

ALTERNATIVE STRATEGIES FOR A DEMOCRATIC U.S. CONGRESS



Philippe Ferreira
Senior Strategist

Jean-Baptiste Berthon
Senior Strategist

Pierre Carreyn
Hedge Fund Analyst

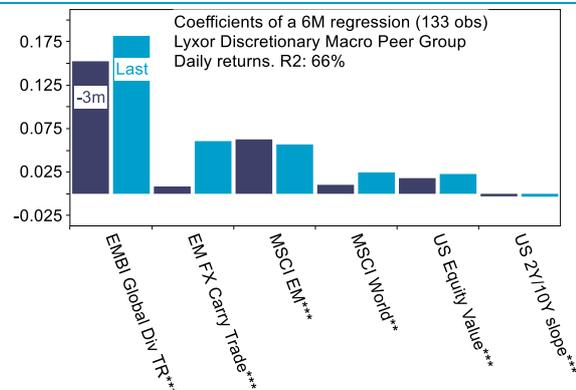
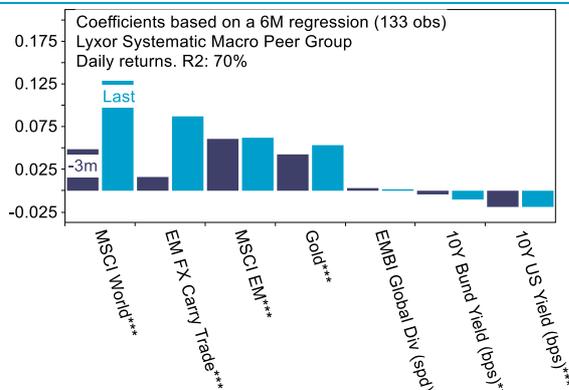
CrossAssetResearch@lyxor.com

As we go to press, it looks likely that Democrats will also run the Senate, in addition to the White House and the House of Representatives. With expectations that this will translate into greater fiscal stimulus in the near-term, bond yields moved upwards in the U.S. and the Treasury curve steepened. European rates were also under pressure, though the surge in yields was more limited there. Considering the current level of bond yields, the upside potential is huge under a Democratic sweep and would have global reverberations across countries and asset classes.

In our view, Covid-19 headwinds and Fed bond purchases should contribute towards containing any substantial rise in yields in the near term. In the longer term, structural factors such as demographics and technology advances should also prevent a normalization in yields to levels seen before the Global Financial Crisis. Yet, we will probably converge in the next couple of years to the range of 2 to 3% last observed in 2017-2018. How fast we will get there is what matters for markets at this critical juncture. Our base case assumes we will not get there in H1-2021.

In the space of alternatives, Global Macro strategies appear interesting to play this partial and back ended normalization in bond yields. Their long position on fixed income has been reduced lately and, in some cases, turned slightly short on Treasuries. Inflation linked bonds and EM bonds now represent the bulk of the fixed income exposure. Discretionary strategies also appear to have reduced their sensitivity to a steepening of the Treasury curve. Meanwhile, their short USD bias in FX could also be rewarded under a Democratic Congress with twin deficits pushing the USD lower. The worst-case scenario, whose probability is low, would be a brutal rise in yields that would derail equities, lifting the USD and hurting EM assets. Under that scenario of a sharp trend reversal across asset classes, Global Macro strategies still have the potential to outperform other hedge fund strategies, in our view. Our stance thus remains Overweight.

Global Macro to benefit from Dollar depreciation vs. EM under a Democratic Congress



As of 31/12/2020. ** Significant at 95% confidence level; *** Significant at 99% confidence level. Sources: Bloomberg, Macrobond, Lyxor AM

Hedge Fund Performance: Directional strategies lead the pack

	Dec. 2020	Q4 2020	Y2020
MSCI World	3.5%	12.5%	14.1%
Event-Driven: Special Situations	3.2%	10.3%	4.1%
L/S Equity Directional	2.8%	6.8%	4.9%
Global Macro	1.6%	4.6%	1.7%
Global Lyxor UCITS Peer Group	1.9%	4.2%	1.3%
Event-Driven: Merger Arbitrage	1.3%	4.1%	2.1%
L/S Credit	1.0%	3.4%	3.9%
CTAs	3.5%	3.1%	-1.4%
Bloomberg Barclays Global Aggregate Bond Index	0.3%	0.9%	5.6%
L/S Equity Market Neutral	1.0%	0.9%	0.0%
Risk Premia	0.6%	-0.9%	-10.1%

*As of December 31st, 2020. Source: Bloomberg, Lyxor AM

Most hedge fund strategies ended 2020 in the black, with Directional L/S up +4.9% and Special Situations up +4.1%. L/S Credit was also up almost +4%.

On a negative note, CTAs ended slightly down (-1.4%) despite their strong performance in December (+3.5%).

The last quarter brought substantial relief to those strategies with a higher equity market beta, as the MSCI World was up a massive +12.5%. Alpha generation was nonetheless also substantial. Some strategies with low market directionality, such as Merger Arbitrage and Global Macro, were up in excess of +4% in Q4.

Risk premia strategies remain the only source of disappointment, both in Q4 (-0.9%) and for the full year (-10.1%).

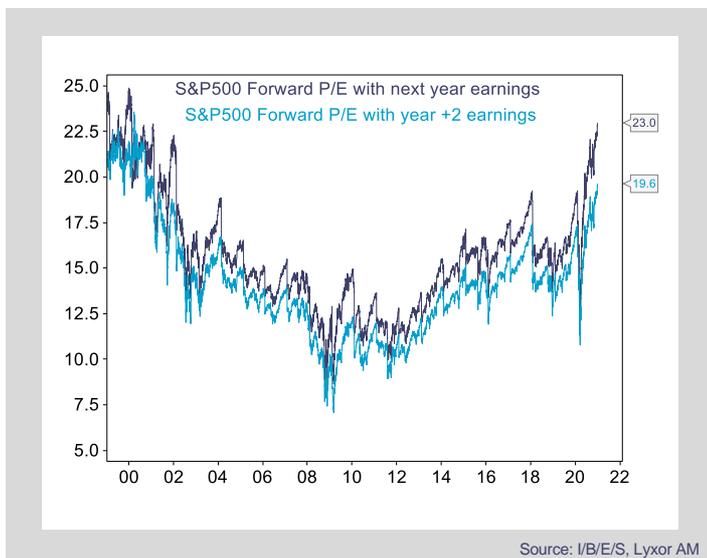
EM Macro strategies increased EMFX carry trade positions



EM Macro strategies have significantly bulked up their positions on EM currencies vs. USD in recent months. The EM FX carry trade, a strategy that borrows low-yield currencies to invest in high yield ones, is back. It was popular in the late '00s but did little since then, according to Bloomberg's EM-8 Carry Trade index. Yet, current positions from Global Macro strategies on EMFX appear to be backed by fundamental analysis, not a systematic risk premia approach. Carry trade strategies are also popular across the spectrum of Global Macro strategies, not only EM ones.

Overall, both EM currencies and bonds contribute towards explaining the 70% of the returns of our EM Global Macro Peer Group, which pools together 11 strategies. Our stance on EM Global Macro strategies has been Overweight for several months.

Rich valuation in U.S. equity markets: a headwind for future returns



According to both Bloomberg and I/B/E/S, the 12-months forward P/E of the U.S. equity market is back to levels close to the late '90s, at 23x. The next 12-months remain challenging for corporate earnings as Covid-19 headwinds will continue to bite in the first half of the year. Meanwhile, equity markets value long term flows, not just the earnings of the following year.

The valuation picture with 2022 expected earnings by I/B/E/S looks less stretched, at 19.6x. But it remains above the levels observed since the Tech bubble bust in the early '00s.

From that perspective mid- to long-term equity returns could be low and investors with a long-term perspective should probably diversify this source of risk. With bond yields close to record lows, some alternative strategies bring value-added to achieve that objective without giving up on performance.

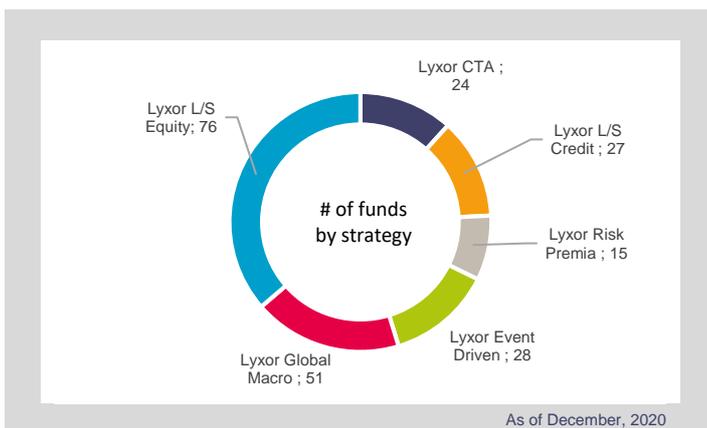
METHODOLOGICAL APPENDIX

The information contained in this report on the performance of hedge funds is based on publicly available information. The universe of underlying funds is relatively stable but varies depending on the criteria of inclusion presented below. It is based on an unbiased selection from our hedge fund analyst team.

Performance is calculated on a weekly basis, as of end-Tuesday, using an arithmetic average (equally weighted average).

Regarding share classes used in these peer groups, we selected the primary share class as referenced in Bloomberg. Non-USD share classes are hedged in USD based on hedging costs available on Bloomberg.

Lyxor Hedge Fund Peer Groups: number of funds by strategy



- 221 strategies across the main categories in the industry
- USD 176 billion of assets under management

Criteria of inclusion

The criteria of inclusion are fourfold:

- We only include UCITS strategies;
- Assessment by Lyxor's Hedge Fund selection team based on funds' materials or manager interaction;
- We only include strategies with assets under management of at least USD 50 million; and
- We only include strategies with at least a one-year track record.

-

DISCLAIMER

The circumstances in which this publication has been produced are such that it is not appropriate to characterize it as independent investment research as referred to in MiFID and that it should be treated as a marketing communication even if it contains a research recommendation. This publication is also not subject to any prohibition on dealing ahead of the dissemination of investment research. However, Lyxor is required to have policies to manage the conflicts which may arise in the production of its research, including preventing dealing ahead of investment research.

This material has been prepared solely for informational purposes only and does not constitute an offer, or a solicitation of an offer, to buy or sell any security or financial instrument, or to participate in any investment strategy. This material does not purport to summarize or contain all of the provisions that would be set forth in any offering memorandum. Any purchase or sale of any securities may be made only pursuant to a final offering memorandum. No advisory relationship is created by the receipt of this material. This material should not be construed as legal, business or tax advice. A more robust discussion of the risks and tax considerations involving in investing in a fund is available from the more complete disclosures incorporated into the offering documentation for such fund.

This material has not been prepared in regard to specific investment objectives, financial situations, or the particular needs of any specific entity or person. Investors should make their own appraisal of the risks and should seek their own financial advice regarding the appropriateness of investing in any securities or financial instrument or participating in any investment strategy. Before you decide to invest in any account or fund, you should carefully read the relevant client agreements and offering documentation. No representation is made that your investment objectives will be achieved. This material is not intended for use by retail customers.

Any descriptions involving investment process, risk management, portfolio characteristics or statistical analysis are provided for illustrative purposes only, will not apply in all situations, and may be changed without notice. Past performance is not indicative of future results, and it is impossible to predict whether the value of any fund or index will rise or fall over time.

While the information in this material has been obtained from sources deemed reliable, neither Société Générale ("SG"), Lyxor Asset Management S.A.S. ("Lyxor AM") nor their affiliates guarantee its accuracy, timeliness or completeness. We are under no obligation to update or otherwise revise such information if and when it changes. Any opinions expressed herein are statements of our judgment on this date and are subject to change without notice. SG, Lyxor AM and their affiliates assume no fiduciary responsibility or liability for any consequences, financial or otherwise, arising from an investment in any security or financial instrument described herein or in any other security, or from the implementation of any investment strategy. Lyxor AM and its affiliates may from time to time deal in, profit from the trading of, hold, have positions in, or act as market-makers, advisers, brokers or otherwise in relation to the securities and financial instruments described herein. Service marks appearing herein are the exclusive property of SG and its affiliates, as the case may be.

Hedge funds may invest in futures and other derivative instruments. Futures trading and other derivatives may permit extremely high degrees of leverage and expose the funds to, among other things, volatility, market illiquidity, market risks, legal risks and operational risks. Hedge funds may be exposed to risks relating to non-domestic markets, including, without limitation, risks relating to currency exchange, tax, lack of liquidity, market manipulation, political instability and transaction costs. An investment in a hedge fund is subject to a total loss. This presentation contains the views of Lyxor AM analysts and/or strategies. The views espoused in this presentation may differ from opinions and recommendations produced by other departments of SG.

Note about Indices: Indices are not available for direct investment. A comparison to an index is not meant to imply that an investment in a fund is comparable to an investment in the funds or securities represented by such index. A fund is actively managed while an index is a passive index of securities. Indices are not investable themselves, and thus do not include the deduction of fees and other expenses associated with an investment in a fund. Not all the funds that comprise indices cited herein are suitable for U.S. Investors as a result of, among other things, the implementation of the Volcker Rule. Please see the offering documentation for these funds for more details.

Notice to U.S. Investors: Any potential investment in any securities or financial instruments, the categories of which are described herein, may not be suitable for all investors. Any prospective investment will require you to represent that you are an "accredited investor," as defined in Regulation D under the Securities Act of 1933, as amended, and a "qualified purchaser," as defined in Section 2(a)(51) of the Investment Company Act of 1940, as amended (the "40 Act"). The securities and financial instruments described herein may not be available in all jurisdictions.

Investments in or linked to hedge funds are highly speculative and may be adversely affected by the unregulated nature of hedge funds and the use of trading strategies and techniques that are typically prohibited for funds registered under the '40 Act. Also, hedge funds are typically less transparent in terms of information and pricing and have much higher fees than registered funds. Investors in hedge funds may not be afforded the same protections as investors in funds registered under the '40 Act including limitations on fees, controls over investment policies and reporting requirements.

Notice to Canadian Investors: Any potential investment in any securities or financial instruments, the categories of which are described herein, may not be suitable for all investors. Any prospective investment will require you to represent that you are a "permitted client," as defined in Canadian Regulation National Instrument 31-103, and an "accredited investor," as defined in National Instrument 45-106. The securities and financial instruments described herein may not be available in all jurisdictions of Canada.

For more information, U.S. and Canadian investors and recipients should contact Lyxor Asset Management Inc., 1251 Sixth Avenue, New York, NY 10020 or invest@lyxor.com.

Notice to U.K. Investors: This communication is issued in the UK by Lyxor Asset Management UK LLP, which is authorised and regulated by the Financial Conduct Authority in the UK under Registration Number 435658.

Source: This document has been prepared by Lyxor Asset Management S.A.S., 17 cours Valmy, 92800 Puteaux. Lyxor AM is a French management company authorized by the Autorité des marchés financiers and placed under the regulations of the UCITS (2014/91/UE) and AIFM (2011/61/EU) Directives. Lyxor AM is also registered with the U.S. Commodity Futures Trading Commission as a registered commodity pool operator and a commodity trading advisor.