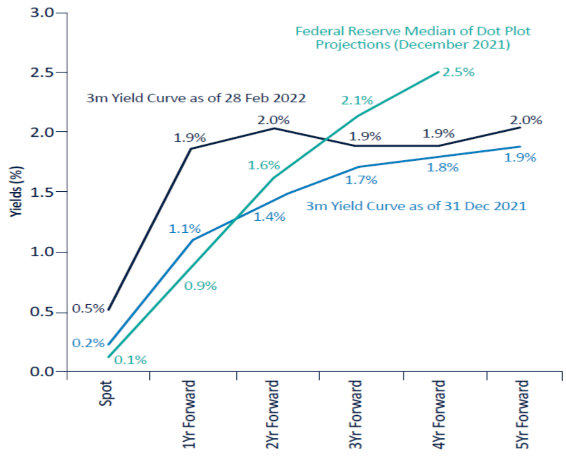
What is the outlook for interest rates?

Rate hikes commence

The higher inflation of 2021 has prompted an abrupt change in the forward guidance of central banks. The US Federal Reserve (Fed) has indicated that it expects to raise rates at least 3 times in 2022. The market has moved ahead of this and is now pricing in nearly 5 rate hikes this year, with the Fed funds rate expected to rise to 1.5% by the end of 2022 and to 2.0% by mid-2023. Interestingly while Fed participants expect short rates to continue to rise over the next five years, with a terminal rate of 2.5%, the forward market expects the pace of rate hikes to slow in 2023 and rates to plateau below 2% until 2027 (Exhibit 1).

Exhibit 1

US interest rates markets discount a more aggressive initial tightening cycle, but expect short rates to plateau below 2% thereafter

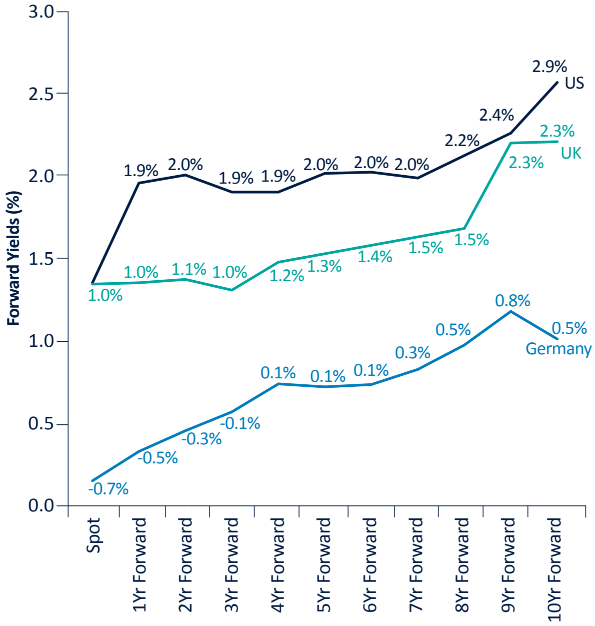


***Source:** Bloomberg*

The Bank of England (BoE) increased interest rates in December 2021 and is expected to undertake a further five rate hikes in 2022, lifting the base rate to 1.7%. The European Central Bank (ECB) remains the least likely to hike, faced with the least core inflation pressures and more recently heightened geopolitical risks which impact the growth outlook. Tightening monetary policy would not resolve the energy supply chain issues that are the primary cause of inflation pressure in the bloc. As shown in Exhibit 2, short rates are expected to stay very low in Europe compared to US or UK.

Exhibit 2

The US and UK will raise rates more than Europe



***Source:** Bloomberg as of 28 February 2022*

Quantitative Tightening (QT) will reduce DM central bank balance sheets by c. -$1.6T by end-2023

Balance sheet reduction by DM central banks will also begin this year and accelerate into next, with asset runoff among most English-speaking central banks and the wind-down of pandemic-related lending schemes by the ECB and BoJ leading to a $1.6T net reduction in holdings by end-2023—about 15% of the post-pandemic build-up. DM balance sheets are expected to peak at around $27.6 trillion by the middle of this year and decline to about $25.6 trillion by the end of 2023. For the G4 (US, EU, Japan and UK), this will still mean central banks own over 60% of nominal GDP (Exhibit 3 and 4).

Exhibit 3

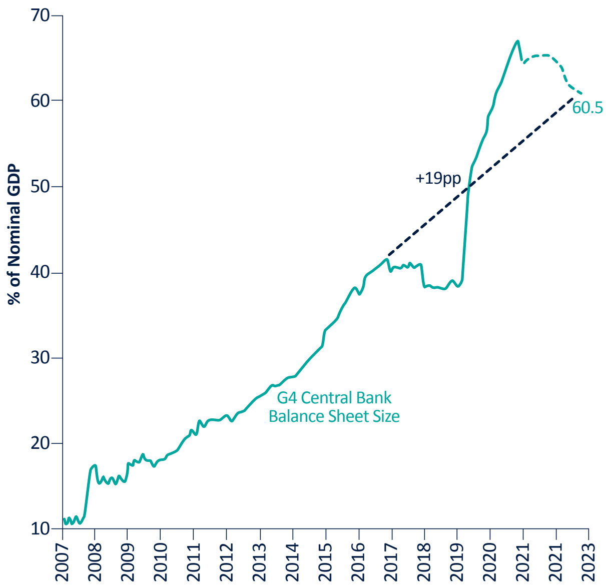
DM central bank balance sheets are expected to contract by c. $1.6T by end-2023 (12m change as of Dec, $B)

	2017	2018	2019	2020	2021	2022	2023
Fed	-9	-385	115	3161	1431	-237	-999
ECB	900	259	-34	2628	1801	532	-350
BoJ	390	266	182	1124	149	-487	60
BoE	135	37	-13	430	303	-48	-41
BoC	4	4	3	341	-40	-10	-33
RBA	9	-7	0	104	227	27	-86
RBNZ	2	1	-4	34	13	2	-5
Total	**1430**	**174**	**249**	**7822**	**3885**	**-221**	**-1454**

Source: *Fed, ECB, BoJ, BoE, BoC, RBA, RBNZ, JPM*

Exhibit 4

G4 central bank balance sheets will still exceed 60% of aggregate nominal GDP by 2023

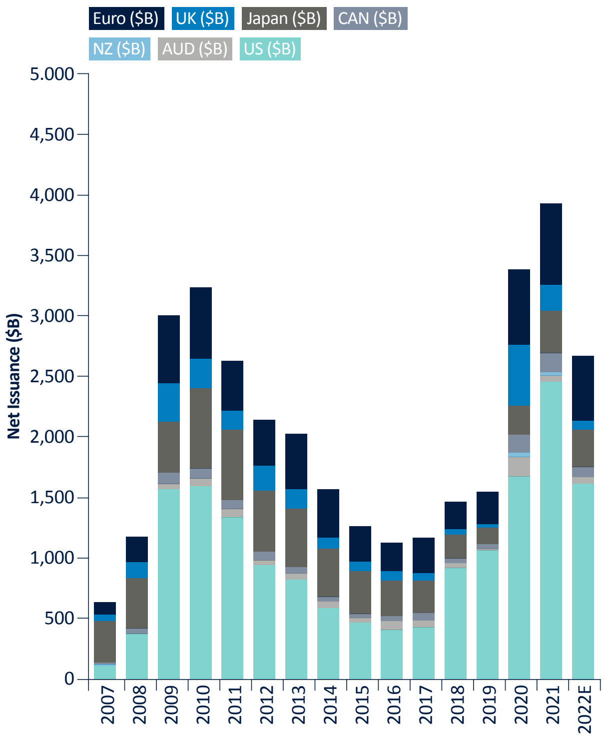


Source: *Morgan Stanley*

The impact of Quantitative Tightening (QT) on financial conditions, and therefore on the likely path for DM policy rates, is clouded by the large bond supply coming from higher fiscal deficits. Net issuance of coupon bonds (i.e., not including bills and net of maturing securities) is estimated to be $2.7 trillion across the G7 in 2022. While high, this would still be a decrease in net issuance across the G7 of about $1.4 trillion in 2022 relative to 2021, a 34% decline. If we further net out the assets likely to be purchased by central banks, the issuance is $2.0 trillion, modestly higher than last year's issuance net of QE purchases which was $1.7 trillion, illustrating the extent to which central banks absorbed supply in 2021 (Exhibit 5a and 5b).

Exhibit 5a

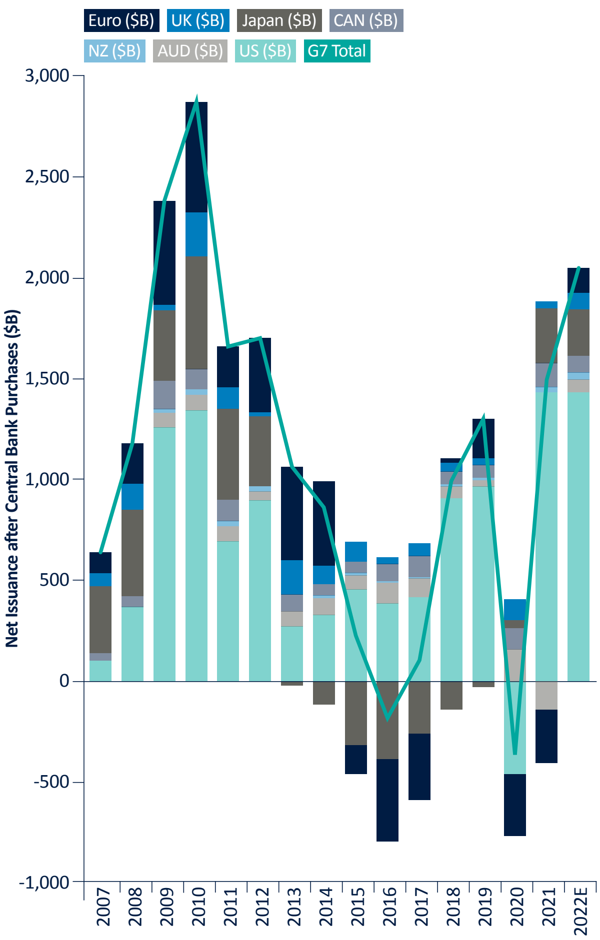
G7 bond issuance net of maturing securities



Source: *Morgan Stanley Research estimates, National Treasuries*

Exhibit 5b

G7 bond issuance net of maturing securities and central bank purchases



***Source:** Morgan Stanley Research estimates, National Treasuries*

Net coupon bond supply after central bank purchases of US$2.0 trillion will still mean investors have to absorb the third highest amount of net issuance since 2007, with only 2009 and 2010 seeing higher new supply. Financial theory suggests that as this degree of bond supply is already well known by the market, it should already be factored into the price of bonds. Nevertheless, our view is that such a large amount of issuance is likely to put modest upward pressure on G7 bond yields over 2022.

Investment implications:

Our expectation is that developed market bond yields will move higher in 2022 at a rate that is faster than what is discounted by the forward markets, primarily driven by higher inflation and high debt issuance. While inflation may stabilise or decline over the coming quarters, much depends on how longer-term inflation develops. In our tail scenario of higher inflation, the Fed and other central banks will likely be forced to raise interest rates even further, thereby engineering an economic slowdown sufficient to reduce aggregate demand so that aggregate supply can rebalance. Our summary growth, inflation and interest rate scenarions are shown in Exhibit 6 below.

Hence, at current yield levels 10-year bonds remain an unappealing use of capital. We maintain a c.5% underweight to the asset class relative to benchmark weight, favouring liquid Absolute Return, ILBs and uncorrelated strategies. We will look to reduce this underweight if yields on US Treasuries were to rise above 2.5%, as bonds are still attractive from a portfolio diversification standpoint.

This also has implications for equity sectors. Equity prices declined in early 2022 in response to a sharp increase in bond yields, with the 10-year Treasury climbing from 1.5% to 1.8% in January. This decline in prices means that valuations in these markets have come down from peak levels, but they are still above pre-pandemic levels on a multiples basis and rich compared to long-term history. We recommend maintaining exposure to emerging tech managers, but we are not increasing exposure targets given continuing volatility in 2022, noisy earnings environment and managing portfolio risk.

Exhibit 6

Partners Capital Growth, Inflation and Interest Rate Scenarios

	Recovery Falters	Stagflation	Gradual Normalisation	Reflation 2.0	Expected Value
Probability	10%	10%	60%	20%	
DM Growth	2.5%	5.5%	3.9%	4.4%	**4.0%**
DM Inflation	2.5%	5.5%	3.9%	4.5%	**4.0%**
Expected 10yr US Treasury Yield	1.0%	3.5%	2.5%	3.0%	**2.6%**
Expected 10yr US Breakeven	1.5%	4.0%	2.3%	2.5%	**2.4%**
Expected 10yr US Real Yield	-0.5%	-0.5%	0.3%	0.5%	**0.2%**

***Source:** Partners Capital Analysis*

DISCLAIMER

Within the United Kingdom, this material has been issued by Partners Capital LLP, which is authorised and regulated by the Financial Conduct Authority of the United Kingdom (the "FCA"), and constitutes a financial promotion for the purposes of the rules of the Financial Conduct Authority. Within Hong Kong, this material has been issued by Partners Capital Asia Limited, which is licensed by the Securities and Futures Commission in Hong Kong (the "SFC") to provide Types 1 and 4 services to professional investors only. Within Singapore, this material has been issued by Partners Capital Investment Group (Asia) Pte Ltd, which is regulated by the Monetary Authority of Singapore as a holder of a Capital Markets Services licence for Fund Management under the Securities and Futures Act and as an exempt financial adviser. Within France, this material has been issued by Partners Capital Europe SAS, which is regulated by the Autorité des Marchés Financiers (the "AMF").

For all other locations, this material has been issued by Partners Capital Investment Group, LLP which is registered as an Investment Adviser with the US Securities and Exchange Commission (the "SEC") and as a commodity trading adviser and commodity pool operator with the Commodity Futures Trading Commission ("CFTC") and is a member of the National Future's Association (the "NFA").

This material is being provided to clients, potential clients and other interested parties (collectively "clients") of Partners Capital LLP, Partners Capital Asia Limited, Partners Capital Investment Group (Asia) Pte Ltd, Partners Capital Europe SAS and Partners Capital Investment Group, LLP (the "Group") on the condition that it will not form a primary basis for any investment decision by, or on behalf of the clients or potential clients and that the Group shall not be a fiduciary or adviser with respect to recipients on the basis of this material alone. These materials and any related documentation provided herewith is given on a confidential basis. This material is not intended for public use or distribution. It is the responsibility of every person reading this material to satisfy himself or herself as to the full observance of any laws of any relevant jurisdiction applicable to such person, including obtaining any governmental or other consent which may be required or observing any other formality which needs to be observed in such jurisdiction. The investment concepts referenced in this material may be unsuitable for investors depending on their specific investment objectives and financial position.

This material is for your private information, and we are not soliciting any action based upon it. This report is not an offer to sell or the solicitation of an offer to buy any investment. While all the information prepared in this material is believed to be accurate, the Group, may have relied on information obtained from third parties and makes no warranty as to the completeness or accuracy of information obtained from such third parties, nor can it accept responsibility for errors of such third parties, appearing in this material. The source for all figures included in this material is Partners Capital Investment Group, LLP, unless stated otherwise. Opinions expressed are our current opinions as of the date appearing on this material only. We do not undertake to update the information discussed in this material. We and our affiliates, officers, directors, managing directors, and employees, including persons involved in the preparation or issuance of this material may, from time to time, have long or short positions in, and buy and sell, the securities, or derivatives thereof, of any companies or funds mentioned herein.

Whilst every effort is made to ensure that the information provided to clients is accurate and up to date, some of the information may be rendered inaccurate by changes in applicable laws and regulations. For example, the levels and bases of taxation may change at any time. Any reference to taxation relies upon information currently in force. Tax treatment depends upon the individual circumstances of each client and may be subject to change in the future. The Group is not a tax adviser and clients should seek independent professional advice on all tax matters.

Within the United Kingdom, and where this material refers to or describes an unregulated collective investment scheme (a "UCIS"), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom a UCIS may lawfully be promoted by a person authorised under the Financial Services and Markets Act 2000 (the "FSMA") by virtue of Section 238(6) of the FSMA and the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (including other persons who are authorised under the FSMA, certain persons having professional experience of participating in unrecognised collective investment schemes, high net worth companies, high net worth unincorporated associations or partnerships, the trustees of high value trusts and certified sophisticated investors) or Section 4.12 of the FCA's Conduct of Business Sourcebook ("COBS") (including persons who are professional clients or eligible counterparties for the purposes of COBS). This material is exempt from the scheme promotion restriction (in Section 238 of the FSMA) on the communication of invitations or inducements to participate in a UCIS on the grounds that it is being issued to and/or directed at only the types of person referred to above. Interests in any UCIS referred to or described in this material are only available to such persons and this material must not be relied or acted upon by any other persons.

Within Hong Kong, where this material refers to or describes an unauthorised collective investment schemes (including a fund) ("CIS"), the communication of this material is made only to and/or is directed only at professional investors who are of a kind to whom an unauthorised CIS may lawfully be promoted by Partners Capital Asia Limited under the

Hong Kong applicable laws and regulation to institutional professional investors as defined in paragraph (a) to (i) under Part 1 of Schedule to the Securities and Futures Ordinance ("SFO") and high net worth professional investors falling under paragraph (j) of the definition of "professional investor" in Part 1 of Schedule 1 to the SFO with the net worth or portfolio threshold prescribed by Section 3 of the Securities and Futures (Professional Investor) Rules (the "Professional Investors").

Within Singapore, where this material refers to or describes an unauthorised collective investment schemes (including a fund) ("CIS"), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom an unauthorised CIS may lawfully be promoted by Partners Capital Investment Group (Asia) Pte Ltd under the Singapore applicable laws and regulation (including accredited investors or institutional investors as defined in Section 4A of the Securities and Futures Act).

Within France, where this material refers to or describes to unregulated or undeclared collective investment schemes (CIS) or unregulated or undeclared alternative Investment Funds (AIF), the communication of this material is made only to and/or is directed only at persons who are of a kind to whom an unregulated or undeclared CIS or an unregulated or undeclared AIF may lawfully be promoted by Partners Capital Europe under the French applicable laws and regulation, including professional clients or equivalent, as defined in Article D533-11, D533-11-1, and D533-13 of the French Monetary and Financial Code.

Certain aspects of the investment strategies described in this presentation may from time to time include commodity interests as defined under applicable law. Within the United States of America, pursuant to an exemption from the US Commodity Futures Trading Commission (CFTC) in connection with accounts of qualified eligible clients, this brochure is not required to be, and has not been filed with the CFTC. The CFTC does not pass upon the merits of participating in a trading program or upon the adequacy or accuracy of commodity trading advisor disclosure. Consequently, the CFTC has not reviewed or approved this trading program or this brochure. In order to qualify as a certified sophisticated investor a person must (i) have a certificate in writing or other legible form signed by an authorised person to the effect that he is sufficiently knowledgeable to understand the risks associated with participating in unrecognised collective investment schemes and (ii) have signed, within the last 12 months, a statement in a prescribed form declaring, amongst other things, that he qualifies as a sophisticated investor in relation to such investments.

This material may contain hypothetical or simulated performance results which have certain inherent limitations. Unlike an actual performance record, simulated results do not represent actual trading. Also, since the trades have not actually been executed, the results may have under- or over-compensated for the impact, if any, of certain market factors, such as lack of liquidity. Simulated trading programs in general are also subject to the fact that they are designed with the benefit of hindsight. No representation is being made that any client will or is likely to achieve profits or losses similar to those shown. These results are simulated and may be presented gross or net of management fees. This material may include indications of past performance of investments or asset classes that are presented gross and net of fees. Gross performance results are presented before Partners Capital management and performance fees, but net of underlying manager fees. Net performance results include the deduction of Partners Capital management and performance fees, and of underlying manager fees. Partners Capital fees will vary depending on individual client fee arrangements. Gross and net returns assume the reinvestment of dividends, interest, income and earnings.

The information contained herein has neither been reviewed nor approved by the referenced funds or investment managers. Past performance is not a reliable indicator and is no guarantee of future results. Investment returns will fluctuate with market conditions and every investment has the potential for loss as well as profit. The value of investments may fall as well as rise and investors may not get back the amount invested. Forecasts are not a reliable indicator of future performance.

Certain information presented herein constitutes "forward-looking statements" which can be identified by the use of forward-looking terminology such as "may", "will", "should", "expect", "anticipate", "project", "continue" or "believe" or the negatives thereof or other variations thereon or comparable terminology. Any projections, market outlooks or estimates in this material are forward –looking statements and are based upon assumptions Partners Capital believe to be reasonable. Due to various risks and uncertainties, actual market events, opportunities or results or strategies may differ significantly and materially from those reflected in or contemplated by such forward-looking statements. There is no assurance or guarantee that any such projections, outlooks or assumptions will occur.

Certain transactions, including those involving futures, options, and high yield securities, give rise to substantial risk and are not suitable for all investors. The investments described herein are speculative, involve significant risk and are suitable only for investors of substantial net worth who are willing and have the financial capacity to purchase a high risk investment which may not provide any immediate cash return and may result in the loss of all or a substantial part of their investment. An investor should be able to bear the complete loss in connection with any investment.

All securities investments risk the loss of some or all of your capital and certain investments, including those involving futures, options, forwards and high yield securities, give rise to substantial risk and are not suitable for all investors.