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Investment Letter No 13
Week 38
2019

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Yield Cockpit

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Overview current effective yields in USD *)

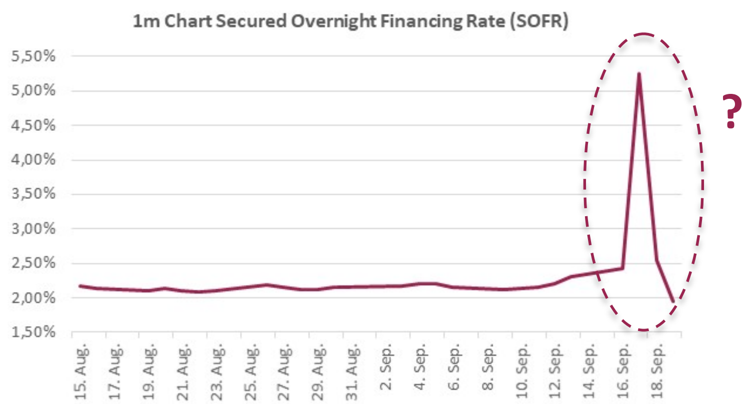
	current	3weeks ago
3 Months US T-Bills	**1.95%**	**1.91%**
2 Year US Treasury	1.73%	1.50%
5 Year US Treasury	1.65%	1.37%
10 Year US Treasury	1.77%	1.47%
3-5 Year IG Corp Bonds	**2.61%**	**2.39%**
7-10 Year IG Corp Bonds	3.11%	2.84%
15+ Year IG Corp Bonds	3.86%	3.56%
High Yield BB-rated	3.96%	3.87%
High Yield B-rated	5.82%	5.96%
EM Corporate Bonds	**4.38%**	**4.32%**
EM Sovereign Bonds	5.36%	5.41%
Spreads & Inflation		
FED Funds Rate	2.00%	2.25%
TED-Spread	0.21%	0.17%
10yr–2yr Treasury Spread	0.03%	-0.03%
5yr Breakeven Inflation	1.40%	1.36%
10yr Breakeven Inflation	1,59%	1.59%

*) derived from relevant BofA Merrill Lynch effective yield indices
mangenta = Gigant Swiss preferences

Source: BofA Merrill Lynch Indices retrieved from Federal Reserve Bank of St.Louis; Bloomberg Barclays Index Data; NY FED; all data as of 19th of September

What to take note of:

- **USD**-Bond **yields have retraced a good part of their massive August-drop**. The 2yr-Treausry yield rose from as low as 1.30% back to almost 1.80%, a level last seen back in July 2019. This is quite a massive move for such a short time frame! While yields rose across the curve, the **short end of the curve finally started to price in fewer rate cuts from the FED** for the months to tome. As regular readers might recall, we advocated hiding in 3 months T-Bill of late which proved to be more resilient. This continues to be the strategy of choice until the form of the yield curve normalizes again.
- **Another finding** of the August/September-yield move is that staying in cash in order to optimize the entry point of an investment is a tactic which is warranted even in fixed income markets. **Price moves may overcompensate the yield** carry (at least in the short run)!
- While not of direct impact to our investors so far, this weeks explosion in USD-funding rates in the interbank market should be monitored closely. Domestic cash demand before tax deadlines seem a reasonable explanation for the sudden rise in demand for USD-cash and the FEDs liquidity injection via Repo-markets should complete its task. However, the extreme volatility of the new SOFR-rate, that is the interbank rate which will be replacing LIBOR as benchmark for trillions in interest-derivatives and other financial instruments, is not exactly what investors want to see.



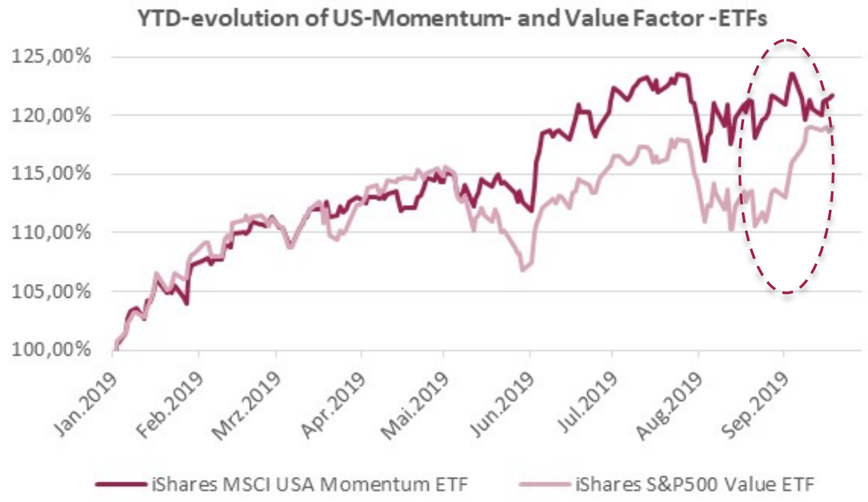
Upside for equities still limited….

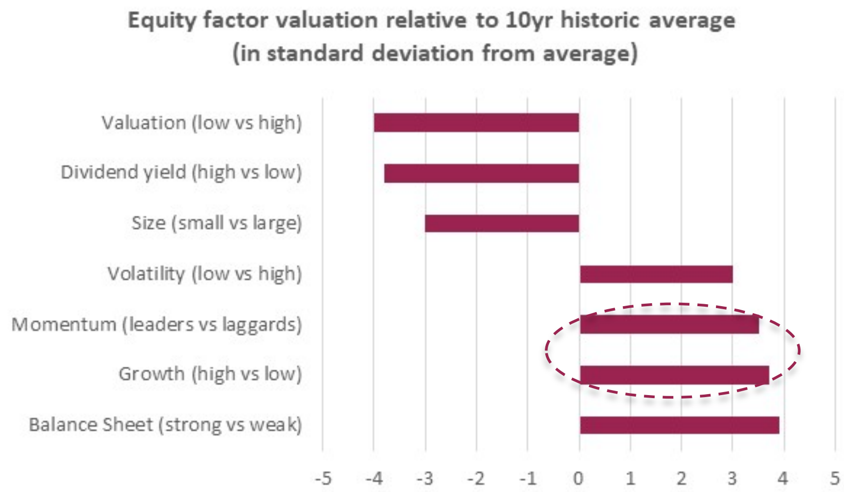
We have extensively covered the fact that **equity prices are currently driven by Central Bank policy and developments on the Sino-US trade war**, rather than corporate earnings. Regarding trade, we argued that with the newly announced tariffs from early August, both, the macro economic outlook as well as risk asset prices look increasingly vulnerable. Then, in another surprising development, came the announcement from early September of renewed high level talks between US and Chinese officials, scheduled for early October. That was enough to send risk asset prices back up within reaching distance to their all time high marked in late July. **Our main scenario is still that there won't be such thing as a "quick fix" to this trade conflict**, but we acknowledge the fact that risk assets remain remarkably resilient, not last thanks to the fact that global macro economic data have held up somewhat compared to lowered expectations. Furthermore, **Central Banks around the globe help to hold up investor sentiment** with their announcement for further Quantitative Easing. For us, there are still way **too many conflicting signals which is way we maintain our defensive positioning** for now, also in light of the accumulated performance this year. Anyhow, we note that **a tail-scenario** could be one **in which risk assets** fuelled by a cocktail of surprisingly good news (et. continued central bank stimulus, "less bad" economic data, non-implementation of announced tariffs and/or others) could lead to a **"melt up"-**scenario of risk-asset prices **in which a wave of under-positioned investors would need to chase prices** higher and higher- no matter how high the valuation would rise. Again, for now this is NOT our base case but we must be aware of the fact that if such a scenario was about to unfold, we would need to adapt our positioning in a rather quick and extensive way. While the broader market advanced only modestly over the last weeks, there were some **major rotations to be witnessed under the surface**. On a sector level, **cyclically-exposed sectors** such as Transport- and Financials- **rallied very sharply** out of oversold-territory **while bond-proxies** like utilities and secular growth stocks such as software & services **sold off** in a rather spectacular way. The **most spectacular move** however occurred on the "factor-front". **Momentum stocks**, i.e. those who have performed best in the past, **tanked by the most in more than 10 years**(!) during the first half of September. Momentum's counterpart, **value-stocks but also small-caps**, i.e. those who performed poorest so far in 2019, **rallied sharply**.

Source: FIS Market Map

..but major reshuffling under the surface

One the one hand, **less bad than feared economic data**, **rising bond yields** as well as the before mentioned **perceived improvement in trade negotiations** were cited as **catalyst for this violent rotation**. On the other hand, various investor surveys suggest that momentum was an extremely crowded trade (which at some point needs to be unwound). In retrospective, it does not come at a surprise that the unwind of momentum came precisely at a time the 10year Treasury yield surged from 1,45% to 1.75% as most of the stocks within the momentum group were perceived as "bond-proxies". Going forward, the all important **question is whether this reversal** in momentum **signals the start from a broader rotation from "growth" into "value"** (remember: value stocks being those stocks which appear under-priced from a fundamental perspective) as the later group has suffered a multi-year trend of underperformance? It is well known that the valuation of "value"-stocks are extremely cheap, both in absolute terms but also relative to other groups such as momentum or quality-stocks- a situation which by the way has persisted for the last few years. However, rather than the valuation dispersion, **the speed of economic growth is key for determining the performance of various investment styles**. Historically, value stocks have performed best during times of either very strong or poor / negative economic growth. During times of modest positive growth (like what we have seen for most of the past decade), growth stocks (i.e. those who tend to grow above the rate of the overall economy) but also value-stocks performed best. Going forward, despite the fact that valuation dispersion among factors is high, **we believe that "growth" will remain the style of choice** for investors….unless the economy finally dips into a recession at some point.





Source: FIS Market Map; Goldman Sachs

Our Tactical Asset Allocation (6months horizon)

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EQUITIES –> REMAIN UNDERWEIGHT

- Since early August, we hold an "underweight" rating on equities for which we argued **the current risk-reward ratio** (high valuation, trade war) **is rather poor** since equity markets have performed between 15-20% year-to-date and we prefer to lock in parts of the accumulated gains. Anyhow, as highlighted on page 4, we are aware of the fact that under a scenario of surprisingly positive developments, we would be required to not only increase our equity allocation but also to rotate in more cyclical sectors and higher beta-stocks. The **trigger for this scenario would likely be a decisive break above the upwards-trend line** which has not been broken since more than 20 months *(see chart on page 4).*
- As long as we maintain our base case scenario, **we also maintain most of our defensive sector preferences for now** (pharma, consumer defensives and technology). We remain highly selective within technology who is exposed to the deteriorating momentum-factor. **Utilities, a classic bond-proxy is removed from our preferred list** as yields seem to have marked an intermediate low.
- Factor- and style-wise, we remain tilted towards growth and remain equally selective in term of momentum (*see page 5 for details).*

CASH –> REMAIN NEUTRAL

- **Boring but save & stable**. With stocks near record highs and after one of the strongest quarters for bonds in a decade, holding cash for some time is by no means wrong. As we explained in our last edition, **holding cash in form of short term fiduciary deposits or Treasury-Bills is most likely more attractive than buying longer term bonds**. An as a side effect, keeping cash leaves investors with enough dry powder for eventual future opportunities (wherever they might arise). One of the most renowned investors of our time, Warren Buffet's Berkshire Hathaway is doing exactly this- they are sitting on a record high cash pile worth 122bn USD of cash- and are happy with it.

Our Tactical Asset Allocation (6months horizon)

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BONDS –> REMAIN NEUTRAL

- The **reversal in yields** over the last 2 weeks **is not the beginning of a new trend** but suits as a good example that duration adds leverage to a portfolio- both to the up- as well as to the downside. If one does not get compensated for taking this extra risk, holding longer duration bonds (whose yield is lower than that of short term bonds) implies betting on even lower rates and that is not our investment case for now.
- Corporate leverage is at all time high and thus an eventual sharp global economic downturn would send credit spreads substantially higher- maybe not a risk for tomorrow but the more intermediate future. True, high earnings margins and low rates have supported low spreads for now but we are of the opinion that the current credit spreads do offer a poor risk reward-ration. **We** rather **buy / hold corporate bonds with relatively solid credit fundamentals**.
- We are of the opinion **that demand for "carry trades"** which are "en vogue" during period of low rates will continue to **keep demand for Emerging Market Bonds high**, no matter that the US-Dollar remains notoriously strong and an escalating trade war weighting on macro economic growth dynamics.
- We continue to avoid riskier buckets of the bond market such as High Yield, Senior Loans or Convertible Bonds.

ALTERNATIVES –> REMAIN OVERWEIGHT

- We have advocated exposure to gold for some time and **we continue to believe that over the medium term (i.e. > 12months time), gold will shine further**. Some weeks ago, when gold was approaching the 1'550 USD per ounce-level we also noted, that it could be due for a pause. Now, **around 1'500 USD, those who do not yet have any exposure to gold may well start adding positions**. Around 1'460, there is ample support for the yellow metal.

House View: our Preferences on one Slide

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Asset Class	We Like	We Don't Like
Equities	*Area*: **Diversification among US, EM** *Sectors*: **Pharma, Consumer Defensives, ~~Utilities~~, Technology** *Style:* **Growth (with Quality)**	*Area*: **China; UK, Switzerland** *Sectors:* **Telecom, Energy** *Style:* **High growth *without* quality**
Bonds	*Duration:* **Medium term duration** up to **5** years. *Area:* **US**; ***selected* Emerging Markets** *Credit:* **low grade IG**	*Duration*: **long term duration >10 years** *Area*: **China** *Credit:* **EU & US High Yield; Senior Loans; Convertible Bonds**
FX & Commo-dities	*FX Majors:* **USD; JPY, CHF** *Commodities:* **Gold**	*FX Majors:* **GBP** *FX Minors:* **TRY** *Commodities:* **Base Metals, Crude Oil**
Alternatives	*Alternatives:* **Gigant Option Based Equity Growth Strategy; strategies with uncorrelated payoffs to equity & bond market direction**	

mangenta = recent changes

Overview US Equity Model Portfolio

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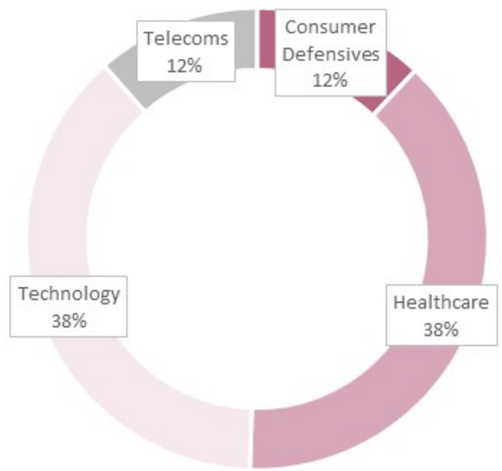
Performance Overview	2019	2018	2017	ITD *)
Gigant US Equity Model Portfolio	**+23.94%**	**-1.24%**	**+17.56%**	**+43.90%**
S&P 500	+20.20%	-6.24%	+19.4%	+34.59%
Dow Jones	+16.15%	-5.63%	+25.1%	+37.10%
Nasdaq 100	+24.83%	-1.04%	+27.1%	+62.47%

Current Situation:	
Current Value:	1’419’048 USD
Start Value:	1’000’000 USD
Realized Gains:	+386’722 USD
Unrealized Gains:	+26’306 USD
Cash:	636’662 USD (44%)
Equities:	802’386 USD (56%)

Evolution of 1Mio USD invested into the Gigant US Equity Model Portfolio since inception:

Current Sector Allocation:



computed by stockopedia.com; all data as of 19th of September; *) inception date = 31th of Dec 2016

Constituents of our US Equity Model Portfolio

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GICS Sector	Stock & Performance		
Energy			
Basic Materials			
Industrials			
Consumer Discretionary			
Consumer Defensives	**CVS Health** -21,00%	**Philipp Morris** -3,72%	**Intuitive Surgical** 11,60%
Health Care	**Merck** 42,60%		
Financials			
Technology	**Alphabet** 19,40%	**Microsoft** 18,20%	**YY** -36,00%
Telecom	**AT&T** 2,54%		
Utilities			
Real Estate			

performance = price return exluding dividends

computed by stockopedia.com; all data as of 19th of September

Changes to our USD Bond Portfolio:
SELL BNP Paribas 2025 to BUY Bank of Montreal Perpetual

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BNP PARIBAS

3.375% BNP Paribas 09.01.2025

Rating:	A-
Sold at:	103.00%
Hold. Period:	**119 days**
Tot. Return	**+5.63% *)**

Rationale of Disposal: We have bought this bond just 4 months ago for 2 reasons: 1) to add duration to the portfolio and 2) in expectation that the spreads of IG-bonds would compress further. Both effects have now materialized and after 4 months, we can now lock in a return which equals that of 1,6-years of coupon carry.

About the Issuer: BNP Paribas SA is a universal bank headquartered in Paris with four domestic retail banking markets: France, Belgium, Italy and Luxembourg. It has other retail banking operations throughout Europe, as well as in the US and in the Mediterranean basin (e.g. TEB in Turkey). BNP Paribas is also a significant player in the consumer finance and in the insurance space and, on top of that, provides wealth and asset management services. In addition, the bank allocates as much as c30% of its capital to its corporate and institutional banking unit, a leading franchise in Europe.

BMO

4.8% Bank of Montreal Perpetual

Rating:	BBB-
Buy Price:	100.35%
YTM:	**4.78%**
Duration:	**20.83**
Min. Size:	200'000 USD

Investment Rationale: ***This bond is a subordinated additional Tier 1-security. It is a perpetual-bond without final maturity but the issuer may early call it on 25th of August 2024. If not, the interest will automatically be reset at a pre-defined spread-level.*** During times of compressed yields, we are of the opinion that subordinated bank debt of top tier banks (Bank of Montreal's senior bond is AA-) is offering a superior risk-reward profile. We consider the likelihood of a call in 2024 as relatively high which is why we are not concerned by the perpetual-nature of this instrument.

About the Issuer: Bank of Montreal which was established back in 1817 making it Canada's oldest bank serves more than 12mio personal, corporate and institutional clients in North America and internationally. The bank, which is considered to be the 8th largest in America by assets (774bn CAD) generated a net income of 5,8bn USD in 2018

*) non-annualized total return including coupon payments, changes in accrued interest and price changes; all price data from FIS Market Map

Changes to our USD Bond Portfolio:
SELL Pemex 2022 to BUY Hyderabad Airport 2024

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PEMEX

5.375% Petroleos Mexicanos 13.02.2022

Rating:	BBB+
Sold at:	104.875%
Hold. Period:	**92 days**
Tot. Return	**+7.17% *)**

Rationale of Disposal: Back in June, we bought this bond after its yield increased by about +1% over the course of a few weeks on fears of an imminent loss of Pemex' investment grade-rating. In mid September, the Mexican government injected approx. 5bn capital into Pemex which then announced to use this it to buy back some of the existing debt (among them this security). This news lead to a collapse in Pemex's credit spreads and we are more than happy to tender our bonds at current levels so that we can use the proceeds for an investment into a higher yielding alternative (see below).

About the Issuer: Pemex is Mexico's national oil company and it is 100% owned by the Mexican state. We remain of the view that the Mexican government will continue to support Pemex, if needed, to ensure that the company remains current with financial and supplier obligations.

HYDERABAD RAJIV GANDHI INTERNATIONAL AIRPORT

5.375% GMR Hyderabad Int. Airport 10.04.2024

Rating:	BBB
Buy Price:	103.25%
YTM:	**4.57%**
Duration:	**3.91**
Min. Size:	200'000 USD

Investment Rationale: In our eyes, Hyderabad Airport is one of the ever smaller group of BBB-rated issuers offering a decent yield of 4-5% in the 5-year maturity bucket, a maturity frame which saw a flood of new issued recently. By switching the tendered Pemex (see details above), we may pick up >+1,5% yield for two years of duration, which in the context of our total portfolio, is perfectly fine.

About the Issuer: GMR Group is one of India's leading Infrastructure companies with business interests across Airports (6 airports in operation, 3 in planning); Energy (14 power projects, 9 operational (4,4MW)); Transportation (toll roads) & Urban Infrastructure. GMR Infrastructure Limited ("GIL"), the flagship entity of the group, which houses all the assets is listed on Bombay Stock Exchange & National Stock Exchange. GMR Hyderabad is the 4th largest private airport operator worldwide.

*) non-annualized total return including coupon payments, changes in accrued interest and price changes; all price data from FIS Market Map

Overview USD Bond Model Portfolio

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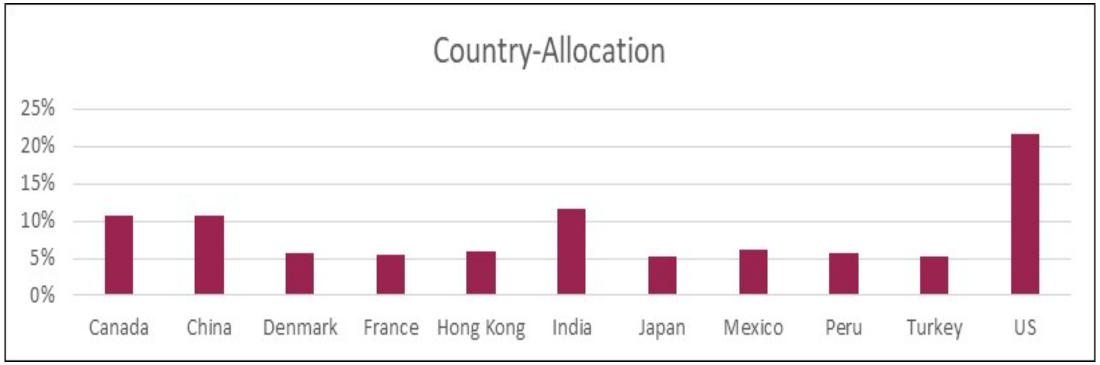
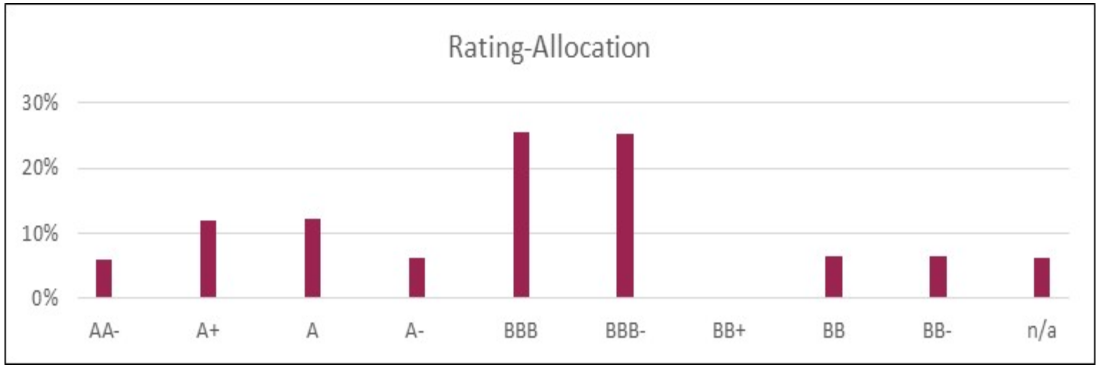
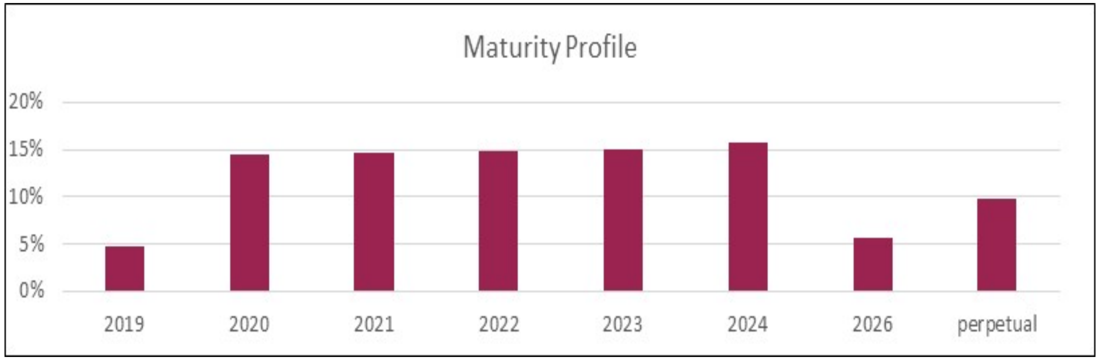
Performance Overview	YTD	2018	2017
Gigant USD Bond Model Portfolio	**+7.07%**	**+1.00%**	**+4.70%**
Bloomberg Barclays US Aggregate Index	+7.95%	+0.01%	+1.17%
Bloomberg Barclays EM USD Aggregate Index	+7.76%	-2.46%	+6.87%

Current Situation:	
Weighted average YTM:	3.26%
Weighted average Duration:	4.1







Source of data: FIS Market Map; own calculation; all data as of 20th of September

Constituents USD Bond Model Portfolio

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	Coupon	Bond Instruments	Maturity	Rating	Country	Industry	YTM	Duration	Bid-Price	minimum size	Allocation
	4,125%	SEMICONDUCTOR MANUFACTURING INTERNATIONAL CORPO	07.10.2019	BBB-	China	Electrical & Electronic	1,74%	0,0	100,09	200.000 USD	4,79%
	4,950%	BARRICK (PD) AUSTRALIA FINANCE PTY LTD	15.01.2020	BBB-	Canada	Mining & Refining	1,46%	0,3	101,07	2.000 USD	4,88%
	4,375%	AFRICA FINANCE CORPN	29.04.2020	A3		Supranational Agency	3,09%	0,6	100,75	200.000 USD	4,85%
	2,343%	FORD MOTOR CREDIT COMPANY LLC	02.11.2020	BBB	US	Finance & Investment	2,98%	1,1	99,31	200.000 USD	4,71%
	5,950%	GAP INC	12.04.2021	BB-	US	Supermarkets & Stores	3,31%	1,5	103,98	200.000 USD	5,16%
	2,362%	CENTRAL NIPPON EXPRESSWAY COMPANY LIMITED	28.05.2021	A1	Japan	Railways & Transportation	2,43%	1,6	99,88	200.000 USD	4,77%
	2,125%	CORPORACION ANDINA DE FOMENTO (CAF)	27.09.2021	AA-		Supranational Agency	2,37%	1,9	99,52	1.000 USD	4,73%
	5,375%	VOLCAN COMPANIA MINERA S.A.A.	02.02.2022	BB	Peru	Mining & Refining	3,99%	2,1	103,08	200.000 USD	5,08%
	2,750%	STATE GRID OVERSEAS INVESTMENT (2016) LIMITED	04.05.2022	A+	China	Utilities	2,51%	2,5	100,61	200.000 USD	4,84%
	2,500%	PHILIP MORRIS INTERNATIONAL INC.	22.08.2022	A	US	Tobacco	2,27%	2,7	100,66	1.000 USD	4,84%
	3,100%	GENERAL ELECTRIC CAPITAL CORPN	09.01.2023	A	US	Finance & Investment	2,67%	3,0	101,34	200.000 USD	4,91%
	5,250%	LOUIS DREYFUS COMPANY B.V.	13.06.2023	n/a	France	Commodity Trading	4,75%	3,2	101,67	200.000 USD	4,94%
	3,875%	DANSKE BANK A/S	12.09.2023	A-	Denmark	Banking & Finance	3,02%	3,5	103,18	2.000 USD	5,09%
	4,750%	INDIAN OIL CORPN LTD	16.01.2024	A-	India	Oil & Petroleum	3,14%	3,8	106,43	200.000 USD	5,41%
	5,250%	ALFA, S.A.B. DE C.V.	25.03.2024	BBB-	Mexico	Industrial (General)	3,39%	3,9	107,70	200.000 USD	5,54%
	5,375%	**GMR HYDERABAD INTERNATIONAL AIRPORT LIMITED**	**10.04.2024**	**BBB**	**India**	**Services**	**4,62%**	**3,9**	**103,06**	**200.000 USD**	**5,07%**
	4,215%	COCA COLA ICECEK URETIM AS	19.09.2024	BBB	Turkey	Food Manufacturing	4,41%	4,3	99,15	2.000 USD	4,70%
	5,150%	GAZPROM OJSC	11.02.2026	BBB	Russia	Oil & Petroleum	3,55%	5,3	109,09	200.000 USD	5,69%
*)	4,750%	TOWNGAS FINANCE LTD		A-	Hong Kong	Utilities	4,46%	15,6	104,80	200.000 USD	5,25%
***)**	**4,800%**	**BANK OF MONTREAL**		**BBB-**	**Canada**	**Banking & Finance**	**4,80%**	**20,8**	**100,00**	**200.000 USD**	**4,78%**

Source: FIS MarketMap; all data as of 20th of September   mangenta = recent changes   *) = Perpetual Bonds with next call date in 2024

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