



Lethame Capital Management

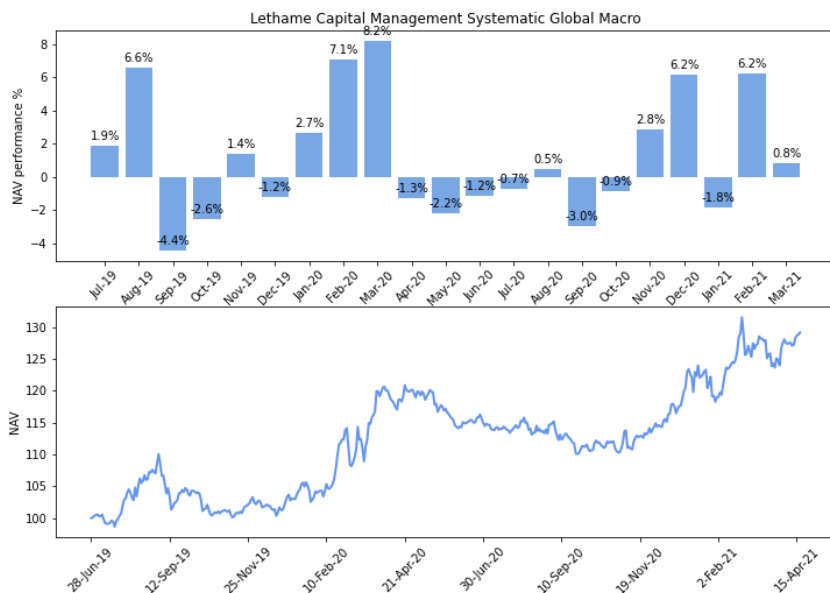
Technology : Research : Investing

Program Update Q4 2020

	Q1	6M	12M	Inception*
Lethame Capital Management	5.1%	13.8%	5.1%	26.6%

This commentary refers to the performance of the strategy of the personal investment vehicle of Piers D. Watson, please see disclaimer. *System running from 1st July 2019.

"The big money is not in the buying or selling, but in the waiting." – Charlie Munger



First Quarter Review

Lethame Capital Management’s (LCM) strategy return in the First Quarter was 5.1% which results an annualised return over the twenty-one months since inception of 13.5%.

In risk adjusted terms the best performances came from Oil, Copper and Soybeans all of which increased by over 10 percentage points in absolute terms. The most negative risk adjusted performances came from Interest rates (10 Year Treasuries and Eurodollars) and the Japanese Yen.

Soft commodities: Strong import demand for Soybeans and Corn from China continued in the first quarter boosted by strong demand from the

livestock sector. Chinese demand continues to improve as the pig industry recovers from the outbreaks of African swine fever, harsh weather in Argentina and Brazil delayed harvest and shipments adding to the upward pressure on prices. Corn prices reached their highest level since 2013 during the quarter.

LCM’s strategy benefitted from long positions in both assets during the quarter.

Rates: Fixed income markets suffered their worst quarter since 1980 as yields rose substantially reaching pre-pandemic levels. The surge in US yields relative to other countries yields helped to drive a surge in the US Dollar. The Japanese Yen fell

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as a consequence suffering its worst quarter since 2016.

In positioning terms, LCM's strategy started the quarter with long positions in all three assets but this positioning was reversed by mid-February allowing the strategy to recapture some return during the quarter.

Strategy

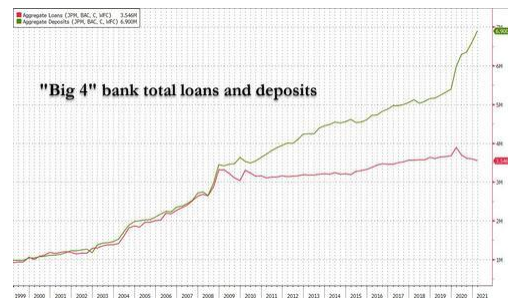
The market continues to believe that U.S. authorities will be successful in creating inflation with the policies they are using to combat the COVID-19 pandemic. The combination of Quantitative Easing and extremely significant fiscal deficit spending is thought to be enough and the reflation trade has performed extremely well. LCMs strategy has observed these trends with strong positive returns from commodity related sectors and negative returns in the interest rate complex. The question remains whether these policies will result in a secular shift in inflation or simply a cyclical upturn.

LCM notes a rather unusual position exists in inflation breakevens as in recent months the market has consistently priced higher inflation over five years than it does over ten. This inversion of the normal term structure of inflation expectations may suggest that the market is not yet fully convinced by the secular inflation story.

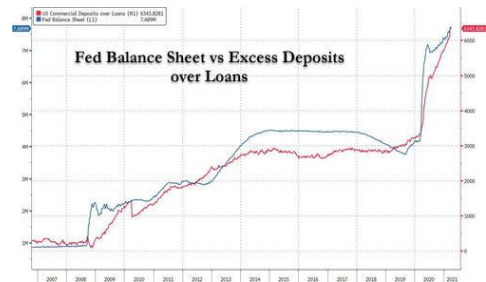
LCM has previously noted flaws in the narrative that Quantitative Easing represents money printing. LCM's analysis indicates that central banks are more likely to be replacing money previously created by the private banking system. Central banks find themselves required to do this since the demise of the offshore Eurodollar market in August 2007. Since that time the private banking sector has significantly pulled back from multi decade enthusiastic credit creation.

This dynamic can be seen from recent results from US banks. JP Morgan's latest earnings report showed that at the end of Q1 total deposits had

risen 24% from a year earlier compared to loans which fell 4% over the year. Zero Hedge reports that at the end of Q1 JPM had *"double the deposits than it had loans for the first time in its history"*.



The above chart shows that since 2008 the big 4 banks have seen deposit growth consistently outpace loan growth. The banks are simply not lending. The money the Fed is pushing into the system via QE in large part remains as reserves on bank balance sheets. As the next chart shows the increase in the Fed's balance sheet tracks very closely this build-up in surplus deposits.



Up to this point banks have been unwilling to lend and it is likely that this lack of credit creation is disinflationary. For a secular uptick in inflation to take hold banks will have to demonstrate a willingness to take risk and start lending again. As of the end of Q1 the signs are that this is not happening.

The U.S. has attempted unprecedented stimulus since COVID-19 both monetary and now fiscal. This stimulus has to overcome powerful disinflationary forces playing out since the 2008 crisis. Despite the markets optimism it remains to be seen whether inflation will sustainably return.

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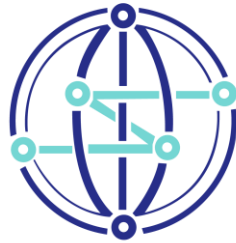
Lethame Capital Management

Lethame Capital Management (LCM) is a private company established to manage capital using proprietary software and algorithms developed by Principal, Piers Watson, CFA FRM CQF. LCM's investment program utilises his thirty years of experience as a portfolio and risk manager covering multiple asset classes and follows years of research, analysis and technology development. The program is designed to provide a comprehensive and systematic exposure to a diversified range of return streams.

Program design has been borne out by the performance of the system since inception and is backed by comprehensive back-testing over the past 25 years (see the performance graph and table on the following page).

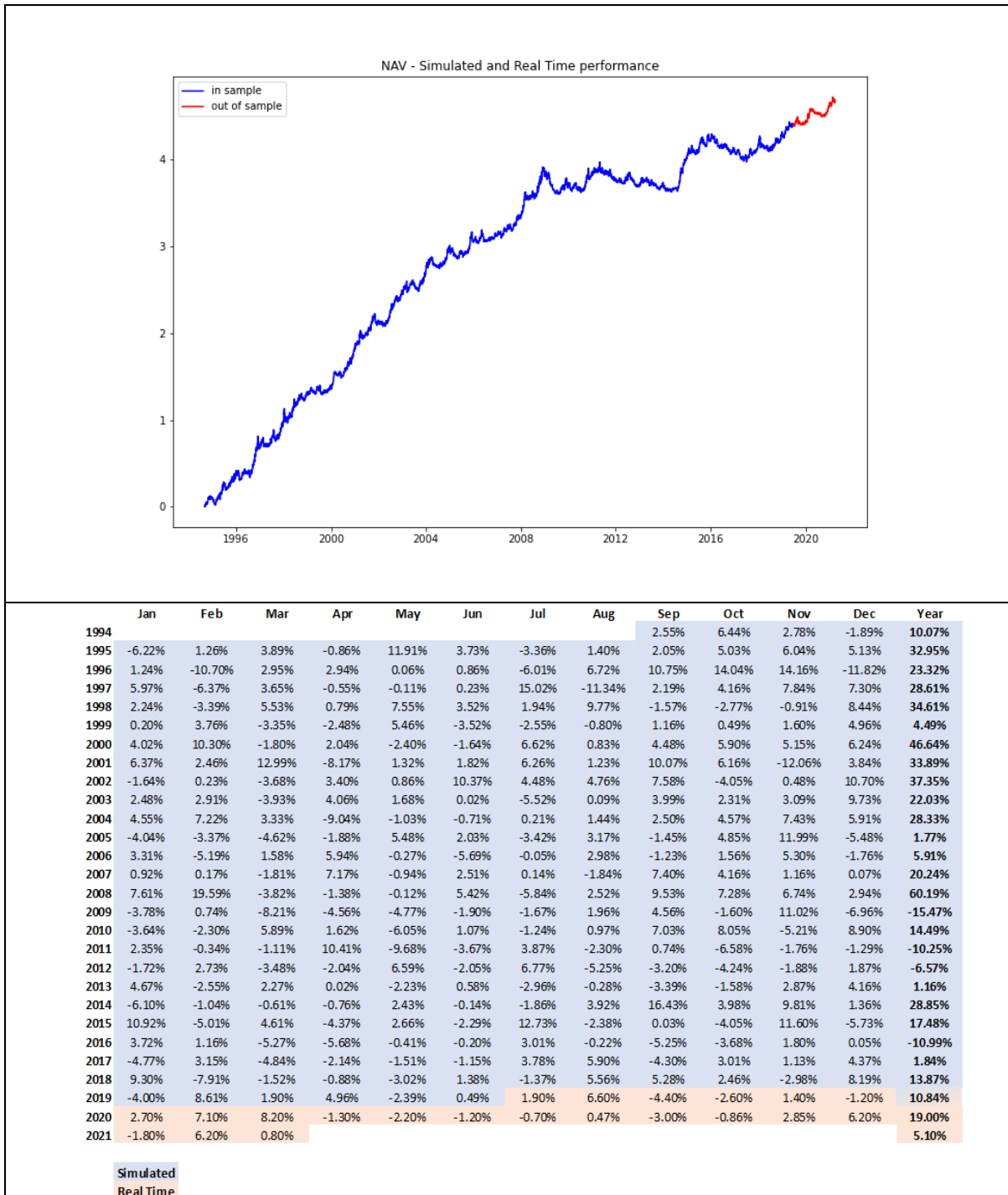
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