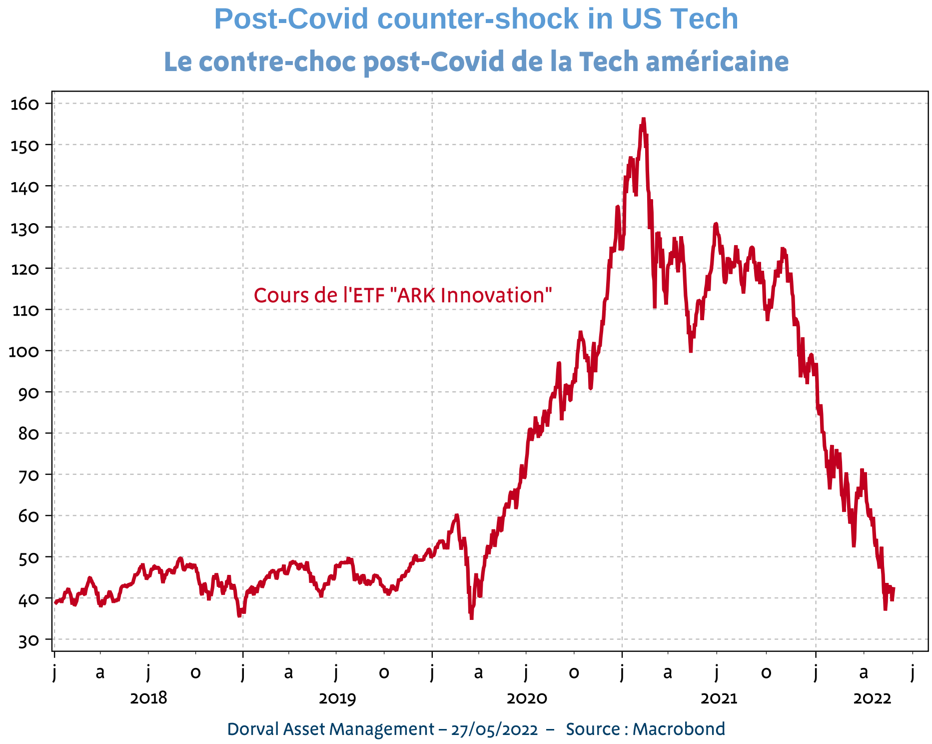
Exposure rates of the Dorval Asset Management Range – 27th May 2022

Dear Clients and Partners,

With the decline in US tech stocks petering out and the US bond market stabilizing, a rebound on the equity markets could be on the cards for the short term. However, the oft-mentioned notion of a peak in inflation must be set into context.

The key event of recent weeks for US investors was the fresh correction for tech stocks (cf. chart 1). This correction has no direct connection to recent macro-economic developments and rather reflects the ongoing stabilization after the bubble on so-called stocks of the future, which individual investors bought massively during 2020. The good news is that the current normalization in share prices now seems to be very mature, as reflected by major sell-offs on the cryptocurrency sector.



- *Price of "ARK innovation" ETF*

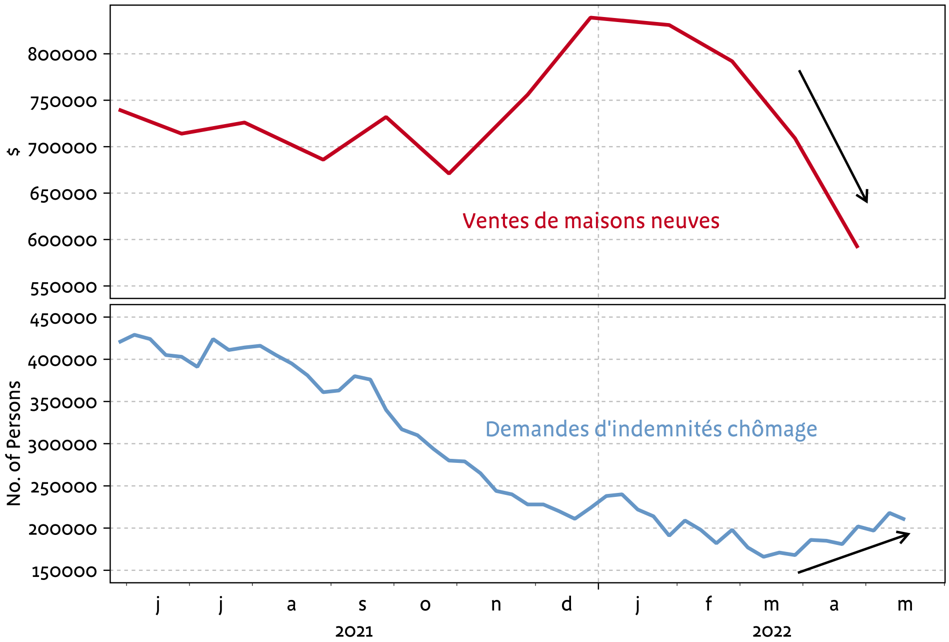
In addition to the good news on the healthier situation on the tech market, recent economic indicators suggest that the US economy could be moving from a phase of overheating to a period of moderation (cf. chart 2). The vast surge in real estate prices and soaring mortgage rates finally seem to be putting off buyers, as shown by the plunge in new home sales in April, shedding 16.6% after a 0.5% dip already in March. However, it is important to maintain a cautious approach as this decline also – or even primarily – reflects a lack of supply on the

NEITHER BEAR NOR BULL
BUT CAMELEON

market, while demand remains buoyant. So this is more of a crack than a crash. Meanwhile the composite PMI slid considerably in May to 53.8 vs. 56.0 in April, pointing to a normalization in growth. Lastly, jobless claims have edged up slightly again over recent weeks, settling above the 200,000 mark per month. If the US economy were to confirm its moderation, this would fuel the optimistic idea of a peak in inflation: this notion has been bandied about on the markets over recent days, fueled by easing core inflation stats over the past few months (+0.3% for the consumption deflator excluding food and energy in April, for the third month in a row).

Are the first cracks showing in the US economy?

Premiers craquements pour l'économie américaine ?



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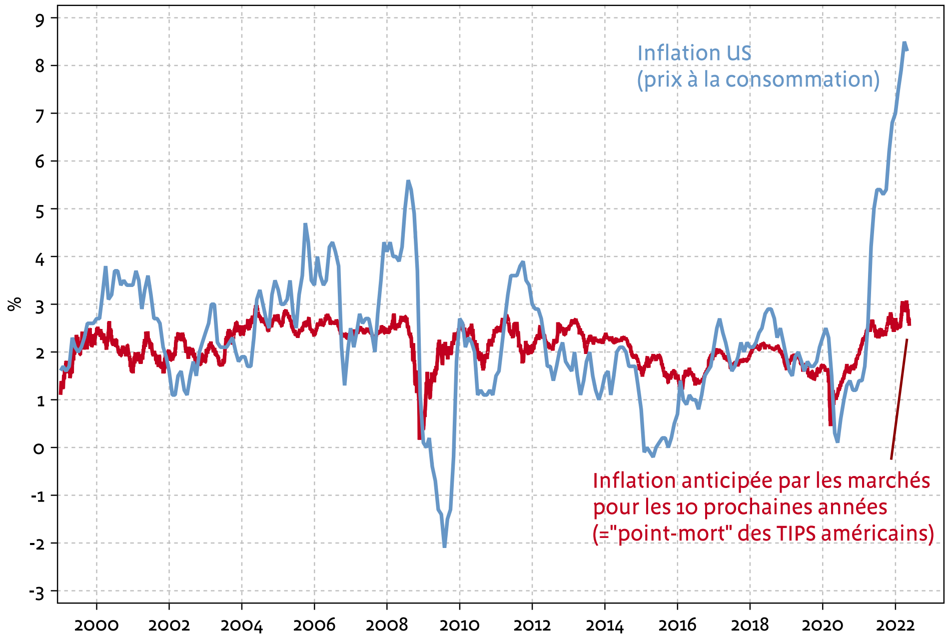
- *New home sales* / *Jobless claims*

However, this idea of a peak in inflation would merely serve to confirm the financial markets' – and even households' – already firmly rooted ideas. The markets have never priced in the scenario of lastingly high inflation (cf. chart 3). US inflation is currently at +8% yoy, yet the markets are expecting an average of less than +3% p.a. for the next ten years. This anchoring of inflation projections for the medium and long term is also visible among consumers, as shown month in month out by the University of Michigan survey. With normalized inflation already factored in by the various market participants, it has little chance of triggering a sharp plunge in long-term rates if it were to materialize, unless we expect a recession, which we feel is premature.

The markets do not believe in sustainably high inflation

Les marchés ne croient pas à une inflation durablement forte



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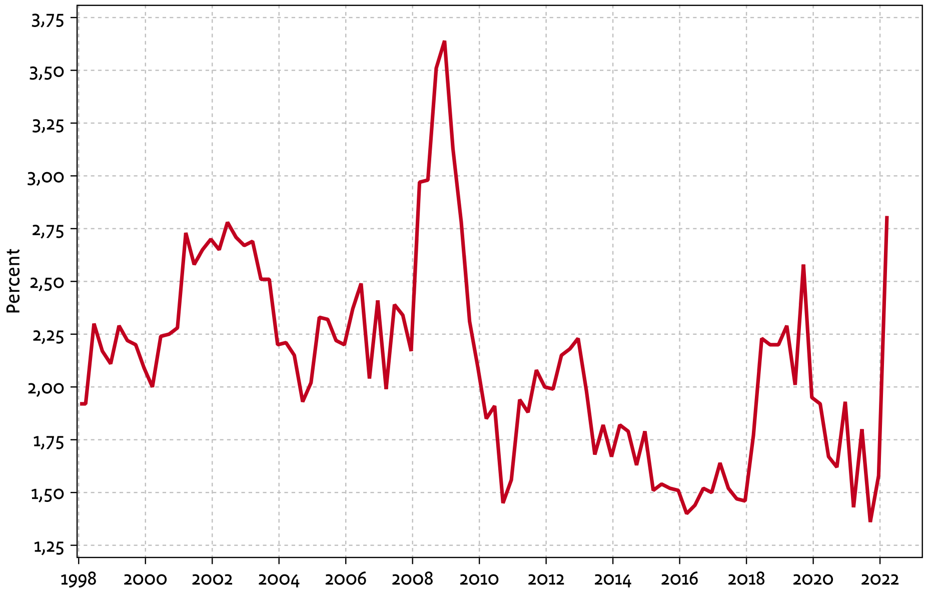
- *US inflation (consumer prices)* / *Inflation expected by the markets for the next ten years (= "breakeven" for US TIPS)*

On this side of the pond, a slowdown in inflation does not yet seem to be on the horizon. In recent surveys (Ifo, INSEE, PMI), euro area corporations have attested to strong economic resilience despite the dent from Ukraine, and indicated a continued rise in their sales prices. Wages are also climbing, with an upsurge of close to 3% in annual terms (cf. chart 4). Lastly, while the recent drop in gas prices is a welcome event, Brent prices are again drawing close to $120 per bbl. In light of these various factors, the ECB announced that it intended to step up interest rate normalization, with the aim of steering money market rates into positive territory by the end of the summer. The European bond markets – particularly the short end of the yield curve – therefore remain fragile.

Clear rebound in wages in euro area
Euro area composite indicator of negotiated wage rates (ECB compilation)

Net rebond des salaires en zone euro
indicateur composite des salaires négociés en zone euro (compilation BCE)



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Overall, the stabilization for both tech and the US bond market, as well as investors' currently overly pessimistic positioning have carved out some breathing space for the equity markets. Over the past two weeks, we have unwound the hedging previously taken out in our flexible portfolios. We have also further reduced our exposure to the dollar vs. euro in light of the tougher tone from the ECB. For the moment, we continue to steer clear of the bond markets, as their appeal is curbed by low inflation projections, subdued real rates and ongoing monetary tightening. Our international equity exposure remains highly diversified from a geographical standpoint: we believe that this diversification is particularly timely in the current environment, where situations change and contrast from one region to another now more than ever.

Our exposure rates are as follows:

- **Dorval Convictions**: our exposure rate is 69%.

DORVAL ASSET MANAGEMENT

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