October '21

To:	Our Valued Investors	**From:**	Chan Wai Chee
Letter:	M02/2021/10	**Dept:**	Managed Account
Email:	MAenquiries@phillip.com.sg	**Date**	4 October 2021
Re:	Bond yields rising, Another reflation play, Slowing China, Forex, Gold, US	**Re:**	Functions, as fundamentals

Bond yields have risen

After hardly moving in August and most of September, the US Treasury 10-year yield has taken off from 22 September from 1.32% to 1.52% (recent high 1.56%). JGB has moved from 0.035% to 0.06%. Together with the Bund, these three are saying that the low on 4 August is the low for now.

Taper talk is a little aged. But one cannot rule it out, as a reason.

Perhaps it is window-dressing of some kind, as postulated by Jeff Snider (Alhambra Investments), resulting from the annual G_SIB assessment. The logic is that if banks unwind derivatives, there would be less demand for Treasuries, as collateral. Less demand means lower price and higher yield. Parallels are yield-bottoming in 2021, 2020, 2019, 2018 and 2017 happened on 4 Aug, 4 Aug, 28 Aug, 20 Aug and 5 Sep respectively. The strangest (sans fundamentals) was 2019, when the IMF announced global synchronized slowdown and the Fed cut interest rates. https://www.youtube.com/watch?v=6kfwRs-xlpY

Demand for T-bills remains high. The cost-beneficial way of getting the bills still remains via the RRP, which hit $1.6T on 30 Sep. Bills are bought in the secondary market, as well as at auctions, at yields below the RRP rate of 5 bps.

So, rise in yields may just be seasonal and temporary. How temporary? In 2017, it lasted 8 months, when there was the "global synchronized recovery" play. In 2018, it lasted 2 months, when October saw a mad scramble for safe-haven assets. In 2019, it lasted 4 months, when the world remembered that the Fed cut rates and the IMF issued a "global synchronized slowdown" statement few months before. In 2020, it lasted 8 months, when there was the first Covid-reopening and rising commodity prices.

In 2021, we may have the ultimate Covid-reopening, as global vaccination reaches acceptable levels and reopening protocols are being agreed between countries. The football crowds are not going away. On the other hand, slowing new orders and the eventual sorting-out of supply disruptions may put a stop to this run.

Important to us is that we have exited sovereign bonds in our SMART portfolio holdings, although on hindsight we would rather have done this earlier. Perhaps, next year, we exit on 4 August, regardless.

Also, important to us is to see if REIT prices will suffer as most did from 4 Aug 2020, and the years before. This would mean that the cash held back would be deployed if prices drop meaningfully, in line with rising yields. The aim will be to hold on or buy back the REITs that are less likely to lose value due to their defensiveness, or value, or if they benefit from Covid-reopening, or some positive corporate developments.

Another reflation play?

Or, if some kind of reflation play may tempt us into the local banks.

And, how do we do the reflation trade? This would be decided very soon, as markets react. For one month, the Vanguard Total Stock Index Fund (VTI) lost 2.5%, the Dow lost 3%, and the Nasdaq lost 5%. So far, we think we would more likely be in value instead of growth, either in US or global.

Meanwhile, we have been increasing our weightage in the older Energy stocks in certain portfolios, as the world tackles energy supply disruptions. Other portfolios probably will also participate, valuations permitting.

China

We have also been reducing our exposure to China, as its economy continues to slow, preferring the high dividend ones, which yield as high as 9%.

China Evergrande missed its USD interest payment, but paid its RMB interest payment. So, it appears that there is enough RMB but not enough USD in China. There have been decreases in China’s and Belgium’s (an agent?) holdings of US Treasuries in July. There have been sales of China’s strategic reserves of aluminum, zinc and copper for 3 months. Are these to curb inflation or to secure USD?

The RMB exchange rate is holding up well, and so is our holding of the Fullerton RMB bond fund.

Forex

USD strengthens a bit.

Gold

As bond yields are rising, we reduce gold holdings.

As long as the current repo-financing (collaterals vs unsecured) system remains, we need Gold as a deflation hedge (little opportunity cost). This remains in the core part of SMART and Global Funds portfolios, and some customized portfolios, but at a weightage that is lower than before.

US

CFNAI for August is +0.29. So, it is positive, as far as US national economic activity is concerned.

Thank you

We are grateful for your continuing support.

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