RUBRICS

Tightening Fallout Continues

Fixed Income Macro View

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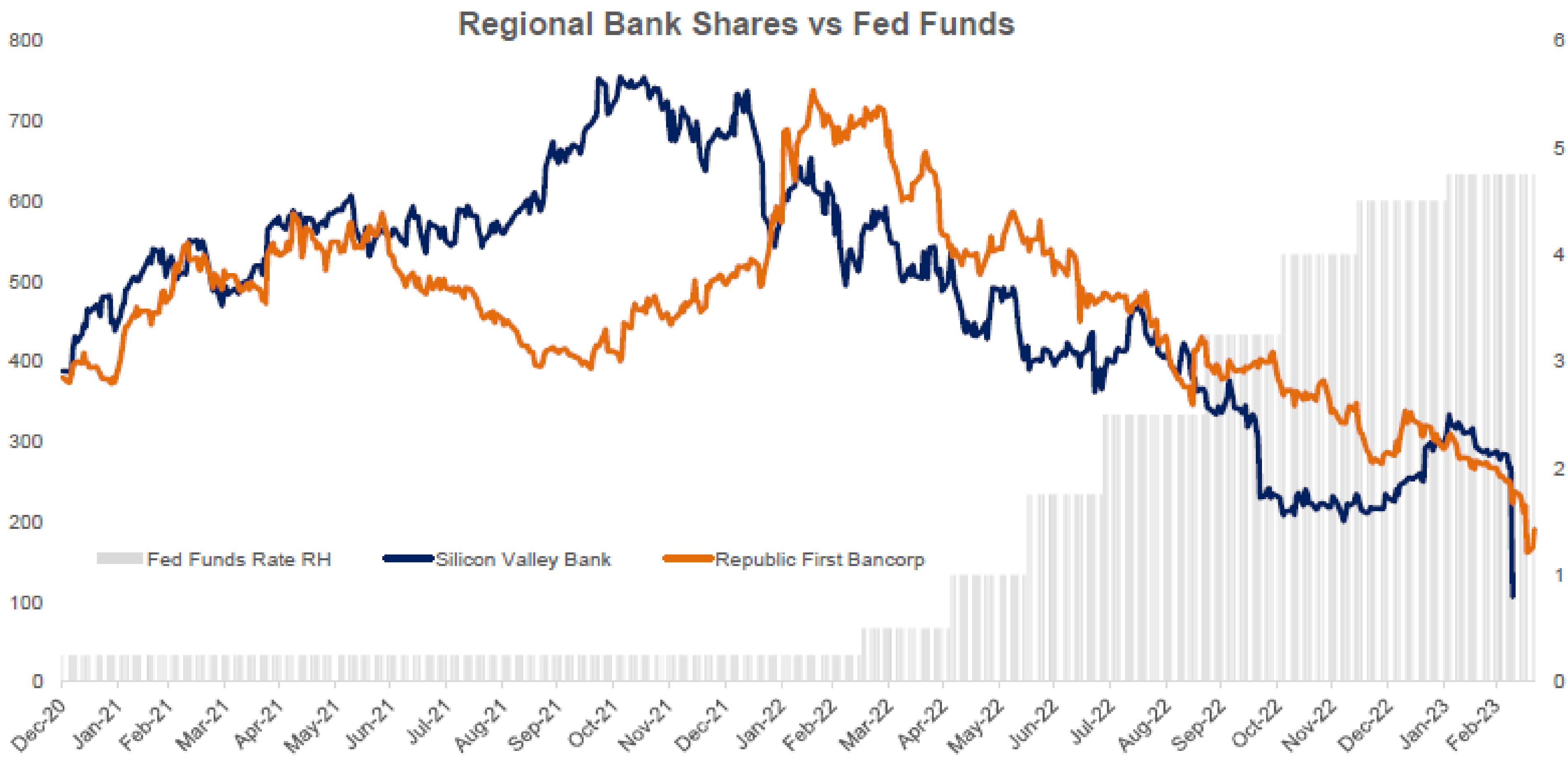
Same Same, but Different

Fears of a re-run of the 2008 banking crisis have gripped the US and Europe in recent weeks. At such times it is important to look through the hysteria and identify the drivers of the disarray. Key differences are evident between what we are witnessing today and the maelstrom of 2008. As we have written previously, confidence (or a lack thereof) is at the heart of today's crisis which has been driven not by impairments to loan books (or broader asset quality) but investment losses. The root cause of the erosion in confidence was the stretch for yield that occurred throughout the low rate environment of the last cycle (e.g. buying 10 Yr UST vs 1 Yr) and the failure to risk manage the exposure when the macro environment turned (higher inflation). This is a very different scenario to being on the hook to borrowers in an imploding asset class (e.g. subprime mortgages) with exposure to poor quality AAA (!?!) assets.

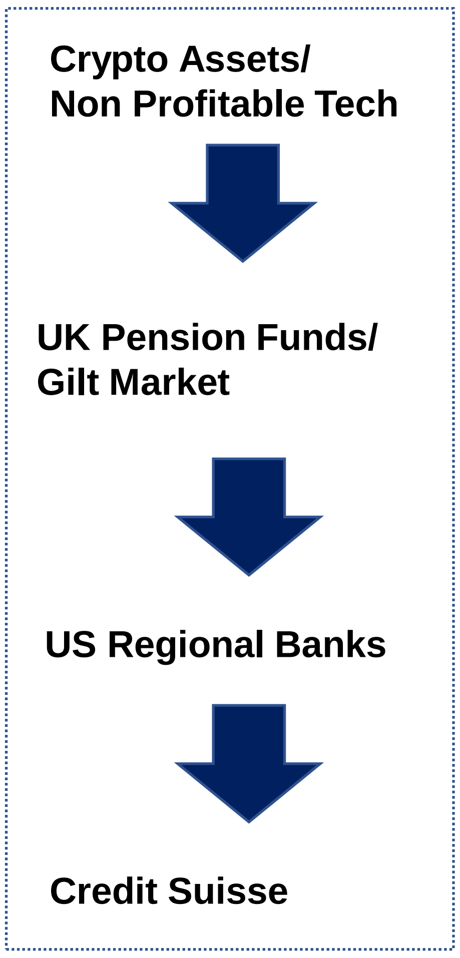
Why then does today's crisis feel eerily similar, particularly in terms of the speed of the collapse of certain banks? The answer lies in the fact that markets have been dominated by flow of liquidity not by fundamentals. Central banks have not only encouraged excessive risk taking by putting in place zero interest rates, but also through balance sheet expansion (QE) they have impacted the speed of growth in asset prices more than any other factor since 2008. Liquidity in - markets up, liquidity out - markets down. This fixation on flow over fundamentals has left the financial markets in a precarious position badly exposed to a changing macro environment. Just like the Asian crisis in the mid-1990's markets will continue to search out the next weakest link to try and exploit it – Deutsche Bank was next in line the markets mind regardless of the significant balance sheet improvements over the last 5 years.

Rate Hike Crunch - Silicon Valley Bank/First Republic vs Fed Funds



Source: Bloomberg as at 14/03/23

Domino Effect



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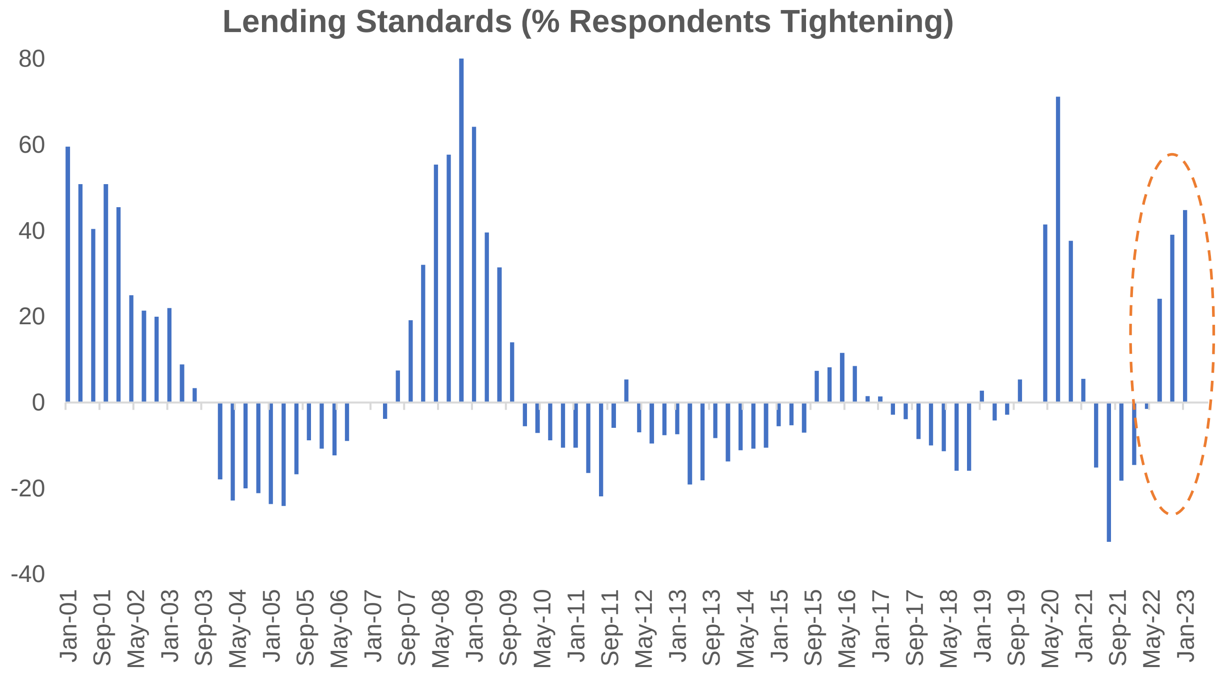
28 March 2023

Given the missed opportunity in early 2021 to head off the rise in inflation, Central Banks currently find themselves in a near impossible predicament: ignore the rising tensions in financial markets and risk an all-out financial crisis, or ease financial conditions and risk a resurgence in inflation like we saw in the early 1980's. Many of the talking heads in Financial Markets Media are clearly favouring an easing of financial conditions by rate cuts and the end of QT. Currently central banks are attempting to manage financial stability through increased access to liquidity while continuing to fight inflation with higher interest rates (albeit at a slower pace than was forecasted pre-SVB crisis).

Tightening vs Loosening

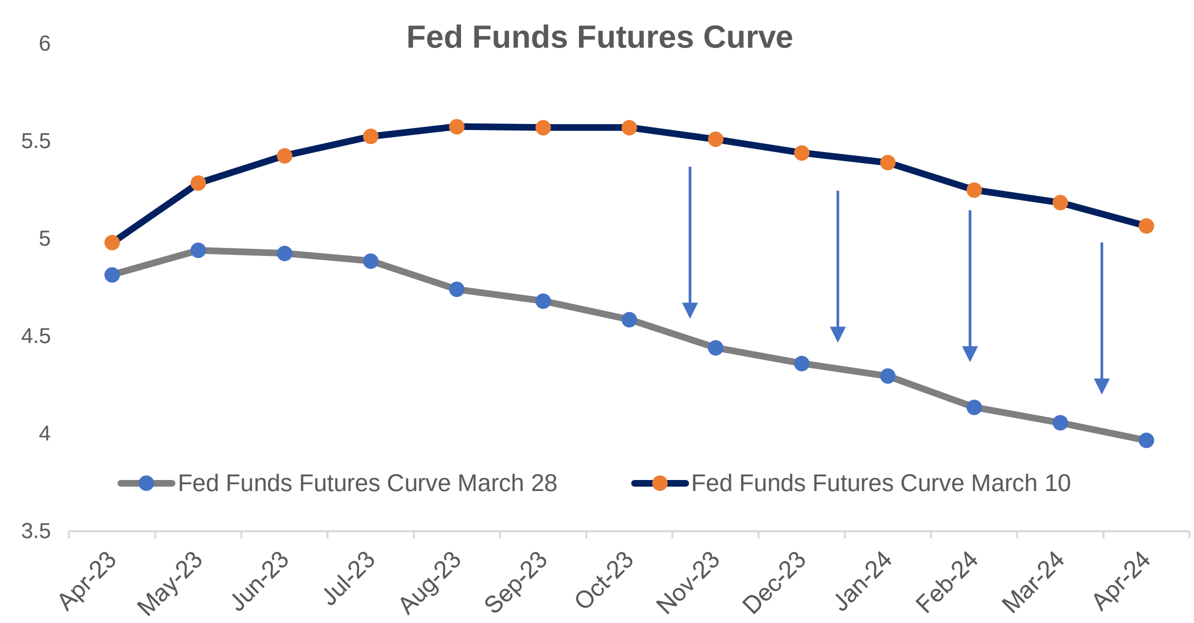
The reason the Federal Reserve, in particular, is indicating a slowing of interest rate rises is because they believe the current crisis, centred on the weaker (less diversified) regional banks which have been poorly risk managed, will tighten financial conditions. The Fed themselves have indicated that the impact could be equivalent to 50bps in rate hikes. Others, like the alternative investment firm Apollo Asset Management see the number closer to 150bp in rate rises due to a significant increase in bank lending standards. While it is unquestionable that the runs on bank deposits will have a material impact on banks appetite for lending, other offsetting factors do exist. Firstly the yield curve has already priced in a significant decline in interest rates going forward - the 2 year Treasury yield alone has fallen 100bp. We have also seen a significant increase in the Feds balance sheet through the increase in liquidity provided to the broader banking system as well as a significant shift of

De Facto Tightening – Bank Lending Standards



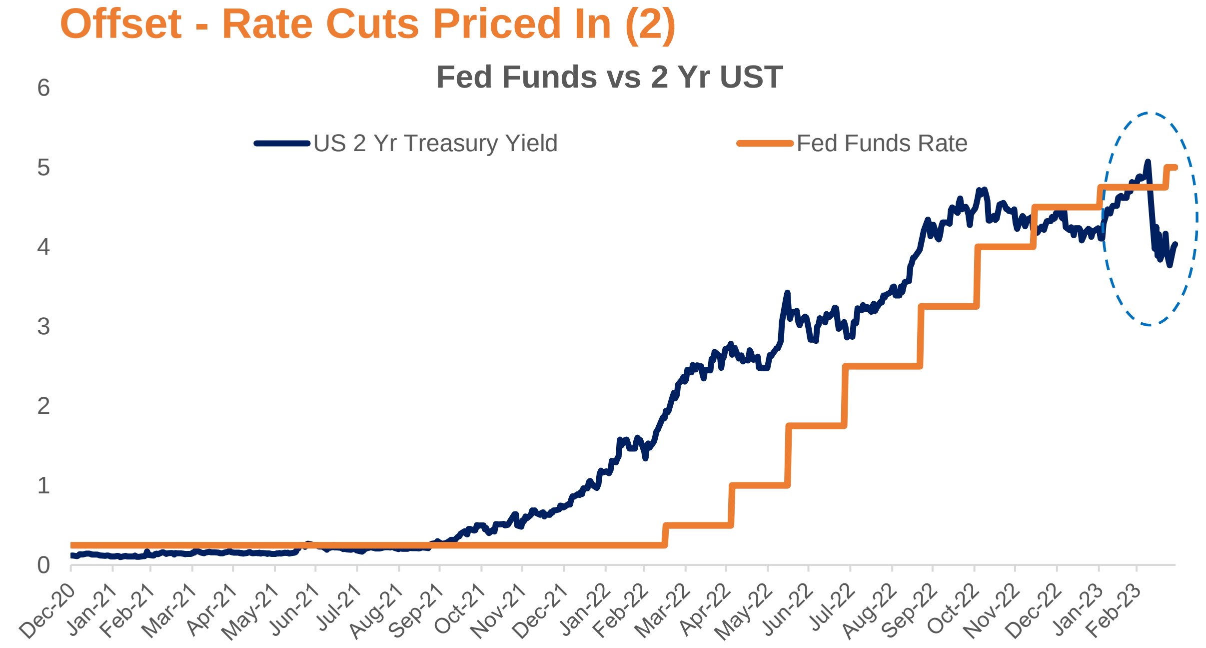
Source: Bloomberg as at 31/01/23

Offset - Rate Cuts Priced In (1)



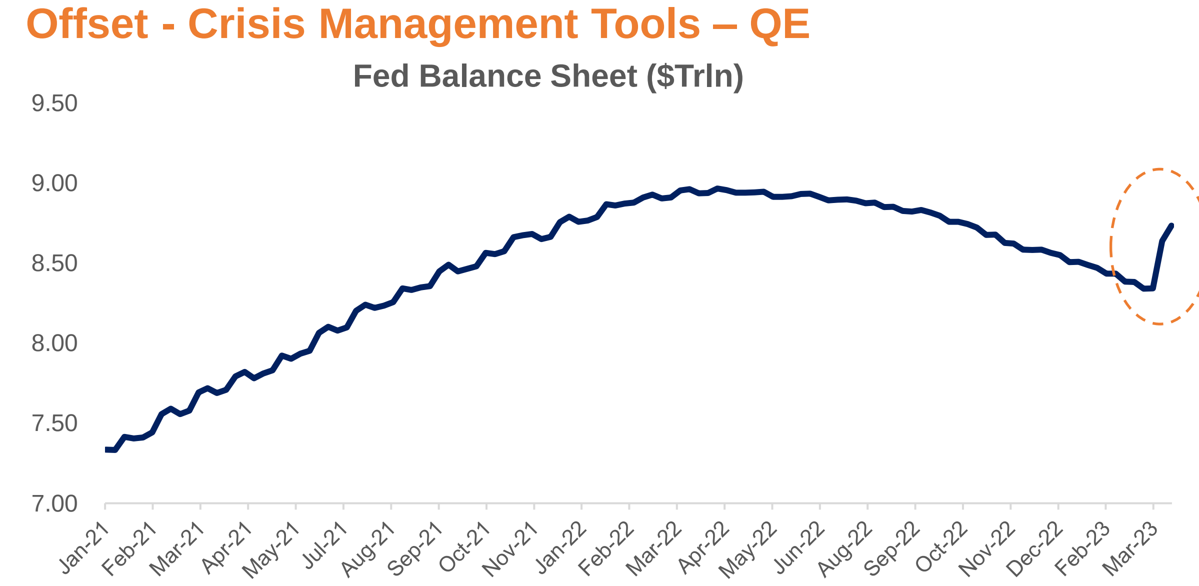
Source: Bloomberg as at 22/02/23

Offset - Rate Cuts Priced In (2)



Source: Bloomberg as at 22/02/23

Offset - Crisis Management Tools – QE



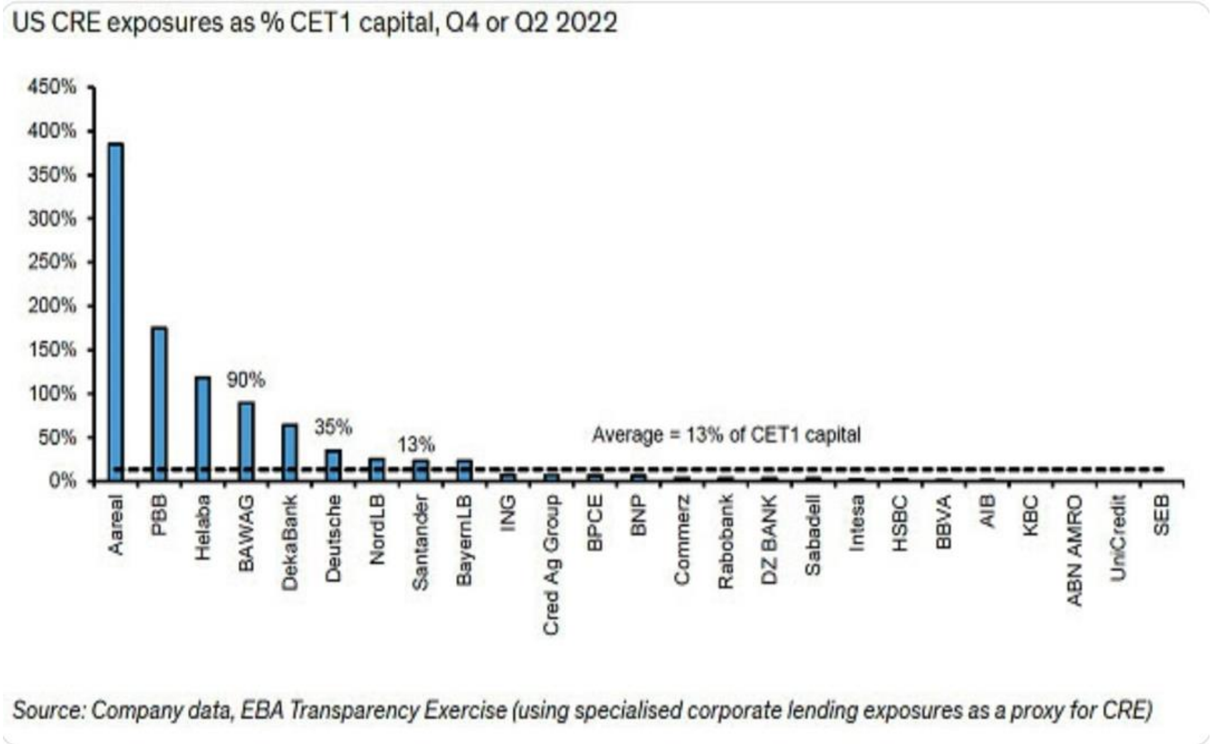
Source: Bloomberg as at 22/02/23

deposits from some of the regional banks to the majors like Bank of America or JP Morgan. While these positives don't necessarily offset the current crisis of confidence they are helping to assuage aspects of the markets' current concern.

While the focus is still very much on the banks, other asset classes continue to feel the heat of the rise in interest rates, in particular commercial real estate. Blackstone have already highlighted this issue with suspended redemptions on some of their larger funds in this area. Post Covid this has been an area of concern with a shift in business practices to a more remote (digital) working environment . Banks and other institutions with exposures to this asset classes will continue to come under great scrutiny over the coming months. In many cases however, in Europe for example, banks' activity in this area should not be significant enough to challenge their balance sheet strength, ceteris paribus.

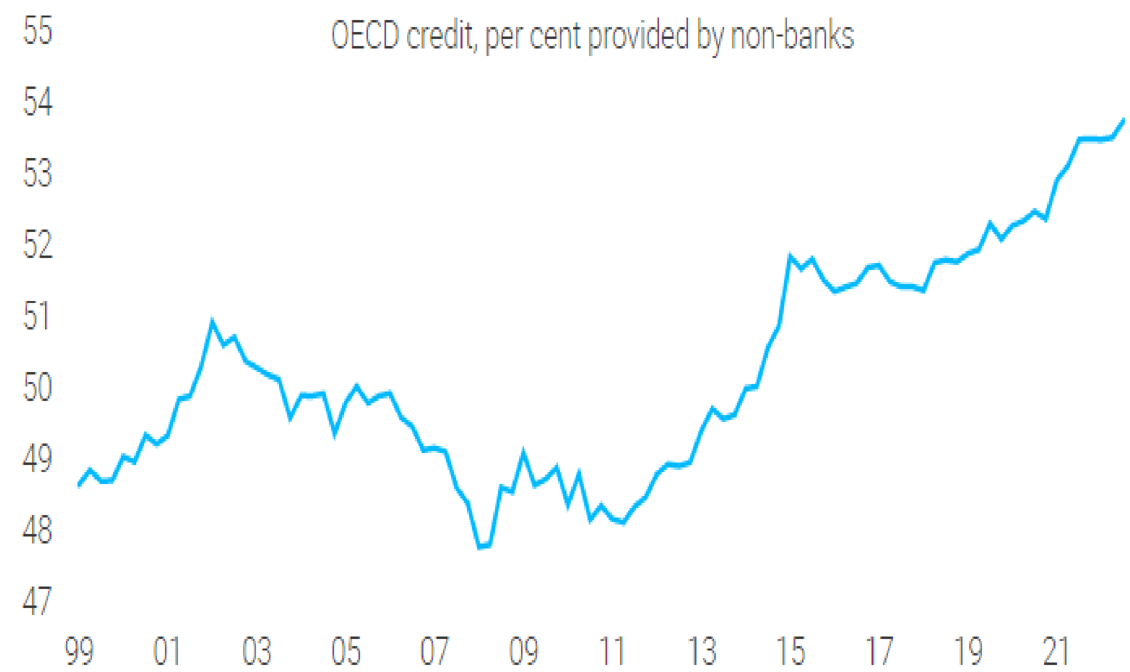
Where much of the lending has been undertaken in this is in the specialist lending, private debt markets. This is an area which we feel is most susceptible to a tightening of financial conditions given the explosion of debt in this space over the last cycle - the scale of which has been under appreciated by the regulatory and investment community alike. One of the key reasons for our concern is the shorter duration nature of the debt. Unlike the majority of investment grade bond market, private debt markets have much lower durations which means debt needs to be rolled on a more frequent basis. Much like the credit crunch that occurred in the corporate credit market in 2008, private debt markets might experience something similar over the next 12-18 months as the markets once again move to a world where liquidity is king.

US Commercial Exposure for European Banks (% CET1)



Source: Autonomous Research 24/03/23

% Credit Provided by Non Banks (OECD)



Source: TS Lombard Research 22/03/23

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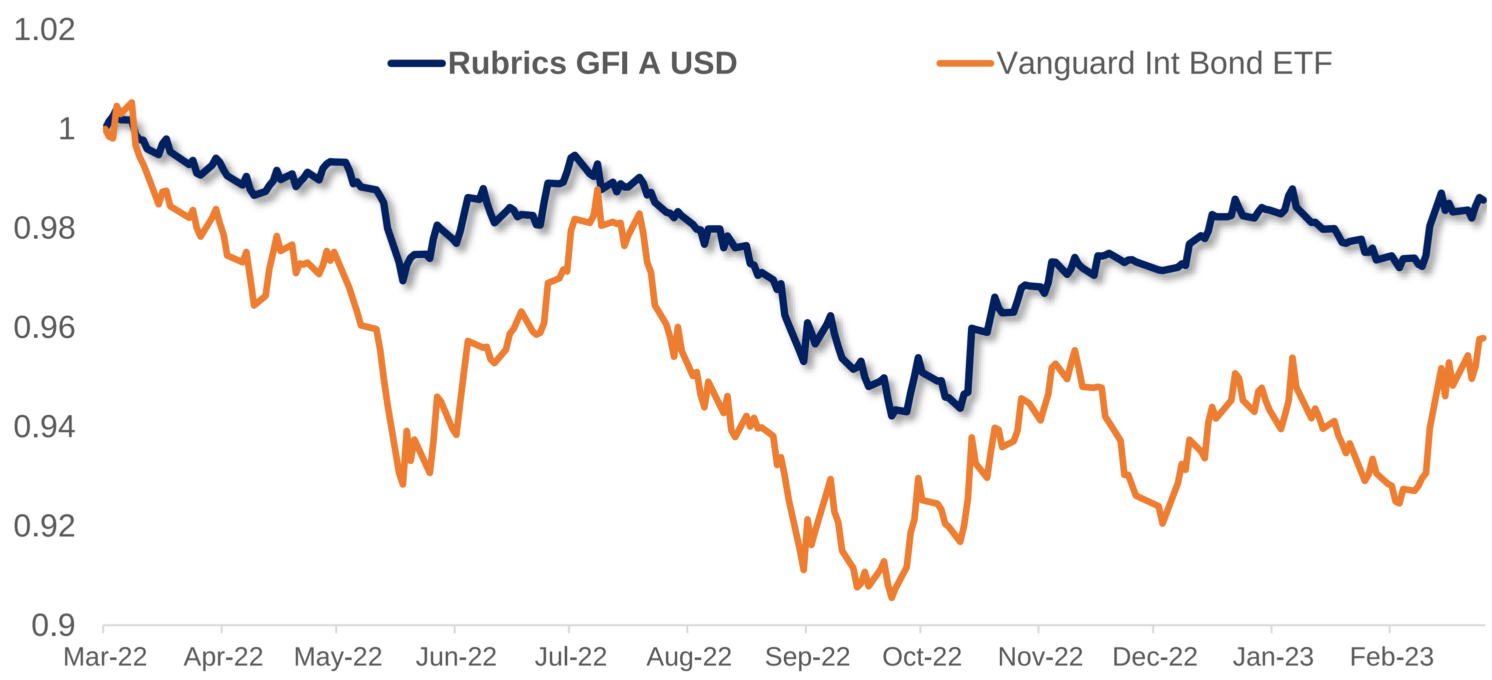
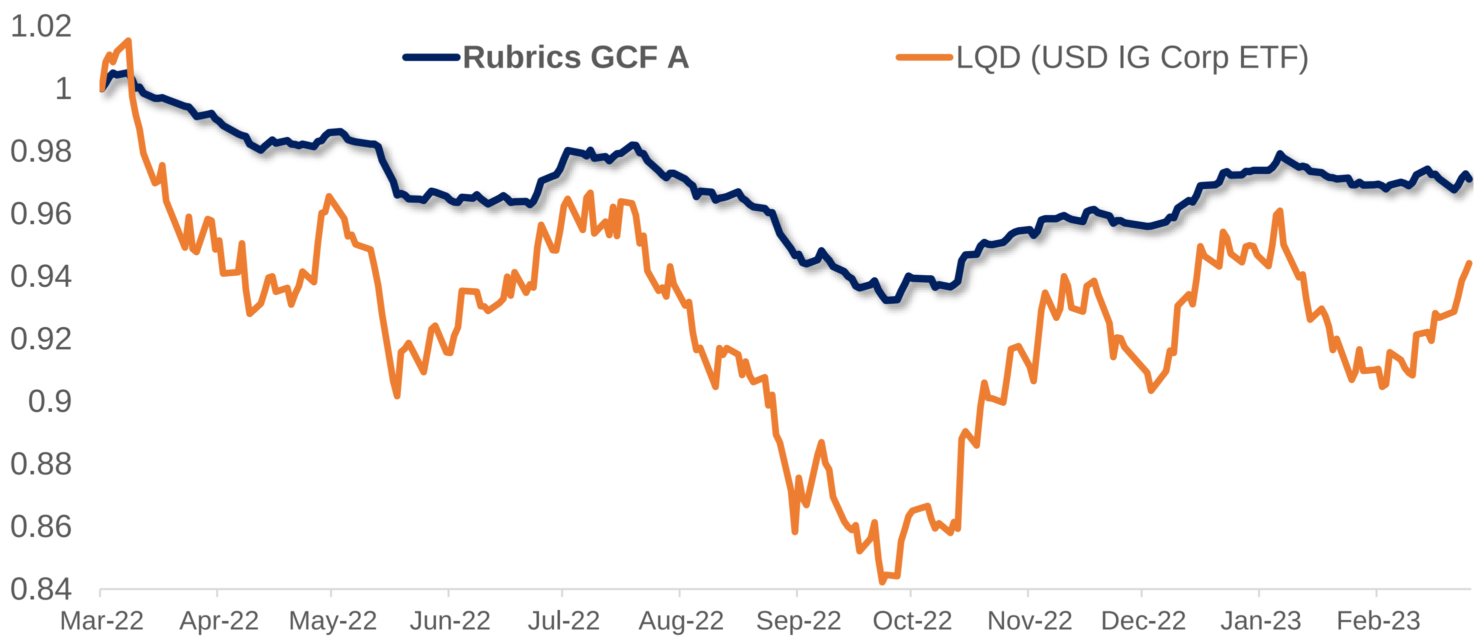
From the LDI crisis in the UK in sept 2022 to the US Regional bank stresses & Credit Swiss bank takeover the markets are clearly recalibrating to a world of less liquidity and easy money. This won't be the last time we see flare ups in the markets, far from it. As growth continues to slow financial conditions will tighten (growth is the key component) and the more the tide will continue to go out exposing poor risk management. This is an increasingly difficult balancing act for central banks and one in which a goldilocks outcome becomes ever more unlikely. What is clear to us is that there are asset classes that do offer protection, yield and liquidity against this difficult backdrop, and that is what we at Rubrics will be focusing on right now.

Rubrics UCITS Fund Performance – 1 Year



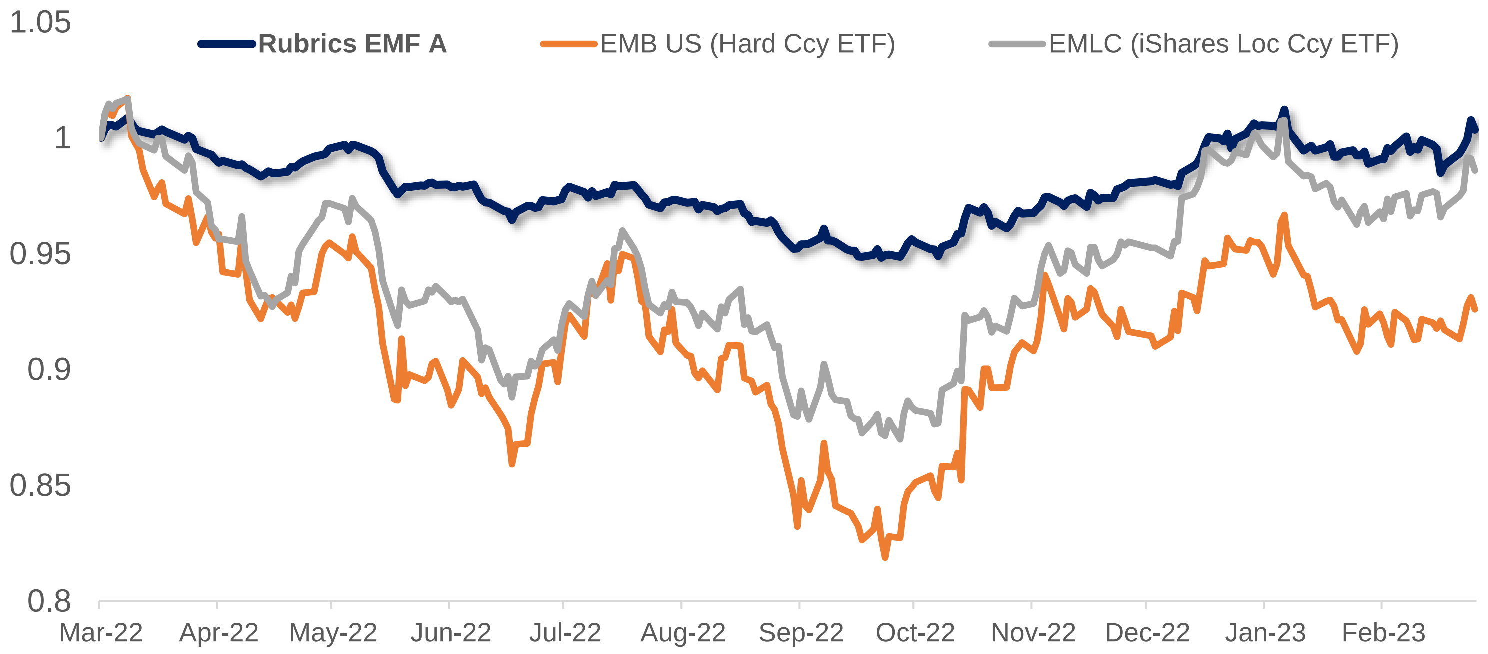
Return	1 Yr	3 Yr*	5 Yr*
Rubrics GFI	**-1.44**	**-1.62**	**1.20**
Vanguard	-4.22	-2.42	0.44

*Annualised
Source: Bloomberg as at 24/03/23



Return	1 Yr	3 Yr*	5 Yr*
Rubrics GCF	**-2.89**	**0.97**	**1.22**
LQD ETF	-5.59	-0.96	1.77

*Annualised
Source: Bloomberg as at 24/03/23



Return	1 Yr	3 Yr*	5 Yr*
Rubrics EMF	**0.34**	**0.90**	**-0.09**
EMB ETF	-7.44	-0.17	-0.86
EMLC ETF	-1.43	0.68	-3.32

*Annualised
Source: Bloomberg as at 24/03/23

IMPORTANT INFORMATION

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Additional Information for Switzerland: The prospectus and the Key Investor Information Documents for Switzerland, the articles of association, the annual and semi-annual report in French, and further information can be obtained free of charge from the representative in Switzerland: Carnegie Fund Services S.A., 11, rue du Général-Dufour, CH-1204 Geneva, Switzerland, tel.: + 41 22 7051178, fax: + 41 22 7051179, web: www.carnegie-fund-services.ch. The Swiss paying agent is: Banque Cantonale de Genève, 17, quai de l'Ile, CH-1204 Geneva. The last share prices can be found on www.fundinfo.com. For the shares of the Funds distributed to non-qualified investors in and from Switzerland and for the shares of the Funds distributed to qualified investors in Switzerland, the place of performance is Geneva. Carne Global Fund Managers (Ireland Limited reserves the right to terminate the arrangements made for the marketing of this product in any EEA jurisdiction in accordance with the UCITS Directive.