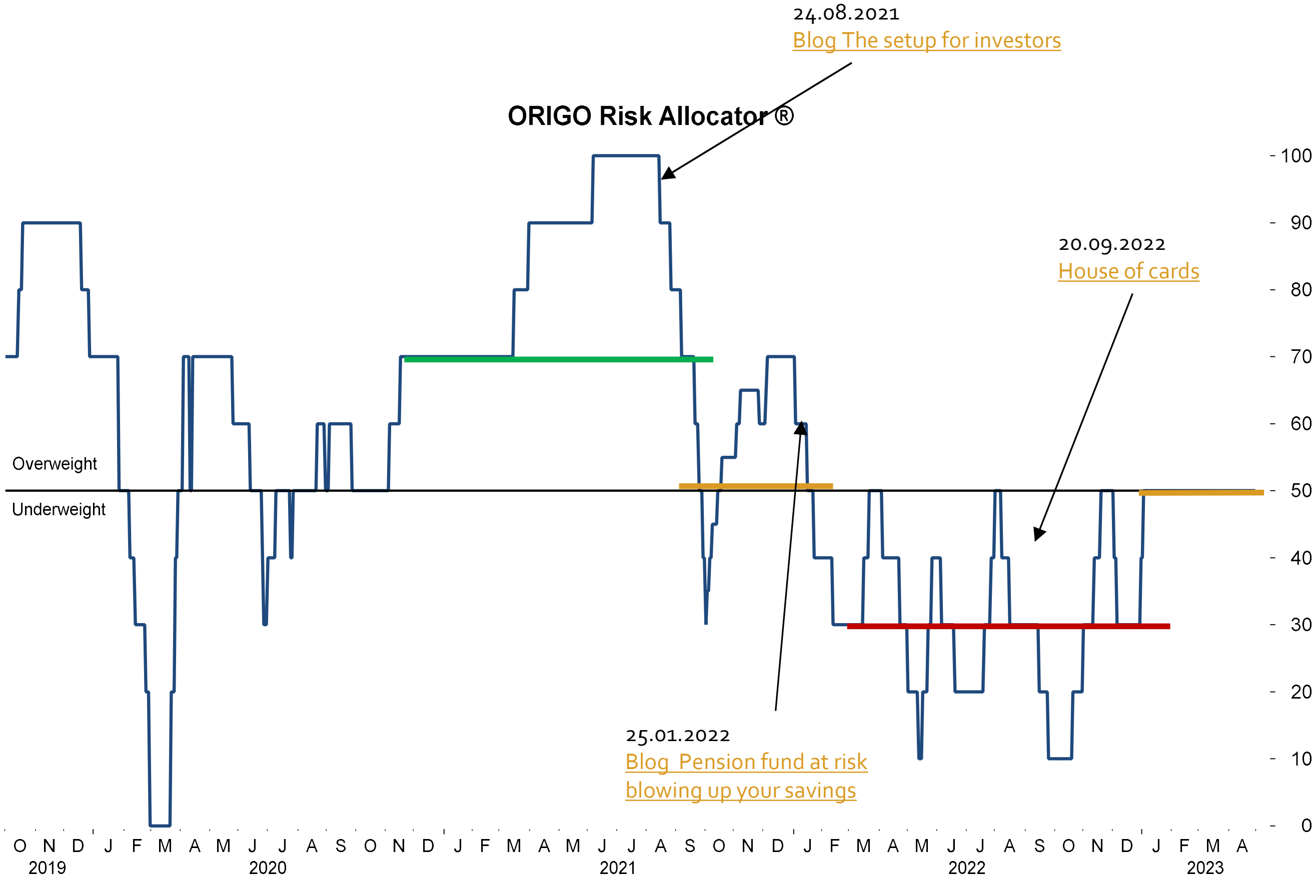


Fundamentals	Proprietary macro and micro economic models
Risk models	The investment value of diversification, volatility and correlations
Market intelligence	Market positioning, risk perception and dynamics
Trend following	Trends, direction and strength

Market Intelligence finally takes a step towards Fundamentals

OPRA®
Origo Portfolio Risk Allocator

Timeline, 2019 -



OMRI®
Origo Market
Risk Indicator

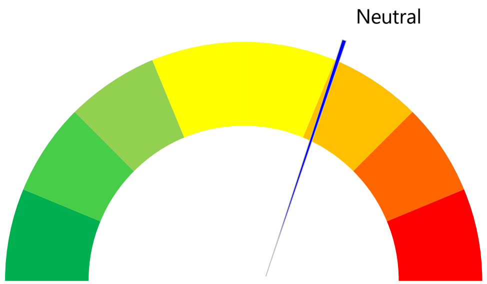
Short-term risk gauge

Market intelligence factors deteriorate

Geographically, EU financial conditions continue to deteriorate

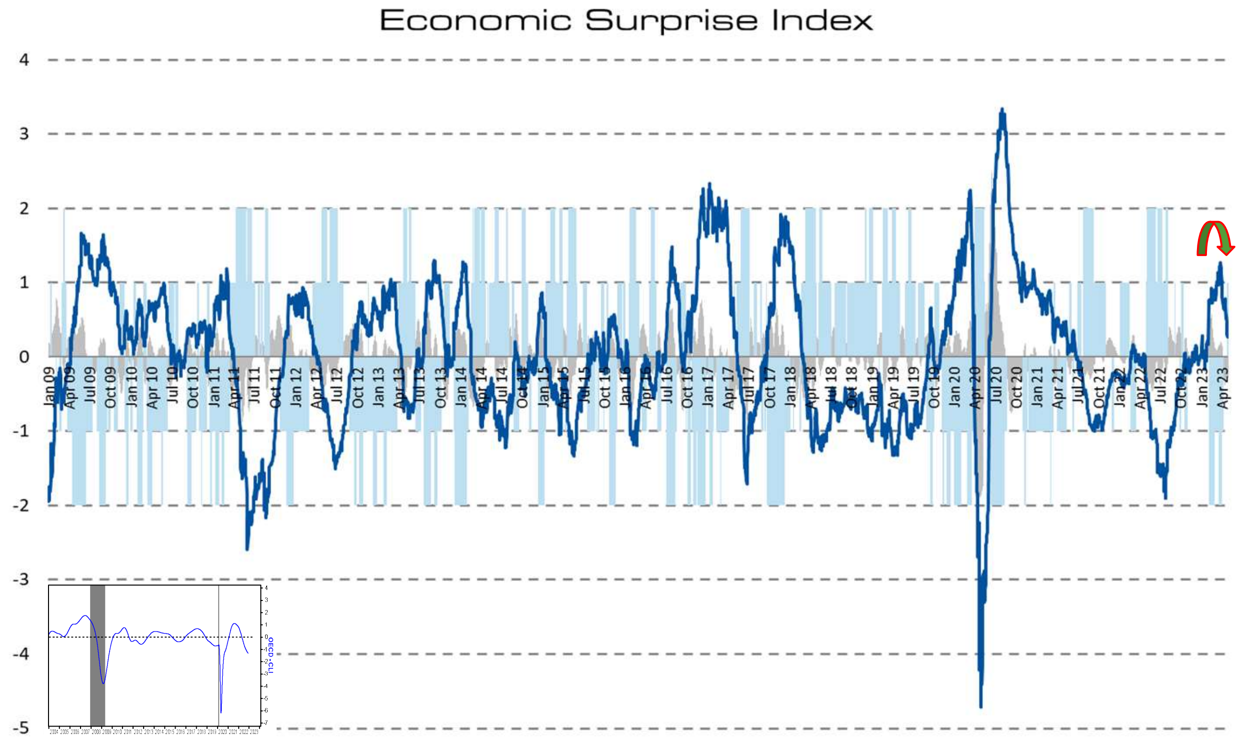
01 May 2023

Indicator	Sentiment	Last update
X-Asset correlation	Neutral	01 May 2023
Economic Surprises	Tense	01 May 2023
Financial Conditions	Tense	02 May 2023
Global Financial Stress	Neutral	01 May 2023
Gepolitical Risk	Feels good	30 Apr 2023



Fundamentals

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



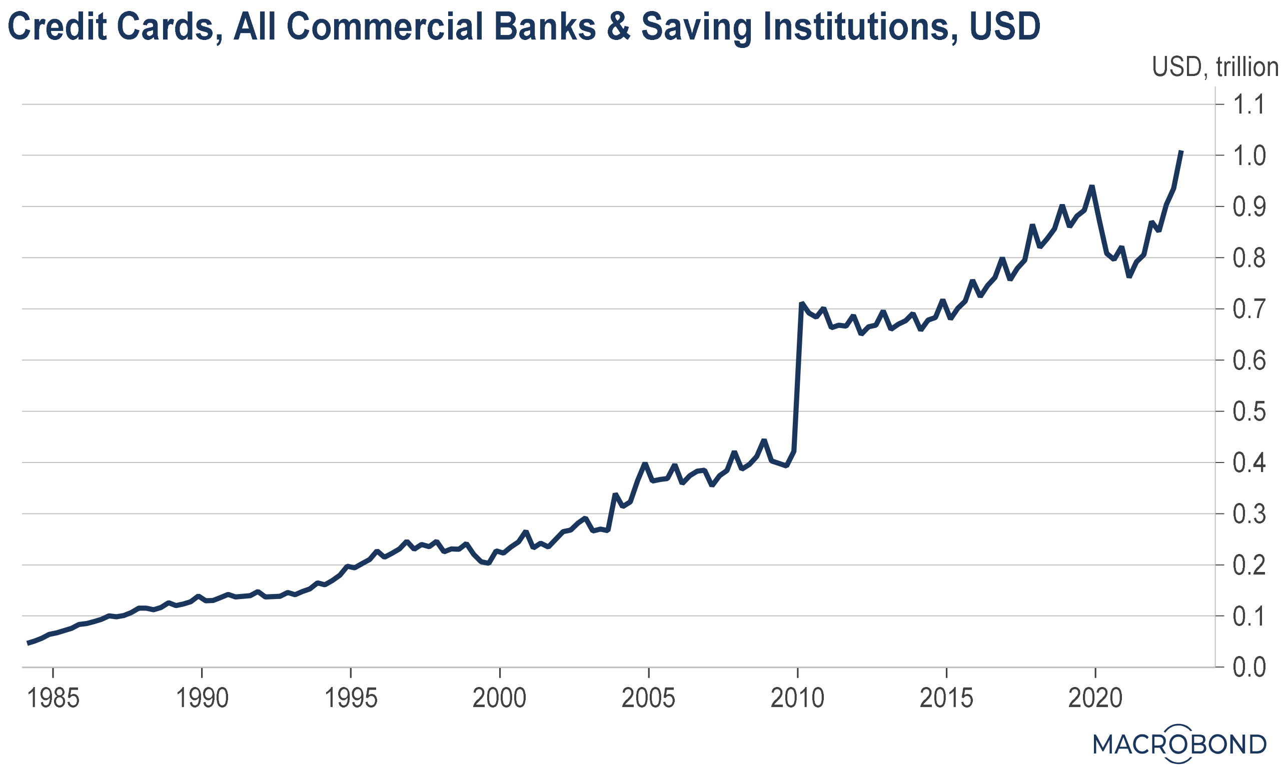
The phase of better-than-expected data has peaked

Consumer consumption holding up, service economy boom, production sector crater. Mid-2023 remains the challenging phase, as consumer savings deplete and 1 year of monetary policy takes effect.

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

Fundamentals .. Consumer consumption

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



Sub-component, consumer spending:
- Excess CoVid savings, getting depleted
- Consumers now running up credit card debt

… as the maximum impact of monetary tightening is about to land

Volatility and Risk budgeting

- Macroeconomic models
- **Volatility and risk budgeting**
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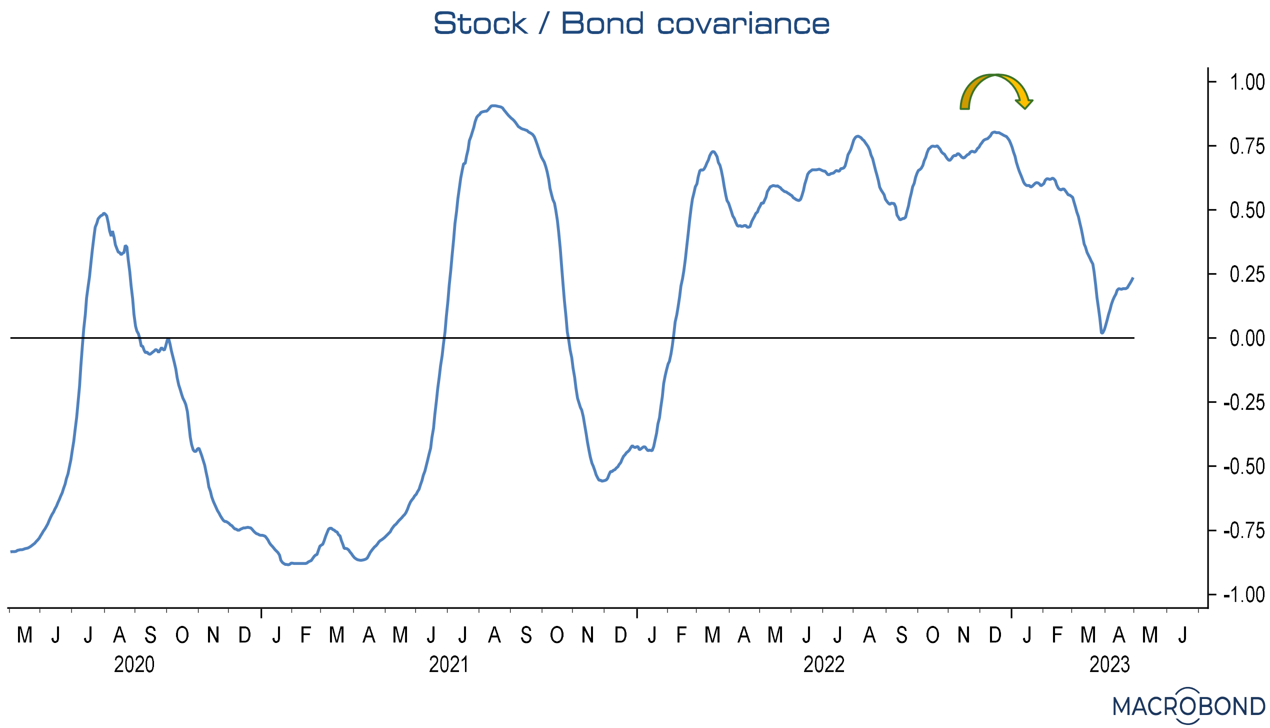

Correlations turned random

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 – as the entire year of 2022 is a constant reminder.
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
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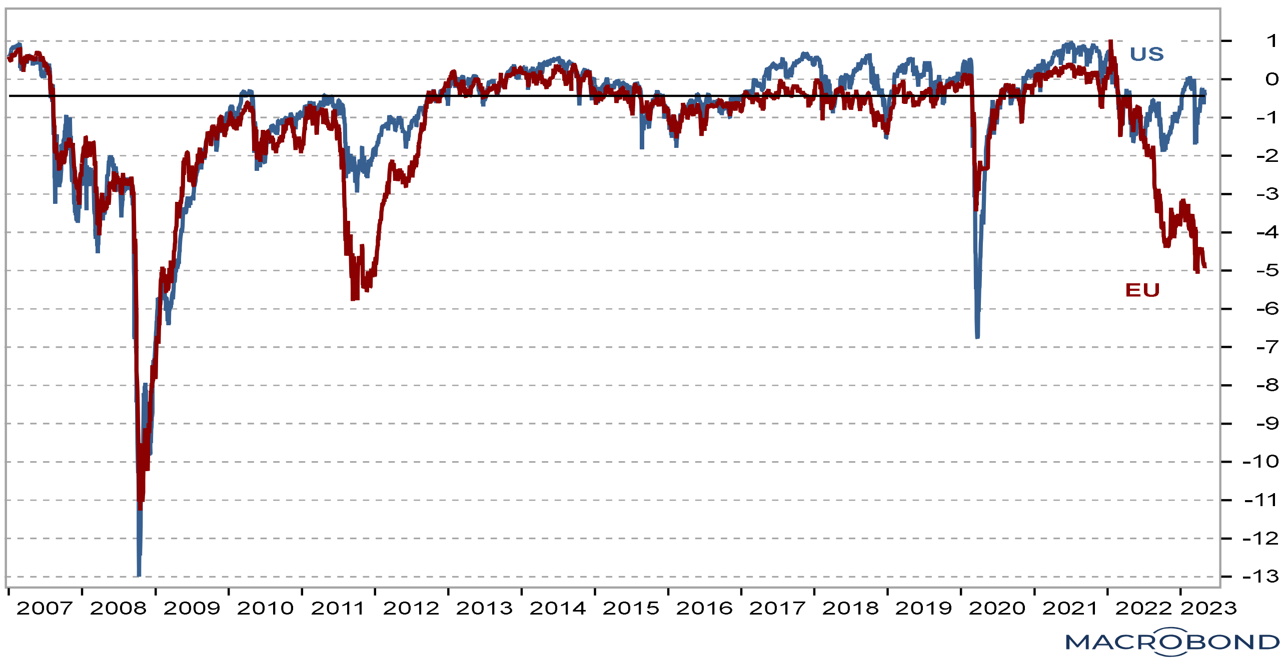
Financial Conditions



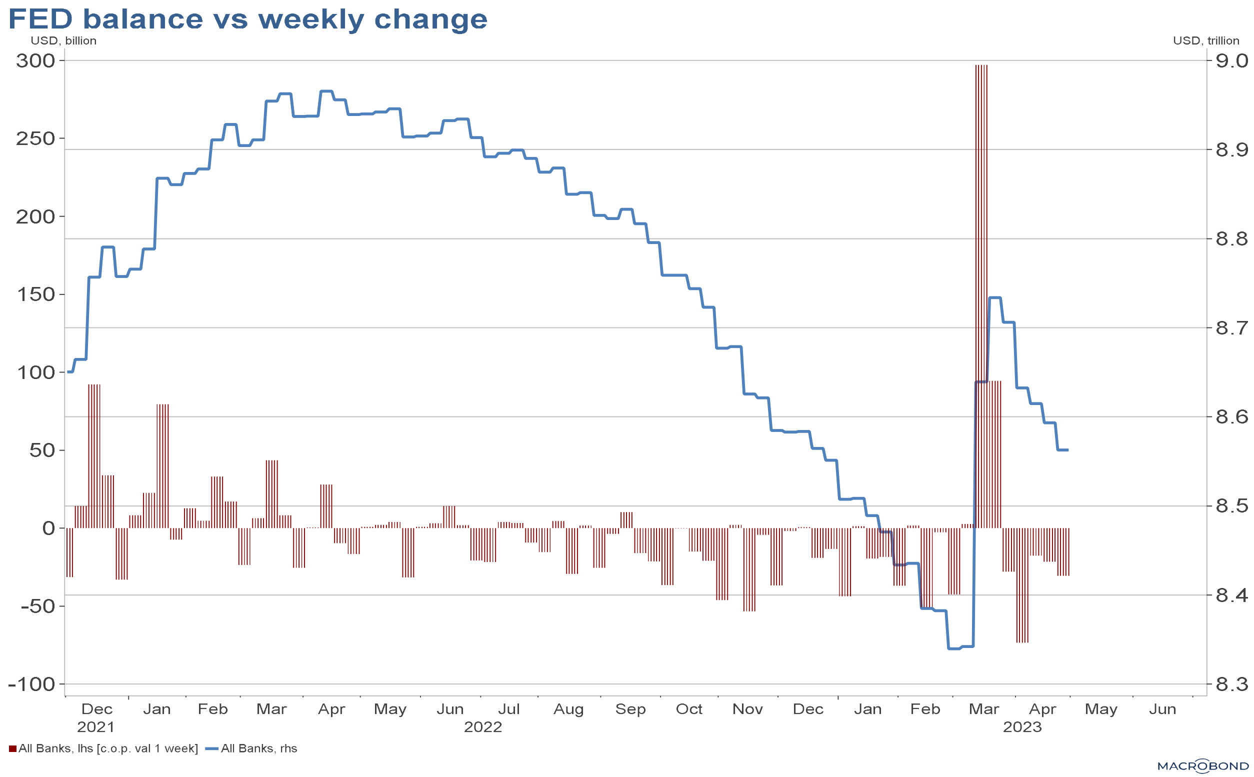
The sub-component for financial conditions, US remarkably neutral – but deteriorating in Europe

Credit conditions have as a trend tightened since Dec 2021. Recent "US bank crisis 2023" is an expected effect of centralbank tightening, so far contained and NOT the next credit crunch.

A measure of global cross-market measure of risk, credit conditions, hedging demand(volume, skew) and investor flows in the financial system.
The component may move quite fast in both directions reflecting the bi-polar nature of financial market participators' perception of risk and risk premia.

Market intelligence
.. the “bank crisis”

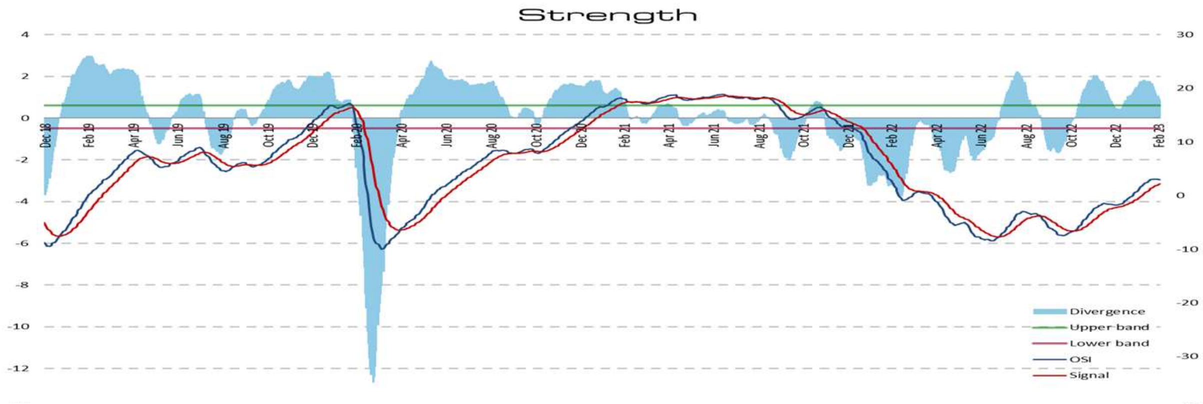
- ▢ Macroeconomic models
- ▢ Volatility and risk budgeting
- ▢ **Market intelligence**
- ▢ Technicals and trend following

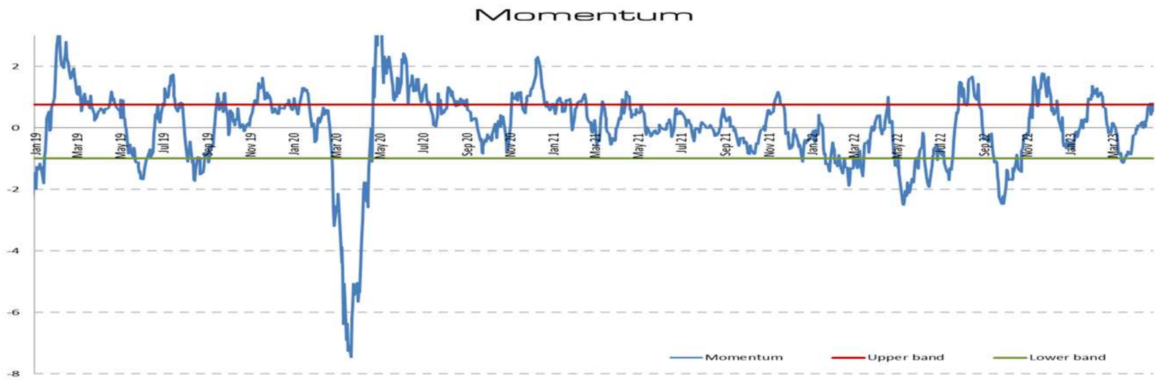


Fed balance knee-jerk rise on bank term funding (BTFP) announced 12th May, providing a brief risk-on boost. This has reversed to resume QT

Technicals

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





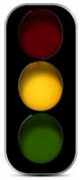
Short-term negative in a risk channel. Odds switching towards negative return on 1 month horizon.
Medium-term trend is stable, suggesting range-trading on the level.

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

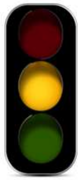
Current status

Macroeconomics
Policy rates higher for longer. The point; not peak inflation, nor peak policy rate.
China housing bubble to stymie Grand Reopening 2.0 as will contraction in consumer demand.
IMF's "1/3 of world 2023 in recession" holding up towards a period of sub-par growth – all according to plan.

Market Risk and market intelligence
US financial conditions are impressively balanced.
US "mini-bank crisis ongoing, yet deterioration in credit condition regionally center on Europe.
Powell has stayed off verbal intervention in 2023, for now, but might just step up again, at least one more time.



Technicals
Medium-term trend in risk assets are stabilising.
Short-term technicals keep switching between buy/sell.



Volatility and risk budgeting
Portfolio risk is unattractive. Volatility now in low end of channel and correlations has turned stochastic.

The correlation & volatility patter is adapting to a new regime probably entered Sep 2021.

Active Risk Allocation

2023

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Business as usual ?

ORIGO Sep 2021: ”A regime change is in the making …”

	2009-2021	Today
System	Neo-liberal multi-lateralism	Zero-sum nationalism?
Geopolitics	Stable	War (trade/conventional)
Clima	Predictable	Greater variance
Trade	Global	De-globalisation
Central bank behavior	Highly stimulative	Tightening
Inflation	Dormant	40-year high
Economic outlook	Positive	Global recession a 50/50
Likelihood of distress	Minimal	Rising
Mood	Optimistic	Guarded
Buyers	Eager	Hesitant
Holders	Complacent	Undertain
Key worry	FOMO	Investment losses
Risk aversion	Absent	Rising
Credit window	Wide open	Constricted
Financing	Plentiful	Scarce
Interest rates	Lowest ever	More normal

On the radar

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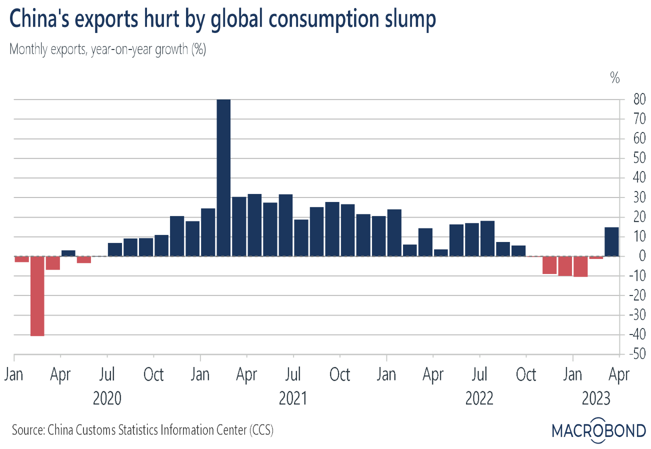
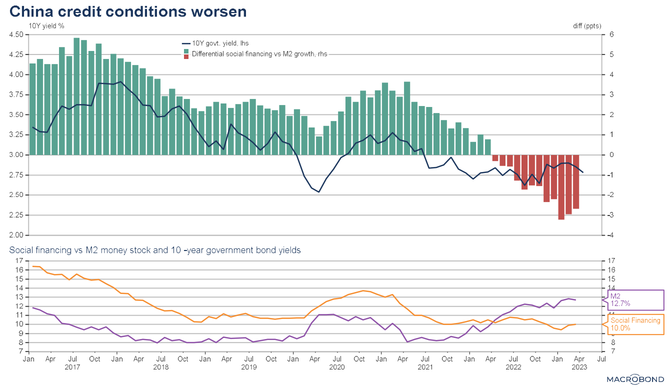
Macro risk - China

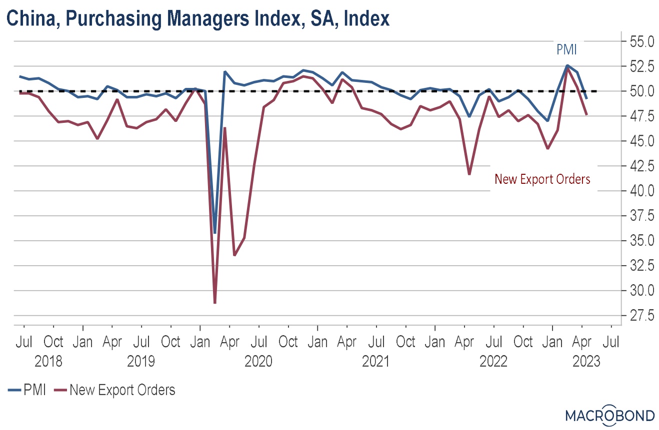
"Grand opening 2.0" – already sputtering

PBoC May 2022 stimulus

- Zero-CoVID policy
- Tech sector crackdown
- Changing demographics
- De-globalisation
- Real estate recession
- Major draught
- Belt & Road debt trouble





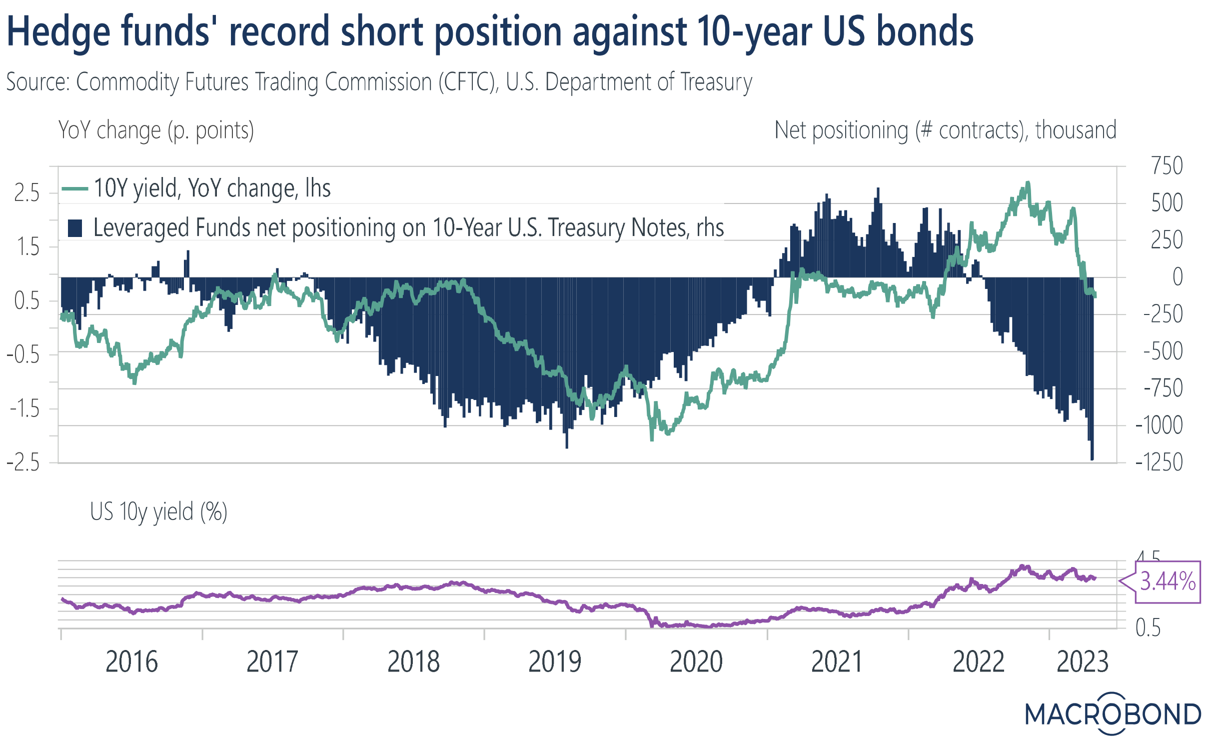


Manufacturing rebound is not quite stable, as global demand is fading

Macro risk - US debt ceiling

June deadline

Not news to speculators, but NOT priced into markets



Market intelligence
.. the "bank crisis"

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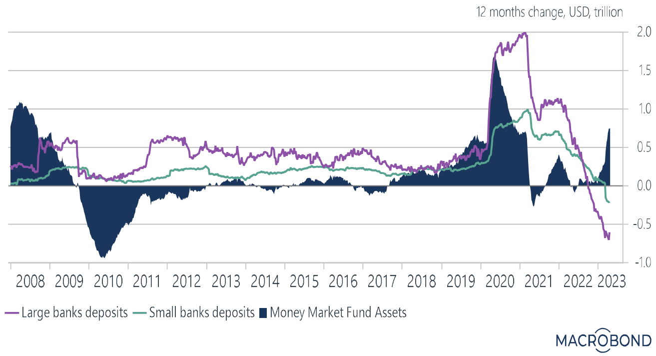
US bank balance sheets: deposits are melting

Source: Investment Company Institute (ICI), Federal Reserve



Bank deposits are seeping away as banks offer 0.40% vs Fed 5-6% pa.
Net bank deposit outflow are likely to continue but size, so far, a paltry -3% ytd

US Banks drip drip (relative S&P500)

Bank sector weighting is fading, which is by systematic regulatory design

First Republic Joins List of Biggest-Ever Bank Failures
Collapse is second-largest, behind Washington Mutual

Bank	Assets	Deposits
Washington Mutual	$307 billion	$188 billion
First Republic	**$229 billion**	**$104 billion**
Silicon Valley Bank	$167 billion	$119 billion
Signature Bank	$110 billion	$89 billion
IndyMac	$32 billion	$19 billion
Colonial Bank	$25 billion	$20 billion

Sources: Company filings, FDIC statements
Note: Data represent failures from October 2000 to the present

Bloomberg

Conclusion; A blueprint is in place for the US regional bank consolidation

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